

## Washington Supreme Court Rules on Duty Defend and Discovery

In a unanimous decision<sup>1</sup> on an issue it identified as a matter of first impression in Washington, the Washington Supreme Court held discovery that is potentially prejudicial to an insured in underlying litigation must be stayed until the underlying litigation is fully adjudicated.<sup>2</sup> The Court also held that the trial court erred when it delayed ruling on a motion for summary judgment filed by the insured, Expedia, regarding its insurer's duty to defend against numerous underlying lawsuits.<sup>3</sup>

The underlying litigation involved multiple lawsuits brought against Expedia by state and local taxing authorities. Expedia tendered most of the suits to Zurich; however, some were tendered late. Zurich declined Expedia's tender on several grounds, including late tender and that the underlying suits may be excluded from coverage.

In November 2010, Expedia filed suit against Zurich for declaratory judgment, insurance bad faith, and violation of Washington's Consumer Protection Act. Zurich responded with a counterclaim for declaratory judgment regarding its coverage obligations. Zurich also asserted various defenses, including late tender, known loss, material misrepresentation, and mistake. The trial court declined to make a determination of Zurich's duty to defend Expedia and ordered Expedia to produce discovery that Expedia claimed may be prejudicial to it in the underlying actions.

When the matter reached the Washington Supreme Court, the Court rejected Zurich's argument that under *Nat'l Sur. Corp. v. Immunex Corp.*,<sup>4</sup> it was entitled to discovery related to its late tender defense, which requires an insurer to prove that it was "actually and substantially prejudiced" by a late tender.<sup>5</sup> In so holding, the Court stated the following regarding its holding in *Immunex*:

At most, *Immunex* indicates that the actual prejudice question is relevant only to the late tender defense and that actual prejudice caused by late tender may relieve the insurer of the duty to pay the cost of defense incurred after the insurer obtains a judicial declaration that it owes no duty to defend.

---

<sup>1</sup> *Expedia, Inc. v. Steadfast Ins. Co.*, No. 88673-3 (July 3, 2014).

<sup>2</sup> The Court's ruling is understandable, and it is curious why the Court even deemed this a matter of first impression in view of its prior ruling in *Mut. Of Enumclaw v. Paulsen Construc.*, 161 Wn.2d 903, 918 (2007) that "[w]hile defending under a reservation of rights, an insurer acts in bad faith if it pursues a declaratory judgment that it has no duty to defend and that 'action might prejudice the insured's tort defense.'" The only distinction between *Paulsen* and the current case is that the insurer in *Paulsen* was defending while Zurich had denied a defense.

<sup>3</sup> The opinion refers to the petitioner insureds collectively as Expedia and refers to respondent insurers collectively as Zurich.

<sup>4</sup> 176 Wn.2d 872, 297 P.3d 688 (2013)

<sup>5</sup> *Immunex Corp.*, 176 Wn.2d at 890.

The Court held the trial court should have adjudicated the duty to defend issue first. Then, Zurich could attempt to prove its defenses, including prejudice from late tender. “In the meantime, however, Zurich should have been required to defend Expedia if the court found that the duty to defend had been triggered.” The Court also held:

Unless actual prejudice can be established by the insurer as a matter of law, an insurer’s allegations of prejudice cannot preclude a determination that the underlying claim is conceivably covered.

The Court then addressed Zurich’s argument based upon *Overton v. Consolidated Insurance Co.*,<sup>6</sup> that it should be permitted to discover and present extrinsic evidence to negate its duty to defend. The Court held that to the extent *Overton* supported Zurich’s argument “the opinion predates and conflicts with the extrinsic evidence rule as clarified in *Truck Insurance Exchange* and its progeny.”<sup>7</sup>

Citing a California Court of Appeal decision, *Haskel, Inc. v. Superior Court*,<sup>8</sup> the Washington Supreme Court held “an adjudication of the duty to defend cannot be delayed by discovery.” Therefore, the trial court erred by delaying adjudication of Expedia’s summary judgment motion concerning the duty to defend until Expedia complied with potentially prejudicial discovery.

The Court remanded the case to the trial court to determine Zurich’s duty to defend Expedia in each of the underlying cases subject to Expedia’s motion. The Court also ordered the trial court “to stay discovery in the coverage action until it can make a factual determination as to which parts of discovery in the coverage action are potentially prejudicial to Expedia in the underlying litigation.” Finally, the Court instructed that “[a]ll discovery logically related to the underlying claims should be stayed until such claims are fully adjudicated.”

*Soha & Lang, P.S. attorneys are available to assist insurer clients in understanding and addressing the impact of this decision.*

*Disclaimer: The opinions expressed in in this article are those of the author and do not necessarily reflect those of Soha & Lang, P.S. or its clients.*

---

<sup>6</sup> 145 Wn.2d 417, 38 P.3d 322 (2002).

<sup>7</sup> *Truck Ins. Exch. v. Vanport Homes, Inc.*, 147 Wn.2d 751, 58 P.3d 276 (2002) (the duty to defend must be determined from the “eight corners” of the insurance contract and the underlying complaint; the two exceptions to this rule may be used only to trigger the duty to defend, not to foreclose it).

<sup>8</sup> 33 Cal. App. 4th 963, 39 Cal. Rptr. 2d 520 (1995).