Case No. 100466-4

SUPREME COURT OF THE STATE OF WASHINGTON

PREFERRED CONTRACTORS INSURANCE COMPANY, RISK RETENTION GROUP, LLC,

Plaintiff,

v.

BAKER AND SON CONSTRUCTION, a Washington for-profit corporation; ANGELA COX, as Personal Representative of the Estate of RONNIE E. COX, deceased; ANGELA COX, individually and as mother of G.C., a minor,

Defendants.

BRIEF OF *AMICUS CURIAE* UNITED POLICYHOLDERS

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I. INTRODUCTION

United Policyholders (UP) submits this brief as *amicus curiae*.

II. IDENTITY AND INTEREST OF *AMICUS CURIAE*

Founded in 1991, UP is a non-profit organization that serves as a voice and information resource for insurance consumers in all 50 states. UP is a tax-exempt § 501(c)(3) entity sustained by individual and corporate donations and grants from foundations. Volunteers across the country donate thousands of hours each year to support the organization's work. Through its *Roadmap to Recovery*™ program, UP promotes insurance and financial literacy, and helps individuals navigate the insurance claim process and recover fair and timely settlements. UP has been providing claim and recovery assistance to Washington State residents for decades, including the 2014 Carlton Complex Fire in Pateros, and the 2020 Labor Day Complex fires in Okanogan and Douglas Counties. Through its *Advocacy and Action* program which includes

coordination with Washington Insurance Commissioner Mike Kreidler and his staff, UP helps solve insurance problems by working with public officials, other non-profit and faith-based organizations, and a diverse range of other entities, including insurers and producers.

III. STATEMENT OF THE CASE

UP adopts the facts as presented by the injury-claimant, Angela Cox ("Cox") and by the policyholder Baker and Son Construction, Inc. ("Baker"). The question presented in this case arises from the fact that the policies issued to Baker by Preferred Contractors Insurance Company Risk Retention Group, LLC ("PCIC") are "claims-made" policies. UP briefly describes the main features of a "claims-made" policy before turning to the parties' arguments.

The more familiar type of liability insurance policy is an "occurrence" policy, which covers the policyholder for legal liability for negligence for an "occurrence" happening during the policy period. In contrast, under "a 'claims-made' policy,"

the "coverage is triggered by the filing of a claim rather than the occurrence of the injury or property damage for which coverage is sought." *State v. Zurich Specialities London Ltd.*, 2003 WL 1824966, at *3, 116 Wn. App. 1033 (2003) (unpublished) (citing *Weyerhaeuser Co. v. Commercial Union Ins. Co.*, 142 Wn.2d 654, 679 n.12, 15 P.3d 115 (2000)).

A standard feature of a claims-made policy is the "retroactive date." The insurer typically agrees to cover the policyholder for any claims received during the policy period, but only for conduct stretching back to the "retroactive date." *See*, *e.g.*, *Zurich Specialities*, 2003 WL 1824966, at *2 (evaluating coverage for a policyholder with a claims-made policy covering claims received in 1999 arising out of conduct stretching back to a retroactive date in 1990).

As discussed further below, PCIC issued Baker a highly unusual and arguably notorious type of claims-made coverage in which each successive policy re-set the retroactive date to the start of the new policy period. Thus, the 2019 policy covered

Baker for claims made in the 2019 policy period, but only for conduct occurring in that same period; and then the 2020 policy covered Baker for claims made in the 2020 policy period, but only for conduct occurring in *that* period; and so forth. This has been called *nonretroactive* claims-made coverage, because no one policy renewal ever responds to conduct which occurred before its policy period.

When this style of coverage was first introduced in the 1980s, it was met with alarm among commentators and indeed courts, because it is well known to professionals in the claims business that it is highly unrealistic and ultimately fortuitous to expect claims to both arise and be formally presented all within a given 12-month period. PCIC seeks to revive a style of coverage that is unrealistic and fundamentally dangerous to policyholders, because it gives the appearance of providing coverage for the policyholder's operations for the periods for which the insurance is purchased, without actually doing so.

Worse, because the concept of the "retroactive date" is unfamiliar even to many legal professionals, let alone the insurance-buying public, the extremely limited nature of nonretroactive claims-made coverage is not readily apparent to policyholders. They typically learn about the limited nature of their coverage only when it does not respond to a claim based on events occurring while they had insurance, made while they had insurance, and made well within the applicable statutory limitations period.

In the present case, the statutory requirement that contractors carry insurance to respond to claims, RCW 18.27.050, presents a clear basis for this Court to hold that the insurance PCIC sold to Baker does not meaningfully meet the requirements of the statute, and so violates Washington's declared public policy.

IV. ARGUMENT

A. The PCIC Coverage Trigger Creates a Latent Coverage Gap that is Inconspicuous to the Purchaser of Insurance.

PCIC argues that courts applying Washington law have "affirmed the applicability of retroactive dates in claims-made policies." Resp't Br. at p. 12. But PCIC's argument that claims-made policies are valid *in general* fails to account for the highly unusual nature of the policies PCIC sold Baker. As Cox has already pointed out, the cases PCIC cites as upholding claims-made policies with retroactive time limitations provided coverage stretching back over a many-year period. Cox's Reply Br. at p. 8 n.2.

In contrast, because each successive PCIC policy sold to Baker required both the occurrence of an injury and a related claim to occur within the same policy period, Baker could appear to purchase coverage spanning both 2019 and 2020 yet not have coverage doing so. The coverage gap exemplified by the facts in this case represents a trap that was met with

immediate criticism in the insurance industry from the first days of claims-made policies.

In the mid-1980s, the ISO[1] introduced a new commercial general liability form that for the first time included a claims-made provision. Carolyn M. Frame, "Claims-Made" Liability Insurance: Closing the Gaps with Retroactive Coverage, 60 Temp. L.Q. 165, 173 (1987). In the same period, the ISO added terms establishing "a retroactive date which allows insurers to exclude coverage for occurrences that have transpired before a particular date." *Id*. However, the intended practice at the time was that, "[i]n most cases, the insurer will designate the effective date of the insured's *first* claims-made policy as the retroactive date." *Id*. (emphasis added).

[1] "The Insurance Services Organization ('ISO') is an association of domestic property and casualty insurers. One of the ISO's services is to develop standard policy forms for member insurers." *E.I. du Pont de Nemours & Co. v. Admiral Ins. Co.*, 711 A.2d 45, 52 (Del. Super. Ct. 1995).

The reason for this practice becomes clear if the Court considers the effect it would have in this case. If PCIC had commenced insuring Baker with the 2019 policy, for claims reported *and occurring* in 2019, and then continued the coverage in a subsequent 2020 policy for claims reported in 2020 *but still using the original 2019 policy as the retroactive date*, then Baker would have been covered. What stirred controversy in the 1980s was the possibility that insurers would do exactly what PCIC attempts in this case, and sell sequential *nonretroactive* claims-made policies, because "[a] nonretroactive claims-made policy, [] can cause *severe gaps in coverage for the insured*." Frame, 60 Temp. L.Q. at 184 (emphasis added).

When ISO proposed new claims-made forms, policyholder-side insurance brokers immediately called out ways in which insurers could unfairly game the new language. For example, if the insured learned of and reported facts which could lead to a claim, but the injured party had not made the

claim at the time of the policy renewal, the insurer could condition the issuance of a renewal policy on a new retroactive date bypassing the potential claim. *Id*. at 184 n.126 (citing Donahue, Undecided Regulators Hear Pros, Cons of ISO's Claims-Made Policy, National Underwriter Prop. & Cas. Ins. Ed., Aug. 2, 1985, at 39, col. 2 & 3.). PCIC's successive nonretroactive policies effectively did this automatically.

It was the limited retroactive coverage that caused the court to hold a policy violated public policy in *Sparks v. St. Paul Ins. Co.*, in which the court explained:

> [The policy] provides neither the prospective coverage typical of an "occurrence" policy, nor the retroactive coverage typical of a "claims made" policy. During the first policy year, coverage was limited to acts of malpractice that occurred, were discovered, and were reported to the insurance company during the same year. Although there was slight retroactive coverage during the second and third renewal years of the policy, the retroactive coverage was significantly more limited than that contemplated in the standard "claims made" policy. See S. Kroll, *supra*, 13 Forum at 843, 850, 854 (1978); D. Shand, "'Claims Made' vs 'Occurrence,'" 27 Int'l Ins. Monitor 269, 270, 273 (1974); D. Shand, "Is Your

> Policy on a 'Claims Made' Basis?," The Weekly Underwriter, Sept. 15, 1973, at 8; J. Parker, *supra*, 1983 Det.C.L.Rev. 25, 27 & n. 3.

495 A.2d 406, 410 (N.J. 1985). What is compelling about the *Sparks* analysis is that the PCIC policies issued to Baker were *even more* restrictive than the policy in *Sparks*. In *Sparks*, the insurer followed the practice of using as the retroactive date the time it first provided coverage in a succession of claims-made policies. 495 A.2d at 408. Thus, the coverage "gap" the court found to be violative of public policy was that the original policy provided "no retroactive coverage whatsoever during its first year." *Id*. This contrasted with the retroactive coverage provided by a "standard 'claims made' policy," which the court upheld as valid in a companion case. *Id*. (citing *Zuckerman v. National Union Fire Ins. Co.*, 495 A.2d 395, 397 (N.J. 1985)).

Sparks was not absolute in its condemnation of nonretroactive claims-made policies, but left open the possibility that the insurer could produce evidence that the parties specifically bargained for such a policy with an

understanding as to its limitations. As a result, *Sparks* established a "presumption" that a claims-made policy lacking retroactive coverage is invalid, which can be rebutted by "proof that the terms of the policy were specifically understood and bargained for by the insured." Kenneth F. Oettle, Zuckerman and Sparks: The Validity of "Claims Made" Insurance Policies As A Function of Retroactive Coverage, 21 Tort & Ins. L.J. 659, 665-66 (1986).

Thus, from the introduction of claims-made policies, courts and commentators responded with alarm that successive, nonretroactive claims-made policies would create "severe gaps in coverage." Frame, 60 Temp. L.Q. at 184. One commentator described this as a "forfeiture risk," because the new combination of coverage triggers created "the potential that in some circumstances even an insured who maintains continuous unaltered coverage with the same insurer may find that fortuities of timing of some of the events in the tort liability sequence mean that none of those policies has been triggered."

Bob Works, Excusing Nonoccurrence of Insurance Policy Conditions in Order to Avoid Disproportionate Forfeiture: Claims-Made Formats As A Test Case, 5 Conn. Ins. L.J. 505, 511 (1999).

Since these alarms were sounded in the 1980s, insurers have generally not sought to test the validity of nonretroactive claims-made policies in court. This explains why PCIC fails to point to any decisional law broadly supporting such coverages. To the contrary, PCIC relies on case law upholding claims-made policies *generally*, with retroactive dates that would *meet* the *Sparks* test of providing reasonable retroactive coverage. PCIC's cited case law provides *no defense* for the "severe gaps in coverage" resulting from the form of policies it sold.

Just as was true when the industry first flirted with these types of forms in the 1980s, it is no less true today that the coverage gaps they create are inconspicuous to the average lay purchaser of insurance. Baker purchased successive liability policies apparently providing coverage over the periods of the

successive renewals. As with other such policies, "these policies are comprehensive general liability policies, and the average purchaser would expect broad coverage for liability arising from business operations." *Queen City Farms, Inc. v. Cent. Nat. Ins. Co. of Omaha*, 126 Wn.2d 50, 78, 882 P.2d 703 (1994). An insurer may limit its liability on such policies only "so long as it does so with clear language." *Cook v. Evanson*, 83 Wn. App. 149, 153, 920 P.2d 1223 (1996). These standards are foundational to insurance law, for, as Judge Learned Hand explained, the policy "was to go to persons utterly unacquainted with the niceties of [] insurance, who would read it colloquially," and "[i]t is the understanding of such persons that counts." *Gaunt v. John Hancock Mut. Life Ins. Co.*, 160 F.2d 599, 601 (2d Cir. 1947). PCIC's policies fail to meet these standards, because they do not clearly convey to the insured the coverage gap resulting from reliance on successive nonretroactive claims-made policies.

B. PCIC's Policies Violate Washington's Declared Public Policy.

Against the backdrop of these policy forms having been decried when first marketed forty years ago, PCIC's sale of them to Baker ostensibly to satisfy Baker's statutory insurance obligation now gives this Court its first opportunity to assess whether these policy forms comport with Washington's declared public policy.

Under this Court's case law, "limitations in insurance contracts which are contrary to public policy and statute will not be enforced." *State Farm Gen. Ins. Co. v. Emerson*, 102 Wn.2d 477, 481, 687 P.2d 1139 (1984). The Court is "careful to look to a particular statute to guide it in defining public policy." *Mendoza v. Rivera-Chavez*, 140 Wn.2d 659, 663, 999 P.2d 29 (2000).

Under RCW 18.27.050(1), a contractor must, as part of registering with the Department of Labor & Industries, furnish proof of "insurance or financial responsibility" in the amount of

"one hundred thousand dollars for injury or damage including death to any one person." If the insurance ceases to be in effect, the contractor's license is "automatically" suspended, RCW 18.27.050(2), and failure to properly register as a contractor is a crime, RCW 18.27.020(2). The class of persons protected by the statute are those who have suffered injury, damage, or death because of the negligence of a licensed contractor, and the protection the statute intends to provide is financial liquidity to answer claims. The federal court record discloses that Baker obtained this coverage by responding to an internet advertisement and being specifically assured that this policy satisfied Baker's insurance requirements under Washington law. Declaration of Gary L. Baker, *Preferred Contractors Ins. Co., Risk Retention Grp., LLC v. Baker and Son Constr. et al*., No. 2:32-cv-05016-RJB, Document 28 (May 6, 2021) at pp. 1-2.

Regarding the public policy analysis, this *amicus* focuses on one point: the holding of *Sparks*, which invalidates

insurance policy limitations identical to those at issue here, is entirely consistent with this Court's law of public policy applicable to insurance contracts. To the extent PCIC argues that *Sparks* is inapplicable merely for the reason that New Jersey has applied a "reasonable expectations" test in interpreting insurance contracts whereas this Court has not, Resp't Br. at p. 26, this is an insufficient basis to avoid the *Sparks* analysis.

In explaining that the nonretroactive claims-made policy was "violative of [] public policy," 495 A.2d at 414, *Sparks* focused on the policy's providing "only minimal protection against professional liability claims"; its defining the coverage "so narrowly" that it was "incompatible with the objectively reasonable expectations of purchasers of professional liability coverage"; such that the ultimate result was leaving "such unrealistically narrow coverage to professionals, and, derivatively, to the public they serve," that the policy amounted to a "broad injury to the public at large." *Sparks*, 495 A.2d at

414. The policy did not meet reasonable expectation because it did not fit the "realities" of professional liability claims (in that case against lawyers) which seldom both occur and are made all within a one-year policy period.

The PCIC policies in this case, with their hidden gaps in coverage, fail in all the same ways to realistically cover Baker for its potential liabilities and to reliably provide the protection the statute intended for Cox. When Cox's death ensued, Washington law afforded three years to his estate to present claims. *Deggs v. Asbestos Corp. Ltd.*, 186 Wn.2d 716, 722, 381 P.3d 32 (2016). The nonretroactive claims-made PCIC policies fail to allow Baker to answer claims for "injury," "damage," or "death" as intended by RCW 18.27.050(1). This Court has recognized that the interests of an injured claimant such as Cox are "vitally affected" by the existence or not of coverage for an at-fault party such as Baker. *Trinity Universal Ins. Co. v. Willrich*, 13 Wn.2d 263, 271, 124 P.2d 950 (1942). While the public can see from the Department of Labor & Industries

website that a contractor has or does not have insurance, an injured claimant such as Cox cannot learn the policy period nor that the timing of making the claim could impact the applicability of the disclosed coverage. The PCIC policies do not provide Baker the liquidity, nor Cox the protections, intended by RCW 18.27.050. Yet that was the entire point of Baker's obtaining them.

The failure of the policies to realistically provide the protections intended by the statute is an "injury to the public at large" under *Sparks*, 495 A.2d at 415. It just as much, under this Court's decisions, "tend[s] clearly to injure the public health, the public morals, [t]he public confidence in the purity of the administration of the law, or to undermine that sense of security for individual rights, whether of personal liberty or of private property." *LaPoint v. Richards*, 66 Wn.2d 585, 594-95, 403 P.2d 889 (1965) (quotation omitted).

Because the PCIC policies issued to Baker fail to meaningfully fulfil the statutory aim of allowing Baker to

answer claims for "injury," "damage," or "death," RCW 18.27.050(1), they falter in a way that is analogous to other cases in which this Court found that insurance contracts fell short of the public policies expressed in statutory law. *E.g*. *Durant v. State Farm Mut. Auto. Ins. Co.*, 191 Wn.2d 1, 15, 419 P.3d 400 (2018) ("Excluding payment for palliative care from the reasonable and necessary medical expenses that are required to be paid under PIP coverage violates the public policy reflected in the statutory and regulatory scheme underlying PIP coverage, which is to fully compensate insureds for their actual damages from automobile accidents."); *Brown v. Snohomish Cty. Physicians Corp.*, 120 Wn.2d 747, 756, 845 P.2d 334 (1993) (health insurance exclusion void for undermining statutory underinsured motorist coverage); *Touchette v. Nw. Mut. Ins. Co.*, 80 Wn.2d 327, 333, 494 P.2d 479 (1972) ("The statute does not contemplate a piecemeal whittling away of liability for injuries caused by uninsured motorists.").

Finally, *Sparks* points to the appropriate relief, which is to decline to enforce the restrictive notice requirements rendering the coverage incapable of fulfilling the purposes of RCW 18.27.050, and deem the notice given to the insurer "sufficient to invoke" the coverage. 495 A.2d at 416.

RESPECTFULLY SUBMITTED this 1st day of April, 2022.

I hereby certify that this document contains 3,067 words in accordance with RAP 18.17.

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By *s/ Ian S. Birk*

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