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Washington Supreme Court Limits the Scope of the Insurance Fair Conduct Act

by Meredith Dishaw

Recently, the Washington Supreme Court narrowly interpreted the Insurance Fair Conduct Act ("IFCA"), limiting the scope of conduct that constitutes a violation under the act. In *Isidoro Perez-Crisantos v. State Farm Fire & Casualty Company*, the Court determined whether a violation of the insurance regulations under the Washington Administrative Code ("WAC") constituted a violation of IFCA. 187 Wn.2d 669 (Feb. 2, 2017). Since the enactment of IFCA, claimants have asserted that a violation the WAC provisions, even a merely technical or procedural violation, was a violation of IFCA and subjected insurers and sureties to the increased penalties under the Act, including treble damages and the claimant's reasonable attorneys' fees. The Court disagreed and held that a cause of action under IFCA could not be predicated solely on a violation of the WAC regulations. Instead, a cause of action under IFCA will only exist if there was an "unreasonabl[e] deni[al] of a claim for coverage or payment of benefits."

IFCA was enacted in 2007 to provide a first party claimant with a cause of action "to recover the actual damages sustained, together with the costs of the action, including reasonable attorneys' fees and litigation costs," if an insurer "unreasonably denied a claim for coverage or payment of benefits." RCW 48.30.015 (1). IFCA also provides increased penalties for an insurer's alleged unreasonable behavior, including an award of treble damages and reasonable attorneys' fees. *Id.* at (2)-(3). Creating some confusion, which the *Perez-Crisantos Court* addressed, IFCA provided that such increased penalties could be awarded where an insurer unreasonably denied coverage or a benefit or had "violated a rule in subsection (5) of this section...." *Id.* Subsection 5 identifies certain specific WAC provisions and states "[a] violation of any of the following is a violation for the purposes of subsections (2) and (3) of this section." *Id.* at (5).

In *Perez-Cristantos*, the insured was injured in a car accident and sought coverage under his personal injury protection ("PIP") and uninsured motorist coverage ("UIM") with State Farm. State Farm paid the limits of the PIP coverage, but did not issue any payments under the UIM policy. The insured asserted that State Farm denied coverage under the UIM policy, but State Farm responded that it merely disagreed with the insured's valuation of the claim. The claim was arbitrated and an award was issued in the insured's favor. The insured had also brought a separate lawsuit against State Farm, alleging violations of IFCA, the WAC regulations, and Washington's Consumer Protection Act ("CPA"), which was primarily stayed during arbitration. After the award, the insured amended his IFCA claim to allege "that State Farm forced him to litigate in order to get payments that were due to him," allegedly in violation of WAC 284-30-330 (7). State Farm moved for summary judgment, which the trial court granted.

This is the first time the Court had been asked to interpret the provisions of IFCA since it was enacted. The Supreme Court noted that the federal courts sitting in Washington had reached opposing conclusions on whether an IFCA claim may be predicated solely on a WAC violation. In interpreting the statute, the Court concluded that IFCA did not state that it "creates a cause of action for first party insureds... whose claims were processed in violation of the insurance regulations listed in (5)," which "strongly suggests that IFCA was not meant to create a cause of action for regulatory violations." The Court did find, however, that the statute was ambiguous and looked to extrinsic evidence, which offered conflicting evidence on the legislative intent. However, the Court found that the legislative history ultimately supported its conclusion that IFCA did not create a separate cause of action for WAC violations. The Court noted that the Washington Pattern Jury Instructions provided that a violation of the WAC regulations was a violation of IFCA, but, the Court stated that jury instructions were not the law and stated that implying an IFCA cause of action for violations of the WAC regulations is not "consistent with the legislature's intent as expressed in the actual statutory language." Further, in analyzing the specific WAC regulations identified, the Court concluded that it was unlikely that the legislature intended to create a cause of action for at least some of those regulations. The Court noted that providing an independent cause of action for a WAC violation would allow a first-party claimant to bring an IFCA claim for merely procedural or technical violations such as when an insurer paid a claim that was "not accompanied by a statement setting forth the coverage under which the payment is made," or where the insurer did not respond to a "pertinent communication from a claimant reasonably suggesting that a response was required" until the 11th working day, instead of the 10th day.

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Thus, the Court held that IFCA did not intend to create a cause of action solely for WAC violations. The Court did state that a WAC violation is "relevant to the apportioned attorneys' fees and damages associated with that derivative violation." But, before reaching that derivative violation, the insurer must have first denied a claimant's demand for coverage or benefits. However, the Supreme Court did note that a violation of a WAC regulation would establish an unfair act which occurred in trade or commerce, two of the requirements to establish a CPA claim. Nevertheless, the *Perez-Crisantos* decision would seem to provide insurers and sureties with some flexibility in investigating and resolving a claimant's demand for coverage or benefits under the WAC regulations without a looming threat of an IFCA violation for mere technical or procedural violations of the WAC regulations. Insurers and sureties must still timely and fully investigate and strive to comply with their duties under Washington's statutory and common law, but this opinion does clarify that any alleged technical violations of the WAC regulations do not amount to an IFCA claim.

Washington State *Legislative Alert:* 2017 Regular Session

by Paul Friedrich

On January 17, 2017, the Senate introduced Bill No. 5222 for referral to the Committee on Commerce, Labor & Sports for consideration. Senate Bill 5222 proposes changes to Washington's retainage statute, RCW 60.28.011(6), which would require a contractor on a public improvement project, at the request of a subcontractor, to submit a bond to the public owner of the project for the portion of the prime contractor's retainage that pertains to the subcontractor.

This proposed legislation is notable because Washington's retainage statute can become a trap for sureties issuing Release of Retainage bonds in the context of a public works contract. As a result of 2009 legislative amendments to RCW 60.28.040, sureties issuing Release of Retainage bonds are exposed liability for tax claims on non-bonded projects. Furthermore, the 2009 amendments to RCW 60.28.040 subordinated sureties' ability to recover, by way of subrogation, retainage funds from a public owner to offset losses.

As a result of the 2009 legislative amendments, the priority of liens on the retainage fund, pursuant to RCW 60.28.040, is as follows:

(1) Employees for unpaid prevailing wages;

(2) Department of Revenue for all taxes, increases and penalties owed by the contractor under Title 82 RCW on the current public works project;

(3) Department of Revenue for all other taxes, increases and penalties owed by the contractor under Title 82 RCW;

(4) Department of Labor & Industries and the Employment Security Department for all taxes, increases and penalties due under Title 50 and 51 RCW on the current public works project;

(5) Statutory Lien Claims; and

(6) All other taxes, increases and penalties due and owing from the contractor to the Department of Labor & Industries and Employment Security Department on other public works projects.

Effectively, under the 2009 amendments to RCW 60.28.040, the Department of Revenue now has stepped in front of other statutory lien claimants and is entitled to recover taxes and penalties owed by the prime contractor on any other projects. Thus, a surety's possible subrogation claims are now subordinate to multiple tax claims from three state agencies and a surety's release of retainage bond is now subject to tax claims from state agencies on the principal's other non-bonded projects.

The proposed changes to the current retainage statute, RCW 68.28.011 are being advanced by subcontractor trade groups. If enacted, sureties will be called upon to issue a growing number of Release of Retainage bonds. Going forward, sureties should exercise caution before issuing Release of Retainage bonds given the increased exposure to tax claims on the principal's non-bonded projects, pursuant to RCW 60.28.040, and sureties' diminished subrogation rights.

We will continue to monitor the proposed bill and any other bills that may impact the surety industry.

UPCOMING EVENTS

WESTERN STATES SURETY CONFERENCE

Williams Kastner is pleased to be participating in the 2017 Western States Surety Conference. This program addresses a variety of interesting and timely topics including presentations on indemnity, specific bond language issues, financing, computer data mining, subcontractor default insurance products, and controlled insurance programs. There will also be a site televisit to the Washington Supreme Court and, back by popular demand, there will be a construction panel discussing progress on a large local public works project.

The program will feature a number of presentations and panels comprised of surety industry professionals and practitioners. Every attendee will receive a copy of the 2017 Quick Reference Guide to Western States Surety Law, in addition to the written program materials.

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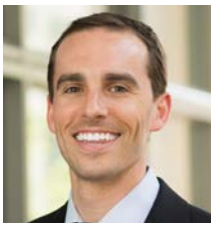

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