Covenant Judgment Found Unreasonable by Washington Federal District Court

Despite the challenges facing carriers in Washington when disputing the reasonableness of a covenant judgment, Soha & Lang, P.S. attorneys have once again obtained a judicial determination that a stipulated covenant judgment settlement was unreasonable.

On January 9, 2012, Federal District Court Judge John Coughenour ruled that a $5.75 million covenant judgment settlement of a condominium construction defect lawsuit was unreasonable, that the reasonable settlement value of all of the plaintiff homeowners association's claims was $1,921,525.70, and that the value of the association's breach of fiduciary duty claim, the only potentially covered claim, was $300,000.[i]

Applying the first of the factors identified in *Chaussee v. Maryland Cas. Co.*,[ii] the releasing party's damages, Judge Coughenour first considered the association's cost of repair claim. Judge Coughenour found that the defense repair estimate prepared by McBride Construction, which was about $1.8 million less than the association's estimate, was more reasonable than plaintiff's repair cost estimate prepared by Charter Construction. The court also reduced the association's loss of use claim from $963,012 to $96,000—a reduction of over 90%—and reduced the association's attorney fee claim by about 65%. As a result of the court's adjustments, the amount of the association's damages was reduced from $8,463,679 to $4,270,057 before the court applied the remaining *Chaussee* factors.

Judge Coughenour then discussed several of the remaining *Chaussee* factors, including the merits of the association's liability theories, the merits of the defense theories, and the defendants' ability to pay. Based upon the weaknesses in the association's legal theories, evidentiary problems with the association's case, and the defendants' lack of material assets to satisfy a judgment, the court applied a 55% reduction to the association's adjusted damage claim of $4,270,057 to arrive at $1,921,525.70 as the reasonable settlement value of the all of the association's claims.

Recognizing that the association's breach of fiduciary duty claim was the only potentially covered claim, Judge Coughenour separately addressed this claim's value The association argued that the measure of damages for this claim was the cost of repair. However, Judge Coughenour expressed doubt that any alleged breach of fiduciary duty by the developer-appointed pre-turnover board *caused* water damage to the complex. Moreover, citing *Water's Edge Homeowners Ass'n v. Water's Edge Assocs.*,[iii] the court held that the cost of repair is not the proper measure of damages for a breach of fiduciary duty claim. Based upon evidence presented by the intervening insurers represented by Soha & Lang, P.S., the court held that the reasonable value of the only potentially covered claim was $300,000.

Judge Coughenour's analysis reflects further recognition by Washington courts that stipulated settlements involving judgment-proof defendants raise concerns about the reasonableness of such settlements. The court explained that because of the defendants' lack of material assets, the defendants did not have incentive to obtain the best possible settlement amount. Accordingly, the court held that the "final settlement amount must be discounted to reflect this reality."

[i] *Aspen Grove Owners Ass'n v. Park Promenade Apartments, LLC et al.*, No. CV09–1110 (W.D.Wash. Jan. 9, 2012). Soha & Lang, P.S. attorneys Tyna Ek, Mary DeYoung, and Paul Rosner represented the intervening insurers.

[ii] 60 Wn. App. 504, 803 P.2d 1339 (1991).

[iii] 152 Wn. App. 572, 216 P.3d 1110 (2009).