No. 94246-3

SUPREME COURT
OF THE STATE OF WASHINGTON

MUTUAL OF ENUMCLAW INSURANCE COMPANY,

Respondent/Cross-Petitioner,

v.

MYONG SUK DAY, dba STOP IN GROCERY,

Petitioner/Cross-Respondent.

DAY'S ANSWER TO CROSS-PETITION FOR REVIEW

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A. Introduction.

Petitioner Myong Day asks this Court to deny respondent Mutual of Enumclaw's cross-petition, which presents no grounds for review under RAP 13.4(b). The Court of Appeals correctly held that MOE was not entitled to instructions on reformation, an issue that was separate and distinct from Day's claim of bad faith, because, by MOE's stipulation, all factual issues concerning Day's right to reform the insurance contract were tried to the court without a jury. The Court of Appeals did not abuse its discretion in refusing to consider under RAP 2.5(a) MOE's argument, raised for the first time on appeal, that emotional distress damages are unavailable under the Insurance Fair Conduct Act, RCW 48.30.015. And because this Court has rejected MOE's argument that an insured's remedies for the tort of bad faith are available only where the insurer has breached its duty to defend, MOE's conditional request for review should also be denied.

B. Argument Why MOE's Cross-Petition Should Be Denied.

1. The jury should not have been instructed on reformation, which was an issue for the court.

MOE breached its good faith duty to investigate Day's right to liquor liability coverage. MOE mischaracterizes its bad faith

investigation of Day's right to coverage in arguing that the jury was charged with "evaluating an insurer's investigation of a reformation claim." (Answer 13) The jury in this case was properly instructed on the elements of the tort of insurance bad faith, not contract reformation. The Court of Appeals correctly held that the trial court "adequately instructed the jury on the requirements for a showing of bad faith and the elements Day was required to prove to establish bad faith." (Op. 8) The separate issue of contract reformation "was a theory reserved to the trial court." (Op. 7)

The jury found MOE liable for bad faith based on substantial evidence that it failed to "fully inform the insured of all developments relevant to policy coverage" and "demonstrate[d] a greater concern for the insurer's financial interest than for insured's financial risk." (CP 1753) *See Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 715 P.2d 1133 (1986).[1] MOE put its own interests above its insured Day's when it failed to apprise her that her oral request to MOE's agent to obtain the same liability coverage her seller had was enough to bind MOE to provide liquor liability coverage. MOE breached its duty to investigate the coverage Day

[1] MOE's cross-petition relies upon an improper recital of the "facts" in a light most favorable to it, contrary to both the jury's verdict and the trial court's findings on reformation. (CP 2377-82)

requested and to which she was entitled in 2003 under its own standards, not under a standard for contract reformation.

MOE's contention that reformation is the *"only* basis" for a court to "alter[] the content of a policy of insurance" (Answer 14) (emphasis added), ignores Day's theory of the case and the jury's verdict. MOE's refusal to inform Day of her agent's authority to bind MOE deprived Day of her ability to obtain liquor liability coverage when she was sued, as MOE's own director conceded. (11/20 RP 33-36, 68) Rather than investigating Day's right to indemnity and covering the claim against her, MOE maintained its reservation of rights, requiring Day to bring an action for reformation in which she was held to an onerous clear and convincing burden of proving mutual mistake.

MOE's Claims Director conceded at trial that had it investigated and found evidence that Day had asked for liquor liability coverage in 2003, MOE would have removed the reservation of rights and covered the claim against her without a court decree of reformation. (11/19 RP 113) MOE would have covered the claim based on less than a preponderance of the evidence because where there is uncertainty regarding coverage, "the benefit of the doubt [goes] to the policyholder." (11/19 RP 114)

And the trial court found, in assessing Day's separate claim for reformation, that Day would have prevailed under a preponderance of the evidence standard because "Ms. Day probably did, at least indirectly, request liquor liability coverage by asking Mr. Huh to write the same policy for her as he had done for Mr. Kim." (FF 7, CP 2381)

MOE's proposed "instructions that elucidated the true nature of a reformation claim" (Answer 14-15) had no bearing on the issue of MOE's good faith.[2] The issues for the jury did not require it to find a temporary "binder" under RCW 48.18.230 (CP 1715), or whether the statute of frauds, RCW 48.18.190, applied (CP 1716), but whether MOE's own actions deprived Day of a right to coverage under MOE's own internal policies. (12/3 RP 52-53, 62)

Jury instructions are sufficient if they "(1) allow each party to argue [its] theory of the case, (2) are not misleading, and (3) when read as a whole, properly inform the trier of fact of the applicable law." *Caruso v. Local 690, Int'l Bhd. of Teamsters,* 107 Wn.2d 524, 529, 730 P.2d 1299 (1987). The Court of Appeals correctly held that "[t]he trial

[2] This issue presents no grounds for review to this Court for the additional reason that MOE did not take formal exception when the trial court declined to give its proposed instructions relating to the statutory requirements for binders or the common law requirements for reformation or modification of written contracts. (12/3 RP 49-58)

court focused on the instructions necessary to argue the theories presented." (Op. 8) That holding comports with settled law and presents no issue of substantial public concern. RAP 13.4(b)(1), (2), (4).

2. The Court of Appeals' discretionary refusal under RAP 2.5(a) to address a damages issue raised for the first time on appeal presents no issue for review.

In the trial court, MOE agreed that the jury could award Day damages for her "fear, aggravation or distress" (CP 1755), and compensate her "for such fear, aggravation, or distress as you find were proximately caused by [MOE]'s failure to act in good faith and/or violation of the Insurance Fair Conduct Act." (CP 1758; *see* 12/3 RP 80-81) MOE argued for the first time in the Court of Appeals that IFCA does not authorize an award of damages for emotional distress. The Court of Appeals did not abuse its discretion in declining to address MOE's new argument "[b]ecause this issue was not preserved for appeal." (Op. 8 & n.53, citing RAP 2.5(a)).

The Court of Appeals' refusal to review an issue that was never brought to the attention of the trial court presents no issue for review by this Court. MOE concedes that the appellate court had discretion to decline consideration of an issue raised for the first time on appeal. (Answer 18) *See* RAP 2.5(a) ("appellate court may refuse to review any claim of error which was not raised in the

trial court."). MOE's various justifications for failing to raise the issue in the trial court are without merit, and, in any event do not demonstrate the Court of Appeals' abuse of discretion.

First, the Court of Appeals correctly rejected MOE's contention that it could not raise its new argument because cases supporting the contention that emotional distress is not "actual damages" under IFCA were first decided after entry of the trial court judgment here. (Op. 8, n.51).[3] Second, MOE's excuse that "the issue of culling out damages that were only related to emotion distress for trebling was not directly presented at the trial court" (Answer 17-18) further ignores that MOE agreed to the undifferentiated special verdict, which did not distinguish the damages available upon a finding of common law bad faith from those available for a violation of IFCA. (CP 1765) MOE in fact resisted a verdict form that would have required the jury to distinguish between these two claims, arguing that "there really isn't anything that could be covered in bad faith that wouldn't also be an IFCA violation." (12/3 RP 79)

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[3] MOE relied on *Schreib v. Am. Family Mut. Ins. Co.*, 129 F. Supp. 3d 1129, 1139-41 (W.D. Wash. 2015). But as the Court of Appeals noted (Op. 8, n.51), *Schreib* itself cites cases that had addressed the meaning of "actual damages" years earlier. *See, e.g., White River Estates v. Hiltbruner,* 134 Wn.2d 761, 769, 953 P.2d 796 (1998) (emotional distress damages not available under Mobile Home Landlord Tenant Act).

Third, while the Court of Appeals correctly noted that MOE's failure to raise this argument earlier deprived the trial court of "the opportunity to correct any error" (Op. 8), MOE's reversal of course once the jury awarded Day emotional distress damages also prejudiced Day. Had Day known that MOE would challenge the availability of emotional distress damages, she could have sought recovery of her out of pocket expenses incurred as a result of MOE's denial of coverage, including the costs of consulting with bankruptcy counsel. It was not an abuse of discretion to prevent MOE from trying the case on one theory and arguing another theory on appeal.

Finally, and most significantly, MOE's argument is simply wrong. Because bad faith is a tort, *Coventry Assocs. v. American States Ins. Co.*, 136 Wn.2d 269, 284, 961 P.2d 933 (1998), Washington courts have allowed recovery of emotional distress damages upon an insurer's breach of the duty of good faith. *Miller v. Kenny*, 180 Wn. App. 772, 80-02, ¶ 57, 325 P.3d 278 (2014); *Anderson v. State Farm Mut. Ins. Co*, 101 Wn. App. 323, 333, 2 P.3d 1029 (2000), *rev. denied*, 142 Wn.2d 1017 (2001). Emotional distress is compensable under other remedial statutes that authorize "actual damages." *See Rasor v. Retail Credit Co.*, 87

Wn.2d 516, 530-531, 554 P.2d 1041 (1976) ("actual damages" include emotional damages under the Fair Credit Reporting Act); *Martini v. Boeing Co.*, 137 Wn.2d 357, 367-68, 971 P.2d 45 (1999) (Washington Law Against Discrimination allows for emotional damages as part of "actual damages"). MOE's argument is contrary to the remedial purpose of IFCA.[4]

3. This Court has not distinguished the remedies available for an insurer's breach of the good faith duty to defend from those available for breach of the good faith duty to indemnify.

MOE's conditional cross-petition erroneously asserts that the remedies available for an insurer's breach of the good faith duty to indemnify are more limited than those that apply when the insurer breaches its good faith duty to defend. This Court should refuse to consider the argument because MOE never presented it to the trial court or the Court of Appeals. *Fisher v. Allstate Ins. Co.*, 136 Wn.2d 240, 252, 961 P.2d 350 (1998) (party may not raise a new issue for the first time in a petition for review). Moreover, the

[4] "The purpose of IFCA is to protect individual policy holders from unfair practices by their insurers." *Trinity Universal Ins. Co. Trinity Universal Ins. Co. of Kansas v. Ohio Cas. Ins. Co.*, 176 Wn. App. 185, 201, ¶ 31, 312 P.3d 976 (2013) (*citing* S.B. Rep. on Engrossed Substitute S.B. 5726, at 2, 60th Leg., Reg Sess. (Wash. 2007); H.B. Rep. on Engrossed Substitute S.B. 5726, at 1, 60th Leg., Reg Sess. (2007)), *rev. denied*, 179 Wn.2d 1010 (2014). Division One held that pain and suffering "constitute damages under IFCA" in *Nelson v. Geico Gen. Ins. Co.*, 192 Wn. App. 1007 at *8 (2016) (unpublished).

distinction espoused by MOE is unsupported by Washington precedent, which grants an insured coverage by estoppel and a presumption of harm where the insurer's bad faith directly implicates the duty to provide coverage and indemnify its insured, as did Day's claim against MOE.

This Court has rejected MOE's argument that the remedies available for bad faith – a presumption that the insured was harmed by the insurer's breach of the duty of good faith, and the insurer's liability beyond policy limits under the doctrine of coverage by estoppel – apply only where the insurer has breached its duty to defend. *Besel v. Viking Ins. Co. of Wisconsin*, 146 Wn.2d 730, 737, 49 P.3d 887 (2002). In *Besel,* the insurer failed to settle within limits. This Court rejected the argument MOE makes here, holding that the remedies for bad faith were available even though the insurer had not breached its duty to defend:

> Viking further argues *Butler's* presumption of harm should not apply because *Butler* involved a defense tendered under a reservation of rights. This is a distinction without a difference. The principles in *Butler* do not depend on how an insurer acted in bad faith.

Besel, 146 Wn.2d. at 737, citing *Safeco Ins. Co. of America v. Butler*, 118 Wn.2d 383, 823 P.2d 499 (1992).

This Court "express[ed] no opinion regarding a factual situation in which the insurer fully and satisfactorily discharges its duty to defend and only thereafter engages in bad faith conduct solely in connection with its coverage duties" in *Mut. of Enumclaw Ins. Co. v. Dan Paulson Const., Inc.*, 161 Wn.2d 903, 924, ¶ 41, 169 P.3d 1 (2007). MOE seizes on this language (Answer 19), ignoring that its bad faith conduct in this case occurred simultaneous to its decision to provide a defense under a reservation of rights while denying coverage. As in *Dan Paulson,* MOE's bad faith "conduct cannot be segregated from" its defense decision. 161 Wn.2d at 924, ¶ 41.

MOE ignores that this Court (in a case relied upon by MOE) subsequently held that that the bad faith remedies of coverage by estoppel and the presumption of harm apply unless the bad faith claim alleges "claims handling that is *not* dependent on the duty to indemnify, settle, or defend." *St. Paul Fire & Marine Ins. Co. v. Onvia, Inc.*, 165 Wn.2d 122, 132, ¶ 23, 196 P.3d 664 (2008) (Answer 19) (emphasis added). The Court of Appeals has also rejected the argument that an "insured must show actual harm" where the insurer defended its insured without reservation, but breached its duty to settle within limits. *Moratti ex rel. Tarutis v. Farmers Ins.*

Co. of Washington, 162 Wn. App. 495, 504, ¶ 13, 254 P.3d 939 (2011) (failure to settle implicates insurer's duty to indemnify), *rev. denied*, 173 Wn.2d 1022 (2012). And this Court's Pattern Jury Instruction Committee has recommended instructing a jury on the presumption of harm in insurance bad faith cases involving "a duty to defend, settle, or indemnify." 6A *Wash. Prac.*, WPI 320.01.01, Note on Use (6th ed. 2013 Supp.)

MOE's bad faith deprived Day of her right to a fair coverage determination under the proper standard, when it would have mattered the most, at the outset. As the jury found, MOE breached its core good faith duty to "fully inform the insured of all developments related to policy coverage; and [to] refrain from conduct that demonstrates a greater concern for the insurer's financial interest than for the insured's financial risk." (CP 1753) This was not a case arising from MOE's technical "claims handling," *Onvia*, 165 Wn.2d at 132, ¶ 23, but a breach of an insurer's duty to investigate its insured's right to indemnity.

C. Conclusion

This Court should grant Day's petition and deny MOE's cross-petition.

Dated this 24th day of April, 2017.

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DECLARATION OF SERVICE

The undersigned declares under penalty of perjury, under the laws of the State of Washington, that the following is true and correct:

That on April 24, 2017, I arranged for service of the foregoing Day's Answer to Cross-Petition for Review, to the court and to the parties to this action as follows:

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DATED at Seattle, Washington this 24th day of April, 2017.

Patricia Miller

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April 24, 2017 - 4:12 PM

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