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SUPREME COURT
STATE OF WASHINGTON
4/19/2019 3:07 PM
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No. 96185-9

SUPREME COURT OF THE STATE OF WASHINGTON

No. 75727-0-I

COURT OF APPEALS, DIVISION ONE
OF THE STATE OF WASHINGTON

LAZURI DANIELS, individually and on behalf of all those similarly situated,

Petitioner,

v.

STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY,

Respondent.

**STATE FARM'S RESPONSE TO *AMICUS CURIAE* BRIEF OF
WASHINGTON INSURANCE COMMISSIONER MIKE KREIDLER**

SHEPPARD MULLIN RICHTER &
HAMPTON LLP
Frank Falzetta, Cal Bar No. 125146
Jennifer M. Hoffman, Cal Bar. No. 240600
333 South Hope Street, 43rd Floor
Los Angeles, California 90071-1448
Telephone: 213-620-1780
Facsimile: 213-620-1398
ffalzetta@sheppardmullin.com
jhoffman@sheppardmullin.com

BETTS PATTERSON & MINES P.S.
Joseph D. Hampton, WSBA #15297
701 Pike Street, Suite 1400
Seattle, Washington 98101-3927
Telephone: (206) 292-9988
Facsimile: (206) 343-7053
jhampton@bpmlaw.com

Attorneys for Respondent

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I.
INTRODUCTION

The Amicus Brief submitted by Washington Insurance Commissioner Mike Kreidler (the “Commissioner”) acknowledges that his office amended WAC 284-30-393 in 2011 to be consistent with *Averill v. Farmers Ins. Co. of Washington*, 155 Wn.App. 106, 229 P.3d 830 (2010)(“*Averill*”), that the amendment was a valid exercise of his regulatory authority, and that the amended regulation applied to Ms. Daniels’ claim.

The Commissioner now urges the Court to overrule *Averill*. But overruling *Averill* will not change the fact that the regulation still exists and binds all Washington insurers. Consistent with *Averill*, current WAC 284-30-393 makes it clear that an insured will not receive a full deductible refund out of a subrogation recovery reduced for fault. WAC 284-30-393. Instead, an insurer must reimburse an insured’s deductible from any recovery “less applicable comparable fault.” WAC 284-30-393.

The Commissioner carefully considered that four-word amendment before making it law. For nearly a year, his office sought public comment, prepared draft reports, published final analyses, and held open hearings before finally adopting the amendment. (*See* CP pp. 32-36; APCIA Amicus Brief, pp. 4-5 & Appx. 3). The Commissioner took all of those

steps because Washington's Administrative Procedure Act (chapter 34.05 RCW) required it.

The Commissioner now urges the Court to construe WAC 284-30-393's four-word amendment as adding a number of affirmative requirements that do not appear in the regulation. This Court may interpret a regulation, but cannot rewrite it. Although the Commissioner has the power to revise WAC 284-30-393 so as to be consistent with his current view, in order to do so, he must comply with the procedures set forth in Washington's Administrative Procedures Act. This appeal cannot circumvent those formal procedures.

The Commissioner also advances common law and contract arguments in his Amicus Brief. But his argument that *Averill* should be overruled falters, because he bases it on a misstatement of the common law subrogation doctrine. Contrary to the Commissioner's assertions, State Farm's traditional subrogation right did not include Ms. Daniels' deductible – only WAC 284-30-393 obligated State Farm to include Ms. Daniels' deductible along with its subrogation demand. And State Farm's pursuit of its subrogation right and Daniels' deductible through arbitration with the tortfeasor's insurer in no way prevented Daniels from pursuing her entire deductible from the tortfeasor if she was dissatisfied with the recovery (which ultimately turned out to be 100% in this case).

The Commissioner’s contract argument is flawed, because it centers on a dictionary definition of “loss” that actually *supports* the Court of Appeal’s decision below. It also ignores the terms of WAC 284-30-393, which the Commissioner now contends “is in fact a part of the contract.” If the Court accepts that argument, then the policy’s “fully compensated” language cannot mean any more than payment of the collision deductible “less applicable comparable fault,” consistent with the WAC.

The Commissioner clearly desires Washington insurers to follow a different rule than that set forth in current WAC 284-30-393. He has a statutory mechanism to accomplish that result under the APA, but he cannot do so through hindsight on this appeal. State Farm followed WAC 284-30-393, its contract, and the holding of *Averill* in handling Daniels’ claim, and respectfully requests that the Court affirm the decision below.

II. **ARGUMENT**

A. The Commissioner’s Regulatory Argument Urges a Rewrite of WAC 284-30-393, Not an Interpretation of It.

The Commissioner asks the Court to construe WAC 284-30-393 as “requir[ing] full payment of all deductibles unless the carrier has determined and communicated applicable fault” of the insured to the insured, and “allowing proportional recovery of deductibles” as only an

“exception in this rule.” (Comm’r Brief, pp. 6-7). That reading would not interpret the regulation—it would rewrite it. Specifically, it would require Court to read the following italicized language into the regulation:

The insurer must include the insured’s deductible, if any, in its subrogation demands. Any recoveries must be allocated first to the insured for any deductible(s) incurred in the loss, *unless the insurer has determined that the insured bears comparable fault and communicated that fault determination to the insured, in which case the insurer must allocate any recovery first to the insured, less applicable comparable fault.*

This Court is not at liberty to do that.

General rules of statutory construction, relied upon by the Commissioner, bar courts from reading words into a regulation that are not there. *Dot Foods, Inc. v. Dep’t of Revenue*, 166 Wn.2d 912, 921, 215 P.3d 185 (2009) (rejecting the department’s interpretation of a statute as requiring the court to “import additional language into the statute”). They also instruct that substantial weight may be afforded an agency’s interpretation of a regulation only if (1) the regulation is ambiguous, (2) the interpretation does not conflict with the regulation, and (3) the interpretation is genuine. *Pub. Util. Dist. No. 1 of Pend Oreille Cty. v. Dep’t of Ecology*, 146 Wn.2d 778, 790, 51 P.3d 744 (2002); *Cowiche Canyon Conservancy v. Bosley*, 118 Wn.2d 801, 815 (1992) (“If an agency is asserting that its interpretation of an ambiguous statute is

entitled to great weight, it is incumbent on that agency to show that it has adopted and applied such interpretation as a matter of agency policy.”).

The Commissioner’s proffered interpretation of WAC 284-30-393 is not entitled to substantial weight here for at least three reasons. First, the Commissioner has not shown that it has actually adopted and applied that interpretation as a matter of agency policy. *Cowiche Canyon*, 118 Wn.2d at 815.

Second, the Commissioner has not shown, and does not contend, that the regulation is ambiguous.

Third, the Commissioner’s interpretation conflicts with the intent of the regulation, as shown by excerpts of the rulemaking file for the 2011 amendment already in the record. The Final Cost Benefit Analysis does not reflect an intent that the *insurer* determine applicable fault and reimburse an insured consistent with that unilateral determination. (CP 36). To the contrary, it explained that the 2011 amendment “clarifies that [policyholders] will not be able to receive a larger recovery of their deductible *than if they had attempted to collect directly*” and that insurers “will not have to allocate to the insured the recovery of the deductible that would be more *than what the insured would have been able to collect directly.*” (CP 34). That reflects an understanding that fault is not “applicable” until a recovery is achieved, and that fault corresponds to the

amount of the insured's deductible actually recovered from the tortfeasor (or his or her insurer), not any prior fault determination made and communicated by the insurer.

That intent is also reflected in the express terms of the regulation. The Commissioner included the phrase "applicable comparable fault" in the sentence setting forth what portion of a subrogation recovery must be allocated to an insured. Given that context, the only reasonable interpretation of "applicable comparable fault" is fault applied to the subrogation recovery actually obtained, not some prior determination of fault made and communicated by the insurer and not referenced anywhere in the regulation. *Dot Foods*, 166 Wn.2d at 920 (rejecting the department's interpretation of disputed phrase by looking at what the phrase modified "in the wording of the statute").

Nothing prevents the Commissioner from amending WAC 284-30-393 again to incorporate his current view that "applicable comparable fault" refers only to fault "of the insured, as previously determined and communicated by the insurer." However, the Commissioner must follow the mechanism set forth in RCW 34.05.310 et seq. Neither he nor this Court may rewrite the regulation on this appeal. *Chi. Title Ins. Co. v. Office of Ins. Comm'r*, 178 Wn.2d 120, 144, 309 P.3d 372 (2013) ("An agency may not circumvent the APA by announcing new rules through

adjudication.”). The Court must enforce WAC 284-30-393 as written, according to its plain and unambiguous terms.

B. The Commissioner’s Common Law “Made Whole” Argument Fails.

1. The Commissioner’s regulation moots his common law argument.

The Commissioner also argues that the Court should overturn *Averill* and find that the “made whole” doctrine applies to the collision deductible subrogation context. But changing the common law will not change WAC 284-30-393, which requires an insurer to reimburse an insured’s deductible in an amount “less applicable comparable fault.”

As amici APCIA and NAMIC cogently explained in their brief, Washington insurers are duty-bound to follow the OIC’s regulations, including WAC 284-30-393. (APCIA Amicus Brief, pp. 7-8). The Court must also enforce WAC 284-30-393 as written, since no party has challenged the validity of the regulation in this proceeding, (*Id.* at p. 6), and the Commissioner has not taken any formal steps to amend WAC 284-30-393.

The regulation also supplants the equitable considerations that drove the decision in *Thiringer*. *Thiringer* explained that equitable factors should be considered in resolving issues relating to an insurer’s right of subrogation and the “made whole” rule “*unless otherwise directed by*

statutory requirements.” *Thiringer v. American Motors Ins. Co.*, 91 Wn.2d 215, 220, 588 P.2d 191 (1978) (emphasis added). This Court echoed that principle in *Brown v. Snohomish Cty. Phys. Corp.*, 120 Wn.2d 747, 845 P.2d 334 (1993), by recounting that *Thiringer* observed that “absent statutes to the contrary, courts resolved cases like the one before it by considering equitable factors....” *Id.* at 755 (emphasis added).

Here, we *do* have a controlling regulation, adopted pursuant to the Commissioner’s statutory authority, that governs the collision deductible subrogation context. The mandate of WAC 284-30-393 must, therefore, control over equitable considerations underlying *Thiringer*’s discussion of what it means to be “fully compensated.” Even if the Court overturns *Averill*, Washington insurers will still be required to reimburse an insured’s collision deductible “less applicable comparable fault” pursuant to the regulation.

2. The common law argument rests on a misstatement of Washington’s subrogation doctrine.

The Commissioner argues that *Averill* should be overruled because it “allows carriers to put their insureds in a worse position than they would be if they pursued their claims directly.” (Comm’r Brief, p. 17). The Commissioner bases that assertion on the proposition that a subrogated insurer assumes “the insured’s right to his or her full recovery, not merely

the amount of insurance payments that have already been received.”

(Comm’r Brief, p. 19). That is incorrect.

As this Court made clear in *Mahler v. Szucs*, an insurer is subrogated only to the extent of its payments to the insured. *Mahler v. Szucs*, 135 Wn.2d 398, 413, 957 P.2d 632 (1998) (“In the insurance context, the ‘doctrine of subrogation enables an insurer that has paid an insured’s loss pursuant to a policy... to *recoup the payment* from the party responsible for the loss.’ [citation] ... [U]pon payment of the loss to the insured, the property insurer would be subrogated *to the extent of its payment* to the remedies of the insured against the party that caused the loss.”)(emphasis added).

As the *Mahler* Court also recognized, State Farm and other insurers typically enforce their subrogation right to recover collision payments through intercompany arbitration¹:

The intercompany arbitration agreement is not new. Insurance companies recognized many years ago the disadvantages in costs, delay, and public relations stemming from litigation of subrogation actions among insurers. The use of arbitration to resolve such disputes occurred first in New York in 1929. A Nationwide Inter-Company Arbitration Agreement was drafted and became effective on February 1, 1952. [citation] Approximately

¹ Plaintiff acknowledges in her Complaint that “State Farm sought property damage loss from the other drivers’ applicable liability coverage” provided by GEICO. (CP, p. 2, ¶ 11).

2,000 insurance companies are signatories to the current version of the agreement.

Mahler, 135 Wn.2d at 422. *Averill* similarly involved intercompany arbitration. *Averill*, 155 Wn.App. at 109-110.

There is no basis to conclude that an insurer's pursuit of intercompany arbitration to recover a collision payment made to its insured in any way harms or prejudices the insured's right to pursue recovery of any uninsured losses against the tortfeasor. In addition, as State Farm discussed in its Supplemental Brief, courts have repeatedly rejected the proposition that an insurer's pursuit of its subrogation rights, whether through intercompany arbitration or otherwise, necessarily harms an insured's ability to recover its losses directly. (State Farm Supp. Brief, pp. 7-10) (discussing *Winkelman v. Excelsior Ins. Co.*, 85 N.Y. 2d 577, 583, 650 N.E.2d 841 (1995) and *Chandler v. State Farm Mut. Auto Ins. Co.*, 598 F.3d 1115 (9th Cir. 2010)).

Thus, the Commissioner's assertion that, "[b]ecause of *Averill*, if a carrier contractually demands the right to subrogation, they are also contractually demanding their insureds release any entitlement to recovery of their entire deductible," is incorrect. (Comm'r Brief, p. 20). Daniels does not, and cannot, claim that State Farm's pursuit of its subrogation right through intercompany arbitration prevented her from recovering her

full deductible directly. Daniels always retained the right to pursue recovery of her deductible from the tortfeasor. She just never had to do so, because State Farm ultimately refunded her *entire* deductible after successfully pursuing its subrogation demand to completion.²

The Commissioner’s argument that “*Averill* offers no principle” for its holding also fails. (Comm’r Brief, po. 19). *Averill* reasoned, as other courts have, that its result was “consistent with the purpose of the deductible.” *Averill*, 155 Wn.App. at 114; *Jones v. Nationwide Prop. & Cas. Ins. Co.*, 613 Pa. 219, 326, 32 A.3d 1261 (2011). Unlike PIP or UIM coverage, which offer dollar one coverage, collision coverage includes a deductible which “indicates the amount of risk retained by the insured.” *Averill*, 155 Wn.App. at 114. *Averill* continued:

The insurance policy shifts the remaining risk of any damages above the deductible to the insurance company. [citation] *Averill* contracted to be out of pocket for the first \$500. Farmers’ subrogation interest was for the amount of the loss it paid *Averill*, not including the deductible amount. When Farmers pursued its subrogation interest, that interest did not include *Averill*’s deductible. Allowing *Averill* to recover her deductible from Farmers’ subrogation recovery would have changed the insurance

² Plaintiff alleged in her Complaint that State Farm initially received funds from GEICO “representing approximately 70% of the cost to repair Plaintiff’s vehicle.” (CP, p. 2, ¶ 11). Plaintiff’s counsel later conceded at oral argument before the Court of Appeal that GEICO ultimately agreed to pay the remaining 30% when Plaintiff was determined not to be at fault. (State Farm’s Answer to Petition for Review, Appendix 1, p. 7).

contract to one without a deductible. We are not at liberty to rewrite the policy in this manner.

155 Wn.App. at 114.

Averill thus recognized both that a subrogating insurer has no right to pursue an insured's deductible under the common law, and that an insured who receives payment of the collision loss less the deductible has received the full benefit of the collision coverage they purchased. The Pennsylvania Supreme Court reached the same conclusion in *Jones*:

[T]he deductible in a collision coverage policy is a 'thin layer of first dollar liability retained by the consumer (and specifically not transferred to the insurer) to ensure risk-sharing and loss-avoidance. [citation] The insurer, thus, accepted only the risk of paying if the loss exceeded the amount of the deductible, with premiums calculated based upon the amount of first dollar liability accepted by the insured. Application of the made whole doctrine in such a case would force the insurer essentially to cover the risk of the deductible where the insured has not paid premiums to cover that risk. It follows that the insured should not get preferential treatment in a collision coverage case, when he or she accepted the risk of paying the deductible in the event of an accident.

Jones, 613 Pa. at 236.

In sum, because the Commissioner bases its argument against *Averill* on a misstatement of an insurer's subrogation rights, and ignores the policy underlying *Averill*, the Court should reject it.

C. The Commissioner’s Contract Arguments are Misplaced.

1. The plain language argument rests on a flawed assumption.

The Commissioner’s plain language argument asserts that State Farm’s “fully compensated” policy language must refer to “all damages as a result of a motor vehicle accident,” because “loss” in this context must mean “the insured’s total financial detriment.”³ (Comm’r Brief, pp. 11-12). But, the Commissioner’s own authority disproves that proposition.

Specifically, the Commissioner’s authority supports that “loss” refers to an insurer’s liability under the policy, *not* an insured’s total damages. (Comm’r Brief, p. 11). According to the Commissioner, Webster’s defines “loss” as “the amount of an insured’s financial detriment ... in such a manner as to *charge the insurer with a liability under the policy*” and Black’s defines it as “the amount of financial detriment ... *for which the insurer becomes liable.*” (OIC Brief, p. 11)(emphasis added). Both of these definitions equate “loss” with an insurer’s payment obligation under the policy. Thus, the Commissioner’s authority actually supports State Farm’s position, and the Court of Appeal’s holding, that an insured is “fully compensated” for “loss” under

³ The Court of Appeal below correctly recognized that “loss” is a defined term in the policy, but is not in the record.

the policy upon payment of the State Farm's liability under the policy *i.e.* payment of the collision loss less the deductible.

That interpretation is also consistent with *Meas v. State Farm Fire & Cas. Co.*, 130 Wn.App.527, 123 P.3d 519 (2005), and *Chen v. State Farm Mutual Auto. Ins. Co.*, 123 Wn.App. 150, 94 P.3d 326 (2004), which the Commissioner ignores. As State Farm detailed in its Brief to the Court of Appeals, *Meas* involved the same language at issue here:

Our right to recover our payments applies only after the *insured* has been fully compensated for the *bodily injury*, *property damage* or *loss*.

(Respondent's Brief, p. 18)(citing *Meas*, 130 Wn.App. at 530). *Meas* complained that State Farm had violated this provision by asserting its subrogation right for its collision payment against the other driver's insurer before he received compensation for his bodily injury. He demanded that State Farm tender its entire subrogation recovery to *Meas* until all of his claims were settled. *Id.* at 531. According to *Meas*, State Farm could not yet pursue subrogation for its collision payment because he was not yet "fully compensated" for his entire loss.

Division Two of the Court of Appeals disagreed. Finding State Farm's policy language "clear and unambiguous," the court held that *Meas* was "fully compensated or 'made whole' for the property loss claimed under his collision coverage when he received payment from

State Farm.” *Meas*, 130 Wn. App. 527 at 538-539. In so holding, *Meas* interpreted State Farm’s policy language in light of the particular coverage at issue, and relied on *Mahler v. Szucs*, 135 Wn.2d 398, 957 P.2d 632 (1998), and *Chen v. State Farm Mutual Auto. Ins. Co.*, 123 Wn.App. 150, 94 P.3d 326 (2004), which did the same. *Meas*, 130 Wn.App. at 534-37. As *Meas* explained, *Chen* held “as a matter of law that State Farm’s payment for collision damages, and the insured’s acceptance of that payment, triggered the assignment of the insured’s right to recover for property damage to State Farm under the policy’s express language.” *Meas*, 130 Wn.App. at 537; *Chen*, 123 Wn.App. at 157.

Thus, as *Meas* and *Chen* reasoned, the subject policy language simply provides when State Farm’s subrogation or reimbursement rights are triggered, which may be at different times for different coverages. Indeed, the “Our Rights to Recover Our Payments” section relates to many different coverages. (CP, p. 80). Depending on the coverage, the policy provides State Farm with (i) no recovery rights, (ii) subrogation and reimbursement rights, or (iii) subrogation rights only. (*Id.*). In the *collision* context, the policy provides only a “traditional subrogation right.” *Mahler*, 135 Wn.2d at 420. And in that context, State Farm’s subrogation right arises upon payment of the collision loss, regardless of whether or when the insured has yet obtained a collision deductible

refund. *Meas*, 130 Wn.App. at 537-539. Thus, contrary to the Commissioner's assertion, State Farm has offered significant case authority supporting its and the Court of Appeal's interpretation of "fully compensated" here.

Finally, the Commissioner argues that the Court should interpret the phrases "right of recovery" and "right to recover" as having fundamentally different meanings. (Comm'r Brief, p. 13). He offers no authority in support of this proposition. Interpreting "right to recover" as referring only to State Farm's "right to keep any funds" does not make sense for at least two reasons. First, that phrase applies to State Farm's subrogation and reimbursement rights, and in the reimbursement context, State Farm has nothing to keep—it can only take from an insured's recovery from the tortfeasor. (CP, p. 80). Second, the interpretation incorrectly assumes that State Farm has the right to pursue an insured's collision deductible under the contract. The contract does not create any such right. The "Our Right to Recover Our Payments" section limits the "right to recover" to State Farm's payments, and nowhere mentions the insured's deductible. (CP p. 80). Only WAC 284-30-393 requires State Farm to include an insured's deductible in its subrogation demand. Thus, the only reasonable interpretation of the "right to recover" phrase is as a trigger of the respective right, *i.e.* when State Farm can assert a

reimbursement or subrogation right, as reasoned in *Meas* and below, not as some unspecified allocation provision.

2. **The “viewed in its entirety” argument ignores WAC 284-30-393.**

The Commissioner next argues that State Farm’s contract must be viewed in its entirety, but again does not account for WAC 284-30-393, which the Commissioner contends “is in fact a part of the contract.” (Comm’r Brief, p. 7) (citing RCW 48.18.510).

According to the Commissioner, State Farm’s policy language must be construed together with WAC 284-30-393 “for the purpose of giving force and effect to each clause.” *Morgan v. Prudential Ins. Co. of America*, 86 Wn.2d 432, 435, 545 P.2d 1193 (1976). WAC 284-30-393 expressly contemplates that an insurer will assert its collision payment subrogation right *before* an insured receives their collision deductible. It also directs an insurer to refund that deductible “less applicable comparable fault,” *not* in full.

Consistent with *Meas*, the Court of Appeal construed State Farm’s “fully compensated” language as governing when recovery rights are triggered. When considered in light of WAC 284-30-393, the Court of Appeal correctly found that the only reasonable interpretation of that

trigger provision in the collision subrogation context was “payment of the collision loss less the deductible.”

The Commissioner now contends that the “fully compensated” language should be construed as an allocation provision governing how recoveries must be shared between State Farm and Ms. Daniels. But, even if the Court accepts that argument, the phrase “fully compensated for the ... loss” in State Farm’s policy form cannot mean any more than “payment of the deductible, less applicable comparable fault” in this context, when construed together with the regulation. The Commissioner’s more expansive interpretation of “fully compensated” fails, because it would not give effect to the “less applicable comparable fault” limitation in WAC 284-30-393.

3. Sherry does not control interpretation of the policy for all the reasons discussed in State Farm’s prior briefing.

The Commissioner next argues that *Sherry’s* interpretation of “fully compensated” under the common law “made whole” governs its meaning under the contract. (Comm’r Brief, p. 15). State Farm has already briefed why *Sherry’s* common law holding in the PIP and UIM context does not control the meaning of State Farm’s policy language in the collision subrogation context, and why Washington courts interpret policy language based on the specific coverage and loss at issue.

(Respondent’s Brief, pp. 22-30). In the interest of judicial economy, State Farm refers to its prior briefing rather than repeat those arguments here. (*Id.*).

4. The “equal consideration” argument again misconstrues an insurer’s subrogation right.

Finally, the Commissioner argues that interpreting “fully compensated” to mean payment of the collision loss less the deductible prioritizes State Farm’s interests above an insured’s, and leaves an insured in a worse position. (Comm’r Brief, p. 15). That argument fails because it is based on the same flawed assumption addressed above—that a subrogating insurer acquires the right to pursue recovery of all of an insured’s losses.

State Farm has no contractual or common law subrogation right to pursue an insured’s uncovered losses, including a collision deductible. Only WAC 284-30-393 creates that obligation. That regulation also requires an insurer to reimburse a deductible on a proportionate basis consistent with its own subrogation recovery reduced for fault. Under the regulation, State Farm gives the insured the amount of the deductible it successfully recovers from the tortfeasor—the same amount the insured would have recovered had he or she pursued that recovery directly.

III.
CONCLUSION

For all of the foregoing reasons, and those detailed in its Supplemental Brief to this Court, its Respondent's Brief to the Court of Appeal below, and its briefing in the trial court, State Farm respectfully requests that the Court affirm the judgment of the Court of Appeal.

RESPECTFULLY SUBMITTED this 19 day of April, 2019.

BETTS, PATTERSON & MINES, P.S.

By /s Joseph D. Hampton
Joseph D. Hampton, WSBA #15297
Attorneys for Respondent
State Farm Mutual Automobile Insurance Company

SHEPPARD MULLIN RICHTER & HAMPTON, LLP

By /s Jennifer Hoffman
Frank Falzetta, *admitted pro hac vice*
Jennifer Hoffman, *admitted pro hac vice*
Attorneys for Respondent
State Farm Mutual Automobile Insurance Company

BETTS, PATTERSON & MINES, P.S.

April 19, 2019 - 3:07 PM

Transmittal Information

Filed with Court: Supreme Court
Appellate Court Case Number: 96185-9
Appellate Court Case Title: Lazuri Daniels v. State Farm Mutual Automobile Insurance Company
Superior Court Case Number: 16-2-08824-4

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