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**SUPREME COURT  
STATE OF WASHINGTON**

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CERTIFICATION FROM UNITED STATES COURT OF APPEALS FOR THE  
NINTH CIRCUIT IN:

AFFILIATED FM INSURANCE COMPANY, a Rhode Island corporation,

Plaintiff-Appellant,

v.

LTK CONSULTING SERVICES, INC., a Pennsylvania corporation,

Defendant-Appellee.

U.S.D.C. W.D. Wa. Case No. CV-06-01750-JLR  
Ninth Circuit Case No. 07-35696

*Plaintiff*  
**OPENING BRIEF OF APPELLANT  
AFFILIATED FM INSURANCE COMPANY**

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## TABLE OF CONTENTS

I.	ASSIGNMENTS OF ERROR.....	1
II.	STATEMENT OF THE CASE.....	1
	A. Procedural Background.....	1
	B. Factual Background.....	
III.	LEGAL ARGUMENT.....	12
	A. Affiliated FM's Insured Possessed a Sufficient Legal Interest in the Monorail at the Time of the Fire To Sue LTK in Tort.....	12
	B. The "Economic Loss Doctrine" Does Not Apply In This Case.....	20
	C. Economic Loss Doctrine in Other States.....	31
IV.	CONCLUSION .....	35

## TABLE OF AUTHORITIES

### Cases

<i>Alejandre v. Bull</i> , 159 Wn.2d 674, 153 P.3d 864 (2007).....	24
<i>Atherton Condominium Apartment – Owners Association v. Blume Development Co.</i> , 115 Wn.2d 506, 799 P.2d 250 (1990).....	30
<i>Baddeley v Seek</i> , 138 Wn. App. 333, 156 P.3d 959 (2007).....	22
<i>Barnett v. Lincoln</i> , 162 Wash. 613, 299 Pac. 392 (1931).....	14
<i>BerschauerPhillips Construction Co. v. Seattle School District No. 1</i> , 124 Wn.2d 816, 881 P.2d 986 (1994).....	29
<i>Carlson v. Sharp</i> , 99 Wn. App. 324, 994 P.2d 851 (1999), <i>review denied</i> , 141 Wn.2d 1024 (2000).....	23
<i>Casa Clara v. Charley Toppino and Sons, Inc.</i> , 620 So.2d 1244 (Fla. 1993).....	33
<i>CLS Mortgage v. Bruno</i> , 86 Wn. App. 390, 937 P.2d 1106 (1997).....	19
<i>Erich v. Menezes</i> (1999) 21 Cal.4 <sup>th</sup> 543, 87 Cal.Rptr. 886, 981 P.2d 978.....	31
<i>J’Aire Corporation v. Gregory</i> (1979) 24 Cal.3d 799, 157 Cal.Rptr. 407, 598 P.2d 60.....	31
<i>Miller v. U.S. Steel Corp.</i> , 902 F.2d 573 (CA7 1990).....	28,29
<i>Moransais v. Heathman</i> , 744 So.2d 973 (Fla. 1999).....	34
<i>Nobl Park, LLC of Vancouver v. Shell Oil Co.</i> , 122 Wn. App. 838, 95 P.3d 1265 (2004).....	24
<i>Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.</i> , 652 F.2d 1165 (CA31981).....	25
<i>Robinson v. Avis</i> , 106 Wn. App. 104, 22 P.3d 818 (2001).....	21
<i>Seely . White Motor Co.</i> (1965) 63 Cal.2d 9, 45 Cal.Rptr. 17, 403	

P.2d 145.....	31
<i>Shekhter v. Seneca Structural Design, Inc.</i> (2004) 121 Cal.App.4 <sup>th</sup> 1055, 18 Cal.Rptr. 83.....	31
<i>Staton Hills Winery Co. v. Collons</i> , 96 Wn. App. 590, 980 P.2d 784 (1999).....	26
<i>Stuart v. Coldwell Banker Commercial Group, Inc.</i> , 109 Wn.2d 406, 745 P.2d1284 (1987)....	24,29,30
<i>Touchet Valley Grain Growers, Inc. v. Opp &amp; Seibold Gen. Constr., Inc.</i> , 119 Wn.2d 334, 831 P.2d 724 (1992).....	24
<i>Washington Water Power Co. v. Graybar Elec. Co.</i> , 112 Wn.2d 847, 774 P.2d 1199, 779 P.2d 697 (1989).....	23,25

### Statutes

RCW 2.60.020.....	5
RCW 2.60.030.....	5

### Rules

RAP 1616.....	5
---------------	---

### Treatises

Christopher Scott D'Angelo, <i>The Economic Loss Doctrine: Saving Contract Warranty Law From Drowning in a Sea of Torts</i> , 26 U. Tol. L. Rev. 591 (1995).....	28
Comments, <i>Manufacturers' Liability to Remote Purchasers for "Economic Loss" Damages – Tort or Contract</i> , 114 U. Pa. L. Rev. 539 (1966).....	29
<i>Restatement of Property</i> , §521(2)(1944).....	13

## I. ASSIGNMENTS OF ERROR

1. Did the federal district court below err in concluding the *Monorail Concession Agreement* was a license agreement as opposed to a lease agreement?

3. Did the federal district court below err in dismissing appellant's, AFFILIATED FM INSURANCE CO. ("Affiliated FM"), lawsuit against appellee, LTK CONSULTING SERVICES, INC. ("LTK"), by concluding that a license agreement to operate the Seattle Monorail was an insufficient legal interest to sustain a negligence action against defendant-appellee?

4. Did the federal district court below err in concluding the economic loss doctrine applied to the circumstances involved in this case?

## II. STATEMENT OF THE CASE

### A. PROCEDURAL BACKGROUND

The fire which forms the basis of this lawsuit occurred on May 31, 2004 and damaged the Blue and Red Trains of the Seattle Monorail as the Blue Train was leaving the Seattle Center Station that afternoon. ER 384. At the time of the fire, Affiliated FM insured the Monorail. ER 385. Affiliated FM contends in this lawsuit an electrical ground fault was responsible for causing

the fire and would have been avoided if the electrical grounding system for the Blue Train had not been changed in 2002 at the direction of LTK. LTK denies these allegations. ER 398-399.

Affiliated FM originally filed this lawsuit in King County Superior Court on November 7, 2006 alleging a single cause of action for negligence. ER 001-005. LTK removed this lawsuit to federal court on December 7, 2006. ER 006-008.

In April, 2007 LTK brought a motion for summary judgment seeking to dismiss Affiliated FM's lawsuit. ER 382-393. LTK claimed Affiliated FM's insured, Seattle Monorail Services ("SMS"), did not "own" the Monorail at the time of the fire and therefore any negligence action brought by Affiliated FM was barred by the economic loss doctrine as recognized in Washington. ER 383.

Affiliated FM responded to this motion by arguing there was no privity of contract between Affiliated FM's insured and LTK, and therefore under Washington state substantive law the damages being pursued in this case were compensable in tort, not contract. ER400. Affiliated FM also opposed LTK's motion on the grounds that the contract Affiliated FM's insured entered into with the City of Seattle in 1994 to operate the Monorail amounted to a lease agreement and therefore Affiliated FM's

insured had a sufficient legal interest in the Monorail to preclude the application of the economic loss doctrine in this case. ER 400.

The federal district court below granted LTK's motion for summary judgment. ER 422-429. The district court concluded the contract to operate the Monorail amounted to a license, not a lease, and therefore ruled Affiliated FM was barred from pursuing a tort action against LTK under the economic loss doctrine. ER 426-428. The district court further held that Affiliated FM's claim for business interruption losses was also barred by the economic loss doctrine for the same reason. ER 428.

Affiliated FM then brought a timely motion for reconsideration. ER 431-441. Affiliated FM contended the district court erred in granting LTK's motion because it had assumed, without citation to any legal authority, that a license agreement did not convey to Affiliated FM's insured a sufficient legal interest in the Monorail to allow Affiliated FM or its insured to sue LTK in tort for the damages the to the Monorail suffered as a result of the fire. ER 433.

Affiliated FM's motion for reconsideration was premised on the fact the district court considered its characterization of the

contract in question as purely a question of state law. As such, the district court should have looked to the substantive law of Washington, as announced by the Washington Supreme Court, in making this determination. ER 433. Affiliated FM observed the district court did do this in deciding whether the contract in question was a lease versus a license agreement. ER 433. After reviewing relevant Washington state legal authority, the district court decided the contract was more analogous to a license than a lease. ER 433.

However, Affiliated FM argued the district court was bound to go further in deciding LTK's motion for summary judgment. ER 434. Since LTK had the burden of demonstrating it was entitled to dismissal of Affiliated FM's negligence claim as a matter of law, LTK had the burden of demonstrating to the district court below that, under Washington substantive law, a license agreement did not convey to Affiliated FM's insured a sufficient legal interest in the Monorail to allow Affiliated FM to sue LTK in tort for property damage to the Monorail as a result of the fire. ER 434. In granting LTK's motion, the district court did not cite any legal authority to the effect that a license agreement failed to afford LTK's insured a sufficient legal interest in the Monorail to allow Affiliated FM to sue LTK in tort

for property damage to the Monorail. ER 434. Furthermore, Affiliated FM stated after careful and extended research of Washington state legal authority on this topic, it did not appear any Washington appellate court has ever addressed this specific issue. ER 434.

Consequently, in light of these circumstances, Affiliated FM argued the district court was left with two possible courses of action. First, it could certify this legal question to the Washington Supreme Court for decision. ER 434. In the alternative, the district court below could do its best to review all relevant legal authority and predict how the Washington Supreme Court would likely decide the issue if presented with it. ER 434. The district court below chose neither of these two avenues and summarily denied Affiliated FM's motion for reconsideration.

Affiliated FM consequently filed a timely notice of appeal to the U.S. Ninth Circuit Court of Appeals on August 17, 2007. Oral argument took place before a three judge panel of the Ninth Circuit on December 12, 2008. On February 17, 2009, by way of published decision, the Ninth Circuit certified this appeal to this court in accordance with RCW 2.60.010, 2.60.030 and RAP 16.16.

## B. FACTUAL BACKGROUND

Affiliated FM, in opposition to LTK's motion for summary judgment below, agreed the following facts were undisputed:

1. The Seattle Monorail is the well-known transportation system linking downtown Seattle with the Seattle Center. The Monorail includes two trains: the Red Train and the Blue Train. This lawsuit arises out of a fire that damaged the Monorail on May 31, 2004, which broke out underneath the Blue Train, causing significant damage to both trains, in addition to substantial business interruption losses. ER 395.

2. The fire broke out when Blue train's drive shaft disintegrated. In disintegrating, the drive shaft came in contact with a positive-current "collector shoe" causing an electrical fault that ignited the fire. ER 395.

3. The Monorail is owned by the City of Seattle (the "City"). On April 22, 1994, the City executed the *Monorail Concession Agreement* with Seattle Monorail Services ("SMS"). ER 395.

4. SMS agreed to assume a series of obligations, including the payment of a fee to the City and the responsibility

to provide maintenance and repair to the monorail trains, track and passenger stations. ER 395.

5. SMS's maintenance and repair obligations pursuant to the *Monorail Concession Agreement* included "emergency maintenance" when needed to bring the trains back into service following an accident. ER 395.

6. Over time, the City and SMS entered into a series of agreements amending the *Monorail Concession Agreement*. ER 395.

7. At all times relevant to this dispute, SMS carried an insurance policy issued by Affiliated FM. Pursuant to that policy, Affiliated FM paid over \$3 million to SMS for damages caused by the May, 2004 fire. In the present action, Affiliated FM seeks to recover these sums from LTK. ER 395.

8. LTK separately contracted with the City (but not with SMS) to provide the City with certain engineering services before the fire relating to refurbishment of the Monorail. ER 396.

In opposition to LTK's motion for summary judgment, Affiliated FM disputed LTK's contention that the *Monorail Concession Agreement* did not grant any property rights in the Monorail to SMS. ER 396.

Section III of the *Monorail Concession Agreement* stated:

III. GRANT OF CONCESSION RIGHTS  
TO, MONORAIL SYSTEM & ANCILLARY  
AREAS.

A. Monorail System Concession Right. The City hereby grants to the Concessionaire for the **Operating Period** and upon the conditions and provisions herein, the concession right and privilege to **maintain and exclusively operate** the Monorail System including the facilities, personal property and equipment, **together with the right to use and occupy the areas**, described in this section, all subject to the conditions and requirements set forth in this Agreement.

1. **Trains.** The two (2) Monorail System, four-unit, triple-articulated, double-ended, electric trains riding on dual pneumatic rubber traction tires with horizontal pneumatic rubber tires pressing against the sides of the guideway beam for stability and guiding.

2. **Guideway.** The approximately nine-tenths of a mile long, dual, three (3) foot wide by five (5) foot high, prestressed concrete beam guideway structure together with its supporting T-shaped II pylons approximately 25' high, which structure extends over portions of the following Seattle Center properties before it narrows to form a gauntlet track area for approximately the last tenth of a mile as the train enters the Westlake Center station... (Emphasis added).

ER 030-033.

At section V of the *Monorail Concession Agreement*, it states:

V. PAYMENTS TO THE CITY.

A. Fees and Charges. The Concessionaire shall pay to the City the concession fees and charges described in this Section V, plus any extra charges described in sections IX, X, XII, XIII, XIX, and XXII hereof. **The concession fees payable by Concessionaire hereunder represent the consideration payable for the concession to operate and to exclusively maintain the Monorail System and to operate and maintain the Westlake Center station pursuant to the Monorail Operating and Easement Agreement, as described in Subsections III.A.1, 2 and 3; and those portions of the Seattle Center Station, the Monorail System Annex and the Supplemental Storage Area described in Subsections III.A.4, 5, and 6, that are necessary or incidental to the operation and maintenance of the Monorail System; together with the consideration payable for the exclusive concession to engage in food, beverage, and merchandise wholesale and retail sales activity in and from the Monorail System, as authorized by Subsection VII.B, hereof. (Emphasis added).**

ER 034.

Section XVII of the *Monorail Concession Agreement* stated:

XVII. INSURANCE REQUIREMENTS

A. Liability and Property Damage

Insurance. **The Concessionaire shall secure and maintain during all authorized periods of use, at no expense to the city, insurance by one or more companies authorized to do business in the state of Washington, as follows:**

1. **A policy for fire and extended coverage, upset, collision and overturn, vandalism, malicious mischief, and other perils commonly included in the special coverage form. Coverage need not include earthquake and flood. This direct damage insurance shall be primary to any insurance secured and maintained by the city.** The valuation basis shall be on a replacement cost basis with no coinsurance penalty provision. The limit to be carried shall be a \$5,000,000 loss limit per loss and annual aggregate for direct physical damage to the cars, track, support system, equipment, and other improvements that are to be the subject of this insurance. The city shall be the loss payee on the direct damage insurance policy, and the Westlake Center Associates shall be named as an additional insured if such entity requires such action. .

All losses under this direct damage policy shall be adjusted jointly by the Concessionaire and the City. Any loss payable under such direct damage insurance shall be paid to the Concessionaire and the City for application to the cost of rebuilding, repairing, replacing, or restoring the Monorail System; provided, that in the event the Concessionaire elects to exercise its termination right under Section XXII.C, hereof, then the City shall be paid the portion of the insurance proceeds that is commensurate with the direct physical damage subject to the loss limit insured. Such payment shall be made to the City within

seven (7) days after receipt by the Concessionaire of the insurance proceeds or the effective date of termination, whichever is later. (Emphasis added).

ER 081-082.

In its memorandum in support of its motion for summary judgment, LTK characterized the basis for Affiliated FM's lawsuit against it as follows:

Rather, [Affiliated FM] claims that LTK recommended to the City of Seattle, as the owner of the Monorail System, to implement certain changes to the monorail grounding system, the implementation of which permitted the fault to occur when the driveshaft did disintegrate. LTK denies that it ever made such a recommendation and maintains that the grounded system - which was present on the Monorail System at the time of the accident and which remained unchanged by LTK's engagement - is the safest possible system for the application. For the purposes of this motion, LTK will assume - without conceding - that it recommended changes to the City, that those changes were implemented, and that their implementation resulted in a condition where the fault that occurred as the result of the drive shaft disintegration was not prevented.

ER 384.

## V. LEGAL ARGUMENT

### A. **Affiliated FM's Insured Possessed a Sufficient Legal Interest in the Monorail at the Time of the Fire To Sue LTK in Tort.**

LTK's motion for summary judgment was based on its contention that Affiliated FM's insured, Seattle Monorail Services ("SMS"), did not "own" (*i.e.* possess any "proprietary interest") the Seattle Monorail at the time of the fire and therefore any action brought by it or Affiliated FM was barred by the economic loss doctrine. In granting LTK's motion, the district court below concluded the *Monorail Concession Agreement*, the contract under which Affiliated FM's insured operated the Monorail, amounted to a license, not a lease, and therefore ruled Affiliated FM was barred from pursuing a claim for property damages sounding in tort against LTK under the economic loss doctrine as announced by the Washington Supreme Court.

The district court below did not cite any legal authority for the proposition that, under Washington state law, a license agreement did not convey to Affiliated FM's insured a sufficient enough legal interest in the Monorail to allow Affiliated FM to sue LTK in tort for property damage to the Monorail. No reported Washington decision has ever held a party to a contract

must possess *exclusive* control over the property that is the subject of the contract in order to sue a third party for damages to that property. The district court's decision below is also contrary to the position taken by the American Law Institute that a license agreement conveys a sufficient legal interest in property to sustain a tort action against a third party that damages that property, the situation involved in this case. *Restatement of Property*, §521(2)(1944).

Affiliated FM argued to the federal district court below that the *Monorail Concession Agreement* entered into between the City of Seattle and Affiliated FM's insured (Seattle Monorail Services) should be legally characterized as a lease. If this agreement is legally characterized as a lease, then Affiliated FM's insured (and Affiliated FM as subrogee) has more than sufficient ownership interest in the Monorail to sustain its present negligence action against LTK.

The district court below disagreed and characterized the relationship between the City of Seattle and Seattle Monorail Services as closer to that of licensor/licensee than landlord/tenant. The district court based this holding on the finding that the *Monorail Concession Agreement* did not convey "exclusive control or possession over the premises." ER 426-

427. The district court below did not explain exactly what it meant when it used the term "premises". The district court did observe the agreement gave Affiliated FM's insured the right to maintain and exclusively operate the Monorail. ER 426. However, the district court below held that the right to exclusively operate the Monorail was not sufficient to create a leasehold interest in the Monorail. ER 427.

The most authoritative case decided by the Washington Supreme Court analyzing the difference between a lease and a license is *Barnett v. Lincoln*, 162 Wash. 613, 299 Pac. 392 (1931). In the *Barnett* decision, a local taxpayer challenged the rental by the Port of Seattle of warehouse space on pier 40 along the Seattle waterfront to a canned seafood company. The propriety of the contract reached between the Port of Seattle and the canned seafood company turned on whether the contract agreed to constituted a lease versus a license. The Washington Supreme Court held the agreement reached in question constituted a lease, not a license agreement. *Id.*, 162 Wash. at 621.

Generally speaking, the court noted in the *Barnett* decision that no particular words, technical or otherwise, are necessary to constitute a lease, and the existence of the

relationship of landlord and tenant is primarily a fact question to be determined from the intent of the parties ascertained from a consideration of the entire instrument creating the tenancy. *Id.*, 162 Wash. at 617. If exclusive possession *or control* of the premises, *or a portion thereof*, is granted, even though *the use* is restricted by reservations, the instrument will be considered to be a lease and not a license. *Id.* (Emphasis added.)

In the *Barnett* decision, the Washington Supreme Court observed the agreement at issue gave the canned seafood company the exclusive right to use and possess 334,000 feet of warehouse space on Pier 40 and the preferential right to use berthing space along Pier 40. The canned seafood company was to repair all equipment, bear all operating expenses associated with the warehouse and pier, pay the Port of Seattle a tariff on all goods sold, pay for the rental of certain office space at a set rate, was for a definite period of five years and could not be assigned without the written consent of the Port of Seattle. Despite the agreement referring to itself as a preferential agreement granting certain "privileges" to the canned seafood company, the Washington Supreme Court held the agreement constituted a lease agreement, not a license. *Id.*, 162 Wash. at 621.

The district court below treated the question of whether the *Monorail Concession Agreement* constituted a lease versus a license as a question of law, not as a question of fact. The *Barnett* decision makes it plain this question is a question of fact that should be submitted to the fact finder at trial for determination. The district court consequently erred in deciding this question as a matter of law.

As the district court below itself observed, Affiliated FM's insured was given the exclusive right to operate the Monorail. ER 030. Affiliated FM's insured had the responsibility to maintain and repair the entire Monorail system (including the train tracks and passenger stations), and bear all expenses associated with doing so, including routine repairs and maintenance, emergency maintenance and even janitorial service. ER 053-074. Affiliated FM was obligated to pay the City of Seattle a "concession fee" to operate the Monorail. ER 035. Affiliated FM's insured had the obligation to purchase at its expense property insurance covering the Monorail in the event it was damaged by fire. ER 081. Affiliated FM's insured could not assign its rights under the agreement without the written consent of the City of Seattle. ER 096. Under the *Barnett* decision, all of these factors would indicate the *Monorail Concession Agreement*

should be properly characterized as a lease agreement. Although the district court acknowledged the existence of the *Barnett* decision, it did not attribute any particular importance to its holding other than its definition of what constituted a license. ER 426.

The district court below went out of its way to conclude the City of Seattle's right to "access the Monorail System" remained paramount after reviewing the entire contents of the *Monorail Concession Agreement*. ER 427. The district court based this conclusion on the fact that: (1) the City could not be sued for unlawful entry if it entered onto the Monorail to make any repair or improvement, *without imposing any duty on the City to actually make any such repair or improvement*; (2) the City had a key to unlock the doors to the Monorail stations in case of emergency; and (3) the City had the right to contract with other entities, like LTK, to use or occupy the Monorail to make repairs. ER 095-096. The district court below failed to cite any portion of the *Monorail Concession Agreement* that supported this third basis. ER 427. Rather, the only basis for this holding was an unsubstantiated assertion to this effect contained in LTK's memorandum in support of motion for summary judgment.

The express language of the *Monorail Concession Agreement* states nothing in the agreement should be construed to impose a duty on the City of Seattle to repair or improve the Monorail. Therefore, the district court erred in concluding that such an illusory “right” of the City to enter the Seattle Center or Westlake stations if they should be locked precluded this agreement from being considered a lease.

Affiliated FM does not believe it would be error for this Court to take judicial notice of the fact that landlords typically maintain keys for properties they rent. To conclude that the express retention of such a right by the City of Seattle in the *Monorail Concession Agreement* thereby precludes this agreement from being considered a lease agreement constituted reversible error.

Finally, there is nothing in the *Monorail Concession Agreement* to support the district court’s conclusion that the City had the right to contract with other entities, like LTK, to use or occupy the Monorail to make repairs.

The district court below also ignored two towering and undisputed facts.

First, Affiliated FM’s insured, SMS, had enough of an insurable interest in the Monorail to secure fire insurance for the

Monorail. The fact that Affiliated FM's insured had a legally sufficient insurable interest in the Monorail should be considered by this Court as a sufficient enough "proprietary interest" in the Monorail to sustain the present subrogation negligence action against LTK. Under the decision reached by the district court below, Affiliated FM's insured's supposed lack of a sufficient proprietary interest in the Monorail effectively negated Affiliated FM's insured's ability to possess a sufficient insurable interest in the Monorail. *CLS Mortgage v. Bruno*, 86 Wn. App. 390, 394-395, 937 P.2d 1106 (1997). Any legal or equitable interest in property can create an insurable interest. *Id.* A license agreement would therefore qualify as an insurable interest. If Affiliated FM's insured had a sufficient insurable interest in the Monorail, it follows it had a sufficient legal or equitable interest to sustain the present subrogation action against LTK.

Secondly, the Monorail is a mode of transportation (more aptly described as a Seattle icon) that is ridden by thousands of members of the public (primarily tourists) every day. The whole point of maintaining the Monorail is to invite people into it, not keep people from entering it. Given the function of the Monorail, the critical question in this case is not who had the "exclusive" right to "possess" the Monorail, but who had the

exclusive right to "operate" it. As everyone who has lived in the City of Seattle for the past several years knows, the Monorail is of little use to anyone if it sits idly parked in its Seattle Center departure bays. It is undisputed in this lawsuit that the only entity that can operate the Monorail and charge anyone to ride the Monorail is Affiliated FM's insured. The City of Seattle and LTK, like any other member of the public, can ride the Monorail but will be charged a fare for doing so; The City of Seattle and LTK cannot turn the Monorail on, operate a throttle to make it go forward or charge anyone to ride on it. The *Monorail Concession Agreement* would have no economic value unless it provided for the right to operate the Monorail. Since Affiliated FM's insured had the *exclusive* right to operate the Monorail under the *Monorail Concession Agreement*, the corresponding duty to complete all required maintenance and day-to-day upkeep of the Monorail and pay these associated costs itself, the exclusive right to charge a fare for anyone to ride the Monorail and the duty to pay for the property insurance to protect the Monorail from property damage caused by a catastrophe such as a fire, this Court should find Affiliated FM's insured, Seattle Monorail Services, had more than the requisite degree of "control" over the Monorail to possess a sufficient property

interest in the Monorail to bring the present negligence action against LTK.

By analogy, when an individual "rents" a car from a rental car company at Sea-Tac airport, the rental agreement constitutes a lease agreement for the vehicle. The person renting the car has the exclusive right to operate the vehicle being rented. The person renting the car obviously doesn't have the exclusive right to possess either the parking area utilized for the return of rented vehicles or the maintenance bays used by the rental car company to clean and maintain the vehicles made available to rent. Nevertheless, the law considers the rental agreement between the driver and the rental car company to be a lease with respect to the vehicle being rented, not a license, because the driver receives upon payment of a fee the exclusive right to operate the vehicle being rented. *See Robinson v. Avis*, 106 Wn. App. 104, 22 P.3d 818 (2001).

**B. The "Economic Loss Doctrine" Does Not Apply In This Case.**

There was no privity of contract between Affiliated FM's insured (Seattle Monorail Services) and LTK in this case to begin with. LTK readily admits there was no contractual relationship between Seattle Monorail Services and LTK. Thus, the

economic loss rule has no application in this case because there was no contractual relationship between Affiliated FM's insured and LTK.

This point was explicitly made by Division Three of the Washington Court of Appeals in *Baddeley v. Seek*, 138 Wn. App. 333, 156 P.3d 959 (2007). The *Baddeley* decision involved the collapse of a retaining wall. Plaintiff homeowners sued an engineering firm hired by the general contractor who built the retaining wall. The general contractor had hired this engineering firm after the construction of the retaining wall but before its collapse in order to secure an overlooked building permit. In considering plaintiff homeowners' negligent misrepresentation claim against the engineering firm, Division Three of the Washington Court of Appeals stated, "Since no contract relationship exists between STI [the engineering firm] and the Baddeleys [homeowners], the economic loss doctrine does not apply." *Id.*, 138 Wn. App. at 339.

Furthermore, there was no evidence introduced by LTK in support of its motion for summary judgment to indicate LTK was an intended beneficiary under the *Monorail Concession Agreement* concluded between AFM's insured (SMS) and the City of Seattle to operate the Monorail. The economic loss

doctrine, as recognized by Washington courts, prevents a party from bringing an action sounding in negligence where the complaining party has an adequate remedy for breach of contract. *Washington Water Power Co. v. Graybar Elec. Co.*, 112 Wn.2d 847, 851-852, 774 P.2d 1199, 779 P.2d 697 (1989). Affiliated FM submits it would be unfair for this Court to apply a rule of contract law to a situation where its insured did not contract with LTK. In the absence of this privity of contract, Affiliated FM submits it should be obvious to this court that tort law, traditionally concerned with the obligations imposed by the common law rather than by bargain, ought to be applied in this case instead of contract law. *See Carlson v. Sharp*, 99 Wn. App. 324, 328, 994 P.2d 851 (1999), *review denied*, 141 Wn.2d 1024 (2000).

Under the economic loss rule, defects in the quality of materials evidenced by internal deterioration are characterized as economic losses, for which claims sounding in tort are barred; defects causing physical injury or harm to other objects are not characterized as economic losses, and actions for such damage are not barred by the rule. *Griffith v. Centex Real Estate Corp.*, 93 Wn. App. 202, 213, 969 P.2d 486 (1998). *See also Stuart v.*

*Coldwell Banker Commercial Group, Inc.*, 109 Wn.2d 406, 420, 745 P.2d1284 (1987).

In this case, there is no claim for any defect in any material evidenced by deterioration. Rather, LTK concedes for purposes of this appeal that the event that caused the fire at issue in this lawsuit was the sudden disintegration of a drive shaft which allowed the drive shaft to come in contact with a positive current collector shoe leading to an electrical ground fault and ensuing fire. This lawsuit does not involve damages for the disintegration of the drive shaft, but the resulting property damage stemming from the fire that ignited as a result of the drive shaft disintegrating. By definition, this case does not involve an *economic* loss as defined by Washington courts.

Washington courts have adopted a "risk of harm" analysis and apply two tests to determine whether a loss is an "economic loss" compensable in contract, or a sudden, catastrophic injury compensable in tort. The two tests are the "sudden and dangerous test" and the "evaluative approach." *Touchet Valley Grain Growers, Inc. v. Opp & Seibold Gen. Constr., Inc.*, 119 Wn.2d 334, 351, 831 P.2d 724 (1992). See also *Nobl Park, LLC of Vancouver v. Shell Oil Co.*, 122 Wn. App. 838, 95 P.3d 1265 (2004).

Under the "sudden and dangerous test," a party may recover in tort if a sudden and dangerous event caused the damage. *Touchet Valley*, 119 Wn.2d at 351. A fire is a sudden, dangerous and calamitous event normally compensable in tort. It would be appropriate for this court to take judicial notice that the fire not only damaged the Monorail, but initially imperiled the lives of approximately 150 passengers on board the Monorail when the fire first broke out.

A party need not always wait for a calamitous event before being able to recover in tort. Under the "evaluative approach," a vulnerable party may act before calamity strikes. *Touchet Valley*, 119 Wn.2d at 351 (citing *Washington Water Power Co. v. Graybar Elec. Co.*, 112 Wn.2d 847, 866-67, 774 P.2d 1199, 779 P.2d 697 (1989)). The evaluative approach requires that a court consider three factors: (1) the nature of the defect; (2) the type of risk; and (3) the manner in which the injury arose. *Touchet Valley*, 119 Wn.2d at 353 (citing *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1173 (CA3 1981)).

First, as to the nature of the defect, a court considers whether the product failed to meet the purchaser's expectations, such as a gradual internal deterioration, or whether it was

generally defective; that is, whether it suddenly leaked, exploded, or came apart, such as in a violent collision. *Staton Hills Winery Co., Ltd. v. Collons*, 96 Wn. App. 590, 598, 980 P.2d 784 (1999); *Touchet Valley*, 119 Wn.2d at 353-54. In this case, the fire started when a drive shaft suddenly disintegrated causing a massive electrical fault that resulted in fire quickly breaking out.

Second, as to the type of risk, a court considers whether the risk was foreseeable, whether the purchaser had bargaining power to reduce the risk, and whether the risk was to persons or property. *Staton Hills Winery*, 96 Wn. App. at 598. LTK has presented no evidence that Affiliated FM's insured (SMS) was aware the drive shafts for the Monorail were prone to disintegration during normal operation of the Monorail which could lead to a fire and that SMS expressly assumed the risk of any damages to the Monorail due to fire if this should happen. LTK did not contract with SMS. Obviously, a fire poses a clear and present danger to both persons and property.

Finally, a court considers the manner in which the injury arose, specifically whether the defect arose gradually by stealth or whether it was obvious after initial use. *Staton Hills Winery*, 96 Wn. App. at 599. As previously noted, the fire started when a drive shaft suddenly disintegrated during normal operation of the

Monorail leading to a massive electrical fault and a fire quickly breaking out.

Under either the "sudden and dangerous test" or the "evaluative approach", the fire that damaged the Monorail is the type of event normally compensable in tort. Consequently, the "economic loss doctrine" does not apply in this lawsuit.

Justice Tom Chambers' concurrence in *Alejandre v. Bull*, 159 Wn.2d 674, 153 P.3d 864 (2007), explains when the economic loss doctrine should and should not be applied under Washington law. As Justice Chambers explains, claims for breach of contract and some tort claims often bear great similarity to one another. Tort remedies are often, perhaps always, significantly larger than contract remedies. The economic loss rules are a response to the risk that the tort remedies, if applied in contract law, would effectively gut contract law. One way courts have prevented the death of contract law is through the economic loss rule. This rule prevents one party to a contract from rewriting the damage provisions after a breach by artfully pleading the case in tort, rather than contract.

The insight beside the [economic loss] doctrine is that commercial disputes ought to be resolved according to the principles of

commercial law rather than according to tort principles designed for accidents that cause personal injury or property damage. The disputant should not be permitted to opt out of commercial law by refusing to avail himself of the opportunities which that law gives him.

*Alejandre v Bull*, 159 Wn. 2d at 874, quoting *Miller v. U.S. Steel Corp.*, 902 F.2d 573, 575 (CA7 1990).

Justice Chambers writes the economic loss doctrine is unfortunately named and can be positively misleading.

It would be better to call it a “commercial loss” not only because personal injuries and especially property losses are economic losses, too – they destroy values which can be and are monetized – but also, and more important, because tort law is a superfluous and inapt tool for resolving purely commercial disputes. We have a body of law designed for such disputes. It is called contract law.

*Alejandre v Bull*, 159 Wn. 2d at 874, quoting *Miller v. U.S. Steel Corp.*, 902 F.2d at 574.

“Economic loss” (more aptly described as “commercial loss”) includes “the diminution in the value of a product because it is inferior in quality and does not work for the general purposes for which it was manufactured and sold.” Christopher Scott D’Angelo, *The Economic Loss Doctrine: Saving Contract Warranty Law From Drowning in a Sea of Torts*, 26 U. Tol. L.

Rev. 591, 592 (1995) quoting Comments, *Manufacturers' Liability to Remote Purchasers for "Economic Loss" Damages – Tort or Contract*, 114 U. Pa. L. Rev. 539, 541 (1966)).

As Justice Chambers observes, merely because a loss can be expressed in economic terms, it is not necessarily an “economic loss” triggering application of the unfortunately named “economic loss rule.” See *Miller v. U.S. Steel Corp.*, 902 F.2d at 575. Any property damage that can be expressed in a dollar figure is not presumptively an economic loss that cannot be pursued in tort.

In *Berschauer/Phillips Construction Co. v. Seattle School District No. 1*, 124 Wn.2d 816, 881 P.2d (1994), there was no evidence presented of any personal or physical injury resulting from the manner in which the buildings at issue were constructed. The Washington Supreme Court explicitly observed in the *Berschauer* decision, “*This matter involves no claims for injury or death to person, or to property*” (emphasis in original). *Id.*, 124 Wn.2d at 819.

The same was true in the two other Washington Supreme Court decisions applying the economic loss doctrine to preclude an action in tort: *Stuart v. Coldwell Banker Commercial Group, Inc.*, 109 Wn.2d 406, 745 P.2d 1284 (1987); *Atherton*

*Condominium Apartment – Owners Association v. Blume Development Co.*, 115 Wn.2d 506, 799 P.2d 250 (1990).

In the present case, as in *Stuart [v. Coldwell Banker Commercial Group Inc., supra]*, **Owners have presented no evidence of personal or physical injury** resulting from the manner in which Atherton was constructed. Rather, Owners seek only economic damages. Accordingly, the claims are barred by *Stuart*. (Emphasis added.)

*Atherton Condominium Apartment – Owners Association v. Blume Development Co.*, 115 Wn.2d 506, 526-527, 799 P.2d 250 (1990).

The nature of the defect here is that the decks and walkways were not of the quality desired by the buyers. The “injury” or damage suffered was that the decks themselves deteriorated, not through accident or violent occurrence, but through exposure to weather.

Commentators and courts faced with this issue have found it necessary to distinguish economic loss from physical injury or property damage. This distinction is usually drawn depending on the nature of the defect and the manner in which the damage occurred. Defects of quality are evidenced by internal deterioration, and designated as economic loss, while loss stemming from defects that cause accidents involving violence or collision with external objects is treated as physical injury. [citations omitted]

*Stuart v. Coldwell Banker Commercial group, Inc.*, 109 Wn.2d at 420, 749 P.2d at 1291-92 (emphasis added).

This case does involve over \$3 million in **property damages** resulting from the May, 2004 fire that was caused by the defective design of the grounding system conceived of by defendant in 2002 that resulted in the fire. Thus, the *Berschauer* decision principally relied on by the district court below in dismissing Affiliated FM's lawsuit against LTH does not apply to this case.

### **C. Economic Loss Doctrine in Other States.**

The birth place of the economic loss doctrine was in California with the decision in *Seely v. White Motor Co.* (1965) 63 Cal.2d 9, 45 Cal.Rptr. 17, 403 P.2d 145. California courts will not ordinarily allow a person to recover in tort for the breach of duties that merely restate contractual obligations. *Erlich v Menezes* (1999) 21 Cal.4th 543, 552, 87 Cal.Rptr.2d 886, 981 P.2d 978. However, California courts do allow claims for damages, whether economic losses or not, based on a theory of negligence by parties who are not in contractual privity. *J'Aire Corporation v. Gregory* (1979) 24 Cal.3d 799, 157 Cal.Rptr. 407, 598 P.2d 60.

In *Shekhter v. Seneca Structural Design, Inc.* (2004) 121 Cal.App4th 1055, 18 Cal.Rptr. 83, the owners of an apartment complex damaged in the 1994 Northridge earthquake sued,

among others, an engineering firm (Seneca Structural Design) for damages stemming from an allegedly defective earthquake repair plan devised by the engineering firm. The apartment complex owners and the engineering firm were not in privity of contract; the engineering firm had contracted with the general contractor hired by the owner to carry out the repairs to the apartment complex.

The trial court dismissed the apartment owner's negligence claim against the engineering firm on various grounds. The Second District (Los Angeles) California Court of Appeal overruled the trial court based on the following reasoning:

In sum, the cases have long held that conduct amounting to a breach of contract becomes tortious when it also violates a duty independent of contract, and such an independent duty is recognized in cases assessing liability for construction defects causing property damage. (Aas, supra, 24 Cal.4th at p. 643.) Those cases require, inter alia, a showing of "appreciable, nonspeculative, present injury" as a "fundamental prerequisite," and "[c]onstruction defects that have not ripened into property damage, or at least into involuntary out-of-pocket losses, do not comfortably fit the definition" of appreciable harm. (Id. at p. 646.) In this case, the defects have "ripened into property damage," including "substantial and progressive

cracking throughout the elevated decks," "observable failures . . . at supporting walls, and in various other particulars," and "water intrusion drainage problems and related conditions"; "Building 2 is also beginning to manifest property damage . . . ." The Shekhters clearly cannot recover for repairs that are merely "cosmetically unsatisfactory" or for damage that has not yet occurred. They can, however, recover damages in tort if they are able to prove, among other things, that the defective design resulted in "appreciable, nonspeculative, present" physical damage to the repaired structure. On demurrer, of course, we must assume the allegations of "substantial and progressive cracking throughout the elevated decks" and other damage in fact constitutes appreciable harm. It was therefore error to sustain the demurrers to the negligence cause of action.

It may also be instructive to consider the Florida Supreme Court's closely divided decision in *Casa Clara v. Charley Toppino and Sons, Inc.*, 620 So.2d 1244 (Fla. 1993). There, a condominium association sued the supplier of concrete for having provided defective concrete with a high salt content that caused it to crack, putting at risk the dwellings constructed with the concrete. The Florida high court, employing a broad interpretation of *Seely v. White Motor Co. supra*, concluded that homebuyers should "bear the cost of economic losses sustained by those who failed to bargain for adequate contract remedies' ". *Id.*, 620 So.2d at 1247.

Six years later, the Florida Supreme Court, by a six-to-one vote, effectively overruled the *Casa Clara* decision in *Moransais v. Heathman*, 744 So.2d 973, 985 (Fla. 1999). In the *Moransais* decision, a homeowner sued a professional engineer who had inspected the plaintiff's home prior to purchase. The inspection had failed to disclose various defects that rendered the home uninhabitable. The plaintiff was not in privity with the defendant engineer, but was with the engineer's employer. The plaintiff sued the engineer personally for his negligent inspection of the home.

In the *Moransais* decision, the Florida Supreme Court allowed the negligence suit against the engineer. In the process, the Florida Supreme court explained that its prior decisions "[u]nfortunately" had extended the economic loss doctrine "beyond its principled origins and have contributed to applications of the rule . . . well beyond our original intent." *Id.*, 744 So.2d at 980. The court held that henceforth, the doctrine would be limited in order to avoid precluding traditional and well-established actions in tort.

Today, we again emphasize that by recognizing that the economic loss rule may have some genuine, but limited, value in our

damages law, we never intended to bar well-established common law causes of action, such as those for neglect in providing professional services. Rather, the rule was primarily intended to limit actions in the product liability context, and its application should generally be limited to those contexts or situations where the policy considerations are substantially identical to those underlying the product liability-type analysis. . . . The rule, in any case, should not be invoked to bar well-established causes of actions in tort . . . ."

Id., 744 So.2d at 983.

#### IV. CONCLUSION

The district court below erred as a matter of law in dismissing Affiliated FM's lawsuit against LTK. Affiliated FM sued LTK in negligence for damages caused by a fire that damaged the Seattle Monorail in May, 2004. At the time of the fire, there was no contractual relationship between Affiliated FM's insured and LTK. Affiliated FM's interest in operating the Monorail was a sufficient legal interest in the Monorail to sustain an action for damages to the Monorail by Affiliated FM's against LTK. The economic loss doctrine, as defined by Washington courts, has no application in this case.

RESPECTFULLY SUBMITTED this 20<sup>th</sup> day of March,  
2009.

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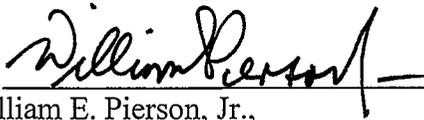
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