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No. 84686-3

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

OLGA MATSYUK,
individually, and on behalf of all those similarly situated,

Appellant,

v.

STATE FARM FIRE & CASUALTY COMPANY,

Respondent.

OPENING BRIEF OF APPELLANT OLGA MATSYUK

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TABLE OF CONTENTS

TABLE OF AUTHORITIES iii

I. INTRODUCTION 1

II. ASSIGNMENTS OF ERROR 5

III. ISSUES PERTAINING TO ASSIGNMENTS OF ERROR 5

IV. STATEMENT OF THE CASE 6

V. ARGUMENT 8

A. STANDARD OF REVIEW 8

1. Standard of Review for the Order of Dismissal 8

2. Standard of Review for the Order Denying Plaintiff Partial Summary Judgment 10

B. STATE FARM IS OBLIGATED TO PAY A SHARE OF MATSYUK'S LEGAL EXPENSE 11

1. State Farm's Obligation to Pay a Share of Matsyuk's Legal Expense Arises From Washington Law & Public Policy 11

a. *Mahler, Winters & Hamm* 11

b. *Young v. Teti* 20

c. State Farm, Not the Tortfeasor Stremditskyy, Paid the PIP to Its Insured, Matsyuk 24

2. State Farm's Obligation to Pay a Share of Matsyuk's Legal Expense Also Arises From the Insurance Policy Language 25

a. Interpretation of Insurance Policy Language Is A Question of Law; To Be Construed As An Average Insured Would 26

b. A Proper Interpretation of the State Farm Policy Language Requires State Farm to Pay a Share of Matsyuk's Legal Expense 27

C. THE COMPLAINT STATES VIABLE CLAIMS BASED ON STATE FARM'S ATTEMPT TO LINK THE LIABILITY SETTLEMENT TO A RELEASE OF SEPARATE CLAIMS AGAINST STATE FARM 30

D. THE TRIAL COURT SHOULD HAVE GRANTED LEAVE TO AMEND TO ADDRESS ANY DEFICIENCIES IN THE COMPLAINT 33

VI. CONCLUSION 34

TABLE OF AUTHORITIES

Cases

American Nat'l Fire Ins. Co. v. B&L Trucking & Constr. Co.,
134 Wn.2d 413, 951 P.2d 250 (1998) 27

Banuelos v. TSA Wash., Inc.,
134 Wn. App. 603, 613-14, 141 P.3d 652 (2006) 32

Barney v. Safeco Ins. Co.,
73 Wn. App. 426, 869 P.2d 1093 (1994) 27

Bravo v. Dolsen Cos.,
125 Wn.2d 745, 888 P.2d 147 (1995) 9

Butzberger v. Foster,
151 Wn.2d 396, 89 P.3d 689 (2004) 26

Caruso v. Local Union No. 690,
100 Wn.2d 343, 670 P.2d 240 (1983) 33-34

Coventry Assocs. v. American States Ins. Co.,
136 Wn.2d 269, 961 P.2d 933 (1998) 32

Denaxas v. Sandstone Court of Bellevue, L.L.C.,
148 Wn.2d 654, 63 P.3d 125 (2003) 10

Folsom v. Burger King,
135 Wn.2d 658, 958 P.2d 301 (1998) 10

Halvorson v. Dahl,
89 Wn.2d 673, 574 P.2d 1190 (1978) 9

Hamm v. State Farm Mut. Auto. Ins. Co.,
151 Wn.2d 303, 88 P.3d 395 (2004) 1, 4, 13, 17-24, 26, 34

Harris v. Drake,
152 Wn.2d 480, 99 P.3d 872 (2004) 25

Hoffer v. State,
110 Wn.2d 415, 755 P.2d 781 (1988) 9

Industrial Indem. Co. of the Northwest, Inc. v. Kallevig,
114 Wn.2d 907, 792 P.2d 520 (1990) 31

Kinney v. Cook,
159 Wn.2d 837, 154 P.3d 206 (2007) 9

Mahler v. Szucs,
135 Wn.2d 398, 957 P.2d 632 (1998) 1, 4, 11-14, 16-17, 19-21, 34

Mercer Place Condo. v. State Farm,
104 Wn. App. 597, 17 P.3d 626 (2000) 26

Oregon Auto. Ins. Co. v. Salzberg,
85 Wn.2d 372, 535 P.2d 816 (1975) 27

Orwick v. Seattle,
103 Wn.2d 249, 692 P.2d 793 (1984) 9

Osborn v. Mason Cty.,
157 Wn.2d 18, 134 P.3d 197 (2006) 10

Overton v. Consol. Ins. Co.,
145 Wn.2d 417, 38 P.3d 322 (2002) 31

Panorama Vill. Condo. Owners Ass'n Bd. of Dirs. v. Allstate Ins. Co.
144 Wn.2d 130, 26 P.3d 910 (2001) 26

Post v. City of Tacoma,
140 Wn. App. 155, 165 P.3d 37 (2007) 10

Professional Marine Co. v. Underwriters at Lloyd's,
118 Wn. App. 694, 77 P.3d 658 (2003) 25

Roller v. Stonewall Ins. Co.,
115 Wn.2d 679, 801 P.2d 207 (1990) 26, 27

San Juan Cty. v. No New Gas Tax,
160 Wn.2d 141, 157 P.3d 831 (2007) 8, 9

Safeco Ins. Co. v. Butler,

118 Wn.2d 383, 823 P.2d 499 (1992) 31-32

Smith v. Arnold,
127 Wn. App. 98, 110 P.3d 257 (2005) 25

Smith v. Safeco Ins. Co.,
150 Wn.2d 478, 78 P.3d 1274 (2003) 31, 32

Tank v. State Farm Fire & Cas. Co.,
105 Wn.2d 381, 715 P.2d 1133 (1986) 32

Thiringer v. American Motors Ins. Co.,
91 Wn.2d 215, 588 P.2d 191 (1978) 13

Tenore v. AT&T Wireless Servs.,
136 Wn.2d 322, 962 P.2d 104 ..... 8, 9

Truck Ins. Exch. v. Vanport Homes, Inc.,
147 Wn.2d 751, 58 P.3d 276 (2002) 31

Van Noy v. State Farm Mut. Auto. Ins. Co.,
142 Wn.2d 784, 16 P.3d 574 (2001) 32

Weyerhaeuser Co. v. Commercial Union Ins. Co.,
142 Wn.2d 654, 15 P.3d 115 (2000) 10

Wilson v. Horsley,
137 Wn.2d 500, 974 P.2d 316 (1999) 33

Winters v. State Farm Mut. Auto. Ins. Co.,
99 Wn. App. 602, 994 P.2d 881 (2000) 14

Winters v. State Farm Mut. Auto. Ins. Co.,
144 Wn.2d 869, 31 P.3d 1164 (2001) 1, 4, 13, 14-19, 20, 21, 34

Woo v. Fireman's Fund Ins.,
161 Wn.2d 43, 164 P.3d 454 (2007) 10, 26

Young v. Teti,
104 Wn. App. 721, 16 P.3d 1275 (2001) 3, 4, 20-22, 34

Rules

CR 12(b)(6) 8, 26

CR 15 33

CR 56 10

I. INTRODUCTION

Plaintiff/Appellant Olga Matsyuk was riding as a passenger in a car being driven by Omelyan Stremditskyy. The car was insured by Defendant/Respondent State Farm Fire & Casualty Company under a policy that included, *inter alia*, liability and Personal Injury Protection ("PIP") coverage (the "Policy").

The car was involved in an accident, Matsyuk was injured, and sought and received medical treatment. Because of her status as a passenger, Matsyuk was a State Farm insured under the Policy. Thus, her medical bills were paid by State Farm under the obligations it directly owed to her under the PIP coverage.

Matsyuk believed Stremditskyy was at fault for the accident, so she asserted a personal injury claim against him. Her attorney negotiated a settlement of the claim against Stremditskyy with his liability insurer, State Farm. State Farm indicated that it would recoup its PIP payments from Matsyuk through an offset to the liability settlement it was paying on behalf of Stremditskyy. State Farm denied, however, that it had any obligation to pay a share of the legal expense Matsyuk incurred to obtain the liability settlement from Stremditskyy.

Matsyuk disagreed with State Farm's position on the sharing of legal expense. She agreed, however, to go forward with the settlement

and release Stremditskyy as long as she maintained her separate rights against State Farm concerning the legal expense sharing issue. State Farm, though, insisted that she also release her separate claims against State Farm. When Matsyuk persisted with her desire to simply preserve her separate and independent rights against State Farm, State Farm threatened to repudiate the liability settlement on behalf of Stremditskyy.

As a result of the foregoing, Matsyuk instituted suit. Her Complaint asserts claims for violation of the Consumer Protection Act, Bad Faith, Conversion and Breach of Contract.

It is firmly established in Washington that if a PIP insurer recoups its PIP payments from the insured's liability recovery, it must pay its share of the legal expense she incurred to effect that recovery. The applicable line of precedent confirms that this rule applies when the liability recovery is from a fully insured tortfeasor (*Mahler*[1]), from a underinsured tortfeasor (*Winters*[2]), and from an uninsured tortfeasor (*Hamm*[3]). Here, although the tortfeasor was fully insured, as in *Mahler*, the same insurance policy provided both the PIP and the liability funds, as in *Hamm*.[4]

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[1] *Mahler v. Szucs*, 135 Wn.2d 398, 957 P.2d 632 (1998).

[2] *Winters v. State Farm Mut. Auto. Ins. Co.*, 144 Wn.2d 869, 31 P.3d 1164 (2001).

[3] *Hamm v. State Farm Mut. Auto. Ins. Co.*, 151 Wn.2d 303, 88 P.3d 395 (2004).

[4] Although in *Hamm* the liability funds were recovered from UIM coverage, while here the liability funds were recovered from liability coverage.

The primary question presented is whether, since State Farm recouped its PIP payments from the liability funds Matsyuk recovered from Stremditskyy, State Farm is obligated to pay its share the legal expense Matsyuk incurred to make that recovery. The Complaint alleges that State Farm is so obligated, and asserts two bases: (i) State Farm is obligated as a matter of law under the aforementioned precedent and the public policies they reflect; and (ii) apart from of the requirements of Washington law, State Farm is obligated under its own policy language to pay a share of the legal expense.

State Farm filed a motion to dismiss.[5] In its motion, State Farm did not argue that any of the Complaint's claims were insufficiently pled, but rather contended that a single dispositive issue barred any relief. Essentially, State Farm asserted that the Court of Appeals' *Young*[6] opinion was controlling, not *Mahler*, *Winters* or *Hamm*, and that this foreclosed any relief. Notably, in its opening brief State Farm did not address plaintiff's allegation that its policy language provided an independent basis for the legal expense sharing obligation.

The trial court granted State Farm's motion to dismiss for failure to

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[5] Matsyuk filed a cross motion seeking partial summary judgment on the legal expense sharing issue only. The trial court denied the motion.

[6] *Young v. Teti*, 104 Wn. App. 721 (2001).

state a claim upon which relief could be granted. Although the trial court did not disclose the basis of its ruling, it appears it accepted defendant's argument that *Young* controlled, and not *Mahler*, *Winters* or *Hamm*. There is nothing that indicates, however, that the court considered or even acknowledged the allegation that the policy language provides an independent basis for the legal expense sharing. Indeed, since State Farm had not addressed this basis in its opening brief, it was not even properly before the trial court.

In addition, the Complaint also alleges a basis for its claims that is separate and independent from the resolution of the legal expense sharing question. Specifically, the Complaint alleges that State Farm leveraged its position as both PIP and liability insurer and attempted to link the payment of the liability settlement on behalf of Stremditskyy, to a release of wholly separate claims Matsyuk may have possessed against State Farm. Because of the duty of good faith and fair dealing State Farm owed to Matsyuk as its insured, State Farm's conduct was improper. This allegation provides an alternative basis, independent of the resolution of the legal expense sharing issue, for viable claims of bad faith, CPA and breach of contract.

In its opening brief for its motion to dismiss, however, State Farm did not address this alternative basis either. Thus, not only is there nothing to indicate that the trial court considered it, but the issue was not

properly before the trial court in any event.

II. ASSIGNMENTS OF ERROR

1. The trial court erred by concluding that the Complaint failed to state a claim upon which relief could be granted, and thereby dismissing the case. (February 13, 2009 Order Granting Defendant's Motion to Dismiss).

2. The trial court erred by declining to rule as matter of law that State Farm was obligated to pay a share of the legal expense Matsyuk incurred to effect the liability recovery from the tortfeasor Stremditskyy. (February 13, 2009 Order Denying Plaintiff's Motion for Partial Summary Judgment).

III. ISSUES PERTAINING TO ASSIGNMENTS OF ERROR

1. Did the trial court err in dismissing for failure to state a claim, given the Complaint alleges that State Farm was obligated under Washington law to pay a share of the legal expense Matsyuk incurred to effect the liability recovery from Stremditskyy, and from which funds State Farm benefited by recouping its PIP payments?

2. Did the trial court err in dismissing for failure to state a claim, given the Complaint alleges that State Farm, independent of Washington law, was obligated under its insurance policy language to pay

a share of the legal expense Matsyuk incurred to effect the liability recovery from Stremditskyy?

3. Did the trial court err in dismissing for failure to state a claim, given the Complaint alleges that State Farm acted wrongfully when it tried to use the liability settlement on behalf of Stremditskyy as leverage to obtain a release from its PIP insured, Matsyuk, of separate claims she might possess against State Farm as her PIP insurer?

4. Did the trial court err in not granting Matsyuk an opportunity to amend the Complaint to cure any deficiencies?

5. Did the trial court err in not granting Matsyuk partial summary judgment on the issue of whether Washington law and public policy requires State Farm, in its capacity as PIP insurer, to pay a share of the legal expense Matsyuk incurred to make the liability recovery from Stremditskyy, from which funds State Farm recouped its PIP payments?

IV. STATEMENT OF THE CASE

On May 20, 2008, Matsyuk was a passenger in a vehicle driven by Stremditskyy. CP 4.[7] They were involved in an accident; Stremditskyy was at fault. CP 4. At the time, Stremditskyy's liability was covered by

[7] The statement of facts is taken from the Complaint (CP 3-11). These facts are presumed true for purposes of the review of the order of dismissal. The majority of operative facts are undisputed in any event.

an auto policy issued by State Farm (the "Policy"). CP 4. Because Matsyuk was a passenger in the Stremditskyy vehicle, State Farm also provided Personal Injury Protection ("PIP") insurance coverage to Matsyuk. CP 4. Matsyuk received medical treatment for injuries she sustained in the accident, and as Matsyuk's PIP insurer, State Farm paid the bills. CP 4.

Matsyuk sought to recover against Stremditskyy as the responsible party. CP 4. She reached a settlement of her liability claim against him for $5,874, which was to be paid on Stremditskyy's behalf by his liability insurer, State Farm. CP 4. Because State Farm had already paid PIP benefits for Matsyuk as her PIP insurer, State Farm indicated it would recoup its PIP payments from Matsyuk through an offset to the liability payment it was to make on Stremditskyy's behalf. CP 4. Thus, State Farm provided a check for the difference only. CP 4.

Matsyuk took the position that since State Farm was recouping its PIP payments from the liability recovery Matsyuk made from Stremditskyy, it was obligated to pay its share of the legal expenses she incurred in creating those funds. CP 5. State Farm disagreed, asserting that it could offset the full amount of the PIP benefits paid, without any regard to or reduction for its share of the legal expense Matsyuk incurred in obtaining the liability recovery. CP 5. To make matters worse, State

Farm then refused to effectuate the agreed settlement of the liability claim against Stremditskyy, unless Matsyuk also released wholly separate claims she might have against State Farm as its PIP insured. CP 5.

Based on the foregoing, the Complaint pleads claims for violation of the Consumer Protection Act, Bad Faith, Conversion and Breach of Contract. *See* Cmplt. at 6-8 (CP 8-10). It seeks damages, injunctive relief and declaratory relief. *See* Cmplt. at 1, 6, 8 (CP 2, 8, 10). Because it appears that State Farm's refusal to pay a share of legal expense in these circumstances is consistent with its conduct towards other insureds, *see* Cmplt. 3 (CP 5), the Complaint seeks class-wide relief.[8] Cmplt. 3-6 (CP 5-8).

V. ARGUMENT

A. STANDARD OF REVIEW

1. Standard Of Review For the Order of Dismissal

The appropriateness of a dismissal under CR 12(b)(6) is reviewed *de novo*. *San Juan Cty. v. No New Gas Tax*, 160 Wn.2d 141, 164, 157 P.3d 831 (2007); *Tenore v. AT&T Wireless Servs.*, 136 Wn.2d 322, 329-30, 962 P.2d 104 (1998). Dismissal is not appropriate unless it appears <u>beyond doubt</u> that the plaintiff cannot prove <u>any set of facts</u>, consistent

[8] No class determination had been made at the time of dismissal.

with the complaint, that would justify recovery. *San Juan Cty.*, 160 Wn.2d at 164 (citing *Bravo v. Dolsen Cos.*, 125 Wn.2d 745, 750, 888 P.2d 147 (1995)); *Kinney v. Cook*, 159 Wn.2d 837, 842, 154 P.3d 206 (2007) (citing *Tenore*, 136 Wn.2d at 330).

Motions to dismiss should be granted "sparingly and with care," and only in the unusual case in which the plaintiff's allegations show on the face of the complaint an insuperable bar to relief. *San Juan Cty.*, 160 Wn.2d at 164 (citing *Tenore*, 136 Wn.2d at 330; *Hoffer v. State*, 110 Wn.2d 415, 420, 755 P.2d 781 (1988)). When considering the motion, the court presumes that all facts alleged in the complaint are true, and may also consider hypothetical facts supporting the plaintiff's claims. *Kinney*, 159 Wn.2d at 842 (citing *Tenore*, 136 Wn.2d at 330). Indeed, "<u>any</u> hypothetical situation <u>conceivably</u> raised by the complaint defeats a CR 12(b)(6) motion if it is legally sufficient to support plaintiff's claim." *Halvorson v. Dahl*, 89 Wn.2d 673, 674, 574 P.2d 1190 (1978) (emphasis added). Moreover, a motion to dismiss "must be tested in light of CR 8(a)(1) which only requires 'a <u>short and plain</u> statement of the claim.'" *Orwick v. Seattle*, 103 Wn.2d 249, 254, 692 P.2d 793 (1984) (emphasis added).

2. Standard Of Review For the Order Denying Plaintiff Partial Summary Judgment

"A motion for summary judgment presents a question of law reviewed *de novo*." *Osborn v. Mason Cty.*, 157 Wn.2d 18, 22, 134 P.3d 197 (2006) (citing *Denaxas v. Sandstone Court of Bellevue, L.L.C.*, 148 Wn.2d 654, 662, 63 P.3d 125 (2003)). Thus, the reviewing court engages in the same inquiry as the trial court. *Woo v. Fireman's Fund Ins.*, 161 Wn.2d 43, 54, 164 P.3d 454 (2007) (citing *Weyerhaeuser Co. v. Commercial Union Ins. Co.*, 142 Wn.2d 654, 692 n.17, 15 P.3d 115 (2000)).

For purposes of the summary judgment analysis, the reviewing court will "construe the evidence in the light most favorable to the nonmoving party, *Folsom v. Burger King*, 135 Wn.2d 658, 663, 958 P.2d 301 (1998), and grant summary judgment if 'there is no genuine issue as to any material fact' and 'the moving party is entitled to a judgment as a matter of law.'" *Osborn*, 157 Wn.2d at 22 (quoting CR 56(c)). *See also Post v. City of Tacoma*, 140 Wn. App. 155, 161, 165 P.3d 37 (2007) ("Summary judgment is rendered where there is no genuine issue of material fact and the moving party is entitled to a judgment as a matter of law.") (citing CR 56(c)).

B. STATE FARM IS OBLIGATED TO PAY A SHARE OF MATSYUK'S LEGAL EXPENSE

There are two grounds underlying State Farm's obligation to pay a share of Matsyuk's legal expense. The first is that State Farm is so obligated under Washington law and to effectuate stated Washington public policy. The second is that, independent of the requirements of Washington law, State Farm is obligated under the language of its own insurance policy.

1. State Farm's Obligation to Pay a Share of Matsyuk's Legal Expense Arises From Washington Law & Public Policy

a. *Mahler, Winters & Hamm*

There is a clear line of Washington Supreme Court authority on the legal expense sharing issue, starting with *Mahler v. Szucs*, 135 Wn.2d 398, 957 P.2d 632 (1998). In that case, the Court firmly established the rule that when a PIP insurer recoups its payments out of liability funds recovered by its PIP insured, the PIP insurer is obligated to pay a pro rata share of the legal expense the PIP insured incurred to obtain that recovery. *See id.* at 396.

The *Mahler* Court essentially conducted a two step analysis. First, the Court considered whether the PIP insurer had a right to seek reimbursement of its PIP payments. *See id.* at 418-21. In its analysis, the

Court noted that reimbursement rights in connection with personal injury claims were relatively new and problematic. *See, e.g., id.* at 413-15. Even so, the Court ultimately concluded that the PIP insurer did have such a right. *Id.* at 421. Although the policy at issue termed this right as the PIP insurer being "subrogated" to its insured's settlement proceeds, the Court pointed out that the term was a misnomer. *Id.* at 419-20. Rather, because no right of subrogation arises against an insurer's own insured, the PIP insurer had "simply contracted for a right to reimbursement of its PIP payments from its insureds from the proceeds of a settlement." *Id.* at 420 (emphasis omitted). *See also id.* at 421 (policy language "creates a contractual right of reimbursement, not a right to subrogation, when an insured pursues an action or seeks recovery from a tortfeasor.").

Importantly, even while recognizing the PIP insurer's right to seek reimbursement, the Court made it clear that this right was in no ways absolute. For example, in addition to the insurer's obligation to comply with the "duties to [its] insureds [required] by statute, regulation, or common law," the PIP insurer's right to seek reimbursement is limited by and subordinate to "the public policy in Washington of full compensation of insureds." *Id.* at 436. *See also id.* at 418 (right to seek reimbursement "is governed by the general public policy of full compensation of the

insured").[9]

The Court then went on to the second step, what it earlier described as the "more troublesome question [of] the precise enforcement mechanism for the [insurer's] right of reimbursement. *Id.* at 412. More specifically, "the central issue in this case: whether, and to what extent, State Farm must share with its insureds any expenses necessary to obtain a settlement from a tortfeasor." *Id.* at 421.

The Court concluded that the PIP insurer was obligated to bear its pro rata share of the PIP insured's legal expense. It identified the "common fund" doctrine as the rationale for such a legal expense sharing rule. *See id.* at 426-27 ("This equitable sharing rule is based on the common fund doctrine, which ... applies to cases where litigants preserve or create a common fund for the benefit of others as well as themselves.") (citation omitted). Although the *Mahler* analysis actually dealt with the specific policy language before it, the Supreme Court later clarified that the applicable principles (*e.g.*, full compensation for the insured, etc.) were of general application based on equitable principles and Washington public policy. *See Hamm*, 151 Wn.2d at 310-11; *Winters*, 144 Wn.2d at 878-79.

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[9] *See also Thiringer v. American Motors Ins. Co.*, 91 Wn.2d 215, 219-220, 588 P.2d 191 (1978) (Washington's public policy that the insured's right to receive full compensation is superior to the insurer's right to seek recovery of its payments).

In *Mahler*, the tortfeasor was adequately insured, and so the PIP insured's liability recovery was actually paid by the tortfeasor's liability insurer. *Id.* at 407, 436. Regardless, the liability funds are considered to have come from the tortfeasor himself. *E.g., Winters v. State Farm Mut. Auto. Ins. Co.*, 99 Wn. App. 602, 612, 994 P.2d 881 (2000), *aff'd*, 144 Wn.2d 869, 31 P.3d 1164 (2001) ("The liability carrier stands in the tortfeasor's shoes, and its payments are treated as if the tortfeasor made them."). In that respect, the situation here is the same. The tortfeasor, Stremditskyy, was adequately insured. Thus, even though the liability payment was funded by his liability insurer, the funds are considered to have come from him, and the rule of *Mahler* applies.

In *Mahler*, the PIP coverage and the tortfeasor's liability coverage were from two different insurance companies. Here, both PIP coverage and the tortfeasor's liability coverage happen to be provided by the same insurance company. That this fact makes no difference in the result is illustrated by the two cases following *Mahler*.

In *Winters v. State Farm Mutual Automobile Insurance Company*, 144 Wn.2d 869, 31 P.3d 1164 (2001), Winters[10] was injured in an automobile accident and received PIP benefits under coverage applicable

[10] Although *Winters* involved two cases consolidated for the appeal, for simplicity the facts discussed are those of the plaintiff Sara Winters.

to her vehicle provided by State Farm Mutual. 144 Wn.2d at 873. She pursued a personal injury claim against the tortfeasor, and recovered his liability insurance limits from his insurer. *Id.* Believing that she had not been fully compensated by that recovery, Winters also sought to recover from State Farm Mutual under the UIM coverage. *Id.* Stepping into the shoes of the tortfeasor under the UIM coverage, State Farm Mutual was ultimately required to pay additional damages to Winters as compensation for her personal injury. *Id.*

The parties agreed that State Farm Mutual could recoup the payments it had already made to Winters under the PIP coverage. They also agreed that this could be accomplished by offsetting the amount of the PIP payments against the liability payment State Farm Mutual was to make under the UIM coverage. State Farm Mutual claimed, however, that it could take the offset without a reduction for its share of the legal expense Winters incurred to make the total liability recovery. *Id.* at 873.

The Court identified the issue as "whether a PIP insurer must pay a pro rata share of its [PIP] insured's attorney fees associated with recovering full compensation from an UIM insurer." *Id.* at 875. Unlike in *Mahler*, the insurance company providing the liability payment (under UIM coverage) was the same company that had provided the PIP payments. Indeed, they were being provided under the same policy.

It made no difference. Finding no reason to deviate from the legal expense sharing rule articulated in *Mahler*, the Court ruled that it applied equally in *Winters*. The PIP insured had effected a liability recovery that consisted of proceeds from the tortfeasor (albeit paid by the tortfeasor's insurer) and proceeds from the PIP insured's own UIM carrier (who had stepped into the shoes of the tortfeasor). *See id.* at 882. These funds "became the common fund from which the PIP insurer was able to recoup [the PIP] payments it had made." *Id.* (Emphasis added.)

In its analysis, *Winters* refers to several important public policy considerations that inform the decision. For example, the Court noted that the decision promotes uniformity among of insurance companies. *Id.* at 881. It also noted the important public policy rule that the insured's right to full compensation is superior to the insurer's right to seek to recoup its payments. *Id.* at 882 ("the insurer may not recover before the PIP insured has been fully compensated") (citing *Mahler*, 135 Wn.2d at 417-18, 436). *See also id.* at 883 ("as between the insured and the insurer, we balance their interests and decide that the insurer should pay its share of the costs associated with recovery"). Finally, the Court also observed that "[t]he fact that the same insurer provides both UIM coverage and ... PIP coverage should not result in the insured's bearing a greater amount of legal expenses." *Id.* at 881.

Three years after *Winters* came the decision in *Hamm v. State Farm Mutual Automobile Insurance Company*, 151 Wn.2d 303, 88 P.3d 395 (2004). Hamm was covered by an insurance policy issued by State Farm Mutual that included both PIP and UIM coverage. After being injured in an automobile accident, Hamm sought and received PIP benefits. *Id.* at 306.

The at-fault driver was uninsured, so Hamm pursued her personal injury claim under her own insurance policy's UIM coverage. *Id.* State Farm Mutual, as UIM carrier, stepped into the shoes of the tortfeasor. After Hamm's personal injury damages were determined in an arbitration proceeding, State Farm Mutual, as UIM insurer, tendered a check. The check, however, reflected an offset to the liability recovery for the amount of PIP payments State Farm Mutual had previously paid Hamm under PIP. *Id.* at 306-07. Hamm filed suit challenging the extent of the offset. *Id.* at 307.

The Court identified the issue presented:

> Does the pro rata sharing rule for legal expenses articulated in *Mahler* (recovery from a <u>fully</u> insured tortfeasor) and in *Winters* (combined recovery from an <u>under</u>insured tortfeasor and a UIM carrier) apply when the tortfeasor is uninsured and the insured recovers only from a UIM carrier?

Id. (Emphasis in original.) After discussions of *Mahler* and *Winters*, *see*

id. at 309-12, the Court concluded that the pro rata sharing of legal expense rule articulated in those cases similarly applied to Hamm's situation. *See id.* at 312. It made no difference that State Farm Mutual provided both the PIP funds and the liability (under UIM) funds, or that both of the coverages were under the same insurance policy. If the insurer was to recoup its PIP payments from the insured's liability recovery (in that case, via offset), then the insurer was obligated to pay its share of the legal expense its insured incurred to make that recovery: "In order to take the PIP offset, State Farm must pay its pro rata share of the legal expenses Hamm incurred in order to obtain the UIM recovery." *Id.* at 321. That rule is equally applicable here.

The analysis and reasoning of *Hamm* is informing in several regards. One is that, for the legal expense sharing question, it makes no difference if the PIP funds and the liability recovery funds come from the same insurance company, even under the same insurance policy. *Hamm* recognizes that with regard to even a single insured on a single claim, an insurer might be acting in multiple capacities, or in essence wearing different "hats" (*e.g.*, for no-fault PIP coverage and fault-based coverage, such as UIM). In that circumstance, *Hamm* points out, the insurer has distinct rights and obligations depending on the capacity in which it is acting. *See, e.g., id.* at 317 ("As in *Winters*, the issue presented ... does

not depend on State Farm's role as UIM carrier but rather on 'whether or not the PIP carrier should pay a pro rata share of legal expenses for its insured in recovering PIP benefits from an UIM insurer.'") (quoting *Winters*, 144 Wn.2d at 882).

In addition, *Hamm* focuses on the true nature of the liability recovery. No matter who ultimately pays the liability recovery, the funds are deemed to have come from the actual tortfeasor. *See, e.g.*, *Hamm*, 151 Wn.2d at 319 ("'UIM payments are treated as if made by the tortfeasor'") (quoting *Winters*, 144 Wn.2d at 880); *Winters*, 144 Wn.2d at 880 ("the tortfeasor's liability carrier ... stands in the shoes of the tortfeasor [and] the payments are treated as if the tortfeasor made them."). *See also Mahler*, 135 Wn.2d at 396 (although paid by his liability insurer, the liability payment was treated as if made by tortfeasor). An insurer's payment of the liability funds on the tortfeasor's behalf changes nothing.

Hamm also details an important touchstone analysis for determining whether the equitable *Mahler* rule should apply. Echoing *Winters*, it looks to whether the PIP insured would be worse off simply because a single insurer provided two different coverages, as compared to how she would fare if two different insurers provided the respective coverages. *Hamm*, 151 Wn.2d at 312. Similarly, *Hamm* also looks at it from the insurance company perspective, considering whether a single

insurer would unfairly benefit from providing two different coverages, as compared to two different insurers providing the same two coverages. *See id.* at 314-15.

On the facts here, either analysis leads to the same result: the *Mahler* legal expense sharing rule should apply. For example, if there were two separate insurers providing the PIP and liability coverages here, Matsyuk would plainly be entitled to have her PIP insurer pay a portion of the legal expense she incurred for the liability recovery. Indeed, that is essentially the facts of *Mahler*. Hence, denying Matsyuk the benefit of *Mahler* legal expense sharing simply because State Farm happens to provide both the PIP coverage and the liability coverage would make her worse off. Likewise, if the liability coverage had been provided by a different insurer, the PIP insurer would plainly have to pay *Mahler* fees. Thus, permitting State Farm to avoid *Mahler* fees simply because it has the two separate insurance coverage obligations would provide it with an unfair benefit, as compared to two separate insurers providing the exact same coverage. From either perspective, consistency with *Hamm*, as well as *Winters*, dictates that the *Mahler* should apply. *See Hamm*, 151 Wn.2d at 312; *Winters*, 144 Wn.2d at 882.

b. *Young v. Teti*

Standing outside the foregoing line of *Mahler* cases is a Court of

Appeals opinion, *Young v. Teti*, 104 Wn. App. 721, 16 P.3d 1275 (2001). The case came after *Mahler*, but before *Winters* or *Hamm*.

Teti caused an automobile accident that injured Young, his passenger. The car was covered by an Allstate insurance policy. Under the PIP coverage, Allstate paid for Young's medical bills and wage loss. *See* 104 Wn. App. at 723. Young thereafter pursued a personal injury claim against Teti, and received a jury award in her favor. *Id.* Teti sought an offset to the jury award in the amount of PIP payments Allstate had made to her.[11] Young agreed to Teti's offset request, but that she was entitled to the benefit of the *Mahler* legal expense sharing rule. *Id.* Although the trial court agreed with Young, the Court of Appeals did not, and reversed. The reasoning underlying *Young*, however, plainly conflicts with the law and principles laid out in the after-decided *Hamm*.

For example, the Court believed that *Mahler* did not apply because the liability recovery by Young against Teti did not "benefit" Allstate:

> Because Young's litigation [against Teti] did not benefit Allstate, *Mahler* does not apply; and Allstate need not share in Young's litigation costs. ... Unlike in *Mahler*, Young's lawsuit produced no <u>additional party</u> to reimburse Allstate.

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[11] Since Allstate was not a party, the offset issue should not even have been before the court. When Young agreed to Teti's offset request, however, it became part of the case. *See id.* at 723 n.4. Young presumably understood the request as being made on Allstate's behalf by the attorneys that Allstate had undoubtedly been retained by Allstate to defend Teti.

Id. at 725-26 (emphasis added). In making this statement, the Court viewed Allstate in a single, unitary sense, and did not appreciate or consider that Allstate acted in two different capacities (*i.e.*, liability insurer for Teti and PIP insurer for Young[12]). The Court only compounded the error when it also failed to make any distinction between Allstate (in any capacity) and its liability insured, Teti.

> [W]hen Young ... recovered [from Teti], she did not create a fund to benefit, or to reimburse, anyone other than herself. Young's jury verdict increased Teti's, and his insurer's financial obligation to Young [for] more than the [amount] Allstate had already paid her ... under ... PIP coverage.

See id. at 725 (footnote omitted).[13]

In short, the Court of Appeals believed that since the PIP money was paid by Allstate, and the liability judgment against Teti was paid by Allstate, the liability recovery did not benefit Allstate because all of the money came from Allstate.

The foregoing statements and reasoning of *Young* are impossible to reconcile with *Hamm*, particularly where the Supreme Court recognizes

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[12] In fact, the Court actually referred to Allstate as Teti's PIP insurer, referring to him as the "at-fault PIP insured." *Id.* at 727 n.14 (citation omitted). But the PIP insured was not Teti – it was Young; just as the PIP insured here is not Stremditskyy, it is Matsyuk.

[13] In a similar vein is the Court's statement that "there is no contractual or legal basis for requiring Teti to share Young's litigation expenses in suing him." *See id.* at 726 (emphasis added). But the question was not whether the tortfeasor Teti needed to pay a portion of the legal expense, but whether the PIP insurer Allstate need to.

and analyzes the separate rights and obligations of an insurer under the different coverages it provides:

> [T]he Court of Appeals conclude[d] that "Hamm's *UIM* carrier received no benefit." *Hamm*, 115 Wn. App. at 777 (emphasis added). Focusing on State Farm's capacity as UIM carrier, the Court of Appeals decided that Hamm is not entitled to reimbursement from her UIM carrier for the legal expenses she incurred to create the UIM arbitration award. *Id.* at 778. In doing so, the Court of Appeals applied the rule for UIM carrier setoffs from *Dayton* rather than the rule for PIP carrier offsets from *Mahler* and *Winters*.
>
> The Court of Appeals' conclusions with respect to State Farm's obligations in its capacity as UIM carrier may be correct. As in *Winters*, however, "[t]he question presented here is totally different: whether or not the PIP carrier should pay a pro rata share of legal expenses for its insured in recovering PIP benefits from an UIM insurer." *Winters*, 144 Wn.2d at 882. Although the Court of Appeals notes that "[i]t appears that Hamm is seeking to have State Farm pay a portion of her fees in its capacity as PIP carrier," it erroneously concludes that "*Winters* is distinguishable because Hamm's PIP carrier received no reimbursement," *Hamm*, 115 Wn. App. at 778, and "State Farm as UIM carrier received an offset for the PIP payment previously made." *Hamm*, 115 Wn. App. at 777 n. 1. [Footnote omitted.]
>
> The offset at issue in this case, just as in *Winters*, is a benefit to the PIP carrier, not the UIM carrier.

Hamm, 151 Wn.2d at 312-13 (underlining added). The Supreme Court later summarized:

> in effect, Hamm received $16,000.00 from State Farm in its capacity as UIM carrier and no money from State Farm as PIP carrier because, as PIP carrier, State Farm was

> reimbursed [via offset] the entire amount of its prior PIP payments. Just as any PIP carrier under *Mahler* and *Winters*, State Farm must pay a pro rata share of its insured's legal expenses in order to receive the PIP reimbursement.

Id. at 318 (emphases added).

c. State Farm, Not the Tortfeasor Stremditskyy, Paid the PIP to Its Insured, Matsyuk

For its collateral source rule argument, State Farm takes the position that a common fund was never created because all of the money received by Matsyuk – the PIP payments and the liability recovery – was money from the tortfeasor, Stremditskyy. In essence, State Farm asserts that the PIP payments were, in reality, liability "down payments." State Farm is only half correct. While the liability recovery is considered to have come from Stremditskyy as the insured tortfeasor, the PIP payments clearly came from State Farm.

There no dispute that Matsyuk, for purposes of the PIP coverage, was a State Farm insured. Thus, State Farm owed Matsyuk certain duties and obligations, including the duty to pay her accident related medical expenses. This duty was owed to Matsyuk by State Farm alone; Stremditskyy owed her nothing. Consequently, when State Farm made the PIP payments, it made them for and on its own behalf. In short, State Farm's PIP payments were wholly separate from and had nothing to do

with the later liability claim. *See Smith v. Arnold*, 127 Wn. App. 98, 110, 110 P.3d 257 (2005) ("action taken between an insurer and an insured under a PIP policy is distinct from tort litigation between the insured and a third-party tortfeasor.") (citing *Harris v. Drake*, 152 Wn.2d 480, 99 P.3d 872 (2004)). *See also id.* ("The Arnolds' policy contractually bound Allstate to cover Smith's PIP claim, and its handling of the [PIP] claim is separate from ... any future lawsuit Smith might have brought.") (citing *Professional Marine Co. v. Underwriters at Lloyd's*, 118 Wn. App. 694, 711, 77 P.3d 658 (2003)).

2. State Farm's Obligation to Pay a Share of Matsyuk's Legal Expense Also Arises From the Insurance Policy Language

The allegation of an obligation to share legal expense based on the insurance policy language provides an entirely separate and alternative basis for relief. State Farm did not raise the issue in its motion to dismiss opening brief; its argument only came in its reply after Matsyuk pointed out that fact in her opposition brief. *See* CP 57. Consequently, the issue was not properly before the trial court for purposes of the motion to dismiss. Furthermore, there is nothing to indicate that the trial court even considered, much less analyzed, whether the insurance policy language

provided an alternative basis for State Farm's obligation to share in the legal expense.[14] These facts alone should result in remand.

a. Interpretation of Insurance Policy Language Is A Question of Law; To Be Construed As An Average Insured Would

To the extent this Court evaluates the insurance policy, the "[i]nterpretation of an insurance contract is a question of law reviewed de novo." *Woo v. Fireman's Fund Ins.*, 161 Wn.2d 43, 54, 164 P.3d 454 (2007) (citing *Roller v. Stonewall Ins. Co.*, 115 Wn.2d 679, 682, 801 P.2d 207 (1990), *overruled on other grds. by Butzberger v. Foster*, 151 Wn.2d 396, 89 P.3d 689 (2004)).

"[C]ourts justifiably look [at insurance contracts] in a light most favorable to the insured." *Hamm*, 151 Wn.2d at 323 (Sweeney, J., dissenting) (citing *Panorama Vill. Condo. Owners Ass'n Bd. of Dirs. v. Allstate Ins. Co.*, 144 Wn.2d 130, 137-38, 26 P.3d 910 (2001)). *See also Mercer Place Condo. v. State Farm*, 104 Wn. App. 597, 602-03, 17 P.3d 626 (2000) (insurance policies liberally construed in favor of the insured). When the Court construes insurance policy language, it must "give it the same construction that an 'average person purchasing insurance' would

[14] The trial court dismissed the Complaint under CR 12(b)(6); the trial court did not enter an order of summary judgment for the defendant.

give the contract." *Id.* (emphasis added; quoting *Roller*, 115 Wn.2d at 682). *See also American Nat'l Fire Ins. Co. v. B&L Trucking & Constr. Co.*, 134 Wn.2d 413, 427, 951 P.2d 250 (1998) (policy interpreted as average insurance purchaser would understand it). Any ambiguity in the policy language must be resolved in favor of the insured. *E.g., Barney v. Safeco Ins. Co.*, 73 Wn. App. 426, 429, 869 P.2d 1093 (1994). Moreover, "insurance policies ... are simply unlike traditional contracts, *i.e.*, they are not purely private affairs but abound with public policy considerations...." *Oregon Auto. Ins. Co. v. Salzberg*, 85 Wn.2d 372, 376, 535 P.2d 816 (1975) (emphasis added).

b. A Proper Interpretation of the State Farm Policy Language Requires State Farm to Pay a Share of Matsyuk's Legal Expense

Beginning with the Policy section regarding the PIP coverage, there is nothing in those provisions to indicate that any PIP payments to an insured will be made on behalf of anyone other than State Farm itself. *See* Policy, Personal Injury Protection Coverage Section, at 10-15 (CP 90-95). There is nothing to indicate, for example, that PIP payments will be made on behalf of a tortfeasor, another insured under the policy, or as advance liability payments. *See id.* Rather, the PIP "Insuring Agreement" makes it clear that the duty to provide the PIP benefits is a duty directly owed to the

PIP insured, and owed solely by State Farm: "***We*** will provide ***personal injury protection benefits*** to an ***insured*** for ***bodily injury*** sustained by that ***insured*** and caused by an ***automobile*** accident." Policy, Personal Injury Protection Coverage Section, at 11 (CP 91) (emphasis in original).

The foregoing is in contrast to the "Insuring Agreement" pertaining to the Liability Coverage, which makes it clear that any payments made will be not on State Farm's own behalf, but on behalf of its insured: "***We*** will pay: a. damages an ***insured*** becomes legally liable to pay because of: (1) ***bodily injury*** to others ...." Policy, Liability Coverage Section, at 6 (CP 86) (emphasis in original).

Under the provision governing State Farm's "Right to Recover Payments" applicable to PIP, the Policy provides, *inter alia*:

> (1) If ***we*** are obligated under this policy to make payment to or for a ***person*** who has a legal right to collect from another party, then ***we*** will be subrogated to that right to the extent of ***our*** payment.
>
> (2) If ***we*** make payment under this policy and the ***person*** to or for whom ***we*** make payment recovers or has recovered from another party, then that ***person*** must:
>
> ...
>
> (b) reimburse ***us*** to the extent of ***our*** payment.
>
> ...

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

Policy, General Terms Section, at 42 (CP 122) (emphasis in original).

Matsyuk received PIP from State Farm. She had a right to collect from another, Stremditskyy, and did so. Under the circumstances, and given the foregoing provisions, the average insured in Matsyuk's situation would interpret the Policy as meaning that the PIP payments were payments from State Farm on its own behalf, and that the liability payment by State Farm was made on behalf of Stremditskyy as its liable insured. The average insured would interpret the right to recovery language as meaning that State Farm had the right to seek recovery of the PIP payments its had made to her, subject to and limited by her right to first be fully compensated. Given that she would not be fully compensated if she were forced to bear all of the legal expense from a recovery that benefits them both, the average insured in Matsyuk's situation would interpret the policy as providing for a sharing of that legal expense.

As long as these are reasonable interpretations, any doubt or ambiguity in them they should be resolved in favor of the Matsyuk. In addition, further support for these interpretations is found in relevant Washington public policies, such as full compensation for insureds taking

precedence over insurer recoveries, that insureds not end up either better or worse off based on the vagaries of whether one insurer or two provide the relevant coverages, and that, similarly, insurance companies be treated uniformly.

C. THE COMPLAINT STATES VIABLE CLAIMS BASED ON STATE FARM'S ATTEMPT TO LINK THE LIABILITY SETTLEMENT TO A RELEASE OF SEPARATE CLAIMS AGAINST STATE FARM

The Complaint alleged that State Farm tried to use its position as UIM insurer as leverage in order to try to benefit itself at the expense of its PIP insured, Matsyuk. Specifically, that State Farm (initially) refused to effectuate the agreed liability settlement on behalf of Stremditskyy unless Matsyuk released claims as a PIP insured against State Farm. *See* Cmplt at 3, 6 (CP 5, 8). The Complaint sufficiently alleges that this misconduct caused her injury and damages. *See* Cmplt at 6 (CP 8). On the face of the Complaint, these allegations are sufficient to support viable claims for bad faith, CPA and breach of contract, and with at best a modest amendment, the claim for conversion.

To begin with, State Farm did not raise the issue in its motion to dismiss opening brief; its argument only came in its reply after Matsyuk pointed out that fact in her opposition brief. *See* CP 57. As a result, the issue was not properly before the trial court for purposes of the motion to

dismiss. Additionally, there is nothing to indicate that the trial court even considered, much less analyzed, this independent and alternative basis for three of the four claims in the Complaint (bad faith, CPA and breach of contract). These facts alone should result in remand. Furthermore, since the claims based on these allegations are not dependent on the resolution of the legal expense sharing issue, they stand viable regardless of the outcome of that question.

"[A]n insurer has a duty of good faith to its policyholder and violation of that duty may give rise to a tort action for bad faith."[15] *Smith v. Safeco Ins. Co.*, 150 Wn.2d 478, 484, 78 P.3d 1274 (2003) (citing *Truck Ins. Exch. v. Vanport Homes, Inc.*, 147 Wn.2d 751, 765, 58 P.3d 276 (2002)). An insured succeeds on a bad faith claim by showing that the insurer's breach of its contractual obligations was unreasonable, frivolous, or unfounded. *See id.* (citing *Overton v. Consol. Ins. Co.*, 145 Wn.2d 417, 433, 38 P.3d 322 (2002)).

Importantly, the insurers duty to act in good faith is separate from their coverage obligations to their insureds. *See, e.g., Safeco Ins. Co. v.*

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[15] The allegations that State Farm breached the duty of good faith it owed to Matsyuk suffices to establish that viable CPA and breach of contract claims are pled, in addition to the bad faith claim. *See, e.g., Industrial Indem. Co. of the Northwest, Inc. v. Kallevig*, 114 Wn.2d 907, 917, 921-22, 792 P.2d 520 (1990) (same acts and omissions by insurer constitute CPA violation and tort of bad faith). Thus, this discussion focuses on State Farm's duty of good faith and the conduct that Matsyuk asserts violates that duty.

Butler, 118 Wn.2d 383, 393, 823 P.2d 499 (1992); *Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 385-86, 715 P.2d 1133 (1986). This means that the insurer can commit actionable bad faith even if, for example, there is no coverage. *See, e.g., Coventry Assocs. v. American States Ins. Co.*, 136 Wn.2d 269, 279, 961 P.2d 933 (1998). Also, "[w]hether an insurer acted in bad faith is a question of fact." *Smith,* 150 Wn.2d at 484 (emphasis added) (citing *Van Noy v. State Farm Mut. Auto. Ins. Co.*, 142 Wn.2d 784, 796, 16 P.3d 574 (2001)).

Here, during the effectuation of the liability settlement on Stremditskyy's behalf, State Farm injected an entirely unrelated matter: a release of claims that Matsyuk might possess against State Farm as her PIP insurer. In doing so, State Farm was clearly not acting on behalf of Stremditskyy. Rather, State Farm was acing solely for its own benefit and in its own interest. More particularly, State Farm was acting in its interests in its capacity as Matsyuk's PIP insurer, and was placing its own interests above that of its PIP insured. If nothing else, it caused injury and damages Matsyuk by the resulting delay in completing the liability settlement and the lost time value of money that entailed. *See, e.g., Banuelos v. TSA Wash., Inc.*, 134 Wn. App. 603, 613-14, 141 P.3d 652 (2006). This is plainly sufficient to state a claim for bad faith. Whether

this conduct actually constitutes bad faith is ultimately to be determined by the trier of fact.

D. THE TRIAL COURT SHOULD HAVE GRANTED LEAVE TO AMEND TO ADDRESS ANY DEFICIENCIES IN THE COMPLAINT

In her opposition to State Farm's motion to dismiss, Matsyuk requested that she be granted leave to amend the Complaint to address any deficiencies found by the trial court. *See* CP 46. Amendment to pleadings is governed by CR 15, which provides that a "party may amend his pleading once as a matter of course at any time before a responsive pleading is served .... Otherwise, a party may amend his pleading only by leave of court or by written consent of the adverse party; and leave shall be freely given when justice so requires." (Emphasis added.) "The decision to grant leave to amend the pleadings is within the discretion of the trial court." *Wilson v. Horsley*, 137 Wn.2d 500, 505, 974 P.2d 316 (1999) (citations omitted). "These rules serve to facilitate proper decisions on the merits, to provide parties with adequate notice of the basis for claims and defenses asserted against them, and to allow amendment of the pleadings except where amendment would result in prejudice to the opposing party." *Wilson*, 137 Wn.2d at 505 (citations omitted). "The touchstone for denial of an amendment is the prejudice such amendment would cause the nonmoving party." *Caruso v. Local*

Union No. 690, 100 Wn.2d 343, 350, 670 P.2d 240 (1983) (citations omitted). The appellate court reviews the denial of leave to amend for abuse of discretion. *Id.* at 351 (citations omitted).

Since the trial court did not identify the basis for its decision, it is unclear what deficiencies the court found in plaintiff's allegations. But, as discussed above, even if the trial court believed that *Young* controlled over *Mahler*, *Winters* and *Hamm*, that would not provide a basis for the dismissal of claims based on the allegation that the insurance policy provided an independent basis for the legal expense sharing. Likewise, it would not provide a basis for dismissing claims based on the allegation that State Farm breached duties owed to Matsyuk as her PIP insurer by trying to leverage its position as the UIM insurer. Although Matsyuk submits that the order of dismissal should be reversed on these claims in any event, to the extent they might have been dismissed for unstated deficiencies, the trial court abused its discretion in not permitting an amendment to address them.

VI. CONCLUSION

The trial court apparently believed that Washington law did not require State Farm to bear a portion of its PIP insured's legal expense, and that this presented Matsyuk with an insuperable bar to relief. This is

erroneous on several grounds. First, it ignores the Complaint's allegations that the language of insurance policy itself provided a separate and independent basis for State Farm's obligation to bear a portion of Matsyuk's legal expense. It also ignores the Complaint's allegations that State Farm's conduct in trying to link the liability settlement with a release of claims against State Farm as PIP insurer provides another independent basis for relief.

Most fundamentally, however, the trial court erred when it failed to recognize that Washington law and public policy mandate that State Farm, as a PIP insurer recouping its payments, bear its fair share of the legal expense Matsyuk incurred to effect the liability recovery from Stremditskyy.

For the reasons stated, Matsyuk asks the Court to reverse the order of dismissal and remand this case to the trial court for further proceedings on the claims asserted. In addition, Matsyuk asks the Court to enter judgment as a matter of law in her favor on the issue of whether *Mahler*-type legal expense sharing is required of a PIP insurer in these circumstances.

May 18, 2009.

s/ Matthew J. Ide, WSBA No. 26002
Matthew J. Ide, WSBA No. 26002
IDE LAW OFFICE

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* * *

DECLARATION OF SERVICE

I certify that on May 18, 2009, I caused to be filed with the Supreme Court of the State of Washington, via electronic filing, the foregoing Opening Brief of Appellant Olga Matsyuk, and caused to be delivered, via messenger, true and accurate copies to:

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I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

Executed in Seattle, Washington, this 18th day of May, 2009.

s/ Matthew J. Ide, WSBA No. 26002
Matthew J. Ide

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