

COURT OF APPEALS  
DIVISION II

09 JUL 23 AM 9:52

NO. 38921-5-II

STATE OF WASHINGTON  
BY JW  
DEPUTY

COURT OF APPEALS STATE OF WASHINGTON  
DIVISION II

---

BRUCE CEDELL, a single man,

Plaintiff/Respondent,

v.

FARMERS INSURANCE COMPANY OF WASHINGTON,

Defendant/Appellant.

---

APPELLANT'S OPENING BRIEF

---

Curt H. Feig, WSBA #19890  
Michael A. Guadagno, WSBA #34633  
Attorneys for Petitioner

NICOLL BLACK & FEIG, PLLC  
816 Second Avenue, Suite 300  
Seattle, Washington 98104  
(206) 838-7555

F 111 1623 700 Exp.

TABLE OF CONTENTS

	Page
I. ASSIGNMENTS OF ERROR .....	1
<i>Assignments of Error</i> .....	1
<i>Issues Pertaining to Assignments of Error</i> .....	2
II. STATEMENT OF THE CASE.....	3
A. Factual Background .....	3
B. Discovery Dispute and Motion Practice.....	6
C. Grays Harbor County Superior Court's "Order Re: <i>In Camera Review</i> of Claim File," dated March 2, 2009.....	10
III. ARGUMENT.....	14
A. Standard of Review.....	14
B. The superior court erred by ordering the disclosure of confidential and privileged information with no basis to invoke the fraud exception to the attorney-client privilege.....	15
C. The superior court erred by ordering an <i>in camera</i> review of the claim file without a sufficient factual basis related to the fraud exception to the attorney-client privilege.....	21
D. The superior court erred by ordering the disclosure of the privileged materials without finding a "foundation in fact" for a claim of civil fraud.....	23
E. The superior court erred by ordering Farmers to pay terms payable to plaintiff that were excessive and not based on a <i>Lodestar</i> calculation.....	24
F. The superior court erred by ordering Farmers to pay sanctions payable to the court without any finding that Farmers violated a court order.....	27

V. CONCLUSION .....28

## TABLE OF AUTHORITIES

Page

### Washington State Cases

<i>Barry v. USAA</i> , 98 Wn. App. 199, 989 P.2d 1172 (1999)..	16, 20, 22
<i>Edmonds v. John L. Scott Real Estate, Inc.</i> , 87 Wn. App. 834 857, 942 P.2d 1072 (1997).....	26
<i>Ellwein v. Hartford Accident &amp; Indem. Co.</i> , 142 Wn. 2d 766 15 P.3d 640 (2001).....	20
<i>Escalante v. Sentry Ins. Co.</i> , 49 Wn. App. 375, 394, 743 P.2d 832 (1987).....	9, 16, 19, 21, 22, 23
<i>Fisher v. Allstate Ins. Co.</i> , 136 Wn.2d 240, 249, 961 P.2d 350 (1998).....	18
<i>In re Disciplinary Proceeding Against Schafer</i> , 1249 Wn.2d 148, 66 P.3d 1036 (2003).....	20
<i>John Doe v. Puget Sound Blood Ctr.</i> , 117 Wn.2d 772, 778, 819 P.2d 370 (1991).....	14
<i>Jones v. Allstate Ins. Co.</i> , 146 Wn.2d 291, 327, 45 P.3d 1068 (2002).....	16
<i>McGreevey v. Oregon Mut. Ins. Co.</i> , 90 Wn. App. 283, 291, 951 P.2d 798 (1998).....	26
<i>Seattle Northwest Securities Corp. v. SDG Holding Co.</i> , 61 Wn. App. 725, 740, 812 P.2d 488 (1991).....	23
<i>State v. Lewis</i> , 115 Wash.2d 294, 298-299, 797 P.2d 1141 (1990)	15
<i>State v. Rohrich</i> , 149 Wn.2d 647, 654, 71 P.3d 638 (2003).....	15

<i>State ex rel. Carroll v. Junker</i> , 79 Wn.2d 12, 26, 482 P.2d 775 (1971).....	14
<i>State ex rel. Clark v. Hogan</i> , 49 Wn.2d 457, 462, 303 P.2d 290 (1956).....	14
<i>Van Noy v. State Farm Mut. Auto. Ins. Co.</i> , 142 Wn.2d 784, 791, 16 P.3d 574 (2001).....	16

**Non-Washington State Cases**

<i>Baker v. CNA Ins. Co.</i> , 123 F.R.D. 332, 336 (D. Mont. 1988).....	18
<i>Ferrara v. DiMercurio, Inc. v. St. Paul Mercury Ins. Co.</i> , 173 F.R.D. 7 (1997).....	20
<i>Haines v. Liggett Group, Inc.</i> , 975 F.2d 81, 95-96 (3d Cir. 1992).....	20, 22
<i>Hartford Financial Services Group, Inc. v. Lake County Park and Recreation Board</i> , 717 N.E.2d 1232 (1999).....	20
<i>Lexington Ins. Co. v. Swanson</i> , 240 F.R.D. 662 (W. D. Wash. 2007).....	20
<i>Ring v. Commercial Union Ins. Co.</i> , 159 F.R.D. 653 (1995).....	20
<i>Silva v. Fire Ins. Exch.</i> , 112 F.R.D. 699 (D. Mont. 1986).....	17

**Rules and Regulations**

CR 11.....	13
CR 26.....	13
CR 26(g).....	24, 25, 27
CR 37(a)(4).....	24, 25
CR 37(b).....	27

## I. ASSIGNMENTS OF ERROR

### *Assignments of Error*

1. The superior court erred by ordering the disclosure of confidential and privileged information with no basis to invoke the fraud exception to the attorney-client privilege.

2. The superior court erred by concluding that in the first-party insurance claim context the insurer has a fiduciary duty to its insured.

3. The superior court erred by ordering an *in camera* review of the claim file without a sufficient factual basis for invoking the fraud exception to the attorney-client privilege.

4. The superior court erred by ordering the disclosure and production of the privileged materials without finding a “foundation in fact” for the charge of civil fraud.

5. The superior court erred by ordering Farmers to pay terms payable to plaintiff that were excessive and not based on a *Lodestar* calculation.

6. The superior court erred by ordering Farmers to pay sanctions payable to the court without any finding that Farmers violated a court order.

*Issues Pertaining to Assignments of Error*

1. Should the superior court have denied plaintiff's request for disclosure of confidential and privileged information where there existed no basis to invoke the fraud exception to the attorney-client privilege?

2. Did the superior court commit error in concluding that in the first-party insurance claim context an insurer has a fiduciary duty to its insured under existing Washington law?

3. Should the superior court have declined to conduct an *in camera* review of the claim file where there was no factual basis for invoking the fraud exception to the attorney-client privilege?

4. Should the superior court have denied plaintiff's request for the disclosure and production of the privileged materials without finding a "foundation in fact" for the charge of civil fraud?

5. Did the superior court commit error when it ordered Farmers to pay terms payable to plaintiff that were excessive and not based on a *Lodestar* calculation?

6. Did the superior court commit error when it ordered Farmers to pay sanctions payable to the court without any finding that Farmers violated a court order?

## **II. STATEMENT OF THE CASE**

Farmers asks that this court reverse the superior court's order denying Farmers' Motion for Protective Order and granting plaintiff's Motion to Compel. The superior court's order effectively found that no insurer is entitled to the protections afforded under the attorney-client privilege when sued for bad faith.

This case involves an insurance coverage dispute that arises from a suspicious fire occurring at the plaintiff/respondent's residence, located at 1211 Young Street, Elma, Washington.

### **A. Factual Background.**

Farmers issued a Homeowners Policy to Mr. Cedell insuring his residence and contents against certain covered occurrences, including fire. CP 364-65. On November 24, 2006, Mr. Cedell's

property caught fire. CP 365-68. On the day of the loss, Mr. Cedell was at his residence with his girlfriend, Melissa Ackley. *Id.* Although Mr. Cedell allegedly left his residence immediately before the fire took place, Ms. Ackley was present during the entire loss. *Id.*

Mr. Cedell reported the loss to Farmers 5 days later, and Farmers began its investigation. *Id.* During Farmers' investigation, however, Mr. Cedell and Ms. Ackley provided false information to Farmers' investigator. *Id.* They had also provided inconsistent stories in their Examinations Under Oath. *Id.* Ms. Ackley also admitted to engaging in criminal activity at the residence on the day of loss. *Id.*

The policy provided exclusions for intentional acts and for intentionally concealing or misrepresenting any material fact or circumstance relating to a loss. CP 364-65. The policy also required Mr. Cedell to report any loss immediately thereafter and cooperate in all investigations. *Id.* Given Mr. Cedell's failure to immediately report the loss, his failure to provide truthful testimony to Farmers regarding the loss, and his admission that criminal activity had

occurred in close proximity – in both location and time – to the loss, Farmers undertook a lengthy investigation and was unable to make an immediate coverage determination. CP 365-68. Additionally, Farmers retained counsel to advise it on legal issues in making a coverage determination. *Id.*

During Farmers' investigation, the City of Elma Fire Department concluded that the fire was probably caused accidentally. CP 456-61; *see also* CP 474-77. Further, Farmers' investigator reported that the fire was consistent with an accidental burning of a candle, as described by Ms. Ackley. *Id.* Both reports, however, relied in large part on false information provided by Ms. Ackley. CP 365-68. Ultimately, through its investigation, Farmers estimated the damage to the property to range between \$56,498.84 and \$90,000. CP 458-60.

Despite the numerous bases on which to deny coverage pursuant to the Policy's Conditions and Exclusions, Farmers offered \$30,000 to Mr. Cedell in compromise of his disputed claim. CP 458; *see also* CP 465-68. The offer explained that Farmers had several bases on which to deny coverage, and listed each reason. *Id.*

The offer was made as a “one-time only offer” and remained open for 10 days. *Id.*

On November 5, 2007, plaintiff filed suit in Grays Harbor County Superior Court against Farmers for breach of contract and bad faith. CP 336-40; 331-335.

**B. Discovery Dispute and Motion Practice.**

During discovery, plaintiff propounded Interrogatories and Requests for Production to Farmers. CP 9-18. The discovery requests sought both privileged and non-privileged materials. *Id.*

In response to the discovery requests, Farmers produced its entire claim file, redacting or withholding only portions thereof containing information protected by the attorney-client privilege and work product doctrine. CP 9-313.<sup>1</sup> When Farmers produced its claim file to plaintiff’s counsel on January 25, 2008, it included a privilege log identifying those documents withheld or redacted and the basis for the withholding or redaction. CP 341-61.

---

<sup>1</sup> As a side note, Farmers also redacted “reserve” information from the claim file on the basis of relevance. *Id.* The superior court ordered Farmers to produce “reserve” information even though plaintiff did not specifically seek that information in his Motion to Compel. CP 490-96.

Over one year later, on January 28, 2009, plaintiff moved to compel the production of the redacted, privileged information, CP 1-8, arguing that no insurer is entitled to protections afforded by the attorney-client privilege or work product protection in any bad faith litigation. CP 2-3; *see also* CP 6 (“Farmers claimed the attorney-client privilege, which we believe does not apply in this bad faith litigation.”).

On February 10, 2009, Farmers filed its opposition to the motion and filed a Cross-Motion for Protective Order Re: Privileged Information. CP 363-76. Farmers argued that insurers are afforded the same protections under the attorney-client privilege and work product doctrine in bad faith litigation as any other client in any other litigation. CP 369-76.

On February 13, 2009, plaintiff filed a supplemental “Memorandum Re: Attorney-Client Privilege Work Product / Protective Order,” and abandoned his argument that the attorney-client privilege and work product doctrine do not apply. CP 456-65. Instead, he acknowledged that the privilege and protection do apply, but argued that the fraud exception should apply in the context of his

lawsuit. CP 461-65. In support of that argument, plaintiff indicated that he “suspected” (VRP 5:2) that Farmers attempted to commit a civil fraud, because (1) it had given plaintiff a “one time offer only” that plaintiff felt was insufficient; CP 464, ll. 22-32; and (2) Farmers’ valuation of the damaged property “proved to be wholly inadequate and possibly even fraudulent”; CP 458, ll. 18-19. Plaintiff offered no other evidence to support its contention that Farmers engaged in fraudulent conduct. *See generally*, 456-471; Verbatim Report of Proceedings (VRP) 2-25.

The motions were heard on February 23, 2009. VRP 1. At oral argument, plaintiff again acknowledged that the privilege and protection apply, but argued that he had met the factual showing necessary to invoke the fraud exception to the privileges. VRP 2-3. Farmers argued that plaintiff was not entitled to the redacted or withheld information, because it was protected by the attorney-client privilege. VRP 10-17. Farmers argued that the fraud exception to the privilege did not apply, because plaintiff failed to present a sufficient factual showing to establish a good faith belief by a reasonable person that wrongful conduct occurred rising to the level

of civil fraud. VRP 13:12 – 17:13. Relying on *Escalante v. Sentry Ins. Co.*, 49 Wn. App. 375, 743 P.2d 832 (1987), Farmers also argued that plaintiff was not entitled to request an *in camera* review of the documents, because he had failed to make a sufficient factual showing of fraudulent conduct. *Id.*

With respect to the attorney-client privilege *Escalante* says that the trial court may in its discretion conduct an *in camera* inspection of the requested documents. However, that *in camera* inspection may not occur **unless the discovering party establishes a factual showing adequate to support a good faith belief by a reasonable person that wrongful conduct sufficient to invoke the fraud exception to the privilege has occurred.** The only evidence that has been presented to this Court saying that fraud existed here, which is a nine element claim ... is found on [Pages 3 and 9 of plaintiff's brief]. [On page 9,] Mr. Cedell claims that Farmers attempted to commit a civil fraud upon him by giving him a one-time only offer at \$30,000 on such and such a date, period, suggesting it was coercive.

On Page 3, [Mr. Cedell claims that the valuation ... by Farmers, [“] proved to be wholly inadequate.[”] ... [“][a]nd possibly even fraudulent.[“] Mr. Olson, Mr. Cedell's counsel here, stated in his argument, I suspect there was fraud here but that's not the test. That doesn't get you over the burden of – of having the Court conduct an *in camera* review. It's required that a factual showing be made, [a] good faith belief by a reasonable person that wrongful conduct sufficient to invoke the fraud exception has occurred. Only then does the Court get to do an *in camera* inspection. In

the *in camera* inspection the Court **then** determines whether [the] attorney-client privilege applies to the documents, materials, information at issue, and then the Court determines whether [the discovering party] have overcome the privilege by showing [a] foundation in fact for civil fraud.

What the *Escalante* case did not hold is that bad faith equals civil fraud. No case has ever held that.

VRP 14:1 – 15:8 (emphasis added).

**C. Grays Harbor County Superior Court’s “Order Re: *In Camera* Review of Claim File,” dated March 2, 2009.**

In its oral ruling of February 23, 2009, the superior court judge implicitly found that the privilege applied, but ruled that plaintiff had made a factual showing adequate to support a good faith belief by a reasonable person that wrongful conduct sufficient to invoke the fraud exception to the attorney-client privilege had occurred. VRP 20:20 – 21:8.

As to the claim file and the redacted materials which range from claims of attorney-client privilege, to work product, to relevancy, I’m going to order that they be produced for an *in camera* inspection by me. I do not agree with your [Mr. Guadagno’s] summary of *Escalante*. *Escalante* doesn’t require that I make a – a finding of civil fraud. **It requires that – that the Court find that there is at least some found – some foundation and [sic] fact to support a good faith belief by reasonable person that – that there may**

**have been wrongful conduct which could invoke the fraud exception** and the facts recited here, particularly surrounding the offer from Mr. Hall and – and how inconsistent it appeared to be with Farmers own appraisal evidence and the fact that it – there was a very short time placed on – on the offer.

VRP 20:20 – 21:8 (emphasis added). The superior court judge ruled the “inconsistency” between Farmers’ valuation of the damaged property and the short time limit placed on the offer to settle were sufficient to justify an *in camera* inspection. *Id.*; CP 490-94. As such, the superior court judge ordered the *in camera* review of the privileged materials to determine whether the materials that were redacted indeed qualified as attorney-client information. *Id.*; CP 495.

On February 25, 2009, Farmers complied with the superior court’s order and produced its entire claim file with no redactions. CP 510. On the same day, the superior court judge conducted an *in camera* review of the redacted portions of Farmers’ claim file. *Id.* On February 26, 2009, the superior court judge issued a letter ruling, which was later entered as an “Order Re: *In Camera* Review of Claim File” on March 2, 2009. CP 509-14. The superior court judge did **not** find that the information reviewed *in camera* established a “foundation in fact” for the charge of civil fraud. *See*

*generally, id.* Instead, the order effectively finds that insurers are never entitled to the protection afforded under the attorney-client privilege or work product doctrine in bad faith litigation. *Id.*

The present litigation arises from a fire damage claim and not a UIM claim. The decision in *Escalante* may have limited application to the facts and circumstances of the present case.

**In the context of a claim arising from a residential fire, the insurer owes the insured a heightened duty – a fiduciary duty, which by its nature is not, and should not be, adversarial. Under such circumstances, the insured is entitled to discover the entire claims file kept by the insured without exceptions for any claims of attorney-clients privilege.**

CP 511-12 (emphasis added).

The superior court judge concluded that Farmers was therefore not entitled to redact or withhold any privileged information and ordered Farmers to produce and disclose all confidential and privileged communications to Mr. Cedell and his counsel by Friday, March 6, 2009. CP 513-14. The superior court did not indicate in its letter ruling, or at any time, why the *in camera* review was even necessary, given the court's conclusions regarding the inapplicability of the privilege. *See generally*, CP 509-14.

The superior court judge also imposed terms in the amount of \$15,000 to be paid to plaintiff and sanctions of \$25,000 to be paid to the court.<sup>2</sup> *Id.* These terms and sanctions were imposed for two reasons only: (1) because Farmers redacted “reserve” information on the basis of privilege and did not immediately move for a protective order; and (2) because Farmers redacted information protected by the attorney-client privilege and the work product doctrine where the superior court found no privilege applied. *Id.* The superior court did not indicate what portion of the terms or sanctions applied to which of the two violations. *Id.* However, the portion of the sanctions that were imposed due to the redactions of the “reserve” information is not at issue in this appeal. This appeal is limited solely to the application of the attorney-client privilege and work product doctrine and the sanctions that follow therefrom.

---

<sup>2</sup> With respect to plaintiff’s discovery requests seeking non-privileged materials, the superior court found that Farmers’ objections and answers violated CR 11 and CR 26 and imposed up to \$7,500 in sanctions. *Id.* This portion of the superior court’s orders is *not* at issue in this appeal as Farmers has paid \$5,000 in sanctions to the Grays Harbor County Superior Court and does not challenge the \$2,500 in terms awarded to Mr. Cedell. For purposes of this appeal only, Farmers does not contest the superior court’s order with respect to the non-privileged aspects of plaintiff’s discovery requests. These earlier terms and sanctions were imposed by the Court before it conducted its *in camera* inspection and based on its conclusion that Farmers’ answers to plaintiff’s interrogatories were inadequate.

On March 10, 2009, this Court accepted discretionary review of the superior court's orders and entered a stay of all superior court proceedings pending appeal.

### III. ARGUMENT

#### A. Standard of Review

An appellate court reviews a superior court's discovery order for an abuse of discretion. *John Doe v. Puget Sound Blood Ctr.*, 117 Wn.2d 772, 778, 819 P.2d 370 (1991). Judicial discretion "means a sound judgment which is not exercised arbitrarily, but with regard to what is right and equitable under the circumstances and the law, and which is directed by the reasoning conscience of the judge to a just result." *State ex rel. Clark v. Hogan*, 49 Wn.2d 457, 462, 303 P.2d 290 (1956). An appellate court will find an abuse of discretion "on a clear showing" that the court's exercise of discretion was "manifestly unreasonable, or exercised on untenable grounds, or for untenable reasons." *State ex rel. Carroll v. Junker*, 79 Wn.2d 12, 26, 482 P.2d 775 (1971). A superior court's discretionary decision "is based 'on untenable grounds' or made 'for untenable reasons' if it rests on facts unsupported in the record or was reached by applying the wrong

legal standard.” *Id.* at 423-24 (citing *State v. Rohrich*, 149 Wn.2d 647, 654, 71 P.3d 638 (2003)). A court’s exercise of discretion is “manifestly unreasonable” if “the court, despite applying the correct legal standard to the supported facts, adopts a view ‘that no reasonable person would take.’” *Id.* at 424 (quoting *State v. Lewis*, 115 Wash.2d 294, 298-99, 797 P.2d 1141 (1990)).

**B. The superior court abused its discretion by ordering the disclosure of confidential and privileged information with no basis to invoke the fraud exception to the attorney-client privilege.**

In the present case, although Farmers had already produced its entire claim file redacting or withholding privileged and protected information only, the superior court erroneously ordered production of all privileged information by Friday, March 6, 2009, at 5:00 pm. In support of this order, the superior court effectively held that no insurer is ever entitled to the protections afforded by the attorney-client privilege and the work product doctrine where that insurer is sued for violations of the Consumer Protection Act or for bad faith.

In the context of a claim arising from a residential fire, the insurer owes the insured a heightened duty – a fiduciary duty, which by its nature is not, and should not be, adversarial. Under such circumstances, the insured is entitled to discover the entire claims file

kept by the insured without exceptions for any claims of attorney-client privilege. ... In the present case, the defendant's claims of attorney-client privilege are without merit. The plaintiff is entitled to receive all documents which were withheld and/or redacted in reliance upon the attorney-client privilege.<sup>3</sup>

CP 512. Notably, the superior court did not evaluate whether the redacted information qualifies as attorney-client communications. Instead, the superior court ruled that Farmers is entitled to no such privilege at all. This order is directly contrary to Washington law.

In support of its ruling, the superior court referred to *Escalante v. Sentry Ins. Co.*, 49 Wn. App. 375, 743 P.2d 832 (1987) and purported to rely on *Barry v. USAA*, 98 Wn. App. 199, 989 P.2d 1172 (1999). These two cases involved discovery disputes arising in the context of UIM claims. The court acknowledged that these two cases cited to a case from another jurisdiction, which simply stated:

---

<sup>3</sup> The superior court also committed obvious error in concluding that in the first-party insurance claim context the insurer has a fiduciary duty to its insured. Washington law has found nothing more than a "quasi-fiduciary" duty in which the insurer is entitled to treat its interest equally with that of its insured. See, e.g., *Van Noy v. State Farm Mut. Auto. Ins. Co.*, 142 Wn.2d 784, 791, 16 P.3d 574 (2001) ("[the quasi-fiduciary relationship] requires an insurer to deal fairly with an insured, giving equal consideration in all matters to the insured's interests as well as its own."); *Jones v. Allstate Ins. Co.*, 146 Wn.2d 291, 327, 45 P.3d 1068 (2002), reconsideration denied ("this court has made it clear that an insurer is not a true fiduciary even to its insured. Rather, an insurer's duty is one of good faith. '[A]n insurer must deal fairly with an insured, giving equal consideration in all matters to the insured's interests.'" (quoting *Van Noy*, supra)).

The time-worn claims of work product and attorney-client privilege cannot be invoked to the insurance company's benefit where the only issue in the case is whether the company breached its duty of good faith in processing the insured's claim.

*Silva v. Fire Ins. Exch.*, 112 F.R.D. 699 (D. Mont. 1986). The *Barry* case quoted this section from *Silva* and then held further: "We have good reason to treat first-party bad faith claims involving the processing of UIM claims differently, however." From these three cases, the superior court in this case erroneously held that an insurer's right to the protections afforded by the attorney-client privilege and the work product doctrine are limited to UIM claims.

Significantly, however, no case has ever applied the *Silva* rule stripping an insurer's claim file of the attorney-client privilege and work product doctrine outside of the UIM context. The only Washington cases to address the *Silva* case are *Barry* and *Escalante*. Each of these cases involved a UIM claim, and in each of these cases, the Washington Courts of Appeals declined to apply the *Silva* case in the context of a UIM claim. The reason why the courts declined to follow *Silva* – and, thus, why Farmers correctly chose to

redact privileged information in its claim file in this case – is key to understanding the basis of this appeal.

The superior court failed to recognize that the *Barry* and *Escalante* cases were distinguishing UIM claims from situations where “[an] attorney is engaged and paid by the carrier to defend the insured and therefore operates on behalf of two clients.” *Barry*, 98 Wn. App. at 204 (citing *Baker v. CNA Ins. Co.*, 123 F.R.D. 322, 326 (D. Mont. 1988)). The *Barry* case further holds that insurers in a UIM setting should be afforded the protections of the attorney-client privilege, “[b]ecause the provision of UIM coverage is by nature adversarial [and] an inevitable conflict exists between the UIM carrier and the UIM insured.” *Id.* at 205 (citing *Fisher v. Allstate Ins. Co.*, 136 Wn.2d 240, 249, 961 P.2d 350 (1998)). Again, the *Barry* case was distinguishing UIM claims – not from **all** first party coverage disputes – but from situation where an attorney is engaged and paid by the carrier to defend the insured.

The friction between this adversarial relationship and the traditional fiduciary relationship of an insured and an insurer is difficult to resolve. The difficulty is complicated by those cases where an attorney represents an insured in an action against the tortfeasor and then must represent the carrier when the insured

makes a UIM claim. Such was not the case here, however. **Considering the fact that [the insurer's] attorney was only involved in [the insured's] UIM claim, it follows that communications between [the insurer] and its attorney concerning the UIM claim are privileged for the purposes of [the insured's] bad faith insurance suit.**

*Id.* at 205 (emphasis added). Thus, *Barry* stands for the proposition that an insurer is entitled to the protections afforded by the attorney-client privilege – not only in UIM claims – but in any first party coverage disputes where the insurer's attorney is retained solely to represent the carrier only in an adversarial setting with its insured. That is precisely the situation here.

Thus, the single sentence from *Silva*, which *Barry* and *Escalante* quoted in *dicta*, and on which the superior court relied, has extremely limited precedential value. Further, the two-page *Silva* ruling neither refers to nor relies on any law or case in support of its conclusion. Instead, the *Silva* court fabricates its rule out of whole cloth.

Washington courts have consistently held that insurers are entitled to the protections afforded under the attorney-client privilege and work product doctrine. *See, e.g., Escalante*, 49 Wn.

App. 375, *reversed on other grounds*, *Ellwein v. Hartford Accident & Indem. Co.*, 142 Wn.2d 766, 15 P.3d 640 (2001); *Barry*, 98 Wn. App. 199; *Lexington Ins. Co. v. Swanson*, 240 F.R.D. 662 (W. D. Wash. 2007). Nothing contained in *Escalante* or *Barry* explicitly or implicitly limits the protections afforded under the attorney-client privilege to UIM claims alone.

Other jurisdictions recognize the same protections. *See, e.g.*, *Hartford Financial Services Group, Inc. v. Lake County Park and Recreation Board*, 717 N.E.2d 1232 (1999) (Indiana law); *Ferrara v. DiMercurio, Inc. v. St. Paul Mercury Ins. Co.*, 173 F.R.D. 7 (1997) (Massachusetts law); *Ring v. Commercial Union Ins. Co.*, 159 F.R.D. 653 (1995) (Montana law); *Haines v. Liggett Group, Inc.*, 975 F.2d 81, 95-96 (3d Cir. 1992)).

The court's ruling here – that Farmers was not entitled to the protections afforded from the attorney-client privilege – is directly contrary to Washington law and creates an unprecedented exception to one of the most fundamental privileges recognized in our judicial system. *See generally In re Disciplinary Proceeding Against Schafer*, 149 Wn.2d 148, 66 P.3d 1036 (2003) (“While we laud the

principles protecting the sanctity of attorney-client confidences and secrets, we are cognizant that there are occasions when revealing a client's statements may be justified. These occasions are extremely limited, however, consistent with the profession's goals of establishing and maintaining trust in the judicial process.'"). In doing so, the superior court abused its discretion and this Court should reverse its order for the disclosure of confidential and privileged information.

**C. The superior court abused its discretion by ordering an *in camera* review of the claim file without a sufficient factual basis related to the fraud exception to the attorney-client privilege.**

Under *Escalante*, Washington law **acknowledges the protections of the attorney-client privilege** and protects confidential communications between an insurer and its counsel unless an insured can establish that they qualify for the fraud exception. *Escalante*, 49 Wn. App. at 394. Generally, the exception is invoked only when the insured presents a prima facie showing of bad faith tantamount to civil fraud. *Id.* To strip a communication of the attorney-client privilege, the insured must show that (1) the insurer was engaged in or planning a fraud at the time the privileged

communication was made, and (2) the communication was made in furtherance of that activity. *Id.*; *Barry*, 98 Wn. App. at 205 (citing *Haines*, 975 F.2d at 95-96).

Even to warrant an *in camera* review, the insured must make a “factual showing adequate to support a good faith belief by a reasonable person that wrongful conduct sufficient to invoke the ... fraud exception ... has occurred.” *Escalante*, 49 Wn. App. at 394. Here, the superior court found that there was such a good faith belief based solely on the alleged “inconsistency” between Farmers’ valuation of the damaged property in the context of a disputed, suspicious claim, and the short time limit placed on the offer to settle. The trial court based its “good faith belief” that Farmers committed fraud on nothing else.

Under *Barry*, the “good faith belief” is not satisfied by mere evidence of bad faith or CPA violations. *Barry*, 98 Wn. App. at 206-07. More is needed. *Id.* In *Barry*, the insured sought an *in camera* review of the insurer’s claim file and argued that there was a factual basis to support a good faith belief that the insurer had committed fraud. The insured based this assertion on her allegations that the

insurer had significantly delayed responding to and settling her claim. However, the Court of Appeals ruled that such evidence was insufficient to support a good faith belief that the insurer had committed fraud.

Accordingly, the superior court's determination here that Farmers engaged in fraud based on virtually identical facts is an abuse of discretion, and this Court should reverse its order.

**D. The superior court abused its discretion by ordering the disclosure and production of the privileged materials without finding a “foundation in fact” for a claim of civil fraud.**

Even if there exists a factual basis to support a good faith belief that an insurer committed fraud, that is insufficient to invade the privilege. In order to strip a communication of the attorney-client privilege, the court must “subject[] the documents to an *in camera* inspection to determine whether there is a foundation in fact for the charge of civil fraud.” *Escalante*, 49 Wn. App. at 394; *Barry*, 98 Wn. App. at 206 (citing *Seattle Northwest Securities Corp. v. SDG Holding Co.*, 61 Wn. App. 725, 740, 812 P.2d 488 (1991)). Here, the superior court conducted the *in camera* review, but then failed to determine whether any redacted portions of the claim file

supported a foundation in fact for the charge of civil fraud. Indeed, the superior court's letter ruling failed to provide any analysis whatsoever – or even any allegation, supported or otherwise – of any fraudulent conduct on the part of Farmers. Instead, the letter ruling finds only that Farmers is not entitled to the privilege at all.

Accordingly, the superior court's order to produce and disclose the privileged materials contained in the claim file constitutes an abuse of discretion, and this Court should reverse its decision.

**E. The superior court abused its discretion by ordering Farmers to pay terms payable to plaintiff that were excessive and not based on a *Lodestar* calculation.**

The superior court erroneously ordered that Farmers pay \$15,000 in terms to plaintiff and \$25,000 in sanctions to the Court over a simple motion to compel involving no complex issue of law. The portion of the award involving \$15,000 in terms to plaintiff violates both CR 26(g) and CR 37(a)(4). Under CR 26(g), a superior court may only impose terms if it finds that an attorney, by signing responses and/or objections to a discovery request, violated his certification that “to the best of his knowledge, information, and

belief formed after a reasonable inquiry it is ... consistent with [the civil rules] and warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law[.]” Given that no Washington case has ever before applied the *Silva* case to any first party coverage disputes (whether or not involving a UIM claim), Farmers’ decision to redact privileged information from its claim file did not constitute a violation of CR 26(g), and the Court’s imposition of terms for that redaction and withholding is an abuse of discretion. Therefore, this Court should reverse the superior court’s order of terms.

Further, CR 37(a)(4) limits the terms a superior court can order to “reasonable expenses incurred in obtaining the order, including attorney fees, unless the court finds that the opposition to the motion was substantially justified or that other circumstances make an award of expenses unjust.” CR 37(a)(4). At a rate of \$200 per hour, the superior court’s terms of \$15,000 constitutes 75 hours worth of attorneys fees. By comparison, plaintiff’s counsel has charged approximately \$35,000 in total attorneys fees in this case

since its inception. Plaintiff's counsel requested only \$750 in terms for the motion. CP 8.

In awarding attorney fees, Washington courts follow a well-settled formula. Attorney fee awards are calculated by using the lodestar method to establish the fee award and then adjusting the award up or down. *Edmonds v. John L. Scott Real Estate, Inc.*, 87 Wn. App. 834, 857, 942 P.2d 1072 (1997). The lodestar award is determined by multiplying a reasonable hourly rate by the number of hours reasonably expended on the matter. *McGreevy v. Oregon Mut. Ins. Co.*, 90 Wn. App. 283, 291, 951 P.2d 798 (1998).

In the present case, no bill affidavit was filed by plaintiff's counsel. Instead, the superior court arbitrarily selected \$15,000 as a sanction to award to plaintiff. The court failed to engage in the lodestar inquiry in any form whatsoever. In fact, the superior court specifically indicated that "[i]t is impossible to determine the full extent of the additional time expended and expense incurred by plaintiff as a result of being denied access to this information." CP 513. It appears that such a determination was impossible because the court had absolutely no information regarding fees or costs

associated with the motion when it made the award. Accordingly, the superior court's determination that Farmers must pay \$15,000 to plaintiff is an abuse of discretion, and this Court should reverse the decision.

**F. The superior court abused its discretion by ordering Farmers pay sanctions payable to the court without any finding that Farmers violated a court order.**

The superior court's order for Farmers to pay \$40,000 in terms and sanctions included \$25,000 in sanctions to be paid to the court. This portion of the award violated CR 26(g) and CR 37(b).

As noted above, sanctions under CR 26(g) are inappropriate given Washington courts' limited analysis of the *Silva* decision. It does not constitute a violation of an attorneys' or party's certification to argue that Washington courts' **rejection** of the *Silva* case cannot be deemed as an automatic outright **acceptance** of the rule in all other circumstances. Thus, any sanctions against Farmers under CR 26(g) is error.

Further, CR 37(b) limits a superior court's authority to impose sanctions payable to the court to situations that involve a

party's failure to obey a court order. *See* CR 37(b). In the present case, Farmers has not violated any court orders.

Accordingly, the superior court's order for Farmers to pay \$25,000 to the court is an abuse of discretion, and this Court should reverse its decision.

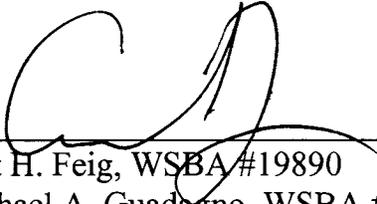
#### IV. CONCLUSION

This Court should reverse the superior court's Findings and Order, dated March 2, 2009, and Order Re: In Camera Review of Claim File, dated March 2, 2009, as they each relate to the issues addressed herein.

RESPECTFULLY SUBMITTED this 22nd day of July, 2009.

NICOLL BLACK & FEIG

By: \_\_\_\_\_

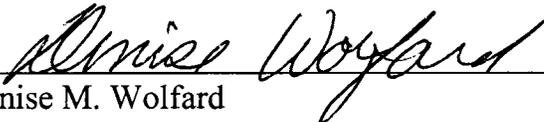
  
Curt H. Feig, WSBA #19890  
Michael A. Guadagno, WSBA #34633  
Of Attorneys for Petitioner

**CERTIFICATE**

The undersigned certifies under penalty of perjury under the laws of the State of Washington, that on July 22, 2009, I caused service of the foregoing pleading on each and every attorney of record herein:

Stephen L. Olson (via overnight mail)  
Olson Zabriskie & Campbell, Inc.  
104 West Marcy Avenue  
Montesano, Washington 98563

DATED this 22nd day of July, 2009, in Seattle, Washington.

  
\_\_\_\_\_  
Denise M. Wolfard