CLM CLAIMS & LITIGATION MANAGEMENT ALLIANCE™

ADVANCING ETHICS, COOPERATION AND EDUCATION

2014 CLM Annual Conference

April 9, 2014 – April 11, 2014

Boca Raton Resort
501 E. Camino Real
Boca Raton, FL 33432

Roundtable 3: Thursday, April 10, 2014 (3:30 pm – 4:30 pm)

The Vanishing Privileges: A Discussion of Attorney-Client and Work Product Privileges in Bad Faith Cases and How to Best Protect Confidential Communications

1. Traditional Breadth and Scope of Privileges

Attorney-Client Privilege is the Oldest Evidentiary Privilege Known to the Common Law Whose Purpose is to Encourage Full and Frank Conversations and Enable Attorneys to Give Sound Legal Advice - *Upjohn v. United States*, 449 U.S. 383, 389 (1981).

Privilege was accepted in cases as early as the reign of Elizabeth I in the Sixteenth Century.

Purpose was to protect the attorney from violating his honor as a "gentleman" and testifying against his client. The attorney held the privilege.

Today, the privilege belongs to the client and can only be raised or waived by the client.

A. Attorney-Client Privilege – Four Elements Required

i. Communication;

ii. Between Client and Counsel;

iii. Made in Confidence; and

iv. For Purpose of Getting or Giving Legal Advice.

B. Work-Product Privilege - Broader than the attorney-client privilege – and of more recent vintage - the work-product privilege includes materials prepared by persons other than the attorney. The materials may have been prepared by anybody as long as they were prepared **in anticipation of litigation**. Additionally, it includes materials collected for the

attorney for the prosecution or defense of a case including mental impressions, conclusions, opinions, or legal theories – First established in the case of *Hickman v. Taylor*, 329 U.S. 495 (1947).

i. Fact Work-Product – can be obtained if party can show need and inability to obtain facts any other way.

ii. Opinion/Core Work-Product – virtually sacrosanct.

iii. Does not Include Documents Prepared in the Ordinary Course of Business – But For Test.

C. Who is the Client for Attorney-Client Communications?

i. Can be Individual or Corporation.

ii. If the Client is a Corporation then Individual Employees of the Corporation are Generally Not Being Represented by the Same Attorney and should be informed accordingly.

iii. Most State's Ethical Rules Require Disclosure: A lawyer should explain the identity of the client when the lawyer knows or reasonably should know that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing. In such circumstances, the attorney needs to advise the organization's directors, officers, employees, members, shareholders or other constituents that discussions with counsel may not be privileged, that the corporation retains the right to waive privilege, and that the employee may wish to obtain individual counsel. C.R.P.C. 3-600.

iv. Three Tests Have Evolved in the Different State Jurisdictions to Determine Who is the Client in a Corporate Setting:

1. The Control-Group test is the most-narrow application of privilege. It provides that the client is only someone from the group of people who can control or be significantly involved in the direction of the company;

2. The Subject-Matter test is when an employee is a client for purposes of attorney-client privilege if the communication occurred at the direction of the employee's superior and the subject matter of the communication falls within the scope of the employee's duties; and

3. The Upjohn test is similar to the subject-matter test but slightly more flexible. Under this test, an employee is a client for purposes of attorney-client privilege if the employee made the communication to in-house counsel at the direction of the employee's superior, the communication related to the employee's duties, individuals within the control group did not possess the information, and the employee knew that the

communication was being made so that the company could obtain legal advice.

2. <u>Privilege May or May Not Attach To Third Parties</u>

A. Functional Equivalent Doctrine – Are Third Parties Acting In the Role/Function of an Employee?

B. Outside Insurance Adjuster, the court in *Residential Constructors v. Ace Property & Casualty Insurance Co.* noted:

> The Court sees no rational distinction between applying the attorney-client privilege to confidential communications between the insurer's counsel and its claims employee … but refusing to apply the privilege to counsel's confidential communications with an independent insurance adjuster who performs the same functions as an "in-house" claims employee. The Court, therefore, finds that confidential communications between Defendant's coverage counsel and Defendant's adjuster GAB Robins North America, Inc., for purposes of providing legal advice or to obtain information in order to render legal advice to the Defendant, are entitled to protection under the attorney-client privilege. *Residential Constructors, LLC v. Ace Property and Cas. Ins. Co.*, 2006 WL 3149362, at *15 (D. Nev. 2006).

C. Insurance Brokers – Depends on their Role

i. Communications between employees of the defendant and insurance brokers are privileged <u>to the extent that they were shown to have been made to facilitate the rendering of legal services</u> and involved an attorney. *In re TETRA Technologies, Inc. Securities Litigation*, 2010 WL 1335431, at *5 (S.D. Tex. 2010).

ii. However, if the communications surround a dispute between the insured and the insurer and the brokers are involved in the conversation, there may be no privilege. *In re TETRA Technologies, Inc. Securities Litigation*, 2010 WL 1335431, at *5 (S.D. Tex. 2010).

iii. Broker considered "insider" and thus privilege attaches – **"**According to Pera, he was the main conduit of information between Royal and SDG during the negotiations for the policy… Royal even goes so far as to refer to Sedgwick as SDG's insurance agent.'…SDG had no employees knowledgeable about complex commercial insurance. Furthermore, SDG knew that substantial ongoing exposure from personal injury suits related to the manufacture of orthopedic bone screws would make obtaining coverage a 'complex and difficult undertaking raising many possible legal issues and would require a great deal of care to avoid future insurance problems'…Although the policy in question was issued on November 24, 1995, this did not end Pera's involvement with SDG. Rather things were just getting started. Almost immediately, Royal began to question its obligation to cover costs of additional bone screw claims presented by SDG. At this point, Pera claims he met with Sedgwick's assistant general counsel, Darryl Martin to discuss the controversies. Apparently, it was agreed that since Sedgwick and SDG shared a common interest in the dispute, Pera would continue to work with SDG and its attorneys to defeat attempts by Royal to avoid

its obligations. To this end, Pera participated in meetings and strategy sessions with SDG and SDG's counsel. Given the level of complexity involved in the transaction, and the extent to which Sedgwick, through Pera, was involved in the negotiations on behalf of SDG, the court concludes he should be deemed an "insider" with respect to communications he shared in both before and after the issuance of the policy. *Royal Surplus Lines v. Sofamor Danek Group,* 190 F.R.D. 463 (W.D. Tenn. 1998).

D. Financial Consultant - Not recognized as a functional employee. The court noted that the privilege had to be applied narrowly here because many companies often have to hire the services of financial consultants and if the functional equivalent doctrine were extended to every situation where a financial consultant worked exhaustively to guide a company through a restructuring deal the exception would swallow the basic rule.

E. Public Relations Consultations

i. View that documents were privileged - GSK's corporate counsel "worked with these consultants in the same manner as they d[id] with full-time employees; indeed, the consultants acted as part of a team with full-time employees regarding their particular assignments" and, as a result, the consultants "became integral members of the team assigned to deal with issues [that] ... were completely intertwined with [GSK's] litigation and legal strategies." In these circumstances, "there is no reason to distinguish between a person on the corporation's payroll and a consultant hired by the corporation if each acts for the corporation and possesses the information needed by attorneys in rendering legal advice." *Federal Trade Comm'n v. GlaxoSmithKline,* 294 F.3d 141, 148 (D.C. Cir. 2002).

Confidential communications between lawyers and public relations consultants hired by lawyers to assist them in dealing with media were protected by attorney-client privilege when communication was made for purpose of giving or receiving advice directed at handling client's legal problems. *In re Grand Jury Subpoena dated Mar. 24 2003,* 265 F. Supp. 2d 321, 331 (S.D. N.Y. 2003)(applying federal common law).

ii. View that they are not Privileged – "BGR was retained before this litigation began. Moreover, it was not called upon to perform a specific litigation task that the attorneys needed to accomplish in order to advance their litigation goals—let alone a task that could be characterized as relating to the 'administration of justice.' Rather, it was involved in a wide variety of public relations activities aimed at burnishing Egiazaryan's image." *Egiazaryan v. Zalmayyev*, 2013 WL 945462, at *13 (S.D. N.Y. 2013) (applying NY law).

iii. Also found that Work Product Did Not Apply to Documents Not Made in Contemplation of Litigation – Even if Created at Behest of Attorney – "a number of the e-mails concern BGR's efforts to lobby Congress…Materials prepared in furtherance of lobbying activities, even when conducted by a lawyer, are generally unprotected under the work product doctrine. *See In re Grand Jury Subpoenas* dated Mar. 9, 2001, 179 F.Supp.2d 270, 285 (S.D. N.Y. 2001); *P. & B. Marina Ltd, Partnership v. Logrande*, 136 F.R.D. 50, 59 (E.D. N.Y. 1991), aff'd, 983 F.2d 1047 (2d Cir.1992). Some e-mails show the public relations staff

gathering facts about Egiazaryan's situation… Others relate to a proposed public relations strategy for Egiazaryan to follow… A number relate to the efforts to bolster Egiazaryan's image, and/or the actual implementation of a public relations strategy. There is no evidence that any of these e-mails were generated specifically to assist an attorney in preparing for litigation of this case." *Export-Import Bank of the U.S. v. Asia Pulp & Paper Co., Ltd.*, 232 F.R.D. 103, 113 (S.D. N.Y. 2005).

3. <u>Role of In-House Counsel</u>

A. Business Advice – Relaying information for purposes of testifying at a congressional hearing was found to not be linked to the rendering of legal advice – as RJR is in the "business of litigation" documents not tied to a particular case were also not considered work-product – even though they were discussing potential expert witnesses – *Burton v. RJ Reynolds Tobacco,* 200 F.R.D. 661 (D. Kansas 2001).

B. Merely Relaying Status of Litigation – Not considered to be attorney-client communications – Attorney was acting more as a claims adjuster or a claims investigator and thus communications were not privileged - *Cont'l Cas v. Marsh*, 2004 WL 42364 (N.D. Ill. Jan. 6, 2004).

C. Investigations – Generally Attorney-Client Privileged if Conducted by Attorney for Purposes of Giving Legal Advice – *AMCO Insurance Company v. Madera Quality Nut LLC*, 2006 WL 931437, *6 (E.D. Ill. April 11, 2006) ("Here, the declaration of Claiborne demonstrates that she was assistant general counsel for Leaf and as such was responsible for providing legal advice to UC and to the other defendants in the action. She was informed of the allegations of fraud, and without delay she undertook to perform an investigation with respect to fraud in relation to the fire for the purpose of assessing the claim and its veracity, giving advice if necessary, taking corrective action, and minimizing legal exposure, which she anticipated in the form of potential litigation, including claims by governmental agencies, the insurance company, and the employee. The purpose was to consider the criminal and civil liability of her client and to give legal advice regarding those problems. These functions concern consulting an attorney in her capacity as such. The communications between Claiborne and her client, including communications from and to employees interviewed in the course of Claiborne's investigation, are presumed to be confidential.")

i. If Not Conducted by Counsel - Not Necessarily Attorney Client Privileged but May be Subject to Work Product Privilege - *Southern Bell v. Deason*, 632 So.2d 1377 (Fla. 1994) – internal audit done at request of counsel in response to outside agency investigation was work product.

1. However, even though written statements by employees were work product, panel recommendations subsequently drafted by managers based on these statements were not work product as they were the basis for disciplining employees. *Id.*

ii. If Investigative Report is utilized as a remedial measure and measured is an affirmative defense in litigation– privilege will be waived. *McGrath v. Nassau County Health Care Corp.*, 204 F.R.D. 240 (E.D. N.Y. 2001).

iii. A preventability determination conducted by defendants in the ordinary course of business is not subject to protection. *Smith v. Marten Transp., Ltd.*, No. 10–cv–293, 2010 WL 5313537, at *4 (D.Colo. Dec.17, 2010) (holding that original investigation report was not privileged when produced in the ordinary course of business to investigate multi-car accident involving one of defendant's trucks and drivers); *Sajda v. Brewton*, 265 F.R.D. 334, 340 (N.D. Ind. 2009) (finding that company's accident report and computer template used to compile accident information were discoverable when generated in the ordinary course of business and forwarding the information to counsel did "not cloak it in attorney-client privilege"); *cf. Carlson v. Freightliner LLC*, 226 F.R.D. 343, 366 (D. Neb.2004) (stating that "risk management documents prepared by investigators" are not protected from discovery as privileged, unless they disclose "the individual case reserves for files and any mental impressions, thoughts, and conclusions in evaluating a legal claim").

D. Forwarding Emails – Communications – Generally sending privileged emails to third parties will waive the attorney-client privilege but maybe not work product.

i. *United States v. Stewart*, 287 F. Supp. 2d 461 (S.D. N.Y. 2003), found waiver of attorney-client but not work product. Martha Stewart prepared an E-mail to her lawyers purporting to recap the circumstances surrounding her sale of ImClone stock. The next day she forwarded the very same E-mail to her adult daughter, Alexis. Prosecutors claimed that by doing so Martha waived the attorney-client privilege and work product immunity. The court flatly declared that the privilege was waived. However, the court found that work product immunity was not. The court cited cases that held that sharing work product materials with persons allied with the client did not waive work product immunity because the risk of the opposition obtaining the information was slight. The court said: "By forwarding the e-mail to a family member, Stewart did not substantially increase the risk that the Government would gain access to materials prepared in anticipation of litigation." *Id.* at 469.

ii. Inadvertent Disclosure and the New Federal Rule of Evidence 502 - Prior to the adoption of the Rule, courts were in conflict over whether an inadvertent disclosure of a communication or information protected by the attorney-client privilege or work-product doctrine constituted a waiver. Under the new Rule, if privileged material is disclosed "inadvertently" in a federal proceeding, the disclosure does not operate as a waiver of privilege in a federal or state proceeding if: (1) the disclosure is inadvertent; (2) the holder of the privilege or protection took reasonable steps to prevent disclosure; and (3) the holder promptly took reasonable steps to rectify the error. Fed. R. Evid. 502(b).

Under the prior law, disclosure of one protected communication risked the loss of protection of privilege or work product as to all documents containing the same subject matter. The new rule provides that a voluntary disclosure of protected information in a federal proceeding or to a federal government agency exercising regulatory, investigative or enforcement authority results in a waiver only of the communication or information actually disclosed. The waiver extends to an undisclosed communication or information only in those unusual situations where the waiver is intentional, and fairness requires a further disclosure of

related, protected information in order to prevent a selective and misleading presentation of evidence to the disadvantage of the adversary. Fed. R. Evid. 502(a).

4. <u>Bad Faith Considerations</u>

A. No Attorney-Client or Work-Product Privilege in Third Party Claims - A plethora of cases have held that no attorney-client privilege can be asserted against an insured or an assignee of an insured in its action against an insurance company with respect to materials prepared as part of the insured's defense in the underlying action. *Medical Assur. Co., Inc. v. Weinberger*, No. 4:06–cv–117, 2013 WL 501746, at *10 (N.D. Ind. Feb. 7, 2013); *Glacier Gen. Assurance Co. v. Superior Court*, 95 Cal.App.3d 836 (Cal. App. Ct. 1979) ("To permit the insurer to use the attorney-client privilege to shield from its insured, communications which relate to the insurer's decision concerning settlement would be to place the insured in a secondary rather than a primary position in his relationship with the attorney, seriously eroding the insured's ability to establish that the insurer had failed in its duty to him."); *Simpson v. Motorists Mut. Ins. Co.*, 494 F.2d 850, 855 (7th Cir. 1974) (finding that the attorney-client privilege did not attach to communication between the insurance company and its attorney as against the assignee of the insured's claims against the insurance company); *Athridge v. Aetna Cas. & Sur. Co.*, 184 F.R.D. 200, 204 (D.D.C. 1998) (discussing the principle that "when a lawyer represented two persons and they later had a falling out and one sued the other, neither could claim the attorney-client privilege....That principle had also been applied when an insurance company hired an attorney to represent its insureds. When the insured then sued the insurance company, the courts had rebuffed any attempts by the insurance company to claim the attorney-client privilege to prevent its insured access to the documents that the attorney had created when she represented the insured and the insurance company's common interest in defeating the case brought against the insured.... [T]he courts had applied this principle when the insured assigned whatever claim she had against the insurance company to the person who sued the insured in the first place."); *Dome Petroleum Ltd. v. Employers Mut. Liab. Ins. Co. of Wisc.*, 131 F.R.D. 63, 68–69 (D. N.J. 1990) (relying on Seventh Circuit's holding in *Simpson* and finding there is no attorney-client privilege by insurer against subrogee of insured)); *see also Barry v. USAA*, 989 P.2d 1172, 1175–76 (Wash. Ct.App. 1999) ("[I]t is a well-established principle in bad faith actions brought by an insured against an insurer under the terms of an insurance contract that communications between the insurer and the attorney are not privileged with respect to the insured.") (citation omitted); *Silva v. Fire Ins. Exchange*, 112 F.R.D. 699, 699–700 (D. Mont. 1986) ("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."); *Cozort v. State Farm Mutual Auto. Ins. Co.*, 233 F.R.D. 674 (M.D. Fla. 2005) (holding that under Florida law, the entire claim file from an underlying coverage cause of action is discoverable in a subsequent bad faith action because Florida recognizes no privileges or limitation with respect to claim file materials in such an action); *Nationwide Mut. Fire Ins. Co. v. Bourlon*, 617 S.E. 2d 40 (N.C. Ct.App. 2005) (concluding that a tripartite attorney-client relationship existed whereby the lawyer hired to defend an insured represented both the insurer and the insured and that the common interest or joint client doctrine applies to the context of insurance litigation such that communications are not privileged as between the insurer and the insured); *Henke v. Iowa Home Mutual Cas. Co.*, 87 NW.2d 920 (Iowa 1958) (holding that communications between an insurer and the attorney employed by the insurer to defend the insured were

not privileged because the defense attorney represented both parties).

B. Further Erosion of Privilege in First Party Claims

i. Attorney for homeowners' insurer performed quasi-fiduciary functions of investigating, evaluating, negotiating, and processing underlying claim, in addition to advising insurer as to the law and strategy, so as to support presumptive waiver of attorney-client privilege by insurer and entitle insured to discovery of claims file in first-party bad faith claim filed by insured. *Cedell v. Farmers Ins. Co. of Washington*, 295 P.3d 239 (Wash. 2013).

ii. Where a claim of privilege is asserted, the judge should conduct an *in camera* inspection to determine whether the sought-after materials are truly protected by the attorney-client privilege or whether the materials pertain to the investigation or evaluation of the underlying claim. To the extent that the materials would implicate the work product rule and not the attorney-client privilege, the rationale of *Ruiz* would apply and those portions of the materials would be discoverable. *Genovese v. Provident Life and Accident Ins. Co.,* 74 So.3d 1064, 1070 (Fla. 2011).

iii. In an action alleging bad faith denial of insurance coverage, the insured is entitled to discover claims file materials containing attorney-client communications related to the issue of coverage that were created prior to the denial of coverage. *Boone v. Vanliner Insurance Co*., 91 Ohio St.3d 209, 744 N.E.2d 154 (2001).

iv. Insurance company's claim file is permissible discovery in a bad faith action brought by its insured for failure to pay a claim. *In re Bergeson*, 112 F.R.D. 692, 697 (D. Mont. 1986).

C. Waiver of Privilege if Defense of Bad Faith is Based on Advice of Counsel - Litigant may not use reliance on advice of counsel to support claim or defense as sword in litigation, and also deprive opposing party opportunity to test legitimacy of that claim by asserting attorney-client privilege or work-product doctrine as shield. *Aspex Eyewear, Inc. v. E'Lite Optik, Inc.*, 276 F. Supp. 2d 1084 (D. Nev. 2003).

D. No Privilege for Documents Provided in Rate Filings – "The principal business function of an HMO is to act as a third-party payor to providers of health care services for participants who pay fees for this service. The mere fact that AHCA requests a rate explanation from an HMO is about as routine as this business gets. The mere fact that an HMO consults with a specialist in provider reimbursement is also routine. [footnote omitted] Explaining rates to government agencies concerned with reimbursement to providers of health care services is an unending business activity of third-party payors, like these HMOs.**"** *Neighborhood Health Partnership, Inc. v. Peter F. Merkle M.D., P.A.,* 8 So.3d 1180 (Fla. 4th DCA 2009).

E. Generally, a party may not waive the attorney-client privilege for its own benefit to a third party government agency, then hide behind the privilege in civil litigation. *In re Qwest Communications International, Inc.,* 450 F.3d 1179, 1187 (10th Cir. 2006)

(rejecting selective waiver); *Westinghouse Elec. Corp. v. Republic of Philippines*, 951 F.2d 1414, 1418 (3d Cir. 1991) (disclosing documents to the SEC and the DOJ to cooperate with investigation waived attorney-client and work product privilege); *In re Columbia/HCA Healthcare Corporation Billing Practices Litigation*, 293 F.3d 289, 295–302, 305–306 (6th Cir. 2002) (rejecting selective waiver, finding that disclosure to SEC waived privilege); *United States v. Mass. Inst. of Tech.*, 129 F.3d 681, 686 (1st Cir. 1997) (same); *In re Steinhardt Partners, L.P.*, 9 F.3d 230, 235, 236 (2d Cir. 1993) (work product protection waived with respect to a document defendant had produced to SEC in hopes of preventing a formal investigation); *In re Martin Marietta Corp.*, 856 F.2d 619, 623–624 (4th Cir. 1988) (rejecting limited waiver of attorney-client privilege); *In re John Doe Corp.*, 675 F.2d 482, 489 (2d Cir. 1982) ("A claim that a need for confidentiality must be respected in order to facilitate the seeking and rendering of informed legal advice is not consistent with selective disclosure when the claimant decides that the confidential materials can be put to other beneficial purposes."); *Permian Corp. v. United States*, 665 F.2d 1214 (D.C. Cir. 1981) (disclosure of privileged information to any third party, including the government, destroys the privilege); accord *In re Subpoenas Duces Tecum*, 738 F.2d 1367, 1370 (D.C. Cir. 1984) (client cannot pick and choose among opponents, waiving the privilege for some and resurrecting claim of confidentiality to obstruct others or to invoke privilege as to communications whose confidentiality he has already compromised for his own benefit) (citation omitted).

F. Other courts have reached the opposite conclusion. See *Diversified Industries Inc. v. Meredith*, 572 F.2d 596 (8th Cir.1977) (the disclosure of privileged information to the government as a third party waived the attorney-client privilege only with respect to the government); *In re Grand Jury Subpoena Dated July 13, 1979*, 478 F.Supp. 368, 373 (D. Wis. 1979) (same); *In re LTV Securities Litigation*, 89 F.R.D. 595, 605 (N.D. Tex. 1981) (same); *Byrnes v. IDS Realty Trust*, 85 F.R.D. 679, 689 (S.D. N.Y. 1980) (same); *Schnell v. Schnall*, 550 F.Supp. 650 (S.D. N.Y. 1982). *See also In re Steinhardt Partners, L.P.*, 9 F.3d 230, 235, 236 (2d Cir. 1993) (declining to adopt a per se rule that all voluntary disclosures to the government waive the protection of privilege); *Mallinckrodt Chemical Works v. Goldman, Sachs & Co.*, 58 F.R.D. 348, 352 (S.D. N.Y. 1973) (a demand for document production that satisfies requirements of the Federal Rules must be honored, and the fact that the documents were submitted to the SEC is "wholly irrelevant," but "[t]he production of documents to an agency or other investigative body does not automatically make those documents discoverable in a separate proceeding.")

5. Tips to Protect the Privileges

A. Separate legal advice from business advice/information in all communications.

B. Clearly Mark Documents/Emails as Confidential Attorney-Client Work Product Privileged Communications – Ensure that the communication makes clear that it is seeking/providing legal advice.

C. Only Distribute/Copy Individuals Within Company With a Need to Know – Be careful about forwarding Emails/Reply to All.

D. Ensure that Third Parties are Designated as "Insiders" or Necessary for Communications with Counsel.

E. Make Sure Internal Investigation Reports Provide Legal Advice.

F. If Disclosure Must be Made to Regulators – Attempt to Obtain a Confidentiality/Privilege Preservation Agreement – However, this may not be possible if documents are subject to Public Records Laws or in jurisdictions with No Selective Waiver.

G. Assume that Everything May Be Discoverable – Be Selective as to What to Document and How to Document.