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ISN'T ANYTHING SACRED ANYMORE?

I. Current Trends

A. The Erosion of Privilege

Over the last fifteen years there has been a trend in some jurisdictions, to erode assertions of privilege by insurers in extra-contractual litigation. Beginning with the 2001 decision of the Ohio Supreme Court in Boone v. Vanliner Insurance Co. **1,** several jurisdictions have seemingly sought to create a second class of litigants: insurers defending extra-contractual claims.

In Boone, the Ohio Supreme Court suggested that mere allegations of bad faith are enough to vitiate attorney client privilege with respect to communication between the insurer and coverage counsel. In 2013 the Supreme Court of Washington followed with Cedell v. Farmers Ins. Co. of Washington.**2** Cedell is often viewed as having effectively abrogated insurers' privilege claims in extra-contractual litigation. The opinion actually stated that there is a presumption of discoverability. The insurer might overcome the presumption by showing that its attorney was not engaged in the quasi-fiduciary tasks of investigating and evaluating or processing the claim but instead the attorney was providing the insurer with counsel as to its own potential liability, for example, whether or not coverage exists under the law.

Interestingly, in Cedell in footnote 5 the Washington Supreme Court noted that when an attorney is acting in more than role, insurers may wish to set-up and maintain separate files so as to not co-mingle different functions.

The Cedell opinion concluded by instructing trial courts that if an insurer overcomes the presumption of discoverability it may still be required to produce otherwise privileged materials if a reasonable person would have a reasonable belief that an act of bad faith has occurred and there is a "foundation to permit the claim of bad faith to proceed." All in all, a fairly stacked deck, against the insurer.

In Florida, in first party extra-contractual cases, work product is discoverable, but attorney-client privileged communications are not.**3**

Even in New York, it seems that at least in the view of one part of the Appellate Department, coverage opinions of counsel written before a coverage decision is made, are discoverable.**4**

B. The Maintenance of Privilege

Not all jurisdictions have accepted the invitation of Boone and Cedell to create a less privileged class of litigants. In Anastasi v. Fidelity National Title Ins. Co.**5** Hawaii's Intermediate Court of Appeals specifically declined to follow Cedell. Significantly, Major Claims Counsel for Fidelity ("McGinnity") had served a dual role. While communication between McGinnity and outside coverage counsel was recognized as privileged, internal communication required a thorough analysis – the pertinent inquiry being whether the communication was primarily of a "legal character." Meaning, was the primary purpose the rendering of legal advice or services. Does the communication reflect the lawyer's judgment and recommended legal strategies? Underlying facts, however, are discoverable.

The Anastasi opinion is instructive in its thorough analysis of the insurer's successes and failures, in seeking to differentiate McGinitty's blended roles. With respect to work product, the inquiry declared by the court was: Would the at issue document in substantially similar form have been created but for the prospect of litigation?

Other jurisdictions afford the insurer protection by directing that where a coverage claim and extra-contractual claim are both asserted, the extra-contractual claim should be bifurcated and stayed – until the insured establishes coverage as to which there is no reasonable debate.**6**

II. Factual Investigation and "Claim Handling" as Opposed to Strategic Legal Analysis

Regardless of whether a case with both a coverage claim and extra-contractual claim is being litigated in Washington, Hawaii, Ohio, New Jersey or anywhere in between, there are basic distinctions that all Courts, at a minimum, take note of and address differently:

A. Factual investigations are inevitably discoverable.
B. Claims handlers evaluation of facts, their thoughts and strategy are inevitably discoverable.
C. Reports and draft reports of independent adjusters, experts, and consultants, prepared in the ordinary course of claim handling before litigation is clearly anticipated, are inevitably discoverable.
D. Internal counsel's notes and memos to the extent they contain items 1, 2 or 3 are likely discoverable.

E. Internal counsel's notes and memos, to the extent they reflect outside counsel's legal analysis and recommended strategies may not be and should not be discoverable.
F. Outside counsel's legal analysis and recommended strategies may not be and should not be discoverable.
G. Privilege claims can be viewed through at least three very different prisms: in conjunction with claims files handling, in conjunction with in-house counsel, and in conjunction with outside coverage counsel.

III. What Steps Should Always be Employed to Protect Privilege Regardless of the Jurisdictions?

A. Split the file – early.
B. Really split the file.
C. Neither internal counsel nor outside counsel should investigate the facts.
D. Is it preferable for outside coverage counsel to communicate directly to inside counsel, not Claims?
E. Should outside coverage counsel always "call first"?
F. Once the file is split, if a written coverage opinion is desired by the Insurer, what should be sent? To whom?
G. In the case of a third party claim if inside counsel is evaluating reports from defense counsel and/or monitoring the claim, to whom should counsel's thoughts and recommendations be communicated?

IV. Advice of Counsel, Subjective Good Faith and Other Traps.

Is assertion of "advice of counsel" as a defense to an extra-contractual claim ever a prudent tactical decision? In most jurisdictions it waives any claims of attorney-client privilege and probably exposes coverage counsel to being deposed as well. If the reasons for the coverage decision are comprehensively set forth in a letter which a claims representative can point to, what strategic advantage is gained?

In some jurisdictions an insurer's "state of mind" with respect to denial of a claim is relevant. In other's the question is one of objective reasonableness. If it is a valid defense under applicable law that the claim handling was objectively reasonable, is there any strategic advantage to rely on "subjective good faith"? Can an "objectively reasonable" defense enhance the strategic importance of expert testimony on the applicable standard of claim handling?

V. The Discoverability of Reinsurance and Reserves.

In many jurisdictions, in a liability case, information about insurance that may be available for indemnity is readily discoverable. While some courts have begun to analogize to reinsurance information in coverage/extra-contractual litigation, are there important distinctions? Is reinsurance relevant, privileged or confidential and proprietary?

Insured's counsel seek discovery of reserves because they can paint a stark contrast to the ultimate coverage decisions made by an insurer. The setting of reserves is undeniably part of the claim handling process.

Court's that have denied the discoverability of reserves recognize the difference between the process of setting a reserve and determining coverage:

> "A reserve essentially reflects an assessment of the value of the claim taking into consideration the likelihood of an adverse judgment. Such estimates of potential liability do not normally entail an evaluation of coverage based on a thorough factual and legal consideration when made as a claim analysis; rather when the reserves have been established on legal input, the results and supporting papers most likely will be work-product and may also reflect attorney-client privileged communications."**7**

Should the regulatory/financial imperatives which drive the setting of reserves also inform the courts' decisions? Are reserve changes late in the claim cycle any more or less relevant?

1. Boone v. Vanliner Insurance Co., 91 Ohio St. 3d 209, 744 N.E. 2d 1544 (2001) cert. denied 5344 U.S. 1014 (2001).

2. Cedell v. Farmers Insurance Co. of Washington, 176 Wash. 2d 686 (2013).

3. Genovese v. Provident Life & Accident Ins. Co., 74 So. 3d 1064, 1068 (Fla. 2011); Allstate Indemnity Co. v. Ruiz, 899 So. 2d 1121 (Fla. 2005).

4. Lalka v. ACA Insurance Co., 128 A.D. 3d 1508 (N.Y. App. Div. 4th Dept. 2015) *See also* Nat'l Industrial Transformers, Inc. v. AH Mutual Ins. Co., No. 91 Civ. 7192, 1993 WL 158373 at *9* 10 (S.D. N.Y. 1993) *but See* All Waste Sys. Inc. v. Gulf Ins. Co., 295 A.D. 2d 379, 743 N.Y.S. 2d 535 (2nd Dept. 2002).

5. Anastasi v. Fidelity National Title Ins. Co., 134, Hawaii 400 (Intermediate Court of Appeals 12/30/14).

6. Procopio v Government Employees Ins. Co., 443 N.J. Super. 377 (App. Div. 2013).

7. Leski, Inc. v. Federal Ins. Co., 129 F.R.D. 99, 107 (D.N.J. 1989). *See also* Rhone-Poulenc Rorer, Inc. v. Home Indem. Co., 139 F.R.D. 609, 613-614 (E.D.Pa. 1991).