

Attorney-Client Privilege in Bad Faith Litigation: Privilege Issues From Perspectives of Policyholders and Insurers

WEDNESDAY, OCTOBER 7, 2020

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

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Introductions



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Overview of Today's Discussion

- **Attorney-Client Privilege in First Party and Third Party Bad Faith Cases**
 - When Claims and Litigation File Discovery Is Sought
 - How the Privilege Can Be Pierced
- **Important Considerations**
 - Privilege in the Tripartite Relationship
 - Privilege in Complex Multi-Party, Multi-Insurer Litigation
 - Preserving Privilege: Common Interest Doctrine and Joint Defense Agreements

Difference Between Attorney-Client Privilege and Work Product Doctrine

- **Attorney-Client Privilege**
 - Generally governed by state law
 - Scope
 - Discoverability
- **Work Product Doctrine**
 - Fact Work Product
 - Opinion Work Product

Bad Faith Claim Hypotheticals

- First-party coverage claim for damage to commercial building
 - Insurer does not assert advice of counsel
 - Insurer does assert advice of counsel
- Third-Party Plaintiff Claim for Failure to Settle within Policy Limits
 - Insurer has witness interview memoranda that it declines to produce as work product
 - The memoranda recount what the witness said
 - The memoranda recount the attorney's thoughts and impressions about the interview

How can you obtain information claimed to be privileged?

- Information not privileged (attorney acting as adjuster)
- Insurer asserts advice of counsel
- Waiver of the privilege (disclosure of attorney-client communications)
- Implied waiver
- Crime-fraud exception

Implied Waiver

When the insurer voluntarily injects an issue into the case, whether legal or factual, the insurer voluntarily waives attorney-client privilege.

Example: In *State Farm Mutual Automobile Ins. Co. v. Lee*, 13 P.3d 1169., 1173-74 (Ariz. 2000) –

Attorney-client communications were discoverable because the insurer defended its denial of coverage based on its agents' subjective understanding of the law as informed by counsel even though the insurer said it was not asserting an advice of counsel defense.

***In re Mt. Hawley Ins. Co.*, 829 S.E.2d 707, 717 (S.C. 2019).**

- An insurer does not waive the privilege simply by denying liability for bad faith in its answer.
- South Carolina adopted the *Lee* standard -
 - (1) The insurer defends a bad faith claim on the basis of its subjective and allegedly reasonable understanding of the law and
 - (2) that understanding necessarily involves what the insurer learned from its counsel.

But added one additional requirement:

- (3) the party seeking waiver of the attorney-client privilege must also make a *prima facie* showing of bad faith.

Crime – Fraud Exception

- Applies when legal advice has been obtained in furtherance of an illegal or fraudulent activity.
- Standard applied by some courts in the insurance context (*Hutchinson v. Farm Family Cas. Ins. Co.*, 273 Conn. 33, 867 A.2d 1 (2005)):

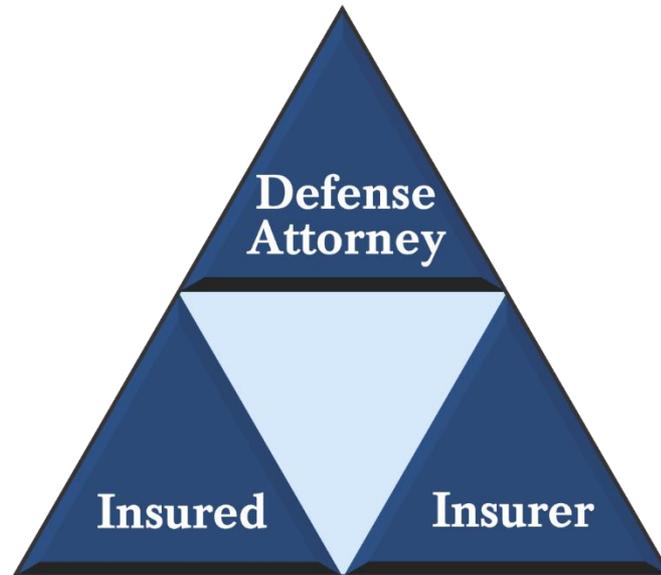
“[W]hether the plaintiffs have established, on the basis of nonprivileged materials, that there is probable cause to believe that:

- (1) the defendant has acted in bad faith and
- (2) the defendant sought the advice of its attorneys in order to conceal or facilitate its bad faith conduct.”

Piercing the Privilege

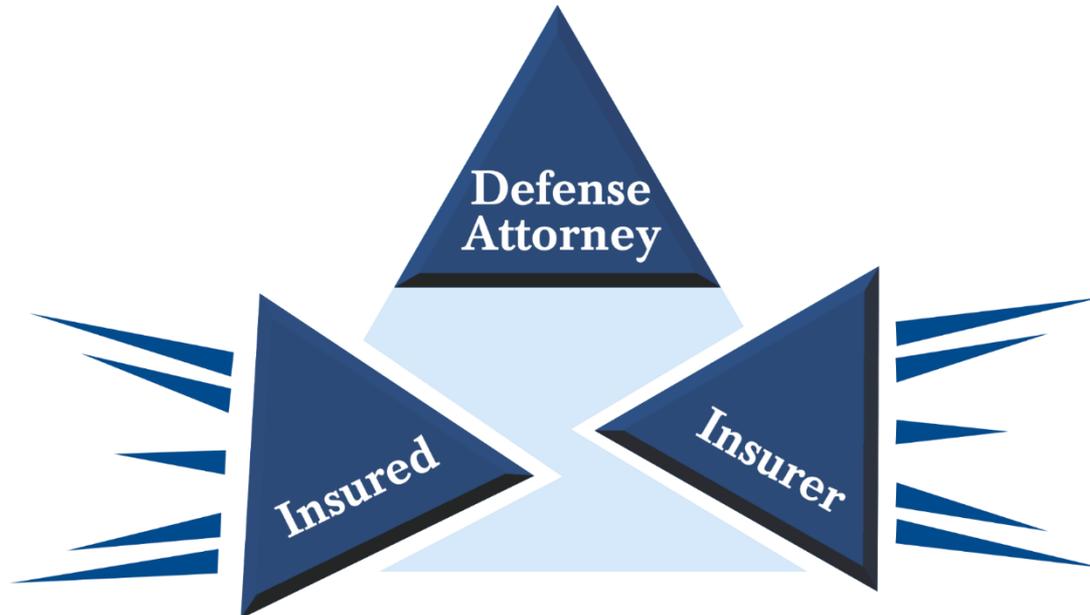
- **Plaintiff Perspective**
- **Defense Perspective**

The Tripartite Relationship



The Tension

Conflict of Interest between Insurer and Insured



Hypothetical 1

- Garden variety auto accident – Mary crashes into Joe, and Joe sues Mary. Mary’s insurance company appoints counsel to defend her.
- No real coverage issues, plaintiff’s demand well within policy limits
- No reservation of rights
 - Privilege as between Insurer and Insured?
 - Privilege with regard to Third-Party Plaintiff?
 - What if the case doesn’t settle, the plaintiff hits a surprise home run and gets a judgment well in excess of policy limits, then comes after the insurance company for failure to settle/bad faith?
 - What if the insured settles with the plaintiff and assigns her claims against the insurance company to the plaintiff?

Hypothetical No. 2

- Commercial liability case, involving covered and uncovered claims
- Insurer reserves rights with regard to uncovered claims
 - How does that impact the relationship and the privilege?
 - Privilege as between insured and insurer?
 - What if insured gets separate counsel at insurer's expense?
 - What if insurer does not reserve rights but demands are well in excess of policy limits?
 - Any impact on tripartite relationship?

Hypothetical No. 2 Continued

- Commercial liability case, involving covered and uncovered claims
 - Will communications between the insurance company and defense counsel be discoverable in a subsequent bad faith action brought by the insured against the insurer?
 - Are those communications discoverable by third parties?

Hypothetical No. 3

- What if multiple insurers are defending a single insured?
- Construction defect suit: A developer and a general contractor are being defended by the general contractor's insurance company even though the developer and general contractor's interests are in part adverse. (The developer is being defended as an additional insured.)
- What safeguards should be in place to protect attorney-client privileged communications between the developer, its counsel, and the insurer from being discovered by the general contractor and vice versa?

What if you want to share some information?

- Generally, communications between an attorney and client that are disclosed to third parties are not privileged.
- Under the common interest doctrine, attorney client communications disclosed to a third party remain privileged if:
 - (1) the party shares a common legal interest with the client who made the communication;
 - (2) The communication is made in furtherance of that common interest; and some states also require a showing that
 - (3) The communication relates to pending or anticipated litigation.

Common Interest and Joint Defense Agreements

- Do you need them?
- What should they say?



Case-Related Examples

- Have you ever won or defeated a challenge to attorney-client privilege?
- Under what circumstances?



Questions?

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