THE "ADVICE OF COUNSEL DEFENSE" IN COVERAGE CASES: YOU MIGHT BE WAIVING MORE THAN YOU REALIZE

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Co-Authored by: **Donald Myles**, **Patrick Gorman** & **Eileen GilBride**

In *United Specialty Ins. Co. v. Dorn Homes Inc.*,__ F.R.D. __, 2020 WL 443872,(D. Ariz. Jan. 28, 2020), the United States District Court, District of Arizona, analyzed whether the insurer's assertion of the advice of counsel defense operates to waive the work-product defense for documents its counsel created but did not communicate to the insurer client. The court said yes, assertion of the defense waives the work-product protection. The insurer must disclose those work-product protected documents if it affirmatively waives the attorney client privilege by relying on advice of counsel defense. Moreover, the court ordered the insurer to produce work-product documents that were created even after it had filed its declaratory judgment action, though many courts hold that the waiver ends with the filing of the declaratory lawsuit.

In this case, coverage counsel for the insurer, United Specialty, filed a declaratory judgment action against the insured, Dorn Homes, claiming there was no coverage for construction defects on 87 homes alleged against Dorn. The day before the lawsuit was filed, the insurer had issued a coverage determination for five of the 87 homes. Dorn Homes was continuing to pay for repairs and remediation on the 87 homes, and the claims adjustment process was ongoing at the time of filing. Dorn counterclaimed for bad faith, and the insurer asserted advice of counsel as a defense, thus waiving the attorney-client privilege.

The insured sought disclosure of coverage counsel's file, and asked for "All documents relating to coverage of Dorn's claim including time entries of the law firm whether before or after the case was filed." Dorn cited three reasons for obtaining these documents: (1) the insurer's assertion of the advice of counsel defense waived work product protections for pre- and post-lawsuit documents related to coverage; (2) the insurer waived work product protection under Evidence Rule 502 (which discusses the attorney-client privilege and work product doctrines and limits on waiver); and (3) Dorn had a "substantial need" for the information and had no other way to obtain it.

The insurer argued it was not required to disclose attorney work product that its counsel had not communicated to it (since the insurer could not have relied on its attorney's uncommunicated work product in making coverage decisions); and that its assertion of the advice of counsel defense did not waive the protection for post-lawsuit attorney work product.

The court disagreed with the insurer on both points. First, the court held that the insured could obtain attorney work product even though it had not been communicated to the insurer. Said the court, "A party may not invoke the sword of an advice of counsel defense and also raise the shield of the work-product doctrine." The court reasoned that fairness required giving the insured the opportunity to fully test the legitimacy of the advice of counsel defense, which would involve allowing Dorn to inquire into the basis and facts surrounding the advice provided by counsel, not just those materials that communicated the advice to the insurer. The court agreed with the insured that to rule otherwise "would ignore the vast number of ways [coverage counsel] could share information with [the insurer] without technically sending a document, especially with modern technology." Work product, including uncommunicated work product, might reveal communications between the insured and counsel and thus be probative of what information the insurer's counsel considered, the reasonableness of its advice, and whether the insurer relied on the advice in good faith. In short, permitting the work-product documents to remain privileged would ignore "the potential for litigation abuses, and erects too much of an impediment to the truth seeking process."

Second, the court said the insured could obtain work product material created even after the lawsuit was filed. Many courts conclude that the privilege waiver ends upon the lawsuit's filing because once the lawsuit is filed, defense counsel is engaged in critical trial preparation, including analyzing the weaknesses of their client's case. As such, there is an enhanced interest in protecting against disclosure of trial strategy and planning. The disclosure of such analyses would chill communications between trial counsel and client and would impair trial counsel's ability to give the client candid advice regarding the merits of the

case. In this case, however, the insurer's waiver of the privilege lasted throughout the case due to the specific circumstances involved here. Specifically, the filing of the complaint did not form a clear cutoff of research and analysis that would inform the advice of counsel defense. The suit was filed the day after the insurer issued a coverage determination for five of the 87 homes at issue; the insured was continuing to pay for repairs and remediation on the 87 homes; the claims adjustment process remained fluid and ongoing at the time of filing; and counsel's billing records reflected their research on coverage in the days immediately after the filing. In short, said the court, the presumption that nothing transpiring during litigation is pertinent to the client's state of mind was "not in accord with the reality of litigation."

As the court concluded, "invoking the advice of counsel defense is not a painless decision or a free lunch. There are discovery consequences to such an assertion. Fairness requires that a party who seeks to be absolved of willful infringement because it relied on counsel's advice pay the discovery price."

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Donald Myles represents clients in matters involving bad faith and extra-contractual liability, professional liability, insurance coverage, and catastrophic injury and wrongful death claims.

Patrick Gorman concentrates his practice in the areas of bad faith and extra-contractual liability, breach of contract claims, insurance coverage, professional liability and other general civil litigation matters.

Eileen GilBride leads the firm's Appellate Department and focuses her practice on representing clients in federal and state appellate matters and dispositive motions. She has handled more than 400 appeals at every level of the state and federal courts, in Arizona and other states, which have resulted in more than 80 published decisions.