Attorney-Client Privilege in First-Party Bad Faith Litigation

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§ 16.08 Trial Lawyers' Perspective: Institutional Discovery

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§ 16.04 Attorney-Client Privilege and Work Product Protection in Bad Faith Cases

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[3] Material with Limited Protection in Bad Faith Cases

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[c] Attorneys Used as Claim Adjusters—Illustrative Case

Insurers sometimes use attorneys to conduct the investigation of a claim, rather than just to provide legal advice based on evidence produced by the insurer's own representation. The factual results of such an investigation might be work product, but they would typically be ordinary work product and discoverable in a bad faith case. (*See* § 16.04[3][b], *above*.) But that would leave the possibility that they would be protected by the attorney-client privilege. If that protection were available, it could greatly hamper a bad faith plaintiff in determining the adequacy of the investigation or even what evidence the insurer had when it denied the claim.

For precisely that reason (and because privilege does not apply to gathering of information from third parties), courts will generally refuse to find the factual results of an attorney's investigation protected by attorney-client privilege. *Dakota, Minnesota, & Eastern Railroad Co. v. Acuity*[100] involved a complicated claim. Julian Olson, an employee of DM&E, was seriously injured in a motor vehicle accident in the scope and course of his employment. He was driving a car equipped with a Hy-Rail System which allowed it to be driven on railroad tracks. He sued DM&E under the Federal Employers Liability Act for negligent maintenance of the Hy-Rail System, ultimately settling with DM&E, and Acuity was found to provide no coverage for that liability.[101]

But DM&E had uninsured motorist ("UM") coverage with Acuity, applicable to the accident, and Olson claimed the accident was caused, in part, by a negligent "phantom motorist" who had cut him off and whose car never made contact with his.[102] The UM coverage required independent corroboration of the facts of any such accident.[103] Shortly after the accident, three independent witnesses told DM&E that there had been an unusually slow moving vehicle ahead of Olson as he entered the interstate highway, and one expressed the belief that this vehicle had probably caused the accident.[104] When the UM claim was presented, Acuity hired a lawyer, Gary Thimsen, to investigate the claim and provide a coverage opinion; Acuity did no investigation of its own.[105] Thimsen recommended that the claim be denied for want of

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[100] 2009 SD 69.

[101] 2009 SD 69, ¶¶ 2–3.

[102] 2009 SD 69, ¶¶ 2, 5.

[103] 2009 SD 69, ¶ 5 n.3 (" '[i]f the hit-and-run vehicle does not hit an *insured*, a covered *auto*, or a vehicle an *insured is occupying*, the facts of the accident must be corroborated by competent evidence provided by an independent and disinterested person and not by the *insured* or any person occupying the same vehicle as the insured.' " (emphasis original)).

[104] 2009 SD 69, ¶ 6.

[105] 2009 SD 69, ¶¶ 5, 7–8.

independent corroboration.[106]

DM&E obtained an order compelling Thimsen's deposition, but the deposition was deferred pending resolution of the liability insurance coverage question.[107] DM&E prevailed on that coverage and that judgment was affirmed. DM&E then requested Thimsen's deposition, and Acuity moved for summary judgment on bad faith, arguing that the liability coverage trial showed that UM coverage had always been fairly debatable. The circuit court granted the motion, without addressing DM&E's request for delay to take Thimsen's deposition. The South Dakota Supreme Court reversed.

Only if Acuity had properly investigated and evaluated the claim could it reasonably deny the claim, and, under South Dakota law, only evidence in Acuity's possession when it denied coverage could be used to defend that denial.[108] Without knowing what investigation Thimsen had made and what facts he had discovered, it was "*unclear* what facts were available to suggest that the claim was fairly debatable when Acuity denied the claim."[109] That lack of information precluded summary judgment, because "Acuity [had] the initial burden to '*clearly* show an absence of any genuine issue of material fact and an entitlement to judgment as a matter of law.' "[110]

Moreover, the factual results of Thimsen's investigation were not privileged.[111] The court relied on and quoted cases denying work product protection in similar circumstances:

> It would not be fair to allow the insurer's decision in this regard to create a blanket obstruction to discovery of its claims investigation. To the extent that [the lawyers] acted as claims adjusters, then, their work-product, communications to client, and impressions about the facts will be treated herein as the ordinary business of plaintiff, outside the scope of the asserted privileges.[112]

Strictly speaking, there is no "ordinary business" exception to the attorney-client privilege, as contrasted with work product. (*See also* § 16.04[3][b].) But the result is right, even if the reason given is not. The attorney-client privilege only protects *communications* between *privileged persons* (typically, the attorney, the client, and representatives of either).[113] Unlike an internal investigation, where information is gathered from the client's own personnel and the process may be privileged (*see* § 16.04[2][a]), a claim investigation involves gathering information from non-client sources. Gathering such information is not part of any privileged communication, so that process is not privileged.[114] The lawyer's legal analysis

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[106] 2009 SD 69, ¶ 5.

[107] 2009 SD 69, ¶ 9. It is unclear why DM&E was suing to compel payment of UM benefits that would have been payable to Olson, as Acuity's payment of those benefits would not reduce DM&E's liability to Olson. Rather, Acuity would have been subrogated to Olson's rights against DM&E. But the opinion does not address this issue.

[108] 2009 SD 69, ¶¶ 21–27. (Restrictions on defensive use of evidence obtained after claim denial are discussed in § 17.03[4][[d][iii], below.)

[109] 2009 SD 69, ¶ 26.

[110] 2009 SD 69, ¶ 26.

[111] 2009 SD 69, ¶¶ 55–57.

[112] 2009 SD 69, ¶ 56, *quoting* Mission Nat'l Ins. Co. v. Lilly, 112 F.R.D. 160, 163 (D. Minn. 1986).

[113] RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 68 (2000).

[114] Anastasi v. Fid. Nat'l Title Ins. Co., 134 Haw. 400, 421 (Ct. App. 2014), *rev'd in part on other grounds,* 137 Haw. 104 (2016). *See* Venture v. Preferred Mut. Ins. Co., 61 N.Y.S.3d 210, 214–15 (App. Div. 2017) (ordering discovery and hearing on whether and to what extent lawyer acted as investigator); Nat'l Union Fire Ins. Co. v.

based on the information gathered may be privileged or opinion work product, but the factual investigation is not.

This analysis can also be used to separate privileged communications from nonprivileged investigation under the Florida Supreme Court decision of *Genovese v. Provident Life & Accident Insurance Co.*[115] Ideally, the lawyer should segregate the file for the matter between coverage investigation and legal advice on coverage, in order to maximize the ability to protect the latter by asserting privilege. If the lawyer is retained solely to provide legal advice and not to conduct any investigation, making that fact clear in the engagement letter may be useful resisting discovery regarding the lawyer's work. But the insured would be entitled to inquire whether any such limitation was actually observed during the lawyer's work.

In *Dakota, Minnesota, & Eastern Railroad Co. v. Acuity,*[116] the court stated the relevant rule as being that "where an insurer unequivocally delegates its initial claims function and relies exclusively upon outside counsel to conduct the investigation and determination of coverage, the attorney-client privilege does not protect such communications."[117] But *Andrews v. Ridco, Inc.* held that any claim that this has occurred must be supported by factual findings based on the record.[118] Ordinarily, that requires an *in camera* review of the disputed material.[119]

It has been said that, where counsel both investigates (characterized in Washington as a quasi-fiduciary activity) and provides legal advice, "waiver of the attorney-client privilege is likely since 'counsel's legal analysis and recommendations to the insurer regarding liability generally or coverage in particular will very likely implicate the work performed and information obtained in his or her quasi-fiduciary capacity.'"[119.1] But any waiver should be limited to the investigative activity and conclusions as long as the legal advice can be segregated.

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[4] When Can Attorney-Client Privilege Be Pierced?

[a] "At Issue" Waiver

[i] Majority Narrow Rule, Exemplified by *Rhone-Poulenc*

[A] Mere Relevance or Need Is Not Enough To Divest Privilege

TransCanada Energy USA, Inc., 119 A.D.3d 492, 493 (2014), *appeal dism'd,* 24 N.Y.3d 990 (2016).

[115] Genovese v. Provident Life & Accident Ins. Co., 74 So. 3d 1064, 1068 (Fla. 2011) (noting distinction between privilege for communications involved in obtaining legal advice and qualified work product protection for investigation).

[116] 2009 SD 69.

[117] 2009 SD 69, ¶ 56.

[118] Andrews v. Ridco, Inc., 2015 SD 24, ¶ 28.

[119] Andrews v. Ridco, Inc., 2015 SD 24, ¶¶ 34–37.

[119.1] Canyon Estates Condo. Ass'n v. Atain Specialty Ins. Co., 2020 U.S. Dist. LEXIS 10915, at *3–4 (W.D. Wash. Jan. 22, 2020). But mere assistance to the adjuster in drafting a denial letter does not waive privilege, even though that is not a privileged activity. 2020 U.S. Dist. LEXIS 10915, at *3.

[I] Overview

A client may waive the privilege by disclosing them to nonprivileged parties (*see* § 16.04[6][a][i], *below*) or by placing privileged communications "at issue."[120] Most obviously, waiver occurs when the client relies on a defense of acting in accordance with advice of counsel.[121] (An insurer also cannot waive privilege as to appellate counsel whose advice is relied upon in defense without also waving privilege as to the files of trial counsel that appellate counsel necessarily had to review.)[122] On the other hand, mere disclosure to the insured of the conclusions reached by counsel, without disclosure of the substance of the opinion, does not waive the privilege.[123]

The logic of the "at issue" waiver rule reflects a point stated by Learned Hand regarding the Fifth Amendment privilege: "the privilege is to suppress the truth, but that does not mean that it is a privilege to garble it; … it should not furnish one side with what may be false evidence and deprive the other of the means of detecting the imposition."[124] But such garbling occurs only where the privileged party has utilized privileged evidence or other evidence that directly depends on privileged communications.[125] Similar logic would seem to apply in determining whether a party has waived the nearly absolute protection of opinion work product.

While the scope of "at issue" waiver is a matter of dispute, the more numerous and better reasoned authorities hold that waiver cannot occur on account of the assertion of issues by the privilege holder's opponent that would create a supposed need to examine the privileged materials to prove the opponent's assertions. *In re Kellogg Brown & Root, Inc.*[126] was a mandamus proceeding arising out of a False Claims

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[120] Ohio has a statutory privilege against actual attorney-client communications, and the statute does not provide for any "at issue" waiver. Jackson v. Greger, 854 N.E.2d 487, 489–90 (Ohio 2006). Apparently, a common-law privilege exists for certain matters outside the scope of the statute. 854 N.E.2d at 489. Presumably, the latter might be waived by putting the material at issue.

[121] *E.g.*,

United States: United States v. Walters, 913 F.2d 388 (7th Cir. 1990);

Alaska: Hikita v. Nichiro Gyogyo Kaisha, Ltd., 713 P.2d 1197, 1203 (Alaska 1986) (client's offer of attorney's testimony as to client's state of mind waives privilege);

Florida: Savino v. Luciano, 92 So. 2d 817, 819 (Fla. 1957) (accountant-client privilege waived by bringing suit based upon a privileged audit);

Maryland: Beckette v. State, 31 Md. App. 85, 94 (1976) (calling attorney as character witness to client's truthfulness waives privilege).

[122] Lee v. Med. Prot. Co., 858 F. Supp. 2d 803, 806–09 (E.D. Ky. 2012).

[123] State *ex rel.* Montpelier US Ins. Co. v. Bloom, 757 S.E.2d 788, 794–798 (W. Va. 2014) (collecting cases).

[124] United States v. St. Pierre, 132 F.2d 837, 840 (2d Cir. 1942), *cert. granted*, 318 U.S. 751, *cert. dism'd,* 319 U.S. 41 (1943).

[125] *In re* Lott. 424 F.3d 446, 454 (6th Cir 2005) ("To be sure, litigants cannot hide behind the privilege if they are relying upon privileged communications to make their case. 'The attorney client privilege cannot at once be used as a shield and a sword.' But while the sword stays sheathed, the privilege stands.");
In re Geothermal Res. Int'l, Inc., 93 F.3d 648, 652 (9th Cir. 1995) ("The privilege is waived … only when the client tenders an issue touching directly on the substance or content of a privileged communication—not when the testimony sought would be only 'one of several forms of indirect evidence' about an issue.")

[126] *In re* Kellogg Brown & Root, Inc., 796 F.3d 137 (D.C. Cir. 2015).

Act suit. KBR had conducted an internal investigation of the allegations that were the subject of the suit pursuant to its Code of Business Conduct ("COBC"), and the plaintiff, Barko, was seeking discovery of the materials generated by that investigation. In a footnote to its motion for summary judgment, KBR had stated:

> KBR has an internal Code of Business Conduct ("COBC") investigative mechanism that provides a means of identifying any potentially illegal activities within the company. When a COBC investigation reveals reasonable grounds to believe that a violation of 41 U.S.C. §§ 51–58 (the "Anti-Kickback Act") may have occurred requiring disclosure to the government under [federal regulations], KBR makes such disclosures. KBR has made reports to the Government when it had reasonable grounds to believe that a violation of the Anti-Kickback Act occurred. KBR intends for these investigations to be protected by the attorney-client privilege and attorney work product privilege (indeed, they are not even given to the Government as part of disclosures), but has not asserted privilege over the fact that such investigations occurred, or the fact of whether KBR made a disclosure to the Government based on the investigation. Therefore, with respect to the allegations raised by Mr. Barko, KBR represents that KBR did perform COBC investigations related to [the KBR subcontractor and employee at the center of the fraud alleged by Barko], and made no reports to the Government following those investigations.[127]

The district court held that this put the COBC investigation at issue and waived the privilege. In its view, KBR's discussion of the COBC investigation "added up to a 'message' that the COBC reports 'contain no reasonable grounds to believe a kickback occurred.' Thus, it concluded that KBR created an implied waiver by 'actively' seeking 'a positive inference in its favor based on what KBR claims the documents show.' "[128]

The DC Circuit disagreed: "Where KBR neither directly stated that the COBC investigation had revealed no wrongdoing nor sought any specific relief because of the results of the investigation, KBR has not 'based a claim or defense upon the attorney's advice.' "[129] It explained

> "Corporations may protect their privileges without manipulation simply by being forthright with their regulators and identifying material as to which they claim privilege at the time they submit their voluntary disclosure reports. They will, of course, bear the risk that their reports will not be accepted as full disclosures. *But if they choose to make a pretense of unconditional disclosure*, they bear another risk—that we will imply a waiver of privilege with respect to any material necessary for a fair evaluation of their disclosures."[130]

In *KBR*, "there was no pretense of unconditional disclosure."[131]

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[127] 796 F.3d at 142 (citations omitted).
[128] 796 F.3d at 146.
[129] 796 F.3d at 147.
[130] 796 F.3d at 147, *quoting In re* Sealed Case, 676 F.2d 793, 823 (D.C. Cir. 1982) (emphasis by the *KBR* court).
[131] 796 F.3d at 147.

Another leading case is *Rhone-Poulenc Rorer, Inc. v. Home Indemnity Co.*[132] In *Rhone-Poulenc*, the Third Circuit declined to follow authorities that have extended the waiver rule to "cases in which the client's state of mind may be in issue."[133] (Even if such an exception were recognized, it would not apply in most first-party bad faith cases, because state of mind is not at issue on most such claims.) Any such extension would be contrary to the fundamental basis of the privilege:

> While [such] opinions dress up their analysis with a checklist of factors, they appear to rest on a conclusion that the information sought is relevant and should in fairness be disclosed. Relevance is not the standard for determining whether or not evidence should be protected from disclosure as privileged, and that remains the case even if one might conclude the facts to be disclosed are vital, highly probative, directly relevant, or even go to the heart of an issue.[134]

As the attorney-client privilege is intended to assure a client that he can consult with counsel in confidence, finding that confidentiality may be waived depending on the relevance of the communication completely undermines the interest to be served. Clients face the greatest risk of disclosure for what may be the most important matters. Furthermore, because the definition of what may be relevant and discoverable from these consultations may depend on the facts and circumstances of as yet unfiled litigation, the client will have no sense of certainty or assurance that the communication will remain confidential.[135]

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[132] Rhone-Poulenc Rorer, Inc. v. Home Indemnity Co., 32 F.3d 851, 863 (3d Cir. 1994) (PA law).

[133] 32 F.3d. at 864.

[134] 32 F.3d. at 864. *Accord* Note: *Developments in the Law: Privileged Communication*, 98 HARV. L. REV. 1450, 1640 (1985) ("Absolute privileges, such as the attorney-client … privilege[], should not depend upon case-by-case balancing of the harm to the relationship against an opposing litigant's need for the information. These privileges have been instituted on the basis of a system-wide balancing of costs and benefits. Once all the technical requirements of a privilege have been met, courts should not impose their own sense of the equities, because trial judges may tend to give decisive weight to the needs of the parties before them, without adequately considering the full, system-wide benefits of a privilege." (footnotes omitted)); Richard L. Marcus, *The Perils of Privilege: Waiver and the Litigator*, 84 MICH. L. REV. 1605, 1632–33 (1986) (waiver should only be recognized where party has attempted to garble the truth by injecting privileged material itself into the case).

[135] 32 F.3d. at 864. This approach is followed by most state courts and many federal courts. *E.g.*,

United States: Pritchard v. County of Erie, 546 F.3d 222, 229 (2d Cir. 2008) (privilege not waived unless holder relies in litigation on privileged advice);

United States/Mississippi: In re Itron, Inc., 883 F.3d 553, 560–63 (5th Cir. 2018) (predicting that Mississippi would not find waiver based on an opponent's supposed need for evidence of the privileged communications); *but see* Travelers Prop. Cas. Co. v. 100 Renaissance, LLC, 2020 Miss. LEXIS 409 (Oct. 29, 2020) (finding waiver of privilege for reasons discussed in § 16.04[4][a][i][B][II][bb], *below*);

United States/Indiana: Lorenz v. Valley Forge Ins. Co., 815 F.2d 1095, 1099 (7th Cir. 1987) (no special privilege rule for bad faith cases);

Alabama: Ex parte State Farm Fire & Cas. Co., 794 So. 2d 368, 373–76 (Ala. 2001) (suit for reimbursement of attorney fees does not waive privilege; waiver occurs only when content of the privileged communications has been put in issue);

California: Aetna Cas. & Surety Co. v. Superior Ct., 153 Cal. App. 3d 467, 477, [200 Cal. Rptr. 471, 476–77]

Other courts have agreed with and elaborated on these points. The purpose of the privilege "is to encourage and promote full and frank consultation between a client and a legal advisor by removing the fear of compelled disclosure of information."[136] The privilege cannot have that effect unless the client is confident of its operation. "An uncertain privilege, or one that purports to be certain but results in widely varying applications … is little better than no privilege at all.[137] Certainty cannot be provided if the protection is conditioned on case-by-case balancing:

> The attorney-client privilege, like all other evidentiary privileges, may obstruct a party's access to the truth. Although it may be inequitable that information contained in privileged materials is available to only one side in a dispute, a determination that communications or materials are privileged is simply a choice to protect the communication and relationship against claims of competing interests. Any inequity in terms of access to information is the price the system pays to maintain the integrity of the privilege. An unavailability exception is, therefore, inconsistent with the nature and purpose of the privilege.[138]

The Wright & Miller treatise agrees on this point:

> some courts have carried this waiver concept beyond the situation in which the privilege-holder affirmatively uses privileged materials to support a claim or defense, … and also applied it when the privilege-holder raises certain legal or factual issues. These cases do not fit within any sensible concept of waiver, and might best be viewed as ad hoc

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(1984) (no implied waiver unless insurer puts its own state of mind at issue; assertion that conduct objectively proper does not do so);

Connecticut: Hutchinson v. Farm Family Cas. Ins. Co., 273 Conn. 33, 44–45 (2005) (bad faith plaintiff's alleged need, even if compelling, cannot justify disclosure of privileged materials);

Indiana: Hartford Fin. Servs. Grp., Inc. v. Lake County Park & Recreational Bd., 717 N.E.2d 1232, 1235–36 (Ind. Ct. App. 1999) (fact that case involves bad faith claim does not limit application of privilege);

Missouri: Mo. *ex rel.* Shelter Mut. Ins. Co., 575 S.W.3d 476, 482–83 (Mo. App. 2018) (no waiver of attorney-client privilege where insurer had not asserted advice of counsel defense, even though insurer's corporate representative had testified in a deposition that the insurer did rely on counsel's advice in refusing to settle the claim against its insured);

Montana: Palmer by Diacon v. Farmers Ins. Exch., 261 Mont. 91, 108–09 (1993) (even in first-party bad faith cases, privilege applies unless waived and mere disclosure that advice was obtained does not waive unless insurer relies on that advice as defense; need for evidence does not permit discovery or use of privileged communications); State *ex rel.* United States Fid. & Guar. Co. v. Montana Second Jud. Dist. Ct., 240 Mont. 5, 13 [783 P.2d 911, 914–16] (1989) (privilege applies in third-party bad faith cases; need does not prevent application of privilege);

New Mexico: Public Serv. Co. of N.M. v. Lyons, 129 N.M. 487, ¶¶ 20–23 (2000).

[136] Fischel & Kahn, Ltd. v. van Straaten Gallery, Inc., 189 Ill. 2d 579, 584–85 (2000).

[137] Upjohn Co. v. United States, 449 U.S. 383, 392–93 (1981) (citations omitted).

[138] Admiral Ins. Co. v. United States District Court, 881 F.2d 1486, 1494 (8th Cir. 1989).

adjustments by courts in the scope of privilege.[139]

After quoting *Rhone-Poulenc*, the treatise observes that:

> Other courts have generally followed this path. As the Supreme Court put it in a different context, "[p]arties may forfeit a privilege by exposing privileged evidence, but do not forfeit one merely by taking a position that the evidence might contradict."[140]

[II] Automatic Waiver re Communications Prior to Claim Denial

There is a line of federal district court decisions predicting that Kentucky will not recognize any attorney-client privilege in first-party bad faith cases where those communications show "how the company processed the claim and why it made the decisions it did."[1] The later decisions all rely

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[139] 8 CHARLES ALAN WRIGHT, ARTHUR R. MILLER & RICHARD L. MARCUS, FEDERAL PRACTICE & PROCEDURE, § 2016.6 (3rd ed 2012) (footnotes omitted). One of the omitted footnotes quotes Richard L. Marcus, *The Perils of Privilege: Waiver and the Litigator*, 84 MICH. L. REV. 1605, 1632–33 (1986):

> "To the extent these decisions rest on forecasts about the privilege-holder's injection of privileged material at trial, the results are consistent with the truth-garbling fairness analysis. In form, however, they involve no such prediction. Instead, they seem to turn on allocation of burdens of pleading and proof and, on that basis, to rob the privilege-holder of privilege protection as the price for raising a given legal issue even though he will not make affirmative use of privileged material. Thus, the courts emphasize what the privilege-holder has to prove, not how he is going to prove it. Ultimately this shift in focus perverts waiver because it rests on the unfairness of having a privilege rather than the unfairness of the act relied upon to show a waiver."

See

United States: Pritchard v. County of Erie, 546 F.3d 222, 229 (2d Cir. 2008) (while "at issue" waiver exists to prevent unfairness, that unfairness must be based on the privileged party's presentation of evidence that depends on counsel's advice, so that examination of the actual content of that advice is necessary to assess that evidence);

Louisiana: Smith v. Kavanaugh, Pierson & Talley, 513 So. 2d 1138, 1143–46 (La. 1987) (agreeing with the standard proposed by Prof. Marcus);

New Hampshire: Aranson v. Schroeder, 671 A.2d 1023, 1030 (N.H. 1995) (same);

Nevada: Wardleigh v. Second Jud. Dist. Ct., 891 P.2d 1180, 1187 (Nev. 1995) (same).

[140] 8 WRIGHT & MILLER § 2016.6 (footnotes omitted), *quoting* United States v. Salerno, 505 U.S. 317, 323 (1992).

[1] Woods v. Std. Fire Ins. Co., 2020 U.S. Dist. LEXIS 83437, at *7–12 (E.D. Ky. May 12, 2020); Minter v. Liberty Mut. Fire Ins. Co., 2012 U.S. Dist. LEXIS 88199, at * 3–7 (W.D. Ky. June 26, 2012); Shaheen v. Progressive Cas. Ins. Co., 2012 U.S. Dist. LEXIS 120475 (W.D. Ky. Aug. 24, 2012).

substantially on *Shaheen v. Progressive Casualty Insurance Co.,*[2] so that is where discussion should start. *Shaheen* was actually a third-party case in which the claimant, Shaheen, was alleging that Progressive had improperly delayed payment of its policy limit with regard to Shaheen's claim against its insured, as to which liability and damages were allegedly never in doubt.[3] But Kentucky gives claimants a statutory claim analogous to that of a first-party insured. (*See* § 10.04[2][c][i]–[ii], *above*.) Shaheen sought disclosure of Progressive's full claim file, and Progressive asserted privilege for all communications by Progressive or its insured with counsel in the underlying case.

In reviewing the law regarding privilege in bad faith cases, the court asserted that, in actual first-party cases, the court recognized that "[t]hough broad claims of privilege are discouraged, 'when balanced against the need for litigants to have access to relevant or material evidence,' 'the privilege is not overridden by necessity or lack of available alternative sources.'"[4] Nonetheless, "[i]n first-party litigation, the entire insurance file is generally discoverable. Issues of privilege raised by insurance companies are often discarded with these cases because the insurance file was created by the insurer on the insured's behalf."[5] In third-party cases, like *Shaheen,* the court found the rule "less definite":

> On one hand, almost all of the evidence of an insurer's potential bad faith in failing to settle was created either proceeding up to or during the legal action against the insured. It contains confidential communications between the insured and the attorney retained by the insurance company; thus, much of the insurance file maintained by the insurer necessarily raises issues of attorney-client or work-product privilege. On the other hand, the evidence that would most assist the plaintiff to show bad faith on the part of the insurer is the communications maintained in the insurance file. "Often, the plaintiff in a third-party bad faith suit has no reasonable means of proving his or her claim without the benefit of certain documents contained in the claim file." Courts are caught between the competing interests of protecting privileged communications and releasing the most impactful evidence.[6]

The *Shaheen* court noted that authority elsewhere was divided and it found no clear guidance from Kentucky courts, though it said that the Kentucky Supreme Court had rejected an opportunity to create an exception to the privilege in bad faith cases. In *George v. Guaranty National Insurance Co.,*[7] the Kentucky Court of Appeals had rejected a request to create an exception to the privilege but reversed a summary judgment for the insurer on the bad faith claim.[8] The supreme court found summary judgment for the insurer appropriate, mooting the privilege issue.[9]

Nonetheless, the *Shaheen* court upheld privilege and work product protections for communications between the insureds and their defense lawyers, even if disclosed to the insurer. It

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[2] Shaheen v. Progressive Cas. Ins. Co., 2012 U.S. Dist. LEXIS 120475 (W.D. Ky. Aug. 24, 2012).

[3] 2012 U.S. Dist. LEXIS 120475, at *1–2.

[4] 2012 U.S. Dist. LEXIS 120475, at *6–7 (citations omitted).

[5] 2012 U.S. Dist. LEXIS 120475, at *7–8 (citations omitted).

[6] 2012 U.S. Dist. LEXIS 120475, at *7–8 (citations omitted).

[7] George v. Guar. Nat'l Ins. Co., 1996 Ky. App. LEXIS 39 (Mar. 8, 1996), *rev'd in part,* 953 S.W.2d 946 (Ky. 1997).

[8] George v. Guar. Nat'l Ins. Co., 953 S.W.2d 946, 948 (Ky. 1997) (summarizing opinion below).

[9] 953 S.W.2d at 948.

rejected protection for communications and materials shared with a third party and to communications involving neither legal advice nor work product.[10] As a result, everything that had been said about privilege in bad faith cases was dictum, having nothing to do with the court's actual decision.

Minter v. Liberty Mutual Fire Insurance Co.[11] rejected privilege in a first-party bad-faith case, relying in part on the dicta asserting that "'[f]or discovery requests in first-party cases, because the insurance file is created on behalf of the insured, the entire file is typically discoverable by the plaintiff.'"[12] The court recognized that "[t]he Kentucky Supreme Court has repeatedly declared that the attorney-client privilege is generally sacrosanct and may not be overridden, even by an opposing party showing its need to obtain the information contained in privileged communications."[13] But the Kentucky Rules of Evidence had recognized an exception for communications made in furth of crimes or frauds, and the court thought this apposite because "Minter alleges that her insurer violated the terms of the Unfair Claims Settlement Act, which was enacted 'to protect the public from unfair trade practices and fraud.'"[14] The court held that the privilege did not shield attorney-client materials from protection, reasoning that

> first-party bad-faith actions against an insurer can only be proved by showing exactly how the company processed the claim and why the company made the decisions it did. Without the claims file, a contemporaneously-prepared history of the handling of the claim, it is difficult to see how an action for first-party bad faith could be maintained without requiring an overwhelming number of depositions, whose costs would thereby render all but the rare wealthy few first-party bad faith claimants financially unable to proceed. This court is therefore unwilling to predict that Kentucky's highest court would enter an opinion that would shield portions of a claims file from discovery in a first-party bad faith case on the basis of the attorney-client privilege, and therefore rules that the attorney-client privilege does not shield materials contained in Ms. Minter's underlying claims file.[15]

Woods v. Standard Fire Insurance Co.[16] was another first-party bad-faith case. It relied on *Minter* and *Shaheen* to find the attorney-client privilege inapplicable in first-party bad-faith cases, except that the privilege does apply to advice rendered with respect to the bad-faith case itself.[17]

Insofar as *Minter* relied on the crime-fraud exception to the privilege, it ignored the fact that invoking that exception requires the party seeking disclosure to make a prima facie showing that the legal advice in question was sought for the purpose of perpetrating or concealing a crime or fraud. (*See* § 16.04[4][[b][i], *below*.) There is no suggestion in any of these cases that there was any basis (let alone a prima facie showing) of any such illicit purpose in seeking the legal advice. At most, the suggestion is that disclosure of that advice (and the communications requesting it) would aid the plaintiff in showing

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[10] *Shaheen*, 2012 U.S. Dist. LEXIS 120475, at *14–24.

[11] Minter v. Liberty Mut. Fire Ins. Co., 2012 U.S. Dist. LEXIS 88199 (W.D. Ky. June 26, 2012).

[12] 2012 U.S. Dist. LEXIS 88199, at *6.

[13] 2012 U.S. Dist. LEXIS 88199, at *3.

[14] 2012 U.S. Dist. LEXIS 88199, at *3–4 (citation omitted).

[15] 2012 U.S. Dist. LEXIS 88199, at *6–7.

[16] Woods v. Std. Fire Ins. Co., 2020 U.S. Dist. LEXIS 83437 (E.D. Ky. May 12, 2020).

[17] 2020 U.S. Dist. LEXIS 83437, at *7–12.

that the insurer lacked an adequate basis to withhold payment and knew that it lacked such a basis.

All of these cases ignored significant contrary guidance from the Kentucky courts. *Shaheen* recognized that the Kentucky Supreme Court has held that "'the privilege is not overridden by necessity or lack of available alternative sources.'"[18] Yet *Shaheen* and the cases relying on it failed to recognize that the great weight of authority elsewhere holds that this principle precludes setting aside the privilege in bad faith cases. (*See* § 16.04[4][a][i][A][I], *above*.) This point is reinforced by the fact that the Kentucky Court of Appeals had held that an insurer's attorney-client privilege is fully effective in a first-party bad faith case.[19] While that decision was reversed based on another issue, it is still an indication of how the Kentucky courts are likely to rule in the future.

Moreover, the cases relied upon by the district courts to support limiting the privilege do not support that result in the factual context presented by those cases. One of them presented no privilege issue and did not comment on it, even in dicta.[20] Two of them addressed issues of work product rather than privilege,[21] an important distinction, as non-opinion work product is routinely discoverable on a showing of need. (*See* § 16.04[3][b], *above*.) Two of the cases involve claims of privilege regarding communications between the insurer and the defense counsel it retained to defend its insured (who later suffered an excess judgment), a context in which both insured and insurer were represented by that defense counsel, so there was no privilege between the two. [22] The last of those cases involved privilege regarding communications between the insurer and the defense counsel it retained to defend its insured but reached a similar result on a different basis.[23]

Additionally, the court in *Shaheen* asserted that insurance claim files are generally discoverable in bad faith litigation because "the insurance file was created by the insurer on the insured's behalf."[24] But

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[18] *Shaheen*, 2012 U.S. Dist. LEXIS 120475, at *6–7, *quoting* St. Luke Hospitals, Inc. v. Kopowski, 160 S.W.3d 771, 777 (Ky. 2005).

[19] George v. Guar. Nat'l Ins. Co., 953 S.W.2d 946, 948 (Ky. 1997) (summarizing opinion below).

[20] Silva v. Basin W., Inc., 47 P.3d 1184, 1191 (Colo. 2002), *cited in Shaheen*, 2012 U.S. Dist. LEXIS 120475, at *7–8, for the proposition that "[i]ssues of privilege raised by insurance companies are often discarded with these cases because the insurance file was created by the insurer on the insured's behalf"; *Silva* actually discussed discoverability of reserves, not privilege).

[21] Chitty v. State Farm Mut. Auto. Ins. Co., 36 F.R.D. 37 (D.S.C. 1964), *cited in Shaheen*, 2012 U.S. Dist. LEXIS 120475, at *7, for the proposition that "[i]n first-party litigation, the entire insurance file is generally discoverable"); Allstate Indem. Co. v. Ruiz, 899 So. 2d 1121 (Fla. 2005), *cited in Shaheen*, 2012 U.S. Dist. LEXIS 120475, at *7, for the proposition that "[s]ome jurisdictions permit discovery of the entire [claim]file" in claims of failure to protect the insured from an excess judgment). The Florida Supreme Court had already held, when *Shaheen* was decided and despite *Ruiz*, that the protection of the privilege is not diminished in first-party bad faith cases. Genovese v. Provident Life & Acc. Ins. Co., 74 So. 3d 1064, 1069 (Fla. 2011).

[22] Dumas v. State Farm Mut. Auto. Ins. Co., 111 N.H. 43, 274 A.2d 781 (N.H. 1971); Groben v. Travelers Indem. Co., 49 Misc. 2d 14, 15, 266 N.Y.S.2d 616 (N.Y. Sup. Ct. 1965). This distinction was pointed out to the court in *Woods v. Standard Fire Insurance Co.*, 2020 U.S. Dist. LEXIS 83437, at *7–9 (E.D. Ky. May 12, 2020), but it was dismissed because both *Minter* and *Silva* were first-party bad faith cases not involving joint representation.

[23] State *ex rel.* Allstate Ins. Co. v. Gaughan, 508 S.E.2d 75, 89–91 (W. Va. 1998), *cited in Shaheen*, 2012 U.S. Dist. LEXIS 120475, at *7, for the proposition that "West Virginia permits the insurer to withhold privileged portions of the insurance file insofar as the plaintiff cannot show a compelling need for the material and insured has executed a release for the file"; court held that defense counsel retained by insurer to defend insured does not represent insurer, so the insurer has no attorney-client privilege, but held that the insurer did enjoy a quasi-attorney-client privilege, similar to the attorney-client privilege, but subject to divestment on a showing of substantial need).

[24] 2012 U.S. Dist. LEXIS 120475, at *7–8 (citations omitted).

whatever may be true of the claim file generally, one can be sure that an insurer's request for advice of counsel on whether benefits were due to the insured was not made "on the insured's behalf." Thus, the premise of this argument is simply wrong.

Minter argued that privilege should be denied because "first-party bad-faith actions against an insurer can only be proved by showing exactly how the company processed the claim and why the company made the decisions it did."[25] To be sure, the insured's need to show how the claim was processed and what information the insurer had available at the time does create a substantial need for discovery, which justifies requiring disclosure of ordinary work product otherwise protected from discovery. (*See* § 16.03[3][b], *above*.) But, as already noted, need for discovery does not justify invasion of the attorney-client privilege. Moreover, there is no need to address any subjective culpability of the insurer unless the insured can prove that the insurer acted without any objectively reasonable grounds for its action. Once that is proven, it would often be permissible to infer that the insurer recklessly disregarded that lack.

Thus, this line of federal district court cases should not be considered authoritative, even in Kentucky. Certainly, that line should not be followed elsewhere.

[B] Asserting Subjective Understanding of the Law May Put Legal Advice at Issue

[I] *State Farm Mutual Automobile Insurance Co. v. Lee*

Even under the slightly broader test for waiver applied in *State Farm Mutual Automobile Insurance Co. v. Lee,*[141] waiver would still be an exceptional finding.[142] State Farm had taken the position that a policy providing uninsured and underinsured motorist coverage for multiple cars did not permit "stacking" of coverages to provide higher limits for a single accident. The Arizona courts later decided otherwise. Lee sued, alleging bad faith in the refusal to permit stacking on her claim. Under Arizona law, bad faith requires both the absence of a reasonable basis for denying the claim and knowledge or reckless disregard of the absence of such a basis.[143] So there are both objective and subjective elements. In *Lee,* State Farm contended that its position was objectively reasonable under Arizona law at the time it denied Lee's claim. It also asserted that its adjusting personnel subjectively believed, in good faith, that their action was proper. The Arizona Supreme Court held that because State Farm chose to maintain the latter defense, it had waived the privilege as to the legal advice those personnel had received on the issue.

The *Lee* court reasoned that by asserting subjective good faith, State Farm was necessarily relying on the legal advice:

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[25] 2012 U.S. Dist. LEXIS 88199, at *6.

[141] State Farm Mut. Auto. Ins. Co v. Lee, 199 Ariz. 52 (Sup. Ct. 2000).

[142] The *Lee* court relied on *Hearn v. Rhay*, 68 F.R.D. 574 (E.D. Wash. 1975), discussed in § 16.04[4][a][ii], *below*. But the basis of the *Lee* decision can be read more narrowly than *Hearn*. So, this analysis treats *Lee* as a different, narrower standard than *Hearn*. Counsel for insureds can, of course, argue that *Lee* followed and adopted the *Hearn* standard. *See* Mendoza v. McDonald's Corp., 222 Ariz. 139, ¶ 39 (Ct. App. 2009) (so reading *Lee*); Roehrs v. Minnesota Life Ins. Co., 228 F.R.D.642, 646 (D. Ariz. 2005). *But see* Empire W. Title Agency v. Talamante, 323 P.3d 1148 (Ariz. 2014) (discussed in this section, arguably reading *Lee* more narrowly than *Hearn*). Even if *Lee* is read to follow *Hearn*, other courts that find the *Lee* result appropriate might do so without going so far as *Hearn*.

[143] Noble v. Nat'l Amer. Life Ins. Co., 128 Ariz. 188–190 (Sup. Ct. 1981).

> State Farm had its agents evaluate the law—policy provisions, statutes, and cases. On the basis of this evaluation, including, we must suppose, the information gained from counsel, State Farm's agents denied the claims in good faith based on their view of the law, not because of what its lawyers had advised. We note, of course, that State Farm does not claim … that the lawyers' advice formed no part of the evaluation … . [W]e believe the trial judge was well within his discretion in concluding that advice of counsel was part of the basis for State Farm's defense. What State Farm knew about the law obviously included what it learned from its lawyers.
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> … . [I]n cases such as this in which *the litigant* claiming privilege *relies* on and advances as a claim or defense a subjective and allegedly reasonable evaluation of the law—but an evaluation that necessarily incorporates what the litigant learned from its lawyer—the communication is discoverable and admissible.[144]

But the court explained that waiver arises only from an affirmative act putting the privileged material at issue; mere denial of the plaintiff's allegations is not an implied waiver.[145] Had State Farm merely denied Lee's allegations that it knew its conduct was unlawful, it could have insisted that Lee prove those allegations without waiving the privilege.[146]

[II] *Lee*'s Progeny

[aa] Applications of *Lee*

In *Mendoza v. McDonald's Corp.*,[147] *Lee's* waiver standard was read to extend beyond assertions of reasonable subjective understanding of the law. Mendoza was a McDonald's employee who suffered a work-related injury. McDonald's was self-insured and handled the claim itself. Under Arizona law, injuries caused by bad faith claim-handling, as opposed to the consequences of the original work injury,

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Arizona: 199 Ariz. 52, ¶¶ 4–15 (emphasis original).

See

United States: Livingston v. North Belle Vernon Borough, 91 F.3d 515, 537 (3d Cir. 1996) (civil rights plaintiff who claimed not to have understood release negotiated as part of prior plea bargain necessarily waived privilege as to advice received from lawyer who negotiated plea bargain);
United States v. Bilzerian, 926 F.2d 1285, 1292 (2d Cir. 1991) (defendant waived privilege by asserting good faith based on a subjective understanding that his transactions were legal).

145 *Lee*, 199 Ariz. 52, ¶ 28 ("The party that would assert the privilege has not waived unless it has asserted some claim of defense, such as the reasonableness of its evaluation of the law, which necessarily includes the information received from counsel.").

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Arizona: 199 Ariz. 52, ¶ 33 n.7.

147 Mendoza v. McDonald's Corp., 222 Ariz. 139 (Ct. App. 2009).

are outside the workers' compensation immunity.[148] Mendoza sued for bad faith and obtained a $250,000 verdict.[149] But the trial court had improperly limited the damages that could be presented to the jury and improperly failed to instruct the jury on issue preclusion by findings in the workers compensation proceedings, requiring a retrial on both compensatory and punitive damages.[150] It had also allowed McDonald's to redact its claim file to exclude production of communications regarding legal advice, and Mendoza challenged this on appeal. The court of appeals concluded that the privilege had been waived.[151]

The court agreed that McDonald's had not defended by asserting a reasonable subjective understanding of the law, but concluded that this was not necessary to find a waiver under *Lee*. In its view,

> [a]t the heart of *Lee* is the recognition that, in the bad faith context, when an insurer raises a defense based on factual assertions that, either explicitly or implicitly, incorporates the advice or judgment of its counsel, it cannot deny an opposing party the opportunity to discover the foundation for those assertions in order to contest them.[152]

McDonald's had presented testimony that its adjusters were "motivated by a desire to make sure that Mendoza received 'the care that was most appropriate or at least [she] explored her options.' "[153] Moreover,

> [t]hrough this and other evidence, McDonald's depicted its claims adjusters as attempting to act in Mendoza's best interest, using information from the independent medical examinations to determine what treatment would be best for her, and encouraging her to receive the best care available after a full consideration of all of her options. In representing its conduct this way, McDonald's affirmatively placed in issue the subjective motives of its adjusters in administering Mendoza's claim. It thus defended this case based on the subjective reasonableness of its conduct.[154]

The adjusters admitted having based decisions to request independent medical examinations and the selection of examining doctors on the advice of counsel and had no independent recollection of the reasons for doing so. Other evidence arguably suggested that "McDonald's forced Mendoza to 'go through needless adversarial hoops to achieve' her workers' compensation benefits." Because it had acted based on the advice of counsel, the testimony regarding its subjective motivation placed counsel's advice at issue.[155]

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[148] 222 Ariz. 139, ¶ 30.
[149] 222 Ariz. 139, ¶ 29.
[150] 222 Ariz. 139, ¶¶ 30–34, 57–61.
[151] 222 Ariz. 139, ¶¶ 35–53.
[152] 222 Ariz. 139, ¶ 42.
[153] 222 Ariz. 139, ¶ 45.
[154] 222 Ariz. 139, ¶ 46. *See* Roehrs v. Minnesota Life Ins. Co., 228 F.R.D. 642, 646–47 (D. Ariz. 2005) (where defendant relied on subjective good faith of adjusters who stated that they had considered advice of counsel in denying the claim, privilege waived).
[155] 222 Ariz. 139, ¶ 51. The superior court did not find waiver with respect to the attorneys' file relating to litigation of the workers' compensation case, as contrasted with adjustment of the claim, and Mendoza did not raise that issue on appeal, so she would not be permitted to examine that file on remand. 222 Ariz. 139, ¶ 53 n.25.

More recently, the Arizona Supreme Court emphasized the narrowness of *Lee*, finding no waiver of privilege in *Empire West Title Agency v. Talamante*.[156] Jemmett was interested in buying a vacant lot, and discovered a quitclaim deed abandoning an easement essential to developing the lot. Empire West allegedly told him that the deed would not affect his claim to the easement. Jemmett then told Empire West that DOS Land Holdings, Inc. would purchase the lot. DOS sent Empire a Closing Instructions Letter ("CIL") directing it to obtain a deed with a description including the easement. Empire West took a deed that did not refer to the easement. DOS sued the adjacent landowner, seeking to confirm the easement, but the suit was dismissed. DOS then sued Empire West, alleging that it had "reasonably believed that [the easement] was represented in the documents used at closing." Empire West sought to compel production of attorney-client communications indicating what DOS knew before closing. The superior court held the privilege not waived, the court of appeals granted a writ requiring production, and the supreme court reversed grant of the writ.

The court reasoned that

> In contrast to State Farm's defense against the bad faith claims in *Lee*, the breach of contract claim in this case does not depend on DOS's mental state or subjective knowledge. And, unlike State Farm, DOS has not affirmatively put those matters at issue. It simply alleged that Empire breached the parties' contract by failing to comply with the CIL's terms. Although DOS's knowledge of the alleged title defect might be material to Empire's defense, DOS has done nothing to inject that issue into the litigation. Merely pleading a claim, as we noted in *Lee*, does not waive the attorney-client privilege.[157]

Because the allegation regarding DOS's reasonable belief was not essential to its contract claim, that allegation did not place DOS's mental state or subjective knowledge "at issue."[158] Moreover, even were its mental state at issue, the knowledge its law firm obtained from others about the state of the title would be imputed to it and could be ascertained without invading the privilege, so fair adjudication could be achieved while respecting the privilege.[159] DOS had not " 'thrust its lack of knowledge into the litigation' as a basis for its claim, while at the same time asserting the privilege so as to frustrate discovery of what it actually knew."[160]

The narrowness of *Lee* was also emphasized in *Everest Indemnity Insurance Co. v. Rea*.[161] The court stated the facts and the issue as follows:

> In the underlying case, Rudolfo claims that Everest committed bad faith by entering into a settlement agreement that exhausted the liability coverage of an Owner Controlled Insurance Program (OCIP) policy to the alleged detriment of certain insureds such as Rudolfo. Everest contends that the decision to settle was made in good faith based on its subjective beliefs concerning the relative merits of the various available

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[156] Empire W. Title Agency v. Talamante, 323 P.3d 1148 (Ariz. 2014).
[157] 323 P.3d 1148, ¶ 14.
[158] 323 P.3d 1148, ¶ 15.
[159] 323 P.3d 1148, ¶ 16.
[160] 323 P.3d 1148, ¶ 17.
[161] Everest Indem. Ins. Co. v. Rea, 236 Ariz. 503 (Ct. App. 2015).

> courses of action. Everest acknowledges that it communicated with counsel during the process of making that decision. The issue is whether Everest impliedly waived the attorney-client privilege regarding those communications by asserting its subjective belief in the good-faith nature of its actions and by consulting with counsel during that period of time.[162]

Rudolfo contended that the privilege is waived whenever a party defends based on the subjective reasonableness of its conduct after consulting with counsel. The *Everest Indemnity* court rejected this contention as inconsistent with *Lee*, which it quoted as follows:

> "We assume client and counsel will confer in every case, trading information for advice. This does not waive the privilege. We assume most if not all actions taken will be based on counsel's advice. This does not waive the privilege. Based on counsel's advice, the client will always have subjective evaluations of its claims and defenses. This does not waive the privilege. All of this occurred in the present case, and none of it, separately or together, created an implied waiver."[163]

Everest Indemnity concluded that "[t]o waive the privilege, something more is required. Under *Lee*, the attorney-client privilege is impliedly waived only when the litigant asserts a claim or defense that is dependent upon the advice or consultation of counsel."[164] It pointed to the following language in *Lee*:

> "But the present case has one more factor—State Farm claims its actions were the result of its reasonable and good-faith belief that its conduct was permitted by law and its subjective belief based on its claims agents' investigation into and *evaluation of the law*. It turns out that the investigation and evaluation included information and advice received from a number of lawyers. It is the last element, combined with the others, that impliedly waives the privilege. State Farm claims that its actions were prompted by what its employees knew and believed, not by what its lawyers told them. But a litigant cannot with one hand wield the sword—asserting as a defense that, as the law requires, it made a reasonable investigation into the state of the law and in good faith drew conclusions from that investigation—and with the other hand raise the shield—using the privilege to keep the jury from finding out what its employees actually did, learned in, and gained from that investigation."[165]

That analysis was applied to uphold the privilege in *Everest Indemnity*:

> Under *Lee*, to waive the attorney-client privilege, a party must make an affirmative claim that its conduct was based on its understanding of the advice of counsel—it is not sufficient that the party consult with counsel and receive advice. Here, there has been no showing that Everest was in

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[162] 236 Ariz. 503, ¶ 3 (footnote omitted).

[163] 236 Ariz. 503, ¶ 6, *quoting* State Farm Mut. Auto. Ins. Co v. Lee, 199 Ariz. 52, ¶ 38 (Sup. Ct. 2000).

[164] 236 Ariz. 503, ¶ 7.

[165] 236 Ariz. 503, ¶ 7, *quoting Lee*, 199 Ariz. 52, ¶ 38 (emphasis by the *Everest Indemnity* court).

> doubt as to any legal issue. Rather, it made decisions during the course of litigation and, of necessity, involved lawyers in that litigation. The decision Everest made to settle the case was not necessarily the product of legal advice, and Everest has not yet asserted—expressly or impliedly—that it was.[166]

The South Carolina Supreme Court has adopted the standard enunciated in *Lee*, but without evident consideration of the subsequent Arizona jurisprudence construing *Lee*.[167] South Carolina federal district courts, however, have recognized the limits of *Lee*.[26]

An unusual issue was presented in *Birth Center v. St. Paul Cos.*[168] St. Paul had defended a medical malpractice case to an excess judgment. It then consulted counsel about the risk of a bad faith case. After receiving counsel's advice, it paid the entire excess judgment. But the insured medical facility still sued for bad faith, alleging other damages from the failure to settle. St. Paul was compelled to disclose the opinion letter that was used at trial of the bad faith case, which it lost. Among the errors asserted on appeal was admission of the opinion letter in evidence. In Pennsylvania, the lawyer's communications to the client are privileged only to the extent that they reveal the client's communications to the lawyer, and there was no privilege here because the opinion was based solely on the unprivileged file of the malpractice case.[169] Work product protection was held to be waived because St. Paul argued to the jury that its prompt payment of the excess judgment showed its good faith in its entire handling of the case; that put its state of mind at issue and required consideration of the opinion received before payment to fully assess that.[170]

[bb] Improper Extension of *Lee*: *Travelers Property Casualty Co. v. 100 Renaissance, LLC*

The Mississippi Supreme Court found waiver of the privilege, based in part on *Lee*, in *Travelers Property Casualty Co. v. 100 Renaissance, LLC*.[27] In fact, *Lee* does not support that result on the facts in *100 Renaissance*, though there is another ground, arguably relied on by the court, that could possibly support the result.

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[166] 236 Ariz. 503, ¶ 9 (citations omitted).

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

[26] ContraVest Inc. v. Mt. Hawley Ins. Co., 2020 U.S. Dist. LEXIS 69430, at *14, 17–18 (D.S.C. Jan. 21, 2020) ("if an insurer asserts a claim or defense that necessarily includes information learned from counsel, and if the truth cannot be found unless that issue is explored, then implied waiver exists"; "If an insurance company simply asserts that its position is legally correct or that the language of its policy supports its position, privilege will not conceal the truth of either of those arguments. Either the law or the court's interpretation of the policy language will show whether the insurer's position was objectively unreasonable. In these scenarios, the truth as to whether the insurer acted in an objectively reasonable manner can be found without exploring advice provided by the insurer's counsel. To impliedly waive privilege, an insurance company must take one step further and assert that its position and handling of the claim is objectively reasonable in part because the insurance company's legal evaluation of the claim or some other fact that necessarily includes information from counsel."); Harriman v. Assoc. Indus. Ins. Co., 2020 U.S. Dist. LEXIS 93649, at *12–18 (D.S.C. May 29, 2020).

[168] Birth Ctr. v. St. Paul Cos., 727 A.2d 1144 (Pa. Super. Ct. 1999).

[169] 727 A.2d 1144, ¶¶ 47–50.

[170] 727 A.2d 1144, ¶¶ 63–64.

[27] Travelers Property Cas. Co. v. 100 Renaissance, LLC, 2020 Miss. LEXIS 409 (Oct. 29, 2020).

An unidentified driver had hit and damaged a flagpole owned by 100 Renaissance ("Renaissance"), which submitted a claim to Travelers under the uninsured motorist ("UM") property damage coverage of its auto policy. The UM coverage defined "property damage" to mean

> "injury to or destruction of:
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> a. A covered 'auto';
>
> b. Property contained in the covered 'auto' and owned by the Named Insured or, if the Named Insured is an individual, any 'family member'; or
>
> c. Property contained in the covered 'auto' and owned by anyone else 'occupying' the covered 'auto'."[28]

The claim was submitted by Renaissance's lawyer, Rick Wise, whose letter recognized that the flagpole did not fit this definition but argued that the definition improperly narrowed the scope of the statutorily required UM coverage:

> "I am aware that Travelers' policy language attempts to limit this legally mandated coverage by narrowly defining the term 'property damage' and excluding all forms of property other than an insured's auto and its contents. However, Section [Miss. Code Ann.] 83-11-101(2) contains no such limitation and requires coverage for 'all sums' for which the uninsured driver is liable as to 'property damage.' There is abundant legal precedent for the proposition that this coverage may not be limited or denied by policy provisions that are inconsistent with the statutory requirements.
>
> "As you may also be aware, the purpose of UM coverage—and the purpose of the law mandating its inclusion in all policies—is to provide to the insured (100 Renaissance) the same protection that would have been afforded the insured if the negligent driver had possessed legally required minimum auto liability coverage. I'm sure that Travelers would not claim that if this motorist had been an insured under a Travelers auto liability policy, and had run into a person's house, that liability coverage would not apply to the resulting 'property damage.' The result under UM coverage should be the same."[29]

The claim representative, Charlene Duncan, sought advice from in-house counsel, Jim Harris, and then replied to Wise by denying the claim based on the definition.[30] Renaissance sued alleging bad faith and took Duncan's deposition. [31] She was unable to explain the reasons for the denial, even by discussing how the policy limited coverage to "property damage" satisfying the definition. She certainly offered no reasons for rejecting Wise's argument that the definition impermissibly narrowed statutorily required coverage.[32]

Travelers moved for summary judgment and 100 Renaissance sought a continuance to seek

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[28] 2020 Miss. LEXIS 409, ¶ 2.
[29] 2020 Miss. LEXIS 409, ¶ 4.
[30] 2020 Miss. LEXIS 409, ¶ 5.
[31] 2020 Miss. LEXIS 409, ¶¶ 6–7.
[32] 2020 Miss. LEXIS 409, ¶ 7.

discovery of the correspondence between Duncan and Harris, which it also sought to compel. Travelers objected that these were privileged but, after in-camera review, the trial court ordered them produced. The supreme court granted a petition for interlocutory review of that order.[33]

The court began by noting that "Mississippi law requires that insurers have an arguable or legitimate basis to deny an insurance claim," and observed that the discovery at issue "sought to understand Travelers' reasons, or arguable or legitimate basis, to deny the claim."[34] The court first concluded that the privilege was inapplicable because the lawyer did not act as an adviser, but instead acted as a decisionmaker:

> Travelers sent the denial letter to Renaissance in an effort to explain its arguable and legitimate basis to deny the claim. The letter was signed by Duncan; but based on her deposition testimony, it clearly was prepared by someone other than Duncan, most likely Harris. If so, Harris did not act as legal counsel and give advice to Duncan to include in the denial letter. Instead, the denial letter contained Harris's reasons to deny the claim. Duncan's signature was simply an effort to hide the fact that Harris, not Duncan, had the personal knowledge of Travelers' reasons to deny the claim and to use the attorney-client privilege as a sword to prevent Renaissance from discovering the reasons from the person who had personal knowledge of the basis to deny the claim.[35]

The court regarded its decision as supported by *Lee*, quoting the following passage:

> When a litigant seeks to establish its mental state by asserting that it acted after investigating the law and reaching a well-founded belief that the law permitted the action it took, then the extent of its investigation and the basis for its subjective evaluation are called into question. Thus, the advice received from counsel as part of its investigation and evaluation is not only relevant but, on an issue such as this, inextricably intertwined with the court's truth-seeking functions. ***A litigant cannot assert a defense based on the contention that it acted reasonably because of what it did to educate itself about the law, when its investigation of and knowledge about the law included information it obtained from its lawyer, and then use the privilege to preclude the other party from ascertaining what it actually learned and knew***.[36]

What the *100 Renaissance* failed to understand is that *Lee* involved a different role for the legal advice, one not present in *100 Renaissance.* Under Arizona law, bad faith requires both the absence of a reasonable basis for denying the claim and knowledge or reckless disregard of the absence of such a

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[33] 2020 Miss. LEXIS 409, ¶¶ 7–9.

[34] 2020 Miss. LEXIS 409, ¶ 14.

[35] 2020 Miss. LEXIS 409, ¶¶ 15–17.

[36] 2020 Miss. LEXIS 409, ¶ 20, *quoting* State Farm Mutual Automobile Ins. Co. v. Lee, 199 Ariz. 52, 13 P.3d 1169, 1177 (Ariz. 2000) (emphasis by *100 Renaissance*). The court also relied on *Bertelsen v. Allstate Insurance Co.*, 796 N.W.2d 685, 703 (S.D. 2011) ("While the insurer did not expressly raise an advice-of-counsel defense, the claims adjusters' knowledge of the law consisted entirely of the advice of counsel. Because the insurer's evaluation of state law necessarily included the advice of counsel, the Arizona Supreme Court . . . held that the insurer affirmatively injected the advice of counsel into the case."). 2020 Miss. LEXIS 409, ¶ 21.

basis.[37] In *Lee,* State Farm not only sought to defend the reasonableness of its legal position, but also to defeat liability on the ground that its adjusters did not know or recklessly disregard any lack of a reasonable basis because they subjectively believed that the law was consistent with State Farm's position. *Lee* held that where "*the litigant* claiming privilege *relies* on and advances as a claim or defense a subjective and allegedly reasonable evaluation of the law—but an evaluation that necessarily incorporates what the litigant learned from its lawyer—the communication is discoverable and admissible."[38] But the *Lee* court explained that waiver arises only from an affirmative act putting the privileged material at issue; mere denial of the plaintiff's allegations is not an implied waiver.[39] Had State Farm merely denied Lee's allegations that it knew its conduct was unlawful, it could have insisted, without waiving the privilege, that Lee prove both the objective and subjective elements of bad faith.[40]

Unlike Arizona, Mississippi does not require a bad faith plaintiff to prove that the insurer knew or recklessly disregarded its lack of a reasonable or arguable basis to deny the insured's claim.[41] Because there was no issue in *100 Renaissance* as to Travelers' state of mind (and, in any event, Travelers had offered no defense based on its state of mind), *Lee* offers no support for denying the privilege in *100 Renaissance.*

The argument that the lawyer acted as a decisionmaker rather than an adviser (*see* § 16.04[3][c], *above*) requires separate consideration. Here, the policy language cited in the denial letter clearly supported the denial (although Duncan apparently could not explain how it did so). But, in submitting the claim, Wise had argued that the language was unenforceable, because he claimed that it improperly narrowed the statutorily required coverage. Duncan's request for legal advice must be read as focusing on whether that was a correct reading of the law. Harris apparently advised that this either was an incorrect reading of the law or that the issue was arguable. Had there been an explicit exchange to that effect, Duncan's decision to follow the legal advice should not have waived the privilege. There is no apparent reason why the less explicit mechanism actually used should make any difference.

Nor is there any reason why Renaissance need to know more about the basis of the decision. It could present Wise's argument that the relevant policy language was unenforceable. Travelers would necessarily respond by presenting an argument to the contrary. If Travelers prevailed on that argument, the issue of bad faith would go away. If not, the court would have been presented with the question of whether the argument presented by Travelers constituted a "reasonable or arguable basis" for denying the claim. (*See* § 17.03[5], *below*.) That said, Travelers might have avoided the privilege issue had its denial letter provided some explanation for its rejection of Wise's legal argument (*see* § 8.09, *above*), rather than leaving such an explanation to Duncan, who did not even understand the issue, let alone the explanation.

[III] ***Tackett v. State Farm Fire & Casualty Insurance Co.***

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[37] Noble v. Nat'l Amer. Life Ins. Co., 128 Ariz. 188–190 (Sup. Ct. 1981).

[38] *Lee,* 199 Ariz. 52, ¶¶ 4–15 (emphasis original).

[39] 199 Ariz. 52, ¶ 28 ("The party that would assert the privilege has not waived unless it has asserted some claim of defense, such as the reasonableness of its evaluation of the law, which necessarily includes the information received from counsel.").

[40] 199 Ariz. 52, ¶ 33 n.7.

[41] Mut. Life Ins. Co. v. Estate of Wesson, 517 So. 2d 521, 528 (Miss. 1987) (insurer liable for bad faith even though it mistakenly believed that the insured's policy did not contain the automatic premium loan provision that prevented its lapse for nonpayment of premium). *See 100 Renaissance,* 2020 Miss. LEXIS 409, ¶ 14 (stating only requirement that the insurer lack a reasonable or arguable basis, without mentioning any subjective element).

Something like the *Lee* rationale may also explain the otherwise puzzling decision in *Tackett v. State Farm Fire & Casualty Insurance Co.*[171] Tackett sued for bad faith delay in paying an underinsured motorist claim. After settling for the tortfeasor's $25,000 policy limit and obtaining State Farm's agreement to reform Tackett's policy to have underinsured motorist limits of $50,000 per person, Tackett's lawyer demanded that limit and provided evidence that, even disregarding future medical expenses or pain and suffering, Tackett would be unable to pursue her previous employment and would suffer a wage loss of more than $110,000 before reaching retirement age. State Farm ordered an independent medical examination, based on a suspicion that a prior accident contributed to Tackett's injuries. That produced an opinion that Tackett's current accident had activated a prior back condition and that she would now be able to perform sedentary occupations, such as secretary or receptionist. State Farm then offered $20,000 and was met with a renewed demand for limits, which it eventually agreed to pay. But the delay in payment was alleged to have been in bad faith.

In the bad faith case, State Farm denied the allegation that it lacked a reasonable justification for delaying payment of the full limit. It produced the claim file, while withholding materials for which it claimed privilege or work product protection. In answer to an interrogatory asking for all facts in support of any claim of reasonable justification, State Farm referred to the claim file and an affidavit of its claim superintendent, which together were said to show " 'a reasonable and orderly pattern of claims handling which ultimately and in due course led to the payment of the policy coverage.' "[172] The affidavit stated that:

> "Based on my experience of ten years, this claim was handled routinely, without any undue delay, with no bad faith on the part of State Farm Mutual Automobile Insurance Company or its employees. Furthermore, no reason existed to handle this claim unlike any other claim that comes through this office, and based on my experience, State Farm handled this claim as expediently as any other claims office in this local [sic] would have handled a similar claim."[173]

The trial court held that this waived privilege and work product protection and compelled production. After presentation of these materials at trial, the jury found bad faith and awarded damages. State Farm appealed, but the Delaware Supreme Court upheld the finding of waiver.[174]

It reasoned that:

> A party cannot force an insurer to waive the protections of the attorney-client privilege merely by bringing a bad faith claim. Where, however, an insurer makes factual assertions in defense of a claim which incorporate, expressly or implicitly, the advice and judgment of its counsel, it cannot deny an opposing party "an opportunity to uncover the foundation for those assertions in order to contradict them."[175]

It found that State Farm had made such factual assertions here:

> In its answer to the Tacketts' complaint, State Farm denied any

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[171] Tackett v. State Farm Fire & Cas. Ins. Co., 653 A.2d 254 (Del. 1995).
[172] 653 A.2d at 258 (emphasis omitted).
[173] 653 A.2d at 258.
[174] 653 A.2d at 258–59.
[175] 653 A.2d at 259 (citations omitted).

> unreasonable justification for denying the Tacketts' claim and asserted as an affirmative defense that the Tacketts had failed to supply information necessary for their claim to be processed. While this defense does not directly relate to any protected communications, it does suggest that there was nothing in the routine handling of the claim that contributed to the delay. When State Farm was required, in the course of discovery, to set forth factors in support of its claim of reasonable justification for nonpayment of the claim, it relied upon Rinehardt's affidavit and the claim file which, State Farm asserted, showed "routine handling." This Court has ruled "that the disclosure of even a part of the contents of a privileged communication surrenders the privilege as to those communications." Once State Farm alleged particularized facts that implicitly relied upon communications with counsel contained in the Tacketts' file, the first prong of the waiver analysis was satisfied—disclosure of otherwise protected facts relevant to a particular subject matter relied upon as a defense.[176]

This conclusion has been contested, on the ground that asserting that the claim file showed "a reasonable and orderly pattern of claims handling" and that it was handled "routinely" "is nothing more than a factual explanation of why [State Farm] did not act in bad faith" and made no implicit assertion of reliance on, or even receipt of, legal advice.[177] While that criticism has force, it is nevertheless true that the affidavit was based on the claim superintendent's review of the entire file, including the privileged and work product materials. Thus, it literally relied on those materials as part of the basis for the defense, and could be characterized as a "partial disclosure."

The court's decision to so characterize the interrogatory response may have been influenced by what production of the privileged and work product materials had revealed. Before State Farm ordered the independent medical examination, its outside counsel, Tybout, had reported that " 'there is not much more that can be done in the taking of additional discovery. The possible benefit of an independent medical examination is questionable.' "[178] Moreover, he had advised that " 'the arbitrator would probably find the [Tackett's] claim had a value of $50,000 or more even though it has some obvious disabilities.' "[179] This could be taken to suggest that State Farm was grasping at straws in seeking the independent medical examination, and the findings of the examination could be seen as doing little to dispel such a conclusion.

The reasoning of the Delaware court is inconsistent with the minority view (*see* § 16.04[4][a][ii], *below*) that bases waiver in part on the bad faith plaintiff's general need for access to privileged materials to prove bad faith. It clearly requires reliance on a "partial disclosure" of privileged materials before waiver can be found.[180]

[C] Putting Opinion Work Product "At Issue"

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[176] 653 A.2d at 259–60 (citation omitted).

[177] Douglas R. Richmond, *Advice of Counsel and Insurance Bad Faith*, 73 MISS. L.J. 95, 126–27 (2003).

[178] 653 A.2d at 257.

[179] 653 A.2d at 257.

[180] *See* Thomas v. Harford Mut. Ins. Co., 2004 Del. Super. LEXIS 158, at *16–19 (Del. Super. Ct. April 20, 2004) (finding no waiver based on the absence of any "partial disclosure").

In *Birth Center v. St. Paul Cos.*,[42] St. Paul was concerned about possible bad faith liability after its insured suffered an excess judgment. It asked outside counsel to review the underlying claim file and advise on its possible bad faith exposure. It then paid the excess judgment, but was sued for consequential damages allegedly caused by its failure to settle.[43] When the bad faith case was litigated, the trial court allowed evidence of this advice to be presented to the jury, and St. Paul suffered a large judgment. The superior court held that the attorney-client privilege did not apply. (*See* § 16.04[2][a], *above*.) St. Paul also argued that counsel's advice was protected as opinion work product, but the superior court held that this protection was waived because St. Paul had put in issue its reasons for its payment of the excess judgment:

> St. Paul attempted to use the evidence of its payment of the excess verdict not merely as evidence to show that its conduct was not extreme and outrageous, or to limit Birth Center's contractual damages, but as conclusive evidence that St. Paul's decision not to settle the *Norris* Case was made in good faith. By framing its argument and the evidence in such a manner, St. Paul placed the reasons behind its payment of the excess verdict directly in issue. Thus, St. Paul made its state of mind, at the time it satisfied the excess verdict on behalf of Birth Center, relevant to the issue of whether its payment of the excess verdict was conclusive evidence of its good faith. Hence, assuming without deciding that the letters, memoranda, and notes were protected work product …, St. Paul waived its right to challenge discovery of these materials on appeal because St. Paul made them relevant to its state of mind at the time it paid the excess verdict.[44]

[ii] The Minority Broader Rule Exemplified by *Hearn v. Rhay*

While narrow waiver rules like those in *Rhone-Poulenc* and *Lee* are both predominant and better reasoned, many courts take a broader view of what will put privileged communications "at issue."[181] The leading case taking such a broader view is *Hearn v. Rhay*.[182] That was a suit against prison officials, and the court held that they placed at issue the legal advice they had received when they raised the defense of qualified immunity. This defense required the plaintiff to prove that the defendant " 'knew or reasonably should have known that the action he took … would violate the constitutional rights of the [plaintiff] or … took the action he did with the malicious intention to cause a deprivation of constitutional rights or other injury.' "[183] While defendants argued that they only sought to assert the objective reasonableness of their conduct, the court asserted that the defense necessarily put their state of mind at issue.[184] It articulated the following test for finding waiver:

> (1) the assertion of the privilege was the result of some affirmative act,

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[42] Birth Center v. St. Paul Cos., 727 A.2d 1144 (Pa. Super. Ct. 1999), *overruled on another issue*, Mishoe v. Erie Ins. Co., 573 Pa. 267 (2003).

[43] 727 A.2d 1144, ¶ 13.

[44] 727 A.2d 1144, ¶ 64 (footnote omitted)

[181] *Rhone-Poulenc* characterized such cases as being of "doubtful validity." Rhone-Poulenc Rorer, Inc. v. Home Indem. Co., 32 F.3d 851, 864 (3d Cir. 1994).

[182] Hearn v. Rhay, 68 F.R.D. 574 (E.D. Wash. 1975).

[183] 68 F.R.D. at 578, *quoting* Wood v. Strickland, 420 U.S. 308, 322 (1975).

[184] 68 F.R.D. at 581 n.15.

> such as filing suit, by the asserting party; (2) through this affirmative act, the asserting party put the protected information at issue by making it relevant to the case; and (3) application of the privilege would have denied the opposing party access to information vital to his defense.[185]

In addition to the criticisms already noted (*see* § 16.04[4][i][A], *above*), it has been argued that

> the logic of the *Hearn* approach cannot be contained. Some examples from recent case law should illustrate how easily the logic of *Hearn* can be expanded. In *United States v. Exxon Corp.*,[186] Exxon's motion to dismiss the government's action for failure to join indispensable parties was deemed a waiver of its attorney-client privilege with respect to the question of whether Exxon caused unlawful overcharges on the sale of oil by other co-owners of an oilfield. The court's logic came straight from *Hearn*: Exxon's motion asserted that Exxon was not responsible for the overcharges and thereby affirmatively placed the question of causation at issue; the only way for the government to prove such causation was by examining attorney-client "discussions wherein such a scheme may have been concocted."[187] The result, however, was outrageous. No matter what Exxon might have pleaded, so long as attorney-client communications were the easiest way for the government to attack Exxon's position, the privilege would be waived.[188]

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[185] 68 F.R.D. at 581. The Rice treatise states that "[w]hile *Hearn* has not been without its detractors, the court's logic has received overwhelming support in the courts that have addressed the issue." PAUL R. RICE, ATTORNEY-CLIENT PRIVILEGE IN THE UNITED STATES, § 9:52, at n. 15 (2018 update). *See also*

Washington: Pappas v. Holloway, 114 Wn. 2d 198, 207 (1990) (relying on *Hearn*); *cf.*

United States: Greater Newburyport Clamshell Alliance v. Public Serv. Co., 838 F.2d 13, 18–22 (1st Cir. 1988) (applying *Hearn* to balance the defendants' need for privileged evidence against plaintiffs' interests in preserving the privilege find limited waiver of privilege, but considering only the alternative of finding that the bringing of suit waived the privilege without any need for balancing). Other authorities cited in §§ 16.04[4][a][i]-[ii] suggest that the Rice treatise is mistaken on this point.

At one time, some courts that that the Florida Supreme Court had abrogated the privilege in bad faith case as to materials contained in an insurer's claim file. *E.g.*, Nowak v. Lexington Ins. Co., 464 F. Supp. 2d 1241, 1246–47 (S.D. Fla. 2006). The Florida Supreme Court has now held that any attorney-client privilege attaching to such documents cannot be lost except on grounds applicable to privileged materials generally. Genovese v. Provident Life & Acc. Ins. Co., 74 So. 3d 1064, 1069 (Fla. 2011). Moreover, while a judgment creditor under an excess judgment stands in the shoes of the insured to pursue a claim for bad faith failure to settle, the judgment creditor is not thereby entitled to access privileged communications between defense counsel and the insured or insurer. Maharaj v. Geico Caso Co., 289 F.R.D. 666, 670–71 (S.D. Fla. 2013), *aff'd* 2013 U.S. Dist. LEXIS 68535 (S.D. Fla. April 5, 2013); Boozer v. Stalley, 146 So. 3d 139, 144–48 (Fla. Ct. App. 2014) (collecting cases), *appeal dismissed per settlement*, 2015 Fla. LEXIS 900 (April 17, 2015).

[186] United States v. Exxon Corp., 94 F.R.D. 246 (D.D.C. 1981) [court's footnote renumbered].

[187] 94 F.R.D. 249 [court's footnote renumbered].

[188] Note: *Developments in the Law: Privileged Communication*, 98 HARV. L. REV. 1450, 1642 (1985).

Similarly, the South Dakota Supreme Court rejected *Hearn* in *Bertelsen v. Allstate Insurance Co.*[189] It reasoned that

> Application of the *Hearn* test alone provides insufficient guidance to be just and workable. In *Lee*, for example, an insurer argued that it acted in subjective good faith based on its evaluation of state law. While the insurer did not expressly raise an advice-of-counsel defense, the claims adjusters' knowledge of the law consisted entirely of the advice of counsel. Because the insurer's evaluation of state law necessarily included the advice of counsel, the Arizona Supreme Court applied the *Hearn* test and held that the insurer affirmatively injected the advice of its counsel into the case. The court thus ordered the disclosure of communications between the insurer and its counsel. We believe that *Lee* goes too far, demonstrating that the *Hearn* test does not strike an appropriate balance of the need for discovery with the importance of maintaining the privilege.[190]

Bertelsen supplemented *Hearn*

> to emphasize further the importance of protecting the attorney-client privilege. First, the analysis of this issue should begin with a presumption in favor of preserving the privilege. Second, a client only waives the privilege by expressly or impliedly injecting his attorney's advice into the case. A denial of bad faith or an assertion of good faith alone is not an implied waiver of the privilege. "Rather, the issue is whether Allstate, in attempting to demonstrate that it acted in good faith, actually injected its reliance upon such advice into the litigation." The key factor is reliance of the client upon the advice of his attorney.[191]

Arguably, this "supplementation" of *Hearn* effectively adopted the *Rhone-Poulenc* standard.

In *Andrews v. Ridco, Inc.*,[192] the South Dakota court emphasized the narrowness of *Bertelsen.* It rejected an argument that Twin City "injected its reliance upon the advice of counsel into the bad faith litigation by embedding attorney-client privileged communications in the … claim file notes and then redacting the communications," something that Andrews, the insured, contended "has compromised his 'ability to determine [Twin City's] claim handling decisions and the grounds thereof.' "[193] Andrews relied on a statute requiring insurers to maintain a complete claim file.[194]

The court responded that Andrews' theory of implied waiver misconstrued *Bertelsen:*

> Regardless of whether Twin City "embedded and redacted" attorney-client communications into the claim files notes as Andrews suggests, this practice does not demonstrate that Twin City injected its reliance on

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[189] Bertelsen v. Allstate Ins. Co., 2011 SD 13.
[190] 2011 SD 13, ¶ 52 (citation omitted).
[191] 2011 SD 13, ¶ 53 (citations omitted).
[192] Andrews v. Ridco, Inc., 2015 SD 24.
[193] 2015 SD 24, ¶ 22.
[194] 2015 SD 24, ¶ 22, *citing* S.D. COMP. LAWS 58-3-7.4.

> the advice of counsel into the bad faith litigation. Under *Bertelsen*, Andrews must demonstrate that Twin City asserted the attorney-client privilege as a result of an affirmative act, such as raising an affirmative defense, *and then that Twin City specifically relied on the advice of counsel to support its argument that it acted in good faith.*[195]

In *Andrews*, no waiver had been shown, because, so far as Andrews had shown, "Twin City has not placed at issue its subjective good-faith reliance on the advice of counsel such as would invoke an implied waiver of the … claim file notes."[196] Nor had the circuit court made any finding of any affirmative act by Twin City injecting privileged communications into the litigation "by specifically relying on the advice of counsel in support of its argument that it acted in good faith."[197] Moreover, it was improper to find a blanket waiver as to privileged material in the Andrews claim file (and 199 other claim files). The privilege is waived only to the extent necessary to reveal the advice that has been placed at issue, and the circuit court had made no findings supporting the conclusion that privilege had been waived as to all privileged communications reflected in the files.[198] Accordingly, the order compelling production could not be supported on the record before the court.

Andrews confirms that, despite its reliance on *Hearn*, the South Dakota court has not authorized a waiver standard broader than that in *State Farm Mutual Automobile Insurance Co. v. Lee*.[199] (*See* discussion in § 16.04[a][i], *above*.)

A Missouri court of appeals has similarly rejected any broadened application of *Hearn* allowing the "affirmative act" placing privileged material to be implied from the fact that counsel had been consulted; it reasoned that

> [t]he resulting application of such a rule would mean that an insurance company would always waive privilege if it ever consulted an attorney because the attorney's counsel would likely form at least part of the basis for the insurance company's behavior. An insurance company would never be entitled to attorney-client privilege in cases of bad faith settlement, even if the attorney's advice was but a part of the information the insurance company used in its decision making process.[200]

It is also noteworthy that *Hearn* itself might have reached the same result on narrower grounds. Like the claim handlers in *Lee*, if the prison officials testified that they did not know of the plaintiffs' rights, they would have necessarily placed at issue what they had been told by the counsel who advised them. If they chose not to testify, the prisoners could still have proven that they should have known of those rights, and might have been able to find other evidence of actual knowledge. But, absent intentional reliance on evidence that necessarily implicates privileged communications, it is contrary to the purpose of the privilege to allow the seeking of legal advice to be the mechanism for proving what otherwise cannot be proven.

Some states have appeared to look both ways in addressing "at issue" waiver, and have not clearly

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[195] 2015 SD 24, ¶ 23 (emphasis added).
[196] 2015 SD 24, ¶ 24.
[197] 2015 SD 24, ¶ 25.
[198] 2015 SD 24, ¶ 26.
[199] State Farm Mut. Auto. Ins. Co v. Lee, 199 Ariz. 52 (Ariz. 2000).
[200] State *ex rel.* Shelter Mut. Ins. Co. v. Wagner, 2018 Mo. App. LEXIS 701, *9–12 (Mo. Ct. App. June 26, 2018).

defined the standard for finding such waiver. For example, the Massachusetts Supreme Judicial Court has said that

> where a defendant raises a statute of limitations defense that is met by the plaintiff's reliance on the discovery rule, the statute of limitations invocation, by itself, does not permit the defendant to intrude into the attorney-client relationship between the plaintiff and her lawyer only to locate a statement by the client that might contradict a statement or position that she has taken in the particular case. Nor, more generally, does it allow such an intrusion "simply to determine whether the plaintiff may have revealed something to … her attorneys that might be helpful to the defendant[s'] case."[201]

This is reminiscent of the *Rhone-Poulenc* approach. On the other hand, the court also said

> we continue to recognize the concept of an at issue waiver of the attorney-client privilege, and, like a number of other courts, accept in general the premise that such waiver might come into play where a statute of limitations defense is met by the plaintiff's reliance on the discovery rule.[202]

But that recognition was limited by a rule that " 'there can be no 'at issue' waiver [of the attorney-client privilege] unless it is shown that the privileged information sought to be discovered is not available from any other source.' "[203] Taken together, the recognition of possible waiver and the limitation seem more consistent with the *Hearn* approach than with *Rhone-Poulenc*. Until the Massachusetts court confronts a case where the information sought is not discoverable from any other source, the Massachusetts rule will likely remain uncertain.

[iii] The Waiver Standard Makes No Difference When Mental State Is Not at Issue

The *Hearn* test only finds waiver when the information is "vital" to the other party's opposition to the case being presented by the client claiming privilege. Mere relevance is not enough. Given the purely objective standard applicable to most bad faith claims, privileged communications would not be "vital."

Such cases would be similar to *Frontier Refining, Inc. v. Gorman-Rupp Co.*,[204] which found it unnecessary to decide between *Hearn* and *Rhone-Poulenc,* because there was no waiver even under *Hearn.* Frontier sued Gorman-Rupp, a manufacturer of pumps used in Frontier's operations for equitable indemnity with respect to personal injury claims against Frontier arising out of an explosion allegedly caused by the pumps. To assess the reasonableness of personal injury settlements, Gorman-Rupp sought discovery of Frontier's communications with its counsel concerning the cases settled. But the

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[201] McCarthy v. Slade Assocs., 463 Mass. 181, 191 (2012), *quoting* Darius v. Boston, 433 Mass. 274, 282 (2001). Additionally, " '[t]he only reason we can see for the [defendant's] attempting to obtain [the] information from present counsel is to test the credibility of the plaintiffs—in other words, to see whether the plaintiffs confided to their counsel anything that contradicted their assertion that they did not know of a causal connection before being informed of it by counsel. We shall not allow the [defendant] to pit counsel against their clients in that fashion.' " 463 Mass. at 191 n.23, *quoting Darius*, 433 Mass. at 280.

[202] 463 Mass. at 192.

[203] 463 Mass. at 192.

[204] Frontier Refining, Inc. v. Gorman-Rupp Co., 136 F.3d 695 (10th Cir. 1998) (WY law).

reasonableness of the settlements could be determined by reviewing the evidence in the underlying cases and Gorman-Rupp could inquire of Frontier's employees about Frontier's motivations for settling. Consequently, "the privileged and protected information at issue [on the discovery motion] was not truly 'vital' to Gorman-Rupp's defense."[205]

Similar analysis was an alternate ground for finding no waiver in *Metropolitan Life Insurance Co. v. Aetna Casualty & Surety Co.*[206] (The court also held that even a showing of need would not have permitted privileged information to be discovered.)[207] Metropolitan sought coverage from its own insurers for 200,000 asbestos personal injury cases. Two of the excess carriers sought to discover attorney-client communications in the underlying actions, contending that Metropolitan had placed those communications at issue by bringing the coverage action, thereby waiving the privilege. The defendant insurers argued that they needed the privileged communications to determine the reasonableness of the settlements made in the underlying cases. The court disagreed. Metropolitan would have the burden of proving the settlements reasonable, and that question could be determined without any use of privileged materials. It

> should be examined under an objective standard. Reasonableness is determined according to factors such as, but not limited to, "whether there is a significant prospect of an adverse judgment, whether settlement is generally advisable, [whether] the action is taken in good faith, and whether it is not excessive in amount.
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> … [D]efendants in the present case can assess whether the settlements were reasonable by examining the facts of the asbestos tort actions—the same material that [Metropolitan] had available to it when making its decision—and by consulting experts, just as [Metropolitan] had the opportunity to do.[208]

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[205] 136 F.3d at 702. There are also cases predicting that state law would follow *Hearn* but where that prediction is arguably dictum. *E.g.*, Spargo v. State Farm Fire & Cas. Co., 2017 U.S. Dist. 96823, at *19–24 (D. Nev. June 22, 2017) (no waiver found: *in camera* inspection of the privileged materials revealed no support for the bad faith claim).

[206] Metropolitan Life Ins. Co. v. Aetna Cas. & Surety Co., 249 Conn. 36 (1999).

[207] 249 Conn. at 56–57.

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United States/Mississippi: In re Itron, Inc., 883 F.3d 553, 565 (5th Cir. 2018) (rejecting *Hearn*, but also holding that there would be no waiver under *Hearn* for the reasons stated in *Metropolitan v. Aetna*);

Connecticut: 249 Conn. at 57 (citations omitted).

See, e.g.,

Pennsylvania: United States Fire Ins. Co. v. Asbestospray, Inc., 182 F.3d 201, 212 (3d Cir. 1999) (claim that objective circumstances made it reasonable to delay filing interpleader action did not place legal advice at issue);

Florida: Home Ins. Co. v. Advance Mach. Co., 443 So. 2d 165, 168 (Fla. Dist. Ct. App. 1983) (in subrogation action, insurer's allegation that its settlement of the underlying action was reasonable did not waive privilege with respect to underlying action);

New York: Occidental Chem. Corp. v. Hartford Acc. & Indem. Co., 184 A.D.2d 1038 (1992) (insurance coverage action did not waive insured's privilege as to communications with defense counsel in the underlying actions).

Home Indem. Co. v. Lane Powell Moss & Miller[209] likewise found no waiver, even under *Hearn.* The Lane law firm had defended Home's insured, which suffered an excess judgment Home had to settle for $7 million. Home sued Lane, claiming that it had made a policy limits offer that Lane had failed to transmit to the plaintiffs. Lane argued that its failure was not the cause of the loss, because plaintiffs had never intended to settle within limits, seeking only to set Home up. On this basis, it sought discovery of the plaintiffs' lawyers' files. But the court found exploration of state of mind unnecessary, because plaintiffs had made a within-limits offer that Home had rejected only because it thought it had already insulated itself against excess liability by the offer Lane had failed to transmit.[210] Similarly, Home proved the reasonableness of its settlement with plaintiffs without relying on the advice of its counsel, so that advice was never put into issue.[211]

But see

United States/Florida: GAB Bus. Servs., Inc. v. Syndicate 627, 809 F.2d 755, 762 (11th Cir. 1987) (following *Hearn;* where indemnitee sought to prove reasonableness of settlement, indemnitor entitled to discovery from lawyer who advised indemnitee regarding the settlement);

United States/California: Walters Wholesale Elec. Co. v. Nat'l Union Fire Ins. Co., 247 F.R.D. 593, 596–97 (C.D. Cal. 2008) (where insured contributed to within-limits settlement and sued insurer for bad faith refusal to settle with only its own funds, insured waived privilege regarding personal counsel's advice regarding evaluation of the settled claim);

Massachusetts: Global Investors Agent Corp. v. Nat'l Fire Ins. Co., 927 N.E.2d 480, 488–89 (Mass. App. Ct. 2010) (after insurer improperly failed to defend, insureds sought recovery of a settlement of what they claimed was a meritless case, allegedly forced on them by the lack of a defense, and offered evidence of the litigation costs their lawyer told them they would incur if they did not settle; court held that this waived privilege as to counsel's evaluations of all factors concerning settlement value).

[209] Home Indem. Co. v. Lane Powell Moss & Miller, 43 F.3d 1322 (9th Cir. 1995).

[210] 43 F.3d at 1326–27.

[211]

Alaska: 43 F.3d at 1327;

See also

Washington: Lexington Ins. Co. v. Swanson, 240 F.R.D. 662, 670 (W.D. Wash. 2007) (even under *Hearn* test, privileged materials could not be discovered without a showing that they would be necessary to claimant's contention of bad faith);

Louisiana: Dixie Mill Supply Co. v. Continental Cas. Co., 168 F.R.D. 554, 556–58 (E.D. La. 1996) (no special limitation of privilege in bad faith cases; "reasonableness of the insurers' actions in a bad faith case can be proved by objective facts, which are not shielded from discovery and do not *necessarily* require the introduction of privileged communications at trial. The facts, rather than the legal advice or opinions, underlying the insurers' decisions at issue in the instant litigation can be developed through … discovery of non-privileged information");

Indiana: Hartford Fin. Servs. Grp., Inc v. Lake County Park & Recreational Bd., 717 N.E.2d 1232, 1235–36 (Ind. Ct. App. 1999) (similar holding and reasoning);

West Virginia: State *ex rel*. Med. Assur., Inc. v. Recht, 213 W. Va. 457, 468–470 (2003) (special privilege rule for bad faith cases unnecessary, because plaintiff could discover the underlying facts necessary to prove or disprove bad faith without discovering attorney-client communications).

[iv] Scope of Waiver

A waiver of privilege as to some documents or communications may extend to other documents. The law does not permit a party to seek benefit in litigation from disclosing privileged communications that aid the party while using the privilege to conceal related communications that might aid an adversary.[212] This rule is codified in Federal Rule of Evidence 502(a):

> When the disclosure is made in a federal proceeding or to a federal office or agency and waives the attorney-client privilege or work-product protection, the waiver extends to an undisclosed communication or information in a federal or state proceeding only if:
>
> (1) the waiver is intentional;
>
> (2) the disclosed and undisclosed communications or information concern the same subject matter; and
>
> (3) they ought in fairness to be considered together.[213]

The test is driven by the facts in the particular case.

> Because scope is determined on the basis of fairness, the breadth of communications included within the waiver will extend beyond the disclosed communications to whatever additional communications must be provided to the third party in order to give that party a fair chance to meet the advantages gained by the privilege holder through disclosure.[214]

Thus, where an insurer waived privilege for a coverage opinion, the waiver extended to all information in the lawyer's file regarding the claim.[215]

But extrajudicial disclosures which the client does not seek to use in the litigation are not waivers as to any communications not actually disclosed.[216]

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[212] *In re* Bulow, 828 F.2d 94, 101 (2d Cir 1981) ("it has been established law for a hundred years that when a client waives the privilege by testifying about what transpired between her and her attorney, she cannot thereafter insist that the mouth of the attorney be stopped").

[213] FED. R. EVID. 502(a).

[214] PAUL R. RICE, ATTORNEY-CLIENT PRIVILEGE IN THE UNITED STATES § 9:81, at 638–39 (2012).

[215] Willis v. Allstate Ins. Co., 2014 U.S. Dist. LEXIS 64963, at *5–6.

[216] *Bulow*, 828 F.2d at 102.