WHEN WORLDS COLLIDE: RESOLVING CONFLICTS OF LAW AS TO INDEPENDENT DEFENSE COUNSEL'S DUTY TO SHIELD OR SHARE PRIVILEGED COMMUNICATIONS WITH THE INSURER

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Self-evidently, one of the fundamental ethical duties of any lawyer is to protect confidential information shared by the client including communications covered by the attorney-client and work product privileges. This seemingly obvious ethical obligation becomes complicated, however, for independent defense counsel when an insurer who is funding the defense of the suit pursuant to a reservation of rights seeks information that ordinarily would be considered subject to those privileges – e.g., communications relating to the lawyer's analysis and investigation of the underlying claim.

The majority of jurisdictions hold that, because the attorney has been appointed as independent counsel and the insurer has not unqualifiedly accepted coverage of the claim, neither the attorney nor the policyholder may be compelled to provide the insurer with such privileged communications.[2] However, a minority of jurisdictions – most notably Illinois – hold that regardless of the attorney's status as independent counsel and the insurer's reservation of rights, the attorney nonetheless must share privileged information with the insurer that bears on the defense of the underlying case. The Illinois Supreme Court took this position in *Waste Management, Inc. v. International Surplus Lines Insurance Co.,* holding that the "cooperation clause" of the policy, the policyholder's and insurer's "common interest"

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[2] *See, e.g., Metropolitan Life Ins. Co. v. Aetna Cas. & Sur. Co.*, 249 Conn. 36, 730 A.2d 51 (1999); *State v. Hydrite Chem. Co.,* 220 Wis. 2d 51, 74–78, 582 N.W.2d 411, 420–22 (1998); *Rockwell Internat'l Corp. v. Super. Court,* 26 Cal. App. 4th 1255, 32 Cal. Rptr. 2d 153 (1994); *Owens–Corning Fiberglas Corp. v. Allstate Ins. Co.,* 74 Ohio Misc. 2d 174, 181, 660 N.E.2d 765, 769 (1993); *North River Ins. Co. v. Phila. Reins. Corp.,* 797 F. Supp. 363, 367–69 (D.N.J. 1992); *Remington Arms Co. v. Liberty Mut. Ins. Co.,* 142 F.R.D. 408, 416–18 (D. Del. 1992); *Bituminous Cas. Corp. v. Tonka Corp.,* 140 F.R.D. 381, 386–87 (D. Minn. 1992).

in defeating the underlying suit, and the law of privity all support compelling the production of such otherwise privileged communications.[3]

This split in authority creates substantial uncertainty for independent defense counsel as to whether they have a legal duty to share or shield such communications from the insurer when the geographic contacts of the dispute span jurisdictions following the majority and minority rules. The uncertainty is illustrated by two coverage lawsuits litigated in Illinois, discussed below, in which the courts reached opposite conclusions as to whether independent defense counsel's communications with an out-of-state policyholder located in a jurisdiction that follows the majority rule could be subjected to Illinois's minority *Waste Management* rule.

Allianz v. Guidant

In *Allianz Insurance Co. v. Guidant Corp.*, an intermediary Illinois Appellate Court held that out-of-state policyholders were required to produce to insurers (who had disclaimed coverage) the files maintained by their non-Illinois lawyers relating to underlying claims and communications between the policyholder and its lawyers with respect to those underlying claims.[4]

The policyholders consisted of a parent corporation, Guidant, that was incorporated and headquartered in Indiana, and a subsidiary, EVT, incorporated in Delaware and headquartered in California.[5] Underlying defense counsel were located in Colorado and Indiana.[6] Multiple insurers were joined in the suit, one of which was headquartered in California and another in Illinois.[7] The policyholder's broker was located in Illinois, as was the policyholder's risk manager who worked out of her home; Illinois was also where the policies were deemed "negotiated" and "delivered."[8] The underlying suits were brought in states scattered throughout the country.[9]

The Appellate Court relied upon the conflict-of-law approach set out in Section 139(2) of the *Restatement (Second) of Conflicts* (1971) to conclude that Illinois's

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[3] 144 Ill. 2d 178, 579 N.E.2d 322 (1991).

[4] 373 Ill. App. 3d 652, 869 N.E.2d 1042 (2007).

[5] *Id.* at 653, 869 N.E.2d at 1043.

[6] *Id.* at 669, 869 N.E.2d at 1058 (identifying lead counsel as based in Colorado and presuming that local counsel was from Indiana).

[7] *Id.* at 653, 670, 869 N.E. 2d at 1045, 1059.

[8] *Id.* at 670, 869 N.E.2d at 1059.

[9] *Id.* at 653, 869 N.E.2d at 1045.

Waste Management rule controlled the insurers' rights to access to these privileged documents.[10] Section 139(2) provides that:

> Evidence that is privileged under the local law of the state which has the most significant relationship with the communication but which is not privileged under the local law of the forum will be admitted unless there is some special reason why the forum policy favoring admission should not be given effect.[11]

The court assumed *arguendo* that either California or Indiana had the most significant relationship with the communications between the policyholders and their attorneys relating to the underlying lawsuits.[12]

Nonetheless, pursuant to the last clause of Section 139(2), the court held that there was no "special reason" not to apply Illinois law, as the local law of the forum. Applying the four factors addressed in Comment *d* to Section 139,[13] the court found that two of the factors weighed in favor of applying Illinois law, while two weighed against: (1) Illinois had the most numerous and significant contacts with the parties and the transaction as both the broker and the policyholder's risk manager were located there and the policy was negotiated and delivered in Illinois; (2) the evidence was highly material to the insurers' efforts to rescind the policies for material

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[10] *Id.* at 667-72, 869 N.E.2d at 1056-60.

[11] Quoted, *id.* at 668, 869 N.E.2d at 1057.

[12] *Id.* at 669-70, 860 N.E.2d at 1058.

[13] Comment *d* states:

> Among the factors that the forum will consider in determining whether or not to admit the evidence are (1) the number and nature of the contacts that the state of the forum has with the parties and with the transaction involved, (2) the relative materiality of the evidence that is sought to be excluded, (3) the kind of privilege involved and (4) fairness to the parties. If the contacts with the state of the forum are numerous and important, the forum will be more reluctant to give effect to the foreign privilege and to exclude the evidence than it would be in a case where the contacts are few and insignificant …. A second factor is the relative materiality in the particular case of the evidence that is sought to be excluded. The forum will be more inclined to give effect to the foreign privilege and to exclude the evidence if the facts that would be established by this evidence would be unlikely to affect the result of the case or could be proved in some other way …. The kind of privilege involved is also important. So the forum will be more inclined to give effect to a foreign privilege that is well established and recognized in many states than to a privilege that is relatively novel and recognized in only a few states …. The forum will be more inclined to give effect to a privilege if it was probably relied upon by the parties. Such reliance may be found if at the time of the communication the parties were aware of the existence of the privilege in the local law of the state of most significant relationship. Such reliance may also be found if the parties, although unaware of the existence of the privilege, made the communication in reliance on the fact that communications of the sort involved are treated in strict confidence in the state of most significant relationship ….

misrepresentations, which weighed in favor of Illinois's position that the information was discoverable; (3) the disfavored, minority position of the *Waste Management* doctrine weighed against applying the Illinois rule; and (4) that the policyholders and their lawyers could not reasonably have anticipated that Illinois law would govern privilege also weighed against Illinois's interest.[14] Given this even split among the four factors, the court could "not say that there is some 'special reason' for overriding Illinois's policy favoring the admission of such evidence."[15]

Apex Mortgage v. Great Northern

More recently, in *Apex Mortgage Corp. v. Great Northern Insurance Co.*, a federal Magistrate Judge presiding over a coverage suit pending in the United States District Court for the Northern District of Illinois held that independent Illinois counsel, defending under a reservation of rights, was not required to provide an insurer with communications with its Pennsylvania-headquartered policyholder-client concerning the defense of an underlying Illinois lawsuit arising from an incident that took place in Illinois.[16]

The coverage lawsuit initially was filed by the policyholder in federal court in Pennsylvania but then transferred to Illinois pursuant to 28 U.S.C. § 1404. Accordingly, pursuant to *Van Dusen v. Barrack*,[17] the court was required to apply Pennsylvania choice-of-law jurisprudence to resolve the conflict between Illinois and Pennsylvania law as to the insurer's right to these communications.[18]

The court concluded that Pennsylvania follows a "governmental interests" approach to conflicts that selects:

> the law of the predominantly concerned jurisdiction, measuring the depth and breadth of that concern by the relevant contacts each affected jurisdiction had with ... the policies and interests underlying the particular issue before the court.[19]

The court rejected the insurer's argument that Illinois had the greater interest in the application of its law given that the lawyers were located in Illinois and that the underlying lawsuit, underlying incident, and settlement negotiations of the

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[14] *Id.* at 670-72, 869 N.E.2d at 1059-60.

[15] *Id.* at 672, 869 at 1060.

[16] No. 17 C 3376, 2018 WL 3184981 (N.D. Ill. Jan. 8, 2018).

[17] 376 U.S. 612, 639 (1964).

[18] *See Apex Mortgage*, 2018 WL 3184981 at *2.

[19] *Id.* at *3, *quoting Samuelson v. Susen*, 576 F.2d 546, 551 (3d Cir. 1978) (ellipses in original).

underlying suit all took place in Illinois.[20] Rather, because the privilege belonged to the client, which was located in Pennsylvania, and because the attorney-client relationship "arose" in Pennsylvania, Pennsylvania had the most significant contacts to the attorney-client relationship.[21] In addition, Pennsylvania had "a compelling interest in protecting the confidential communications of its citizens."[22] Applying Pennsylvania's law of privilege was also consistent with the parties' stipulation that Pennsylvania's substantive law applied to the claims and defenses.[23]

Lessons for Independent Defense Counsel

As is typical of disputes that involve choice-of-law, neither *Guidant* nor *Apex Mortgage* provides much certainty as to how another court would resolve a similar conflict as to whether, in coverage a dispute with similar multi-state contacts, independent defense counsel is bound under the *Waste Management* doctrine to share privileged communications with the insurer. In the abstract, the factors dictated by Comment *d* to Section 139 upon which the court relied in *Guidant* are not much different than those identified in *Apex Mortgage* pursuant to Pennsylvania's governmental interest standard. Indeed, one could argue that Illinois had a more compelling basis for applying its rule to the privilege dispute in *Apex Mortgage* than in *Guidant* given that *Apex Mortgage* entailed an accident, underlying lawsuit, and defense counsel located in Illinois, unlike *Guidant*. On the other hand, it is easy to fault the analysis of the court in *Guidant*, which woodenly counted up which of the four factors from Comment *d* weighed in favor or against Illinois law, even though the language of the Comment *d* suggests a more nuanced analysis.

Both *Guidant* and *Apex Mortgage* recognize that a client and its attorneys would reasonably expect that the law of the state where the client is located and the attorney-client relationship arose would determine the existence of privilege. *Apex Mortgage* rightly gave paramount consideration to that factor. *Guidant*, by contrast, gave equal weight to the happenstance that the policyholder's risk manager worked out of her Illinois home, rather than at her employer's Indiana headquarters.

Guidant reinforces the perception that most state courts are inclined to apply their own law, and may stretch the choice-of-law analysis to reach that result. *Apex* supports the perception that federal judges – who have a significant docket arising under diversity jurisdiction – are more open to the application of out-of-state law.

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[20] *Id.* at *4.

[21] *Id.*

[22] *Id.*

[23] *Id.*

Both cases illustrate that races to the courthouse may matter. In *Guidant*, the *California-based* insurer, Allianz, filed its coverage suit in Illinois before the policyholder filed its own suit in Indiana state court.[24] In *Apex*, the policyholder sued first, in Pennsylvania.

[24] *See* 373 Ill. App. 3d at 653-54, 869 N.E.2d at 1045-46.