David vs. Goliath: How Policyholders Hold Great Power When Insurers Issue Reservations Of Rights And Panel Counsel Fail To Obey Ethical Rules

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Definitions

- Dependent counsel
- Disqualifying conflict of interest
- Independent counsel
- Informed written consent
- Reservation of rights

Page 2 of the Course Materials

The Narrow Situation

1. Plaintiff sues policyholder
2. Insurer reserves its rights to later deny coverage
3. Insurer appoints dependent counsel to represent the policyholder
4. Reservation of rights always creates conflicts of interest that may or may not disqualify dependent counsel – Three purposes

Page 3 of the Course Materials

Some insurers and dependent counsel do behave honorably

The remainder of this course will assume that neither does behave honorably and thus will focus on how the Rules may be applied in real time to achieve policyholder goals

Page 4 of the Course Materials

How Dependent Counsel Often Behave

1. Do not ask for copy of RoR, nor read it, nor analyze it, nor disclose analysis
2. Will not respond to questions about RoR
3. Will refer client to insurer for answers
4. Will represent to not worry about RoR
5. Will not comply with Rules

Page 4 of the Course Materials

Solution in a Nutshell

Just Say No

Policyholders should expressly withhold consent to representation until dependent counsel comply with numerous Rules

Page 4 of the Course Materials

Delivery Package

- Reservation of Rights
- Policy
- Model emails
- Excerpts of Rules
- Six Prongs of Rule 1.7
- Coverage Questionnaire
- Ethical Compliance Questionnaire
- Model Disclosure Letter
- Memorandum of Law
- Complaint to State Bar
- Complaint to Dept of Insurance

Page 4 of the Course Materials

Ethical Compliance Is Hard For Dependent Counsel

Rule 1.7 compels undivided loyalty with six prongs

Rule 1.4 requires lawyers to educate clients

Rule 1.6 requires confidentiality

Rule 1.8 requires consent for insurer payment

Page 5 of the Course Materials

Obtaining Admissible Evidence Is Easy

1. Rule 1.4 (disclosure)
2. Rule 1.7 (loyalty)
3. Rule 1.6 (confidentiality)
4. Rule 1.8 (payment)

Page 5 of Course Materials

Goals Of This Course

1. Limit Insurer's reservation of rights
2. Achieve prompt settlement at no policyholder cost
3. Pressure dependent counsel to quit
4. Urge plaintiffs and policyholder to cooperate to enforce rights to mutual benefit
5. Avoid, but prepare for, coverage litigation
6. Complete work in 2-6 weeks

Page 6, 12 of the Course Materials

Principals Informing Goals

1. **Power:** Rules empower policyholder/clients
2. **Burden:** It is easy for policyholder to challenge compliance
3. **Proof:** Policyholder should develop admissible evidence
4. **Timing:** Clear conflicts of interest **before** representation
5. **Uniformity:** The insurance industry behaves uniformly
6. **Protection:** Policyholder should take prompt steps to protect themselves **from** reserving insurers and their lawyer

Page 6 of the Course Materials

Techniques To Achieve Goals

1. The policyholder (not counsel) asks questions
2. The policyholder expressly withholds consent
3. Report dependent counsel to the State Bar
4. Report insurer to the Department of Insurance
5. Do not negotiate or compromise
6. Plaintiff tells Defendant or Counsel attaches documents to deposition
7. Motion to recuse own counsel

Page 7 of the Course Materials

Record Tele & Zoom?

PC § 632 prohibits secret eavesdropping of recording. Inform everyone at outset so recording is permitted because objectors may hang up. (*Kearney v. Salomon Smith Barney, Inc.* (2006) 39 Cal.4th 95; 45 Cal.Rptr.3d 730, 749.)

Page 7 of the Course Materials

Primary Jurisdiction Doctrine

Courts may defer to regulatory bodies

1. Report dependent counsel to the State Bar
2. Report reserving insurers to the Department of Insurance

Neither is likely to enforce the law

Page 8 of the Course Materials

Basic Insurance Defense Principles

1. Insurer accepts duty to defend because of potential for indemnity coverage
2. A failure to defend may require insurer to pay a non-covered judgment
3. A failure to reserve rights may forfeit coverage defenses
4. Dependent counsel owes policyholder duties of undivided loyalty, disclosure, and confidentiality
5. Insurers have rights of reimbursement

Page 8 of the Course Materials

Policyholder Guide

1. **Power**: Just say “no” to dependent counsel
2. **Burden**: Dependent counsel bears the burden of conflict resolution. Reserving insurers have burden to explain
3. **Proof**: Policyholders lose for “failure of proof”
4. **Timing**: Dependent counsel must clear conflicts **BEFORE** accepting representation

Principles Of Developing Evidence

1. Dependent counsel and claims agent must answer
2. Recorded **conduct** reveals actual violations of law
3. Policyholder alone should have direct contact
4. Policyholder counsel should not appear to exist
5. Policyholder should offer to accept any ethical dependent counsel – **never demand** independent counsel

Guide To Deliver Package

Model E-mails

1. Dependent Counsel does NOT have RoR
2. Accurately and completely confirm all oral contact
3. Ask for detailed explanation of coverage defenses
4. Send and complete Questionnaires
5. Deliver entire package
6. Report to regulatory authorities

Six Prongs Of Rule 1.7 Must Be Satisfied

No representation without informed written consent

1. Clients are directly adverse
2. Significant risk of lawyer being materially limited by relationships with insurer
3. or materially limited by the lawyer's own interests
4. Lawyer reasonably believes can do a good job
5. representation is prohibited by law.
6. representation involves the assertion of adverse claim

Rule 1.4 Requires Disclosure - Emails Make A Written Record

A lawyer shall promptly comply with reasonable requests for information and copies of significant documents when necessary to keep the client informed to make informed decisions

Pages 18,20 of the Course Materials

Rule 1.6 Requires Protection of Confidential Information

Dependent counsel shall not reveal the policyholder's secrets to the reserving insurer impacting coverage

How can dependent counsel know what to tell or not tell the reserving insurer without analyzing the reservation of rights?

Pages 18, 20 of the Course Materials

Rule 1.8 Requires Policyholder's Consent To Pay Dependent Counsel

1. No interference with independent professional judgment or with the lawyer-client relationship
2. Protect Confidential information
3. Obtains informed written consent before payment

Pages 19, 21 of the Course Materials

Disparate Case Law

1. California (Restatement) Rule
2. Per Se Rule
3. Enhanced Duties Rule

Since Rule 1.7 is universal, should judicial results also be universal?

Pages 64-68 of the Course Materials

Restatement of Law
Liability Insurance § 16

When the insurer reserves rights “and there are facts at issue that are common” to the liability action and the coverage dispute “the insurer must provide an independent defense of the action.”

Insurance Industry Defenses

1. Tripartite relationship eliminates conflicts
2. Dependent counsel does not represent the insurer
3. Dependent counsel does not get involved in coverage
4. Policyholder has the burden of conflict resolution
5. Deadlock on Rule 1.7 violation may require litigation
6. Violation of cooperation clause
7. Civil Code 2860 limits conflicts of interest
8. Duty to favor policyholder

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