



The Limited Scope of the Duty to Cooperate

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Historically, liability insurance policies have imposed on policyholders a duty to cooperate with insurers in the defense of actions. More recent policies have expanded this duty to impose upon policyholders an obligation to cooperate in the investigation of claims, as well. Commonly, however, insurers investigate claims or defend actions under reservations of rights to deny indemnity coverage for settlements by or judgments against policyholders, creating an adversarial relationship between policyholder and insurer. In light of this adversarial relationship, courts typically recognize limits on the duty to cooperate, protecting the policyholder's rights both to select and control defense counsel and to have confidential, privileged communications with that defense counsel regarding matters bearing upon the coverage dispute. Case law and ethics rules in various jurisdictions establish and illustrate these principles.

Determining the Existence and Expressed Limits of Any Duty to Cooperate

A threshold issue in regard to the duty to cooperate is whether the duty exists at all. Resolving the issue involves at least two steps. First, the parties must review the policy to determine whether it contains an express duty to cooperate. Most standard form policies, particularly more recent ones, impose such a duty. Certain historic policies or manuscript policies, however, may not.

If a policy purports to impose a duty to cooperate, the policyholder, in particular, must proceed with the second step of this threshold analysis, which is determining whether the insurer is fulfilling its policy obligations, such as they may exist at the time, or whether, in contrast, the insurer is in breach. During the early stages of a claim, when the duty to cooperate typically first is invoked, an insurer may breach its obligations in various ways, such as by refusing to defend to the full extent required by the policy and applicable law; by taking positions on trigger, allocation, or deductible/retention issues that are unwarranted under the policy and applicable law; or by issuing an improper partial or complete denial of indemnity obligations, which would amount to an anticipatory breach. If an insurer is in breach, it cannot insist upon performance by the policyholder of any duty under the policy, including the duty to cooperate — in other words, an insurer cannot have it both ways. *Monaghan v. Admiral Ins. Co.*, 1994 WL 118021 at *5 (9th Cir. 1994) ("the insurer's breach of its duties released [the policyholder] from its covenant of cooperation ... "); *Continental Cas. Co. v. City of Jacksonville*, 283 Fed. Appx. 686, 689 (11th Cir. 2008) ("An insurer's wrongful refusal to defend forfeits its corresponding right to control the defense.").

If the policy imposes a duty to cooperate, and if the insurer is not in breach, such that it can insist on the policyholder's cooperation, the parties must then determine the exact extent of the duty. Under third-party policies, which may provide defense coverage, the duty typically is limited. Further, the extent of the duty has evolved over time. A policy issued during the 1960s, for instance, might limit the duty to assisting with the actual defense of an underlying claim, such as by "attending hearings or trials" or "securing or giving evidence" or "obtaining the attendance of witnesses in legal proceedings." Under such a policy, if an insurer is not defending, the policyholder has no duty to cooperate, separate and apart, perhaps, from any duty of reasonableness or fair dealing that might arise under general principles of contract law. *BellSouth Communications, Inc. v. Church & Tower of Fla., Inc.*, 930 So.2d 668, 672 (Fla. 3d. Dist. Ct. App. 2006) ("[I]t is well established that an insurer's unjustified refusal to defend a suit against the insured relieves the insured of his contract obligation to leave the management of such suit to the insurer ... "); *Hospital Underwriting Group, Inc. v. Summit Health, Ltd.*, 63 F.3d 486, 496 (6th Cir. 1995) (It would be "illogic[al]" to "hold that where the insurer breaches by denying coverage and refusing to defend, it may still require the insured to abide by the cooperation clause in the policy ... ").

Later policies may broaden the duty to include assisting in the "investigation" of a claim or generally providing the insurer "with all information, assistance, and cooperation that the insurer reasonably requests." Variations on such language are numerous, and the parties should examine the policy carefully to determine the exact expressed extent of, and corresponding limitations on, any duty. If the insurer is not in breach, such clauses may purport to impose a broad duty upon the policyholder, although the duty may be limited as a matter of law, as discussed below.

Impact on the Selection and Control of Defense Counsel

The cooperation clause may be cited by insurers in disputes over the parties' respective rights to select and control defense counsel. When an insurer agrees to defend a policyholder under a reservation of rights, however, it generally loses the ability to select counsel or to control the defense, including the right to control the decision on whether to settle. *See, e.g., Asonia Associates Ltd. Partnership v. Public Service Mut. Ins. Co.*, 693 N.Y.S.2d 386, 390 (N.Y. Sup. Ct. 1998) ("In New York, 'When a conflict of interest exists, the remedy is to permit the insured to select defense counsel ...'"); *Rhodes v. Chicago Ins. Co.*, 719 F.2d 116, 120 (5th Cir. 1983) ("When a reservation of rights is made ... the insured may ... pursue his own defense. The insurer remains liable for attorneys' fees incurred by the insured and may not insist on conducting the defense."); *Twin City Fire Ins. Co. v. City of Madison*, 309 F.3d 901, 907 (5th Cir. 2002) ("When an insurer is defending under a reservation of rights, the carrier 'should afford the insured ample opportunity to select his own independent counsel to look after his interest.'"); *Moeller v. Amer. Guarantee and Liability Ins. Co.*, 707 So.2d 1062, 1071 (Miss. 1996) ("Because [policyholders were] being defended ... under a reservation of rights, [insurer] was obligated to let them select their own attorney at [insurer's] cost to represent them."); *United Services Auto. Ass'n. v. Morris*, 154 Ariz. 113, 119 (1987) (observing that the "majority" rule is that "an insurance carrier should not be allowed to insist upon exclusive control of the defense while reserving coverage issues ... " and holding that cooperation clause did not bar settlement of underlying claim by policyholder when insurer had reserved rights); *see also Insurance Co. of North America v. Spangler*, 881 F.Supp 539, 545 (D. Wyo. 1995) (holding that "the cooperation clause prohibition against settling without the insurer's consent forbids an insured from settling *only* claims for which the insurer *unconditionally* assumes liability under the policy.") (emphasis added).

These limitations on the insurer largely derive from the ethical rules that govern the conduct of defense counsel. Rules of professional conduct generally require attorneys to represent their clients loyally and zealously. To do so, an attorney must first determine the identity of his or her client. In other words, an attorney must first identify the person or entity he or she represents. In most jurisdictions, courts have held that when an insurer has reserved rights and/or partially denied claims, the defense counsel's client is the policyholder, not the insurer. *See Jackson v. Trapier*, 247 N.Y.S.2d 315, 316 (N.Y. Sup. Ct. 1964) ("defendant is the client and not the insurance carrier even though the latter may have chosen the counsel and may be paying his fee"); *Continental Cas. Co. v. Pullman, Comley, Bradley & Reeves.*, 929 F.2d 103, 108 (2nd Cir. 1991) ("It is clear beyond cavil that in the insurance context the attorney owes his allegiance, not to the insurance company that retained him but to the insured defendant."); *Point Pleasant Canoe Rental Inc. v. Tinicum Tp.*, 110 F.R.D. 166, 170 (E.D. Pa. 1986) ("When conflicts-of-interest arise between an insurance carrier and its insured, the lawyer representing the insured must act exclusively on behalf of, and in the best interests of the insured."); *First American Carriers Inc. v. Kroger Co.*, 787 S.W.2d 669, 671 (1990) ("When a liability insurer retains a lawyer to defend an insured, the insured is considered the lawyer's client").

Identifying the client is especially important because of the potential conflicts of interests that can arise between the insurer and the policyholder. *In re Rules of Professional Conduct*, 2 P.3d 806, 813 (Mont. 2000) (stating the "stark reality [is] that the relationship between an insurer and insured is permeated with potential conflicts"). Further, in the insurer/policyholder context, rules pertaining to the duties of loyalty are particularly relevant. Included among such rules are those prohibiting an attorney from accepting compensation for representation by someone other than the client unless: 1) the client gives informed consent; 2) the third party does not interfere with the attorney's independence of professional judgment or with the client-attorney relationship; and 3) the information relating to the representation of the client is protected as required under Rule 1.6. Rule 1.8(f), Model Rules Prof. Conduct (2007); *In Re Rules of Professional Conduct*, 2 P.3d at 809.

Along the same lines, it is important that the attorney exercise independent professional judgment on behalf of his or her client and render candid advice. Rule 2.1, Model Rules Prof. Conduct (2007). An attorney's loyalty to his or her client cannot be compromised by allegiance to others or by the attorney's personal interests. *Smoot v. Lund*, 369 P.2d 933, 936 (Utah 1962). An attorney, further, cannot permit a person who recommends, employs, or pays the attorney to render legal service for another to direct or regulate the attorney's professional judgment in rendering such legal services. Rule 5.4(c), Model Rules Prof. Conduct (2007).

These principles notwithstanding, insurers may provide defense counsel with various litigation "guidelines" that test the loyalty, zeal, and independent judgment of such counsel. Further, insurers may insist upon policyholder acquiescence in such guidelines on the basis of policy "cooperation" clauses. Litigation guidelines, however, may impinge improperly upon applicable ethical rules, which are absolute, by attempting to impose restrictions upon the professional judgment of defense counsel. The guidelines may, for instance, purport to require defense counsel to obtain insurer approval of strategic litigation decisions, such as those concerning taking depositions, filing motions, retaining experts, staffing case initiatives, conducting research, and a host of other matters. Generally, an attorney may comply with such attempted restrictions only to the extent they do not interfere with the attorney's independent professional judgment in representing the policyholder. Ohio Bd. of Comm'rs on Grievances & Discipline, Op. 2000-3. As a practical matter, insurance defense counsel who accede to such guidelines, deferring to an insurer in regard to the exercise of professional judgment, "violate their duties under the Rules of Professional Conduct to exercise their independent judgment and to give their undivided loyalty to [policyholder]." In *Re Rules of Professional Conduct*, 2 P.3d at 816; Ohio Bd. of Comm'rs on Grievances & Discipline, Op. 2000-3.

Defense counsel, in short, owes an unqualified duty of loyalty to the policyholder and must at all times protect the policyholder's interests, without being compromised by an insurer's instructions. Such counsel may not make any agreement with an insurer or comply with any guidelines or instructions from an insurer that limit the effectiveness or scope of the attorney's representation or interfere with the attorney's duties under the rules of professional conduct. Correspondingly, cooperation clauses cannot force policyholders to consent to such ethical violations.

Impact on Privileged Communications

Insurers also may use the cooperation clause to test the limits of the attorney-client privilege between policyholders and their defense counsel. As discussed above, policyholders may have a duty to cooperate with their insurers, depending upon policy language and other circumstances, but there are limits to any such duty. These limits, perhaps, are most critical to identify and observe in the area of attorney-client privilege.

Ethical rules limit the extent to which an insurer may obtain information from defense counsel. As discussed above, when an insurer has reserved rights and/or partially denied a claim, defense counsel can function as counsel for the policyholder only. An attorney cannot reveal confidential information relating to the representation of a policyholder client unless the client gives informed consent or the disclosure is impliedly authorized in order to carry out the representation. Rule 1.6, Model Rules Prof. Conduct (2007). Absent such consent or authority, the attorney must maintain information provided by the policyholder client in confidence. *Id.* Correspondingly, an attorney is forbidden from using information relating to representation of a policyholder client to the disadvantage of the client, unless the client gives informed consent. Rule 1.8(b) Model Rules Prof. Conduct (2007).

The privilege analysis is complicated by the fact that, in some respects, an insurer is not a third party vis-à-vis its policyholder, such that the policyholder and insurer can share certain information within the penumbra of the privilege that exists as against underlying claimants, without risk of waiver. Such instances, however, are limited to those in which the insurer is defending the policyholder and the information being shared pertains solely to matters of the defense, as opposed to matters concerning any coverage dispute. In regard to the defense of the underlying claim, the policyholder and the insurer typically have a common interest, rather than an adverse one. *Northwood Nursing & Convalescent*, 161 F.R.D. 293, 296 (E.D. Pa. 1995). However, that common interest does not extend beyond the defense of the underlying claim. *Remington Arms Co. v. Liberty Mut. Ins. Co.*, 142 F.R.D. 408, 417 (D. Del 1992) ("[T]he cooperation clause here does not imply a duty to produce documents protected by the attorney-client privilege in a coverage dispute. [The insurer] does not seek these documents in order to cooperate on underlying litigation, but to succeed in [the] coverage dispute ...").

In *Bituminous Cas. Corp. v. Tonka Corp.*, 140 F.R.D. 381 (D. Minn. 1992), the insurer filed an action seeking a declaration that there was no coverage for an environmental claim, and it sought production, based on the policy's cooperation clause, of documents generated during the investigation and cleanup of the subject groundwater contamination. Specifically, the insurer contended that the requested documents necessarily would be discoverable in the coverage case because they contained information about how, when, where, and why the contamination occurred, all of which were relevant to coverage issues. *Id.* at 385. The court agreed that the documents would be relevant, but it "rejected the insurer's contention that the attorney-client privilege is unavailable" to the policyholder. *Id.* at 387. It also rejected the insurer's argument that the policyholder, by agreeing in the policy to "cooperate," thereby "forever contractually waived the attorney-client privilege." *Id.* at 386. The court held, rather, that a policyholder could protect as privileged confidential matters bearing on the coverage dispute. *Id.* at 387. Such principles similarly protect from discovery confidential documents sought by reinsurers in disputes with ceding, direct insurers. *North River Insurance Co. v. Philadelphia Reinsurance Corp.*, 797 F. Supp. 363, 369

(D.N.J. 1992).

Many courts have embraced the view of the *Bituminous* court. In *State v. Hydrite Chemical Co.*, 582 N.W.2d 411 (Wis.Ct.App. 1998), for instance, the policyholder filed a third-party action against its insurers, seeking defense of the underlying claim and indemnification for the damages. The insurers, on the basis of the cooperation clause, requested copies of confidential, privileged documents that the policyholder had withheld. The court in *Hydrite* found that the cooperation clause did not impose a duty to produce documents protected by the attorney-client privilege in a coverage dispute: "To hold that an insurance policy creates a contractual waiver of the attorney-client privilege, even when the insurance company later sues the insured contending the insured's claim is not covered by the policy, would completely eviscerate the attorney-client privilege." *Id.* at 421.

Similarly, in *Nationwide Mutual Fire Insurance Company v. Bournon*, 617 S.E. 2d 40, 47 (N.C. App. 2005), the court held that a policyholder and its defense counsel can have communications that are privileged vis-à-vis the insurer and that the attorney-client privilege protects communications that are not related to the defense of the underlying action, but, rather, are related to matters about which the insurer and the policyholder are adverse. The policyholder will always be adverse to the insurer in regard to a contested coverage issue. *Id.*; see also, *Eastern Air Lines, Inc. v. U.S. Aviation Underwriters, Inc.*, 716 So.2d 340, 343 (Fla. 3rd Dist.Ct.App. 1998) (stating that, in a coverage contest, the policyholder and insurer are adverse and the cooperation clause does not override the attorney-client privilege).

Essentially, courts have held that as long as the documents relating solely to the underlying claim are produced, then the duty to cooperate under the insurance policy has been fulfilled. Courts consistently have held, however, that policyholders need not produce documents or other communications concerning legal advice or other information transmitted with a reasonable expectation of confidentiality, such as communications between policyholders and their defense counsel relating to coverage disputes. *Gulf Ins. Co. v. Transatlantic Reinsurance Comp.*, 788 N.Y.S.2d 44, 46 (N.Y. 1st App. Div. 2004).

One type of confidential document merits specific mention — defense fee bills. Typically, if an insurer is paying for the defense of an action, a policyholder does not waive any attorney-client privilege that applies to such bills vis-à-vis the underlying claimants by sending the bills to the insurer. *In Re Rules of Professional Conduct*, 2 P.3d at 818-19. Waiver may arise, however, to the potentially severe prejudice of the policyholder, if the insurer sends the defense bills to an outside, third-party bill auditor. Accordingly, absent the policyholder client's consent, defense counsel typically is not permitted to provide detailed billing information at the insurer's request to an outside auditing company. *Id.* at 822; Ohio Bd. of Comm'rs on Grievances & Discipline, Op. 2000-2. Rather, the attorney is permitted to give detailed billing information to the insurer only if it will not adversely affect the interests of the policyholder. ABA Formal Ethics Op. 01-421 (2001). Accordingly, an attorney cannot agree to any guidelines an insurer attempts to impose that contemplate sending fee bills to an outside auditor without the policyholder's consent. *In Re Rules of Professional Conduct*, 2 P.3d at 816, 822; Ohio Bd. of Comm'rs on Grievances & Discipline, Op. 2000-2.

Conclusion

Cooperation clauses have long been common in liability insurance policies. Although it is important for both policyholder and insurer to review such clauses carefully to determine their precise, expressed scope, it also is important for the parties to recognize that ethical rules and decisional law may serve to limit the stated scope of any duty to cooperate. Being mindful and protective of any such limits, ultimately, is in the interest of both policyholder and insurer. Defense counsel is retained by the insurer to represent the policyholder, and it serves the interest of neither policyholder nor insurer to place such counsel in violation of any applicable rules of professional conduct. Similarly, it serves the interest of neither to cause a waiver of the attorney-client privilege between the policyholder and defense counsel, which waiver can lead to forced disclosure of confidential information to an underlying claimant. Neither a policyholder nor an insurer, each of which has an interest in successfully defending the claim against the policyholder, should have any interest in giving an underlying claimant the advantage of access to highly confidential, privileged information.

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