

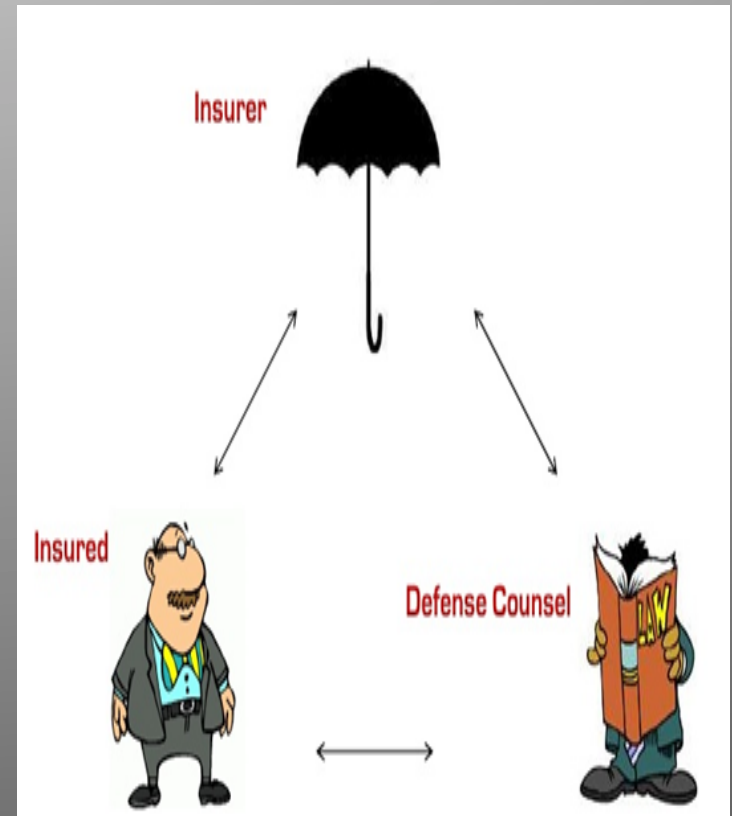


# ***The Ongoing Ethical Dilemma: Managing The Tri-Partite Relationship***

A Panel Discussion

# Overview

- Introduction to the Tri-Partite Relationship
- Insurance Defense Counsel Can and Must Serve Two Masters, But Only One is King
- Tensions, Problems and Conflicts in the Tri-Partite Relationship



# Tri-Partite Relationship Defined

- The Tri-Partite Relationship:  
The relationship among an insurer, its insured, and defense counsel retained by the insurer to defend the insured against third-party claims
- Although common, this relationship presents potential and actual problems that would “tax Socrates”
  - Hartford Acc. & Indem. Co. v. Foster, 538 So.2d 255 (Miss. 1988)



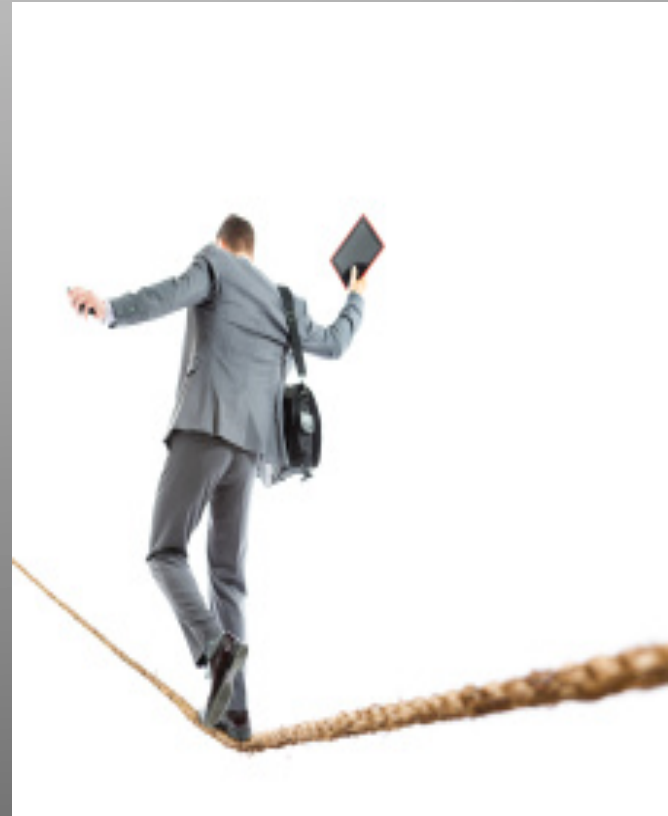
# Why Is It Important to Understand the Tri-Partite Relationship



- Preserve confidentiality and the attorney-client privilege
- Instill confidence in the insured as to the basis and nature of defense counsel's duties and loyalties
- Align interests of all and avoid disqualification of counsel
- Provide the best possible defense and achieve mutually beneficial outcomes for insured and insurer

# *History of the Tri-Partite Relationship*

- There Is A Potential For Tension Inherent in the Tri-Partite Relationship
- Defense counsel's representation of the insured and implied contractual obligation to simultaneously serve the interests of the insurer is a delicate balancing act



# The Tilley Doctrine



- Employers Cas. Co. v. Tilley, 496 S.W.2d 552 (Tex. 1973)
  - Texas Supreme Court held defense counsel who assisted insurer in developing evidence adverse to insured in insurer's separate declaratory judgment action to deny coverage acted improperly.
  - Held: Defense counsel owes the insured "the same type of unqualified loyalty as if he had been originally employed by the insured." *Tilley*, 496 S.W.2d at 558

# “Dual” or “Single” Client Relationship?



Jurisdictional Split:

- Majority Rule: “Dual Client Relationship”
- Minority Rule: “Single Client Relationship”

# “Dual Client Relationship”

- Majority of jurisdictions (including NY, AZ and MA) hold that counsel retained by the insurer to represent its insured has two clients, both the insurer and insured, and owes duties of care, confidentiality, etc to both.
- See, e.g., McCourt Co., Inc. v. FPC Props., Inc., 434 N.E.2d 1234, 1235 (Mass. 1982); Tudor Ins., Co. v. McKenna Assocs., 2003 U.S. Dist. LEXIS 10853 (S.D.N.Y. June 25, 2003); Restatement of the Law Governing Lawyers §§ 26(1) & (215).





# “Single-Client Relationship”



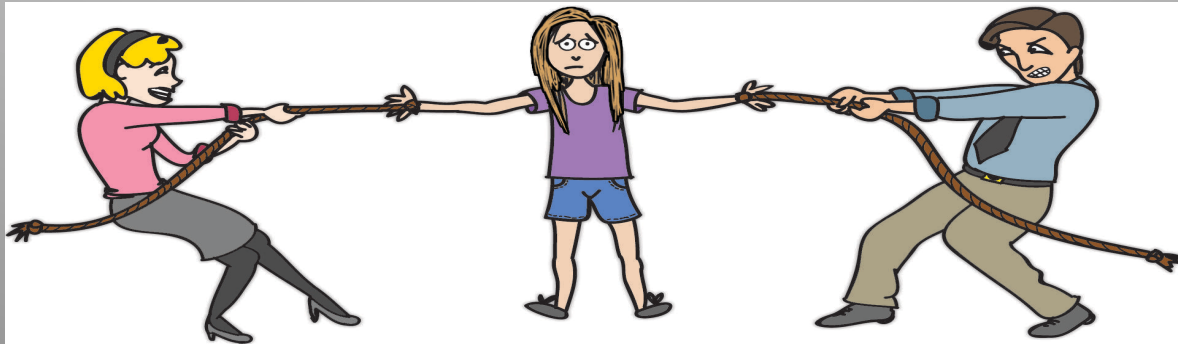
- A significant (and growing) minority of jurisdictions hold that counsel represents only the insured and that there is no tri-partite relationship.
  - The judicial trend in recent years increasingly moving towards this view
- “Single-Client Relationship” states include: Connecticut, Michigan, Montana, New Hampshire, Hawaii and Minnesota.

# Payment of Counsel's Fees Is Not Determinative



- In both “dual” and “single” client relationship jurisdictions, insurer’s payment of defense counsel’s fees does not impact the attorney’s duty of loyalty and obligation to zealously represent the insured.
- Defense counsel is always duty bound to represent the insured with undivided loyalty; that obligation is not diminished by counsel’s relationship with the insurer

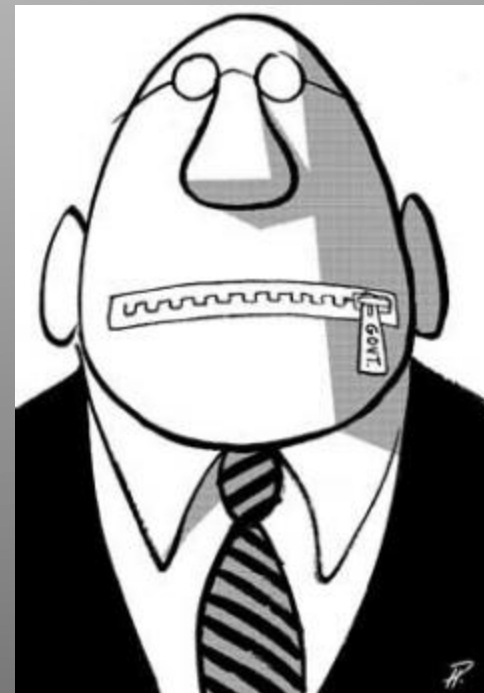
# *Issues Presenting Potential Sources of Tension Arising in the Tri-Partite Relationship*



- **Counsel Learns of Adverse Coverage Information**
  - Reservation of Rights
- **Counsel Acts Unduly Beholden to One or the Other**
- **Insured Not Fully Cooperating In Its Own Defense**
- **Directly Conflicting Interests of Insured and Insurer**
  - Potential For an Excess Judgment
  - Punitive Damages
  - Other

# Counsel Learns of Adverse Coverage Information

- Defense counsel has a duty not to disclose adverse coverage information to the insurer
  - i.e., Insured's late notice of claim, intentional conduct giving rise to claims, or of misrepresentation of facts on insurance application
  - See Liability Ins. Co. v. Superior Ct., 38 Cal. App. 3d 579, 592 (1974); Employer's Casualty Co. v. Tilley, 496 S.2d 552 (Texas 1973).



# Counsel Acts Unduly Beholden to One or the Other

- Defense counsel must act in a manner consistent with professional and contractual duties to both the insurer and the insured
  - Counsel must manage perceptions and maintain confidence of both
  - Insureds can be skeptical where carrier requires use of panel counsel



# Insured's Duty to Cooperate



Insured has a duty to cooperate fully and vigorously in its own defense even when the insurer has taken an adverse coverage position.

See Waste Management, Inc. v. International Surplus Lines Ins. Co., 144 Ill.2d 178 (1991).

# Conflicting Interests of Insured and Insurer



- If insurer's and insured's interests diverge, defense counsel will confront a conflict and may have to withdraw if unable to reconcile the divergent interests and obtain informed consent
  - ABA Model Rules of Professional Conduct for Lawyers, Rule 1.7
  - Where a true conflict exists, insurer typically must offer independent counsel to the insured
  - Insured always has the right to decline coverage and obtain its own independent counsel outside of the policy

# Potential Sources of Conflict

- Potential Excess Judgment:
  - Where the claimed damages exceed coverage, defense counsel must advise insured
    - See R.D. Wegman Constr. Co. v. Admiral Ins. Co., 629 F.3d 724 (7<sup>th</sup> Cir. 2011).
  - Situation ordinarily does not require appointment of independent counsel
    - See, e.g., Allstate Ins. Co. v. Campbell, 334 MD. 381 (Md. App. 1994).
  - Settlement demand within policy limits often brings this issue to a head
- Punitive Damages:
  - Many policies exclude coverage for punitive damages
  - Jurisdictions are split as to whether a punitive damages claim creates a conflict



## *Potential Sources of Conflict – Cont'd*

- Insurer Attempts to Limit the Cost of Defense
  - Right to control the defense is usually allocated to the insurer under the policy, but insurers must exercise care and good faith, and must not impede defense counsel's exercise of independent professional judgment
  - Tension arises where insurer does not authorize defense measures recommended by defense counsel, or refuses to pay for defense work during pendency of the lawsuit
  - Defense counsel has a duty to protect the interests of the insured at all times, especially if those interests would be compromised by insurer's instructions in managing the litigation

# *Potential Sources of Conflict – Cont'd*

- Insurer and Insured disagree over whether to settle
  - Under Model Rule 1.2 of the Rules of Professional Conduct for Lawyers, the client (i.e., the insured) has ultimate authority concerning decisions to settle
  - Many insurance policies, however, give the carrier the right to settle claims within the policy limits
    - Under such policies, the insurer is contractually authorized to settle the claim even over the insured's objection
      - See Caplan v. Fellheimer Eichman Braverman & Kaskey, 68, F.3d 828 (3<sup>rd</sup> Cir. 1985).

## *Potential Sources of Conflict – Cont'd*

- Insurer provides a defense to insured under a reservation of rights (ROR) letter giving notice that insurer reserves the right to deny coverage at a later date
  - In a majority of jurisdictions (including NH, NJ, and CA), an ROR does not automatically require appointment of independent counsel
  - A minority of jurisdictions (including MO, FL, and LA), hold that an ROR automatically gives the insured a right to independent counsel

# QUESTIONS