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NEW YORK APPELLATE COURT RULES THAT INSURERS MAY NOT INVOKE COMMON INTEREST PRIVILEGE PRIOR TO DENIAL OF CLAIM

A New York appellate court recently struck a significant blow against a common practice employed by many insurers: attempting to withhold attorney-generated claim investigation documents from discovery in subsequent coverage litigation. In *National Union Fire Insurance Co. of Pittsburgh, Pa. v. TransCanada Energy USA, Inc.*, Nos. 650515/10, 400759/11, slip op. at 69 (1st Dept. Feb. 25, 2014) ("*TransCanada*"), the Appellate Division in Manhattan upheld a lower-court order rejecting the insurers' claims of attorney-client privilege and compelling production of a broad swath of documents generated by outside counsel involved in the insurers' pre-denial claim investigation.

Of particular significance, the *TransCanada* court ruled that insurers cannot rely upon a "common interest," or joint defense, privilege to shield from disclosure any attorney-generated investigation documents shared among them before their actual denial of the policyholder's claim. The court reaffirmed the established rule in New York that, for purposes of privilege or work product protection, an insurer cannot "anticipate litigation" before making the business decision whether to pay or deny the claim. *See Brooklyn Union Gas Co. v. Am. Home Assur. Co.,* 23 A.D.3d 190, 190-91 (1st Dep't 2005). Further, because the common interest privilege applies only when litigation is reasonably anticipated, insurers have no common legal interest, and may not invoke that privilege, before they have made a firm decision to deny coverage. *See TransCanada*, slip. op. at 69.

The claim in *TransCanada* arose in 2008 from the failure of a generator turbine in Queens, New York. TransCanada's primary and excess insurers jointly hired outside counsel to assist with an extensive claim investigation and advise the insurers on coverage. In litigation following their 2010 denial of the claim, the insurers objected to production of a wide variety of documents, including communications shared among the insurers and their joint counsel, on the grounds that they contained attorney-client privileged legal advice and were protected from disclosure under the common interest doctrine.

In New York, as in many other jurisdictions, an insurer's investigation and determination as to whether to pay or deny a claim is part of the insurer's ordinary-course business activities. *See Melworm v. Encompass Indem. Co.*, 112 A.D.3d 794, 794 (2d Dep't 2013). Consequently, documents generated by attorneys that "aid [an insurer] in the process of deciding which of the two indicated actions to pursue" are not privileged, unless they are "primarily and predominantly of a legal character." *Id.*; *see also Bertalo's Restaurant Inc. v. Exchange Ins. Co.*, 240 A.D.2d 452, 454-55 (2d Dep't 1997).

After reviewing the documents *in camera*, the lower court in *TransCanada* rejected the insurers' contentions, finding that outside counsel were coordinating the investigation and were involved in core investigative activities, such as collecting documents and hiring expert consultants to evaluate the claim. The court held that the claim investigation was ordinary-course claims adjustment rather than legal work, and that the vast majority of attorney-generated documents therefore did not constitute legal advice. Moreover, the insurers lacked a common legal interest during the investigation and consequently waived any claim to privilege by freely sharing the documents among

themselves. In the context of coverage, "insurance companies must decide to deny coverage before they may invoke the common interest privilege and protect their communications with third parties from disclosure." *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. TransCanada Energy USA, Inc.*, Nos. 650515/10, 400759/11, Dkt. Nos. 226, 409 at 9 (Sup. Ct. N.Y. Cty., Aug. 15, 2013).

On appeal, the First Department affirmed in a brief opinion. The court reiterated the rule that coverage determinations are part of an insurer's ordinary course of business, and held that in this case "the insurance companies retained counsel to provide a coverage opinion, i.e. an opinion as to whether the insurance companies should pay or deny the claims." *TransCanada*, slip. op. at 68. Documents generated for that purpose in the context of a claim investigation do not become privileged "'merely because [the] investigation was conducted by an attorney.'" *Id.* at 68-69 (quoting *Brooklyn Union Gas*, 23 A.D.3d at 191).

Further, the First Department held that the common interest exception to waiver of the attorney-client privilege by disclosure was not applicable, "since there was no pending or reasonably anticipated litigation in which the insurance companies had a common legal interest." *Id.* at 69. Thus, the insurers remained third parties to each other even though they had jointly retained counsel to assist with the claim investigation, and documents shared among them were not privileged.

The *TransCanada* decision should bolster policyholders' efforts in litigation to obtain the claim-investigation documents needed to probe the true basis for insurers' disputed claim determinations. *TransCanada* holds that, in addition to factual reports and analysis, even "coverage opinions" provided by attorneys participating in an insurer's claim investigation do not constitute privileged legal advice. Rather, they are part and parcel of the insurer's regular business activity of deciding whether to pay or deny claims.

Moreover, where multiple insurers outsource a claim investigation to jointly-retained counsel, the unavailability of a "common interest" privilege suggests that any pre-denial communications shared among those insurers during the investigation will be subject to discovery. In this respect as well, *TransCanada* provides insureds with a potentially powerful lever for prying open the "black box" of insurer decision-making once litigation has ensued.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our insurance practice group:

P. Benjamin Duke	+1.212.841.1072	pbduke@cov.com
Jennifer Farina	+1.212.841.1140	jfarina@cov.com