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IN THE SUPREME COURT OF FLORIDA

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MAY 27 1998
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Chief Deputy Clerk

UNITED SERVICES AUTOMOBILE ASSOCIATION, a Reciprocal Interinsurance Exchange,

Petitioner,

v.

DALE E. JENNINGS, JR., and TAMMY M. JENNINGS,

Respondents.
_____/

CASE NO. 92,776

Petition from the District Court of Appeal, First District - No. 97-2668

AMICUS CURIAE STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY'S INITIAL BRIEF ON THE MERITS

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PRELIMINARY STATEMENT

Petitioner, United Services Automobile Association, will hereafter be referred to as "USAA". Petitioner USAA's insured, Broxton, will hereafter be referred to as "Broxton." Respondent, Dale E. Jennings, Jr., will hereafter be referred to as "Jennings." Amicus Curiae State Farm Mutual Automobile Insurance Company will hereafter be referred to as "State Farm."

References to the appendix will be designated A. followed by the appendix document number. i.e., (A1).

STATEMENT OF CASE AND OF FACTS

State Farm hereby adopts the Statement of Case and of Facts contained within USAA's Initial Brief on the Merits.

SUMMARY OF ARGUMENT

Before Cunningham, issues relating to bad-faith arose for the first time only after an insured was subjected to a judgment in excess of liability limits. Traditionally, an insurer was entitled to invoke the attorney-client privilege only after it reached an adversarial position to its insured because of such an excess judgment. Since this Court's holding in Cunningham, when an insurer is asked to consider entering into a tri-partite "Cunningham Agreement", issues of bad-faith are prematurely injected into the otherwise fiduciary relationship between the insurer and the insured. In determining whether to enter into such an agreement, the insurer has its own interest, distinct from its insured, for which it should be entitled to seek the advice of counsel. As such, to the extent USAA's claim file contains communications to and from its own separate counsel concerning the threatened bad-faith suit and the "Cunningham Agreement", such communications should be protected by the attorney-client privilege. To hold otherwise would undercut "Cunningham Agreements" and the statutory right of insurers to seek the advice of counsel on non-fiduciary issues.

ARGUMENT

I. WHETHER AN INSURER MAY SEEK AND OBTAIN ADVICE AND SERVICES OF ITS OWN SEPARATE COUNSEL IN ANTICIPATION OF A THREATENED BAD-FAITH CLAIM, AND IN PARTICULAR TO ASSIST IN THE DECISION AS TO WHETHER AND ON WHAT TERMS TO ENTER INTO A "CUNNINGHAM AGREEMENT", WITHOUT FEAR THAT THEREAFTER SUCH COMMUNICATIONS WILL BE SUBJECTED TO DISCOVERY IN THE BAD-FAITH SUIT.

The District Court of Appeal, First District, State of Florida, certified to this Court the following question as being one of great public importance:

> WHETHER THE FACT THAT A THIRD PARTY BAD-FAITH CLAIM HAS BEEN BROUGHT PURSUANT TO A CUNNINGHAM STIPULATION RATHER THAN AN EXCESS JUDGMENT MAKES ANY DIFFERENCE WHEN ATTORNEY-CLIENT AND WORK PRODUCT PRIVILEGES ARE ASSERTED DURING DISCOVERY IN THE BAD-FAITH ACTION AS TO MATERIAL CONTAINED IN THE CLAIMS FILE.

In the proceedings below, USAA addressed issues as to the applicability and/or waiver of both attorney-client and work

product privileges, both as they might be enjoyed by its insured, Broxton, and separately by itself. As set forth in State Farm's Motion to Appear as Amicus Curiae, State Farm supports in its entirety the position of USAA. However, State Farm requested amicus status to address a more narrow issue encompassed within the District Court's certified question:

> Whether, when faced with a threatened bad-faith claim and the question of whether to enter into a "Cunningham Agreement," insurers have the right to obtain attorney advice from separate counsel, not otherwise involved in the defense of the insured, and thereafter protect such communications from discovery in a third party bad-faith action to the same extent as any other litigant.

In the instant case, the three parties: USAA's insured, Broxton; the injured parties, the Jennings; and USAA, the liability insurer, each chose to enter into a stipulation and agreement of a type authorized by this Court in Cunningham v. Standard Guaranty Ins. Co., 630 So. 2d 179 (Fla. 1994). (A.3) This agreement gave the Jennings the right to file a lawsuit against USAA for bad-faith failure to settle their claims against Broxton without first obtaining an excess judgment in favor of Jennings and against Broxton. State Farm contends that when presented with such circumstances an insurer must be

entitled to seek the advice of separate counsel on issues pertinent to the threatened bad-faith claim and the proposed stipulation such as whether to enter into such an agreement and to advise the insurer regarding the terms of such an agreement without subjecting such communications to discovery in the later third party bad-faith action.

Protecting the attorney-client privilege of insurers who seek advice as to whether to enter into a "Cunningham Agreement" furthers the public policies inherent in the attorney-client privilege as well as the public policy in allowing "Cunningham Agreements". Irrespective of how this Court rules on whether the USAA file is subject to production in general, this Court should recognize USAA's right to protect from production any privileged communications and documents concerning issues pertinent to the threatened bad-faith claim and the advisability of entering into "Cunningham Agreements."

A. Insurers are Entitled to the Protections of the Attorney-Client Privilege.

This Court has already established that corporations, such an insurers, have the right to seek advice of counsel and to invoke the attorney-client privilege to protect resulting

communications. See Southern Bell Telephone & Telegraph Co. v. Deason, 632 So. 2d 1377, 1380 (1994). A corporation's right to seek such counsel is statutorily protected in Section 90.502, Florida Statutes (1997). Section 90.502, Florida Statutes (1997) provides that a client, which may be a corporation, has:

> [A] privilege to refuse to disclose, and to prevent any other person from disclosing, the contents of confidential communications when such other person learned of the communications because they were made in the rendition of legal services to the client.

The attorney-client privilege serves to protect the public interest by furthering frank and full communication between clients and their attorneys thereby furthering a broader public interest in the observance of law and administration of justice. Upjohn Co. v. United States, 449 U.S. 383, 389 (1981). The attorney-client privilege is absolute and is not subject to a "good cause" exception. See National Security Fire & Casualty Co. v. Dunn, 705 So. 2d 605, 608 (Fla. 5th DCA 1997); United Services Auto Ass'n v. Crews, 614 So. 2d 1213, 1214 (Fla. 4th DCA 1993); Staton v. Allied Chain Link Fence Co., 418 So. 2d 404 (Fla. 2d DCA 1982).[1]

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[1]The attorney-client privilege protects communications to and from, and documents prepared by and for, in-house counsel as well as outside counsel. See, e.g., Shell Oil Co. v. Par Four Partnership, 638 So. 2d 1050, 1050 (Fla. 5th DCA 1994); Southern

Except where an insurance company is acting as a fiduciary of its insured, it is entitled to this privilege to the same extent as any other litigant. Manhattan Nat'l Life Ins. Co. v. Kujawa, 522 So. 2d 1078, 1080 (Fla. 4th DCA 1988), approved, 541 So. 2d 1168 (Fla. 1989).

B. "Cunningham Agreements" Insert Issues of Bad-Faith Prior to Entry of an Excess Judgment

In contrast to an indemnity policy, in modern liability insurance policies, the insurance company is contractually afforded both the right and the duty to defend liability claims brought against its insured. State Farm Mutual Automobile Ins. Co. v. LaForet, 658 So. 2d 55, 58 (Fla. 1995). Indeed, it is this contractual right to control the defense and make decisions regarding the litigation of disputed claims that is the very underpinning of a third party bad-faith cause of action. Id.; Boston Old Colony Ins. Co. v. Gutierrez, 386 So. 2d 783, 785 (Fla. 1980); Baxter v. Royal Indemnity Co., 285 So. 2d 652, 656 (Fla 1st DCA 1973).

The actions of an insurance company in the defense of claims asserted against its insured are taken for both the

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Bell, 632 So. 2d at 1386; Manhattan Nat'l Life Ins. Co. v. Kujawa, 522 So. 2d 1078, 1079 (4th DCA 1988), approved, 541 So. 2d 1168 (Fla. 1989).

benefit of the insurer and the insured, and it is this dual role that has been cited by the courts as the basis for holding the insurance company to the standard of a fiduciary. Stone v. Travelers Ins. Co., 326 So. 2d 241, 243 (Fla. 3d DCA 1976); Boston Old Colony Ins. Co. v. Gutierrez, 325 So. 2d 416, 417 (Fla. 3d DCA 1976). Because the insurer is acting not just for itself, but also as a fiduciary for its insured, a third party claimant (who stands in the shoes of the insured in a bad-faith claim) has consistently been held to be entitled to discovery of the insurer's file up to the time of the entry of judgment against the insured. See, e.g., Dunn v. National Security Fire & Casualty Co., 631 So. 2d 1103, 1109 (Fla. 5th DCA 1993). Continental Casualty Co. v. Aqua Jet Filter System Inc., 620 So. 2d 1141, 1142 (Fla. 3d DCA 1993). Discovery of file materials post-judgment, however, has consistently been held to be subject to attorney-client privilege considerations, because on the issues presented post-judgment, i.e., bad-faith, the insurance company is no longer acting as a fiduciary, but rather at that point is clearly in a position adverse to the insured. See Dunn, 631 So. 2d at 1109; Continental, 620 So. 2d at 1141.

In Cunningham, this Court was asked to consider circumstances in which the three parties to an underlying tort claim/bad-faith claim had each agreed to waive their

respective and discreet interests in the requirement for a final judgment before a third party bad-faith claim. Cunningham, 630 So. 2d at 180. The three parties had entered into a stipulation to waive the requirement for an excess judgment and try the bad-faith claim first.[2] In Cunningham, this court ruled for the first time that a court may determine an insurer's liability for bad-faith handling of a liability claim prior to a final determination in the underlying tort action where the insurer, the insured party, and the insured, each agree to proceeding in this fashion. Id. at 182. This Court acknowledged that a third party bad-faith action arises only after an insured is exposed to an excess judgment. Id. at 181; see also Fidelity & Casualty Co. of New York v. Cope, 462 So. 2d 459, 460 (Fla. 1985); Thompson v. Commercial Union Ins. Co. of New York, 250 So. 2d 259, 264 (Fla. 1971). In the agreement in Cunningham, the insurer waived this excess judgment requirement, and this Court held that the insurer could do so. Cunningham, 630 So. 2d at 181. This court went on to state that:

> This Court has looked with favor upon stipulations designed to simplify, shorten, or settle litigation and save cost to parties. Such stipulation should

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[2]In Cunningham, all three parties also agreed that if the insurer was found not to have acted in bad-faith, the injured party's claim against the insured would be settled for the policy limit. Id. at 180.

> be entered and enforced if entered into with good faith and not obtained by fraud, misrepresentation, or mistake, and not against public policy. In an arrangement such as the one in the instant case, trying the bad-faith claim, before the underlying negligence action would result in a full release of the insured if no bad-faith were found, thereby avoiding a time consuming and expensive trial on negligence and damages. We see no reason why the stipulation should not have been recognized.

Id. at 182 (citations omitted).

Prior to the Cunningham decision, courts had held that in a third party bad-faith action, the claims file of the insurer was subject to discovery up to the point an excess judgment was entered against the insured. Dunn, 631 So. 2d at 1109; Continental Casualty, 620 So. 2d at 1142; General Accident Fire & Life Ins. Corp. Ltd. v. Boudreau, 658 So. 2d 1006, 1006 (Fla. 5th DCA 1994). The rationale behind this "bright line" is clear: before entry of the judgment, and while the issues presented were exclusively those related to the claim against the insured, the insurer owed a fiduciary obligation to its insured. After the judgment, the insurer's fiduciary obligation ended and on the issues presented in a bad-faith claim, the interests of the insured and insurer are adverse. Before Cunningham, a judgment provided a clear demarcation of when the insured's fiduciary duty to its insured ended and the two became adversaries. The insurer's file was therefore subject to discovery in third party bad-faith actions up to the date of the judgment but was not subject to discovery to

the extent of applicable privileges after the date of judgment.

With this court's approval of "Cunningham Agreements," issues of "bad faith" for liability insurers now have the potential to arise prior to the entry of an excess judgment. The insurer, while simultaneously acting in furtherance of its fiduciary obligations to its insured, is prematurely confronted with issues relating to alleged bad-faith as to which its interests are by definition adverse to its insured. The insurer must decide whether it is in its interest to enter into a "Cunningham Agreement" and, if so, under what terms. By entering into a "Cunningham Agreement," the insurer is waiving its contractual right to resolve by jury the issues presented in the underlying liability suit against its insured. Like any other litigant, an insurer's right to seek counsel on these non-fiduciary issues should be protected.

By definition, consideration of the issues involved in a threatened bad-faith claim and the possibility of entering into a "Cunningham Agreement," as to which the interests of the insurer and the interests of the insured are potentially adverse, will arise only prior to judgment against the insured. This Court has forcefully stated the potential benefits that might be obtained if the parties choose to enter into such a stipulation. To the extent that any potential

party to such an agreement is precluded from seeking the advice and counsel of an attorney for fear that such communication would later be the subject of disclosure through discovery, the rationale of the court in approving such agreements is frustrated. As Judge Farmer recognized in his concurring opinion in United Services, 614 So. 2d at 1215, an attorney-client privilege should be recognized for "those discrete communications occurring between the carrier and counsel specifically asked to assess the case from a bad-faith standpoint."

In other factual situations, the courts have recognized that fiduciaries may have a dual interest. In Barnett Banks Trust Co., N.A. v. Compson, 629 So. 2d 849, 851 (Fla. 2d DCA 1993), the court recognized that a fiduciary, in that case a trustee, has the right to maintain the privacy of privileged communications between itself and counsel. In Barnett, the beneficiary sued the trustee and sought to discover documents the trustee considered privileged by arguing that the trustee had a fiduciary obligation to her to disclose all affairs of the trust and, therefore, no privilege could exist. While recognizing the trustee's fiduciary duties to the beneficiaries, the court noted that as to the communications at issue, the client was the trustee seeking advice on a

matter in which the beneficiary's interest was adversarial. The trustee's privilege was upheld.

Other states have also upheld the right of a fiduciary to seek advice of counsel and to protect such communications from further discovery. For example, in Huie v. DeShazo, 922 S.W.2d 920, 923 (Tex. 1996), the Supreme Court of Texas upheld the fiduciary's right to assert the attorney-client privilege where the fiduciary was seeking advice of counsel. The Court reasoned that:

> The attorney-client privilege serves the same important purpose in the trustee-attorney relationship as it does in other attorney-client relationships. A trustee must be able to consult freely with his or her attorney to obtain the best possible legal guidance. Without the privilege, trustees might be inclined to forsake legal advice, thus adversely affecting the trust, as disappointed fiduciaries can later pour over the attorney-client communications and second-guess the trustee's actions. Alternatively, trustees might feel compelled to blindly follow counsel's advice, ignoring their own judgment and experience.

Huie, 922 S.W.2d at 924. Likewise, in Beck v. Manufacturers Hanover Trust Co., 632 N.Y.S.2d 520, 530 (N.Y. App. Div. 1995), the court held that where a trustee consults counsel to defend itself against conflicting claims of its beneficiaries, such communications will be protected under the attorney-client privilege.

In short, the fact that USAA has fiduciary obligations to the insured does not vitiate USAA's rights to seek advice of counsel on issues as to which its interests and the interest of its insured are potentially adverse. This Court should uphold USAA's right to seek advice concerning a potential "Cunningham Agreement" in the face of a threatened bad-faith claim.

C. Kujawa Dictates that "Cunningham" Attorney-Client Communications be Immune from Discovery.

Because the insurer who seeks advice from separate counsel concerning "Cunningham Agreements" is seeking advice as to its own non-fiduciary interest, this Court's decision in Kujawa mandates reversal of the District Court's decision. In Manhattan v. Kujawa, 522 So. 2d at 1079, the insurer argued that its legal department file was protected from production in a first party statutory bad-faith case due to the attorney-client privilege. The Fourth District Court of Appeal recognized that courts have allowed production of claim files, but held that:

> an insurer which is not in a fiduciary relationship to its insured and against which a cause of action is brought under section 624.155 is entitled to protection against production of its legal department file (and its claim file by whatever

> name) on the basis of both work product immunity and attorney-client privilege to the same extent as any other litigant.

Id. at 1080.

This Court approved the Fourth District Court of Appeal's decision, reasoning that where the issues that exist between the parties are adversarial and not fiduciary, the attorney-client privilege and work product immunity will not be abrogated, even in a bad-faith claim. Kujawa v. Manhattan National Life Ins. Co., 541 So. 2d 1168, 1169 (Fla. 1989).

While Kujawa involved a first party bad-faith claim, the analysis is applicable in the instant case. Pursuant to Kujawa, privileges are recognized, even in bad-faith suits, where an adversarial relationship exists as to the issue which is the subject of the communication. If a bad-faith claim is threatened and a "Cunningham Agreement" is being considered, an insurer is not acting in its fiduciary capacity when it seeks advice of separate counsel as to whether to enter into a such an agreement and, if so, on what terms. The rule established in Kujawa applies with equal force to such circumstances, and the insurer's privileges should be recognized. If the insurer's file at issue in the instant case contains communications with and documents to and from counsel hired to advise USAA on issues relevant to the bad-faith claim and whether to enter into the "Cunningham

Agreement", issues which only arise at that time because of the holding in Cunningham, any such communications are protected under the attorney-client privilege immunity as applied in Kujawa.

If this Court agrees with USAA's position and holds that the entire file is protected by the attorney-client privilege and work product immunity absent a provision to the contrary in the stipulation, any documents and communications to and from USAA to counsel relating to the "Cunningham Agreement" will fall under the umbrella of this protection. State Farm supports this position. Even if this Court disagrees and instead approves in general the holding of the District Court below, on the more narrow issue, this Court should recognize that insurers have a right to seek the advice of counsel concerning threatened bad-faith claims and proposed "Cunningham Agreements."

In the instant case, USAA had fiduciary obligations to the insured, but because of Cunningham, was prematurely called upon to address non-fiduciary issues for which it may have sought advice of counsel. Any such advice and communications must be protected from discovery. An in-camera inspection of the insurer's file by the Trial Court is necessary to ensure that the privacy of such privileged documents is respected. See National Security, 705 So. 2d at 608; United Services, 614

So. 2d at 1213; Allstate Ins. Co., Inc. v. Walker, 583 So. 2d 356, 358 (Fla 4th DCA 1991). Accordingly, if this Court generally agrees with the opinion of the District Court below, on this more narrow issue, this Court should reverse and remand this case to the Trial Court for an in-camera inspection of the file. To the extent that the file contains advice and communications to and from USAA's separate counsel as to the threatened bad-faith claim and the "Cunningham Agreement," such communications and documents should be shielded from discovery. As the Fourth District Court of Appeal stated in Manhattan v. Kujawa, 522 So. 2d at 1080 (citations omitted):

> Whether all or a portion of the matter sought to be discovered is protected by work product immunity, or by the attorney-client privilege, and, if protected by work product immunity but not the attorney-client privilege, whether the appropriate showing under rule 1.280(b)(2), Florida Rules of Civil Procedure, can be made, are matters which remain for the trial court's determination.

CONCLUSION

State Farm supports the position of USAA and respectfully requests that this Court reverse the District Court of Appeal's ruling. In the alternative, on the more narrow issue discussed above, State Farm requests that this Court reverse and remand this case to the Trial Court for an in-camera inspection of the documents at issue to determine whether the file contains communications and documents to and from separate counsel advising USAA as to the threatened bad-faith claim and the "Cunningham Agreement." If so, the Trial Court should be instructed to protect such privileged communications and documents from disclosure.

Respectfully Submitted,

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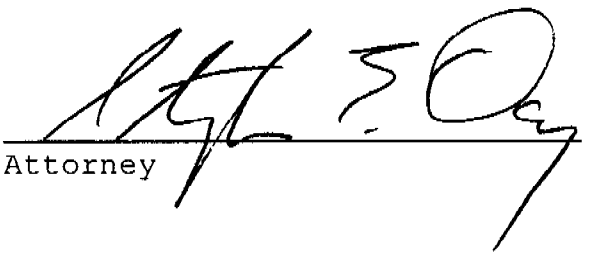
CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a copy of the foregoing Amicus Curiae State Farm Mutual Automobile Insurance Company's Initial Brief on the Merits has been furnished to **Robert C. Gobelman, Esquire**, counsel for Petitioner, 200 West Forsyth Street, Suite 1700, Jacksonville, Florida 32202, **Thomas S. Edwards, Esquire**, counsel for Respondent, 1301 Riverplace Blvd., Suite 1609, Jacksonville, Florida 32207, and to **Tracy Raffles Gunn, Esquire**, counsel for amicus curiae Florida Defense Lawyers Association, P. O. Box 1438, Tampa, Florida 33601, by U.S. Mail, this 26th day of May, 1998.



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