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Insurance Bad Faith

Breaking Down Privileges: Discovery Of The Claim File In Florida Bad-Faith Actions

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Commentary

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I. The Claim File In Context

Insurance bad-faith actions generally arise from the alleged mishandling of a claim for benefits under a policy. In the typical bad-faith action, the claim has failed to settle, leading to damages incurred by the insured. In order to determine whether the insurance carrier violated its duties of good faith and fair dealing, the finder of fact will be asked to examine the manner in which the claim was handled and determine whether it was handled in good faith or bad.

The best evidence of the manner in which the claim was handled is often the insurance company's claim file itself. Ordinarily, insurers enjoy protections of privilege over the contents of their claim files.[1] This privilege, however, is designed to protect the strategies and thought processes of the insurer during litigation of the claim for benefits under the policy (or, in the case of liability insurance, during the litigation of the liability claim against the insured). Once that case has concluded, and a subsequent suit for bad faith is filed, the necessity for maintaining those privileges is drawn into question. And when the issue being litigated in the bad-faith claim is the manner in which the insurance carrier has handled the claim, most courts hold that the privileges once applicable to the claim file can be overcome and the claim file documents are subject to production.

II. What Constitutes The Claim File

In recent years, many insurers have embraced modern technology and now maintain all of the pertinent "documents" relating to a claim electronically. This includes electronic log notes, e-mail and scanned images of paper documents. The concept of a "claim file," then, is no longer a physical folder kept in a filing cabinet in a claims office. It is instead an aggregation of bits of data associated together under a common claim number. Requests to produce the "claim file," then, require a certain level of interpretation by the insurance carrier defendant. Usually, this means producing all of the relevant records pertinent to the underlying claim in electronic or paper form.

Difficulties can arise where certain documents ordinarily not considered part of the claim file are nevertheless associated with the underlying claim number. For example, if an allegation is made by a plaintiff's attorney that the carrier has acted in bad faith during the pendency of the underlying action, the claims personnel may evaluate the claim handling in anticipation of the bad-faith claim or even retain company counsel to provide advice as to how to respond to those allegations. When these documents are commingled with the underlying claim-file documents, questions arise during the litigation of the bad-faith claim over whether those documents (which relate to strategies and impressions concerning the bad-faith case, not the underlying case) are discoverable.

III. The Privileges — Work Product And Attorney/Client

There are two legal privileges at work in protecting the claim file from discovery. The first is work product, which is generally defined as a party's mental impressions and strategies prepared in anticipation of litigation. This privilege is limited, however, and can be overcome with a showing of necessity and an inability to obtain the information elsewhere.[2] During the pendency of the underlying claim, the privilege remains intact because there is no need for the claimant to discover the insurer's thoughts, impressions or strategies in defending the case. That is because the manner in which the claim is defended is not relevant to the underlying claim itself. Once that claim is concluded, however, and the bad-faith claim begins, the manner in which the claim was defended is now the issue before the court. Suddenly, there is a need to discover those materials. And because the claim file is usually the only reliable source of evidence as to how the claim was handled, the work product privilege can be (and usually is) overcome.[3]

The attorney-client privilege is treated completely differently. It is one of the most ancient privileges recognized by the common law. A client must be able to speak freely with his attorney in order to receive sound legal advice, and the best way to insure free and honest communication is to guarantee that the contents of it will never be subject to later revelation.[4] Thus, the attorney-client privilege is often considered "inviolate" and, absent a waiver, will not be discoverable even if the contents of the communication are relevant or the opposing party is unable to find the information elsewhere.

IV. Attorney/Client Privileges — Which Attorney And Which Client?

In 2005, the Florida Supreme Court issued a sweeping decision, the primary holding of which was to apply the discovery standards of third-party bad faith cases to first-party bad faith cases. *Allstate Indemnity Co. v. Ruiz*.[5] As a result, work product which was previously protected in first-party bad-faith cases became discoverable. In issuing its ruling, the Court quoted a lower-level appellate court which used the following broad language:

> In contrast, a case like this one is totally indistinguishable from the familiar "bad faith" failure to settle or defend a third-party's action against a liability carrier's insureds. In those cases, like this one, the pertinent issue is the manner in which the company has handled the suit including its consideration of the advice of counsel so as to discharge its mandated duty of good faith. Virtually the only source of information on these questions is the claim file itself. Accordingly . . . it has been consistently held in our state that a claim file is subject to production in such an action.[6]

Although *Ruiz* appears to be limited to work product, several federal courts have interpreted this broad language (particularly the reference to "consideration of the advice of counsel") to indicate that, in the bad faith litigation, even attorney-client communications are discoverable in the subsequent bad-faith suit.

For example, in *Nowak v. Lexington Insurance Co.*,[7] the federal judge found that the "sweeping language" of *Ruiz* constituted a "persuasive indication" that the Florida Supreme Court would find that the attorney-client privilege simply does not apply to insurance companies in bad-faith suits.[8] Specifically, the court stated: "While the [insurer] is correct that the Supreme Court in *Ruiz* did not address the precise issue, the Florida Supreme Court did use sweeping language to suggest that it would allow documents traditionally protected by the attorney-client privilege to be discoverable in bad faith litigation once the underlying coverage case was completed."[9] Other states have also found that the attorney-client privilege is inapplicable upon the institution of the subsequent bad-faith suit.[10]

Despite these decisions, the Florida appellate courts examining *Ruiz* have reached the opposite conclusion. In each case that has considered the issue, the intermediate courts have concluded that *Ruiz* did not abrogate the attorney-client privilege.[11] Indeed, most courts recognize that certain attorney-client communications are discoverable in the bad-faith case. Specifically, communications between the insured and the insured's retained counsel are usually discoverable.[12] This is because the insured, or the claimant with an assignment from the insured, is prosecuting the bad-faith action. Thus, the privilege is his and

cannot be used to shield communications between his attorney and the insurer. The *Scoma* decision noted, however, that when the bad-faith claim is brought by a claimant without an assignment (as is permissible under Florida law), the privilege still applies and the communications with retained counsel are not discoverable.

Notably, all of these decisions (including the federal cases discussed above) recognize that there is a line which will not be crossed in the production of attorney/client communications in a bad-faith claim. That is where the insurer consults with its *own* counsel and seeks advice concerning the very bad-faith claim being litigated, the privilege remains inviolate. The same is true with respect to work product. Beware, however, that if communications or work product concerning an anticipated bad-faith claim are commingled with materials in the underlying claim file, the bad-faith plaintiff will argue that those communications are discoverable as "part of the claim file."

V. Practical Considerations

Perhaps the single best method of protecting attorney-client and work product privileges where a bad faith claim is anticipated is to "split the file." The insurer should create a separate claim file, supervised by a separate adjuster, to handle analysis of any extracontractual allegations and seek advice from the company's bad-faith counsel. This way, when the request to produce "the claim file" arrives in the bad-faith case, all of the communications and work product concerning the bad-faith claim can safely be considered outside of that request. It would be a rare circumstance that a court would require an insurer to produce its own internal file and disclose its own attorney communications concerning the very bad-faith claim being litigated. Thus, whenever it appears that a bad-faith claim may arise, and the carrier seeks an opinion from counsel, such documents should be kept separately from the "claim file."

It should be remembered by every adjuster, however, that the remaining documents in the claim file are likely fair game for discovery in a subsequent bad-faith suit. Whether a bad-faith claim is won or lost is often dependent upon the quality of the record keeping in that file. It goes without saying that a claim file should be free of inappropriate commentary or off-color remarks. What is more important to realize, however, is that the claim file will be the "road map" to the bad-faith claim. The carrier's defense that it acted in good faith can only be demonstrated by a well-documented claim file, which can provide a judge or jury with an accurate picture of the good-faith claim handling undertaken in the defense of the company's insured. Clear, contemporaneous, thorough and accurate documentation can win a bad-faith claim years before the complaint is ever served.

Endnotes

1. *See* Am. States Ins. Co. v. Kransco, 641 So. 2d 175 (Fla. 5th DCA 1994); Utica Mut. Ins. Co. v. Croft, 432 So. 2d 196 (Fla. 1st DCA 1983).

2. *See* Fed. R. Civ. P. 26(b)(3)(A) (2009); Hickman v. Taylor, 329 U.S. 495, 67 S.Ct. 385, 91 L. Ed. 451 (1947).

3. *See* Joyner v. Continental Ins. Cos., 101 F.R.D. 414 (S.D.Ga.1983) (insurance statements prime candidates for determining what carrier knew); APL Corp. v. Aetna Casualty & Sur. Co., 91 F.R.D. 10, 14 (D.Md. 1980) (claim file "may constitute quite important evidence" as to whether insurance company acted in good faith); Handgards, Inc. v. Johnson & Johnson, 413 F.Supp. 926 (N.D.Cal.1976) (insured can demonstrate bad faith only through discovery of information in hands of insurance company and its attorneys); Fidelity and Cas. Ins. Co. of N.Y. v. Taylor, 525 So. 2d 908, 910, n.4 (Fla. 3d DCA 1987) (citing Brown v. Superior Court, 137 Ariz. 327, 336, 670 P.2d 725, 734 (1983)) ("The claims file is a unique, contemporaneously prepared history of the company's handling of the claim [and] in an action [for bad faith] the need for the information in the file is not only substantial but overwhelming."); Hodges v. Southern Farm Bureau Casualty Ins. Co., 433 So. 2d 125 (La. 1983) (without documents from claim file insured would be unable to effectively present case).

4. *See* West Bend Mut. Ins. Co. v. Higgins, 9 So. 3d 655, 657-58 (Fla. 5th DCA 2009).

5. 899 So. 2d 1121 (Fla. 2005).

6. *Id.* at 1128 (quoting Fidelity and Cas. Ins. Co. of N.Y. v. Taylor, 525 So. 2d 908, 909 (Fla. 3d DCA 1987)) (ellipses in original).

7. No. 05-21682, 2006 WL 3613760 (S.D. Fla. June 22, 2006).

8. *Id.* at *1.

9. *Id.*; *see also* Cozort v. State Farm Mut. Auto. Ins. Co., 233 F.R.D. 674 (M.D. Fla. 2005) ("Plaintiff is entitled to production of all claim file or litigation file materials pertaining to coverage issues, despite State Farm's assertion of attorney-client privilege.").

10. United Servs. Auto. Ass'n v. Werley, 526 P.2d 28, 33 (Alaska 1974) ("When an insurer through its attorney engages in a bad faith attempt to defeat, or at least reduce, the rightful claim of its insured, invocation of the attorney-client privilege for communications pertaining to such bad faith dealing seems clearly inappropriate."); *In re* Bergeson, 112 F.R.D. 692 (D.Mont. 1986); Gibson v. Western Fire Ins. Co., 682 P.2d 725 (Mont. 1984).

11. *See* West Bend Mut. Ins. Co. v. Higgins, 9 So. 3d 655, 657 (Fla. 5th DCA 2009); Progressive Exp. Ins. Co. v. Scoma, 975 So. 2d 461, 467 (Fla. 2d DCA 2007); Liberty Mut. Ins. Co. v. Bennett, 939 So. 2d 1113 (Fla. 4th DCA 2006); Provident Life & Acc. Ins. Co. v. Genovese, 943 So. 2d 321 (Fla. 4th DCA 2006); XL Specialty Ins. Co. v. Aircraft Holdings, LLC, 929 So. 2d 578, 583 (Fla. 1st DCA 2006); Liberty Mut. Fire Ins. Co. v. Kaufman, 885 So. 2d 905 (Fla. 4th DCA 2004).

12. Progressive Exp. Ins. Co. v. Scoma, 975 So. 2d 461, 467 (Fla. 2d DCA 2007). ■

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