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Alert

Recent Developments in the Use of the Attorney-Client Privilege and Work Product Immunity to Shield Investigative Materials from Discovery in New York

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An appellate-level state court in New York recently examined the applicability of the attorney-client privilege and work product immunity in the context of an insurer's pre-denial-of-coverage retention of outside counsel to assist in evaluating the existence or non-existence of insurance coverage for a claim.

See Nat'l Union Fire Ins. Co. of Pitts., Pa. v. TransCanada Energy USA, Inc., 2014 NY Slip Op 05606 (1st Dep't App. Div.).

The First Department held that "[d]ocuments prepared in the ordinary course of an insurer's investigation of whether to pay or deny a claim are not privileged, and do not become so 'merely because [the] investigation was conducted by an attorney.'" *Id*. 2 (citation omitted). The holding has given rise to questions about whether a bright-line rule now exists in the First Department barring application of work product immunity to documents prepared by retained counsel prior to an insurer's denial of coverage. As discussed below, we do not believe that the holding, when read in context, departs from existing case law concerning investigative tasks performed by counsel. We examine the case and provide our opinion and recommendations below.

The *TransCanada* Holding

In *TransCanada*, the Appellate Division, First Department reviewed cross-motions to confirm or reject the finding of the special referee that "any documents" prepared by outside coverage counsel that pre-dated a denial of coverage issued by National Union Fire Insurance Company of Pittsburgh, PA ("National Union") and other insurers of TransCanada Energy USA, Inc. ("TransCanada") should be produced during discovery. *Id*. As is commonly the case with Appellate Division opinions, the opinion here does not set forth the facts pertinent to the court's analysis. For this, we look to the trial court opinion.

According to the trial court opinion, TransCanada operated a steam turbine power generator located in Queens, New York. *See Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. TransCanada Energy USA, Inc.*, 2013 NY Slip Op 31967(U) ¶ 3 (Sup. Ct. N.Y. Cty.) On September 12, 2008, the steam turbine stopped working and remained out-of-service until May 11, 2009. *Id*. The loss of the steam turbine gave rise to a claim by TransCanada for repair costs and business interruption losses under an insurance policy issued by National Union and other participating insurers. *Id*. (The trial court opinion does not specify the type of insurance policy at issue or participation rates of the insurers.)

National Union and the other participating insurers hired experts, including insurance adjusters from Crawford Global Technical Services, and attorneys at firms Clausen Miller PC and Podvey, Meanor, Catenacci, Hildner, Cocoziello & Chattman to assist in investigating and determining coverage. *Id*. All of TransCanada's participating insurers except for one disclaimed coverage for the loss on June 2, 2010 and filed a declaratory judgment lawsuit against TransCanada on that date. *Id*. The remaining participating insurer disclaimed coverage one month later, on July 2, 2010, and was added to the declaratory judgment lawsuit shortly thereafter. *Id*.

In the declaratory judgment lawsuit, the insurers withheld from discovery numerous documents relating to their investigations of coverage. *Id*. The insurers claimed that the attorney-client privilege and work product immunity shielded the documents from discovery. *Id*. TransCanada moved to compel the production of documents, and the insurers cross-moved for a protective order. *Id*. The documents, nearly all of which were created prior to the insurers' disclaimers of coverage and initiation of the declaratory judgment lawsuit, were reviewed *in camera* by a special referee appointed by the trial court. *Id*. ¶ 3. A second *in camera* review, which included additional documents, was conducted by the court pursuant to a request made by the insurers and modified the referee's finding with respect to certain documents shielded by the attorney-client privilege. *Id*.

In response to the motion to compel and cross-motion for a protective order, the trial court first undertook a detailed review of New York law concerning the scope and application of work product immunity and the attorney-client privilege. *Id*. ¶¶ 5-10. The court found New York law to be well settled in that, for work product immunity to apply, "documents must be prepared for, or in anticipation of, litigation" and an insurer "cannot claim documents are prepared in anticipation of litigation until it makes a firm decision to deny coverage." *Id*. ¶¶ 5-6. In other words, an insurer cannot anticipate litigation with an insured until the insurer makes a determination to deny a claim. *Id*. ¶ 6. Therefore, work product immunity will "not bar the disclosure of materials prepared before the insurance companies made a firm decision to deny coverage." *Id*. The trial court emphasized that the determination of whether work product immunity applies is a fact-intensive process that requires the court to conduct an *in camera* review of the documents at issue. *Id*.

The trial court found that the attorney-client privilege "is not tied to the contemplation of litigation." *Id*. ¶ 7. The key consideration concerning application of the attorney-client privilege is whether a communication was made between an attorney and the attorney's client for the primary purpose of obtaining legal advice or services. *Id*. Nonetheless, the privilege only attaches "to the repetition of

confidences that were supplied to the lawyer by the client" and will not attach to documents prepared in the ordinary course of business, even if drafted by an attorney. *Id*. ¶¶ 7-8. In the context of an attorney retained to investigate coverage, the function of the attorney must be examined to determine whether the attorney was merely gathering factual material about an alleged loss or whether the attorney was providing legal advice to the client about an alleged loss. *Id*. Significantly, the trial court expressly held that "[d]ocuments may constitute privileged attorney-client communications, *even if made before the insurance company decides to deny coverage*, provided that they are primarily of a legal character, and not related to an insurance company's ordinary business activities." *Id*. ¶¶ 8-9 (emphasis added). The court also recognized that disclosures to third-parties will not waive the attorney-client privilege if the disclosing party and third-party share a common interest. *Id*. ¶¶ 9-11.

In applying the above holding, the trial court held that the insurers properly withheld certain documents under the attorney-client privilege and improperly withheld the remaining documents under work product immunity. With respect to the improperly withheld documents, the trial court found that:

The documents reviewed in camera primarily relate to [the insurers'] investigation of [the power plant] and the turbine. They reflect that the attorneys were supervising, coordinating, and directing the investigation, including collecting documents and hiring investigators, such as Crawford. The attorneys also prepared reports summarizing the results of the investigation. None of these documents are privileged. Many are not attorney-client communications, and those that involve the investigation of claims do not constitute legal advice. *The attorneys were primarily working to determine whether to deny coverage, an ordinary business activity for an insurance company*. *Moreover, most of these documents pre-date the decision to deny coverage, so they are not protected work product or trial preparation materials.*

Id. ¶¶ 11-12. The court further found that the insurers that denied coverage and filed suit on June 2, 2010 "were considering coverage until just before the denial letter was issued and lawsuit filed." *Id*. Therefore, the insurers did not meet their burden to show that they reasonably anticipated litigation with TransCanada until at least June 2, 2010, i.e., the date of the disclaimer of coverage. *Id*.

With the above factual background in mind, the Appellate Division, First Department reviewed the case. The First Department initially reviewed the case on February 25, 2014. *See Nat'l Union Fire Ins. Co. of Pitts., Pa. v. TransCanada Energy USA, Inc.*, 114 A.D.3d 595, 595-96 (1st Dep't 2014). The February 25, 2014 decision was re-heard on July 31, 2014. *See TransCanada*, 2014 NY Slip Op 05606. Four-judge panels on both courts affirmed the trial court decision in its entirety. Specifically, the First Department affirmed the trial court holding that certain documents were shielded from discovery under the attorney-client privilege because "they contained legal advice." *Id*. ¶ 2. The First Department also affirmed the trial court holding that the insurers had not met their burden to show that outside counsel was not "primarily engaged in claims handling — an ordinary business activity for an insurance company." *Id*. In affirming the trial court, the First Department held that

"[d]ocuments prepared in the ordinary course of an insurer's investigation of whether to pay or deny a claim are not privileged, and do not become so 'merely because [the] investigation was conducted by an attorney.'" *Id*. (citation omitted). In issuing this seemingly broad statement, the First Department relied on settled authority that an insurer's retention of counsel to investigate a claim, as opposed to providing legal advice or recommendations, will not necessarily shield documents generated during the investigation from discovery. *Id*. (citing *Brooklyn Union Gas Co. v. Am. Home Assur. Co.*, 23 A.D.3d 190, 191 (1st Dep't 2005)).

Conclusion and Recommendations

Although the First Department made a sweeping statement that is likely to be relied upon by policyholders, we believe that the holding must be viewed within the context of the facts of the case, where there was no evidence that the insurer anticipated litigation prior to issuing a disclaimer of coverage. In other words, we believe that the *TransCanada* holding, both at the trial court and appellate levels, restates well-settled New York law. An insurer that engages in-house or outside counsel to investigate the facts of a loss will, in most cases, be unable to shield those facts from discovery. In contrast, legal advice communicated by counsel to an insurer about the existence or non-existence of insurance coverage will, in the absence of waiver, remain shielded by the attorney-client privilege. Indeed, the trial court and First Department acknowledged that the insurers properly withheld certain documents during discovery pursuant to the attorney-client privilege, and that the date of the insurers' disclaimers of coverage was irrelevant in determining whether the privilege applied.

Likewise, materials prepared in anticipation of litigation will remain shielded by work product immunity, provided, however, that litigation is anticipated by the insurer. The determination of whether work product immunity applies is a fact-intensive determination. In *TransCanada*, the insurers could not meet their burden to show that they anticipated litigation any earlier than their denial of coverage on June 2, 2010. The trial court expressly acknowledged that the determination of whether work product immunity applies is a fact-intensive matter, thereby leaving-open the possibility that pre-denial-of-coverage materials could be shielded by work product immunity. Therefore, it is our opinion that *TransCanada* does not necessarily establish a bright-line rule barring application of work product immunity before a denial of coverage. That being said, we anticipate that policyholders will argue that such a bright-line rule now exists.

In response to demands for production of documents, insurers will bear the burden of establishing that litigation was reasonably anticipated. The key will be presenting courts with facts that support application of work product immunity and/or attorney-client privilege. In this regard, we recommend exercising caution when retaining counsel to investigate the facts of a loss. Factual materials gathered during counsel's investigation will not necessarily fall within the purview of the work product doctrine or attorney-client privilege. Instead, courts will look to the function being performed by counsel. If counsel is performing a claim handling function, then insurers will have a more difficult time establishing that the work product doctrine or attorney-client privilege applies. In contrast, if

counsel is communicating legal advice and facts determinative of such legal advice, e.g., in a coverage opinion, then insurers will have a much higher probability of success in showing that the attorney-client privilege or work product doctrine applies.

Finally, we note that the *TransCanada* case is binding authority upon courts sitting in the First Department. The decision is not binding upon, but may be persuasive to, courts sitting in other departments.