Martin, Disiere, Jefferson & Wisdom

The Weekly Update of Texas Insurance News

TEXAS INSURANCE LAW NEWSBRIEF

DEC 6, 2022

FEDERAL MAGISTRATE HOLDS INSURED-BROKER COMMUNICATIONS ARE PRIVILEGED WHEN FACILITATING LEGAL SERVICES

In a discovery ruling that has potentially far-reaching effects on the discoverability of insurance brokers' files in litigation, a federal magistrate judge in Austin recently found a policyholder's communications to an insurance broker about a pending lawsuit were privileged attorney-client communications. *Homeland Ins. Co. of New York v. Clinical Pathology Labs., Inc.*, No. 1-20-CV-783-RP, 2022 WL 17255798 (W.D. Tex. Nov. 28, 2022) (slip op.) involved medical malpractice claims against the insured. The insured apparently communicated regular updates on the litigation to its insurance broker, Aon, and when the carrier sought Aon's file in discovery, the insured argued those updates were privileged attorney-client communications.

This claim led to a careful examination of the boundaries of attorney-client privilege. Although it is generally thought of as existing between attorney and client, the privilege also applies to the client's representatives and the lawyer's representatives. The question then was whether Aon was the insured's representative and thus within the privilege or whether the insured had waived any privilege by sending the communications to a third party.

Texas has a well-developed and varied body of law on the sometimes-thorny question of when an insurance intermediary acts as the agent of the insured versus the agent of the insurer. But relatively little of it focuses specifically on privilege. Here, the court relied on two other federal district court opinions as well as cases from other jurisdictions holding that for privilege purposes, a broker acts as the insured's representative when its communications are made for the purpose of facilitating the rendition of legal services to the insured.

Here, the insured and its attorney had begun including Aon in many of their communications about the pending lawsuit, and the insured put on an affidavit stating they had included Aon so Aon would understand developments in the suit and therefore be able to assist the insured in securing insurance coverage for those claims. The court found this explanation, along with the privilege logs, adequate to support at least a *prima facie* finding of privilege.

Editor's Note: The moral of the story is three-fold: (1) think carefully about whom to copy on privileged communications, (2) do not assume the insurance broker is your representative – they may legally be the representative of the other side; and (3) if you do include an insurance broker in privileged communications, you may be able to protect the privilege by arguing they were facilitating the rendition of legal services. Additionally, this magistrate judge's report has not yet been adopted by the district judge and thus is not yet final.

HOUSTON APPEALS COURT HOLDS FOLLOW-FORM EXCESS POLICY OWES DEFENSE COSTS UNLESS EXPLICITLY EXCLUDED

After a large claim triggered coverage and exhausted both the primary and several layers of excess insurance, a dispute arose over whether the excess carrier had an obligation to reimburse incurred defense costs. Houston's 14th Court of Appeals held it did because its follow-form policy had not unambiguously declared its intent not to follow the wording of the primary policy on this issue. *Ohio Cas. Ins. Co. v. Patterson-UTI Energy, Inc.*, No. 14-22-00026-CV, 2022 WL 17097132 (Tex. App.—Houston [14th Dist.] Nov. 22, 2022, no pet. h.) (slip op.)

The analysis centered on the terms used by the two policies in their insuring agreements. The excess policy generally followed the form of the primary policy except where its terms differed. The primary policy used the defined term "ultimate net loss," which included defense expenses. The excess policy, on the other hand, used the term "loss," which had its own definition of, "sums… you are legally obligated to pay as damages." It never mentioned the term "ultimate net loss" in any way – either to adopt or reject it. Nor did it define the word "damages."

The excess carrier argued that its adoption of a different term with a different definition was an implicit rejection of the general follow-form rule, and also argued the use of the word "damages" excluded defense costs because the common meaning of damages is distinct from defense costs. The court of appeals rejected both arguments, holding the plain ordinary meaning of "damages" simply

meant money claimed or ordered to be paid as compensation for loss or injury, and that the insured's payment of its defense costs was a loss to the insured. The court distinguished this interpretation from existing precedent discussing the term "compensatory damages."

The excess carrier also argued that because its policy clearly stated it had no duty to defend, it could not possibly owe any defense costs. Although the court agreed the duty to defend remained with the primary carrier, it held a duty to defend is distinct from a duty to reimburse the insured for incurred defense costs which were part of the covered "ultimate net loss."

Editor's note: This unusual dispute and unusual ruling grew out of the unusual wording of the primary policy. Typically, a primary liability policy either includes an unlimited defense duty or specifically states that the policy limit is eroded by defense expenses and that the duty to defend ends when the primary limit is exhausted. Either of these types of primary policies leaves little room for the type of dispute seen here. The "ultimate net loss" seen in this primary policy is more typical of excess policies, and we predict it is not that likely to have widespread repercussions. Nevertheless, it is a cautionary tale from an underwriting perspective.