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## **A PRACTICAL GUIDE FOR EFFECTIVELY USING THE ADVICE OF COUNSEL DEFENSE**

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An insurance company's reliance on competent legal advice can greatly enhance its ability to protect itself against extra-contractual liability. In fact, while most states allow juries to consider the issue when evaluating the reasonableness of the insurer's conduct<sup>1</sup>, some states treat an insurer's good faith reliance on the advice of counsel as an absolute defense to claims for bad faith and/or punitive damages.<sup>2</sup> When used properly, the advice of counsel defense therefore can be a powerful weapon in a bad faith litigator's arsenal.

The effective use of the advice of counsel defense requires advanced planning and careful execution. Indeed, insurers who do not fully understand how the defense is used in litigation can unwittingly make it unavailable to their trial counsel. Worse yet, insurers who mismanage their efforts to seek legal advice can actually hurt their cause by opening doors to evidence a skilled plaintiff's attorney can use to convince a jury that the insurer acted unreasonably. This article therefore is designed to provide a practical guide for both seeking legal advice in connection with insurance claims and effectively using the advice of counsel defense in claims-related bad faith litigation.

### **A. Be Prepared to Prove that Reliance on the Advice of Counsel was Reasonable.**

In a bad faith case, it is not enough for the insured to prove that a benefit which is due under the subject policy has not been paid. Rather, the insured typically bears the burden of proving both that the insurer breached the policy and that it somehow acted unreasonably.<sup>3</sup> For that reason, bad faith claims require the trier of fact to evaluate the reasonableness of the insurer's conduct. In turn, insurers usually respond to bad faith claims by offering evidence from the key persons who were involved with the subject claim to explain their actions and (ultimately) why the claim decision was reasonable.

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<sup>1</sup> See, e.g., *Worden v. Tri-State Insurance Co.*, 347 F.2d 336 (10th Cir. 1965) [Kansas law]; *Szumigala v. Nationwide Mutual Insurance Co.*, 853 F.2d 274 (5th Cir. 1988) [Missouri law]; *Dumas v. Hartford Accident & Indemnity Co.*, 94 N.H. 484 (1948); *Decker v. Amalgamated Mutual Casualty Insurance Co.*, 324 N.E.2d 552, 553 (N.Y. 1974); *Barnes v. Oklahoma Farm Bureau Mutual Insurance Co.*, 11 P.3d 162, 174 (Oklahoma 2000); *Bohemia, Inc. v. Home Insurance Co.*, 725 F.2d 506 (9th Cir. 1984) [Oregon law]; *Cotton States Mutual Insurance Co. v. Trevethan*, 390 So.2d 724 (Florida 1980); *Crabb v. National Indemnity Co.*, 205 N.W.2d 633 (S.D. 1973); cf., *Blakely v. American Employers' Insurance Co.*, 424 F.2d 728, 734 (5th Cir. 1970) [holding that relying on the advice of counsel is not a defense under Texas law].

<sup>2</sup> See, e.g., *Davis v. Cotton States Mutual Insurance Co.*, 604 So.2d 354, 359-360 (Alabama 1992); *State Farm Mutual Automobile Insurance Co. v. Superior Court*, 228 Cal.App.3d 721, 725 (1991) [California law]; *Western Line Consolidated School District v. Continental Casualty Co.*, 632 F.Supp. 295, 304 (N.D.Mass. 1986); *Berk v. Milwaukee Automobile Insurance Co.*, 15 N.W.2d 834, 836-39 (Wisconsin 1944).

<sup>3</sup> See, e.g., *Tomaselli v. Transamerica Insurance Co.*, 25 Cal.App.4th 1269, 1280-1281 (1994) ["The mistaken withholding of policy benefits, if reasonable . . . does not expose the insurer to bad faith liability."].

The advice of counsel defense is potentially available whenever an attorney was among the key persons who were involved with the investigation and/or handling of the subject claim. In essence, it is an assertion that the claim decision was reasonable *because* it was based on an expert legal opinion.

To be certain, courts in bad faith cases give significant deference to the advice of counsel. Indeed, the defense can be available to insurers even when the attorney's advice was wrong.<sup>4</sup> However, courts will not dismiss a bad faith claim simply because the insurer professes to have relied on the advice of counsel.<sup>5</sup> Instead, they shift the focus of the lawsuit from an assessment of whether the claim decision was reasonable to whether the insurer actually and reasonably relied on the attorney's advice. As one Court put it, "[t]he ultimate question is whether sufficient evidence was presented to show [the] insurer's purported reliance on its attorney's advice was unreasonable."<sup>6</sup>

Following a few simple rules can make it far easier for insurers to more readily (and convincingly) prove at trial that their reliance on the advice of counsel was reasonable:

**Rule No. 1: Choose Competent Counsel.** In bad faith litigation, there is no defense for relying on the advice of a non-lawyer.<sup>7</sup> Likewise, there is no defense for relying on legal advice that is patently unsound or known to be wrong.<sup>8</sup> To effectively use the advice of counsel defense, an insurer therefore must be certain to choose competent counsel.

Although the published decisions suggest no "hard and fast" rules for determining whether a chosen attorney is competent, insurers planning to assert the advice of counsel defense should anticipate challenges to the attorney's qualifications, as well as his or her familiarity with the subject of the opinion. Accordingly, insurers usually should choose counsel with both a good reputation and demonstrable expertise in the relevant substantive area of law. A failure to do so could undermine the reasonableness of the legal opinion on which the insurer purports to rely.<sup>9</sup>

Of course, following that rule has the ancillary benefit of promoting the likelihood that the legal opinion on which the insurer relies is correct. Indeed, the law in each jurisdiction is everchanging, and attorneys who regularly follow those changes are more likely to provide an opinion that plainly demonstrates why the insurer's claim decision is reasonable.<sup>10</sup>

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<sup>4</sup> See, e.g., *Roesler v. TIG Insurance Co.*, 2007 U.S.App. LEXIS 24115 (10th Cir. 2007) [Oklahoma law]; *TGS Transportation, Inc. v. Canal Insurance Co.*, 2007 U.S.App. LEXIS 520 (9th Cir. 2007) [California law]; *Trask v. Iowa Kemper Mutual Insurance Co.*, 248 N.W.3d 97 (1976) [Iowa law].

<sup>5</sup> After all, they do not dismiss contract claims simply because an attorney told the insurer no benefits were payable.

<sup>6</sup> *Barnes v. Oklahoma Farm Bureau Mutual Insurance Co.*, *supra*, 11 P.3d at 174.

<sup>7</sup> See, e.g., *Zeitounian v. Farmers Insurance Group*, 25 Cal.App.4th 929 (1994) [". . . a menial factual investigator not employed to render legal advice probably cannot furnish the basis for an 'advice of counsel defense.'"]; See also, *Moore v. American United Life Insurance Co.*, 150 Cal.App.3d 610, 640 (1984) [physician's advice].

<sup>8</sup> See, e.g., *Melorch Builders, Inc. v. Superior Court*, 207 Cal.Rptr. 47, 50 (1984) [defense not available if insurer knows counsel's advice to be erroneous]; See also, *Tallent v. Liberty Mutual Insurance Co.*, Opinion No. 88698, Docket No. 1997-1777H, Superior Court of Massachusetts at Suffolk, April 25, 2005 [insurer's reliance on unfounded legal opinions justified awarding double damages].

<sup>9</sup> See, e.g., *Robertson v. Allstate Insurance Co.*, 1999 WL 179754 (E.D.Pa. March 10, 1999).

**Rule No. 2: Fully Inform the Attorney.** A legal opinion can be no more reliable than the information upon which it is based. Most courts therefore hold that the advice of counsel defense is not available without proof that the insurer fully disclosed all of the facts relevant to the claim decision.<sup>11</sup> Even an innocent failure to supply material facts to the attorney has been found sufficient to defeat the advice of counsel defense.<sup>12</sup>

If all of the important facts are not available, the attorney should be permitted to conduct an independent investigation designed to obtain all of the information he or she deems necessary to render an opinion.<sup>13</sup> However, insurers rarely should withhold relevant information from their chosen counsel. Plainly stated, evidence that the insurer “cherry-picked” helpful facts or withheld harmful facts can be offered to *support* a claim of bad faith by suggesting the insurer was interested only in obtaining a favorable legal opinion.<sup>14</sup>

**Rule No. 3: Make Sure the Lawyer is Disinterested.** Any ethical attorney who is retained to provide a legal opinion will take steps to ensure that his or her analysis is not affected by personal bias. Nonetheless, because they only assert the advice of counsel defense in bad faith litigation which challenges an adverse claim decision that was supported by a legal opinion, insurers should expect every such lawsuit to also involve accusations that the attorney who provided the opinion was not impartial. Accordingly, insurers should strongly consider using outside counsel to provide an opinion on which they can rely. Indeed, at least one court has found that an insurer’s reliance on the advice of its in-house attorneys was sufficient to justify a multi-million dollar extracontractual damage award.<sup>15</sup>

An insurer’s ability to defend the attorney’s neutrality normally is enhanced if his or her opinion acknowledges any harmful facts or law and carefully explains why they do not require a different conclusion. In most instances, though, the insurer will seek opinions only from qualified attorneys with whom they have had a long-standing prior relationship. It therefore can be imperative that the insurer take affirmative steps to ensure that the attorney is disinterested in how the subject claim ultimately is decided.<sup>16</sup>

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<sup>10</sup> As one California court recently noted, “[t]he fact that other courts have interpreted the law in the same manner as did the insurer . . . is certainly probative of the reasonableness, if not necessarily the ultimate correctness, of an insurer’s position.” *Morris v. Paul Revere Life Insurance Co.*, 109 Cal.App.4th 966, 976 (2003). For that reason, insurers can secure a significant advantage by seeking advice from attorneys who are familiar with the manner in which relevant legal issues currently are treated in the subject jurisdiction.

<sup>11</sup> See, e.g., *Melovich Builders, Inc.*, *supra*, 207 Cal.Rptr. at 50; See also, *Hamilton County Bank v. Hinkle Creek Friends Church*, 478 N.E.2d 689, 691 (Ind.Ct.App. 1985); *Aetna Casualty & Surety Co. v. Superior Court*, 153 Cal.App.3d 467 (1984); *Szumigala, supra*, 853 F.2d 274.

<sup>12</sup> *Moore v. York*, 271 P.2d 469 (Okla. 1962).

<sup>13</sup> See, e.g., *S.C. Johnson & Son v. Carter-Wallace, Inc.*, 614 F.Supp. 1278 (D.C.N.Y. 1985) [a competent opinion requires factual support from either the client’s disclosures or the attorney’s investigation].

<sup>14</sup> To guard against such an inference, insurers which have withheld information (such as a contradictory opinion from another source) should consider making a full disclosure *after* the attorney provides his or her opinion. When doing so, the insurer should invite the attorney to explain what impact (if any) the withheld information has on his or her opinion. Indeed, depending on the facts, such an approach could allow trial counsel to suggest that the attorney’s opinion was more reliable because it was not influenced by (and, for reasons explained by the attorney who supplied the opinion, actually can be reconciled with) the withheld information.

<sup>15</sup> *Tallent v. Liberty Mutual Insurance Co.*, Opinion No. 88698, Docket No. 1997-1777H, Superior Court of Massachusetts at Suffolk, April 25, 2005 [affirming award of \$4 million in extra-contractual damages].

To that end, the insurer should precisely identify the purpose(s) for which the attorney is being retained. The insurer also should consider expressly clarifying that the substance of the attorney's opinion will have no impact whatsoever on whether he or she is retained for any other purpose in the future. Of course, making such a statement may not suffice if, in fact, attorneys who provide opinions unfavorable to the insurer are not retained again.<sup>17</sup> Insurers therefore should anticipate that the insured's attorney will try to use discovery tools to examine this issue.

### **B. Be Prepared to Prove that Reliance on the Advice of Counsel was in Good Faith.**

When the need for doing so is legitimate, the mere fact that an insurer sought a legal opinion regarding a pending claim can be used to excuse any related delay.<sup>18</sup> However, judges (and juries) generally dislike letting an insurer "hide behind its relationship with counsel to argue that it reasonably ignored its obligations under the insurance policy to its insured."<sup>19</sup> For that reason, the advice of counsel defense typically is not available unless the insurer *actually* relies on the attorney's opinion.<sup>20</sup>

At a minimum, an insurer seeking to use the advice of counsel defense should be prepared to demonstrate that its actions were consistent with the attorney's advice. In most cases, though, the insurer also will be required to prove that it relied on the advice of counsel in good faith.<sup>21</sup> Indeed, the absence of such evidence could allow the insured's attorney to assert that the insurer's reliance on the advice of counsel constitutes independent evidence of its bad faith.<sup>22</sup> Observing these simple rules can better enable an insurer's trial attorney to rebut such an assertion – if not prevent it from being made in the first place:

**Rule No. 4: Consult the Attorney Before a Decision is Made.** Logically, an insurer must perform some factual investigation and claim processing to even identify a need for consulting an attorney. For at least two reasons, though, insurers should be certain to seek the advice of counsel before making a decision about the underlying claim.

First, consulting the attorney before a decision is made allows him or her to become an active participant in the development of those facts which are material to the claim. It therefore enhances the reasonableness of the insurer's reliance on the attorney's advice by ensuring that the attorney had a chance to identify and consider any additional evidence he or she deems important to the claim decision.<sup>23</sup>

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<sup>16</sup> See note 15, *supra*; See also, *Casselman v. Hartford Accident & Indemnity Co.*, 36 Cal.App.2d 700 (1940) [involving attorneys who were employees of the insurance company].

<sup>17</sup> See, e.g., *Roesler, supra*, 2007 U.S. App. LEXIS 24115 [allegation that insurer was "lawyer-shopping"].

<sup>18</sup> See, e.g., *Estate of Grant v. State Farm Life Insurance Co.*, Case No. 2:05-CV-02389-FCD-KJM (E.D.Cal. Oct. 23, 2007) [legitimate question about spouse's capacity to act as the executrix for insured's estate made the delay for consulting the law department reasonable].

<sup>19</sup> *Ravindran v. Harleysville Mutual Insurance Co.*, 65 D.&C.4th 338 (C.P. Phila. 2002).

<sup>20</sup> See, e.g., *Aetna Casualty & Surety Co., supra*, 153 Cal.App.3d at 475.

<sup>21</sup> *Melorch Builders, Inc., supra*, 207 Cal.Rptr. at 50; *Hamilton County Bank, supra*, 478 N.E.2d at 691; *Aetna Casualty & Surety Co.*, 153 Cal.App.3d at 475; *Szumigala, supra*, 853 F.2d 274.

<sup>22</sup> See, e.g., *Allen v. Allstate Insurance Co.*, 656 F.2d 487, 489 (9th Cir. 1981) [reliance on attorney's overly optimistic prediction of trial success was not reasonable]; See also, *Merritt v. Reserve Insurance Co.*, 110 Cal.Rptr. 511, 523 (1973).

<sup>23</sup> See, e.g., *S.C. Johnson & Son, supra*, 614 F.Supp. 1278 [a competent opinion requires factual support from either the client's disclosures or the attorney's investigation]; See also, *Melorch Builders, Inc., supra*, 207 Cal.Rptr. at 50.

Second -- and more importantly -- consulting the attorney before a decision is made supports the notion that the attorney is a reference for the claim department whose opinion is one of many things to be considered when making the claim decision. In that way, it helps guard against an argument that the advice of counsel defense should be unavailable because the insurer was looking only for a “rubber-stamp” approval of its pre-planned denial of the claim.<sup>24</sup> It also allows the insurer to modify its conduct or revise its planned communications about the subject claim to account for any unanticipated advice the attorney may provide.

**Rule No. 5: Get a Written Opinion.** For a variety of reasons, oral opinions carry less weight than written opinions. As one court recently explained, oral opinions “have to be proved perhaps years after the event, based solely on testimony which may be affected by faded memories and the forces of contemporaneous litigation.”<sup>25</sup> An insurer’s failure to secure a written opinion therefore deprives it of a permanent record of the information supplied to the attorney, what it asked the attorney to do, and precisely what advice the attorney gave. In the process, it can needlessly complicate the lawsuit with several new issues to be tested at trial.

Just as importantly, most insurers train their claims personnel to fully document their actions with respect to a benefit claim. In fact, many states have enacted regulations concerning fair claim practices which require that insurers maintain claim files with enough details “that pertinent events and the dates of the events can be reconstructed.”<sup>26</sup> Accordingly, securing a written opinion can help preempt an otherwise persuasive argument that the insurer’s failure to document in sufficient detail the advice of counsel on which it purports to rely should be treated as an admission that the opinion was not “pertinent” to the claim decision.<sup>27</sup>

**Rule No. 6: Explain Why Contrary Opinions were Rejected.** Issues that involve clear-cut answers are easy. After all, they give rise to just one right answer. In contrast, the most difficult issues an insurer can face are those for which more than one right answer seems to exist. Seeking a competent attorney’s advice about a difficult issue (such as whether coverage does or does not exist) therefore can represent a reasonable step in the insurer’s effort to determine which of the seemingly right answers is best.

When seeking the advice of counsel with respect to such an issue, insurers should acknowledge from the outset any evidence that arguably supports paying the subject claim. By doing so, the insurer will give the attorney a meaningful opportunity to consider those facts and explain why they are not enough to support paying the subject claim. Likewise, the insurer should expect the attorney’s opinion to identify any legal authorities that could support paying the subject claim and (if appropriate) to explain in detail why they are being rejected.

By their nature, those elements of the attorney’s opinion will involve some level of advocacy which could adversely affect the fact finder’s assessment of his or her neutrality.

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<sup>24</sup> The advice of counsel defense may fail if the insurer is found to have sought a legal opinion solely for protection against a possible lawsuit. See, e.g., *Beacon National, Inc. v. Reynolds*, 799 S.W.2d 390, 397 (Tex. 1990); *Bertero v. National General Corp.*, 529 P.2d 608, 617-618 (Cal. 1974).

<sup>25</sup> *Minnesota Mining and Manufacturing v. Johnson & Johnson Orthopaedics, Inc.*, 976 F.2d 1559 (Fed. Cir. 1992).

<sup>26</sup> 10 Cal. Code of Regulations Section 2695.3(a).

<sup>27</sup> If the attorney did not provide a written opinion, the insurer should strongly consider adding some written record to the claim file about what the attorney was asked to do, the information to which the attorney was given access, and the substance of the attorney’s opinion.



Without those elements, though, the attorney's opinion could be viewed purely as a piece of advocacy that is unreliable because the attorney did not or consider (or, perhaps, know of) facts or law that arguably lead to a different result.

For similar reasons, an insurer who receives competing legal opinions from different attorneys must carefully document its reason(s) for relying on one over the other. Doing so can provide persuasive evidence that the insurer was not "lawyer-shopping."<sup>28</sup> More importantly, it will provide the trial attorney with documentary evidence he or she can use to prove that the insurer's reliance on a favorable legal opinion was not without reason.

### C. Be Prepared to Produce Otherwise Privileged Documents.

The attorney-client privilege is a hallmark of the attorney-client relationship. It is designed to promote candid communications so that attorneys can be better informed and, in turn, better serve their clients. However, the attorney-client privilege is not unlimited. For example, the *Restatement (Third) of the Law Governing the Law* provides that "the attorney client privilege is waived for any relevant communications if the client asserts as a material issue in a proceeding that . . . the client acted upon the advice of a lawyer or that the advice was otherwise relevant to the legal significance of the client's conduct."<sup>29</sup>

As explained above, the advice of counsel defense makes an issue of both the substance of the attorney's legal advice and the facts upon which it was based.<sup>30</sup> For that reason, most jurisdictions hold that an assertion of the advice of counsel defense waives any privilege with respect to the advice upon which it is based.<sup>31</sup> Insurers who are defending a bad faith case in which the advice of counsel defense can be asserted therefore face a choice between waiving the attorney-client privilege and waiving the advice of counsel defense.<sup>32</sup>

**Rule No. 7: Scan the File for Objectionable Communications.** Once an insurer asserts the advice of counsel defense, the privilege that otherwise protects its communications with the attorney normally will be waived.<sup>33</sup> Arguably, that waiver is a "bell that cannot be unring." Stated differently, asserting the advice of counsel defense could *irrevocably* waive documents that otherwise are protected by the attorney-client and/or attorney work product

<sup>28</sup> See, e.g., *Roesler, supra*, 2007 U.S. App. LEXIS 24115

<sup>29</sup> *Restatement (Third) of the Law Governing the Law* §80(1)(a)(2003).

<sup>30</sup> *Rhone-Poulenc Rorer, Inc.*, 32 F.3d 851, 863 (3rd Cir. 1994) [party takes the affirmative step of placing the advice of counsel "at issue" when a client chooses to make the advice of counsel an essential element of a claim or defense and "attempts to prove that claim or defense by disclosing or describing an attorney client communication."]

<sup>31</sup> See, e.g., *Palmer v. Farmers Insurance Exchange*, 861 P.2d 895, 907 (Mont. 1993) [an exception to the attorney client privilege exists when the insurer "directly relies on advice of counsel as a defense to the bad faith charge."]; *Wade v. State Farm Mutual Automobile Insurance Co.*, 2006 U.S. App. LEXIS 26934 (9th Cir. 2006) [same].

<sup>32</sup> See, e.g., *Minnesota Specialty Crops, Inc. v. Minnesota Wild Hockey Club, L.P.*, 210 F.R.D. 673, 675 (D.Minn. 2002) ["The general rule is that the assertion of an advice-of-counsel defense waives that privilege 'as to communications and documents relating to the advice.'"]; *SNK Corp. of America v. Atlas Dream Entertainment Co. Ltd.*, 188 F.R.D. 566, 570 (N.D.Cal. 1999) [same]; cf., *F&G Scrolling Mouse, LLC v. IBM Corp.*, 190 F.R.D. 385, 391 (M.D.N.C. 1999) ["...maintaining the attorney-client privilege ... in effect, waives [the] advice-of-counsel defense."]

<sup>33</sup> See, e.g., *Palmer, supra*, 861 P.2d at 906-907; See also, *Dion v. Nationwide Mutual Insurance Co.*, 185 F.R.D. 288 (Mont. 1998); *Vicinanzo v. Brunschwig & Fils, Inc.*, 739 F.Supp. 891 (S.D.N.Y. 1990).

privileges. Before asserting the advice of counsel defense, then, the insurer must be confident about its willingness to disclose all of its communications with the attorney.<sup>34</sup> Indeed, a failure to fully disclose those communications and all related documentation could waive the advice of counsel defense.<sup>35</sup>

For that reason, insurers (and their trial counsel) should carefully scan all of the available documentary evidence before asserting the advice of counsel defense. If doing so reveals potentially harmful evidence which they would prefer for the jury to not see, the insurer and its trial counsel should carefully consider foregoing the advice of counsel defense. Such a decision could allow the insurer to protect the potentially harmful evidence from discovery without jeopardizing its ability to use the substance of the attorney's advice as a roadmap for defending the contract and bad faith claims on the merits.<sup>36</sup>

**Rule No. 8: Assert the Defense Before Discovery Closes.** The advice of counsel defense usually need not be raised as an affirmative defense in the insurer's answer.<sup>37</sup> If a delay in asserting the defense causes prejudice to the insured, though, that delay sometimes can be used to estop the insurer from asserting the defense.<sup>38</sup> To guard against that possibility, an insurer wishing to assert the advice of counsel defense should be certain its trial attorney does so early in the lawsuit – usually well before discovery closes.

If an insurer is unsure about whether to assert the advice of counsel defense, it should consider filing an early motion for summary judgment to test its ability to prevail on the bad faith claim with other evidence. If the insurer prevails on that motion, the attorney-client privilege will have been preserved. On the other hand, an order denying summary judgment because the insurer's other evidence leaves some trial controversy about the reasonableness of its conduct will enable the insurer to make a more informed decision about whether to assert the advice of counsel defense.

#### **D. Prepare the Attorney to Testify as an Expert Witness.**

In bad faith cases, insurers routinely resist any attempt at presenting expert testimony. Undoubtedly, they have numerous strategic reasons for doing so. Chief among them, though, is a belief that excluding expert witnesses works to their advantage because trained claims

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<sup>34</sup> See, e.g., *Vicinanzo*, *supra*, 739 F.Supp. 891; See also, *Rhodes v. AIG Domestic Claims, Inc.*, Docket No. 05-1306-BLS2, Superior Court of Massachusetts at Suffolk, January 23, 2006.

<sup>35</sup> See, e.g., *Vicinanzo*, *supra*, 739 F.Supp. 891; See also, *F&G Scrolling Mouse, LLC v. IBM Corp.*, *supra*, 190 F.R.D. at 391; *Cunkling v. Turner*, 883 F.2d 431 (5th Cir. 1989); *Board of Trustees v. Coulter Corp.*, 118 F.R.D. 532 (S.D. Fla. 1987); *Wender v. United Services Automobile Association*, 434 A.2d 1372 (D.C. 1981); *Russell v. Curtin Matheson Scientific, Inc.*, 493 .Supp. 456 (S.D. Tex. 1980); *Handguards, Inc. v. Johnson & Johnson*, 413 F.Supp. 926 (N.D. Cal. 1976); *Hearn v. Rhay*, 68 F.R.D. 574 (E.D. Wash. 1975).

<sup>36</sup> See, e.g., *Thomas v. Hartford Mutual Insurance Co.*, C.A. No. 01C-01-046 HDR, Superior Court of Delaware, Kent (April 20, 2004) [bad faith claimant could not compel disclosure of documents protected as attorney work product when insurer was not claiming to have relied on the advice of counsel].

<sup>37</sup> See, e.g., *State Farm Mutual Automobile Insurance Co. v. Superior Court*, 228 Cal.App.3d 721 (1991) ["...an insurer is not required to affirmatively allege advice of counsel as a defense to ... an insurance bad faith action."]; cf., *Arbuckle Broadcasters, Inc. v. Rockwell International Corp.*, 513 F.Supp. 412 (N.D. Tex. 1981) [insurer waived advice of counsel defense by its failure to plead or prove it at trial].

<sup>38</sup> *Great Northern Storehouse, Inc. v. Peerless Insurance Co.*, 2000 WL 1901266 (D. Maine 2000).

personnel can advocate the insurer's position better than any lay witness can advocate the insured's position.

Regardless of the position they take with respect to expert testimony, insurers can secure another strategic advantage by raising the advice of counsel defense. Specifically, an insurer seeking to assert the advice of counsel defense usually must make an evidentiary showing about the facts presented to the attorney and any investigation the attorney personally performed. Although the attorney may be prohibited from commenting on the law of bad faith<sup>39</sup>, the attorney will be asked to describe his or her legal expertise and, in the process, can describe the laws applicable to the underlying insurance claim. Most importantly, the attorney also will be given a chance to explain why those laws support the insurer's decision under the given set of facts. In that way, the advice of counsel defense can enable an insurer to present additional testimony from a knowledgeable witness who is both able and motivated to comment favorably on the insurer's claim decision.

To best capitalize on that opportunity, the insurer's trial attorney should prepare the coverage attorney to testify as if he or she were an expert witness. In that way, they can preserve an important opportunity to "tie together" all of the important facts at trial and rebut the insured's arguments through the testimony of a hand-selected witness.

**Rule No. 9: Have the Attorney Explain Why the Decision was Correct.** Since it is the trial judge's responsibility to instruct the jurors on the law, most courts hold that expert testimony on issues of law is not admissible.<sup>40</sup> Nevertheless, asserting the advice of counsel defense will require the insurer to present evidence about the basis for the attorney's advice and why it supported the underlying claim decision. Trial attorneys therefore should expect the insured's attorney to ask for a limiting instruction which advises the jury that the attorney's testimony is being offered solely on the issue of whether the insurer's conduct was reasonable.

Unless the trial judge orders otherwise, the trial attorney should nevertheless ask the attorney-witness to explain why the insurer's decision was correct – as opposed to simply inviting him or her to explain why it was "reasonable." Indeed, by explaining why the facts and applicable law support the insurer's claim decision, a skilled (and properly-prepared) attorney witness can supply compelling evidence that both disproves the bad faith claim<sup>41</sup> and – despite any limiting instruction -- reinforces the insurer's defense with respect to the breach of contract claim.

**Rule No. 10: Retain a Different Attorney for Trial.** Since the reasonableness of the opinion on which the insurer claims to have relied is an issue for the trier of fact to decide, the attorney who provided that opinion will almost certainly be called as a witness at trial. In turn, the attorney-witness -- and his or her entire firm -- could be disqualified from acting as an

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<sup>39</sup> *California Shoppers, Inc. v. Royal Globe Ins. Co.*, 175 Cal.App.3d 1 (1985); *Summers v. A. L. Gilbert Co.*, 69 Cal.App.4th 1155 (1999) [lawyer-expert who expounds on the law impermissibly usurps the trial court's role].

<sup>40</sup> See, e.g., *Summers, supra*, 69 Cal.App.4th 1155.

<sup>41</sup> To prevail on a bad faith claim, the insured must show the insurer withheld a benefit that was payable under the contract, unreasonably and without proper cause. See, e.g., *Gruenberg v. Aetna Insurance Co.*, 9 Cal.3d 566, 575 (1973). Evidence that no benefit was payable under the contract therefore can be used to disprove a bad faith claim.



advocate at the time of trial.<sup>42</sup> Insurers therefore should consider the possibility of raising the advice of counsel defense before they select their trial counsel.

In most instances, the additional litigation costs associated with finding new counsel will dictate that the insurer retain a different attorney to act as their trial counsel. As more fully explained above, doing so also will give the insurer an important opportunity to present compelling testimony that the jury might otherwise not be allowed to hear.

### Conclusion

Asserting the advice of counsel defense can dramatically change the complexion of a bad faith case. If mismanaged, it can backfire on the insurer and open a door to new types of evidence that the plaintiff's attorney can offer to prove the insurer's bad faith. If, however, the opinion was sound and was prepared by an informed and competent attorney, it can force the plaintiff's attorney to abandon his or her attack on the insurer's claims personnel and focus, instead, on the reasonableness of its professed reliance on the attorney's advice.

Insurers who have followed the rules discussed in this article should be well-positioned to use the advice of counsel defense to eliminate any extra-contractual exposure. Just as importantly, they can earn themselves an important advantage at trial: the right to call a knowledgeable witness whose testimony can help convince the jury that its decision on the underlying claim was correct.

#### About the Author

*Rob Pohls* has been shaping California insurance law since 1987. He is the Managing Attorney of *Pohls & Associates*, a California law firm that he established in 1999 to represent life, health, disability and long term care insurance companies in bad faith, ERISA and other forms of complex litigation.

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#### TEN RULES FOR EFFECTIVELY USING THE ADVICE OF COUNSEL DEFENSE

1. Choose Competent Counsel.
2. Fully Inform the Attorney.
3. Make Sure the Lawyer is Disinterested.
4. Consult the Attorney Before a Decision is Made.
5. Get a Written Opinion.
6. Explain Why Contrary Opinions Were Rejected.
7. Scan the File for Objectionable Communications.
8. Assert the Defense Before Discovery Closes.
9. Have the Attorney Explain Why the Decision was Correct.
10. Retain a Different Attorney for Trial.

<sup>42</sup> *Model Rules of Professional Conduct*, Rule 1.7.