IN FACT AND IN LAW

Damage Insurance Law

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A Dual Mandate but a Single Duty of Loyalty

By Odette Jobin-Laberge

In Kansa (en liquidation) *v.* Groupe DMR Inc. *(500-09-012340-022, August 18, 2003), the Court of Appeal rendered a key decision with respect to both the scope of the attorney-client privilege where the attorney is retained by the insurer and the attorney's duty of loyalty to the insured whom he or she represents. The Court also confirmed that it is ethically impossible for such an attorney to give opinions in respect of both coverage and liability issues after the attorney retained by the insurer has made an appearance on behalf of the insured.*

The Facts

The facts of this case are complex. The first attorneys retained by the insurer were replaced during the course of the matter.

Kansa's insured, DMR, provided Promutuel with a data processing system which the latter expressed dissatisfaction with by a demand letter in 1987.

DMR then gave a notice of loss to Kansa. An expert was selected by the insurer but an attorney was hired only in March 1988, after Promutuel's action in damages against DMR in the amount of $4 million was filed. For its part, DMR had retained the services of its own attorneys upon receipt of the demand letter.

The first attorney retained by Kansa officially appeared in the case only on October 25, 1989. This delay was due to the fact that DMR's attorneys refused to withdraw from the file until negotiations concerning the apportionment of costs incurred up to that date were concluded.

In November 1990, a new attorney was substituted for the first and an agreement concerning the apportionment of costs was agreed upon.

In March 1993, Promutuel amended its declaration and filed an accounting report re-assessing its damages to be $6 million.

On May 7, 1993, the second lawyer advised DMR that based on "new facts" and the "substantial change" made to the declaration, Kansa no longer intended to extend coverage and was withdrawing itself from the defence.

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In October 1993, DMR instituted third party proceedings against Kansa.

In April 1999, DMR reached a settlement with Promutuel for $1,5 million.

The case between DMR and Kansa was then continued under the *Winding-up Act*, with DMR then claiming $4 million to cover the settlement amount, the fees it incurred and repayment of its extrajudicial costs on the basis of Kansa's abusive behaviour.

In May and June 2002, during the trial, when the second attorney hired by Kansa and the latter's representative, Claude Fauré, were examined, Justice Durand allowed two objections to the evidence based on the attorney-client privilege. DMR was then seeking to obtain the correspondence exchanged between the first attorney and Kansa and the correspondence between the second attorney and Kansa dealing with coverage issues as well as the report of the expert hired by Kansa at the time that the notice of loss was given following receipt of the demand letter.

The Contentions of The Parties

DMR contended that only the insured should benefit from the attorney-client privilege and that the insurer could not prevent the insured from obtaining access to reports issued by his or her own attorney. It also contended that an insurer withdrawing from a case during a trial waives any attorney-client privilege that it may have benefited from, as the insured must then present evidence of the insurer's true knowledge of the facts to demonstrate that these were not new facts.

For its part, Kansa argued that the insurer is the attorney's only "client" with respect to coverage related issues and that the insured has no right whatsoever to get any information pertaining to that relationship. As concerns the second issue raised by DMR, Kansa added that no waiver ever existed and that the sole allegation of bad faith cannot constitute a basis for denying the insurer his right to the attorney-client privilege.

The Court of Appeal Analysis

After reviewing the case law pertaining to the "dual mandate" of the attorney retained by the insurer to defend an insured (*Nobert* v. *Lavoie*[1]; *Zurich* v. *Renaud* & *Jacob*[2]; *Boréal Assurances Inc.* v. *Réno-Dépôt*[3]; *Ville de Fermont* v. *Pelletier*[4]), Chamberland, J., supported by Nuss and Grenier, J.J. referred to an excerpt of the reasons of Lebel, J. in the case of *Renaud & Jacob*:

> **"(...) The insured accepts the fact that his lawyer is entrusted with a type of dual mandate. Within this mandate, he or she (the lawyer) remains bound by his or her normal ethical duties to the insured."**

Noting that the insured benefits from all the rights stemming from the client-attorney relationship (see *Citadel* c. *Wolofsky*[5]), he states the following:

> **"57. (...) However the possibility of a dual mandate vanishes where the interests of the insurer and the insured diverge, for instance, where the insurer wants to settle the case while the insured insists on a trial "to defend his reputation", where the insurer refuses to apply the total insurance coverage to a settlement that the insured knows is possible and that he or she desires or, again, where the insurer requires the attorney to provide an opinion with respect to coverage. The attorney then finds himself or herself tangled in an insoluble conflict of loyalty: carrying on with the dual mandate is simply not possible anymore."**

As a result, the insured is entitled to all the documents relating to the case in the possession of the attorney for the period when the latter acted on behalf of the insured (par. 58) but not those issued prior to such representation and which concern insurance coverage.

The judge pointed out that the current practice of entrusting the mandate relating to coverage to another lawyer with the lawyer retained for the insured abstaining from giving opinions on coverage issues allows for avoiding these conflicts of loyalty. However, he adds the following stern comments:

> **"64. The loyalty that the attorney owes to the client absolutely precludes the former from serving two masters, the interests of whom are contrary or may potentially collide. Where an attorney, at the request of a liability insurer, becomes the attorney *ad litem* for an insured, the attorney becomes, for all intent and purposes, the attorney of the insured and as such, owes absolute loyalty to the insured.**
>
> **65. When that same attorney breaches his or her duty of loyalty by advising a second master – in the present case, the insurer – on an issue about which the insurer's interests collide with those of the insured – for instance, with respect to the application and scope of the insurance coverage, - no attorney-client privilege can apply. The liability insurer simply cannot be the client of this attorney when the issue at hand concerns matters in respect of which the interests of the insurer and those of the insured are contrary or may collide. It is relatively unimportant, in my view, that the breach to the duty of loyalty results from the attorney's negligence or because of concerted action involving the attorney and the insurer."**

In conclusion, the Court did not allow communication of the letters sent by the first attorney to the insurer prior to appearing in the case, but allowed such communication for subsequent letters, even if such letters may discuss coverage issues. The Court also gave access to all correspondence between the second attorney and Kansa from the time such attorney appeared in the case following the substitution in November 1990.

1 *Nobert* v. *Lavoie* [1990] R.J.Q. 55 (C.A.)

2 *Zurich* v . *Renaud & Jacob* [1996] R.J.Q. 2160 (C.A.)

3 *Boréal Assurances Inc.* v. *Réno-Dépôt* [1996] R.J.Q. 46 (C.A.)

4 *Ville de Fermont* v. *Pelletier* [1998] R.J.Q. 736 (C.A.)

5 *Citadel* v. *Wolofsky* [1984] C.A. 277

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Chamberland, J. agreed in part with DMR's second argument that by withdrawing from the case and forcing DMR to institute third-party proceedings, Kansa waived its right under the attorney-client privilege, especially in light of the fact that its good faith was at issue. He was of the view that when the insurer, to justify its change of mind, states that it was not aware of certain facts, its "state of knowledge" at such time becomes the main issue of the case and the opposing party is thus entitled to test the merits of that allegation. Consequently, while the judge granted access to all the insurance adjuster's reports, on the basis that such reports were part of the information available to Kansa when it decided to defend DMR between 1990 and 1993, he nonetheless considered that this did not constitute a waiver of the attorney-client privilege that is broad enough to allow access to the letters sent to Kansa by the attorneys it retained before they appeared as attorneys *ad litem*.

Chamberland, J. dismissed DMR's contention to the effect that the insured should be granted access to the complete investigation file of the insurer as soon as it is alleged that the insurer acted in bad faith. Indeed, where the insurer denies such allegation and asserts that it acted in good faith, it would be unseemly to jeopardize the confidentiality of a document in possession of a party – even a liability insurer – on the basis of a yet unproven allegation of bad faith put forward by the other party.

Comments

This decision on the attorney's obligation of loyalty to the insured whom the insurer required him or her to defend is part of a constant evolution of the Court of Appeal jurisprudence dealing with this issue since the *Wolofsky* case in 1984. The dual mandate exists but is subject to definite limits with respect to relationships with each of the mandators.

An attorney hired by the insurer may voice an opinion on the issue of insurance coverage as long as he or she did not appear on behalf of the insured. If coverage is in force and is not challenged, he or she may then act as attorney *ad litem*. However, the attorney will not be allowed to give an opinion on insurance coverage where new facts are discovered since such attorney appeared because he or she then owes a duty of loyalty only to the insured. If the attorney nonetheless advises the insurer on that issue, his correspondence relating thereto will not be protected under the attorney-client privilege that may otherwise have existed between the insurer and the attorney it hired to represent the insured.

However, this decision leaves open all the issues relating to the attorney's conduct and insurance coverage problem management, where such problems occur during the course of a trial.

The deadline for filing an application for leave to appeal before the Supreme Court of Canada expires on October 17, 2003.

To be continued…

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