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**Defense Conflicts:
Recent Developments for Insurance Defense Counsel
In the Northwest**

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Insurance defense counsel in Oregon and Washington have long had a relatively stable set of court decisions and ethics opinions they could look to when navigating conflict issues arising from the tri-partite relationship among insurance carriers, insureds and their lawyers. Recently, however, there have been important developments in these conflict “navigation aids” for both states. This article surveys developments in both.

Oregon

Since the Oregon State Bar comprehensively updated its ethics opinions in 1991, insurance defense lawyers in Oregon have primarily looked to a trio of opinions in working through conflict issues. They were originally issued as OSB Formal Opinions 1991-30, 1991-77 and 1991-121. Their current counterparts are now numbered OSB Formal Opinions 2005-30, 2005-77 and 2005-121, reflecting a general update to the Oregon State Bar ethics opinion library in 2005 when Oregon moved that year from the former Disciplinary Rules to the current Rules of Professional Conduct. Despite the continued “2005” numerator in each, all three opinions were updated and re-issued in 2016 to reflect a key development.

All three opinions have always focused on different conflict areas for insurance defense counsel: Opinion 30 addresses subrogation issues; Opinion 77 discusses the intersection of coverage and defense work; and Opinion 121 outlines the duties of defense counsel in the reservation of rights context. All three in their original 1991 versions, however, were prefaced on the view that an insurance defense lawyer had two clients: the insured and the carrier.

This “two-client” approach has had important implications for conflicts. Since its original version in 1991, Opinion 77, for example, has counseled that a lawyer cannot simultaneously advise a carrier on coverage while defending the insured in the same matter. Similarly, since its original version in 1991, Opinion 121 has advised that an insurance defense counsel defending a reservation of rights case cannot take actions that would benefit the carrier over the insured without creating a nonwaivable conflict.

At the same time, other Oregon authority, such as the Oregon State Bar’s *Ethical Oregon Lawyer* treatise, noted that nothing in these ethics opinions precluded altering Oregon’s two-client approach by agreement so that a lawyer represented the insured only. The 2006 revision to the *Ethical Oregon Lawyer*, for example, included a “practice tip” to this effect¹ citing a leading ABA ethics opinion recognizing this caveat.²

In 2013, the federal district court in Portland confirmed the ability of Oregon lawyers to alter Oregon’s “default” two-client approach by agreement and, in the process, also illustrated a primary reason for doing it: so a client’s long-time counsel can both advise the client on coverage while also defending the client in the matter involved. *Evrax, Inc., N.A., v. Continental Ins. Co.*, No. 3:08-cv-00447-AC, 2013 WL 6174839 (D Or Nov 21, 2013) (unpublished), was a coverage case that followed on the heels of environmental litigation. The plaintiff corporation was seeking reimbursement of defense costs incurred in the environmental litigation. The corporation’s law firm had represented it in the environmental litigation and later moved to substitute-in as counsel for the corporation in the subsequent coverage case. The defendant insurers, in procedural effect, attempted to disqualify the plaintiff’s law firm—arguing that by virtue of Oregon’s two-client approach the law firm had also implicitly represented the insurers in the environmental case and, therefore, supposedly had a conflict in representing the corporation in the later coverage case against the carriers. The court refused to disqualify the law firm. The court acknowledged the three ethics opinions but concluded that whether an attorney-client relationship exists in a particular instance is governed by a test established by the Oregon Supreme Court in *In re Weidner*, 310 Or 757, 801 P2d 828 (1990), that looks at both the

subjective belief of the putative client and whether that subjective belief is objectively reasonable under the circumstances. The court found the defendant insurers could not meet the *Weidner* test because the law firm had informed the lead insurer on multiple occasions that it was only representing the corporate client in the environmental litigation and not the carrier.³

In the wake of *Evrax*, all three of the OSB ethics opinions were updated in 2016 to include a lead footnote citing *Evrax* and *Weidner* for the proposition that Oregon's "two-client" approach to insurance defense "can be overcome by the specific facts and circumstances in a particular matter."⁴ As in *Evrax*, this is most often accomplished by an engagement agreement with the client and a separate letter to the carrier limiting the representation to the insured.

Varying Oregon's two-client model is not necessary in many instances because there are no coverage issues and the insured and the carrier's interests are aligned fully. Where a corporate client wants its law firm available to both advise on coverage and defend it in the matter involved, however, *Evrax* and the revised Oregon State Bar opinions now provide clear authority for doing so.⁵

Washington

Like Oregon, Washington has a long-defined approach to insurance defense: an insurance defense counsel in Washington⁶ only represents the

insured and not the carrier under *Tank v. State Farm Fire & Cas. Co.*, 105 Wn2d 381, 715 P2d 1133 (1986), and Washington State Bar Association Advisory Opinion 195 (1999).⁷ Washington’s “one-client” approach can present its own issues. There have been significant recent developments in three areas.

First, the Washington Supreme Court in *Stewart Title Guar. Co. v. Sterling Sav. Bank*, 178 Wn2d 561, 311 P3d 1 (2013), reaffirmed Washington’s “one-client” approach in holding that a carrier could not sue a law firm for asserted malpractice in defending one of its insureds. Relying on established Washington precedent generally limiting claimants in legal malpractice cases to current or former clients of the lawyer or firm involved, the Washington Supreme Court in *Stewart Title* held that the carrier failed to meet this required element in light of *Tank*. The Washington Supreme Court also found that the carrier was not an intended beneficiary of the law firm’s work under Washington’s narrow exception governing nonclient claims for legal malpractice.

Second, the federal district court in Seattle in *Atlantic Specialty Insurance Company v. Premera Blue Cross*, No. C15-1927-TSZ, 2016 WL 1615430 (WD Wash Apr 22, 2016) (unpublished), disqualified a law firm from representing the defendant corporation in a Washington coverage dispute because the law firm was also representing an affiliate of the plaintiff carrier in a separate coverage

case in Oregon. The law firm had not used an engagement agreement in the Oregon case defining the client. Instead, the carrier in the Oregon case sent the law firm case handling guidelines that defined the client broadly to include the carrier's entire family of related entities—including the one on the other side in the Washington case. Although not an insurance defense case, *Atlantic Specialty* highlights the importance of using engagement agreements to, among other things, specify the client represented in an environment where carriers often have multiple affiliates.

Third, the Washington Supreme Court in *Arden v. Forsberg & Umlauf*, ___ Wn2d ___, ___ P3d ___, 2017 WL 4052300 (Sept 14, 2017), addressed disclosure obligations when a law firm is defending an insured under a reservation of rights and also does unrelated coverage work for the same carrier. *Arden* involved claims for legal malpractice and breach of fiduciary duty stemming from the defense in a reservation of rights case. The defendant law firm in *Arden* had limited its representation to the insureds in the underlying matter but had not informed them that it did unrelated coverage work for the carrier that had issued the reservation. The underlying case resolved but the insureds pursued a malpractice claim against the law firm on the theory that it should have disclosed that it did unrelated coverage work for the carrier. The

Washington Supreme Court unanimously affirmed the dismissal of the claims against the law firm because the insureds had not been damaged. A five-member majority also addressed the asserted conflict.⁸ While declining to draw a bright-line, the majority observed that a law firm in this position might have a “material limitation” conflict under Washington RPC 1.7(a)(2) if its relationship with a carrier created a significant risk that its professional judgment would be skewed in favor of the carrier to the detriment of the insured. The majority found that this was ultimately a fact question and did not reach a firm conclusion in the face of dueling expert opinions. *Arden* suggests that, at least as a matter of risk management, firms defending a case for an insured under a reservation of rights should disclose any other relationship with the carrier concerned and obtain an appropriate waiver from the insured.

Summing Up

Although the recent developments in Oregon and Washington have not altered their respective “two-client” and “one-client” default approaches to insurance defense, they highlight important nuances for insurance defense counsel in both states.

ABOUT THE AUTHOR

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¹ See Oregon State Bar, *Ethical Oregon Lawyer* § 5.8 at 5-11 (2006 rev 3d ed).

² ABA Formal Op 96-403 at 2 (1996) ("The insurer, the insured, and the lawyer may agree on the identity of the client or clients the lawyer is to represent at the outset").

³ Reconsideration was denied in *Evrax* at 2014 WL 2093838 (D Or May 16, 2014) (unpublished).

⁴ Similar footnotes were added to other ethics opinions touching on other aspects of insurance defense practice. See, e.g., OSB Formal Op 2005-166 (rev 2016) (addressing insurance defense guidelines).

⁵ ORS 465.483, which as enacted in 2013, now provides as a matter of insurance law that an insured in an environmental case with either a reservation of rights or excess exposure must be provided with “independent counsel” paid for by the carrier but only representing the insured. See *Siltronic Corporation v. Employers Insurance Company of Wasau*, 176 F Supp3d 1033, 1047-54 (D Or 2016) (discussing ORS 465.483 and the “independent counsel” requirement); see also *Schnitzer Steel Industries, Inc. v. Continental Casualty Company*, No. 3:10-cv-01174-MO, 2013 WL 12212732 (D Or Dec 17, 2013) (unpublished) (also discussing the legislation leading to ORS 465.483).

⁶ Under choice-of-law provisions in the respective versions of RPC 8.5(b) in Oregon and Washington, the law of the forum in litigation generally controls which state’s professional rules apply.

⁷ WSBA Advisory Op 195 was updated in 2009.

⁸ A four-member concurrence reasoned that it was unnecessary to address the alleged conflict in light of the unanimous conclusion on the lack of damages. The concurrence described the majority’s discussion of the conflict issue as *dicta*.