OVERCOMING ATTORNEY – CLIENT, WORK PRODUCT, BANK PRIVACY AND OTHER EVIDENTIARY OBJECTIONS IN INVESTIGATING FIDELITY BOND CLAIMS

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I. INTRODUCTION

At least implicit in every insurance policy is an agreement by the insured to cooperate during the insurer's investigation of a claim by providing all information and documents necessary for the insurer to make an informed coverage decision. The insured's cooperation is particularly important during the investigation of a fidelity bond claim because, unlike many other forms of insurance, the insured typically will already have conductedat least a partial investigation of the facts, and because most relevant information will be either within the insured's possession or under its control.

In most bond claims insureds recognize their obligation to cooperate, thus enabling the insurer to conduct a thorough investigation without resistance or interference from the insured. However, in recent years this cooperative spirit has come under increasing tension, particularly in large or complicated fidelity bond claims where the parties often retain lawyers to assist in the investigation and claim process. In such situations the insured's

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lawyers often view themselves as having a singular goal: to persuade the insurer that their client's bond claim should be paid in full. Often hardened veterans of trials and discovery wars, these lawyers almost instinctively attempt to paint their client's claim in the best coverage light, and to steer the insurer away from evidence which might negatively impact the insured's claim. While such conduct is normal, indeed expected, in the virtual battlefield of modern litigation, it should not be condoned in what is intended to be a non-adversarial claim investigation.

Objections to the insurer's requests for information often are based upon the attorney-client privilege and/or the work product doctrine. Other requests are refused due to concerns about retaliatory litigation by the allegedly dishonest employee or third parties, and are often based upon a supposed right to financial privacy or on personal privacy grounds. Although typically intended in good faith, such objections are inconsistent with the underlying premise of cooperation and unfairly impede the insurer's right to a fair and thorough investigation.

The purpose of this article is to analyze the more common objections raised by insureds, focusing most closely upon the attorney-client privilege and the work product doctrine, but also considering other objections insurers are now facing on an increasing basis. This analysis leads to the inevitable conclusion that such objections are seldom valid, particularly in light of the cooperation clause now found in most fidelity bonds, and that if insisted upon by the insured they unfairly increase the time and expense involved in the insurer's investigation, with little overall benefit to anyone.

II. THE ATTORNEY-CLIENT PRIVILEGE

A common objection raised to information requests by the fidelity bond insurer is the attorney-client privilege. Often insureds refuse to produce their lawyers investigation report or notes of witness interviews on this basis. Minutes of board of directors' meetings and loan files are also withheld on the same ground if the insured's lawyer has had any involvement in the meetings or transactions. Seldom, however, does the privilege validly apply to requests made during the insurer's investigation. A thorough understanding of the privilege will facilitate the insurer's response to such objections.

A. The Privilege Generally

The attorney-client privilege is the oldest of the privileges pertaining to confidential communications known to the common law.[1] Its purpose is to "encourage full and frank communication between attorneys and their cli-

1. *Hunt v. Blackburn*, 128 U.S. 464, 470 (1988); *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981).

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ents and thereby promote broader public interest in the observance of law and the administration of justice."[2] The privilege recognizes that "sound legal advice or advocacy serves public ends and that such advice or advocacy depends upon the lawyers being fully informed by the client."[3] Nevertheless, because it is contrary to the general American rule of allowing full discovery of the facts, it must be "strictly confined within the narrowest possible limits consistent with the logic of its principal."[4] And, consistent with the restrictive nature of the privilege, both federal and state law place the burden of establishing the attorney-client privilege, including each of its elements, squarely upon the person asserting it.[5]

The scope of the attorney-client privilege in most fidelity bond cases will depend upon state law because the underlying claim - enforcement of a contract - will be governed by state law. Even if a disputed claim will be resolved in federal court (such as in a diversity case, or with a claim involving federal regulators), state law will still typically apply. Rule 501 of the Federal Rules of Evidence specifically provides:

> [I]n civil actions and proceedings, with respect to an element of a claim or defense to which State law provides the rule of decision, the privilege of a witness…shall be decided in accordance with State law.[6]

Thus, in cases filed in state court, or in diversity actions where federal issues are not involved, state law will govern.

In those cases involving both state and federal law, an infrequent occurrence in fidelity bond claims, it is impractical to apply federal law to the federal claims and state law to the pendant state claims. Therefore, courts simply apply the federal privilege in such cases.[7]

Although the federal privilege is similar to that in most states, it is not identical. Thus, the parties must be cognizant of the applicable law.

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2. *Upjohn*, 449 U.S. at 389; *Trammel v. United States*, 445 U.S. 40, 51 (1980).

3. *Upjohn*, 449 U.S. at 389.

4. *NLRB v. Harvy*, 349 F.2d 900, 907 (4th Cir. 1965) (*quoting* 8 Wigmore, Evidence § 2292 (McNaughton rev. 1961)); *see also United States v. Nixon*, 418 U.S. 683, 710 (1974).

5. *See, e.g., In Re Grand Jury Proceedings*, 33 F.3d 342, 352 (4th Cir. 1994); *Clarke v. American Commerce Nat'l Bank*, 974 F.2d 127, 129 (9th Cir. 1992); *Norfolk v. United States Army Corps of Engineers*, 968 F.2d 1438, 1457 (1st Cir. 1992); *United States v. Schwimmer*, 892 F.2d 237, 244 (2nd Cir. 1989).

6. Rule 501, Fed. R. Evid. (1996).

7. *See* EDNA SLEAN EPSTEIN & MICHAEL M. MARTIN, THE ATTORNEY-CLIENT PRIVILEGE AND THE WORK PRODUCT DOCTRINE 8 (2d ed. 1989), *citing Perrignon v. Bergen Brunswig Corp.*, 77 F.R.D. 455, 458 (N.D. Cal. 1978) (federal privilege governs all claims raised in litigation involving federal questions and pendant state claims).

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One of the more commonly quoted statements of the elements of the attorney-client privilege is that found in *United States v. United States Shoe Machinery Corp.*;[8]

> The privilege applies only if (1) the asserted holder of the privilege is or sought to become a client; (2) the person to whom the communication was made (a) is a member of the bar of a court, or his subordinate and (b) in connection with this communication is acting as a lawyer; (3) the communication relates to a fact of which the attorney was informed (a) by his client (b) without the presence of strangers (c) for the purpose of securing primarily either (i) an opinion of law or (ii) legal services or (iii) assistance in some legal proceeding, and not (d) for the purpose of committing a crime or tort; and (4) the privilege has been (a) claimed and (b) not waived by the client.

A review of each of the elements of the privilege demonstrates why the privilege will seldom apply to an insurer's request for documents or other information during the insurer's investigation of a claim.

B. Communications Must be With the Client

It might seem simplistic to emphasize that in order for the privilege to apply the allegedly protected communication must be between a lawyer and the lawyer's *client*. Yet, insureds often raise the privilege in an effort to shield their lawyer's communications with third parties such as bank regulators, law enforcement officials, and even customers of the insured. Such communications clearly are not between the insured and its lawyer, and thus fall outside the privilege.

Determining the identity of a lawyer's client is an easy issue when the client is an individual. However, it is not always so simple when the client is a corporation or other entity, which will always be the case with fidelity bond claims. While there is typically little question that communications between an insured's executive officers and its lawyer are privileged, what about communications between the lawyer and mid or lower level employees of the insured? The answer to this question will usually depend upon whether the applicable jurisprudence follows the "control group" test. If it does, then the privilege will be limited to only those employees within the corporation's "control group."

The control group test was the subject of the United States Supreme Court's decision in *Upjohn Co. v. United States*.[9] In *Upjohn* the company's accountants, while conducting an audit of one of Upjohn's foreign subsidiaries, discovered that the subsidiary made payments for the benefit of foreign

8. 89 F. Supp. 357, 358-59 (D. Mass. 1950).

9. 449 U.S. 383 at 390 (1980).

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government officials in order to secure government business.[10] Outside counsel was retained to assist in an internal investigation into what were termed “questionable payments.” As part of the investigation the attorneys prepared a letter containing a questionnaire that was sent to “All Foreign General Area Managers” over the signature of Upjohn’s Chairman. The letter indicated that Upjohn’s Chairman had requested its General Counsel to “conduct an investigation for the purpose of determining the nature and magnitude of any payments,” and had instructed the managers to “treat the investigation as ‘highly confidential’ and to not discuss it with anyone other than Upjohn employees who might be helpful in providing the requested information.”[11]

Subsequently the company voluntarily submitted a report of its investigation to the Internal Revenue Service, which immediately began an investigation to determine the tax consequences of the payments. As part of its investigation, the IRS served Upjohn with a subpoena demanding production of all files relevant to the investigation, including the written questionnaires. Upjohn refused on the ground that the questionnaires constituted communications between Upjohn and its lawyers, and thus were privileged. On appeal the Sixth Circuit ruled that communications with employees who were outside Upjohn’s “control group” — those officers and agents of Upjohn not responsible for directing Upjohn’s actions in response to legal advise — were not privileged.[12] The United States Supreme Court disagreed, reasoning that such a limitation upon the attorney-client privilege would frustrate the purpose of the privilege “by discouraging the communication of relevant information by employees of the client to attorneys seeking to render legal advice to the client corporation.”[13] Important to the Court was the fact that in order to provide advice to a corporate client, the attorney must be free to communicate with all relevant employees, including mid-level and lower-level employees who have information relevant to the subject matter of the lawyer’s representation.[14]

The Court refused a request by the parties (as well as various *amici*) to develop a bright line test concerning the attorney-client privilege. Rather, the court reasoned that application of the privilege must be determined on a “case-by-case” basis.[15] Some guidance can be obtained, however, from the emphasis the Court placed upon the facts surrounding Upjohn’s investigation, including the following:

10. *Id.* at 386.

11. *Id.* at 387.

12. *Id.* at 388.

13. *Id.* at 392.

14. *Id.* at 683.

15. *Id.* at 396.

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1. Information from middle and lower level employees was needed to supply the basis for the legal advice.

2. The communications concerned matters within the scope of the employees' corporate duties.

3. The employees were sufficiently aware that they were being questioned in order for the corporation to obtain legal advice.

4. The questionnaire identified the person sending the questionnaire as the company's General Counsel;

5. A statement of policy accompanying the questionnaire clearly indicated the legal implications of the investigation; and

6. Pursuant to express instructions from Upjohn's Chairman, the communications were considered "highly confidential."[16]

Presumably then, application of the privilege will be questionable to the extent the above factors are not present. For instance, the privilege might be unavailable if the need for input from lower level employees is not great. Or, if it is not made abundantly clear, as was the case in *Upjohn*, that the communications would be strictly confidential, then the privilege presumably might not apply. As the Court pointed out, however, application of the privilege must necessarily be applied on a case by case basis.

While *Upjohn* is obviously controlling when the federal privilege is at issue, not all state courts follow *Upjohn*.[17] Also, several states seem to have endorsed the control group test through statute.[18] Thus, the insurer must be familiar with the test applicable in the state in which its investigation is being conducted.

The typical fidelity bond claim will involve discussion between the insured's president, board of directors, or other senior officials. However, as in *Upjohn*, an investigation by an insured's lawyer typically also includes communications with lower level employees. Thus, if the claim is being pursued in a state which adopts the control group test, the lawyers' communications with lower level employees might not be privileged for the sole reason that the employees were not within the insured's control group. Even in federal cases, the facts of each case will need to be closely scrutinized to determine whether *Upjohn* is controlling.

16. 449 U.S. at 394-95.

17. *See, e.g., Samaritan Foundation v. Super. Ct.*, 844 P.2d 593, 600-603 (Ariz. Ct. App. 1992); *Consolidation Coal Co. v. Bucyrus-Erie Co,* 432 N.E.2d 250, 254-258 (Ill. 1982).

18. *See, e.g.*, Alaska R. Evid. 503(a)(2) (1996); Arkansas R. of Evid. 502(a)(2) (1996); Maine R. of Evid. 502 (1996).

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C. The Privilege Excludes Communications Only

Trial lawyers are accustomed to objecting to the disclosure of any of their work product on the basis of the attorney-client privilege and the work product doctrine. The work product doctrine (which will be discussed more thoroughly in the following section) extends only to documents prepared *in anticipation of litigation*. The attorney-client privilege, on the other hand, is available even if litigation is not anticipated; however, it extends solely to *communications* between the lawyer and the client. It does not protect disclosure of the underlying facts, nor that part of a document which does not contain a communication between the lawyer and client. As the U.S. Supreme Court noted in *Upjohn*:

> '[T]he protection of the privilege extends only to *communications* and not to facts. A fact is one thing and a communication concerning that fact is an entirely different thing. The client cannot be compelled to answer the question, 'what did you say or write to the attorney?' but may not refuse to disclose any relevant fact within his knowledge merely because he incorporated a statement of such fact into his communication to his attorney.[19]

In *Upjohn* the Court was careful to focus on the distinction between communications between Upjohn's employees and its counsel (which included the employees' responses to the questionnaires and the notes reflecting responses to interview questions), on the one hand, and the lawyer's notes and memoranda of the interviews to the extent they went beyond recording responses to the lawyers' questions.[20] The court recognized that to the extent the lawyers' notes went beyond communications with employees, the protection potentially available would be the work product doctrine, rather than the attorney-client privilege.

This point was also made by the Court, although in a slightly different manner, in its earlier opinion in *Hickman v. Taylor*.[21] In this case the Court held that the protective cloak of the attorney-client privilege "does not extend to information which an attorney secures from a [third party] witness while acting for his client in anticipation of litigation."[22] The Court also explained that the privilege does not extend to the "memoranda, briefs, communications and other writings prepared by counsel for his own use in prosecuting his client's case; and it is equally unrelated to writings which

19. 449 U.S. at 396 (*citing Philadelphia v. Westinghouse Elec. Corp.*, 205 F. Supp. 830, 831 (E.D. Pa. 1962)).

20. 449 U.S. at 397.

21. 329 U.S. 495, 508 (1947).

22. 329 U.S. at 302.

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reflect an attorney's mental impressions, conclusions, opinions or legal theories."[23] Thus, an attorney's notes concerning his observations about his investigation do not necessarily fall within the privilege.[24]

Thus, to the extent the notes or memoranda of a lawyer contain communications with the insured, they might be privileged. However, to the extent they contain matters other than communications, such as the lawyers' thoughts and conclusions about the investigation or claim, they arguably fall outside the privilege.[25]

An illustrative case is *Bird v. Penn Central Co.*,[26] in which Underwriters at Lloyds of London attempted to rescind two directors and officers' insurance policies based upon misrepresentations in the insured's application. The insured sought production of various documents prepared by underwriters' counsel on the basis that the documents established that underwriters had waived their right to rescission of the policy. The court found that the attorney-client privilege was inapplicable to documents which contained information the lawyers had gathered from other sources.[27] "To the extent the information sought to be discovered was not conveyed to counsel by his client, the attorney-client privilege is inapplicable."[28]

D. Acting as a Lawyer

The heart of the attorney-client privilege is protecting *legal advice* from a lawyer to his client.[29] In order for the privilege to apply, the attorney must have been consulted by the client for the purpose of obtaining legal advice or services, rather than nonlawyer services.[30] Thus, courts have held that communications in which the client seeks business advice, rather than legal advice, are not privileged.[31] Similarly, communications made to aid an attorney acting as a business negotiator are not privileged.[32]

23. *Id.*

24. *See, e.g., In re Walsh*, 623 F.2d 489, 494 (7th Cir. 1980), *cert. denied*, 449 U.S. 994 (1980).

25. *But see, e.g., Cedrone v. Unity Sav. Ass'n*, 103 F.R.D. 423, 429 (E.D. Pa. 1984) (holding that lawyer's memorandum to another lawyer protected by the privilege).

26. 61 F.R.D. 43 (E.D. Pa. 1973).

27. 61 F.R.D. 46.

28. *Id.*

29. *See* EPSTEIN & MARTIN, *supra* note 7, at 36.

30. *See, e.g., Diversified Indus., Inc. v. Meredith*, 572 F.2d 596, 602 (8th Cir. 1978).

31. *See, e.g., United States v. IBM Corp.*, 66 F.R.D. 206, 212-13 (S.D.N.Y. 1974).

32. *See, e.g., United States v. Wilson*, 798 F.2d 509, 513 (1st Cir. 1986).

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As the Sixth Circuit has noted:

> Once the attorney-client relationship is established, inquiry will focus upon the nature of the communication or information sought. The relationship itself does not create '[a] cloak of protection [which is] draped around all occurrences and conversations which have any bearing, direct or indirect, upon the relationship of the attorney with his client.' The privilege 'protects only those disclosures necessary to obtain informed legal advice which might not have been made absent the privilege.'[33]

In the context of a bond claim, a common issue is whether the insured's lawyer was retained to provide legal advice, *or to act as an investigator* merely to gather facts. In *Diversified Industries, Inc. v. Meredith*[34] an initial panel of the Eighth Circuit concluded that the law firm retained to conduct an investigation into a possible slush fund kept by a client was acting as an investigator, not a lawyer, and that the privilege did not apply. The panel's opinion explained:

> [W]e are persuaded that Law Firm was not hired by Diversified to provide legal services or advice. It was employed solely for the purpose of making an investigation of facts and to make business recommendations with respect to the future conduct of Diversified in such areas as the results of the investigation might suggest. The work that Law Firm was employed to perform could have been performed just as readily by non-lawyers aided to the extent necessary by a firm of public accountants.[35]

On rehearing *en banc*, the full court reversed the panel's opinion, concluding that a *prima facie* showing had been made that the law firm had been retained to give legal advice simply because the firm was "a professional legal advisor."[36] The court's ruling clearly begs the question. A bar card does not mean that a lawyer is retained only to give legal advice. Nor, and more to the point, should an insured be permitted to selectively shield the facts surrounding its loss by hiring a lawyer to conduct an investigation or submit the bond claim. For this reason, the initial panel opinion is intellectually more sound.

Most courts have not concluded that a *prima facie* showing has been made simply because a lawyer is involved. In *In re Kearney*,[37] for instance, an audit of Richmond County National Bank disclosed widespread irregularities in various loans that had been made by the bank. The bank employed a firm of accountants to make an extensive investigation of the questioned

33. *In Re: Walsh*, 623 F.2d at 494 (citations omitted).

34. 572 F.2d at 596.

35. 572 F.2d at 603.

36. *Id.* at 610.

37. 227 F. Supp. 174 (S.D.N.Y. 1964).

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transactions. The investigation included a detailed examination of the bank's records, and interviews with various witnesses. Subsequently the accountants submitted a comprehensive report to the bank, parts of which were a cooperative effort between the accountants and the bank's lawyer. Subsequently, the Internal Revenue Service conducted an investigation and subpoenaed the report. The bank refused to produce the report, and the IRS filed a motion to enforce its summons. The court ordered production of the report, reasoning:

> The document is not a confidential communication from the Bank to its counsel for the purpose of securing legal advice, nor does it, as far as I can see, contain any legal advice from the counsel to the Bank. It is a report of a factual investigation.[38]

Similarly, in *United States Fidelity & Guaranty Co. v. Canady*[39] USF&G retained a lawyer to assist it in investigating a suspicious fire claim. During the ensuing litigation USF&G refused to produce its lawyer's report to the insured on the basis of the attorney-client privilege. On appeal the West Virginia Supreme Court recognized that the report "could be exempted from discovery under the attorney-client privilege," but refused to "adopt a *per se* rule making ordinary investigative employees, who hold licenses to practice law, attorneys for purposes of the attorney-client privilege."[40] The court reasoned as follows:

> To do so could pose an absolute bar to discovery of relevant and material evidentiary facts. In the insurance industry context, it would shield from discovery documents that otherwise would not be entitled to any protection if written by an employee who holds no law license but who performs the same investigation and duties. To enlarge the scope of protection to those not performing traditional attorney duties would be fundamentally incompatible with this State's broad discovery policies designed for the ultimate ascertainment of truth.[41]

Although *Canady* addresses the privilege as raised by the insurer, it applies equally to the insured's investigation.

And, in *Dawson v. New York Life Insurance Co.*[42] a former employee of New York Life sued the company for defamation. During the lawsuit the employer sought to discover communications from New York Life's employees to its lawyers. The district court overruled New York Life's objection

38. *Id.* at 176-77.

39. 460 S.E.2d 677 (W. Va. 1995).

40. *Id.* at 689-690.

41. *Id.*

42. 901 F. Supp. 1362 (N.D. Ill. 1995).

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on the basis of the attorney-client privilege, finding that the information sought was purely of a factual nature. The court reasoned:

> The information communicated by the attorneys was surely of a legal nature…. However, common sense tells us that there is a difference between merely providing legal information and providing 'advice.' Here, the attorneys were simply called upon to provide factual information to the New York Life employees at issue…. [T]he Court agrees with Dawson that the attorneys were acting more as 'courier[s]' of factual information, than 'legal advisors.' Therefore, the communications of the employees to the attorneys are not subject to the attorney-client privilege.[43]

Similarly, in *North American Mortgage Investors v. First Wisconsin National Bank*,[44] for instance, the court found that a memorandum analyzing a participation agreement that was prepared by a mortgage banking officer who was also an attorney in the legal department of the mortgage company, was not prepared for purposes of rendering legal advice. The court explained:

> The possession of a law degree and admission to the bar is not enough to establish a person as an attorney for purposes of determining whether the attorney-client privilege applies. For the privilege to exist, the lawyer must not only be functioning as an advisor, but the advice given must be predominantly legal, as opposed to business, in nature.[45]

In most bond cases counsel for the insured is hired primarily as an investigator.[46] His goal is typically to determine - from a factual standpoint - whether an employee of the insured has acted in a dishonest manner and caused the insured to sustain a loss. His investigation typically consists of reviewing various documents, often loan files, and interviewing employees of the insured, as well as third-party witnesses, typically including current and former customers or borrowers of the insured institution. It makes no sense, then, to permit the insured to shield the facts revealed by such an investigation from the insurer. In fact, it is counterproductive to do so. First, it results in two different entities (the insured and later the insurer) covering

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43. *Id.* at 1367.

44. 69 F.R.D. 9 (E.D. Wis. 1975).

45. *Id*. at 11; *see also Puerto Rico v. SS Zoe Colocotroni*, 61 F.R.D. 653, 660 (D.P.R. 1974).

46. This is not, however, necessarily the case with counsel hired by the insurer. In many cases the insurer retains counsel only when it perceives a coverage problem. Although the insurer is often involved in the factual investigation of the claim in such situations, the lawyer has been hired for the specific purpose of advising the insurer whether the insured's claim is covered under the bond. Plus, although the insurer's lawyer may also be acting as a gatherer of facts, those facts are gathered for the specific purpose of determining whether they give rise to a covered claim. Therefore, under such circumstances the lawyer is clearly acting as a legal advisor, rather than an investigator of facts.

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the same ground, an exercise which benefits no one and unnecessarily increases the insurer's cost, which inevitably leads to increased premiums. Second, if an incorrect coverage decision is made because of a lack of all relevant facts, one of the parties will be harmed (and premiums again unfairly affected).

E. Expectation of Privacy

Basic to application of the attorney-client privilege is the expectation of the client that the communications with the lawyer will remain confidential. Query how an insured who has submitted a bond claim can have an expectation of confidentiality with respect to the facts pertaining to its loss? Why should the insured be permitted to shield pertinent facts discovered by its counsel merely because a lawyer is conducting the investigation, rather than an employee of the insured?

Several courts have specifically held found that insureds do not have a legitimate *expectation of privacy* in such situations, although the cases involve third-party insurance claims. In *EDO Corp. v. Newark Insurance Co*.[47] the plaintiff, EDO, refused to produce documents that had been prepared in connection with claims that had been asserted against it in an underlying lawsuit arising from EDO's alleged role in connection with environmental contamination of certain property. EDO asserted both the attorney-client privilege and the work product doctrine as grounds for withholding the documents. Newark Insurance Company, which had issued an environmental indemnity policy to EDO, responded by maintaining, *inter alia*, that assuming the attorney-client privilege and work product doctrine were otherwise applicable, EDO's implied duty of good faith and fair dealing, which arose from the insurance policies, as well as the duty to cooperate provided in the various policies, deprived EDO of a reasonable expectation that communications with, or the work product of, its counsel made in connection with the underlying EPA action would remain confidential as to the defendant insurers. The court agreed, reasoning that, based "upon EDO's explicit duty to cooperate with its insurers *and* its implied duty of good faith and fair dealing under its contracts for insurance, EDO cannot presently contend that it expected discussions with its attorneys regarding the underlying EPA action would remain confidential as to the defendants."[48]

In reaching its decision the district court relied heavily upon *Carrier Corp. v. Home Insurance Co.*,[49] involving a similar situation, in which the court reasoned:

47. 145 F.R.D. 18 (D. Conn. 1992).

48. *Id.* at 23.

49. No. CV-35-23-83, 1992 W.L. 478585 (Conn. Sup. Ct. Aug. 18, 1992).

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> Given the fact that the insured is required to disclose to its insurer relevant information when it makes a claim for coverage under an insurance policy, and given the fact that the insured is required to deal in good faith with its insurers, the insured cannot, in good faith, entertain a *reasonable* expectation at the time the communication is made that the facts underlying those claims will not be disclosed to its insurer once a claim for coverage is made.[50]

In *Carrier Corp*. the court recognized the "irreconcilable conflict between the plaintiff insured's duty to disclose and to deal in good faith, to refrain from taking unconscientious advantage of it [sic] 'insurers even through the forms of technicalities of law,'" and the insured's assertion that the communications at issue were made in strict confidence and were not to be disclosed.[51] The court reconciled this conflict in favor of the insurer, reasoning that the communications at issue were not made "with a reasonable expectation of confidentiality."[52]

Both the *EDO* court and the *Carrier Corp*. court rejected the insured's contention that once the insurer denies coverage, the insured may use the attorney-client privilege to shield confidential communications from the insurer, reasoning as follows:

> It should be kept in mind, however, that the plaintiff insured is demanding that the insurer be held liable on the insurance policy. If the plaintiff is successful, the insurer will be required to fulfill its contractual obligation to the insured. For that reason, an insurer does not forfeit its right to fall unfair disclosure merely by denying liability into the policy and, further, the insured's expectation of confidentiality as to its insurer does not become reasonable once the insurer denies coverage if the insured continues to demand coverage under its contracts for insurance.[53]

A similar case, although on different facts, is *Waste Management, Inc. v. International Surplus Lines Insurance Co*.[54] *Waste Management* involved an insured's claim for indemnification under environmental indemnification policies following the insured's settlement of a toxic tort lawsuit. During discovery the insurers requested production of the files maintained by the insured's defense counsel in the underlying lawsuit. The insured refused to produce such files on the basis of the attorney-client privilege. As did the courts in *EDO Corporation v. Newark Insurance Co*.[55] and *Carrier Corp. v. Homes Insurance Co*.,[56] the Illinois Supreme Court found that the insured

50. *Carrier Corp*., at * 3 (emphasis added), *cited in EDO Corp.*, 145 F.R.D. at 22.

51. *Carrier Corp.*, 1992 W.L. 478585, at * 4.

52. *Id.*

53. *Carrier Corp*., at * 4, *cited in EDO Corp.*, 145 F.R.D. at 23.

54. 579 N.E. 2d 332 (Ill. 1991).

55. 145 F.R.D. 18.

56. 1992 W.L. 478585.

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had no reasonable expectation of privacy under the circumstances. The court reasoned:

> A fair reading of the terms of the contract renders any expectation of attorney-client privilege, under these circumstances, unreasonable. We conclude that the element of confidentiality is wanting and, therefore, the attorney-client privilege does not apply to bar discovery of the communications in the underlying lawsuits.[57]

While not all states recognize that the insured owes the insurer a duty of good faith and fair dealing, many either do, or appear to be heading in that direction.[58] Even without such a duty, however, it is arguable that there should not be an expectation of privacy when the relationship between the parties is contemplated to be one of cooperation, rather than of an adversarial nature. Fundamental to the coverage decision is a determination of the complete and true facts relating to the insured's loss. Therefore, the insured should not be permitted to screen facts from the insurer through the guise of the attorney-client privilege.

There is another line of cases with a similar result, but based upon slightly different reasoning. These cases hold that, in the context of third party insurance, communications between the insured and his lawyer in connection with the underlying lawsuit against the insured may be shared with the insurer without waiving the privilege where the insurer has a *common interest* in the subject matter of the communications.[59] Fundamental to this doctrine is the existence of a common interest between the insurer and its insured in minimizing exposure in the underlying lawsuit to the benefit of both the insurer and the insured. Under such circumstances the insured does not have a reasonable expectation of privacy in documents generated in defense of the underlying lawsuit.[60] As the district court recognized in *Metro Wastewater Reclamation District v. Continental Casualty Co.*,[61] both the insured and its insurers had, "and continue to have, precisely the same interests in (a) preventing further claims against [the insured]…, and (b) defeating or favorably resolving by settlement any such claims."

57. 579 N.E.2d at 328.

58. *See, e.g., Diamond Heights Homeowner's Assoc. v. Nat'l Am. Ins. Co.*, 277 Cal. Rptr. 906, 914 (1991); *Andrew Jackson Life Ins. Co. v. Williams*, 566 So.2d 1172 (Miss. 1990); *N.A. Van Lines, Inc. v. Lexington Ins. Co.*, No. 94-1635, 1996 W.L. 364764 (Fla. July 3, 1996).

59. *See, e.g., Metro Wastewater Reclamation Dist. v. Continental Cas. Co.*, 142 F.R.D. 471, 476 (D. Co. 1992); *Indep. Petrochemical Corp. v. Aetna Cas. & Surety Co.*, 654 F. Supp. 1334, 1365 (D.D.C. 1986); *Truck Ins. Exchange v. St. Paul Fire & Marine Ins. Co*., 66 F.R.D. 129, 132 (E.D. Pa. 1975); *Car & General Ins. Corp. v. Goldstein*, 179 F. Supp. 888, 893 (S.D.N.Y. 1959), *aff'd* 277 F.2d 162 (2nd Cir. 1960).

60. *See, e.g., Metro Wastewater Reclamation Dist. v. Continental Cas. Co.*, 142 F.R.D. at 471-476.

61. *Id.*

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In the context of a fidelity bond claim, the insured and the insurer also have a common interest in investigating the facts concerning the insured's loss, preventing any further loss, and taking any appropriate action against allegedly dishonest employees or other third persons involved in the loss. Until such time as it becomes apparent to the parties that a coverage dispute is at hand they are, or should be, working together to determine exactly how the insured's loss was incurred. Thus, the *common interest* exception to the privilege should apply equally to documents pertaining to the insureds' claim, at least until such time as an adversarial relationship develops between the parties.

Another situation that arises occasionally that calls into question the insured's expectation of confidentiality is where the insured provides part or all of its investigation report to either the insurer, or other entities. The author has on several occasions, for instance, been provided with a report from an insured's lawyer setting forth the facts surrounding the insured's loss and opining that the facts give rise to coverage. Yet, when a request was made for the documents upon which the report was based the insured refused to provide them on the basis of the attorney-client privilege. In such cases, the underlying documents are usually highly relevant, and typically more complete than those provided by the lawyers' report, which typically is limited to those facts most favorable to the insured's claim.

A case involving such a situation is *Gottlieb v. Wiles*.[62] In *Gottlieb*, as part of an investigation current and former employees of MiniScribe Corporation were interviewed by the company's lawyers. Notes were taken during the interviews and, thereafter, served as the basis for the preparation of interview summaries, as well as a report. The report cited extensively to the interview summaries, and even attached many of the summaries. While the report was released the materials relating to the report were not. In finding that there was no expectation of privacy in the supporting materials, the district court reasoned:

> [T]he *sine qua non* for invocation of the privilege is that the communications in question were intended to be confidential. Furthermore, one may not release documents which pervasively cover a particular subject matter and then claim that the underlying supportive data is privileged. These limitations on the scope of the privilege are consistent with the principle that the attorney-client privilege is to be strictly construed.[63]

62. 143 F.R.D. 241 (D. Colo. 1992).

63. *Id.* at 249 (citations omitted).

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F. Offensive Use of Privilege

The offense use doctrine recognizes that a privilege is meant to be used defensively, as a shield against divulging privileged information, rather than offensively as a sword.[64] Thus, when information otherwise protected by the privilege is placed at issue through some affirmative act of the owner of the privilege for the owner's benefit, the privilege is deemed to have been waived on the theory that to hold otherwise would be manifestly unfair to the party seeking disclosure.[65]

The doctrine makes sense when it is remembered that the purpose of a privilege is the "protection of interests and relationships which, rightly or wrongly, are regarded as of sufficient social importance to justify some sacrifice of availability of evidence relevant to the administration of justice."[66] Thus, once the holder of the privilege places the information at issue the essential function of the privilege - to protect a confidence - is no longer served.[67]

A good discussion of the doctrine is contained in the D.C. Circuit's opinion in *In Re Sealed Case*.[68] In this case the court recognized that even though privileges usually provide categorical protection from discovery, implied waiver, - or the offensive use doctrine - is one of two common law doctrines which give courts a limited ability to make sure that privileges do not serve ends to which they were not intended.[69] In the court's words, the doctrine "deals with an abuse of a privilege itself rather than of a privileged relationship. Where society has subordinated its interest in the search for truth in favor of allowing certain information to remain confidential, it need not allow that confidentiality to be used as a tool for manipulation of the truth-seeking process."[70] Quoting Dean Wigmore, the court continued:

> [R]egard must be had to the double elements that are predicated in every waiver, i.e., not only the element of implied intention, but also the element of fairness and consistency. A privileged person would seldom be found to waive, if his intention not to abandon could alone control the situation. There is al-

64. *See, e.g., Conkling v. Turner*, 883 F.2d 431, 434 (5th Cir. 1989) (*citing Pitney Bowes, Inc. v. Mestre*, 86 F.R.D. 444, 446 (S.D. Fla. 1980)); *United States v. Moody*, 763 F. Supp. 589, 597 (M.D. Ga. 1991); *United States v. Mierzwicki*, 500 F. Supp. 1331, 1335 (D. Md. 1980); *Republic Ins. v. Davis*, 856 S.W.2d 158, 163 (Tex. 1993).

65. *See, e.g., Conkling v. Turner*, 883 F.2d at 434, *and cases cited therein.*

66. 1 MCCORMICK ON EVIDENCE, 269 (4th ed. 1992).

67. *Id.* at 342.

68. 676 F.2d 793 (D.C. Cir. 1982).

69. *Id.* at 807.

70. *Id.*

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> ways also the objective consideration that when his conduct touches a certain point of disclosure, fairness requires that his privilege shall cease whether he intended that result or not. He cannot be allowed, after disclosing as much as he pleases, to withhold the remainder.[71]

In *Pavlinko v. Yale-New Haven Hospital*[72] the reasoning of the Connecticut Supreme Court, in the context of a litigant claiming the Fifth Amendment privilege, is illustrative of the doctrine:

> The privilege against self-incrimination is a constitutional shield against a person being compelled to convict himself out of his own mouth. It may not be used as a sword to deny others information which is rightfully theirs. A plaintiff cannot use one hand to seek affirmative relief in court and with the other lower an iron curtain of silence against otherwise pertinent and proper questions which may have a bearing upon his right to maintain his action.[73]

A common issue in fidelity bond claims is the date on which the insured discovered its loss. This question impacts issues such as which of several bonds are applicable to the insured's claim, whether the insured's notice of loss was timely, and whether coverage previously terminated as to the allegedly dishonest employee. Occasionally an insured's discovery of a loss will occur as a result of the investigation by the insured's lawyers. The author has had an opportunity to consider more than just an occasional claim in which the insured took the position that discovery of its loss did not occur until the insured received the investigation report of its outside counsel, often at a board of directors meeting, notwithstanding the fact that it appeared discovery should have occurred long before such time. Under such circumstances, the insured cannot reasonably expect that its counsel's report, or the applicable board minutes, will remain privileged. To refuse production in such a situation would clearly constitute an offensive use of the privilege as a sword, rather than merely as a shield, to protect information not otherwise at issue.

This was precisely the case in *Leucadia, Inc. v. Reliance Insurance Co*.[74] in which an insured's loss was reportedly discovered during an investigation conducted by its lawyers. Reliance Insurance Company maintained that any privilege applicable to the report was overcome by "the critical importance of these documents to the litigation."[75] The court recognized that, [e]ven "where the technical requirements of the privilege are satisfied, it may, nonetheless, yield in a proper case, where strong public policy requires

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71. *Id.* (*quoting* 8 J. WIGMORE, EVIDENCE IN TRIALS AT COMMON LAW § 2327, at 636 (J. McNaughton rev. 1961)).

72. 470 A.2d 246 (Conn. 1984).

73. *Id.* at 251.

74. 101 F.R.D. 674 (S.D.N.Y. 1983).

75. *Id.* at 679.

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disclosure."[76] Interestingly, even though the court found that evidence tending to demonstrate late notice and prior knowledge by the insured which might have terminated the bond as to the dishonest employee constituted relevant evidence, Reliance did not demonstrate a "need" to the documents rising to the level of a strong public policy that would justify overcoming the privilege. However, the court found a waiver of the attorney-client privilege to the extent the insured relied upon its counsel's report to establish the date it discovered its loss.[77] The court went on to conclude that the report constituted "a necessary element in plaintiff's case, or is in any event so critical to plaintiff's case, that the privilege must yield. In the context of this case, counsel's communication with plaintiff constituted an important disputed fact essential to plaintiff's proof. It cannot be withheld."[78]

Similarly, in *Apex Municipal Fund v. N-Group Securities*,[79] the plaintiff sued a law firm for fraud, alleging that its lawyer had made misrepresentations when acting as legal counsel to Drexel, Burnham & Lambert, Inc. in issuing revenue bonds. Plaintiffs attempted to obtain from the law firm the underlying documents used to prepare certain public offering statements. The law firm maintained that the attorney-client privilege protected the documents because they were prepared to facilitate the rendition of legal services. In response, the plaintiffs argued that the law firm waived the attorney-client privilege with respect to all communications regarding the public offering statements through selective disclosures by the lawyers during their depositions. For instance, in response to a question during a deposition of one of the lawyers asking whether competitive bidding was required on the underlying projects, the lawyer responded by explaining that he had asked this same question of another one of the lawyers in his firm. Also, in response to the plaintiff's allegation that the law firm knew or should have known of material misrepresentations and omissions in the public offering statements, the lawyer maintained it was the view of all lawyers working on the transaction that they were not required to make any disclosures.

The district court found that the defendant lawyers did not merely deny the plaintiff's allegations, but also injected into the case their own understanding and interpretation of the law in order to deny any fraudulent intent on their part. The court ruled that because the defendants inserted their own understanding of the law as a basis for the reasonableness of its actions, the attorney-client privilege had been waived with respect to those topics.[80] The court reasoned: "When confidential communications are made a material

76. *Id.*

77. *Id.*

78. *Id.* at 680.

79. 841 F. Supp. 1423 (S.D. Tex. 1993).

80. *Id.* at 1431.

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issue in a judicial proceeding, fairness demands treating the defense as a waiver of the privilege."[81]

The offensive use doctrine has also been relied upon in the context of directors and officers insurance cases to require directors and officers to divulge advice they received from their counsel in settling an underlying lawsuit against them. For instance, in *Charlotte Motor Speedway, Inc. v. International Insurance Co.*[82] the minority shareholders of Charlotte Motor Speedway sued the directors of the company for various security law violations following a merger. Following settlement of the case International was sued on its policy to recover the amount paid in settlement. International defended on various grounds, including the ground that the settlement of the underlying lawsuit was not reasonable. The issue before the court was whether International would be permitted to obtain the work product of the lawyers representing the defendant directors in the underlying action in order to determine their views concerning the reasonableness of the settlement. Plaintiff took the position that production was not required because of the work product doctrine (although they could have also have argued application of the attorney-client privilege). The court found an implied subject matter waiver, reasoning that "the activities and advice of plaintiff's counsel in the settlement of the underlying action are inextricably interwoven with the issue of International's liability under the Policy. Specifically, the discovery of the nature of these activities of counsel goes to whether [the insured] met its obligations under the policy in constructing the settlement agreement and whether it reached the agreement in good faith."[83]

Finally, in *Harding v. Dana Transport, Inc.*[84] Dana Transport retained a lawyer to investigate a sexual discrimination complaint by one of its former employees. In the lawsuit that was subsequently filed against Dana in district court, Dana defended, in part, on the ground that it had fully investigated the complaints raised by the plaintiff and found no evidence of sexual harassment. Based upon this defense the plaintiff sought to take the deposition of the lawyer who performed the investigation. Dana Transport refused to allow any substantive inquiry into the lawyer's investigation on the basis of the attorney-client privilege and the work product doctrine. In finding that Dana had waived its attorney-client privilege the court reasoned:

> By asking Mr. Bowe to serve multiple duties, the defendants effused the roles of internal investigator and legal advisor. Consequently, Dana cannot now

81. *Id.* (*quoting Conkling v. Turner*, 883 F.2d 431, 435 (5th Cir. 1989)).

82. 125 F.R.D. 127 (M.D.N.C. 1989).

83. *Id.* at 129; *see also Chevron Corp. v. Penzoil Co.*, 974 F.2d 1156, 1162 (9th Cir. 1992); *Potomas Elec. Power Co. v.Calif. Union Ins. Co.*, 136 F.R.D. 1, 4-5 (D.D.C. 1990); *United States v. Mierzwicki*, 500 F. Supp. 1331, 1335 (D. Md. 1980).

84. 914 F. Supp. 1084 (D.N.J. 1996).

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> argue that its own process is shielded from discovery. Consistent with the doctrine of fairness, the plaintiffs must be permitted to probe the substance of Dana's alleged investigation to determine its sufficiency. Without having evidence of the actual content of the investigation, neither the plaintiffs nor the fact finder at trial can discern its adequacy.[85]

G. Conclusion

In summary, the attorney-client privilege should seldom constitute a valid basis for the insured to withhold information from the insurer during the investigation of a fidelity bond claim. As discussed above, there simply can be no legitimate expectation of privacy concerning facts pertinent to the insured's loss. Retaining a lawyer to conduct the investigation neither changes this point, nor magically provides protection over facts which fall outside the privilege in most cases. Importantly, the insured certainly should not be permitted to utilize the privilege as a sword to hide behind in order to shield information necessary to establish its position.

III. WORK PRODUCT DOCTRINE

Another objection being raised more frequently by insureds is based upon the work product doctrine. Under the work product doctrine insureds maintain either that their lawyer's work product is protected from discovery because it was prepared in anticipation of litigation with the insurer, or with a third party, such as the dishonest employee or possibly a former loan customer. Once again, however, there are few fidelity bond claims in which this objection can be raised validly.

A. The Doctrine Generally

Although intertwined, the attorney-client privilege and work product doctrine are independent principles which are applied quite differently. The attorney-client privilege was founded to encourage free and frank discussions between the lawyer and his client, and thus is limited to *communications*. The work product doctrine, on the other hand, is premised on encouraging careful and thorough preparation by an attorney in preparation for or anticipation of litigation, and thus extends to all of the work product of an attorney, not just communications. However, it is limited to only those documents actually prepared in anticipation of litigation. As with the attorney-client privilege, the burden of establishing application of the work product doctrine is squarely on the party asserting it.[86]

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85. 914 F. Supp. at 1096.

86. *See, e.g., Kent Corp. v. NLRB*, 530 F.2d 612, 623-624 (5th Cir. 1976), *cert. denied*, 429 U.S. 920 (1976); *In re Perrier Bottled Water Litigation*, 138 F.R.D. 348, 351 (D. Conn. 1992); *Auto Owners Ins. Co. v. Total Tape, Inc*., 135 F.R.D. 199, 201 (M.D. Fla 1990).

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The genesis of the work product doctrine is, as every lawyer learned in law school, the well known case of *Hickman v. Taylor*.[87] *Hickman* was a wrongful death lawsuit against the owners of a tug boat that sank. In the course of discovery, attorneys representing the family of one of the deceased crew members sought discovery of written statements taken of survivors and other witnesses concerning the accident, and records, reports, and other memoranda made concerning the incident. The owners admitted that statements had been taken, but refused to produce them on the grounds of privilege. Rejecting plaintiff's discovery request the court reasoned as follows:

> Historically, a lawyer is an officer of the court and is bound to work for the advancement of justice while faithfully protecting the rightful interests of his clients. In performing his various duties, however, it is essential that a lawyer work with a certain degree of privacy, free from unnecessary intrusion by opposing parties and their counsel. Proper preparation of a client's case demands that he assemble information, sift what he considers to be the relevant from the irrelevant facts, prepares legal theories and plan of strategy without undue and needless interference. That is the historical and the necessary way in which lawyers act within the framework of our system of jurisprudence to promote justice and to protect their clients' interest. His work is reflected, of course, in interviews, statements, memoranda, correspondence, briefs, mental impressions, personal beliefs, and countless other tangible and intangible ways — aptly though roughly termed by the Circuit Court of Appeals in this case as the *'Work product of the lawyer.'* Were such materials open to opposing counsel on mere demand, much of what is now put down in writing would remain unwritten…. The effect on the legal profession would be demoralizing. And the interests of the clients and the cause of justice would be poorly served.[88]

Three main points follow from *Hickman*:

1. Material collected by counsel in the course of preparation for possible litigation is protected from disclosure;

2. That protection is qualified, in that the adversary may obtain discovery by showing sufficient need for the material.

3. The attorney's thought process is at the heart of the adversary system, and privacy is essential for the attorney's thinking; thus, the protection is greatest, if not absolute, from materials that would reveal the attorney's opinion work product.[89]

87. 329 U.S. 495 (1947).

88. 329 U.S. at 510-511.

89. *Epstein & Martin, supra* note 7, at 102.

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B. Applicable Law

As the Supreme Court pointed out in *Hickman*, the work product doctrine is not a true "privilege."[90] Instead, it is a common law doctrine which recognizes that certain requests for information in documents fall "outside the arena of discovery and contravenes the public policy underlying the orderly prosecution and defense of legal claims."[91] As a result, in federal court Rule 26(b)(3) of the Federal Rules of Civil Procedure, as well as the Court's decision in *Hickman v. Taylor*, govern the issue in discovery disputes, rather than state principles under Rule 501 of the Federal Rules of Evidence.[92] Most state rules are similar to Rule 26, which provides, in pertinent part, as follows:

> Subject to the provisions of subdivision (b)(4) of this rule, a party may obtain discovery of documents and tangible things otherwise discoverable under subdivision (b)(1) of this rule and prepared in anticipation of litigation or for trial by or for another party or by or for that other party's representative (including the other party's attorney, consultant, surety, indemnitor, insurer, or agent) only upon a showing that the party seeking discovery has substantial need of the materials in the preparation of the party's case and that the party is unable without undue hardship to obtain the substantial equivalent of the materials by other means. In ordering discovery of such materials when the required showing has been made, the court shall protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation.

The Rule differs from the doctrines set forth in *Hickman v. Taylor* in several key respects:

(1) It's application is limited to pretrial discovery;

(2) It protects materials prepared by a party's representative other than the party's attorney; and

(3) It relates only to discovery of "documents and tangible things."[93]

As a result, *Hickman v. Taylor* remains the benchmark when a court is faced with questions such as whether the privilege applies at trial or to oral statements.[94]

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90. *Hickman v. Taylor*, 329 U.S. at 509-510.

91. *Id.* at 510.

92. *See, e.g., United Coal Cos. v. Powell Constr. Co.*, 839 F.2d 958, 966 (3rd Cir. 1988).

93. Rule 26(b)(3), FED. R. CIV. P.; *see* Kevin M. LaCroix, *Work Product in the Claim File*: *The Insurer's Perspective*, 3 COVERAGE 26 (ABA Press 1992).

94. *EPSTEIN & MARTIN, supra* note 7, at 103.

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Rule 26(b)(3) thus provides qualified immunity from discovery where materials are:

(1) Documents and tangible things otherwise discoverable;

(2) Prepared in anticipation of litigation or for trial; and

(3) By or for another party or by or for that other party's representative.

To overcome the qualified immunity, the party seeking discovery must make a showing of:

(1) Substantial need for the materials; and

(2) An ability to obtain the substantial equivalent of the information without undue hardship.

However, special protection is given to a lawyer's "mental impressions, conclusions, opinions or legal theories,"[95] which are seldom discoverable if formed in anticipation of litigation.

C. Anticipation of Litigation

Promulgating a test for use in determining when someone anticipates litigation would not appear to be difficult. This has not, however, proven to be the case. Various so-called tests have been followed by the courts in attempting to discern whether a document was prepared in anticipation of litigation.[96] However, these tests do little more than restate the question. A common sense approach has been suggested by Wright & Miller:

> The pertinent parties anticipate litigation, and begin preparation prior to the time suit is formally commenced. Thus the test should be whether, in light of the nature of the document and the factual situation in the particular case, a document can fairly be said to have been prepared or obtained because of the prospect of litigation.[97]

National Union Fire & Insurance Co. v. Murray Sheet Metal Co.[98] demonstrates a similarly common sense approach:

> [T]he mere fact that litigation does eventually ensue does not, by itself, cloak materials" with work product immunity. The document must be prepared because of the prospect of litigation or the preparer faces an actual claim or a

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95. *Id.* at 104.

96. *LaCroix, supra* note 93, at 29 (discussing the "direction of counsel test," the "whole file test," and the "case by case test").

97. 8 WRIGHT AND MILLER, FEDERAL PRACTICE AND PROCEDURE § 2040, at 343 (1994).

98. 967 F.2d 980, 984 (4th Cir. 1992).

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> potential claim following an actual event or series of events that reasonably could result in litigation…. Determining the driving force behind the preparation of each requested document is therefore required in resolving a work product immunity question.

The insurer must simply be prepared to familiarize himself with the test followed in the jurisdiction in which the claim is being investigated.

D. Investigation of the Insured's Claim.

In order for an insured to legitimately raise the work product doctrine it must maintain that while conducting its investigation it believed not only that it would eventually determine that it suffered a loss which is covered under its fidelity bond, but also that it had reason to believe that the insurer intended to deny its bond claim, and that it further believes that litigation would eventually ensue. This would seem to be a difficult argument to make in the majority of cases. This is precisely the basis of the district court's decision to overrule the insured's objection to producing its underlying claim file in *EDO Corp. v. Newark Insurance Co*.[99] In EDO Corporation the court recognized that a line should be drawn at the point when the insured receives notice that its claim has been denied. Before that time, the court reasoned, the insured "lacked a reasonable basis to anticipate litigation with the [insurers]."[100]

There are many cases which stand for the proposition that an insurance company's investigation of a claim is conducted in the ordinary course of business and thus *not* in anticipation of litigation.[101] These cases typically deal with property and casualty claims and thus are overly simplistic. The inquiry in each case must not be guided by the fact that investigations are typically performed - whether by the insurer or the insured - in connection with bond claims, but rather by focusing on whether there was a basis upon which the insurer did reasonably anticipate litigation resulting from the claim. Thus, in *Janicker v. George Washington University*[102] the district court explained as follows:

> The mere contingency that litigation may result is not determinative. If in connection with an accident or an event, a business entity in the ordinary

99. 145 F.R.D. 18, 24 (D. Conn. 1992).

100. *Id.*

101. *See, e.g., Harper v. Auto - Owner's Ins. Co.*, 138 F.R.D. 655 (S.D. ID. 1991); *Hawkins v. District Court*, 638 P.2d 1372, 1378 (Colo. 1982); *Langdon v. Champion*, 752 P.2d 999, 1004-1007 (Alaska 1988); *see also* Kurt A. Pasich and Jennifer Ann Semple, *The Work Product Doctrine in the Context of Insurance Coverage Disputes*, III COVERAGE 18, 19-20 (ABA Press 1992).

102. 94 F.R.D. 648, 650 (D.D.C. 1982).

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> course of business conducts an investigation for its own purposes, the result ing investigative report is producible in civil pretrial discovery.
>
> ….
>
> A more or less routine investigation of a possibly resistible claim is not sufficient to immunize an investigative report developed in the ordinary course of business…. While litigation need not be imminent, the primary motivating purpose behind the creation of a document or investigative report must be to aid in possible future litigation.

Although litigation may be a contingency when an insured hires a lawyer to investigate an actual or potential loss, litigation is typically is not the primary motivating purpose behind the investigation. Therefore, in most circumstances the work product doctrine will not be available to prevent production of a lawyer's investigation report and accompanying materials.

The logic behind application of the doctrine becomes clearer when it is recognized that the work product doctrine was developed as part of our adversary system. As Justice Jackson noted in his concurring opinion in *Hickman v. Taylor*:

> Counsel for the petitioner candidly said on argument that he wanted this information to help prepare himself to examine witnesses, to make sure he overlooked nothing. He bases his claim to it in his brief on the view that the Rules were to do away with the old situation where a lawsuit developed into 'a battle of wits between counsel.' But a common law trial is and always should be an adversary proceeding. Discovery was hardly intended to enable a learned profession to perform its functions either without wits or with wits borrowed from the adversary.[103]

An insurer's investigation of a fidelity bond claim is not and never was intended to be an adversary proceeding. Unlike discovery in a lawsuit, an insurer's investigation of a claim is indeed intended to enable it to perform its functions "on wits borrowed from" the insured.[104] Thus, except in those limited situations where the information sought from the insured was prepared specifically in anticipation of litigation it makes no sense to keep it from the insurer on the basis of the work product doctrine.

E. Anticipation of Litigation With Others.

Occasionally an insured will argue that it cannot provide the insurer various documents because they were prepared, not in anticipation with the insurer, but instead in anticipation with the allegedly dishonest employee or other third parties involved in the insured's loss. Courts are split on whether

103. 329 U.S. at 516.

104. *Id.*

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documents are protected under such circumstances. Some courts hold that the work product doctrine applies only to documents prepared in anticipation of the claims at issue, and that documents prepared in anticipation of another lawsuit are freely discoverable.[105] Both *Hickman v. Taylor* and Rule 26 leave this issue open. However, following the U.S. Supreme Court's decision in *Federal Trade Commision v. Grolier, Inc.*,[106] most lower federal courts have liberally applied the doctrine regardless of whether the documents were prepared in anticipation of the subject lawsuit, or another.[107] Not all states, however, follow this liberal rule. Therefore, this is again an issue that the insurer must consider in light of applicable state law.

F. Offensive use of doctrine.

As with offensive use of the attorney-client privilege, offensive use of the work product doctrine also results in a waiver of the right to raise the doctrine.[108] *Charlotte Motor Speedway, Inc*.[109] contains a good discussion of the offensive use doctrine where an objection to discovery has been raised on the basis of the work product doctrine. Essentially, as with offensive use of the attorney-client privilege, when the insured places activities of its counsel at issue, it is considered to be fundamentally unfair to shield such activities from the insurer. As the court explained:

> [T]he activities of the counsel employed by [the insured] in the underlying action are directly in issue here for they are the only means of discovering whether [the insured] met its obligations under the insurance contract and reached its settlement agreement in good faith. The settlement materials are therefore critical to [the insurer's] defense. As the courts which have addressed this issue indicate, these circumstances warrant the application of a narrow exception to Rule 26(b)(3) for the information from which protection is sought is directly in issue.[110]

In summary, as with the attorney-client privilege, the work product doctrine should seldom serve as support for an insured's refusal to provide information concerning its loss to the insurer. Very seldom will the insured be conducting an investigation with the legitimate belief that the insurer

105. *See* WRIGHT & MILLER, *supra* note 97, § 2024, at 350, *and cases cited therein*.

106. 462 U.S. 19, 26 (1983)(holding that for purposes of requests under the Freedom of Information Act protection under the doctrine existed with respect to subsequent litigation whether or not the later case was "related" to the case in which the material was originally prepared).

107. WRIGHT & MILLER, *supra* note 97, § 2024, at 351, *and cases cited therein*.

108. *See e.g., Charlotte Motor Speedway, Inc. v. Int. Ins. Co*., 125 F.R.D. 127 (M.D.N.C. 1989); *Waste Management, Inc. v. Int. Surplus Lines Inc.*, 560 N.E.2d 1093 (Ill. App. Ct. 1990), *aff'd in relevant part*, 579 N.E. 2d 322 (Ill. 1991).

109. 125 F.R.D. at 131.

110. *Id.* at 131.

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will deny a claim that might or might not eventually be submitted, and thus end up in litigation with the insurer.

III. COOPERATION CLAUSE; THE CORNERSTONE OF THE RELATIONSHIP

Regardless of whether the attorney-client privilege or work product doctrine apply to an insured's request for information, because almost all modern fidelity bonds contain cooperation clauses, there will be very few instances when the insured should be permitted to withhold from the insurer any documents or other information relevant to the insurer's investigation of the insured's claim. Although fidelity bond insurers have always expected their insureds to cooperate during their insurer's investigation of a claim, they had mixed results without the benefit of a cooperation clause. Thus, when the standard form Banker's Blanket Bond was revised in 1980, a cooperation clause was added.[111] The provision remained when the standard form bond was revised in 1986, and now reads as follows:

> (d) Upon the Underwriter's request and at reasonable times and places designated by the Underwriter the Insured shall:
>
> (1) submit to examination by the Underwriter and subscribe to the same under oath;
>
> (2) produce for the Underwriter's examination all pertinent records; and
>
> (3) cooperate with the Underwriter in all matters pertaining to the loss.
>
> (e) The Insured shall execute all papers and render assistance to secure to the Underwriter the rights and causes of action provided herein. The Insured shall do nothing after discovery of loss to prejudice such rights or causes of action.[112]

Somewhat surprisingly, there is a dearth of decisions directly addressing the cooperation clause in financial institution bonds.[113] However, there are

111. Bankers Blanket Bond, Standard Form No. 24 (revised July 1980), *reprinted in* STANDARD FORMS OF THE SURETY ASSOCIATION OF AMERICA (SURETY ASS'N OF AMERICA).

112. Financial Institution Bond, Standard Form No. 24 (revised Jan. 1986), *reprinted in* STANDARD FORMS OF THE SURETY ASS'N OF AMERICA (SURETY ASS'N OF AMERICA).

113. *See Mercedes-Benz of N.A., Inc. v. Hartford Accid. & Indemn. Co*., 974 F.2d 1342, 1992 W.L. 207892, *3 (9th Cir. 1992) (implicitly recognizing that cooperation clause in a fidelity bond is a condition precedent to coverage, while holding that it is not a promise which entitles insurer to assert affirmative claim for damages if breached)(unpublished disposition; opinion available only on electronic data base).

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numerous decisions enforcing similar provisions in fire policies, and more recently, environmental and directors and officer's insurance policies. These decisions, particularly those enforcing the clause over an insured's objection to providing documents or to submitting to a sworn examination on the basis of the Fifth Amendment of the United States Constitution, are persuasive authority for enforcement of the cooperation clause in fidelity bonds.

A. Historical Perspective

Since the early 1900s the standard form fire insurance policy in use in the United States has contained a cooperation clause requiring the insured to submit to an examination under oath, and to produce all pertinent documents. The standard clause in such policies provides:

> The insured, as often as may be reasonably required, shall exhibit to any person designated by this company all that remains of any property herein described and submit to examinations under oath by any person named by this company, and subscribe the same; and, as often as may be reasonably required, shall produce for examination all books of account, bills, invoices and other vouchers, or certified copies thereof if originals be lost, at such reasonable time and place as may be designed by this company or its representative and shall permit extracts and copies thereof to be made.[114]

The purpose of the cooperation clause in fire policies is to enable the insured to thoroughly investigate losses where either the cause of the fire is at issue, or the loss appears to have been exaggerated by the insured.[115]

As early as 1884, the United States Supreme Court recognized the sweeping nature of cooperation clauses, reasoning:

> The object of the provisions in the policies of insurance . . . was to enable the company to possess itself of all knowledge, and all information as to other sources and means of knowledge, in regard to the facts, material to their rights, to enable them to decide upon their obligations, and to protect them against false claims. And every interrogatory that was relevant and pertinent in such an examination was material, in the sense that a true answer to it was of the substance of the obligation of the assured.[116]

The Court's reasoning in *Claflin* is persuasive. The cooperation clause clearly entitles the insurer to discovery of all facts surrounding a loss, and arguably extends even further, to the opinions of investigators and counsel. Although insureds have attempted to avoid the reach of cooperation clauses, their efforts have been largely unsuccessful.

114. James Knoll, *Examinations Under Oath: The Insurance Company's Best Friend*, 16 FORUM 777 (Spring 1981).

115. *Id.* at 778.

116. *Claflin v. Commonwealth Ins. Co.*, 110 U.S. 81, 94-95 (1884).

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B. Courts Have Consistently Enforced the Cooperation Clause In Fire Cases

Since the Supreme Court's holding in *Clafin* over a century ago, courts have consistently enforced cooperation clauses in liability policies.[117] The logic behind enforcing cooperation clauses today has changed very little from the first cases surrounding the clause. One court has opined:

> The reason for including a cooperation clause in the policy for conducting examinations pursuant to it is obvious enough. The company is entitled to obtain, promptly and while the information is still fresh, 'all knowledge, and all information as to other sources and means of knowledge, in regard to the facts, material to their rights to enable them to decide upon their obligations, and to protect them against false claims. And every interrogatory that [is] relevant and pertinent in such an examination [is] material, in the sense that a true answer to it [is] of the substance of the obligation of the assured.'[118]

Application of the cooperation clause is almost commonsensical. For instance, in *Ausch v. St. Paul Fire & Marine Insurance Co.*[119] the insured refused several requests to appear at an examination under oath and to supply information regarding his financial status in violation of the cooperation clause. The court concluded:

> Moreover, the plaintiffs have not satisfactorily explained Abbey's failure to provide the defendant with material and relevant documentation relating to its financial status at the time of the fire, in further breach of the cooperation clause. This is not a case where the insured's attempt to comply has fallen short through some 'technical and unimportant omissions or defects,' to warrant a finding that 'substantially performed its obligation to cooperate.' Rather, the record is indicative of a pattern of noncooperation and avowed obstruction.[120]

C. Fifth Amendment Cases

An occasional issue in fire cases is whether the insured intentionally started the fire. In such cases the insured might be reluctant to answer ques-

117. *See, e.g.*, *Powell v. USF&G Co.*, 88 F.3d 271 (4th Cir. 1996); *Pervis v. State Farm Fire & Cas. Co.*, 901 F.2d 944 (11th Cir. 1990), *cert. denied*, 498 U.S. 899 (1990); *Tillman v. Great American Indem. Co.*, 207 F.2d 588 (7th Cir. 1953); *Pisa v. Underwriters at Lloyds,* 788 F. Supp. 283, 285-86 (D.R.I.) *affirmed*, 966 F.2d 1440 (1st Cir. 1992); *Kisting v. Westchester Fire Ins. Co.*, 290 F. Supp. 141, 145-48 (W.D. Wis. 1968), *aff'd*, 416 F.2d 967 (7th Cir. 1969); *Schoenfeld v. N.J. Fidelity & Plate Glass Ins. Co.*, 197 N.Y.S. 606 (N.Y. App. Div. 1922); 8 J. APPLEMAN, INSURANCE LAW AND PRACTICE, § 4771 (1981).

118. *Dymo-Bite, Inc. v. The Travelers Cos.*, 439 N.Y.S.2d 558, 80 (1981) (*quoting Clafin v. Commonwealth Ins. Co.*, 110 U.S. 81 (1884)).

119. 511 N.Y.S.2d 919 (N.Y. App. Div. 1987).

120. *Id.* at 925 (citations omitted).

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tions under oath, particularly where a criminal investigation has begun. As a result, the insured will often assert his fifth amendment right against self-incrimination in response to the insurer's request for a sworn statement or the production of financial records. Courts considering this issue have consistently held that the fifth amendment privilege against self-incrimination does not negate an insurance policy's duty to cooperate.[121]

Thus, in *Pervis v. State Farm Fire and Casualty Co.*,[122] the trial court granted summary judgment in favor of State Farm for violation of the policy's cooperation clause due to the insured's refusal on the basis of the fifth amendment. On appeal the insured argued that the Court in effect forced him to forfeit his claim for insurance, thereby penalizing him for exercising his fifth amendment privilege, and thereby violating his right to due process.[123] The Eleventh Circuit disagreed:

> Pervis cannot assert the privilege and maintain this action. Pervis seeks to recover proceeds based on the insurance contract to which he was a party; he must be held to the express terms of his agreement. He is not compelled to incriminate himself. He is, however, bound by the provisions to which he stipulated when he signed the insurance agreement and cannot expect State Farm to perform its obligations under the contract ... without compliance on his part.[124]

Similarly, in *Aetna Casualty & Surety Co. v. State Farm Mutual Auto Insurance Co.*[125] the district court held:

> More importantly, Aetna's argument that a Fifth Amendment privilege trumps the insurance policy's duty to cooperate requirement falls of its own weight. A person may not be penalized for asserting the Fifth Amendment privilege against self incrimination, but that does not mean that if a person refuses to make a statement in a civil proceeding that the failure to provide evidence may not have adverse consequences.[126]

At the heart of this reasoning is the nature of the contractual obligation at issue. Thus, in *Mello v. Hingham Mutual Fire Insurance Co.*[127] the court reasoned:

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121. *See, e.g., Powell v. United States Fidelity and Guar. Co.*, 88 F.3d 271 (4th Cir. 1996); *Pervis v. State Farm Fire and Cas. Co.*, 901 F.2d 944 (11th Cir. 1990), *cert. denied*, 498 U.S. 899 (1990); *Aetna Cas. and Surety Co. v. State Farm Fire and Cas. Co.*, 771 F. Supp. 704 (W.D. Penn. 1991); *Mello v. Hingham Mutual Fire Ins. Co.*, 656 N.E.2d 1247 (Mass. 1995).

122. 901 F.2d 944 (11th Cir. 1990).

123. *Pervis*, 901 F.2d at 946.

124. *Id*. at 947 (emphasis added).

125. 771 F. Supp. 704 (W.D. Pa. 1991).

126. *Id.* at 707.

127. 656 N.E. 2d 1247, 1250 (Mass. 1995).

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> A person may not seek to obtain a benefit or to turn the legal process to his advantage while claiming the privilege as a way of escaping from obligations and conditions that are normally incident to the claim he makes. The principle holds true particularly where the benefit he seeks is from another private party, who is being asked to make good on its obligation forgoing the countervailing advantages that were part of the bargain.

In addressing Mello's Fifth Amendment defense, the court went on to note:

> Where the undesirable consequences arise from the claimant's own voluntary actions, the privilege against self-incrimination cannot be used to extricate the claimant from such a dilemma of his own making…. Thus it is not by the Commonwealth or by Hingham that the plaintiff 'is compelled to… furnish evidence against himself,' but by his own contractual undertaking.[128]

More recently, in *Powell v. United States Fidelity & Guaranty Co.*[129] the Fourth Circuit reasoned:

> Any argument of the Powells, that giving the provision such a broad scope would effectively abnegate their right against self-incrimination, is unavailing; they may avoid incriminating themselves by refusing to submit to relevant requests made by USF&G under the policy provision, although to do so may ultimately cost them insurance coverage under the terms of the contract for which they and USF&G bargained.[130]

In short, most courts have found the cooperation clause to be the result of a contractual relationship willfully entered into by the parties. Therefore, choosing to breach this obligation in order to protect some other interest has been viewed as just that, a choice, rather than a Constitutional deprivation. The power of the cooperation clause is thus impressive. It is consistently upheld by courts in this context, despite the criminal implications which are inherently present. It is logical then, that the courts will afford similar treatment to objections based upon the attorney-client privilege and the work product doctrine.

D. The Cooperation Clause in Non-Fire Cases

More recently courts have afforded similar treatment to cooperation clauses in cases involving environmental and directors and officers' insurance policies. For instance, in *Waste Management, Inc. v. International Surplus Lines Insurance Co.*,[131] the insured sought indemnification under

128. *Id.* at 1251.

129. 88 F.3d 271 (4th Cir. 1996).

130. *Id.* at 274.

131. 579 N.E.2d 322, (Ill. 1991).

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an environmental insurance policy for amounts paid in settlement of a toxic tort lawsuit. During discovery in the lawsuit the insurer requested production of the insured's defense counsel's files in the underlying litigation. Some of these files were produced, but others were withheld on the basis of the attorney-client privilege and the work product doctrine. The insurer responded that because of the cooperation clause of the environment indemnification policy the insured had no right to withhold the files. The court agreed, reasoning as follows:

> The scope of the duties imposed upon an insurer and its insured are defined and controlled by the terms of the insurance contract. Any condition in the policy requiring cooperation on the part of the insured is one of great importance, and its purpose should be observed.
>
> ….
>
> Here, the cooperation clause imposes a broad duty of cooperation and is without limit or qualification. It represents the contractual obligations imposed upon and accepted by insureds at the time they entered into the agreement with insurers. In light of the plain language of the cooperation clause in particular, and language in the policy as a whole, it cannot seriously be contended that insureds would not be required to disclose contents of any communications they had with defense counsel representing them on a claim for which insurers had the ultimate duty to satisfy.[132]

A similar case also involving an environmental policy is *EDO Corp. v. New York Insurance Co.*,[133] in which the court overruled the insured's objection to producing its underlying claim file. The court specifically found that the insured had no reasonable expectation of privacy under the circumstances due to the cooperation clause in its policy and because of an implied duty of good faith and fair dealing.[134]

Similarly, in *First Fidelity Bancorporation v. National Union Fire Insurance Co. of Pittsburgh, Pa.*[135] the court was faced with a similar issue in the context of a directors and officers' insurance policy. In attempting to determine the reasonableness of a settlement of the underlying lawsuit against the directors and officers of First Fidelity Bancorporation, National Union sought to obtain essentially all documents generated in connection with the underlying litigation, including otherwise privileged documents generated by Fidelity's lawyers. The court found that the cooperation clause of National Union's policy was dispositive of the issue, reasoning:

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132. *Id.* at 327-328.

133. 145 F.R.D. 18 (Conn. 1992).

134. *Id.* at 21.

135. No. 90-1866, 1992 WL 55742 (E.D. Pa. March 13, 1992).

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> Additionally, there is a sharp dispute over whether the Policy's cooperation clause requires disclosure of the Privileged Discovery. I find that as to the sophisticated parties involved in the present case, the Policy's language is clearly all encompassing and would normally include privileged documents, for otherwise an insurer could not reasonably assess the proposed settlement.[136]

The reasoning of the courts in the above cases is persuasive. Just as the parties in those actions are sophisticated, the parties to a fidelity bond also are sophisticated. Thus, the parties' voluntary agreement should be enforced by requiring insureds to produce all relevant documents to the insurer during its investigation of the claim.

E. Examination under oath

There is little dispute that a failure to submit to a sworn statement alone constitutes a breach of the cooperation clause of a policy negating coverage.[137] Also, if an insured appears but refuses to answer all relevant questions it is tantamount to not appearing at all. As one court has noted:

> We agree that when an insured ostensibly submits to an EUO, but says she does not remember relevant information that in fact she does, or claims that relevant documents have been destroyed when in fact they were not, she has in effect refused to submit to an examination.[138]

In conclusion, the cooperation clause now found in most fidelity bonds is a powerful tool in the hands of the insurer. Although it remains untested in the context of a fidelity bond claim, there is a plethora of persuasive decisions in environmental, directors and officers, and auto policy cases, (particularly those enforcing the clause despite objections based upon the fifth amendment). These cases are persuasive authority for the proposition that the insured must provide the fidelity bond insurer with full cooperation, including sitting for a sworn examination and providing all relevant documents, including those generated by the insured's lawyer concerning upon the facts and circumstances surrounding the insured's loss.

IV. OBTAINING CUSTOMER LOAN FILES

Most fidelity bond claims involve, to one extent or another, information and files pertaining to the insured's customer. The typical claim involving a financial institution will involve customer loans or forged checks. Claims

136. 1992 WL 55742, at *2.

137. *Wood v. Allstate Ins. Co*., 21 F.3d 741 (7th Cir. 1994); *U.S. Fidelity & Guar. Co. v. Wiggington*, 964 F.2d 487 (5th Cir. 1992); *Rosenthal v. Prudential Prop. and Cas. Ins. Co*., 928 F.2d 493 (2nd Cir. 1991); *Purvis v. State Farm Fire and Casualty Co*., 901 F.2d 944 (11th Cir.), *cert. denied*, 498 U.S. 899 (1990).

138. *Wood v. Allstate Ins. Co.*, 21 F.3d at 746.

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involving other insureds also involve customer accounts, often extending to sensitive, although typically not privileged, information pertaining to the customer. In these claims insureds have grown increasingly cautious in producing their customers' files due to concerns of retaliatory litigation by the customers. Although the insured's concern in such circumstances is understandable, there will be few claims where the onus should not be upon the insured to produce all relevant files.

A. No Expectation of Privacy Under Federal Law

Occasionally a financial institution will maintain that it is not permitted to provide an insurer with its customer's financial records because it violates the customer's Constitutional right to financial privacy in their bank records. Very clearly, however, no such right exists. In *United States v. Miller*,[139] the United States Supreme Court found that the Fourth Amendment of the United States Constitution does not provide a constitutionally protected privacy interest in bank records.[140] Rather, bank records contain information voluntarily conveyed to banks and exposed to bank employees in the ordinary course of business. Thus, a customer does not have a legitimate expectation of privacy in such documents, at least from a constitutional standpoint.[141] Nor does the Federal Right of Privacy Act of 1978[142] affect the disclosure of bank records in civil proceedings.[143] While the Act preempts conflicting state law, it applies only to federal government authorities. Accordingly, a bank may not justify its refusal to provide records to an insurer on the basis of the statute or some other undefined Constitutional right to financial privacy.[144] The same reasoning obviously also applies to customers of other businesses.

B. State Law

While federal law does not provide protection to bank customers in a civil context, state law does. Most state courts considering the issue have found that banks at least implicitly agree to keep their customers' records confidential.[145] The seminal case on this issue, and one repeatedly cited by

139. 425 U.S. (1976).

140. *Id.* at 443.

141. *Id.*; *see also O'Neill v. Q.L.C.R.I., Inc.* 750 F. Supp. 551, 556 (D.R.I. 1990).

142. 12 U.S.C. § 3401, *et seq.* (1978).

143. *See Snierson v. Chemical Bank*, 108 F.R.D. 159, 161-162 (D. Del. 1985).

144. *See Clayton Brokerage Co. v. Clement*, 87 F.R.D. 569, 570-571 (Md. 1980).

145. *See, e.g., Indiana Nat'l. Bank v. Chapman*, 482 N.E.2d 474, 480 (Ind. Ct. App. 1985); *Suburban Trust Co. v. Waller*, 408 A.2d 758, 762-65 (Md. Ct. App. 1979); *Graney Development Corp. v. Taksen*, 400 N.Y.S.2d 717, 719 (N.Y. Sup. Ct. 1979); *Richfield Bank & Trust Co. v. Ogren*, 244 N.W.2d 648, 651 (Minn. 1976); *Milohnich v. First Nat'l Bank of Miami Springs*, 224, So.2d 759, 760-61 (Fla. Ct. App. 1969); *Peterson v. Idaho First Nat'l Bank*, 367 P.2d 284, 290 (Idaho 1961).

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courts, is the English decision in *Tuornier National Prudential and Union Bank of England*.[146] In *Tuornier* the plaintiff failed to make good on a draft written on his account to a bookmaker. The bank called his employer and disclosed that one of Tuornier's checks had been made out to a bookie. As a consequence, Tuornier was fired, and he later sued the bank. The court held that the bank had breached an implied contract not to disclose Tuornier's financial information, reasoning as follows:

> The court will only imply terms which must necessarily have been in the contemplation of the parties in making the contract. Applying this principal to such knowledge of life as a judge is allowed to have, I have no doubt that it is an implied term of a banker's contract with his customer that the bank shall not disclose the account, or transactions relating thereto, of his customer….[147]

The Idaho Supreme Court repeated the rule now followed by most American courts:

> It is implicit in the contract of the bank with its customer or depositor that no information may be disclosed by the bank or its employees concerning the customer's or depositor's account, and that unless authorized by law or by the customer or depositor, the bank must be held liable for breach of the implied contract.[148]

Other courts have reached the same results, although on different grounds, including constitutional guarantees,[149] the existence of a fiduciary relationship[150] or because the relationship between the bank and its customer is one of principal and agent.[151]

Most courts considering the issue frame it in terms of an obligation to keep confidential information pertaining to the customers' *accounts* and *deposits*, at least implicit in this statement of the law is that *loan information which* does not touch upon the customer's *accounts* is not confidential. Indeed, this was the holding by the court in *Graney Development Corp. v. Taksen*.[152] In *Graney* a bank officer informed officers at another bank, as well as an individual who intended to sell property to the plaintiff on credit, that the plaintiff had failed to repay a loan at the bank. As a result the bank

146. 1 K.B. 461 (1923).

147. *Id.* at 480.

148. *Peterson v. Idaho First Nat'l Bank*, 367 P.2d 284, 290 (Idaho 1961).

149. *Zimmermann v. Wilson*, 81 F.2d 847, 849 (3rd Cir. 1936); *Brecks v. Smith*, 146 A. 34, 36 (N.J. 1929); *see also Alva State Bank & Trust Co. v. Dayton*, 755 P.2d 635, 638 (Ok. 1988).

150. *United States v. First Nat'l Bank of Mobile*, 67 F.Sup. 616, 624 (S.D. Ala. 1946).

151. *Brecks v. Smith*, 146 A. at 36; *see also Alva State Bank & Trust v. Dayton*, 755 P.2d at 639.

152. 400 N.Y.S.2d 717 (N.Y. Supp. Ct. 1978).

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and the property owner refused to transact business with the plaintiff. Plaintiff thereafter sued on theories of slander, breach of an implied agreement that the bank would not disclose information about plaintiff's financial affairs, and negligence. After reviewing *Tuornier* and other applicable cases, the court found that the implied agreement of confidentiality did not extend to loans:

> [T]he information revealed by the bank did not concern the plaintiff's *deposit* with the bank; it concerned a *loan* made by the bank. As to that *loan*, the relation between the bank and the plaintiff was solely that of creditor and debtor. The information the bank imparted about the state of plaintiff's *loan* was not information received in its capacity as agent for a *depositor*; it was information it obtained as a party to a *loan* agreement. It was not information that the borrower would normally expect would be kept confidential. One who defaults on his debts owed to a merchant cannot expect that its default will be kept a secret. Although the creditor who publishes his debtor's defaults to the public at large may be liable for beach of privacy, he will not be liable (in the absence of malice) if he divulges the default not to the public at large, but privately to selected individuals.[153]

Although it can be argued that by revealing that its customer had defaulted on a loan it was, in essence, revealing account information to others, the decision at least raises an interesting issue. Do loan documents contain the type of information over which a customer normally has a reasonable expectation of privacy? Arguably much of the information is not regarded as confidential, such as correspondence between the bank and its customer, or information from the bank's collateral file not containing information about the borrower.

1. Exception to the Rule.

The duty to maintain confidentiality over a customer's records is not absolute. The most obvious exception is when a financial institution discloses information in response to a law enforcement or judicial inquiry.[154] In these cases the courts generally recognize that the duty of confidentiality must give way in the face of legal compulsion.[155] There is also support for the proposition that the bank may disclose the customer's information when the disclosure of such information is *in the public interest* or where the *interest of the bank* requires such disclosure.[156] This exception, which dates back to the original decision in *Tuornier*,[157] is not well defined. And, many

153. *Id.* at 720.

154. *See, e.g., Indiana Nat'l Bank v. Chapman*, 482 N.E.2d 474, 482-483 (Ind. 1985).

155. *Id.; Barnett Bank v. Hooper*, 498 So.2d 923, 925 (Fla. 1986).

156. *Indiana Nat'l Bank*, 482 N.E.2d at 41-42.

157. 1 K.B. at 473.

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courts challenge the exception based upon the bank's interest as being too vague. Thus, for instance, in *Suburban Trust v. Waller*,[158] the court held:

> Presently, the vital information placed within the bank's control presents potential sources of use as well as abuse. Courts have not hesitated to find that a bank implicitly warrants to maintain in strict confidence, information regarding its depositor's account.
>
> We specifically reject both the *Tuornier* four-fold classification of qualifications to the implied contractual obligation of confidentiality on a bank to its depositors . . . because we believe that [*Tuornier*] confers upon a bank entirely too much discretion.

Nevertheless, records of a customer who is directly implicated in a dishonest scheme should be made available to an insurer. First, to the extent the customer is implicated in the scheme, he cannot have any expectation that his records would remain confidential. Certainly to the extent that there is implicit in the relationship between the bank and its customer an agreement to maintain the customer's records as confidential, it is also understood that, to the extent the customer has been acting dishonestly, the bank may disclose pertinent records to the extent necessary to protect its interest. While this exception would clearly extend to disclosing records to law enforcement authorities, it should also extend to providing records to insurers in an effort to recover or mitigate the bank's loss through insurance.

C. STATE STATUTES

Numerous states have enacted financial privacy statutes to control the disclosure of bank customers' financial records to third parties, although most statutes apply to only existing litigation.[159] The state statutes are generally worded more broadly than the federal Act and focus on the responsibilities of the financial institution and the procedures that must be followed to obtain the records, rather than addressing privacy issues. The statutes as a whole set forth a method by which a third party can seek to obtain depositors' financial records and set forth conditions that must be met prior to the release of such information by the financial institution.[160]

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158. 408 A. 2d 758, 764 (Md. Ct. App. 1979).

159. *See, e.g.*, Ala. Code, § 5-5A-43 (1980); Conn. Gen. Stat., § 36a-43 (1995); Ga. St. Ann., § 7-1-360 (1989); La. Rev. Stat. Ann., Title 6, § 333 (1995); Tenn. Code Ann., § 45-10-101 *et seq*. (1983); Tex. Civ. Prac. & Rem. Code, § 30.007 (1995).

160. *See Ouachita Nat'l Bank v. Palowsky*, 554 So.2d 108, 111 (La. App. 1989) ("[t]he exclusive method by which a litigant may obtain customer records from a bank is found in LSA-R.S. 6:333."); *Alva State Bank and Trust Co. v. Dayton*, 755 P.2d 635, 636 (Ok. 1988) ("[o]ur Financial Privacy Act. . . sets out the exclusive lawful means of obtaining [bank customer] records….").

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For example, under § 7-1-360 of the Georgia Code, the financial institution's responsibilities are as follows:

> (a) Neither shall any financial institution be required to disclose or produce to third parties, or permit third parties to examine any records pertaining to a deposit account, loan account, or other banking relationship except:
>
> (1) where the financial institution itself is a proper or necessary party to a proceeding in a court of competent jurisdiction.
>
> (2) where the records of accounts or other customer records are requested through subpoena or other admini-strative process issued by a state, federal, or local administrative agency having competent jurisdiction over the depositor or other customer.

Most statutes are similar to the Georgia Code in that they allow third parties access to bank records once litigation has begun, as long as certain procedures are followed. If the subpoena appears valid on its face, the bank cannot be held liable for complying with it.[161] However, the financial institution may contest the subpoena in good faith, as with any other subpoena issued under state law.[162]

In addition to the payment of costs, the majority of state statutes require that the requesting party provide notice to the customer(s) whose records are to be reviewed and provide proof of service of such notice as required under local law. State law dictates the rights of the customer to object, waive objections to the request, or both. For example, under Texas law, if the requesting party does not receive written consent from the customer, the requesting party may file a motion for *in camera* inspection to request the court to inspect the records and produce those documents deemed relevant.[163] On the other hand, under Louisiana law the bank may disclose financial records so long as it has not received written notice from a customer that the customer has taken legal action to enjoin or otherwise restrain the release of financial records.[164] However, because each state's statute has its own unique characteristics, the insurer should study the applicable statute carefully before requesting records.

V. OBTAINING LAW ENFORCEMENT RECORDS

An often times valuable source of information to the insurer is records of law enforcement agencies, including the Federal Bureau of Investigation.

161. Ill. General Statues § 36-91.

162. *See State Dep't of Revenue v. Moore*, 722 S.W.2d 367, 376 (Tenn. 1986).

163. Tex. Civ. Prac. & Rem. Code § 30.007(e).

164. La. Rev. Stat. § 6:333(C)(3).

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Because federal criminal statutes are typically implicated in fidelity bond claims involving financial institutions, the FBI often conducts an independent investigation of an allegedly dishonest bank employee. In such cases the FBI records can often provide valuable information, particularly where the investigation was completed sometime before the insurer was provided notice of the insured's loss. A logical question in such cases is whether discovery occurred prior to inception of the insurers' bond, or whether the insured's notice of loss was given in a timely manner.

Initially, there is no prohibition known to the author to prevent the information provided to such agencies, such as Report of Apparent Crime forms, from being turned over to the insurer. However, at least with respect to the FBI, there is also no mechanism available to the insurer to obtain government records without a subpoena. Thus, while law enforcement agencies will occasionally provide the insurer information from their files on a voluntary basis, they can only be required to do so through a subpoena. With respect to the FBI, there is a specific regulation permitting access to their records.

The mechanism for obtaining information from the FBI's files, and even for deposing employees of the FBI, is set forth in 28 C.F.R. § 16.21, *et seq.*[165] Section 16.21 sets forth procedures to be followed concerning the production of "material contained in the files of the Department, any information or relating material contained in the files of the Department, or any information acquired by any person while such person was an employee of the Department…."[166] In order to depose a person involved in the FBI's investigation the insurer is required to provide an affidavit or statement setting forth a summary of the testimony sought and its relevance to the proceeding.[167] If documents or other information are sought, the insurer should submit both a list of the information sought together with a statement of its relevance to the proceeding.[168] Section 16.26(a) sets forth relatively simple factors to be analyzed in determining whether the requested discovery will be allowed:

> 1. Whether such disclosure is appropriate under the rules of procedure governing the case or matter in which the demand arose; and
>
> 2. Whether disclosure is appropriate under the relevant substantive law concerning privilege.

165. 28 C.F.R. § 16.21 *et seq*. (1996).

166. *Id.* at § 16.21(d).

167. *Id.* at § 16.22(d).

168. *Id.*

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The regulations also prohibit disclosure of certain specific information, including the following:

1. Information which would violate a statute, such as the income tax law;

2. Information which would violate a specific regulation;

3. Information which would reveal classified information;

4. Information which would reveal a confidential source or informant;

5. Information which would reveal investigatory records compiled for law enforcement purposes, and which would interfere with enforcement proceedings; and

6. Information which would improperly reveal trade secrets without the owner's consent.[169]

In conclusion, in most cases the insurer will be able to obtain, at a minimum, the facts revealed by the FBI's investigation. State law should be reviewed to determine whether a similar mechanism exists for obtaining records of state or local law enforcement authorities.

VII. CONCLUSION

In conclusion, the relationship between the fidelity bond insurer and its insured is, and always has been intended to be, one of cooperation. The burden is squarely upon the insured to establish all necessary elements of its bond claim, and to provide the insurer with all documents necessary to do so. Furthermore, the insured is obligated to cooperate during the insurer's investigation of the claim. Objections based upon the attorney-client privilege or work product doctrine should be closely scrutinized as they will seldom apply. Even in those few instances where they are applicable, the cooperation clause of the bond will force the insured to make a decision between pursuing its claim or resting upon its objection, and therefore forfeiting its claim. Documents available to the insured should include a customer's records, notwithstanding financial privacy concerns, when those records are relevant to the insured's claim. Finally, relevant records of law enforcement authorities can often be of great assistance in the insurer's investigation, and in many cases will be available to the insurer if the requisite procedures are followed.

169. 28 C.F.R. § 16.26(b).

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