July 27, 2015

VIA HARD COPY MAIL

Honorable Tani Gorre Cantil-Sakauye
California Supreme Court
Office of the Clerk
350 McAllister Street, Room 1295
San Francisco, CA 94102

Re: Petition for Review in *Centex Homes v. St. Paul Fire and Marine Ins. Co. and St. Paul Mercury Co.* (Case No. E060057, Court of Appeal, Fourth District).

Dear Chief Justice Tani Gorre Cantil-Sakauye and Honorable Associate Justices:

Pursuant to Rule 8.500(g) of the California Rules of Court, United Policyholders ("UP") and Consumer Attorneys of California ("CAOC") respectfully request that the California Supreme Court grant review in *Centex Homes v. St. Paul Fire and Marine Ins. Co. and St. Paul Mercury Co.* (Case No. E060057, Court of Appeal, Fourth District, 2014). Review is needed in order to clarify the standard for appointing independent "*Cumis"* counsel in insurance disputes. *San Diego Federal Credit Union v. Cumis Ins. Society, Inc.* (1984) 162 Cal.App.3d 358.

I. STATEMENT OF INTEREST

UNITED POLICYHOLDERS

United Policyholders ("UP") is a non-profit consumer advocacy organization dedicated to helping preserve the integrity of the insurance system. UP serves as a voice and an information resource for consumers in all 50 states and is based in San Francisco, California. UP was founded in 1991 after the Berkeley/Oakland Hills Firestorm to assist homeowners. UP's work is supported by donations, grants, and volunteer labor. UP does not sell insurance or accept funding from insurance companies.

While much of UP's work is aimed at helping individuals and businesses purchase appropriate insurance and repair, rebuild, and recover after disasters through its *Roadmap to Preparedness* and *Roadmap to Recovery Programs*, through its *Advocacy and Action Program*, UP engages with regulators, including the California Department of Insurance and Commissioner Dave Jones, other public officials, academics, and various stakeholders in connection with legal and marketplace developments relevant to all policyholders and all lines of insurance. UP's Executive Director is an official consumer representative to the National Association of Insurance Commissioners and an Adviser to the American Law Institute's Restatement of the Law of Liability Insurance Project where the standard for *Cumis* counsel has been discussed at length.

A diverse range of individual and commercial policyholders throughout the U.S. regularly communicate their insurance concerns to UP which allows UP to submit amicus curiae briefs to assist state and federal courts decide cases involving important insurance principles. UP has filed *amicus curiae* briefs in more than 360 cases throughout the U.S. since the organization's founding in 1991. UP's *amicus curiae* brief was cited in the U.S. Supreme Court's opinion in *Humana, Inc. v. Forsyth*, 525 U.S. 299 (1999) and arguments from UP's *amicus curiae* brief were cited with approval by the this Court in *Vandenburg v. Superior Court* (1991) 21 Cal. 4th 815.[1] UP submitted a letter supporting review (denied) of *Federal Ins. Co. v. MBL, Inc.* (2013) 219 Cal.App.4th 29, a case which also (wrongly) addressed the standard for independent counsel.

CONSUMER ATTORNEYS OF CALIFORNIA

Founded in 1962, The Consumer Attorneys of California ("CAOC") is a voluntary non-profit membership organization of over 3,000 consumer attorneys practicing in California. Its members predominantly represent individuals subjected to personal injuries, insurance bad faith, consumer fraud, and unlawful employment practices. CAOC has taken a leading role for 50 years in advancing and protecting the rights of injured victims, consumers and employees in both the courts and in the Legislature. CAOC therefore has a substantive interest in the cases that interpret and apply statutes and the common law to insurance contracts and tort actions involving workers and consumers.

CAOC has a long history of participating as amicus curiae in significant cases involving insurance and tort claims, including *Essex Ins. Co. v. Five Star Dye House, Inc.,* (2006) 38 Cal.4th 1252 [upholding Brandt fees in subsequent assigned tort action for wrongfully withheld insurance benefits], *Cassim v. Allstate Ins. Co.* (2004) 33 Cal.4th 780 [upholding "Brandt" attorney fees to reimburse plaintiffs for a portion of shared contract/tort work to prove insurance contract in insurance bad faith action], *Haynes v. Farmers Ins. Exchange* (2004) 32 Cal.4th 1198 [holding limitation on permissive users in insurance contract not sufficiently conspicuous, plain and clear to be enforceable], Ennabe v. Manosa (2014) 58 Cal.4th 697 [holding noncommercial host potentially liable for the "sale" of alcohol to obviously intoxicated minor], Beacon Residential Community Association v. Skidmore, Owings & Merrill LLP (2014) 59 Cal.4th 568 [holding principal architect of new residential construction owes a duty of care to eventual homeowners], and *Vanhooser v. Superior Court* (2012) 206 Cal.App.4th 921 [allowing loss of consortium claim].

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[1] UP's website hosts all of its previous *amicus curiae* briefs on its website at: www.uphelp.org/amicus.

[2] *See, e.g., James No. 3 Corp. v. Truck Ins. Exch.* (2001) 91 Cal.App.4th 1093, 1101 ("For independent counsel to be requires, the conflict of interest must be significant, not merely theoretical, actual not merely potential."); *Gulf Ins. Co. v. Berger, Kahn et al.* (2000) (79 Cal.App.4th 114, 130 ("A mere possibility of an unspecified conflict does not require independent counsel. The conflict must be significant, not merely theoretical, actual, not merely potential."); *Swanson v. State Farm Gen. Ins. Co.* (2013) 219 Cal.App.4th 1153, 1164 ("To be disqualifying, the conflict of interest must be significant, not merely theoretical, actual, not merely potential); *Federal Ins. Co. v. MBL Inc., supra* ("For independent counsel to be required, the

The amicus committee of CAOC (then CTLA) also has participated over the years as amicus curiae in some of the landmark appellate decisions involving insurance, tort liability, collateral source and evidentiary issues involving pain and suffering, including *Crisci v. Security Ins. Co. of New Haven, Conn.* (1967) 66 Cal.2d 425 [breach of implied covenant of good faith and fair dealing exists and emotional distress damages are allowed when insurer unwarrantedly refuses offered settlement within policy limits], *Johansen v. California State Auto. Assn. Inter-Ins. Bureau* (1975) 15 Cal.3d 9 [failure to accept reasonable settlement offer by insurer breaches duty of good faith to insured], *Hrnjak v. Graymar, Inc.* (1971) 4 Cal.3d 725 [upholding the collateral source rule], *De Cruz v. Reid* (1968) 69 Cal.2d 217 [upholding collateral source rule], and *Beagle v. Vasold* (1966) 65 Cal.2d 166 [endorsing per diem arguments to jury for pain and suffering].

II. REASONS WHY GRANTING REVIEW IS PREFERABLE

A. *CUMIS* AND THE CALIFORNIA RULES OF PROFESSIONAL CONDUCT REQUIRE AN INSURER TO APPOINT INDEPENDENT COUNSEL WHEN AN ACTUAL OR POTENTIAL CONFLICT ARISES

The insured's right to independent counsel when a conflict arises between the insured and the insurer, both represented by the same defense lawyer, is a bedrock principle of California insurance law. The *Cumis* court, relying on the sound approach to conflicts among multiple clients taken by the Rule 3-310 of the California Rules of Professional Conduct, held that an insured's right to independent counsel is triggered by "actual" and "potential" conflicts. The *Cumis* court explained:

> "Cumis makes a distinction between "potential" and "actual" conflicts of interest which is invalid and unworkable. Recognition of a conflict cannot wait until the moment a tactical decision must be made during trial. It would be unfair to the insured and generally unworkable to bring in counsel midstream during the course of trial expecting the new counsel to control the litigation. Contrary to Cumis' argument, the existence of a conflict of interest should be identified early in the proceedings so it can be treated effectively before prejudice has occurred to either party. It may well be in a given case special verdicts will not be requested or given, and other indicators of the basis of liability such as punitive damages will not come into play. Nevertheless, this often cannot be known until shortly before the case is submitted to the jury. By that time, it is normally too late to prevent prejudice." *Cumis* 162 Cal.App.3d at 371 (fn.7).

Further, Rule 3-310 of the California Rules of Professional Conduct, upon which the *Cumis* decision is largely based, prohibits an attorney from representing multiple clients whose interests are actually or potentially adverse. Rule 3-310, entitled: Avoiding the Representation of Adverse Interests, reads, in relevant part:

> (C) A member [of the State Bar of California] shall not, without the informed written consent of each client: (1) Accept representation of more than one client in a matter in which the interests of the clients **potentially** conflict; or (b) or (2)

> Accept or continue representation of more than one client in a matter in which the interests of the clients **actually** conflict…(emphasis added).

Thus, if there is no informed consent, a policyholder, under *Cumis* and Rule 3-310(C) has an unqualified right to independent counsel. Rule 3-310 provides additional reasons require independent counsel in such situations. In order for a lawyer to be able to vigorously represent the interests or his or her client in actual or potential litigation, confidential information protected by Business and Professions Code § 6068(e)(1) must be collected. In fulfilling his or her duties in the matter that is the subject of the representation it is highly likely that a lawyer will by necessity collect information that goes to the heart of any "potential" conflict of interest notice sent to an insured by an insurance company. An attorney who is representing an insured who received a potential conflict notice and is concurrently paid by an insurance company which retains control and reporting requirements over aspects of the case has dual masters and risks violating Rule 3-310 Sections E and F (1) and (2).

> (E) A member shall not, without the informed written consent of the client or former client, accept employment adverse to the client or former client where, by reason of the representation of the client or former client, the member has obtained confidential information material to the employment.
> (F) A member shall not accept compensation for representing a client from one other than the client unless:
> (1) There is no interference with the member's independence of professional judgment or with the client-lawyer relationship; and
> (2) Information relating to representation of the client is protected as required by Business and Professions Code section 6068, subdivision (e); and
> (3) The member obtains the client's informed written consent, provided that no disclosure or consent is required if:(a) such nondisclosure is otherwise authorized by law;…

The saying goes that one cannot serve two masters, thus the insurer-appointed defense counsel cannot zealously represent both the insurer and the insured. This Court addressed the common law duty of loyalty, noting, "It is ... an attorney's duty to protect his client in every possible way, and it is a violation of that duty for him to assume a position adverse or antagonistic to his client without the latter's free and intelligent consent.... By virtue of this rule an attorney is precluded from assuming any relation which would prevent him from devoting his entire energies to his client's interests." (*Anderson v. Eaton* (1930) 211 Cal. 113, 116, 293 P. 788.). *Santa Clara County Counsel Attys. Assn. v. Woodside* (1994) 7 Cal.4th 525, 28 Cal.Rptr.2d 617, 869 P.2d 1142.

This dilemma to be avoided is especially relevant where two or more insureds are subject to the same litigation and have **potentially** adverse interests and differing levels of culpability. This is precisely the issue in *Centex*.

The *Centex* court, relying on the wrongly decided case of *Dynamic Concepts, Inc. v. Truck Ins. Exchange* (1998) 61 Cal.App.4th 999 and its progeny, incorrectly held that

there was no conflict of interest, which would have entitled appellant Centex Homes to independent counsel under *Cumis* and California Civil Code section 2860. However, the *Centex* court all but ignores the rationale behind the *Cumis* decision and Rule 3-310 and Insurance Code Section 2860, which reads, in relevant part:

> (a) If the provisions of a policy of insurance impose a duty to defend upon an insurer and a conflict of interest arises which creates a duty on the part of the insurer to provide independent counsel to the insured, the insurer shall provide independent counsel to represent the insured…

Section 2860(a) does not differentiate between "actual" and "potential" conflicts and it does not need to. *Cumis* and Rule 3-310 are instructive. Unfortunately, a number of wrongly decided cases[2], chief among them *Dynamic Concepts, supra*, have attempted to modify the *Cumis* rule with little regard for precedent. Thus, review by California Supreme Court is necessary to clarify the *Cumis* rule.

B. A GENERAL RESERVATION OF RIGHTS LETTER IN A CASE INVOLVING MULTIPLE POTENTIALLY ADVERSE INSUREDS IS SUFFICIENT TO TRIGGER THE RIGHT TO *CUMIS* COUNSEL

The *Centex* court takes the extraordinary position, as the *MBL* court did before it, that a general reservation of rights by the carrier does not trigger the right to *Cumis* counsel. This, however, cannot be reconciled with Section 2860(a). Section 2860(a) is instructive on this point as well, which reads, in relevant part:

> (b) …a conflict of interest does not exist as to allegations or facts in the litigation for which the insurer denies coverage; **however, when an insurer reserves its rights on a given issue and the outcome of that coverage issue can be controlled by counsel first retained by the insurer for the defense of the claim, a conflict of interest may exist**.

This is precisely the issue in *Centex*. The insurer, St. Paul Fire and Marine Ins. Co. and St. Paul Mercury Co. ("Travelers") agreed to defend its insured, Oak Leaf Landscape, ("Oak Leaf"), a subcontractor, and Centex Homes as a named additional insured, in a construction defect case, under a general reservation of rights. Given the possibility that Oak Leaf and Centex's interests would diverge in the litigation, Centex Homes requested *Cumis* counsel. Travelers denied the request.

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[2] *See, e.g., James No. 3 Corp. v. Truck Ins. Exch.* (2001) 91 Cal.App.4th 1093, 1101 ("For independent counsel to be requires, the conflict of interest must be significant, not merely theoretical, actual not merely potential."); *Gulf Ins. Co. v. Berger, Kahn et al.* (2000) (79 Cal.App.4th 114, 130 ("A mere possibility of an unspecified conflict does not require independent counsel. The conflict must be significant, not merely theoretical, actual, not merely potential."); *Swanson v. State Farm Gen. Ins. Co.* (2013) 219 Cal.App.4th 1153, 1164 ("To be disqualifying, the conflict of interest must be significant, not merely theoretical, actual, not merely potential); *Federal Ins. Co. v. MBL Inc., supra* ("For independent counsel to be required, the conflict of interest must be significant, not merely theoretical, actual, not merely potential.").

In its briefing, petitioner Centex Homes notes that Travelers reserved its rights stating that its obligations were limited to matters relating to Oak Leaf yet also asserted it had the right to select defense counsel for Centex Homes. This created the potential for a conflict because counsel for Oak Leaf would necessarily direct its efforts at shifting liability away from Oak Leaf and on to other potentially responsible parties such as Centex Homes. This is a common *Cumis* counsel scenario.

A murky *Cumis* rule with regard to a reservation of rights gives *carte blanche* to insurers to deny claims they agree to defend. Yet, they are given complete control of the litigation in which they may have prejudiced the insured's coverage position. Under such a reservation of rights, the carrier does not identify the specific portion of the policy as to which it is reserving its rights, yet is then free to pick and choose from all the policy provisions to deny coverage when the case is over. *Centex* (and *MBL*) fail to address why a reservation of rights is sufficient to deny coverage at the end of the case, yet insufficient to trigger the right to *Cumis* counsel at the beginning.

C. THE LOWER COURTS' MISAPPLICATION OF THE *CUMIS* RULE HAS CREATED AN ENVIRONMENT IN WHICH INSURERS RESIST NEARLY EVERY REQUEST BY AN INSURED FOR *CUMIS* COUNSEL

Since *Cumis*, many lower courts (*e.g., Dynamic Concepts, MBL, supra*) have struggled to apply the correct standard for independent counsel, creating confusion in the law. Many courts have wrongly held that *Cumis* only applies only to *actual* conflicts, not potential *conflicts*. The practical result is an arrogance in which insurers attempt to classify all conflicts as "potential" that will never become "actual."

The lower courts appear to misunderstand that *Cumis* counsel is designed to be a proactive measure rather than a remedy once an actual conflict has arisen, or worse, once defense counsel has made an irreversible decision that prejudices the insured's coverage position in violation of the Rules of Professional Conduct. This is tantamount to "closing the barn door *after* the horse has already escaped," so to speak. UP and CAOC are aware that it has become increasingly difficult for insureds to obtain *Cumis* counsel since *Dynamic Concepts* because in almost every scenario the carrier says no "actual conflict" has arisen. Not only is this problematic from a coverage standpoint, but when an insurer defends under a reservation of rights, it places insurance defense counsel in a difficult position where they must favor the carrier over the insured, or vice versa.

The public policy implications of *Cumis* counsel are also significant. Without a clear rule, insurers will continue to deny insureds' requests for independent counsel, further devaluing the insurance they have purchased and encouraging the violation of the Rules of Professional Conduct by counsel on their select lists. Insureds have a *reasonable expectation* that their insurer will defend them when they are sued. When a conflict of interest arises, either between multiple insureds as here, or between the insurer and a single insured, it is critically important that insurers meet their obligation to provide the insured with a zealous advocate who is competent and impartial.

Dynamic Concepts and its progeny (*see* fn. 2) have enunciated an unworkable standard for when an insurer is required to appoint independent counsel. The language of these cases includes ominous terms such as "significant" and "theoretical" with little analysis or explanation. These cases make it nearly impossible to tell, from the insured's point of view, whether the conflict of interest is "actual" or merely "potential" but that should not matter. *Cumis* is clear, Section 2860 is clear, and the Rules of Professional Conduct are clear: an insured has the right to independent counsel when a conflict of interest arises. This Court simply needs to say it, once and for all.

III. GRANTING THE PETITION FOR REVIEW IS PREFERABLE

As noted above, the *Centex* decision misapplies the standard for *Cumis* counsel and creates further confusion in the law. This Court should grant review to clarify that both "actual" and "potential" conflicts trigger an insured's right to *Cumis* counsel and to buttress the mandates of the Rules of Professional Conduct.

Respectfully Submitted,

_____s/_____

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Respectfully Submitted,

_____s/_____

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