No. 15-1351

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

MOUNT VERNON FIRE INSURANCE COMPANY,

Plaintiff-Appellee

v.

VISIONAID, INC.

Defendant-Appellant

AMICUS REPLY BRIEF OF UNITED POLICYHOLDERS IN SUPPORT OF DEFENDANT-APPELLANT VISIONAID, INC.

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I. INTRODUCTION

United Policyholders respectfully submits this *amicus* reply brief for the Court's consideration because the resolution of this case is highly important to policyholders in Massachusetts who rely upon their liability insurance policies for defense of potentially covered claims. Further, United Policyholders submits that the positions taken in the brief submitted by the insurance industry *amici* must be addressed so that the Court has fully briefed arguments before it.

II. ARGUMENT

A. An Insurance Company's Reservation of Rights Is Not Required for an Actual Conflict of Interest To Exist between and Insurance Company and a Policyholder.

Although a conflict of interest clearly exists when an insurance company seeks to defend its policyholder under a reservation of rights, to the objection of the policyholder, *see, e.g., Three Sons, Inc. v. Phoenix Ins. Co.*, 357 Mass 271, 275-76 (1970); *Magoun v. Liberty Mut. Ins. Co.*, 346 Mass. 677, 684-685 (1963), courts outside of Massachusetts have found actual conflicts of interests in situations where no reservation of rights was issued, applying principles recognized in Massachusetts decisions on fundamental conflict of interest rules. *See Allstate Ins. Co. v. Campbell*, 639 A.3d 652 (Md. 1994); *Pub. Serv. Mut. Ins. Co. v. Goldfarb*, 425 N.E.2d 810 (N.Y. 1981); *Md. Cas. Co. v. Peppers*, 355 N.E.2d 24 (Ill. 1976). A reservation of rights may show an actual conflict of interest (and provide a policyholder with notice of that conflict if not otherwise

apparent), but there is no blanket rule that it is a prerequisite to finding a conflict of interest. The significance of the policyholder's entitlement to appoint independent counsel when there is an actual conflict of interest with the insurance company is the fact that there is a conflict of interest. *See id.*

Indeed, in a prominent case cited by the insurance *amici* the Texas Supreme Court observed that an actual conflict of interest may exist when "the attorney hired by the carrier acts unethically and, at the insurer's direction, advances the insurer's interests at the expense of the insured's." *Northern County Ins. Co. v. Davalos*, 140 S.W.3d 685, 689 (Tex. 2004). Here, that is the precise risk—that Mount Vernon's hired counsel will improperly serve two masters with conflicting interests, but will advance Mount Vernon's interests at the expense of VisionAid's counterclaim. *See also McCourt Co., Inc. v. FPC Props., Inc.*, 386 Mass. 145, 145-466 (1982).

As the Texas Supreme Court further recognized, in such a situation "the insured may rightfully refuse an inadequate defense and may refuse any defense conditioned on an unreasonable, extra-contractual demand that threatens the insured's independent legal rights." *Davalos*, 140 S.W.3d at 689. The example that court used is on point here: "[the insurance company] could not have required [the policyholder] to dismiss his Matagorda suit [an affirmative suit brought by the policyholder] as a condition for defending him, and such a demand

would have justified [the policyholder's] rejection." *Id.* Here, the risk that Mount Vernon could direct defense counsel to seek dismissal of VisionAid's counterclaim or otherwise interfere with successful prosecution of the counterclaim creates the same risk and creates the same ethical conflict for insurance-appointed counsel, to the harm of VisionAid. *See* Supplemental Brief of Appellant VisionAid, Inc. Following Answers to Certified Questions, at p. 12. Therefore, VisionAid—and any other policyholder in a similar position—should be entitled to independent counsel with the defense paid for by the insurance company.

The facts of the instant case demonstrate the existence of an actual conflict of interest necessary to give rise to VisionAid's right to select independent counsel, with the defense portion of counsel's work paid by Mount Vernon. *See Mount Vernon Fire Ins. Co. v. VisionAid, Inc.*, 477 Mass. 343, 345, 76 N.E.3d 204, 206-07 (2017). The situation is analogous to prior case law in which courts found an actual conflict of interest due to the underlying claims alleged against the policyholder fitting entirely within either covered claims or uncovered claims, such as causes of action for negligence and intentional tortious conduct based on the same activities by the policyholder. *See Goldfarb*, 425 N.E.2d at 815 ("inasmuch as the insurer's interest in defending the lawsuit is in conflict with the defendant's interest – the insurer being liable only upon some of the grounds for recovery asserted and not upon others – defendant [policyholder] is entitled to defense by an

attorney of his own choosing, whose reasonable fee is to be paid by the insurer"). In those situations, a defense must be mounted against both the covered and non-covered claim, although the insurance company is interested only in the defense against the covered claim so as to defeat its possible liability. *See id.*

In this case, Mount Vernon is interested only in defending against a covered claim, while VisionAid has a counterclaim that must be asserted and, if proven, not only will help defeat liability but will provide a valuable recovery separate from merely succeeding on its defense. Stated otherwise, Mount Vernon's appointed counsel, as guided by Mount Vernon, will seek to develop a theory of the case only to the extent of defeating possible liability, which may be accomplished faster than resolution of the counterclaim. However, VisionAid wants both to defeat possible liability and to prevail on its counterclaim to recover valuable funds. Independent counsel can and should pursue both objectives, with Mount Vernon paying reasonable fees for the defense portion of that attorney's case. *Cf. Gorman v. Pattengell*, 535 N.Y.S.2d 402, 403-04 (App. Div. N.Y. 1988).

This would be consistent with Massachusetts rules of professional conduct, Massachusetts law, and law from other jurisdictions. *See, e.g.*, *McCourt*, 386 Mass. at 146 ("A lawyer shall not continue multiple employment . . . if it would be likely to involve him in representing differing interests."); *Peppers*, 355 N.E.2d at 30 ("Because of this conflict of interests, serious ethical questions

prohibit an attorney from representing both the interest of [the insurance company] and [the policyholder].". If a policyholder such as VisionAid gave its consent to the defense provided by insurance company-appointed counsel (which it has not in this case), then ethical obligations are satisfied. But, when there is no such consent, as here, the policyholder must be allowed to appoint independent counsel. *See Peppers*, 355 N.E.2d at 30.

B. The Insurance Industry *Amici*'s Slippery-Slope Arguments Should Be Disregarded As Entirely Speculative Scenarios in Search of an Actual Problem.

In its *amici* brief, the insurance industry *amici* contend that policyholders may "manufacture" conflicts for various reasons that are not present in the case before this Court. VisionAid's counterclaim seeks real money. Its counterclaim is the very type that would bring real value to a policyholder, and is thus a valid reason for litigation until that value is recognized. This is not a so-called "manufactured" conflict where a policyholder "wants to defend the case to the bitter end because it views settlement as an admission of culpability" or some other fear that its business may be impacted. *Amicus Curiae* Brief of American International Group, Inc. and Massachusetts Insurance Federation, Inc., at p. 6. Those concerns may exist in other matters, but they do not exist here. In any event, they are speculative and not *per se* indicative of an actual conflict of interest giving rise to a policyholder's right to appoint independent counsel—defending a

case to the "bitter end" is not out of line with the provision of a full defense (assuming the insurance company provides a full defense). The Supreme Judicial Court has decided that a counterclaim that would require additional litigation is beyond the duty to defend, but has not clearly addressed how the interests of the policyholder are to be advanced contrary to the interests of the insurance company in ending the defensive portion of the case and defeating liability.

The insurance industry *amici*'s other arguments are similarly speculative and concern "manufactured" potential conflicts of interest, not actual conflicts of interest such as those that exist when providing a simple defense is contrary to fully prosecuting a counterclaim (even if that counterclaim may serve to defeat or lessen liability of the policyholder).

Moreover, there is no prejudice to the insurance company if it must pay for independent counsel to defend a policyholder when that counsel will also prosecute a counterclaim at the policyholder's expense. The only conceivable "prejudice" is that the insurance company may have to cede some level of control over counsel. However, any claim of such prejudice fails because the insurance company's promise to provide a defense implicitly includes a promise to pay for counsel who can defend the policyholder consistent with that counsel's obligations under the Rules of Professional Conduct. *See Liss v. Studeny*, 450 Mass. 473, 477 (2008) ("Every contract is subject to an implied covenant of good faith and fair

dealing."); *Gore v. Arbella Mut. Ins. Co.*, 932 N.E.2d 837, 845 (Mass. Ct. App. 2010) (observing that good faith is implied in insurance policy); *see also Wieder v. Skala*, 609 N.E.2d 105, 108-09 (N.Y. 1992) (holding that compliance with Rules of Professional Conduct is implied in good faith in contracts for employment of lawyers). The policyholder is not imposing on the insurance company something to which it never agreed and for which it never received any premium. In fact, the insurance company would receive a premium in major part to defend the policyholder, and the insurance company would be paying reasonable fees for that defense.[1] The policyholder would be furnishing the costs for the prosecution of its counterclaim.

On the other hand, if the insurance company seeks to impose its interests on the policyholder by limiting counsel's ability to fully develop a case that includes an affirmative counterclaim, it creates an actual conflict of interest. The conflict of interest requires independent counsel so that the policyholder both receives the benefit of its bargain in purchasing insurance coverage and in fully protecting and developing its legal rights.

[1] Of course, the insurance industry *amici* ignore that in Massachusetts insurance companies must defend their policyholders against all claims in a case if any one claim is covered under the "in for one, in for all" rule. *See GMAC Mortg., LLC v. First. Am. Title Ins. Co.*, 464 Mass. 733, 738 (2013) (noting that "if an insurer has a duty to defend one count of a complaint, it must defend them all", and holding that "[i]t is not uncommon for a lawsuit against an insured to assert some claims that are covered by the insurance policy and others that are not"). That includes claims for which the insurance company may never have received a premium, but against which the insurance company nevertheless must defend.

III. CONCLUSION

Accordingly, and as set forth in United Policyholder's *amicus* brief, the Court should recognize that a conflict of interest exists when an insurance company has an interest in devaluing or otherwise impairing a policyholder's counterclaim, as in the present matter. That conflict of interest should entitle the policyholder to select the attorney who defends the claim against it, at the insurance company's expense, and who prosecutes the counterclaim against the underlying claimant.

Dated: September 19, 2017

Respectfully submitted,
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I certify that on September 19, 2017, a copy of this document was served on the following counsel for the parties, electronically through the ECF system, as registered participants in this case, and by regular mail at the addresses stated below:

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