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S.C. SUPREME COURT

THE STATE OF SOUTH CAROLINA
In The Supreme Court

CERTIFIED QUESTION FROM THE UNITED STATES COURT OF
APPEALS FOR THE FOURTH CIRCUIT

Appellate Case No. 2018-001170

In re: Mt. Hawley Insurance Company Petitioner,

In Which Contravest, Inc., Contravest Construction
Company, and Plantation Point Horizontal Property
Regime, as assignees, are Respondents.

FINAL BRIEF OF PETITIONER

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STATEMENT OF ISSUE ON APPEAL

1. Does South Carolina law support application of the “at issue” exception to the attorney-client privilege such that a party may waive the privilege by denying liability in its answer?

STATEMENT OF THE CASE¹

This Certified Question involves a fundamental principle of South Carolina law, as the answer will shape the contours of the attorney-client privilege in this State. The District Court’s order giving rise to the question presented applied an exception to the attorney-client privilege that has never been recognized by an appellate court of this State, and utilized a test for analyzing waiver (“the *Hearn* test”) that conflicts with South Carolina law. *Hearn* has been criticized by courts and commentators and has lost favor due to the potential for unfair and inconsistent results. As detailed below, the *Hearn* test conflicts with existing South Carolina precedent governing waiver of the attorney-client privilege, which is sufficient to support answering the Certified Question “no.” However, if the Court is inclined to adopt a specific test, the test from *Rhone-Poulenc Rorer Inc. v. Home Indemnity Co.*, 32 F.3d 851 (3d Cir. 1994) comports with South Carolina law, and should be adopted. This test supports that waiver occurs only where a party “interjected the advice of counsel as an essential element of a claim in this case,” meaning the party “asserts a claim or defense, and attempts to prove that claim or defense by disclosing or describing an attorney client communication.” *Id.* at 864.

Regardless of the analysis applied, the Court should answer the Certified Question in the negative. As detailed herein, to hold otherwise would deprive insurance companies of one of the

¹ Pursuant to Rule 244(b), SCACR, the Court’s review is limited to the Certification Order. The Certification Order sets forth “the question[] of law to be answered, all findings of fact relevant to the question[] certified, and a statement showing fully the nature of the controversy in which the question[] arose.” *Id.* The Court “will not consider any documents or other evidentiary materials unless the certifying court has submitted those materials.” *Id.* Prior to the Court’s action on a Certification Order, a party may notify the Court and the certifying court that it believes additional materials from the record are necessary. Respondents did not make such a motion.

Therefore, because the Fourth Circuit did not submit any evidentiary materials and Respondents did not move to add materials to the Record, the Statement of the Case is limited to the facts and background set forth in the Certification Order. In accordance with this restriction, Mt. Hawley sets forth the background from the Certification Order verbatim.

foundational privileges recognized at law in any suit in which bad faith is alleged. The Court should decline to recognize such a fundamentally unfair rule.

The Fourth Circuit's Certification Order provides the following background:

Mount Hawley provided ContraVest Construction Company ("Contravest") with excess commercial liability insurance from July 21, 2003, to July 21, 2007. During that period, Contravest constructed the Plantation Point development in Beaufort County, South Carolina. In 2011 the Plantation Point Horizontal Property Regime Owners Association ("the Owners Association") sued Contravest for alleged defective construction of Plantation Point. Mount Hawley refused Contravest's demands to defend or indemnify Contravest in the suit, as Contravest contended was required by its insurance policies, and Contravest ultimately settled the case.

Contravest and the Owners Association subsequently sued Mount Hawley in South Carolina court, alleging bad faith failure to defend or indemnify, breach of contract, and unjust enrichment. Mount Hawley removed the case to the United States District Court for the District of South Carolina pursuant to 28 U.S.C. § 1441 (2012), and federal subject matter jurisdiction exists under 28 U.S.C. § 1332 (2012) based upon complete diversity of citizenship between the parties and damages alleged to be greater than \$75,000.

During discovery, the plaintiffs sought production of, first, Mount Hawley's file on Contravest's claim for excess coverage relating to the Plantation Point suit, and later, Mount Hawley's files relating to all of Contravest's claims under its excess liability policies. *See* Fed. R. Civ. P. 26(b)(1), 34(a)(1)(A). Mount Hawley contended that these files contained material protected by the attorney-client privilege, and produced the files in redacted form with accompanying privilege logs. *See* Fed. R. Civ. P. 26(b)(5)(A).

The plaintiffs filed multiple motions to compel, arguing that Mount Hawley waived the attorney-client privilege as to these files. *See* Fed. R. Civ. P. 37(a)(3)(B)(iv). The district court adopted the recommendation of the magistrate judge, granted the motions to compel, and ordered Mount Hawley to produce the files for in camera inspection. *Contra Vest Inc. v. Mt. Hawley Ins. Co.*, 273 F. Supp. 3d 607, 622-23 (D.S.C. 2017). The district court subsequently denied Mount Hawley's motion for reconsideration.

Mount Hawley then sought a writ of mandamus from this court to vacate the district court's order granting the motions to compel.

In its petition for a writ of mandamus, Mount Hawley challenges the district court's holding that the relevant files were not protected by the attorney-client privilege because Mount Hawley put them "at issue" in the case by denying liability for bad faith failure to defend or indemnify. Because this is a diversity action involving claims for which South Carolina law provides the rule of decision, South Carolina's law of attorney-client privilege applies. *See Ashcraft v. Conoco, Inc.*, 218 F.3d 282, 285 n.5 (4th Cir. 2000); Fed. R. Evid. 501. In South Carolina the attorney-client privilege is defined as follows:

(1) Where legal advice of any kind is sought (2) from a professional legal adviser in his capacity as such, (3) the communications relating to that purpose (4) made in confidence (5) by the client, (6) are at his instance permanently protected (7) from disclosure by himself or by the legal adviser, (8) except the protection be waived.

Tobaccoville USA, Inc. v. McMaster, 387 S.C. 287, 293, 692 S.E.2d 526, 530 (2010). "In general, the burden of establishing the privilege rests upon the party asserting it." *Wilson v. Preston*, 378 S.C. 348, 359, 662 S.E.2d 580, 585 (2008).

In finding that the relevant files were not protected by South Carolina's attorney-client privilege, the district court relied on *City of Myrtle Beach v. United Nat. Ins. Co.*, No. 4:08-1183-TLW-SVH, 2010 WL 3420044 (D.S.C. Aug. 27, 2010) (unpublished). *City of Myrtle Beach* also involved a bad faith insurance suit under South Carolina law in which the insured sought to compel the insurer to produce the relevant claims file, and the insurer argued that the file contained material protected by the attorney-client privilege. *Id.* at *1-2. The district court adopted the approach articulated in *Hearn v. Rhay*, 68 F.R.D. 574 (E.D. Wash. 1975), as "consistent with established South Carolina law." *Id.* at *5. Applying *Hearn*, the district court found that

there is no per se waiver of the attorney client privilege simply by a plaintiff making allegations of bad faith. However, if a defendant voluntarily injects an issue in the case, whether legal or factual, the insurer voluntarily waives, explicitly or impliedly, the attorney-client privilege. Thus

“voluntarily injecting” the issue is not limited to asserting the advice of counsel as an affirmative defense. A party’s assertion of a new position of law or fact may be the basis of waiver.

Id. (citation omitted).

Applying this definition of waiver, the court in *City of Myrtle Beach* found that “for the purposes of the motion to compel, . . . the [insured] has presented a prima facie case of bad faith,” and the insurer failed to meet its burden of establishing the absence of waiver of the attorney-client privilege on account of the defenses asserted in its answer, including that the insurer acted reasonably and in good faith. *Id.* at *7. The court noted that “[w]hile this ruling amounts to a virtual per se waiver of the privilege in this case, this result is based on the facts and issues presented by [the insurer] in its Answer and its failure to meet its burden as to the applicability of the privilege with this in mind.” *Id.*

In the present case, the district court rejected Mount Hawley’s argument that *City of Myrtle Beach* was inconsistent with South Carolina law in light of the fact that one member of the Supreme Court of South Carolina criticized the *Hearn* decision in a separate opinion concurring in part and dissenting in part. *See Davis v. Parkview Apartments*, 409 S.C. 266, 291-96, 762 S.E.2d 535, 549-51 (2014) (Pleicones, J., concurring in part and dissenting in part) . . .

Following the approach articulated in *City of Myrtle Beach*, the district court concluded that because the plaintiffs had established a prima facie case of bad faith failure to insure, and Mount Hawley in its answer denied bad faith liability, Mount Hawley waived the attorney-client privilege with respect to the attorney-client communications in the claim files, to the extent such communications are relevant under Fed. R. Civ. P. 26. [273 F. Supp. 3d] at 611-23. The court thus ordered Mount Hawley to produce the files for in camera review. *Id.* at 623.

Mount Hawley contends, and we agree, that if South Carolina law does not support the “at issue” exception applied in *City of Myrtle Beach*, the district court’s order granting the motions to compel was erroneous. . . .

Fourth Circuit’s Certification Order at 2-7 (footnotes omitted).

ARGUMENT

I. Summary of the Arguments

The Certified Question presented in this matter is a critical question concerning one of the most sacrosanct of privileges recognized by the law of this State: the attorney-client privilege. The District Court's order relied on an emerging body of federal District of South Carolina case law recognizing a waiver of the attorney-client privilege *under circumstances that have never been recognized by the appellate courts of this State*. The only South Carolina appellate jurist examining the concept applied by the District Court—the “at issue” exception as detailed in *Hearn*—contended that it is inconsistent with South Carolina law.

Existing general principles of South Carolina law as to when a party waives the attorney-client privilege are supportive of Mt. Hawley's position in this matter. However, if the Court is inclined to adopt a specific test for the “at issue” waiver, it will find that courts in other jurisdictions have generally applied one of three standards in examining whether there has been an “at issue” waiver. As detailed below, the most limited test, articulated in *Rhone-Poulenc Rorer Inc. v. Home Indemnity Co.*, 32 F.3d 851 (3d Cir. 1994), is consistent with the law of this State and the important policy underlying the attorney-client privilege.

Additionally, the District Court's holding here expands all tests, even the liberal so-called *Hearn* test, beyond its previously recognized boundaries. At a minimum, to find an “at issue” waiver, even the courts that adopted the liberal *Hearn* standard have all required a party to have affirmatively pled its good faith, reasonableness, or reliance on the advice of counsel. The District Court's order extends this expansive basis for waiver even further, holding that by merely denying allegations of bad faith in its answer and asserting it complied with the terms of the insurance policy, Mt. Hawley waived the attorney-client privilege pursuant to the “at issue”

waiver exception. Adopting such a standard would result in South Carolina becoming one of the least-friendly states towards the attorney client privilege.² The Court should reject such a broad standard as inconsistent with South Carolina law.

The District Court's expansive interpretation of the "at issue" exception eviscerates an insurance company's right to the confidential advice of counsel in any matter in which bad faith could subsequently be alleged. The impact of the District Court's holding means that *any* time an insurer denies acting in bad faith and/or asserts it complied with its policy, it will waive the attorney-client privilege. Under the rule adopted by the District Court, an insurer has two options when faced with a bad faith suit: (1) either defend itself and thereby waive the attorney-client privilege, or (2) admit liability and preserve the privilege. This false choice all but erases the privilege for insurance companies. Moreover, such a rule essentially permits the party's *opponent* to force a waiver of privilege by placing the insurer's bad faith at issue. The Court should decline to adopt such a fundamentally unfair rule.

Furthermore, to the extent the Court finds that waiver applies, if it holds that it only applies in the context of insurance bad faith as Respondents desire, such would deny insurance

² As the Southern District of Florida noted last year, it was unable to find any "case or principle that supports the contention that *merely denying allegations constitutes a waiver of privilege*," and if this position was correct, "it would *eviscerate the attorney-client privilege* or work product doctrine because, as soon as a defendant denied certain allegations, a waiver would occur and privileged documents could be discoverable." *Ctr. for Individual Rights v. Chevaldina*, No. 16-20905-CIV, 2017 WL 5905191, at *7 (S.D. Fla. Nov. 29, 2017) (emphasis added); *see also Lorenz v. Valley Forge Ins. Co.*, 815 F.2d 1095, 1098 (7th Cir. 1987) ("To waive the attorney-client privilege by voluntarily injecting an issue in the case, a defendant must do more than merely deny a plaintiff's allegations."); *Contogouris v. Westpac Res.*, No. 10-4609, 2012 WL 13001036, at *1 (E.D. La. Apr. 11, 2012) ("Waiver of the attorney client privilege occurs only in those instances where a party has put a specific fact or argument at issue; not where, as here, the defendant had simply made general denials."); *Carpenter v. Mohawk Indus., Inc.*, No. 4:07-CV-0049-HLM, 2007 WL 5971741, at *10 n.10 (N.D. Ga. Oct. 1, 2007) ("The Court therefore rejects the contentions made by the Plaintiffs . . . that Defendant . . . waived its attorney-client privilege by denying Plaintiffs [sic] allegations in its Answer to Plaintiff's First Amended Complaint.").

companies equal protection under the law. All contracts have an implied duty of good faith and fair dealing under South Carolina law. To hold that insurance companies cannot defend their good faith actions without waiving the right to confidential attorney-client communications—when no other party is constrained by such a rule—would place insurers at a disadvantage when compared to similarly situated persons. Applying the waiver in this context only would lack any rational basis and thus it should be rejected.

Finally, Mt. Hawley urges that if the Court does formally recognize a specific test for the “at issue” waiver, particularly if it adopts *Hearn*, that it do so on a prospective basis only. Mt. Hawley’s actions were in accordance with the law of this State in effect at the time. If the Court recognizes an expansive “at issue” waiver, Mt. Hawley should not be punished for failing to act in accordance with a principle that was not previously recognized in this State.

II. Existing South Carolina law supports Mt. Hawley’s position and not the test applied by the District Court.

A. The attorney-client privilege is an important issue of South Carolina policy.

The attorney-client privilege is a bedrock principle of South Carolina jurisprudence. As this Court has explained, it is “based upon a public policy that the best interest of society is served by promoting a relationship between the attorney and the client whereby utmost confidence in the continuing secrecy of all confidential disclosures made by the client within the relationship is maintained.” *Wilson v. Preston*, 378 S.C. 348, 359, 662 S.E.2d 580, 585 (2008). The attorney-client privilege is “rooted in the imperative need for confidence and trust.” *Hartsock v. Goodyear Dunlop Tires N. Am. Ltd.*, 422 S.C. 643, 647 n.1, 813 S.E.2d 696, 699 n.1 (2018) (quoting *Jaffee v. Redmond*, 518 U.S. 1, 10 (1996)). Moreover, “[a] review of privileges in general reveals the common thread is that public policy *favours the confidentiality* of these communications or information.” *Id.* at 648, 813 S.E.2d at 699 (emphasis added). The Supreme

Court of the United States and this Court have both recognized the attorney-client privilege's "importance to society." *Id.* at 647 n.1, 813 S.E.2d at 699 n.1.

The scope of the attorney-client privilege, and any exceptions thereto, must be viewed through the lens of these underlying principles. If communications in the context of adversary proceedings are not confidential, then there will be no communications, thereby depriving insurers of advice and significantly eroding these principles.

B. South Carolina law on waiver of the attorney-client privilege supports that the Certified Question should be answered "no."

This court generally takes a restrictive view of when a waiver of privilege has occurred. This restrictive view conflicts with the application of the "at issue" waiver as articulated by the District Court and in *Hearn*.

South Carolina courts have stated the general proposition that "[t]he attorney-client privilege belongs solely to the client and can only be waived by the client." *State v. Thompson*, 329 S.C. 72, 76, 495 S.E.2d 437, 439 (1998). As this Court has cautioned, however, "[a]lthough a client may waive his attorney-client privilege, the *waiver must be distinct and unequivocal*." *Id.* (emphasis added). Moreover, "[w]here an implied waiver is claimed, *caution must be exercised, for waiver will not be implied from doubtful acts*." *Id.* at 440 (quoting 28 Am. Jur. 2d *Estoppel and Waiver* § 160 (1966)) (emphasis added).³

Floyd v. Floyd, 365 S.C. 56, 615 S.E.2d 465 (Ct. App. 2005), *superseded on other grounds by* 2008 S.C. Act No. 211, § 1, examined waiver of privilege in the context of the trial doctrine of "opening the door." *Id.* at 92, 615 S.E.2d at 484. The *Floyd* court **did not** consider whether South Carolina law recognizes the "at issue" waiver such that a party might waive the

³ In discussing the doctrine of waiver generally, the Court has also found that "[t]he party asserting waiver has the burden of proof." *SPUR at Williams Brice Owners Ass'n, Inc. v. Lalla*, 415 S.C. 72, 91, 781 S.E.2d 115, 125 (Ct. App. 2015).

attorney-client privilege via its pleading. Rather, in *Floyd*, the court found that where a party chooses to forego protection of a rule and introduce evidence or testimony that the opposing party would otherwise be unable to address, then it would be unfair to prohibit the opposing party from addressing the issue. *See id.* In *Floyd*, the party claiming privilege introduced trial testimony that a witness took a certain action because his attorney told him to do so. *See id.* The court found this opened the door to introduction of letters suggesting that the attorney told him to do the opposite. *Id.* Thus, *Floyd* presented an example of a waiver that was “distinct and unequivocal” consistent with *Thompson*. *See Thompson*, 329 S.C. at 76-77, 495 S.E.2d at 439.

This existing South Carolina law already details when a party may waive the attorney-client privilege. As this Court has explained, it must be explicit, and cannot be grounded on doubtful acts. This conflicts with the District Court’s application of the *Hearn* test, which found that waiver may occur even where a party does not expressly assert that it relied on the advice of counsel in either a claim or defense. The Court should continue to adhere its general precedents and reject the District Court’s sweeping “at issue” waiver analysis.⁴ Mt. Hawley did not take any “unequivocal” or “distinct” act supporting a waiver of privilege, and therefore the Court should confirm that the answer to the Certified Question is “no” under South Carolina law.

III. If the Court adopts a specific test for determining whether there has been an “at issue” waiver, it should adopt the most restrictive test since it comports with South Carolina precedent.

A. Courts have applied three tests in determining whether a party has placed privileged communications at issue.

When confronting this issue, courts have generally applied one of three tests to determine whether a party has waived the attorney client privilege. *See generally* Douglas R. Richmond,

⁴ As detailed below, adopting the District Court’s standard would have far ranging implications for the attorney-client privilege under South Carolina law.

The Frightening at-Issue Exception to the Attorney-Client Privilege, 121 Penn St. L. Rev. 1 (2016). As detailed below, the “*Rhone-Poulenc* test” is most in line with South Carolina law and, if the Court adopts a test, it should rely on that standard. The three tests are explained below.

The *Hearn* test is the “most liberal,” *id.* at 17, and, as detailed above, originates from a federal case from the Eastern District of Washington. *See Hearn v. Rhay*, 68 F.R.D. 574 (E.D. Wash. 1975). *Hearn* was a civil rights action brought by an inmate against several prison officials pursuant to 42 U.S.C. § 1983. *Id.* at 577. Those officials denied any liability and asserted the defense of qualified immunity, contending they acted with a good faith belief that their actions complied with the law. *See id.* at 580. In discovery, the plaintiff sought information concerning legal advice rendered to the defendants by the Washington Attorney General insofar as the advice related to plaintiff’s confinement and tended to prove defendants’ bad faith. *See id.* at 578.

Looking to federal common law, the court noted that the privilege issue appeared to be an “issue of first impression . . . spawned by the evolution of the qualified immunity defense.” *Id.* at 578, 580. The *Hearn* court determined that, based upon a review of the evolution of the qualified immunity defense, it was “compelled to recognize a *new* and *narrowly limited exception* to the attorney-client privilege, which applies to civil rights suits against state officials under 42 U.S.C. § 1983, wherein the defendant asserts the *affirmative defense of good faith immunity.*” *Id.* at 580 (emphasis added). The *Hearn* court found that privilege may be waived when a party places privileged communications “at issue” and the following three factors are met:

- (1) assertion of the privilege was a result of some affirmative act, such as filing suit, by the asserting party;
- (2) through this

affirmative act, the asserting party put the protected information at issue by making it relevant to the case; and (3) application of the privilege would have denied the opposing party access to information vital to his defense.

Id. at 581.⁵ The court explained, however, that if the exception applies, the party seeking the information must also make a “substantial showing of merit” to its case before the court should apply the exception. *Id.* at 582.

The second test is from *In re County of Erie*, 546 F.3d 222 (2d Cir. 2008). *In re County of Erie* noted that the *Hearn* test had been criticized by courts and academics and applied unevenly. *Id.* at 227-28 (collecting authorities). It explained that the *Hearn* test “cut too broadly,” particularly in light of its relevance element. *Id.* at 229. Privileged information “may in some sense be *relevant* in any lawsuit,” and a “mere indication of a claim or defense certainly is insufficient to place legal advice at issue.” *Id.* (emphasis in original). The Second Circuit noted that the essential element of reliance on privileged advice was missing from the *Hearn* test, and conclusively held that for a waiver to occur “***a party must rely on privileged advice from his counsel to make his claim or defense.***” *Id.* (emphasis added). The court declined to specify the degree of reliance required, but noted that privilege was not waived in the case before it because the petitioners did not “rely upon the advice of counsel in asserting their defense.” *Id.*

The final test is from *Rhone-Poulenc Rorer Inc. v. Home Indemnity Co.*, 32 F.3d 851 (3d Cir. 1994). The *Rhone-Poulenc* court also criticized *Hearn*, noting that it was “of dubious

⁵ The Washington Court of Appeals has suggested that *Hearn* is primarily confined to the legal malpractice context. *Steel v. Philadelphia Indem. Ins. Co.*, 381 P.3d 111, 119 (Wash. Ct. App. 2016) (“We acknowledge that a party who seeks to apply *Hearn*’s implied waiver test beyond the context of a legal malpractice case must bear a significant burden.”). The *Steel* court noted that “a party seeking to apply it beyond that context must offer a fact-specific explanation for each element of the test to demonstrate why it should be applied, and courts must carefully apply the test to see if waiver has occurred in order to preserve the sanctity of attorney-client privilege.” *Id.*

validity” since it and other similar decisions “dress up their analysis with a checklist of factors,” but ultimately “appear to rest on a conclusion that the information sought is relevant and should in fairness be disclosed.” *Id.* at 864. The *Rhone-Poulenc* court held that even where advice of counsel is relevant to a party’s state of mind, there is no waiver unless the party “interjected the advice of counsel as *an essential element of a claim in this case.*” *Id.* (emphasis added). As the court explained: “The advice of counsel is placed in issue where the client asserts a claim or defense, *and attempts to prove that claim or defense by disclosing or describing an attorney client communication.*” *Id.* at 863 (emphasis added).

B. Despite existing South Carolina guidance, courts in the District of South Carolina unilaterally adopted the *Hearn* test.

The District of South Carolina first recognized the “at issue” waiver in *City of Myrtle Beach v. United Nat. Ins. Co.*, No. 4:08-1183, 2010 WL 3420044 (D.S.C. Aug. 27, 2010). This was an unpublished order from a magistrate judge. Nevertheless, it was apparently the genesis of a branch of District of South Carolina case law on the applicability of the “at issue” waiver. *City of Myrtle Beach* was a bad faith action brought by the city against its insurer relating to an underlying lawsuit against the city. *Id.* at *1. The city sought communications between the insurer and its attorneys. *Id.* at *2.

The court began by examining South Carolina law on the attorney-client privilege and how other courts have treated the privilege in bad faith litigation. The court looked to *Hearn* for guidance, noting (ultimately what has shown to be erroneously) it was the “most widely accepted approach.” *Id.* at *5.⁶ The court explained that there is no per se waiver simply because a

⁶ Note that *Hearn* involved a defense of qualified immunity, where the defendants did not merely assert “good faith” or “reasonableness” in their affirmative defense, but rather “good faith *immunity.*” 68 F.R.D. at 580 (emphasis added). Moreover, the *Hearn* court cautioned that its holding was narrow in light of the nature of the qualified immunity defense, *see id.*, which

plaintiff alleges bad faith, but if a defendant “voluntarily injects an issue in the case, whether legal or factual, the insurer voluntarily waives, explicitly or impliedly, the attorney-client privilege.” *Id.* The court also noted—without any supporting citation—that this is not limited to “asserting the advice of counsel as an affirmative defense,” but may also apply based on “[a] party’s assertion of a new position of law or fact.” *Id.* It ultimately held that under South Carolina privilege law, the mere assertion of reasonableness or good faith in the context of an insurance contract gave rise to a waiver of the attorney-client privilege. *Id.*⁷

The *City of Myrtle Beach* court created a waiver of the attorney-client privilege out of whole cloth and proceeded to define its contours without any directive from this Court. Subsequent District of South Carolina judges, including in this case, looked to *City of Myrtle Beach* for guidance and have continued to apply it, even despite the opinion of the former Chief Justice from *Davis v. Parkview Apartments*, 409 S.C. 266, 762 S.E.2d 535 (2014), which offered blistering criticism of the *Hearn* test. This was an improper usurpation of the authority of this Court, and the Court owes no allegiance to this detour from established general South Carolina common law. As detailed herein, the Court should repudiate these cases as inconsistent with the law of this State.

“protects officers who commit constitutional violations but who, in light of clearly established law, could reasonably believe that their actions were lawful,” *Henry v. Purnell*, 652 F.3d 524, 531 (4th Cir. 2011).

⁷ In a case alleging bad faith against an insurer, the assertion of “good faith” or “reasonableness,” is best described as the denial of the plaintiff’s claim of bad faith rather than an affirmative defense. No appellate court of this State has recognized general “good faith” or “reasonableness” as an affirmative defense to such a claim.

C. The *Hearn* test conflicts with South Carolina law and policy.

The only South Carolina authority to have directly addressed the “at issue” waiver is a partial concurrence and partial dissent from former Chief Justice Pleicones in *Davis*.⁸ In *Davis*, the majority found that the waiver of privilege issue was not reviewable due to the Appellants’ failure to appeal the relevant order addressing privilege. Justice Pleicones, however, disagreed and examined whether the trial court’s privilege order, which applied the “at issue” exception as detailed in *Hearn*, comported with South Carolina law. *See Davis*, 409 S.C. at 290-95, 762 S.E.2d at 549-51 (Pleicones, J., concurring in part and dissenting in part). After reviewing *Hearn* and its progeny in detail, along with current South Carolina law, he found that it *did not*. *See id.*

He began by noting that, in his opinion, the *Hearn* “at issue” waiver test “substantially diminishes the attorney-client privilege without regard to the important public interests that privilege is designed to advance.” *Id.* at 292, 762 S.E.2d at 549. After referring the important policy considerations underpinning the privilege, he noted that, in his view, the “*Hearn* at-issue waiver rule sweeps far too broadly, eviscerating the attorney-client privilege without regard to the weighty public interest it serves.” *Id.* at 295, 762 S.E.2d at 550.

As he explained, South Carolina’s implied waiver rule states that a claim of waiver “should be treated with caution,” and waiver must be “distinct and unequivocal.” *Id.* at 292, 762 S.E.2d at 549. However, “[n]otwithstanding that caution must be exercised in finding waiver, it is widely recognized that a client impliedly waives the privilege when he relies on confidential *communications* with his attorney to make out a claim or defense.” *Id.* at 292-92, 762 S.E.2d at

⁸ Mt. Hawley acknowledges that this opinion is not binding on the Court. However, the analysis succinctly and effectively details the problems with the *Hearn* test and its conflict with South Carolina policy.

549 (emphasis in original). *Hearn*, however, “alters this traditional implied waiver standard” and “*dramatically expands* the traditional rule.” *Id.* at 293, 762 S.E.2d at 550 (emphasis added).

As Justice Pleicones explained, because the attorney-client privilege only has significance where the protected information is relevant to the case and the opposing party believes the information is vital to his defense, “factors two and three [of *Hearn*] operate merely to limit waiver of the privilege to the most sensitive of the client’s communications.” *Id.* Likewise, the first factor expands implied waiver beyond situations where the client “inserts the privileged *communications* into controversy” to situations where the client raises “any *issue* to which the privileged communications are relevant.” *Id.* at 294, 762 S.E.2d at 550 (emphasis in original).

Thus, as stated by Justice Pleicones, the *Hearn* test “virtually eliminates attorney-client privilege in a wide range of cases without taking into account the public policy on which attorney-client privilege is grounded or that the well-settled contours of the attorney-client privilege already balance the competing public interests.” *Id.* Hence, it “has been rejected by most courts and many commentators.” *Id.* (discussing numerous cases and articles criticizing and/or rejecting the *Hearn* test); see e.g., *Remington Arms Co. v. Liberty Mut. Ins. Co.*, 142 F.R.D. 408, 413 (D. Del. 1992) (“The core problem, according to [authorities criticizing *Hearn*], is that expansive language for determining implied waiver leads to a type of ad hoc determination that ignores the system-wide role of the attorney-client privilege and undermines any confidence that parties can place in that privilege. These authorities contend that extremely liberal waiver rules increase litigation costs and judicial time spent on discovery disputes, favor

the wealthiest litigants, undermine the values served by the privilege rules, and vary according to the identity of the litigants and their purported need for privileged information.”⁹

Therefore, the only South Carolina authority to have directly reached the issue, albeit not a binding decision of the Court, flatly rejected its application. Additionally, as Justice Pleicones noted, many courts and academics have denounced the test. *See, e.g., In re County of Erie*, 546 F.3d at 227-28 (discussing the criticism of courts and academics and the “uneven” application of the test); *Pub. Serv. Co. of New Mexico v. Lyons*, 10 P.3d 166, 172 (N.M. Ct. App. 2000) (noting that the *Hearn* test was the majority view at that time, but finding that the *Rhone-Poulenc* test was the more appropriate standard, as *Hearn* “has been applied in a confusing and uneven manner, leading to considerable criticism”).

A principal critique of the test is the lack of limits on its scope. As the *Lyons* court noted, only the third prong has any limiting force on waiver. 10 P.3d at 173. Moreover, the “case-by-case balancing approach runs counter to the United States Supreme Court’s emphasis on the need for certainty.” *Id.* Ultimately, the test “does not succeed in targeting a type of unfairness that is distinguishable from the unavoidable unfairness generated by every assertion of privilege.” *Id.*

⁹ Justice Pleicones also cited the following authorities, **all of which criticized Hearn**: *Rhone-Poulenc Rorer Inc. v. Home Indem. Co.*, 32 F.3d 851, 864 (3d Cir. 1994); *Trs. of Elec. Workers Local No. 26 Pension Trust Fund v. Trust Fund Advisors, Inc.*, 266 F.R.D. 1 (D.D.C. 2010); *United States v. Ohio Edison Co.*, No. C2-99-1181, 2002 WL 1585597 (S.D. Ohio July 11, 2002); *Hewlett-Packard Co. v. Bausch & Lomb, Inc.*, 115 F.R.D. 308 (N.D. Cal. 1987); *Smith v. Kavanaugh, Pierson & Talley*, 513 So.2d 1138 (La. 1987); *Wardleigh v. Second Judicial Dist. Ct.*, 891 P.2d 1180 (Nev. 1995); *Aranson v. Schroeder*, 671 A.2d 1023 (N.H. 1995); *Pub. Serv. Co. of N.M. v. Lyons*, 10 P.3d 166 (N.M. Ct. App. 2000); *Mortg. Guar. & Title Co. v. Cunha*, 745 A.2d 156 (R.I. 2000); *State v. Hydrite Chem. Co.*, 582 N.W.2d 411 (Wis. Ct. App. 1998); Kevin Bennardo, *At Issue Waiver of the Attorney-Client Privilege in Illinois: An Exception in Need of a Standard*, 30 N. Ill. U. L. Rev. 553, 561 (2010); and *Developments in the Law: Privileged Communications*, 98 Harv. L. Rev. 1450, 1641-42 (1985) (explaining that *Hearn*’s concept of unfairness refers to incompleteness of evidence rather than traditional concept in privilege context of unfairness as abuse of a privilege and that the logic of *Hearn* leads to “outrageous” results).

Thus, the *Hearn* test “has been criticized by many jurisdictions as potentially chilling the freedom to engage in confidential communications by a client with his or her attorney, causing an increase in litigation costs concerning discovery disputes, and tending to favor wealthier litigants.” *Mortg. Guar.*, 745 A.2d at 159.

The law review article cited above (the “Richmond article”) succinctly summarizes many of the problems with *Hearn*:

First, courts generally agree that a party does not place its lawyer’s advice at issue simply by filing suit. The first element of the *Hearn* test, therefore, ***contradicts settled law***.

Second, relevance is not the standard for deciding whether evidence should be shielded from disclosure because “privileged information may be in some sense relevant in any lawsuit.” Furthermore, because the definition of relevance will depend on the facts and circumstances of unspecified future litigation, the ***client cannot judge whether a communication with her lawyer may be relevant to some future issue, and thus can never be assured that it will stay confidential***. Such uncertainty and unpredictability undermines the purposes behind the privilege.

Third, whether upholding the privilege will deny an opponent information vital to its claim or defense should not be a factor because it ***confuses the attorney-client privilege with tangible work product immunity***. This is a material error. While a party may discover an opponent’s tangible work product by showing substantial need for the materials and the inability to obtain their substantial equivalent without undue hardship, attorney-client communications do not become discoverable by virtue of the requesting party’s inability to obtain the information from other sources. Privileged information is simply not subject to discovery based on another party’s substantial need or undue hardship.

Richmond, *supra*, at 28 (footnotes omitted) (emphasis added).

Therefore, as Justice Pleicones noted, in light of these flaws, many courts have declined to apply or repudiated their prior approval of the *Hearn* test. *See Davis*, 409 S.C. at 294, 762 S.E.2d at 550; *see also Richmond, supra*, at 20 (noting that, in light of the criticism, “the *Hearn*

test has lost favor with the courts”). Cases are litigated under an adversarial system of justice, and for the system to be fair it must not give one party an advantage to the detriment of the other. The *Hearn* test, however, does precisely that by giving one side an insight into advice, research, and recommendations received by the other side from its counsel. The potential for such opinions of counsel to be revealed to an adversary would likely affect the very substance and nature of the advice itself. This leads to an unequal and unfair playing field.

The rules of procedure and evidence already allow an insured to discover the insurer’s claim file and its rules and policies for handling claims, and to question under oath the person who decided the claim. In order to establish bad faith, it is entirely unnecessary and inappropriate to vest the insured with an additional tool via obtaining the insurer’s advice of counsel on the claim. Therefore, the Court should adopt the former Chief Justice’s rationale from *Davis* and confirm that the *Hearn* test is incompatible with South Carolina law and policy.

D. The *In re County of Erie* test is an improvement on *Hearn*, but still lacks sufficient protection of the privilege.

Recognizing the problems inherent with the *Hearn* test, many courts require additional or different factors in the analysis of waiver. Central to both *In re County of Erie* and *Rhone-Poulenc* tests is a reliance element, requiring that a party *rely* on portions of privileged communications as part of the party’s claim or defense to effect a waiver. This standard provides a clearer, more bright-line rule easier for the parties and courts to apply. Litigants can better anticipate when a waiver would occur, and can expect that if they explicitly assert the advice of counsel to support a claim or defense, it may result in waiver of the privilege. A more ephemeral pleading and relevance standard like the *Hearn* test contemplates is more difficult to apply, and could result in divergent results due to the case-by-case nature of the analysis. Therefore, at a minimum, the Court should look to *In re County of Erie* for guidance.

A number of other courts have adopted this test or an analogous one. The Southern District of West Virginia, for example, specifically rejected a plaintiff's assertion that *City of Myrtle Beach* should apply and applied a similar test to *In re County of Erie. Westfield Ins. Co. v. Carpenter Reclamation, Inc.*, No. 5:13-12818, 2014 WL 4187017, at *5 (S.D.W. Va. Aug. 21, 2014). The court explained that, under West Virginia law:

advice is not in issue merely because it is relevant, and it does not come in issue merely because it may have some affect on a client's state of mind. Rather, it becomes an issue where a client ***takes affirmative action to assert a defense and attempts to prove that defense by disclosing or describing an attorney's communication.***

Id. (quoting *State ex rel. U.S. Fidelity and Guar. Co. v. Canady*, 460 S.E.2d 677, 684 (W. Va. 1995)) (emphasis added). The *Westfield* court explained that even though the insurer retained coverage counsel and relied upon counsel's opinion in denying coverage, it did not waive the privilege because it did not explicitly rely on the advice of counsel as a defense or place the decisions and conclusions "conspicuously in issue in any other way." *Id.* at *5.¹⁰

In a recent case, the South Dakota Supreme Court explicitly modified its previous adoption of the *Hearn* test to add the reliance element from *In re County of Erie*:

We supplement the *Hearn* test to emphasize further the importance of protecting the attorney-client privilege. First, the analysis of this issue should begin with a presumption in favor of preserving the privilege. Second, a client only waives the privilege by expressly or impliedly injecting his attorney's advice into the case. ***A denial of bad faith or an assertion of good faith alone is not an implied waiver of the privilege.*** Rather, the issue is whether Allstate, in attempting to demonstrate that it acted in good faith, ***actually injected its reliance upon such advice into the litigation. The key factor is reliance of the client upon the advice of his attorney.***

¹⁰ *Performance Drilling Co., LLC v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, No. 3:14-CV-254-DPJ-FKB, 2015 WL 12979208 (S.D. Miss. Oct. 21, 2015) reached a similar conclusion, finding that an insurer did not waive privilege where it engaged an attorney to provide a coverage opinion and the insurer did not assert the advice of counsel as an affirmative defense or otherwise place the attorney's advice in issue. *See id.* at *1.

Finally, a client only waives the privilege to the extent necessary to reveal the advice of counsel he placed at issue.

Bertelsen v. Allstate Ins. Co., 796 N.W.2d 685, 703 (S.D. 2011) (citations omitted) (emphasis added).

The Northern District of Georgia also applied a test akin to *In re County of Erie* in *Liberty Mut. Fire Ins. Co. v. APAC-Se., Inc.*, No. 1:07-CV-1516-JEC, 2008 WL 11320055, at *6 (N.D. Ga. May 16, 2008). As the court explained, Liberty Mutual did not place the advice of counsel at issue because it did not base a claim or defense on that advice. *Id.* at *6. Reference to advice of counsel only became an issue when the insurer's adjuster was deposed and testified that some litigation decisions were based on the advice of counsel. *Id.* As the court reasoned, "[w]here a party notes that it relied on the advice of counsel in connection with the subject matter of a claim, **but does not rely on that advice to assert or prove a claim or defense**, it has not waived the attorney-client privilege." *Id.* (emphasis added).

The District of Massachusetts also adopted *In re County of Erie* in *Bacchi v. Mass. Mut. Life Ins. Co.*, 110 F. Supp. 3d 270 (D. Mass. 2015). The *Bacchi* court noted that *In re County of Erie*'s reliance element "addresses the concern that, as a practical matter, there will be very few privilege disputes where the *Hearn* factors are not met." *Id.* at 276. The court reasoned that in showing reliance it is sufficient that the defendant's defense "**relies on certain facts that can only be tested or rebutted if the adversary is given access to the privileged material.**" *Id.* (emphasis added).

The Maryland Supreme Court likewise applied a similar standard, holding that a "client's simple denial of an allegation by the opposing side that an act was committed with a particular intent does not inject advice of counsel into the case, even though that advice may have been the reason why the intent was not present." *CR-RSC Tower I, LLC v. RSC Tower I, LLC*, 56 A.3d

170, 207 (Md. 2012). As the *CR-RSC Tower* court explained, the waiver doctrine “certainly leaves room for a defendant to deny bad faith without waiving the attorney-client privilege.” *Id.* The court reasoned instead that waiver is only implicated where defendants “defend a charge of bad faith *by referencing specific communications with attorneys* that purportedly provided a good-faith basis for certain actions, and then refuse to allow any further investigation into those communications.” *Id.* (emphasis added).

In re County of Erie provides a clearer standard than *Hearn* and leads to a more balanced test for determining whether there has been a waiver of privilege. The reliance element gives more clarity to litigants since it is directly tied to the actions of the party seeking to protect the communications rather than the allegations of the complaint and degree of relevance. If the party has relied on the advice of counsel as an element of a claim or defense, it is logical that it should expect that this could effect a waiver. The relevance standard in *Hearn*, however, simply gives too much leeway to the *opposing* party, who has no direct relationship with the privilege, to establish a waiver.

Nevertheless, the *In re County of Erie* court signaled continued approval of the third element of *Hearn*, which examines whether upholding the privilege would deny the opposing party information vital to its claim or defense. *See* 546 F.3d at 229 (noting that no unfairness occurred to the party seeking the information as they were not denied access to any such vital information). Thus, *In re County of Erie* and its progeny still continue to focus, at least in part, on issues that are extraneous to the waiver question. Ultimately, if a party has been diligent in maintaining the confidential nature of its communications with counsel and has not asserted reliance on the advice in support of a claim or defense, the privilege should hold. The importance of the information or unfairness that would result from its protection should have no

bearing on the analysis in these circumstances. To hold otherwise would contradict longstanding South Carolina policy upholding the protections of the attorney-client privilege.

E. If the Court is inclined to adopt a specific test, the *Rhone-Poulenc* test offers the most protection and is aligned with South Carolina law.

The *Rhone-Poulenc* test closely comports with existing South Carolina law and policy, as it involves an entirely objective analysis. The court looks to whether the party in question placed the advice of counsel directly at issue by asserting a claim or defense and then attempting to prove that claim or defense by describing or relying on an attorney-client communication. *See* 32 F.3d at 863. If it did, the party waives the privilege; if it did not, the privilege remains intact.

Essentially, this prevents a party from using the privilege both as a sword and shield, and is consistent with South Carolina law on waiver, which focuses on the waiving party's acts or conduct supporting waiver rather than external factors. *See Raleigh & C.R. Co. v. Jones*, 104 S.C. 332, 88 S.E. 896, 898 (1916) (explaining that attorney-client privilege is waived if a party "testifies on cross-examination as to communications between him and his attorney, without insisting upon his right to refuse to testify as to privileged communications"); *Floyd*, 365 S.C. at 70, 615 S.E.2d at 473 (affirming trial judge's finding that party waived privilege and opened the door to admission of two letters by testifying that "he followed the advice of counsel"); *see also Davis*, 409 S.C. at 292-93, 762 S.E.2d at 549 (Pleicones, J., concurring in part and dissenting in part) ("Notwithstanding that caution must be exercised in finding waiver, it is widely recognized that a client impliedly waives the privilege when he relies on confidential communications with his attorney to make out a claim or defense."); *cf. State v. Thompson*, 329 S.C. 72, 77, 495 S.E.2d 437, 439 (1998) (rejecting argument that defendant impliedly waived attorney-client privilege because he should have known his attorney would have to disclose statements he made to a psychiatrist in order to effectively negotiate a plea agreement, noting that it was "reasonable"

that defendant expected the attorney would “make a recommendation based on [the] Psychiatrist’s report, without revealing his actual statements”); *State v. Hitopoulos*, 279 S.C. 549, 551, 309 S.E.2d 747, 749 (1983) (rejecting argument that defendant waived the attorney-client privilege by testifying on behalf of the State pursuant to a plea negotiation, noting that “[m]erely taking the witness stand does not constitute waiver of the privilege”).¹¹

The *Rhone-Poulenc* test, or an analogous one, has been adopted by a number of courts, including one case from the District of South Carolina. See *First S. Bank v. Fifth Third Bank, N.A.*, No. 7:10-2097-MGL, 2013 WL 1840089, at *9 (D.S.C. May 1, 2013) (quoting the *Rhone-Poulenc* standard). Despite the body of law from the District of South Carolina applying the *Hearn* test, the court in *First South Bank* explained that for waiver to occur via assertion of an affirmative defense of good faith, the party must both assert a claim or defense and attempt to prove it by disclosing or describing an attorney-client communication. *Id.* The court took a different approach from the other cases in the District analyzing the at issue waiver under the *Hearn* test, but did not detail why other than noting the “rationale does not apply squarely to this case.” *Id.*

Many other jurisdictions have also followed this standard. Wisconsin’s Court of Appeals, for example, rejected the “expansive” view of the “at issue” waiver, favoring instead the more restrictive view supporting that “the attorney-client privilege is waived when the privilege holder *attempts to prove a claim or defense* by disclosing or describing an attorney-client communication.” *State v. Hydrate Chemical Co.*, 582 N.W.2d 411, 418 (Wis. Ct. App.

¹¹ Additionally, as the Court of Appeals has explained in the context of waiver generally: “An implied waiver results from *acts and conduct of the party* against whom the doctrine is invoked from which an intentional relinquishment of a right is reasonably inferable.” *SPUR at Williams Brice*, 415 S.C. at 91, 781 S.E.2d at 125 (emphasis added) (quoting *Lyles v. BMI, Inc.*, 292 S.C. 153, 158–59, 355 S.E.2d 282, 285 (Ct. App. 1987)).

1998) (emphasis added). Thus, the mere fact that a privileged document is relevant to a claim or defense does not result in a waiver. *Id.* Instead, the privilege holder must specifically intend to use that document to prove the claim or defense. *Id.*

Louisiana courts have reached the same conclusion. See *Dixie Mill Supply Co. v. Cont'l Cas. Co.*, 168 F.R.D. 554, 555-56 (E.D. La. 1996) (“Under Louisiana law, a party waives the attorney-client privilege when he ‘pleads a claim or defense in such a way that he will be forced inevitably to draw upon a privileged communication at trial in order to prevail.’” (citation omitted)); *Ill. Union Ins. Co. v. La. Health Serv. & Indem. Co.*, No. CV-16-6604, 2017 WL 2955355, at *3 (E.D. La. Apr. 13, 2017) (“At-issue waiver occurs under Louisiana law when a party places privileged communications ‘at issue,’ which means more than simply that the client’s communications with his lawyer or accountant have been referred to in litigation or that they may be relevant to the subject matter of the litigation.”). As have Florida courts. See *Coates v. Akerman, Senterfitt & Eidson, P.A.*, 940 So. 2d 504, 508 (Fla. Dist. Ct. App. 2006) (“[W]hen a party has filed a claim, based upon a *matter ordinarily privileged, the proof of which will necessarily require that the privileged matter be offered in evidence*, we think that he has waived his right to insist, in pretrial discovery proceedings, that the matter is privileged.” (emphasis in original) (quoting *Savino v. Luciano*, 92 So.2d 817, 819 (Fla. 1957))).

The Eastern District of Michigan also adopted this test in *U.S. Fire Ins. Co. v. City of Warren*, No. 2:10-CV-13128, 2012 WL 1454008, at *7 (E.D. Mich. Apr. 26, 2012). The *U.S. Fire* court rejected as meritless the defendant’s argument that an insurer’s denial of almost every allegation in its answer to a bad faith claim “implicitly placed at issue the good faith or bad faith nature of its claims handling activities and coverage determinations.” *Id.* As the court explained, although a party may impliedly waive a privilege by placing the subject matter of

privileged communications at issue, “this waiver is construed narrowly.” *Id.* “An implied waiver occurs *only* where the party’s ‘pleading places at issue the subject matter of a privileged communication in such a way that the party holding the privilege will be *forced to draw upon the privileged material at trial in order to prevail.*’” *Id.* (emphasis added) (quoting *In re Lott*, 424 F.3d 446, 453 (6th Cir. 2005)). As the court explained, the cases on this issue:

stand for the principle that when a party asserts a defense of good faith or reasonableness, *and affirmatively offers testimony* that the party consulted with their attorney as factual support for the defense, *and when counsel’s advice in some way supports the defendant’s good faith belief*, the defendant has put his counsel’s advice “at issue” and thereby waives the attorney client privilege on the narrow subject matter of those communications.

Id. (emphasis added) (quoting *Henry v. Quicken Loans, Inc.*, 263 F.R.D. 458, 469 (E.D. Mich. 2008)).

The Northern District of Illinois noted that Illinois courts have not adopted a specific test, but it believed they would follow the reasoning in *Rhone-Poulenc*, a “leading case” on the subject. *Am. Nat. Bank & Tr. Co. of Chicago v. Allmerica Fin. Life Ins. & Annuity Co.*, No. 02 C 5251, 2005 WL 6249757, at *2 (N.D. Ill. July 14, 2005). The *American National* court explained that “[b]y denying that it acted in bad faith [the defendant insurer] has done nothing to waive the attorney-client privilege concerning communications which might be relevant to the issue of bad faith.” *Id.*

New Jersey Manufacturers Ins. Co. v. Brady, No. 3:15-CV-02236, 2017 WL 264457 (M.D. Pa. Jan. 20, 2017) applied the *Rhone-Poulenc* test in the context of a case involving insurance bad faith issues. *Id.* at *12. The court found that the insurer did not place its attorneys’ advice at issue by attempting to prove a claim or defense by disclosing or describing an attorney-client communication. *Id.* at *13. The court further explained that even where the

insurer stated it relied on the advice of counsel in making a decision that, standing alone, “does not show that the party took an ‘affirmative step’ to place that advice in issue.” *Id.* This was “especially true” since the deposition testimony upon which the purported waiver was based was “elicited in response to questions posed by defense counsel.” *Id.*

If this Court does adopt a specific test, therefore, it should follow these decisions and adopt the *Rhone-Poulenc* test. As previously noted, this test comports with South Carolina law on privilege and waiver, as it centers on the actions of the party seeking protection. As the Richmond article explains:

The *Rhone-Poulenc* test is superior first because it adheres to the principle that the attorney-client privilege is a shield, not a sword.

Second, by leaving to the client the decision whether to surrender the privilege by placing its lawyer's advice at issue, the test ***provides certainty, consistency, and predictability*** as to any possible application of the at-issue exception and the circumstances in which the privilege may be lost. For this reason, the *Rhone-Poulenc* test also ***honors the principle that the client alone—not an adversary—holds and controls the privilege.***

Third, by stabilizing the at-issue exception, the *Rhone-Poulenc* test encourages clients to confide in their lawyers without having to fear that their communications will be disclosed without their consent. In this way the test ***embraces the basic principle underlying the attorney-client privilege, which is to encourage full and frank communications between lawyers and clients,*** thereby promoting the broader public interest in fidelity to law and the administration of justice.

Fourth, by restricting the at-issue exception to well-defined circumstances, the *Rhone-Poulenc* test ***discourages discovery disputes and thus reduces litigation costs.***

Fifth, this test promotes fundamental principles of justice by ***discouraging parties from seeking an unfair litigation advantage*** through the attempted discovery of adversaries’ privileged communications.

Richmond, supra, at 30-31 (citations omitted) (emphasis added).

Therefore, for all of the reasons specified herein, Mt. Hawley would urge the Court to adopt the *Rhone-Poulenc* test if it is inclined to formally recognize a test for the “at issue” waiver under South Carolina law. This standard aligns with existing South Carolina law requiring “distinct” and “unequivocal” action to effect a waiver of attorney-client privilege. At its heart, the “at issue” waiver attempts to prevent the attorney-client privilege from being used both as a sword and a shield at the same time. In other words, it recognizes that it would be inequitable for a party to affirmatively assert that it complied with the law because it followed its attorney’s advice, while at the same time depriving the opposing party any information about the nature of the advice. This is the basic thrust of both *Floyd* and *Rhone-Poulenc*, and therefore this test comports with South Carolina law.

IV Even if the Court were to adopt a specific test for determining waiver of the attorney-client privilege, it should reject the District Court’s broad formulation.

As noted above, *City of Myrtle Beach* was the genesis of the body of District of South Carolina cases applying the “at issue” waiver exception.¹² That decision itself relied on *Hearn* for guidance on the applicability of the test. As detailed above, Mt. Hawley would reiterate that the Court should reject any formulation of the *Hearn* test. However, if the Court is inclined to approve of *Hearn*, it should confirm that the District Court’s ruling here reached beyond the boundaries of even that broad standard.

¹² The District Court’s recognition and application of this exception was an improper expansion of South Carolina policy. See *St. Paul Fire & Marine Ins. Co. v. Jacobson*, 48 F.3d 778, 783 (4th Cir. 1995) (“[T]he federal courts in diversity cases, whose function it is to ascertain and apply the law of a State as it exists, should not create or expand that State’s public policy.”). The proper forum to speak on such a fundamental alteration of South Carolina policy was this Court, not the District Court or even the Fourth Circuit (as that court acknowledged by certifying the question presented). This Court is not beholden to those cases and is fully empowered to define the scope of the attorney-client privilege as it sees fit.

A. The District Court’s ruling is even more liberal than the *Hearn* test.

Even the previous decisions from the District of South Carolina that found the waiver of the attorney-client privilege based on the *Hearn* test were more protective than the District Court in this case.

The *City of Myrtle Beach* order appears to have been the genesis of the “at issue” waiver of attorney-client privilege by the District of South Carolina. After setting forth the analysis detailed above, the *City of Myrtle Beach* court ultimately determined that ***by raising certain affirmative defenses*** in its answer, the defendant “injected into th[e] case the issues of law and fact contained in the documents for which it seeks protection,” and thus a waiver occurred. 2010 WL 3420044 at *7. Therefore, despite its unsupported proclamation that waiver can occur due to a party’s “assertion of a new position of law or fact,” *City of Myrtle Beach* implicitly recognized what numerous other courts have found—to find a waiver pursuant to *Hearn*, the party must at the very least have affirmatively pled its good faith and/or reasonableness.

Other District of South Carolina cases examining the issue also support, at a minimum, this affirmative pleading requirement. *See, e.g., E. Bridge Lofts Property Owners Ass’n, Inc. v. Crum & Forster Specialty Ins. Co.*, No. 2:14-CV-2567-RMG, 2015 WL 12831737 (D.S.C. June 11, 2015). In *East Bridge*, Judge Gergel determined that a party may waive attorney-client privilege if it places a privileged communication at issue. *Id.* at *2. However, as he explained, “where an insurer in a bad faith claim ***asserts as an affirmative defense that it acted in good faith and with a reasonable basis***, the insurer puts at issue the evidence it had before it at the time it denied the claim.” *Id.* (emphasis added).¹³ In *East Bridge*, the insurer did not simply deny liability, but instead pled an affirmative defense of “no bad faith – reasonable basis for

¹³ As noted above, “good faith” is not a recognized affirmative defense to a claim for bad faith under South Carolina law.

denying coverage.” See Ans. to Second Am. Compl., *E. Bridge Lofts Property Owners Ass’n, Inc. v. Crum & Forster Specialty Ins. Co.*, No. 2:14-CV-2567-RMG (D.S.C. Apr. 7, 2015), ECF No. 40 at ¶ 149.

Likewise, in a subsequent decision, Judge Gergel reiterated that a party “can waive the attorney-client privilege by ‘*asserting reliance on the advice of counsel as an affirmative defense*, thereby placing that advice directly at issue.’” *U.S. ex rel. Lutz v. Berkeley Heartlab, Inc.*, No. 9:11-CV-1593-RMG, 2017 WL 1282012, at *3 (D.S.C. Apr. 5, 2017) (emphasis added) (quoting *Smith v. Scottsdale Ins. Co.*, 40 F. Supp. 3d 704, 724 (N.D.W. Va. 2014)). As he explained, “[w]hen a party asserts an advice of counsel defense, he waives the attorney-client privilege as to the entire subject matter of that defense.” *Id.*

The other decisions applying the “at issue” waiver from the District of South Carolina are in accord. See *Graham v. Nat’l Union Fire Ins. Co. of Pittsburgh, PA*, No. 0:16-cv-01153-MBS, 2017 WL 116798, at *4-5 (D.S.C. Jan. 12, 2017) (“Defendant asserts *as an affirmative defense* that it ‘did not act unreasonably or in bad-faith.’ . . . The court finds that Defendant implicitly waived attorney-client privileged by asserting the affirmative defense [that it did not act unreasonably or in bad faith].” (emphasis added)); *State Farm Fire & Cas. Co. v. Admiral Ins. Co.*, No. 4:15-cv-2745-RMG, 2016 WL 4051271, at *4 (D.S.C. July 25, 2016) (noting the plaintiffs’ answer to the counterclaim admitted it “owed a duty to act in good faith and reasonably in handling the claim . . . *and asserts that it did so*” (emphasis added)); *Wade v. Chase Bank USA, N.A.*, No. 2:12-cv-3565-RMG, 2013 WL 12154996, at *2 (D.S.C. July 3, 2013) (“[W]here an insurer in a bad faith claim *asserts as an affirmative defense that it acted in good faith*, the insurer puts at issue the evidence it had before it at the time it denied the claim,

including communications with counsel relevant to its state of mind.” (emphasis added))¹⁴; *Hege v. Aegon USA, LLC*, No. 1:10-cv-1635-GRA, 2011 WL 1791883, at *5 (D.S.C. May 10, 2011) (“Like the insurer in *City of Myrtle Beach*, Transamerica asserts, *as affirmative defenses*, that it acted in good faith” (emphasis added)).

B. The District Court’s ruling goes beyond these other cases and eviscerates, for insurance companies at least, the attorney-client privilege in this State.

This is not a case where the defendant has pled the advice of counsel. It is not even a case where the defendant asserted “good faith” as a defense. In the Magistrate Judge’s Report and Recommendation, which the District Court adopted in its entirety, the court determined that Mt. Hawley waived the attorney client privilege simply by *denying* allegations it acted in bad faith and asserting in its answer that it complied with the terms of the insurance policy. This simple act of challenging the Plaintiff’s allegation placed privileged information “at issue.” As the cases cited above explain, a denial did not affirmatively inject Mt. Hawley’s communications with counsel into the case and cannot effect a waiver, even under the *Hearn* test. Mt. Hawley did not assert, expressly or impliedly, that it has relied on the advice of counsel as a defense or counterclaim, or even assert in its answer an affirmative defense or counterclaim that it should prevail because it acted in good faith. Therefore, even if the Court were to recognize that the *Hearn* test applied under South Carolina law, the Court should reject the District Court’s holding.

The District Court’s interpretation of the “at issue” waiver will hamstring the ability of the Mt. Hawley and other insurers to defend against bad faith actions in the District of South Carolina and to seek advice of counsel. Instead, insurers will be confronted with a Hobson’s choice of admitting bad faith or forfeiting privileged communications with counsel. Under the

¹⁴ Here, Mt. Hawley has not denied the claim, and thus *Wade* is inapposite.

District Court's framework, the mere denial of an allegation of bad faith places the attorney-client privilege "at issue." An insurer, of course, should be entitled to deny it acted in bad faith (*i.e.*, deny liability) if such a denial would be with good reason. It would be illogical to expect otherwise. Under the District Court's holding, however, this will automatically result in a waiver of attorney client privilege for *any* information relating to plaintiff's bad faith claim. Although the District Court asserts that there is no "per se" waiver in bad faith cases, in operation this is precisely what would be the result in the vast majority of instances.

Furthermore, the District Court's decision held that a waiver occurred despite the *plaintiff* placing the question of good or bad faith at issue, not Mt. Hawley. Undoubtedly a party can waive its own privilege. The District Court's rule, however, permits the party's *opponent* to force a waiver of privilege by placing the insurer's bad faith at issue. This is unreasonable, unfair, and impractical.

The District Court's holding, therefore, reaches further than the other District of South Carolina cases, which all recognized an affirmative pleading requirement either via affirmative defense or counterclaim for the information to be "at issue." The District Court's standard is fundamentally unfair, as privilege is waived primarily because the information contained in the communication is relevant to a claim or defense. No amount of precaution permits a party to protect the confidential nature of the communications. To illustrate the perversity of this rule, it would effectively prevent an insurer from seeking confidential legal advice on whether a particular action could subject it to liability under South Carolina's bad faith law. This result would fly in the face of the policy underlying the attorney-client privilege under South Carolina law. Therefore, the Court should reject it.

C. The District Court’s requirement that there be a prima facie showing of the element of bad faith fails to temper the sweeping effect of the *Hearn* test.

In addition to finding that a waiver occurred, the *City of Myrtle Beach* court relied, in part, on the fact that the plaintiff presented a “prima facie case of bad faith” in issuing its order compelling production of the privileged materials. *City of Myrtle Beach v. United Nat. Ins. Co.*, No. CIV.A. 4:08-1183, 2010 WL 3420044, at *7 (D.S.C. Aug. 27, 2010). The District Court noted that it is “debatable” whether such a showing is required under *City of Myrtle Beach*, as that court “never fully explained the significance of this discussion.” *ContraVest Inc. v. Mt. Hawley Ins. Co.*, 273 F. Supp. 3d 607, 618 (D.S.C. 2017).¹⁵ The District Court expressed uncertainty over whether to recognize this requirement, but noted this is akin to *Hearn*’s requirement that “a substantial showing of merit to plaintiff’s case must be made before a court should apply the exception.” *Id.* (quoting *Hearn*, 68 F.R.D. at 582). The District Court thus held that if “the *City of Myrtle Beach* court’s rejection of the per se waiver rule has any meaning, that decision must be read to require a prima facie showing of bad faith before the at-issue waiver can be applied.” *Id.* at 619. The District Court explained that this means a prima facie showing only as to the “element of bad faith, not the entire cause of action.” *Id.* at 620 (emphasis in original).

The District Court appears to believe that this additional element offers protection to insurers and sufficiently tempers the impact of the *Hearn* test. However, the inherent unfairness of the *Hearn* test is not mitigated by the “prima facie” showing requirement.

¹⁵ In fact, another District Judge argued that this is *not* part of the waiver analysis under *City of Myrtle Beach/Hearn*. See *E. Bridge Lofts*, 2015 WL 12831737, at *3 (“While the court in *City of Myrtle Beach* found that the city had presented a prima facie case of bad faith, nothing in the opinion indicates that such a finding is necessary for Defendant to have waived the privilege. When the Defendant has voluntarily injected an issue into the litigation and the Defendant bears the burden of establishing lack of waiver of the privilege, the Court sees no reason to require Plaintiff to make a prima facie case of bad faith.”).

First, *Hearn* supports that this “merits” element does not come into effect until after the court has determined that a waiver occurred. If the court finds there has been a waiver, then it determines whether the party seeking the information made a substantial showing of merit sufficient to warrant production. *See Hearn*, 68 F.R.D. at 582. The District Court’s order conflates the prima facie analysis and the *Hearn* factors, resulting in a confusing and unnecessarily fact-based inquiry. *See generally ContraVest*, 273 F. Supp. 3d at 617-22. This Court should reject such a formulation, which would result in inconsistent results.

Second, the “prima facie” test is really no test at all. It is but a small speed bump on the highway to discovering privileged, sensitive communications. And it will not end there. The next shoe to fall will be depositions of claim representatives and counsel on their communications because, after all, if a *writing* is not privileged, an *oral* communication is not either.

This supposed failsafe of a “prima facie showing” is merely window dressing attempting to avoid the appearance of an automatic waiver rule, which the District Court acknowledged would seem to result in its absence. To make a prima facie showing on the element of bad faith, a party would merely need to obtain an affidavit from an expert noting that he or she believes that there may have been bad faith for one reason or another. This would become a pro forma step in any bad faith case and the end result would be precisely what the District Court was attempting to avoid—an automatic waiver rule.

Because the District Court’s “prima facie” standard fails to offer sufficient protection to parties seeking to preserve privilege, the Court should reject it. Even if the Court adopts *Hearn*, this analysis applied by the District Court is inconsistent with the standard articulated by that court. Thus, the Court should decline to adopt it.

V. Recognition of the “at issue” waiver only in cases involving insurance companies would violate equal protection.

Respondents have intimated that special circumstances surrounding insurance bad faith cases warrant a different standard for waiver of the attorney-client privilege. Such a result would deny insurance companies equal protection under the law.

Both the United States and South Carolina Constitutions provide that no “person shall be denied the equal protection of the laws.” U.S. Const. amend. XIV, § 1; S.C. Const. art. I, § 3. “The sine qua non of an equal protection claim is a showing that similarly situated persons received disparate treatment.” *Grant v. S.C. Coastal Council*, 319 S.C. 348, 354, 461 S.E.2d 388, 391 (1995); *see also Sloan v. Bd. of Physical Therapy Exam’rs*, 370 S.C. 452, 481, 636 S.E.2d 598, 613 (2006) (“A crucial step in the analysis of any equal protection issue is the identification of the pertinent class. . . .”), *overruled on other grounds by Joseph v. S.C. Dep’t of Labor, Licensing & Regulation*, 417 S.C. 436, 790 S.E.2d 763 (2016).

“A government classification does not violate the Equal Protection Clause, however, if the classification can survive the applicable level of scrutiny.” *Id.* “So long as the statute ‘does not implicate a suspect class or abridge a fundamental right, the rational basis test is used’ to determine whether the classification falls into the prohibited group.” *Bodman v. State*, 403 S.C. 60, 69-70, 742 S.E.2d 363, 367-68 (2013) (quoting *Denene, Inc. v. City of Charleston*, 359 S.C. 85, 91, 596 S.E.2d 917, 920 (2004)). “A classification will survive rational basis review when it bears a reasonable relation to the legislative purpose sought to be achieved, members of the class are treated alike under similar circumstances, and the classification rests on a rational basis.” *Id.* “The fact that the classification may result in some inequity does not render it unconstitutional.” *Davis v. Cnty. of Greenville*, 313 S.C. 459, 465, 443 S.E.2d 383, 386 (1994).

If the court only applies the “at issue” exception with regard to insurance companies defending their actions in complying with insurance contracts, it would deprive insurance companies of equal protection. Insurance companies would be placed at a distinct disadvantage compared to other persons and entities, because they—alone among the persons and entities who enter contracts in this State every day—would be denied the right to confidential legal advice in connection with those contracts.

Such a result would not meet the rational basis test. All contracts in South Carolina have a covenant of good faith and fair dealing. *Peterson v. W. Am. Ins. Co.*, 336 S.C. 89, 102, 518 S.E.2d 608, 614 (Ct. App. 1999); *Calcaterra v. City of Columbia*, 315 S.C. 196, 198, 432 S.E.2d 498, 500 (Ct. App. 1993). Therefore, every breach of contract claim could support a waiver argument if the plaintiff asserts the defendant acted in bad faith. If the Court is going to recognize a waiver, it should not limit it solely to insurance contracts. Singling out insurance companies to remove the right to confidential legal advice would have no rational basis since all parties have a duty to act in good faith under all contracts.

Moreover, limiting the “at issue” waiver to the insurance bad faith context would place insurance companies on a different footing based on the type of claims asserted against them. There are a number of torts and contractual claims that a claimant may bring against an insurance company. Under claims for fraud, negligent misrepresentation, or even breach of the insurance contract, attorney-client privileged advice would likely be just as desirable for the claimants to obtain. Only insurers sued for bad faith, however, would be at risk of losing the privilege under the “at issue” waiver. Confining the exception to insurance bad faith lacks any reasonable justification and would result in arbitrary classification simply due to the type of claims asserted against the insurer.

VI. If the Court formally recognizes an exception to the attorney-client privilege, the holding should only apply prospectively.

Finally, no matter what test it adopts, if the Court formally recognizes the “at issue” exception to the attorney-client privilege, it should find that it will only apply prospectively. This Court has long recognized that “a judicial decision that creates a new liability where none formerly existed is applied prospectively only.” *Hardaway v. Cnty. of Lexington*, 314 S.C. 22, 24, 443 S.E.2d 569, 570 (1994); *see also Hupman v. Erskine College*, 281 S.C. 43, 44, 314 S.E.2d 314, 315 (1984) (“Prospective application is required when liability is created where formerly none existed.”). South Carolina cases have also “held prospective application to be appropriate” in cases where “immunities have been dissolved,” or the holding “effected more than remedial or procedural changes.” *Toth v. Square D Co.*, 298 S.C. 6, 9, 377 S.E.2d 584, 586 (1989) (collecting cases).

Expansion of the waiver rules relating to the attorney-client privilege would be akin to dissolving immunity and/or creating new liability for defendants. Existing South Carolina law does not support such a waiver and therefore many persons and entities, like Mt. Hawley here, operated under the expectation that their privileged communications with counsel would remain protected assuming there was not a distinct and unequivocal waiver. Retroactive application would deny Mt. Hawley the fundamental right to confidential legal advice under circumstances in which it believed the privilege would be preserved.

Therefore, to the extent the Court expands waiver principles under South Carolina law, the holding should only apply on a prospective basis.

CONCLUSION

For the reasons stated above, the Court should repudiate the *Hearn* test and answer “no” to the certified question. Regardless of the test applied, the Court should find that South

Carolina law does not support application of the “at issue” exception to the attorney-client privilege such that a party may waive the privilege by denying liability in its answer.

Respectfully submitted,

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October 22, 2018

THE STATE OF SOUTH CAROLINA
In The Supreme Court

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OCT 22 2018

CERTIFIED QUESTION FROM THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT
S.C. SUPREME COURT

Appellate Case No. 2018-001170

In re: Mt. Hawley Insurance Company..... Petitioner,

In Which Contravest, Inc., Contravest Construction Company, and Plantation Point Horizontal Property Regime, as assignees, are..... Respondents.

CERTIFICATE OF COUNSEL

The undersigned certifies that this Final Petitioner's Brief complies with Rule 211(b),
SCACR.

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THE STATE OF SOUTH CAROLINA
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CERTIFIED QUESTION FROM THE UNITED STATES COURT OF
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OCT 22 2018

S.C. SUPREME COURT

Appellate Case No. 2018-001170

In re: Mt. Hawley Insurance Company..... Petitioner,

In Which Contravest, Inc., Contravest Construction
Company, and Plantation Point Horizontal Property
Regime, as assignees, are..... Respondents.

PROOF OF SERVICE

I, the undersigned Attorney of the offices of Nelson Mullins Riley & Scarborough LLP, attorneys for Petitioner, do hereby certify that I have served all counsel in this action with a copy of the pleading(s) hereinbelow specified by mailing a copy of the same by United States Mail, postage prepaid, to the following address(es):

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