

NO. 46301-6-II

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COURT OF APPEALS, DIVISION II  
OF THE STATE OF WASHINGTON

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BY *[Signature]*  
DEPUTY

LISA STEEL, individually and as Guardian ad litem for J.T., a  
minor; DOUGLAS THOMPSON and KRISTI BARBIERI, individually  
and as Guardian ad litem for S.R.B., a minor,

Petitioners/Plaintiffs,

vs.

OLYMPIA EARLY LEARNING CENTER, et al.,

Respondents/Defendants,

vs.

PHILADELPHIA INDEMNITY INSURANCE COMPANY

Respondent/Intervenor,

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**REVISED BRIEF OF RESPONDENT  
PURSUANT TO COURT ORDER OF OCTOBER 30, 2015**

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## I. INTRODUCTION

[A] reasonableness determination is based upon what was known by the parties at the time of settlement.<sup>1</sup>

[T]he only way to determine the knowledge of the parties is by looking in the attorneys' files. This is especially true where the attorneys are the primary source of *Glover/Chaussee*<sup>2</sup> information.<sup>3</sup>

The above is a verbatim quote taken from a brief filed by *Appellants/Plaintiffs* prior to this appeal and reflects Plaintiffs' position regarding privileged documents in the files of Respondent Philadelphia Indemnity Insurance Company ("Philadelphia").<sup>4</sup>

Now, on appeal, Plaintiffs' position is that *their* attorney files are irrelevant to the reasonableness of the settlement. Plaintiffs' new position is not only wrong (reasonableness is determined based upon what was known by the parties at the time of settlement,<sup>5</sup> and, in this case, the only way to determine the knowledge of the parties is by looking in the attorneys' files), it is inconsistent with how Appellants proceeded below. Thus, Plaintiffs have waived any right to argue the trial court abused its discretion or erred in permitting Philadelphia limited discovery of

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<sup>1</sup> CP at 0-000002183

<sup>2</sup> *Glover v. Tacoma General Hospital*, 98 Wn.2d 708, 711, 658 P.2d 1230 (1983); *Chaussee v. Maryland Casualty Co.*, 60 Wn. App. 504, 803 P.2d 1339 (1991).

<sup>3</sup> CP at 0-000002536

<sup>4</sup> CP at 0-000002532-2538

<sup>5</sup> *Bird v. Best Plumbing Grp., LLC*, 175 Wn.2d 756, 775-776, 287 P.3d 551 (2012).

privileged documents that focused directly on the reasonableness factors.

This Court should reject Plaintiffs' attempt to recast the trial court's case-specific ruling related to this stipulated settlement, which presents unique and extreme facts, as a blanket ruling effecting privilege following any stipulated settlement. Philadelphia did not seek, and the trial court did not establish, a blanket rule regarding attorney-client privilege and work product in the context of reasonableness hearings. Rather, the trial court exercised its discretion based upon the unique facts of this case and in accord with existing Washington law regarding reasonableness determinations, the scope of privilege, and waiver of privilege.

It is Plaintiffs who seek a special blanket rule that would strip trial courts of the ability to apply ordinary rules of discovery related to the reasonableness of a stipulated judgment. The special exception Plaintiffs seek would unreasonably obstruct discovery at the very heart of reasonableness and conceal unwarranted practices, such as fraud and collusion. It would also be contrary to *Bird v. Best Plumbing*,<sup>6</sup> which reaffirmed that trial courts need broad discretion in determining reasonableness.

To the extent the trial court ultimately found there was a limited waiver of Plaintiffs' privilege as to some specific documents, this was in a

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<sup>6</sup> *Best Plumbing*, 175 Wn.2d at 774-75.

case-specific factual setting in which Plaintiffs' counsel exclusively controls virtually all information about the proposed \$25 million settlement and is a necessary witness concerning its reasonableness. Courts have long held that when an attorney is a material witness, privilege is waived.<sup>7</sup> Moreover, the trial court exercised its discretion to tailor discovery to the case, which is precisely what appellate courts have directed trial courts to do when tasked with determining the reasonableness of stipulated settlements.

The court did not abuse its discretion in finding a limited waiver of privilege as to specific documents directly relevant to the reasonableness of the stipulated settlement. Therefore, the trial court's decision should be affirmed.

## **II. ASSIGNMENTS OF ERROR AND ISSUES PERTAINING TO ASSIGNMENTS OF ERROR**

### **A. Objections to Appellants' Assignments of Error**

Philadelphia requests the Court to strike Assignment of Error No. 1 and all related Issues Pertaining to Assignments of Error No. 1 because the trial court's August 27, 2013 order appointing the special master is not subject to this appeal. Philadelphia requests the Court strike Assignment

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<sup>7</sup> *Kammerer v. W. Gear Corp.*, 96 Wn.2d 416, 420, 635 P.2d 708 (1981).

of Error No. 2 and Issues 1 through 6 because they exceed the limited issue under appeal.

Issues No. 1 through 6 should be struck because Philadelphia did not ask for, and the trial court did not adopt, a blanket waiver rule. The trial court's ruling was clearly based upon the unique circumstances of this case and a review of the documents withheld from production. Further, there are multiple bases under existing Washington law for the trial court's ruling. In addition, Issue No. 5 should be struck because the trial court did not rule that work product is waived regardless of relevancy.

**B. Philadelphia's Statement of Issues Pertaining to Assignments of Error**

Did the trial court abuse its discretion in finding a limited waiver of privilege as to specific documents directly relevant to the factors that must be evaluated to determine the reasonableness of the stipulated settlements in this case?

**III. STATEMENT OF THE CASE**

**A. The Lawsuit and Settlement**

Eli Tabor, a former employee of Olympia Early Learning Center ("OELC"), who was never a defendant in the underlying consolidated litigation, has been convicted and incarcerated for sexual molestation of two children who attended daycare at OELC, including one of the minor

plaintiffs and another child, whose family has not yet brought a claim against OELC. In addition, despite a lack of evidence, Plaintiffs alleged that Tabor sexually abused other children who attended the daycare. OELC's insurer, Philadelphia retained as defense counsel attorney Michael Bolasina, a lawyer experienced in defending sex abuse cases. Philadelphia never disputed coverage, defended without reserving rights, looked for early opportunities to settle, offered to participate in mediation, and offered its policy limits to settle all claims against the defendants.

But there were impediments to settlement. First, defense counsel and the insureds were concerned about another potential claimant, a child identified as N.D., who Tabor had been convicted of molesting.<sup>8</sup> Second, defense counsel reported that five of the six existing claims were nuisance value claims.<sup>9</sup> Police and DSHS/CPS found evidence that only one of the six minor plaintiffs had been abused, and that he had been abused in his home, not the OELC facility.<sup>10</sup> Further, Plaintiffs had "done little to construct a serious damage case" for the child abused at his home.<sup>11</sup> Third, Plaintiffs claimed that they could "stack" four \$1 million limits to achieve \$4 million in insurance. Fourth, defense counsel believed the case

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<sup>8</sup> CP at 0-000001217.

<sup>9</sup> CP at 0-00000234.

<sup>10</sup> CP at 0-000002318-2323.

<sup>11</sup> CP at 0-000002323.

could not settle until the stacking issue was resolved.<sup>12</sup>

Thus, after conferring with defense counsel, Philadelphia proposed a coverage mediation to address the stacking issue.<sup>13</sup> However, mediation never occurred because Plaintiffs rejected Philadelphia's requests to engage in mediation.<sup>14</sup> Then, after again conferring with defense counsel and also with personal counsel for the two defendants,<sup>15</sup> Philadelphia filed a declaratory relief/interpleader action in federal district court. When defense counsel provided a copy of the interpleader complaint to Plaintiffs' counsel, instead of agreeing to stay the underlying litigation so that the limits and additional claimant issues could be resolved to facilitate settlement, Plaintiffs' counsel offered a take-it-or leave-it \$25 million stipulated settlement.<sup>16</sup>

On September 24, 2012, before either side had conducted expert discovery and before potential witnesses had been disclosed in three of the cases, Defendants agreed to Plaintiffs' counsel's request that they stipulate to entry of judgments totaling \$25 million in exchange for Plaintiffs' written agreement that they would only seek to collect the judgments from Defendants' insurer. The proposed stipulated judgments were supported

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<sup>12</sup> CP at 0-000000464.

<sup>13</sup> CP at 0-000002030 – 2031.

<sup>14</sup> *Id.*

<sup>15</sup> CP at 0-000000466 – 468.

<sup>16</sup> CP at 0-000000484, 0-000001084 – 1085.

by factual “confessions” drafted by Plaintiffs’ counsel and signed by Defendants, which contradicted the evidence, defense counsel’s reports to Philadelphia, and Defendants’ prior statements and testimony.<sup>17</sup>

As part of the settlement, Plaintiffs’ counsel “represents both Plaintiffs and Defendants in seeking a reasonableness determination concerning the settlement.”<sup>18</sup> Defendants produced to plaintiffs’ counsel complete un-redacted copies of their defense and personal counsels’ files including attorney-client communication and mental impression work product, which, as discussed below, Plaintiffs have been using offensively in the reasonableness phase of the litigation.

**B. Reasonableness Phase**

Shortly after the settlement, Plaintiffs requested a ruling that the proffered judgments totaling \$25 million reflected the “reasonable” value of Plaintiffs’ claims, offering as support, factual “confessions” that were drafted by Plaintiffs’ counsel. As soon as Philadelphia moved to intervene and conduct focused discovery related to the reasonableness of the settlement, Plaintiffs’ counsel began offering testimony regarding his own subjective beliefs regarding the reasonableness of the settlement:

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<sup>17</sup> See e.g. the factual confession related to the claims of M.M., CP at 0-000004956, ll. 10-18, and see CP at 0-00000477, ¶ 60, quoting an email defense counsel sent on the same day the stipulated settlements were executed, which stated that M.M is one of the children who never disclosed abuse at any time.

<sup>18</sup> CP at 0-000002533.

With six child abuse victims and a very strong liability claim, Plaintiffs' counsel believed from the very beginning that the combined value of the claims represented a multi-million dollar case, both in terms of settlement value and certainly in terms of potential jury verdicts.<sup>19</sup>

Plaintiffs' counsel offered testimony regarding facts and his strategy related to the stipulated settlements:

I learned many years ago that to demonstrate the absurdity of such claims of "collusion" that I must keep discussions with defense attorneys extremely limited and primarily in writing. I have done so here.

. . . I had no discussions with the defense attorneys about any of the terms of the agreement other than briefly with Paul Meyer for the Olympia Early Learning Center about whether I would agree to include a covenant not to execute against the Center to protect a piece of property it owned, and I ultimately agreed to do so. Other than that, I negotiated no terms with them: I simply advised them that I would either seek multi-million dollar jury verdict judgments and seek to execute against them personally and their insurance company or I would accept the offered consent judgments/assignments for the defense/insurance issues in exchange for covenants not to execute against them personally.<sup>20</sup>

Indeed, the amount of testimony offered by Plaintiffs' counsel related to the stipulated settlement is astounding. In the interest of brevity,

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<sup>19</sup> CP at 0-000000395.

<sup>20</sup> CP at 0-000004023, ¶¶ 77-78.

additional examples from Plaintiffs' counsel's declaration in opposition to Philadelphia's motion to intervene are discussed briefly in a footnote.<sup>21</sup>

Plaintiffs' counsel has continued to offer his testimony to support arguments on various issues. For example, in a March 7, 2013 motion, Plaintiffs' counsel explained why he refused to engage in mediation.<sup>22</sup>

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<sup>21</sup> Plaintiffs' counsel's 31-page declaration (CP at 0-00000456 – 486) is replete with his testimony regarding the reasonableness factors. In ¶ 6, he states that the liability case was "very simple and very compelling." In ¶ 7 he states "we felt very strongly" about the liability claim and that he believed this was a "multi-million dollar case." In ¶ 14, he testifies that he invited defense counsel to set depositions, which defense counsel never set. In ¶ 25, Plaintiffs' counsel explains why he reduced his \$4 million demand to \$3.95 million. In ¶ 34, he testifies regarding when he learned that OELC had personal counsel. In ¶ 37, he testifies about a phone call he had with defense counsel regarding the impact of Philadelphia's interpleader and his opinion regarding when Philadelphia should have filed the interpleader. In ¶ 42, he testifies about another unrelated sexual abuse case he was litigating. In ¶ 53, Plaintiffs' counsel opines that a letter Philadelphia's counsel sent to him was "the kind of which you only receive when the other side knows they are in deep trouble and have to begin attempting to revise history ..." In ¶ 55, he opines about why Philadelphia's counsel contacted defense counsel while he was in trial in another matter. In ¶ 63, he describes his reaction to and interpretation of an email that Philadelphia's counsel sent to defendants' attorney to argue that it "belies the incessant incantation of 'collusion' seen in [Philadelphia's counsel's] briefing and declaration here on this motion." In ¶¶ 64 and 65, Plaintiffs' counsel opines regarding why Philadelphia's counsel called Defendant Steve Olson's personal counsel and also opines that this phone call showed a lack of collusion in the stipulated settlements. (Not only is this an example of testimony by Plaintiffs' counsel, it is based upon information Plaintiffs' counsel gleaned from the files of Mr. Olson's personal counsel. Also, note that Philadelphia's counsel's communications with personal counsel were entirely proper and not at issue in this case.) In ¶ 68, Plaintiffs' counsel testifies about another communication between Philadelphia's counsel and Mr. Olson's personal counsel and argues it "belies ... Philadelphia Indemnity's argument that [Defendants' attorneys] have somehow 'colluded' against [Philadelphia]." In ¶ 69, he provides a list of reasons why the settlement was reasonable and not the product of collusion. In ¶ 71, he testifies about the verdict he received in another unrelated case. In ¶¶ 73 and 74, he testifies about defense counsel's lack of preparation based upon Plaintiffs' counsel's personal experience in other cases. He again testifies to a litany of problems for the defense while repeatedly stating that each problem was "a first in my experience in a case like this" and closes by stating "I have never seen such a high profile liability and damages case with literally no defense prepared for the first of a series of child sexual abuse trial less than four weeks away." In ¶ 75, he testifies about why this matter settled by consent judgment. In ¶ 76, he testifies about his experience in dealing with insurance bad faith issues and stipulated settlements.

Plaintiffs also forcibly argued that Defendants had no choice but to accept the \$25 million stipulated settlement because their counsel was ill prepared for trial:<sup>23</sup>

Philadelphia ... left them completely exposed to a trial *without having deposed a single plaintiff, without examining the plaintiffs in a defense psychological evaluation, without deposing a single lay witness, without deposing a single expert, without having a single expert of their own to contradict plaintiffs' experts, without having filed a summary judgment motion of any kind, without having submitted a single shred of evidence under the ER 904 procedure* and knowing that the liability position was not only weak, but potentially very explosive given that a number of employees were prepared to testify that OELC administrators had destroyed documents and lied under oath about their knowledge of the dangers posed by pedophile, Eli Tabor.<sup>24</sup>

\* \* \*

As of September 15, 2012, roughly four weeks prior to the first scheduled trial date before this Court, not a single one of my six child plaintiffs had been deposed and none of my seven plaintiff parents had been deposed – a first in my experience in a case like this; not a single child plaintiff or parent plaintiff had been asked to submit to defense medical/psychological examinations – a first in my experience in a case like this; the defendants took no depositions of lay witnesses – a first in my experience in a case like this; the defendants took no deposition of any of

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<sup>22</sup> CP at 0-000001255.

<sup>23</sup> Plaintiffs continue to infuse bad faith allegations against Philadelphia into the reasonableness hearing. However, these scurrilous allegations are irrelevant to the determination of reasonableness and they lack merit. Philadelphia retained counsel experienced in defending sex abuse cases to defend OELC and the managerial employees under policies that contained a sexual abuse rider subject to a single \$1 million limit. Philadelphia never disputed coverage, defended without a reservation of rights, and offered to pay its limits to settle the claims.

<sup>24</sup> Declaration of Darrell L. Cochran in Support of Plaintiffs' Response to Defendants' Motion to Intervene, ¶ 69, CP at 0-000000481 (emphasis added).

the five, nationally-renowned experts we had retained in the case – a first in my experience in case like this; the defendants provided no expert reports of their own and refused to provide their identified experts for deposition, thereby facing a motion to exclude all of their experts for trial; the defendants filed no summary judgments motions, filed no Evidence Rule 904 submission of evidence and had filed no motions in limine concerning issues in our case. I have never seen such a high profile liability and damages case with literally no defense prepared for the first of series of child sexual abuse trials less than four weeks away.<sup>25</sup>

Plaintiffs’ counsel also testified in court regarding facts and his legal opinion related to reasonableness of the settlements:

(Mr. Cochran) ...[T]here’s not a shred of evidence to support collusion. There’s nothing. I didn’t talk -- I’ve never met these guys. And it’s -- you can’t support a claim of collusion saying, “Well, if Cochran drafted it all, that proves collusion.”<sup>26</sup>

Even in this appeal, Plaintiffs’ counsel has offered testimony regarding his thought process:

Appellants’ counsel reduced Appellants’ settlement demand to defendants and Philadelphia to gain defendants’ **approval** of the settlement demand by securing “continuing coverage and defense under [their] Philadelphia policy in the event that any other claims ever come forward.”<sup>27</sup>

In addition, Plaintiffs’ counsel offered subjective testimony of Defendant Steve Olson’s personal counsel that revealed privileged

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<sup>25</sup> CP 0-000000482 – 483.

<sup>26</sup> 10/26/2012 RP at 31:10-16.

<sup>27</sup> Appellants’ Answer to Motion to Supplement the Record on Appeal, pp. 9-10 (emphasis original). In fairness, Plaintiff’s counsel was responding to arguments made by Philadelphia regarding the meaning of a particular document. However, the point is that Plaintiffs’ counsel is a necessary witness.

communications and mental impression work product of Defendant

Olson's attorney:

7. . . . I advised Mr. Olson to sign the settlement agreements and consent judgments because, in my professional opinion, it was necessary to protect him from personal liability.

\* \* \*

10. Under no circumstances did I "collude" with the plaintiffs to execute settlement agreements and consent judgments. In my professional judgment, they were necessary to protect Mr. Olson from potentially jeopardizing his personal assets in an excess judgment situation.<sup>28</sup>

Plaintiffs have also selectively used attorney-client privilege and work product obtained from Defendants' attorneys' files. For example, Plaintiffs have:

- Quoted a confidential correspondence between OELC's Board Chair and its personal counsel;<sup>29</sup>
- Quoted a confidential report from defense counsel;<sup>30</sup>
- Quoted a confidential correspondence between Defendant Horgdahl and defense counsel;<sup>31</sup>
- Disclosed confidential communications between defense counsel and the claims handler including correspondence in which defense counsel expressed surprise regarding the size of a verdict in an unrelated sexual abuse case of Plaintiffs' counsel;<sup>32</sup> and
- Used confidential Defense Counsel correspondence to the claims handler to argue the settlement was not the product of collusion

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<sup>28</sup> Declaration of J. William Ashbaugh. CP at 0-000000509 – 511.

<sup>29</sup> CP at 0-000000399, II. 16-23.

<sup>30</sup> CP at 0-000000400, II 1-4

<sup>31</sup> CP at 0-000000400, II. 5-11

<sup>32</sup> CP at 0-000000409; II. 15-17.

and to introduce defense counsel's mental impression about a surprising large verdict in another unrelated sexual abuse case.<sup>33</sup>

In addition, Plaintiffs' counsel contacted a defense expert, William Bainbridge, and then used information he learned from Mr. Bainbridge to argue defendants were not prepared for trial.<sup>34</sup>

Plaintiffs' counsel appears to be the only witness who has any material knowledge about the basis of the \$25 million settlement amount he unilaterally set, the unequal allocation of that settlement among six stipulated judgments, and the factual confessions he authored to support the judgments. Defendants' attorneys testified in post-settlement depositions that Plaintiffs' counsel unilaterally set the settlement figure; they have no idea how the \$25 million figure was derived or the bases of its allocation among the Plaintiffs.<sup>35</sup> Defendants' attorneys could not explain the factual contradictions between their clients' pre-settlement testimony and written confessions offered in support of the proposed judgments. They testified that Plaintiffs' counsel drafted their clients' confessions without any input from Defendants, and first presented the

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<sup>33</sup> CP at 0-000000421 and 0-000000430.

<sup>34</sup> CP at 0-000002536, l. 18 – 0-000002537, l. 2. Plaintiffs' counsel used this confidential information to argue that *Plaintiffs* had a substantial need to know what led defense counsel to believe that the child abuse claims lacked merit (CP at 0-000002536, ll. 13-17), which is the exact opposite of their position regarding privilege in this appeal.

<sup>35</sup> See CP 0-000002753 – 2754, including quoted excerpt from the 6/5/13 Deposition of Paul Meyer, at CP 0-000002781 – 2782.

confessions in final form for Defendants' signature with the final draft of the settlement documents.

### **C. Overview of Procedural History**

On October 26, 2012, the trial court granted Philadelphia's motion to intervene and conduct discovery related to the *Glover* factors. Over the next year, the trial court issued a series of discovery orders tailored to the extraordinary facts of this case. Despite these extraordinary facts, the trial court did not find a blanket privilege waiver. Rather, on April 19, 2013, the trial court ruled that attorney opinion and mental impression work product protection would be narrowly construed and subject to production only when it directly related to one of the eight applicable *Glover/Chaussee* factors."<sup>36</sup> The trial court's August 27, 2013 order directed the special master to apply this standard when conducting *in camera* review of documents withheld from production based on privilege.<sup>37</sup>

The special master issued a series of directives and recommendations following an arduous, multi-phase *in camera* review of documents. On November 22, 2013 the trial court held a hearing to address whether the trial court should adopt the discovery master's

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<sup>36</sup> 4/19/2013 RP at pp. 27-28 and 33:5-6.

<sup>37</sup> CP 0-000002826.

recommendations. Plaintiffs submitted no briefing nor did they present any substantive argument at the hearing.<sup>38</sup> The trial court then entered the November 22, 2013 Order adopting the special master's detailed document-specific recommendations.

In all, Plaintiffs were required to produce four percent of the documents they withheld following the *in camera* review and determination that the documents were critical to a reasonableness determination. The trial court properly exercised its discretion to tailor discovery to this case, which is precisely what appellate courts have directed trial courts to do when tasked with determining the reasonableness of stipulated settlements.

#### IV. ARGUMENT

##### A. This Court Should Decline to Review Issues Not Presented to the Trial Court

Plaintiffs cannot include issues, theories, or arguments on appeal that they did not present to the trial court.<sup>39</sup> Plaintiffs' only argument regarding attorney-client privilege came in a June 14, 2013 motion for a protective order when Plaintiffs argued that a subpoena issued by

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<sup>38</sup> See 11/22/13 RP at pp. 7-16.

<sup>39</sup> *Herberg v. Swartz*, 89 Wn.2d 916, 925, 578 P.2d 17, 22 (1978) (issue, theory or argument not presented at trial will not be considered on appeal). *Davis v. Globe Mach. Mfg. Co., Inc.*, 102 Wn.2d 68, 75, 684 P.2d 692, 697 (1984) (counsel must "state distinctly the matter to which he objects and the grounds of his objection", apprising the trial judge of the nature and substance of the objection.)

Philadelphia “disregards the attorney-client communications and attorney work product privileges.”<sup>40</sup> The totality of Plaintiffs’ argument related to attorney-client privilege was:

. . . a reasonableness determination is not an opportunity for the Intervenor to receive ‘super discovery’ to which it would not be entitled under any other circumstances. *Pappas v. Holloway*, 114 Wn.2d 198, 209-10, 787 P.2d 30, 37 (1990) (quoting *Hickman v. Taylor*, 329 U.S. 495, 511, 67 S. Ct. 385, 91 L. Ed. 451 (1947)).<sup>41</sup>

Moreover, as the quote at the beginning of the Introduction to this brief demonstrates, Plaintiffs’ current position that privileged communications are irrelevant to reasonableness is the exact opposite of the position Plaintiffs took in a motion filed prior to the trial court’s decision adopting the special master’s recommendations. Specifically, in May 2013, Plaintiffs argued to the trial court that reasonableness is determined by what was known by the parties and “the only way to determine the knowledge of the parties is by looking in the attorneys’ files. This is especially true where the attorneys are the primary source of *Glover/Chaussee* information.”<sup>42</sup>

In addition, Plaintiffs did not file a motion seeking to limit the scope of Defendants’ personal counsels’ depositions. Questions related to the details of the settlements and supporting factual confessions signed by

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<sup>40</sup> CP at 0-000002749.

<sup>41</sup> *Id.*

<sup>42</sup> CP at 0-000002536, ll. 2-4.

the Defendants as well as all of the *Glover* factors were asked and answered without objection.<sup>43</sup>

Further, Plaintiffs agreed to the appointment of the special master to resolve the discovery dispute, agreed to the scope of the special master's assignment, and did not object to the standard set by the trial court for the special master's review in the trial court's August 27<sup>th</sup> order.

Plaintiffs' new arguments that the contents of an attorney's files are irrelevant to reasonableness should not be considered on appeal. Appellants' new arguments regarding attorney-client privilege should also be rejected under the invited error doctrine, which precludes a party from setting up an error at trial and then complaining of it on appeal.<sup>44</sup>

In sum, the trial court's November 22, 2013 order should be affirmed because Plaintiffs waived every basis for this appeal.

#### **B. Standard of Review**

The standard of review applied to a trial court's discovery orders, including those involving attorney-client privilege and work product protection, is abuse of discretion.<sup>45</sup> A trial court's discovery rulings will only be reversed "on a clear showing" that the court's exercise of

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<sup>43</sup> CP at 0-000002982 - 2983.

<sup>44</sup> *In re Pers. Restraint of Thompson*, 141 Wn.2d 712, 723, 10 P.3d 380 (2000).

<sup>45</sup> *Cedell v. Farmers Ins. Co. of Washington*, 176 Wn.2d 686, 694, 295 P.3d 239, 243 (2013)

discretion was ‘manifestly unreasonable, or exercised on untenable grounds, or for untenable reasons.’”<sup>46</sup>

### **C. Overview of Attorney-Client Privilege and Work Product**

Civil Rule 26 sets forth the general rules of discovery in civil matters. That rule allows for discovery of anything material to the litigation and not protected by privilege. The right to discovery is an integral part of the right to access the courts embedded in our constitution.<sup>47</sup> As an intervener, Philadelphia has the same right to conduct discovery as any other party.

#### **1. Attorney-Client Privilege**

The attorney-client privilege is not absolute, but rather is “subject to recognized exceptions” and “must be strictly limited to the purpose for which it exists.”<sup>48</sup> The attorney-client privilege exists to protect open communication for the purpose of rendering legal advice, but not for the purpose of plotting fraud, insurance bad faith or undermining the administration of justice.<sup>49</sup> “Employing the attorney-client privilege to prohibit testimony must be balanced against the benefits to the

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<sup>46</sup> *Id.*

<sup>47</sup> *Lowy v. PeaceHealth*, 174 Wn.2d 769, 776–77, 280 P.3d 1078 (2012) (citing *Dietz*, 117 Wn.2d at 780–81, 819 P.2d 370).

<sup>48</sup> *Dike v. Dike*, 75 Wn.2d 1, 11, 448 P.2d 490 (1968); see, *Dietz v. Doe*, 131 Wn.2d 835, 842-43, 935 P.2d 611 (1997)

<sup>49</sup> See, *Cedell* 176 Wn.2d at 700; *Dietz v. Doe*, 131 Wn.2d at 842-43.

administration of justice stemming from the general duty to ‘give what testimony one is capable of giving.’”<sup>50</sup>

In Washington, the privilege is waived by: 1) voluntary disclosure of the substance of the attorney-client privilege;<sup>51</sup> 2) selective disclosure;<sup>52</sup> 3) where the attorney is a necessary witness;<sup>53</sup> 4) where the attorney or client conveys privileged information in court,<sup>54</sup> or by declaration;<sup>55</sup> and 5) by placing confidential communications at issue.<sup>56</sup> In addition, the attorney-client privilege cannot be asserted when allegations of bad faith are at issue.<sup>57</sup>

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<sup>50</sup> *Dietz v. Doe*, 131 Wn.2d at 843 citing *United States v. Bryan*, 339 U.S. 323, 331, 70 S. Ct. 724, 730, 94 L. Ed. 884 (1950).

<sup>51</sup> *Seattle Nw. Sec. Corp. v. SDG Holding Co., Inc.*, 61 Wn. App. 725, 739, 812 P.2d 488, 496-97 (1991)

<sup>52</sup> ER 502; *Seattle Nw. Sec. Corp.*, 61 Wn. App. at 739 (waiver extends to material relating to the same subject matter if the selective disclosure is used to gain a tactical advantage in litigation).

<sup>53</sup> *Seattle Nw. Sec. Corp.* 61 Wn. App. at 744, 812 P.2d 488 (1991) (“If [appellant] wishes to preserve the privilege during discovery, it cannot have it both ways. It must either choose to use or forego [the attorney’s] testimony in order to allow [respondent] to pursue discovery in a meaningful manner.”); *Kammerer v. Western Gear Corp.*, 96 Wn.2d 416, 635 P.2d 708 (1981) and authorities cited therein.

<sup>54</sup> *State v. Vandenberg*, 19 Wn. App. 182, 575 P.2d 254 (Div. 2 1978).

<sup>55</sup> *Stephens v. Gillispie*, 126 Wn. App. 375, 108 P.3d 1230 (2005) (in a dispute about whether the parties to a settlement agreement did or did not intend that a certain defendant would be bound by the agreement, the attorney-client privilege did not restrict the plaintiff from deposing the defendants’ attorney about the intent of the agreement; the court said the defendants waived the privilege when they filed declarations with the court, regarding their intent with respect to the settlement agreement).

<sup>56</sup> *Seattle Nw. Sec. Corp.*, 61 Wn. App. 725 (but case remanded for further factual determinations).

<sup>57</sup> *Seattle Nw. Sec. Corp.*, 61 Wn. App. at 740

## 2. Work Product

Protection for work product is codified in the civil discovery rules. *See* CR 26(b)(4)-(5). The work product rule protects documents prepared by lawyers in anticipation of litigation, basically “permitting attorneys to work with a certain degree of privacy and plan strategy without undue interference.”<sup>58</sup>

Under CR 26(b)(4), even if material is protected work product, the material is still discoverable if the discovering party shows “substantial need.”<sup>59</sup> To justify disclosure, a party must show the importance of the information to the preparation of his case and the difficulty the party will face in obtaining substantially equivalent information from other sources if production is denied.<sup>60</sup> The clearest case for ordering production is when crucial information is in the exclusive control of the opposing party.<sup>61</sup> The work product privilege does not apply “[w]here relevant and non-privileged facts remain hidden in an attorney’s file and where production of those facts is essential to the preparation of one’s case.”<sup>62</sup>

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<sup>58</sup> *Coburn, et al. v. Seda, et al.*, 101 Wn.2d 270, 677 P.2d 173 (1984)

<sup>59</sup> *Escalante v. Sentry Ins. Co.*, 49 Wn. App. 375, 393, 743 P.2d 832 (1987), *review denied*, 109 Wn.2d 1025 (1988), *overruled on other grounds by Ellwein v. Hartford Accident & Indem. Co.*, 142 Wn.2d 766, 15 P.3d 640 (2001).

<sup>60</sup> *Pappas v. Holloway*, 114 Wn.2d 198, 210, 787 P.2d 30 (1990).

<sup>61</sup> *Id.*

<sup>62</sup> *Lowy, supra, citing Hickman v. Taylor*, 329 U.S. 495, 511-12, 67 S. Ct. 385, 394, 91 L. Ed. 451 (1947).

As with the attorney-client privilege, there also appears to be an exception to the work product rule for civil fraud.<sup>63</sup>

**D. Reasonableness Hearings Guard Against Excessive Judgments**

The Court of Appeals adopted the statutory reasonableness determination to evaluating covenant judgment settlements in *Chaussee v. Maryland Casualty Co.*<sup>64</sup> The *Chaussee* court adopted the factors set out by the Washington Supreme Court in *Glover v. Tacoma General Hospital*, 98 Wn.2d 708, 717, 658 P.2d 1230 (1983)<sup>65</sup> for a reasonableness hearing under RCW 4.22.060:

- (1) the releasing person's damages;
- (2) the merits of the releasing person's liability theory;
- (3) the merits of the released person's defense theory;
- (4) the released person's relative faults;
- (5) the risks and expenses of continued litigation;
- (6) the released person's ability to pay;
- (7) any evidence of bad faith, collusion, or fraud;
- (8) the extent of the releasing person's investigation and preparation of the case; and
- (9) the interests of the parties not being released.<sup>66</sup>

These factors protect the insurer from fraud and collusion between the insured defendant and injured plaintiff in the covenant judgment

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<sup>63</sup> See *Soter v. Cowles Publishing Co.*, 131 Wn. App. 882, 895, 130 P.3d 840 (2006) (recognizing but not applying exception), *aff'd*, 162 Wn.2d 716, 174 P.3d 60 (2007).

<sup>64</sup> 60 Wn. App. 504, 509–10, 803 P.2d 1339 (1991).

<sup>65</sup> 98 Wn.2d 708, 717, 658 P.2d 1230 (1983).

<sup>66</sup> *Glover*, 98 Wn.2d at 717..

context just as they protected non-settling, joint-tortfeasor defendants in the contribution context.<sup>67</sup>

Washington law recognizes that the *only* purpose of the covenant judgment is to attempt to establish damages that an insurer may be required to pay in an assigned bad faith claim.<sup>68</sup> Consequently, Washington appellate courts have repeatedly cautioned trial courts to be aware that Washington law regarding covenant judgments provides plaintiffs and insured defendants with a financial incentive for collusion and inflated settlements designed to obtain windfalls from insurance companies. The Washington Supreme Court recognized from the beginning, when it established the reasonableness hearing procedure, that a covenant not to execute inherently raises the “specter” of insurance fraud or collusion.<sup>69</sup> The Court of Appeals has similarly warned that:

an insured may settle for an inflated amount to escape exposure and thus call into question the reasonableness of the settlement. We share this concern about consent judgments coupled with a covenant not to execute.<sup>70</sup>

Consequently, the Washington appellate courts have advised trial courts conducting a reasonableness hearing to examine the information

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<sup>67</sup> *Bird v. Best Plumbing Grp., LLC*, 175 Wn.2d 756, 781, 287 P.3d 551, 564 (2012).

<sup>68</sup> *Werlinger v. Warner*, 126 Wn. App. 342, 350-351, 109 P.3d 22 (2005) (“the sole purpose of the covenant judgment [is] to serve as the presumptive measure of damages in a separate bad faith lawsuit.”).

<sup>69</sup> *Besel v. Viking Ins. Co.*, 146 Wn.2d 730, 737, 49 P.3d 887 (2002).

<sup>70</sup> *Chaussee*, 60 Wn. App. at 510-11.

available to each party related to eight express factors that ordinarily bear on a claim's value (e.g., liability and damage evidence) and in addition, expressly cautioned the trial court to affirmatively look for "any evidence" of "bad faith, collusion or fraud."<sup>71</sup> Further, Washington courts have explained that at the reasonableness hearing stage, traditional "fraud" need not be proven, but rather the trial court should be looking for "any evidence" that the settling parties are improperly inflating the value of their claim to obtain an insurance windfall.<sup>72</sup> Washington appellate courts have intentionally given the trial courts great latitude regarding how to apply the *Glover* factors and how to conduct a reasonableness hearing.<sup>73</sup>

Relying on *Dana v. Piper*,<sup>74</sup> Plaintiffs argue that the trial court erred in adopting the special master's recommendations because reasonableness is determined by an objective standard. However, Plaintiffs

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<sup>71</sup> See *Best Plumbing*, 175 Wn.2d at 766 (reasonableness hearing protects the interest of insurers against excessive judgments; trial court required to evaluate reasonableness based upon *Glover* factors including whether there is any evidence of bad faith, collusion, or fraud"); see also *Besel*, 146 Wn.2d at 738 (application of the *Glover* criteria "promotes reasonable settlements and discourages fraud and collusion.").

<sup>72</sup> *Water's Edge Homeowners Ass'n v. Water's Edge Associates*, 152 Wn. App. 572, 594-595, 216 P.3d 1110, rev. denied, 168 Wn.2d 1019 (2010).

<sup>73</sup> *Brewer v. Fibreboard Corp.*, 127 Wn.2d 512, 524, 901 P.2d 297 (1995) ("The trial judge faced with this task [of determining reasonableness] must have discretion to weigh each case individually."); *Best Plumbing*, 175 Wn.2d at 774-75 ("Trial courts retain broad discretion in determining reasonableness, and we review under an abuse of discretion standard"); *Schmidt v. Cornerstone Investments, Inc.*, 115 Wn.2d 148, 159, 795 P.2d 1143 (1990) ("we are confident that trial judges will develop their own procedures for handling these cases"); *Pickett v. Stephens-Nelsen, Inc.*, 43 Wn. App. 326, 335, 717 P.2d 277 (1986) ("the procedures for handling evidence at these hearings are within the trial court's discretion.").

<sup>74</sup> 173 Wn. App. 761, 295 P.3d 305, rev. den., 178 Wn.2d 1006 (2013).

never made any such argument below. Rather, at every turn Plaintiffs offered subjective testimony, gathered and used privileged information from Defendants' files, and, at one point, when it suited them, even adopted Philadelphia's position.<sup>75</sup>

Moreover, as discussed below, in *Dana*, the Court of Appeals appropriately applied the *Hearn* test for implied waiver adopted in *Pappas v. Holloway*,<sup>76</sup> based upon the facts of that case.

Further, unlike in *Dana*, Plaintiffs' counsel has testified in court and by declaration as to facts and Plaintiffs' counsel's legal opinions regarding the *Glover* factors that the trial court must consider including: Plaintiffs' damages; the merits of the Plaintiffs' liability theory; the merits of the defense theory; the Defendants' relative faults; the risks and expenses of continued litigation; and evidence of bad faith, collusion, or fraud. Plaintiffs' counsel has also testified about the extent of Defendants' investigation and preparation of the case.<sup>77</sup>

The only source of evidence regarding how the amount of the settlement was determined, and the basis of the factual confessions, is

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<sup>75</sup> As discussed above, Plaintiffs adopted Philadelphia's argument that the only way to determine the knowledge of the parties is by looking in the attorneys' files in a motion to compel production of Philadelphia's coverage counsel files.

<sup>76</sup> 114 Wn.2d 198, 787 P.2d 30 (1990).

<sup>77</sup> The reasonableness factor actually looks at the extent of the *releasing* person's investigation and preparation of the case, meaning Plaintiffs' investigation and preparation is at issue; however, Plaintiffs have opened the door on this issue.

Plaintiffs' file material. Also, unlike some stipulated settlements, such as those involving a construction defect claim where the court can compare the parties' repair estimates to determine damages, damages from alleged sexual abuse of young children cannot be easily quantified.

Moreover, it is questionable whether Plaintiffs' counsel actually believed that a \$25 million settlement was a reasonable amount. In several briefs, Plaintiffs' counsel stated the amount of the settlement was \$22.5 million.<sup>78</sup> Of course, misstating the amount of the settlement by \$2.5 million is not direct evidence that the amount was unreasonable. The point is that access to Plaintiffs' counsel's file materials is necessary to Philadelphia's defense; without these materials it will be impossible to examine whether Plaintiffs' counsel had any factual bases for crafting the confessions and requiring defendants to sign them. If Plaintiffs' counsel did not, or worse if Plaintiffs' counsel's file like defense counsel's file contains evidence that these factual confessions as drafted were untrue, then this would be powerful evidence of bad faith, fraud, or collusion.

Further, Philadelphia expects the trial court will find that the \$25 million settlement is unreasonable. If so, the court will be required to

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<sup>78</sup> In several pleadings and during oral argument, Plaintiffs' counsel stated that the settlement amount was \$22.5 million instead of \$25 million. *See e.g.* 3/22/2013 RP at p.18, ll. 13-17 ("They are willing to say all they want and try to persuade this Court that \$22.5 [million], which is the number, by the way, was not reasonable for these six child abuse victims and their parents, go ahead. This Court will set what amount is reasonable.")

determine the reasonable amount based upon evidence related to the *Glover* Factors. *Meadow Valley Owners Ass'n v. St. Paul Fire & Marine Ins. Co.*, 137 Wn. App. 810, 820, 156 P.3d 240, 245 (2007). Thus, both sides must be prepared to present evidence as to what amount is reasonable based upon the *Glover* Factors. Plaintiffs' counsel has had defense counsel's files including defense counsel's mental impression work product and privileged communication regarding the value of Plaintiffs' claims since the ink was dry on the settlement agreements and has been using privileged information offensively. That bell cannot be unrung. However, the trial court's order did create a more level playing field.<sup>79</sup> Clearly, this case involves issues and unique circumstances that were not present in *Dana*.

Finally, the Washington Supreme Court recently emphasized that a reasonableness hearing "is an equitable proceeding."<sup>80</sup> It would be inequitable to allow Plaintiffs to have access to the complete files of both parties, while denying Philadelphia access to the portions of Plaintiffs' file that the special master has determined are directly relevant to the *Glover* factors.

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<sup>79</sup> As discussed above, the trial court found there was a limited waiver of Plaintiffs' privilege as to some specific documents. Thus, unlike Plaintiffs, who have their former opponents' complete files, Philadelphia will not receive Plaintiffs' complete files if this Court upholds the trial court's order.

<sup>80</sup> *Best Plumbing*, 175 Wn.2d at 770.

**E. Plaintiffs Seek a Special Exemption**

Contrary to Plaintiffs' assertions, Philadelphia *never* argued, and the trial court never ruled, that a Plaintiff *always* waives attorney-client privilege or work product protection by requesting a reasonableness hearing. Each case and each settlement is different and calls for uniquely focused discovery. In this case, Philadelphia argued that Plaintiffs' counsel was the central factual witness to the settlement, and critical information could only come from his knowledge and documents.<sup>81</sup>

Further, the trial court's November 22, 2013 order does not rely upon a *per se* rule that whenever a plaintiff requests a reasonableness hearing, they automatically waive privilege. The trial court could have ordered Plaintiffs to produce their entire unredacted file, which was precisely what was already required of defense counsel.<sup>82</sup> Instead, the trial court applied extra protection and required that a discovery master review the documents with instructions to narrowly construe relevance such that

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<sup>81</sup> Supp. Briefing on Mot. to Reconsider, CP at 0-000001794 – 1810.

<sup>82</sup> Once privilege has been waived, it is not unusual for a court to order an attorney's entire file be produced. Indeed, in the *Best Plumbing* case, Plaintiffs' counsel's entire unredacted file was produced in discovery. See Decl. of Tyna Ek, Resp't Appx. at pp. 75-78, Decl. of Janis Puracal (counsel for intervening insurer in *Best Plumbing*, 175 Wn.2d 756, verifying that Plaintiffs' counsel's entire unredacted file was produced in discovery in that case, Resp't Appx. at pp. 69-70.

only documents directly related to the reasonableness determination would be produced.<sup>83</sup>

What Appellants seek is a blanket rule providing absolute protection of privilege for plaintiffs in any reasonableness hearing no matter the circumstances. However, the purpose of a reasonableness hearing is to guard against inflated settlements. It is hard to imagine a case that better demonstrates why plaintiffs who enter a stipulated settlement should not be granted special protection.

**F. Plaintiffs Waived Privilege Related to the Reasonableness Factor under Recognized Exceptions to Attorney-Client Privilege**

**1. Plaintiffs Waived Privilege by Selective Disclosure**

A party may not selectively disclose parts of privileged communications that are favorable to the client's position and then raise the privilege to prevent disclosure of the remaining portions that give context and meaning to what the client has disclosed.<sup>84</sup>

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<sup>83</sup> Order Appointing Special Master, Pet'rs' Appx. at pp. 294-295.

<sup>84</sup> *Martin v. Shaen*, 22 Wn.2d 505, 156 P.2d 681, 685 (1945) ("Having testified to a specific fact for the sole purpose of creating the presumption vital to the establishment of his case, the attorney executor could not, by invoking the principle of privileged communications, prevent an inquiry into the circumstances surrounding the fact concerning which he testified. *He could not be permitted to disclose so much of the transaction as he saw fit and then withhold the remainder.*") (emphasis added) (citing 8 Wigmore, Evidence, 3d ed., at 633, § 2327, which states: "The client's offer of his own or the attorney's testimony as to a part of any communication to the attorney is a waiver as to the whole of that communication ..."); *State v. Ingels*, 4 Wn.2d 676, 104 P.2d 944, 959 (1940) ("[I]f the client opens up the subject in his testimony by voluntarily testifying thereto, the privilege is deemed waived."); *State v. Vandenberg*, 19 Wn. App. 182, 575

Here, Plaintiffs have selectively disclosed privileged information related to the reasonableness of the settlement by disclosing both Plaintiffs' and Defendants' privileged communications related to the reasonableness of the settlement.

First, Plaintiffs' counsel testified in court and by declaration as to firsthand accounts of settlement communications and his mental impression work product related to the reasonableness of the settlement. This included his opinion regarding the strength of Plaintiffs' liability theory and damage claim, Plaintiffs' settlement strategy, weakness in defense counsel's defense, and his opinions about whether the settlement was the product of collusion. This alone was a sufficient basis for the trial court's November 22, 2013 order.

Second, Plaintiffs inserted testimony of OELC's personal counsel regarding reasonableness and attorney-client and mental impression work product of defense counsel and personal counsel. Philadelphia anticipates that Plaintiffs may argue that Defendants waived privilege when they turned over their files to Plaintiffs. However, Plaintiffs' counsel testified by declaration that he obtained attorney-client privileged documents and mental impression work product of Defendants' personal and defense

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P.2d 254, 256 (Div. 2 1978) (“The client’s offer of his own or the attorney’s testimony as to a part of any communication to the attorney is a waiver as to the whole of that communication ....”) (citation omitted).

counsel after he began representing both plaintiffs and defendants in the reasonableness phase and Plaintiffs refused to produce these documents to Philadelphia without a court order.<sup>85</sup>

Accordingly, Plaintiffs waived privilege by selectively disclosing both their own privileged information and those of the defendants related to the reasonableness of the settlement for tactical advantage. Thus, the trial court did not abuse its discretion in adopting the special master's recommendations.

**2. Appellants Waived Privilege By Making Appellant's Counsel a Necessary Witness**

In *Stephens v. Gillispie*, the Court of Appeals held that parties to a stipulated settlement waived attorney-client privilege by submitting declarations as to their intent in entering into the stipulated agreement.<sup>86</sup> The Court of Appeals held that when a party asserts a claim that necessarily requires the disclosure of communications between himself and his attorney because it is the only available evidence, the privilege does not protect his communications with legal counsel.<sup>87</sup>

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<sup>85</sup> CP at 0-000002533.

<sup>86</sup> *Stephens v. Gillispie*, 126 Wn. App. 375, 108 P.3d 1230 (Div. 3 2005),

<sup>87</sup> *Id.* at 382. Although the ruling was based upon the crime-fraud exception (discussed below), one commentator has opined that “[t]his result seems a better fit with implied waiver than with the crime/fraud exception.” 1 Attorney-Client Privilege: State Law Washington § 9:52.

Washington courts have also clearly held that when an attorney is a necessary witness, as Plaintiffs' counsel is here, the attorney-client privilege is relinquished during discovery.<sup>88</sup> Plaintiffs' counsel testified through declaration and during oral argument regarding his own beliefs and opinions regarding each of the reasonableness factors and regarding facts pertaining to the settlement, including the lack of any negotiations regarding the amount of the settlements.

Plaintiffs claim necessary information is available from other sources and that experts can opine on the reasonableness of the settlement. However, Plaintiffs have failed to explain who, other than Plaintiffs' counsel, has information about the basis for the factual confessions that Plaintiffs' counsel drafted and who, other than Plaintiffs' counsel, knows the basis for each of the stipulated settlement amounts Plaintiffs' counsel set.<sup>89</sup> Nor have Plaintiffs explained how they could meet their burden of proving that the \$25 million settlement of these claims is reasonable

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<sup>88</sup> *Kammerer v. W. Gear Corp.*, 96 Wn.2d 416, 420, 635 P.2d 708 (1981); *Seattle Nw. Sec. Corp. v. SDG Holding Co., Inc.*, 61 Wn. App. 725, 812 P.2d 488 (1991) (to avoid "trial by ambush" if an attorney will testify at trial, attorney-client privilege does not apply during discovery).

<sup>89</sup> Reasonableness cannot be determined in a vacuum. In *Fortin v. Hartford Underwriters Ins. Co.*, 139 Conn. App. 826, 59 A.3d 247 (2013), the Appellate Court of Connecticut refused to admit expert testimony regarding reasonableness where the expert lacked adequate factual basis upon which to evaluate whether there was significant prospect of adverse judgment, whether settlement was advisable, whether claims were brought in good faith or whether amount for which plaintiffs ultimately settled claims was excessive. There the expert testified that his opinion was based primarily upon parties' mediation statements, and that he did not determine whether allegedly libelous statements forming the basis of the action against plaintiffs were truthful.

without Plaintiffs' counsel's testimony when there is a complete lack of evidence related to abuse of 5 of the 6 child plaintiffs (other than the factual confessions that contradict Defendants' prior testimony and the objective evidence) and the settlement occurred before any mediation, without negotiation, and without even discussion of liability and damages.

Moreover, Plaintiffs have refused to state whether Plaintiffs' counsel's testimony will be offered to support the reasonableness of the stipulated settlements. Plaintiffs' failure to make such an election during discovery constitutes a waiver of attorney-client privilege under *Seattle Nw. Sec. Corp. v. SDG Holding Co., Inc.*<sup>90</sup>

Plaintiffs' counsel is a key witness regarding the factual confessions, which state that abuse occurred at OELC, that the abuse was due solely to the negligence of the Defendants, and Plaintiffs' counsel is also a key factual witness as to the extent of Plaintiffs' investigation and preparation of the case. In addition, what Plaintiffs' counsel knew about the Defendants' ability to pay is clearly relevant since the Defendants were released without contributing a dime to the settlement.<sup>91</sup> Plaintiffs'

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<sup>90</sup> 61 Wn. App. 725, 744, 812 P.2d 488, 499 (1991) ("Allowing a party to sit on the fence and not specify whether a potential witness will testify in order to preserve the advantages of not testifying while enjoying the future possibility of allowing that testimony frustrates the other party's attempt to construct an adequate case")

<sup>91</sup> Defendants had few assets other than 1) the Philadelphia policy, which is subject to a \$1 million limit for all sexual abuse claims; and 2) a building owned by OELC worth about \$150,000. As discussed above, in addition to the Plaintiffs' claims, Defendants

counsel is a key factual witness regarding the reasonableness of the settlement.

Plaintiffs waived privilege regarding reasonableness by offering Plaintiffs' counsel's testimony regarding the reasonableness factors and because Plaintiffs' counsel is a necessary witness. Accordingly, the trial court did not abuse its discretion in adopting the special master's recommendations.

**3. Appellants Waived Privilege under the Implied Waiver Test Adopted in *Pappas v. Holloway***

Twenty-five years ago, in *Pappas v. Holloway*, the Washington Supreme Court adopted the test set out in *Hearn v. Rhay*, 68 F.R.D. 574, 581 (E.D. Wash. 1975) to determine whether an implied waiver of the attorney-client privilege has occurred:

1. The assertion of the privilege was the 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 its defense.<sup>92</sup>

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were concerned about a potential claim by N.D.'s family, which, unlike 5 of the 6 plaintiffs' claims, was not a nuisance claim. Yet the stipulated settlement amount is 25 times the limits of the Philadelphia policy! The privileged portion of Plaintiffs' counsel's file likely contains information regarding his evaluation of N.D.'s claim as well as other aspects of the Ability to Pay Factor.

<sup>92</sup> *Pappas v. Holloway*, 114 Wn.2d 198, 207, 787 P.2d 30 (1990) (citing *Hearn v. Rhay*, 68 F.R.D. 574 (E.D. Wash. 1975))

On appeal, Plaintiffs argue that *Pappas v. Holloway* and *Dana* limit the implied waiver doctrine to cases involving legal malpractice. However, rather than limiting the *Hearn* test to malpractice claims, *Pappas v. Holloway*, directs that the *Hearn* test should be applied based upon “the particular facts presented.”<sup>93</sup> Similarly, in *Dana*, the Court of Appeals appropriately applied the *Hearn* test for implied waiver and held that the trial court had abused its discretion in finding Dana waived the privilege under the unique facts before the court in that case. Neither decision limited the *Hearn* test to malpractice cases. Indeed, in *1st Sec. Bank of Washington v. Eriksen*<sup>94</sup>, a case cited by Plaintiffs, the Washington Federal District Court applied the *Hearn* test in the context of a stipulated settlement stating:

Like many other jurisdictions, Washington courts have adopted the test set out in *Hearn v. Rhay*, 68 F.R.D. 574, 581 (E.D.Wash.1975) when determining whether an implied waiver of the attorney-client privilege has occurred.<sup>95</sup>

The Ninth Circuit Court of Appeals has also applied the *Hearn* test to determine whether privilege had been waived in the context of a

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<sup>93</sup> *Pappas*, 114 Wn.2d at 204

<sup>94</sup> CV06-1004RSL, 2007 WL 188881, \*2 (W.D. Wash. Jan. 22, 2007). There, the Federal District Court held privilege was not waived because, unlike here, defendants had access to witnesses other than plaintiff’s attorney who could shed light on the reasons for settlement, and to experts who could opine on the reasonableness of the settlement.

<sup>95</sup> *Id.*

stipulated judgment. In *Home Indem. Co. v. Lane Powell Moss & Miller* , the Ninth Circuit held that privilege is not waived where, unlike here, the plaintiff does not rely upon privileged communications and where there is sufficient objective evidence of the reasonableness of the settlement amount to prove reasonableness without resorting to its attorneys' communications.<sup>96</sup>

In *GAB Bus. Servs., Inc. v. Syndicate 627*,<sup>97</sup> the Eleventh Circuit applied the *Hearn* test and held that the attorney-client privilege had been waived with respect to the evidence necessary to evaluate the reasonableness of a settlement because the party seeking privilege injected an issue into the litigation that required testimony from the party's attorneys or testimony concerning the reasonableness of its attorneys' conduct.<sup>98</sup> Clearly, the *Hearn* test applies to stipulated settlements.

All of the elements of the *Hearn* test are satisfied. First, seeking a reasonableness determination is an affirmative act like filing a lawsuit. Contrary to Plaintiffs' assertion, it was Plaintiffs' choice to ask the trial

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<sup>96</sup> 43 F.3d 1322, 1327 (9th Cir. 1995).

<sup>97</sup> 809 F.2d 755, 762 (11th Cir. 1987)

<sup>98</sup> See also *Cooper v. Meridian Yachts, Ltd.*, 06-61630-CIV, 2008 WL 2229552, at \*10-11 (S.D. Fla. May 28, 2008) ("Third-Party Plaintiffs must necessarily demonstrate the reasonableness of their settlement with Cooper, they have waived claims of privilege with respect to the evidence necessary to evaluate that issue").

court to make a reasonableness determination.<sup>99</sup> Plaintiffs could have allowed the Federal District Court to allocate the applicable policy limits in the interpleader/declaratory relief action, pursued a garnishment action, or elected to prove damages in a subsequent bad faith suit.

More importantly, Plaintiffs did not merely seek a reasonableness hearing. Plaintiffs obtained attorney-client privileged and work product protected documents of defense counsel and Defendants' personal counsel, and have been using them against Philadelphia in the reasonableness proceedings. Thus, even if the seeking of a reasonableness hearing in and of itself was not an affirmative act putting the Plaintiffs' attorney-client communications at issue, obtaining and using attorney-client communications as a sword clearly was an affirmative act that put the Plaintiffs' attorney-client privileged communications at issue.

In addition, Plaintiffs' counsel unilaterally set the amount of the stipulated settlements and drafted factual confessions signed by Defendants that have been used in the reasonableness proceedings. Clearly, the assertion of the privilege was the result of an affirmative act of Plaintiffs.

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<sup>99</sup> Plaintiffs argue that they were required to seek a reasonableness determination under *Best Plumbing and Meadow Valley Owners Ass'n v. St. Paul Fire & Marine Ins. Co.*, 137 Wn. App. 810, 816, 156 P.3d 240, 243 (2007). However, read in context, it is clear the courts were referring to statutory reasonableness hearings involving the right of contribution between joint tortfeasors not in the context of covenant judgments against insurers.

Second, Appellants also put the protected information at issue by making it relevant to the case. The Washington Supreme Court has directed trial courts to evaluate the reasonableness of a stipulated settlement based upon the nine *Glover* factors based upon “what was known to the parties at the time of settlement.”<sup>100</sup>

In this case, what was known to Plaintiffs is particularly important because: 1) the factual “confessions” unilaterally authored by Plaintiffs’ counsel completely contradict the Defendants’ prior sworn testimony and the evidence that has been produced to date; 2) virtually all of the pertinent information about the reasonableness of this \$25 million settlement appears to be in the exclusive possession of Plaintiffs’ counsel; 3) every client communication, internal file note and thought process of defense counsel and Defendants’ personal counsel were immediately turned over to Plaintiffs’ counsel without redaction; and 4) Defendants’ personal counsel were deposed without restriction as to all relevant reasonableness factors providing Plaintiffs’ counsel unfettered access to every weakness that existed in the defense case at the time of settlement.

Third, application of the privilege would deny Philadelphia access to information vital to its position regarding the reasonableness of the

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<sup>100</sup> *Best Plumbing*, 175 Wn.2d at 775-76

settlement. The privileged information is vital because it is directly relevant to the reasonableness of the stipulated settlement. Philadelphia has shown that the information is not available from any other source because the only evidence offered to support the covenant judgment amounts has been factual confessions of Defendants that contradict their prior sworn testimony and legal positions taken throughout the case; confessions that were *authored exclusively by Plaintiffs' counsel* without input from Defendants or their attorneys and which Plaintiffs' counsel required Defendants to sign in order to be released from personal liability.

Philadelphia has also shown that it would be manifestly unfair to allow Plaintiffs to use attorney-client privilege as a shield where Plaintiffs structured the settlement such that only Plaintiffs' counsel knows how the amount of the settlement was determined and the basis of the factual confessions, and where Plaintiffs obtained and have been using their former opponents' previously privileged and protected materials to argue weaknesses in Defendants' case, while not allowing Philadelphia the reciprocal.

All of the elements of the *Hearn* test are satisfied. This is yet another basis for the trial court's November 22, 2013 order. Accordingly, the trial court did not abuse its discretion when it adopted the special master's recommendations on November 22, 2013.

**G. Plaintiffs Waived Privilege Related to the Reasonableness Factors under Recognized Exceptions to the Work Product Doctrine**

**1. Work Product Protection Expressly or Impliedly Waived**

Work product protection, like any privilege, may be waived.<sup>101</sup> Even in their preliminary motions leading up to the reasonableness hearing proceeding, Plaintiffs have selectively disclosed Plaintiffs' counsel's mental impressions, legal theories and other work product as well as those of its former opponents.<sup>102</sup> As discussed above, the record is replete with example of Plaintiffs' counsel selectively disclosing his own mental impression work product and Defendants' mental impression work product.

In addition, Plaintiffs have impliedly waived any work product protection. Plaintiffs have asked the trial court to apply the *Glover* Factors to determine the reasonableness of stipulated settlement agreements they claim were the exclusive creation of their attorney, and thereby have placed the mental impressions and preparation of their counsel directly at issue. The work product doctrine never protects an attorney's mental impressions when the attorney's knowledge and impressions are directly at issue. As the Washington Supreme Court explained in *Pappas v.*

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<sup>101</sup> See e.g., *Harris v. Drake*, 152 Wn.2d 480, 495, 99 P.3d 872, 879 (2004).

<sup>102</sup> See *Hickman v. Taylor*, 329 U.S. 495, 67 S. Ct. 385, 91 L. Ed. 451 (1947) (discussing the nature of attorney work product).

*Holloway*, “where the material sought to be discovered is central to a party’s claim or defense, an exception to the strict rule created by CR 26(b)(3) should apply and discovery should be allowed.”<sup>103</sup> Moreover, work product privilege does not apply “[w]here relevant and non-privileged facts remain hidden in an attorney’s file and where production of those facts is essential to the preparation of one’s case.”<sup>104</sup>

The information known to Plaintiffs’ counsel at the time the case was settled, as well as Plaintiffs’ counsel’s preparation for trial including anticipated expert testimony, is critical to an assessment of the reasonableness factors Plaintiffs have asked the trial court to apply in ruling on whether the settlements were reasonable.

Plaintiffs’ counsel’s knowledge, information and mental impressions at the time of settlement are particularly central in this case in which plaintiffs claim their attorney unilaterally authored the defendants’ “confessions,” came up with the dollar amounts and controlled all terms to the settlement. Denying Philadelphia access to information and knowledge available to Plaintiffs’ counsel under these circumstances would preclude Philadelphia, and ultimately the trial court, from examining the factual

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<sup>103</sup> See also *Soter v. Cowles Pub. Co.*, 131 Wn. App. at 895 (“Cowles correctly contends that an attorney’s mental impressions are not protected from discovery if what the attorney knew and when he knew it is directly at issue in the litigation”); *Escalante* at 49 Wn. App. at 397

<sup>104</sup> *Lowy v. PeaceHealth*, 174 Wn.2d 769, 776-77, 280 P.3d 1078 (2012).

bases and true motivation of the settlements when they were made, which is the central purpose of a reasonableness hearing.

Finally, the Washington Supreme Court recently emphasized that a reasonableness hearing “is an equitable proceeding.”<sup>105</sup> Plaintiffs’ counsel has been using attorney-client and work product protected documents of defense counsel offensively against Philadelphia with the obvious intent of continuing to do so throughout the reasonableness hearing process. If Plaintiffs’ counsel’s work product is not produced while defense counsel’s is produced and used as a sword by Plaintiffs, Philadelphia will not be placed on an equal footing and equity will not be served. There is no logical reason nor equitable basis to withhold Plaintiffs’ counsel’s work product from discovery while requiring the disclosure of defense counsel’s work product.

## 2. Substantial Need

The burden is upon Plaintiffs, as the party claiming privilege, to first show that the materials they seek to protect against discovery are privileged.<sup>106</sup> The discovery of otherwise protected work product is permitted upon a showing that the party seeking discovery (Philadelphia) has “substantial need of the materials in the preparation of his case” and

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<sup>105</sup> *Best Plumbing Group*, 175 Wn.2d at 770

<sup>106</sup> *Soter*, 131 Wn. App. at 745.

that Philadelphia is “unable without undue hardship to obtain the substantial equivalent of the materials by other means.” CR 26(b)(4). In this case, Philadelphia has shown that some of the information essential to an examination of the *Glover* reasonableness factors is likely only to be found in Plaintiffs’ counsel’s file materials. Accordingly, the trial court did not abuse its discretion in adopting the Special Master’s recommendations.

#### **H. The Civil Fraud Exception Applies**

It is also well settled that Washington follows the “fraud” or “civil fraud” exception to the attorney-client privilege.<sup>107</sup> The civil fraud exception appears to apply equally to work product protection.<sup>108</sup>

Attorney-client communications are not protected from disclosure when they “pertain to ongoing or future fraudulent conduct.”<sup>109</sup> The threshold showing necessary to trigger this exception to the attorney-client privilege is quite low, requiring that “an *in camera* inspection of the communication itself is warranted upon a showing of a factual basis adequate to support a good faith belief by a reasonable person that

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<sup>107</sup> *Cedell*, 176 Wn.2d at 697.

<sup>108</sup> *See Soter*, 131 Wn. App. at 895 (recognizing but not applying exception), *aff’d*, 162 Wn.2d 716, 174 P.3d 60 (2007)

<sup>109</sup> *Stephens v. Gillispie*, 126 Wn. App. 375, 382, 108 P.3d 1230 (2005)

wrongful conduct sufficient to invoke the crime or fraud exception to the privilege has occurred.”<sup>110</sup>

In *Stephens v. Gillispie*, the Washington Court of Appeals held that parties who made affirmative representations as to their intent in entering a stipulated settlement waived their attorney-client privilege:

[T]o allow Mina and Bob to “understand” one intention following discussions with, and negotiations by, their lawyer with Ms. Stephens and then represent to the court something different is tantamount to civil fraud[.]<sup>111</sup>

Washington appellate courts have repeatedly cautioned trial courts to beware that covenant judgments provide plaintiffs and insured defendants with a financial incentive for collusion or fraudulently inflated settlements designed to obtain windfalls from insurance companies:

We are aware that an insured’s incentive to minimize the amount of a judgment will vary depending on whether the insured is personally liable for the amount. Because a covenant not to execute raises the specter of collusive or fraudulent settlements, the limitation on an insurer’s liability for settlement amounts is all the more important. A carrier is liable only for reasonable settlements that are paid in good faith.<sup>112</sup>

Consequently, the Washington appellate courts have advised trial courts conducting a reasonableness hearing to affirmatively look for “any

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<sup>110</sup> *Whetstone v. Olson*, 46 Wn. App. 308, 331-312, 732 P.2d 159, 161 (1986)

<sup>111</sup> *Stephens*, 126 Wn. App. at 381-82

<sup>112</sup> *Besel v. Viking Ins. Co.*, 146 Wn.2d 730, 737, 49 P.3d 887 (2002).

evidence” of “bad faith, collusion or fraud.”<sup>113</sup> Further, Washington courts have explained that at the reasonableness hearing stage, traditional “fraud” need not be proven, but rather the trial court should be looking for “any evidence” that the settling parties are improperly inflating the value of their claim to obtain an insurance windfall.<sup>114</sup>

Recently, in the context of insurance bad faith litigation, the Washington Supreme Court provided insight into how it wishes trial courts to address the tension between the attorney-client privilege and the need to uncover “bad faith” or similar conduct between an attorney and client that is undermining the administration of justice. The Supreme Court broadly extended the long-recognized “fraud” *exception* to attorney-client privilege and held there is “a presumption of no attorney-client privilege” when an insured alleges his insurance company acted in bad faith in handling his insurance claim.<sup>115</sup> In that context, the presumption of no privilege results from the nature of the claim and the insureds’ purported need to examine the attorney communications to discover facts to support a claim of bad faith.<sup>116</sup> A covenant judgment raises the same

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<sup>113</sup> See *Best Plumbing*, 175 Wn.2d at 766 (reasonableness hearing protects the interest of insurers against excessive judgments; trial court required to evaluate reasonableness based upon *Glover* Factors including whether there is any evidence of bad faith, collusion, or fraud”).

<sup>114</sup> *Water’s Edge*, 152 Wn. App. at 594-595.

<sup>115</sup> *Cedell*, 176 Wn.2d at 700

<sup>116</sup> *Id.* at 696.

considerations because the insurer needs to discover evidence related to each of the *Glover* factors including whether there is “any evidence of bad faith, collusion, or fraud.” In each instance, the concern with examining any evidence of bad faith animates the analysis.

Here, there clearly is *prima facie* evidence that Plaintiffs inflated the value of their claims in a bad faith effort to obtain unjustified and otherwise unobtainable insurance proceeds. In exchange for a cost-free full release, Defendants stipulated that judgments could be entered against them in the collective amount of \$25 million even though the police and DSHS/CPS found evidence that only one of the six minor plaintiffs had been abused, and that he had been abused in his home and not at OELC. Moreover, the only evidence offered to support the covenant judgment amounts has been factual “confessions” authored by Plaintiffs’ counsel that contradict Defendants’ prior sworn testimony and legal positions taken throughout the case. Further, recently produced evidence, such as the internal email correspondence discussed above, indicates that Plaintiffs’ counsel’s files likely contain evidence that the amount of the stipulated settlements was many times higher than Plaintiffs’ counsel’s own evaluation.

Accordingly, it is clear that Plaintiffs’ counsel’s files contain information relevant to the “any evidence of bad faith, collusion or fraud”

*Glover* factor. Thus, the trial court did not abuse its discretion in ordering an *in camera* inspection of the privileged documents or in adopting the special master's recommendations requiring production of some documents withheld from production.<sup>117</sup>

**I. The Trial Court's Decision Is Consistent with Public Policy**

Appellants seek to strip the trial courts of all discretion and make a blanket rule that it is error for a trial court to ever permit an intervening insurer to obtain discovery of attorneys' legal files in preparation for a reasonableness hearing. This would be contrary to Washington precedent that has always acknowledged that "[t]he trial court is inarguably in the best position to determine the nature and extent of the burdens and risks" in granting or limiting discovery.<sup>118</sup> This would also contravene Washington law in this precise area since the Supreme Court and Courts of Appeals have repeatedly indicated that they wish to leave the management of reasonableness hearings to the trial court's discretion.

In addition, Plaintiffs' argument concerning the chilling effect the trial court's decision could have on future plaintiffs is unfounded and ignores the potential chilling effect on future defendants if this Court were to reverse the trial courts' decision. First, given the unique circumstances

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<sup>117</sup> *Cedell*, 176 Wn.2d at 697-98(*in camera* inspection matter of discretion).

<sup>118</sup> *Gillett v. Conner*, 132 Wn. App. 818, 826, 133 P.3d 960 (2006).

of this case, it is highly unlikely that this decision will have any chilling effect on future plaintiffs' communication with their attorneys. Future plaintiffs and their attorneys will not alter their communication based upon the possibility that at some point there might be a stipulated settlement based upon the trial court's exercise of discretion under the unique facts of this case.

Moreover, the attorney-client privilege is just as important to defense counsel and their clients. In this case, Plaintiffs obtained defendants' privileged communications and used it as a weapon. If Plaintiffs are allowed to use attorney-client privilege as a sword and as a shield, the attorney-client privilege will be weakened not strengthened.

Plaintiffs also rely upon spurious accusations against Philadelphia to argue that Philadelphia should have obtained the discovery it now seeks prior to the stipulated settlement. This argument lacks merit. First, Philadelphia's conduct is not at issue.<sup>119</sup> Second, Philadelphia was not a party to this litigation prior to the stipulated settlement. Third, discovery in preparation for a reasonableness hearing is focused on what information was known or available to the settling parties and their counsel at the time the settlement was reached. Thus, the focus of discovery is different than

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<sup>119</sup> In reasonableness proceedings, the court is required to protect the insurer's interests by ensuring the amount of the judgment is reasonable.

the discovery the parties were engaged in prior to settlement. Fourth, Plaintiffs' arguments are built upon Plaintiffs' counsel's testimony and privileged information that Plaintiffs gleaned from Defendants' files.

Finally, the purpose of a reasonableness hearing is to ensure the integrity of our judicial system and the reasonableness hearing process by preventing inflated settlements and settlements tainted by bad faith, collusion, and fraud. By his own admission, Plaintiffs' counsel refused to negotiate with Defendants because he thought it would preclude any inquiry into whether the \$25 million stipulated settlement was the product of bad faith, collusion, or fraud.<sup>120</sup>

Allowing Plaintiffs to shield their privileged communications related to the reasonableness of this settlement would create a roadmap for future plaintiffs to prevent our courts from fairly evaluating the reasonableness of covenant judgments, which would undermine the integrity of Washington courts.

## V. CONCLUSION

The stipulated settlement in this case presents unique and extreme facts. Appellants have waived privilege in almost every way possible. The privileged information is vital to Philadelphia's ability to contest the reasonableness of the stipulated settlement. Thus, it would be manifestly

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<sup>120</sup> CP at 0-000004023, ¶¶ 77-78.

unfair to deny Philadelphia access to the information necessary for Philadelphia to present its case, and, ultimately, for the trial court to determine reasonableness.

The trial court did not abuse its discretion in finding a limited waiver of Plaintiffs' privilege as to specific documents directly relevant to the reasonableness of the stipulated settlement. Accordingly, the trial court's discovery order should be affirmed.

DATED this 6<sup>th</sup> day of November, 2015.

SOHA & LANG, P.S.

By:   
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NO. 46301-6-II

COURT OF APPEALS, DIVISION II  
OF THE STATE OF WASHINGTON

BY \_\_\_\_\_  
DEPUTY

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COURT OF APPEALS  
DIVISION II  
2015 NOV 12 PM 1:21  
STATE OF WASHINGTON

LISA STEEL, individually and as Guardian ad litem for J.T., a  
minor; DOUGLAS THOMPSON and KRISTI BARBIERI, individually  
and as Guardian ad litem for S.R.B., a minor,

Petitioners/Plaintiffs,

vs.

OLYMPIA EARLY LEARNING CENTER, et al.,

Respondents/Defendants,

vs.

PHILADELPHIA INDEMNITY INSURANCE COMPANY

Respondent/Intervenor,

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COURT OF APPEALS DIV I  
STATE OF WASHINGTON  
2015 NOV -6 PM 2:29

**RESPONDENT PHILADELPHIA INDEMNITY INSURANCE  
COMPANY'S DECLARATION OF SERVICE**

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**ORIGINAL**

I am employed in the County of King, State of Washington. I am over the age of 18 and not a party to the within action; my business address is SOHA & LANG, PS, 1325 Fourth Avenue, Suite 2000, Seattle, WA 98101.

On November 6, 2015, I served a true and correct copy of **REVISED BRIEF OF RESPONDENT PURSUANT TO COURT ORDER OF OCTOBER 30, 2015** on the parties in this action as indicated:

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Agreement**

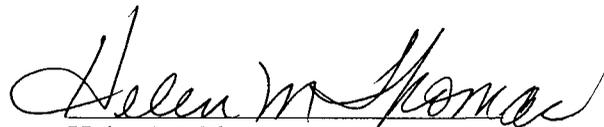
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Executed on this 6<sup>th</sup> day of November, 2015, at Seattle,  
Washington.

**I declare under penalty of perjury under the laws of the State  
of Washington that the above is true and correct.**



Helen M. Thomas  
Acting Legal Secretary to Paul  
Rosner