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8 **UNITED STATES DISTRICT COURT**

9 **DISTRICT OF ARIZONA**

10 Western Surety Company, a South Dakota
Corporation,

11 Plaintiff,

12 vs.

13 The United States of America

14 Defendants.
15

Case No.: 4:16-CV-00761-TUC-
CKJ

**EMPLOYERS MUTUAL
CASUALTY COMPANY'S
RESPONSE TO WESTERN
SURETY COMPANY'S
MEMORANDUM REGARDING
DISCOVERABILITY OF
RESERVE INFORMATION**

Hon. Cindy K. Jorgenson

16
17 Pima County, a political subdivision of
the State of Arizona,

18 Intervenor/Plaintiff,

19 vs.

20 Western Surety Company, a South Dakota
21 corporation; The United States of
America; Blue Diamond Contracting,
22 L.L.C., an Arizona limited liability
company; Employers Mutual Casualty
23 Company, an Iowa corporation; Select
Development & Construction, Inc., an
24 Arizona corporation,

25 Intervenor/Defendants.
26

27 Employers Mutual Casualty Company ("EMC"), through undersigned counsel,
28 hereby responds to Western Surety Company's ("Western") Memorandum regarding the

1 discoverability of reserve information. Western’s latest objection fails on two substantive
2 grounds: (1) Western, by claiming a bond loss, has waived any privilege that would
3 normally allow it to keep confidential the reserve information necessary to prove those
4 losses; and (2) Western does not satisfy its burden of showing the applicability of
5 attorney-client/work product protection for the reserve information.

6 **A. Western’s Assertion It Sustained Bond Losses Waives the Privilege as to the**
7 **Underlying Documents Evidencing that Loss**

8 The Court does not need to reach the issue of whether the reserve information is
9 privileged because any privilege has been waived. EMC’s need for limited discovery on
10 Western’s reserve information—by amount and date only—relates to **the** central issue
11 in the case: Did Western *itself* actually suffer performance bond losses? It is only by
12 suffering a loss **paid with its own money from its reserve** that Western can obtain the
13 equitable subrogation rights needed to have a valid claim to the money that is the subject
14 of this interpleader action. By placing at issue the existence and amount of its bond
15 losses, Western has waived any privilege with regard to the evidence that establishes
16 those losses.

17 By analogy, in Arizona, medical records and doctor/patient communications are
18 privileged—by statute, no less. See A.R.S. § 12-2235 (doctor cannot be examined
19 regarding communications made by patient with reference to medical condition); A.R.S.
20 § 32-2085(A) (psychologist-patient privilege). However, once a party enters litigation
21 claiming injuries, the privilege is waived as to those records and doctor/patient
22 communications. *Phoenix Children’s Hosp., Inc. v. Grant*, 228 Ariz. 235, 237-38, ¶ 9
23 (App. 2011) (“When a patient files a medical malpractice lawsuit, the privilege is
24 impliedly waived to allow the defendant access to information necessary to make a
25 defense.”); *Bain v. Superior Court*, 148 Ariz. 331, 334, 714 P.2d 824, 827 (1986) (holding
26 that when a psychological patient “places a particular medical condition at issue by means
27 of a claim or affirmative defense then the privilege will be deemed waived with respect
28 to that particular medical condition.”).

1 Western is no more entitled to invoke a privilege regarding the reserve information
2 that would substantiate its claim to have bond losses than a plaintiff is entitled to claim
3 injuries and then deny the defendant access to the medical records that are related to those
4 injuries. None of the cases Western cites for the view that the amount and date of reserve
5 information is subject to the attorney-client/work product privilege involve the situation
6 here, where a surety is claiming bond losses which are required to create the equitable
7 subrogation rights it claims in the lawsuit. As set forth in EMC's summary judgment
8 briefing, the record before this Court establishes that Western's co-indemnitor loaned its
9 own money to Select Development so that Select could complete the La Canada project.
10 Such an arrangement makes sense given that R&O is contractually obligated to hold
11 Western harmless from any bond losses. Now Western is attempting to retroactively
12 designate R&O as its "agent" so that it can claim subrogation rights for the money R&O
13 paid to Select. If Western wants to invoke privilege and withhold evidence that it paid
14 **its own money from its reserves**, then Western should be prohibited from offering
15 testimony that it paid a performance bond claim using its own money.¹

16 **B. Western Does Not Carry Its Burden to Establish Work Product Protection**

17 Although Western asserts the attorney-client privilege, "the communication must
18 be made to or by the lawyer for the purpose of securing or giving legal advice, must be
19 made in confidence, and must be treated as confidential." *Samaritan Foundation v.*
20 *Goldfarb*, 176 Ariz. 497, 501 (Ariz. 1993). A reserve is not legal advice, it is a dollar
21 amount. The same applies to the date the reserve is set.

22

23

24 ¹ Western's objection is waived as a matter of procedure as well. Western's initial
25 interrogatory objections, made August 9, 2018, did not mention work product or attorney-
26 client privilege. See **Exhibit A** hereto. On October 26, 2018, in email correspondence to
27 this Court outlining its position on this discovery dispute, Western again did not mention
28 attorney-client communications or attorney work product. The parties held a telephonic
hearing before this Court on November 7, 2018 regarding this dispute, and at that hearing
Western never mentioned attorney-client privilege or attorney work product. Only on
November 9, 2018 did Western first raise the issue. This Court should not be disposed to
entertain successive, new and untimely justifications for withholding documents by
Western.

1 It is axiomatic that the burden of establishing alleged work product is on the
2 proponent. *Yurick ex rel. Yurick v. Liberty Mut. Ins. Co.*, 201 F.R.D. 465, 472 (D. Ariz.
3 2001) (“[I]t must be specifically raised and demonstrated rather than asserted in a blanket
4 fashion.”) (internal citation omitted). The work product doctrine protects from discovery
5 documents and tangible things prepared by a party or a party’s representative **in**
6 **anticipation of litigation**. *Schreib v. Am. Family Mut. Ins. Co.*, 304 F.R.D. 282, 285
7 (W.D. Wash. 2014) (emphasis added) (citing Fed. R. Civ. P. 26(b)(3)). Whether work
8 product protection attaches depends on whether loss reserves were set “during the routine
9 adjustment of a potential . . . claim” or “primarily for the purpose of future litigation.”
10 *Hartford Lloyd’s Ins. Co. v. Flexible Foam Prods., Inc.*, No. 3:11-CV-0259-N, 2012 WL
11 13026945, at *1 (N.D. Tex. July 2, 2012) (internal citations omitted).

12 Western fails to carry its burden of establishing work product protection for the
13 dates and amounts of its reserves. Western’s blanket contention that it has been involved
14 in “various cases related to Select Development dating back to 2013, the date Mr. Mraz
15 first set reserves, and was certainly aware of the possibility of litigation” (Doc. 81, p.
16 2:19-22) is insufficient to show applicability of privilege or work product protection and
17 insufficient to show loss reserves were set specifically “in anticipation of litigation” as
18 opposed to in the ordinary course of business. The mere involvement of counsel in setting
19 Western’s reserves does not automatically cloak all reserve information with protection
20 from discovery. *See State ex rel. Erie Ins. Prop. & Cas. Co. v. Mazzone*, 220 W. Va.
21 525, 537, 648 S.E.2d 31, 43 (W. Va. 2007) (insurer failed to meet burden where it argued
22 that “the reserves information [was] prepared in anticipation of specific litigation since
23 the reserves are set by the company’s claims representatives and embody the mental
24 impressions of those representatives concerning issues of coverage, liability and
25 damages,” with the court concluding that “[t]his assertion hardly addresses the discerning
26 issue of whether the primary or driving motivation behind setting the reserves in this case
27 was anticipation of litigation rather than for routine business purposes”); *see also* U.S.
28 *Fire Ins. Co. v. Bunge N. Am., Inc.*, No. 05-2192-JWL-DJW, 2007 WL 1531846, at *11

1 (D. Kan. May 25, 2007), *aff'd*, 244 F.R.D. 638 (D. Kan. 2007). Western fundamentally
2 does not substantiate its work product objection.

3 **C. Reserve Information Is Generally Not Protected Work Product**

4 Sureties must set reserves as a matter of complying with state and federal law.²
5 Setting reserves is a matter of ordinary business; it is not a practice uniquely reserved for
6 litigation scenarios. As the Supreme Court of Alaska concluded in *Loyal Order of Moose,*
7 *Lodge 1392 v. Int'l Fid. Ins. Co.:*

8 Discovery of the existence and character of [the surety's] reserves appears
9 reasonably calculated to lead to the discovery of admissible evidence. In
10 reaching this conclusion we reject [the] assertion of attorney-client privilege
11 and the work product immunity doctrine. The existence and amount of any
12 loss reserve is not a protected "confidential communication [] made for the
13 purpose of facilitating the rendition of professional legal services [sic]." . . .
14 Neither is a loss reserve prepared in anticipation of litigation . . . rather, the
15 reserve is established in the "ordinary course of business."

16 797 P.2d 622, 628 n. 14 (Alaska 1990) (internal citations omitted). *See also Mazzone,*
17 648 S.E.2d at 42–43 (upholding trial court's finding that "**reserve amounts and the dates**
18 **the amounts were set are subject to discovery**" and observing that aggregate reserves
19 documents not developed primarily in anticipation of specific litigation but produced for
20 general business purposes are not protected by the work product rule) (emphasis added).
21 As a concurring opinion in *Mazzone* clearly states:

22 Simply put, in most cases I believe that the documents created in the
23 establishment of a reserve are nothing more than routine business records,
24 not opinion work product created in response to litigation. The primary
25 motivating purpose behind the creation of an insurance reserve is to comply
26 with state law, and to comply with good insurance accounting procedures.
27 These documents are therefore fully discoverable.

28 *Id.* at 533 (Starcher, J., concurring).

Western's cases to the contrary are fundamentally distinguishable. The *Rhone-*
Poulenc Rorer, Inc. v. Home Indem. Co. opinion does not indicate that reserves were

² See *J.R. Stevenson Corp. v. Dormitory Auth. of State of N.Y.*, 112 A.D.2d 113, 119 (N.Y. App. Div. 1985) (observing that "adequate reserves" must be maintained as a matter of state insurance law); see also *Acuity v. Comm'r of Internal Revenue*, T.C. Memo. 2013-209 (2013) (discussing federal regulatory and tax law implications of reserve practices).

1 sought for the basis of indicating a surety's bond losses (as here). *See* 139 F.R.D. 609,
2 613–14 (E.D. Pa. 1991). Moreover, *Rhone-Poulenc* is inapposite in that it involved “case
3 reserve figures” that were “[b]y their very nature . . . prepared in anticipation of
4 litigation[.]” *Id.* at. 614. *Prevost v. Westchester Fire Ins. Co.* involved **settlement**
5 **reserve documents**, not amounts/dates of general claim reserves, with documents that
6 “contain legal advice provided . . . by counsel.” No. 1:13-CV-00046, 2014 WL
7 12748051, at *1 (D.V.I. Feb. 4, 2014). Reserve information was not discoverable in
8 *Sundance Cruises Corp. v. American Bureau of Shipping* because it was sought for an
9 “indication of potential liability.” No. 87 CIV. 0819 (WK), 1992 WL 75097, at *1
10 (S.D.N.Y. Mar. 31, 1992). Not so here: EMC only seeks the amounts of Western's
11 reserves and the dates set as relevant information to whether Western sustained
12 performance bond losses on the La Canada project.

13 Only in “exceptional situations” and “unique circumstances”—*e.g.*, when
14 aggregate reserves documents include information developed for general litigation
15 purposes or for a particular set of cases—will reserve information be entitled to protection
16 from discovery. *Mazzone*, 648 S.E.2d at 41–42. Again, Western has not proven such
17 unique circumstances transform its basic reserve information from the stuff of ordinary
18 surety business to protected work product.

19 DATED this 30th day of November, 2018.

20
21 JENNINGS, HAUG & CUNNINGHAM, L.L.P.

22 s/ Joseph A. Brophy

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25 Attorneys for Interpleader Defendant Employers
26 Mutual Casualty Company

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CERTIFICATE OF SERVICE

I hereby certify that on November 30, 2018, I electronically transmitted the above referenced document to the Clerk's Office using the CM/ECF System for filing and transmittal of a Notice of Electronic Filing to the following CM/ECF registrants:

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s/ A. Bell _____