

The Tripartite Relationship and *Tilley*

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I. The Tripartite Relationship

The “tripartite relationship” refers to the relationship between the insured, insurance company and defense counsel. Each of those parties has a different relationship, and obligations, to the other. Under the policy, the insurer owes the insured a duty to defend and indemnify, while the insurer is typically granted the right to control the defense and is owed a duty of cooperation by the insured. Defense counsel is paid (and typically selected) by the insurance company, but acts as the attorney and representative of the insured in the litigation. Because of the conflicting interests that can arise between those parties, it has been referred to by a former Texas Supreme Court justice as “a source of unending ethical, legal, and economic tension.” *State Farm Mut. Auto. Ins. Co. v. Traver*, 980 S.W.2d 625, 633 (Tex. 1998) (Gonzales, J., concurring and dissenting).

While most cases address the ethical obligations owed by defense counsel to the insured, the nature of the relationship between defense counsel and the insurance company has been difficult for the courts to label. A majority of other states have called it an attorney-client relationship, expressly adopting a “two client” approach. The Texas Supreme Court has not directly resolved that issue, although Texas case law has gravitated towards the “one client” approach, albeit with some mixed signals along the way. Nevertheless, under *Tilley* and its progeny, it is clear that defense counsel is the attorney for and representative of the insured and owes the insured a duty of “unqualified loyalty.”

II. *Tilley*

Tilley is the Texas Supreme Court’s 1973 opinion in *Employers Casualty Co. v. Tilley*, 496 S.W.2d 552 (Tex. 1973), which first began to define the obligations of defense counsel that is retained by the insured. “*Tilley* counsel” generally refers to a lawyer hired by the insurance to defend an insured. Lawyers also sometimes use “*Tilley*” or “*Tilley* duties” as a general reference to the ethical obligations that defense counsel owes in his relationship with the insured and the insurance company, as described initially in *Tilley* and as further refined in subsequent cases.

By today’s standards, the facts of *Tilley* seem shocking. Basically, the insurance company hired an attorney to represent the insured in the defense of a third party claim, but that attorney also helped the insurance company to develop evidence to support a late notice defense that it subsequently used to deny coverage to the insured. While the attorney was both defending the insured and helping the insurance company develop its coverage defense, neither the attorney nor the carrier told the insured that there was a conflict in the services that were being provided by the attorney. Although that conduct seems obviously inappropriate by today’s standards, it apparently was not so at the time – the Texas Supreme Court specifically referenced the attorney’s “impeccable reputation” and suggested that his conduct was typical for attorneys in his position.

The Texas Supreme Court’s primary focus in *Tilley* was to determine the duty owed to the insured by defense counsel appointed by the insurance carrier. The court held that an attorney, although selected, employed and paid by the liability carrier, was nonetheless the legal representative of the insured, and as such owed the insured the same type of unqualified loyalty

as if he had been originally employed by the insured. *Id.* at 558. The majority opinion by the Supreme Court did not go so far as to unequivocally state that the insured is defense counsel's only client, but Justice Johnson did so in his concurrence: "[T]he representation provided by the attorney more appropriately should be construed as representation of a single client, Tilley." 496 S.W.2d at 563 (Johnson, J., concurring). Nonetheless, the majority's mandate of "*unqualified* loyalty" does not leave much room for debate. (emphasis added).

The Texas Supreme Court held that the attorney and the insurance company had a duty to notify the insured of the conflict on the specific coverage issue. No one had told the insured about the specific coverage defense – breach of the notice provision – that the insurance company intended to pursue. Although the insured had signed a general non-waiver agreement that said that no action by the insurer would waive the right to deny coverage, the court held that such a nonspecific agreement did not immunize the insurance company and the attorney from the failure to notify the insured of the conflict. The Court held that the failure to so notify the insured was prejudice as a matter of law, and the insurance carrier was therefore estopped to deny coverage.¹

III. Post-*Tilley* Clarifications of the Tripartite Relationship

Based upon *Tilley*, it was clear that defense counsel owed his primary duty of loyalty to the insured. Subsequent cases reiterated that principal, enhancing the connection between defense counsel and the insured while limiting the obligations between defense counsel and insurance company. *Tilley* also gave rise to the widely-held view that defense counsel should not be involved in insurance coverage issues. As subsequent cases have made clear, however, that broad perception is not entirely true, because defense counsel's duty of loyalty to the insured includes the obligation to be sensitive to conduct in the litigation that can have a potential impact on the coverage available to the insured.

A. *Garcia*

The Court provided a further clue regarding the nature of the tripartite relationship in *American Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842 (Tex. 1994), suggesting in a footnote that the insured is defense counsel's sole client under *Tilley*. In *Garcia*, the defendant, a medical doctor, was sued for malpractice. *Id.* at 843. During the relevant time period, the insured was covered by two separate policies, issued by two separate insurers (ICA and APIE). *Id.* at 843-44. The two insurers agreed to retain counsel for the insured and split the defense costs. *Id.* at 844. Although not directly related to the main issues in the case, the Supreme Court took another opportunity to proclaim the proper relationship among defense counsel, the insurer and the insured. The Court stated that defense counsel "was Garcia's [the insured], not APIE's [the insurer], attorney," and then added a reference to the *Tilley* case and its holding: "an attorney

¹ The Texas Supreme Court later clarified the application of the estoppel doctrine, distinguishing the forfeiture of the insured's rights through breach of a condition, as was involved in *Tilley*, from the situation in which an estoppel would enlarge the coverage provided by the policy, which was not permissible. *Texas Farmers Ins. Co. v. McGuire*, 744 S.W.2d 601 (Tex. 1988). The Court has also held that an insurer's defense of an insured without a reservation of rights does not estop the insurer from raising noncoverage unless the insurer's conduct prejudiced the insured. *Ulico Cas. Co. v. Allied Pilots Assoc.*, 262 S.W.3d 773 (Tex. 2008).

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