ETHICS OPINION

OFFICE OF GENERAL COUNSEL

RO-98-02

QUESTION:

The Office of General Counsel has received numerous opinion requests from attorneys who represent insureds pursuant to an employment agreement whereby the attorney is paid by the insured's insurance carrier. Some insurance companies have begun to submit to the attorney billing guidelines and litigation management guidebooks which place certain restrictions on discovery, the use of experts and other third party vendors. The billing guidelines also restrict the lawyers who will be allowed to work on the files and require pre-approval of time spent on research, travel and the taking and summarization of depositions. Some insurance companies also require the attorneys they employ to submit their bills to a third party billing review company for their review and approval. The bills obviously contain descriptions of work done on behalf of the insureds. In most instances, the insureds have not been consulted and have not approved the use of the billing guidelines and litigation management guidebook or the billing review process. The inquiry presented is whether there is any ethical impropriety in following these procedures which some insurance companies are attempting to impose.

ANSWER:

It is the opinion of the Disciplinary Commission of the Alabama State Bar that a lawyer should not permit an insurance company, which pays the lawyer to render legal services to its insured, to interfere with the lawyer's independence of professional judgment in rendering such legal services, through the acceptance of litigation management guidelines which have that effect. It is further the opinion of the Commission that a lawyer should not permit the disclosure of information

relating to the representation to a third party, such as a billing auditor, if there is a possibility that waiver of confidentiality, the attorney-client privilege or the work product privilege would occur. The Disciplinary Commission expresses no opinion as to whether an attorney may ethically seek the consent of the insured to disclosure since this turns on the legal question of whether such disclosure results in waiver of client confidentiality. However, the Commission cautions attorneys to err on the side of non-disclosure if, in the exercise of the attorney's best professional judgment, there is a reasonable possibility that waiver would result. In other words, if an attorney has any reasonable basis to believe that disclosure could result in waiver of client confidentiality, then the attorney should decline to make such disclosure.

DISCUSSION:

The Disciplinary Commission of the Alabama State Bar has addressed the conflict of interest issues raised by dual representation of the insurer and the insured in several earlier opinions. In one of those, RO-87-146, the Commission concluded as follows:

> **"Although you were retained to represent the insured by the insurance company and are paid by the company, your fiduciary duty of loyalty to the insured is the same as if he had directly engaged your services himself. See, RO-84-122; *Nationwide Mutual Insurance Company v. Smith*, 280 Ala. 343, 194 So.2d 505 (1966) and *Outboard Marine Corporation v. Liberty Mutual Insurance Company*, 536 F. 2d 730, 7th Cir. (1976). Since the interests of the two clients, the insurance company and the insured, do not fully coincide, the attorney's duty is first and primarily to the insured."**

Similar conclusions were reached in RO-90-99 and RO-81-533. Additionally, the Alabama Supreme Court discussed the insurer-insured relationship in *Mitchum v. Hudgens,* 533 So.2d 194 (Ala. 1988) and confirmed the Disciplinary Commission's analysis of that relationship, *viz:*

> **"It must be emphasized that the relationship between the insured and attorney is that of attorney and client. That relationship is the same as if the attorney were hired and paid directly by the insured and therefore it imposes upon the attorney the same professional responsibilities that would exist had the attorney been personally retained by the insured. These responsibilities include ethical and fiduciary obligations as well as maintaining the appropriate standard of care in defending the action against the insured." 533 So.2d at 199.**

See also, Hazard and Hodes, *The Law of Lawyering*, 2nd Ed. §§ 1.7: 303-304. These authorities conclusively establish the proposition that the insured is the attorney's primary client and it is to the insured that the attorney owes his first duty of loyalty and confidentiality.

Effective January 1, 1991, the Alabama Supreme Court promulgated the Rules of Professional Conduct of the Alabama State Bar. Rule 1.8(f) of the Rules of Professional Conduct provides as follows:

> **"Rule 1.8 Conflict of Interest: Prohibited Transactions**
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> **(f) A lawyer shall not accept compensation for representing a client from one other than the client unless:**
>
> **(1) the client consents after consultation or the lawyer is appointed pursuant to an insurance contract;**

(2) there is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and

(3) information relating to representation of a client is protected as required by Rule 1.6."

A similar and related prohibition is found in Rule 5.4(c) of the Rules of Professional Conduct which provides as follows:

"Rule 5.4 Professional Independence of a Lawyer

(c) A lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services."

The Disciplinary Commission has examined a "Litigation Management Guidebook" which the Commission understands to be one example among many of the procedures which some insurance companies have requested attorneys to follow in representing insureds. This guidebook contains various provisions and requirements which are of concern to the Commission. The guidebook requires a "claims professional", who in most instances is a non-lawyer insurance adjuster, to "manage" all litigation. An excerpt from the guidebook provides as follows:

"Accountability for the lawsuit rest with the defense team. This team is composed of the claims professional and the defense attorney. The claims professional is charged with fulfilling all the responsibilities enumerated below and is the manager of the litigation."

Other responsibilities of the claims professional include "evaluation of liability, evaluation of damages, recommendation of discovery and settlement/disposi-

tion." The guidebook requires the claims professional and the defense attorney to jointly develop an "Initial Case Analysis" and "Integrated Defense Plan" which are "designed for the claims professional and defense attorney to reach agreement on the case strategy, investigation and disposition plan." Furthermore, the attorney "must secure the consent of the claims professional before more than one attorney may be used at depositions, trials, conferences, or motions." The claims professional must approve "[e]ngaging experts (medical and otherwise), preparation of charts and diagrams, use of detectives, motion pictures and other extraordinary preparation ...." The Litigation Management Guidebook also requires that all research, including computer time, over three hours be pre-approved by the insurance company and restricts deposition preparation by providing that the "person attending the deposition should not spend more time preparing for the deposition than the deposition lasts."

It is the opinion of the Disciplinary Commission of the Alabama State Bar that many of the requirements of the Litigation Management Guidebook such as described above could cause an "interference with the lawyer's independence of professional judgment or with the client-lawyer relationship" in violation of Rule 1.8(f)(2) and also possibly constitute an attempt "to direct or regulate the lawyer's professional judgment" in violation of Rule 5.4(c). The Commission is of the opinion that foremost among an attorney's ethical obligations is the duty to exercise his or her independent professional judgment on behalf of a client and nothing should be permitted to interfere with or restrict the attorney in fulfilling this obligation.

An attorney should not allow litigation guidelines, or any other requirement or restriction imposed by the insurer, to in any way impair or influence the independent and unfettered exercise of the attorney's best professional judgment in his or her representation of the insured.

The Commission has also examined the insurance company's "Billing Program" pursuant to which attorneys are required by the insurance company to submit their bills for representation of the insureds to a third party auditor for review and approval. Not only are the bills themselves to be submitted to the auditor, but all invoices must be accompanied by the most recent Initial Case Analysis and Integrated Defense Plan which contains the defense attorney's strategy, investigation and disposition plans. Each activity for which the attorney bills "must be described adequately so that a person unfamiliar with the case may determine what activity is being performed."

It is the opinion of the Disciplinary Commission that disclosure of billing information to a third party billing review company as required by the billing program of the insurance company may constitute a breach of client confidentiality in violation of Rules 1.6 and 1.8(f)(3) and, if such circumstances exist, such information should not be disclosed without the express consent of the insured.

However, the Commission also has concerns that submission of an attorney's bill for representation of the insured to a third party for review and approval may

not only constitute a breach of client confidentiality, but may also result in a waiver of the insured's right to confidentiality, as well as a waiver of the attorney-client or work product privileges. While it is not within the purview of an ethics opinion to address the legal issues of whether and under what circumstances waiver may result, the fact that waiver is a possibility is a matter of significant ethical concern. A recent opinion of the United States First Circuit Court of Appeals, *U.S. v. Massachusetts Institute of Technology*, 129 F.3d 681 (1st Cir. 1997), held that the IRS could obtain billing information from MIT's attorneys, which would otherwise be protected under the attorney-client privilege and as work product, because MIT had previously provided this same information to Defense Department auditors monitoring MIT's defense contracts. The Court held that the disclosure of these documents to the audit agency forfeited any work product protection and waived the attorney-client privilege. MIT argued that disclosure to the audit agency should be regarded as akin to disclosure to those with a common interest or those who, though separate parties, are similarly aligned in a case or consultation, e.g., investigators, experts, codefendants, insurer and insured, patentee and licensee. The Court rejected this argument holding that an outside auditor was not within the "magic circle" of "others" with whom information may be shared without loss of the privilege.

> **"Decisions do tend to mark out, although not with perfect consistency, a small circle of 'others' with whom information may be shared without loss of the privilege (e.g., secretaries, interpreters,**

> **counsel for a cooperating codefendant, a parent present when a child consults a lawyer).**
>
> **Although the decisions often describe such situations as one in which the client 'intended' the disclosure to remain confidential, the underlying concern is functional: that the lawyer be able to consult with others needed in the representation and that the client be allowed to bring closely related persons who are appropriate, even if not vital, to a consultation. An intent to maintain confidentiality is ordinarily necessary to continue protection, but it is not sufficient.**
>
> **On the contrary, where the client chooses to share communications outside this magic circle, the courts have usually refused to extend the privilege." 129 F.3d at 684.**

As indicated above, the question of whether disclosure of billing information to a third party auditor constitutes a waiver of confidentiality or work product is essentially a legal, as opposed to ethical, issue which the Commission has no jurisdiction to decide. The Commission is also aware that this may be a developing area of the law which could be affected, or even materially altered, by future decisions. However, while the Commission recognizes that the MIT opinion may not be the definitive judicial determination on this issue, the possibility that other courts could follow the 1st Circuit makes it incumbent on every conscientious attorney to err on the side of caution with regard to such disclosures. If disclosure to a third party auditor waives confidentiality, the attorney-client privilege or work product protection, then such disclosure is clearly to the detriment of the insured to whom the defense attorney owes his first and foremost duty of loyalty. Attorneys who represent the insured pursuant to an employment contract with the insurer should err

on the side of non-disclosure when there is any question as to whether disclosure of confidential information to a third party could result in waiver of the client's right to confidentiality or privilege.

Furthermore, while a client may ordinarily consent to the disclosure of confidential information, the Commission questions whether an attorney may ethically seek the client's consent if disclosure may result in a waiver of the client's right to confidentiality, the attorney-client privilege or the work product privilege. This concern was specifically addressed by the State Bar of North Carolina in Proposed Ethics Opinion 10. The opinion points out that "the insured will not generally benefit from the release of any confidential information." To the contrary, release of such information could work to the detriment of the insured.

> **"The release of such information to a third party may constitute a waiver of the insured's attorney-client or work product privileges. Therefore, in general, by consenting, the insured agrees to release confidential information that could possibly (even if remotely) be prejudicial to her or invade her privacy without any returned benefit."**

The North Carolina opinion discusses the comment to Rule 1.7(b) which states that the test of whether an attorney should ask the client to consent is "whether a disinterested lawyer would conclude that the client should not agree." The opinion concludes as follows:

> **"When the insured could be prejudiced by agreeing and gains nothing, a disinterested lawyer would not conclude that the insured should agree in the absence of some special circumstance. Therefore, the lawyer must reasonably conclude that there is some benefit to the insured to outweigh any reasonable expectation of**

prejudice, or that the insured cannot be prejudiced by a release of the confidential information, before the lawyer may seek the informed consent of the insured after adequate consultation."

In reaching the above stated conclusions, the Disciplinary Commission has examined and considered, in addition to opinion of the North Carolina Bar referenced above, opinions issued by, or on behalf of, the Bar Associations of Florida, Indiana, Kentucky, Louisiana, Missouri, Montana, North Carolina, Pennsylvania, South Carolina, Utah, Washington and the District of Columbia. All of these opinions appear to be consistent with the conclusions and concerns expressed herein. Only Massachusetts and Nebraska have released opinions which may, in part, be inconsistent with this opinion, and it appears that the opinions from these two states are not official or formal opinions of those states' Bar Associations.

In summary, and based upon the foregoing, it is the opinion of the Disciplinary Commission of the Alabama State Bar that a lawyer should not permit an insurance company, which pays the lawyer to render legal services to its insured, to interfere with the lawyer's independence of professional judgment in rendering such legal services, through the acceptance of litigation management guidelines which have that effect. It is further the opinion of the Commission that a lawyer should not permit the disclosure of information relating to the representation to a third party, such as a billing auditor, if there is a possibility that waiver of confidentiality, the attorney-client privilege or the work product privilege would occur.

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