

## ETHICS OPINION

RO-2007-01

OFFICE OF GENERAL COUNSEL

### **INSURANCE STAFF COUNSEL**

#### **QUESTION:**

The Disciplinary Commission has determined that it would be appropriate to give further consideration to the conclusions reached in RO-1981-533 which addresses the issue of whether and/or to what extent liability insurers may employ staff counsel to represent insureds.

#### **ANSWER:**

A lawyer who is a full-time employee of a liability insurer may represent his employer's insured where the interests of the insured and the insurer are fully aligned and where the insurer has a direct financial interest in the outcome of the litigation. At the outset of representation, staff counsel must disclose that he/she is a full-time employee of the insurer and disclose any limitations upon the representation. In representing an insured, a staff attorney should ensure that the insurer does not interfere with the lawyer's independence of professional judgment, and must otherwise comply with the Rules of Professional Conduct.

#### **DISCUSSION:**

In RO-1981-533, the Disciplinary Commission determined that it was ethically permissible for a liability insurer carrier to prosecute subrogation actions on behalf of the carrier and the insureds' deductible, to handle worker's compensation claims against the carrier's insureds, and to represent the insured wherein the carrier is made a direct party to the civil action. At the time RO-1981-533 was released, Alabama was operating under the former Alabama Code of Professional Responsibility. Alabama has since adopted a new code based primarily on the ABA's Model Rules of Professional Conduct. As such, the Disciplinary Commission feels that it is appropriate at this time to revisit the holding of RO-1981-533 in light of the current Alabama Rules of Professional Conduct and evolving standards of ethical conduct.

In doing so, the Disciplinary Commission believes it is first necessary to answer a question that was not addressed in RO-1981-533 – whether the utilization of staff counsel<sup>1</sup> by an insurance carrier constitutes the unauthorized practice of law. Rule 5.5, Ala. R. Prof. C., prohibits attorneys from assisting a non-lawyer entity in the “performance of activity that constitutes the unauthorized practice of law.” The Supreme Court of Alabama has not addressed the issue of whether the utilization of staff counsel by an insurance carrier constitutes the unauthorized practice of law. Therefore, the Disciplinary Commission relies on its own interpretation of relevant case law and statutory authority.

The Supreme Court of Alabama has stated that “the specific acts which constitute the unauthorized practice of law are and must be determined on a case-by-case basis.” Coffee Cty. Abstract and Title Co. v. State, ex rel. Norwood, 445 So. 2d 852, 856 (Ala. 1983). As a starting point, § 34-3-6, Ala. Code 1975, which defines the practice of law, provides, in pertinent part, as follows:

(a) Only such persons as are regularly licensed have authority to practice law.

(b) For the purposes of this chapter, the practice of law is defined as follows:

Whoever,

(1) In a representative capacity appears as an advocate or draws papers, pleadings or documents, or performs any act in connection with proceedings pending or prospective before a court or a body, board, committee, commission or officer constituted by law or having authority to take evidence in or settle or determine controversies in the exercise of the judicial power of the state or any subdivision thereof; or

(2) For a consideration, reward or pecuniary benefit, present or anticipated, direct or indirect, advises or counsels another as to secular law, or draws or procures or assists in the drawing of a paper, document or instrument affecting or relating to secular rights; or

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<sup>1</sup> In various treatises and opinions, these lawyers have been referred to as “house counsel”, “captive attorneys”, and/or “trial division employees”. The term “staff attorney” is used throughout this opinion to designate such lawyers.

(3) For a consideration, reward or pecuniary benefit, present or anticipated, direct or indirect, does any act in a representative capacity in behalf of another tending to obtain or secure for such other the prevention or the redress of a wrong or the enforcement or establishment of a right; or

(4) As a vocation, enforces, secures, settles, adjusts or compromises defaulted, controverted or disputed accounts, claims or demands between persons with neither of whom he is in privity or in the relation of employer and employee in the ordinary sense; is practicing law.

(c) Nothing in this section shall be construed to prohibit any person, firm or corporation from attending to and caring for his or its own business, claims or demands, nor from preparing abstracts of title, certifying, guaranteeing or insuring titles to property, real or personal, or an interest therein, or a lien or encumbrance thereon, but any such person, firm or corporation engaged in preparing abstracts of title, certifying, guaranteeing or insuring titles to real or personal property are prohibited from preparing or drawing or procuring or assisting in the drawing or preparation of deeds, conveyances, mortgages and any paper, document or instrument affecting or relating to secular rights, which acts are hereby defined to be an act of practicing law, unless such person, firm or corporation shall have a proprietary interest in such property; however, any such person, firm or corporation so engaged in preparing abstracts of title, certifying, guaranteeing or insuring titles shall be permitted to prepare or draw or procure or assist in the drawing or preparation of simple affidavits or statements of fact to be used by such person, firm or corporation in support of its title policies, to be retained in its files and not to be recorded.

The Supreme Court of Alabama has repeatedly held that the purpose of § 34-3-6 is to ensure that laymen do not serve others in a representative capacity in areas that require the skill and judgment of a licensed attorney. Porter v. Alabama Ass'n of Credit Executives, 338 So.2d 812 (Ala.1976). Moreover, the Alabama Rules of Professional Conduct expressly recognize that corporations may employ in-house to represent their own interests in litigation. The term "firm" is defined in the Alabama Rules of Professional Conduct to include "lawyers employed in the legal department of a corporation." Rule 1.13, Ala. R. Prof. C., specifically applies to attorneys employed or retained by a corporation or other organization. As a result, staff attorneys are subject to the same ethical obligations that apply to attorneys in other forms of practice. There is no dispute that properly admitted staff attorneys may

practice law in representing their employer and, as such, are subject to the Rules of Professional Conduct. The question then becomes whether the staff attorney for an insurance company may also represent an insured.

The Disciplinary Commission notes that the insurer is not employing staff counsel as a means of generating revenue, but as a means of limiting the financial liability of its insureds. Staff counsel are employed to limit costs and losses associated with the employer's primary business of issuing insurance policies.<sup>2</sup> In Alabama, the insurer, absent an actual conflict of interest, is traditionally viewed as a co-client with the insured. The Comment to Rule 1.8, Ala. R. Prof. C., states that, "[i]n the normal insurance defense relationship where, for example, there are no coverage issues, appointed counsel has two clients, the insured and the insurer. Hence, the insurer is not a third party." This position was endorsed by the Disciplinary Commission in RO 1994-08. Moreover, in Mitchum v. Hudgens, 533 So.2d 194 (Ala. 1988), the Alabama Supreme Court implied the same thing stating: "When an insurance company retains an attorney to defend an action against an insured, the attorney represents the insured as well as the insurance company in furthering the interests of each." Id. at 198. In most instances, the insured and not the insurer, is the one whose financial interest is at risk. As such, the Disciplinary Commission finds that the utilization of staff counsel to represent insureds, where the interests of the insured and the insurer are fully aligned and where the insurer has a direct financial interest in the outcome of the litigation, does not constitute the unauthorized practice of law.

Having determined that the use of staff counsel by an insurance carrier to defend its insureds does not constitute the unlawful practice of law, the Disciplinary Commission must now determine whether the use of staff counsel violates other provisions of the Alabama Rules of Professional Conduct. The primary question, as it was in RO-1981-533, is whether an inherent conflict of interest exists when an insurer's staff attorney represents an insured. In RO-1981-553, the Commission found no reason to differentiate –under the former code of professional responsibility – between staff counsel and outside counsel when determining whether an inherent conflict of interest exists. Moreover, the American Bar Association and the majority of states who have issued an opinion on the use of staff counsel, have held that it is ethically permissible. Cincinnati Ins. C. v. Wills, 717 N.E. 2d 151, 154 (Ind. 1999).

Under the Alabama Rules of Professional Conduct, the Disciplinary Commission sees no reason to distinguish between staff counsel and outside counsel. The potential for actual conflicts of interest remains the same in either arrangement as it was under the former code. An insurer's use of staff counsel to represent an insured against a third party's lawsuit does not create an inherent conflict of interest in violation of the Rules of Professional Conduct. As discussed earlier, the Alabama Rules of Professional Conduct have previously defined

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<sup>2</sup> In instances where an insured has valid cross or counter claims, the insurer should refer the insured to outside counsel.

the relationship between insurer and insured as one in which the parties are co-clients. There are plainly many situations where representation of both an insured and the insurer is inconsistent with the Rules of Professional Conduct. However, where the interests of the insured and the insurer are fully aligned and where the insurer has a direct financial interest in the outcome of the litigation, there is not a conflict of interest that would prevent staff counsel for the insured from representing the insurer.

Staff counsel, however, should be mindful of their unique status when undertaking representation of insureds. The Rules of Professional Conduct apply to staff counsel to the same extent as any other attorney.<sup>3</sup> As such, the following measures should be taken by staff counsel when undertaking representation of insureds.

- 1) The staff attorney should, soon after commencing representation of an insured, disclose any and all limitations upon the representation. Rule 1.2(c), Ala. R. Prof. C. Examples of such limitations may include provisions in the insurance policy that authorize the insurer to control the defense and/or to settle within policy limits.
- 2) The staff attorney must disclose that he/she is a full-time salaried employee of the insurer. It is impermissible for in-house attorneys who are employed to represent insureds to state or imply that they practice in a separate independent law firm. The relationship between the attorney and the insurer should be disclosed, in writing, to the client at the outset of representation.
- 3) A staff attorney may not permit the insurance company to direct or regulate the staff attorney's professional judgment in rendering legal services to the client. Rule 5.4(c), Ala. R. Prof. C.

Rule 5.4(c), Ala. R. Prof. C., provides as follows:

**RULE 5.4: PROFESSIONAL INDEPENDENCE OF A LAWYER**

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<sup>3</sup> This Opinion is not intended to negate any prior formal opinion regarding the ethical obligations of an attorney who is representing the insured on behalf of an insurer. For example, see RO 1990-99, which requires the attorney for the insured to withdraw pursuant to Rule 1.16, Ala. R. Prof. C., if the client refuses to disclose a fraudulent act of the insured to the insurer. RO 1990-99 also held that under Rule 1.6, the lawyer is "impliedly" authorized to disclose the existence of an insurance question and to request separate counsel for the insured with regard to coverage. However, the disclosure is limited to such information "necessary to the purpose".

(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.

- 4) To comply with the confidentiality requirements of Rule 1.6, Ala. R. Prof. C., staff attorney offices should be maintained in a manner that is physically and organizationally distinct from other offices of the insurer. Where staff attorney offices are housed in the same building as other offices of the insurer, care should be taken to ensure that only staff attorneys and their administrative personnel have access to an insured's files and confidential information.
- 5) Where staff attorneys operate under a separate "firm name", the nature of the relationship between the attorneys and the insurer must be clearly disclosed on the letterhead and/or business card of the attorney. The relationship should also be disclosed at office entrances, phone book listings, and when answering the phone.

The American Bar Association and other ethics committees have found that it is unethical and deceptive for salaried in-house attorneys, employed by an insurance company, to represent themselves to be outside counsel. See ABA Opinion 03-430. Rule 7.5(a), Ala. R. Prof. C., states, in pertinent part, as follows:

#### RULE 7.5: FIRM NAMES AND LETTERHEADS

(a) A lawyer shall not use a firm name, letterhead, or other professional designation that violates Rule 7.1. A trade name may be used by a lawyer in private practice if it does not imply a connection with a government agency or with a public or charitable organization and is not otherwise in violation of Rule 7.1 or Rule 7.4.

Rule 7.1, provides, in part, as follows:

#### RULE 7.1: COMMUNICATIONS CONCERNING A LAWYER'S SERVICES

A lawyer shall not make or cause to be made a false or misleading communication about the lawyer or the lawyer's services. A communication is false or misleading if it:

- (a) Contains a material misrepresentation of fact or law, or omits a fact necessary to make the statement considered as a whole not materially misleading; . . .

Many times, staff attorney offices are operated under “firm names” that do not specifically reference the insurer. For example, a staff attorney’s office may operate under the name of “XYZ Law Offices”. One justification for the practice of using “firm names” for a staff attorney’s office is to prevent the issue of insurance from being disclosed to juries or third parties during litigation. However, the use of “firm names” by staff attorneys may constitute a misleading communication about the true nature and independence of the “firm”. As such, all letterhead and/or business cards must clearly disclose that the “firm” is an office of the insurer and its attorneys and staff are employees of the insurer. The relationship between the “firm” and the insurer should also be disclosed at office entrances, phone book listings, and when answering the phone.

- 6) To avoid loss of a counterclaim, insurance defense counsel should inform the insured about potential counterclaims that may be available to the insured.

The Disciplinary Commission finds it difficult to imagine an instance where an insured, represented by staff counsel, would have the legal acumen to consult with a private attorney concerning potential counterclaims. Rather, an insured would most often, and rightfully so, rely on the staff attorney to advise him of his legal rights, including the potential for counterclaims. As such, by undertaking representation of the insured, staff attorneys also acquire a duty to advise insureds about potential counterclaims. If a staff attorney determines that a potentially valid counterclaim exists, he must advise the insured of the potential counter claim. In most cases, the staff attorney should recommend that the insured consult with another attorney about the possibility of pursuing the counterclaim on the insured’s behalf.

The Disciplinary Commission does not believe that an insurer’s staff attorney may ethically represent an insured on a counterclaim. First, the potential for conflict of interest between the insured and the insurance company is even greater. For example, if the insurance company desires to settle the case, but the insured wishes to pursue the counterclaim, a conflict would arise. Secondly, the insurer would not have a direct financial interest in the counter claim. As such, the insurer’s use of staff counsel to pursue a counterclaim on behalf of an insured may constitute the unauthorized practice of law.

If the insured retains private counsel for representation on a counterclaim, the staff attorney representing the insured on the original claim should not take any action that is detrimental to the insured’s interest in the counterclaim, unless the insured consents.<sup>4</sup> If the insured refuses to consent because of the effect it will have on his counterclaim, then the staff attorney must either withdraw due to the conflict of interest or forgo the proposed course of action.

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<sup>4</sup> The insured’s private counsel should be consulted prior to the obtaining of the insured’s consent and waiver.

### CONCLUSION

In summation, the Disciplinary Commission finds that the utilization of staff counsel to represent insureds, where the interests of the insured and the insurer are fully aligned and where the insurer has a direct financial interest in the outcome of the litigation, does not constitute the unauthorized practice of law and is not prohibited by the Alabama Rules of Professional Conduct. At the outset of representation, however, a staff attorney must disclose that he is a full-time employee of the insurer and disclose any limitations upon the representation. In representing an insured, a staff attorney should ensure that the insurer does not interfere with the lawyer's independence of professional judgment, and must otherwise comply with the Rules of Professional Conduct.

To comply with the confidentiality requirements of Rule 1.6, Ala. R. Prof. C., staff attorney offices should be maintained in a manner that is physically and organizationally distinct from other offices of the insurer. Where staff attorney offices are housed in the same building as other offices of the insurer, care should be taken to ensure that only staff attorneys and their administrative personnel have access to an insured's files and confidential information. Staff attorney offices that employ a "firm" name must disclose that the "firm" is an office of the insurer and its attorneys and staff are employees of the insurer at office entrances, in phone book listings, when answering the phone, and on all letterhead and business cards. Finally, a staff attorney has an ethical obligation to notify and advise the insured of possible counterclaims that may be available to the insured. Ordinarily, staff counsel may not represent the insured on the counterclaim, but should, instead, advise the insured to consult with a private attorney.

JWM/s

3/14/07