ETHICS IN SETTLEMENT NEGOTIATIONS

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State Bar of Texas
ADVANCED INSURANCE LAW COURSE
April 2-3, 2009
Dallas

CHAPTER 22
Michael Sean Quinn has been a licensed lawyer in Texas since 1980. He has practiced mostly insurance law since then, with a wide variety of other kinds of cases. Until 1995, a good deal of his practice was subrogation litigation, coverage opinions and litigation, plus bad faith opinions and litigation. During this period he taught insurance, among other things, at the SMU Law School in Dallas, Texas. In 1995, he joined the Law School of the University of Texas at Austin full time for two years, where he taught insurance among other things, and then part time for several years. He has also taught insurance at the Law School of the University of Houston as an adjunct and at the graduate B-school of St. Edwards University in Austin. Starting in the 1990s, Mr. Quinn began testifying as an expert on insurance matters, and issues pertaining to lawyer conduct. (He had testified as to attorneys fees in the 1980s, as well.) Quinn's activities as an expert witness have grown over the last 10 years or so, so that they now take up as much as 80% of his practice, and sometimes more. A detailed resume can be found at my expert witness website: www.michaelseanquinn.com.
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All Lawyers Lie

Everybody lies.


A trial is a contest of lies. And everybody in the courtroom knows this. The judge knows this. Even the jury knows this. They come into the building knowing they will be lied to. They take their seats in the box and agree to be lied to.

The trick if you are sitting at the defense table is to be patient. To wait. Not for just any lie. But for the one you can grab on to and forge like hot iron into a sharpened blade. You then use that blade torip the case open and spill its guts out on the floor.

That's my job, to forge the blade. To sharpen it. To use it without mercy or conscience. To be the truth in a place where everybody lies.

Michael Connelly, THE BRASS VERDICT: A NOVEL 3 (New York: Little, Brown, 2008). (This is a crime novel in which the lead character is a criminal defense lawyer. He has appeared in at least one more of Connelly's novels.)
American Lawyers Have to Lie

Unlike juries and judges, adversary lawyers should not pursue a true account of the facts of a case and promote a dispassionate application of the law to these facts. Instead, they should try aggressively to manipulate both the facts and the law to suit their clients' purposes. This requires lawyers to promote beliefs in others that they themselves (properly) reject as false. Lawyers might, for example, bluff in settlement negotiations, undermine truthful testimony, or make legal arguments that they would reject as judges. In short, lawyers must lie. [p. 3]

Lawyers are professionally obligated to lie and cheat [i.e., treat people unfairly], both under the positive law of lawyering as it stands and under any alternative regime of professional regulation that remains consistent with adversary adjudication's basic commitment to a structural separation between advocate and tribunal. . . . The center of gravity of my argument remains the genetic structure of adversary lawyers, and in particular the separation between advocates and tribunals that constitute adversary adjudication’s core[.] [p. 4]

Professional ethics requires lawyers to betray their own senses of truth and justice in ways that contravene the ethic of self-assertion that dominates ordinary morality[.] [p. 5]

Lawyers' professional obligations to mislead and to exploit are incidents not of any specific, elaboration of the adversary ideal[,] but rather of that ideal itself. The arise ineliminably out of the structural separation between advocate and tribunal, and the
associated principles of lawyer loyalty and client control, that belong to every conception of adversary advocacy, no matter what its limits. [p. 8]

Daniel Markovits, *A Modern Legal Ethics: Adversary Advocacy in a Democratic Age* (Princeton: Princeton University Press, 2008). The author is a law professor at Yale, and the son of Richard Markovits a law professor at the University of Texas—Austin. Daniel’s Ph.D. is in philosophy from Oxford, while that of his father is in economics.)
An Argument About Lying

Not all of those who have considered the matter think that lying us 'Wrong under all circumstances. Utilitarians, for example, are committed to the view that lying is not only permissible, but morally obligatory when it would enhance the net aggregate happiness of everyone. Fifteen years ago, a non-utilitarian philosopher, David Nyberg, wrote a book entitled THE VARNISHED TRUTH: TRUTH TELLING AND DECEIVING IN ORDINARY LIFE (1993). He argues as follows:

"[T]he suggestion that the moral perfectionist requirement of being set against all deception is like telling us to loath and distrust all bacteria, including the ones responsible for wine, cheese, and normal digestive functions. It is clearly a mistake to neglect context in evaluating bacteria, only some of which are culprits of disease; others contribute to the flourishing of life. The same is true for deception, which is not only, or always a moral problem." Id. At 61. "The great battle between principled truth telling and lying represents a deep, strong current in moral and religious traditions. It's another way of describing the timeless mythic opposition of Good and Evil, Light and Darkness..." Id. At 60. "It's the artfulness we have evolved for avoiding both truth telling and lying at the same time that interests me most—the varnishing, the adding and subtracting, the partial display and concealment of what one person takes to be the truth while communicating with another. As a communicative strategy, deception is so often rewarded that it would seem to have become unavoidable and indispensable. It may actually serve to promote and preserve emotional equilibrium on a personal level, and a civilized climate for communicating with each other and living our lives together on a social level.

"It is important to stress, given [my] strong pitch...for a re-evaluation of deception, that truth telling has, had, and always will have, an important place in moral conduct and, indeed in all of social life. The point is that we need not assume it to be a moral good in every instance, nor need we assume it to be present as the background in every situation. People don’t tell the truth merely to tell the truth. They tell the truth for some reason. Truth telling is a means for accomplishing purposes. So is deception. My approach to an understanding of deception is not the usual one (top down) of focusing on the virtue of truth as a given, then finding ways to make benevolent compromises. It is, rather to focus on human communication (bottom up), and to see what roles both truth telling and deception play in furthering the process toward the achievement of worthwhile goals. The patterns and designs we create for telling the truth and deceiving express who we are, both as individuals and socially in relation to others. Both honesty and deceit are rooted in us, in our moral expectations such as ‘Avoid doing harmful things and try to do good whenever you can.’" Id. At 53-54.

Quinn’s Quote: Contemplate the following: “when all else fails, philosophize.” J.M. Coetzee, DISGRACE (1999). Quinn’s View: Most lawyers do not believe that they are engaged in a serious search for truth. Most lawyers view themselves as mouthpieces present to explain someone else’s view. Quinn’s Question: Is this view true or false?
The Importance of Being Honest

How Lying, Secrecy, and Hypocrisy Collide with Truth in Law

Steven Lubet
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Introduction

IT IS IMPORTANT to be honest, but that does not mean it is easy. Consider the challenges of simply providing truthful testimony in court. Numerous discrete steps are involved, with opportunities for error at each stage.

- First, a witness needs to have been in a position to observe the relevant events, free from distraction or obstruction.
- In addition, the witness must have been able to observe the entire event, or at least its significant aspects, rather than some unrepresentative part.
- Moreover, the witness must reliably know — not merely assume — that she saw and heard everything of consequence.
- Even then, there is no guarantee that the witness perceived the events accurately — she may have seen things out of context or from an odd angle, or she may have misconstrued certain words and gestures.
- Next, of course, she has to understand everything she perceived, drawing accurate conclusions and avoiding inappropriate suppositions.
- When she finally gets to court — perhaps months or years later — she has to remember the necessary facts, without gaps or elaboration.
- Even total recall is not enough, however, because she also has to articulate her memories with sufficient clarity and in coherent order.
- Then there is the question of emphasis — our witness must be able to stress the truly important details, without dwelling on trivia or meandering through meaningless details.

But even if our witness somehow manages to succeed in all that, there is no guarantee that the fact-finder will actually understand her. The judge or jury will also have to overcome comparable difficulties of perception,
perspective, comprehension, memory, and interpretation. And these may be skewed by extraneous factors (subtle or otherwise) such as bias, preconception, self-interest, self-doubt, self-delusion, fear, caution, sympathy, cynicism, mistrust, attraction, resentment, idealism, conjecture, and more.

Honesty is elusive for all of the players in the legal system — clients, lawyers, judges, teachers — even with the best intentions, because it is inherently difficult to recognize, communicate, and appreciate the truth. Other values, such as confidentiality, autonomy, and fairness, also play a role. Sometimes secrets must be kept and accurate information must be barred. Still, most lawyers do their best to be honest, dealing as much as possible only in truth, within the limits of self-awareness and procedural constraints.

No one pays much attention to honest lawyers, however, for the excellent reason that there is not much to say about them. To paraphrase Leo Tolstoy's famous observation about happy families, all honest lawyers are alike. Or to put it somewhat differently, there is really only one way to be honest — whether we define honesty as truthfulness, candor, integrity, or something else ineffable — which ultimately makes the subject unremarkable, mostly routine if not quite mundane.

Without basic honesty, our entire judicial system — with its structure of rights, autonomy, due process, and the rule of law — would collapse because we could not rely on the good faith of the human beings who administer it. Honesty-deficient lawyers and judges — and, yes, law professors — can do enormous and unpredictable harm to both individuals and institutions because, again paraphrasing Tolstoy, every dishonest lawyer is dishonest in his or her own way.

And it is not only the out-and-out liars who spell trouble. There are nearly innumerable ways, either bold or subtle, in which lawyers can fall short: obfuscation, exaggeration, guile, concealment, misrepresentation, trickery, omission. It is intriguing simply to list these potential departures from pristine honesty, and there are many more, because — let's face it — not all such conduct is prohibited by the legal profession, and sometimes it is even rewarded. In this context, honesty is an elusive aspiration — a platonic ideal — and its negative complement is not so much dishonesty as imperfection.

It is that conundrum, of course, which proves to be endlessly engaging. The legal professions turn out to have a complex and often discomfiting approach to honesty. To be sure, we prize its positive virtues, including
disclosure, transparency, and forthrightness. In contrast we condemn such subversive behaviors as lying, cheating, scamming, and fraud. That seems clear enough, but not everything in the world, much less in the courts, can be easily characterized as true or false. Most lawyers operate in the vast distance between those two absolutes, where facts are muddy, motivations are enigmatic, loyalties may be clouded, and duties are frequently vague or contradictory. It is there that we find not only the ever-present temptations to deceit, but also several inescapable impediments to absolute honesty that affect even the most sincere attorneys.

It is a given that faithful lawyers are required to keep clients’ confidences and pursue clients’ goals. Thus, law practice invariably involves a good deal of selective omission, skillful evasion, and, shall we say, the artful characterization of inconvenient facts. In addition, there are other factors that make it difficult—for lawyers, clients, judges, critics, and everyone else—to recognize or accept the truth. No one is immune to some small measure of hypocrisy, self-delusion, denial, or wishful thinking, all of which diminish our ability to appreciate—and therefore our ability to convey—the utter truth.

The essays in the following pages will explore the strained relationship between honesty and the major participants in the legal system, dividing the discussion into five parts: Clients, Lawyers, Judges, Professors, and a final section on the frequently posited analogy between law practice and medicine. The focus is primarily on poor behavior and questionable practices—not because they are more prevalent or important than elementary decency, but because they are more instructive. In every field, much knowledge is gained from negative examples: pathologists study illnesses to learn more about health; city planners observe traffic jams so that they may eliminate congestion; climatologists measure CO₂ emissions in order to preserve the environment. Thus, we can learn a great deal about improving the legal system by understanding where and how it goes wrong.

Clients

We begin where lawyers always begin, with the perpetually challenging complexities of clients, who, as the Greek philosopher Protagorus would have put it, are the measure of all things. It is not unusual to divide the universe of clients into the two general categories of innocent and guilty (or perhaps blameless or at fault in civil cases, or, more broadly, either decent
or unworthy), but that would be inaccurate. From a lawyer's perspective, clients are best described as either reliable or unreliable.

Reliable clients are the best sort because they provide their attorneys with accurate and complete information, thus making possible effective representation. In that sense, reliability stands quite apart from whether a client is right or wrong on the merits. Bad people can be represented quite well, within the bounds of the law, so long as counsel has a realistic understanding of the situation. Good people, alas, hurt only themselves when they keep their lawyers in the dark.

In litigation, some clients simply lie to their lawyers in the misguided hope of selling a phony story to a credulous judge, jury, or adversary. In business transactions, unscrupulous clients entangle unsuspecting lawyers in their slick schemes by getting them to "paper" all manner of crooked deals, fraudulent stock offerings, fictional enterprises, or other imaginative swindles. These baneful characters, though dismayingly difficult to recognize, are bad news for their unfortunate attorneys—lost cases, unpaid fees, professional embarrassment, tort liability, disciplinary proceedings, and sometimes even indictment. Such clients are willfully unreliable, and the only true remedy is to avoid them at all cost.

But a client does not need to be treacherous in order to be unreliable. Because everyone is fallible, especially when it comes to memory and communication, many otherwise respectable clients may convey unpredictable information. They may do so because they are intimidated, naïve, suspicious, ignorant, arrogant, or merely foolish, and while some of these motives and causations are more excusable than others (it is much easier to forgive fear than bravado), most can be overcome through close questioning and patient explanation of the lawyer's role.

It doesn't always work, but clients tend to become more reliable as their attorneys become more trustworthy.

Lawyers

Every lawyer must constantly contend with the conflicting demands of client loyalty and responsibilities to others, generally putting the client's interests first. Clients may be selfish, inconsiderate, greedy, or mean, but it is nonetheless important to protect their rights and pursue their objectives. It is only a slight overstatement to say that respect for individual autonomy is the defining characteristic of constitutional government and a successful
free-market economy, and that lawyers are therefore the stewards of political liberty and social prosperity. Unfortunately, it does not always appear that way.

It is a sad reality that some lawyers abuse their clients' trust or exploit their privileged position in the legal system. They lie or steal or assist in all sorts of nefarious deeds. When caught, they bring disrepute upon themselves and betray their profession. Every bad actor helps create the impression that most lawyers, if perhaps not all, are corrupt connivers dedicated solely to self-enrichment.

That is a hard image to shake because good attorneys do, in fact, doggedly seek to maximize outcomes for their clients, often at considerable cost to others. There are winners and losers in every litigated case, and often in settlements and commercial transactions as well. It is difficult for the public to understand that lawyers provide a widespread social benefit by single-mindedly representing individual interests, especially when the particular individuals are marginalized, unpopular, or disgraced. Unfortunately, many political commentators have seized upon this phenomenon as an excuse to discredit the entire profession, ignoring the diffuse benefits of the adversary system while vilifying the advocates who labor within it.

It is important to be honest about the role of counsel in a free society. Thus, this section of this book will address not only the failings of attorneys themselves, but also the ways in which the legal system has been regrettably, and dangerously, mischaracterized for political purposes.

Judges

Certain judges, needless to say, have their own set of problems with honesty, and I'm not just talking about graft and extortion. Relatively few judges ever take bribes or solicit kickbacks, although judicial miscreants naturally make headlines when they are caught. Fortunately, most lawyers, and litigants, will spend their lifetimes in the courts without ever directly encountering a corrupt judge.

Many more judges, however, fail badly at the task of honest self-appraisal. Entrusted with enormous authority over the rights and fortunes of their fellow citizens (and granted lifetime tenure, in the case of federal judges), they delude themselves into believing that they have special powers of perception and wisdom. Some few judges exhibit the well-known
“God complex,” demanding abject obeisance from all who appear before them (and pity the mortal lawyer who offers an affront). Others intermittently demonstrate less serious episodes of “black robe fever,” becoming overbearing, short tempered, or arbitrary. And even the best judges have their occasional lapses — ignoring rules of conduct, flouting public expectations, dismissing legitimate concerns — usually because they are unable to recognize in themselves the faults they would censure in others.

These dispositions can be deeply corrosive, verging on the sort of intellectual dishonesty that ultimately tends to undermine the judicial process — “I know it’s the right decision, because I’m the one who is making it!” More frequently, the problem amounts only to what we might call “introspection deficit disorder,” which is still unpleasant when encountered but not nearly as destructive as absolutism and grandiosity.

It is ironic that so many judges — whose jobs ideally call for reflection, discernment, patience, and, as Chief Justice John Roberts explained at his confirmation hearing, humility — so often fall prey to the vices of egoism, obduracy, arrogance, and (it has to be said) narcissism. Perhaps some preternatural measure of prideful confidence comes in handy, and may even be necessary from time to time, if one is to deliver decisive judgments. In any event, it is no small feat, particularly among the anointed and august, to “see ourselves as others see us.” It is therefore understandable, though far from optimal, that judges can be less than searchingly candid when they assess their own behavior or evaluate their own performance.

Academics

Judges and lawyers all began their careers as law students, eager to pursue an onerous course of study and ready for their instructors to initiate them in the intricacies of their chosen profession. At least during the first few semesters, law students look up to their teachers, expecting them to be not only knowledgeable about the black-letter law, but also candid about their own viewpoints and interpretations. A good teacher openly flags his or her opinions and does not try to pass them off as revealed truth. In a world where arguments are evaluated largely on their formal “strength” rather than according to some measure of elemental validity, a diligent law professor can inject a much-needed counterweight of intellectual rigor, and perhaps even objectivity. Many professors are in fact idealists, committed to open-minded inquiry and determined to teach their charges to
be thoughtful and tolerant, but the academy also has its fair share (if not more) of cynicism and hypocrisy.

The failings of law professors are often manifested by sharp inconsistencies between what they say and what they do. It is not hard to identify professors who are dedicated to “cutting-edge” research, although increasingly detached from the real world; theoretically broad-minded, but actually narrow and doctrinaire; stern and demanding when it comes to students’ assignments, while enjoying the leisure of a minimal teaching load; ostensibly devoted to “neutral principles” that (just coincidentally, mind you) always lead to conveniently partisan results.

Law professors seem to resemble judges in the general nature of their faults—much self-regard and little self-doubt—but there is a significant difference. Judges make meaningful, and sometimes momentous, decisions about people’s lives. The impact of teaching and scholarship, with few exceptions, is far less dramatic and much less immediate. After all, what difference does a student’s grade make, or the publication of a law review article, compared to a hefty money judgment or a prison sentence? You might therefore expect academics to be rather modest about their enterprise and qualified in their conclusions, but that is not always so. Instead, we find teachers in every field who are dogmatic in their beliefs, rigid in defense of the academic (if not social) status quo, defensive of their perquisites, devoted to hidden agendas, and impatient with outsiders.

Then again, universities have always been a soft target for critics, easily portrayed as the province of absent-minded, fuzzy-thinking, self-indulgent eggheads. Beyond the campus, does anyone even use the word “intellectual” without some slight hint of mockery? Henry Kissenger never really observed that “academic politics are vicious because the issues are so petty,” but the caricature is attractive and the imagery is indelible. Every institution can benefit from a little ridicule now and then, but let’s be fair. Professors are sincerely committed, by and large, to free expression and the unlimited exchange of ideas. Such lofty ideals are far easier to profess than they are to achieve, so it is foreseeable that we will often stumble.

Medical Practice

There was a time in American life, not so long ago, when lawyers and doctors formed a fairly small and relatively cohesive professional elite—living in the same neighborhoods, belonging to the same clubs and civic
organizations, and generally holding each other in good regard. That was before the advent of managed care, the explosion in the sheer number of lawyers, the expansion of state and federal regulatory regimes, the rise of consumer advocacy, the demise of “professional courtesy,” the proliferation of tawdry prime-time soap operas, and many similar social and political developments. In the old days, doctors and lawyers believed that they shared, or mutually appreciated, a core set of professional values. Lately, not so much.

Today, doctors and lawyers often seem to be at war. Many physicians complain that they are under assault by a legal system run amok — victimized by ridiculous standards of malpractice liability, penalized by runaway juries, coerced into unfair settlements, and driven to debt by exorbitant insurance premiums. For all of that, and more, they are resentful of judges and angry at lawyers.

In response, lawyers tend to be, frankly, jealous. Doctors, for all their travails, have managed to maintain great public respect. They are widely admired for their altruism, dedication, education, competence, and (despite the occasional scandal) integrity. Lawyers, on the other hand, have become the objects of derision and the subjects of low humor. Even lawyers tell lawyer jokes, whose punch lines inevitably play on some variation of deceit, cupidity, or richly deserved popular scorn.

When doctors are idealized as saintly healers, while attorneys are stereotyped as ethically challenged con artists, it is predictable that many lawyers and lawyer-commentators will look to physicians as models for a better practice paradigm. Perhaps the legal profession could redeem itself — maybe even regain some public trust — if only lawyers behaved more like doctors.

As attractive and hopeful as it may be, the analogy between law practice and medicine is plainly inaccurate. Lawyers proceed from an ethic of autonomy and are required to advocate a client’s self-determined goals (so long as they are evidently lawful). Physicians, on the other hand, proceed from an ethic of care (sometimes called benevolence or even paternalism), in which they may administer or withhold treatments according to considerations that may go beyond a patient’s immediate requests.

It is that very dissimilarity, however, that makes it useful to compare the practices of law and medicine, with each as a foil for the other. This is particularly the case concerning such honesty-freighted issues as candor, disclosure, and confidentiality, where the norms of attorneys and physicians call for sharply different approaches. Indeed, the comparison of the
two professions — single-minded champions of individual rights versus tempered guardians of public health — can help explain just why lawyers do what they do. Surprisingly, lawyers' ethics (the formal rules, that is, if not the daily instantiations) may sometimes provide important lessons for physicians, especially when it comes to practical matters such as conflicts of interest and informed consent.
PROFESSIONAL ETHICAL RULES GOVERNING LAWYERS' LYING, E.G., IN NEGOTIATIONS

1. "As negotiator, a lawyer seeks a result advantageous to the client but consistent with requirements of honest dealing with others." (ABA, Preamble [2], Texas. Preamble [2].)

2. A lawyer may not knowingly counsel a client to or assist a client in committing a crime or fraud, although a lawyer may advise a client as to the probable consequences of such a contemplated action. (A-1.2(d), T-1.02(c).) Both systems of rules define the term "knowingly" the same way, but they define the word "fraud" slightly differently, although both definitions of their "fraud"-definitions involve the idea and the language of "purpose to deceive.")

3. A lawyer shall reasonably consult with his/her client about the means by which the client's objective may be achieved. This would include informing and explaining to the client what a lawyer cannot do as the result of controlling law, including the applicable ethical rules. (A-1.4(a)(2) & (4), T-1.02(f).)

4. A lawyer may disclose confidential information from or regarding the client when it is reasonable to accomplish one or more of the following: to prevent the client from committing a crime or fraud, to prevent rectify, or mitigate injury in furtherance of the lawyer's services when the act or activity has already begun, to obtain legal advice, to avoid criminal or ethical charges against the lawyer, to deal with a lawsuit between the lawyer and client. (A-1.6(b)(2)-(5), T-1.05(C0((4)-(7).) The rules are worded somewhat differently and applications may differ a bit. The foregoing tried to capture both of them, but tends more toward the ABA rule.)

I am tired of using the words "lawyer," "attorney," and "client" to summarize and paraphrase the rules. I will therefore switch to "L" and "C."

5. L shall (must = is obligated to) withdraw from representing C, if L's continued representation of C would result in L's violating the Rules of Professional Conduct or some other law, e.g., law forbidding fraud. (A-1.16(a)(1).)

6. L may withdraw if C persists in conduct which L has characterized to C as involving crime or fraud and has (at least thereby) advised not to perform or quite performing (A-1.16(b)(2)), or if L has advised C regarding the criminal or fraudulent character of his

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1 Citations will hereinafter be abbreviated by "A-" for rules, etc., of the ABA, MODEL RULES OF PROFESSIONAL CONDUCT and "T-" for the TEXAS DISCIPLINARY RULES OF PROFESSIONAL CONDUCT. All of the underlinings in this list are mine, and they emphasize fraud, since that is more or less the focus of this presentation.

2 This rule is related to the "Misconduct" rules in Rule 8.4.
contemplated conduct, and C goes forward anyway (A-1.16(b)(3).) [For the purposes of this discussion Item #5 is vastly more significant than Item #6.]

7. L shall not knowingly “make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by” L. (A-3.3(a)(1), T-3.03(a)(1) & 3.03(B). The A-rule and the T-rule are different when it comes to correcting past errors; the former covers corrections with respect to both fact and law, while the latter covers only facts.)

8. L shall not knowingly offer evidence L knows to be false, and if has done so, he will correct the error upon learning the truth. (A-3.3(a)(3), T-3.03(a)(5)-(b).)

9. If L is representing C in an adjudicative proceeding, and L knows that C was, is or intends to engage in criminal or fraudulent conduct related to the proceeding, then L “shall take reasonable remedial measures, including, if necessary, disclosure to the tribunal.” (A-3.3(b); the T-rules have no independent or equivalent or analogue to 3.3(b) in T-3.03(b).)

10. “In the course of representing [C, L] shall not knowingly: (a) make a false statement of material fact or law to a third person; or (b) fail to disclose a material fact when disclosure is necessary to avoid assisting a criminal or fraudulent act by [C], unless disclosure is prohibited by Rule 16.” (A-4.1. T-4.01(a) is the same and A-4.1(a).)

Comment [2] to the A-rule reads as follows: “Under generally accepted conventions in negotiation, certain types of statements ordinarily are not taken as statements of material fact. Estimates of price or value placed on the subject of a transaction and a party’s intentions as to an acceptable settlement of a claim are ordinary in this category, and so is the existence of an undisclosed principal except where nondisclosure of the principal would constitute fraud.4

11. If L₁ knows that L₂ has violated the applicable rules of professional conduct and if that violation “raises a substantial question about [L₂’s] honesty, trustworthiness, or fitness as a lawyer in other respects, [L₁] shall inform the appropriate [professional/disciplinary] authority. (A-8.3, T-8.03.)

12. It is professional misconduct, so no L shall violate the ethical rules or either induce or assist someone else to do so, nor shall L commit [T: any “serious”] criminal acts [or any]

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3 The T-rule is different when it comes of §(b). Here is how T reads: 4.04(b): “fail to disclose a material fact to a third person when disclosure is necessary to avoid making [L] a party to a criminal act or knowingly assisting a fraudulent act perpetrated by [C].” This is different from A-4.1(b): (1) the A-rule talks about “assisting” the T-rule talks about being a “party.” (2) The A-rule except disclosures prohibited by A-1.6, which prohibits the disclosure of lots of confidential information, whereas the T-rule contains no such exception. Question: Why is law included in both sections (a) but left out of both sections (b)?

4 The T-Comment is almost the same. As to a party’s intention regarding settlement, the T-Comment #1 reads slightly different: “a party’s supposed intentions as to an acceptable settlement of a claim may be viewed merely as negotiating positions rather than as accurate representations of material fact.”
at all] that reflect adversely upon L's "honesty, trustworthiness, or fitness"; of "engage in conduct involving dishonesty, fraud, deceit or misrepresentations[]." (A-8.4(a)-(e), T-8.04(a)(1)-(3).)
FEATURE ARTICLE
Lawyer-Performance Suits Brought by Liability Insurers Against Defense Counsel 245
Michael Sean Quinn & Susan Scott Hayes

CASES

Additional Insureds/Property Damage
Subcontractor’s liability insurer has no duty to defend additional insured general contractor, where the homeowners’ underlying complaint did not establish property damage sustained as a result of the subcontractor’s negligence

Agents & Brokers
Insurance Network of Texas v. Koesel (Tex. App.) 267
Whatever duty a policyholder owes his intermediary to read and understand the policy acquired is simply a rebuttably presumptive component of the comparative negligence defense available to the intermediary

West v. Nationwide Mutual Insurance Co. (S.D. Miss.) 273
Hurricane Katrina victim states claims against insurance agent for negligent misrepresentation based on agent statement regarding scope of coverage under wind policy

Automobile Insurance/Accident
North Star Mutual Insurance Co. v. Peterson (S.D.) 274
Discharge of rifle in truck prior to hunting trip was “auto accident”

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Endangered Species Act limits extension of the National Flood Insurance Program in the Florida Keys, thereby curbing development
Lawyer-Performance Suits Brought by Liability Insurers against Defense Counsel

Michael Sean Quinn & Susan Scott Hayes

This article discusses three questions. Better put, it explores three groups of questions, where each group can be formulated as if it were a single question. First, should liability carriers be able to sue for malpractice when they have defended or paid for the defense of an insured but the case has been lost—and probably fueled up by the defense lawyer(s)? The problem here arises from a strong rule of law, which is nearly absolute in many places. Here is the rule: only a client ("C") of a given lawyer ("L") can sue that lawyer for malpractice ("LM"), even broadly conceived to include, for example, breaches of fiduciary duty ("LM+").\(^1\) Often this is called the "Privies Rule,"\(^2\) the "Rule of Privies," or the "Rule of Legal Malpractice Requiring Privities," and to at least some degree this rule is applied in the great majority of states. We will be arguing that defending liability insurers should be able, in legal contemplation, to sue the defense counsel for LM or LM+ when the carrier has hired, directed, (perhaps) supervised, and/or paid defense counsel, and when neither the insured-defendant involved nor the relevant liability insurer is (very much) at fault in handling the defense, and the defense is arguably botched.

Second, if liability insurers should be able "validly" to sue defense lawyers they hire (or pay) for their insured, then what is (are) the best legal doctrine(s) upon which to base that right? This question can be addressed from two points of view: jurisprudential and practical. The latter of these two points of view, in answering virtually any legal question, pays special attention to temporally relevant recent legal history. As already pointed out, temporally relevant legal history is such that only relevant client(s), and (almost) no one else, may ever sue their lawyers for malpractice using the established tort theory of lawyer malpractice.\(^3\) Ultimately, we suggest that liability insurers should be able to use breach of contract—as opposed to some tort theories—as their foundational theory in suing defense lawyers, even if actual clients cannot.

In many jurisdictions, breach of contract is officially recognized as unavailable to those suing lawyers for poor performance. Why this is so is a bit of a mystery. Given this history and that state of the law today, inviting liability insurers to use breach of contract while actual clients use negligence might be quite efficient. We will also suggest that what might be called *injury to an intended contract beneficiary* could also be a valid cause of action, although this suggestion is more radical than simply using breach of contract.

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1. So that the idea of legal malpractice includes other legal theories and hence types of claims, including breach of fiduciary duty and perhaps even applicable statutes. This we name "LM+" for short.
3. The major exceptions are, of course, fraud, deceit, and some forms of misrepresentation. Nonclients can sue lawyers for these, even though the lawyers are functioning as lawyers in their professional capacity. M & S §6.7. Lawyers-acting-as-lawyers can also be liable to nonclients for holding onto money to which the nonclient has a right. Id. at § 6.4. The same goes for money over which a nonclient has a lien. Id. In addition, lawyers while representing can be liable for malicious prosecution when they bring obviously unsound lawsuits and lawsuits they know to be unsound. Id. at § 6.5. Also, absent an explicit contract, lawyers are probably not liable to expert witnesses for fees which their clients have failed to pay. Id. at § 6.5. Of course, when lawyers are acting not as lawyers for a client, but as lawyers in the "law biz," they can be sued for all the usual business reasons.
Third, are there other legal theories, which may not be the best—or even better—legal foundations for liability insurers that wish to sue the lawyers who have defended their insured, but which are still satisfactory or reasonable foundations for such suits, even if the theories have flaws? Of course this last question can be answered in either theory or in practice. In theory, there are other legal doctrines which are satisfactory, and in at least one case the alternative may be better than the contract theory, namely the assignment theory. In practice, however, as a matter of still recent legal history, there is no better legal doctrine than something contractually based, whether it be breach of contract—which is quite simple and straightforward—or injury to an intended beneficiary—which is less simple, less historically grounded, and which contains more difficulties.

I. Some Background: A Sketch

Legal malpractice (LM) is a tort cause of action which C has against L for what is often described as professional negligence (e.g., poor, unreasonable, below standard, sub-par, below accepted standards, etc.). This also could be called unintentionally poor lawyerly performance. This idea includes gross negligence, i.e., really poor performance that L (or someone in L’s group) consciously knew was very, very high risk. Often gross negligence is described as “recklessness.” Usually, recklessness is classifiable as a type of negligence; it is not quite an intentional tort; but it is closer to that than it is mere sloppiness. It would be helpful—since informative—if grossly negligent professional conduct by lawyers was called “gross attorney malpractice,” but this is not customary.4 One more additional category is often included in this same category—LM+—which is breach of fiduciary duty by a lawyer with respect to a client.5

Here is yet another way to conceive malpractice and fiduciary duty violations. One court has said that, under Texas law, there is a way completely to distinguish legal malpractice from breach of fiduciary duties: (1) “If a claim, regardless of what it is called, involves a lawyer’s performance in representing a client, then it is a legal malpractice claim.”6 (2) “If a claim involves a lawyer’s ‘integrity and fidelity,’ then it is a breach of fiduciary duty claim.”7 Any claim involving only the latter category is purely a fiduciary duty breach claim. On this account, a deliberate breach of the fiduciary duty running from lawyers to their client is never a subcategory of legal malpractice. It remains open how to think about negligent breaches of fiduciary duties by lawyers owed to clients. The court under discussion seems to want to classify all the causes of action as a separate category of tort, although one involves negligence and another involves contract. The law would count breach of contract, if it applies, as a species of LM+; it would certainly not be unified with LM simpliciter.

Several questions come to mind when reflecting on the quoted language being discussed. (i) One wonders if this way of distinguishing the two types of action is really correct, impressive though it is. After all, L could “throw” a performance by accepting a bribe from the other side, but the loss was much larger than either side expected. Surely that would be both malpractice and a breach of fiduciary duties, given the court’s definitions. (ii) One might wonder how this way of demarcating the two ideas would fare if there was an accusation of negligent breach of fiduciary duties. (iii) One might also wonder if all breaches of fiduciary duties by lawyers should be conceived of as being subcategories of legal malpractice. To the extent that malpractice is a child of or a sibling of negligence, this equation does not—in the end—make sense. (iv) Finally, if we are right that liability insurers should be able to sue defense lawyers, even when the former are

4. The leading treatise on this general subject is the 5 volume set, Ronald Mullen & Jeffrey M. Smith, LEGAL MALPRACTICE (5th Ed. 2000) (“M & S”). The phrase “legal malpractice” is often treated broadly to cover any civil action which might be brought against a lawyer for allegedly injurious errors or omissions. “Historically, an attorney’s malpractice exposure for negligence has been limited to a client. Within that confines, attorneys can gauge the nature of their duties and how to fulfill those duties. Beginning in the 1970s, there has been an expansion of liability to persons who are not clients but to whom attorneys can owe a duty of care.” M & S, n. 1, at § 7.1, p. 675 of V. 1. Gross legal malpractice could be abbreviated LMG.
5. Id. at Ch 17.
7. Id. (Emphasis added)
not clients of the latter, should they be able to sue those lawyers on the basis of breach of fiduciary duty, if the fiduciary duty runs only to a client? (vi) Can breach of fiduciary duty be conceived as breach of contract, as well as a tort of sorts? If so, does the liability insurer have the right contract with L for that? (v) Should assignment be permitted for causes of action of breach of fiduciary duties? It should be noted that giving affirmative answers to (iv)-(vi) is more radical that the actual conclusions of this paper. Interestingly, the court opinion quoted in the preceding paragraph at least may be impliedly committed to exactly this. Lawyers who treat clients without integrity and/or fidelity deserve to take legal "licks," and their conduct does not systematically "ask" for protection.

Perhaps the Cardere court is implying that if a client's claim involves both categories—legal malpractice and breach of fiduciary duty—then it is a malpractice claim. If this proposition is true, that would account for the assertion of some courts of appeals (here and there) that a plaintiff should not be able to assert both types of claims against a lawyer. Sometimes this move by courts is called the "Anti-Fracturing Rule"; this phrase was invented and has been deployed since the strategy or option of plaintiffs which it condemns is called "fracturing." One wonders if the courts have this fundamental distinction right. Why couldn't one group of actions—or even one single action—count as both. What should L's selling C out in litigation be called? Perhaps deliberate conduct which would be malpractice if done negligently with respect to consequences, but counted as breach of fiduciary duty if done deliberately, with an understanding of what the consequences would most probably be. The trouble is that the tort law does not—probably ever—permit these kinds of subterfuge distinctions. They are just too difficult to work with.

Now for a summary of some of what has been explored so far. Causes of action for both legal malpractice and breaches of fiduciary duty are often restricted to clients; only clients have standing to be these sorts of plaintiffs. This is most obviously true if—or to the extent that breach of fiduciary duty is a subcategory of legal malpractice. Consequently, these theories exclude liability for insurers, except to the extent that the liability insurers are clients of the lawyers, but no more. The central argument of this essay is the following: even if, or to the extent that, a liability insurer is not the defense lawyer's client, if the errors of the lawyer injure the insurer, it should be able to recover from that defense lawyer.

II. More Specific Introduction

To repeat: in many states, when L and C by themselves have or have had an attorney-client relationship, so that there are no additional Cs involved in the relationship, only C can sue L for malpractice arising in or out of that relationship. This makes a certain degree of sense, since the responsibilities of lawyers run to clients. But what if C's liability insurer hired L, paid L, and had to pay the judgment which resulted for L’s errors? Thus, L’s errors did not cost C anything except for anxiety. It has cost the insured's liability insurer (possibly) huge amounts, however. Shouldn't the insurer be able to sue L for its damages? And what if the relevant insurer—plaintiff in the contemplated malpractice action—is other than a primary liability carrier, say, an excess carrier? What if the allegedly injured party and plaintiff in the legal malpractice action is an insurer? Should not these injured entities be able to sue L for having harmed them? If corporations are persons that have due process rights, would those rights not be violated by this prohibition?

Insurer as Client. Obviously, liability insurers might have any of the causes of action already mentioned against a lawyer that has provided it with coverage opinion or who represented the insurer badly in a lawsuit brought against it by the insured or the assignee of an insured. These are paradigms of

8. Id. Of course the two types of causes of action are different. For one thing it is necessary to prove damages and causation in malpractice cause of action, but not in a breach of fiduciary duties cause of action. Burress v. Apeco, 997 S.W.2d 229 (Tex.1999) (restitution is a proper remedy and/or punishment when there has been a violation of fiduciary duties).
10. Charles W. Wolfram, MODERN LEGAL ETHICS § 5.6.2 at 209-10 (1980). This is the legal ethics hornbook and has been for years.

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the orthodox attorney-client relationship and its possible twists and turns. No one has ever thought an insurer could not be the client of one or more lawyers.

Some History. Malpractice-type cases against lawyers have always been difficult to win. The work of litigation attorneys is almost never as simple as lots of other kinds of work—even lots of other kinds of lawyer work—and it often involves more complexity, more prolonged time intervals for rendering services, more uncertainties, more doubts, more vagaries, more "snags," more "reverse currents," as well as more "cross-currents" than other forms of lawyer work, and is hence more influenced by numerous uncertain judgments. High-risk discretionary judgments which go wrong versus negligent lawyer error in representing clients in litigation are sometimes hard to distinguish. Negligent analyses in representing litigation clients are hard to classify convincingly as LM, even though that is exactly what they may be. LM is thus hard to prove with respect to legalistic hypothesizing, thinking, imagining, acting, interacting, rhetorical designing questions, psychological insight, and much more. Legal duties and standards of care are not the only problems, of course. Most types of malpractice cases against attorneys are still difficult to win, hard to develop, and expensive to conduct, and this last point includes underlying prosecution, as well as defense. There are always questions of causation and damages. Lawyers defending malpractice suits love to set up causation as a defense. Of course, most of that defense hinges on the complexity and ambiguity of the word "cause" and its derivatives.

Nevertheless, legal malpractice cases have become somewhat more common in the last few decades, and now more lawyers are pursuing them for their clients. Some lawyers do them on contingency fees, and a few lawyers are even advertising to take them. Many believe that this most recent part of the trend is a consequence of "tort reform," which is politically popular in a number of states. Interestingly, as already noted, although LM and LM+ cases are difficult to prosecute all the way through, often lengthy, and usually expensive, the lawyer for the plaintiff in a legal malpractice case is usually safe from being sued for malpractice if he or she loses it.

A Digression on Vocabulary. The attorneys used regularly by liability insurers to defend their insureds have for a long time been called "insurance defense lawyers" and their business organizations have, for a long time, been—and still are—called "insurance defense firms." Lawyers who represented insurers directly are not insurance defense lawyers, and they had no common designation. The relevant public would be better off—from a communications point of view, as well as a social/business understanding standpoint—if the lawyers representing insurance companies directly were called "insurance company lawyers," "insurer lawyers," "insurance lawyers," or something of the sort.

Often, these lawyers are called "coverage lawyers," but this phrase is misleading. Obviously, this phrase means that the lawyer analyzes insurance policies in various contexts and provides legal opinions to whoever hires him. For one thing, (1) policyholders need "coverage counsel" just as insurers do, so the mere phrase being used does not any longer indicate the probable client of the lawyer. Of course, given "coverage counsel" is not any longer always—or, routinely, at least on one side or the other, but this is still often true. For some odd reason, many lawyers are uncomfortable about doing coverage work for their clients. That's nice for coverage lawyers, but not really necessary.

For another thing, (2) the phraseology under discussion does not explicitly refer to the role such lawyers frequently play in litigated coverage disputes, where the insurer might be either a plaintiff (as in declaratory judgment actions the insurer brings) or a defendant (as in declaratory judgment actions brought against them by or on behalf of insured). Some coverage lawyers are fit to be involved in litigation, and some are not. Not all coverage lawyers,

11. The matter of assignments will be discussed later herein. In our view, they should be uniformly permitted in this context. Most courts—though not all—do not agree.

12. Of course, the practice of law is not usually like those professions and vocations which depend upon sophisticated mathematics and advanced high-precision science. It is not difficult in that way.

unfit to be involved in litigation, realize that they are not.

In addition, there is a third point. (3) The phrases “coverage lawyer” or “coverage counsel” do not indicate the other sorts of things lawyers for insurers do in litigation with current or former policyholders. They might, for example, defend against common law and/or statutory bad faith claims of various sorts, including those involving so-called “Stowers Claims”; they might handle suits seeking the payment of premiums; they might handle suits in which the insurer is seeking court approval or authorization for policy cancellation or rescission; they might handle insurer-intermediary or intermediary-customer disputes; they might work on restitution cases; and/or they might handle suits or administrative actions involving state governing bodies, not to mention lobbying that might involve insurance departments, legislatures or both.

Another very useful phrase, at least in some contexts, is “insurance lawyer.” The phrase “insurance lawyer” does not divide, even though customary usage, those who work for insurers from those who work for policyholders or those who are mainly a type of plaintiff’s lawyer trying to get recovery from a resisting insurer after having prevailed against a policyholder. Nor does it separate all of the various activities listed in the preceding paragraph. One distinguishing phrase, when one is needed, is “policyholder lawyer.” Some lawyers who now restrict themselves to policyholders like it.

Historical Change. The system surrounding the insurance defense “industry” — or “market” — began to change dramatically about 20-25 year ago. Many liability insurers developed and now have captive firms handling most of their work defending policyholders. From a practical point of view, these are really — or, at least to some extent — “in-house” firms, though this claim is not a true description from a legal standpoint. Extensive auditing systems have become common among liability insurers using outside lawyers. At the same time, hourly rates have not gone up as quickly as or as proportionate to the rest of the legal profession. Litigation fees of $500-$750 an hour are not unheard of at senior levels in high prestige law firms in large cities, but they are nonexistent for insurance defense lawyers. Indeed, outside of extremely large complex cases, carriers still pay substantially lower fees than wealthy individuals or families pay per hour for complex, big money litigation services, including divorces. Moreover, various types of liability insurers are now suing Ls representing insureds for malpractice. Usually, they are suing when they themselves are the principal and perhaps only client. Sometimes insurers are suing when L’s principal and perhaps only client was an insured, and liability insurers had to pay bunches of money on behalf of its insured, arguably as the result of L’s negligence. The money paid is usually (i) for defending the insurer’s insured, (ii) for discharging the liability insurer’s duty to defend reasonably well, and (iii) if it was a duty to indemnify, for the amount owed under the judgment, which would usually go up to policy limits but no further, unless a reasonable settlement offer was unreasonably rejected by the insurer.

Some liability insurers now insist that the Ls they utilize for any purpose whatsoever have to purchase and prove that they have purchased legal malpractice insurance. Lawyers should take this as an admonition, if not a warning. Unless the liability insurer intends to do something about the actionable conduct of lawyers they hire to represent their insured, why would the liability insurer care whether the L has legal malpractice insurance? (Keep in mind that this kind of liability insurance covers more than legal malpractice as described above. It covers a variety of tort actions which can be brought against lawyers for


15. See Unauthorized Practice of Law Committee v. American Home Assurance Society, No. 04-0139 (Supreme Court of Texas, March 28, 2008, after having been argued on September 28, 2005)(permitting captive defense firms under all non-conflict situations).

16. Sometimes fees run even higher, e.g., in New York.
professional errors. Thus, the insurance might better be called "Lawyer Error & Omission Insurance"; that's what it really is.)

The Present. How does this system work now? Like Gaul, the insurance industry is, roughly speaking, divisible into three parts. (1) There is life insurance. (2) There is first-party coverage, where insurers pay for losses involving their properties, their assets, or their bodies (e.g., property, loss of value in an intangible asset, business interruption, and health insurance) or pay for insureds' covered expenses (e.g., hotel bills, medical bills, or losses which the insured does not pay but which are paid for him, roof repair, ransom to kidnappers, and so forth). (3) There is third-party coverage, a/k/a liability insurance, where a liability insurer defends the insured (or pays for the defense), and pays settlements or judgments when appropriate or when the insured's responsibility is established and found to be within coverage.17

Insurers hardly ever sue the Ts in life insurance cases, although disappointed beneficiaries sometimes do.18 This might happen when an angry relative who thinks he should have been a (larger) beneficiary sues the estate and trust lawyer for malpractice. Usually these beneficiaries are not clients of the willing lawyers they sue, although testators could make them into the clients by fairly simple devices. Because there is no attorney-client relationship in these cases, the plaintiffs often lose these cases in many jurisdictions, but not always.

Property insurers occasionally sue their lawyers. The foundations here are usually poor coverage advice or opinions, poor adjustment advice, or poor litigation regarding either coverage—as in declaratory judgment actions—or adjustment practices—as in statutory or common-law bad faith actions. Property insurers functioning as plaintiffs in subrogation cases could also sue their lawyers, but these cases are rare.

IV. Some Hypotheses Stated and Discussed

Some Insurer v. Lawyer malpractice—or lawyer-error cases—arise in various areas of liability insurance. Sometimes they result from I representing liability insurer directly. In these cases, the insurer is usually the only relevant client of L.

Sometimes these suits result from the way L, hired by liability insurer, represented insured (when he/she/it was sued. Sometimes that same lawyer has provided the insurer with legal advice. In the first of these two situations, of course, L represented only the insured. In the second one L represents both insured and liability insurer in the same litigation and perhaps regarding the same topic—for example, the settlement value of the case. Trouble begins here. For the most part, as already stated, in most states, only clients can sue their lawyers for malpractice,19 although lawyers can be sued by non-clients on the basis of some legal theories, e.g., malicious prosecution.20

Perhaps a diversity of examples from different sectors of the insurance industry might help place the problems facing liability insurers in context. Each of these examples is real from a historical standpoint, or nearly so. Some fiction has been added, for concealment purposes, as have some twists and turns, for other purposes. For the sake of comprehensive treatment, and to set up a contrast, we begin with something other than liability insurer (L).

(1) Here is a simple case. L advises a property insurer that it need not pay a building loss resulting from Hurricane Rita because water damage is excluded, although the wind blew the insured's roof off first-in-time, and then the building's not having a roof caused the water damage, since—rain—not flood—got in. The roof was old and therefore probably decrepit, depreciated, and deteriorated, and so therefore not covered at all, for any amount, said L.

17. Probably most liability insurance policies have a first-party consent, namely the right to a defense if sued and the factual assertions in the pleadings add up to a covered claim if proved. Lamar Homes Inc. v. Mid-Continent Casualty Co., No. 05-0832 (Tex. Aug. 31, 2007).
18. See 3 M & S, Chapter 32.
20. See 1 M & S, Ch. 6, §§ 6.8-23. Non-clients can also sue lawyers for fraud, conspiracy, abuse of process, false arrest or imprisonment, intentional infliction, defamation, invasion of privacy, conversion, etc. See William T. Barker, Floyd F. Beisstock, and Bennett Evan Cooper, Litigating About Litigation: Can Insurers Be Liable for Too Vigorously Defending Their Insureds? 42 TORT TRIM. & INS. PRAC. 1, 827 (2007) (not often with respect to abuse of process).
Ethics in Settlement Negotiations

Chapter 22

Trust me! This advice is horrible. This point is true even if there is a concurrent causation exclusionary clause in the policy. If the carrier followed that clause and L’s advice, I might think that he had an affirmative defense: “My advice was so obviously poor, that you are fools to take it, so I ought not have to pay.” No such affirmative defense—if made explicit—has ever worked, and it never will.

(2) Now suppose the insurer rejects the defense of “absolute valuelessness,” but suggests that the insured was comparatively negligent since he did not replace a roof which needed replacing. Comparative negligence may work well in many types of negligence cases, but it will not work well in property insurance disputes. First, they start with breach of the contract running from the carrier to the insured and back again. Second, the negligence of a property owner is not—in and of itself or by name—usually excluded. Furthermore, extending the previous point, it is unclear how the comparative negligence defense could be possibly be used against an allegation of bad faith, whether common law or statutory, where that very negligence is not an explicit exclusion in the insurance contract and that fact is well known in the industry.

(3) Here is another property insurance hypothetical case. Suppose the carrier insured someone for a number of years, say 26 of them, and the insured now seeks coverage for accidental events which happened during the 15th year, but cannot find the policy. Further, suppose that this insurer does not have computerized or microfilmed records going back that far, so it denies coverage, although the policies in Years 12-14 and 16-19 are all exactly the same, and the only difference between Year 19 and Year 20 is an increase in the policy limits. Finally, suppose the insurer did not know of the property damage until very shortly before it reported the claim to the insured and that empirical facts established that the time of the property damages was a long time before its discovery. If L advised the insurer that there is very little risk in denying coverage for Year 15, L has almost certainly committed malpractice. If a lawyer does not explain historical tendencies in the law to his client, the insurer, malpractice has been committed.

(4) Now for a clear liability insurer hypo. Suppose an insured is sued. The case is a big deal. It is also a complex case. The plaintiff’s opening Petition (or Complaint) contains four causes of action. Three of them are obviously not covered under a liability insurance policy, but one of them is, so the whole defense bill will—in most states—must be paid by the insured’s liability insurer, as will the indemnity price for the covered cause of action, if it is proved. L has told the insurer to refuse to defend but to offer to pay one quarter of reasonable legal fees, not to exceed $125.00 per hour. Besides, L tells his client, the factual assertions in the one claim clearly covered, are clearly false. The policy says nothing about any of these matters. It is a standard liability policy.

L is guilty of at least three different forms of malpractice in the advice it provided. (a) In Texas and similar states,21 if liability insurer has a legal obligation to defend one cause of action, it has a legal obligation to defend all of them, as already indicated. (b) Liability insurer’s duty to defend is determined by the fact pleadings in a case against an insured, whether or not true, and not by the expressly stated causes of action. (c) The amount of money specified for attorney’s fees is way too small for a serious and complex case.

(5) Here is what is your regard as the most interesting type of hypothetical case. It involves liability carriers. Suppose L is representing insured, having been hired by liability insurer. The suit is a large and serious one. The plaintiff offers to settle for primary policy limits or a shade less. In Texas this is called a “Learned Demand,” if it is done right.

L tells both the primary carrier, and the excess carrier, that they need not worry. L provides primary carrier with a “need not worry” opinion. The primary carrier passes it at the excess carrier. The opinion states and argues that the case against the liability insured will be won, and if lost the damages will be less than ¼ the policy limits of the primary carrier. L then loses the case in excess of primary limits. The primary carrier pays its policy limits and becomes insolvent (in part as a result of exactly this). The excess carrier pays the rest of the judgment. There is substantial evidence that if primary carrier had offered ⅛ of its policy limits, the case would have settled. L knew this but failed to tell anyone. He forgot to speak at the time, but his records are clear, and they indicate

that he should have told at least primary carrier about the settlement opportunity. Who has malpractice actions against L?

(6) Lastly, consider the following case. Suppose a stripper falls off a stage and injures a customer. The customer then sues the bar, but the liability insurer denies a defense, based upon L's advice, where L is representing the carrier. (Remember: There is a difference between a lawyer's representing someone and a lawyer's working for someone.) The basis of the advice was that the stripper was called "independent contractor" by the bar, a category of persons whose conduct the policy explicitly excluded. Now, suppose that the plaintiff's pleading is not sufficiently clear, that the bar is accused of inadequate supervision, and—although not mentioned in the tort pleadings—the joint actually had a set of rules for "its" strippers entitled "Dancers' Decalogue: Dance-Determined Do-Clothing." Suppose further that the L representing the liability insurer, knew about this document, which was always given to every new dancer. This is an easy case! The liability insurer will have to pay both defense expenses and indemnity. Once a liability insurer is forced to pay the customer's damages, L will lose the malpractice case brought against her by her client. Now, what if L for the insured and L for the carrier were the same person or came from the same firm?

Some Principles. Now, what principles govern lawyer conduct in these areas of practice? Here are a few.

• Do not do insurance work alone without the experience of or supervision by an experienced coverage lawyer.

• When doing coverage work, read and reread relevant cases. Do not depend upon memory, usually.

• Do not advise insurers by telling them what they want to hear, or what you think they want to hear. Find out what their initial hypothesis is. Try to falsify it. Affirm an insurer's original hypothesis—its hope—only if it cannot be refuted or undermined. 22

*Read relevant case law you have read recently but don't remember.

*Remember: Insurers are at least close to being fiduciaries of their insured. This is what it means to say that an insurer has a "special relationship" with an insured, so that the insurer must treat its insured's interests as at least equal to its own. The business of insurance is to take care of insured (within the range of the contract of insurance), to protect them from various problems, and to attend to the risks which injure them. This point applies with special force to liability insurers providing defenses to their insured, although this point is not succinctly written law.

*Is advising liability insurers should look for ambiguities in policies and advise their clients—usually in writing—about possible exposures and consequent dangers. Of course if L for insured is also advising liability insurer, both clients should be aware of any communications.

*Finally, L is working for liability insurer needs to think carefully about how to write denial letters and reservation-of-right letters. 23

*Look for coverage! 24

*Absent indications of dishonesty on the part of the lawyer the carrier should not try to defeat coverage by subtle and energetic means and should encourage his client to avoid the same thing.


23. Michael Sean Quinn, Reserving Rights Rightly: The Romance and the Temptations, 7 COVERAGE 1 (August 1997)


There is something radically wrong with liability carriers not being able to sue the lawyers they retain, direct (at least to some extent), and pay for defending their insured. As already indicated herein (and demonstrated elsewhere), a lawyer defending an insured frequently renders legal services to the liability insurer that hired L to defend insured, and sometimes this happens in the very case where the lawyers are defending insured.

Even if Ls do not provide legal services to the liability insurers that hire them, the following facts can all obtain. (i) The Ls have been paid for rendering legal services, although they have not been paid by their explicit (and perhaps only actual) client but by liability insurer. (ii) Those legal services were defective. (iii) The Ls caused financial injury to the entity that was paying the legal bills. Under these circumstances, it is hard to think of reasons why the actually injured party—liability insurers—should not be able to recover from L (or its professional liability carrier). In fact, there are no good reasons for this gap; there are very good reasons why the gap should be closed or abolished: and there are some elegant ways to do precisely this.

The remainder of this essay will concern that issue. Curiously, even quite recent cases deny that an entity or person that agrees to pay and does pay for legal services rendered to another has no standing to bring a legal malpractice case against the lawyer paid. One person’s paying L to represent a person other than the payor does not establish the existence of an attorney-client relationship between the payor and L, so that the former has no standing to sue L. Only a person seeking and receiving legal advice from an attorney can be involved as a client in an attorney client relationship. Non-engagement agreements do not create the relationship. The case just sketched involved a stepfather who paid for the criminal defense of his stepson. Presumably this same rule would apply to a liability insurer that only paid legal bills, and did not direct the defense and for that reason did not receive legal services and/or advice. What about liability insurer that pays for and directs the defense? Of course, even it may lack standing to sue L for insured and may not be able to attain it.

Y. Routes to Rightness

There are several routes by means of which liability insurers can become the genuine legal owners of their insureds’ rights against the Ls who defend insureds and whose bills for defense of the insureds usually the liability insurers receive and mostly pays. Coming to own these claims is an easy route to standing. Another route to standing would be giving a liability insurer a right of its own which is—in and by its nature—identical to or substantially similar to the right a client has. Here they are: (A-1) L-insurer clienthood, (A-2). Quasi- or pseudo-clienthood, (B) subrogation, (C) assignment, (D) the use of liens, (E) provisions of the RESTATEMENT (THIRD) THE LAW GOVERNING LAWYERS, (F) common law breach contract, and (G) injury inflicted upon an intended third-party beneficiary. Each of these will be discussed.

A. Liability Insurer Clienthood

There is a controversy in relevant legal circles regarding whether a liability insurer providing a defense to an insured is automatically a client of a defense lawyer used. To some extent, the answer to this question hinges on the meaning of the word “provide” in this context, and there are three alternatives. First, liability insurer may provide a defense by paying for it. Second, liability insurer might provide a defense by picking L and then watching. Third, liability insurer might provide a defense by controlling the defense and therefore, at least, having the right to provide orders to L. Fairly obviously, only the third case matters. In the first and second cases, there is no reason to think that liability insurer is a client of L, or anything like a client. It receives no legal services and no legal advice.

So, is L automatically liability insurer’s lawyer if

liability insurer picks L and controls him? After all, L is providing legal services and liability insurer is using them to discharge its contractual obligations to insured. If the answer to this question is affirmative, then there is what the profession is calling a genuinely "tripartite"—"Three Part"—legalistic relationship exists amongst (1) the insured (Id), (2) L for Id, and (3) liability insurer. It is difficult to see why "Tripartitism" is impelled upon the profession, if L provides legal services to Id and provides liability insurer with no legal advice and/or no legal services—i.e. the type of advice and services only lawyers can legally provide. After all, L is not automatically or necessarily rendering legal services to insurer, instead; it is helping liability insurer discharge its insurance services by functioning as a defense lawyer for the insured. In other words, L is providing legal services to the insured and only for the liability insurer. Still, when abstraction is eliminated and the real world is the focal point, defense lawyers often—almost always in larger and more complex cases—render at least some real legal services to liability insurers by providing advice to them about how to conduct a lawsuit brought against an insured, what the settlement value probably is, how to conduct lawsuit settlement negotiations, evaluations of civil trials as they go forward, and how to conduct a trial and an appeal.29 These are all considered real legal services, and they are rendered directly to liability insurer. Of course, liability insurer then uses them to perform its duties as a liability insurer, but it needs legal advice to do this well.30 If L provides liability insurer bad advice—or no advice, when advice is needed and sought—say, as to settlement value, and this act or omission results in a necessary but mistaken judgment, the injury and damages are caused by insurer, assuming that liability insurer would have done significantly better had good legal advice been provided and followed.31

Thus, the third category—liability insurers controlling the defense—really has two forms. One of them is that liability insurer runs the show and is the commander in chief without receiving legal advice from L. The other one is that liability insurer runs the show and is the commander in chief, but receives legal advice from L along the way. An attorney client relationship does not exist in the former case but does exist in the latter case.

This conclusion is sound. Alas, it has not been deployed much as a foundation for liability insurer's standing to sue L for insured for fouling up the defense of an insured. One wonders why not. Of course, it could not always be used. Liability insurers would have to prove that the "foul up" resulted from something with respect to which the lawyer gave advice, whether directly or indirectly.

Nevertheless, there are two obvious reasons for not using the lawyer-client relationship between defense lawyers and defending liability insurers. First, it would drive up legal fees which carriers would have to pay. For one thing, lawyers working for insurers directly usually charge more than insurance defense lawyers. Furthermore, Ls will not work on complex and lengthy cases at cheap rates, if their mistakes are more probable than not to trigger expensive lawsuits in which they will be defendants. Of course, this problem may be avoided to some extent by setting up arbitration agreements between lawyers representing liability insurers and the carrier clients.

Second, the fact that liability insurer and Ls have attorney-client relationships with respect to the legal advice L has provided the carrier does not entail or even imply that this relationship is as broad as the attorney-client relationship between L and the insured. Indeed, it will be much narrower. Many negligent acts and omissions of defense lawyers

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29. In our experience, we have commonly seen directives provided by insurance companies to defense counsel which include reporting requirements, requirements that certain staff members (i.e. paralegals, secretaries) perform certain functions, and strict guidelines on what and how much will be paid for a given activity. Also, insurers will require that defense counsel seek its permission prior to undertaking certain activities in a case, i.e. depositions, hiring an expert witness and the like. In its reporting requirements, many insurers are very specific as to what defense counsel must provide such as, percentage of likelihood of success at trial and/or reasonable settlement amounts. It would seem that this type of information would constitute legal advice in that the insurer is relying upon the attorney's judgment and expertise in making decisions on a particular claim.

30. This is true even when the adjuster is herself a lawyer, as often happens in cases involving legal malpractice insurance or involving D & O insurance.

31. Interestingly, many easier legal malpractice cases involve not just one blunder by the lawyer but a series or an interconnected system of blunders by several.

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would not fall within the temporally guppy, metaphorical pin-points that constitute the areas of attorney-client relationship between L and liability insurer. Consequently, this use of tripartitism will be unreliable and so not entirely helpful, although it might be a little bit helpful occasionally and so should not be written off.

A-2. Quasi- or pseudo-clienthood

Recently, and without meaning to, the Texas Supreme Court made a suggestion which could be used to argue for permitting us all to think about liability insurers defending their insured as something like or something close to clients of the defense lawyers. This suggestion occurred in Unauthorized Practice Law Committee v. American Home Insurance Company a case in which the use of staff counsel or captive law firms was justified for use in many insurance defense cases.32 Justice Hecht writing for the seven judge majority formulated the following three principles for determining whether a corporation using staff counsel to serve someone other than the corporation is itself engaged in the practice of law. Here are the three factors: (1) Whether the corporation interest being served by the rendition of legal services is existing or only prospective; (2) "Whether the [corporation] has a direct, substantial financial interest in the matter for which it provides legal services" and (3) "Whether the [corporation]'s interest is aligned with that of the person to whom the company is providing legal services." When the third factor in particular is satisfied, "for all practical purposes, there is only one client involved."33

If the third principle is understood, then in a variety of insurance defense cases the defense lawyer has only one client, practically speaking, and that one client consists of two parts: the insured and the insurer. According to Justice Hecht, this situation arises when, "a liability insurer and an insured have the same interest defeating a liability claim[]." When this view is understood generally, liability insurers should be able to sue defense lawyers in the vast majority of cases.

As powerful as the logic of this argument is, courts may be unwilling to follow the reasoning, since this was not the explicit intent of the Texas Supreme Court. On the other hand, perhaps Justice Hecht has subtly set forth an invitation for subsequent legal argument.

B. Subrogation

Not every state permits a defending liability insurer to be subrogated to its insured's legal malpractice rights,34 although a number do. Some states are just beginning to consider the issue.35 Primary liability carriers may acquire an insured's right of legal malpractice through subrogation under Texas law.36 Even excess liability insurers can as well,37 although reinsurers probably cannot. Subrogation is not open to liability insurers in all states, however, as already stated.

A Court of Appeals of Indiana, refused to allow an excess carrier to be subrogated in a legal malpractice action.38 Oddly enough, it did this on the grounds that legal rights cannot be assigned. Why "odd"? Subrogation and assignment are not the same things.

In one recent case,39 the Court of Appeals of Ohio rejected equitable subrogation for a defense

32. No. 01-0138 (March 28, 2008).
33. Justice Hecht is quoting from Opinion 343 of the Committee on Interpretation of the Canons of Ethics (1968). This committee was then and is now part of the State Bar of Texas.
36. For a systematic summary of the law of subrogation, see Michael Sean Quinn, Subrogation, Restitution and Indemnity, 74 Tex. L. Rev. 1351 (1996) (an aging account but mostly right). For a recent change in Texas law of subrogation, see Farris Benefit Co. v. Cantu, 2007 WL 1861000 (Tex., June 29, 2007).
37. See also Kuch, Mahin & Cate v. Nat'l Union Fire Ins. Co. of Pbg., Pa., 20 S.W.2d 692 (Tex. 2000).
39. Swiss Reinsurance America Corp. Ins. Co. v. Reitzel, 887 N.E.2d 1215 (Ohio App. 2005). The actual primary carrier in that case was Frontier. It was the second-named plaintiff, and Swiss Re was Frontier's reinsurer.
primary liability carrier finding it would drive a wedge between attorney and client. "Indeed," said the court, "the attorney would be placed in an even more precarious position than is inherent in a tripartite relationship."

The Ohio case presented in the last paragraph was quite different. There, a conflict clearly existed between the insurer and the insured, since the insured wanted the case settled. According to the court, if L had done as the insurer wished, the insured would have sued him, but if he had done as the insured wished, the insurer would have sued him. "To permit such a result would 'substantially impair an attorney's ability to make decisions that require a choice between the best interests of the insurer and the best interests of the insured.'" 40

There is a Texas Supreme Court case which explicitly holds that excess carriers may sue "insurance defense" lawyers under a subrogation theory. 41 There is no reason why that decision would not apply to primary carriers that have had to pay amounts above policy limits. Besides, the advice L provides the primary carrier about whether to pay policy limits to settle a case may make it liability insured's temporary client on a relatively narrow issue. This would even be true if L provided the carrier contradictory advice over time at first saying "Don't pay" but second and later saying "Pay." If the second advice came just before trial or at trial and there was no literature, records, or correspondence to back it up, the insurer would have an excellent claim.

However, subrogation is a good place to start when thinking about liability insurer bringing a malpractice action against defense counsel. If L, through his negligence, injures a liability insured, who is also his client, and injures the relevant liability insurer who that ran the case, paid the bills, and received advice from counsel for liability insured regarding how to conduct the case, then liability insurer is perfectly suited to obtain liability insured's right to sue L. The long existing legal process of subrogation is the way to do this.

Courts occasionally say that the attorney-client relationship is uniquely personal—so personal, in fact, that the client's right cannot move from him to anyone else. The idea is that the relationship is so intimate and needs to be so intimate, that if the right to bring a malpractice action was transferred, a fundamental feature of the attorney client relationship would be destroyed. 42 Several things are wrong with this argument. First, even if it works for assignment, it does not work for subrogation. The latter is much more restrictive than the former. Second, insurance defense cases are often quite different from other kinds of attorney client matters, since usually one case—or one pattern of cases—is involved, and usually they do not involve disclosures which must be kept secret. Third, courts could restrict the disclosures of secrets which are irrelevant to the pending case.

Subrogation has its genuine dangers, however. Since the subrogee steps into the shoes of the subrogor, any defenses which could be asserted against the subrogor can be asserted against the subrogee. Further, if "Gee" and "Gor" are co-plaintiffs, a procedural error by "Gor" which causes the dismissal of its case, can lead to the dismissal of "Gee's" case as well. The same is also true with respect to recovering value if Gor is the only named plaintiff and is running the show. This situation would arise if, for example, Gor was the only named plaintiff and there was a contractual agreement under which Gee would get some of the recovery. This arrangement might involve Gee paying the legal bills. It might even involve Gee running the subro case. In addition, if there will be substantial court or judicial resistance to this approach. Judges who are unsympathetic to insurers will try to find hidden ways to throw out such cases. The more Gee runs a subro case from behind the scenes or from the sidelines, the more likely resistance is. Of course, this is not a legal point but more like a political point. Still it is an influential and important consideration.

C. Assignment

An assignment is a document by which A transfers ownership of an asset to B. Sometimes this asset is A's

40. Id. at ¶[15] & ¶ 33.
41. Cited in the previous note.
42. See id. at 275 (Ariz. 2008) (insurance agent case discussing and distinguishing legal malpractice cases).

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status as a creditor; sometimes it is A's legal rights; sometimes it is an intangible asset the ownership of which is changing hands.\textsuperscript{43} Assignments can be voluntary or involuntary. The latter of these two is often where ownership changes hands by means of a court order of some sort. Not really very interesting. The majority of states that have considered the issue of whether legal malpractice rights can be voluntarily assigned have come down in the negative side of this question. Texas is one of these,\textsuperscript{44} and (unfortunately, in our view) this rule of prohibition is likely to remain. Even though a few other states have rejected rejecting it and has approved assignment,\textsuperscript{45} others have not and have joined the majority in rejecting assignment as a source of legal malpractice rights.\textsuperscript{46}

Under Texas law, legal malpractice rights are not assignable,\textsuperscript{47} but they can move from person to person by other means. They can move (a) through an award from a bankruptcy court,\textsuperscript{48} and therefore presumably (b) through the order of a district court controlling Id's insolvency, and so also they can probably move (c) through subrogation\textsuperscript{49} without any court order.

The following independent reasons have been given for this anti-assignment rule:

1. Permitting assignability would drive an immediate wedge between lawyers and client. (As if there aren't wedges any how!)?\textsuperscript{50}

2. Having a rule permitting assignability would reduce the eminence of the legal system. (One wonders why and how.)\textsuperscript{51}

3. Assignability would destroy the sanctity of the attorney-client relationship. (Why?)\textsuperscript{52}

4. Clients would pull rugs out from under their Is in order to settle cases. (And this would increase lawyer liability? How?)\textsuperscript{53}

5. Assignability would create a commercial market for buying these rights and that would demean the legal profession. (Why is this such a bad thing?)\textsuperscript{54}

\textsuperscript{43} See Assignments. 7 Tex. Jur. 2d 178 (1997). See also Assignments. 6 Am. Jur. 2d 143 (1999).

\textsuperscript{44} Zuniga v. Groce, Locke & Heald, 878 S.W.2d 313 (Tex. App.—San Antonio 1994, writ ref'd). The use of the last phrase in the citation at that time means that the Supreme Court adopted the decision as its own. See Malitos v. Baker, 11 S.W.3d 157 (Tex. 2000) (involving partial assignment to judgment broker).


\textsuperscript{47} Zuniga v. Groce, Locke & Heald, 878 S.W.2d 313 (Tex. App.—San Antonio, 1994, writ ref'd). Given that the Texas Supreme Court refused the writ in this case, a rare event, instead of refusing it explicitly because there was "no reversible error." This decision became a Supreme Court decision. There have been few of these over a long time. The high court itself refers to Zuniga as its case. See Malitos v. Baker, 11 S.W.3d 157, 163 (Tex. 2000).

\textsuperscript{48} Douglas v. Delp, 987 S.W.2d 879, 882 (Tex. 1999).

\textsuperscript{49} This is true even when the plaintiff is an Excess carrier. Am. Centennial Ins. Co. v. Conrail Ins. Co., 843 S.W.2d 480 (Tex. 1992). Subrogation is permissible when assignment is not because assignment endangers the lawyer-client relationship, while subrogation does not. The latter does not impact the structure or level of the attorney-client relationship. The court here was following Atlanta Int'l Ins. Co. v. Bell, 475 N.W.2d 294, 298 (Mich. 1991), which is one of the most influential cases on this matter nationwide.

\textsuperscript{50} One is inclined to doubt this blanket claim. Even when it's true, one cannot be certain that it is a bad idea, for it would encourage lawyer to dispatch written evaluations to clients on a more regular basis.

\textsuperscript{51} Besides, the interests of lawyers are supposed to be subordinate to the interests of clients. Thus clients are in some sense more important, if not more eminent, than lawyers.

\textsuperscript{52} For a comprehensive discussion of the general topic of assignability of legal claims, see Michael Ahmounowicz, On the Assignability of Legal Claims, 114 Yale L. Rev. 697 (2005).

\textsuperscript{53} One doubts that rug pulling would be a safe foundation upon which to build a new case.

\textsuperscript{54} If such a market was created, it would not be a large market. Legal mal cases are just too hard to win.
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D. Creation of Lic

One wonders if there might not be devices somewhat like assignments which could be used, without any of its various apparent “dangers.” The Texas Supreme Court has held that a former client may sue an attorney for malpractice even if the client executed a partial assignment to a person or entity that was financing the suit. A partial assignment which is legally invalid does not destroy the client’s right to file and pursue suit. The client still owns something, namely, a right to pursue a chose in action, which can be the foundation of a lawsuit. If so, isn’t there something somewhat like an assignment which might do the same work?

 Couldn’t the former client of a lawyer—now the plaintiff against him in a legal malpractice case—provide the person or entity financing his claim some sort of lien on what is recovered? One should think he could. After all, plaintiffs’ lawyers can have a lien on a contractually determined amount of any recovery. Under § 1.08(h) of the TEXAS DISCIPLINARY RULES OF PROFESSIONAL CONDUCT a plaintiff’s lawyer (among others) cannot own a property interest in his client’s claim. He or she can have a lien on the recovery, however, and various sorts of people can be notified about this in various sorts of ways. More directly, liens are security devices which can be created by contract, and they apply to specified property. Thus, if X finances malpractice litigation, X could have a lien on the recovery.

Now, consider this question. If a liability insurer financed and conducted the defense of its insured in

55. Presumably the temptation would be to kill a debt, in part, by revealing a secret. Adults can rationally think about this. Thus the foundation of this consideration is a kind of paternalism.

56. Of course, this consideration presupposes that an assigned claim automatically involves some sort of injustice. What ever happened to American liberties, capitalist freedom, and open markets?

57. Maybe, then again, maybe not! Besides if more justice was done and lawyers became more attentive and more disciplined, what would be wrong with that?

58. See Kevin Pennell, Note: On the Assignment of Legal Malpractice Claims: A Contractual Solution to a Contractual Problem, 82 Tex. L. Rev. 481 (2003) (a legal malpractice claim is a form of property and should be freely assignable; however, attorneys should be allowed to limit a prospective client’s right to assign a potential legal malpractice claim, provided the client provides his informed consent.” Id. at 482-83. Thus, “attorneys should be allowed to include anti-assignment provisions in their retainer agreements, assuming that they fully inform the client of the effect of that provision.” Id. at 488. For a bibliography of commentaries, sec 4b, at n.11). See also Michael Scan Quinn, On the Assignability of Legal Malpractice Claims, 37 S. Tex. L. Rev. 1203 (1996) (Quinn rejects Pennell’s view that lawyers should be free to forbid assignment in their retainer agreements with respect to any client, even if they do not explain the “no assignment” provision to them.)


60. Where there is an invalid partial assignment, can the former client sue for all the damages? One would think so if the assignment is invalid.
underlying litigation and then had to pay a judgment because of an error of L, can the insurer file a lien on the insured’s recovery from L in a malpractice suit? The answer should be yes, but it is absolutely predictable that L and his or her insurer will oppose this.

Another trouble with the “Lien Theory” is that, outside established property law, the law of liens is vague, unclear, undeveloped, misunderstood, and unstable. Consequently, enforcing alleged grants of liens depends very much on at least judicial cooperation. Therefore, the “law of liens” is not to be trusted as a way to provide insurers with causes of action against negligent defense lawyers. Besides, by definition in “Lien Theory,” the right of recovery would not be direct.

It’s hard to find much of this kind of enterprise floating around. One wonders why not. Too speculative? Too complicated? Too many uncertainties? Maybe this is not the place to develop the law of liens further. There is also no systematic legal literature on this precise topic, and it is not discussed in the usual encyclopedic sources.51

E. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERING

This next theory is based on § 51(3)(c), cmt. g of the RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS (2000). This section is entitled “Duty of Care to Certain Nonclients,” and its main body plus subsection (3)(c) reads as follows: For the purposes of the elements of legal malpractice and a lawyer’s duty of care, a lawyer owes the usual and recognized duty of care to non-clients under certain circumstances. Here is one of the important situations: Lowes the usual duties of care to a non-client when and to the extent that “the absence of such a duty would make enforcement of [L’s] obligations to the client unlikely.” Comment g begins as follows: A “lawyer designated by an insurer to defend an insured owes a duty of care to the insurer with respect to matters as to which the interests of the insurer, and the insured are not in conflict, whether or not the insurer is held to be a co-client of the lawyer.”62 Notice that this formula works in reverse of the usual strategy. It creates a right to sue for malpractice in something which is not a client.

One of the most interesting cases on the nature of malpractice law to be decided in the last decade is Paradigm Ins. Co. v. Langerman Law Office, PA., decided by the Arizona Supreme Court.63 Paradigm hired Langerman to defend its insured in a medical malpractice case. The doctor insured was the medical director of Samaritan Health Service, also a defendant in the case. Langerman failed to investigate whether the doctor was covered by Samaritan’s liability insurance and did not tender his defense to the other insurer.

During the lawsuit, Paradigm terminated Langerman’s representation of its insured (for reasons unrelated to the claim at issue) and hired another lawyer. The second lawyer discovered that the insured doctor was, in fact, covered by Samaritan’s insurance; Samaritan’s policy was primary to the Paradigm policy; and he therefore tendered the claim and defense to Samaritan’s insurer. Samaritan’s insurer rejected the claim on the grounds that the tender was untimely. Paradigm eventually settled the claim for an amount within its policy limits, acting as the primary carrier, without being able to look to the other insurer for contribution or indemnification.

Langerman presented Paradigm with a statement for legal services. Paradigm refused to pay claiming that Langerman had been negligent both in failing to advise it of the other carrier’s exposure as the primary carrier and by not promptly tendering the defense to the other carrier. A lawsuit between Langerman and Paradigm followed.

The Arizona Supreme Court examined three issues: 1) Whether an express agreement is required to form an attorney-client relationship; 2) whether the attorney can owe a duty of care to the insurer, even if the insurer is not a client; and 3) whether an allegation of attorney malpractice toward a client is necessary to a third person’s claim against the

63. 24 P.3d 593 (Ariz. 2001).
attorney.

The Court, relying on the Restatement, first ruled that an express agreement was not required either to permit Langerman to represent Paradigm or for an attorney-client relationship to have formed between the two. Second, the Court held that in the context of defense counsel hired and paid for by an insurer to represent its insured, absent a conflict, the attorney has two clients—the carrier and the insured. The Court refused to adopt a hard and fast rule with regard to this issue and did not endorse the view that the lawyer automatically represents both the insurer and insured.

The issue of primary importance in the case was whether the lawyer owed a duty to the insurer and whether that duty was breached. The Court rejected the idea that a lawyer's liability to the insurer depended entirely on the existence of an attorney-client relationship. Citing the Restatement, the Court noted that a lawyer may, in certain circumstances, owe a duty to a nonclient. Again, the Court did not adopt a hardline rule. According to the Court, the balancing of various factors is involved, including the extent to which the transaction was intended to affect the plaintiff, the foreseeability of harm to him, the degree of certainty that injury was suffered, and the closeness of the connection between the defendant's conduct and the injuries sustained.

Accordingly, the Court held that a lawyer has a duty and therefore may be liable for negligent breach, to a nonclient under the conditions described and the Restatement. The Court declined to rule on whether Langerman's actions constituted negligence, or a breach of duty, and remanded the case to the trial court for this determination.

F. Breach of Contract

It has been true in Texas for many years, and in other jurisdictions as well, that actions against a lawyer for injurious screw-ups sound in tort, not contract. One well-known Texas treatise is fairly clear on this point: "For most purposes, current Texas law apparently treats legal malpractice claims, even those framed as breach of contract, as tort claims." Thus, although the edges of relevant doctrine are fuzzy, the heart of client versus lawyer litigation seems to be that breach of contract is not available to the client-plaintiff.

Perhaps the argument for this is that breach of contract focuses and is restricted to the breakage of specific promises and explicit commitments. In contrast, the tort of legal malpractice is looser and more wide open. Is this really true? Are there not such things as implied contractual promises? If so why would they not apply to contracts for legal advice or services? Let's see what the major treatise writers say about this.

Similarly, not much is said about the possibility of using breach of contract as a cause of action. This point is true even of the Mallen & Smith legal malpractice treatise. In fact, its § 8.6 begins by saying this: "Few modern actions against attorneys are for breach of a written or express contract." Their reason is interesting: "The prevailing rule is that there is no cause of action for breach of an express contract unless the wrong sued for is breach of a specific promise." In addition, implied promises to do a reasonably good job are difficult to distinguish from negligence actions, and the authors say, "there is no difference between the remedies for the different theories, except that a negligence claim usually is subject to a shorter statute of limitation." Thus the matter is discussed in three short sentences in Volume 1 of a five (5) volume treatise. The discussion is too short to be convincing, and no arguments are really

64. Charles F. Herring, TEXAS LEGAL MALPRACTICE & LAWYER DISCIPLINE, 91 (6th ed. 2007). Immediately after this statement, Herring cites numerous cases. He also cites a very small number of Texas cases saying that contract theory might be used. See Michael Sean Quinn, THE ELEVEN COMMANDMENTS OF PROFESSIONAL RESPONSIBILITY: CALLAWAY'S SPIRITUALITY 128-29 (2004) (discussing legal malpractice and pointing out that contracts between lawyers and clients are presumed to be unfair, and the attorney has burden to prove fairness). See Honeycutt v. Bittlingsley, 992 S.W.2d 570, 582 (Tex. App.—Houston [14th Dist.] 1999, writ denied) citing Archer v. Griffith, 390 S.W.2d 735, 739 (Tex. 1964).
65. Id. at 818. (Emphasis added)
66. Id. at §6.7 at 819-20.
given.

Even the relevant parts of the RESTATEMENT reject this view. Section 55(1) in 1 RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS (2000), entitled “Civil Remedies of a Client Other Than for Malpractice,” unequivocally affirms the use of contract law as a way to sue lawyers. It reads this way: “A lawyer is subject to liability to a client for injury caused by breach of contract in the circumstances and to the extent provided by contract law.” Comment c says this, in part: “A client’s claims for legal malpractice . . . can be considered either as tort claims or as contract claims for breach of implied terms in a client-lawyer agreement.” The “Reporter’s Note” goes on to discuss the idea of “warranty of result,” which is obviously a dramatic remedy possibility. Interestingly, the same text makes it clear that a breach of fiduciary duty could also be treated as a contract action.) Now, ask yourself, “If § 55(1) can be the foundation of legal malpractice claims, what would be wrong with permitting assignments?”

In any case, as already stated, in Texas, and various other jurisdictions, legal malpractice does not constitute a contract action. This is true even though breach of contract is often pleaded by plaintiffs in legal malpractice cases everywhere, and then ignored by the judge, the defendants, and ultimately plaintiff’s counsel herself. Why this is or should be true is extremely difficult to grasp. Lawyers and clients have agreements which must be contracts. Lawyers can sue clients and former clients for breach of contract. This is what it is to sue for unpaid fees. The statute of limitations for contract in Texas anyway is longer for contract than for tort; thus it would be helpful to clients to allow actions for breach of contract. The usual problems of injury to wit: economic and financial loss, are the sorts of thing which are covered in contract cases, to wit: economic and financial loss. Contract actions seldom, if ever, involve the infliction of either bodily injury or property damages, yet this is what most ordinary and historical negligence actions concern. And besides, contract actions often authorize the recovery of attorney’s fees whereas tort actions usually do not. True, tort actions permit the recovery of punitive damages, whereas contract actions do not. Then again, punitive damages in legal malpractice cases are a rarity. Perhaps it is relevant that liability insurers have much less hesitancy about providing defense and indemnity when the actions pleaded are tort actions and not contract actions. In theory, at least, this should ultimately make no difference.

Now, let’s change the discussion slightly. What could be said about a liability insurer suing a lawyer who agreed to provide a defense to an insured and then fouled the whole thing up? Isn’t there an agreement—and hence a contract—involving this. The insurer basically says, “Defend this insured ably. Consult with us. Do what I say, if I say anything. Keep us posted. And I will pay you. If you keep the file and start to work, you have accepted this deal.” If I loses a case which should have been won, or if I loses a case at $10 million when it should have been lost for $5 million but no more, the lawyer has not done what he promised or contracted to do.

What is neat—even elegant—about this idea is that there would be two separate causes of action: the tort of legal malpractice for clients of I, and breach of contract to defend ably in the case of the liability insurer. Of course, liability insurer would still have the tort, when it was the sole relevant client or when it was the direct client.

Our suggestion here, if adopted or even if attempted, creates a whole new opportunity for legal creativity. Lawyers for insurance companies should advise their insurer clients to form written contracts with the defense lawyers the insurers hire to represent their insureds. Everything an insurer might need to establish to be able to bring a pseudomalpractice suit should be agreed to. This would include at least the following:

1. the document is a contract;

2. one of the promisors is a lawyer working as an “insurance defense lawyer,”

3. the other promisor is a liability insurer;

68. See Quinn, at 129 n. 35.
69. The majority opinion for American Home Insurance Company case discussed above both asserts and implies that there are contractual relationships between defending liability carriers and the defense lawyers.
4. the lawyer will form an attorney-client with an insured of the insurer-promisor;

5. the insurer will direct and supervise the defense of the suit;

6. the lawyer will perform the functions of a litigating lawyer for an insured of the insurer contact-party;

7. the lawyer agrees that the interests of the insured (his client to be) and the insurer (his customer to be) are sufficiently aligned to permit this arrangement;

8. it would be appropriate for an insurer in this situation to be able to sue a law firm in this situation for damages resulting from the mistakes of the lawyer which would be—or would have been—actionable by the client, if the client had been damaged by the lawyer's mistake;

9. the law firm consents to such a lawsuit;

10. so long as the suit sounds in contract.

Obviously lots of other components of these types of contracts would also be appropriate, but this may be where to start.

This new cra will also create two more avenues for lawyerly creativity. Lawyers would have to advise insurance defense firm how to react and deal with such proposals from liability insurers. In addition, legal malpractice insurers would have to think through how they wanted to handle this new idea.

Nothing more should be said about this revolutionary idea just now. It's too new. More reflection is required.

G. Third Party Beneficiary

There is another contract theory which is attractive. When a contract between A and B is designed to benefit C, C has legal standing (under at least some circumstances) to enforce the contract as to the intended benefits he, she, or it has not received.\(^7\) Significantly, the third party beneficiary theory was discussed recently in an important case—Minnesota's *McIntosh* case—concerning the law of lawyering.\(^7\)

Fairly obviously, whatever contract there is between Land insurer when L is defending an insurer in an action where a liability insurer is running the show is intended to benefit insured. It is also, however, intended to benefit liability insurers; the litigation is designed to get liability insured out without a finding of liability, and it is designed to minimize the about liability insurers will have to pay the plaintiff on liability insurer's behalf. Of course there are other contracts involved in the tripartite relationship: one running between liability insurer and liability insured and another running between liability insured and L. The second and third contracts need not be relevant here, except that they provide the socio-legal context in which the third-party beneficiary relationship exists.

In the *McIntosh* case, the law firm rendered legal services in a transaction to a firm selling “participation interests” (“PIs”) in loans by means of “Participation Agreements” and “Pledge Agreements” (“2PAs”). The loans had already been obtained for a firm which was to build and run a gambling casino on a Mohawk Indian reservation in Minnesota. Eventually repayment of the loans failed, and the banks that had bought the PIs sued the law firm who had been involved in setting up the sale of the PIs. The major problem was that the firm had advised the entity that was clearly its client that the sale of altered PIs through revised PAs—this time “Pledge Agreements”—could proceed without the consent of National Indian Gaming Commission; the client communicated this to the banks that were buying the PIs, and they elected to close their deals without Commission approval.

There were a number of bankruptcies, so the banks tried to recover from the law firm. The theory the banks tried to deploy was that of third-party

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71. *McIntosh Count Bank v. Durmey & Whitney, LLP*, 745 N.W.2d 538 (Minn. 2008)
beneficiary. The court held that C is a third-party beneficiary contract of a contract between A (Lawyer) and B (Client) as to the rendition of legal services only if C (the third party) is a "direct and intended beneficiary" of the attorney's services.\textsuperscript{72} An earlier Minnesota Supreme Court case had held that this could happen only "when the client's sole purpose was to benefit the third party directly, and the attorney's negligent act caused the beneficiary to suffer a loss." The court did not repeat the sole purpose requirement in the McIntosh case, so—presumably—it has dropped it, although this point is not crystal clear. In McIntosh all the court says is that "in order for a third party to proceed in a legal malpractice action, that party must be a direct and intended beneficiary of the attorney's services."\textsuperscript{73}

"[A] party is a direct beneficiary of a transaction if the transaction has as central purpose an effect on the third party and the effect is intended as a purpose of the transaction."\textsuperscript{74} Indeed, the benefit of the third party must be "at the heart of the contract."\textsuperscript{75} In addition "the attorney must be aware of the client's intent to benefit the third party in order for the exception to be applicable. Such a requirement is in keeping with the fiduciary and ethical duties attorneys owe their clients." On the basis of these principles, the Court held that the banks did not have standing.

One would think that exactly the opposite would be true with respect to L's fouling up the defense of his client, a liability insured, and thereby injuring the liability insurer of his client. Presumably, the liability insurer will have hired L to defend its liability insured, and it intends to benefit both liability insured and itself. If the insured accepts L, there will be a contract between L and the policyholder-defendant. This complex is a transaction of sorts. Insurance defense lawyers will know all this. Of course, L's being hired to defend Id is not for the sole benefit of liability insurer, and both L and liability insurer will know this, but McIntosh does not require this, although some earlier cases did. Thus a third party beneficiary theory might help liability insurers sue defense counsel.

It contains certain problems, however, which tend to make simple breach of the L-Id contract by L a better route for the insurer to use in pursuing damages from L. First, historically most third party beneficiary cases have arisen in transactions which did not connect immediately to litigation. Second, under at least some circumstances, a third beneficiary may enforce a contract to which it is not actually a party. Now, does this principle ever apply to the liability insuring enforcing a contract between defense lawyers and liability insured?\textsuperscript{76} If it the principle does apply, and the liability insurer is regarded as a third party beneficiary, and can enforce the L-Id contract, then—quite obviously—it could the contract between L and Id (the insured). But this leads to an odd situation. If Id cannot base its malpractice case on the contract involving it and L, then perhaps the insurer should not be able to do that either. (Clearly, of course, Id cannot base its malpractice suit against L based upon whatever contract there is between L and its liability insurer). Third, in third party beneficiary situations A and B often form the contract precisely for the benefit of C. That does not happen when liability insurer hires a defense lawyer for its liability insured. The sued insured usually does not itself hire L, although this can occasionally happen, and the liability insurer is not hiring L precisely and primarily for its own benefit, although that might be involved. Fourth, at least one of the justifications of the doctrine of third-party beneficiary is that the contract does not fit in the contract. Historically, the law articulating the rights of third party beneficiaries conceptualized the actual promisee to the relevant contract as the legal agent for the third party beneficiary. That does not work here, since—under most circumstances—it is the third party beneficiary (the liability insurer) who hires L for the promisee (the liability insured). Fifth and finally, usually in the paradigm under discussion, there is not a separate, additional contract between the third party beneficiary (the liability insurer) and

\textsuperscript{72} Id. at 547.

\textsuperscript{73} Not every state requires intention. See 13 Williston at 10-11.

\textsuperscript{74} McIntosh County Bank supra n. 72 at 547.

\textsuperscript{75} Id., citing Glazer v. Shepard, 135 N.E. 275, 275-76 (N.Y. 1922) (Carroll, J.)

\textsuperscript{76} 13 Williston at 18-19.

\textsuperscript{77} Id at 12.
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the promisor (L) for the latter to serve the explicit promisee (the liability insured).

Thus, we hypothesize that the third party beneficiary theory works in abstract theory, but will have lots of problems in the practical world of litigation. The use of a straight breach of liability insurer-L contract is a much better practical approach, since it is so straight-forward, although something-like revolutionary. We do not argue that the third party beneficiary theory should not be tried. We only suggest that it not be counted on.

Conclusion

We close this essay by posing and then contemplating a hypothetical and asking a question. A man suffering from a deadly disease is treated for it at a doctor's clinic. A mistake is made by the nurse delivering the medication, and the man dies on the spot. His estate and his family sue: the doctor, the nurse, and the corporate entity employing them both. Everyone involved in or who reflects upon the defense case comes to believe that this case is a defense loser, indeed, an extremely dangerous one. The doctor was inattentive to clinical supervision; the nurse was ill-trained; and the entity was an administrative nightmare. Everyone on the defense side also believed that the case against the corporate entity is more serious than the one against the doctor.

The case against the doctor is settled, but the one against the corporation is not. This happened even though the field adjuster saw disaster coming and tried tactfully to inform his administrative and decision-making superiors. Interestingly, neither defense counsel—not the one for the doctor and not the one for the entity and the nurse—told the insurer that the whole case needed to be settled, although both believed this proposition to be true. There were several opportunities to settle within policy limits, and an appropriate "Stowers Demand" was timely delivered.78

None of the lawyers involved ever advised the insurer that the case would be lost "big-time" and should be settled for policy limits, if no lower number was possible. This happened even though there was a controversy in one of the firms about what should be done. One of the associates helping on the case wrote a strong memo arguing that precisely this advice should be given and that it was a legal error for a lawyer not to give it.

The medical malpractice case against the entity was tried. Hardly any affirmative defense was attempted, and the argument given by the defense was that it was the doctor's fault and not that of the nurse or the entity, even though the entity employed not only the nurse but the doctor as well. The nurse dropped dead in the ladies' restroom at the end of the defense lawyer's closing argument. The jury returned a large— multimillion-dollar verdict against the entity, including punitive damages; judgment was entered upon it; the judgment was affirmed. There was no verdict rendered against the nurse, since she died dramatically and—of course—the doctor herself was gone from the case.

The trial-verdict-and-judgment were highly publicized. The doctor lost his patients. Her practice closed. She was treated for depression. Her husband divorced her and got custody of the children. She changed back to her maiden name, moved, and joined a gigantic multi-doctor practice as a "minor player," who seldom actually saw patients in person.

During the late parts of the appellate process, the doctor and the entity assigned any causes of action they might have against the insurer to the plaintiffs—the decedent's estate and his many children. They did not assign their causes of action for legal malpractice against the lawyers that represented them, but they and their assignors created a lien against all proceeds recovered in Plaintiffs v. Insurer until all their litigation expenses were paid and then a specified sum ($X.00) from all recoveries went to the plaintiffs in the underlying case:

Thereafter, suit was filed. It included causes of action against the lawyers for malpractice and breach of fiduciary duties, and it included causes of action against the insurer for breach of contract and both statutory and common law bad faith. This happened three years after the entry of judgment in the underlying case.

There are lots of issues here, but focus contemplation on just a few of them just now. Could the insurer sue the lawyers it hired to defend its insured, by means of cross-claims? Would there be any

78. Remember—what "Stowers" means.
statute of limitations problems? Could the insurer seek indemnity of some sort from the lawyers? What would the lawyers' defenses be? Would it be malpractice for the insurer's lawyer to fail to recommend that these cross-actions be filed?

Now comes the big question of drama and justice. Doesn't justice require that the insurer have causes of action against the lawyers under circumstances like this one?
Ethics in Settlement Negotiations

Chapter 22

SECTION OF LITIGATION
American Bar Association

ETHICAL GUIDELINES FOR SETTLEMENT NEGOTIATIONS

August 2002
ETHICAL GUIDELINES FOR
SETTLEMENT NEGOTIATIONS

Section 2 Settlement Negotiations Generally

2.1 The Purpose of Settlement Negotiations

The purpose of settlement negotiations is to arrive at agreements satisfactory to those whom a lawyer represents and consistent with law and relevant rules of professional responsibility. During settlement negotiations and in concluding a settlement, a lawyer is the client’s representative and fiduciary, and should act in the client’s best interest and in furtherance of the client’s lawful goals.

2.2 Duty of Competence

A lawyer must provide a client with competent representation in negotiating a settlement.

2.3 Duty of Fair-Dealing

A lawyer’s conduct in negotiating a settlement should be characterized by honor and fair-dealing.

3.1.3 Consultation Respecting Means of Negotiating Settlement

A lawyer must reasonably consult with the client respecting the means of negotiation of settlement, including whether and how to present or request specific terms. The lawyer should pursue settlement discussions with a measure of diligence corresponding with the client’s goals. The degree of independence with which the lawyer pursues the negotiation process should reflect the client’s wishes, as expressed after the lawyer’s discussion with the client.

3.3.2 Client Directions Contrary to Ethical or Legal Rules

If a client directs the lawyer to act, in the context of settlement negotiations or in concluding a settlement, in a manner the lawyer reasonably believes is contrary to the attorney’s ethical obligations or applicable law, the lawyer should counsel the client to pursue a different and lawful course of conduct. If a mutually agreeable and proper course of action does not arise from the consultation, the lawyer should determine whether withdrawal from representing the client is mandatory or discretionary, and should consider whether the circumstances activate ethical obligations in addition to withdrawal, such as disclosure obligations to a tribunal or to higher
decision-making authorities in an organization.

3.5 Multiple Clients Represented by the Same Counsel

A lawyer who represents two or more clients shall not counsel the clients about the possibility of settlement or negotiate a settlement on their behalf if the representation of one client may be materially limited by the lawyer’s responsibilities to another client, unless the lawyer reasonably believes the lawyer will be able to provide competent and diligent representation to each affected client, the representation is not prohibited by law and does not involve assertion of a claim by one client against another, and each client gives informed consent in writing.

3.7 Clients With Insured Claims/Dealing with Insurers

The ordinary principles governing an attorney’s obligations in connection with settlements apply to clients covered by insurance. The insured may be the sole client even though the insurance contract obligates the insurer to pay the attorney’s fees and to indemnify the insured. The insurer may or may not also be the client depending upon applicable law, the contract, and the facts of the particular case. If both the insured and the insurer are the lawyer’s clients, the lawyer should be governed by the rules respecting representation of multiple clients.

Committee Notes: Insurance contracts provide for a broad range of possible arrangements by which one or the other of an insurer and insured select the counsel who will represent the insured and be paid by the insurer. See, e.g., N.Y. State Urban Dev. Corp. v. VSL Corp., 738 F.2d 61 (2d Cir. 1984) (insurer may participate in selection of the insured’s independent counsel); San Diego Navy Federal Credit Union v. Cumis Ins. Soc’y, Inc., 208 Cal. Rptr. 494 (Cal. App. 4 Dist. 1984) (consent to insurer’s choice of counsel deemed withdrawn when insured retained independent counsel); Nandorf, Inc. v. CNA Ins. Cos., 479 N.E.2d 988 (Ill. App.1 Dist. 1985) (insurer obliged to pay for separate counsel for insured). In all of these contexts, the insured is the client, and the lawyer’s duty is to the insured without regard to the insurer’s payment of legal fees or past relationship with the lawyer. See Model Rule 1.8(f) (lawyer cannot accept compensation from anyone other than the client unless the client gives informed consent and the compensation arrangement does not interfere with the lawyer’s independence or the client-lawyer relationship); Model Rule 5.4(c) (lawyer “shall not permit a person who . . . pays the lawyer to render legal services to another to direct or regulate the lawyer’s professional judgment”); Model Rule 1.7, comment 13 (“A lawyer may be paid from a source other than the client, . . . if the client is informed of that fact and consents and the arrangement does not compromise the lawyer’s duty of loyalty or
independent judgment to the client.”) ("when an insurer and its insured have conflicting interests on a matter arising from a liability insurance agreement and the insurer is required to provide special counsel for the insured, the arrangement should assure the special counsel’s professional independence"). This duty of loyalty extends to all aspects of a lawyer’s duties relating to settlement. In some jurisdictions, the law treats the attorney as representing both the insurance carrier and the insured. Such multiple representation is ethically permitted in appropriate circumstances. See, e.g., ABA Formal Op. 96-403 (1996), at 2, 3 (1996) ("Provided there is appropriate disclosure, consultation and consent, any of these arrangements would be permissible. . . "). cf. Silver & Syverud, The Professional Responsibilities of Insurance Defense Lawyers, 45 Duke L.J. 255 (1995). See also Model Rule 1.7(b)(2). The determination whether only the insured or both insured and insurer (as co-clients) have entered into a client-lawyer relationship with the designated lawyer must be made based on the facts of the particular case and applicable law. See Restatement §§ 14 and 134 (formulation of the attorney-client relationship and the status of insureds and insurers). When the lawyer is formally representing both insured and insurer, the lawyer’s obligations in the settlement context are governed by the rules respecting multiple client representation. See Model Rule 1.7(b)(2). In defending and settling a dispute in which the defendant has insurance coverage, the financial and other interests of the insurance carrier and those of the insured will often diverge. The insured’s economic interests may focus on the deductible rather than the full amount claimed (particularly if future premiums are not expected to be heavily experience-rated) and may often be supplanted by non-economic interests if it appears that the deductible will be lost and the insured’s funds consequently no longer seem at risk. By contrast, the insurer’s economic interests may correspond only with its own different range of coverage, and insurers typically have little or no interest in non-economic considerations. When such divergences arise in the context of the lawyer’s representation of both the insured and the insurer, the attorney is obliged to advance the interests of the insured, and to inform the insurer that the attorney is treating the insured’s interests as paramount. See ABA Formal Op. 96-403 (1996), at 5-6 (1996) (dispute between insurer and counsel over settlement may require lawyer’s withdrawal; thereafter former-client conflicts rule may preclude lawyer from assisting insurer in reaching a settlement objected to by the insured). Insured clients, acting under contractual obligations or otherwise, often authorize the lawyer to consult with or take direction from the insurer concerning settlement. Some insurance contracts require the insured to delegate to the insurer the right to settle claims. Cf. Rogers v. Robson, Masters, Ryan, Brummund & Belom, 407 N.E.2d 47 (Ill. 1980). The lawyer’s representation of the insured often may include consultation with the client about the client’s obligations under the insurance contract and the ramifications of failing to comply with the requirements of that contract. Irrespective of the scope of delegation by the insured, however, the insured remains a client, and the lawyer may need to consult with and obtain authorization from the insured before finalizing settlement of a claim.
Section 4 Issues Relating To A Lawyer’s Negotiations With Opposing Parties

4.1 Representations and Omissions

4.1.1 False Statements of Material Fact

In the course of negotiating or concluding a settlement, a lawyer must not knowingly make a false statement of material fact (or law) to a third person.

Committee Notes: A lawyer is required to be truthful when dealing with others on a client’s behalf. Unethical false statements of fact or law may occur in at least three ways: (1) a lawyer knowingly and affirmatively stating a falsehood or making a partially true but misleading statement that is equivalent to an affirmative false statement; (2) a lawyer incorporating or affirming the statement of another that the lawyer knows to be false; and (3) in certain limited circumstances, a lawyer remaining silent or failing to disclose a material fact to a third person. This section addresses the first two of these situations; the next section deals with silence and nondisclosure.

4.1.2 Silence, Omission, and the Duty to Disclose Material Facts

In the course of negotiating or concluding a settlement, a lawyer must disclose a material fact to a third person when doing so is necessary to avoid assisting a criminal or fraudulent act by a client, unless such disclosure is prohibited by the ethical duty of confidentiality.

4.2.3 Agreements Not To Report Opposing Counsel’s Misconduct

A lawyer must not agree to refrain from reporting opposing counsel’s misconduct as a condition of a settlement in contravention of the lawyer’s reporting obligation under the applicable ethics rules.

4.3 Fairness Issues

4.3.1 Bad Faith in the Settlement Process

An attorney may not employ the settlement process in bad faith.

Committee Notes: It is axiomatic that lawyers may not use the settlement process in bad faith. Ethics rules, procedural rules and statutes forbid the bad faith use of the litigation process. It is not bad faith for a party to refuse to engage in settlement discussions or to refuse to settle.