Ethical Considerations for Defense Counsel, The Client and The Insurance Client in the Tripartite Relationship

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The majority of liability cases are defended by insurers on behalf of their insureds. When an insured tenders its defense of a liability case and the insurer agrees to provide a defense, whether unconditionally or under a reservation of rights, three parties are involved: (1) the insurer, (2) the insured, and (3) the defense lawyer. This is known as the tripartite relationship.

There has been much written about the ethical issues that arise when the insurer retains defense counsel to represent the insured, particularly when the defense is provided under a reservation of rights. While some commentators have opined that there is (almost) always a conflict of interest in light of defense counsel’s ongoing financial relationship with the insurer, there should be no question that the insurer and the insured share the common interests of effectively defending, defeating, or at least deflating, the claims made against the insured. Nonetheless, conflicts may arise during the defense of the case and there are not always easy answers in resolving these issues. This paper will discuss some of the most common ethical issues that can arise for defense counsel, the insured and the insurer in the defense of liability cases under the tripartite relationship.

Who is the client?

The traditional approach and the majority view adopted by most states is that defense counsel appointed by the insurer has two clients: the insured and the insurer. A few jurisdictions consider the insured the “primary client,” which suggests that defense counsel has a lesser obligation to the insurer. A minority of jurisdictions hold that the insured is defense counsel’s only client. Notably, the ABA Model Rules of Professional Conduct provide little guidance and ABA ethics opinions have declined to take any position as to the identity of the client in the tripartite relationship. Even if the insured is not treated as defense counsel’s only or primary client, it is important for counsel not to take any action in the defense of the case that could harm the insured. There are a variety of situations in which conflicts can arise, but they can be broken down into four main categories: (1) the control of the defense; (2) reporting information that could be detrimental to coverage; (3) the cost of the defense; and (4) control of settlement.

1 One commentator described the relationship as “deeply and unavoidably vexing.” Charles Silver, Does Insurance Defense Counsel Represent the Company or the Insured?, 72 Tex. L. Rev. 1583, 1587 (1994). And the Mississippi Supreme Court famously observed that “the ethical dilemma thus imposed upon the carrier-employed defense attorney would tax Socrates.” Hartford Acci. & Indem. Co. v. Foster, 528 So. 2d 255, 273 (Miss. 1988).


3 See, e.g., Paradigm Ins. Co. v. Langerman Law Offices, P.A., 24 P.3d 593, 598 (Ariz. 2001) (“In the unique situation in which the lawyer actually represents two clients, he must give primary allegiance to one (the insured) to whom the other (the insurer) owes a duty of providing not only protection, but of doing so fairly and in good faith”).

4 See Safeway Managing General Agency, Inc. v. Clark & Gamble, 985 S.W.2d 166, 168 (Tex. App.-San Antonio 1998) (no attorney-client relationship exists between an insurance carrier and the attorney it hired to defend one of the carrier’s insureds); In Re Rules of Professional Conduct and Insurer Imposed Billing Rules and Procedures, 2 P.3d 806, 814 (Mont.2000) (“We hold that under the Rules of Professional Conduct, the insured is the sole client of defense counsel.”); Atlanta Int’l Ins. Co. v. Bell, 475 N.W.2d 294, 297 (Mich.1991) (“the relationship between the insurer and the retained defense counsel . . . [is] less than a client-attorney relationship”); Metropolitan Life Ins. Co. v. Aetna Cas. & Sur. Cor., 730 A.2d 51, 65 (Conn.1999) (“we have long held that even when an insurer retains an attorney in order to defend a suit against an insured, the attorney’s only allegiance is to the client, the insured.”).

5 ABA Standing Comm. on Ethics & Prof’l Responsibility, Formal Op. 96-403 at 2 (1996) (refusing “to enter the debate as to whom the lawyer represents” in the tripartite relationship).
Who controls the defense?

With few exceptions, almost every liability insurance policy gives the insurance company the right to control the defense of the case. In most situations, this does not present a problem, as it will be generally be in the common interest of both the insured and the insurer to successfully defeat or limit the claims presented against the insured. But what happens if the insurer is providing a defense under a reservation of rights? Many jurisdictions have held that the insured is entitled to retain “independent counsel” (at the expense of the insurer) to protect its interests when the insurer issues a reservation of rights, as there is a conflict between the interests of the insurer and the insured. But even if the insured has independent counsel (whether at its own expense or at the expense of the insurer), defense counsel retained by the insurer may still be confronted with a situation where some action taken in defense of the case could impact coverage under the policy and the defense provided to the insured.

The general rule is that the insurer must defend the entire lawsuit if at least one claim pled against the insured triggers coverage under the policy. Situations may arise in which a dispositive motion could eliminate the covered claim, in which case the insurer might withdraw the defense. While defense counsel should not provide advice regarding coverage issues, counsel may be aware that the insurer is providing a defense based on only one count of a multi-count complaint. In that case, should defense counsel even report that the potential for filing such a motion exists? Yet, counsel has a duty to keep the insurer informed of the defense of the case, particularly in those jurisdictions in which the insurer is a dual client. The safest course of action is to include the possibility of filing dispositive motions when reporting on the defense of the case, without commenting on any potential coverage issues. If the insured/client asks counsel whether such a motion could impact coverage, counsel should respond that they cannot comment on coverage or address coverage issues. Likewise, counsel should not engage in any discussion with the insurer regarding coverage. The situation becomes even more complicated if counsel is asked whether he or she recommends filing the motion.

There are no easy answers, nor is there clear guidance from the case law or rules of professional conduct. We recommend that defense counsel follow best practices to minimize potential conflicts. We think it is prudent for defense counsel to identify the potential coverage issue(s), advise the clients to seek counsel on any perceived coverage issues and not advise either client regarding those issues. As the coverage issues unfold, defense counsel should not only continue proper joint communications, but should also seek and obtain the consent and direction of both clients regarding defense actions to be taken. At times, this could require withdrawal if the carrier persists in directing a course of action (which it may be entitled to take under its contract) to avoid coverage. Defense counsel should not undertake any action in the defense of the case that they have been directed by the insurer to pursue if the insured objects.

Reporting information that could be detrimental to coverage?

Defense counsel has a duty to disclose to the insurer all information concerning the action relevant to the underlying lawsuit, and to timely inform and consult with the insurer on all matters relating to the action. A related issue can arise when the defense lawyer learns of confidential information that might impact coverage or the defense provided to the insured. As the Minnesota Supreme Court observed:

[Defense counsel and the insurer inevitably share information about claims. With defense counsel and the insurer in frequent contact over the details of the

6 For example, the standard Commercial General Liability (CGL) coverage form provides that the insurer has both the “right” and “duty” to defend any suit against the insured seeking damages within the policy’s coverage. See, e.g., Rx.com Inc. v. Hartford Fire Ins. Co., 426 F. Supp. 2d 540, 559 (S.D. Tex. 2006) (applying Texas law) (stating “an insurer’s ‘right to defend’ a lawsuit encompasses the authority to select the attorney who will defend that claim and to make other decisions that would normally be vested in the insured as the named party in the case”).

7 The leading case is the well-known Cumis decision in California, later adopted by California Civil Code §2860 (1996), which provides that a conflict of interest creates a duty for the carrier to provide independent counsel, unless the policyholder waives the right in writing. See San Diego Navy Federal Credit Union v. Cumis Ins. Society, 162 Cal.App. 3d 358, 208 Cal.Rptr. 494 (1984). Other jurisdictions follow variations of this rule. See, e.g., Travelers Indem. Co. of Ill. v. Royal Oak Enters., Inc., 344 F. Supp. 2d 1358, 1372 (M.D. Fla. 2004); aff’d, 171 Fed. Appx. 831 (11th Cir. 2006) (applying Florida law) (recognizing a sufficient conflict of interest warrants the “insurer’s retention of its own counsel at the expense of the insurer”). But when there is no conflict of interest, the insurer generally retains the right to select counsel and the policyholder may retain its own counsel but at its own expense. See Twin City Fire Ins. Co. v. Ben Arnold-Sunbelt Beverage Co. of S.C., 433 F.3d 365 (4th Cir. 2005) (applying South Carolina law) (holding where no conflict of interest exists and the policyholder does not consent to counsel chosen by the insurer, the policyholder can employ another counsel at its own cost).


9 Many of the decisions allowing (or articles advocating) the insured’s right to insist on independent counsel seem to suggest (or at least imply) that insurance defense counsel will not always act in the best interests of the insured when forced to choose between the interests of the insured and the interests of the insurer, who might be a significant source of repeat business. See United States Fidelity & Guaranty Co. v. Louis A. Roser Co., 585 F.2d 932, 938 (8th Cir. 1978) (requiring independent counsel due to the fear that counsel retained by the insurer “would be inclined, albeit acting in good faith, to bend his efforts, however unconsciously, toward establishing that any recovery by [plaintiff] would be grounded on the theory of [the] claim which was not covered by the policy”). Other courts have rejected this view (and implicit criticism) of the ethics of defense counsel. See Twin City Fire Ins. Co. v. Ben Arnold-Sunbelt Bev. Co. of S.C., LP, 433 F.3d 365, 373 (4th Cir. 2005) (applying South Carolina law) (disagreeing that “the Supreme Court of South Carolina would profess so little regard for the principles of professional ethics that it would allow a defense counsel to take actions to be taken if the insured were to retain independent counsel”).

10 Some courts have held that the insured is entitled to independent counsel at the insurer’s expense when a dispute arises regarding defense strategy. See 69th Street and 2nd Ave. Garage Associates, L.P. v. Ticor Title Guarantee Co., 622 N.Y.S.2d 13, 14 (App. Div., 1st Dept.), appeal denied, 661 N.E.2d 999 (N.Y. 1995) (policyholder was entitled to counsel of its own choosing where the policyholder and the insurer disagreed on defense strategy, and insurer’s proposed course of action could result in severe adverse consequences to the policyholder). But compare Roussos v. Allstate Insurance Co., 665 A.2d 40, 44 (Md. Ct. Spec. App.), cert. denied, 683 A.2d 73 (Md. 1995) (refusing “to extend an insurer’s duty to provide independent counsel to a situation where the insured merely disagrees with the manner in which he or she is being defended”).
litigation, the insurer has ample opportunity to inform defense counsel how different approaches to the claim might affect its interests. When the interests of the insurer differ from those of the insured, defense counsel who represents both may find itself in what we have called “an exceedingly awkward position.”

Most courts hold that defense counsel cannot communicate information detrimental to the insured to the insurance company. In that situation, defense counsel’s safest course of action is to obtain the informed consent of the insured client before sharing any facts which may jeopardize coverage. If a coverage-jeopardizing fact is material to the case, counsel should advise the client to seek advice from coverage counsel before taking any action.

Comment [g] to Section 51 of the Restatement of Law Governing Lawyers states:

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…however, such a duty does not arise when it would significantly impair, in the circumstances of the representation, the lawyer’s performance of obligations to the insured.

In some instances, the insurer will “split” the file, with one adjuster assigned to the defense and one to coverage. There will be times when the “defense adjuster” will learn of facts that cannot be shared with the “coverage adjuster.” Because there are no clear rules regarding “splitting files” and not all insurers follow the practice, defense counsel should be clear as to the role of the claims professional to whom he or she is reporting.

The cost of the defense and defense strategy

Beyond the question of whether to file a dispositive motion that might eliminate coverage, conflicts can also arise regarding whether to pursue certain defense strategies. For example, the insurer and the insured might disagree about whether to retain certain experts or pursue particular lines of discovery. Billing guidelines can also present similar challenges. The insured will want the best defense possible, and may feel that the effectiveness of the defense is compromised by billing guidelines or the insurer’s (understandable) desire to control defense costs. Situations do arise in which the insured becomes dissatisfied with defense counsel’s lack of preparation for trial (or proposed trial strategy), and uses its own attorneys to ensure an adequate defense.

Rule 2.1 of the Model Rules of Professional Conduct states that “[i]n representing a client, a lawyer shall exercise independent professional judgment and render candid advice.” A conflict most commonly occurs when defense counsel makes a recommendation to the insurer regarding a proposed plan of action, which the insurer refuses to approve. Where the recommended strategy or action is critical to the defense and defense counsel believes the insured would be harmed by failing to perform that act, a conflict of interest can arise. This is most critical in cases where there is potential for excess exposure.

The American Bar Association’s Formal Opinion 01-421, Ethical Obligations of a Lawyer Working Under Insurance Company Guidelines and Other Restrictions, would require defense counsel to first ask the insurer to reconsider the refusal. If the insurer stands firm in its rejection of the suggested course of action, defense counsel must then inform the insured of his/her recommendation and the insurer’s refusal. Counsel can then seek the insured’s consent to proceed as directed by the insurer. This would necessarily require a discussion of the risks and benefits of each proposed course of action. If the insured does not consent, the ABA recommends defense counsel withdraw from the matter as he/she cannot adequately represent the interests of both parties.

Effective communication is the best way for all involved to work through any potential conflicts. Defense counsel should be mindful to keep the insured and the insurer informed of any proposed strategy or action regarding a proposed plan of action, which the insurer refuses to approve. Where the recommended strategy or action is critical to the defense and defense counsel believes the insured would be harmed by failing to perform that act, a conflict of interest can arise. This is most critical in cases where there is potential for excess exposure.

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The Montana Supreme Court has held that any requirement of prior approval impermissibly interferes with a lawyer’s obligation to exercise independent judgment on behalf of the policyholder. See In Re Rules of Professional Conduct and Insurer Imposed Billing Rules and Procedures, 2 P.3d at 814-15.

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informed of defense strategy and developments in the defense of the case. If a dispute arises regarding strategy, it is reasonable for defense counsel to provide their professional advice and recommendations, and counsel should not let the cost of the defense determine their proposed strategy – with the understanding that it is certainly reasonable to provide a budget. It should also be noted that with some liability policies, the available liability limits will be reduced by defense costs, and this can become another consideration in determining defense strategy.

Who controls settlement?

For defense counsel, this should be easy. Defense counsel does not decide when to settle or how much to pay, they simply evaluate the claims presented and make recommendations. Counsel should promptly report all settlement offers and keep the insurer and the insured advised regarding settlement negotiations. If a dispute arises regarding whether to settle, the defense lawyer does not make the call. But who does?

Rule 1.2 of the Model Rules of Professional Conduct states that “[a] lawyer shall abide by a client’s decision whether to accept an offer of settlement of a matter.” As discussed above, most jurisdictions consider the insurer to be defense counsel’s client, along with the insured, in the tripartite relationship. Most liability insurance policies allow the insurer to settle without the insured’s consent, and there is a large body of law regarding the insurer’s liability to the insured if it acts unreasonably or in bad faith in rejecting an offer to settle. These rules will govern most situations, and defense counsel should be careful to stay out of any dispute between the insured and insurer regarding settlement. For example, if the insured wants to demand that the insurer accept a settlement offer, defense counsel should not be involved in those discussions beyond communicating the insured’s request (after advising the insured that it should communicate directly with the insurer or through their respective coverage counsel).

The Restatement of the Law of Liability Insurance – A Reimagining of the Tripartite Relationship

In May 2018, The American Law Institute membership approved the final draft of the Restatement of the Law of Liability Insurance (“RLLI”). The RLLI has been the subject of much criticism in the insurance industry, including objections from a number of state insurance regulators. Much of this criticism has focused on the RLLI’s adoption of minority or entirely new principles of law, so that it is not a “restatement” of settled common law. Among its many departures from settled law, the RLLI adopts new principles regarding the tripartite relationship.

First, Section 11 of the RLLI provides that the insurer “does not have the right to receive any information of the insured that is protected by attorney–client privilege, work-product immunity, or a defense lawyer’s duty of confidentiality under rules of professional conduct, if that information could be used to benefit the insurer at the expense of the insured.” In effect, defense counsel would be required to hide information from the insurer if it could harm the insured. As discussed above, the situation is already complicated enough for defense counsel. Moreover, these issues are governed by professional rules of ethics and, in some states, decisions by the courts.

Second, Section 12 provides that the insurer may be held liable for the conduct of defense counsel retained to represent the insured, as well as “negligent selection of defense counsel.” Section 12 provides:

§ 12. Liability of Insurer for Conduct of Defense

(1) If an insurer undertakes to select counsel to defend a legal action against the insured and fails to take reasonable care in so doing, the insurer is subject to liability for the harm caused by any subsequent negligent act or omission of the selected counsel that is within the scope of the risk that made the selection of counsel unreasonable.

(2) An insurer is subject to liability for the harm caused by the negligent act or omission of counsel provided by the insurer to defend a legal action when the insurer directs the conduct of the counsel with respect to the negligent act or omission in a manner that overrides the duty of the counsel to exercise independent professional judgment.

While a number of jurisdictions have considered whether insurers may be held liable for the conduct of defense counsel, the issue is far from settled. Many jurisdictions have explicitly rejected claims that the insurer could be vicariously liable for the conduct of defense counsel, reasoning that the insurer does not have the right to actually pass a statute specifically to prevent the adoption of the RLLI, providing that the RLLI “does not constitute the public policy of this state and is not an appropriate subject of notice.” Ohio Rev. Code § 3901.82.

21 See Remodeling Dimensions, Inc. v. Integrity Mut. Ins. Co., 819 N.W.2d 602, 615 (Minn. 2012) (“The question of whether an attorney appointed to represent an insured to defend a claim is an agent for the insurer is one that has divided courts, and often turns on specific facts.”).
control the attorney’s professional judgment. Other courts have held that the insurer may be held liable if it expressly directs the conduct of defense counsel. The new approach under the RLLI would create liability on the part of the insurer if it negligently selects defense counsel to protect the insured. This goes beyond situations where the insurer oversteps its role in the defense of the case and is likely to create a great deal of conflict between the insurer and insured over the selection of defense counsel.

One can imagine the insured citing the RLLI and asserting that the insurer’s preferred attorney is not properly qualified to defend the case. While some policyholders negotiate the right to select defense counsel, such a right is not present in every contract of insurance. And what happens when there is a bad outcome and the insured claims, in hindsight, that the insurer was negligent in the selection of defense counsel?

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22 See, e.g., Ingersoll-Rand Equip. Corp. v. Transp. Ins. Co., 963 F. Supp. 452, 454 (M.D. Pa. 1997) (an attorney’s ethical obligations to the insured “prevent the insurer from exercising the degree of control necessary to justify the imposition of vicarious liability”); Lifestar Response of Ala., Inc. v. Admiral Ins. Co., 17 So. 3d 200, 214-18 (Ala. 2009) (insurer not vicariously liable for defense attorney’s negligence because insurer did not have the right to control the attorney’s professional judgment); Feliberty v. Damon, 72 N.Y.2d 112, 527 N.E.2d 261, 265, 531 N.Y.S.2d 778 (N.Y. 1988) (“The insurer is precluded from interference with counsel’s independent professional judgments in the conduct of the litigation on behalf of its client.”); Merritt v. Reserve Ins. Co., 34 Cal. App. 3d 858, 110 Cal. Rptr. 511, 526 (Cal. Ct. App. 1973) (“In our view independent counsel retained to conduct litigation in the courts act in the capacity of independent contractors, responsible for the results of their conduct and not subject to the control and direction of their employer over the details and manner of their performance.”). See also 1 WINDT, INSURANCE CLAIMS AND DISPUTES § 4.40, at 275 (3d ed. 1995) (“There is . . . no theoretical justification for imputing a defense counsel’s negligence to the insurer.”).

23 Givens v. Mulliken, 75 S.W.3d 383, 395 (Tenn. 2002) (“an insurer can be held vicariously liable for the acts or omissions of an attorney hired to represent an insured when those acts or omissions were directed, commanded, or knowingly authorized by the insurer.”). However, the Givens court was careful to note that “cases in which an insurer may be held liable under an agency theory will be rare indeed” and that the plaintiff must show that the “attorney’s tortious actions were taken partly at the insurer’s direction or with its knowing authorization.” Id. at 396.

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Practice Areas
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- Bad Faith Litigation
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- Commercial Litigation
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- Insurance Coverage
- Premises Liability

Publications

Awards/Recognition
- The Best Lawyers in America©, 2018 – present
- AV Preeminent® Rating, Martindale-Hubbell Peer Review
- Georgia Super Lawyers Rising Stars

Speaking Engagements
- Swift Currie Taking Stage at ACA Seminar - 04.27.2017
- All About the Benjamins: Evaluating and Settling New Claims - 01.26.2017

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