Advisory Opinion 2000-2

June 20, 2000
Lawyer Duties Relating to Insurer's Requirement that Defense Counsel Submit Legal Services Bills to Third-Party Auditor

I. Factual Background
In recent years, some insurance companies have developed billing guidelines for the lawyers they retain to represent their insureds. Among other requirements, these billing guidelines require the "insurance defense lawyers" to submit detailed legal services bills regarding the lawyers' representation of the insureds to independent auditing companies for review and approval. This requirement is between the insurers and the lawyers only, without express agreement from the insured parties and, at least at present, is not part of the insurance contract.

II. Question Presented
May a lawyer retained by an insurer to defend an insured submit legal defense bills pertaining to the representation of the insured to a third-party auditing company without informed consent by the insured client?

III. Brief Answer
No. Absent informed consent of the insured client, an insurance defense lawyer must not disclose legal defense bills pertaining to the representation of the insured to third parties, including auditing companies. Further, an insurance defense lawyer ordinarily may not seek consent from the insured because of inherent impermissible conflicts, which would compromise the lawyer's independent professional judgment.

IV. Scope of Opinion
This opinion discusses the lawyer's duties under the New Mexico Rules of Professional Conduct, Rules 16-101 to 805 NMRA 2000, as they relate to the disclosure of legal defense bills to third-party auditors. The Advisory Opinions Committee is constituted for the purpose of advising inquiring lawyers on the interpretation of the Rules of Professional Conduct, as applied to the inquiring lawyer's duties. The committee does not render opinions on matters of substantive law.

The committee expresses no opinion on the traditional tripartite relationship between insurer, insured and defense counsel. That relationship is assumed as the basis of the inquirer's question. The protection of information that flows among the parties to the tripartite relationship under the lawyer-client privilege is a well-settled principle of insurance law and is not addressed in this opinion.

The analysis contained in this opinion applies only to those cases in which the following conditions exist:

1) The bill review or audit companies in question are wholly independent third parties which stand outside of the tripartite relationship between insurer, insured and the defense lawyer; and

2) The billing guidelines at issue require the lawyer to include a level of detail in the lawyer billing statements which, if discovered by third parties, could reveal information otherwise subject to confidentiality rules, the lawyer-client privilege, the lawyer work product doc-trine, or other similar protections against disclosure.

V. Discussion
The question presented to the committee poses a significant and substantial ethical dilemma. The disclosure of any information relating to the representation of an insured necessarily implicates the lawyer's duties to maintain and to protect client confidences, the client-lawyer relationship, and lawyer work product relating to the representation. The insurer required submission of legal defense bills to third-party auditors would obviously compromise these duties, absent client consent. Further, submission to the auditor of protected information may waive the client's right and privilege of confidentiality, permitting discovery of the information by opposing parties or others.

In *United States v. Massachusetts Inst. of Tech.*, 129 F.3d 681 (1st Cir. 1997), the First Circuit Court of Appeals held that disclosure of information to third-party auditors constituted a waiver of the lawyer-client privilege, and ordered production of otherwise privileged information in the auditor's possession. The Supreme Court of Montana recently has held that third party auditors of insurance-defense bills are not part of the privileged community within which confidential information may be shared without potential waiver of confidentiality privileges. *In re Urgin, Alexander, Zadick & Higgins, P.C.,* 2000 MT 110, 2000 Mont. LEXIS 104, 2000 WL 668915, 57 Mont. St. Rep. 433 (2000). New Mexico courts have not addressed this issue. To the extent a risk of waiver exists as indicated by the above authorities, such waiver could cause irreparable damage to the insured's defense.

A. The Insured Client Must Grant Informed Consent to Disclose Legal Services Bills to Third-Party Auditors
In the context of the tripartite relationship among insurer, insured and defense counsel, the lawyer typically is hired and compensated by the insurer, but the lawyer owes a primary duty of loyalty to the insured. This principle is articulated in Rule 16-108(F) of the New Mexico Rules of Professional Conduct which provides:

A lawyer shall not accept compensation for representing a client from one other than the client unless:

> 1) the client consents after consultation;
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> 2) there is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and
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> 3) information relating to representation of a client is protected as required by Rule 16-106.

Rule 16-108(F) NMRA 2000. *See also*, Rule 16-504(C) NMRA 2000, "A lawyer shall not permit a person who recommends, employs or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services."

As the primary client, the insured is entitled to all the protections afforded by the client-lawyer relationship, including the protection of confidential information. Rule 16-106(A) governs the disclosure of information relating to the representation and provides:

> A lawyer *shall not reveal information relating to representation of a client unless the client consents after consultation*, except for disclosures that are impliedly authorized in order to carry out the representation, and except as stated in Paragraphs B, C and D [of this Rule].

Rule 16-106(A) NMRA 2000 (emphasis added). The client in the client-lawyer relationship is entitled to determine how information relating to the client's case is to be used and disseminated. The information contained in detailed legal service bills constitutes "information relating to the representation of a client." Consequently, Rule 16-106(A) imposes a duty upon the defense lawyer not to disclose defense bills to third party auditors "unless the client consents after consultation." Rule 16-106(A) provides exceptions for certain disclosures, including disclosures "impliedly authorized to carry out the representation" of the insured. The ABA Comment to Rule 16-106 clarifies that "[a] lawyer is impliedly authorized to make disclosures about a client when appropriate in carrying out the representation. . . ." No implied authorization can extend to parties outside of the tripartite relationship in light of the potential waiver of confidentiality of otherwise privileged and protected information. Therefore, the disclosure of legal service bills to third-party auditors does not qualify as an impliedly authorized disclosure under Rule 16-106(A). Nor does such disclosure fall within the other exceptions enumerated in Paragraphs B, C or D of Rule 16-106.

The disclosure of bills to third-party auditors without the insured's consent under the circumstances described above would violate a New Mexico lawyer's duty of confidentiality to the insured client. This conclusion is in accord with ethics committee opinions of Alabama, Alaska, the District of Columbia, Florida, Hawaii, Indiana, Kentucky, Louisiana, Maryland, Massachusetts, Mississippi, Missouri, New York, North Carolina, Ohio, Oregon, Pennsylvania, South Carolina, South Dakota, Utah, Vermont, Virginia, and Washington, and the recent Montana Supreme Court opinion, *In re Urgin,* 2000 MT 110, ¦78.

B. Defense Counsel Cannot Ordinarily Seek Informed Consent from the Insured to Allow Disclosure

The Advisory Opinions Committee questions whether an insurance defense lawyer can ethically counsel the insured client as necessary to seek informed consent to disclose defense bills in light of potential conflicts of interests and the lawyer's other duties under the New Mexico Rules of Professional Conduct. *See,* Rules 16-201 ("In representing a client, a lawyer shall exercise independent professional judgment and render candid advice."); 16-104(B) ("A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation."); and 16-102(A) ("A lawyer shall abide by a client's decisions concerning the objectives of representation . . . and shall consult with the client as to the means by which they are to be pursued.").

Rule 16-107(B) addresses pertinent conflict of interest concerns:

> Unless otherwise required by these rules, a lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client or to a third person, or by the lawyer's own interests, unless:
>
> 1) the lawyer reasonably believes the representation will not be adversely affected; *and*
>
> 2) the client consents after consultation . . .

Rule 16-107(B) NMRA 2000 (emphasis added); *see also,* Rule 16-108(F) NMRA 2000. In general, the lawyer in the tripartite relationship typically enjoys an ongoing professional relationship with the insurer who often provides a steady stream of work to the lawyer. However, when a lawyer is hired by the insurer to represent its insured, the lawyer's primary duty of loyalty is to the insured, not the insurer. Defense counsel may not permit the ongoing professional relationship with the insurer to interfere with the duty of loyalty to the insured. *See,* Rules 16- 504(C), and 16-108(F)(2).

An insurance carrier's requirement that defense counsel submit its defense bills to third parties for review and approval exposes the insured to the potential waiver of confidentiality to otherwise privileged and protected information. The insurer's interest in having the defense bills submitted to a third-party auditor, and the lawyer's interest in getting paid, are facially in conflict with the insured's interests in maintaining confidentiality and a strong legal defense. Rule 16-107(B) allows a lawyer to represent the insured's interests notwithstanding these conflicts only if two conditions are satisfied: 1) the lawyer *reasonably believes* the representation of the insured will not be adversely affected by disclosure of the defense bills to the third-party auditor; *and* 2) the insured provides informed consent to the third-party disclosure. Given the potential waiver problems, the committee believes the first condition rarely, if ever, can be satisfied in this context. Any attempt by the lawyer to obtain the insured's informed consent to disclose defense bills could be viewed as favoring the insurer's and lawyer's interests to the detriment of the insured client's interests, and should be avoided. And given the grave risks of waiver, obtaining consent could constitute a breach of the lawyer's duty to maintain independent professional judgment and to render candid advice to the insured regarding the representation. *See*, Rules 16-201, 16-108(F)(2), and 16-504(C).

Ethics committees in Alabama, North Carolina, Mississippi, Virginia, and Washington also have determined that the Rules of Professional Conduct may preclude an insurance defense lawyer from seeking informed consent from the insured client to disclose bills to third party auditors.