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The Doctor and His Lawyer: Conflicts of Interest

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THE DOCTOR AND HIS LAWYER: CONFLICTS OF INTEREST

Richard H. Underwood*

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I. INTRODUCTION

Almost thirty years ago Robert Keeton observed that the attorney retained by an insurance company to defend a claim against its insured represents two clients with potentially conflicting interests.¹ Noting that defense lawyers did not disclose such conflicts to either the insured or the insurer under the then “prevailing practice,”² Keeton anticipated an increase in the number of legal malpractice suits instituted by either the insured or the insurer against defense attorneys.³

Notwithstanding Keeton's prophetic warning and the formulation of supplementary ethical guidelines for insurers and “their” defense attorneys,⁴ a significant number of lawyers still fail to identify the ethical problems inherent in simultaneous representation of the insured and the insurer. A recent trial court opinion described the lawyer's dilemma:

[T]he relationship between the liability insurer and the insured rests upon a hardboiled commercial transaction. The purchaser has a powerful need for protection against the potentially devastating effects of a large money judgment against him or her. The seller is prepared to provide that protection for a price, but, understandably, only on several conditions including the right to choose the defense lawyer, and the right to control and supervise the defense. There is an inescapable tension for a lawyer, subject to ethical commands far more stringent than those of the

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³ Id. at 1171. 
⁴ Id. at 1171-73. 
* See infra note 31 and accompanying text.
insurance marketplace, who must be faithful to the interests of the insurer-client in control of the defense, and must also "represent the insured as his client with undivided fidelity."\(^5\)

A new malpractice crisis may not be at hand, but several factors have contributed to an increase in the number of reported appellate decisions involving charges of defense malpractice.\(^6\) First, the insurer's obligations to the insured have changed rapidly through judicial expansion of the tort of "insurer's bad faith,"\(^7\) as well as through legislative definitions of "unfair" claims settlement practices.\(^8\) The insurer's duties have evolved into a "checklist of required actions, breach of any one of which may result in the insurer's extracontractual liability [rather] than . . . a workable guide to foreseeability of such damages in a given case."\(^9\) As long as the outer limits of "bad faith" are uncertain and "subject to the convincing art of the trial lawyer,"\(^10\) some defense lawyers, although acting in good faith, may render poor advice to their carrier clients and subject those clients to extracontractual liability. The lawyer may then be called upon to indemnify his insurer-employer for any loss it suffers due to the lawyer's negligence.\(^11\) In addition, plaintiffs' lawyers are learning to identify and in some cases engineer conflicts between the insured and the insurer. The plaintiff's counsel then exploit such conflicts to obtain settlement leverage or an additional "deep pocket," the unwary defense counsel.\(^12\) Finally, some observers argue that a new wave of public criticism of the legal profession, and the publicity associated with the "countersuit phenomenon,"\(^13\) have contributed to a legal environment in which the attorney is viewed as the "new target defendant."\(^14\)

This Article will not survey and catalog all available cases dealing with the "insurance counsel's tightrope."\(^15\) Instead, it will focus on the identification and

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\(^7\) See, e.g., 1 R. LONG, THE LAW OF LIABILITY INSURANCE § 5.34 (1981) [hereinafter cited as 1 LONG].


\(^10\) Id. at 629.

\(^11\) See Keeton, supra note 1, at 1173 (arguing that the potential exposure of the attorney employed by the insurer should "give him pause," unless he is confident that the company will not look to him for indemnity).

\(^12\) See infra text accompanying note 97.

\(^13\) Berlin, Counterfit, in LEGAL MEDICINE 117-18 (1980).

\(^14\) Zilly, Recent Developments in Legal Malpractice, 6 Litigation 8, 12 (1979) [hereinafter cited as Zilly]. A recent survey of the law of conflicts of interest observes that the percentage of attorneys facing malpractice claims rose from one-half of one percent in 1973 to eight percent five years later, although claims arising from conflicts of interest accounted for only a small percentage of all claims. Developments in the Law—Conflicts of Interest, 94 HARV. L. Rev. 124, 1487 & n.83 [hereinafter cited as Conflicts of Interest]; cf. National Law Journal, Oct. 26, 1981, at 3, col. 1 (conflicts accounting for a larger percentage of claims).

\(^15\) The terminology is Zilly's, supra note 14, at 16. For such a survey see R. MalLen & V. LevitT, LEGAL MALPRACTICE (1977) [hereinafter cited as MalLen & LevitT].
resolution of conflicts of interest that may arise at various stages of the litigation of a medical malpractice action in which a lawyer has been retained to represent the interests of both the physician policy-holder and his insurance carrier. Many of the problems examined are applicable to all insurance defense litigation, and the combination of large claims and complex issues presented in medical malpractice cases, together with the distrust of lawyers shared by many doctors, provides particularly fertile ground for conflicts of interests and legal malpractice claims.

Before turning to specific conflicts of interest found in a hypothetical litigation, it is appropriate to review the source and nature of the lawyer's obligations to the insured and the insurer.

II. THE SOURCE AND NATURE OF THE LAWYER'S OBLIGATIONS

A. Who Is the Lawyer's Client

In order for the attorney to perform his role properly, he must never lose sight of the fact that he is working for two different and distinct parties—the insured and the insurer. He must fully disclose to both parties the information he has obtained as a result of his unique relationship with them. Whenever he cannot both legally and ethically perform his duties to the best of his ability, he must disqualify himself from acting contrary to those principles. Regardless of anything else, the attorney must never forget that his primary obligation is to his client, and that client is the insured.

The physician defendant in a third party action is the lawyer's client, even though he does not pay the fee. The defense of the insured is the primary reason for the lawyer's retainer, and the lawyer's obligations to the insured arise from this attorney-client relationship. Therefore, the lawyer's potential liabilities to the insured are broader than the insurer's. They are not derived from or negated by the express terms of the policy, or subject to any limitation implicit in a subjective definition of "bad faith." Liability is imposed on the attorney for professional negligence in the conduct of his client's affairs, and not on the basis of any covenant of good faith and fair dealing implicit in the contract of insurance.

In addition to the physician defendant, the defense counsel also has the malpractice carrier as a client, even though the carrier is not a formal party to the

16 See, e.g., Havener, Observations Regarding Investigation and Preparation of Medical Malpractice Litigation, in DEFENSE OF MEDICAL MALPRACTICE CASES 7, 9-10 (DRI Monograph No. 4, 1977) [hereinafter cited as Havener].


19 See infra text accompanying note 118; see also Heller v. Alter, 143 Misc. 783, 257 N.Y.S. 391 (1952) (defense counsel retained by insurance company to defend its insured not relieved of his duty to represent the insured by the insurer's insolvency).

litigation.\textsuperscript{21} The carrier relies upon the attorney's professional acumen to insure that it does not blunder in the handling of the claim and increase the carrier's exposure to the claimant or invite a suit by the insured for an act of "bad faith."\textsuperscript{22}

Accordingly, the attorney is in a position that has traditionally been avoided—the representation of multiple clients with potentially conflicting interests in a litigation setting.\textsuperscript{23}

B. The Standard of Care

Because the attorney's obligations arise out of the attorney-client relationship, as opposed to the contract of insurance, his duty, found in general tort law, is to advise both of his clients with the skill and care that a reasonable attorney would exercise under the circumstances.\textsuperscript{24} To determine if this customary standard has been violated, the jury in a legal malpractice action needs a yardstick for identifying prudent attorney conduct. The Code of Professional Responsibility, together with formal and informal "opinions" construing it, provides a baseline for identifying acceptable defense practice.\textsuperscript{25} An increasing number of trial judges are finding that violations of the Code are evidence of negligence,\textsuperscript{26} ignoring the disclaimers contained in the Code discouraging use of its provisions as evidence of a standard of care.\textsuperscript{27}

The Code provides a formula for resolving actual conflicts of interest, whether such conflicts arise from divided loyalties or the disclosure of client confidences or secrets. Specifically, the Code permits simultaneous representation of multiple clients who consent to such representation after "full disclosure." In addition, it must remain "obvious" during the course of the litigation that adequate representation can be provided to each client.\textsuperscript{28} To satisfy the Code the attorney must


\textsuperscript{24} Lysick v. Walcom, 258 Cal. App. 2d at —, 65 Cal. Rptr. at 414. But see Keeton, supra note 1, at 1171 (arguing that the standard is measured by an attorney specializing in insurance defense litigation).

\textsuperscript{25} Conflicts of Interest, supra note 14, at 1489; see Model Code of Professional Responsibility ECs 5-14 to -17; DRs 4-101, 5-105.

\textsuperscript{26} In Rogers v. Robson, Masters, Ryan, Brummond and Belom, 74 Ill. App. 3d 467, 392 N.E.2d 1365 (1979), aff'd, 81 Ill. 2d 201, 407 N.E.2d 47 (1980) the intermediate appellate court opined:

"It is true that the present action is one for malpractice and not a disciplinary proceeding, but it would be anomalous indeed to hold that professional standards of ethics are not relevant in a tort action, but are in a disciplinary proceeding. Both malpractice actions and disciplinary proceedings involve conduct failing to adhere to certain minimum standards, and we must reject any suggestion that ethical standards are not relevant considerations in each."

Id. at —, 392 N.E.2d at 1371; see also Woodruff v. Tomlin, 616 F.2d 924, 936 (6th Cir. 1980); In re Kuzman, 335 N.E.2d 210, 212 (Ind. 1975); cf. Moritz v. Medical Protective Co., 428 F. Supp. 865 (W.D. Wis. 1977); Employers Cas. Co. v. Tilley, 496 S.W.2d 552 (Tex. 1973).


"The Code... (does not) . . . undertake to define standards for civil liability of lawyers for professional conduct.

28 Model Code of Professional Responsibility DR 5-105(C) (1981) provides:

"In the situations covered by DR 5-105(A) and (B), a lawyer may represent multiple clients if
identify potential conflicts and explain their nature and significance in such detail that each client, physician and carrier, can understand the desirability of obtaining an independent attorney. If both clients elect to continue simultaneous representation after the attorney's explanation, then he has fulfilled his initial obligations to each of them. The attorney must continue to satisfy the condition that it remain "obvious" that he can exercise his independent professional judgment on behalf of each client. In the event that he can no longer exercise this judgment, the attorney must withdraw. Using this standard, if the attorney fails to disclose a conflict that prevents him from fulfilling the full measure of his responsibilities to one or the other of his clients, or if he advances the interests of one client to the detriment of the other during any stage of the case, he exposes himself to a malpractice claim.

Unfortunately, the Code provides little guidance to assist an attorney in identifying specific conflicts peculiar to insurance defense litigation, making it difficult for him to apply this consent-disclosure formula of the Code. The Code also provides no guidelines for assessing the consequences that might flow from a given conflict. Such guidelines could help the attorney determine whether it is no longer "obvious" that he can represent both clients fairly. Moreover, the Code is silent as to the mechanics of withdrawal, and does not suggest any rule of priority between the conflicting client interests before or after withdrawal. Several courts have suggested that the defense counsel's obligations to the insured are primary, but if such language is factored into the consent-disclosure formula, the Code does not explicitly take account of it.

The Code's lack of specificity was cured, to some extent, by the formulation of the Guiding Principles of the National Conference of Lawyers and Liability Insurers. The Guiding Principles adopted the consent-disclosure formula as a means of insuring that an attorney would advance the interests of both of his clients. The Principles also identified many of the recurring conflicts of interest between the insured and the insurer, and provided some additional guidance for the timing and scope of disclosures. While the courts did not accept all of the

it is obvious that he can adequately represent the interest of each and if each consents to the representation after full disclosure of the possible effect of such representation on the exercise of his independent professional judgment on behalf of each.

29 See, e.g., Moritz v. Medical Protective Co., 428 F. Supp. at 872, which provides: "The canons and disciplinary rules do not address themselves frankly and explicitly to this special set of relationships, and there is awkwardness in attempts to apply the canons and rules."


solutions proposed in the Guiding Principles, they did adopt them in part and often cited them as secondary authority when formulating standards for identifying defense malpractice and bad faith in civil actions brought against attorneys and their employer insurers. Although their uncertain status raises some question as to their admissibility in future malpractice cases, the Guiding Principles continue to provide a useful restatement of the case law of attorney liability in this area of legal malpractice. Moreover, a malpractice plaintiff may still use the standards as a checklist of potential claims, and then translate his arguments into the more readily acceptable formulae of the Code or case law.

III. Identifying and Resolving Conflicts of Interest: A Hypothetical Litigation

In July 1980 the plaintiff suffered a serious brain injury while under the care of Dr. Mensa, a neurosurgeon, and Dr. Carpenter, an orthopedic surgeon. A lawsuit was filed on July 6, 1981 naming both physicians as defendants. Both Dr. Mensa and Dr. Carpenter are insured by Insurer, with policy limits of $500,000 and $1,000,000 respectively. Dr. Carpenter reported the claim promptly and demanded that the Insurer provide a defense. On July 21 Dr. Mensa’s wife reported the claim to Insurer, although Dr. Mensa had not been served with summons. Insurer’s claims manager told her that some forms would be sent to Dr. Mensa, but that he need not consider himself sued until he was served with summons. Summons was not served until October 8, 1981.

The complaint against the two physicians contained multiple counts of negligence, as well as allegations of gross, willful, and wanton conduct. The plaintiff sought compensatory damages of $5,000,000 and punitive damages of $3,000,000.

A short time after Dr. Mensa was served with summons, and before the defense attorney was retained, the plaintiff’s attorney initiated preliminary negotiations with Insurer’s claims manager. It was during these initial discussions that he learned of the policy limits. He immediately forwarded the following correspondence to Insurer:

Dear Sirs: In view of the maximum limits of coverage under your Insured’s policies, my client has authorized me to make a written demand of

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32 See, e.g., cases cited infra note 54.
33 Rogers v. Robson, Masters, Ryan, Brummond and Belom, 74 Ill. App. 3d at —, 392 N.E.2d at 1371; Y.M.C.A. v. Commercial Standard Ins. Co., 552 S.W.2d 497, 503 (Tex. Civ. App. 1977). In Employers Cas. Co. v. Tilley, 496 S.W.2d at 559, the court stated:

We approve of the above quoted "guiding principles" as conforming to the public policy of this state heretofore enunciated by this Court in our Canons of Ethics. They follow the same general principles earlier recognized by Texas courts.

No reported case has considered the weight to be given such standards when presented as a matter of defense to justify counsel’s conduct. In support of their use as a matter of defense, compare Thornton v. United States, 357 A.2d 429 (D.C.), cert. denied, 429 U.S. 1024 (1976) (trial attorney for murder defendant followed ABA STANDARDS RELATING TO THE PROSECUTION FUNCTION AND THE DEFENSE FUNCTION § 7.7 (1971); claim of ineffective assistance of counsel rejected).

34 The facts of this hypothetical litigation are drawn from reported medical malpractice cases, which are cited at appropriate points in the text.
36 In connection with disclosure of policy limits see Slotkin v. Brookdale Hosp. Center, 357 F. Supp. 705 (S.D.N.Y. 1972) (applying New York law, the court entertained a damage action against the insurer and "others" because the plaintiff had been induced to settle a claim by fraudulent representations concerning the policy limits).
$1,000,000. Refusal upon the part of your company to settle for this sum would be tantamount to an act of "bad faith" against my client as well as your insureds, and if judgment is obtained in excess of this amount, I will make every effort to collect the full amount of such judgment from your company.37

The physicians' malpractice policies contain the following provisions:

(1) A. TO PAY all loss by reason of the liability imposed by law upon the Insured for damages on account of professional services rendered or which should have been rendered by the Insured or any assistant to the Insured during the term of this Policy including the dispensing of drugs or medicine or any counterclaims in suit brought by the Insured to collect fees providing such damages are claimed under any of the foregoing.

B. TO DEFEND the Insured without limit of cost in any suit against the foregoing specifications filed at any time, and to furnish any bond not exceeding in amount the minimum limit of this Policy which may be incidentally necessary for such suits, for appeals or the release of attachments or garnishments; it being understood, however, that no law costs shall be incurred without the consent of the Company.38

In the event the Insured refuses to consent to the settlement or compromise by the Company of a claim or suit against the Insured, either the Insured or the Company shall have the right to submit the matter to an advisory committee of three members in good standing of the Medical Society of the State. The Insured shall nominate one member of the committee, the Company the other, and the two members so chosen shall select a third member who shall act as umpire in case of disagreement between the two members chosen by the Insured and the Company. The facts of the case shall be presented to the committee and the decision of a majority of said committee shall be binding on the Insured and the Company.39

Attorney was retained by Insurer to defend both physicians in the medical malpractice action.

A. The Attorney's Role in Coverage Disputes

Assume that Attorney tentatively accepted the retainer pending a review of the claims file. Upon examining the file, Attorney noted the absence of any correspondence to the Insured physicians regarding the claims for punitive damages or claims for compensatory damages in excess of the policy limits. When Attorney called Insurer for clarification, Insurer's claims manager asked Attorney to prepare and forward to each Insured an "excess letter"40 and a notice that the defense would be conditioned on the Insured's acceptance of a reservation of rights allowing Insurer to litigate coverage in a separate proceeding.41

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37 The text of this letter is suggested by Manchester Ins. and Indem. Co. v. Grundy, 531 S.W.2d 493 (Ky. 1975), and C. Robbins, ATTORNEY'S MASTER GUIDE TO EXPEDITING TOP DOLLAR CASE SETTLEMENTS (1977).


40 Sample forms for "excess situations" are provided in EXCESS LIABILITY, (DRI Monograph No. 3, 1973).

41 A specimen reservation of rights letter and a sample nonwaiver agreement are provided in INSURER'S DUTY TO DEFEND, APPENDICES A & B (DRI Monograph No. 3, 1978).
claims manager also sought advice with respect to potential coverage defenses, including Dr. Mensa’s “late notice” and his unilateral settlement of an earlier unrelated claim.

Generally, in malpractice actions in which the defendant doctor is insured, the carrier will advise the attorney of any coverage problems when it forwards the claims file. The coverage issues that are routinely brought to the attorney’s attention at this point may arise from claims for punitive damages for which the insurer is not liable, allegations in the complaint that describe conduct specifically excluded from coverage, or evidence that the insured failed to provide timely notice of the claim or otherwise failed to “cooperate” with the insurer. For purposes of the hypothetical, discussion will be limited to Attorney’s discovery of potential coverage issues during his preliminary review of the file, Insurer’s request for assistance in the preparation of correspondence to the Insured, and Insurer’s request that Attorney research and advise Insurer as to the availability of declaratory relief.

If coverage problems are apparent from counsel’s examination of the claims file, ordinarily the malpractice carrier will expect the attorney to draw attention to them. Beyond that, a prudent insurer will direct the attorney not to become involved in any coverage issues, and concentrate on the merits of the insured’s defense. In the hypothetical case, Attorney may draw the carrier’s attention to the absence of an “excess letter” and “reservation of rights,” but he should not prepare such correspondence, or procure a stipulation from either Insured that the Insured accepts a conditional defense. Such activities are not only adverse to the Insured’s interest, but also create an appearance of impropriety that could undermine the validity of any stipulations the Attorney might procure.

Moreover, an attorney should never research and advise the insurer on the merits of any coverage dispute, or participate in simultaneous or subsequent litigation of such issues. To do so would be tantamount to advancing a position on behalf of the carrier that the attorney would be bound to oppose on behalf of

43 2 LONG, supra note 39, § 12.04.
44 Malpractice policies ordinarily contain provisions excluding coverage for liability arising from criminal acts or bodily injury caused as the result of the violation of any statute, injuries arising from practice in an area outside the scope of the physician’s professional license, injuries caused while the physician was under the influence of intoxicants or narcotics, or claims arising from the physician’s failure to produce a guaranteed result. 2 LONG, supra note 39, §§ 12.27-30; LOUISELL & WILLIAMS, supra note 38, § 20.04.
45 Policy conditions requiring prompt notice of claims or unusual occurrences and cooperation by the insured have been the frequent source of litigation between the insured physician and his carrier. It is not uncommon for the malpractice carrier to refuse to defend, or tender a conditional defense by invoking such provisions. See LOUISELL & WILLIAMS, supra note 38, § 20.05. Often such defenses are colorable at best. See, e.g., Public Serv. Mut. Ins. Co. v. Levy, 87 Misc. 2d 924, 387 N.Y.S.2d 962 (1976).
46 The attorney’s exploitation of his fiduciary relationship to discover evidence adverse to the insured for use in a coverage dispute is discussed at text accompanying notes 40-54 infra.
48 Employers Cas. Co. v. Tilley, 496 S.W.2d 552 (Tex. 1973). There are other reasons to adopt a neutral position toward coverage issues. For example, the insurer may be tempted to tender a conditional defense on a colorable ground as in Medical Protective Co. v. Davis, 581 S.W.2d 25 (Ky. Ct. App. 1979), from which the facts of the hypothetical case were drawn. If the court concludes that the insured properly rejected a conditional defense, and that the ground for the refusal to defend unconditionally was without merit, the insurer may be held liable for any subsequent verdict up to the policy limits, plus any costs of defense, and possibly extracontractual damages in an appropriate case. The risk that the insurer will seek indemnity from counsel who advised the insurer to tender the conditional defense is very real.
the insured.\textsuperscript{50} In the hypothetical case, Attorney should limit his activities to disclosure of the nature and extent of the potential conflicts between the Insured physicians and Insurer, so that all of his clients understand the importance of securing independent counsel.\textsuperscript{51} In disclosures to the Insureds, Attorney should explain any limitations on his role as defense counsel relative to the allegations of "gross, willful and wanton" misconduct as well as his inability to assume a relationship adversary to the carrier on any issue unrelated to the defense on the merits.\textsuperscript{52} With respect to the potential conflicts that arise from claims in excess of the policy limits or claims for punitive damages, the Guiding Principles set forth general guidelines for a sufficient minimum disclosure.\textsuperscript{53} With respect to other coverage disputes that may be suggested by the file, arguably Attorney should go further than the Guiding Principles and advise the Insureds that the expenses of independent counsel are the carrier's responsibility.\textsuperscript{54} This disclosure might influence the Insureds' decision to seek independent counsel rather than acquiesce in continued representation by an attorney appointed by the carrier.

\textbf{B. Pleadings and Parties}

\textbf{1. Representing Multiple Insureds}

Potential conflicts arise when a single carrier insures more than one defendant.\textsuperscript{55} Nonetheless, some courts find that there is no actionable impropriety inherent in joint representation of multiple insureds in the absence of an actual conflict of interest. For example, in \textit{Spindle v. Chubb/Pacific Indemnity Group}\textsuperscript{56} a neurosurgeon and an orthopedic surgeon were both represented by a firm retained by their common insurer. The two physician insureds had different policy limits, their exposure had been reinsured in different amounts, and their poten-


\textsuperscript{51}See infra text accompanying notes 92 & 110.

\textsuperscript{52}For example, an attorney should not suggest that the insured write the insurer a bad faith letter or advise the insured on the merits of the coverage dispute. Bianches, \textit{Coverage Disputes With The Insured: The Insurer's Perspective}, 48 INS. COUNS. J. 153, 154 (1981).

\textsuperscript{53}See infra text accompanying note 110. When the coverage dispute arises from claims for punitive damages or other damages in excess of the policy limits, the attorney's ethical obligation to defend the insured's liability should preclude any qualification of the defense. Malley & Levit, supra note 15, at 141 (Supp. 1980). The insurer is not attempting to terminate all benefits under the policy. Instead it is the real party in interest up to the amount of the policy limits. It retains the right to control the defense, and it need not pay for independent counsel selected by the insured, because the insured is getting all that he bargained for under the policy. If, on the other hand, the insurer's policy defense would void the insurance contract or terminate all policy benefits, then the insured is exposed to the entire amount of any adverse judgment. Accordingly, the insured should have the right to control the defense through independent counsel, at the insured's expense.


\textsuperscript{55}The possibility of suits against multiple defendants with the same insurer is increasing as fewer carriers provide malpractice coverage. See Havener, supra note 16, at 13.

\textsuperscript{56}89 Cal. App. 3d 706, 152 Cal. Rptr. 776 (1979).
tial liability differed. Upon tendering notice of the plaintiff's claims against him, the neurosurgeon was advised by the carrier that there were no apparent conflicts of interest between the codefendants, and that it would be more economical to share common counsel. He consented to simultaneous representation, but refused to consent to any settlement of the lawsuit. After trial, but before verdict, the plaintiff offered to compromise all her claims against both physicians for $350,000. No settlement was concluded, although the neurosurgeon's codefendant had directed the insurer to settle the claims against him within his $500,000 policy limit. The jury returned a verdict of $404,000 and the attorney negotiated the release of the codefendant for $300,000. The insurer paid the entire judgment, allocating $300,000 to the codefendants' policy limit and $104,000 to the neurosurgeon's policy. The neurosurgeon then brought separate actions against the insurer and his former defense attorney, contending that the insurer's initial representation that there were no apparent conflicts between him and his codefendant were false and fraudulent, and made to induce him to forego independent counsel. He reasoned that if he had known of his codefendant's policy limit, reinsurance, and degree of exposure, he would have secured independent counsel and tried to get a compromise of all claims to be funded by his codefendant's policy, thereby eliminating the chance that any judgment would be entered against him. The court rejected these contentions on the ground that the insurer's representations were true when made, that none of the alleged conflicts were actual conflicts, and that the neurosurgeon had no right to have his codefendant's policy applied to settle his own potential liabilities. In the companion case against the law firm, the court rejected the neurosurgeon's theory of damages without reaching the questions of the firm's liability or the recoverability of damages for injury to the neurosurgeon's reputation attributable to the judgment that was entered against him.

Although Spindle and its companion case suggest that simultaneous representation of multiple insureds may be permissible in some instances, the two cases provide little comfort or practical guidance to defense counsel. In order to avoid malpractice claims, counsel must recognize potential conflicts, and then recommend employment of separate counsel if at all possible. To help the lawyer in this process, the Guiding Principles suggested the following prophylactic rule:

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57 Id. at 710, 152 Cal. Rptr. at 778.
59 The attorney allegedly did not inform the neurosurgeon of this offer, and the opinion does not contain any discussion of findings relevant to such nondisclosure. The court did not consider how disclosure of the offer and the alleged conflicts of interest might have affected the physician's settlement posture before verdict. With respect to an attorney's obligation to keep the insured informed of settlement negotiations see infra text accompanying notes 106-20.
60 89 Cal. App. 3d at 713, 152 Cal. Rptr. at 780. The court stated that none of the alleged conflicts, when viewed separately, would render the attorney's simultaneous representation less effective, thereby resulting in actual conflict. The court reasoned that the alleged inadequacies of the insurer's disclosures, when viewed in the context of the neurosurgeon's persistent refusals to settle, did not state a claim for fraud or bad faith. Id. at 714, 152 Cal. Rptr. at 781.
61 The neurosurgeon's damage claims were somewhat contrived. For example, he sought recovery of the full amount of the $404,000 judgment although the carrier, not he, had paid the full amount of the judgment and expressed satisfaction with the result. In addition, he sought recovery of any judgment that might be awarded in a later filed, but unrelated, malpractice action against him, on the theory that but for the verdict in the first case, the second plaintiff would not have discovered her claim against him. While the viability of such a damage claim was not properly before it, the court expressed little enthusiasm for it. 59 Cal. App. 3d at 146, 131 Cal. Rptr. at 421.
62 Id. But see cases cited infra notes 118 & 119.
VII. Suit Involving More Than One Insured In the Same Company

If the same company insures two or more parties to a lawsuit, whose interests are diverse, the complete factual investigation made by the company should be made available to each insured or his attorney with the exception that any statement given by one insured or his employees shall not voluntarily be given to any other party to the litigation whose interest may be adverse to such insured or to any attorney representing such other party.

The company should employ separate attorneys not associated with one another to defend each insured against whom any suit is brought, if the interest of one such insured is diverse from or in conflict with that of any other insured; and all insureds should be informed by the company of the fact that it insures the liability of the others and the method being employed to handle the litigation.63

Under this standard if the codefendant insureds have differing interests that have not yet ripened into actual conflicts, the insurer will retain its right to control their defense only if it employs independent counsel for each insured, at the insurer's expense.64 Accordingly, one may question the sufficiency of the disclosures made to the neurosurgeon in *Spindle* and the wisdom of continuing simultaneous representation in that case.

Aside from the general problems inherent in representing more than one insured, the hypothetical case should suggest a welter of additional conflicts to a prudent attorney. For example, an attorney's initial review of the file may suggest a potential cross-claim between the co-parties,65 or the necessity of vigorously contending on behalf of one insured that the other was solely responsible for the plaintiff's injury.66 Moreover, the attorney may be wise to assume, before the initial interview, that one client's testimony may weaken or disparage the other's position, or that one client may confide information that should be kept from the other.67 The attorney has an obligation to make sure that both insureds are fully aware of the perils of simultaneous representation prior to any joint consultation, and take care that the confidences and secrets of one client are not furnished to the other.68 Such potential conflicts probably will occur in all cases in which an attorney is retained to represent multiple insureds. It would be wise, therefore, for the attorney to reject such employment as a general rule, and thereby avoid the consequences of a belated withdrawal or future litigation.69

63 See *supra* note 31.
64 Carriers often insure medical partnerships. 2 *LONG*, *supra* note 39, § 12.20. In Joseph v. Markovitz, 27 Ariz. App. 122, 571 P.2d 57 (1976), a partner who had suffered a judgment in excess of his malpractice coverage filed a third-party claim against his partner asserting that the partnership agreement provided for indemnity for 20% of the amount of the excess. The partner's common insurer was required to pay the costs of defending the third-party action by independent counsel.
67 In *Spindle* v. Chubb/Pacific Indem. Group, 89 Cal. App. 3d at 714 n.5, 152 Cal. Rptr. at 781 n.5, the court took care to point out that nothing was said by one codefendant about the other that would have weakened his position on the merits of the case. *Cf.* Aetna Cas. & Ins. Co. v. United States, 570 F.2d 1197 (4th Cir.), cert. denied, 439 U.S. 821 (1978); Kerry Coal Co. v. U.M.W., 470 F. Supp. 1032 (W.D. Pa. 1979).
68 See *infra* text accompanying notes 75-97.
69 *Conflicts of Interest*, *supra* note 14, at 1308.
2. Representing One Insured

Assume in the hypothetical case that Attorney refused to represent multiple defendants prior to the initial interview, and was retained to defend only Dr. Mensa. At the initial interview Dr. Mensa suggested that the plaintiff's injury, if any, was attributable to the conduct of Dr. Carpenter. Dr. Mensa urged Attorney to file a cross-claim or take some other action that would focus attention on his codefendant or some other party.

Joinder of all potential claims and parties may not always be wise tactically. Particularly in cases in which both defendants are insured by the same carrier, the carrier may wish to avoid a fight between the codefendants. Conventional wisdom suggests that infighting between codefendants will enhance the plaintiff's position in settlement negotiations and at trial.\(^7^0\) On the other hand, an attorney must insure that any decision that is made regarding joinder of claims or parties is made only with the consent of the insured after full disclosure. For example, the Guiding Principles provided:

VII. Counterclaims

In any suit where the company or the attorney selected by the company to defend the suit becomes aware that the insured may have a claim for damages against another party to the lawsuit, which is likely to be prejudiced or barred unless it is asserted as a counterclaim in the pending action, the insured should be advised that the pending suit may affect or impair such claim; that the insurance company does not provide coverage for any legal services or advice as to such claim; and that the insured may wish to consult an attorney of his choice with respect to it.\(^7^1\)

Although the Guiding Principles isolated counterclaims due to the harsh consequences that follow from nonjoinder in many jurisdictions,\(^7^2\) potential conflicts of interest between the insured and the insurer may arise any time nonjoinder is to the advantage of the insurer. Specifically, the attorney must take care to apprise the insured of any limitation imposed by the insurer on the scope of the attorney's employment, as well as any period of limitations applicable to his claims. The attorney should advise the insured to seek an independent attorney's assistance in the prosecution of any claims the insured insists on injecting into the litigation over the insurer's objection.

An attorney may not simply ignore the insured's potential claims. For example, in *Daugherty v. Runner*\(^7^3\) an attorney was retained by a decedent's estate to pursue a wrongful death action arising out of an automobile accident. The attorney did not pursue a potential malpractice claim against the hospital that had treated the decedent prior to her death. In a subsequent legal malpractice action the attorney testified that he was not hired to pursue such a claim. Although the appellate court affirmed a jury verdict for the attorney defendant on the evidence presented at trial, the court opined:

We are not ready to hold that Mr. Runner had absolutely no duties to his client with regard to a medical malpractice action simply because the

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\(^7^0\) Havener, *supra* note 16, at 13.

\(^7^1\) See *supra* note 31.

\(^7^2\) But see Suchta v. Robinette, 596 P.2d 1380 (Wyo. 1979) (settlement of insured's liability and dismissal of action will not, without more, result in loss of insured's own claim against another party).

\(^7^3\) 581 S.W.2d 12 (Ky. App. 1979).
written contract did not specifically mention a malpractice suit. To do so would require the client, presumably a layman who is unskilled in the law, to recognize for himself all potential legal remedies. An attorney cannot completely disregard matters coming to his attention which should reasonably put him on notice that his client may have legal problems or remedies that are not precisely or totally within the scope of the task being performed by the attorney.\footnote{\textit{Id.} at 17.}

\section*{C. Investigation of the Claims: Confidences and Secrets of the Insured}

Assume that Dr. Mensa appeared at the initial client interview in a state of agitation. He presented a history of his past disagreements with Insurer as a result of its decision not to appeal an adverse judgment in a prior case, as well as his unilateral settlement of another small claim. He inquired about Attorney's duty to represent his interests as opposed to those of Insurer, and after satisfying himself as to Attorney's loyalty, discussed the merits of the claim in considerable detail.

Assume further, however, that out of fear of some future difficulty, Dr. Mensa confided to Attorney that his temporary permit to practice in the forum state had expired prior to the incident in suit. After the expiration of his permit and before the claimant's injury, he applied for a renewal of his malpractice policy in a letter written on stationery bearing his old address in a state in which he was still licensed. Unfortunately, the declarations of the renewal policy, which had been forwarded to his old address, required that he be duly registered and licensed to practice under the laws of all jurisdictions in which he intended to practice.\footnote{\textit{See Aetna Cas. \\& Surety Co. v. Evers, 590 F.2d 600 (5th Cir. 1979).}} Also assume that Dr. Mensa sought to explain his conduct as the consequences of his use of a drug, thereby inadvertently providing Insurer with an arguable claim of exclusion under the policy's "drug" clause.\footnote{\textit{See} LOUISELL \\& WILLIAMS, supra note 38, \S 20.04. For other examples of inadvertent disclosures suggesting policy defenses see Hutcheson, supra note 65.}

This interview with Dr. Mensa illustrates a recurring source of conflicts of interests in defense practice. During the course of the client interview, the insured reveals a "fraud" in obtaining the policy that could render the contract void \textit{ab initio}, or a fact that might provide a basis for denying policy coverage.

The attorney might have avoided such disclosures by carefully explaining his limited role at the beginning of the client interview.\footnote{Allen, \textit{Selected Conflicts of Interest Problems in Insurance Litigation}, in \textbf{CONFLICTS OF INTEREST IN INSURANCE PRACTICE} 51 (DRI Monograph No. 5, 1971) [hereinafter cited as Allen].} It is customary, however, for the attorney to engage in some questioning of the insured physician concerning his background and experience, and his knowledge of other facts that might bear on the attorney's evaluation of the claim.\footnote{Hutcheson, supra note 65, at 39.}

As a result of such questioning, the attorney may receive information from the insured physician that the insurer does not know and that would provide a coverage defense for the insurer. It might be argued in our hypothetical case that Insurer will learn of the physician's licensing problem or use of alcohol or drugs during discovery. On the other hand, an experienced plaintiff's counsel may withhold allegations involving such issues, or refrain from questioning the physi-
cian on such matters to guarantee the availability of the policy proceeds.\textsuperscript{79} Once Dr. Mensa makes the disclosures, Attorney needs to choose one of the following courses of action: (1) disclosure of all facts to Insurer, (2) withdrawal, or (3) continued representation of the Insured without disclosure to Insurer.

Traditionally, communication by one joint client to common counsel concerning a matter in which both clients have sought representation has not been considered privileged as to the other joint client, in an evidentiary sense. Indeed, an early ABA Opinion held that the attorney should disclose to the insurer all information received from the insured relating to coverage.\textsuperscript{80} This opinion finds support in several appellate opinions which hold that the insured's consent to disclosure is implied from his agreement to accept simultaneous representation.\textsuperscript{81} This position is unacceptable. First, the attorney's ethical obligation to preserve the confidences and secrets of each client is not coextensive with the rules of evidentiary privilege. Evidence rules do not take into account the pervasive requirement that an attorney not act to the detriment of either of his joint clients.\textsuperscript{82}

Second, application of this joint client rule presupposes that the clients are united in a common interest. This assumption is not necessarily true. Arguably, information bearing on the ability of the insured and the insurer to work together, such as the insured's dissatisfaction with the handling of prior claims, may not be confidences and secrets of either client. Instead, this information may be a legitimate subject of the insurer's inquiry if the information relates to the feasibility of a continued relationship between the insured, the insurer, and their common counsel.\textsuperscript{83} All parties have an interest in determining if common representation may proceed amicably. On the other hand, if the insured gives information to the attorney that might provide a basis for denying policy coverage, then the clients are no longer united in a common interest, because the policyholder sees their common interest as a successful defense of the claim on the merits. Application of a joint client disclosure rule invariably runs counter to these expectations of the insured, and favors the insurer over the insured. In the absence of a full explanation to the insured that disclosure may prejudice his interests, the insured cannot be held to have consented to disclosure.\textsuperscript{84}

Withdrawal is also problematical. In the event of withdrawal, the attorney may not represent either client, and will be under a continuing obligation to preserve inviolate the insured's confidences and secrets. Accordingly, there is some merit in the argument advanced by one commentator that:

The best way out is for [defense counsel] to withdraw from the case. The insured loses nothing by his withdrawal because the attorney has been silenced by permitting this confidential communication in the belief the attorney would treat it as confidential. The company may be the loser, but since the attorney had not been retained to ascertain coverage defenses or grounds of recission he has not breached any duty to the insurer.

\textsuperscript{79} LOUISELL \& WILLIAMS, supra note 38, § 20.04.
\textsuperscript{80} ABA Comm. on Professional Ethics, Informal Op. 822 (1965).
\textsuperscript{83} Moritz v. Medical Protective Co., 428 F. Supp. at 873.
by nondisclosure. His immediate withdrawal subject to reasonable notice of his intention to do so, seems to be the only appropriate course and, as I see it, no insurance company could expect an attorney to pursue any other course.\footnote{Allen, \textit{supra} note 77, at 52. Allen's suggestion that counsel must withdraw is supported by several reported cases. \textit{See, e.g.}, State Farm Mut. Ins. Co. v. Walker, 382 F.2d 548 (7th Cir. 1967); Allstate Ins. Co. v. Keller, 17 Ill. App. 2d 44, 149 N.E.2d 482 (1958).}

On the other hand, the attorney must provide some explanation for his withdrawal, if only a cryptic reference to a potential "ethical problem."\footnote{Guiding Principle \textit{IX} provides:} The very act of withdrawal may alert the insurer to the need for further investigation or discovery relating to coverage.\footnote{\textit{Cf.} Fidelity and Cas. Co. of N.Y. v. McConnaughty, 228 Md. 1, 179 A.2d 117 (1962). The \textit{American Lawyer's Code of Conduct} Rule 6.6 (1980), appears to prohibit counsel from offering any explanation for his withdrawal, \textit{albeit} simply a reference to a potential conflict of interest, if that would prejudice the insured's confidences or secrets. Allen, \textit{supra} note 77, recognizes that a defense attorney has not been retained to ascertain coverage defenses, and therefore has no obligation to pass on the insured's confidences regarding coverage to the insurer. Even so, he contends that withdrawal is the only appropriate course of action, although he appears to accept the possibility that the defense attorney's initial withdrawal might prejudice the clients confidence by stimulating the curiosity of the insurer's claims department.}

Since withdrawal may prejudice the insured, and since counsel owes no duty to the insurer to ascertain or otherwise develop evidence pertinent to coverage, the best course of action in our hypothetical is for Attorney to represent the insured without disclosure of the insured's confidences.

The ABA apparently recognized the difficulties associated with disclosure or withdrawal, and it overruled the earlier joint client disclosure rule. It adopted the position that the attorney may not pass along to the insurer any confidence or secret of the insured that might provide a defense in any post-judgment garnishment proceeding against the insurer.\footnote{ABA Comm. on Professional Ethics, Informal Op. 949 (1966).} This rule was incorporated into the Guiding Principles in Paragraph VI.

\section*{VI. Duty of Attorney Not To Disclose Certain Facts and Information}

Where the attorney selected by the company to defend a claim or suit becomes aware of facts or information, imparted to him by the insured under circumstances indicating the insured's belief that such disclosure would not be revealed to the insurance company but would be treated as a confidential communication to the attorney, which indicate to the attorney a lack of coverage, then as to such matters, disclosures made directly to the attorney, should not be revealed to the company by the attorney, nor should the attorney discuss with the insured the legal significance of the disclosure or the

\textit{See supra} note 31. There is some apparent conflict between \textit{IX}'s requirement that the insured be advised of the reasons for withdrawal, and \textit{VI}'s requirement that the attorney not discuss with the insured the legal significance of facts indicating a lack of coverage. Presumably an attorney may tell his clients that withdrawal is necessitated by ethical considerations, which the attorney may not explain further. An attorney's dilemma is very much like that faced by the criminal defense attorney who is convinced that his client is about to commit perjury. Any suggestion to the court by the attorney that there is an "ethical problem," or attempted withdrawal, may suggest to the court or jury that the client's testimony is not to be credited. Such conduct is viewed by some authorities as a betrayal of the client. \textit{See, e.g.}, Freedman, \textit{Perjury: The Lawyer's Trilemma}, \textit{1 Litigation} 26 (1975).
nature of the coverage question.\textsuperscript{89}

If the attorney acquires information suggesting lack of coverage under circumstances indicating the insured's belief that such disclosure would not be revealed to the company, the attorney may not betray the insured's confidence by revealing such information to the insurer.\textsuperscript{90} Nor may he use the confidential relationship with his client to gather information detrimental to the client's interest. The requirement that the disclosure be "imparted to him by the insured under circumstances indicating the insured's belief that such disclosure would not be revealed to the insurance company" should be read liberally. The insured should not have to express a desire to withhold the information from the insurer. If the information is given during the course of consultation with the attorney and concerns a matter not bearing directly on the claim, then it should not be disclosed to the insurer. The information, however, must "indicate to the attorney a lack of coverage."\textsuperscript{91}

On the other hand, if a question of coverage arises because the attorney incidentally becomes aware of facts from some other source (not the client, the client's agents or employees, or the client's files), the attorney may follow the course of action set forth in Guiding Principles Paragraphs IV and V:

IV. Conflicts of Interest Generally—Duties of Attorney

In any claim or in any suit where the attorney selected by the company to defend the claim or action becomes aware of facts or information which indicate to him a question of coverage in the matter being defended or any other conflict of interest between the company and the insured with respect to the defense of the matter, the attorney should promptly inform both the company and the insured, preferably in writing, of the nature and extent of the conflicting interest. In any such suit, the company or its attorney should invite the insured to retain his own counsel at his own expense to represent his separate interest.

V. Continuation By Attorney Even Though There is a Conflict of Interest

Where there is a question of coverage or other conflict of interest, the company and the attorney selected by the company to defend the claim or suit should not thereafter continue to defend the insured in the matter in question unless, after a full explanation of the coverage question, the insured acquiesces in the continuation of such defense.

If the insured acquiesces in the continuation of the defense in the pending matter following a reservation of rights by the company or under an agreement that the rights of the company and the insured as to the coverage question are not waived or prejudiced, the company retains the exclusive rights to control and conduct the defense of the case in good faith, subject to the right of the insured or the additional attorney acting at the expense of the insured to participate.

If the insured refuses to permit the insurance company and the attorney selected by the company to defend the claim or suit to continue the defense of the pending matter while reserving the rights of the company

\textsuperscript{89} See supra note 31.

\textsuperscript{90} But see Continental Ins. Co. v. Hancock, 507 S.W.2d 146 (Ky. App. 1974).

\textsuperscript{91} Other general information not relating to coverage but bearing on the working relationship between the insured and the insurer may be the legitimate subject of inquiry by the insurer, who must determine, together with the attorney, whether their tripartite relationship should continue. Moritz v. Medical Protective Co., 428 F. Supp. at 873.
and of the insured as to the coverage question, or if the full protection of the separate interests of the insured and the company requires inconsistent contentions which cannot be presented in a common defense of the pending matter, the insurance company or the insured should seek other procedures to resolve the coverage question.

If facts or information indicating to the attorney a lack of coverage for the insured should first come to the attention of the attorney after the trial of the lawsuit has begun, the attorney should at the earliest opportunity inform and advise the insured and the company of the possible conflicting interests of the insured and the company. The attorney should further seek to provide both the insured and the company with time and the opportunity to consider the possible conflict of interests and take appropriate steps to protect their individual interests.92

Under these standards, the attorney may inform the insured and the insurer of the nature and extent of the conflict and invite the insured to retain independent counsel at the company's expense.93 Counsel may not actively seek or develop information from such sources, however.94

Returning to the hypothetical, Attorney may pass on the general information imparted to him concerning the Insured's difficulties with the company. Attorney should be leery, however, of providing information to Insurer relating to Dr. Mensa's licensing problem or use of drugs, because Attorney obtained this information through his position as a fiduciary.

The consequences of disclosure of the insured's confidences and secrets are not limited to disciplinary proceedings. The attorney who abuses his client's confidences and secrets to provide his employer with a coverage defense may face the embarrassing prospect of later having to explain to the favored client why the court held that its coverage defenses were waived by the attorney's breach of his fiduciary duty. Moreover, he may expose himself to a claim for indemnification if the insurer passed up a favorable settlement in reliance on the attorney's negligent advice on the coverage defense, or suffered extracontractual liability as a result of the attorney's breach of duty to the insured.

For example, in Parsons v. Continental National American Group95 the insurer appointed an attorney to defend a "troubled" minor in a civil action for assault. The policy contained a standard exclusion for intentional acts of the insured, but the insurer had not invoked the exclusion, believing that the youth was mentally incompetent at the time the tort was committed. On the basis of confidential information obtained from the insured's medical records and from client interviews, the attorney decided that the youth knew that what he was doing was wrong. The attorney forwarded this information to the insurer and represented

92 See supra note 31.
93 Underwood, Conflicts and Malpractice: A Primer for Insurance Defense Counsel, 1 KY. DEF. COUNS. 2, 5 (1981); see also the AMERICAN LAWYER'S CODE OF CONDUCT (1980), which provides the following illustration of "unethical" attorney conduct:

1(1) A lawyer is retained by an insurance company to represent its insured, who is being sued in a personal injury action. Without the insured client's consent, the lawyer informs the insurance company of possible defenses of the company against the insured client under the policy. The lawyer has committed a disciplinary violation.

94 Employers Cas. Co. v. Tilley, 496 S.W.2d at 560-61.
the insurer in post judgment garnishment proceedings. Without discussing the possibility that the confidential information might have been discovered from another source, the Supreme Court of Arizona held that the insurer was estopped to deny coverage because of the attorney’s duplicity. In addition, the court concluded that the carrier had failed to give due consideration to a proposed settlement offer within the policy limits, relying on the strength of the attorney’s advice with respect to the coverage defense. As a consequence of its failure to consider the interests of the insured, the carrier was required to pay the full amount of the judgment, an amount that exceeded its policy limits. Although the court was not presented with the issue of the attorney’s liability to the insurer, one can foresee an action by the insurer for the difference between the settlement offer and the policy limits, as well as the excess judgment.

D. Discovery

As court-reporting and lawyer’s fees increase, more insurance carriers will impose significant restrictions on defense costs. Indeed, some commentators perceive no problem with carrier imposed limitations on discovery, as long as the plaintiff’s claims do not exceed the policy limits. A restricted budget for the defense presents a dilemma for a defense attorney in a medical malpractice action. Even if a judgment will be paid in full by the carrier, the physician policyholder’s reputation is at stake, and his insurance premiums may increase drastically as a result of an adverse judgment. The disappointed physician will look for someone to blame for the adverse judgment, and if counsel’s pretrial preparation of the case suffered as a result of the carrier’s frugality, the insured may legitimately ask why he was never informed of the potential prejudice to his case. The physician can be expected to argue that if he had known of the carrier’s cost consciousness and understood the consequences, he would have hired independent counsel, or at least pressured the carrier for the active defense that he bargained for when he procured the policy of insurance.

In Bevenino v. Saydjari an automobile accident victim suffered multiple and near fatal injuries of the spine, torso, and head. He was taken to the emergency room of a local hospital where the doctor successfully treated all injuries, except for one eye, which he believed had been destroyed at the moment of impact. After the eye had been enucleated at another hospital, the patient sued the physician alleging that the eye could have been saved with prompt attention at the emergency room. By the time of the second pretrial conference the attorney selected by the malpractice carrier still had not spoken to the defendant physician about his version of the case. As a further “economy measure,” local counsel was appointed to represent the physician at a “foreign” deposition. Local counsel made no attempt to review the medical records with his client prior to the deposition, or otherwise prepare him for the rigors of the upcoming deposition.

96 Id. at —, 550 P.2d at 100; see also State Farm Mut. Ins. Co. v. Walker, 382 F.2d 548 (7th Cir. 1967) (the attorney procured statements from the insured demonstrating that he had lied to the insurer in his initial accounts of the accident, thereby allowing the insurer to invoke the “cooperation clause” as a policy defense); Employers Cas. Co. v. Tilley, 496 S.W.2d 552 (Tex. 1973).
98 Hutcheson, supra note 65, at 41.
100 Id. at 90. The physician’s trial attorneys were full-time employees of the carrier. Id. at 93 n.9.
The physician understandably “took refuge in the unprepared layman’s haven of ‘I don’t remember.”’

The deposition was presented at trial with disastrous results. Moreover, the carrier failed to present any other testimony from the doctor himself, or from any of the hospital personnel who could have described the critical nature of the situation confronting the defendant at the time emergency treatment was administered. Finally, the carrier spent no time preparing the expert witnesses that provided the core of the defense, and their testimony was ineffective.

The jury returned a verdict of $550,000, which the trial judge attributed to the carrier’s neglect:

Since the carrier is in the business of defending lawsuits, it must be presumed to know the necessary ingredients of a proper defense. We therefore can only conclude that the above described neglect was a function of the carrier’s deliberate decision not to spend enough money to have the lawsuit properly defended. . . . Presumably it has concluded that by taking all its assumed risks as a package it saves money in the end by skimping on preparation costs and hoping for settlements.

While the trial judge’s observations were made in passing on a motion for judgment n.o.v. in the medical malpractice action, the court could not resist giving its opinion on the propriety of legal action against the carrier and its appointed counsel. If the carrier’s budgetary restrictions threaten the adequacy of the defense, the attorney should let the insurer and the insured know, and withdraw if necessary, while taking care not to prejudice either client’s interests.

A restricted defense budget is not the only source of conflicts of interest that arise during discovery. For example, the attorney may be induced by the carrier to resist legitimate discovery requests to delay the proceedings or to obtain settlement leverage. In a recent case the attorney’s overly combative approach to discovery caused the plaintiff’s attorney to withdraw his client’s settlement offer and proceed to trial. The jury returned a verdict in excess of the policy limits, exposing both the carrier and the defense attorney to liability to the insured for extracontractual damages.

E. Settlement

Most personal injury lawyers, and probably all insurance defense lawyers, are familiar with the consequences of an insurer’s failure to exercise good faith toward its insured in deciding whether to try to settle an action in which the plaintiff’s claims exceed the policy limits. A “bad faith” refusal to settle the tort claim may result in the insurer’s liability not only for the policy limits, but also for any excess judgment above the policy limits. This extracontractual liability results from judicial recognition of a conflict of interest between the insured and the insurer. If the plaintiff’s claims exceed the policy limits, it is in the interest of the insured to have the case settled within the policy limits. As the plaintiff’s de-

101 Id. at 91.
102 Id. at 91-92.
103 Id. at 93.
104 Id. at 94 n.11.
106 The leading case is Grisci v. Security Ins. Co., 66 Cal. 2d 425, 426 P.2d 173, 58 Cal. Rptr. 13 (1967), in which a tort claimant obtained an assignment of the insured’s rights against the insurer, and recovered not only the excess judgment but also substantial damages for the insured’s mental suffering.
mand approaches the policy limits, however, the insurer has little to lose by try-
ing the case to a jury if it will not be liable for any excess. The insurer reserves
the power to control the defense and settlement. It must use this power in the
best interest of the insured and avoid exposing the insured to personal liability
for any excess as it resolves this conflict. The insurer’s excess liability resulting
from this particular conflict has become standard fare in law school courses and
Continuing Legal Education programs. Less consideration has been paid to de-
fense counsel’s liabilities arising from this conflict, and other conflicts of interest
that arise during the course of settlement negotiations.

Our hypothetical litigation presents an increasingly common scenario. The
plaintiff’s claims exceed the policy limits and threaten to expose the Insured phy-
sician to personal liability for any excess judgment or award of punitive damages.
The plaintiff’s counsel has discovered the policy limits and has offered to settle all
of his client’s claims within those limits. He has forwarded a “bad faith” letter
in the hope of gaining some psychological advantage over the Insurer, or to cre-
ate a record for subsequent litigation. What are Attorney’s ethical obligations
when he reviews the file and discovers the settlement demand?

Assume that Attorney contacted Insurer regarding the settlement demand.
He was told by Insurer’s claims manager that Dr. Mensa has given his consent to
a settlement of the claims against him, and that settlement is therefore author-
ized under the terms of the policy. As a matter of custom or practice, however,
Insurer will not settle any case in which the Advisory Committee of the State
Medical Society has reviewed the patient’s hospital records and determined that
there has been no malpractice. Relying on this custom, Insurer refuses to give
Attorney any settlement authority.

At this point a prudent attorney will follow the course of action set forth in the
Guiding Principles:

II. Claim Or Suit In Excess Of Limits

In any claim where there is a probability that the damage will exceed
the limits of the policy and the company has retained counsel to defend
the claim, or in any suit in which the prayer of the complaint exceeds the
limit of the policy, or in which there is an unlimited or indefinite prayer
for damages and a probability that the verdict may exceed the coverage
limit, the company or its attorney should timely inform the insured of the
danger of exposure in excess of the limit of the policy. The insured should
be invited to retain additional counsel at his own expense to advise him
with respect to that exposure. So long as the financial interest of the com-
pany in the outcome of the litigation continues, the company retains the
exclusive right to control and conduct the defense of the case.

See supra text accompanying note 37.

An attorney may not forward such correspondence directly to the insured or the insurer once a
defense attorney has been retained. MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 7-104 (1981).
However, if he believes that the defense attorney is not relaying settlement offers submitted in connection
with a pending suit, he may file a copy of the communication with the court. ABA Comm. on Ethics and
Rule 3.9 (1980), would permit a lawyer to send a written offer of settlement directly to an adverse party
seven days or more after that party’s attorney has received the same offer of settlement in writing.

See supra text accompanying note 17.

See supra note 31.
III. Settlement Negotiations In Claims Or Suits With Excess Exposure

In any claim where there is a probability that the damage will exceed the limit of the policy and the company has retained counsel to defend the claim, or in any suit in which it appears probable that an amount in excess of the limit of the policy is involved, the company or its attorney should inform the insured or any additional attorney retained by the insured at his own expense of significant settlement negotiations, whether within or beyond the limits of the policy. Upon request, the insured, or such additional attorney, shall be entitled to be informed of all settlement negotiations. The Company shall, upon request, make available to the insured or such additional attorney all pertinent factual information the company and its attorney may have for evaluation by the insured or such additional attorney.

It is obvious that neither Insurer nor Attorney may base its legal duty to Dr. Mensa on the findings of the medical review committee. The language of the hypothetical policy authorizes Insurer to settle if either the Insured or the medical committee consent. Once the Insured has authorized settlement, Insurer must consider all aspects of the case, including the probability of a verdict and its range if adverse, the strengths and weaknesses of all the evidence that may be presented by either side, the quality of the medical result, the experience and capacity of the opposing counsel, and the history of such litigation in the particular jurisdiction. In addition, both Insurer and Attorney have an obligation to forward the settlement offer to Dr. Mensa, advise him of the nature of the potential conflict, and recommend that he employ independent counsel to protect his interests. If Attorney fails to recognize these obligations suggested by the Guiding Principles, fails to recommend a reasonable settlement, or fails to utilize the full amount of his settlement authority, and the failure subjects either of his clients to an unnecessary loss, he may be held liable to Dr. Mensa or Insurer in subsequent malpractice litigation. Moreover, the Insured's malpractice claim is assignable. Plaintiffs in malpractice suits often obtain an assignment of the insured's rights in full or partial settlement of any excess judgment against the insured personally, and then pursue the defense attorney as an additional defendant. A prudent defense attorney therefore will follow the recommendations of the Guiding Principles when faced with the carrier's arbitrary methods, and document his efforts to fully inform both of his clients and secure their cooperation.

The necessity of keeping the insured informed and securing his cooperation takes on added significance in medical malpractice actions. Professional liability policies usually contain a provision restricting the insurer's power to settle a

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112 Id. at 849-50, 107 Cal. Rptr. at 608.
claim without the insured's consent. This policy feature permits the policyholder to reject a settlement that will blemish his reputation. Even a modest settlement of a nuisance claim may be against the physician's best interest, and he buys this privilege to reject settlement offers without concern for the carrier's exposure. Accordingly, a situation may arise in which the physician will reject what appears to be a reasonable settlement offer. Clearly, an attorney who concludes a settlement at the request of his billpaying client over the objection of the physician policyholder faces a risk of being named a codefendant in an action for injury to the insured's reputation, loss of an opportunity to file a countersuit, or for reimbursement for any increased insurance costs attributable to a wrongful settlement. Further, counsel may incur liability to the physician even if the insurer is authorized to settle over the insured's objection. In Rogers v. Robson, Masters, Ryan, Brumund and Belom the doctor alleged that defense counsel negotiated a nominal settlement at the request of the carrier even though discovery had produced no evidence of malpractice on his part and the doctor had expressed a desire to take the case to trial. The policy authorized settlement without the insured's consent if the insured physician was no longer a policyholder, which was the case. The court, however, ruled that the physician was entitled to a full disclosure of the insurer's intent to settle the litigation without his consent and contrary to his express instructions. The attorney's obligation to disclose the conflict of interest between the insurer and the insured arose from his attorney-client relationship with the plaintiff, and was not affected by the extent of the insurer's authority under the terms of the policy. Because the defense attorney did not disclose the conflict and advise the insured to release the carrier from its responsibilities and continue the defense at his own expense, the attorney was liable for any damages that the doctor could prove he suffered as a result of the attorney's malpractice.

One final case arising from the settlement of a medical malpractice case is noteworthy. In Zalta v. Billips a doctor and his medical group had been two of thirteen codefendants in a medical malpractice action. An attorney was retained by their insurer to represent them. After several conferences a settlement was concluded. Under the terms of the settlement neither the doctor nor the medical group were required to contribute any amount. The doctor, however, was erroneously named as a contributing defendant in a newspaper article concerning the litigation. He sued his former defense attorney alleging that the attorney's failure to announce in open court that his clients were not contributing to the settlement led to the adverse publicity and injury to his reputation. While the court held that the defense attorney is not an insurer of either his client's self-esteem or his public reputation, and that the attorney's failure to publicize the terms of the settlement was not the proximate cause of any damage to the attorney's former

118 Lieberman v. Employers Ins. of Wausau, 84 N.J. 325, 419 A.2d 417, 424-27 (1980). Only one reported case appears to place any qualification on the exercise of such a power. Transit Cas. Co. v. Spink Corp., 78 Cal. App. 3d 473, 144 Cal. Rptr. 488 (1978). The reported cases have given some substantive content to the concept of a wrongful settlement. Specifically, a jury will be permitted to find that the physician would have lost the case in any event. In such a case, the attorney's misconduct cannot be found to have been the proximate cause of any damages. See, e.g., 84 N.J. at —, 419 A.2d at 426-27.
119 81 Ill. 2d 201, 407 N.E. 2d 47 (1980).
client, the case serves as a final compelling illustration and reminder of the delicate position occupied by insurance defense attorneys in medical malpractice litigation.

IV. CONCLUSION

The attorney retained by an insurance company to defend a claim against its insured finds himself in a position that lawyers traditionally have avoided: the representation of multiple clients with potentially conflicting interests in a litigation context. The interrelationships among the insurer, the insured, and defense counsel are unique and the ethical problems that arise are not always apparent, even to prudent attorneys. This Article has suggested how conflicts might arise at various stages of the litigation of a hypothetical medical malpractice action in which an attorney has been retained to represent the interests of both the physician policyholder and his insurance carrier, and how such conflicts may give rise to legal malpractice claims instituted by one or the other of the attorney's clients. The problems discussed are recurring and are not limited to this particular type of insurance defense litigation.

While several commentators have contended that a new malpractice "crisis" is at hand, this Article suggests that a defense attorney's continued attention to developments in the area of "insurer's bad faith," more systematic monitoring of his litigation files, and strict adherence to available ethical standards should prove to be sufficient preventive medicine in this area of legal practice.