Unethical Indemnity Issues in Settlement Releases

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I. Introduction

Traditionally, the standard practice in New Hampshire when resolving medical malpractice and personal injury cases with outstanding healthcare liens had been for the plaintiff to warrant in the release that he or she would pay the lien and agree to indemnify the releasees in the event the lien was not paid. Recently, however, some insurers have begun seeking further assurances by insisting, as a condition of settlement, that plaintiff's attorneys agree to hold the releasees harmless and indemnify them against subrogation interests, reimbursement claims, and statutory liens asserted by government entities, private insurers, and/or healthcare providers.

Although the New Hampshire Bar Ethics Committee has not addressed the propriety of an attorney indemnification clause, every other ethics committee to consider this issue—of which we are aware—has concluded that it is improper for a plaintiff's attorney to sign a release requiring the attorney hold harmless and indemnify the releasees from claims arising out of the plaintiff's failure to pay liens.[1] This article will discuss these ethics opinions and the ethical rules that are implicated when an attorney agrees to such a settlement term.

II. Background

Medical malpractice and personal injury plaintiffs often have medical expenses that were paid by private health insurers or federal and state assistance programs. If the case settles, the release usually requires a plaintiff to resolve any valid liens and to indemnify and hold the defendant, the defense attorney, and the insurer harmless against claims made as a result of the plaintiff's failure to do so. If the plaintiff refuses to or is unable to pay those liens, lienholders may make a claim or file suit against the releasees who settled with the plaintiff.[2] Typically, the recourse for the releasees would be against the plaintiff who agreed to indemnify them against all lien claims. In an effort to minimize their risk and avoid subsequent litigation over liens, defendants, defense attorneys, and insurance carriers have begun insisting that the plaintiff's attorneys indemnify and hold them harmless against such claims. The rationale behind these demands is that the plaintiff's lawyer will ensure that the liens are paid before distributing the settlement proceeds to the plaintiff because he or she has a financial interest in resolving the liens.

At least 23 ethics committees in various jurisdictions, however, have found that plaintiff's attorneys cannot ethically agree to enter into such agreements. The majority of these committees have concluded that attorney indemnification clauses violate ethical rules that are identical and/or analogous to Rules 1.2(a), 1.7(a)(2), 1.8(e), and 2.1 of the New Hampshire Rules of Professional Conduct.

III. Rules 1.2(a) and 2.1 Violations

Ethics committees in Arizona, Maine, Montana, Indiana, Tennessee, Maryland, and Los Angeles County have determined that a settlement agreement that requires a plaintiff's lawyer to hold harmless and indemnify the opposing party from claims asserted against the plaintiff's settlement proceeds violates Rule 1.2(a) of the respective Rules of Professional Conduct in those states.[3] Like each of these jurisdictions, Rule 1.2(a) of the New Hampshire Rules of Professional Conduct provides, in part:

> (a)…a lawyer shall abide by a client's decisions concerning the objectives of representation, and, as required by Rule 1.4, shall consult with the client as to the means by which they are to be pursued.[4]

Accordingly, pursuant to Rule 1.2(a), a lawyer is required to abide by the client's decision on whether to accept a settlement offer. If the client chooses to accept an offer that is conditioned on his or her attorney agreeing to indemnify the defendant and the insurer, the indemnification demand may cause the lawyer to reject the settlement offer or dissuade the client from accepting it in order to protect his or her own financial interests. Such reluctance to incur personal liability as well as any concessions made to avoid potential liability interferes with the lawyer's obligation to effectuate the settlement that his or her client desires in violation of Rule 1.2(a).[5]

As the Arizona Ethics Committee explained:

> The insistence upon an attorney's agreement to indemnify as a condition of settlement, could, for example, cause the lawyer to recommend that the client reject an offer that would be in the client's best interest because it would potentially expose the lawyer to the payment of hundreds of thousands of dollars in lien expenses, or litigation over such lien expenses.[6]

Likewise, the Indiana Legal Ethics Committee noted that a lawyer's 1.2(a) obligation to his or her client "can be compromised by an offer that injects the attorney's own financial exposure into the process."[7]

Most lawyers will not risk financial exposure in order to secure a settlement for their clients. However, "[e]ven if the lawyer were willing to accept that potential financial burden, and even if the lawyer were ethically permitted to provide such financial assistance, such an agreement might compromise the lawyer's exercise of independent professional judgment and rendering of candid advice in violation of [Rule] 2.1."[8] Rule 2.1 of New Hampshire's Rules of Professional Conduct requires that an attorney exercise independent professional judgment and render candid advice in his or her representation of the client.[9] If a lawyer is forced to balance the benefits of the settlement to the client with his or her own financial risk, it is certainly possible that the lawyer's judgement would be clouded and his or her ability to provide advice compromised. Thus, taken together, Rules 1.2(a) and 2.1 of the New Hampshire Rules of Professional Conduct likely prohibit plaintiff's attorneys from agreeing to indemnify the releasees in their client's cases.

IV. Rule 1.7(a)(2) Violation

Nearly every ethics body to consider whether it is ethical for a plaintiff's lawyer to agree to an indemnification provision have concurred that entering into such agreements is improper because they have the potential to create conflicts of interest between the lawyer and the client in violation of Rule 1.7(a)(2). In New Hampshire, Rule 1.7(a)(2) provides:

> (a) …a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:
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> (2) there is a significant risk that the representation of one or more clients will be materially limited by…a personal interest of the lawyer.[10]

Attorney indemnity agreements may create a conflict between the attorney and his or her client because the client—who may desperately need the settlement money—may wish to accept a settlement offer that requires the lawyer to take on a financial burden that he or she is unwilling to, and cannot, assume.[11] The attorney's representation, therefore, would be materially limited by his or her own financial interest because the attorney would be inclined to reject the settlement to avoid personal liability for the client's debts. This point is emphasized in the American Bar Association's Comment [8] to Rule 1.7, which provides:

> Even where there is no direct adverseness, a conflict of interest exists if there is a significant risk that a lawyer's ability to consider, recommend or carry out an appropriate course of action for the client will be

> materially limited as a result of the lawyer's other responsibilities or interests.[12]

Furthermore, a conflict may arise if a plaintiff's lawyer enters into an indemnity agreement because "the client's failure or refusal to repay a lien could make the client's lawyer its guarantor."[13] Thus, if the plaintiff's lawyer is forced to defend and indemnify the opposing party against reimbursement claims, the lawyer's only recourse is to make a claim against his or her client.[14] In light of the potential conflicts that could arise, as well as the near-unanimous opinion among the other ethics committees, it is likely that the New Hampshire Bar Ethics Committee would also conclude that that an attorney's signing a personal indemnification agreement would violate Rule 1.7(a)(2) of the New Hampshire Rules of Professional Conduct.

V. Rule 1.8(e) Violation

Numerous ethics authorities have also found that attorney indemnity agreements are prohibited by their jurisdictions' equivalent to Rule 1.8(e) of New Hampshire's Rules of Professional Conduct[15], precluding attorneys from directly or indirectly providing financial assistance to their clients.[16] Indeed, "[a]greeing to act as an indemnitor, and hence ultimate guarantor of payment of a client's medical expenses, as a condition of settlement, indirectly provides financial assistance" that would otherwise be impermissible for an attorney to provide.[17] As the Los Angeles County Bar Ethics Committee observed, personal indemnification agreements by lawyers essentially provide the client with credit, which is undoubtedly a form of financial assistance.[18] Moreover, if the client ultimately defaults on payment of the liens, "the plaintiff will be benefited because the settling defendants would have little incentive to pursue the plaintiff to obtain its recovery."[19] Instead, the defendant would "much more readily look to the lawyer" who is more likely to have the financial ability to indemnify the defendant.[20]

While Rule 1.8(e) has an exception that allows attorneys to advance court costs and expenses of litigation, several ethics committees have found that indemnification clauses, which guarantee payment of the client's medical expenses, do not fall within this exception.[21] As the Illinois State Bar Association Ethics Committee explained:

> Providing a personal guarantee that lien/subrogation claims will be paid does not fall within the exception to Rule 1.8(d)[22] that "a lawyer may advance or guarantee the expenses of litigation." The Rule's reference to such expenses relates to those costs which are important to ensure that the litigation can be pursued. Providing a guarantee that liens or subrogation claims will be paid

> would be done in resolution of the litigation and has nothing to do with ensuring that the litigation may be properly prosecute. Therefore, such claims are not "expenses of litigation."[23]

VI. Conclusion

In the last few years, we have seen a proliferation of requests by defense counsel and insurance carriers for indemnity agreements. We have declined each request. Given the number of ethics authorities that have found entering into such agreements would be unethical, it is our view that doing so would also be a violation of the New Hampshire Rules of Professional Conduct. In the rare instances that this settlement term becomes an obstacle, we have allowed the insurer to pay the liens directly before issuing the settlement funds. We have also let our clients agree to escrow a portion of the settlement in an amount equal to or greater than the lien until the final lien is negotiated. Then, liens are paid from the escrow account and the balance is disbursed to the client.[24] Although these methods are more time consuming and may delay the disbursement of the settlement to the client, they help avoid failure at mediation and allow for the ethical resolution of the matter.

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[1] *See e.g.*, L.A. County Opinion No. 532 (2019); Or. Formal Op. 2015-190 (2015); Alaska Ethics Op. 2014-4 (2014); Ga. Adv. Op. 13-2 (2013); Mont. Ethics Op. 131224 (2013); Md. Ethics Op. 2012-03 (2012); Philadelphia Bar Association Professional Guidance Committee Op. 2011-6 (2012); Me. Ethics Op. 204 (2011); Supreme Court of Ohio Op. 2011-1 (2011); Fla. Bar Staff Op. 30310 (2011); Del. Ethics Op. 2011-1 (2011); Va. Legal Ethics Op. 1858 (2011); Okla. Ethics Op. 328 (2011); Utah Adv. Op. 11-01 (2011); Tenn. Formal Ethics Op. 2010-F-154 (2010); S.C. Ethics Adv. Op. 08-07 (2008); Mo. Formal Op. 125 (2008); Ill. Adv. Op. 06-01 (2006); Ind. Ethics Op. 1 of 2005 (2005); Ariz. Ethics Op. 03-05 (2003); Kan. Op. 01-05 (2001); Tenn. Formal Ethics Op. 97-F-141 (1998); N.C. State Bar Ethics Op. RPC 228 (1996); Wisc. Formal Ethics Op. E-87-11 (1987).

[2] *See e.g.*, 42 U.S.C. 1395y(b)(2(B)(ii) and 42 C.F.R. 411.24(e) & (g) (providing that Medicare has a "direct right of action" against a primary plan, entity, insurer, a physician, or lawyer that has received primary payment). In medical negligence and personal injury cases, the primary payer is usually the defendant's insurance carrier. *See also* R.S.A. 448-A:3 (1987); (providing that for one year from the date of settlement or payment of a plaintiff's claim, the party paying the settlement to the plaintiff, whether the third-party defendant or the attorney disbursing funds, remains liable for the properly noticed lien asserted by a hospital or home health care provider).

[3] *See* Mont. Ethics Op. 131224 (2013); Me. Ethics Op. 204 (2011); Ind. Ethics Op. 1 of 2005 (2005); Ariz. Ethics Op. 03-05 (2003).

[4] *See N.H. R. Prof. Conduct* 1.2(a).

[5] *See* Del. Ethics Op. 2011-1 (2011).

[6] Ariz. Ethics Op. 03-05 (2003).

[7] Ind. Ethics Op. 1 of 2005 (2005) (discussing agreements to indemnify against claims related to non-Medicare and Medicaid liens).

[8] Ariz. Ethics Op. 03-05 (2003); *see also* L.A. County Opinion No. 532 (2019) (explaining that the "lawyer's exercise of independent professional judgment on behalf of the client would be compromised, creating an impermissible conflict between the client's desire to finalize the settlement of the client's action and the lawyer's understandable reluctance to be liable for reimbursement payment or the costs of defending against such a claim").

[9] *See N.H. R. Prof. Conduct* 2.1 (providing "[i]n representing a client, a lawyer shall exercise independent professional judgment and render candid advice. In rendering advice, a lawyer may refer not only to law but to other considerations such as moral, economic, social and political factors that may be relevant to the client's situation).

[10] *See N.H. R. Prof. Conduct* 1.7(a)(2).

[11] *See* Utah Adv. Op. 11-01 (2011) (finding "[t]he tension between the layer, who wishes to obtain the best possible settlement for his client without putting herself personally on the line to the client's creditors, and client who may desperately want and need the settlement proceeds after what may be many months and perhaps years of litigation…is simply untenable"); Va. Legal Ethics Op. 1858 (2011) (explaining "[b]ecause the insurer will not agree to the settlement in the absence of an indemnification agreement, the lawyer's personal interest in avoiding liability for the debts of his client may be at odds with his client's desire to settle the case"); Ind. Ethics Op. 1 of 2005 (2005) (noting that "[a]cceptance of an otherwise favorable settlement that hinges on the attorney assuming uncertain personal exposure may render the attorney's interests in conflict with those of the client).

[12] American Bar Association Comment [8] to Rule 1.7(a).

[13] Ariz. Ethics Op. 03-05 (2003).

[14] *See* Alaska Ethics Op. 2014-4 (2014); Philadelphia Bar Association Professional Guidance Committee Op. 2011-6 (2012).

[15] *See N.H. R. Prof. Conduct* 1.8(e). Rule 1.8(e) provides:

(e) A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:

(1) a lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter.

[16] *See e.g.*, Supreme Court of Ohio Op. 2011-1 (2011) (noting that personal indemnification agreements by a lawyer "is, in essence, an agreement by the lawyer to provide financial assistance to the client. The lawyer is undertaking an obligation to pay the client's bills"); Va. Legal Ethics Op. 1858 (2011) (finding that indemnification agreements constitute improper financial assistance to the client because they obligate the lawyer to pay the client's debts); Ariz. Ethics Op. 03-05 (2003) (stating "[s]ince, under ER 1.8, an attorney cannot ethically provide financial assistance to a client by paying, or advancing, the client's medical expenses before or during litigation, an attorney cannot ethically agree, voluntarily or at the client's or Releasees' insistence, to guarantee, or accept ultimate liability for, the payment of those expenses").

[17] S.C. Ethics Adv. Op. 08-07 (2008).

[18] *See* L.A. County Opinion No. 532 (2019).

[19] Ill. Adv. Op. 06-01 (2006).

[20] *Id.*

[21] *See* L.A. County Opinion No. 532 (2019); Ga. Adv. Op. 13-2 (2013); Mont. Ethics Op. 131224 (2013); Philadelphia Bar Association Professional Guidance Committee Op. 2011-6 (2012); Va. Legal Ethics Op. 1858 (2011); Supreme Court of Ohio Op. 2011-1 (2011); Ill. Adv. Op. 06-01 (2006); Ind. Ethics Op. 1 of 2005 (2005).

[22] New Hampshire's equivalent to Illinois' rule 1.8(d) is rule 1.8(e).

[23] Ill. Adv. Op. 06-01 (2006).

[24] According to Montana's Ethics Committee, "[i]t is ethical for plaintiff's counsel to hold money in a trust account to resolve the lawyer's obligation to secure funds that are subject to a lien by a third party…" Mont. Ethics Op. 131224 (2013).