

NYCLA ETHICS OPINION NO. 731

TOPIC:

DISCLOSURE OF EXISTENCE OF INSURANCE COVERAGE IN SETTLEMENT DISCUSSIONS.

DIGEST:

A LAWYER WHO IS NOT OTHERWISE LEGALLY OBLIGATED TO DISCLOSE THE EXISTENCE OF INSURANCE COVERAGE NEED NOT REVEAL THE EXISTENCE OF INSURANCE COVERAGE PROVIDED THAT THE LAWYER MAY NOT KNOWINGLY MATERIALLY MISLEAD ADVERSE COUNSEL AS TO THE EXISTENCE OF APPLICABLE INSURANCE. IN ADDITION, A LAWYER SHOULD WITHDRAW AN INACCURATE PRIOR MATERIAL MISREPRESENTATION MADE DURING SETTLEMENT NEGOTIATIONS, WHETHER MADE BY THE LAWYER OR HIS OR HER CLIENT, ABOUT THE EXISTENCE OF INSURANCE.

CODE:

DR 7-102; DR 4-101; DR 1-102 (A) (4).

QUESTIONS:

A: Where not otherwise required by law, does a lawyer have an ethical obligation to disclose the existence of insurance coverage when his client's ability to pay a judgment or settlement is at issue or reasonably could be considered to be an issue in settlement negotiations?¹

B. (1) Should a lawyer disclose the existence of insurance prior to settling a claim under circumstances in which the lawyer has herself introduced into settlement negotiations the existence of a liability insurance policy? (2) Would the answer be different if the source of the misconception is not the lawyer but the lawyer's client? (3) What if the source is not the client but some other third person?

OPINION:

In the course of settlement negotiations, adversary counsel has come to learn from another source (*e.g.*, a third party or a news story) that the inquiring attorney's client, a corporate defendant in a commercial arbitration, is on the verge of insolvency. Recognizing this fact, the claimant's counsel announces that she is prepared to accept a settlement of fifteen cents on the

¹ The question assumes the subject of insurance coverage has not been previously raised by either side.

dollar, an amount far less than the plaintiff is likely to garner at the hearing. Defense counsel is aware that there is an undisclosed insurance policy that would be more than adequate to satisfy the claim in full. Assuming that the claim is not in suit, or that it is brought in a forum that does not require its disclosure, inquiring counsel asks whether there is an ethical duty to disclose the existence of the insurance.

At the outset it should be noted that we find no provision in The Lawyer's Code of Professional Responsibility (or, for that matter, in the ABA's Model Rules) which specifically addresses the settlement process. DRs 1-102(A)(4) and 7-102 are, however, certainly relevant. DR 1-102 (A)(4) forbids engaging "in conduct involving . . . deceit or misrepresentation" and DR 7-102 (A)(5) precludes knowingly making "a false statement of law or fact." Puffery and exaggeration, which have long been prevalent in settlement negotiations, is not prohibited conduct *per se*.

The situation of negotiation in a pre-suit or administrative context raises unique ethical issues. While lawyers generally aspire to high standards of decency and professionalism, by convention a good negotiator will not disclose such crucial information as her client's bottom line or willingness to bear the burdens and uncertainties of litigation or verdict. It is customary and appropriate for negotiators to conceal how far their clients are prepared to go to resolve disputes amicably, but the ethical line is drawn short of making material misrepresentations or knowingly offering false statements by others.

The ABA Section on Litigation has released, in August 2002, its "Ethical Guidelines for Settlement Negotiation" (See ABA Website, www.abanet.org/litigation) "as a resource . . . to facilitate and promote ethical conduct in settlement negotiations." Section Four of the Guidelines is headed "Issues Relating to a Lawyer's Negotiations with Opposing Parties" and Guideline 4.1.1 alludes to the applicability of Model Rule 4.1 (the Model Rule counterpart of DR7-102(A)(5)) to settlement negotiations. The Model Rule differs from DR7-102(A)(5) by limiting its prohibition to false statements of "material" fact or law.

Comment [1] to Model Rule 4.1 notes that "generally" a lawyer "has no affirmative duty to inform an opposing party of relevant facts" but "[a] misrepresentation can occur if the lawyer incorporates or affirms a statement of another person that the lawyer knows is false." And that "can also occur by failure to act." These observations from the Model Rules are also instructive as a subtext to DR 7-102 (A) (5). Thus, it does not matter whether the lawyer is responding to a counter party's inquiry or the lawyer volunteers information about the client's financial means.

In general, a lawyer may not "conceal or knowingly fail to disclose that which the lawyer is required by law to reveal." DR 7-102 (A) (3). For example, in a federal lawsuit, disclosure of insurance information is self-executing, and must be disclosed automatically, "without awaiting a discovery request." Fed. R. Civ. P. 26 (a) (D). Yet under New York law, disclosure of insurance information, while available, may await formal demand, and can be waived by an adversary's failure to request it. CPLR 3101 (f); CPLR 3102. And some administrative and arbitration forums have no provision for such discovery. *See, e.g.* NASD Code of Arbitration Procedure; NASD Discovery Guide; New York Stock Exchange Arbitration Rules, Section 619. And many negotiations take place in the context of pre-suit negotiations.

An outright lie about “law or fact” is proscribed by DR 7-102, and a lawyer who affirmatively misrepresents the existence or extent of insurance coverage may be held civilly liable. *See, Slotkin v. Citizens Casualty Co.*, 614 F.2d 301 (2d Cir. 1979) (lawyer and insurance adjuster affirmatively denied, on the record, existence of excess insurance coverage, resulting in settlement of infant’s medical malpractice case within primary policy limits). *See also, In re McGrath*, 96 A.D.2d 267, 468 N.Y.S.2d 349 (1st Dep’t 1983) (suspension of attorney who negligently misrepresented the absence of excess coverage in *Slotkin*).

There is a line of authority, not directly analogous to our concern here, holding that an attorney should disclose the death of his client before accepting a settlement offer. *Kentucky Bar Association v. Geisler*, 938 S.W.2d 578 (Kentucky 1997); *Virzi v. Grand Truck Warehouse*, 571 F. Supp. 507 (E.D.Mich. 1983). As the American Bar Association has stated: “When a lawyer’s client dies in the midst of settlement negotiations of a pending lawsuit in which the client was the claimant, the lawyer has a duty to inform opposing counsel and the court in the lawyer’s first communication with either after the lawyer has learned of that fact.” ABA Formal Op. 95-397. Since the death of a client terminates or at least changes the attorney’s authority to act on behalf of the client, “a failure to disclose that occurrence is tantamount to making a false statement of material fact” within the meaning of the Model Rules. *Id.*

However, in the opinion of the Committee, there is a difference between the death of a client – which is a matter of public record and generally terminates an attorney’s ability to act on behalf of a client – and the disclosure of insurance information, which, under some circumstances, could be considered a secret or confidence. A client may have a confidentiality concern about disclosing the details of its finances, and may similarly wish to conceal the existence of an insurance policy. As a matter of general policy, a corporate client may not wish to disclose to the general public, and to the plaintiff’s bar in particular, the existence of insurance out of a desire not to encourage numerous frivolous suits. Disclosure of insurance information could affect a client’s ability to settle other cases.

Under DR 4-101, the duty to maintain the confidentiality of “secrets” is broader than the scope of confidences, as the former can pertain to information derived from sources other than the client. If the client requests that such information be kept confidential, or if it is likely to embarrass or injure the client, it is protected from disclosure by DR 4-101. *See, James Altman, The Secret About Secrets*, 224 N.Y.L.J. 24 (7/14/2000), p. 24, col. 1.

Nonetheless, the Code provides that a lawyer *may* reveal a clients’ confidences and secrets to the extent required to correct a materially inaccurate representation “previously given by the lawyer and believed by the lawyer still to be relied upon by a third person. ...” DR 4-101 (C) (5). As this Committee has previously opined, a lawyer may withdraw an inaccurate representation which he previously made and was relied upon by his adversary in the course of negotiations. NYCLA Eth. Op. 686 (1991), 1991 WL 755942. As this Committee wrote: “Thus, the lawyer may inform the party to whom the statement was made that the statement is withdrawn, even if the client objects on the grounds that disclosure will be detrimental to the negotiations.” 1991 WL 755942 *1.

It is the opinion of the Committee that it is not necessary to disclose the existence of insurance coverage in every situation in which there is an issue as to the available assets to satisfy a claim or pay a judgment. While an attorney has a duty not to mislead intentionally, either directly or indirectly, we believe that an attorney is not ethically obligated to prevent an adversary from relying upon incorrect information which emanated from another source. Under those circumstances, we conclude that the lawyer may refrain from confirming or denying the exogenous information, provided that in so doing he or she refrains from intentionally adopting or promoting a misrepresentation.

CONCLUSION:

A lawyer has no duty in the course of settlement negotiations to volunteer factual representations not required by principle of substantive law or court rule. Nor is the lawyer obliged to correct an adversary's misunderstanding of the client's resources gleaned from independent, unrelated sources. However, while the lawyer has no affirmative obligation to make factual representations in settlement negotiations, once the topic is introduced the lawyer may not intentionally mislead.

If a lawyer believes that an adversary is relying on a materially misleading representation attributable to the lawyer or the lawyer's client, or a third person acting at the direction of either, regarding insurance coverage, the lawyer should take such steps as may be necessary to disabuse the adversary from continued reliance on the misimpression created by the prior material misrepresentation. This is not to say that the lawyer must provide detailed corrective information; only that the lawyer may not permit the adversary to continue to rely on a materially inaccurate representation presented by the lawyer, his or her client or another acting at their direction.