

KENTUCKY BAR ASSOCIATION

Ethics Opinion KBA E-404

Issued: June 1998

Law Firm represents and defends insureds under liability policies issued by Insurance Company. Insurance Company sends Law Firm's bills to an outside audit company, which is not affiliated with or an employee of Insurance Company. Audit Company makes recommendations to Insurance Company as to payment or nonpayment. Law Firm's bills contain detailed information about the services performed pursuant to the representation. In addition to this, Insurance Company has asked Law Firm to allow Audit Company to review the detailed bills which Law Firm has sent to other insurance companies, unrelated to Insurance Company.

Question 1: Would Law Firm's submitting its Insurance Company bills directly to Audit Company, rather than to Insurance Company, without the law firm's obtaining the fully informed consent of the insured, violate the Kentucky Rules of Professional Conduct?

Answer: Yes

Question 2: Would the Law Firm's submitting other clients' bills to Audit Company violate the Kentucky Rules of Professional Conduct?

Answer: Yes

References: KRPC 1.8(f)(3), 1.5(b); South Carolina Op. 97-22; Utah Op. 98-03 (1998); For The Defense, *Outside Audits and Defense Counsel - Ethical Considerations 4* (February 1998); United States v. MIT, 129 F.3d 681 (1st Cir. 1997); June 1998 DRI *For The Defense*, pages 4-5.

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Rule 1.8(f) provides that "[a] lawyer shall not accept compensation for representing a client from one other than the client unless: (1) such compensation is in accordance with an agreement between the client and the third party or the client consents after consultation; (2) there is no interference with the lawyer's independence of professional judgment or with the lawyer-client relationship; and (3) information relating to representation of a client is protected as required by Rule 1.6."

Rule 1.5(b) states that "[w]hen the lawyer has not regularly represented the client, the basis or rate of the fee should be communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation."

The basis or rate of the lawyer's fees is a matter of contract between the client or the third-party payor. Ordinarily, no question of ethics arises. But see, American Insurance Association v. KBA, 917 S.W.2d 568 (Ky. 1996). We assume, arguendo, that a third-party payor may review the lawyer's charges and conduct appropriate billing

“audits.” We also assume that the insurer may delegate the auditing function to a third party. We also assume that the insurer and the insured may [subject to regulatory review] modify the insurance contract to accommodate their respective interests.

On the other hand, the relationship between the insured and the defense lawyer is an attorney-client relationship governed by the Kentucky Rules of Professional Conduct. Historically, lawyers have sent their bills to the insurer for payment. The disclosure of billing information to the insurance company would have been routine, and “impliedly authorized” by the insurance contract and the nature of the representation.¹ See KRPC 1.6(a). However, these bills are now quite detailed, and contain information about the nature of the legal services performed, information about legal research conducted, and information which could contain strategic decisions made regarding the handling of the case. Sometimes legal bills could include information which would tend to embarrass the insured client. It is reported that some “audit” firms are developing databases from the insureds’ billing information “to serve larger interests.”²

The Committee agrees with the views expressed in South Carolina Bar Op. 97-22 that a lawyer may submit his or her bills directly to a third-party auditing firm only with the informed consent of the insured as well as the insurer, and only so long as the lawyer reasonably believes that doing so will not substantially and adversely affect the representation of the insured client.

Likewise, the Law Firm may not ethically release other clients’ billing records to the audit company in the absence of full and informed consent of the clients. We note in passing that obtaining the full and informed consent of “other clients” could prove problematic given the absence of benefit to such clients and the potential effects of misuse or abuse of such information. Full disclosure would presumably include an elaboration of the type of information that might be found in the records, and the potential legal effects of disclosure, including waiver of privileges and work product. See, e.g. **United States v. MIT**, 129 F.3d 681 (1st Cir. 1997).

Note to Reader

This ethics opinion has been formally adopted by the Board of Governors of the Kentucky Bar Association under the provisions of Kentucky Supreme Court Rule 3.530 (or its predecessor rule). Note that the Rule provides: “Both informal and formal opinions shall be advisory only; however, no attorney shall be disciplined for any professional act on his part performed in compliance with an opinion furnished to him on his petition, provided his petition clearly, fairly, accurately and completely states his contemplated professional act.”

¹ Caveat: the Committee has noted that some information may not be disclosed to the insurer without the insured’s express consent. See, e.g., KBA E-340 (1990) (discussing conflicts and coverage disputes).

² Letter of concern from Washington Defense Trial Lawyers’ Association to Washington State Bar dated November 18, 1996, on file with the KBA. Compare the concerns about patients’ medical information in an era of “managed care.”