Ethical Issues in Class Action Settlements

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A defendant contemplating entering into a class action settlement is generally focused on important goals: closure; minimizing the number of opt-outs from the settlement; preventing new claims from arising; an affordable price tag; and a deal that will withstand legal scrutiny. In an ideal world, the defendant would like to achieve a settlement that resolves all (or all of the significant) existing cases, prevents future cases, and does not "break the bank." There are of course many tactical, legal and financial issues that often arise to prevent a defendant from achieving some or all of these goals in a class action settlement. But there can be ethical obstacles as well. This paper attempts to explore some of the ethical issues that may arise in connection with class action settlements.

I. Communications with Potential Class Members

Defense counsel may wish to communicate with putative class members for a variety of reasons, some of which are wholly unrelated to the putative class action. For example, in the context of employment litigation, defense counsel may need to communicate with employees regarding the client's ongoing business activities or litigation wholly unrelated to the subject matter of the putative employment litigation class claims. It is axiomatic that the ethics rules prohibit communicating with persons represented by counsel on the subject of that representation without the permission of their counsel or court approval. Model Rules of Prof'l Conduct R. 4.2 (2009) (hereinafter "Model Rule") ("In representing a client, a lawyer shall not communicate about the subject of the representation with a person the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized to do so by law or a court order.").[1] When defense counsel makes such communications with employees it knows to be putative class members, it is especially important to communicate to the employee that he or she represents the company, not the employee, in order to avoid the possibility of the claimant misunderstanding the defense counsel's relationship or creating an attorney-client relationship with the employee, which could lead to potential or actual conflicts of interest.

If, however, defense counsel wish to communicate with putative class members directly about the subject of the putative class action or to try to settle the claims of individual putative class members, can counsel do so ethically? Defense counsel can, but should be advised that precaution is advisable. When a

[1] *See also* Model Code of Prof'l Responsibility DR 7-104(A) and (A)(1) (1980) (hereinafter "Disciplinary Rule") ("During the course of his representation of a client a lawyer shall not: (1) Communicate or cause another to communicate on the subject of the representation with a party he knows to be represented by a lawyer in that matter unless he has the prior consent of the lawyer representing such party or is authorized by law to do so.").

class action is filed, the question is raised whether such putative class members are actually represented by class counsel. There is a split of opinion regarding this ethical issue.[2] Under the majority view, the ethical prohibition against contacting represented parties on the subject matter of the representation is not implicated in the context of putative class members who are not known to be represented by individual counsel. *See* The Restatement (Third) of Law Governing Lawyers § 99 cmt. l; *see also* ABA Comm. On Ethics and Prof'l Responsibility, Formal Op. 07-445; Michigan Comm. on Prof'l and Judicial Ethics, Op. RI-219 (1994). The minority view, however, is that such putative class members are actually represented by class counsel. For example, Rule 4.2 of the Pennsylvania Rules of Professional Conduct has been applied to bar defense counsel from contacting current and former employees regarding the subject matter of the lawsuit prior to a decision on certification (unless done through formal discovery). *See* Philadelphia Bar Ass'n Prof'l Guidance Comm., Ethics Op. 2009-1 (citations omitted). Complicated issues are presented when multiple, overlapping putative class actions in various jurisdictions have been filed. *Id.*

Defense counsel considering whether to contact putative class members, before class certification and the expiration of the opt-out opportunity, on the subject-matter of the class action should carefully consider the applicable law and ethics rules of the applicable jurisdiction(s) before making such contact. As noted above, there may be situations in which a minority jurisdiction's ethics rules could potentially apply. Accordingly, defense counsel may wish to seek the protection of court approval before making such communications in all the relevant court(s) in which a class action allegedly covering a putative class member's claims is(are) pending. *See* Michael J. Steiner & Kurt B. Opsahi, *Attorney Communications in Class Action Litigation*, 115 Banking L. J. 430, 442 (1993) (courts generally allow pre-certification communications by defense counsel with putative class members as long as communications involve legitimate efforts to settle the case and do not involve threats, suspect motives, or coercion). In addition, defense counsel should also be mindful of informing the putative class member that the lawyer represents the defendant and not the putative class member. *See* Model Rule 4.3. Further, it may be good practice to document all such communications.

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[2] These opinions specifically address the ethical implications of defense counsel contacting putative class members. They do not purport to address issues of substantive law that could impact whether defense counsel is permitted to contact putative class members before class certification and the opportunity to opt-out has expired, such as principles of principal and agent, Rule 23 of the Federal Rules of Civil Procedure and the First Amendment to the United States Constitution.

II. Ethical Issues in Representing Claimants in Class Actions

A. Limiting Representation of Both Class Members and Class Members

Obtaining closure in a class action settlement also depends on capturing all the relevant existing and potential cases so that they will not be litigated in the future. One of the concerns faced by defendants in doing some class action settlements is that plaintiffs' lawyers may "cherry pick" their best cases to "opt-out" of the class action settlement, thus depriving the defendant of one of the main incentives to agree to a class action settlement -- to achieve finality and rid itself of the most troublesome cases.

In class action settlements, defendants typically retain the right to "walk away" from the settlement if a threshold number or percentage of all class members, or particular sub-classes, opt-out of the class action settlement -- or even without a specific number of opt-outs, with a "walk away" right entirely at defendants' discretion. Ethics rules require that plaintiffs' lawyer make a recommendation to each client whether or not to opt-out based solely on what is in the best interests of that client. *See* Model Rule 1.7(a)(2); *see also* Model Rule 1.7 cmt. 33. However, the dynamics of a class action settlement with such walk-away provisions could encourage some lawyers to recommend that their clients opt-out in order to either "blow up" the settlement or at least to gain the leverage that results from the potential to do so. Conversely, class counsel who support the class action settlement could be motivated to discourage opt-outs, even when it may be in the best interests of particular clients to do so.

As a practical matter, class action settlement should of course contain some provisions to ensure a minimal comfort level that the plaintiffs' lawyers are acting ethically with regard to class members who choose to participate and those who choose to opt-out of the settlement. A measure of protection provided by the class action settlement is the notice provision, which requires the best practical notice to class members of the terms of the settlement.

One of the provisions in some class action settlements that is sometimes subject to criticism is the requirement that plaintiffs' lawyers, to the extent ethically permissible, withdraw from representing plaintiffs who opt-out of the settlement or perhaps seek to challenge collaterally the settlement before participating class members have received their benefits. Although this may appear to be problematic, there is an argument that this provision merely codifies the existing ethics rules. The ethics rules clearly allow for the representation of multiple plaintiffs by the same attorney, even where a conflict of interest may arise. *See, e.g.*, Model Rule 1.7. When such a conflict does arise, the plaintiffs' counsel can continue to represent both plaintiffs when the lawyer "reasonably believes that the lawyer will be able to provide competent and diligent

representation to each affected client" and "each affected client gives informed consent, confirmed in writing." Model Rules 1.7(b)(1) and (4). There is an argument that an incurable conflict arises in certain contexts.

First, prior to the expiration of a defendant's "walk away" right, a plaintiff's lawyer who advises some class members to opt-out of the settlement could injure the class members who want to participate in the settlement by causing the defendant to exercise its "walk away" right, thus depriving the class members who wished to participate in the settlement from the opportunity to do so.

Second, at any time before participating class members actually receive benefits under the class, class members who wish collaterally to attack the settlement threaten to undo the settlement altogether, thus also depriving the class members who wished to participate in the settlement from the opportunity to do so. When such conflicts arise, there is nothing in the ethics rules that necessarily requires the withdrawal from all clients. Therefore, it can be permissible for the lawyer to continue representing the class members for whom the objective of their representation is the settlement of their claims -- *i.e.*, those who participate in the class action settlement -- or those whose objective is to litigate them.

B. Prohibiting Plaintiffs' Counsel from Pursuing Collateral Attacks on the Settlement or Those Asserting Latent Diseases

It is clear that under the applicable ethics rules defense counsel cannot ask, and plaintiffs' counsel cannot agree, to an arrangement that prohibits the plaintiffs' counsel from representing future clients in exchange for monetary compensation. Model Rule 5.6 states that, "A lawyer shall not participate in offering or making… (b) an agreement in which a restriction on the lawyer's right to practice is part of the settlement of a client controversy."[3] A lawyer's right to practice is restricted when an agreement expressly prohibits a lawyer from agreeing not to represent other plaintiffs in the future, as a lawyer is prohibited "from agreeing not to represent other persons in connection with settling a claim on behalf of a client." Model Rule 5.6(b) cmt. 2. This ethical prohibition against foregoing future representation in explicit exchange for consideration is generally

[3] This prohibition is not limited to the Model Rules. Disciplinary Rule 2-108(B) states that, "In connection with the settlement of a controversy or suit, a lawyer shall not enter into an agreement that restricts his right to practice law." Similarly, Rule 1-500(A) of the California Rules of Professional Conduct states that, "A member shall not be a party to or participate in offering or making an agreement, whether in connection with the settlement or a lawsuit or otherwise if the agreement restricts the right of a member to practice law."

accepted, with one notable exception,[4] in non-binding ethics guidelines[5] and opinions.[6] Thus, in the context of a class action settlement, defense counsel could not, for example, ask a plaintiffs' lawyer who is negotiating or supporting the class action settlement to refrain from taking on future claimants, such as opt-outs, participating class members who subsequently attempt collaterally to attack the class action settlement or claimants who seek to assert claims in the future on the basis that such injuries were latent disease.

The language in the various versions of the rule suggests that an agreement to restrict opposing counsel *might* not be ethically prohibited by Model

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[4] *See* Va. State Bar Standing Comm. on Legal Ethics, Op. No. 1715 (1998). A provision of the settlement agreement in an employment discrimination case for a plaintiff's counsel to provide consulting services to a defendant was determined not to violate the ethics rules. In that case, the plaintiff was aware of and wanted her counsel to enter into the agreement because she had brought the litigation to improve the conditions to the company, as a term of the settlement the plaintiff agreed to forego ever-seeking employment from the same company, and her counsel did not have an expectation of representing other employees of that company in the future. *Id.*

[5] The American Bar Association's Section of Litigation prohibits a lawyer from "propos[ing], negotiat[ing] or agree[ing] upon a provision of a settlement agreement that precludes one party's lawyer from representing clients in future litigation against another party." Ethical Guidelines for Settlement Negotiations § 4.2.1 (Aug. 2002). Section 13(2) of The Restatement (Third) of Law Governing Lawyers contains a similar prohibition on a lawyer's right to practice law, stating, "In settling a client claim, a lawyer may not offer or enter into an agreement that restricts the right of the lawyer to practice law, including the right to represent or take particular action on behalf of other clients."

[6] *See*, *e.g.*, Wash. State Bar Ass'n Rules of Prof'l Conduct Comm., Advisory Op. 2125 (2006); Or. State Bar Legal Ethics Comm., Formal Op. No. 2005-47; Fla. Bar Prof'l Ethics Comm., Ethics Op. 04-2 (2005); Va. State Bar Standing Comm. on Legal Ethics, Op. No. 1788 (2004); N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Op. No. 730 (2000); Alaska Bar Ass'n Ethics Comm., Ethics Op. No. 2000-2; Ass'n of the Bar of the City of N.Y. Comm. on Prof'l and Judicial Ethics, Formal Op. 1999 - 03; Wash. State Bar Ass'n Rules of Prof'l Conduct Comm., Advisory Op. 1850 (1999); Vt. Bar Ass'n Prof'l Responsibility Comm., Advisory Ethics Op. 95-11; Tex. Comm. on Prof'l Ethics, Op. 505 (1995); N.C. State Bar Ethics Comm., Ethics Op. RPC 179 (1994); Colo. Bar Ass'n Ethics Comm., Formal Op. 92 (1993); Cal. State Bar Standing Comm. on Prof'l Responsibility and Conduct, Formal Op. No. 1988-104; Michigan Comm. on Prof'l and Judicial Ethics, Op. CI-1165 (1986); Va. State Bar Standing Comm. on Legal Ethics, Op. No. 649 (1985); State Bar of N.M. Ethics Advisory Ops. Comm., Op. 1985-5.

Rule 5.6(b) and its equivalents if the agreement were not made "as part of" or "in connection" with the settlement of a case or controversy. Agreements made between counsel have generally been deemed to be made "in connection with" or "as part of" settlement agreements where the terms of the agreements were negotiated concurrently with the terms of the settlement of the clients' controversies.[7] Whether one could ethically negotiate an agreement not to take additional cases in a separate, subsequent transaction is an open question for which we have found no authority. Given the substantial authority disfavoring such agreements, it seems like a risky proposition even to try. However, as discussed below, there may be other ways ethically to attempt to achieve similar goals, though they are not without risk and are not necessarily of value.

1. Consulting Agreements with Plaintiffs' Counsel

One possible means of preventing future litigation, at least from a particular plaintiff's lawyer, would be for the defendant to hire that plaintiff's lawyer as a consultant once the class action settlement has been achieved. This might be an effective way of preventing a particularly talented or experienced plaintiff's lawyer from becoming counsel to other plaintiffs in the future. While this approach may raise some practical and, shall we say, "cultural" issues, it generally has been found not to violate ethical prohibitions. There is a strong argument that a defendant is not *per se* prohibited from employing a former plaintiff's attorney as a consultant on the same subject matter for which the attorney previously represented adverse plaintiffs. Ethics rules and the case law do, however, limit the manner in which a consulting relationship may be appropriately negotiated and impose other limitations on the retainer of a plaintiff's attorney by the defendant.[8]

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[7] *See In re Hager*, 812 A.2d 904 (D.C. 2002) (an agreement made by plaintiffs' counsel with the defendant to receive fees in exchange for not pursuing similar litigation in the future was determined to be a violation of Rule 5.6(b) of the District of Columbia Rules of Professional Conduct, even though one of the plaintiffs' lawyers argued that this deal was made in their capacity as individual lawyers, not as lawyers for a group of potential claimants); *see also In re Conduct of Brandt*, 10 P.3d 906, 917-19 n.10 (Or. 2000) (plaintiffs' counsel concurrently negotiated a retainer agreement for them to represent the defendant with the negotiation of the plaintiffs' claims. Even though the retainer agreement was held in escrow until the settlement of the plaintiffs' claims was finalized, the restriction on the plaintiffs' counsel's ability to practice law was deemed to have been made "in connection" with the settlement of the plaintiffs' claims in violation of Disciplinary Rule 2-108(B) of the Oregon Code of Professional Responsibility).

[8] It also has been suggested in academic literature that a defendant could potentially incur civil liability for such agreements. *See* George M. Cohen &

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As a general principle, consulting agreements effectively restrict an attorney's right to practice and are therefore likely subject to the limitations of Model Rule 5.6(b).[9] The Committee Notes to Section 4.2.1 of the ABA's Ethical Guidelines for Settlement Negotiations cite a consulting agreement as an example of an arrangement calculated indirectly to achieve the desired result of conflicting out a plaintiff's attorney from representing similarly situated plaintiffs in the future. However, agreements that restrict an attorney's right to practice are not *per se* prohibited. In a leading treatise, it was noted that a consulting agreement, while having the same preclusive effect in practice as a restrictive provision in a settlement agreement due to the operation of conflict of interest rules, is in a form consistent with the ethics rules. *See* Geoffrey C. Hazard, Jr. & W. William Hodes, 2 The Law of Lawyering § 47.6, at 47-10 (2d ed. Supp. 2002).

As indicated *supra*, Model Rule 5.6(b) prohibits an attorney from entering into an agreement that restricts the lawyer's right to practice when the agreement is in connection with the settlement of a client's controversy. Exactly what "in connection with" or "as part of" a settlement means is a matter of debate. As a general rule, however, defense counsel should refrain from raising the possibility of entering into such consulting agreements until after the class action settlement has received final court approval.[10] As a practical matter, however, if the class

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Susan P. Koniak, *Under Cloak of Settlement*, 82 Va. L. Rev. 1051 (1996) (arguing such behavior, if intended to "buy out" plaintiffs' counsel, could give rise to liability under antitrust and unfair competition laws. The theoretical possibility of antitrust issues arising under such agreements is beyond the scope of this paper.

[9] A defendant creates the conflict of interest between a plaintiff's former attorney and future claimants arising out of the same transaction by hiring the former plaintiff's attorney to advise the defendant on the suit's subject matter after the attorney has finished representing the plaintiffs. *See* Yvette Golan, *Restrictive Settlement Agreements: A Critique of Model Rule 5.6(b)*, 33 Sw. U. L. Rev. 1, 9 (2003).

[10] In *Florida Bar v. St. Louis, Jr.*, 967 So. 2d 108 (Fla. 2007), a plaintiffs' attorney who negotiated a retainer agreement was found to have violated Rule 4-5.6(b) of the Rules Regulating the Florida Bar by entering into a retainer agreement with the defendant after the dollar amounts for a group settlement were reached, but before the settlement agreement was drafted, even though the retainer agreement provided that the plaintiffs' counsel's engagement would not begin until after it had completed work for its clients. The Florida Supreme Court found the engagement agreement was a sham, as neither plaintiffs' counsel nor defendants ever expected to perform unspecified work to earn the approximately $6.5 million fee. The plaintiffs' attorney violated other ethics rules by failing to report the engagement agreement to the court when reporting the settlement, and failing to

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action settlement takes years to receive final approval and to be implemented, it will be difficult to enter into a consulting agreement within a reasonable timeframe, thus leaving such plaintiffs' counsel a sufficient amount of time to obtain other clients.

Even if the practice restrictions are imposed only on the plaintiffs' counsel, ethics rules are implicated for the defendant's counsel who participates in making a restrictive agreement in connection with or as part of the settlement of the underlying claims. *See Adams v. BellSouth Telecomm, Inc.*, 2001 WL 34032759 at *2-9 (defense counsel found to have violated applicable Florida ethics rules by negotiating and agreeing to a consulting agreement concurrently with the settlement of all the plaintiffs' claims, even though the consulting agreement only restricted the right to practice law of the opposing party's attorneys). In an ethics opinion, the ABA Committee on Ethics and Professional Responsibility found that the scope of the prohibition in Model Rule 5.6(b) extends to attorneys who offer or require a restriction on a lawyer's right to practice in connection with the settlement of a client controversy because Model Rule 5.6(b) operates in conjunction with Model Rule 8.4(a). Formal Op. 371 (1993); *see also* Joanne Pitulla, *Co-Opting the Competition: Beware of Unethical Restrictions in Settlement Agreements*, 78 A.B.A. J. 101 (Aug. 1992).

There is a scarcity of decisional law or persuasive analysis applying Model Rule 5.6(b) where attorneys preliminarily discuss the prospect of entering into a consulting agreement concurrently with the settlement of the pending controversy, but do not affirmatively offer to enter into a consulting agreement or discuss the details of any such agreement until after a settlement has been reached. Even if a particular jurisdiction's equivalent of Model Rule 5.6(b) is interpreted as not prohibiting such discussions, an attorney is probably required to inform every present client during the settlement negotiations of the concurrent consulting agreement discussions and obtain all the present clients' informed consent in writing. *See* ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 400 (1996). In addition, when submitting a proposed class action settlement to the court, counsel for both the plaintiffs and defendants may be under a duty of candor to report these discussions. *Cf. St. Louis, Jr.*, 967 So. 2d at 114. This

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report it to clients when discussing whether they would accept the defendants' offers. The Florida Supreme Court disbarred the plaintiffs' counsel, and, in separate opinions, imposed other penalties on various members of his firm, depending on their awareness of the engagement agreement. *See Fla. Bar v. Rodriguez*, 959 So. 2d 150 (Fla. 2007); *see also Fla. Bar v. Friedman*, 940 So. 2d 428 (Fla. 2006) (table citation); *Fla. Bar v. Ferraro*, 839 So. 2d 700 (Fla. 2003) (table citation).

could be deemed a type of "side deal" that is really part of the class action settlement, and could heighten judicial scrutiny of the proposed class action settlement.[11]

Even after an attorney completes representation of a client in the matter, the attorney may still be required to obtain the consent of the former client in order to enter into a consulting agreement with the defendant. *See* Model Rule 1.9(c)(2) ("A lawyer who has formerly represented a client in a matter or whose present or former firm has formerly represented a client in a matter shall not thereafter… (2) reveal information relating to the representation except as [Model] Rule 1.6 or 3.3 would permit or require with respect to a client.").[12] If not disclosing the former client's confidential information would pose a "significant risk" that the consultant's representation of the defendant would be materially limited, then a concurrent conflict of interest may exist. *See* Model Rule 1.7(a)(2). The former plaintiff's attorney can still represent the defendant if informed consent is given, by both the former and the present clients, and the attorney reasonably believes competent and diligent representation can still be provided. *See* Model Rules 1.7(b)(1) and (4).

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[11] In addition to ethical concerns, consulting agreements and underlying settlement agreements may be subject to attack in a legal proceeding seeking to void enforcement. Courts differ on the enforceability of consulting agreements when Model Rule 5.6(b) is violated. At least one court has found that the failure to inform the settling plaintiffs of the consulting agreement required setting aside a settlement agreement and gave the plaintiffs a new right to opt-out because the plaintiffs lacked sufficient information when they agreed to the settlement agreement. *See Adams*, 2001 WL 34032759 at *12.

[12] One commentator has suggested that the former client's consent to his counsel's subsequent representation of the defendant may always be required before the plaintiffs' lawyer enters into the consulting relationship on the same or substantially related matter, implying that the there may be a positional conflict caused by the change of sides. *See* Golan, 33 Sw. U. L. Rev. at 9. There is strong authority, however, that this interpretation overstates the rule. A comment to the rule points out that even a lawyer who routinely handles a type of problem for a client is not later precluded from representing another client in a similar, though factually distinct, matter even if the subsequent position is adverse to the prior client's position. Model Rule 1.9, cmt. 2. A leading treatise suggests that adverse consequences from a positional conflict of interest are rarely sufficient to preclude later representation. Hazard, Jr. & Hodes, 1 The Law of Lawyering § 13.3, at 13-7 n.5 (2d ed. Supp. 2003). Accordingly, there is a reasonably strong argument that – unless non-disclosure of confidential information would limit the attorneys' representation of his or her new client – consent of the former client is unnecessary.

Another ethical issue related to consulting agreements between a defendant and a former plaintiff's counsel is that the agreement must result in a valid attorney-client relationship. An attorney is prohibited from collecting unreasonable or clearly excessive fees. Model Rule 1.5(a) states that, "A lawyer shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses." Disciplinary Rule 2-106(a) states that, "A lawyer shall not enter into an agreement for, charge, or collect an illegal or clearly excessive fee." Arrangements that merely add members of the plaintiffs' bar to a defendant's payroll without any real requirement of performing legal services for the defendant would therefore raise serious questions about the agreements' validity and ethical propriety. *See* Golan, 33 Sw. U. L. Rev. at 45; *see also St. Louis, Jr.*, No. S.C04-49 at p. 8.

Moreover, consulting agreements may not restrict the right of a lawyer to practice law after the employment relationship ends. Model Rule 5.6(a) prohibits a lawyer from participating in the offering or making of an employment agreement "that restricts the right of a lawyer to practice after termination of the relationship." Disciplinary Rule 2-108(a) prohibits a lawyer from being part of an employment agreement with another lawyer "that restricts the right of a lawyer to practice law after the termination of a relationship created by the agreement." A wholesale prohibition in employment agreements that prevent an attorney from ever suing the employer in relation to any action on behalf of any client violates Model Rule 5.6(b). *See, e.g.*, ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 400 (1996).

Provisions in consulting agreements that seek to expand by contract existing legal and ethical responsibilities, such as confidentiality and privilege, would also restrict a lawyer's right to practice in violation of Model Rule 5.6(a). *See id.* The Colorado Bar Association Ethics Committee found the following are examples of provisions that restrict a lawyer's right to practice by impairing the lawyer's independent judgment in future cases against the other party: forum and venue limitations, agreements not to subpoena certain records or witnesses, and obligations to turn over attorney work-product to opponent's counsel. Formal Op. 92 (1993). On the other hand, contractual provisions that merely codify ethical or legal duties, such as a nondisclosure provision of a settlement agreement, have been held not to restrict a lawyer's right to practice. *See* State Bar of N.M. Ethics Advisory Ops. Comm., Op. 1985-5.

2. Limiting or Eliminating Plaintiffs' Counsels' Fees

Although plaintiffs' lawyers may have multiple reasons to bring lawsuits against a defendant, one of the principle reasons plaintiffs' attorneys bring suit is for their own financial gain. Limiting or eliminating the fees that the plaintiffs' lawyer could recover in the future would be of great benefit to the defendant in achieving its settlement goals. While it is unlikely that a plaintiffs' lawyer would

voluntarily agree to reduce or limit future fees at the present, they might do so for the right price. If a plaintiffs' counsel was willing to entertain such an offer, could this be done within the ethics rules?

The Professional Ethics Committee of the Texas Supreme Court considered the issue of whether a law firm can, as part of a settlement of a lawsuit, agree "not to share fees with anyone in the future with respect to lawsuits or claims brought against the opposing party." The Committee held that such an outright agreement would be a limitation on the practice of law and would be in violation of Rule 5.06(b) of the Texas Disciplinary Rules of Professional Conduct. *See* Tex. Comm. on Prof'l Ethics, Op. 505 (1995).

III. Third Party Payers

Defendants engaging in class action settlements routinely face the prospect of third party payers, both private and government, seeking to assert liens against the settlement benefits made to class members. Defense counsel face ethical issues in protecting their clients from liability to the third-party payers.

A. Medicare

Defendants, and their counsel, negotiating class action settlements involving claims for personal injury, are likely aware of the potential exposure they face when settling with claimants who are eligible to receive Medicare[13] benefits and who do not actually reimburse Medicare for related payments it has already made or obtain a waiver of those costs.[14] Under the Medicare Secondary Payer Act ("MSPA"), codified at 42 U.S.C. § 1935y(b), the federal government

[13] Medicare, established in 1965 as part of the Social Security Act, was originally intended to provide federal health care coverage to individuals who were 65 years or older. The Medicare program was expanded in 1972 to include coverage of certain persons under 65 years with long-term or permanent disabilities, including persons receiving Social Security Disability benefits and persons with end-stage renal disease.

[14] Under the Medicare statute, the responsibility of a primary payer, which includes, amongst others, a liability insurer and a self-insured entity, to reimburse Medicare is triggered by any settlement -- including a class action settlement -- even where the primary payer denies all liability and responsibility for the alleged injuries. A self-insured entity is "[a]n entity that engages in a business, trade, or profession shall be deemed to have a self-insured plan if it carries its own risk (whether by a failure to obtain insurance, or otherwise) in whole or in part." 42 U.S.C. § 1935y(b)(2)(A)(ii).

has a private right of action to recover from the primary payer an amount equal to double the amount owed to Medicare, even if the primary payer has already paid out the settlement funds to the claimant. In practice, this means that the primary payer could be responsible for paying three times the nominal settlement amount -- 100% of the settlement amount to the claimant and 200% of the settlement amount to the federal government.

By now, most defendants, and their counsel, participating in class action settlements for claims for personal injury are also likely aware that in 2007, the Medicare, Medicaid and SCHIP Extension Act of 2007 ("MMSEA"), codified at 42 U.S.C. § 1935y(b)(7) and (8), was enacted. The MMSEA requires all insurers (including liability, no-fault and workers' compensation insurers) as well as self-insured entities to determine whether a claimant is entitled to Medicare benefits, and, if so, to file an electronic report to the Centers for Medicare and Medicaid Services ("CMS"),[15] including detailed information about the claimant and the claim. Covered entities who fail to comply with these reporting requirements are subject to an imposition of a civil penalty of $1,000 per day of non-compliance with respect to each settling claimant. 42 U.S.C. § 1935y(b)(8)(E)(i).

Considering the significant financial penalties potentially at stake to a defendant who participates in a class action settlement, defense counsel would be ethically required by the rules of competency to inform their clients about the requirements risks of non-compliance before finalizing a class action settlement that involves payment of claims for personal injuries. *See* Model Rule 1.1; *see also* Disciplinary Rule 6-101. Since Medicare benefits are only available for medically related coverage, it would seem that defense counsel's basic ethical requirement of competent representation would not extend to informing their clients about Medicare reporting requirements when claims for medical costs are not even made. However, the CMS has determined that a covered entity must report a settlement whenever the injured party is a Medicare beneficiary and any medical claims are released.[16] Thus, counsel for a defendant must be cautious

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[15] CMS is an agency within the Department of Health and Human Services that administers Medicare, Medicaid and other health related programs. CMS' website address is http://www.cms.gov/.

[16] CMS has indicated that settlements must be reported for Medicare beneficiaries where all "medicals are claimed and/or released or the settlement, judgment, award, or other payment *has the effect of* releasing medicals." MMSEA Section 111, Medicare Secondary Payer Mandatory Reporting, Liability Insurance (Including Self-Insurance), No-Fault Insurance, and Workers' Compensation, User Guide, Version 3.1 (issued July 12, 2010) at §§ 6 and 11.10.2 (emphasis added) (available for downloading at

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that the use of broad language releasing all medical claims, even if the settlement is for claims unrelated to medical injuries, can trigger the defendant's Medicare reporting obligations, and if not addressed, open the defendant to not insignificant exposure to fines.[17]

B. Indemnification from Plaintiffs' Counsel

A defendant entering into a class action settlement in any area in which claims for personal injury are released, even if they are not even claimed, may be held liable to third parties who assert liens that the settling claimants do not satisfy. It is often standard practice for settling class members to indemnify defendants for claims against defendants by third parties. However, such indemnification is often of limited practical use, as the plaintiffs who do not satisfy their third-party liens are often the ones without any financial means who promptly spend their settlement funds. Additionally, there may be public relations issues associated with suing such plaintiffs.

Defendants have instead often tried to require the plaintiffs' counsel to indemnify them against third party liens. But is this ethical? The recently increasing number of non-binding ethics opinions addressing the issue uniformly state that it is unethical for a plaintiff's counsel to indemnify defendants or their counsel for the third party liens of their plaintiffs.[18] The primary concerns

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http://www.cms.gov/MandatoryInsRep/03_Liability_Self_No_Fault_Insurance_and_Workers_Compensation.asp#TopOfPage, as of July 1, 2011).

[17] Despite some references in teleconferences with CMS, at this time there is no exemption to exclude reporting settlements releasing medicals as to Medicare beneficiaries even if there are no medical claims alleged. *See*, *e.g.*, Transcript of April 6, 2011 Centers for Medicare and Medicaid Services Town Hall Teleconference for Liability Insurance (Including Self-Insurance), No-Fault Insurance, and Workers' Compensation Responsible Reporting Entities at p. 6; *see also* Transcript of March 9, 2011 Centers for Medicare and Medicaid Services Town Hall Teleconference for Liability Insurance (Including Self-Insurance), No-Fault Insurance, and Workers' Compensation Responsible Reporting Entities at pp. 4 - 5.

[18] *See*, *e.g.*, Me. Bd. of Overseers of the Bar, Prof'l Ethics Comm'n, Op. No. 204 (Apr. 22, 2011); Ala. State Bar Office of the Gen. Counsel, Formal. Op. 2011-01 (Feb. 25, 2011); Ohio Sup. Ct., Bd. Comm'rs on Grievances & Discipline, Advisory Op. 2011-1 (Feb. 11, 2011); N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Op. No. 852 (Feb. 10, 2011); Bd. of Prof'l Responsibility of the Tenn. Sup. Ct., Formal Op. 2010-F-154 Ass'n of the Bar of the City of N.Y. Comm. on Prof'l and Judicial Ethics, Formal Op. 2010-3; Advisory Comm. of the Sup. Ct. of Mo., Formal Op. 125 (2008); S.C. Bar Ethics Advisory Comm., Op. 08-07; Ill.

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expressed in the ethics opinions is that such indemnifications are essentially providing financial assistance to the client, which is prohibited under Model Rule 1.8(e)[19] and creates an unwaivable conflict of interest under Model Rule 1.7. The rationale for Model Rule 1.8(e), as stated in Comment 10 to Model Rule 1.8, is that providing such assistance would give lawyers too much of a financial stake in the litigation. This rule has been critiqued as based on notions of the historical doctrines of champtery, maintenance and barratry. In practice, providing such assistance produces at most a conflict of interest like those waivable under Model Rule 1.7(b). *See, e.g.*, James F. Moliterno, *Broad Prohibition, Thin Rationale: The "Acquisition of an Interest and Financial Assistance in Litigation" Rules*, 16 Geo. J. Legal Ethics 223 (Winter 2003); *see also* Danielle Z. Cohen, *Advancing Funds, Advancing Justice: Adopting the Louisiana Approach*, 19 Geo. J. Legal Ethics 613 (Summer 2006). Further, as even a few[20] of the ethics opinions prohibiting indemnification as to private defendants note, plaintiffs' counsel may already be obligated by statute to indemnify Medicare for the full amounts owed

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State Bar Ass'n Comm. on Prof'l Ethics, Advisory Op. 06-01; Ind. State Bar Ass'n Legal Ethics Comm., Op. No. 1 (2005); State Bar of Ariz. Ethics Comm., Op. 03-05; Kan. Bar Ass'n Ethics Advisory Comm., Op. 01-05 (2001); Wash. State Bar Ass'n Rules of Prof'l Conduct Comm., Advisory Op. 1736 (1997) (implicitly overruling Wash. State Bar Ass'n Rules of Prof'l Conduct Comm., Advisory Op. 1263 (1989), in which the state bar refused to rule on whether an attorney could ethically sign a hold-harmless agreement as part of a settlement because it was a legal, not an ethical, issue); N.C. State Bar Ethics Comm., Ethics Op. 228 (1996); State Bar of Wis. Prof'l Ethics Comm., Formal Op. 3-87-11; *cf.* Fla. Bar Prof'l Ethics Comm., Ethics Op. 70-8 (revised 1993) (not permissible for an attorney to give a letter of indemnification to a "bonding company on behalf of an out-of-state plaintiff when the terms of the proposed indemnification agreement require the attorney to reimburse the surety only after the plaintiff has failed to do so.").

[19] "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; and (2) a lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client."

[20] Ind. State Bar Ass'n Legal Ethics Comm., Op. No. 1 (2005) (noting that while "[c]ourts are divided as to whether Medicare and Medicaid benefits may be recovered from the claimant's attorney if not reimbursed from the settlement proceeds," the prohibition against indemnification by plaintiff's counsel applies to non-Medicare and Medicaid settlement agreements); Bd. of Prof'l Responsibility of the Tenn. Sup. Ct., Formal Op. 2010-F-154 at *5 n. 4.

by their clients to Medicare.[21] There has not been any practical reason advanced why plaintiffs' counsel's indemnification of Medicare poses any less harm, from an ethics viewpoint, than plaintiffs' counsel indemnifying a private defendant in a settlement.

However, in light of the overwhelming majority of non-binding ethics opinions prohibiting defense counsel from asking for, and plaintiffs' counsel from agreeing to, a settlement in which plaintiffs' counsel agrees to indemnify the defendants from third party claims, defense counsel who are licensed in a jurisdiction in which such an ethics opinion exists or in which such jurisdiction's ethics rules apply to either of the parties' counsel, should be extremely cautious about drafting a class action settlement with such an indemnification provision, and also should realize the likelihood that plaintiffs' counsel will refuse to accept such an indemnification agreement.

How, then, can defense counsel ethically protect their clients from third party claims for reimbursement? As already discussed, there is no such prohibition against requiring the plaintiff to indemnify the defendant, although that is often of questionable value. Defense counsel can require that plaintiffs' counsel warrant that they will adhere to the applicable ethics rules and opinions, such as Model Rule 1.l5 (addressing the safekeeping of client property and dealing with disputed funds), prohibiting them from disbursing disputed funds. However, those rules are limited in that they may not ensure the payment of those funds which do not presently rise to the level of a valid dispute or lien, but which could subsequently result in a claim against the defendant. Unfortunately, to the extent that counsel does not want to risk the ethical consequences of obtaining indemnification from plaintiffs' counsel, defendants' best measure to protect

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[21] In *Haro v. Sebelius*, 2011 U.S. Dist. LEXIS 58036 (D. Az.), the Secretary of the Department of Health and Human Services asserted that plaintiffs' counsel is amongst those entities that are required by 42 U.S.C. § 1935y(b)(2)(B)(ii) ("A primary plan, and an entity that receives payment from a primary plan, shall reimburse [Medicare] for any payment made by the Secretary…"), to reimburse Medicare for conditional payments. *See Haro*, 2011 U.S. Dist. LEXIS 58036 at *8; *see also* 42 C.F.R. § 411.24(g) (in which the Secretary of the Department of Health and Human Services defined an entity as including an attorney that has received payment from a primary payer). However, the District Court rejected the Secretary's interpretation of 42 U.S.C. § 1935y(b)(2)(B)(ii) as impermissible under the second step of *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842 (1984), and held that plaintiffs' counsel was not amongst the "entities" from whom Medicare was permitted to file an action to recover the conditional payments. *See Haro*, 2011 U.S. Dist. LEXIS 58036 at *8 - 11.

against actions by third party payers to recover conditional payments is to withhold the maximum amount of settlement funds potentially subject to such liens, which can add not insignificant costs to administering the settlement.