

What to Do— A Third Party is Paying My Client's Fees

by Rachel L. Kranz and Christopher B. Little

You have been referred a new client, Wendy Wife, who hasn't worked in a decade and wishes to divorce her spouse, Henry Husband. Henry has just left Wendy for a younger woman and has frozen her out of all of their joint accounts. How is Wendy going to afford your retainer fee so she can file for divorce before Henry has depleted all of their assets and moved to Fiji with the new girlfriend? Luckily, Wendy has wealthy parents who want to assist their daughter any way they can, including helping their daughter pay for her divorce. So, they accompany Wendy to the intake meeting and pay your retainer fee with their credit card.

As shown in this example, clients sometimes will bring a friend, family member, or other third party to an initial consultation to retain an attorney. This person may be attending the meeting for moral support, but in some cases, he or she may be there to pay the lawyer for the representation. This can happen in a variety of legal settings, including criminal defense and personal injury cases, as well as in representations involving personal and business transactions.

Although it might not seem problematic to have a third-party payer, this type of a situation presents a number of challenges for the lawyer. Among them are conflicts of interest, complications related to confidentiality, and COLTAF management concerns.¹ This article discusses issues that may arise when a third party is funding your legal services.

Overview

Third persons paying for a lawyer's services often will be a client's relative, friend, insurance company, or co-client.² Colorado Rule of Professional Conduct (Rule) 1.8(f) prohibits a lawyer from accepting compensation from a third party for representation of a client unless:

(1) the client gives informed consent; (2) there is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and (3) information relating to representation of a client is protected as required by Rule 1.6.

There is very little case law in Colorado regarding third-party funding of domestic actions. The domestic practitioner, of course, frequently encounters the paradigm, and the situation has potential for many risk management problems.³ To begin, the third person is not the lawyer's client.⁴ The issues of privilege and confidentiality are not fully discussed in this article, but the attorney should discuss the parameters and obligations of confidentiality and waiver of confidentiality with the client and the potential third-party payer.⁵

The Attorney's Role

First, documenting every aspect of an attorney's legal representation, though sometimes tedious, is paramount in risk management. There should be a paper trail showing you explained every situation to your client. The documentation will assist the lawyer in defending a claim, and will inform the trial judge about relevant discussions between counsel and client.

As with many ethical issues, the threshold question often is: Who is the client? Because most of a lawyer's ethical and legal duties arise out of the attorney-client relationship, this question is critical in determining the scope of an attorney's duties. For example, it is the client who sets the objectives of the representation,⁶ who decides whether to accept an offer of settlement or compromise,⁷ and with whom the lawyer must communicate.⁸ Identifying the client is seemingly easy, but it can become complicated when third-party payers are themselves interested parties and/or want to become interested parties in a related matter.



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Imagine the common situation where an insurance carrier hires and pays a lawyer to represent its insured. The Colorado Bar Association Ethics Committee has written that the insured is the client to whom the lawyer owes the duty of loyalty, regardless of any contractual arrangement between the lawyer and the insurance carrier.⁹ The lawyer's relationship with the carrier is "less clear," but it is not, according to the Committee, a *per se* lawyer-client relationship, even though its communications with the lawyer are protected. In contrast to Colorado, other jurisdictions have held that the lawyer represents both the insured and the insurer.¹⁰ Although this view is a minority position, it is seemingly inconsistent with the traditional view that an attorney always puts his or her client's interests first.

Conflicts of Interest

Third-party payers may have interests that differ from those of your client, such as their interest in minimizing the attorney fees and costs incurred in the representation, as well as the litigation's progress or the eventual outcome.¹¹ Once the identity of the client is clarified, an attorney-client relationship with a third-party payer is subject to several conflict of interest provisions in the Rules. First, the general conflicts of interest standards of Rule 1.7 apply. Second, Rules 1.8 and 5.4 impose specific requirements on a lawyer when there is a third-party payer. Third, Colo. RPC 1.4 requires communication between lawyer and client, and Colo. RPC 1.6 prohibits disclosure of client information to third parties—some of whom may be paying the attorney fees. These differences must be discussed with both the client and third-party payers at the very beginning of the relationship.

If the fee arrangement begins to create a conflict of interest for the lawyer, the lawyer must comply with Rule 1.7.¹² Under Rule 1.7(a),

a conflict of interest exists if there is significant risk that the lawyer's representation of the client will be materially limited by the lawyer's own interest in the fee arrangement or by the lawyer's responsibilities to the third-party payer.

A lawyer cannot represent a client if a concurrent conflict of interest exists and waiver of the conflict would not be allowed.¹³ One of the many ways a concurrent conflict of interest may arise is if there is a significant risk that the representation of the client will be materially limited by a lawyer's responsibilities to a third person.¹⁴ This third person may be the one who is paying the bills.

In the family law arena, these types of conflicts are common. Consider the introductory hypothetical. If Wendy's parents pay her legal bills, they might have a false impression of some authority in the case; they may even think they should have a greater say than Wendy in the proceedings. Parents who are grandparents also may request a parenting time schedule that benefits them, seeking more time with their grandchildren during your client's parenting time. The Colorado Court of Appeals recently ruled that great-grandparents do not have standing to seek visitation under CRS § 19-1-117 (grandparent visitation statute).¹⁵ Should the grandmother nonetheless have expectations of some visitation rights by paying the client's bill, she may find herself at odds with the client. The conflict between the grandparent and the child's other parent has to be considered, as well. This may result in the attorney having to juggle the bill, the client, and the grandparents' disagreement about "rights."¹⁶

Informed Consent

A third-party payer relationship creates the potential for a material limitation because of the third-party payer's interest and the lawyer's interest. For example, the third-party payer may have his or her own interests in the ongoing case, which may differ from those of the client's. The payer's desires to minimize attorney fees and his or her own potential liability are a few of the most obvious interests. As the attorney involved in the case, you may have your own interests in mind, such as maintaining an ongoing, lucrative relationship with the third-party payer. If a lawyer determines that a material limitation exists, he or she must either cease representation or obtain informed consent from the client expressly noting the limitation of the current representation.¹⁷ All of this must be confirmed in writing.

The writing does not replace a lawyer's need to talk to his or her client about the risks and advantages of a representation burdened with a conflict of interest. It simply should impress on the client the seriousness of the decision the client is being asked to make.¹⁸ Before the client can provide this informed consent, the lawyer must reasonably believe that he or she will be able to provide competent and diligent representation to the client. The lawyer also must ensure that the representation is not prohibited by law and does not involve a claim asserted by one client against another represented by the lawyer in the same litigation or other proceeding before a tribunal.¹⁹

Non-Consentable Conflicts

There are some conflicts that cannot be waived by the client, even with informed consent confirmed in writing. If the lawyer reasonably believes that he or she will not be able to provide competent and diligent representation to the client, the representation is prohibited by law.²⁰ If the representation involves a claim asserted by one client against another represented by the lawyer in the same litigation or proceeding, the attorney must withdraw or refuse the representation.²¹ Due to other rules in the code of professional conduct,²² state substantive laws, and institutional interests, the Colorado Supreme Court has determined that these conflicts will prevent attorneys from adequately protecting a client's interests and therefore should be unconditionally prohibited.

Lawyer's Professional Judgment

Even if the conflict provisions of Rule 1.7 are satisfied, a lawyer must still be wary of the specific provisions relating to third-party payers and the lawyer's duty of professional independence, as noted in Rules 1.8(f)(2) and 5.4(c). Both subsections contain provisions concerning a lawyer's independent judgment. As stated earlier, Rule 1.8(f) provides specific conditions under which a lawyer cannot accept compensation from a third party for representation of a client, including informed consent.

Some could argue that informed consent can be satisfied through the transmission of the receipt of payment and the identity of the third-party payer in the billing system.²³ However, many experienced attorneys believe that more information in the conflicts database will be a better standard *post hoc* evaluation of the complicated situation. For instance, if the fee arrangement creates Rule 1.7 conflicts, the consent must comply with the rules surrounding the non-consentable conflict situation discussed above.²⁴ Most clients will not appreciate the significance of any conflict of

interest that is created by having a third party paying attorney fees, unless the lawyer explains any potential effects the conflict could have on the attorney–client relationship. The client should be informed of the steps the lawyer will take to ensure that there will not be any inappropriate interference in the lawyer’s relationship with the client (first and foremost being the lawyer’s assurances that he or she will not communicate with the third-party payer without the client’s consent).

Rule 5.4 both reiterates the requirement of Rule 1.8(f)(2) that a third-party payer may not interfere with a lawyer’s independent professional judgment, and places the burden on the lawyer to ensure his or her independence: “[a] lawyer shall not permit a person who . . . pays the lawyer to render legal services for another to direct or regulate the lawyer’s professional judgment.”²⁵ The importance of independence is such that the source of payment should be irrelevant to the lawyer’s performance. A third-party payer arrangement “should not interfere with the lawyer’s professional judgment.”²⁶

These requirements are essentially a restatement of a lawyer’s basic responsibility to provide independent, professional advice. All of the conflict of interest rules are designed to preserve and protect a lawyer’s ability to give, and a client’s right to receive, such advice.

Protecting Client Confidences

An attorney must protect confidential information. Rule 1.6 states that a “lawyer shall not reveal information relating to representation of a client.” This is absolute. “This foundational duty

encourages a client to trust the attorney completely and to communicate frankly with the attorney ‘even as to embarrassing or legally damaging subject matter.’”²⁷ Although the rule provides no exception for third-party payers, the repetition of the obligation in Rule 1.8(f) makes good sense. Third-party payers often want information, or want a lawyer to disclose information that falls under the umbrella of protection included in Rule 1.6. Requiring copies of detailed billing or third-party audits, for example, impedes on client confidentiality. Only the client may waive the confidentiality requirement, and it is the attorney’s duty to guard that privilege. The duty of confidentiality is so important that the New York City Bar Ethics Committee has decided that an insurance defense lawyer may not disclose information to the carrier, even when the information could eliminate the carrier’s responsibility for paying.²⁸

Conclusion

Third-party payer arrangements are both common and permissible. However, there are certain hurdles that a lawyer must overcome in any case involving third-party payers. A lawyer should always provide his or her client an explanation of how the lawyer will keep the attorney–client relationship intact and obtain the necessary informed consent from the client. However, the lawyer should not ignore the third-party payer’s interests, advising the payer of the attorney’s responsibilities and limitations to clarify any misperceptions about the rights the payer may have.

Documentation is critical. Whenever there is a third-party payer, everything should be memorialized in writing. Only good

can come from properly informing your client and getting the proper consent to the third-party payer relationship.

Notes

1. This article does not include a detailed discussion of the COLTAF issues raised here. Every reader is cautioned to be aware of the obligations of Colo. RPC 1.15 and the earning of fees. *See In Re Sather*, 3 P.3d 403 (Colo. 2000).

2. Colo. RPC 1.8, cmt. 11 (persons paying for a lawyer's services).

3. Colorado's appellate courts have issued three interesting opinions involving lawyers, clients, and third-party payers: *Accident & Injury Medical Specialists v. Mintz*, 279 P.3d 658 (Colo. 2012) (third party may not maintain breach of fiduciary duty tort action against attorney based on COLTAF account responsibilities); *Hudak v. Medical Lien Management*, No. 12CA1694 (May 23, 2013); and *Oasis Legal Finance Group, LLC v. Suthers*, No. 12CA1130 (May 23, 2013) (financial transactions involving loans by third parties to litigants may be subject to the Colorado Uniform Consumer Credit Code, CRS §§ 5-1-101 to 5-13-103). These cases suggest that a great deal of information needs to be discussed with the client before the attorney and the client agree to have mom and dad fund the payments to the attorney for managing the domestic action.

4. CBA Formal Ethics Comm. Op. 43: Duty to Insured (Dec. 13, 1969), available at www.cobar.org/repository/Ethics/FormalEthicsOpion/FormalEthicsOpinion_43_2011.pdf; CBA Formal Ethics Comm. Op. 91: Ethical Duties of Attorney Selected by Insurer to Represent the Insured (Jan. 16, 1993), available at www.cobar.org/repository/Ethics/FormalEthicsOpion/FormalEthicsOpinion_91_2011.pdf.

5. *See Medical Lien Management, Inc. v. Allstate Ins. Co.*, No. 12CA0691 (June 6, 2013) for a recent case dealing with obligations an attorney might unintentionally expose herself or himself to when third-party payers are involved.

6. Colo. RPC 1.2(a).

7. *Id.*

8. Colo. RPC 1.4.

9. CBA Formal Ethics Comm. Op. 91, *supra* note 4.

10. Cal. St. Bar. Comm. Prof. Resp. Formal Op. No. 1995: To Whom Does An Attorney Owe Duties When He or She Acts as Insurance Defense Counsel (1995).

11. Colo. RPC 1.8, cmt. 11.

12. Colo. RPC 1.8, cmt. 12 (persons paying for a lawyer's services).

13. Colo. RPC 1.7(a), cmt. 14.

14. Colo. RPC 1.7(a)(2).

15. *In re Parental Responsibilities of M.D.E.*, No. 12CA2482 (ann'd Jan. 31, 2013).

16. The problem occurs when the lawyer ends up spending more time communicating with the third-party payer, thus becoming a mediator between the client and the third-party payer.

17. Colo. RPC 1.7(b)(4); Colo. RPC 1.8, cmt. 12 (persons paying for a lawyer's services).

18. This includes conversations about using credit cards and careful, methodical, and prudent management of the COLTAF account. *See* Kishbaugh, "Seven Things to Consider Before Accepting Credit Cards," *The Docket* (March 2013), available at www.denbar.org/docket/doc_articles.cfm?ArticleID=8011. The Office of Attorney Regulation regularly suspends lawyers for mis-managing COLTAF accounts. *See People v. Sandoval*, No. 13PDJ004 (May 17, 2013) (attorney disciplined, in part, for taking a retainer from a client without providing her a written statement as to the basis of his fees); *People v. Fiore*, No. 12PDJ076 (March 15, 2013) (attorney suspended, in part, for keeping retained payment without having earned the fees).

19. Colo. RPC 1.7(b)(1)-(3).

20. Colo. RPC 1.7(b).

21. *Id.*

22. *See* Colo. RPC 1.1 and 1.3.

23. Colo. RPC 1.8, cmt. 12.

24. *Id.*

25. Colo. RPC 5.4(c).

26. Colo. RPC 5.4, cmt. 1.

27. *See People v. Albani*, 276 P.3d 64 (Colo. 2011) (lawyer disciplined for violating Colo. RPC 1.6 by revealing confidential client information without the client's informed consent).

28. N.Y. City Law Assn. Comm. Prof. Eth. Op. No. 669: Obligations of Lawyers Appointed by Insurance Company to Provide Representation to an Insured When Lawyer Learns Confidential Information of Client That Would be Grounds for Denial of Coverage (May 17, 1989). ■