TADC

The Texas Association of Defense Counsel, Inc

An Association of Personal Injury Defense, Civil Trial & Commercial Litigation Attorneys—Est. 1960

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Office of the President
James R. "Jay" Old, Jr.
Germer Gertz, L.L.P.
P.O. Box 4915
Beaumont, TX 77704
409/654-6700
409/835-2115 FAX
E-Mail: jrold@germer.com

January 30, 2007

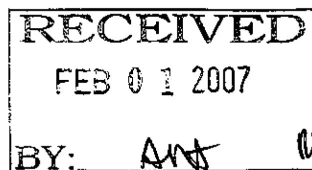
VIA FEDERAL EXPRESS AIRBILL

Mr. Blake Hawthorne
Clerk
Supreme Court of Texas
201 West 14th Street, Room 104
Austin, Texas 78701

Re: No. 02-0730, Excess Underwriters At Lloyd's London & Certain Companies Subscribing Severally, but not Jointly to Policy No. 548/TA4011F01 v. Frank's Casing Crew & Rental Tools, Inc.

Dear Mr. Hawthorne:

Texas Association of Defense Counsel (TADC) submits its second *amicus curiae* letter brief in support of the Respondent, Frank's Casing Crew & Rental Tools, Inc. The letter brief responds to the *amicus curiae* brief filed by the American Insurance Association (AIA) filed on January 10, 2007, specifically to AIA's argument that recoupment creates no significant conflict for insurance defense counsel. TADC adheres to its original assertion: nonconsensual recoupment creates intolerable conflicts for both the insured and defense counsel. The liability insurer's right to recoupment should depend on the insured's agreement.



As stated in our earlier letter brief, the TADC is an association of Texas attorneys whose practice is concentrated on the defense of civil tort lawsuits. In the defense of such cases, the defendants often have insurance, and TADC members have been retained to represent the insured. The TADC is devoted to the just and efficient administration of civil justice. To that end, it advocates a system of tort reparations in which (1) plaintiffs are fairly compensated for genuine injuries; (2) non-responsible defendants are exonerated without unreasonable cost; and (3) responsible defendants are held liable for appropriate damages.

AIA's amicus brief argues that conflicts of interest are more imagined than real in the proposed new world of nonconsensual recoupment. AIA's new world presumes policy holders fall into two categories: (1) those wealthy enough to hire separate counsel to evaluate coverage and settlement issues, as well as fund any settlements, and (2) those whose cannot afford counsel or recoupment. In the AIA scenario, the wealthy insureds are unconcerned about the insurance defense lawyer's conflicts and the poor ones must simply make the best of bad situation. AIA's scenario ignores the fact that most Texas insurance consumers are small businesses and homeowners who have modest assets at risk. They are peculiarly vulnerable to their insurer's demands they contribute to a settlement offer in order to avoid the expense of separate counsel and a recoupment suit. If coverage is disputed, an insurer's willingness to defend or settle may be directly proportional to the reimbursement it believes it can extract from the insured.

While the AIA recognizes that its scenario requires both insured and insurer to have separate "settlement counsel", AIA assumes that the parties will bargain their way to a resolution. This misses the point. If voluntary resolution is the goal, this should occur when the insurer first decides whether to defend under a reservation or rights, not later when a fight with the insured may jeopardize the defense of the case.

Nor is the reservation of rights an uncommon occurrence in liability litigation. Many suits contain claims for punitive damages that are not covered by insurance. And, many suits are settled with those claims unresolved by a finder of fact. Under the AIA scenario, recoupment suits could become the common means for insurers to get back a part of the settlement paid on the theory that the settlement paid some amount in compensation for the "uncovered" punitive damages.

AIA then argues that the insurance defense counsel's duty to give honest and truthful evaluations to both insured and insurer somehow shields counsel from any conflict of interest. This profoundly misapprehends counsel's ethical duties to the client

and the professional judgment calls required to evaluate a case. Counsel's ethical duties to advise their client – the insured1 - about conflicts and protect their confidential information go beyond ordinary honesty in reporting facts.

At the beginning of the relationship, attorneys must advise the client about potential conflicts that affect professional, independent judgment and obtain the client's informed consent. A lawyer is prohibited from undertaking representation if a lawyer's responsibilities to a third person (like the insurer) could adversely limit representation. TEX. DISCIPLINARY. R. PROF'L COND. 1.06(b)(2). The lawyer may undertake representation if (1) the lawyer reasonably believes representation will not be materially affected, and (2) the client gives informed consent after full disclosure. TEX. DISCIPLINARY R. PROF'L COND. 1.06(c). If a disinterested lawyer cannot reasonably conclude that competent and diligent representation will be given, the lawyer cannot properly ask the client to consent. TEX. DISCIPLINARY R. PROF'L COND. 1.06, cmt. 7.

The Restatement amplifies the lawyer's initial duties. Absent the client's consent, the lawyer may not represent the client if there exists a substantial risk that representation will be materially and adversely affected by the lawyer's duties to a third party. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 121 ("Restatement") (2000). A material divergence may exist with the liability insurer if the claim potentially exceeds policy limits. RESTATEMENT §134, cmt. f. The Restatement permits representation if the client receives reasonably adequate information about the risks of representation. RESTATEMENT §122(1). The lawyer is responsible for assuring that the client has adequate information to evaluate the risk or any conflict. RESTATEMENT § 122, cmt. c(i). In fact, this Court is already considering the implications of that issue in the UPL case, *see Unauthorized Practice of Law Committee v. Home Assurance Inc., et al*; No. 04-0138, Texas Supreme Court.

Contrary to the suggestions by AIA, if insurance defense counsel's evaluation exposes the client to a recoupment claim, counsel is not required to disclose his evaluation to the insurer without the client's consent. Counsel has a duty to preserve privileged or confidential information. TEX. DISCIPLINARY R. PROF'L COND. 1.05(b).

1 *See, e.g., State Farm Mut. Auto Ins. Co. v. Traver*, 980 S.W.2d 625, 628 (Tex. 1998) ("[B]ecause the [defense counsel] owes an unqualified duty of loyalty to the insured...the lawyer must at all times protect the interests of the insured if those interests would be compromised by the insurer's instructions." *See also APIE v. Garcia*, 876 S.W.2d 842, 844 n.6 (1994); *Safeway Managing General Agency, Inc. v. Clark & Gamble*, 985 S.W.2d 166, 168 (Tex. App. – San Antonio 1998, no writ) and *Bradt v. West*, 892 S.W.2d 56, 77 (Tex. App. – Houston [14th Dist.] 1994, writ denied).

Counsel cannot reveal confidential information to someone the client has instructed not to receive the information or to the client's disadvantage without the client's consent. Defense counsel owes the same duty of loyalty to the insured as if he or she had been initially selected and hired by the insured. *Traver, Supra*, 980 S.W. 2d at 627 or 28. *See also* Rule 1.06 cmt. 1. TEX. DISCIPLINARY R. PROF'L COND. 1.05(b)(1)(i), 1.05(b)(2). *See also Employers Cas. Co. v. Tilley*, 496 S.W.2d 522 (Tex. 1973). Even in the instance where insurance exists, if the lawyer's client refuses to permit information to be disclosed to the other, the lawyer must honor the request. TEX. DISCIPLINARY R. PROF'L COND. 1.06, cmt.7. *See also* TEX. COMM. PROF'L ETHICS, Op. 532, 63 Tex. B.J. 806 (2000). In short, defense counsel may not disclose information detrimental to his client, the insured. Moreover, insureds exposed to recoupment may forbid counsel to report the evaluation to the insurer. Defense counsel is ethically bound to honor the request. If, as the AIA suggests, the defense counsel's honest evaluation is important to the insurer, the new world of recoupment litigation will almost invariably deny this important information to the insurer.

AIA argues nonconsensual recoupment poses no greater conflict than does the threat of an excess judgment, but the two situations create qualitatively different conflicts. When the attorney recommends settlement of the claim within policy limits to avoid an excess judgment, the insured suffers no loss if the insurer agrees. Under nonconsensual recoupment, if the insurer accepts counsel's recommendation this nearly guarantees the insured a recoupment suit.

Finally, the fact that the defense counsel gives an "honest" evaluation of the claim's merits does not mean counsel has fulfilled all ethical duties to the client nor is that a magic bullet to prevent being sued. Evaluating lawsuits requires judgments that are neither scientific nor mathematical. That evaluation becomes Exhibit A in both the insurer's recoupment suit and the client's breach of fiduciary duty claim. Even the AIA agrees that a defense lawyer's evaluation is often second guessed in later litigation. But, instead of deciding whether the evaluation was reasonably accurate – a decision that judges and juries are not always well equipped to make – recoupment litigation has the added issue of whether the evaluation was colored by defense counsel's divided loyalty to the insured and the insurer. Once the lawyer is charged before a jury with a conflict of interest, the accuracy of his judgment will be eclipsed by the integrity issue. This will be foremost in counsel's mind while writing the evaluation letter, which will not serve the client well .

Texas law already provides the more equitable and practical solution to the problem. An insurer who disputes coverage is entitled to seek a judicial declaration that coverage does not exist under a policy or it can negotiate for recoupment rights before it defends the potentially uncovered claim. This is the surest way for counsel and the insured client to fairly evaluate conflicts of interest at the suit's inception. As a practical matter, the excess carrier who knows of the underlying litigation, and who knows of a coverage issue should not be allowed to sit idly while the merits of the suit are being decided, and to use its coverage issues as leverage in settlement negotiations.

Obtaining the insured's assent to the right of reimbursement is a bright line rule that preserves the rights of all parties without upsetting the posture of the parties that develops through the preparation of the case.2000 The Court should reinforce that principle instead of expanding the right of reimbursement to the point that it is the tail that wags the dog. Reinforcing that principle is a major step to enabling insurance defense counsel to provide the client with zealous, uncompromised fidelity and advocacy.

Very truly yours,

James R. Old, Jr.
President, TADC

Mr. William Fred Hagans
Mr. Carl D. Kulhanek, Jr.
Hagans, Bobb & Burdine, P. c.
3200 Travis, 4th Floor
Houston, Texas 77002

Mr. Kent R. Hance
Mr. Jay B. Stewart
Hance, Scarborough, Woodward, et al
111 Congress Avenue, Suite 500
Austin, Texas 78701

Mr. L. Hayes Fuller, III
Mr. Greg White
Naman, Howell, Smith & Lee, LLP
P. O. Box 1470
Waco, Texas 76703

Mr. Christopher Dove
Locke, Liddell & Sapp, LLP
600 Travis Street, Suite 3400
Houston, Texas 77002-3095

Mr. G. Andrew Veazy
Huval, Veazy, Felder & Aertker, LLC
101 Feu Follett, Suite 101
Lafayette, LA 70598-0948

Mr. J. Clifton Hall
Ms. Karen Milhollin
Westmoreland Hall, P. C.
2800 Post Oak Blvd., 64th Floor
Houston, Texas 77056

Mr. Warren W. Harris
Mr. Tracey C. Temple
Bracewell & Guiliani, LLP
711 Louisiana Street, Suite 2300

Mr. Roger Hughes
Adams & Graham, LLP
P. O. Drawer 1429
Harlingen, Texas 78551-1429

Mr. John N. Ellison
Ms. Jocelyn Gabrynowicz
Anderson, Kill & Olick, P. C.
1600 Market Street, Suite 2500
Philadelphia, PA 19103

Mr. Fred C. Bosse
American Insurance Association
500 West 13th Street
Austin, TX 78701

Mr. Patrick J. Wielinski
Mr. Trevor B. Hall
Cokinso, Bosien & Young
2221 E. Lamar Blvd., Suite 120
Arlington, Texas 76606

Ms. Amy Bach
LAW OFFICES OF AMY BACH
42 Miller Avenue
Mill Valley, CA 94941

Mr. E. Lee Parsley
E. Lee Parsley, P. C.
100 Congress Avenue, Suite 240
Austin, Texas 78701

Mr. E. Thomas Bishop
Mr. Alexander N. Beard
Bishop & Hummert, P. C.
5910 N. Central Expressway, Suite 1600
Dallas, TX 75206

Mr. William T. Barker
Sonnenschein, Nath & Rosenthal, LLP
7800 Sears Tower
Chicago, IL 60606