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Ethical Dilemnas in Mediation: What Would You Do?

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On the ABC series *What Would You Do*, hidden cameras film ordinary people as they confront moral dilemmas created by actors in everyday situations. In the same way, the following mediation scenarios invite you - the ethical lawyer - to make decisions about how to comply with your ethical obligations while also keeping your client happy. So, with apologies to ABC (and without hidden cameras): What would you do?

Scenario 1:

A competitor has just served a complaint -claiming unfair competition - against a company that you represent. The plaintiff wants to proceed immediately to mediation. You know that your client, the defendant, is very cost-conscious and wants to settle right away before it has to pay lawyers. But you have no discovery and really don't know much about the strength of the claims or defenses in the case.

What would you do?

Several Colorado Rules of Professional Conduct ("Colo. RPC") suggest trying to convince your client to delay mediating. First, Rule 1.1 provides, "A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation."[1] Depending on your experience and the complexity of the issues involved, it may be difficult to provide competent representation without more time to prepare for mediation.

Adequate preparation also relates to your duty under Colo. RPC 1.4(b) to "explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation." It is difficult to provide meaningful settlement advice if there has been no discovery, no factual investigation and no opportunity to research relevant law.

A final, though important, concern is that allegations that an attorney failed to prepare for mediation adequately can be the basis for a legal malpractice claim.[2]

On the other hand, your client may want an early settlement for its own reasons, such as to avoid having to produce extensive and potentially damaging discovery. Colo. RPC 1.2(a) provides that "a lawyer shall abide by a client's decisions concerning the objectives of representation and, as required by Rule 1.4, shall consult with the client as to the means by which they are to be pursued . . . A lawyer shall abide by a client's decision whether to settle a matter."[3] Thus, it is the client's decision as to when and on what terms it will settle its case.

So what do you do if, despite your advice to the contrary, your client still wants to mediate immediately?

You will have to decide whether you can proceed with the mediation while also complying with your obligations of competence and communication. At minimum, this is an excellent time to communicate with the client in a clear and detailed writing. Document that you have advised the client against proceeding to mediation this early in the case and explain your reasoning. This may include discussing such matters as:

- The lack of discovery;
- The risks and benefits of settling the case without such discovery and other factual and legal investigation;
- The strengths and weaknesses of the case based on the facts as you know them,
- The client's right to proceed to trial,
- Estimated costs and fees should the case proceed, and
- Potential recovery and potential adverse outcome, as best you can determine.

You should also consider having your client acknowledge the receipt of this letter in writing. Then, if you decide to honor the client's decision and schedule the mediation at this early stage, you will at least have written evidence that the client assumed the risk in so proceeding.

Scenario 2:

You now represent the plaintiff. You have convinced the defendant to schedule a mediation and you send the mediator a confidential settlement statement, complete with a demand for big bucks. You have since learned, however, that your client has decided to take its business in a different direction and is willing to settle for next to nothing. The client doesn't want the defendant to know that. You wonder whether you must tell the mediator your client's true settlement position before the mediation.

What would you do?

Rule 3.3 of the Colorado Rules of Professional Conduct requires candor toward a tribunal. However, a mediator not acting in an adjudicative capacity is not a tribunal as defined by Colo. RPC 1.0(m). Instead, the lawyer's duty of candor toward both the mediator and other parties is governed by Colo. RPC 4.1, which provides that in the course of representing a client a lawyer shall not knowingly make a false statement of material fact to a third person or fail to disclose a material fact necessary to avoid assisting a client's criminal or fraudulent act.[4]

"Whether a particular statement should be regarded as one of fact can depend on the circumstances."[5] Statements of a party's negotiating position or exaggerations of the strengths of its case ordinarily are not considered statements of material fact.[6]

However, the comments to Rule 4.1 also stress that in deciding what statements to make, lawyers should be mindful to avoid criminal and tortious misrepresentation.[7] So while a lawyer in some circumstances may ethically decline to answer questions seeking information as to the client's bottom line settlement number, the lawyer is not justified in lying in response to such an inquiry.[8]

Finally, as Colo. RPC 4.1, comment 1 cautions: "Omissions or partially true but misleading statements can be the equivalent of affirmative false statements." An example is found in *Kath v. Western Media, Inc.*[9] In that case, plaintiffs' counsel learned of a "smoking gun" letter that proved the defense case. Knowing that the defendants and their lawyer were unaware of the letter, plaintiffs' counsel rushed to accept the defendants' settlement offer without disclosing the letter. When defense counsel learned of the letter, defendants revoked the offer of settlement. The trial court upheld the settlement, but the Wyoming Supreme Court reversed, stating that plaintiffs' counsel had a duty to advise the court and defense counsel of the letter.[10]

So do you tell the mediator your client's true settlement position? Making a large settlement demand is not the same as representing that number to be the client's bottom line and should not be considered a representation of fact. In this author's opinion, you are probably safe to head into the mediation without further disclosure. As negotiations proceed, however, you should remain vigilant not to cross the sometimes-fuzzy line between puffing and misrepresentation.

Scenario 3:

You are now at the mediation, once again representing the defendant. Your client has learned that the plaintiff company has committed several environmental infractions that if reported could trigger an EPA investigation. You also have reason to believe that plaintiffs' counsel is embezzling client trust funds. You would like to use both of these facts to force a reasonable settlement.

What would you do?

This answer is relatively clear. Under Colo. RPC 4.5(a), "A lawyer shall not threaten criminal, administrative or disciplinary charges to obtain an advantage in a civil matter nor shall a lawyer present or participate in presenting criminal, administrative or disciplinary charges solely to obtain an advantage in a civil matter." This rule also prohibits you from threatening to bring such charges to coerce a settlement.[11] So you need to tell your client that you can't use the threat of disclosing this information as leverage to force a better settlement.

That does not mean, however, that you can't or should not report the violations to the appropriate authorities. Most significantly, Colo. RPC 8.3(a) requires lawyers to report ethical violations of another lawyer "that raise[ ] a substantial question as to that lawyer's honesty, trustworthiness or fitness as a lawyer in other respects" to the appropriate professional authority. The embezzlement of trust funds likely is the type of issue that lawyers must report. However, to eliminate any question of the improper use of the grievance in the settlement process, you may consider waiting until after a settlement is finalized and performed to make the report.

Scenario 4:

You are still at the mediation, back to representing the plaintiff. The defendant is finally willing to settle but only if you, a powerful plaintiffs' lawyer, will agree not to represent any more plaintiffs in similar suits against the defendant company. You really don't want to file any more lawsuits against

the defendant, so you don't object in principle to the request.

What would you do?

In certain cases, such as mass tort or investment fraud actions, a corporate defendant is often more willing to settle if it can be sure that plaintiff's counsel will not bring more lawsuits against it on behalf of other clients. However, you cannot ethically agree to such a restriction as a condition of settlement, even if you have no intention of filing more cases. Under Colo. RPC 5.6(b), a lawyer may not "participate in offering or making . . . an agreement in which a restriction on the lawyer's right to practice is part of the settlement of a client controversy." As stated in Rule 5.6, comment 2, that rule "prohibits a lawyer from agreeing not to represent other persons in connection with settling a claim on behalf of a client." Thus, Rule 5.6(b) not only bars defense counsel from proposing such a settlement term, but it also prohibits you from agreeing to such a term.

According to the Ethics Committee of the CBA, Rule 5.6(b) also prohibits other restrictions that impede the lawyer's ability to represent other claimants effectively against the settling defendant, such as an agreement that would

- Prevent subpoena of specified documents,
- Prohibit the use of certain expert witnesses in future cases,
- Impose forum or venue limitations in future cases, or
- Prohibit the lawyer's referral of potential clients to other counsel.[12]

However, other settlement provisions affecting a lawyer's conduct may be permissible. Accordingly, in appropriate circumstances, a settlement agreement may be conditioned upon nondisclosure of the terms and amount of the settlement, may ask plaintiffs' counsel to state that he or she has no present intention of filing suit against the defendant in similar cases, and may require a lawyer to return documents obtain in discovery as a condition of settlement.[13] So, you may be able to provide part of the protection that the defendant seeks, even though you can't promise not to file other suits.

Scenario 5:

You are still representing the defendant, but this time the defendant has insurance that likely will cover some but not all of the plaintiff's claims. The insurance company has agreed to pay defense costs under a reservation of rights and has appointed you as counsel for the insured. Your client wants to be sure that insurance covers the settlement and wants you to convince plaintiff's counsel to amend the complaint to include only covered claims or to specify in the settlement agreement that the entire settlement amount is allocated only to covered claims.

What would you do?

This scenario illustrates the inherent tension in the tripartite relationship of an attorney retained by an insurer to defend an insured. It is settled Colorado law that in such circumstances, the attorney's client is the insured, not the insurance company.[14] The insured is the client to whom the lawyer's duty of unqualified loyalty is owed.[15] However, the rights of the insurer can't be ignored. The contract of insurance, which usually gives the insurer the right to control the defense and settlement of the action, defines the insurer's rights and obligations. At times, the insurer's interests may diverge from those of the insured.[16] In that situation, "[t]he attorney's ethical duty is to assure that the interests of the insured are protected, while at the same time fulfilling the insured's contractual obligations to the carrier."[17]

A classic situation of divergence between the interests of the insurer and the insured is when a complaint includes both covered and potentially non-covered claims. An insurance company has a duty to defend its insured so long as the claims for liability allege any facts that fall within the policy.[18] However, if the insurer believes that it has no indemnification obligation, such as where the insured's acts were intentional and outside policy coverage, the insurer may defend under a reservation of rights. "A reservation of rights permits the insurer to fulfill its duty to defend, while also allowing it to dispute its duty to indemnify in a later declaratory action, if a court finds the insured liable."[19]

In our scenario, as in any reservation of rights situation, both the insurer and your client have an interest in establishing no liability. On the other hand, if liability is found, the insurer would prefer that liability be found on non-covered claims; your client, of course, strongly prefers just the opposite. Thus, your client has asked that you try to make it appear, without the insurer's consent, that a settlement is attributable entirely to covered claims. Under Colorado case law and ethical rules, however, you are heading into dangerous territory.

Some of the risks:

1. The client may well be violating the insurance contract. Under the typical insurance contract, the insurer retains the exclusive right to control settlement negotiations, subject to the insurer's duty to act reasonably and in good faith.[20] In addition, an insurance policy typically contains a "cooperation" clause, which obligates the insured to cooperate with the insurer in not admitting liability or settling claims without

the insurer's consent. If the insured violates a cooperation clause in a material and substantial respect, he or she can forfeit recovery under an insurance policy.[21]

2. The allocation of funds to covered claims in the settlement agreement likely will not bind the insurer.[22]

3. The insurer can still bring a declaratory judgment action challenging coverage. In *Shelter Mut. Ins. Co. v. Vaughn*,[23] the plaintiff brought a claim of assault and battery against the insured. He later amended the complaint to allege negligence and dropped the assault and battery claim before trial. The jury found against the insured on the negligence claim, which was the only claim tried. The insurance company, which had defended under a reservation of rights, then sought - and won - a declaratory judgment that in fact the insured's wrongful conduct had been intentional—not merely negligent. Accordingly, the insurer had no obligation to indemnify the insured. The Colorado Court of Appeals affirmed that judgment and found that the insurance company had been entitled to file the declaratory judgment action despite the jury verdict of negligence. It seems likely that an insurer in our circumstance would also be able to file such an action.

4. You may have to consider advising the insurance company of your client's plan. The May 2013 addendum to CBA Formal Op. 91 cautions that Colo. RPC 1.6 recognizes circumstances under which a lawyer may disclose a client's fraudulent conduct to the insurance company. Those circumstances include preventing a fraud that is reasonably certain to result in substantial injury to the financial interests of the insurance company.[24] If your client's conduct rises to the level of fraud, you will have to make that ethical decision.

Finally, be aware that the concept of "informed consent" permeates your obligations to the insured throughout the representation, including in the context of settlement and potential conflicting interests between the insurer and the insured.[25] The requirement of "informed consent" "denotes the agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct."[26]

Scenario 6:

Working late into the night in the mediation, the parties finally reach a settlement. Everyone is too worn out to hammer out a final settlement agreement, so the mediator just makes a list of key points of the settlement. The next day, the other party gets cold feet, claiming there really was no meeting of the minds. Your client is outraged and wants you to sue to enforce the agreed-upon settlement. You are concerned because you don't know how to prove a settlement agreement without revealing information protected by the confidentiality of the mediation process.

What would you do?

Your concern about how you will prove a binding settlement in these circumstances is well founded, as *Yaekle v. Andrews*[27] illustrates. In *Yaekle*, the Colorado Supreme Court addressed the enforceability and admissibility of writings prepared at the conclusion of a mediation in the context of two consolidated cases. In the first case, at the conclusion of mediation the parties had signed a document entitled "Basic Terms of Settlement," which included an acknowledgement that the parties understood the document to be "a binding enforceable agreement." The document contemplated the preparation of further, formal settlement documents that the parties never executed. In the second case, at the end of a 13-hour mediation session, the mediator outlined the apparent terms of settlement but neither party signed the agreement.

The court first addressed Section 13-22-308(1) of the Colorado Dispute Resolution Act, *Settlement of Disputes*, which provides:

> If the parties involved in a dispute reach a full or partial agreement, the agreement upon request of the parties shall be reduced to writing and approved by the parties and their attorneys, if any. If reduced to writing and signed by the parties, the agreement may be presented to the court by any party or their attorneys, if any, as a stipulation and, if approved by the court, shall be enforceable as an order of the court.

The court concluded that while that section provides a means by which an agreement reached in mediation may be presented to a court and made an enforceable court order, it is not the exclusive means by which an agreement reached in mediation may be enforced. Instead, the court found that the common law of contracts, including the principles allowing for the formation of contracts without the signatures of the parties bound by them, remained intact and was not abrogated in the mediation context by C.R.S. § 13-22-308.[28]

Nonetheless, the presence of a written agreement signed by the parties in the first case and the absence of such an agreement in the second case was significant in *Yaekle*, primarily because of the statutory confidentiality protection afforded to mediation communications. As the court explained:

> [C.R.S. § 13-22-307] protects all mediation communications as confidential. "Mediation communications" are in turn

> defined as "any oral or written communication prepared or expressed for the purposes of, in the course of, or pursuant to, any mediation services proceeding." Explicitly excepted from this definition are written agreements to enter into mediation and any "final written agreement ... which has been fully executed." Importantly, protected mediation communications are generally inadmissible as evidence in later judicial proceedings.[29]

Because the parties had signed the agreement in the first case as a binding, enforceable agreement, the court found that it was not a confidential mediation communication within the meaning of these statutory provisions. While the document had not been presented to and made an order of the court under Section 13-22-308, the court could consider it as competent evidence that the parties had in fact reached a settlement. Combined with other post-mediation communications, the document supported the court's finding of a binding settlement contract.[30]

In the second case, however, the mediator's list of settlement terms, which was not signed by the parties and attorney, was not a final executed writing; it remained a confidential mediation communication and could not be considered by the court as evidence of settlement. Accordingly, and in the absence of other evidence of contract formation, the court found that the parties had not reached a settlement agreement.[31]

The preparation of a written settlement document at the mediation, signed by the parties and approved by the attorneys, does not guarantee enforcement. One complicating factor is that when a disgruntled party challenges the scope of an executed settlement agreement prepared during the mediation, the party seeking to uphold the settlement may be barred from presenting evidence of what was discussed during the mediation as support for the enforcement of the bargained-for settlement. Also, the *Yaekle* court made it clear that oral settlement agreements will be enforced if proven. Nonetheless, your chances of enforcing the settlement in these circumstances would be greatly enhanced by preparation and execution of a written document at the conclusion of the mediation forth the material terms of the settlement and specifying that the parties intend it to be a binding and enforceable agreement.

Conclusion

When facing ethical dilemmas in mediation, lawyers must consider not only the Colorado Rules of Professional Conduct, but also the Colorado Rules of Civil Procedure, Colorado statutes, and Colorado case law. Considering all of these authorities, sometimes the answer is clear. When it is not, the ethical lawyer must consider carefully: What would you do? ▲▲▲

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Endnotes:

[1] *Also see* Colo. RPC 1.1, cmt. 5 ("Competent handling of a particular matter includes inquiry into and analysis of the factual and legal elements of the problem, and use of methods and procedures meeting the standards of competent practitioners. It also includes adequate preparation.").

[2] *See, e.g.*; *McCafferty v. Musat*, 817 P.2d 1039 (Colo. App. 1990) (client claimed attorney was negligent in providing advice to settle for $5,000 without adequately conducting discovery; jury awarded the client over $800,000 in damages, which award was affirmed on appeal); *Rino v. Mead*, 55 P.3d 13, 16 (Wyo. 2002) (client claimed that attorney had violated her duty to prepare for, advise the client with regard to, and participate in the mediation).

[3] *See also,* Colo. RPC 1.2, cmt. 1 (the decision whether to settle a matter must be made by the client).

[4] Colo. RPC 2.4, cmt. 5; *See also* Colo. RPC 4.1, cmt. 1 ("A lawyer is required to be truthful when dealing with others on a client's behalf, but generally has no affirmative duty to inform an opposing party of relevant facts.").

[5] Colo. RPC 4.1, cmt. 2.

[6] Colo. RPC 4.1, cmt. 2. *See* ABA Formal Op. 93-370 (a party's actual bottom line or the lawyer's settlement authority is a material fact).

[7] Colo. RPC 4.1, cmt. 2. *See* ABA Formal Op. 93-370 (a party's actual bottom line or the lawyer's settlement authority is a material fact).

[8] *Id.*

[9] *Kath v. Western Media, Inc.*, 684 P.2d 98 (Wyo. 1984).

[10] *Id.*, 684 P.2d at 100.

[11] *See* Colo. RPC 4.5, cmt. [2] ("Threatening to use, or using the criminal, administrative or disciplinary process to coerce adjustment of private civil matters is a subversion of that process. . . .").

[12] *See,* Colo. Bar Assn Ethics Comm., Formal Op. 92 ("[T]he test of the propriety of a settlement provision under Rule 5.6[b] is whether it would restrain a lawyer's exercise of independent judgment on behalf of other clients to an extent greater than that of an independent attorney not subject to such a limitation.").

[13] *Id. See also* ABA Formal Op. 00-417, "Settlement Terms Limiting a Lawyer's Use of Information" (barring settlement term that would prohibit lawyer from using information learned in the current representation in any future representation against

the opposing party, but permitting term that limits or prohibits disclosure of information obtained during the representation).

[14] CBA Formal Op. 91 (1993).

[15] *Id. Also see, State Farm Fire and Cas. Co. v. Weiss*, 194 P.3d 1063 (Colo. App. 2008) (attorney-client relationship is between the attorney and the insured); *Essex Ins. Co. v. Tyler*, 309 F. Supp. 2d 1270, 1272 (D. Colo. 2004) ("In Colorado, an attorney retained by the insurance carrier owes a duty to the insured only; there is no attorney-client relationship between an insurance carrier and the attorney it hires to represent the insured.")

[16] CBA Formal Op. 91 (1993, as amended May 2013).

[17] *Id.*

[18] *Hecla Mining Co. v. New Hampshire Ins. Co.*, 811 P.2d 1083, 1089-90 (Colo. 1991).

[19] *Shelter Mut. Ins. Co. v. Vaughn*, 300 P.3d 998, 1001 (Colo. App. 2013).

[20] *Farmers Group, Inc. v. Trimble*, 691 P.2d 1138, 1141 (Colo. 1984).

[21] *See American Manuf. Mut. Ins. Co. v. Seco/Warwick Corp.*, 266 F. Supp. 2d 1259 (D. Colo. 2003) (insurer had no obligation to indemnify where insured violated cooperation clause by entering into settlement agreement limiting insured's own liability to $5000 and assigning claims against insurer to plaintiff). *Also see Stresscon Corp. v. Travelers Prop. Cas. Co. of America*, 2013 COA 131 (Colo. App. Sept. 12, 2013) (addressing circumstances in which insured's violation of "no voluntary payment" clause by entering into unauthorized settlement will void coverage).

[22] *See Old Republic Ins. Co. v. Ross*, 180 P.3d 427, 434 (Colo. 2008) (settlement agreement and stipulated judgment entered before trial, to which insurer was not a party, could not be enforced against the insurer where insurer had not acted in bad faith, denied coverage, or refused to defend the claim).

[23] *Shelter*, 300 P.3d 998.

[24] Colo. RPC 1.6(b)(3) and (4).

[25] *See* May 2013 addendum to CBA Formal Op. 91 (1993).

[26] *Id.*; Colo. RPC 1.0(e).

[27] *Yaekle v. Andrews*, 195 P.3d 1101 (Colo. 2008).

[28] *Yaekle*, 195 P.3d at 1107-08.

[29] *Id.* at 1106.

[30] *Id.* at 1110-11.

[31] *Id.* at 1112; *also see GSL of ILL, LLC v. Kroskob*, No. 11-CV-00939-WYD-KMT, 2012 WL 10311 (D. Colo. Jan. 3, 2012) (finding that parties came to a full and complete meeting of the minds over the essential terms of their contract despite absence of signed written agreement following mediation where counsel read terms of the settlement into the court record); *Siribuor v. UHS of Denver, Inc.*, No. 12-CV-0077-RBJ-KLM, 2012 WL 3590791 (D. Colo. Aug. 20, 2012) *aff'd in part, dismissed in part,* 514 F. App'x 811 (10th Cir. 2013) (upholding recommendation of magistrate judge who had conducted early neutral evaluation to enforce subsequent settlement agreement); *cf. Sun River Energy, Inc. v. Nelson*, No. 11-CV-00198-MSK-MEH, 2011 WL 3924973 (D. Colo. Sept. 7, 2011) *aff'd,* 11-CV-00198-MSK-MEH, 2012 WL 683519 (D. Colo. Mar. 2, 2012) (finding no meeting of the minds on a material term of the settlement agreement despite counsel having informed the court that the parties had reached an agreement).