Response to Request for Comments

American Bar Association

ABA Commission on Ethics 20/20
Revised Draft Resolution For Comment

Outsourcing

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Comment and Recommendation for an Opinion on:

The Legal Ethics of Outsourcing the Formatting of Law Firm Invoices in Insurance Defense

A John G. Kelly Report

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Executive Summary

Invoicing is a critical component in the service relationship between the lawyer and client. The lawyer has an ethical obligation to provide the client with an after the occurrence accurate invoice for legal/professional services rendered. Invoicing is one step in what is a legal bill management process. Legal bill management in insurance defense is a comprehensive service that consists of a series of “before the occurrence” and “after the occurrence” steps. The before the occurrence steps are driven by litigation management guidelines encompassed in an “e-billing system” that is designed and administered by an outsourced “e-bill systems” vendor. The invoice must conform to an “e” specific format. The after the occurrence preparation of the law firm invoice is the responsibility of the lawyer. Law firms now require “e-invoice” formatting expertise to meet the litigation management demands of their insurer clients. The Model Rules of Professional Conduct authorize lawyers to retain the services of outside experts to massage and format information for clients when the client dictates specifications. E-Invoice formatting of invoices for insurers in conformance with client specific litigation management guidelines can best provided through a direct contractual service between the law firm and an outsourced “e-formatting expert”.

ABA Ethics 20/20 – Outsourcing – Invoice Formatting. John. G. Kelly johngkelly@rogers.com
The Law Firm Invoice

*The law firm invoice is an after the occurrence outcome driven document.*

The invoice is the legal bill for professional services that have been rendered to a client and reimbursement for expenses incurred on that client’s behalf. The law firm invoice is a component of an integrated process in complex legal services such as insurance defense. There are a number of steps that have been developed to ensure that the “invoice for professional services rendered” conforms to the “competent representation” required by Rule 1.1. when complex legal services such as insurance defense are involved. These are:

1. **Rules of Engagement**

   The law firm is retained on the basis of a standard letter that sets out basic terms of reference for the engagement. For example, the law firm is instructed on the timing and frequency for case management reports and submission of invoices. There is a degree of uniformity to rules of engagement in insurance defense and they can be classified as being in the public domain for both the plaintiff and defense bars within the insurance community.

2. **Litigation Management Guidelines**

   The insurer provides the law firm with a detailed set of comprehensive guidelines that specify what items the law firm can and can’t bill the insurer for in conducting its defense and details on the time allowed for specified items as well as rates to be charged to it for services rendered. The guidelines also set out the specifications for e-bills and invoice transmission; usually through a portal developed and managed by an external “e-bill systems vendor”. There is an element of competitive advantage in the design and implementation of the guidelines and insurers consider them to be proprietary.

3. **Litigation Management Strategy/ Budget**
The law firm responds to the retention letter and guidelines with a litigation management strategy that is encompassed in a budget. The budget sets out the strategy for the defense along with an estimate for costs in conformance with the litigation management guidelines. The budget can be deemed to be confidential in whole or part to the extent that the strategy encompasses actions and steps beyond what is a matter of public record. For example, budgeting for the filing of a defense to a statement of claim is a statutory requirement and a matter of public record. Outlining a strategy to negotiate a settlement with estimates for thresholds and a ceiling with a budget for timelines would be considered to be confidential.

4. **Invoice Preparation**

The law firm utilizes its own devices to document the services provided and prepare an invoice for services rendered. Insurance defense firms frequently employ billing clerks to format invoices to conform to the insurer client’s litigation management guidelines. Formatting encompasses the coding of tasks to comply with the guidelines and e-transmission specifications along with the massaging of language to ensure it conforms to the lexicon and vocabulary the client dictates to be utilized in describing tasks and activities. Aside from exceptional situations, the law firm is ethically only permitted to bill the insurer client for services that have actually been rendered. The client, opposing counsel and courts, to the extent that they are either responding parties to these services thereof or involved in court proceedings, are all aware of these actions and activities to date.

*Confidentiality is not an issue at the invoice preparation stage.*

The acknowledged leading ABA Ethical Opinion on insurance company litigation management guidelines states in the opening paragraphs that “*most of the information supplied to insurers through billing records is of a general nature, is publicly known* (e.g. a lawyer’s court appearances), or already known as a result of the insured having forwarded it to the insurer to facilitate the defense (e.g. medical records).”\(^1\)

5. **Invoice Transmission**

Electronic (e-bill) transmission is becoming the norm for transmission of the invoice by the law firm to the insurer. In fact, all major insurers now

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require their law firm panels to submit bills electronically through proprietary “e-bill transmission systems” that are designed and managed by a sophisticated network of competitive e-bill systems providers. There is a business proprietary/confidential business relationship in place between an e-bill systems provider and the client insurer that does not extend to the client/service provider relationship between the insurer and law firm. All of the e-bill management systems are designed to conform to an industry standard Legal Electronic Data Exchange Standard (LEDES). This is an open standard administered by a representative committee of stakeholders in e-bill transmission.2

6. **Legal Bill Review**

Once the invoice is electronically transmitted to the insurer it is reviewed by the insurer’s litigation management bill review unit to ascertain whether it conforms to what was budgeted and to verify the rate for which an action or activity has been charged is within litigation management guidelines. The invoice may be returned for revision with directions to amend it to conform to the budget and guidelines along with directions for reformatting codes and language. A dialogue and appeal may ensue between the bill review unit and the law firm. Once the invoice is accepted as properly formatted and validated the invoice is paid.

**Insurance Defense and Outsourcing**

Property and casualty (P & C) insurance is a regulated financial service.3 One of the requirements imposed on insurance companies by regulators in approving rates is for insurers to manage claims cost effectively.4 The sheer volume of litigation in insurance claims management has placed considerable stress on insurance litigation managers to take a leadership role in embracing innovative approaches to cost effective legal bill management. Insurance defense litigation managers, in keeping with that mandate, explored the outsourcing of legal bill management approximately 20 years ago.

As is the case with many leadership initiatives in legal services management, considerable controversy and debate ensued among the stakeholders in the insurance defense community on the merits, propriety and ethics of legal bill

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2 [www.ledes.org/](http://www.ledes.org/)
3 Susan Randall, [*insurance Regulation in the United States: Regulatory Federalism and the National Association of Insurance Commissioners*]. Vol. 26 Florida State University Law Review at P625,
4 [www.naic.org](http://www.naic.org)
management outsourcing.\textsuperscript{5} The articulation of the full dimension of what is in effect a legal bill management compendium is outlined above. This should have been the foundation for establishing the parameters for informed discussion. Unfortunately, given the nascent state of outsourcing during that period, it became lost in a convoluted misinformed debate on confidentiality and the risk of breach thereof between the lawyer and client if any billing related information was disclosed by an insurance defense firm to an outsourced bill reviewer retained by an insurer. Isolated state court judgments issued judgments that, in at least one instance, bordered on the bizarre by stating that insurance defense firms and their client insurers were in an adversarial relationship, suggesting any sharing of billing information risked compromising confidentiality.\textsuperscript{6}

In response to what was degenerating from informed discussion into histrionic debate the ABA issued \textbf{Formal Opinion 01-421 Ethical Obligations of a Lawyer Working Under Insurance Company Guidelines and Other Restrictions} that definitively articulated the relationship between the insurance defense lawyer and the client insurer.\textsuperscript{7} The opinion contains the following definitive statement on the status of confidentiality between an insurance defense firm and insurer in the context of the unique “\textit{tri-partite}”\textsuperscript{8} relationship in insurance defense wherein the law firm is legal counsel for both the in insured and insurer.

Informing the insurer about the litigation through periodic status reports, detailed billing statements and the submission of other information usually is required, explicitly or implicitly, by the contract between the insurer and insured and also is appropriate in those jurisdictions where the insurer is regarded as a client and there is no conflict between the insurer and insured. \textit{The disclosure of such information usually advances the interests of both the insured and the insurer in the representation and such disclosures are, therefore, “impliedly authorized to carry out the representation” (emphasis added).}\textsuperscript{9}

Fast forward from 2001 to 2008 and beyond. As the \textit{Ethical Outsourcing Opinion} has indicated, outsourcing has assumed an entirely new dimension and become integrated into the mainstream of legal services management. Litigation/legal bill management has also evolved into a robust “\textit{e-litigation management}” integrated service. This white paper will provide insurer defense lawyers and insurers with a


\textsuperscript{7} Supra 6.

\textsuperscript{8} Michael F. Aylward, \textit{Squaring the Triangle}, \textit{The Tripartite Relationship And Its Troubles}. (unpublished research paper 2003). maylward@mail.mmm-m.com

\textsuperscript{9} Supra 6.
timely update and litigation management perspective on the ethics of outsourcing the formatting of law firm invoices.

**Attorney/Client Privilege - The Starting Point**

The “tradition” of assigning the privilege of confidentiality between a client and their lawyer can be traced back to at least Elizabethan times in England.\(^\text{10}\) It was a privilege accorded to the client and implemented to ensure that a client could fully disclose all of the material facts of their legal situation to counsel with the lawyer being accorded legal protection to keep it confidential. The principle became recognized in American law by the early 19\(^{\text{th}}\) century and has evolved into its modern day application with all the inherent complications:

The difficulty in applying this limitation in modern law arises from the fact that lawyers today perform such a wide range of services that it is difficult to say when the consultant has stopped being a lawyer and has become a financial advisor, marriage counselor, or whatever.\(^\text{11}\)

Attorney – client privilege has no association with legal expense management in insurance defense. Because invoicing represents an accounting to the client after the occurrence thereof attorney/client privilege is a misnomer. When discussing confidentiality in the context of legal bill management in general or law firm invoicing specifically what insurance defense lawyers are invariably referring to is either the Work Product Doctrine and/or the ABA Model Rules on Confidentiality.\(^\text{12}\)

**The Work Product Doctrine**

In 1947 the Supreme Court in a landmark case, *Hickman v. Taylor*\(^\text{13}\), expounded on the need for lawyers to be able to incorporate documentation into case strategy secure in the knowledge that opposing counsel would not have an automatic right to access it. The fundamental distinction between Attorney – Client Privilege and the Work Product Doctrine is that the latter is much more expansive in that it is designed to protect “the adversary trial process itself.”\(^\text{14}\)


\(^{11}\) ibid at 1076.


\(^{13}\) *Hickman V. Taylor*, 329 U.S. 495. (1947).

“Most states have adopted discovery procedures similar to those in the federal courts, and they tend to provide similar protection for attorney work product.”

A literal interpretation of rule 26 (b) (3) (discovery rule) requires that three tests be satisfied before materials can be classified as work product. The materials must be:

1. documents and tangible things;
2. Prepared in anticipation of litigation for trial; and
3. by or for another party or by or for that other party’s representative.

Invoices for legal services are derived from the work product. They are documents prepared after the fact that report on what the lawyer has accomplished in the course of the litigation action to that point in time.

*The work product doctrine has no bearing on invoice preparation and formatting.*

**ABA Model Rule 1.6 Confidentiality of Information**

The ABA has long recognized the importance of confidentiality as a primary ethical issue. In the original Canons of Ethics adopted in 1908, Canon 37 dealt with Confidences of a Client. “It is the duty of a lawyer to preserve his client’s confidences.” This canon’s wording and intent was to corroborate and support the common law principle of attorney – client privilege. With the introduction of the Work Product Doctrine and the replacement of canons with the more comprehensive Model Rules of Professional Conduct, Rule 1.6 Confidentiality of Information replaced the more limited Canon 37. The annotation encompassed in the rule is informative in providing background. It indicates that the origin of the rule “derives from both the law of agency and the law of evidence.” Although the reference to evidence has some association with attorney-client privilege, the reference to agency represents the ABA’s own position, which is more expansive than the Work Product Doctrine.

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15 ibid at 487.
16 Ibid.
18 Ibid at 167.
20 Ibid at 87.
The focus on Rule 1.6 is understandable, given the mission of the ABA on the lawyer as opposed to the client in attorney-client privilege or process in the Work Product Doctrine. The rule starts with the premise that:

(a) A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, *the disclosure is impliedly authorized* (emphasis added) to in order to carry out the representation…

The annotation contains a specific reference to an interpretation of Rule 1.6 with respect to litigation bill management. To quote:

The ABA Standing Committee on Ethics and Professional Responsibility in Formal Opinion 01-421 has taken the majority position *that the lawyer is impliedly authorized to give detailed billing information to the insurer* (emphasis added) if it will not adversely affect the interests of the insured, but the lawyer may not submit this information to a third party auditor without the informed consent of the insured.\(^{21}\)

The reference both corroborates Formal Opinion 01-421 and confirms that the exchange of billing information between a lawyer and insurer is in conformance with Rule 1.6. However, as is the case with Formal Opinion 01-421, it fails to delineate what “billing information” encompasses. Again, refer to the above section for the proper articulation of is in effect a legal bill compendium is and what constitutes “billing information”. It’s critical when in rendering an informed opinion on any aspect of billing information to differentiate “before the occurrence” opinions - strategies and budgetary proposals -from “after the occurrence” statement of account invoices for those services which the law firm has actually provided to the client and, to repeat, are either a matter of public record in court documents or otherwise known by opposing counsel and their client.

*The law firm is not just “implicitly authorized” but is “explicitly required” pursuant to ABA Model Rule 1.5: Fees to provide the client with a full accounting for fee for services rendered in a format that conforms to client specifications.*

\(^{21}\) Ibid at 89.
ABA Model Rule 5.3  
*Responsibilities regarding non-lawyer Assistants*\(^\text{22}\)

Lawyers do not work on cases in isolation. Paralegals, legal secretaries and contract service providers work on case files with them. In fact, once the lawyer has prepared the legal bill, the formatting for coding and massaging of language to comply with the client litigation management guidelines along with the follow up for payment is oftentimes delegated to a billing clerk/manager. ABA Model Rule 5.3 specifically authorizes and condones this so long as the appropriate control mechanisms are in place. To quote:

> A lawyer must give such assistants appropriate instruction and supervision concerning the ethical aspects of their employment, particularly regarding the obligation not to disclose information relating to representation of the client, and should be responsible for their work product.\(^\text{23}\)

The nomenclature for “assistant” now extends well beyond the traditional confines of an employment relationship. “Outsourced contract providers” would unquestionably fit into a contemporary definition of “assistant” as articulated in the *Ethical Outsourcing Opinion*. The below repetition of the quote from the preamble is arguably an articulation of the above quote from ABA Model Rule 5.3 in the spirit and context of *ABA Commission on Ethics 20/20*.

> There is nothing unethical about a lawyer outsourcing legal and nonlegal services, provided the outsourcing lawyer renders legal services to the client with the “legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation,” as required by Rule 1.1. (requirement for the lawyer to provide competent representation to a client)

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\(^\text{23}\) Ibid at 453.
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The Restatement

The mission, terms of reference and role of the American Law Institute and its publication, Restatement of The Law Third The Law Governing Lawyers\textsuperscript{24}, speaks for itself as an objective and independent arbiter on the interpretation of ABA ethics opinions. To quote from the Ethics Outsourcing Opinion, “Also available in the broader legal context are existing texts such as the Restatements of Agency and the Law Governing Lawyers”\textsuperscript{25} It’s important to bring the restatement into the confidentiality issue when litigation bill management is involved. As mentioned above, the annotation to ABA Rule 1.6 makes specific reference to the influence of the law of agency section of the restatement on the interpretation of the rule. The restatement addresses the role of agents, a category that includes litigation managers and their referrals to outsourced experts, on the issue of confidential client information.

The restatement makes the interesting observation that “courts generally hold that presence of a translator or other person who facilitates a client’s communication to a lawyer is consistent with confidentiality.”\textsuperscript{26} It goes on to opine that an “accountant acting for a client in translating financial data for benefit of client’s lawyer (is) privileged equally with (a) translator of foreign language.”\textsuperscript{27} There is a logical extension of this rationale to outsourced invoice preparation experts, particularly when in a subsequent topic dealing specifically dealing with insurance defense the restatement validates the right of the insurer to control the defense. Given the realities of the tri-partite professional dynamic in insurance defense the restatement states unequivocally that:

Whether a client-lawyer relationship also exists between the lawyer and client is determined under S.14. Whether or not such relationship exists, communications between the lawyer and “representatives” (outsourcing providers) of the insurer (i.e. litigation invoice consultants) concerning such matters as progress reports, case evaluation and settlement should

\begin{itemize}
\item \textsuperscript{24} Restatement of the Law Third The Law Governing Lawyers, Ch. 5, Confidential Client Information Philadelphia, The American Law Institute, ( 2001),
\item \textsuperscript{25} Supra 4 at P10.
\item \textsuperscript{26} Supra 32, Ch.5, #70, Comment f. at 541.
\item \textsuperscript{27} Supra 32
\end{itemize}
be regarded as privileged and otherwise immune from discovery by the claimant or another party to the proceeding.  

The annotated segments of this excerpt from the restatement are clear and unequivocal in validating the outsourcing the formatting of law firm invoices.

Confidentiality and Data Base Management

Formal Opinion 95-398

Access of Non lawyers to a Lawyer’s Data Base

The use of information management systems as the basis for client file management had emerged as a major practice management mechanism by the mid 1990’s. Many of the systems were a variation of application service providers (ASP’s) installed, maintained and serviced by outsourced vendors. This gave the parties access to confidential material and, in theory, posed a threat to the privileged nature of the information once disclosed to third party computer service providers. The ABA took the position that this was, in effect, an extension of Rule 5.3 and the Standing Committee made the following policy decision:

Under Rule 5.3, a lawyer retaining such an outside service provider is required to make reasonable efforts to ensure that the service provider will not make unauthorized disclosures of client information. Thus when a lawyer considers entering into a relationship with such a service provider he must ensure that the service provider has in place, or will establish reasonable procedures to protect the confidentiality of information to which it gains access, and moreover, that it fully understands its obligations in this regard.

In a footnote to Formal Opinion 01-421 on bill review the Standing Committee distinguished this decision from an insurer’s referral to a third party bill review consultant by indicating that “the present inquiry (on the confidential status of third party bill review) is clearly distinguishable (from 95-398) because the lawyer has neither a contract with nor any right to control the conduct of the third party auditor retained by the insurer.”  The outsourcing of the formatting of law firm invoices takes place through a contract between the law firm and an outsourced

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28 Supra 25 at Ch. 8 at #134 Comment f.
30 Ibid at 2.
31 Supra 6.
32 Ibid n, 28.
service provider. This is a bona fide direct contractual relationship clearly distinguishable from an indirect relationship with a “third party auditor”. The law firm is able to dictate the terms of reference for the contract and has contractual rights for supervision and/or enforcement.

**The law firm is operating well within its ethical obligations in providing the outsourced invoice formatter with access to its invoice data base providing the appropriate measures are in place to protect the confidentiality thereof.**

Confidentiality and E-Billing

*Formal Opinion 99- 413* 33

*Protecting the Confidentiality of Unencrypted E-Mail*

E-mailing is the foundation for e-billing system transmission. There was initially confusion within the ranks among some law firms who were under a misapprehension and/or misunderstanding about whether and to what degree the sending of billing information by e-mail contravened the ABA Model Rule of Professional Conduct 1.6, “The Confidentiality Rule”. The question poised was, regardless of whatever right any party might have to access and review client information in the possession of their lawyer, did Rule 1.6 prohibit the transmission of that information electronically?

The Standing Committee accomplished two important objectives in issuing this formal opinion. First and foremost, it recognized the level of rhetoric that had been reached with the histrionic arguments by factions within the legal profession of the inviolate status of Rule 1.6. In the opening paragraph of the actual opinion the committee qualified the status of the rule by stating that

“**In order to comply with the duty of confidentiality under Model Rule 1.6, a lawyer’s expectation of privacy in a communication medium need not be absolute; it must merely be reasonable**” 34.

Rule 1.6 hasn’t been drafted to require lawyers to function in a top-secret environment. They are professionals required to exercise the standard of care one associates with professionals dealing with sensitive matters.

The second objective was to put the issue of communication in an electronic age context. The formal opinion is a primer on the evolution of information technology


34 Ibid
and how the confidentiality of the lawyer/client relationship has continued to prosper when first the telephone and then the fax came into existence up and until the emergence of e-mail. The Standing Committee acknowledges the existence of hackers and recognizes that there is no such thing as an absolute guarantee of the security of the confidentiality of information in e-mail communications.

However, information is at least as secure, if not more so because of encryption, in e-mail transmissions than telephone and fax exchanges. Just as the legal profession has found that it couldn’t function without the use of the telephone and fax and designed protocols to minimize the risk of breaches of client confidentiality with them so will be the case with e-mails. The benefit, indeed the necessity of using e-mail for the transmission of client information, far outweighs the potential for any breach of the confidentiality rule. The use of e-mail is compatible with Rule 1.6. “E”-bill transmission through secured networks is compliant with all requirements for confidentiality of communications.

This formal opinion provides additional validation for the outsourcing of law firm invoices for formatting by insurance defense firms. The above articulation of the full dimension of legal bill management includes “litigation management guidelines”. Insurers provide their insurance firms with comprehensive case/billing management guidelines that specify in considerable detail the format for billing as well as e-transmission requirements they must adhere to in submitting invoices for payment. The preamble to the formal opinion contains the following statement.

A lawyer may transmit information relating to the representation of a client by unencrypted e-mail sent over the Internet without violating the Model Rules of Professional Conduct (1998) because the mode of transmission affords a reasonable expectation of privacy from a technological and legal standpoint. The same privacy accorded U.S. and commercial mail, landline telephonic transmissions, and facsimiles applies to Internet e-mail. A lawyer should consult with the client and follow her instructions, however, as to the mode of transmitting highly sensitive information relating to the client’s representation. (emphasis added)35

Insurance defense law firms are being explicitly directed by their insurer client to utilize a client specific set of e-billing guidelines and e-invoice transmission system in the formatting and submission of invoices. The complexity of these systems speaks for itself in outsourcing the formatting to specialist invoice formatters in an effort to meet client requirements and provide a cost effective service.

**Ethical Law Firm Invoice Outsourcing**

Insurance is a regulated industry. One of the fundamental dictates of the industry is for all stakeholders to look to providing the consumer with cost effective services. Insurance defense firms are obligated to incorporate cost effective service into their client relationship with insurers and insured. Insurance litigation managers are constantly looking at ways to implement cost effective measures in their relationship with law firms. “Electronic litigation management” is now in the mainstream of that dynamic. “Electronic Invoicing” is integral to that process. E-invoicing formatting and transmission requires technical expertise that is frequently provided more cost effectively and at a best practices level by an outsourced e-invoice formatter in a direct contractual relationship between the law firm and outsourcer.

The Ethical Outsourcing Opinion acknowledges that defining competency in outsourcing is a work in progress that will be fully articulated in the very near future. The release of the next round of the “ABA Commission on Ethics 20/20 reports will be of considerable assistance. However, in the immediate short term the law firm entering into an invoice formatting outsourcing contract should adhere to the following criteria.

- Designate a person in the law firm at either the partner or senior associate level to assume direct responsibility for the invoice formatting outsourcing relationship
- Require the outsource provider to demonstrate that they have professionals in house and/or on contract who have a demonstrated track record in providing billing/invoice services that are compatible with ABA ethical standards.
- Require the outsource contractor to demonstrate it has the technical competency to install technology that will conform to the legal bill management requirements and standards of the client.
- Negotiate an outsourcing contract that conforms to the ethical rules of conduct outlined in the formal opinions contained in this white paper.
In summation, there are no ethical impediments to a law firm outsourcing invoice formatting to a third party provider. To once again, quote from ABA *Formal Opinion 08-451 - Lawyer's Obligations When Outsourcing Legal and Nonlegal Support Services*:

There is nothing unethical about a lawyer outsourcing legal and nonlegal services, provided the outsourcing lawyer renders legal services to the client with the “legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation,” as required by Rule 1.1.

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Rule 1.1 does not require that tasks be accomplished in any special way. The rule requires only that the lawyer who is responsible to the client satisfy her obligation to render legal services competently.36

36 Supra 1 at P2.