HOW TO AVOID ETHICAL LANDMINES IN SETTLEMENT

Reflections for Management Counsel

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In employment litigation, settlement negotiations can be an intricate dance for both the employee/plaintiff’s counsel and the employer/defendant’s counsel. Inevitably, settlement negotiations entail some mix of puffery, bluster, and pontification, as each party tries to convince the other party that it holds the higher cards, even while neither side puts its cards on the table. Especially when settlement discussions take place before discovery occurs, the absence of a clear factual record makes it easy for bluster and puffery to give way to material omissions and even alternative facts. Settlement discussions also can create a bit of a dance between clients and their counsel, since settlement arrangements affect the financial interests of both the party and the lawyer representing it. And these dilemmas become even more complicated when a lawyer attempts to settle a case on behalf of multiple clients. For lawyers representing management, there are several key sets of concerns to keep in mind, in terms of dealing with his or her client, dealing with plaintiff’s counsel, and in reaching and creating the settlement agreement.

1. The Client’s Right to Control Settlement

In the settlement context, the ABA’s Model Rules of Professional Responsibility reflect a concern to prevent the lawyer’s superior knowledge and experience from depriving the client of the ability to exercise ownership over the tactics and terms of settlement. Where the defendant employer is a large corporation with its own in-house counsel, those risks can be somewhat mitigated through the active involvement of experienced in-house counsel. However, where the
employer is a small business without its own legal department, defense counsel needs to communicate more robustly to ensure that the client is in a position to evaluate and direct the settlement process.

With respect to the decision on whether or not to settle, Model Rule 1.2(a) is unequivocal. It plainly states that counsel “shall abide by the client’s decision whether to settle the matter.” The lawyer also is under a duty to “abide by a client's decisions concerning the objectives of representation” and, “consult with the client as to the means by which they are to be pursued.” This obligation requires counsel to communicate with the client about the possibility of settlement and reasonably consult with the client concerning the means of negotiating settlement, including whether and how to present or request specific terms. With respect to tactics and strategy for settlement, the lawyer is empowered only to take such action as he or she has been authorized by the client to take.

Consistent with Rule 1.2, and for myriad reasons, management counsel and the client need to be on the same page regarding settlement as early as possible in the litigation. Some management lawyers are reluctant to raise the settlement issue with their clients, often either for fear of appearing timid or insufficiently aggressive to the client or out of the lawyer’s internal desire to win the case and/or defeat what he or she sees as meritless claims. And, of course, since early settlements reduce the hourly fees that that would be generated for defendant’s counsel by protracted litigation, early settlement tends to run counter to the management lawyer’s immediate pecuniary interest. As a fiduciary with a duty of loyalty to his or her client, however, the management lawyer cannot allow these concerns to impede open discussion of settlement with the employer/defendant. Many clients cannot exercise appropriate control over
the objectives of the representation unless they are adequately informed of the prospects for settlement.1

As a general rule, both the client and the lawyer benefit from a thorough discussion of the strengths and weaknesses of the employer’s case, the importance of the principles at stake, the burdens of litigation and discovery, and the chances of success at summary judgment apart from the chances of success at trial. The discussion also should include a realistic case budget for discovery and summary judgment and a separate budget to take the case to trial, plus an assessment of the risk of an adverse ruling on the merits and the potential for payment of plaintiff’s attorney’s fees and costs. Such a dialogue maximizes the client’s control over the engagement and creates clear expectations that align the lawyer’s tactics with the client’s objectives. When the employer is determined to defeat the plaintiff at all costs, the lawyer’s discussion of options for settlement can be difficult - and often is relatively brief. In these “not-one-thin-dime” cases, even a whiff of surrender can draw the client’s ire. While extended dialogue on the pro’s and con’s of settlement may not be fruitful in these circumstances, that doesn’t mean the discussion should not take place.

2. Negotiations and Misrepresentations.

On occasion, settlement negotiations can be contentious, full-throated affairs, especially where the principals chime in to underscore how “rock solid” their case is. Unlike their clients, lawyers need to be especially careful about the assertions they make regarding the facts or the absence of facts in the case. The statements that lawyers make in settlement negotiations are covered by the Rules of Professional Responsibility. Specifically, under Rule 4.1, a lawyer is

1 Rule 1.4(b) provides that “[a] lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.”
prohibited from knowingly making “a false statement of material fact or law to a third person” in
the course of representing a client. This rule applies to statements or omissions with respect to
material facts. However, it does not apply to other types of statements, such as opinions or
statements regarding “a party’s intentions as to an acceptable settlement of a claim.”

In settlement negotiations, misrepresentations can occur as each side tries to present the
facts in the light most favorable to its settlement position. According to the ABA’s Comment on
Rule 4.1, a misrepresentation can occur “if the lawyer incorporates or affirms a statement of
another person that the lawyer knows is false.” Misrepresentations can also occur “by partially
true but misleading statements or omissions that are the equivalent of affirmative false
statements.” Where a misrepresentation occurs, the management lawyer may have a duty to
make a disclosure to plaintiff’s counsel to correct the record. However, depending on the ethics
rules adopted in a particular jurisdiction, disclosure may be subject to the consent of the client.

3. The Settlement Agreement

Ethical considerations come into play in terms of fashioning the terms to include in the
settlement agreement itself. A lawyer’s duty of competence under Model Rule 1.1 requires the
lawyer to utilize the legal knowledge, skill, thoroughness, and preparation necessary for the
representation. In other words, the lawyer needs to know what he or she is doing when it comes
to the terms that can and should be included in a settlement agreement.

From the standpoint of the employer, the paramount consideration in drafting a
settlement agreement is the finality of the agreement. When an employer agrees to settle a case
with a former employee, management tends to expect that it will never have to deal with that
employee’s complaints again. An employer never wants to pay out a settlement to a former

employee only to have the employee resurface with a new set of claims once the settlement payment is spent.

Consequently, management lawyers need to be focused on the finality and enforceability of the settlement agreements they create. One major issue involves the scope of the employee/plaintiff’s waiver and release. Over the years, the courts have ruled that an employer cannot require an employee to waive its right to file an administrative charge or report unlawful activity to a government agency. Such clauses, say the courts, tend to interfere with the ability of law enforcement agencies to obtain the information they need to enforce the law. On the other hand, clauses that require an employee to release his or her right to additional recovery that the EEOC or another agency might obtain from the employer are permitted. Management counsel needs to be careful as to how such a clause is phrased.

These issues resurfaced in the last couple of years in a string of EEOC enforcement actions and SEC enforcement actions challenging terms of severance agreements that the agencies viewed as intruding on their turf. These actions stand for the proposition that an employer cannot require an employee to agree to waive “any claim or entitlement to additional relief” because that language is broad enough to nullify the incentives created by the SEC’s whistleblower bounty program (not to mention qui tam actions under the False Claims Act). On the other hand, releases that are tailored to state that the employee/plaintiff waives any claim or entitlement to additional monetary relief “from the employer” should pass muster. By their terms, releases tailored in this way do not prevent an employee from receiving amounts payable from the government’s own funds.

Overly broad confidentiality clauses also can create enforceability issues for settlement agreements with current or former employees. Where these clauses prohibit disclosure of
information related to underlying wrongdoing or events that occurred during the employment relationship, they can interfere with the ability of law enforcement agencies to obtain cooperation and testimony of witnesses and deprive the agencies of the information they need to enforce the law. The following is a sample clause that will address these concerns of overly broad release or confidentiality clauses:

Access to and Interaction with Government Agencies. By signing this Agreement, you are barred from accepting any settlement proceeds or any award of damages or other monetary relief paid or payable by [THE EMPLOYER] or any of the Released Parties as a result of any investigation, litigation, or proceeding brought against [THE EMPLOYER] or the Released Parties, provided, however, that this Agreement does not prohibit you from (a) filing an administrative charge or complaint with a federal, state, or local government agency; (b) communicating with or providing government officials with testimony or information regarding possible violations of law in the course of a lawful investigation or proceeding undertaken by any government agency or the U.S. Congress, or (c) receiving any reward from a government agency for providing information to that agency.

On the other hand, clauses that prevent the employee from disclosing the terms or amount of settlement tend to be far less problematic, though they merit an exception permitting disclosures “that are required by law or by order of a court of competent jurisdiction.”

The issue does not tend to arise that frequently, but every now and then, when the parties to a prolonged, expensive, and acrimonious employment lawsuit attempt to settle the case, employers will ask for a clause to prevent “that lawyer from turning around and suing us again.” The lawyer’s answer to this request is a simple “no.” The inclusion of such a clause would violate the plain language of Model Rule 5.6, which provides that a lawyer shall 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.”

4. Individual Defendants.
In employment litigation, it is not uncommon for a current or former employee to assert claims against individual managers or supervisors as well as against the employer itself. In some cases, a single law firm will defend the individual defendants as well as the company. That arrangement is typical where the company believes that the individual manager or supervisor acted appropriately and within the scope of his or her authority. In these cases, the manager will have the company’s support, and the company may offer to have its counsel defend the manager as well as the company itself. In many cases, the company will be willing to negotiate and pay the settlement for both the manager and the company.

On the other hand, separate counsel is the more prudent choice when the company is uncertain about whether the manager acted appropriately and within the scope of his or her authority. In that situation, there is the potential for a conflict of interest that would preclude the same lawyer from representing both parties in litigation or in settlement negotiations. For a variety of reasons, including state law indemnification obligations, the company may agree to pay for the manager’s attorney’s fees. In cases in which EPLI coverage exists, the insurer may have a duty to defend the manager, even though the employer may believe the manager should bear the liability for the plaintiff’s damages. In such situations, it also is important to bear in mind that discussions between the company and the individual manager related to settlement strategy may not be covered by the attorney-client privilege. Parties in that position may wish to consider a joint defense agreement that will confirm their common interest in defending against the plaintiff’s claims and enable cross-party communications to be privileged. If that is the case, however, the company should give full consideration to the appearance that such a close arrangement would create for a jury and the message it would send about whether the company supported the actions of the individual manager.