The Coverage You Desire

Good vs. Great Lawyers' Professional Liability Insurance

(and How to Get It)

By Stephen S. van Wert

It has been said that the enemy of being great is simply being good. In our busy lives, if something is good, then it is often deemed acceptable. But if you are taking the time to read this issue of the annual DRI *Law Practice Management Review*, I believe that you are a person that does not settle for the status quo. Both in law firms and in our lives, we should all continually pursue improvement and growth.

Unfortunately, in our litigious society, many well-run law firms have had allegations of malpractice made against them. Professional liability insurance policy form language is critically important. It can mean the difference between whether your insurance carrier or your firm will pay the claims that may result. You need to know that not all lawyers professional liability (LPL) insurance policies are created equal, and even if the policy under consideration does not contain the policy features that you desire, you can negotiate the coverage that you need, sometimes at little or no additional cost.

Optional Endorsements—The Key to Great Coverage

While it is true that the main body of a policy form is a "filed form," meaning that it has been approved by the applicable state department of insurance, and thus cannot be changed in the same manner as a contract between two private parties, it still can be amended through endorsements. These endorsements are "filed forms" as well. The state departments of insurance recognize that one policy form does not fit every situation, so they allow insurers to use these endorsements to craft coverage that meets the needs of individual law firms.

These endorsements are known as "optional endorsements," meaning that they are attached to the main policy form, and they change the coverage offered under the main policy form at the option of the insurer. Some optional endorsements expand coverage while others take coverage away. You may ask, "Why would a state department of insurance allow an insurer to take away coverage through an optional endorsement?" Because in some cases, an insurer will only offer terms to a law firm if it carves out exceptions to coverage in a particular area of concern. Otherwise, the carrier's only other option would be to decline to offer coverage to the firm at all.

Optional endorsements are structured in a manner very similar to amendments to a contract between two private parties. They often contain language such as, "Section I. INSURING AGREEMENT, paragraph B. is hereby deleted and replaced with the following…."

If a law firm had read paragraph B of the "Insuring Agreement" of the main policy form of its LPL insurance and took comfort in the language provided there, but had not read the optional endorsement that stripped out and replaced language, then the firm could be in for a very unpleasant surprise when it faces a claim.

In recognition of the importance of optional endorsements, it is wise for a law firm to review the language contained not only in the main policy form of its LPL policy, but also in each optional endorsement offered by a carrier. Carriers will include the title and form number of each optional endorsement that they intend to include as part of a policy in their quote letters to insurance brokers, but they usually do not include the actual endorsements themselves. The titles of the optional endorsements give you clues about their content, but to be honest, I have seen titles that are not very descriptive. The better, more sophisticated insurance brokers will ask to review the language in these optional endorsements before presenting quotes to their clients. However, the ultimate responsibility for reviewing policy form language, including all optional endorsements, belongs to the law firm seeking insurance coverage.

Know What to Ask For

In any negotiation, you need to define up front what is important to you. While law-

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yers are trained to review their client's contracts in everyday practice, it has consistently surprised me how often law firms do not even read the policies that will cover their own practices. My thought is that they believe that the policy form is not negotiable, so their purchase decision really just comes down to reviewing a one-page "policy highlights" sheet comparing coverage offered by various carriers in light of the quoted premiums.

There are many policy features that are extremely meaningful in claims scenarios, and it does not take long to determine whether your policy provides this coverage or not. Your insurance broker should be able to readily provide you with this information. If not, you should seriously consider engaging another broker. Here is a description of important coverage options that you should try to negotiate on behalf of your firm, and whether these coverage enhancements are typically available for free or with an additional premium charge.

Mutual Choice of Counsel—Who Is Going to Defend You?

Most lawyers professional liability (LPL) insurance carriers do not offer "mutual choice of counsel" coverage in their standard policies. The reason is that an insurer's claim department wants to maintain as much control over the claims adjustment process as possible. The claims department typically sets up a list of "panel counsel" that handles its LPL claims that occur within a certain geographic area. For example, if an insurance carrier receives a malpractice claim for an insured law firm in Arkansas, then the carrier will typically assign the defense of that claim to one of the law firms on its "panel counsel" list for Arkansas. In my experience, this list usually has anywhere from one to three law firms listed for smaller states, and more for larger states. These "panel counsel" firms have agreed to abide by the insurer's litigation guidelines and to the insurer's hourly rates. These firms also must have demonstrated experience defending lawyers against malpractice claims.

While these "panel counsel" firms should defend your firm well in the event of a claim, your firm may wish to participate in selecting a law firm. In some cases, you may desire to select a firm that is not on a carrier's list of "panel counsel." If you have "mutual choice of counsel" coverage in your policy, then both you and the carrier come to an understanding about which law firm will defend your firm in your claim. If you nominate a law firm that is not on the carrier's "panel counsel" list, then that firm will need to agree to the carrier's litigation management guidelines and the carrier's rates. The law firm will also need to demonstrate expertise in defending legal malpractice claims. In the event that your firm and the carrier cannot agree on a law firm to defend your firm against a malpractice claim, then the carrier will select a defense firm on its own.

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While this coverage is very rarely offered in the main policy form of most carriers, it usually can be added as an optional endorsement. Typically, if a carrier agrees to add this endorsement to its policy, it will do so for no additional premium. Note that carriers will resist adding this endorsement because they desire to retain control of their panel of defense counsel.

Deductibles—The Difference Maker

Almost all LPL insurance include a policy deductible. Typically, carriers seek deductibles in the range of $1,000 or more per attorney in a firm. Deductibles also vary by the liability coverage limits sought by law firms. If a law firm is willing to accept a larger deductible, only then will a carrier offer to provide higher liability coverage limits. For example, if a firm desires a $10 million limit, rarely will a carrier requests a deductible of less than $25,000.

Since a deductible is incurred first in any claims scenario, it has an immediate impact on a firm's finances in the event of a claim. There are many optional endorsements available that lessen the negative impact of a deductible on the law firm. Some of these optional endorsements are offered for additional premiums, and others are offered for free.

Aggregate Deductible—Stop the Bleeding

Most carriers offer "aggregate deductibles." Most LPL policies are written with a "per claim" deductible, meaning that the deductible will apply to each and every claim experienced by the law firm in the policy year. Since claims are relatively rare, per claim deductibles are satisfactory for most claims scenarios. However, sometimes firms experience "serial claims" as the result of some error that has impact across a large volume of clients. For example, if a law firm has an employee that has been engaging in collection activities against a large volume of debtors on behalf of a client, and the employee's practices violated the federal Fair Debt Collection Practices Act, or its state equivalent, then a separate deductible would apply to each claim against the firm. For example, if a deductible was $1,000 per claim, and the damages claimed by each third party amounted to $1,000, then, in essence, the carrier would not pay any damages because a separate $1,000 deductible would apply to each and every claim, even if there were hundreds of

claims against the firm amounting to hundreds of thousands of dollars.

Aggregate deductibles are particularly important to small law firms that are not in position to pay a large number of deductibles if necessary within the same policy year. Most small law firms likely can pay a $5,000 deductible for one claim, but if the same firm experienced five claims in a given year, could it pay $25,000 easily? In some cases, this claims scenario could bring a law firm to its knees, simply because the law firm did not have the right coverage in place.

Loss Only Deductibles—Pay Only If You Are Liable

Most carriers also offer "loss only deductibles," also known as "first-dollar defense" coverage. As the name implies, a law firm's deductible only applies to an indemnity payment made by the carrier on behalf of the firm. The deductible does not apply to defense costs. This coverage is attractive because defense costs are the first costs that a law firm incurs in a claim, and with meritless claims, usually law firms incur only defense costs.

This optional endorsement is available for an additional premium, but it is also subject to a carrier's underwriting standards. If your firm has shown a propensity for facing a large number of small claims or incidents, a carrier may decline to offer you this option. In other words, the underwriter may determine that the additional premium that the carrier will incur will not likely offset the costs that the carrier will incur by defending your firm from the first dollar.

The amount of additional premiums for both the "loss only deductible" and the "aggregate deductible" optional endorsements varies by the size of the deductible. Also, each carrier has its own unique pricing structure for these options. It is wise to ask for alternate quotes for these options from different carriers to make a fully informed decision.

Deductibles and Coverage Enhancements—The Fine Print Can Mean Big Dollars

Over the years, several coverage features that were added to LPL policies to make them more competitive have been gradually adopted into most carriers' policy forms. However, while some carriers have added these enhancements, they have not made corresponding changes to how their deductible for these enhancements work. In other words, if a policy deductible still applies to these enhancements, then their value is greatly diminished. It is not always apparent if the deductible applies to these coverage enhancements or not. You should ask your insurance broker to clarify with a carrier if the policy form is unclear on this point. Here is a brief overview of some of these coverage enhancements.

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Loss of Earnings Coverage—Your Time is Valuable

Many carriers nowadays include "loss of earnings" coverage in their LPL policies. Basically, this coverage reimburses an attorney for his or her lost wages while attending a deposition, trial, or other work time lost by the attorney related to investigating or defending a claim on the request of the carrier. Usually, there are caps to this enhanced coverage on a per day, per claim, and per policy period basis. For example, a carrier may offer up to $500 per insured per day for his or her time spent cooperating with the carrier to defend the claim, subject to a limit of $10,000 per claim and $50,000 per policy period for all insured attorneys in a firm. This coverage is usually provided with no additional premium.

If a firm carries a $5,000 deductible, and it applies to this coverage enhancement, then a firm would incur at least 10 days worth of lost wages before this coverage would come into effect. Clearly, the deductible in this situation would render the coverage enhancement much less advantageous to the firm, so you should investigate how the "loss of earnings" coverage interacts with the policy's deductible.

Disciplinary Proceedings—Complaints Can Be Costly

Another common LPL policy coverage enhancement will pay for the cost of defending an attorney in a proceeding that is brought by a disciplinary board that alleges professional misconduct. Carriers providing this coverage enhancement will pay for the costs of defending one of your firm's attorneys up to a certain limit for each proceeding and an aggregate limit for all such proceedings in a given policy year. For example, a carrier may provide $10,000 of defense costs per disciplinary proceeding and up to $25,000 per policy period.

As with the "loss of earnings coverage," this coverage enhancement is usually provided with no additional premium. However, if a firm's deductible applies to this coverage, then a large portion of the benefit is eliminated.

Pro Bono Services—No Good Deed Goes Unpunished?

One relatively new coverage enhancement eliminates application of a firm's deductible to any legal services rendered by the firm to pro bono clients. Law firms that engage in pro bono services are viewed positively by LPL underwriters because it demonstrates a commitment by those firms to "doing the right thing" rather than on functioning solely as money-making enterprises. If a firm is solely focused on making money, that might signal that the firm would tend to cut expenses to the detriment of prudent risk management.

This coverage feature is nice to have if your firm engages in pro bono activities. Not only does your firm not receive any income from those engagements, but it would be a shame if the firm had the out-of-pocket expense of the amount of a deductible if a pro bono client turned around and sued the firm for legal malpractice. Obvi-

ously, the larger the firm's deductible, the more valuable is this coverage feature. It is not a common optional endorsement, but it is worth asking about. It is usually offered for no additional premium.

Professional Services—Beyond Being a "Lawyer"

Most LPL policies very expansively define "covered professional services" under the policies. These covered professional services typically include services rendered as a lawyer, arbitrator, mediator, notary public, executor, or trustee, for instance. However, sometimes attorneys in your firm perform professional services on behalf of clients that do not meet these definitions. Examples include acting in the capacity of a lobbyist, a member of the board of a bar association, an author of legal articles, or a speaker at legal conferences. Less common additions to a definition of covered professional services under a policy include services rendered as an expert witness or claims adjustment services. If one of your attorneys commits malpractice in one of these capacities, and it is not included in your policy's definition of covered professional services, then the carrier might have the right to deny the claim.

It is often difficult to determine when an attorney takes his or her "lawyer hat" off and puts on his or her "lobbyist hat" instead. Nonetheless, to avoid ambiguity, it is best to evaluate your firm's professional services thoroughly, and make sure that your policy provides the coverage that you need. Most carriers are able to expand the definition of covered professional services through the use of an optional endorsement, and usually without charging an additional premium. However, you will not get this coverage unless you ask for it!

Please note that a carrier will not add professional services that are not typically performed by law firms. For instance, a carrier will not add "accounting services" to its LPL policy definition of covered professional services. In that case, a firm would need to purchase a separate "accountants professional liability" policy to cover the exposure.

Exclusions—What Is Given Can Be Taken Away

LPL insurance policies are written to cover basically anything that a lawyer does in his or her professional capacity for his or her clients, unless otherwise excluded under the policy. Therefore, reviewing the exclusions in an LPL policy is critically important. Once again, it would be incorrect to assume that a carrier's exclusions are not negotiable. Carriers often do have optional endorsements that modify or even eliminate exclusions that are in a policy. However, it is usually much more difficult to have these taken out.

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First, a carrier will not eliminate exclusions that are considered essential to the nature of the LPL policy. For example, a carrier will not agree to remove the "bodily injury" exclusion because that would have the effect of converting the LPL policy into a general liability policy. A carrier also would not agree to eliminate the "intentional bad acts" exclusion because a properly drafted insurance policy would not cover intentionally fraudulent or criminal behavior. However, if there is a particular exclusion that would provide incomplete coverage to your law firm, then it would be wise to at least ask a carrier if it could remove the exclusion. For example, some LPL policies exclude any securities work performed by a law firm because of the severity potential of such claims. If your firm does not perform traditional securities work by representing public companies in connection with their reporting obligations to the SEC, or engaging in private placements or municipal bond work, then you may think that such an exclusion is not meaningful. However, some securities exclusions are written so broadly that even a simple incorporation of your client's business could be an excluded professional service under your policy. Therefore, it is very wise to evaluate all exclusions in a policy in light of your firm's particular practice.

Ownership in Clients—A Conflict of Interest?

LPL policies commonly eliminate coverage for professional services rendered to an entity that is owned by firm attorneys. One of the reasons for this exclusion is to eliminate the potential conflict of interest in those situations. For example, if an attorney owns 50 percent of a client of the attorney's firm, then it would be possible for that attorney to have his or her company sue his or her law firm and collect proceeds from the insurance company if the firm's LPL policy did not exclude "ownership in clients."

To avoid this potential conflict of interest, LPL policies typically exclude coverage for professional services rendered to a client whose stock is more than 10 percent or 15 percent owned by any attorney in the law firm. The actual ownership percentage cutoff varies among LPL carriers. Nonetheless, many carriers have optional endorsements in place that can increase the ownership percentage that is used for your particular law firm's policy. Thus, if your firm has one client that is 25 percent owned by lawyers in the firm, it would be possible to obtain an endorsement that would cover that client under the law firm's LPL policy. In my opinion, it may be possible to negotiate an ownership percentage as high as 35 percent from a carrier, but going beyond that would be difficult. In that case, the carrier might craft the endorsement to apply to a certain client only, instead of giving the law firm a blanket endorsement that would apply to every client of the firm.

Manuscript Endorsements—The Sky Is the Limit

Most of the optional endorsements discussed so far have been filed and approved by your state department of insurance. However, many states allow carriers to use "manuscript endorsements" to craft insurance policy language to meet the unique needs of individual law firms. If your state

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allows insurance carriers to use manuscript endorsements, then you can negotiate the exact language of each word of the endorsement with a carrier. As the endorsement name implies, the endorsement language is "hand-scripted," or tailored, in a manner that is acceptable to both your law firm and your carrier. These endorsements typically contain similar language as other optional endorsements, deleting entire sections of the policy and replacing them with language acceptable to both parties. If the change to the coverage policy form that your firm requests is covered under an already existing optional endorsement that has been approved by the state department of insurance, then the carrier will use that language. However, if the change to the coverage is out of the ordinary, then a "manuscript" endorsement is the way to go.

Manuscript endorsements are not commonly used. In addition, multiple authorizing persons working for a carrier usually need to approve them, including underwriters and claims personnel. As such, it may take some time to negotiate a "manuscript" endorsement with a carrier. It is advisable to begin your review of your insurance policies about 90 days in advance of your policy expiration to build in enough time to negotiate the coverage that you need.

The Unfortunate Truth—Size Matters

Unfortunately, your success in negotiating the exact coverage that you need is often dictated by the size of your law firm. Underwriters are more willing to consider changes to their standard policy form language if a law firm is considered large enough. Because optional endorsements are out of the normal workflow, some underwriters will deny a request to add an optional endorsement because they simply don't want to take the time to do it given the premium that the carrier will earn. However, don't let this tendency dissuade you from asking for what you want. The market for LPL insurance is very competitive right now, and if one carrier says no to your request, there may be several others that are ready to say yes.

It is your firm's financial health and reputation that is on the line. A good LPL insurance policy should not be viewed as "good enough." It is worth your time to read the policy, ask for what you want, and realize the coverage that you need. Your insurance broker is your advocate in this process and can greatly aid you in this process. However, an insurance broker does not know your practice as you do, so you need to ask for these coverage enhancements. Ultimately, it is your firm's responsibility to make sure that you have great coverage in place.