



Lawyers' Professional Liability Claims Trends: 2015

Insurer Survey

Introduction & Overview

As the economy continues its expansion, many law firms are seeing their business stabilize or grow on a year-over-year basis. Yet, the changing nature of legal service delivery has heightened competition among individual law firms both for clients and for talent. The profession is seeing a growing number of mergers, acquisitions and lateral hires as individual firms seek to fill holes in their offerings or take advantage of opportunities to deepen capabilities, expand geographically or diversify into non-core practice areas.

Meanwhile, these dynamics contribute to increased risks of significant professional liability, or legal malpractice, claims. While the frequency of these claims hasn't fluctuated significantly in the past several years, the size of the claims in dollar terms has grown steadily.

Legal malpractice claims continue to represent a significant potential exposure for law firms. They are not only costly – with some now reaching up to eight figures or higher – but can also have enduring negative consequences on the firm, including distracted partners and associates; failed recruitment efforts; and stains on the firm's reputation. Keeping a watchful eye on issues and trends related to legal malpractice claims can therefore be key for law firm leaders in shaping their firm's protection against these exposures.

Ames & Gough, a trusted risk and insurance advisor to law firms, conducted its fifth annual survey of Lawyers' Professional Liability claims during the second quarter of 2015. We asked insurers to provide information on their 2014 claims experience, including the types of claims they experienced as well as trends in claims frequency, severity, and cause.

The study identifies the types of issues most likely to trigger malpractice claims; practice areas seeing the most significant claims activity; and takes a closer look at risks that have been receiving greater scrutiny, such as those related to lateral hires and cyber security. We also examine how insurers are managing the increasing cost to defend claims, including rates paid for legal defense.

This year's survey included nine of the leading insurance companies that write Lawyers' Professional Liability Insurance coverage: AIG/Lexington, AXIS, BRIT, CNA, Catlin, Huntersure, Ironshore, Markel, and Swiss Re Corporate Solutions. Together, they provide insurance to approximately 80 percent of the AM Law 100 firms, with six of the nine insurance companies insuring between 40 - 80 percent of both the AM Law 100 and the NLJ 250 firms. We are grateful for their participation in our study and are pleased to present the findings in this report.

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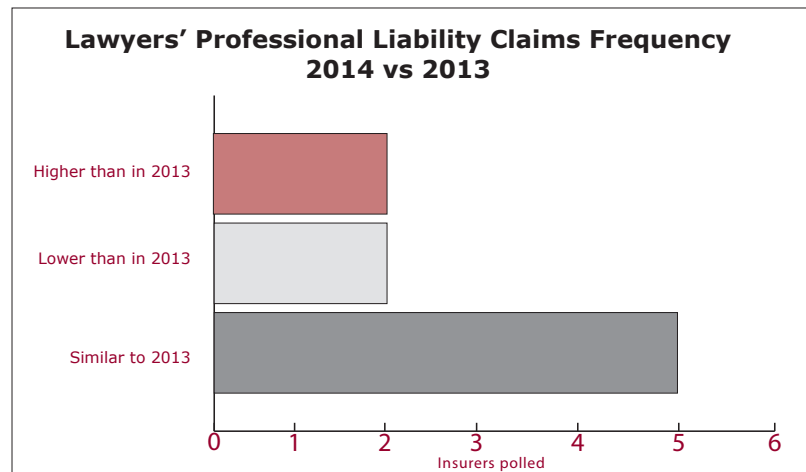
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Survey Findings

1) Legal malpractice claims frequency remains constant.

The number of new malpractice claims brought against law firms is flat on a year-over-year basis, with five of the nine insurers surveyed indicating that the number of claims filed in 2014 was similar to that in 2013 (and another two each of the insurers indicating that it was both higher and lower). Although claim frequency remains constant on a year-over-year basis, it is still higher than it was in the years preceding the recession.



2) Continued surge in severity for legal malpractice claims.

Although claims frequency has leveled off, claim severity continues to be an issue with several insurers involved in multimillion dollar claims.

Claims with Reserves Over \$500,000: Six of the nine insurers surveyed reported they had more claims with reserves of \$500,000 or greater (including loss and expenses) in 2014 than in 2013. Of the nine polled, six had 21 or more claims with a reserve over \$500,000 (combined indemnity and defense costs).

Claims Paid Over \$20M: In the past two years, six insurers participated in paying a claim of \$20 million or more, including three that participated in a claim of \$50 million - \$100 million, and one involved in a claim exceeding \$100 million.

Although it is likely that some of these insurers were involved with the same claim(s) given quota share coverage arrangements and excess limits, it's clear the number of claims resulting in multi-million dollar payouts is not declining.

3) Trusts, Estates & Probate Law claims are on the rise as Real Estate claims decline.

This year, most (67 percent) of the insurers identified Trusts & Estates as the leading practice area for legal malpractice claims, replacing Real Estate, which had been the single largest source of these claims in the past several studies.

On a percentage basis, the insurers citing Trusts & Estates as the leading practice area for malpractice claims rose more than 17 percentage points (from 50 percent in 2013). Trust, estate and probate lawyers provide a broad range of client services, from estate planning, to tax advice, to estate administration and other related services. As an area of practice, Trusts & Estates inherently involves personal and sensitive matters, making it uniquely susceptible to the potential for client dissatisfaction.

Insurer Survey

Effective and clear communication is particularly important if a firm is to avoid conflict of interest claims when working on trust and estate matters. For example, it is not at all unusual for a third party, perhaps a spouse, relative, or family friend to initiate contact with a trust and estate attorney on behalf of an elderly potential client.

This issue can be readily addressed by using stronger disclosure in the engagement process with regard to who is the client; who the firm will or will not be representing; and precisely what services you will and will not perform.

Another issue in matters involving trusts and estates is the potential exposure to lawsuits from multiple sources. In most areas of practice, an attorney may only be sued by a client. However, in many jurisdictions, trust and estate lawyers are an exception to this general rule. Many states permit the beneficiary of an estate to sue an attorney whose negligence caused the testator's intended disposition of the bequest to the beneficiary to fail. To protect your firm against a potential claim brought by a dissatisfied beneficiary, the testator's wishes should be clearly documented, preferably in a document generated by the testator, and the testamentary documents should be checked and re-checked to ensure compliance with the testator's wishes.

Practice Areas Generating Largest Number of LPL Claims*

Area of Practice	Responses (by percentage)				
	2014	2013	2012	2011	2010
Trusts & Estates	67	50	57	0	33
Corp Business Organization & Securities	56	63	57	67	33
Business Transactions - Commercial Law	56	50	43	67	50
Real Estate	44	63	86	67	67
Collection & Bankruptcy	11	0	14	33	33
General Litigation	11	0	0	17	0
Taxation	0	25	14	0	0
Personal Injury Plaintiff	0	13	14	33	17
IP	0	13	0	0	17
Family Law	0	0	0	17	0
Litigation Defense	0	0	0	0	17

**Note: Survey participants provided multiple responses, so the totals sum above 100 percent. The survey also inquired about LPL claim activity in several other practice areas, but received no responses in each of the past five years. These areas include: Labor & Employment, Insurance Defense, Criminal/White Collar, International Law, and Personal Injury Defense.*

Despite fewer claims Real Estate still sees significant claim activity. Insurers citing Real Estate as the leading practice area to generate legal malpractice claims decreased by almost 20 percentage points (to 44 percent in 2014, down from 63 percent in 2013). That stated, although the spate of failed real estate deals during the economic downturn had a long tail, many of these claims appear to have worked their way through the system, which would account for the decline. Nonetheless, Real Estate still remains one of the four highest practice areas for claims.

Other practice areas continue seeing significant claim activity. Corporate and securities and business transactions garnered a fairly equal number of responses from insurers in 2014. Both have been fairly consistent from one year to the next in terms of the percentage of insurers seeing claims generated from these practice areas.

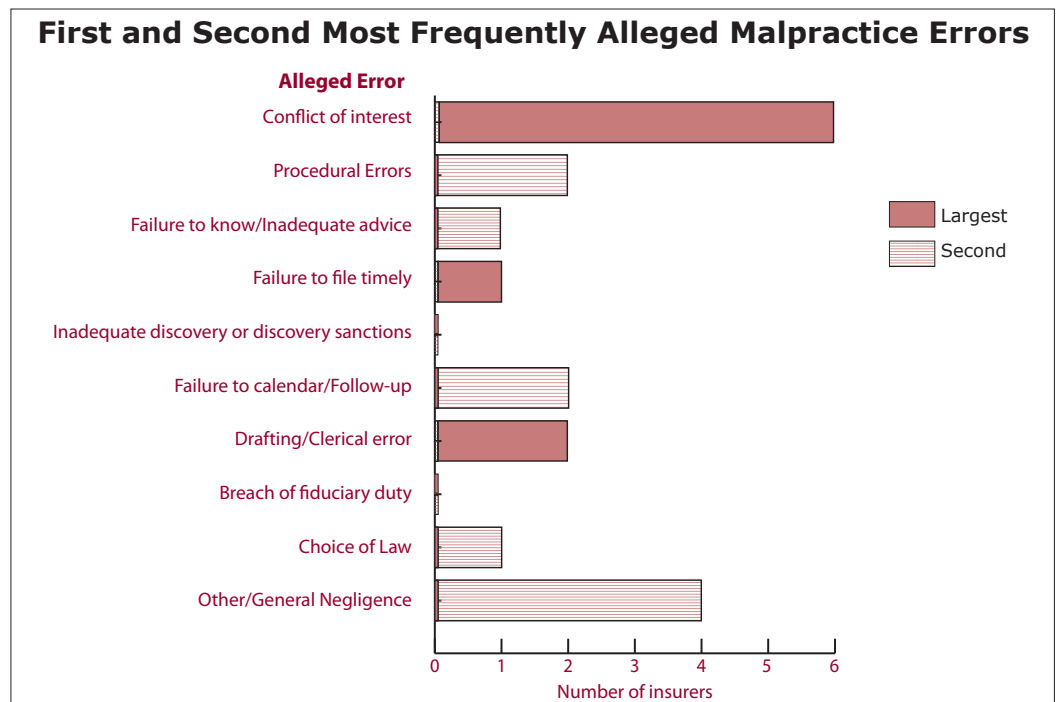
When business deals go bad, clients inevitably start looking to their lawyers. Given the heightened potential for a claim in these circumstances, law firms may be able to minimize risk by maintaining a strong conflicts database; clearly identifying whom they are representing and not representing in the transaction; and by avoiding entering into any business contracts with clients or serving on their corporate boards.

4) Most frequent alleged malpractice error: Conflict of interest.

Year over year, conflict of interest continues to be the most common alleged legal malpractice error. This year, six of the nine insurers surveyed cite conflicts as the leading cause of legal malpractice claims. Conflicts can occur when a lawyer has a personal interest in a matter; however, more often, conflicts arise between multiple current or past clients represented by the same lawyer or firm.

Conflicts are a growing concern today as increasing numbers of law firms seize opportunities for growth and expansion either through mergers and acquisitions or by bringing in lateral hires. Unfortunately, the potential conflicts arising from these initiatives often are not addressed early enough in the process. And when conflicts finally are realized, they are frequently either ignored or overlooked.

When asked specifically about claim issues due to lateral hires or firm mergers, six of the nine insurers cited an uptick in claims arising from the melding of staff at law firms. Of the six insurers seeing an increase in such claims, two indicated the issue could be traced to a lateral hire or merged attorney continuing work for a client of his/her old firm while already at his/her new firm; another stated claims often are the result of the firm not resolving a conflict of interest in advance.



5) Cyber-related malpractice claims: An emerging area.

Cyber-related exposures and their potential to evolve into malpractice claims remains an area for law firms to continue to monitor and address in their risk management efforts. In the current survey, three insurers indicated they have had a Lawyers' Professional Liability Insurance claim arising from a cyber or network security event. Of them, two were the result of stolen laptops; the other involved employee error.

Nonetheless, many predict that numerous other law firms have been hacked, but either aren't aware of it or don't want to go public. Indeed, the portability of

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technology has given rise to new issues concerning security breaches. Stolen laptops, smartphones, tablets, cell-phones or other portable data-bearing devices rank the highest in terms of risk and may provide unauthorized access to your technology systems and confidential information.

Although the typical Lawyers' Professional Liability Insurance policy will cover a firm for a breach to a third party's data if the breach results in a malpractice claim by the client, more firms are turning to the broader cover (to include first-party coverage) offered by a stand-alone cyber liability policy. This is because costs to satisfy regulatory reporting requirements, internal costs to repair the firm's systems, reputational costs, business interruption, and any damage to first-party data would not be covered under a professional liability policy.

6) Legal malpractice defense costs rise along with rates insurers paid defense counsel.

All nine insurers surveyed indicated they saw an increase in the cost to defend legal malpractice claims in 2014. Notably, large claims are often more complex and therefore drive up costs.

At the same time, rates for defense counsel are rising, which is also contributing to higher costs. In the survey, eight of the insurers indicated there was an increase in the rates they paid defense counsel in 2014. Specifically, two insurers paid increased rates to defense counsel of 5 - 10 percent; another three saw rates increase by 2 - 5 percent; and three experienced increases of up to 2 percent.

Average Hourly Rate Insurers Pay Defense Counsel: 2014 vs. Four Prior Years

Rate	2014	2013	2012	2011	2010
\$501 or greater	2	1	-	-	-
\$401 or greater	1	0	3	2	1
\$301 - \$400	2	4	1	1	1
\$251 - \$300	4	3	2	1	1
\$201 - \$250	0	0	1	2	3



Insurer Survey

ABOUT AMES & GOUGH

Ames & Gough, founded in 1992, has established itself as a committed, superior resource for law firms, design professionals, and other consulting firms and professional organizations in need of professional liability insurance and risk management assistance. In recent years, the firm has expanded its capabilities to include management liability, employment practices liability, kidnap & ransom and related insurances; as well as more typical property and casualty insurances. The firm has offices in Boston, Philadelphia, and Washington, DC. Visit the Ames & Gough Website at www.amesgough.com.

Conclusion:

Changing Legal Landscape, Potential for Large Claims Call for Focus on Risk Management

Achieving success in today's market is requiring law firms to navigate through an increasingly difficult environment marked by greater price competition; a constant drive for practice efficiency; the increased commoditization of legal work; growing competition from non-traditional service providers; and non-hourly billing. All of these changes in the legal landscape are having an impact on a firm's susceptibility to legal malpractice claims.

Lateral hires/mergers. As firms see opportunities to grow by recruiting laterals or pursuing mergers, they also must carefully consider the potential for conflicts and take appropriate measures to protect the firm against their consequences.

Watch practice areas with more claims. Firms need to take a closer look at the quality and effectiveness of their client communication protocols and risk management efforts with respect to all individual practice areas, particularly those currently seeing the most significant malpractice claim activity, including: Trusts & Estates, Corporate & Securities, Business Transactions, and Real Estate.

Review cyber/network security. Given how rapidly technology is evolving, it's virtually impossible to be completely insulated from cyber and data security risks and other emerging exposures. In this environment, a greater focus on firm-wide risk management remains a key to reducing the potential for cyber-related claims and their costly consequences. Firms must be willing to invest in the technology and tools to help prevent unauthorized access to client information. They should also consider so-called Network Security/Cyber Liability insurance to provide asset protection in the event they are hacked.

Adopting holistic risk management. From information security and conflicts to outside counsel guidelines, today's management teams at law firms are under significant pressure to address a wide range of client-driven requirements. This underscores the importance of a more holistic approach to risk management.

Active claims management pays off. While much attention is appropriately spent trying to avoid claims, it is also important to ensure that any problems that do arise are addressed promptly. Whether it involves a potential circumstance or an actual lawsuit filed against the firm by a client, it is important to immediately notify your insurance company and evaluate how to best respond to the matter. Time and again, experience has shown that early claims reporting and active claims management are invaluable in holding down the cost of claims.

All of these measures also will go a long way to helping your law firm obtain more favorable pricing, terms and conditions on your professional liability insurance program.