Lawyers Mutual Insurance Co. of Kentucky

Volume 13, Issue 1 Winter 2002

A Message From Pete Gullett
Lawyers Mutual's Chief Operating Officer

As we enter the New Year, I would like to say for Lawyers Mutual's Board of Directors and staff that we are proud to continue to offer affordable professional liability insurance to the practicing bar of Kentucky. That is our number one goal, but for the reasons explained in the following paragraphs we need your help to maintain it.

Everything I have read in the last twelve months confirms that the insurance industry has entered its most challenging environment since Lawyers Mutual was founded. The claims of many insurance companies, both retail and reinsurance, were at unacceptable levels before September 11. The market was just beginning to reflect this when the September 11 catastrophe put an unprecedented strain on the entire risk transference industry. The result is that the insurance hard market predicted for a number of years arrived with a vengeance. Insurance premiums are going up in virtually all lines of insurance.

Similar to many other insurance companies, Lawyers Mutual's claims have increased over the last several years. As a result, we found it necessary to increase our base premium for the first time in eight years. While there are some new malpractice pitfalls and some exotic new malpractice theories of liability, most of the claims we receive are not unprecedented or unduly complex. My own opinion is that a good portion of the increase in Kentucky malpractice claims stems from the pressures caused by more lawyers in practice, more aggressive price shopping by consumers of legal services, and a tighter spiral of increasing law firm overhead around decreasing income per unit of service.

Why am I writing this? By and large, our claims drive our rates. If we, as practicing attorneys, are not more vigilant and careful, premiums will continue to increase. To avoid this, no matter how difficult, we must get cases filed on time. When we file on the last day, we must have the patience to wait and be sure the clerk issues a summons tolling the statute of limitations. Otherwise, the clerk might wait until tomorrow resulting in the client's action not being commenced within the limitations period — CR 3.01.

No matter how many real estate closings are needed to reach an acceptable income, titles must be updated to the moment of closing to cut off subsequent liens and the perhaps innocent — perhaps not — activity of people who often believe that money a borrower takes away from a closing is "income." We must, above all, stay on good terms with clients, taking the time to keep them informed, to listen to all their story, and to be sure they really do understand the advice to which they have consented.

Because Lawyers Mutual provides insurance only to Kentucky lawyers, our malpractice coverage and premium rates are exclusively in the hands of Kentucky lawyers. More frequent mistakes and more costly mistakes mean higher rates. Let us resolve to be more careful and more professional than ever before. It is good client service to do so <u>and</u> good risk management.

2001 MALPRACTICE REVIEW

The year 2001 was another bountiful year for lawyer entanglements with malpractice. In this issue we review cases and new developments reported in 2001 worth considering in your firm's risk management program.

✈ Immigration Law is the "New New" Thing in 2001

As a result of NAFTA and liberal immigration policies large numbers of immigrants have entered the US. Correspondingly, lawyers now see more clients with immigration law issues. This was not a high-risk area of practice because the authorities were liberal in enforcing immigration law and issuing visas. That all changed last September 11. Now immigration law is strictly enforced and poor legal advice can have severe repercussions.

Lawyers should advise all clients not US citizens to carry required documentation with them at all times; *e.g.* green card, student visa, or INS approvals. This is the law, but was not being enforced. It is now. Other considerations are:

- Lawyers defending immigrants in criminal cases are not considering the immigration consequences of pleading guilty to serious crimes. Conviction causes the immigrant to be subject to removal and ineligible for many, if not all, forms of relief from removal. It is essential that defense counsel know the unintended consequences of a guilty plea for immigrants when plea bargaining.
- Lawyers can expect to be asked to help alien clients prepare for border crossings. This requires a comprehensive review of a client's history to prepare the client for a searching background check when attempting to cross the US border. Refer to the US government's list of terrorist organizations in making this review.
- Immigrants who have overstayed their visa and are "out of status" may seek advice on how to apply for an extension. The old practice of returning to the appropriate

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consulate overseas to obtain a visa and return to the US is now problematic. There could be considerable difficulty in obtaining a new visa and re-entry in the US is no sure thing. If immigrant clients do leave the US on a trip, advise them to take their complete file of documentation authorizing US residency and an updated letter of employment. It may be appropriate to seek means other than leaving the US to regain legal status.

- Immigrants seeking permanent residency or citizenship may ask for legal advice in preparing application forms. Stress the absolute necessity for meticulous completion of all forms to avoid automatic rejection for an incomplete submission.
- Alien clients should be advised in the strongest terms not to miss an immigration hearing. If they do, they can expect to be pursued by the authorities and face removal.

See "Threat of Terrorism Yields Surge in Immigration" by Diana Digges, Lawyers Weekly USA, 2001 LWUSA 829, 10/15/01.

Divorce What's Hers? What's His?

Disputes involving division of marital property in divorce actions continued to increase in 2001. As a result of the proliferation of double income families, retirement plans, and investment options it is easy to err when sorting out what belongs to whom. What follows is a recap of recent decisions illustrating the problem:

IRAs and ERISA Plans:

- In New Hampshire a former wife was awarded the husband's IRA even though the divorce agreement provided that "each party is awarded any interest in … any IRA or other retirement account that each one may have … free and clear of any right title, interest or claim of the other." This language was found to be ambiguous in that it could be construed to mean the former wife could still be the beneficiary of the husband's IRA. It is significant to the result that the husband had not removed the wife as beneficiary of his IRA after the divorce. *New Hampshire Supreme Court, Estate of Tremaine v. Tremaine, No. 99-547, 7/31/01.*
- In Maryland a former wife who agreed at divorce that she had no interest in any of the husband's assets got his IRA benefits at his death because he never removed her as beneficiary of the account. *Maryland Court of Appeals, PaineWebber Inc. v. East, No. 44, September Term, 2000, 3/14/01.*
- In a Louisiana divorce action a wife agreed that she was not entitled to any of the husband's property. Since the agreement did not specifically include pensions, however, it was ruled the wife was entitled to a portion of the husband's pension payout. *Louisiana Supreme Court, Coleman v. Robinson, No. 99-C-3097, 1/17/01.*
- The US Supreme Court ruled federal law governing ERISA benefit plans pre-empts state law. Thus, a former spouse got her deceased ex-husband's life insurance and pension provided by his employer's ERISA plan because he failed to remove her as beneficiary before his death. *Egelhoff v. Egelhoff, 121 S.CT. 1322, 3/21/01*

Lessons Learned: IRAs have been in existence over 20 years and are now starting to become a bigger, if not the biggest, part of marital and estate assets. Do not rely on boilerplate language in drafting divorce agreements. Make sure the intent of the parties is covered in detail. Do not leave out asset classes – spell it out. Be sure to stress to divorce clients the urgency of changing IRA, ERISA plan, and insurance policy beneficiaries immediately upon final settlement. Do this verbally and in a closing letter.

Marital Property – Stocks, Stock Options, Trusts, and Inheritances:

- In Alabama assets owned prior to a marriage are not considered when dividing assets upon divorce unless the assets were used during the marriage for the couples common benefit. The wife in a divorce action claimed an interest in the husband's stock acquired before the marriage in a family business worth $7,000,000 because he used dividends from the stock for household expenses. It was ruled that the trial judge had discretion to consider the stock when dividing property and did not err in deciding not to do so. *Alabama Supreme Court, Ex parte Durbin, No. 1000775, 9/7/01.*
- In Massachusetts it was ruled that stock options that did not vest until after the divorce could in whole or part be considered marital property. If the options are for past services, they are marital property even though they had not yet vested. If the options are for future services, a percentage of the options are marital property determined by how long the employee owned the options during the marriage and the length of time between grant of the options and vesting. *Massachusetts Supreme Judicial Court, Baccanti v. Morton, No. SJC-08442, 8/13/01.*
- In Colorado a husband argued in a divorce action that his interest in a family trust was not marital property because his mother had the authority to terminate the trust at will. It was ruled that the mother's authority was a condition subsequent. The husband, therefore, has a present interest in the trust until the mother exercises her authority. Accordingly, appreciation in trust assets during the term of the marriage was marital property. *Colorado Court of Appeals, In re Marriage of Gorman, No. 00CA0998, 10/11/01.*
- In Alaska a husband inherited money from his mother several years before he separated from his wife telling her the funds could be used for their needs. She claimed a share when they were divorced because she had closed her own retirement account and left her job in reliance on those representations. The husband averred that he did not object to her taking those steps, but made no promise that they would share the inheritance. The court held that the husband made no changes that showed intent to convert his inheritance to marital assets. Nonetheless, the case was remanded for a determination whether equity required

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that a portion of the inheritance go to the wife. *Alaska Supreme Court, Sampson v. Sampson, No. S-9088, 12/15/00.*

Lessons Learned: Do not accept a divorce or estate planning matter involving complex financial issues unless you know what you are doing. Use experts in accounting, financial planning, and retirement programs to assist in asset evaluation. Ask clients detailed questions to be sure you have a complete inventory of assets. Use aggressive discovery to identify the opposing party's assets.

Disability Benefits:

- In Kansas a Veteran Administration disability benefit was considered in determining the wife's alimony. The husband argued that federal law prohibits these benefits from being divided. It was ruled that the alimony award was not an interest in the disability benefit. Rather the court merely considered these benefits in evaluating the overall economic situation of the parties to reach a fair result. *Kansas Court of Appeals, In the Matter of the Marriage of Bahr, No. 86,790, 9/28/01.*

Lesson Learned: This decision is consistent with rulings in eight other states and is the clear trend on this issue.

Personal Injury Settlement:

- In New Hampshire if a personal injury settlement is acquired during the marriage it is marital property subject to division upon divorce. At issue was an annuity that had four years to run after the divorce. The husband argued to no avail that this money was for pain and suffering and should not be included in the divorce settlement. *New Hampshire Supreme Court, In the Matter of Preston, No. 99-536, 10/3/01.*

Lesson Learned: If the asset was obtained during the marriage, it is difficult to exclude it from the divorce settlement.

Workers' Compensation:

- In Maine the husband received a $225,000 workers' compensation award four years before his wife filed for divorce. It was ruled that only the portion of the award that compensated the husband for lost wages prior to the divorce was marital property. *Maine Supreme Judicial Court, Doucette v. Washburn, No. CUM-00-382, 2/22/01.*

Lesson Learned: The purpose of the award; i.e., compensatory, pain and suffering, etc., may provide a basis to include or exclude assets from marital property. But see Personal Injury Settlement above.

The Hazards of Representing Older Adults

As older adults increase in number so do the legal services they require. While the legal issues are often prosaic, the older adult's situation frequently involves prickly considerations. Here are a couple of 2001 examples:

- In Virginia an older adult doctor opened a joint bank account with right of survivorship with his daughter. Ten years later the doctor added his wife to the account without the daughter's consent. In the month preceding the doctor's death the wife wrote 35 checks for over $100,000 in total. She cashed a check for $75,000 on the day the doctor died. The daughter sued the bank for adding the wife to the account without her consent. The court ruled that the account terms were broad enough to allow the doctor to unilaterally add an additional party to the account and denied the daughter's claim. *Virginia Supreme Court, Caine v. NationsBank, N.A., No. 002615, 9/14/01.*

Lessons Learned: Joint bank accounts are often used as a simplistic estate planning tool with the advantage for older adults of getting help with paying bills and avoiding probate for account assets. This approach, however, leaves the older adult vulnerable and may have the unintended result of favoring one relative over others when the older adult dies. A good alternative to the joint bank account is a power of attorney. The attorney-in-fact can help with the management of the account for all practical purposes as well as a joint owner and has a fiduciary obligation to act in the grantor's best interest that a joint owner does not have. A revocable living trust is another alternative to a joint bank account. In working with older adult clients on these kind of issues ascertain all potential family and intergenerational conflicts – be especially thorough if there are second marriages and step-relatives to consider. Some lawyers use a questionnaire on which clients list all their accounts and joint owners. Document the file with the advice given and with written client consent in all matters involving substantial amounts of money – gifts, settlements, and client trust account disbursements. See "Bank Added Name To Account, Not Liable" by Allison Bianchi, Lawyers Weekly USA 2001 LWUSA 801, 11/15/01.

- In Michigan a lawyer was requested by H on behalf of a widow in her 80s to draft a will for her excluding relatives and leaving everything to H, a durable power of attorney designating H as the widow's attorney-in-fact, and deeds making H a joint tenant with the widow with right of survivorship. A suit was brought a few months later on the then incompetent widow's behalf in which it was undisputed that H abused his attorney-in-fact powers by pilfering the widow's estate. The widow's appointed conservator then sued the lawyer for malpractice for failing to discourage the widow from appointing H attorney-in-fact. The court found that the widow appeared mentally competent at the time the power of attorney was executed and that the lawyer had reasonably inquired as to the widow's understanding of the legal significance of the power of attorney. He had no duty to assure that the client chose prudently. The client is in

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the best position to make that decision and the lawyer had no duty to second-guess the choice. *Persinger v. Holst, Mich. Ct. App., No. 224635, 12/4/01.*

Lessons Learned: As correct as the court's decision in this case seems, it is hard not to wonder about the lawyer. It is not unusual for a third party to contact a lawyer on behalf of an older adult. A lawyer in these circumstances must not forget that the older adult is the client and not the third party even if the third party is paying the lawyer's fees. It appears that the lawyer in this case saw his function primarily as that of scrivener, simply followed the third party's instructions, and did not engage in the sensitive client communications that older adult clients require. If he had done so, an older adult client and her family might have been spared a difficult experience.

2001 Federal Tax Law Shakes Up Estate Planning

"The Economic Growth and Tax Relief Reconciliation Act of 2001" makes important tax changes with significant impact on estate planning. Some major changes are:

- Graduated increases in the estate tax exemption.
- Reduced gift tax rate.
- Elimination of the step-up of asset basis at death on January 1, 2010.

The new law complicates estate planning because some of the changes are phased-in over a period of years and has a sunset provision effective in 2011. Lawyers are sending letters to all affected clients suggesting an in-office consultation. These consultations are oriented more often now on the desired ultimate outcome of the estate plan and elimination of intergenerational conflicts than on pure tax avoidance. Some lawyers make sure they consider all the implications of the new law by doing "what if" estate planning using the assumption that the client dies in each of the years of the phase-in period and lives to 2011. Other risk management considerations are:

- Use of standard formulas for funding certain shelters may no longer be appropriate. Under the new higher estate tax exemptions standard formulas such as "fund with the maximum that can pass without estate tax" may result in the shelter receiving more property than the client intended to the detriment of a surviving spouse.
- Another risk with standard formulas is that definitions may have changed for the terminology used. Boilerplate language should be reviewed for conformity with the new law's definitions.
- The elimination of the step-up basis at death in 2010 imposes a whole new concept of records keeping for many clients. Some lawyers are advising clients to retain all tax returns and investment account statements indefinitely, keep records of all home improvements, and organize all existing records of asset costs for future reference.

See "Lawyers Reviewing Estate Plans Under New Tax Law" by Reni Gertner, Lawyers Weekly USA, 2001 LWUSA 449, 6/11/01.

"Every great mistake has a split second when it can be recalled and perhaps remedied."

Pearl Buck

For more information about Lawyers Mutual, call (502) 568-6100 or KY wats 1-800-800-6101 or visit our web site at www.lmick.com

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