Lawyers Mutual
www.lmick.com

THE RISK MANAGER

A quarterly newsletter by Lawyers Mutual Insurance Company of Kentucky

SUMMER 2012
Volume 23, Issue 3

WHAT KENTUCKY LAWYERS NEED TO KNOW ABOUT THE ETHICS AND RISK MANAGEMENT OF CLOUD COMPUTING

Cloud Computing Defined: n. A loosely defined term for any system providing access via the Internet to processing power, storage, software or other computing services, often via a web browser. Typically these services will be rented from an external company that hosts and manages them. (The Free On-line Dictionary of Computing)

"You are going to look up one day and all you will be doing is managing the systems that connect all your printers." (Carl Ryden, MarginPro)

"Middle age is when the best exercise is one of discretion."

Laurence J. Peter

Introduction

Perhaps unknowingly, Kentucky lawyers are already using cloud computing in great numbers. The Pennsylvania Bar Association Committee On Legal Ethics And Professional Responsibility in Formal Opinion 2011-200 opens an evaluation of cloud computing with this observation:

> If an attorney uses a Smartphone or an iPhone, or uses web-based electronic mail (e-mail) such as Gmail, Yahoo!, Hotmail or AOL Mail, or uses products such as Google Docs, Microsoft Office 365 or Dropbox, the attorney is using "cloud computing." While there are many technical ways to describe cloud computing, perhaps the best description is that cloud computing is merely "a fancy way of saying stuff's not on your computer."

Formal Opinion 2011-200 is the best recent opinion on cloud computing that includes recommendations for protecting client confidentiality and risk management. It includes a review of other states ethics opinions reflecting a consensus that lawyers by taking the appropriate precautions may use cloud computing. In the absence of any known Kentucky authority specifically on the use of cloud computing by lawyers, this article reviews the key points of Formal Opinion 2011-200 along with other sources to assist you in your appreciation of what cloud computing means to the modern practice of law and the risks it invokes.

Just a Little More Definition

The Internet for Lawyers Website adds to the previous definition of cloud computing as follows:

- Cloud computing and "Software as a Service" (SaaS) are two terms used to describe similar services. They allow you to access software, or store files [STaaS -- storage as a service], on computers that are not at your physical location or even in your physical control.
- Dictionary.com defines Cloud Computing as: Internet-based computing in which large groups of remote servers are networked so as to allow sharing of data-processing tasks, centralized data storage, and online access to computer services or resources.

continued on page 2

continued from page 1

- Wikipedia defines SaaS as: "Software as a service, sometimes referred to as 'on-demand software,' is a software delivery model in which software and its associated data are hosted centrally (typically in the Internet cloud) …. [They] are typically accessed by users using a thin client, … using a web browser over the Internet." Gmail and Flickr are examples of cloud computing or SaaS products because they give you access to e-mail software and message storage, and photo storage (respectively) on computers at a remote location.

Editor's note: Wikipedia defines "thin client" as: A thin client (sometimes also called a lean or slim client) is a computer or a computer program that depends heavily on some other computer (its server) to fulfill its traditional computational roles.

The Teachings of Formal Opinion 2011-200

1. Benefits of using cloud computing:
   - Reduced infrastructure and management;
   - Cost identification and effectiveness;
   - Improved work production;
   - Quick, efficient communication;
   - Reduction in routine tasks, enabling staff to elevate work level;
   - Constant service;
   - Ease of use;
   - Mobility;
   - Immediate access to updates; and
   - Possible enhanced security.

2. The risks of using cloud computing providers include:
   - Storage in countries with less legal protection for data;
   - Unclear policies regarding data ownership;
   - Failure to adequately back up data;
   - Unclear policies for data breach notice;
   - Insufficient encryption;
   - Unclear data destruction policies;
   - Bankruptcy;
   - Protocol for a change of cloud providers;
   - Disgruntled/dishonest insiders;
   - Hackers;
   - Technical failures;
   - Server crashes;
   - Viruses;
   - Data corruption;
   - Data destruction;
   - Business interruption (*e.g.*, weather, accident, terrorism); and,
   - Absolute loss (*i.e.*, natural or man-made disasters that destroy everything).

   (ABA, "Issues Paper Concerning Client Confidentiality and Lawyers' Use of Technology" (Sept. 20, 2010))

3. Key professional responsibility rules implicated:
   - Rule 1.1, Competence ("Part of a lawyer's responsibility of competency is to take reasonable steps to ensure that client data and information is maintained, organized and kept confidential when required. A lawyer has latitude in choosing how or where to store files and use software that may best accomplish these goals. However, it is important that he or she is aware that some methods, like 'cloud computing,' require suitable measures to protect confidential electronic communications and information. The risk of security breaches and even the complete loss of data in 'cloud computing' is magnified because the security of any stored data is with the service provider.");
   - Rule 1.4, Communication ("[I]f an attorney intends to use 'cloud computing' to manage a client's confidential information or data, it may be necessary, depending on the scope of representation and the sensitivity of the data involved, to inform the client of the nature of the attorney's use of 'cloud computing' and the advantages as well as the risks endemic to online storage and transmission.");
   - Rule 1.6, Confidentiality of Information;
   - Rule 1.15, Safekeeping Property; and
   - Rule 5.3, Responsibilities Regarding Nonlawyer Assistants.

4. Reasonable care in selecting a cloud service provider:

Lawyers contemplating using cloud services must be sure that the selected provider takes reasonable precautions to back up data and ensure its accessibility when the user needs it. With this overarching consideration in mind Formal Opinion 2011-200

continued on page 3

"At any moment of the day at least two-thirds of the people around the world are awake and some of them are making mischief."

Dean Rusk

continued from page 2

includes the following risk management guidance for use in evaluating a prospective cloud service provider.

Does the provider have procedures for:

- Backing up data to allow the firm to restore data that has been lost, corrupted, or accidentally deleted;
- Installing a firewall to limit access to the firm's network;
- Limiting information that is provided to others to what is required, needed, or requested;
- Avoiding inadvertent disclosure of information;
- Verifying the identity of individuals to whom the attorney provides confidential information;
- Refusing to disclose confidential information to unauthorized individuals (including family members and friends) without client permission;
- Protecting electronic records containing confidential data, including backups, by encrypting the confidential data;
- Implementing electronic audit trail procedures to monitor who is accessing the data; and
- Creating plans to address security breaches, including the identification of persons to be notified about any known or suspected security breach involving confidential data.

The firm should ensure that the provider:

- Explicitly agrees that it has no ownership or security interest in the data;
- Has an enforceable obligation to preserve security;
- Will notify the lawyer if requested to produce data to a third party, and provide the lawyer with the ability to respond to the request before the provider produces the requested information;
- Has technology built to withstand a reasonably foreseeable attempt to infiltrate data, including penetration testing;
- Includes in its "Terms of Service" or "Service Level Agreement" an agreement about how confidential client information will be handled;
- Provides the firm with right to audit the provider's security procedures and to obtain copies of any security audits performed;
- Will host the firm's data only within a specified geographic area. If by agreement, the data are hosted outside of the United States, the law firm must determine that the hosting jurisdiction has privacy laws, data security laws, and protections against unlawful search and seizure that are as rigorous as those of the United States and … [Kentucky];
- Provides a method of retrieving data if the lawyer terminates use of the SaaS product, the SaaS vendor goes out of business, or the service otherwise has a break in continuity; and,
- Provides the ability for the law firm to get data "off" of the vendor's or third party data hosting company's servers for the firm's own use or in-house backup offline.

The firm should investigate the provider's:

- Security measures, policies and recovery methods;
- System for backing up data;
- Security of data centers and whether the storage is in multiple centers;
- Safeguards against disasters, including different server locations;
- History, including how long the provider has been in business;
- Funding and stability;
- Policies for data retrieval upon termination of the relationship and any related charges; and,
- Process to comply with data that is subject to a litigation hold.

The firm should determine whether:

- Data is in non-proprietary format;
- The Service Level Agreement clearly states that the attorney owns the data;
- There is a 3rd party audit of security; and,
- There is an uptime guarantee and whether failure results in service credits.

Internal firm responsibilities

- Employees of the firm who use the SaaS must receive training on and be required to abide by all end-user security measures, including, but not limited to, the creation of strong passwords and the regular replacement of passwords;
- Protect the ability to represent the client reliably by ensuring that a copy of digital data is stored onsite; and
- Have an alternate way to connect to the Internet, since cloud service is accessed through the Internet.

continued on page 4

"Cheats are always at the mercy of their accomplices."

Miguel Cervantes

continued from page 3

Conclusion

Formal Opinion 2011-200 concluded that:

> [An] attorney may store confidential material in "the cloud." Because the need to maintain confidentiality is crucial to the attorney-client relationship, attorneys using "cloud" software or services must take appropriate measures to protect confidential electronic communications and information.

This opinion is consistent with other jurisdictions that have considered lawyer use of the cloud. While none of these opinions is a substitute for Kentucky authority, it is difficult to think that we would rule differently and the risk management guidance in Formal Opinion 2011-200 is spot on. Accordingly, the information in this article should be helpful to Kentucky lawyers in avoiding malpractice claims and ethically using cloud computing services. We urge you to include in letters of engagement a description of all electronic transmission methods used when communicating client confidential information. In some cases it may be prudent to get client concurrence with the methods used and in others it may be necessary to avoid electronic communications over the Internet and cloud altogether. And always remember – when in doubt call the KBA Ethics Hotline.

Beware the Phantom Statute of Limitations in Some UM and UIM Insurance Contracts

Bob Breetz, Claims Counsel

In *Elkins v. Kentucky Farm Bureau etc.*, Ky.App., 844 S.W.2d 423 (1992) we learned that a contractual limitation period of one year to bring a UM claim was unreasonably short. Three years later the Supreme Court decided *Gordon v. Kentucky Farm Bureau etc.*, Ky. 914 S.W.2d 331 (1995). It was an UIM case which, as Elkins, had a contractual one-year limitation. Since the one-year limitation was invalid because it was unreasonably short and no other time limitation was in the policy, the court applied the fifteen-year provision for limitations on a written contract.

Lawyers Mutual has seen several instances of attorneys getting caught short because they believed that the fifteen-year rule applied universally to UM and UIM suits. Perhaps they didn't notice that the Supreme Court said in Gordon that insurance companies may shorten the fifteen-year period as long as the period was not unreasonable. Insurance companies took the hint and many policies now contain a two-year contractual limitation period. Lawyers Mutual is aware that this two-year contractual limitation period has been upheld as not unreasonable in several trial courts. There are no published appellate decisions on this issue as far as we are aware, but we strongly encourage, indeed exhort, our insureds to abide by the contractual provision. Make the Phantom Statute of Limitations part of your risk management litigation checklist.

Don't Let a Title Opinion Expose You to the Risk of Becoming the Deep Pockets When the Property Is Used as Security for a Business Loan that Goes Bad

A developing trend in the effort to hold lawyers responsible for business deals gone bad is for bank regulators to assert that lawyers performing title searches for property to be used as security for a business loan are also responsible for evaluating the soundness of the loan. To avoid this risk consider adding this paragraph to your title opinion letter of engagement:

> The undersigned has examined title to the subject property solely for the purpose of determining the status of ownership of the subject property. The undersigned has not been requested to, and has not, evaluated the financial soundness of the borrower or the sufficiency of value of the property as collateral for any loan, and expressly disclaims any liability for the decision to enter into the loan, which decision is completely the responsibility of the institution making said loan.

continued on page 5

"A difference of taste in jokes is a great strain on the affections."
George Eliot (Mary Ann Evans)

continued from page 4

This issue suggests it is a good time to review risk management of title opinions. The following is a list of frequent title opinion errors:

- Erroneous description in deed of property to be conveyed
- Misstated date to which interest was to be computed
- Failure to fill in blank on form
- Failure to reserve mineral rights
- Failure to advise on impending change in law
- Unauthorized delay or failure to strictly enforce closing time limits
- Failure to discover encumbrances on the property:
  - mortgage lien
  - vendor's lien
  - tax lien
  - mechanic's lien
  - contract for deed
  - right-of-way
  - mineral lease
- Failure to assure that clients received or conveyed title as represented:
  - remainder
  - dower
  - outstanding life estate
  - lease
- Failure to perfect security interest:
  - failure to prepare mortgage document
  - failure to update title search at time of closing
  - failure to record or timely record a mortgage
  - filing in the wrong county
  - failure to obtain releases of other encumbrances
- Failure to collect or protect security interest
- Failure to attend commissioner's sale
- Failure to know other applicable law, *e.g.*, probate, tax
- Failure to disburse sale proceeds properly

Our standard risk management advice on title opinions is: Always use a letter of engagement to document the work to be done. Is the lawyer to prepare an abstract of title indicating only what land records contain or a title opinion on validity of ownership? Is the search for liens only? Is the lawyer responsible for accuracy through the date and time of the completion of the title search or required to bring the search current to the time of closing? Be precise, detailed, and exclusive in the scope description.

1. Specify in the abstract or opinion the scope of the search, its purpose, authorized uses, and restrictions.
2. If others are preparing evaluations on some parts of the transaction, clearly exclude those parts. If there is reliance on an expert opinion as part of the analysis (*e.g.*, an environmental assessment), show that in detail.
3. Be complete. Advise of any doubts or potential title defects no matter how remote. Taking risks on defects is the client's decision – not the lawyer's.
4. Establish office procedures for quality control of title search documents. Procedures should indicate who is authorized to sign and release them for the firm and provide for a formal and cold review before release.

Keeping Up With the Uniformed Services Former Spouses' Protection Act (USFSPA) Is a Risk Management Must for Kentucky Lawyers Whose Practice Includes Divorce Matters

A few years ago the Kentucky Commission on Military Affairs estimated that there were 24,000 military retirees and family members living in Kentucky receiving $370,000,000 in retirement benefits. No doubt those numbers are even larger today. In this era of "Grey Divorce" the odds are that you will be asked to represent one of the spouses in a military retiree divorce. Getting the division of the retirement pension wrong is a malpractice error that can result in a huge liability when multiplied over the life of the parties.

The recent Kentucky Court of Appeals decision in *Copas v. Copas* (Nos. 2009-CA-000685-MR, 2009-CA-000720-MR (2/3/2012)) is an instructive opinion that is the place to start in coming up to speed on the USFSPA. The case concerned a divorce that occurred at the time Richard had served 21 years and 9 months on active duty during the marriage. He continued to serve on active duty after the divorce retiring with 30 years of active service. The family court's property order ruled that the amount of Richard's military pension attributable to the marriage (21 years and 9 months) be divided equally between Richard and his former wife, Kathy.

Several years prior to Richard's retirement, and contrary to the court's finding, Kathy requested the Defense Finance and Accounting Service (DFAS) to award her 50% of Richard's 30-year pension when he retired.

continued on back

"An education isn't how much you committed to memory, or even how much you know. It's being able to differentiate between what you know and what you don't."

Anatole France

Lawyers Mutual
www.lmick.com

Waterfront Plaza
323 West Main Street, Suite 600
Louisville, KY 40202

PRESORTED STANDARD
U.S. POSTAGE
PAID
LOUISVILLE, KY
PERMIT NO. 879

Malpractice Avoidance Update
Member National Association of Bar Related Insurance Companies

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

continued from page 5

Upon Richard's retirement, and for reasons not clear, DFAS approved this request and awarded Kathy 50% of his pension based on 30 years of service and not on of 21 years and 9 months as ordered by the family court.

The case was further complicated by a monthly reduction of $568.00 in Richard's military pension based on the Veterans Administration (VA) finding that he was 40% disabled. This amount was then paid to Richard by the VA leaving the husband with the same amount of pension, but from two different sources.

In a series of motions beginning in 2007 Richard asked the family court to direct DFAS to compute Kathy's share based only on 21 years and 9 months of service. Kathy countered by asking for 50% of the pension based on 30 years of service and also asked that her share be calculated including the disability payment from the VA.

The family court modified its order to instruct DFAS that Kathy was to receive 50% of the pension based only on 21 years and 9 months of service. It also instructed DFAS to take the disability payment into consideration in its computation of Kathy's share of the pension. Both parties challenged the court's ruling via an appeal and cross-appeal.

In sorting out this confusing situation the Court of Appeals provides Kentucky lawyers with something of a clinic on the USFSPA complete with numerous citations covering both substantive and procedural issues. In short, the Court concluded that Kathy was entitled only to share in the portion of Richard's pension attributable to the 21 years and 9 months of marriage during his service. She was not entitled to any part of the pension he earned after the divorce. Additionally, in the face of clear law on point, the Court held that the VA disability pay was not subject to the USFSPA and she was not entitled to share in it.

We urge you to read and download this opinion for future reference. The DFAS publication on dividing military retired pay cited in the opinion is available on the Internet at http://www.dfas.mil/garnishment/usfspa/attorneyinstructions.html. On reaching the site click on "Guidance for dividing retired pay and sample language for court orders." We also recommend downloading this 20-page guide and making it a part of your USFSPA file.