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THE RISK MANAGER

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"If at first you don't succeed, you're running about average."

Mardy Grothe in "ifferisms"

DON'T TRIP OVER THE RECENT KENTUCKY COURT OF APPEALS INTERPRETATION OF CR 8.01

In *O'Rourke v. Lexington Real Estate Co.** the Court of Appeals construed the requirements of CR 8.01 in a way that surprised many Kentucky lawyers. The case concerned the award at trial of attorney's fees to Lexington Real Estate. O'Rourke appealed resulting in a favorable ruling for him that included this language:

> Moreover, for another sound reason the attorney fees claim against O'Rourke must fail. In the complaint, a party must state in plain and adequate terms the basis for any claim. *Caldwell v. Frazier*, 304 S.W.2d 922 (Ky. 1957). CR 8.01 provides that a claim (sic) "shall contain (a) a short and plain statement of the claim showing that the pleader is entitled to relief, and (b) a demand for judgment for the relief to which he deems himself entitled." Our review of the complaint filed herein reveals that Lexington Real Estate failed to properly plead any claim for attorney's fees, and certainly no claim under KRS 383.660(3). Although the complaint requested an award of attorney's fees in the *ad damnum* clause, it failed to state any claim for attorney's fees in the body of the complaint. CR 8.01 requires notice of the claim, and O'Rourke was not given notice of any acts or omissions alleged against him that would authorize application of KRS 383.660(3). Although KRS 383.660(3) creates a limited exception to the general rule that each party shall pay its own attorney's fees, to invoke that exception notice of the claim must be pled to join the issue. See *Pike v. George*, 434 S.W.2d 626 (Ky.App. 1968).

Read this case and risk manage your pleadings accordingly.

**No. 2010-CA-000108-MR, 10/7/2011. Motion for discretionary review has been filed.*

On December 1, 2011, the 2011 Amendments to the Bankruptcy Rules of Procedure went into Effect

The 2011 Amendments are available on the U.S. Bankruptcy Court, Western District of Kentucky website. While all are important, we especially alert you to the extensive changes in the Bankruptcy Court Miscellaneous Fee Schedule. They include:

Part B. Initial Filing Fees
Part C. Fees for Splitting Cases
Part D. Fees for Converting Cases
Part E. Fees for Interdistrict Transfer
Part F. Miscellaneous Contested Proceedings Fees
Part G. Fees for Complaints/ Adversary Proceedings
Part H. Filing Fees for Appeals and Cross Appeals
Part I. Fees Due Upon Dismissal
Part J. Fee for Reopening Cases
Part K. Miscellaneous Administrative Fees
Part L. Fee Schedule for Electronic Public Access

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Missing a required fee payment risks missing a time limitation that could lead to a malpractice claim. Go to the Western District of Kentucky website for all the details at http://www.kywb.uscourts.gov/fpweb/index.htm. (*last viewed on* 12/13/2011)

With the promulgation of the new Bankruptcy Rules, it is timely to review our bankruptcy practice risk management advice. This advice was encapsulated in the KBA *Bench & Bar* article "Hard Economic Times Mean More Malpractice Claims" (Vol. 73, No. 1, 1/2009). The article reported on the ABA program "The Unique Perils of Representing Parties in Bankruptcy" that included these significant risks of bankruptcy practice:

- Certification by attorney – the signature of a debtor's lawyer certifies that a bankruptcy filing is not an abuse.
- Mandatory advice – bankruptcy law requires that a client be given certain advice.
- Major bankruptcy deadlines in unlikely places – *e.g.*, filing proof of claims; real estate lease assumptions; deadlines for filing Plans of Reorganization.
- Risks of collusion with other bidders in bankruptcy auctions.
- Jurisdictional risks – filing proof of a claim may give unwanted jurisdiction to the bankruptcy court over counterclaims brought by the debtor.
- Violations of Automatic Stay.
- Transfers and Consequences – voidable preferences; fraudulent transfers; fees paid by the wrong entity; "asset planning"; attorney holding funds; and violation of security agreements.
- Potential plaintiffs are increasing in number:
    1. Debtor-in-Possession – 11 U.S.C. §1107
    2. Chapter 7 Trustee – 11 U.S.C. §§701-2
    3. Chapter 11 Trustee – 11 U.S.C. §1104
    4. Creditors' Committee
    5. Chapter 11 Plan Trustee or Administrator – 11 U.S.C. §1123(b)(3)
    6. Individual Creditors
    7. State Receivers

The ABA granted permission to post the program materials on Lawyers Mutual's website. It is a good review of the malpractice risks of practicing bankruptcy law and recommended professional reading for all lawyers. Go to www.lmick.com, click on Resources, Subject Index, and look for the article *The Elevated Risks Associated with Insolvent Clients* under Bankruptcy.

An overriding risk of practicing law in hard economic times is that lawyers are tempted to accept matters outside their competence. With more clients and potential clients facing insolvency there is a temptation to dabble in bankruptcy. If you are not a well-qualified bankruptcy lawyer, do not give in to this temptation unless you are prepared to make the intense effort required to competently represent your client. If a current client needs advice on insolvency, do not hesitate to associate with a lawyer with bankruptcy law experience. Overcome your fear that you will lose the client. The pitfalls of bankruptcy law are just too great for on-the-job training.

The Kentucky Court of Appeals Addressed Attorney-Client Privity and Lawyer Liability to Third Parties in *Anderson v. Pete* *

This opinion is an excellent review of Kentucky malpractice law covering when an attorney-client relationship comes into existence and when duties are owed to unrepresented intended beneficiaries of an action. The underlying case concerned a wrongful death action against the employer of a driver killed in a motor vehicle accident and loss of consortium for the deceased's wife, Elizabeth. Plaintiff's lawyer, Pete, did not name two minor children, Michael and Malik, as plaintiffs and the action did not include claims for loss of consortium/parental love and affection for the children. After the case was lost and the appeal dismissed, a professional negligence case was brought against Pete on behalf of Michael and Malik.

Pete filed a motion for summary judgment "alleging the suit was barred because there was no attorney-client relationship between Pete and the children and because any other claims of the Estate had since been barred by the statute of limitations. The motion was granted by the Jefferson Circuit Court on the grounds that Michael and Malik did not have privity with Pete, and thus did not enjoy an attorney-client relationship with Pete and lacked standing to sue for professional negligence."

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"If at first you don't succeed, try reading the instructions."

Evan Esar

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Privity

The Court of Appeals first considered whether there was a basis to conclude that Michael and Malik had an attorney-client relationship with Pete as Elizabeth claimed she believed:

> The existence of an attorney-client relationship "is a contractual one, either expressed or implied by the conduct of the parties." *Daugherty v. Runner*, 581 S.W.2d 12, 16 (Ky. App. 1978). Restated, the attorney-client relationship need not necessarily arise by contract, but may also arise through the conduct of the parties. *Lovell v. Winchester*, 941 S.W.2d 466, 468 (Ky. 1997). If the relationship is to arise through the parties' conduct, it must be born of a "reasonable belief or expectation" on the part of the would-be client that the attorney has agreed to undertake the representation. *Id*.
>
> Our Supreme Court has recently laid to rest any dispute over whether an attorney may have an attorney-client relationship with a minor in the case of *Branham v. Stewart*, 307 S.W.3d 94, 95 (Ky. 2010). In *Branham*, the high Court held that an attorney representing a minor's next friend on behalf of a minor is in an attorney-client relationship with the minor as a real party in interest and owes professional duties to the minor. *Id. at* 95. The minor is also said to be in privity with the attorney, despite their minority. *Id. at* 99.
>
> ….
>
> In the present circumstances, since Michael and Malik stood to be awarded one-half of any damages recovered in the wrongful death action, it seems quite reasonable that Elizabeth would have believed that Pete was representing the children and raising any and all available claims on their behalf. As such, we are compelled to reverse the trial court's summary judgment.

Third Party Beneficiary Liability

Next the Court considered whether Pete owed Michael and Malik duties as third-party beneficiaries intended to be benefited by Pete's performance:

> [T]here "is no privity requirement for legal malpractice actions in Kentucky." *Sparks v. Craft*, 75 F.3d 257, 261 (6th Cir. 1996). Instead, an attorney can be held "liable for damage caused by his negligence to a person intended to be benefited by his performance irrespective of any lack of privity." *Hill v. Willmott*, 561 S.W.2d 331, 334 (Ky. App. 1978), quoting *Donald v. Garry*, 19 Cal. App. 3d 769, 97 Cal. Rptr. 191 (1971).
>
> When an attorney is retained to file a wrongful death action by the administrator of an estate, the attorney clearly intends to benefit both the client estate and the individuals in the estate who will receive a share of the damages under KRS 411.130 should he successfully defend the suit. They are two sides of one coin that cannot be logically divided from one another. Indeed, the individuals named in KRS 411.130(2) are the real parties in interest in such a suit. *Vaughn's Adm'r*, 179 S.W.2d at 445.
>
> Thus, on remand, even if Pete is found not to be in privity with Michael and Malik because discovery reveals that the parties contracted for him to represent Elizabeth solely and not the children, he will still have owed duties to Michael and Malik as intended beneficiaries of the wrongful death action. Thus, the result is inescapable that Pete owed a duty to Michael and Malik – whether as attorney to client or as *attorney to intended beneficiary*.

Put this decision at the top of your risk management professional reading list.

** No. 2010-CA-000472-MR, 10/7/2011. Motion for discretionary review has been filed.*

Carelessness with Client Files Exposes Two Law Firms to Serious Malpractice Exposure

Case I: In Minneapolis a mother discovered her daughter drawing on paper given to her at school which contained on the back detailed medical information about a woman. It was soon learned that a paralegal working at a Minneapolis law firm had, rather than destroying old documents, donated them to the daughter's school. Needless to say the woman whose confidentiality was breached is upset and the law firm has a serious problem with her and other clients whose confidential information was revealed.

Case II: *The Baltimore Sun* recently reported this careless handling of electronic files:

> A Baltimore law firm lost a portable hard drive containing information about its cases, including medical records for 161 stent patients suing [a] cardiologist … a firm client, for alleged malpractice….
>
> The drive was lost Aug. 4 by an employee of Baxter, Baker, Sidle, Conn & Jones who was traveling on the

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In-house counsel from left to right: Pete Gullett, Jane Broadwater Long, Del O'Roark, Bob Breetz

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"If at first you do succeed, try to hide your astonishment."

Mardy Grothe in "ifferisms"

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> Baltimore light rail, according to a letter obtained by *The Baltimore Sun* that was sent to one of the stent patients last week – two months after the drive went missing.
>
> The storage device held a complete back-up copy of the firm's data, including medical records related to the stent malpractice claims, along with patient names, addresses, dates of birth, social security numbers and insurance information.
>
> It was taken home nightly as a security precaution in case of fire or flood, a firm spokesman said, though ***the portable information was not encrypted*** – among the most stringent security precautions that is standard practice for health professionals dealing with medical records. (*emphasis added*)

In Case I obviously the paralegal made a serious mistake, but so must have the firm's management in not assuring that the paralegal knew client confidentiality requirements and file destruction procedures. In addition to meeting your professional responsibility to train paralegals (*see* SCR 3.130(5.3), Responsibilities Regarding Nonlawyer Assistants), be sure your firm has written file management and destruction procedures. For file destruction we recommend that:

- At the conclusion of a matter assign the file a closed file index number.
- Check for outstanding fees and proper client trust account documentation.
- Return client property such as original documents being sure to copy any returned documents necessary for the firm to have a complete file.
- Strip the file of duplicate documents, *etc*. – do not remove work product such as drafts, phone messages, or research notes.
- Send a closing letter to the client.
- Assign a file destruction date and calendar it in the office closed file index.
- At the time a file is calendared for destruction notify the client by certified mail. Advise that in the absence of instructions to the contrary the file will be destroyed after the date indicated in the notice.
- If the client cannot be located, files may be destroyed in the lawyer's sound discretion. KBA E-300, however, advises that these files should be destroyed only if they contain no important papers.
- In destroying files client confidentiality must be preserved. Firms in states with paper recycling laws failing to shred documents or disposing of files in clear plastic bags have had problems. Literal destruction of the file is recommended – shred or burn.

In Case II it is ironic that in an effort to safeguard client information the firm managed to expose itself to a major breach. It is worse than ironic that the firm would not think to encrypt the data on such an important electronic file that was routinely carried out of the office. In our Spring 2011 Newsletter we offered this checklist from the article *Serious About Confidentiality* (The National Law Journal, October 18, 2010) by Michael Downey of Hinshaw and Culbertson:

1. Adopt clear policies and educate all personnel about the proper use and disclosure of client confidences, including to the media and on the Internet, and the consequences of noncompliance.
2. Purchase travel laptop computers and flash drives protected by full disk encryption, and insist that lawyers and staff use such protected devices when they travel with client-related or other sensitive information.
3. Ensure that all computer systems, scanner/copiers and smart phones that can send and receive data have password protections activated.
4. Ensure that people who have access to firm facilities and information can pass reasonable background checks and agree in writing to preserve confidences.
5. Keep the most sensitive information off the Internet, or at least secured on document-management systems.
6. Provide for secure disposal of confidential information at each workstation, as well as at copiers, printers and the like, and also for secure disposal of any computers (home or office) or data-storage devices that might contain firm-related information.
7. Assess whether the firm should purchase additional insurance or equipment to protect against data disclosure.
8. Plan now how the firm will respond to any disclosure that may occur, including how notice will be given to regulators, affected clients and the public, and what actions the firm will take to re-establish protection and sanction anyone who caused the disclosure.

Lawyers Mutual
www.lmick.com

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

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Do You Really Understand Why You Make the Decisions You Do as Lawyer or Judge?

Thinking Fast and Slow by Daniel Kahneman

Thinking Fast and Slow, acclaimed as one of the ten best books of 2011, is an analysis of just how the mind works in reaching the conclusions it does. It has enormous application to the practice of law and judicial decision-making. Do you know what the "anchoring effect" is and how it can skew settlement negotiations and judicial rulings? Are you subconsciously over-weighting improbable events and settling a case when the better course of action is to go to trial? *Thinking Fast and Slow* is a fascinating study of these and many other situations. It offers a special opportunity to reflect on what is really going on in the mind as complex matters are decided. We recommend it as the Risk Management Book of the Year.