

Mediating the professional-liability case

Both substantive legal issues and practical insurance matters must be addressed to resolve these cases

By Bruce A. Friedman

The professional-liability case presents a number of interesting substantive and insurance coverage issues that must be addressed in mediation in order to settle the case. The substantive elements of the claim must be addressed in terms of what is required to prove the case. Insurance issues such as burning limits policies, the consent/hammer clause and cross claims for fees also may be involved in the case and may need to be resolved in order to reach a settlement.

First things, first

Prior to the mediation, the parties need to brief and prepare to discuss the elements of the claim which include duty, breach, causation and damages. First, duty must be addressed and may present an issue depending on whether the claim is made by a client, a third party, or whether the professional has a legal duty with respect to the subject matter of the claim. In a legal malpractice context, there may be an issue as to whether there was an attorney-client relationship between the parties. This issue looms large in accountant malpractice cases as most courts have limited the ability to assert such claims to those in privity with the accounting firm. Duty may also be a significant issue in an insurance agent/ broker malpractice claim. Whether the insurance professional is acting as an agent of the insurance company or as a broker for the policyholder may negate or create a duty to the policyholder claiming inadequate insurance coverage. The scope of an insurance professional's duty to the policyholder has been circumscribed by the courts in terms of claims arising out of inadequate insurance limits unless the professional has assumed a duty by providing his opinion on limits or coverage.

Professional liability

Professional liability claims by third parties not in direct privity with the professional raise the issue of duty. Courts have recognized such claims where the third party can show that it was reasonable for the professional to assume that third parties would rely on the professional's work or opinion. Lawyers providing opinions with respect to the sale of securities may be exposed to claims by investors, as may accountants who reviewed or audited financial statements that are used by their client in connection with obtaining loans or raising capital. In the real estate agent context, a party may claim a duty owed to him by the real estate professional who represented the other party to the transaction in terms of documenting the deal. Obviously, appraisers and escrow companies may confront claims arising out of real-estate loan transactions by parties not in direct privity with them.

Breach of duty

Breach of duty is the next element of the claim that must be addressed. In the legal malpractice context, this issue often arises in the context of a conflict of interest claim requiring the analysis of whether or not a conflict actually existed and whether it was waived. The issue of whether or not the accountant breached a duty to discover financial fraud is often the focus of an accountant malpractice claim. Accountants argue that they do not have a duty to uncover fraudulent conduct on the part of employees of their client or the entity itself, but this issue is countered by the argument that had the accountants properly performed the audit, the fraud would have been exposed.

Causation

Now we arrive at the causation element or the question of whether the negligence of the professional was the cause of the loss. Causation is a very significant factor in professional-liability cases, particularly legal malpractice claims. In order to prove causation in a transactional malpractice claim, the client is required to show that he would have made a better deal or would have walked away from the deal had the lawyer properly negotiated the transaction. This can be a very difficult burden to overcome, particularly if the adverse party in the underlying transaction testifies that he would have never agreed to the contract term that the client says should have been in the agreement. Causation may also be a fundamental issue in the accountant malpractice context in a case where an entity has suffered financial losses or filed for bankruptcy. Was it the negligently prepared financial statements that caused the loss or bad business decisions by management? In the insurance agent/broker case, the issue of causation is often raised by the argument that it was not the agent/broker's fault in not obtaining the proper coverage, but the insurance company's wrongful denial of a claim under the policy procured by the agent/broker.

Insurance coverage

If the professional liability case wasn't already complex enough, many cases also present numerous insurance coverage related issues. One issue may be the limits of the malpractice policy. These

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policies are referred to as burning-limits policies meaning that defense costs diminish the limits. In a case where a professional has a million dollar limit, the expenditure of a few hundred thousand dollars in defense costs reduces the amount available for settlement to the remaining six figures in the policy. When that is not enough to cover the damages, the situation presents the parties and the mediator with some challenges.

Continued defense of the case will further reduce the amount available for settlement or payment of a judgment and may leave the professional defendant with personal exposure. This may put a lot of pressure on the insurer, defense counsel and the professional defendant to settle the case at mediation. It also puts the professional and his insurer in an adversarial relationship that is delicate and difficult for the mediator to address during the mediation unless the professional is represented by personal counsel.

The professional liability policy also requires the consent of the professional to settle the case. There are cases in which the professional does not want to consent and may have legitimate reasons for not doing so. Perhaps the case includes a cross claim for fees, and the professional does not believe that the malpractice claim has any merit and wants to collect fees due for professional services. The insurer, on the other hand, may want to settle the case either because it assesses the risk of loss differently than the insured or it is concerned about the damage exposure in excess of limits or wants to limit the amount of ongoing defense expenses. The insurance policy does have a provision commonly referred to as a "hammer clause" which provides that if the insurer could have settled the case and the insured will not give his consent, then the exposure covered by the insurance policy is limited to the amount of the putative settlement. This is a thorny issue that the mediator must address in order to reach a settlement.

The successful resolution of a professional liability case involves the juggling of several moving parts. They include presentation and understanding of the elements of the claim, the underlying action or transaction, insurance issues that may be present in connection with the claim and/or an appreciation and understanding of the parties' feelings about the case. The parties and the mediator must work through these issues with counsel in order to create a path to settlement of the case.


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