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IN-HOUSE OPS

E&O Goes In-House

Employed Lawyers Professional (ELP) Liability coverage may help to protect corporate counsel

By Diana Shafter Gliedman / Anderson Kill

Attorneys understand that every job and client brings with it the potential for great reward . . . and the possibility of a lawsuit. As such, law firms and solo practitioners purchase professional liability insurance coverage, also known as errors and omissions (E&O) or legal malpractice insurance, to protect themselves from claims of negligence or malpractice. But lawyers working in private practice are not the only legal practitioners who need to be wary of legal malpractice claims. The past 10 to 15 years have seen a sharp increase in the number of lawsuits brought against in-house counsel by creditors, customers, shareholders, trustees, government regulators and even their own employers. And as in-house lawyers face increased scrutiny, in-house legal departments must scrutinize their insurance programs to ensure that in-house legal staff is adequately protected.

D&O Is Not Always the Answer

Many companies rely on directors and officers (D&O) insurance policies to protect against lawsuits implicating in-house counsel. Traditionally, D&O insurance is designed to protect executives, outside directors and the companies they serve against liability arising from actions taken in the course of doing business. This, of course, raises the question of precisely who constitutes a director, officer or executive. If an in-house counsel is not a director or officer, he or she may end up with no insurance coverage whatsoever. As such, it is crucial that companies amend the policy's definition of directors and officers and/or insured persons to include the general counsel and that they endorse their D&O policies to include all in-house lawyers.

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Even when in-house counsel constitutes an insured person, however, traditional D&O policies frequently do not provide adequate coverage for claims that arise out of the provision of legal services. Some D&O policies contain professional services exclusions that purport to exclude coverage for claims "related to the rendering of, or failure to render, professional services." D&O policies may also contain insured versus insured exclusions, which bar coverage for claims against one insured party by another. Thus, an in-house lawyer may find him or herself with no recourse if sued by the corporation or a member of the board.

Scrutinize insurance programs to ensure that in-house legal staff are adequately protected.

E&O Goes In-House

While traditional E&O policies do not cover claims against in-house counsel, professional liability insurance specifically designed for in-house counsel is becoming increasingly common amongst corporations looking to protect their in-house legal staff. These policies, generally referred to as employed lawyers professional liability policies, or ELP policies, are specifically tailored for lawyers employed by public, private or nonprofit entities and can provide coverage for a company's entire legal team, including paralegals, clerks and patent administrators, as well as lawyers. ELP policies typically cover claims for legal malpractice arising out of legal work that an employed lawyer performs for her company or organization. These may be claims brought by third parties – such creditors, regulators or shareholders – or internal claims brought by other employees or executives. ELP policies may also provide coverage for pro bono services, disbarment and professional disciplinary proceedings, and other claims not covered by D&O policies.

But while ELP policies fill the void left by traditional E&O and D&O policies, in-house counsel should not breathe *too* deep a sigh of relief. Like all professional liability policies, ELP policies are rife with exclusions, conditions and ambiguous language, which insurance companies may rely upon to deny coverage. Although there is almost no existing case law specifically interpreting the scope, reach and intent of ELP coverage, an examination of existing cases interpreting the scope and reach of typical E&O policies sheds light on likely future battles between covered in-house counsel and their ELP insurance companies:

Conduct exclusions: Conduct exclusions, included in almost all ELP policies,

typically exclude coverage for deliberate, fraudulent or criminal acts; illegal personal or financial gain; and/or *intentional* violations of the law. Although most insurance companies will pay defense costs until a final adjudication demonstrates intentional wrongdoing (as opposed to negligence), some insurance companies will halt defense payments if there is an adverse finding of fact during the course of litigation. Policyholders should look for policies that explicitly provide coverage until there is a final adjudication of wrongdoing. Policyholders should also remember that in almost every state, where there is even a *chance* that a part of a claim will be covered, the insurance company has a duty to defend the entire claim. See, *e.g., Bullis v. Minn. Lawyers Mut. Ins.* Co., 2007 U.S. Dist. LEXIS 91457 (D.N.D. Dec. 10, 2007). Thus where a complaint alleges that an attorney has engaged in wrongful acts but also alleges a negligent act, error or omission, that attorney will be entitled to a full defense. Where the complaint raises only allegations of fraud, however, there may be no coverage. *Ill. State Bar Ass'n Mut. Ins. Co. v. Cavenagh*, 2012 IL App (1st) 111810 (Ill. App. Ct. 1st Dist. 2012).

Fortunately, most lawyers' E&O policies contain innocent policyholder provisions, which provide that policyholders who did not commit or participate in committing the wrongful acts at issue are entitled to coverage, notwithstanding any applicable conduct exclusion. See *Nat'l Union Fire Ins. Co. of Pittsburgh, PA v. FDIC.*, Civ. Action No. 3-90-0492-H, 1991 U.S. Dist. LEXIS 21824 (N.D. Tex. Jan. 25, 1991) (finding that an "Innocent Insured Provision serves at least two purposes. . . . It insures coverage to those who work on the matter in which the criminal or fraudulent conduct occurs, but do not participate in that conduct. The second purpose is to protect the firm itself.")

Prior acts and prior knowledge exclusions: ELP insurance policies typically exclude coverage for pending or prior litigation, proceedings, investigations or claims. Many insurance companies also seek to preclude coverage for any acts or circumstances occurring prior to a policy period, which an attorney knew or could have reasonably foreseen would result in a claim. Unsurprisingly, many insurance companies rely upon these exclusions to deny coverage for otherwise covered claims.

Such was the case in *Liberty Ins. Underwriters Inc. v. Corpina Piergrossi Overzat & Klar LLP*, 78 A.D.3d 602 (N.Y. App. Div. 1st Dep't 2010). In *Corpina*, a law firm represented a client in connection with a medical malpractice claim for personal injuries allegedly caused by vaccinations administered when the client was an infant. *Id.* at *1. During the course of the representation, an associate at the law firm wrote a letter to the client's father, informing him that the deadline to file a claim under the National Vaccine Injury Compensation Program (NVICP) was approaching and requesting materials to complete said application. *Id.* The application was never filed, the deadline passed, and the firm ceased its representation of the client. Shortly thereafter, the law firm purchased its first legal malpractice policy from Liberty Insurance Underwriters.

Some years later, the former client's new attorney advised the law firm by letter that he had been retained to prosecute a legal malpractice claim based on the failure to file the NVICP claim. *Id.* According to the new attorney, the failure to file the claim not only focused on compensation under the NVICP but also barred any civil actions for damages, including a medical malpractice action. The law firm promptly provided notice to Liberty. Rather than defend, however, Liberty brought a declaratory judgment action against the law firm, arguing that the policy excluded coverage for "any claim arising out of a wrongful act occurring prior to the policy period if . . . you had a reasonable basis to believe that you had breached a professional duty, committed a wrongful act, violated a Disciplinary Rule, engaged in professional misconduct, or to foresee that a claim would be made against you." *Id*

The law firm argued that even if the associate (and, by imputation, the law firm) knew of the NVICP and the deadline, the law firm did not know that the failure to file a timely administrative claim under the NVICP had the additional legal consequence of foreclosing any civil action for damages. On appeal, the Appellate Division, First Department, applied a two-pronged test in which the court "must first consider the subjective knowledge of the insured and then the objective understanding of a reasonable attorney with that knowledge." *Id.* at *2. More particularly, the court stated, "the first prong requires the insurer to show the insured's knowledge of the relevant facts prior to the policy's effective date, and the second requires the insurer to show that a reasonable attorney might expect such facts to be the basis of a claim." *Id.* [citing *Executive Risk Indem.*]