

Why be concerned about what's happening with claims?

For the past several years, we have been sounding warning bells about consistent increases in claims numbers and costs. This year, those bells are ringing more loudly than ever.

In articles, presentations, our annual report and our Report to Convocation we have been reinforcing with the profession that a worsening claims picture puts pressure on the whole insurance program, and especially on premium stability.

But that message has often been lost (or only slightly heard) during exceedingly good times when the economy boomed and, for reasons unrelated to claims experience, we were able to keep premiums at near-record low levels. After all, as long as the principal barometer (premiums) is holding steady, why worry about what is happening in the background?

Every additional \$1 million in expense to LAWPRO adds about another \$50 per year to the base premium for each lawyer.

We at LAWPRO were and are concerned. And you should be too. This special issue of LAWPRO Magazine has been prepared to remind you of the fundamentals of the insurance program: the relationship between claims reported by lawyers and the money we need to raise to pay those claims, what the claims trends are, and what you can do to help keep claims numbers and costs down as much as possible.

There is no silver bullet here. As you will learn from this publication, the "wobble room" that a buoyant economy provided both LAWPRO (in the form of healthy investment returns) and lawyers (in that clients were less likely to allege malpractice in a rising economy) is no more. Good risk management is more important than ever. And good risk management is largely a matter of hammering away at the fundamentals, such as good communication with clients, good client intake/identification practices, and diligent time and practice management.

Remember this simple fact: Every additional \$1 million in expense to LAWPRO adds about another \$50 per year to the base premium for each lawyer. So, for example, it only takes a single \$1 million loss or two \$500,000 losses for you to notice the impact. In a world where we see 2000 plus claims per year and the number of large losses is increasing, it doesn't take long to figure out the potential impact on the base premium.

Two mitigating factors have enabled LAWPRO to maintain stable premiums (ranging from a high of \$3,150 to a low of \$2,300 over the past nine years) despite a worsening claims picture:

- our ability to tap into a Premium Stabilization Fund (PSF) which, as its name suggests, we were able to access for a number of years to help stabilize premiums, thus effectively offsetting significant claims cost increases; and
- healthy investment returns over the last five years and especially in 2007. The exceptional returns of 2007 made it possible to reduce premiums to their lowest levels ever (at least, for LAWPRO premiums) in 2008, and to increase the base premium a modest \$150 in 2009. The LAWPRO Board and Executive team felt it only right that lawyers should realize the benefit of this investment income through a reduced base premium.

All good things, it is said, must come to an end. In 2008 and 2009 we see a convergence of several adverse trends that have a major effect on the insurance program and our ability to provide premium stability going forward on the same basis as in recent years.

First – and as is more fully explained on the following pages – the balance in the Premium Stabilization Fund stood at about \$16 million at the end of 2008. One of its functions is to cover shortfalls in transaction levy premiums needed to finance the insurance program; the continuing decline in premium revenues from transaction levies (a trend exacerbated by the economic slowdown in real estate in late 2008 and 2009) means we have had to draw on the PSF more than originally anticipated for 2009 – leaving even less in the fund that we can access in future years to mitigate continued increases in claims costs.

Second, investment income for LAWPRO fell sharply in late 2008 and in the first months of 2009, as it has for everyone with equity investments. The \$26 million in investment income in 2007 played a major factor in helping us keep our bottom line in the black. We do not expect to see this kind of return again for some time. In general, interest rates are at an all-time low, and as our existing bonds mature, the new ones available for purchase often have lower interest rates.

Third – and as mentioned by Board Chair Ian Croft in the 2008 LAWPRO Annual Report – we are also coming to grips with the Ontario government's announcement of a harmonized sales tax (HST) regime. The legal costs we pay to lawyers to defend insureds with claims will attract HST (being a financial institution, LAWPRO neither charges GST/HST on our premiums nor are we allowed to deduct GST/HST paid). This will result in an immediate eight per cent increase to our annual legal bill as well as to other operating expenses.

The good news on this front is that, to date, the claims portfolio continues to be fully backed by our asset-liability matched portfolio of fixed income securities. So it is not that we see any existing shortfall in the money needed to pay claims right now, but we are analyzing the impact of HST on the future resolution of existing claims and on the reserves that we have assigned to these reported but still unresolved claims files.

Where does this leave us all? We at LAWPRO are studying the situation and the options available to us extremely carefully as we prepare our Report to Convocation for the 2010 program. We also encourage you to take some time to inform yourself about the issues as described on the following pages, and to work with us in helping keep increases in claims numbers and costs in check.



Kathleen Waters
President and CEO

Transaction levy revenues, Premium Stabilization Fund contribute to premium stability

Premium revenues to meet LAWPRO's fiscal requirements each year come from three principal sources: E&O base premiums, levy surcharges and the Premium Stabilization Fund.

The base premium: The E&O base premium is the company's principal source of revenue. The process of assessing what the premium likely should be starts about six months before the premium is to come into effect. It is based on several factors including: best estimates of revenues from transaction levies, the number of lawyers in practice in the year in which the premium is to be in effect, an actuarial projection of claims costs for the coming year and estimates of the company's operating costs. Although most lawyers pay the base amount of premium, many pay less, depending on the coverages and options selected. For example, a lawyer qualifying for part-time practice or the Restricted Area of Practice Option would be eligible for a discount of 40 per cent off the base premium.

Transaction levies/Claim history levy surcharges: Lawyers practising real estate or civil litigation in 2009 pay a transaction levy surcharge of \$50 per real estate or civil litigation transaction, reflecting the added exposure that these areas of practice represent to the program (see also graph 8). Lawyers with claims on which damages have been paid pay a claims history levy surcharge ranging from \$2,500 to \$35,000 and more, depending on the number of claims reported that attract this surcharge.

Premium Stabilization Fund (PSF): Created in 1999, this fund helps guard against any future shortfall in levy receipts in a given year (forecasting transaction levy revenues in a changing legal and economic landscape is difficult). It has also acted as a buffer against the need for sudden increases in base premiums.

Monies in this fund come from two sources: 1) revenues from transaction levies and claims history surcharges that are in

excess of what LAWPRO had forecasted during the planning process; and 2) a “refund of premium” provision that sees any surplus in funds resulting from claims costs from prior fund years being **lower** than budgeted transferred to the fund for future insurance purposes.

Similarly, if levy revenues fall below projections and/or claims costs are higher than budgeted, monies are drawn from the PSF to offset the shortfall.

Premiums, premium revenues stable over nine years (graphs 1 & 2)

The insurance premium paid by lawyers over the past 10 years has trended downwards – despite an upward trend in E&O claims numbers, costs and frequency as graphs 3 to 7 on the following pages illustrate.

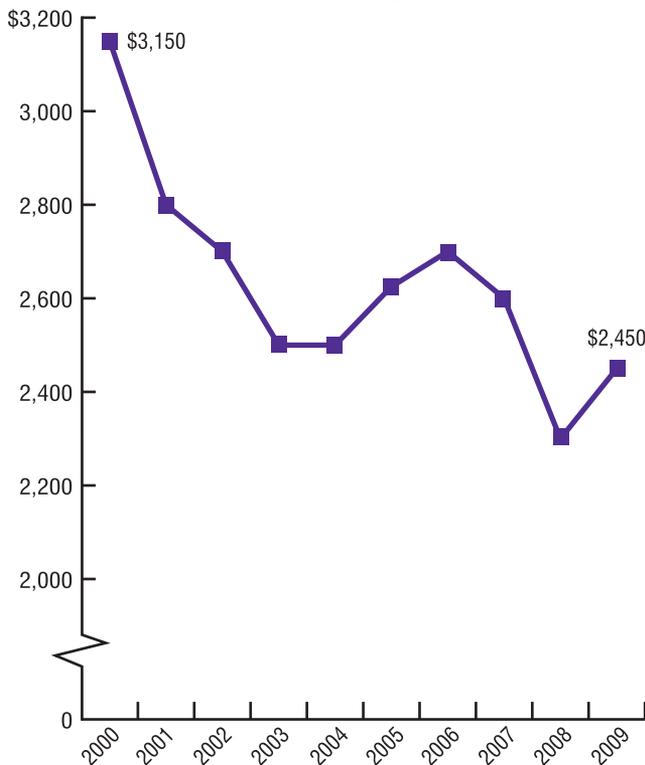
Revenues from base premiums have generally tracked variations in the per lawyer base premium – that is, years in which the per lawyer base premium fell also saw a decline in total revenues from

base premiums. Transaction levies also have trended downwards, largely the result of widespread use of title insurance in real estate transactions (title-insured transactions usually do not attract the \$50 real estate levy surcharge when acting for the purchaser and lender), and more recently of declined economic activity.

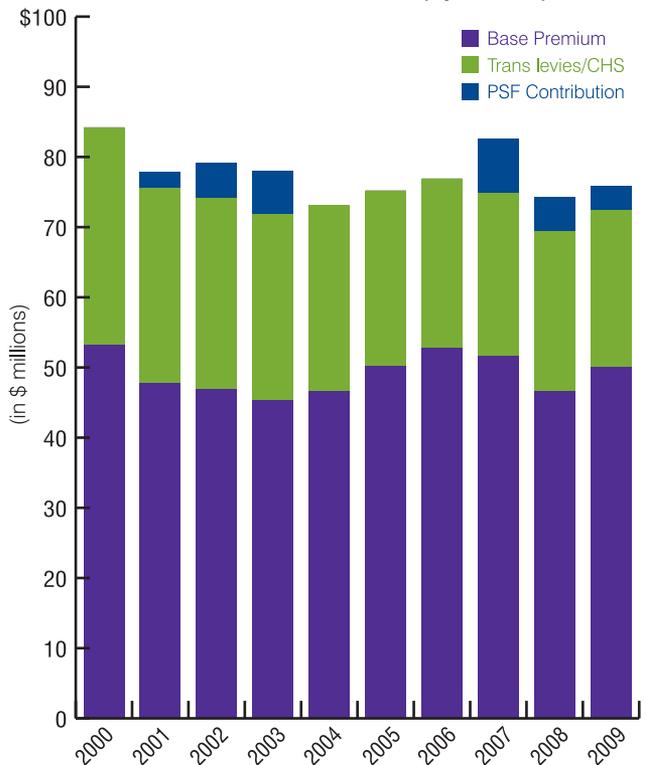
As graph 2 illustrates, years in which base premium and transaction levy revenues declined significantly while claims costs also increased (see graph 5) required LAWPRO to draw funds from the PSF.

Between 2000 and 2008, we drew close to \$30 million from the fund, leaving a balance in the fund as of December 31, 2008, of about \$16 million. For the first six months of 2009, revenues from transaction levies were about \$2 million less than projected – a trend that may require us to dip further into the PSF before the current year is out. We forecast that the PSF balance will be significantly lower at the end of this year than it was at the beginning – leaving us with even less in the fund that we can access in future years to mitigate continued increases in claims costs.

GRAPH 1
Base premium (per lawyer)



GRAPH 2
Premium revenues (by source)



Claims numbers, costs trend upward putting pressure on premiums

Claims-related costs account for more than 85 per cent of LAWPRO's annual budget. Costs to administer the LAWPRO program are minimal, accounting for about 15 per cent of our budgeted annual costs (compared to 25 to 30 per cent for most commercial insurers). In other words, no matter how much we reduce program administration costs (which already are at a minimal level), we cannot achieve the savings needed to cover consistent increases in claims numbers and costs. Claims costs – over which we have little if any control – simply account for too much of our budget.

This reality, coupled with the consistent decline in revenues from transaction levies and a declining balance in the Premium Stabilization Fund, mean base premium revenues figure more importantly than ever. Also important is the need to find new ways to contain claims costs, through more proactive risk management, to avoid having to consider restricting the scope of coverage provided under the insurance policy.

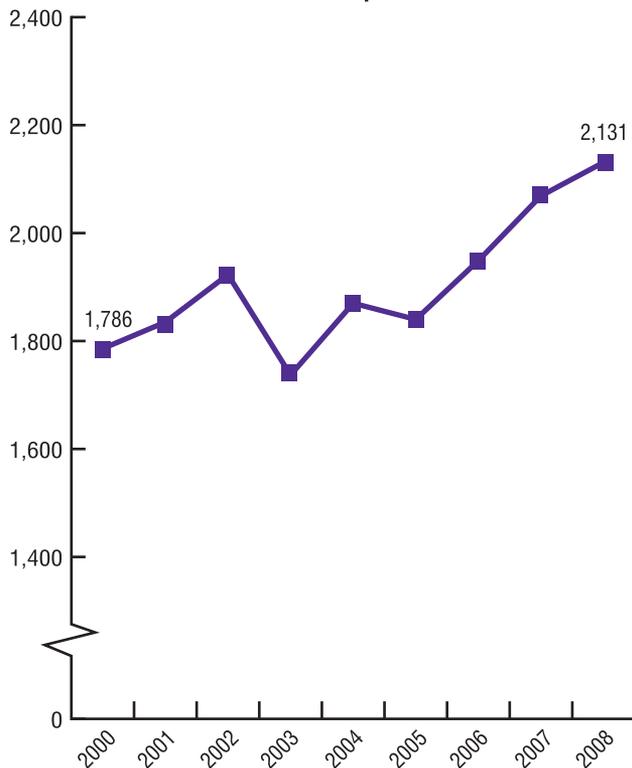
More lawyers are reporting claims (graphs 3 & 4)

The number of claims reported annually has been steadily increasing, topping the 2,000 mark for each of the last two years. Results to date for 2009 indicate the number of claims reported this year may be at the highest levels we have seen since 1995.

Moreover, the rate of increase in the number of claims being reported to LAWPRO has been exceeding the rate at which new lawyers are coming into practice each year. As a result, the claims frequency (the number of claims per 1,000 lawyers) has increased almost 10 per cent in the last four years, from a low of 90 in 2005 to 99 in 2008. In other words, for every 1,000 lawyers we insure, we are now seeing nine additional claims reported.

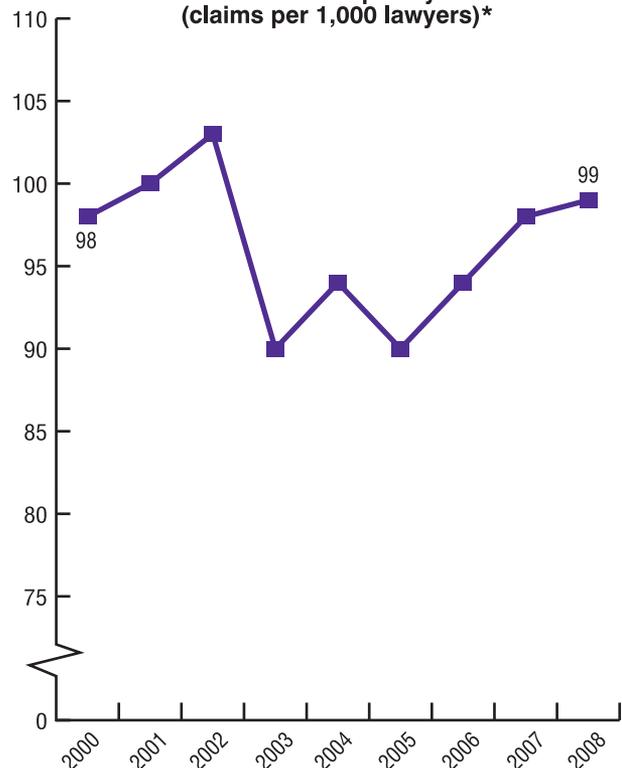
This increase in claims frequency is particularly pronounced in the 2004 to 2008 period – during which premiums generally trended downwards.

GRAPH 3
Claims reported*



* Based on claim reports as of June 30, 2009

GRAPH 4
Claims frequency
(claims per 1,000 lawyers)*



* Based on claim reports as of June 30, 2009

Claims costs rising sharply (graphs 5 to 7)

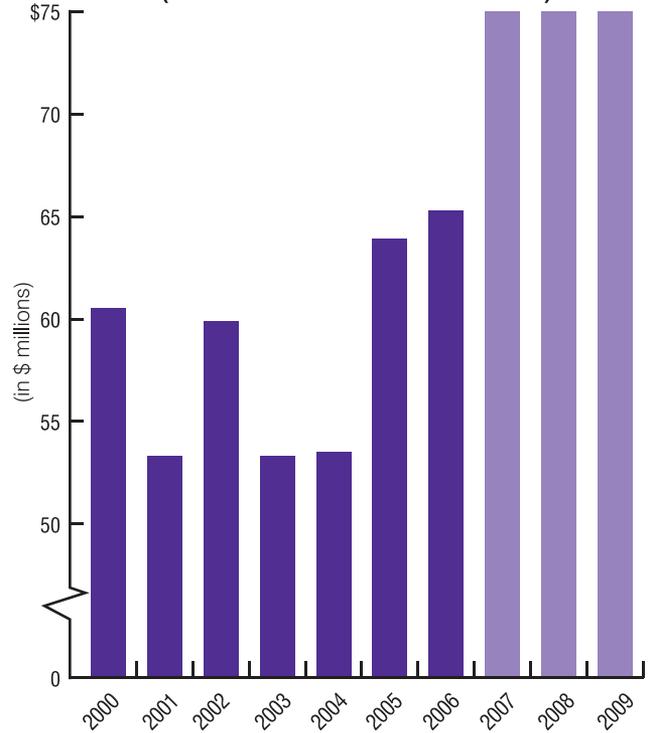
As graph 5 illustrates, claims costs also have been trending upwards, especially in the last three years. Between 2000 and 2004, the average cost of claims reported annually stood at about \$56 million per year; in the 2005 to 2006 period, that average climbed to almost \$65 million. Of real concern are the numbers that we are forecasting for the 2007 to 2009 fund years, as case incurred claims costs for each of those years is trending to be close to or even exceed \$75 million annually.

This same trend is evident when we look at claims severity (graph 6). To ensure we have an apples-to-apples comparison, we looked at claims at the same point in time – in this case, at 30 months after the start of the year in which the claim was reported. It takes on average 24 to 36 months to resolve or adequately assess and reserve a specific year's claims portfolio, so looking at each year's claims 30 months out provides some measure of certainty.

On a per claim basis, the cost per claim file rose from an average of about \$25,500 in the 2000 to 2004 period, to \$29,000 for 2005 and 2006, and to more than \$35,000 for 2007 to 2009. (Severity for these latter three years is a management projection based on current trends.) In other words, in the nine years between 2000 and 2009, the average cost per claim may end up rising close to 40 per cent.

Another measure of what is happening in our claims portfolio is the number of large claims that cost the program \$100,000 or more (graph 7). That number too has been steadily rising – from about 133 per year in the 1999-2001 period, to 146 per year in the 2002 to 2004 period, to 189 per year in the 2005 to 2007 period.

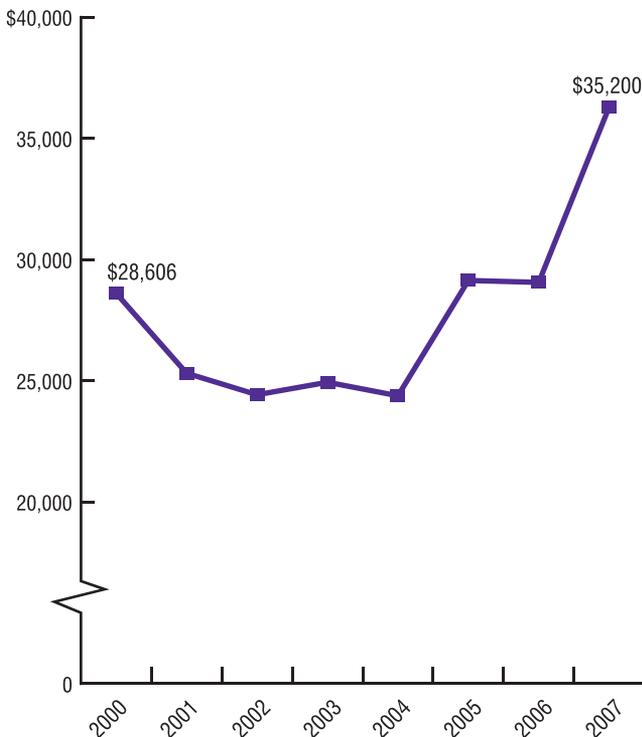
GRAPH 5
Claims cost
(case incurred actual & estimated)*



* For 2000 to 2006, costs above include claims paid plus reserves assigned to unresolved claims for that fund year, but exclude costs for general program administration.

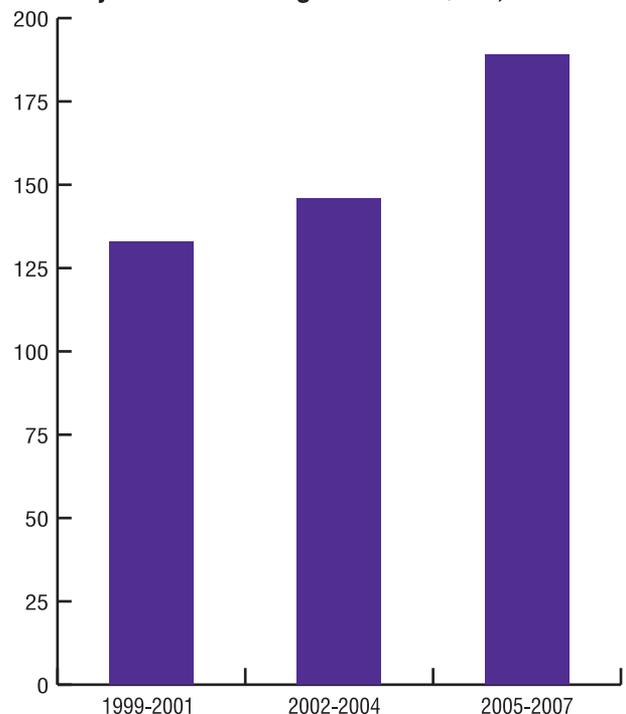
For 2007 to 2009, costs are management projections based on claim reports as of June 30, 2009. More than 25 per cent of claims reported in 2007 are still open, more than 40 per cent of claims reported in 2008 are still unresolved, and only six-month estimates are available for 2009.

GRAPH 6
Average cost per claim at 30 months after
start of year in which claim was reported*



* Based on claim reports as of June 30, 2009

GRAPH 7
Average number of claims reported each
year with a value greater than \$100,000*



* Based on claims reported as of June 30, 2009

Sharp increase in real estate costs (graph 8)

The LAWPRO claims portfolio contains a mix of claims from many areas of law. By numbers of claims, the mix of malpractice claims that LAWPRO sees is roughly in proportion to the amount of work done in all the areas of law in which Ontario lawyers practise.

Although the number of claims in any given area of law changes from year to year (as does the cost to resolve those claims), graph 8 demonstrates some overall cost trends. The majority of LAWPRO's claim costs arise from real estate, litigation and corporate work. Between 2000 and 2007, the costs for real estate, corporate, wills/estates, and family claims have all trended upwards. Over the same period of time, litigation claim costs have fluctuated between \$15 and \$20 million.

While we are seeing more claims involving intellectual property, employment/labour and criminal law, there are no clear trends in the costs of the claims in these areas of law.

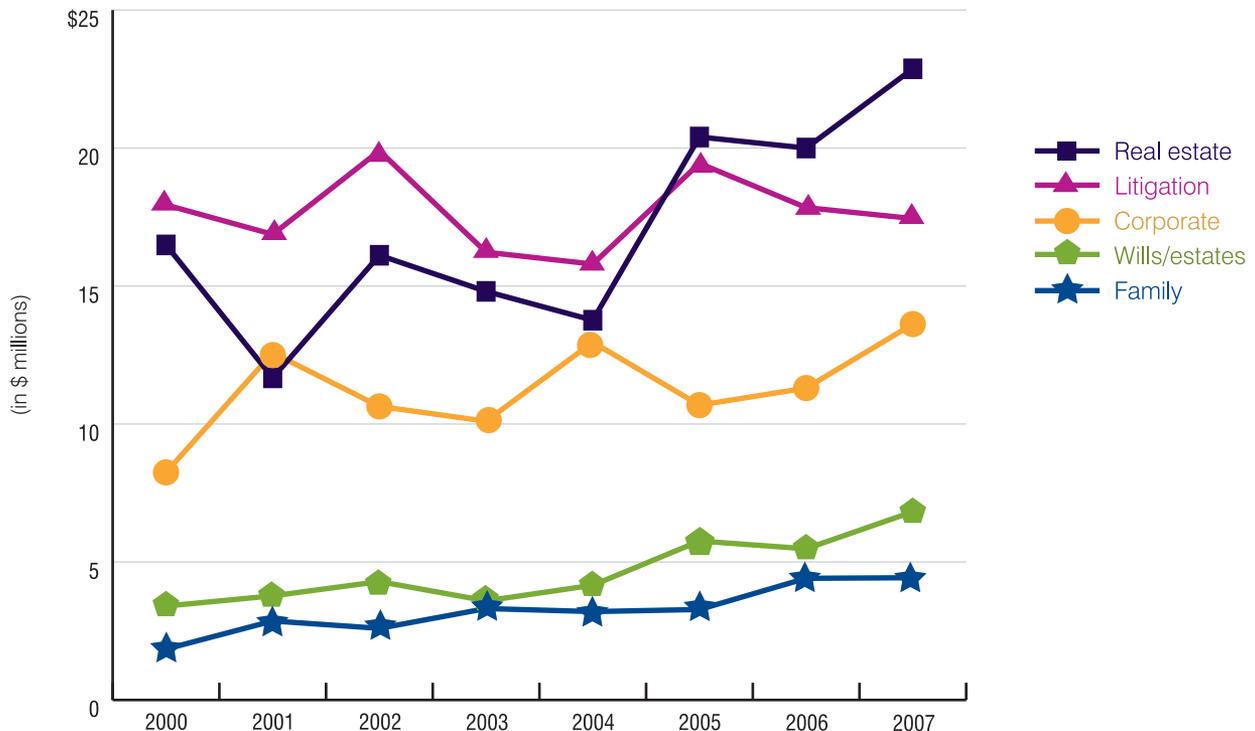
The state of the economy will change the relative amount and types of work that lawyers undertake, which will in turn change the mix of claims. In tough economic times there will be fewer

commercial and real estate deals, and potentially fewer claims arising from this type of work in coming years. However, in tough times there will be more work in the collections, bankruptcy, employment, power of sale and foreclosure areas. Given the current state of the economy, LAWPRO expects to see more claims in these areas in future years.

Rising costs in step with a booming economy

The trends we are seeing in our claims portfolio are not totally unexpected. Over the same 2000 to 2009 period, inflation stood at about 20 per cent. Canada's Gross Domestic Product grew about 26 per cent. Average house prices in Ontario rose 20 per cent between 2005 and 2009 – a factor that no doubt contributed to the fact that real estate consistently accounts for one-third or more of all claims costs incurred. In a robust economy, such as we have seen for much of the past decade, it is not surprising that damages for claims would be rising. Add to that the increased complexity of law practice which results in more complex claims files in our portfolio and you have a claims portfolio that includes more claims that cost more to resolve.

GRAPH 8
Claims costs (case incurred) by area of law*



* Based on claim reports as of June 30, 2009

TitlePLUS policy numbers, claims costs grow

The widespread use of title insurance in real estate transactions not only means that more consumers benefit from the protection that title insurance provides, but also that title insurers are receiving – and paying out – more claims. The TitlePLUS program is no exception.

As the number of TitlePLUS policyholders grows by the thousands year over year, more claims are being reported, and the TitlePLUS program is consistently paying more claims and allocating funds to pay future claims.

For example, in 1999 – only two years after the TitlePLUS launch and with only 13,000 policies in force – fewer than 35 claims were reported, costing the program under \$30,000. By 2007, when hundreds of thousands more Canadians had protected their real estate transactions with TitlePLUS policies, claims paid in 2007 were in excess of \$2 million.

From a consumer (or other policyholder) perspective, that's very good news. It means that the TitlePLUS policy is doing exactly what it is intended to do: It's delivering on the protection that our insurance policy provides by compensating TitlePLUS policyholders for damages and losses they have suffered. According to survey results, it's also delivering the service policyholders expect: On average 85 per cent of respondents give us top marks for handling claims promptly, courteously and professionally, and keeping the claimants well informed.

That's not to say that we are not carefully watching the number of claims reported and their costs – trends that put pressure on TitlePLUS premium amounts.

Of particular concern is the cost of fraud to the TitlePLUS program. To date we have paid out more than \$6 million on TitlePLUS fraud claims – good news for policyholders who were quickly compensated for losses, but of concern for TitlePLUS administration. The TitlePLUS program already has the most stringent underwriting requirements of any title insurer in the Canadian marketplace. To the extent possible, TitlePLUS underwriters are trying to learn more about how these frauds were perpetrated and what can be done at the underwriting end to minimize exposure to frauds in the future.

Despite these concerns, TitlePLUS results are consistent with expectations for the program:

THE MAJORITY OF CLAIMS ARE FOR RELATIVELY MINOR MATTERS

More than 95 per cent of claims reported are minor with payments of less than \$10,000. Tax arrears, adjustment errors, and utility arrears are typical.

OUR CLAIMS RATIO REFLECTS THE ADDITIONAL COVERAGE IN A TITLEPLUS POLICY

An important measure of an insurer's performance is the claims ratio – that is how much of every dollar of premium revenue it has paid out or expects to pay out on claims.

On average, over the history of the TitlePLUS program, its claims ratio for paid claims stands at about 33 per cent. This means for every dollar of premium revenue it has received, it has paid out about 33 cents to policyholders who had claims that were covered under their TitlePLUS policies. TitlePLUS actuaries predict that its average ultimate claims ratio will be in the 55 per cent range when one factors in costs of claims that may yet be received in the future on account of policies already sold.

So, it can take many years to say definitively how a given year of policy sales worked out. Our conservative, prudent approach to reserving ensures the program can absorb anticipated increases in claims costs

The TitlePLUS projected ultimate claims ratio of about 55 per cent is, we believe, consistent with that of its competitors, when you remember that the TitlePLUS policy also includes legal service coverage. Other insurers selling more traditional title insurance often report ratios to the regulator ranging between 20 and 40 per cent (or more in isolated cases), depending on the year and the title insurer. But 12 per cent of the claims in the TitlePLUS program fall into the legal service coverage, thus driving its claims ratio higher than that of a typical title insurance program.

TITLEPLUS RESERVES ENABLE US TO WEATHER INCREASING CLAIMS PAYMENTS

In 2008, the amounts set aside to resolve TitlePLUS claims exceeded 2008 premium revenues. Results such as this are not unexpected in the business world and do not affect the long-term viability of the program.

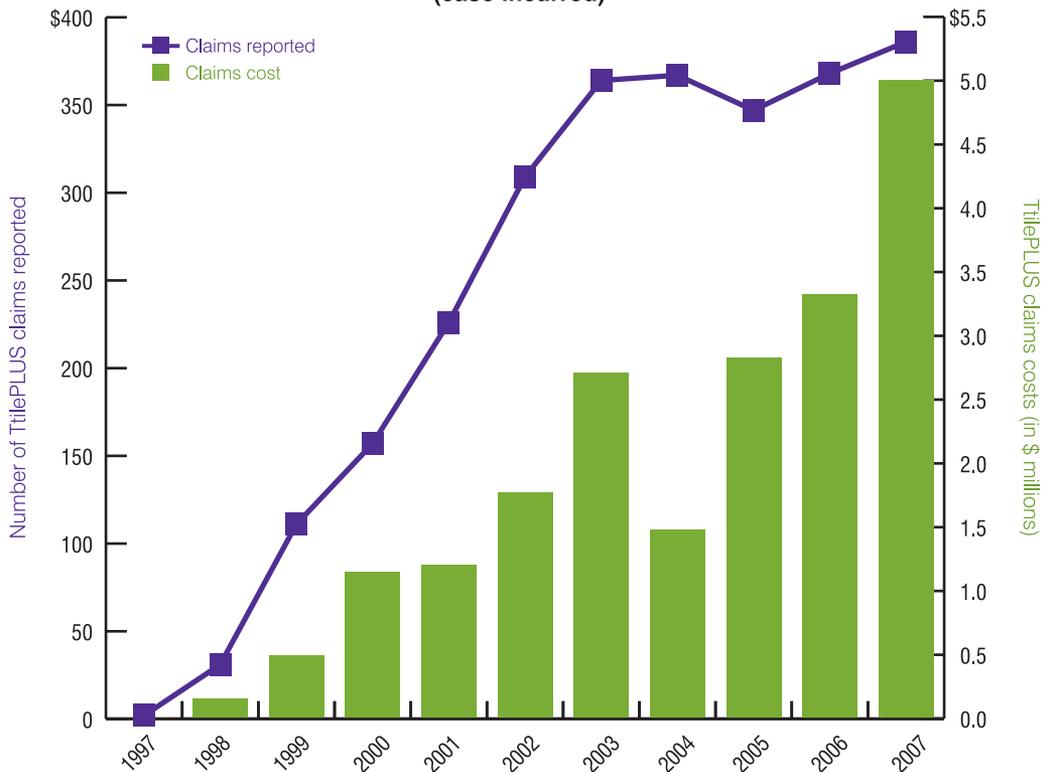
There is an element of volatility and unpredictability to any business – including title insurance. That is why it is important to look at any business results over time, rather than look at a single year in isolation.

Each year actuaries look at both the anticipated claims costs for the policies sold in the current year, and back to earlier years and then decide whether more money should be set aside for claims which may arise from those earlier years. That is what happened in 2008. But comparing money set aside for claims on policies sold over a number of years to only the premium collected

in one year tells us little: Because actuarial adjustments are being made after the fact covering many prior years on the claims side of the equation, it's important to also factor in the premium collected in those earlier years. When we include the seemingly high actuarial adjustments made in 2008, the projected ultimate claims cost is still only about 55 per cent of all TitlePLUS premiums collected over the years.

In other words, prudent and conservative reserving by our financial team ensures that the TitlePLUS program can absorb this additional allocation to TitlePLUS projected costs.

GRAPH 9
TitlePLUS claims reported & costs
(case incurred)*



* Includes claims paid plus reserves for claims reported but not resolved, based on claim reports as of June 30, 2009.

Lawyers as targets of fraud: the common misconceptions

Almost every day LAWPRO receives calls and emails from lawyers who are acting on files that are possible or obvious frauds. The types of sham matters targeting lawyers range from collections and commercial loans to real estate and mortgage transactions.

Based on feedback, we believe that lawyers and law office staff are generally more aware of the red flags that warn of potential fraud. Lawyers are more often identifying and stopping frauds targeting them.

However, these calls also tell us that several recurring misconceptions are preventing some lawyers from recognizing potential frauds. To help you spot matters that may involve a fraud, keep these common misconceptions in mind:

Fraudsters are always “new” clients: Generally this is true, but there are degrees of “newness.” We have seen frauds in which a new client will retain (and pay) a lawyer to do work on a smaller matter that otherwise appears legitimate (e.g., an incorporation), and then come back months later to engage the lawyer to work on the fraudulent matter.

Emails from fraudsters will be very obvious: Probably every lawyer in Ontario has received an email that is clearly an attempt at fraud. The clues can include one or more of the following: promises of large sums of money, a scenario that doesn't add up, bad grammar and loads of spelling mistakes. While the really bad emails are easy to spot, the really good ones are not. We have seen attempted and successful frauds initiated by emails that had little or nothing in them that would raise suspicions. In some frauds, we have seen emails that appear to come from another lawyer (or the staff person of a lawyer who has conveniently gone on vacation). The email will include links to a real law firm's website, where there will be information on the lawyer who allegedly sent the email. However, a careful inspection will show that the email address and phone number for the supposed sender will not be legitimate (i.e., consistent with the information on the website). They will put you in touch with the fraudster instead.

Fraudsters will only contact you by email or telephone: While the initial contact might be an email message or phone call, we have seen frauds in which the perpetrators visit a lawyer's office multiple times over weeks or even months. Fraudsters will provide valid-looking identification, including an Ontario driver's licence. Note: The driver's licence provided by fraudster clients is almost always fake. To confirm that a driver's licence is valid, use the Ministry of Transportation's online Driver Licence Check at www.dlcheck.rus.mto.gov.on.ca/Scripts/OrderForm.asp.

The fraudsters won't go as far as faking contact info on documents or a cheque: We have had a few calls from lawyers who didn't think that the fraudsters would go as far as faking contact information on a forged bank draft. Don't be fooled. This is a critical part of the ruse. See the next point.

The client, lender, seller and buyer can't really all be in cahoots – can they? Yes they can! Don't be fooled. Frauds are getting much more sophisticated, and there are usually multiple accomplices involved. All of the documents will look real and be drafted to make the transaction look legitimate. They will put you in touch with the co-conspirators. In one commercial loan fraud, the target lawyer spent many hours over several days going back and forth with a representative of the supposed lender negotiating terms of the loan and security documentation. On another fraudulent matter, loan instructions came from someone pretending to be a major bank employee.

The fraudsters were so smooth, I never suspected a thing: Several of the lawyers who called us said that in hindsight they were surprised at how friendly and talkative the fraudsters were. The fraudsters seemed to have all the right answers to any questions they were asked. The fraudsters even played on cultural connections where they existed.

Carefully review the above misconceptions so that you don't become a victim of fraud. Remain on high alert and don't let your guard down. Frauds are becoming ever more sophisticated, and the fraudsters appear to be going to ever greater lengths to try to trick lawyers into accepting bogus cheques or bank drafts and disbursing good funds from their trust accounts.

Thankfully, we have not seen another organized fraud similar to the one that occurred just prior to the Victoria Day weekend (but expect we will at some point). Use the fraud prevention resources mentioned in the sidebar below, and call us if you are acting on a matter that is a possible or obvious fraud. We want to help all Ontario lawyers avoid being the victims of fraud and prevent expensive fraud-related claims.

LAWPRO fraud prevention resources

These resources will help you avoid being duped. They are all available at www.practicepro.ca/fraud.

- **The LAWPRO fraud page:** Extensive information on fraud and fraud prevention;
- **Fraud And How You Can Avoid Being Its Next Victim webinar:** Listen to the MP3 (audio file) and follow along with the materials from this online presentation;
- **The LAWPRO Fraud Fact Sheet:** Download this handy checklist and keep it in your desk. It will help lawyers and law firm staff spot the red flags to look out for on a fraudulent matter.

Legal malpractice risks change in tough times

(But the best risk management strategies don't)

When times are good, bumps in the road won't always cause problems. Clients are upbeat and they want the deal to close, their problem resolved or the litigation matter to proceed. Happy clients are far less likely to sue their lawyers for malpractice.

However, in tough times, clients squeezed by money problems can become unhappy and they will be more likely to look for ways to allege that their lawyers made a mistake. In a similar fashion, lawyers squeezed by financial problems can also find themselves more likely to engage in risky behaviour. Unhappy clients and risky lawyer behaviour translate into more LAWPRO claims.

In good times and bad, avoiding a legal malpractice claim requires that you understand where the risks are so that you can respond to them by proactively taking steps to reduce your exposure to a claim. As you will see, the risk management strategies you should employ in good times and bad are essentially the same. And, as clients are likely to hold you to a higher standard when money is tight, being proactive with risk management becomes even more important in tough times.

The most common malpractice claims

As has been highlighted in more detail in past issues of LAWPRO Magazine,¹ in good times and bad, in most areas of the law, lawyer/client communication problems are the number one cause of claims. Deadline and time management issues are the second most common type of error, followed by claims that arise because the lawyer didn't dig deep enough into what the client wanted or needed, substantive law errors, conflicts of interest and then clerical/supervision errors.

Malpractice errors made at solo, small, medium and large firms are virtually identical in proportion and type². People make mistakes and systems don't work properly in similar ways, regardless of firm size.

Tough times make clients more demanding

A client squeezed by financial problems may behave in a less reasonable or rational way. A financially desperate client may act in a totally irrational way. A client's financial health can take a turn for the worse very quickly and unexpectedly. Don't underestimate the impact that financial pressures or changed circumstances can have on an individual, or on the relationships

between family members or business partners. People who were all previously marching in the same direction can all of a sudden want very different things (e.g., a sale of business or a buy-out of an individual interest). If the matter or amount of money at issue is significant, even long-standing and loyal clients can turn on you. They can see a malpractice claim as a potential solution to their financial difficulties.

In response to financial pressures or changed circumstances, clients may want to back out of business deals or delay litigation matters that would have otherwise proceeded in a good economy. To this end, they will look for ways to allege that their lawyers made a mistake. You will be held to a higher standard. Minor questions or issues that would have warranted little or no attention in good times can become deal breakers in bad times. When making an allegation of malpractice, unhappy clients will look to exploit (with or without merit) one or more of the following: retainers with a vague scope; poor lawyer/client communication; missed deadlines or delay; ambiguous language in documents; unanticipated scenarios or circumstances; unexpected results or outcomes; and immaterial conflicts of interest.

Five key risk management strategies

These five risk management strategies will help you reduce the risk of a claim when you are dealing with demanding clients:

1. **Start out on the right foot with a written retainer:** The retainer letter or agreement is your terms of engagement. It should clearly identify who the client is and what you are retained to do. A written retainer can protect you if there are unexpected changes in the scope of the engagement as the matter progresses.
2. **Control client expectations at all times:** Clearly and accurately communicate to your clients the available courses of action and possible outcomes; all the implications of any decisions; how long things will take; and the expected fees and disbursements. This strategy, coupled with the next one, is your best protection from a malpractice claim in good times and bad.
3. **Document everything (almost):** It is just not practical to document everything on every matter, but you should document as much as you can in some contemporaneous manner. Letters are fine, but emails, detailed time entries and marginal notes on documents can be equally effective. In particular, you want

¹ *The Biggest Malpractice Risks* by Dan Pinnington at page 17 of LAWPRO Magazine: **practicePRO: Helping Lawyers for 10 Years** (Volume 7, Issue 2, Summer 2008).

² See *Solo, Small And Big Firms Make Same Errors* at page 25 of LAWPRO Magazine: **Work and Wellness** (Volume 5, Issue 4, Summer 2006).

to record advice or instructions that involve significant issues or outcomes, and major client instructions or decisions. Documenting things is especially important when you are dealing with clients who are difficult or emotional due to financial stresses. Documented communications help confirm what was said or done for the client in the event you ever need or want to look back to explain why or what work was done, to justify an account, or to defend yourself on a malpractice claim.

- 4. Meet or beat deadlines:** Set realistic deadlines when it comes to completing tasks and/or delivering things to clients. Under-promising and over-delivering (i.e., earlier than promised) on work for clients will make them very happy. Don't leave things to the very last minute, as unexpected events beyond your control (blackouts, snow storms, taxi got lost on way to file documents) may prevent things from happening as required. Giving yourself an extra day or two by setting your deadline before the real deadline can be a lifesaver.
- 5. Send interim and final reporting letters:** They should confirm what work was done and the successes obtained for the client, outline future steps, and confirm that the retainer is terminated. This helps keep the client fully informed, and can be critical when it comes to defending a malpractice claim if circumstances unexpectedly change as you work on a matter for a client or after your retainer is terminated.

Risky lawyer behaviour to avoid

Lawyers under economic and financial pressures can also find themselves more likely to engage in a variety of risky behaviours. These are discussed in more detail in the following paragraphs.

Don't dabble in areas of law outside your expertise: When you are not busy and have extra capacity to do work, it is just so tempting to take any client who walks through the door, even if you have limited expertise in the area of law in which they require help. The pressure to do work outside your usual practice area

for an existing client, family or friends can be even greater. Lawyers who hoard work because they are under pressure to increase their billable hours or billings also have a tendency to dabble. Don't do it! Resist the temptation and pressure. As a "dabbler" you will be less efficient and effective – and far more prone to a malpractice claim. LawPRO's claims tell us that dabblers make more than their fair share of mistakes when it comes to knowing and applying substantive law.

That is not to say you should never consider doing more work in or switching to a "growth" area of law. But, if you do so, take steps to become competent by attending CLE programs, working with other lawyers who already know the area or seeking help from a mentor.

Poor client selection: Shortages of work or money pressures can also cause lawyers to engage in another type of risky behaviour: poor client selection. Poor client selection manifests itself in a variety of ways. It can be working for a client that is unwilling or unable to pay an initial retainer or ongoing fees. It could also be acting for a very difficult client or one who has unrealistic expectations about the strength of his case, the cost of proceeding with it, and/or the likelihood of success. With these types of clients, collecting and replenishing retainers is critical to avoid fee disputes. And carefully setting and controlling their expectations by documenting communications is key to avoiding disputes.

Taking shortcuts: Clients under financial stress are going to want lower legal fees. To please a client with a faster turnaround time and/or lower fees, lawyers may find themselves tempted to take shortcuts. Taking shortcuts means a lawyer will do less work than she might otherwise have done on a matter. This could be skipping searches on a real estate deal, taking less care in reviewing or drafting a document, skipping discoveries or not ordering transcripts, not completing enough due diligence or not updating research.

In some cases taking shortcuts will be fine, provided the client fully understands and accepts the risk. But never let the client's

practicePRO claims prevention tools and resources

Numerous tools and resources that can help you reduce the risk of a malpractice claim are available at www.practicepro.ca. These include:

- **LawPRO Magazine Archive:** Articles from all past issues of the magazine (www.practicepro.ca/LawproMag/LawproMagArchive.asp)
- **LawPRO Resources Topical List page:** Articles and resources sorted by topic (www.practicepro.ca/information/default.asp)
- **Retainer precedents** for several of areas of law and matter types (www.practicepro.ca/practice/financesbookletprecedents.asp)
- **Dealing with difficult clients** paper and client file opening information memo precedent (www.practicepro.ca/practice/DifficultClients.asp)
- **Limitation periods charts** (www.practicepro.ca/practice/limitation.asp)
- **ILA checklist** (www.practicepro.ca/practice/checklist.asp)
- **Sample law firm business plan and budget** (www.practicepro.ca/practice/financesbookletprecedents.asp)
- **practicePRO Lending Library:** Books on law practice management issues that Ontario lawyers can borrow for free (www.practicepro.ca/practice/library.asp)
- **practicePRO Wellness and Balance Page:** Tools and resources to help you manage stress (www.practicepro.ca/wellness/default.asp)

financial distress expose you to a malpractice claim because you didn't take all of the necessary and appropriate steps to handle the matter in a competent way. If your client instructs you to take shortcuts, carefully document your advice to her on the risks of doing so.

Don't sue for fees: Tough times mean there will be more clients who are unwilling or unable to pay their legal fees. This will lead to more lawyer/client fee disputes, and in turn, more lawyers suing their clients for fees. Think twice before you sue for fees. A suit for fees almost guarantees a counter-claim alleging negligence.

The better solution: get the money up front so you avoid fee disputes altogether. At the time you are retained, get a retainer that is sufficient to cover all initial work that needs to be done on the matter. Replenish retainer funds *before* they are exhausted (set up your accounting system to monitor and remind you when the amount in trust is getting low). Stop working on the file if the retainer is not replenished – working on credit greatly increases the likelihood you will not get paid for your work, especially in tough times.

Lawyers or staff dipping into trust funds: Financial problems caused by tough times or personal difficulties can be the motive for even the most long-serving and trusted staff or lawyers to commit fraud. Weak internal controls coupled with the knowledge of firm systems and how to get around them create the opportunity for them to get away with it. Internal law firm fraud has been very

costly for the insurance program. See *When The Unthinkable Happens: What To Do When Partners, Associates Or Staff Commit Fraud*³ for information on recognizing when internal fraud may have occurred, and how you should respond.

Watch for conflicts of interest on lateral hires: Lateral hires of partners or associates frequently occur in bad times. A strong desire to hire a transferring lawyer should not lessen the need to identify and honestly assess potential conflicts, and to take appropriate steps to deal with them if necessary (e.g., confidentiality screens or client waivers). A failure to deal appropriately with these conflicts only delays the inevitable: in all likelihood the firm will have to refer any clients with a conflict to another firm.

Conclusion

When times are tough, clients in financial distress are far more likely to sue their lawyers for legal malpractice, and financially-pressed lawyers may be tempted to engage in risky behaviour. In these circumstances, risk management is more important than ever. Use the knowledge you have gained from this article and the tools and resources mentioned in the sidebar on the previous page to reduce your exposure to a malpractice claim.

Dan Pinnington is director of practicePRO, LAWPRO's risk and practice management program. He can be reached at dan.pinnington@lawpro.ca.

3 LAWPRO Magazine **Surviving The Slide: Dealing With The Tough Economy** (Volume 7, Issue 4, Winter 2008-2009) at page 16.



LAWYERS' PROFESSIONAL INDEMNITY COMPANY (LAWPRO®)

President & CEO: Kathleen A. Waters

LAWPRO Magazine is published by Lawyers' Professional Indemnity Company (LAWPRO) to update practitioners about LAWPRO's activities and insurance programs, and to provide practical advice on ways lawyers can minimize their exposure to potential claims.

Editor: Dagmar Kanzler
dagmar.kanzler@lawpro.ca

Contributing editors:
Gary Edgar
gary.edgar@lawpro.ca

Dan Pinnington
dan.pinnington@lawpro.ca

Design & Production: Freeman Communications

Tel: (416) 598-5800 or 1-800-410-1013
Fax: (416) 599-8341 or 1-800-286-7639
www.lawpro.ca

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