

# E&O claims

## The trend is up



**The claims team:**

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(standing, left to right): Doug Scott, Jennifer Ip, Cynthia Martin, Mitch Goldberg, Ian Smyth, Yvonne Bernstein, Dale Herceg, Dalia Fudim, Jack Daiter, Lisa MacLean, Deborah Petch, Rosanne Manson, Tim Clarke, Anna Reggio.

Absent: Nadia Dalimonte, JJ Earle

*In fall 2009 LAWPRO prepared a mid-year status update on claims for lawyers. The reason? No matter how we sliced and diced the numbers, they were headed in the wrong direction – up. And we needed lawyers to be aware of this trend not only because it affects premiums but also because lawyers can help to bring claims numbers and costs down to more acceptable levels.*

### Are claims still going up?

Six months later, this mid-year “heads up” has proven to be well-founded. On virtually all measures, claims numbers and costs at the end of 2009 are at levels we have not seen in more than a decade.

#### 1. LAWYERS ARE REPORTING MORE CLAIMS (GRAPH 1 – PAGE 5)

In 2009, lawyers reported 2,272 claims – more than at any point since 1995, the year LAWPRO assumed management of the Law Society insurance program. For a fourth straight year, claims reported topped the 2,000 mark after hovering in the 1,800 and 1,900 range for the first part of this decade. As well, claims frequency – the number of claims reported per thousand lawyers – is up to 103.1 in 2009 from a low of 90 in 2005. In other words,

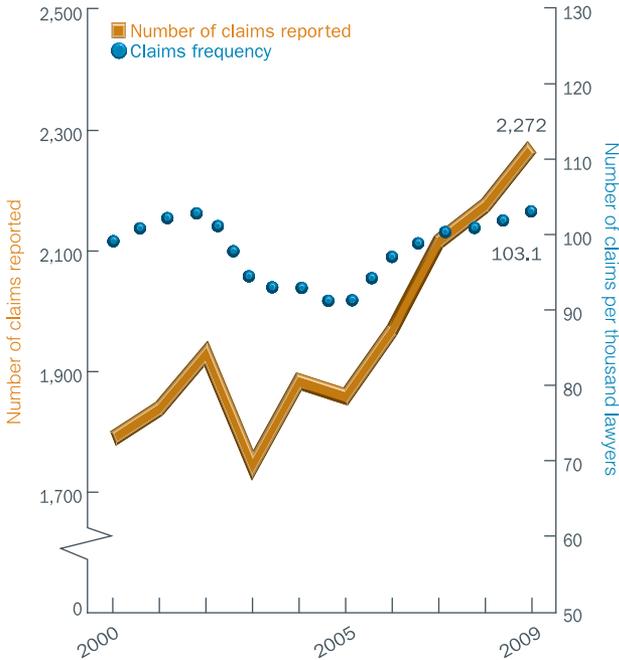
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LAWPRO today sees 13 more claims for every thousand lawyers in practice than we did five years ago.

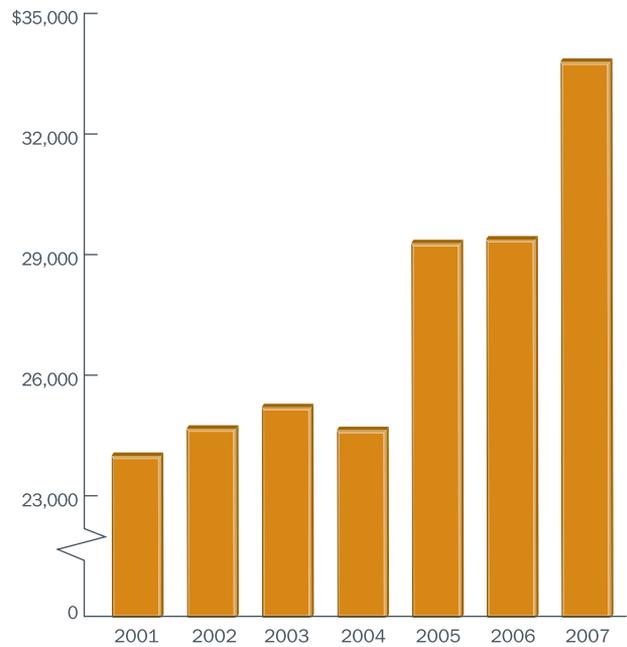
#### 2. CLAIMS ARE MORE EXPENSIVE (GRAPH 2 & 3 – PAGE 5)

As graph 2 shows, claims costs have entered a new era in which annual claims costs are projected to be in the \$85 million range. As recently as last summer, we were warning that claims costs could be in the \$75 million range for 2009. Claim reports made in the second half of the year, resolutions to some complex and costly files, and analysis of past years' trends contributed to a significant increase in 2007 costs and an upwards revision of projected claims costs for both 2008 and 2009.

**1. Number of claims reported & frequency**

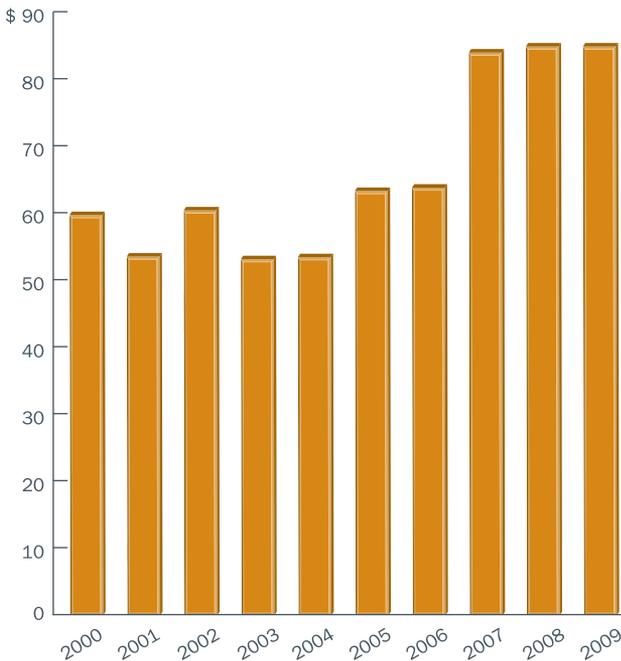


**3. Average cost per claim at 30 months after end of year in which claim was reported\***



\* 2007 numbers are as at February 28, 2010 – 26 months after the end of 2007.

**2. Case incurred claims costs\* (in \$millions)**



\* For 2000 to 2007, costs include claims paid plus reserves assigned to unresolved claims for each fund year, but exclude costs for general program administration and applicable taxes.

For 2008 and 2009, costs reflect management projections based on claim reports as of February 2010. More than 30 per cent of claims reported in 2008 and 50 per cent of claims reported in 2009 are still unresolved.

What this means is that claims costs, on average, are up more than 30 per cent for the last three years of this decade. Between 2000 and 2004, the average cost of claims reported annually stood at about \$56 million a year; that number jumped to \$65 million for

the 2005-2006 period, and now has jumped another \$20 million to about \$85 million annually for the 2007-2009 period.

Another way to look at claims costs is claims severity – or the cost per claim file. That number jumped from a low of \$24,000 in 2001 to close to \$34,000 in 2007 – a 41 per cent increase. Based on a projection of \$85 million in claims costs incurred and 2,272 claims reported, claims severity for 2009 (after the investigation is finished on those claims) is expected to be up another \$3,000, to about \$37,400 per claim.

**3. CLAIMS ARE MORE COMPLEX (GRAPH 4 – PAGE 6)**

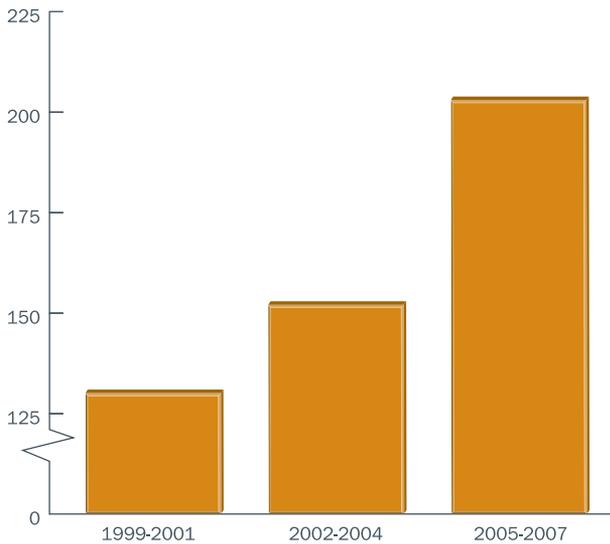
One indication of the increasing complexity of claims is the number of large claims that cost the program \$100,000 or more to resolve. That number too has been steadily increasing: At the beginning of this decade, we saw on average 130 claims per year that cost us \$100,000 or more to resolve; in the 2005 to 2007 period, that number had jumped to more than 200 claims a year that top the \$100,000 mark.

**Why is this happening?**

A number of explanations for this significant increase in claims numbers and costs are possible:

- Many of the files lawyers handle are increasingly complex, a reflection of the more complex nature of business and law practice today.
- Expectations of lawyers' work is on the increase, the result of better-educated clients who have access to more information – perhaps thanks to the Internet.

**4. Number of claims reported each year with a value greater than \$100,000\***



\* As at February 28, 2010

- Clients have become more litigious, prompted perhaps by media and the example set by clients in the United States.

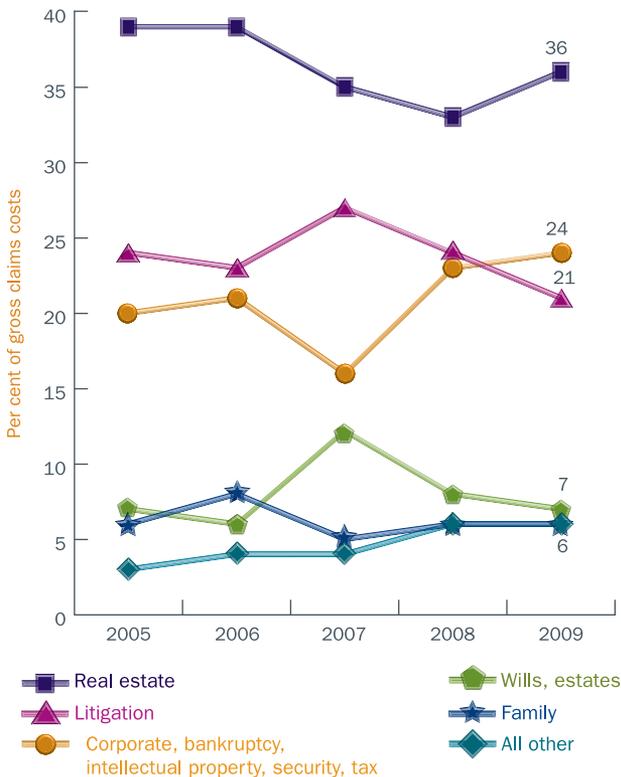
**Is one area of practice more prone to claims than others? (GRAPH 5)**

Generally, when we look at the number of claims reported, the mix of malpractice claims is roughly in proportion to the amount of work done in all areas of law in which lawyers practise.

On the cost side, the area of practice that consistently leads the pack in number of claims and accounts for one-third or more of claims costs is real estate practice. (This is excluding title-insured claims).

Over the last five years, real estate claims have accounted for, on average, 36 per cent of annual claims costs incurred. Litigation practice and corporate work (including security, tax and bankruptcy practice) rank second and third, with corporate work accounting for about 24 per cent of costs incurred, and litigation for about 21 per cent. As graph 5 shows, costs for real estate, corporate, and wills and estates claims have all generally trended upwards over the five-year period.

**5. Distribution of claims by area of practice**



**What does this mean for insurance premiums?**

In our special report on claims of September 2009, we pointed out that claims costs account for more than 85 per cent of LAWPRO’s annual budget. Rising claims costs therefore have a major and immediate effect on our bottom line.

As graph 2 makes clear, where once claims costs incurred for the year stood at about \$65 million, we now live in an era in which costs of \$85 million a year are possible. Each \$10 million increase in claims costs means we need to increase premiums by an additional \$500 – unless we have revenues from other sources to help offset this need to increase premiums.

In the past, we have benefited from both strong investment income and the ability to tap into a premium stabilization fund – a fund that enabled us to maintain relatively stable premiums for many years.

But investment returns have not fared as well in 2009 as in previous years, especially as fixed income securities are renewed at lower interest rates in today’s markets. Overall premium revenues have been largely flat or have even declined; for example, in 2009, transaction and claims history levy revenues fell to \$17.9 million from \$20.3 million a year earlier – the result largely of a sluggish real estate market and widespread use of title insurance in real estate transactions. And the funds available to help stabilize premiums are depleted.

This widening gap between costs and revenues prompted us to increase premiums by \$500 per lawyer for the 2010 primary insurance program. Current trends, which see claims costs continue to rise, will put further pressure on our ability to keep premiums at current levels.

# Principled claims management

Unlike many malpractice insurers who automatically defend and deny, we take a more objective view of things. If there is liability on the part of the lawyer, we will work to resolve that claim as expeditiously and cost-effectively as possible. Our goal is to minimize the emotional and monetary costs – to both you and the program.

If the matter has no merit we vigorously defend the insured, all the way to the Supreme Court where appropriate; we will also defend lawyers in the interests of the bar if a matter is likely to set a precedent. Finally, we will not make economic settlements in these situations.

The 2009 results speak for themselves. We were successful on seven of eight matters at trial, all 10 matters that went to appeal and 11 of 14 applications for summary judgement. As well, lawyers with claims tell us that our claims management services exceed their needs and expectations. In response to a survey, those with closed files responded as follows:

- 96 per cent said that they were satisfied with how LAWPRO handled the claim;
- 86 per cent said they would have the defence counsel firm represent them again; and
- 84 per cent said LAWPRO received good value for defence monies spent.

## What is LAWPRO doing about this?

There is only so much that LAWPRO, as your malpractice insurer, can do to address the issues of more claims and rising claims costs.

### CLAIMS MANAGEMENT

On the claims management side, we are working on several fronts to continue to resolve claims as cost-effectively as possible.

We continue to stick to our principled claims management philosophy – a strategy that continues to generate successes for lawyers, as is detailed in the accompanying article, “Principled claims management.”

If notified in time, we will also step in to help lawyers repair a situation – thus minimizing costs or helping prevent an escalation of events that could lead to a claim. Some examples are documented in the accompanying article “The Kenora gambit” on page 8.

As well, we have recently completed a reorganization of the claims team that will place costly, difficult claims that are in litigation in the hands of senior internal counsel whose time is dedicated to such files. Our two new litigation directors will work in a very focused fashion with outside counsel to resolve the growing portfolio of difficult litigation in the most cost-effective way possible.

### RISK MANAGEMENT

Based on our ongoing analysis of what is happening in the claims portfolio, we are also expanding our efforts to help lawyers avoid claims in the first place. For example, to complement the risk management focus of our *LAWPRO Magazine*, we have launched bimonthly electronic newsletters that get information on evolving risk issues, practice tips to avoid claims and insurance program-related information into lawyers' hands more quickly. We have also launched a practicePRO *Avoid A Claim* blog to provide lawyers with tips and insights into practice issues as they develop.

Last year we delivered more than 40 presentations on risk management-related topics to various law associations, law firms and CLE programs. We will be stepping up this program of presentations focused on claims prevention and will be producing a number of new resources that address the types of problems we are seeing based on our analysis of claims losses and trends.

But the lion's share of responsibility for bringing claims under control rests with the practising bar.

## What can an individual lawyer do about this?

Lawyers actually have more control over preventing malpractice claims than they may believe: That's because the single biggest underlying reason for claims is also among the easiest to prevent.

Across all practice areas and firm sizes, lawyer-client communication-related errors – at about 34 per cent of claims – are the biggest single cause of malpractice claims. In other words, of the projected \$85 million it could cost to resolve 2009 claims, almost \$29 million are the result of communication issues.

Included in this category are failing to follow a client's instructions, failing to obtain the client's consent or keep the client adequately informed, or simply put, poor communications (such as not explaining fees or disbursements or clarifying who is responsible for doing what during or after the matter).

Yet these errors are easy to prevent with some simple procedures. Control client expectations from the outset. Make a point of communicating with clients at all stages of the matter. Create a paper trail that documents instructions and advice and confirms what work was done each step of the way.

Time management issues, such as failing to know or ascertain a deadline (leading to limitations period claims) or poor calendaring account for less than 20 per cent of claims losses over the last decade. Only 14 per cent of claims are the result of a failure to know or apply the law.