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PROFESSIONAL LIABILITY INSURANCE COVERAGE ISSUES

By: Steven Verveniotis

WHAT IS COVERED UNDER TYPICAL LAWYERS PROFESSIONAL LIABILITY POLICY

A. Scope of Professional Services

As the examples set forth in detail in Exhibits 1 and 2 (attached) indicate, the policy language delineates the scope of professional services covered by a legal malpractice policy. Exhibit 2 is representative of the current expansive trend, covering as "professional legal services" activities performed for others as:

- a. a lawyer;
- b. a notary public;
- c. an arbitrator;
- d. a mediator;
- e. a title insurance agent;
- f. a designated issuing lawyer to a title insurance company;
- g. a court appointed fiduciary;
- h. a member of a bar association, ethics, peer review, formal accredited or licensing, or similar professional board or committee;
- i. an author, strictly in the publication or presentation of research papers or similar materials and only if the fees generated from such work are not greater than ten thousand dollars (\$10,000); and/or
- j. an administrator, conservator, receiver, executor, guardian, or any similar fiduciary capacity, or court-appointed trustee, however, no

PROFESSIONAL LIABILITY INSURANCE COVERAGE ISSUES

Page 2

coverage shall apply to any loss sustained by you as the beneficiary or distributee of any trust or estate.

B. Non-Covered Acts, Errors or Omissions

Claims made policies cover only claims first made and first reported during the policy period. Accordingly, claims made prior to the policy's inception date or reported to a prior insurer are not covered under the policy. See Rosenbaum v. Chicago Insurance Co., 306 A.D.2d 29, 761 N.Y.S.2d 637 (1st Dep't 2003).

Professional liability policies also may include a "Retroactive Date" which, depending on its wording may preclude coverage for claims arising from conduct prior to a specific date. See Coregis v. Blancato P.C., 75 F.Supp.2d 319 (S.D.N.Y. 1999).

In addition, not all claims against an attorney are covered under a professional liability policy. The key is whether the claim is for the "wrongful act" or "professional services" covered by the policy. Note the holding in Cohen v. Employers Reinsurance Corporation, 117 A.D.2d 435, 503 N.Y.S.2d 33 (1st Department 1986), which held that there was no insurance coverage under a legal malpractice policy for sanctions imposed on an attorney acting as a trustee of a trust created under a will, as follows:

The Surrogate's opinion in our case very clearly states that the surcharge against plaintiff was imposed solely as a consequence of plaintiff's actions as a co-trustee, to wit, improvidently investing in speculative REITS. Concededly, the circumstances had their origin in plaintiff's actions as a lawyer in drafting Newhoff's will. However, the claim by the beneficiaries in the accounting proceeding related to plaintiff's actions as a trustee only, and not as a lawyer. It is noted that the co-trustee, who is not a lawyer, was similarly surcharged. There is no requirement that a trustee be a lawyer. The policy issued by defendant was to defend and indemnify plaintiff for any liability incurred by him in his capacity as a lawyer. Defendant provided that protection by defending plaintiff in the legal malpractice action brought by the trustee beneficiaries.

It is noteworthy that the coverage agreement in Cohen read as follows:

COVERAGE A--INDIVIDUAL COVERAGE. The Corporation does hereby agree to insure and indemnify the Assured against loss in excess of the Assured's retention and within the limit herein expressed, on account of liability imposed upon the Assured by law for damages caused by any act or omission of the Assured, or of any person for whose acts the Assured is legally liable, and arising out of the performance of professional services for others in the Assured's capacity as a lawyer as respects claims arising out of such acts or omissions occurring during any indemnity period or as respects claims first made against the Assured during any indemnity period and arising out of such acts or omissions occurring prior to the effective date of this policy.

PROFESSIONAL LIABILITY INSURANCE COVERAGE ISSUES

Page 3

A similar result was reached in Rooney v Chicago Insurance Co., 26 Fed.Appx. 53, 2001 WL 1486527 (2d Cir.(N.Y.)), where the Second Circuit – albeit in an unpublished decision – held that there was no coverage for litigation costs on sanctions motion; see also Cowan v Codella, 2001 WL 30501 (S.D.N.Y. 2001).

Exclusions may also remove from coverage claims brought by a claimant related to the insured. See Salzman & Salzman v Home (2d Dep't 1999), where the Second Department held that a policy exclusion barred coverage for claim arising from line of credit transaction involving corporation in which insured had an ownership interest, but did not bar coverage for claim arising from a separate loan transaction involving another insured.

The inclusion of covered and un-covered claims may give rise to defense issues. See Rosenberg & Estis P.C. v. Chicago Insurance Company, 2003 WL 21665680 (N.Y. Sup.), 2003 N.Y. Slip Op. 51085(U)(Sup. NY 2003) citing Public Service Mutual v Goldfarb, 53 N.Y.2d 392, 442 N.Y.S.2d 422 (1981), holding that there are certain limited circumstance, when retained counsel may reach the point of an ethical conflict between his obligation to defend the insured and an insurer's coverage position, that an insurer is obligated to pay for separate counsel.

C. Intentional Acts/Fraud Exclusions

Most policies specifically delineate intentional acts and fraudulent or dishonest conduct as excluded from coverage. Some policies, however, provide “Innocent Insured” coverage for those insured that are not actively involved in the intentional or fraudulent conduct.

Many policies, however, specifically acknowledge the obligation to defend, although not indemnify, even as to insureds alleged to have acted intentionally, dishonestly or in perpetration of a fraud. See Rooney v Chicago Insurance Co., 26 Fed.Appx. 53, 2001 WL 1486527 (2d Cir.(N.Y.)); Admiral Insurance Company v Weitz & Luxenberg, P.C., 202 WL 31409450 (S.D.N.Y. 2002)

Exclusion of fraudulent, criminal or intentional conduct, of course, are enforceable. See Seskin & Sassone v Liberty International Underwriters, 306 A.D.2d 520, 761 N.Y.S.2d 679 (2d Dep't 2003)(Legal malpractice policy did not cover claims against insured for fraud, negligent representation, and deceptive trade practices while acting in his capacity as president of medical equipment manufacturer.); Tartaglia v Home Insurance Co., 240 A.D. 2d 396, 658 N.Y.S. 2d 388 (2d Dep't 1997)(Attorney who devised a scheme to fraud his client's creditors was not covered by professional liability policy and claims were excluded by the dishonest, deliberately fraudulent criminal acts or deliberately wrongful acts exclusion); see also Chicago Ins. Co. v Borsody, 165 F.Supp.2d 592 (S.D.N.Y. 2001)(Attorney misrepresentations to health insurers was not a negligent act and was excluded by fraud and dishonest acts exclusion).

D. Damages Typically Excluded from Coverage

Punitive and Exemplary Damages, including costs, fees, fines, and penalties.
Damages under Securities Act, RICO, ERISA or similar state statute violations.
Claims for return or reimbursement of legal fees, costs or expenses paid to the insured.

PROFESSIONAL LIABILITY INSURANCE COVERAGE ISSUES

Page 4

CLAIM NOTIFICATION AND REPORTING ISSUES

A. What Constitutes a "Claim"

"Claim" means a demand received by any Assured for money or services including the service of suit or institution of arbitration proceedings against the Assured.

B. Notice of Circumstances That May Lead to a Claim

Policies typically provide:

"Notice of Claim, or Circumstances That May Lead to a Claim" provision requires that "if any Claim is made against the Assured," then the Assured must provide "immediate" notice of every demand, notice, summons or other process received by him or his representative.

The same provision also requires notice to Underwriters "[i]f during the Period of Insurance the Assured first becomes aware of any act, error or omission that could reasonably be the basis for a Claim...."

When the insured knows of the claim prior to the inception of the claims made policy, the policy will not cover the claim. Rosenbaum v Chicago Insurance Co., 306 A.D.2d 29, 761 N.Y.S.2d 637 (1st Dep't 2003); Fogelson v The Home Insurance Company, 129 A.D.2d 508, 514 N.Y.S.2d 346 (1st Dep't 1987).

When claim not reported to insurer with policy in effect at the time the claim is known but is later reported to other insurer with policy in effect when the lawsuit is commenced, there is no coverage under either of the two claims-made policies. Ingalsbe v. Chicago Insurance Co., 270 A.D.2d 684, 704 N.Y.S.2d 697 (3d Dep't 2000.)

C. Misrepresentations on the Application for Coverage

A factual misrepresentation may serve to void an insurance contract if " 'knowledge by the insurer of the facts misrepresented would have led to a refusal by the insurer to make such contract.' Insurance Law § 3105(b))." (Abulaynain v. New York Merchant Bankers Mut. Fire Ins. Co., 128 A.D.2d 575, 576, 513 N.Y.S.2d 5; see also, Kulikowski v. Roslyn Savings Bank, 121 A.D.2d 603, 503 N.Y.S.2d 863, app. dsmd., 69 N.Y.2d 705, 512 N.Y.S.2d 364, 504 N.E.2d 691, rearg. denied, 69 N.Y.2d 900, 514 N.Y.S.2d 1029, 507 N.E.2d 1092).

Failure to disclose disciplinary proceedings in application was a misrepresentation warranting rescission. Chicago v Kreitzer & Vogelmann, 265 F.Supp.2d 335 (SDNY 2003).

An associate's hidden acts, however, are not a misrepresentation if unknown to the firm. Halloway v. Sacks and Sacks, 275 A.D.2d 625, 713 N.Y.S.2d 162 (1st Dep't 2000).

PROFESSIONAL LIABILITY INSURANCE COVERAGE ISSUES

Page 5

D. Late Notice

No prejudice required for insurer's disclaimer for late notice, see Cade & Saunders PC v. Chicago Insurance Co., 332 F.Supp.2d 490 (NDNY 2004), but the law is still unsettled as to New York's "no prejudice exception" in cases where there was timely notice of occurrence but late notice of lawsuit. See Varrichio v. Chicago Insurance Co., 312 F.3d 544 (2d Cir. 2003).

Estoppel – to invalidate an insurer's late disclaimer - requires showing of prejudice to the insured. See Adams v Chicago Insurance Co., 49 Fed. Appx. 346, 2002 WL 31398801 (2nd Cir.(N.Y.)) (2d Cir. 2003), holding that while the insurer delayed in disclaiming, there was a factual issue as to whether the insured was prejudiced by the delay in order for common law estoppel to be applied to bar late disclaimer. See also Bluestein & Sandler v. Chicago Insurance Co., 276 F.3d 119 (2d Cir. 2002), where the Court found prejudice to the insured as follows:

Again, under New York law, prejudice to an insured may be presumed where "an insurer, though in fact not obligated to provide coverage, without asserting policy defenses or reserving the privilege to do so, undertakes the defense of the case, in reliance on which the insured suffers the detriment of losing the right to control its own defense." Flack, 51 N.Y.2d at 699, 435 N.Y.S.2d 972, 417 N.E.2d 84. In such cases, "though coverage as such does not exist, the insurer will not be heard to say so." Id. (citing O'Dowd v. Amer. Sur. Co. of N.Y., 3 N.Y.2d 347, 355, 165 N.Y.S.2d 458, 144 N.E.2d 359 (1957)); see also Touchette Corp. v. Merchants Mut. Ins. Co., 76 A.D.2d 7, 429 N.Y.S.2d 952, 955 (4th Dep't 1980)(stating that "proof of prejudice may be implied where the insurer has complete control of the defense"). Here, CIC's designated counsel, Silverman, controlled Bluestein's defense for over two years before any disclaimer by CIC. Consequently, prejudice must be presumed.

In any event, Bluestein suffered actual prejudice. Silverman conducted Bluestein's defense almost to the close of discovery before CIC disclaimed coverage on a ground then advanced for the first time. Despite Bluestein's limited pro se participation in preparation of the answer and possibly in depositions, there is no evidence in the record that either Silverman or Bluestein explored the significance of DFJ's claim for the return of legal fees. Because of CIC's dilatory disclaimer, targeted discovery regarding this issue was no longer possible, or, at the very least, was seriously compromised.

E. Cooperation

Policies typically provide:

*Insurer's right to investigate.
Insured's duty to cooperate.*

Heavy burden on insurer. See Thrasher v. USLIC, 19 N.Y.2d 159, 225 N.E.2d 503(1967).

EXHIBIT 1

The Underwriters agree with the Assured, named in the Declarations made a part hereof, in consideration of the payment of the premium and reliance upon the statements in the application which is made a part of this insurance policy (hereinafter “policy” or “insurance”) and subject to the Limits of Liability, exclusions, conditions and other terms of this insurance:

A. Coverage

To pay on behalf of the Assured Damages and Claims Expenses which the Assured shall become legally obligated to pay because of any Claim or Claims, including Claims(s) for Personal Injury as hereinafter defined, first made against the Assured and reported to the Underwriters during the period of Insurance or Extended Reporting Period, arising out of any act, error or omission of the Assured in rendering or failing to render professional services for others in the Assured’s capacity as a lawyer, Fiduciary or Notary Public, but solely for acts on behalf of the Named Assured designated in Item 1 of the Declarations and caused by the Assured, except as excluded or limited by the terms, conditions and exclusions of this policy.

“Claim” means a demand received by any Assured for money or services including the service of suit or institution of arbitration proceedings against the Assured

“Fiduciary” means an Assured’s capacity as an administrator, conservator, executor, guardian, trustee, receiver, escrow agent or any similar capacity.

“Damages” means a monetary judgment, award or settlement.

“Personal Injury” means:

- (1) false arrest, detention or imprisonment, wrongful entry or eviction or other invasion of the right of private occupancy, or malicious prosecution;*
- (2) libel or slander or other defamation or disparaging material, or a publication or an utterance in violation of an individual’s right of privacy.*

EXHIBIT 2

Coverage

We agree with the named insured that in consideration of the premium paid, your obligation to pay the deductible, and in reliance upon statements made by the named insured in the application, the Declarations, and supplementary information provided by the named insured, and subject to the limits of liability as stated in the Declarations, and the exclusions and all other terms and conditions of this policy, as follows:

We agree to pay on your behalf all damages in excess of the deductible amount and up to the limits of liability stated in the Declarations that you become legally obligated to pay, provided such damages:

- 1. result from claims*
 - a. first made against you during the policy period or any extended reporting period, if applicable, and*
 - b. reported to us in writing; and*
- 2. are caused by a wrongful act which takes place before or during the policy period.*

“bodily injury” means physical injury, sickness, disease or death of any person.

“claim” means a demand received by you for money or services, including the service of suit or institution of arbitration proceedings against you, or a disciplinary proceeding.

“damages” means a monetary judgment or settlement, but does not include fines or statutory penalties, sanctions whether imposed by law or otherwise, any other amount awarded in any disciplinary proceeding, the return of or restitution of legal fees, costs and expenses, punitive or exemplary damages, the multiplied portion of multiplied damages, amounts which you are not financially liable or which are without legal recourse to you or matters which may be deemed uninsured under applicable law.

“disciplinary proceeding” means a proceeding in which a complaint alleging a wrongful act, a violation of any disciplinary rule or other professional misconduct is brought before a tribunal of competent jurisdiction which shall make a determination subject to appeal or other review and/or a final and enforceable determination as to whether such alleged professional misconduct is to be the subject of discipline.

“personal injury” means:

- (a) *false arrest, detention or imprisonment, wrongful entry or eviction or other invasion of the right of private occupancy, or malicious prosecution;*
- (b) *libel or slander or other defamation or disparaging material, or a publication or an utterance in violation of an individual’s right of privacy; or*
- (c) *injury arising out of an offense occurring in the course of the named insured’s advertising activities, including but not limited to infringement of copyright, title slogan, patent, trademark, trade dress, trade name, service mark or service number.*

“professional legal services” means legal services and activities performed for others as:

- k. a lawyer;*
- l. a notary public;*
- m. an arbitrator;*
- n. a mediator;*
- o. a title insurance agent;*
- p. a designated issuing lawyer to a title insurance company;*
- q. a court appointed fiduciary;*
- r. a member of a bar association, ethics, peer review, formal accredited or licensing, or similar professional board or committee;*
- s. an author, strictly in the publication or presentation of research papers or similar materials and only if the fees generated from such work are not greater than ten thousand dollars (\$10,000); and/or*
- t. an administrator, conservator, receiver, executor, guardian, or any similar fiduciary capacity, or court-appointed trustee, however, no coverage shall apply to any loss sustained by you as the beneficiary or distributee of any trust or estate.*

Services performed by you in a lawyer-client relationship on behalf of one or more clients shall be deemed for the purpose of this section to be professional services in your capacity as a lawyer, although such services could be performed wholly or in part by non-lawyers.

“wrongful act” means any actual or alleged act, error, omission or personal injury which arises out of the rendering or failure to render professional legal services.