

TENTATIVE DRAFT

NOTE: It is requested that suggested corrections be sent to the Office of the Secretary, San Francisco, as soon as possible.

MINUTES

BOARD OF GOVERNORS MEETING

SAN FRANCISCO

MARCH 21, 1997

The Board of Governors of the State Bar of California convened in closed session in the Board Meeting Room of the State Bar Office, 555 Franklin Street, San Francisco, California, at 8:37 a.m., on Friday, March 21, 1997, Thomas G. Stolpman presiding.

The following members of the Board of Governors were present: Marc D. Adelman, Jo Ellen Allen, Joseph J. Bell, Wendy H. Borchardt, John J. Collins, Jennifer Feres, Judith A. Gilbert, Leon Goldin, Andrew J. Guilford, Samuel L. Jackson, Peter F. Kaye, Raymond C. Marshall, John G. Morris, George W. Porter, Ann M. Ravel, James M. Seff, John F. Stovall, Jeffrey A. Tidus, Dorothy M. Tucker and Pauline A. Weaver.

The following members of the staff also were present: Jerry Braun, Karen Betzner, Stuart A. Forsyth, Jeffrey T. Gersick, Judy Johnson, Jaclyn Reinhardt, Herbert M. Rosenthal, Toni Smith and Diane C. Yu.

The Board went into open session at 9:58 a.m., and the following members of staff entered the meeting: Heather Anderson, David Bell, Kathleen Beitiks, Art Bernstein, Phyllis Culp, Kristina Horton Flaherty, Karen Hagelund, Dean Kinley, Kris Krobot, David Long and Mary Viviano.

The appointments were considered in confidential session and the action of the Board is reported below.

6011

Upon motion made, seconded and adopted, it was

RESOLVED, upon recommendation of the Board Committee on Appointments, that the Board hereby reappoints Steven M. Gevercer, member, and appoints Ruthe C. Ashley, John A. Cape, Cheryl A. Forbes and Brian Rix, members, Board of Directors, Legal Services of Northern California, each to serve for a

John J. Collins, Kevin R. Culhane, Co-Chair, State Bar Approved Committee on Professional Liability Insurance, and Robert Chick, Chief Executive Officer, Lawyers Mutual Insurance Company, gave a presentation on mandatory malpractice insurance.

151

Upon motion made, seconded and adopted, it was

RESOLVED, upon recommendation of the Board Executive Committee, that the Board hereby refers to the Committee on Professional Liability Insurance and the Board Committee on Regulation and Discipline the following proposals relating to recommendation number 23 [professional liability insurance] of the Final Report of the Commission on the Legal Profession and the State Bar of California:

- a. To amend Business and Professions Code section 6148, which would require every attorney performing services for a client to affirmatively state in writing to the client that he/she does not have Errors and Omissions Insurance to protect against a claim of legal malpractice;
- b. That the Rules of Professional Conduct be amended to provide that in any case where a judgment against an attorney resulting from a claim of legal malpractice becomes final and remains unsatisfied for a period of 90 days on application of the judgment creditor, the attorney shall be suspended from the practice of law until such time as said judgment is satisfied in full; and
- c. That all attorneys engaged in the private practice of law, either full or part time, be required to post a performance bond similar to that required of real estate agents/brokers, contractors and the like, in a sum of at least one hundred thousand dollars (\$100,000); and it is

FURTHER RESOLVED that the Board hereby refers to the Board Committee on Administration and Finance the proposal to include with the fee statement a survey requiring the member to disclose whether or not he or she has a policy of malpractice insurance and the limits thereof, and whether he or she is engaged in government service; this information to be used for a statistical analysis of the current percentage of members having coverage.

152

A presentation on the Medical Injury Compensation Reform Act (MICRA) was given, with David Casey, Kathy Olson and Leroy Hirsch advocating modification of MICRA, and Fred Hiestaud and Mark Zimmerman advocating no modification of MICRA.

133

A motion was made, seconded and passed to refer this item [California Bar Journal Editorial Board] back to the Board Committee on Member and Consumer Relations for reconsideration, and to bring it back to the Board at its next meeting. In the interim, the California Bar Journal Editorial Board Policy adopted in 1993, by the former Board Committee on Communications and Bar Relations, in the form attached to these minutes and made a part hereof, is the policy of the State Bar.



THE STATE BAR OF CALIFORNIA

OFFICE OF RESEARCH

555 FRANKLIN STREET, SAN FRANCISCO, CALIFORNIA 94102-4498

(415) 561-8200

RE: **MARCH 151**
Mandatory Malpractice
Insurance Discussion

DATE: March 14, 1997

TO: Members of the Board of Governors

FROM: David Long, Director, Office of Research

SUBJECT: Background information for Your Discussion of Mandatory Professional Liability Insurance

This memorandum provides background for your March 21 meeting discussion concerning Mandatory Professional Liability Insurance. It briefly describes past studies and proposals relating to mandatory professional liability insurance and surveys which explored professional liability insurance issues. (For further detail on past proposals on mandatory professional liability insurance see the attached February 14, 1989 Board of Governors agenda item relating to the State Bar Approved Professional Liability Insurance Program.) It also considers some of the factual assertions on this subject made by Professor Manny Ramos in a January 30, 1997 letter to Board members.

State Bar 1987 Study of Mandatory Professional Liability Insurance

The last major study of mandatory professional liability insurance was conducted during the period 1986-87 by a Board-appointed Commission on Professional Liability Insurance. This commission, which I staffed, proposed a mandatory professional liability insurance program based on a statutorily-created non-profit entity that would be known as the California Attorneys' Professional Liability Fund that would be the exclusive provider of first-tier insurance for California attorneys.¹

¹ This was the second study of mandatory PLI conducted by the State Bar. The first study arose out of the "hard" insurance market of the mid-1970s following the withdrawal from the California market of the carrier for the State Bar-approved professional liability insurance program. This study also proposed an Attorneys Professional Responsibility Fund to provide first-tier PLI insurance. A bill, AB 209, was introduced to authorize this fund. After a State Bar plebiscite showed that only 52 percent of California lawyers favored this mandatory PLI plan, the bill was amended to become a study bill that would have created a Client Protection Board charged with reporting to the Legislature on a plan to "assure that all attorneys in private practice have errors and omissions insurance or equivalent methods of client protection." (Sen. Amend. to AB 209 (1977-78 Reg. Sess.) August 16, 1977). The study bill passed the legislature but was vetoed by Governor Jerry Brown.

The proposal for a single state fund was predicated on the inability of the private insurance market to ensure that professional liability insurance (PLI) would be available to California's attorneys through both "hard" and "soft" markets. This study was conducted during a "hard" market in which many insurance carriers had left the California attorneys PLI market and premiums quoted by the remaining carriers had increased dramatically in a short period.

When sent out for comment by the Board of Governors after "tentative approval" in the Spring of 1987, the Commission's proposal generated significant negative comment. It was opposed by a number of stakeholders including some large local bar associations, some women, part-time and minority attorneys and others who were afraid the cost of insurance would drive many practitioners out of business, and by the insurance industry. It was opposed by others who practiced in areas of the law considered low risk for claims and who did not want to subsidize premium rates for attorneys in higher risk practices. The possibility of premium surcharges for repeated claims was also a concern because of its potential for driving lawyers who practice in areas in which the risk of claims is higher out of business. In addition, the plan was of little use to large firms which typically have a self-insured retention greater than the amounts of coverage offered under the plan. Consequently, no legislation to implement this proposal was introduced, although Assembly member Phil Eisenberg had a spot bill pending for this purpose in 1987.

Following the demise of this plan there were discussions of other options. One option considered was a state fund similar to the state Worker' Compensation Fund that would compete with private carriers at one level, but would be protected against excessive "adverse selection" by prohibiting private competitors from under-cutting the fund's base rates. This option was considered politically and practically problematic. Another option considered was a State Bar "captive" insurance company. This was viewed as a costly and not particularly popular way to provide insurance since participating attorneys would likely have to make a capital contribution in addition to their premiums; and, because of the risk of adverse selection, a captive could not be viewed as a universal insurance mechanism, i.e., to remain viable it would have to underwrite selectively.

1987 Mandatory Professional Liability Insurance Survey

When the mandatory PLI plans were shelved in the summer of 1987, discussion then focused on the absence of hard data on which to base decisions about mandatory PLI. Consequently, AB 483 was adopted in 1987 to require the State Bar to conduct a survey for the purposes of compiling data on the subject of legal malpractice insurance. This was authorized as a mandatory survey because of the concern that complete and accurate data, particularly about claims, would not be forthcoming from a voluntary survey of attorneys. The actual return rate was 89%, an unheard of response rate. Nearly 4,000 responses were received from the general membership providing a 99% confidence level with an error estimate of 2%. In order to more fully explore issues relating to PLI claims, plaintiffs' and defense attorneys were over sampled because of the view that they would have more information on these issues than the general

membership. In addition, attorneys with disciplinary complaints were over sampled to explore the relationship between malpractice claims and disciplinary complaints..

The 1987 survey found that 36% of all attorneys in private practice and 28% of attorneys in full time private practice did not have professional liability insurance and that 80% of those in part time private practice did not. The survey found a strong relationship between the then "hard" insurance market and percentage of attorneys without insurance. About half of the attorneys without insurance in 1987 had been covered in the past, and 63% of those who previously had insurance had dropped their coverage during the past four years - a period that coincided with reduced availability and rapidly rising premiums.

Several questions were asked in the survey about unsatisfied judgments in malpractice cases.

First, attorneys were asked about judgments against them that were unsatisfied. Only one attorney in the sample general population reported an unsatisfied judgment against the attorney because of insufficient funds. Fifteen attorneys with disciplinary complaints, however, reported that a claim was then unsatisfied because of insufficient funds.

Attorneys were also asked about the malpractice cases they had considered or in which they had provided representation during the last five year (prior to the 1987 survey). More than one-fifth of the membership had been asked to advise in a legal malpractice situation and about 11% had represented plaintiffs and 8% had represented defendants in a legal malpractice claim.

The sample general population of attorneys reported that during the past five years 33 malpractice judgments, settlement agreements, or arbitration awards were not satisfied because the defendant was uninsured and lacked assets. Statistically, this represented about 790 unsatisfied claims over a five year period, statewide, for this reason. The sample general population of attorneys also reported that 51 of the claims in which representation was provided had claimed damages sufficient to warrant prosecution, but were not prosecuted because the defendant was uninsured and lacked assets; statistically, this represented an estimated 1,225 claims not prosecuted for this reason during the five year period in question. The sample general population also reported turning down 90 claims considered meritorious, in which a prospective malpractice plaintiff was seeking advice or representation, on the basis that the attorney involved was uninsured and lacked sufficient assets to satisfy a judgment; this reflects an estimated 2160 turn-downs during that five year period. Of course, there is no way of knowing whether the claims that were turned down were in fact meritorious.

1991 State Bar Demographic Survey

The most recent data on attorneys professional liability insurance in California is from the demographic survey which the State Bar conducted in 1991. Although voluntary, this survey, which went to over 14,000 attorneys, had an extremely high response rate of 73%. This study

found that 69% of the bar was engaged in some private practice - including part-time practitioners. Of those with any private practice, 22% were not covered by professional liability insurance (in comparison to 36% of those in private practice who did not have insurance in 1987) The demographic survey found that sole practitioners were much more likely to not have insurance than those in firms: 49% of sole practitioners (including part-time attorneys) did not have insurance while only 7% of those in law firms were uninsured. The percentage of uninsured in law firms would have been far smaller but for small firms of two lawyers (25% uninsured) and 3 to 5 lawyers (14% uninsured); larger firm size categories varied from one to four percent without insurance. As found in the 1987 survey, part-time attorneys were the most likely to be uninsured: 75% of those practicing 20 hours or less a week were uninsured (Most would also be considered sole practitioners.).

For those without insurance in 1991, unavailability of insurance was seldom cited as a reason for not having it (For example, only 5% indicated that their application had been denied or their coverage canceled or not renewed.) Cost was the most important factor; 84% cited premium expense as a somewhat or very important reasons for not having insurance (This represented 12% of the total bar.). However, almost two-thirds of those without insurance also indicated that the type or size of their practice did not warrant PLI.

The State Bar Approved Professional Liability Insurance Program

Subsequent to the demise of the 1987 mandatory professional liability proposal, the Board of Governors in 1989 adopted a State Bar approved professional liability insurance program to increase the availability of professional liability insurance for California attorneys and to explore innovative loss prevention activities. (For further information see the attached February 1989 Board of Governors agenda item approving the creation of this program.) The approved program is overseen by the Standing Committee on Professional Liability Insurance.

Since the approved PLI program was adopted in 1989, the insurance market in California has remained "soft" and has seen the entry of many new carriers. Because of this highly competitive situation, premiums have remained relatively stable over the last six years - in contrast to the dramatic increases during the "hard" market periods of the 1970's and 1980's during which the past proposals for mandatory professional liability insurance were considered.

Factual Assertions Made by Professor Ramos

Professor Manny Ramos, in a January 30, 1997 letter to the Board made several factual assertions about the number of uninsured attorneys in California.

Professor Ramos challenges the accuracy of the above-described survey data based on data from the California Department of Insurance, which he claims show that the "actual figure" on uninsured attorneys is over 50%. He notes that non-admitted and off-shore insurers do not

report data to the Department, but does not discuss how this may affect the accuracy of the Department's data.

In fact, Department of Insurance data do not accurately reflect the number of insured lawyers in California. First, Department data omit many, perhaps most, large firms which are insured through insurance programs excepted from reporting, e.g., ALAS, AIM, MPC, as well the London market, e.g., direct Lloyd underwriting. Department data also do not include the many attorneys working for California branch offices of firms based in other states that are insured through a policy provided by the head office. In addition, counts of insured lawyers maintained by the Department's data do not appear to reflect all of the growing number of attorneys who act as independent contractors to firms, and are in reality covered under the policies of the firms for which they work, even though not necessarily counted as attorneys under the firms' insurance policies. Thus, the figures exclude large segments of California attorneys, including large firms that are virtually 100% covered by insurance, which would mean that Department percentages are significantly skewed toward underestimating the percentage of insured lawyers. The most recent Department of Insurance data contain information for 18 admitted carriers; however, insurance brokers and carriers report an estimated 30 to 35 separate insurance programs operating in California. Insurance industry experts I have consulted place virtually no reliance on Department of Insurance data as to the number of insured lawyers in California. Indeed, I was informed that some carriers have reported only their number of policies to the Department and not the total number of insureds.

The only basis given for challenging the 1987 and 1991 survey data is that "participants in surveys notoriously underreport negative behavior such as not being insured." However, the premise that being without insurance is viewed as negative behavior is open to question. This is a subject which is commonly discussed among attorneys without stigma for admitting that one does not have insurance. One can imagine distortions of the truth about other "negative behavior", e.g., claims, but the simple fact of not having insurance does not seem to qualify as fact to which much opprobrium attaches - especially when respondents were given ample opportunity to explain why that do not have insurance, including that they do not consider insurance important due to the nature of their practice. Furthermore, the survey data are consistent with external reality. They show that in 1987, after several years of a "hard" insurance market and increasing premiums, more attorneys were uninsured than five years earlier when insurance was easier to obtain; and that by 1991, when the market softened, premiums leveled off and new entrants in the California market were vying for business, fewer attorneys were uninsured than in 1987.

Please let me know if you would like further information.

DCL:jb

AGENDA ITEM

APPROVED 4/24/89
LEGAL MALPRACTICE
INSURANCE

FEBRUARY 1
Consideration of
Professional Liability
Insurance

DATE: February 14, 1989

TO: Members of the Board of Governors

FROM: Kevin Culhane, Chair, Board Committee on Insurance

SUBJECT: State Bar Approved Professional Liability Insurance Program

INTRODUCTION

The Board Committee on Insurance, after exploring a number of options for expanding the market for and stabilizing the cost of professional liability insurance for attorneys, is now recommending that the Board authorize the establishment of a State Bar approved professional liability insurance plan for which Kirke-Van Orsdel Incorporated (KVI) would act as broker and Reliance National Risk Specialists would issue individual insurance policies.

As discussed below, the State Bar has a long history of activity in the area of professional liability insurance for attorneys. This history clearly shows that the availability and cost of professional liability insurance are major concerns to the membership of the State Bar and to the legislature as well. The knowledge and experience gained through this long history of involvement has also shown that the most promising approach to increasing the availability of attorney professional liability insurance while seeking to stabilize the cost of this insurance is the creation of an insurance plan which includes, as an integral feature, a loss prevention program and a greater focus on controlling claims handling costs. Such a plan offers a new insurance option for the protection of attorneys and their clients. A loss prevention program connected with such a plan which focus on improving the competency of attorneys promises substantial additional benefits in terms of improving service to clients and improving the image of the legal profession as a whole.

Background

The State Bar has a long history of activity in the area of professional liability insurance for attorneys. The State Bar has engaged in substantial study of issues related to professional liability insurance for attorneys and of proposals to require attorneys to carry professional liability insurance as a condition of practice. It has conducted an extensive survey of State Bar members on these issues. In addition, the State Bar has reviewed and reacted to legislative proposals relating to this subject, including proposals for mandating attorneys to carry insurance, and has considered proposals for the creation of a captive insurance company. The proposal to establish a State Bar approved professional liability insurance plan which is the subject of this agenda item is the culmination of these past efforts.

Over 15 years ago, in 1974, the State Bar established the BARCAL program, a State Bar approved and recommended professional liability insurance program offered through the Traveler's Insurance Companies. This program offered traditional professional liability insurance, with no special loss prevention or other cost control features. Unfortunately, the State Bar's experience with this program was one of rapidly escalating premiums for decreased levels of coverage. Litigation resulted over these premium increases and reduced coverage and, after five years, the Traveler's left the California attorney professional liability insurance market.

During the same period that the State Bar was facing difficulties with its BARCAL program, the legislature considered a bill to mandate that attorneys carry professional liability insurance and to establish a fund to provide this insurance. When this bill, SB 209, was first introduced by Senator Knox in 1977, the Board of Governors generally endorsed the concept of a legal malpractice fund. The State Bar subsequently conducted a statewide plebiscite asking the membership whether they favored this concept. Based on the results of this plebiscite, which showed only a slim majority of 51% of the membership in support of the fund proposal, and opposition from county bar associations in Los Angeles and San Diego, Senator Knox withdrew the fund proposal and replaced it with a proposal to create a commission to study the problem of attorney malpractice and to develop a plan to protect clients from this malpractice. This proposal was passed by the legislature but vetoed by the Governor.

The most recent series of State Bar and legislative initiatives in the area of professional liability insurance for attorneys began in early 1985, when Speaker of the Assembly Willie Brown introduced a bill, AB 2087, to require attorneys and doctors to maintain insurance covering liability for malpractice. The Board of Governors reviewed this bill and noted that it was sympathetic with the concept of providing further protection to clients. However, based on doubts about the feasibility of the proposed legislation, the Board resolved to disapprove AB 2087. AB 2087 became a two-year bill and died early in 1986.

In February of 1986, the legislature again considered the concept of mandating that attorneys carry professional liability insurance. AB 4225 (Connelly) would have required the Board of Governors to develop a program requiring active members to possess professional liability insurance. In developing such a program, the bill would have mandated that the State Bar study the availability and affordability of privately offered insurance and the necessity and feasibility of the Board's establishing and administering an attorneys' professional liability fund to provide insurance to all active members or those members unable to obtain privately offered insurance. AB 4225 would also have authorized the Board to conduct a compulsory survey of State Bar members, a concept which had been considered and approved by the Board in January of 1986. The State Bar worked with Assemblyman Connelly on this bill.

In late August of 1986, when passage of AB 4225 by the legislature appeared likely, the Board created a ten-member commission to implement AB 4225. The commission's functions were to design, administer, interpret and report on a compulsory survey of State Bar members concerning professional liability insurance and to analyze alternative methods of providing mandatory professional liability insurance to State Bar members.

On September 30, 1986, the Governor vetoed AB 4225. Because of the continuing concern regarding professional liability insurance among State Bar members and in the legislature, the Board, at its October 1986 meeting, ratified its earlier action creating the commission. The Commission on Professional Liability Insurance (COPLI) was given the task of meeting the objectives of AB 4225 on a voluntary basis and reporting to the Board by September 1987.

COPLI began its work in November of 1986. COPLI studied the history of attorney professional liability insurance

in California, reviewed current materials and reports of other bar professional liability insurance programs, received in-depth testimony from insurance industry experts concerning various types of attorney professional liability insurance programs around the country, and studied professional liability insurance programs developed for physicians. The commission also engaged in an intensive study of the Oregon plan, which is the only mandatory professional liability insurance program for attorneys in the country. In addition, the commission conducted seven public hearings on this subject statewide, conducted a statewide survey regarding insurance coverage and the commission's insurance plan, and received hundreds of written comments and suggestions.

COPLI presented its report to the Board of Governors at its May 1987 meeting. The commission proposed a mandatory insurance plan and statutory language to implement this plan. The Board tentatively approved COPLI's report and proposed statute subject to a 60-day comment period and final recommendation of the Board at its August meeting.

The COPLI plan was the subject of hundreds of comments. One feature of the COPLI proposal that was particularly controversial was the requirement that the professional liability fund created by the statute be the exclusive insurance for the minimum level of coverage required under the plan. Comments received and follow-up discussions suggested that another program which included private insurers should be explored as an alternative to the exclusive plan.

In the summer of 1987, a meeting was held in Sacramento with many of the participants in the discussion of the COPLI proposal to discuss the status of that proposal and of AB 344, the "spot bill" that Assemblyman Connelly was sponsoring for legislation with respect to this subject. Since all participants, including State Bar representatives, indicated an interest in having more time to work on the proposal, Mr. Connelly agreed to make AB 344 a two-year bill. It was also agreed that this additional time would be used to refine a financial responsibility plan for attorneys that would include private insurers and to obtain further information relating to attorneys' professional liability issues. Assemblyman Connelly proposed introducing a bill to authorize the State Bar (1) to conduct a mandatory survey of State Bar members on issues related to professional liability insurance and (2) to add \$1.00 per member to State Bar fees to fund the survey.

P. Terry Anderlini, chair of COPLI, reported to the Board at its August 1987 meeting regarding the comments and meetings which had taken place with regard to the COPLI plan and regarding Assemblyman Connelly's proposed survey legislation. Following this report, the Board resolved to postpone further consideration of mandatory professional liability insurance until further notice.

Assemblyman Connelly subsequently amended an existing bill, AB 483, to include the survey authorization. He also sought adoption of the bill on an urgency basis before the end of the 1987 legislative session so that the survey could be conducted during the last quarter of 1987 and paid for by a \$1.00 supplement to 1988 fees. This bill was passed by the legislature and signed into law by the Governor on September 11, 1987.

The State Bar worked with many of the participants in the discussion of the COPLI plan to develop, with the help of survey consultants, the questions to be included in the survey. The survey's main objectives were to obtain information relating to California attorneys' present coverage by professional liability insurance, reason for lack of coverage, and claims experience, and to obtain information relating to the need for coverage among uninsured lawyers and any additional needs among those who are covered. The survey was conducted in late 1987 and the final report was submitted to the Board in February of 1988.

After the survey report was submitted, a follow-up meeting was held in Sacramento in February of 1988. There appeared to be general agreement among the participants in the meeting that, rather than continuing with the proposal to establish a mandatory professional liability insurance system for attorneys, the State Bar should explore the possibility of establishing a captive insurance company to provide professional liability insurance for attorneys.

Substantial consideration was given to the possibility of creating a State Bar captive insurance company to provide professional liability insurance for attorneys. Actuarial analysis indicated, however, that a captive insurance company would need substantial front-end capitalization. The only possible mechanisms for generating this capital were either to require a substantial capital contribution up front from each attorney seeking insurance from the captive or to assess all attorneys by increasing basic membership dues. One of the clear findings of the professional liability insurance survey was that attorneys' demand for professional liability insurance is

extremely price sensitive; high premium cost was one of the primary reasons that attorneys reported for not carrying professional liability insurance. This price sensitivity made it highly unlikely that California attorneys would be willing to make large front end capital contributions. The dues increase option was also impractical because formation of this captive insurance company was being considered contemporaneous with the substantial increase in basic State Bar dues. For these reasons, obtaining the front end capitalization needed to establish a captive insurance company was not considered feasible.

With the mandatory insurance fund and captive insurance company options eliminated, focus was once again turned toward the development of a State Bar approved and endorsed professional liability insurance plan.

The investigation of the mandatory insurance option had revealed that most captive and commercial insurance companies had done very little with respect to loss prevention and control. The principal loss control mechanism used was refusal to renew policies or substantial premium increases. It was also clear from the actuarial analysis performed in connection with the consideration of a captive company that California attorney professional liability insurers generally had very high claims handling costs; approximately \$1.20 for every \$1.00 in claims paid as compared to a national average of between \$.60 and \$.70 per \$1.00 paid. Given these facts, it appeared that efforts to control losses and claims handling costs could have a measurable effect on the cost of professional liability insurance for attorneys. In addition, loss prevention activities designed to improve the competence of attorneys could have substantial additional benefits in terms of enhancing service to clients and improving the image of the profession as a whole. For these reasons, the goal of the Board Committee on Insurance in exploring the possibility of a State Bar approved professional liability insurance program has been to establish a program with a focus on loss prevention and claims cost control.

The Committee explored with four insurance brokerage firms the development of a State Bar approved professional liability insurance program with the desired loss prevention and claims control focus. Kirke-Van Orsdel Incorporated (KVI) responded with the best proposal and appeared to offer the best administrative services; a major focus of KVI's business is the administration of association insurance plans. KVI was therefore asked to work with insurance carriers to develop a proposal for a

State Bar approved program. The proposed program, with KVI serving as the insurance broker and Reliance National Risk Specialists issuing the individual insurance policies, is now being presented for your consideration.

The proposed program has the goal of introducing stability into the legal malpractice insurance market in California. Unlike the BARCAL program approved by the State Bar in the 1970s, the proposed program includes state of the art, sophisticated loss control and claims control features and individual underwriting which are designed to stabilize the cost of the professional liability insurance offered through the program.

A complete description of the program proposal is attached to this agenda item. However, some essential features of the proposed program are set forth here.

I. The Underwriter and the Proposed Insurance Policy.

The insurance policies will be issued by Reliance National Risk Specialists, a major insurance and financial group with 1988 revenues in excess of \$3.3 billion. Reliance is rated A (excellent) by AM best, the leading authority on operating performance of U.S. insurance companies. Reliance will in turn reinsure such portions of underwritten risks as prudent insurance practices dictate.

The insurance policy itself has been designed to provide the most comprehensive coverage available. The policy provides the standard claims made package, but with additional features relating to former partners, incidentally related professional services, personal injury coverage (including malicious prosecution) and a three-year optional extension, with guaranteed annual renewability. Significantly, full prior acts coverage will be available. The program also presents a wide variety of coverage limits and deductible options for California's practitioners. Additional program highlights regarding the policy are set forth at page 6 of the attachment to this agenda item.

II. Program Administration

The program will be administered by Kirke-Van Orsdel, Inc., one of the nation's largest full-service administrators of group insurance and professional liability programs for associations. The administrator will market the program to California attorneys through advertising, direct mail, and telemarketing. The administrator will process all policy applications,

liability claims, and loss prevention components. The loss control programs envisioned are set forth at pages 2-4 of the attachment, and include strategies to conduct annual loss control tours throughout the state to educate California lawyers in the area of law office management, claims prevention, and claims repair. Some of the other loss prevention activities which would be implemented under the program include annual seminars for law office managers, access to a library of videos concerning loss control, and a legal malpractice newsletter. Other concepts include development of a law office practice manual, establishment of a panel of mentor attorneys or experts by area of law, and development of checklists or manuals for specific areas of practice.

The program also envisions substantial claims control strategies, including the assembly of a defense panel, the utilization of a brief bank, and other management strategies that have proven effective in mitigating the transactional costs of handling lawyer malpractice claims.

III. Lawyer Competency and Basic Skills Training Program

The State Bar intends to establish and conduct a Lawyer Competency and Basic Skills Training Program to educate members so as to reduce the number of claims made against the program. The development of this program is currently underway, and it is anticipated that the cost will be paid by funds remitted to the State Bar from KVI and/or the reimbursement of administrative expenses incurred in conducting the program. It is to be noted, however, that the agreement does not require, unless required by law, that the funds paid by KVI be used on loss prevention activities.

FISCAL AND PERSONNEL IMPACT

The proposed State Bar approved professional liability insurance program is not expected to have a negative fiscal impact on the State Bar. The State Bar will not be obligated to pay KVI any compensation under the proposed brokerage agreement; the compensation due KVI for its services will be paid by the underwriting insurance company participating in the State Bar approved professional liability insurance program. The State Bar will also have no obligation to pay the underwriting insurance company; the actual insurance agreements will be between the insurance carrier and the individual applicants.

The personnel impact of this proposal is uncertain and depends upon recommendations yet to be made concerning

the most appropriate mechanisms for conducting the Competency Program and other loss prevention activities. The possible options include conducting the program with staff, by contract, by establishing a separate entity to conduct the program, or by engaging in a cooperative effort with the local bar associations.

THE STATE BAR OF CALIFORNIA
Lawyers Professional Liability Insurance

PROGRAM SUMMARY
February 24, 1989

INTRODUCTION

The goal of the California State Bar endorsed Lawyers' Professional Liability Program will be to introduce stability into the legal malpractice environment in California, with a unique program which includes "State of the Art," sophisticated loss control and claims control features and individual underwriting.

The California marketplace presents a need for new competition with such an innovative approach. Much of the current underwriting in the state is "class rated," instead of being individually underwritten. This may have the effect of penalizing attorneys and law firms with low exposure while undercharging those who create a frequency or severity of losses. Proper pricing has an obvious and desirable policing effect.

Opportunities for a higher level of professionalism also exist in the area of loss control. In addition to providing funding for the State Bar's new competency and basic skills training programs, this insurance program will stress a number of loss control features which have proved dramatically effective in other state programs. A number of these programs are briefly mentioned herein.

Many proven techniques will also be used to reduce the costs of settling claims. There is great potential for lower insurance premiums with a more efficient mechanism for delivering funds to claimants. The process needs to be faster as well as less expensive. A summary of these plans is also included.

Finally, the most efficient distribution system for marketing will be used - a direct response State Bar endorsed program. Such an approach markets "direct," without agents, to the attorney through advertising, direct mail and telemarketing.

This combination of features should lower the frequency and severity of malpractice claims and thus the cost of insurance over time.

LOSS CONTROL

The loss control program for the California State Bar will be an ongoing joint effort between Kirke-Van Orsdel and the California State Bar. The program will be split into programs or techniques that can be implemented immediately for the quickest impact and those which will take future planning and time.

The first items to be implemented would be:

1. A two week loss control tour annually, which would cover as many cities in the state as feasible to take loss control to the attorneys in their practice areas. The program would change annually and be jointly designed by the Bar and KVI. A premium credit may be available for attendance at such a seminar.
2. With the number of claims attributable to law office management as opposed to poor lawyering, we feel it is appropriate to have an annual session for law office staff that would be devoted strictly to law office systems, confidentiality, and law office protocol. As the staff are the people responsible for maintenance of any systems used by the firm, it is critical to involve them in the loss control effort. Initially we would plan one session in Northern California and one in Southern California, however, attendance and need may dictate a larger number of programs in future years.
3. KVI currently maintains a video library, and this library could be expanded and made available to all insureds under the program. These videos deal with loss control as well as office practices.
4. A legal malpractice newsletter should be offered to all insureds under the program. There are several commercial malpractice newsletters available, or the Bar and KVI may wish to design and publish their own newsletter specific to California. This is also an item that can be implemented immediately and will create a continual awareness of the legal malpractice problems. That awareness in itself, according to many experts, will cause attorneys to practice defensively.

5. KVI will, as quickly as possible, identify all firms in the state with more than 25 attorneys and offer to put on programs at any law firm retreats. We have attached a list of programs that staff at KVI are prepared to offer at these retreats. Often, you can get greater participation from a group of attorneys who practice together and face the same problems than you can at a meeting of a County Bar. However, as an additional step, we would notify all County Bars that we would have someone available to provide the same programs at any of their monthly meetings. The same type of programs can also be offered to the Legal Administrators Association in California.
6. KVI would also make speakers available for any State Bar Association meetings, whether it be the annual meeting or Bridge the Gap programs for new admittees to the Bar.

In addition to these immediate steps for loss control, we would also propose that the following concepts be investigated:

1. A practice manual would provide information on model law office systems. The systems could be developed in cooperation with the Economics of Law Practice Section of the California State Bar and then incorporated into a manual which could be provided to attorneys in the state.
2. We would also suggest a mentor panel of experts or knowledgeable attorneys by area of law. These mentors would be volunteer attorneys who would be willing to act as advisors to other attorneys. Thus, an attorney who feels that he/she might be approaching a problem in a certain matter would be able to consult a directory of volunteer attorneys and approach them with the problem. The mentor attorney may feel that the problem requires the younger attorney to associate counsel or may be easily answered in a brief conversation. The idea behind this panel is to eliminate problems before they occur. There may be problems with this concept under current ethics rules, however, such a program is in place in Ohio and Pennsylvania. These may be used as models.

3. We would also suggest that the Bar consider a statute of limitations book similar to that put out by the Professional Liability Fund in Oregon. Several states have compiled such a listing, and if practical and possible, can be a loss prevention technique which eliminates time related errors.
4. We would also suggest working with each practice section of the California State Bar to develop checklists or manuals for areas of practice. If these are not already available, they can be developed with volunteer help and can be very effective in raising the competence level.
5. We would also suggest that thought be given to providing free law office audits for firms of five or less attorneys. While larger firms may be required to have a legal malpractice audit prior to being accepted into the program, it is often the smaller firms who have systems failures, and these are the firms less likely to be able to afford or proceed with a legal malpractice audit. The Professional Liability Fund in Oregon does provide such a function, and I believe that the costs and the benefits of such a system should be weighed carefully for possible future implementation.

CLAIMS CONTROL

The manner in which professional liability claims are handled will also be critical to the overall bottom line and the long-run stability of the program. The current actuary for the California State Bar has indicated that defense costs are currently costing insurers \$1.20 for every \$1.00 paid out to claimants in indemnity. It is anticipated that the program will include proven techniques developed by the Oregon Bar Professional Liability Fund. After ten years of operation in Oregon, defense costs averaged 25 to 30 cents for every dollar paid to the claimants. The national average is 60 cents of every dollar paid in defense costs. It is the immediate goal of the California program to reduce costs as close to the national figures as possible with the ultimate goal of equaling the Oregon results.

Proposed special features for a claims handling program would be:

California Office

Reliance and KVI will have California offices. Claims will be coordinated to the extent feasible using California attorneys and claim administrators.

Defense Panel

A defense panel will be chosen from California attorneys having expertise in the defense of Lawyers' Professional Liability claims. Expertise and fee schedules will be balanced before selection is made.

As a requirement to remaining on the defense panel, the members must attend a two or three day seminar on Professional Liability defense and changes in the law. In addition to being educational, these seminars will provide a forum for sharing of cases, strategies and networking as all participants serve a common insurer.

Expert Witnesses

In addition to our defense panel, we will ask for volunteers to form a review panel. These lawyers would be attorneys who have special expertise in areas of law such as bankruptcy, labor law, admiralty, workmen's compensation, etc. These lawyers would not be defense counsel but would assist in-house counsel on the merits of the case and testify as experts in the areas of their respective expertise. We anticipate that this panel will save substantial dollars and there may be cases that can be repaired by using this volunteer advice.

Brief Bank

The insurer will establish a brief bank for collection of research and decisions. This bank will grow over time and all defense panel members will submit their research to the insurer. Upon receipt of a claim, the brief bank will be searched and if the matter is referred, the available research will accompany the suit papers.

No defense panel member will be paid for research unless authorized by in-house counsel.

THE POLICY

The policy and application have been specifically written for this California Program by KVI and Reliance underwriters, and with California Bar Staff input.

* The following coverage highlights summarize major policy features:

- Claims made coverage offered on a full prior acts basis;
 - Former partner coverage;
 - Predecessor firm coverage;
 - Full fiduciary coverage;
 - Incidental related professional services;
 - Personal injury coverage: including claims for malicious prosecution;
 - Discovery provision for circumstances that could lead to the possibility of a claim;
 - Three year optional extension period; guaranteed annually renewable based upon current rate levels;.
 - Non-practicing optional extension period for retirees on an unlimited basis;
 - Coverage for part-time attorneys
 - Worldwide coverage;
 - Innocent partner coverage;
 - A per claim retention applicable to loss and defense costs.
 - Potential use of Arbitration and ADR for speedy resolution of claims.
 - Defense costs included within the limit of liability, with the availability of limited defense limits in addition to the per claim limit.
- * This description is limited to brief highlights of coverage to be provided. These statements are subject to coverage, conditions and exclusions described in the policy.

UNDERWRITING/PRICING

No program for lawyers' professional liability issued through a commercial carrier can be all things to all people. The policy and underwriting will be as market sensitive as possible without jeopardizing the integrity of the overall program. Attorneys practicing in certain areas of the state and those having certain types of practice will find the program more competitive than those practicing in high risk areas. Each applicant will be considered individually and run through a multitude of tests for acceptability and pricing considerations. It is the goal of the program that the underwriting guidelines be designed to give the underwriter the opportunity to be as flexible as possible in pricing and selection of risks. However, no two law firms are ever identical, therefore, no set guidelines can be categorically applied for all risks.

With the California experience available, our independent actuary and outside consultants have worked with Reliance actuaries in arriving at a final base rate for the program. The details remaining involve only the amount of upfront savings to apply to the base rate from the loss control, claims handling, and underwriting techniques employed.

We are confident that the rate proposed to date will be competitive with other responsible Carriers writing in the state. This rate may not always be the cheapest, but will provide for a long-term, stable program.

PEER REVIEW

Recognizing that any application for legal malpractice can only convey limited information and that in any program an applicant may be declined coverage based upon information contained in the application, the California State Bar program will provide for peer review at the election of the applicant.

The purpose of the peer review is two-fold. First, is to allow an applicant to appeal a decision by the underwriter to decline or cancel coverage to another practicing attorney, and second is to give the carrier access to additional underwriting information on the firm.

The peer reviewers will be voluntary members of the State Bar who are willing to give the time to make an analysis of the underwriters' decision and then to personally meet with the declined attorney. Thereafter, a non-binding recommendation will be made to the underwriter and shared with the attorney who requested the peer review. The list of volunteers should be put together by the State Bar using County Bar assistance, but once a panel exists, they will become an advisory panel to the underwriters. Their work products will not be made available to the State Bar.

OPINION

The problem is implementation

by Kevin Culhane

As California practitioners are aware, the question of mandatory malpractice insurance has resurfaced recently.

The philosophical issues raised by proposals for mandatory malpractice insurance are varied and complex.

Attorneys hold widely divergent views regarding the propriety of "socializing" the cost of attorney negligence across the entire profession, and the related issue of whether "good" lawyers should be required to subsidize "bad" lawyers.

Moreover, the necessary decisions that must be made to implement any mandatory malpractice insurance program (i.e., who should be exempted and the level of mandated coverage) carry implicit value judgments regarding legal education and professional licensure in California, because many of the most perplexing issues derive from the fact that the legal license permits practice in a myriad of potentially unrelated practice areas.

In the late 1980s, the charge of the State Bar's Commission on Professional Liability was to study, design and propose a program of mandatory malpractice insurance for use in California.

In the end, it was implementation factors, rather than philosophical differences, that led to the conclusion that the all-encompassing Oregon fund experience could not be successfully or safely implemented in California.

The commission's study of the data quickly revealed that any structure for mandatory malpractice insurance required an Oregon-style fund, which would be the exclusive provider of first layer malpractice insurance.

It was readily apparent that without an exclusive provider, commercial carriers could continue to selectively underwrite the best risks.

This would in turn create insurmountable "adverse selection" problems within any remaining fund created to insure those who could not obtain malpractice insurance from commercial sources. Public comment most directly revealed the significant problems encountered by a proposal to import the Oregon experience into California.

In general, these problems centered on the significant differences between the lawyer populations in Oregon and California, and the significant disparities between practice types that were not reflected in the much smaller and more homogeneous lawyer population in Oregon.

An all-encompassing professional liability insurance fund, such as Oregon's, cannot work in California. Accordingly, the adoption of such a fund provides no answer to the question of how a mandatory malpractice insurance proposal could be implemented.

Those charged with the regulation of the profession will need to decide whether an attorney without insurance should be precluded from practicing in California, and also whether that judgment should change if it means that underserved client populations will lose access to legal services.

The leaders of the bar also will have to decide whether they will be satisfied with this basic judgment when the insurance market enters its next "hard" cycle, as it inevitably must.

When that occurs, the difficulty in distinguishing between "bad" lawyers who cannot obtain insurance at any price and "good" lawyers who simply cannot afford malpractice insurance during a hard market, will be drawn into its clearest focus.

The difficulties in implementing a mandatory malpractice insurance program do not prevent legitimate steps toward mandatory financial responsibility.

The statute requiring disclosure in the event that an attorney carries no malpractice insurance can be significantly improved, and further analysis is necessary regarding the licensing implications of unpaid malpractice judgments.

These and other pieces of the financial responsibility puzzle clearly deserve the ongoing attention of the State Bar.

Sacramento attorney Kevin Culhane, a former bar board member, is co-chair of the bar's Professional Liability Insurance Committee.

Main Menu

 **JOURNAL** 