LAWYERS MUTUAL | LIABILITY INSURANCE COMPANY OF NORTH CAROLINA

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I Made a Mistake. What Now? Don't Make It Worse!

RISK MANAGEMENT PRACTICE GUIDE OF LAWYERS MUTUAL

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INTRODUCTION

After instituting appropriate risk management practices and procedures, even the most competent, diligent attorneys may still make a mistake. Fortunately, most attorney mistakes are minor, resulting in little consequence to the client. There also may be ways to remedy the mistake before the client is adversely affected. However, when a material mistake does occur, many attorneys make the situation worse by mishandling the matter with their client or their professional liability insurer. The potential consequences of mishandling a material mistake may subject an attorney to significant consequences such as:

1. disciplinary proceedings at the State Bar;
2. additional causes of action (beyond mere negligence) and damages in a legal malpractice claim;
3. fee disgorgement; and
4. potential loss of coverage under your malpractice policy.

Of course, attorneys want to behave ethically and avoid these outcomes, which raises the question: "What should an attorney do after discovering that a mistake may adversely affect a client?"

When a material mistake does occur, many attorneys make the situation worse by mishandling the matter with their client or their professional liability insurer.

DUTY OF DISCLOSURE OF POTENTIAL MALPRACTICE TO A CLIENT

After becoming aware of a mistake that may prejudice your client's interests, you should first remember your ethical obligation to keep the client apprised of information that is material to the representation. Rule 1.4(a)(3) of the N.C. Rules of Professional Conduct requires a lawyer to "keep the client reasonably informed about the status of the matter." Comment [3] clarifies further that the client be kept abreast of "significant developments affecting the timing or the substance of the representation." Certainly, any actual material mistake by the lawyer is a significant development that affects the representation and should be discussed with the client as soon as practicable after learning of the circumstances.

If you are unsure whether the mistake has created a conflict of interest with your client, contact Lawyers Mutual immediately so that we can advise you under our claims repair program.

PRACTICE TIP

Additionally, an attorney must always remember that his client's interest is paramount to his own interest. A lawyer should not withhold information from a client to serve the lawyer's own interest (N.C. Rules of Professional Conduct Rule 1.4, Comment [7]), and the lawyer must avoid impermissible conflicts of interest. A "conflict of interest exists if ... the representation of one or more clients may be materially limited . . . by a personal interest of the lawyer." N.C. Rule of Professional Conduct Rule 1.7(a)(2). If you continue to represent and advise your client without adequate disclosure of your mistake, assuming it is a material mistake, you are likely to run afoul of Rule 1.7 due to the possibility that your representation is limited by your own personal interest (i.e., the desire to avoid a malpractice claim against yourself).

If you know that you have made a material mistake that cannot be fixed, you should **promptly inform the client of the mistake and tell him that due to a conflict of interest you may no longer advise him on the subject of your representation. You should also tell the client that he should seek independent legal advice regarding his rights**. Do not give the client any advice regarding a potential legal malpractice claim against you (whether a malpractice claim exists, the value of the claim, or the statute of limitations for asserting a malpractice claim). Giving legal advice about the potential for a legal malpractice claim is impermissible because you have conflict between your own personal interests and those of your client. You may tell your client that you have informed Lawyers Mutual of the matter and that the client may call us if he wants to make a malpractice claim.

However, not all mistakes require disclosure to the client. In determining whether an attorney's mistake creates a conflict of interest with his client requiring disclosure, the attorney should ask herself whether there is a real likelihood that the mistake will result in a malpractice claim by the client against the attorney. Relevant factors to consider are whether it is clear-cut that the attorney was negligent, whether the error can be fixed, and whether the potential consequences to the client might be severe. The North Carolina State Bar's recently-adopted 2015 Formal Ethics Opinion 4 (2015 FEO 4) discusses the proper analysis of whether

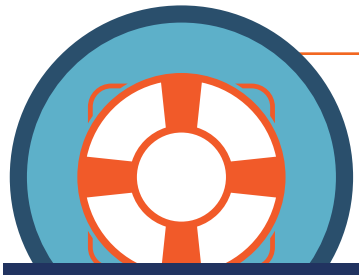
an error must be disclosed in terms of a "spectrum" of errors between material errors that prejudice the client's rights or claims at one end and minor, harmless, non-prejudicial errors at the other. The opinion describes the duty to disclose as follows:

> [W]hether an attorney has an obligation to disclose a mistake to a client will depend on the nature of the lawyer's possible error or omission, whether it is possible to correct it in the present proceeding, the extent of the harm resulting from the possible error or omission, and the likelihood that the lawyer's conduct would be deemed unreasonable and therefore give rise to a colorable malpractice claim. . . . Under this analysis, it is clear that material errors that prejudice the client's rights or interests as well as errors that clearly give rise to a malpractice claim must always be reported to the client. Conversely, if the error is easily corrected or negligible and will not materially prejudice the client's rights or interests, the error does not have to be disclosed to the client.

2015 FEO 4 further advises, "When a lawyer does not know whether disclosure is required, the lawyer should err on the side of disclosure or should seek the advice of outside counsel, the State Bar ethics counsel, or the lawyer's malpractice carrier." If you are unsure whether the mistake has created a conflict of interest that you must disclose to your client, **contact Lawyers Mutual immediately so that we can advise you under our claims repair program**. For instance, service problems are often correctable and default judgments may be set aside for excusable neglect. With a prompt and effective claims repair effort, it may be possible to correct such problems and get your client's matter back on course. Lawyers Mutual frequently engages outside claims repair counsel to assist our insureds and their clients with pleadings, motions, hearings, and appeals when it appears that a mistake may be fixed.

If the error is material but can still be fixed, it is often in the best interests of both the attorney and the client to attempt to remedy the situation or mitigate or avoid a loss. In these instances, your interests will generally be aligned with the interests of your client so that withdrawal is not required under Rule 1.7(b). Again, please contact Lawyers Mutual as soon as possible to discuss potential conflicts of interest and opportunities for repair. **Before undertaking any repair effort, you must obtain the informed consent of the client to continue the representation**. Informed consent requires: (1) disclosing the material facts surrounding the error; (2) informing the client that he has the right to terminate the representation; and (3) informing the client that he has the right to seek other counsel.

When informing your client that you may have made a mistake, keep in mind that the ethics rules prohibit a lawyer from settling a legal malpractice claim "with an unrepresented client or former client unless that person is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent counsel in connection therewith." N.C. Rules of Professional Conduct Rule 1.8(h)(2). This often comes up when a disgruntled client states that she is inclined to sue for malpractice unless the attorney returns



PRACTICE TIP

In determining whether an attorney mistake creates a conflict of interest with his client, ask yourself whether there is a real likelihood that the mistake will result in a malpractice claim. Relevant factors to consider

1. It is clear-cut that the attorney was negligent?
2. Can the error can be fixed?
3. Are the potential consequences to the client possibly severe?

or gives up a fee. If the attorney agrees to do so without meeting the ethical requirements of Rule 1.8(h)(2), it may not only result in an ethical violation, but also add fuel to the fire in a subsequent malpractice claim.

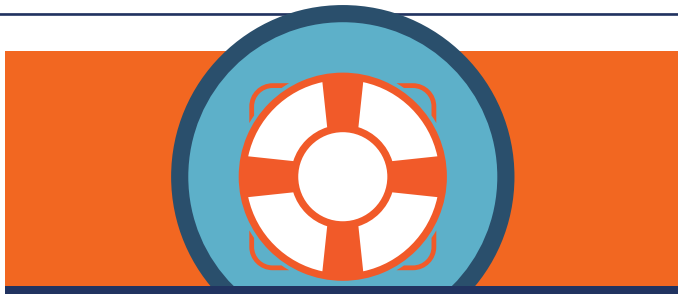
If the mistake is one that requires you to withdraw as counsel due to the conflict of interest with your client, you should also provide your client with their file, **keeping a copy for yourself**. N.C. Rules of Professional Conduct Rule 1.16(d) states that a lawyer "shall take steps to the extent reasonably practicable to protect a client's interests, such as . . . surrendering papers and property to which the client is entitled." Comment [10] to the Rule provides:

> The lawyer may never retain papers to secure a fee. Generally, anything in the file that would be helpful to successor counsel should be turned over. This includes papers and other things delivered to the discharged lawyer by the client such as original instruments, correspondence, and canceled checks. Copies of all correspondence received and generated by the withdrawing or discharged lawyer should be released as well as legal instruments, pleadings, and briefs submitted by either side or prepared and ready for submission. **The lawyer's personal notes and incomplete work product need not be released**. However, if draft documents would be helpful to successor counsel, you may consider including them.

You also should keep your notes and correspondence from communications with Lawyers Mutual's claim staff about reporting the potential legal malpractice claim separate from your client's file. Your correspondence with Lawyers Mutual is yours, not your client's.

MISHANDLING A MISTAKE MAY RESULT IN DISCIPLINARY PROCEEDINGS, INCREASED DAMAGES, AND FEE DISGORGEMENT

A review of the N.C. State Bar Journal's monthly announcements of attorney discipline illustrates the severe disciplinary consequences to an attorney who mishandles a mistake in violation of the ethics rules. Attorneys have been disciplined for hiding their mistakes from clients, lying about mistakes to clients, and misappropriating funds to cover their mistakes. Newsworthy instances of such attorney conduct in North Carolina include an attorney whose negligence resulted in the dismissal of several client cases that he subsequently covered up by telling the client that he had settled the cases. Of course, he had done no such thing, and the money for the "settlements" was misappropriated from other clients' funds. While such egregious conduct is clearly unethical, sticking your head in the sand after discovering a mistake and failing to inform your client may also constitute an ethical breach.



PRACTICE TIP

A client who is promptly informed of a mistake and dealt with honestly may decide not to pursue a legal malpractice claim, especially if there is a good history with the attorney.

At Lawyers Mutual, we frequently see potential claims that never materialize because of the honesty of the attorney with his client and the good will the attorney established with the client in prior representations.

Beyond the potential for discipline from the State Bar, mishandling duties to the client after discovering a mistake may also result in increased malpractice exposure for the attorney. A client who is promptly informed of a mistake and dealt with honestly may decide not to pursue a legal malpractice claim, especially if there is a good history with the attorney. At Lawyers Mutual, we frequently see potential claims that never materialize because of the honesty of the attorney with his client and the good will the attorney established with the client in prior representations. However, when a client discovers that his attorney has not been honest about making a mistake, the likelihood of the client suing for malpractice is increased tremendously.

Obviously, evidence that the attorney was hiding things from a client is also red meat for a legal malpractice attorney before a jury. Evidence that an attorney was not forthcoming about a mistake with his client can inflame a jury, especially given the negative public opinion towards attorneys generally. Many times this evidence will be presented by an expert in legal ethics who opines on all the ways the defendant-attorney violated the ethics rules.

Equally serious may be the increased damages and theories of liability that are opened up where an attorney mishandles his duties after making a mistake. Mere negligence may turn into claims for double damages for breach of fiduciary duty and punitive damages where such claims would not otherwise exist except for the attorney's post-mistake conduct. Not only will these types of claims increase the damages in a legal malpractice case, but they are likely excluded from coverage under your malpractice insurance policy.

Breach of fiduciary duty may also give rise to a claim for disgorgement or forfeiture of fees. For example, in *Booher v. Frue*, 86 N.C. App. 390, 358 S.E.2d 127 (1987), the North Carolina Court of Appeals recognized a claim for constructive trust against an attorney for disgorgement of a fee where the Court found that an attorney was unjustly enriched based on a breach of fiduciary duty to the client. Again, the potential damage to an attorney from such a claim is magnified because legal malpractice insurance policies typically exclude coverage for claims seeking reimbursement of a fee.

Hiding a mistake from your client may also extend the statute of limitations applicable to a legal malpractice case against you. Typically, the statute of limitations on a legal malpractice claim is three years and starts to run on the date of the "occurrence of the last act giving rise to a cause of action." N.C. Gen. Stat. § 1-15(c). However, if the lawyer is not forthcoming with the client about the mistake, the statute of limitations may be extended as much as one additional year, depending on when the client finally learns of the mistake. N.C. Gen. Stat. § 1-15(c) does contain a four-year statute of repose that states that no professional malpractice claim may be brought more than four years after the last act giving rise to the cause of action.

Hiding a mistake from your client may extend the statute of limitations. Typically, the statute of limitations on a legal malpractice claim is three years but can be extended to four if the lawyer is not forthcoming with the client about the mistake.

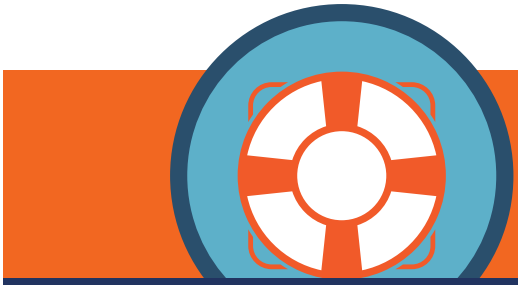
CALL LAWYERS MUTUAL PROMPTLY AND REPORT A POTENTIAL CLAIM

You purchased legal malpractice insurance to protect yourself from personal monetary liability for your mistakes. Make sure that you do not jeopardize such coverage by failing to give prompt notice of a claim to your legal malpractice insurer. One of the most common consequences of trying to hide a mistake or just hoping that it will magically go away is that an attorney will fail to give timely and proper notice of the claim to the insurance company. Such delay may jeopardize your coverage for an otherwise covered claim under your policy.

For instance, your Lawyers Mutual policy is a "Professional Liability Claims-Made and Reported Policy" that provides that Lawyers Mutual will pay money damages you become legally obligated to pay as a result of your rendering of legal services while licensed to practice law. As a claims-made and reported policy, only claims that are first made and reported to the company during a policy year will be covered. Therefore, regardless of when an attorney mistake occurs, if a claim is first presented to Lawyers Mutual after a policy has expired there most likely will be no coverage.

Furthermore, every year when you apply for a re-issue of your professional malpractice policy you are responsible to report any potential claim of which you are aware. Failure to do so may result in loss of coverage for a claim that is first presented to the insurance company after the effective date of the new policy year if that claim should have been reported on the application or during the prior policy year. Just because you think that you may be able to fix a mistake does not mean that you do not have to report it to your insurer. If you have reason to think that you breached a professional duty to your client, then you most likely have reason to foresee that such breach could be the basis for a malpractice claim against you.

Promptly reporting mistakes to your professional liability insurer will avoid any uncertainty about timeliness of the claim under your policy. Prompt reporting to Lawyers Mutual may also result in a **claims repair** opportunity that remedies the situation before a malpractice claim by the client. Remember that the Lawyers Mutual's claims attorneys and outside counsel have extensive experience in claims repairs that fix attorney errors and mitigate damages to the client from those mistakes. We work with our insured attorneys everyday in claims repair efforts both large and small.



PRACTICE TIP

PROMPTLY REPORT A POTENTIAL CLAIM!

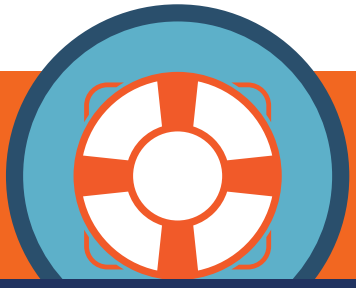
Failure to do so may jeopardize your coverage for an otherwise covered claim under your policy.

COOPERATE IN YOUR DEFENSE AND BE A GOOD CLIENT

After you have reported a claim to Lawyers Mutual, our claims staff will ask you to provide us with a written narrative that summarizes the nature of your representation of the client and the circumstances of the mistake. More than likely, we will also ask you to provide us with a complete copy of your file so that we may conduct our investigation and determine whether the claim has merit. It is important for you to provide us with the information and materials we request in a prompt manner so that we may determine as soon as possible whether there is a chance for a successful claims repair or mitigation of damages that might be lost after a delay.

Providing the necessary information to Lawyers Mutual quickly also allows us to evaluate claims and determine whether there is a good prospect for settling the matter earlier and before incurring defense costs. In many claims, our claims counsel are dealing directly with your former clients who may want to avoid hiring another attorney if the claim can be settled without litigation. If our claims attorneys cannot adequately investigate and evaluate the claim due to an attorney's delay in providing the requested file, the likelihood that the case will settle before a malpractice suit is filed is greatly diminished.

Should Lawyers Mutual retain defense counsel to defend you against a legal malpractice action, please remember that you are a client of that attorney, and treat him or her as you would want to be treated by your clients. You best assist in your defense by fully disclosing all available information to your defense counsel and promptly responding to his requests. As a lawyer, you know what makes a good client and what makes a difficult client, so act accordingly.



PRACTICE TIP

Provide Lawyers Mutual with necessary information in a timely manner.

We can evaluate the claims and determine whether there is a good prospect for settling the matter.

Finally, a legal malpractice defendant frequently has experience and training that may be valuable to Lawyers Mutual's claims staff and your defense counsel when investigating and evaluating a claim. The lawyer-defendant usually knows the former client better than claims staff or defense counsel and may also have expertise in the area of law for which he or she is being sued. Your insight into the substance of the claim against you may be very helpful in reaching a determination of the validity and value of a claim.

DISCLOSING MALPRACTICE TO YOUR CLIENT

At its April meeting, the State Bar Ethics Committee published a proposed ethics opinion (2015 FEO 4) about disclosing potential malpractice claims to clients. Communicating with a client about a mistake is never easy, but avoiding that difficult conversation can have serious consequences. The opinion explains that a lawyer is ethically required to "keep the client reasonably informed about the status of the matter" (Rule 1.4(a)(3)) and this includes a duty to disclose material errors. The proposed opinion also addresses circumstances where the attorney is required to withdraw from the representation, as well as the substance and timing of the disclosure.

"Communicating with a client about a mistake is never easy, but avoiding that difficult conversation can have serious consequences. The opinion explains that a lawyer is ethically required to "keep the client reasonably informed about the status of the matter."

The proposed opinion wisely notes that "the lawyer should seek the advice of her malpractice insurance carrier prior to disclosing the error to the client, and should discuss with the carrier what information, if any, should be provided to the client about the lawyer's malpractice coverage or how to file a claim."

Lawyers Mutual's claims attorneys regularly deal with these issues and are available to help you navigate client communications when an error has occurred. We have recently added new information to our website about this topic. "Communicating About Mistakes" explains the dangers of mishandling mistakes and offers guidance for making the necessary disclosures. If you have specific questions or need to report a potential claim, please contact us as soon as possible.