Developing Malpractice Issues

Divorce and Taxes - Innocent Spouse Elections:

The 1998 IRS Reform law includes an important enhancement to rules protecting the innocent spouse from underpayment of a joint tax return by the other spouse (§ 3201(a), Pub. L. No. 105-206, new §6015). A spouse filing a joint return who is subsequently divorced, or legally separated or lived apart for a year has the option to elect separate tax liability. The key difference in the new law is that the innocent spouse need only show that any tax underpayment would have been the spouse's responsibility if separate returns had been filed. Under the old law, innocent spouses had to show they did not know or have reason to know about the underpayment - a tough position to prove. There is some disagreement over what to advise divorcing clients. Some lawyers urge that an innocent spouse election be filed in every divorce case. Other lawyers say that automatically filing an election is a red flag to the IRS that may result in excessive scrutiny. Additionally, until the IRS issues rules and forms implementing the law, it is not clear when an election is timely and what information must be included with the filing for it to be effective. What is clear is that the innocent spouse election should be discussed in all divorce matters and the advice given and the client's decision thoroughly documented. The *Lawyers Weekly USA articles, Every Divorce Will Be Affected by IRS Law, (98 LWUSA 585, 7/27/98)* and *Innocent Spouses' Tax Relief Explained by IRS (99LWUSA 12, 1/11/99)* are helpful. See IRS Notice 1213 (8/98) and IRS Notice 98-61 (12/7/98) for guidance to include innocent spouse equitable relief for non-payment of taxes.

Firm's Internal Memoranda On Potential Malpractice Claim Not Privileged

A California firm learned the hard way how not to manage a malpractice claim. The firm almost did it right - but almost is expensive when it comes to malpractice. The firm represented a client whose statements caused the firm to believe a malpractice claim would be made. In 1994 the firm retained another law firm to advise on this concern. In 1996 the client sued the firm for malpractice. Subsequent to retaining counsel, the firm generated 60 internal documents that the client sought in discovery. The firm resisted producing the documents on the basis they were internal memoranda written because the firm suspected the client might sue. Thus, the documents were privileged attorney-client communications. The court concluded that the internal memoranda transmitted information within the firm and were not to any outside entity. Specifically, they were not directed to the outside lawyers representing the firm. Their dominant purpose was to communicate among members of the firm and not with the firm's counsel. The court rejected the firm's argument that privilege applied because it was representing itself in

preparing the memoranda with a view to cooperating with outside counsel. All 60 documents were ordered to be produced *(McCormick, Barstow, Sheperd, Wayte & Carruth v. Superior Court* (Nelson), Cal. Ct. App. 5th Dist., No. FO29503,11/21/98; Current Reports, p.590, Vol. 14, No. 25, 1/6/99, *ABA/BNA Lawyers' Manual On Professional Conduct)*. The lesson learned here may seem obvious, but it is harder than it looks to manage an evolving malpractice claim. Good risk management includes:

- Early recognition of the problem. Face up to it.
- Putting one firm lawyer in charge of managing the situation (not the responsible lawyer) who will control the internal investigation, preserve the original client file as is, determine what documentation is appropriate for the firm's malpractice file, and be the point of contact for outside counsel.
- Prompt notification of the firm's professional liability carrier.
- If necessary, retention of outside counsel, either at the firm's expense or the insurance company's appointed defense counsel.
- E-mail is not the way to exchange information internally about a malpractice claim. Document the firm's malpractice file with litigation in mind.

Adequate Preparation In The Age Of Computer Assisted Legal Research - CALR

When will failure to do legal research using the resources computers offer become legal negligence? With increasing real time legal information available on the internet that day draws near. A good example is a products liability case that the trial judge dismissed because it was preempted by federal law. No appeal was timely made. Just 85 days later the Supreme Court limited the preemption defense. When the plaintiff's lawyer attempted to reopen the litigation the 7th Circuit Court of Appeals ruled: "Ignorance of the Supreme Court's docket, although 'neglect,' is not 'excusable' - it is nothing but negligence, which does not justify untimely action." *(Norgaard v. DePuy Orthopaedics, Inc., 121 F.3d 1075* (7th Cir. 1997). To keep up with fast breaking legal news and avoid getting caught short like the lawyer in Norgaard it is critical that lawyers routinely use CALR as a matter of competent client representation and careful risk management.

Recent Change to Client Trust Account Rules: Overdraft Notification

A significant change in Kentucky Rule of Professional Conduct 1.15 Safekeeping Property was effective October 1, 1998. The rule mandates that lawyers hold funds of clients or third parties in a trust account separate from the their own funds. The change adds the requirement that trust accounts "shall be maintained in a bank which has agreed to notify the Kentucky Bar Association in the event that any overdraft occurs in the account." This

amendment applies to every lawyer who maintains any type of client trust account. Failure to place your client trust account with a bank that has agreed to cooperate with this requirement may lead to Bar discipline.

The KBA Bar Counsel advises that the KBA will attempt to identify banks that will report overdrafts on client trust accounts. The change, however, places an affirmative duty on lawyers to locate and maintain trust accounts in such a bank.

Lawyers Mutual has joined forces with IOLTA to publish a Client Trust Account Guidebook. The guidebook, which is near completion, is available free of charge to all members of the Kentucky Bar. If you did not sign up for a copy at the Fall '98 district bar meetings, it's not too late. We will be glad to send you the Guidebook when it is available. Mail or fax us your request - better yet, e-mail your request to rose@lmick.com.

Beware of the Easy Stuff

by Bob Breetz, Claims Counsel

Fire Policies-Don't Get Burned!

Lawyers Mutual has had several claims involving attorneys who mishandled claims against fire policies. Not only did the client's home or business burn, the lawyers got burned when they had to pay their deductibles. We believe these claims were avoidable if the lawyers had only taken the time to read their clients' insurance policies.

Quite often insurance policies contain a provision limiting the time to bring suit to less than the 15-year general statute of limitations on written contracts. A typical fire insurance policy imposes a one-year period of limitations. These contractually shortened periods have been upheld in Kentucky courts at least since 1944. *Johnson v. Calvert Fire Insurance Company*, 298 Ky. 669, 183 S.W. 2d 941 (1944).

Equally enforceable are contractual provisions requiring the insured to give sworn statements to the carrier. The carrier is not required to accept a deposition in litigation in lieu of a sworn pre-litigation statement. The refusal to give a sworn statement to his uninsured motorist carrier cost Mr. Temple his UM claim. *Temple v. State Farm Mutual Insurance Company*, Ky., 548 S.W. 2d 838 (1977). A similar refusal to a fire insurance carrier has twice cost a Lawyers Mutual insured a deductible and placed Lawyers Mutual in the fire insurance business.

Walk carefully through probate.

The staid world of probate has presented us with two problems worth

bringing to your attention concerning the renunciation statute, KRS 392.080.

- That statute requires the renunciation either to be "acknowledged before and left for record with the county clerk or his authorized deputy" or "acknowledged before a subscribing witness and proved before and left with the county clerk or his authorized deputy." Two circuit courts have held a simple acknowledgment before a notary public without "proving" the acknowledgment before the county clerk will not get the job done.
- An attorney instructing a paralegal to prepare a document failed to differentiate between a renunciation under KRS 392.080 and a disclaimer under KRS 394.610. That was a costly mistake.

Why wait?

What rule of law requires an attorney to wait until the last minute to file a date sensitive document? Missed deadlines continue to be a problem for far too many of our insureds. As Pete Reiser said "It doesn't take talent to be on time." Calendar all time sensitive matters (not just litigation) with adequate lead time to meet deadlines. Have two back up systems to make sure you don't forget. Your personal calendar, your secretary's calendar, and a periodic computer calendar printout will work for solos.