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PROFESSIONAL LIABILITY DEFENSE QUARTERLY

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SPECIAL POINTS OF INTEREST:

10th Annual Meeting in Chicago, Illinois on September 25-27, 2019 at the W Lakeshore Hotel

UNUSUAL NAMES, POWERFUL DOCTRINES: USE OF ROOKER-FELDMAN AND RES JUDICATA IN DEFENDING FEDERAL LAWSUITS BROUGHT AGAINST ATTORNEYS ARISING FROM LITIGATION IN STATE COURT BY: ALICE SHERREN, JAMES J. SIPCHEN, AND DONALD PATRICK ECKLER

Defending lawyers in claims arising under federal statutes can be complex and extremely expensive. Often those actions are brought as putative class actions and the statutes they are brought under contain fee shifting provisions. However, many of those cases involve underlying state court lawsuits that may allow for the application of: (1) the *Rooker-Feldman* doctrine to divest the federal court of subject matter jurisdiction and/or (2) a defense based upon claim preclusion or *res judicata*. When defending lawyers in such claims, defense counsel should consider raising these doctrines to defeat a plaintiff's claims in their entirety.

Basics of the *Rooker-Feldman* doctrine.

The *Rooker-Feldman* doctrine takes its name from *Rooker v. Fidelity Trust Co.*, 263 U.S. 413 (1923) and *District of Columbia Court of Appeals v. Feldman*, 460 U.S. 462 (1983). *Commonwealth Plaza Condo. Assoc. v. City of Chicago*, 693 F.3d 743, 745 (7th Cir. 2012). The doctrine, which is a jurisdictional limitation, "prevents lower federal courts from reviewing state-court judgments, over which only the United States Supreme Court has federal appellate jurisdiction." *Commonwealth Plaza Condo. Assoc.*, 693 F.3d at 645; *see also Kelley* v. *Med-l Sols., LLC, 548* F .3d 600, 603 (7th Cir. 2008) ("A state litigant seeking review of a state court judgment must follow the appellate process through the state court system and then directly to the United States Supreme Court."). The *Rooker-Feldman* doctrine applies when the state court's judgment is the source of the injury of which the plaintiffs complain in federal court. *Harold v. Steele*, 773 F.3d 884, 885 (7th Cir. 2014). It does not matter that the underlying state court judgment might be erroneous or even unconstitutional. *Commonwealth Plaza Condo. Assoc.*, 693 F.3d at 745. Nor does it matter that the time for appeal to the Supreme Court has expired. *Gilbert v. Illinois Board of Education*, 2007 U.S. Dist. LEXIS 23429, *7-8 (N.D. Ill.).

A challenge to jurisdiction under *Rooker-Feldman* is considered a factual attack to subject matter jurisdiction. *Flores v. Village of Bensenville*, 2001 U.S. Dist. LEXIS 13953, * 6-7 (N.D. Ill.). The plaintiff bears the burden of establishing the existence of subject matter jurisdiction by competent proof. *Saperstein v. Hager*, 188 F.3d 852, 856 (7th Cir. 1999). In ruling on a factual

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LETTER FROM THE PRESIDENT, BY: JASON JOBE

Happy New Year! That's right, we are now starting a new year for PLDF following our recent Annual Meeting in New Orleans.
But before turning the page, I want to reflect on the organization's accomplishments over the past year. We made amazing progress under the leadership of our President (Erin Higgins), Board of Directors and committee leaders.

Among other things, we saw an increase in membership, retained our new management company (PIVOT Professionals), implemented a Diversity Statement, increased the size of and involvement within practice committees, and launched a very successful Young Professionals Committee. We then celebrated the old year (and rang in the new one) at our amazing Annual Meeting in the Big Easy, where we had a record number of attendees who enjoyed informative programs, fellowship, networking, and all that Bourbon Street has to offer.
This new year brings some changes. On behalf of the entire organization, I want to

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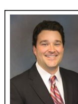

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attack, the Court may properly look beyond the jurisdictional allegations of the plaintiff's complaint to determine whether in fact subject matter jurisdiction exists. *United Transport v. Gateway Western Railway Co.*, 78 F.3d 1208, 1210 (7th Cir. 1996). If the defendant submits evidence that casts doubt on the district court's jurisdiction, the "presumption of correctness" usually accorded to jurisdictional allegations disappears. *Saperstein*, 188 F.3d at 856.

The *Rooker-Feldman* doctrine prohibits indirect attempts to undermine state court decisions. It has been repeatedly held that even where a federal plaintiff's claims "do not on their face require review of a state court's decision," the doctrine still applies if those claims are "inextricably intertwined with a state-court judgment, except where the plaintiff lacked a reasonable opportunity to present those claims in state court." *Jakupovic v. Curran*, 850 F.3d 898, 902 (7th Cir. 2017).

Accordingly, *Rooker-Feldman* bars (1) claims that "directly seek to set aside a state-court judgment;" and (2) "claims that were not raised in state court, or that do not on their face require review of a state court's decision," but are "closely enough related to a state-court judgment." *Mains v. Citibank, N.A.,* 852 F.3d 669, 675 (7th Cir. 2017). To determine whether *Rooker-Feldman* applies, the Court must "ask whether the federal plaintiff is alleging that his injury was caused by the state-court judgment." *Id*. If so, the plaintiff's claim is barred. *Id.* If "the claim alleges an injury independent of the state-court judgment that the state court failed to remedy, *Rooker-Feldman* does not apply." *Id.*

Limitations placed on the scope of the *Rooker-Feldman* doctrine.

In *Exxon Mobil Corp. v. Saudi Basic Industries Corp.*, 544 U.S. 280 (2005), the United States Supreme Court limited the application of the *Rooker-Feldman* doctrine. In *Exxon Mobil*, an oil company entered into a joint venture with a Saudi Arabian corporation, and when a dispute arose over royalties, the foreign entity filed a complaint in Delaware state court against Exxon Mobil. *Exxon Mobil Corp.* 544 U.S. at 289. Shortly thereafter, and before any judgment had been entered in the state court action, Exxon Mobil filed a parallel federal action which the Saudi company moved to dismiss based upon the Foreign Sovereign Immunities Act of 1976. *Id*. at 289-290. The district court denied the motion to dismiss and the Saudi corporation took and interlocutory appeal to the Third Circuit. *Id*. at 290.

During the pendency of the appeal in the federal action, the state court action proceeded to verdict and judgment was entered in favor of Exxon Mobil. *Id*. at 289. On its own motion, the Third Circuit raised the issue of whether federal subject matter jurisdiction abated when the judgment was entered in the state court. *Id*. at 290. The Third Circuit held that there was no subject matter jurisdiction and dismissed the appeal on that basis. *Id*. at 290-291.

In reversing the dismissal of Exxon Mobil's federal court action, the United States Supreme Court limited the application of the *Rooker-Feldman* doctrine. Writing for a unanimous court, Justice Ginsburg held that:

> [*Rooker-Feldman*] is confined to cases of the kind from which the doctrine acquired its name: cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments. *Rooker-Feldman* does not otherwise override or supplant preclusion doctrine or augment the circumscribed doctrines that allow federal courts to stay or dismiss proceedings in deference to state-court actions. *Id*. at 284.

Prior to *Exxon Mobil*, *Rooker-Feldman* had been applied expansively. The result of *Exxon Mobil* is that the *Rooker-Feldman* doctrine "is [now] a narrow doctrine, 'confined to cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments.'" *Lance v. Dennis, 546 U.S. 459, 464 (2006)* (citing *Exxon Mobil, 544 U.S. at 284*). The doctrine will not prevent a losing litigant from presenting an independent claim to a district court. *Exxon Mobil*, 544 U.S. at 293.

The main emphasis of *Exxon Mobil* is that *Rooker-Feldman* does not apply when defendants in a state court action file a parallel action in federal court as a protective measure while the state matter is still pending. *Id*. at 293-294 fn. 9. The Court specifically held that concurrent jurisdiction does not vanish if a state court reaches judgment on the same or related question while the case remains *sub judice* in a federal court. *Id*. at 292.

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Examples of specific application of *Rooker-Feldman* in actions against lawyers.

Despite *Exxon-Mobil's* narrowing of the doctrine, *Rooker-Feldman* has been utilized to bar federal suits seeking to recover on a theory that an attorney acting as a debt collector violated federal law during the course of litigation in state court. *Harold v. Steele,*, 773 F.3d 884, 885 (7th Cir. 2014). In *Harold*, the plaintiff alleged in his federal case that the defendant, an attorney by the name of Harold Steele ("Steele"), had misrepresented the judgment creditor's identity in a state court wage garnishment proceeding in violation of the Fair Debt Collection Practices Act ("FDCPA"). The Seventh Circuit held that *Rooker-Feldman* barred plaintiff's claim and stated: "If Steele's client did not own the judgment, then Harold was entitled to decision in his favor. No injury occurred until the state judge ruled against Harold." *Harold*, 773 F.3d at 886. The Court went on to observe that "[s]ection 1692e [of the FDCPA] forbids debt collectors to tell lies but does not suggest that federal courts are to review state-court decisions about whether lies have been told." *Id.* at 887. "Section 1692e does not even hint that federal courts have been authorized to monitor how debt-collection litigation is handled in state courts." *Id.*

Harold is important for an additional reason. After recognizing a disagreement among the circuits on the issue, the Court commented that interlocutory orders entered prior to the final disposition of a state court lawsuit remain subject to *Rooker-Feldman*. *Harold*, 773 F.3d at 886; *see also*, *Sykes v. Cook County Circuit Court Probate Division*, 887 F.3d 736, 742 (7th Cir. 2016) (applying *Rooker-Feldman* to interlocutory order); *Carpenter v. PNC Bank Nat'l Ass'n, 633 Fed. App'x 346 (7th Cir. 2016)* (non-citable under Seventh Circuit Rules, but holding that interlocutory order of foreclosure subject to *Rooker-Feldman*). Thus, at least in the Seventh Circuit, there is an opportunity for litigants to raise a *Rooker-Feldman* challenge to subject matter jurisdiction where a plaintiff's claim seeks redress for injuries caused by a state court's interlocutory order. However, the matter is far from settled, and one should be aware of contrary authority that exists even within the Seventh Circuit. *See, Kowalski v. Boliker*, 893 F.3d 987, 995 (7th Cir. 2018) (suggesting without deciding that *Rooker-Feldman* may not apply to interlocutory orders); *TruServ Corp. v. Flegles, Inc.*, 419 F.3d 584, 591 (7th Cir. 2005) (holding that *Rooker-Felman* did not apply to interlocutory order).

In *Kelley v. Med-1 Solutions, LLC*, 548 F.3d 600, 605 (7th Cir. 2008), the Court held that *Rooker-Feldman* barred a claim under the FDCPA that an attorney made false misrepresentations in a state court lawsuit that it was entitled to recover attorneys' fees. In doing so, the court rejected plaintiffs' argument that the relief sought was "independent" from the state court judgment because it sought to remedy the defendant's representations and requests concerning attorney fees that preceded entry of the state court judgment. *Id*. The court explained that the plaintiffs' claims were inextricably intertwined with the state court's judgment, despite the fact that the allegedly unlawful actions occurred prior to that judgment, because "[w]e could not determine that defendants' representations ... related to attorney fees violated the law without determining that the state court erred by issuing judgments granting the attorney fees." *Id*.

Similarly, in *Crawford v. Countrywide Home Loans*, 647 F.3d 642, 646 (7th Cir. 2011), plaintiffs who were evicted from their home by sheriff deputies enforcing a state court foreclosure judgment brought suit against the mortgagee, the mortgagee's foreclosure suit counsel, and other defendants alleging that the foreclosure and eviction deprived them of fundamental fairness and equal protection rights. The Court held that plaintiffs' claim was subject to *Rooker-Feldman's* jurisdictional bar because the claim was an impermissible challenge to the state court mortgage foreclosure judgment, and to grant plaintiffs the relief they sought would have required reversal of that judgment. *Crawford*, 647 F.3d at 646-47.

Likewise, in *Taylor v. Federal Mortgage Association*, 374 F.3d 529, 531-32 (7th Cir. 2004), the Court upheld the dismissal of the plaintiff's federal claims against an attorney and others arising out of a state eviction proceeding that the plaintiff claimed was fraudulent. The plaintiff's allegations of civil rights violations arising from the foreclosure proceeding were dismissed because the district court found that the two claims were inextricably linked based upon the plaintiff's injury having been caused by the foreclosure action, not the conduct of the defendants, and that the plaintiff had a reasonable opportunity to be heard in the state court prior to the foreclosure. *Taylor*, 374 F.3d at 532. In upholding the district court's dismissal, the Court found that the injury for which the plaintiff sought recovery did not arise until the foreclosure judgment, and therefore, the two cases were inextricably linked. *Id*. at 534.

It should be noted, however, that not every claim against a lawyer in federal court following a favorable result in state court is barred by the *Rooker-Feldman* doctrine. In *Long v. Shorebank Dev-Corp.*, 182 F.3d 548, 559 (7th Cir. 1999), the Seventh Circuit held that *Rooker-Feldman* did not apply to plaintiff's federal claim for money damages under the FDCPA because the plaintiff was "effectively precluded" from raising her federal claims in an eviction proceeding for unpaid rent previously brought in state court. In that state court proceeding, the defendants had sought to evict the plaintiff in a forcible entry and detainer action. The

***PLDQ*'s Winter 2019 Issue**

We encourage member submission of articles pertinent to professional liability claims administration, defense trial advocacy, or professional liability substantive law. The manuscript deadline for the next issue is:

February 1, 2019

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Seven Circuit determines that plaintiff's claim for damages under the FDCPA would not have been considered "germane" to the forcible entry and detainer action and could not have been presented in that state court. Id at 559-60. The Court explained that plaintiff's alleged injury in her federal FDCPA suit alleging misrepresentation in an attempt to collect a debt was independent of the state court judgment because the defendant could have succeeded in its fraudulent attempt to collect rent from the plaintiff without going through the state court proceedings and obtaining a judgment against her.

Similarly, in *Buford v. Palisadeo Collection, LLC,* 552 F.Supp.2d 800, 803 (N.D. Ill. 2008), consumers filed an action under the FDCPA alleging that a collection agency and law firm violated the statute by attempting to collect time-barred cellular phone service debts in state court. Following *Long,* the court held that *Rooker-Feldman* did not bar this claim because plaintiffs' alleged injuries were "independent of and complete" before entry of the state court judgment. Id. at 805. Specifically, the court concluded:

> Defendants' alleged FDCPA violation occurred when they filed the state court action… past the statutorily allowed two-year period. Defendants' alleged FDCP violation-filing and prosecution of time-barred debts was necessarily accomplished before the entry of the judgments months later in February 2007.

Likewise, in *Dexter v. Tran*, 654 F.Supp.2d 1253, 1259-1260 (E.D. Wash, 2009) the Court held that the doctrine did not apply because the plaintiff was not seeking to overturn the state court's judgment or challenging what the state court did, but rather seeking recovery from the defendant for bringing the state court case in the first instance. The Ninth Circuit in *Noel v. Hall*, 341 F.3d 1148, 1164 (9th Cir. 2003) summarized this distinction as follows:

> [i]f a federal plaintiff asserts as a legal wrong an allegedly erroneous decision by a state court, and seeks relief from a state court judgment based on that decision, *Rooker-Feldman* bars subject matter jurisdiction in federal district court. If, on the other hand, a federal plaintiff asserts as a legal wrong an allegedly illegal act or omission by an adverse party, *Rooker-Feldman* does not bar jurisdiction.

Use of *res judicata* in conjunction with a motion to dismiss under *Rooker-Feldman*.

Given the limitations of the *Rooker-Feldman* doctrine, counsel representing attorneys in FDCPA suits and other federal statutory matters arising out of the entry of state court judgments, should also argue for application of claim preclusion, or *res judicata*. Under 28 U.S.C. § 1738, a federal court must apply the *res judicata* law of the state in which the judgment was entered. *Migra v. Warren City Sch. Dist. Bd. Of Educ.*, 465 U.S. 75, 81 (1984). Most states, like Illinois, require three elements for *res judicata* to apply: (1) identity of parties and their privies in the two suits; (2) identity of cause of action in the prior and current suit; and (3) a final judgment on the merits in the prior suit. *4901 Corporation v. Town of Cicero*, 220 F.3d 522, 529 (7th Cir. 2000). Other states may require additional elements. In Washington state, for example, there are four elements for claim preclusion to apply. There must be: (1) the same subject matter, (2) the same cause of action, (3) the same persons and parties, and (4) the quality of the parties. *Energy Northwest v. Hartje, 148 Wash. App. 454, 464 (2009)*.

The purpose of *res judicata* is to promote judicial economy by requiring the parties to litigate, in one case, all rights arising out of the same set of operative facts. *Chicago Title Land Trust Co. v. Potash Corp.*, 664 F.3d 1075, 1079 (7th Cir. 2011). A court may dismiss a matter based on *res judicata* pursuant to Rule 12(b)(6) where the facts establishing the defense are definitively ascertainable from the allegations of the complaint, the documents incorporated therein, matters of public record, and other matters subject to judicial notice. *U.S. Bank v. JKM Mundelein, LLC*, 2015 U.S. Dist. LEXIS 61619, * 8 (N.D. Ill.).

Taking the basic elements of *res judicata* in turn, it has often been held that there is an identity between a party and its counsel for the purposes of *res judicata. See, Henry v. Farmer City State Bank*, 808 F.2d 1228, 1235, n. 6 (7th Cir. 1986) (holding that a bank and the attorneys it hired to pursue a mortgage foreclosure judgment were in privity for purposes of *res judicata*); *Langone v. Schad, Diamond and Shedden, P.C.*, 406 Ill.App.3d 820, 832, 943 N.E.2d 673 (1st Dist. 2010) (attorneys are in privity with clients for purposes of *res judicata*).

As to the second element, *res judicata* precludes not only claims that were brought in a prior action, but those that *could have been brought* as well. *4901 Cor-*

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poration, 220 F.3d at 530 (emphasis added). According to the Illinois Supreme Court, causes of action are identical "if they arise from a single group of operative facts, regardless of whether they assert different theories of relief." *Id*; *citing, River Park, Inc. v. City of Highland Park*, 184 Ill.2d 290, 311 (1998). Further, "[f]or purposes of determining the *res judicata* effect of a judgment, a 'cause of action' is not limited to those issues that were or might have been offered to sustain the claim; it is also deemed to comprise all defenses that were or might have been offered." *Henry*, 808 F.2d at 1233. As the Seventh Circuit stated in *Henry*:

> *[R]es judicata* bars a party from subsequently raising claims based on facts which could have constituted a defense or counterclaim to a prior proceeding if the successful prosecution of the second action would nullify the initial judgment or would impair rights established in the initial action. *Henry*, 808 F.2d at 1232.

As for the third element, a judgment is deemed final for purposes of *res judicata* if it terminates litigation on the merits so that the only issue remaining is proceeding with its execution. *SDS Partners, Inc. v. Cramer*, 305 Ill. App. 3d 893, 896 (4th Dist. 1999). Often state court collection suits result in an entry of a default judgment in favor of the creditor.

In *Byrd v. Homecomings Financial Network*, 407 F.Supp.2d 937, 945 (N.D. Ill. 2005) the Court applied *res judicata* to bar a plaintiff's claim that the company servicing her mortgage violated the FDCPA by declaring her in default on her mortgage, pursuing foreclosure proceedings, and obtaining a judgment resulting in the sale of her property. The Court held that the FDCPA claim involved the same transaction as the foreclosure suit because the basis for the FDCPA claim was the lender's attempt to recover money owed on plaintiff's mortgage through the foreclosure suit itself. *Id*. The court distinguished the case before it from others where *res judicata* was held not to apply because the FDCPA claim was not based upon the state court proceeding to attach the debt, but rather, involved efforts at debt collection that occurred *before* suit was filed. *Id*.

Conclusion.

While *Exxon Mobil* did narrow the application of *Rooker-Feldman*, the doctrine is not dead when it comes to suits against attorneys in federal court for violation of federal statutes such as the FDCPA. The Seventh Circuit has repeatedly recognized that "even federal claims that were not raised in state court, or that do not on this face require review of a state court's decision, may still be subject to *Rooker-Feldman* if these claims are "inextricably intertwined" with a state court judgment." *Jakupovic v. Cunan,* 850 F.3d 898, 902 (7th Cir. 2017). While the concept of "inextricably intertwined" has been described as a "somewhat metaphysical one," ultimately the determination hinges upon whether the federal claim alleges: (1) injury that was <u>caused</u> by the state court judgment and (2) the plaintiff had a reasonable opportunity to raise the issue in the state court proceedings. Practitioners should also evaluate the applicability of claim preclusion or *res judicata* (or the related doctrine of issue preclusion or collected estoppel) in connection with making a *Rooker-Feldman* argument. Both doctrines may apply, but even if *Rooker-Feldman* does not, *res judicata* may be available as a defense. *See, e.g., Dexter*, 654 F. Supp.2d at 1261-62 (holding that *res judicata* barred plaintiff's claim even though *Rooker-Feldman* was inapplicable).

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PLDF AND DIVERSITY

The Professional Liability Defense Federation supports diversity in our member recruitment efforts, in our committee and association leadership positions, and in the choices of counsel, expert witnesses and mediators involved in professional liability claims.

PRESIDENT'S MESSAGE CONT'D

again thank **Chris Jensen** for her tireless service, vision and leadership since the inception of PLDF. In December, Chris will be transitioning from Managing Director of PLDF to managing the grandchildren (and occasionally Tom). Chris will be missed in the organization's day-to-day operations, but her new role promises to be more rewarding. We look forward to working with **Sandra Wulf** and **Sara Decatoire** of PIVOT Professionals.

I also want to thank the Board members whose terms recently ended. The dedication and services of **Chris Block (Marshall, Dennehey)**, **Mark Gende (Sweeny, Wingate & Barrow)** and **Walter Price (Huie, Fernambucq & Stewart, LLP)** were instrumental to PLDF's growth over the past few years.

We now move to the exciting year ahead. First of all, I want to welcome our five new Board members – **Kiera Goral (QBE)**, **Molly Eiden (Minnesota Lawyers Mutual Insurance Company)**, **Peter Biging (Goldberg Segalla)**, **Dan Church (Morrow Willnauer Church, LLC)** and **Glen Olson (Long & Levit)**. Congratulations are also in order for our newly elected officers - President-Elect: **Lisa Tulk (Kessler Collins, PC)**, Treasurer: **Pat Eckler (Pretzel & Stouffer)**, and Secretary: **Andrew Jones (Furman Kornfield & Brennan, LLP)**.

We are working on several exciting ideas for the coming year that includes additional member benefits and marketing opportunities. For starters, be on the lookout for webinars and new Quarterly contributions, including spotlights on Women in the Profession and a Wellness column.

In the spirit of the "New Year," I want to recommend the following "resolutions" for all members:

1) Make plans NOW to attend the 2019 Annual Meeting in Chicago (September 25th – 27th). The Annual Meeting also provides great marketing opportunities for your firm/company. Please keep this in mind when preparing your 2019 budgets.

2) Spread the word about PLDF to your co-workers, colleagues, and other acquaintances in the profession. Our website makes it easy to join. Remember, membership is FREE for industry professionals.

3) Join and become involved in PLDF practice committees and the Young Professionals committee.

4) Submit an article for the PLDF Quarterly. This is a golden opportunity to gain direct exposure throughout the professional liability industry.

5) Begin preparing to submit a program proposal for the 2019 Annual Meeting. We will be looking for panels that include attorneys and industry members.

6) Think PLDF for assignments and referrals. You can search members by state on our website.

7) Provide feedback. Please contact me, other Board members or your committee leaders with any ideas and/or recommendations you have for the organization. We have received great feedback since the Annual Meeting. Keep it coming.

I look forward to a great new year ahead for PLDF and all members. I wish everyone Happy Holidays!

At the Welcome Reception of the Annual Meeting in New Orleans.

Dinner at Pigeon & Prince at the Annual Meeting in New Orleans

PLDF COMMITTEES

PLDF's nine substantive committees include:

- **Healthcare**
- **LPL**
- **Young Professionals**
- **Financial Professionals**
- **Management & Executive Liability**
- **Insurance Producer**
- **Real Estate Design/Agents**
- **Employment Practices**
- **Miscellaneous PL & Cyber**

ARCHITECTS AND ENGINEERS LIMITATION OF LIABILITY CLAUSES, BY GLEN R. OLSON AND JONATHAN RIZZARDI.

Introduction

Contracts for architectural and engineering services often contain provisions limiting or precluding the professional's liability for certain categories of damages. For engineering and design professionals, these clauses can be sound risk management tools helping to avoid exposure, in particular, to a client's claimed consequential damages. These provisions (referred in some instances as exculpatory clauses and in other instances as limitation of liability provisions), can take several different forms. The design or engineering professional may seek a waiver of such damage claims entirely (which may reciprocal as between clients and the professional), or a liquidated damage provision may be chosen, sometimes limited to the amount of the professional fees charged.

While these can be beneficial risk management provisions, they are on occasion challenged by clients and other parties. As discussed below, the courts have generally held these clauses enforceable against a number of challenges seeking to inviolate them or limit their application. There are exceptions, however, particularly in the area of gross negligence/willful conduct and the application of statutes that preclude professionals from avoiding exposure to certain types of claims in the design and construction defect arena.

Attorneys advising professionals on whether and how to draft these clauses need to carefully review the statutes and common law of their jurisdictions. On occasion, the principles that will be applied to the issue of enforcement come from outside the design and engineering world and address the general topic of adhesion contracts. We survey below some of the different approaches courts have taken on these issues. This is not an exhaustive list of all jurisdictions addressing these clauses but an attempt to highlight some of the varying approaches taken by the courts. We begin with an exception to the general rule of enforceability, with an Alaska decision that refused to enforce such a clause.

Some Differing Approaches to Enforceability

<u>Alaska</u>

Alaska takes an extremely restrictive approach toward limitation of liability clauses, generally interpreting them as void pursuant to Alaska's anti-indemnity statute.

The case of *City of Dillingham v. CH2M Hill Northwest* (1994) 873 P.2d 1271 arose out of the construction of an Environmental Protection Agency ("EPA") sewage treatment facility plant in Dillingham, Alaska. The EPA solicited proposals form engineering firms to prepare plans for the facility, and CH2M submitted a proposal and was selected.

CH2M's proposed agreement for engineering services contained the following limitation of liability clause:

> That, the OWNER agrees to limit the ENGINEER'S liability to the OWNER and to all construction Contractors, Subcontractors, material suppliers, and all others associated with the PROJECT, due to the ENGINEER'S sole negligent acts, errors, or omissions, such that the total aggregate liability of the ENGINEER to all those named shall not exceed Fifty Thousand Dollars ($50,000) or the ENGINEER'S total compensation for services rendered on the portion(s) of the PROJECT resulting in the negligent acts, errors, or omissions, whichever is greater. *Id*. at 1272-73.

The City executed the agreement, without consulting with legal counsel.

During construction of the project, the contractor discovered site conditions which differed from CH2M's plans, the contractor sued the City for increased costs, and the City in turn cross-complained against CH2M for breach of contract. *Id*. at 1273. CH2M moved for partial summary judgment based on the limitation of liability clause. The trial court granted the motion, in part, ruling that the clause applied to breaches of contract and that Alaska Statute section 45.45.900, which dictates that construction contract indemnity agreements are generally void and unenforceable as against public policy, did not apply. The court ruled that the clause was not an agreement that indemnified the promisee (banned under section 45.45.900) but rather was an agreement which indemnified the promisor:

> The promisor is clearly the engineering firm here who's promising to do certain things for the City. The City is the beneficiary or the promisee of the contract, and 45.45.900 by its very language implies [sic] not to those circumstances. It applies clearly to the reverse circumstances and obviously the public policy behind this statute is exactly why it was worded as it was worded.
>
> The idea behind the statute is to not allow owners, who are often governmental entities, from inducing people to contract with them to provide construction

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ARCHITECTS AND ENGINEERS, CONT'D

> services and then have to sign away their right to go after the owner—usually the government—for negligence of that party. Obviously, it's to protect the contractors, it's not to protect the owners of the buildings or projects that are being built. *Id*. at 1273.

The Alaska Supreme Court then granted review to consider four questions: (1) does AS 45.45.900 ban indemnity agreements only when a state or local government is the project owner and indemnitee? (2) should a standardized contractual provision exculpating a party from its own "negligent acts, errors or omissions" be broadly construed to apply to knowing breaches of contract and breaches of fiduciary duty? (3) does AS 45.45.900 apply to reasonable limitation of liability clauses?, and (4) does AS 45.45.900 apply only when the party invoking a particular clause is seeking indemnity? *Id*.

As to the first question, the Court found that there was no indication from the language that the statute was "intended to ban only indemnification clauses that would benefit a public promise at the expense of a private promisor." Id. at 1274. The Court recognized the legislative history indicating the "general goal was to provide remedies for 'all wronged persons.'" *Id*.

As to the second question, the Court concluded that "an exculpatory clause that limits liability for a party's 'negligent acts, errors, or omissions' should be construed to limit liability for 'negligent acts, errors, or omissions' only." *Id*. at 1275. The Court reasoned that negligent acts in the context of contract performance may be contract breaches, thus the clause applies to breaches of contract, but only insofar as the breaches are negligent. *Id*.

As to the third question, the Court rejected CH2M's attempts to "characterize" the legislature's intent and embraced strict constructionism, holding that that the absence of an exemption for limitation of liability clauses in the statutory language indicated the Legislature did not intend to allow an exemption. *Id*. at 1276.

Finally, as to the fourth question, the Court concluded that the statute applies to a clause that is questioned "regardless of whether indemnification has been sought." *Id*. at 1278. The Court noted that the statute expressly rendered "void and unenforceable" an indemnification clause that limits liability for a promisee's negligence; because the statute used the conjunctive "and" the statute was applicable when presented "in a hypothetical context such as this petition." *Id*.

The Court reversed the trial court's holding, determining that the statute applied to render the limitation of liability clause void and unenforceable. The *Dillingham* opinion very effectively lays out Alaska's strong stance against enforcement of limitation of liability clauses in construction-related contracts.

California

In *CAZA* Drilling (California), Inc. v. TEG Oil & Gas USA, Inc. 48 Cal. Rptr. 3d 271(2010), the California Courts of Appeal addressed a limitation of liability provision included in a standardized "Day Work Drilling Contract." The appellant, TEG, hired the respondent, CAZA Drilling, to drill an oil well Castaic, California. A few days after the drilling began a blowout occurred resulting in the death of a CAZA employee, injury to others and complete destruction of the drilling site.

TEG took the position that the blowout occurred due to CAZA's negligence in pulling out drilling equipment from the well hole too quickly, causing a fire, and then failing to close the blowout preventer after the fire began. After CAZA sued TEG for breach of contract and for recovery on an open book account, TEG cross-complained for breach of contract, negligence and negligence *per se*. CAZA obtained summary judgment based upon an exculpatory clause providing in essence that TEG was to "assume liability for damage to or destruction of [its] equipment…regardless of when or how such damage or destruction occurs," and that TEG was to "release [CAZA from] any liability for any such loss or damage." 48 Cal.Rptr. at 275-276. Further, the contract provided that neither party would be liable to the other for "special, and direct or consequential damages resulting from or arising out of the contract, including, without limitation, loss of profit or business interruption including loss or delay of production, however same may be caused."

CAZA argued in its motion that TEG and a related party, Sefton, were not at a disadvantage in negotiating these terms with CAZA and were equally knowledgeable concerning the vagaries of drilling for oil. CAZA also submitted a declaration that tended to show that there were many different contracts available that covered drilling services in addition to the Day Work Drilling Contract the parties chose. *Id.* at 277. CAZA relied primarily for its exculpatory clause argument upon a provision of the 2002 Day Work Drilling Contract that provided that the operator shall be solely responsible and assumes liability for all consequences of operations by both parties while on a day work basis, including results and all other risks or liabilities incurred in or incident to such operations. CAZA argued that that language was dispositive of its liability on the cross-complaint and the trial court agreed, granting the motion for summary judgment.

TEG's argued that there were a number of Califor-

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Please let us know of appeals in your jurisdictions implicating important professional liability issues that might have broad-based significance.

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nia decisions that limited a party's ability to protect itself from the consequences of negligent conduct. However, the Court of Appeal observed that the current state of the law was as set forth in the California Supreme Court decision in *Tunkl v. Regents of University of California*, 383 P.2d 441 (1963), and that TEG's argument -- that a party cannot limit its negligence liability for a duty it has undertaken to perform by contract -- did not represent the current state of the law in this area.

Tunkl addressed a California statute, Cal. Civil Code 1668, which provides that all contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud, or willful injury to the person or property of another, or violation of law, whether willful or negligent, are against public policy. The Supreme Court noted that an exculpatory clause relieving a party from the consequences of its own negligence could not be enforced *when the public interest was involved even if the conduct did not involve a violation of law*. The characteristics of such a public interest transaction are that: (1) the transaction concerns a business of a type generally thought suitable for public regulation; (2) the party seeking exculpation is engaged in performing a service of great importance to the public; (3) the party holds itself out as willing to perform this service for any member of the public who seeks it, (4) as a result of the essential nature of the service the party involving exculpation possesses a decisive advantage of bargaining strength against any member of the public, (5) in exercising the superior bargaining power the party confronts the public with a standardized adhesion contract of exculpation, lacking any provision whereby a purchaser may pay an additional reasonable fee and obtain protection against negligence and (6) as a result of the transaction the personal property of the purchaser of the property is placed under the control of the seller, subject to the risk of carelessness by the seller or its agents.

The *CAZA Drilling* court concluded that the above factors did not apply to the contract before it. First, CAZA did not hold itself out as performing services for the general public. Also, the fact that TEG found itself "backed into a corner" and needing to execute the contract resulted from TEG's failure to plan ahead, leaving it with no choice but to deal with the only company that had a suitable drill rig available.

TEG then pointed to numerous statutes it claimed that CAZA had violated which would implicate the exclusions in §1668; it argued that CAZA would be improperly excused from liability unless the exculpatory language was invalided. The Court distinguished a number of cases cited by TEG on the basis that they involved consumer contracts and personal injuries. In contrast to those decisions, the CAZA – TEG contract involved economic loss to one of the parties. Ultimately the court concluded that the appellants had failed to set forth a specific statute or regulation that was purportedly violated, and the clause was enforced. 48 Cal.Rptr. at at 291.

Florida

The Florida decision in *Witt v. La Gorce Country Club, Inc.* (Fla. 3d Dist. 2010) 35 So.3d 1033 illustrates another interesting exculpatory clause limitation. In 1999-2000, LaGorce Country Club began exploring options to irrigate its golf course using a reverse osmosis water treatment system as an alternative to use of the municipal water supply. LaGorce met with ITT Industries regarding the project and ITT introduced the Club to Witt, a professional geologist licensed in Florida. ITT informed LaGorce that it had previously worked with Witt on another reverse osmosis project.

After Witt then submitted a proposal to supply hydrogeologic consulting services and ITT submitted a proposal to design and build a reverse osmosis water treatment plant, LaGorce and ITT entered into a design build contract. At the same time, Witt's company entered into various contracts directly with LaGorce for consulting services and overall project coordination.

Throughout the design and construction of the project many problems arose including issues with water quality and the operability of the water treatment system. While the system was ultimately delivered to the club it later deteriorated and ultimately failed. LaGorce sued Witt, Witt's company and ITT, a judgment in excess of $4 million resulted.

One issue raised by the judgment was the determination that Witt was personally liable for professional negligence outside the scope of a limitation of liability clause. On that issue, the trial judge concluded that the damage limitation was not applicable to Witt's liability for malpractice because he was not a party to the agreements. The Court of Appeal also questioned whether a professional, such as a lawyer, could legally and ethically limit a client's remedies by contract in the same way that a manufacturer could it a purely commercial setting. *Id.* at 1037 citing *Moransais v. Heathman,* 744 So.2d 973 (Fla. 1999). The Court also observed that Florida law recognizes a cause of action against an individual professional geologist for professional negligence irrespective of whether the geologist practices through a corporation. Section 492.111 of Florida statutes (2005) provides that an officer, agent or employee of a corporation shall be personally liable and accountable only for negligent acts, wrongful acts, or misconduct committed by her or him or committed by any person under her or his direct supervision and control while rendering professional services on behalf

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of the corporation. Witt argued that, although he could be liable for professional negligence, any such liability was capped by the agreements' limitation of liability provisions as to the reverse osmosis project.

The Court of Appeal noted, however, that the Florida Supreme Court concluded that the economic loss rule does not bar a cause of action against a professional for his or her negligence even though the damages are purely economic in nature and the aggrieved party has entered into a contract with the professional's employer. The Court noted that in cases in which the individual professionals provide services public policy dictates that liability is not limited by the terms of the contract. *Id.* at 1039 citing *Indemnity Insurance Co. of North America v. American Aviation, Inc.*, 891 So.2d 532, 536 (Fla. 2004). Therefore, the Court affirmed the judgment entered as to Witt individually.

<u>Montana</u>

In *Zirkelbach Construction, Inc. v. DOWL, LLC* (2017) 389 Mont. 8, the Supreme Court of Montana recently upheld the validity of a contract provision in a professional services agreement between a general contractor and a designer in which the parties waived consequential damages against each other and limited liability of the designer to $50,000.00.

The case arose out of the construction of a FedEx Ground facility in Billings, Montana. General contractor Zirkelbach Construction ("Zirkelbach") and DOWL, LLC, an engineering firm, each presented their own draft form contracts, but ultimately the parties agreed upon and signed DOWL's contract. The agreement provided for Zirkelback to pay DOWL approximately $123,000 for design services. Due to additional services rendered, DOWL's fees ultimately escalated to approximately $665,000 following the execution of several addenda to the Agreement. *Id*. at 9.

The original Agreement between Zirkelbach and DOWL contained a limitation of liability clause in which the parties agreed to mutually waive "any and all claims for or entitlement to special, incidental, indirect, or consequential damages arising out of, or resulting from, or in any way related to the Project." They further agreed that DOWL's liability to Zirkelbach under the Agreement "shall be limited to $50,000." *Id*. at 9-10.

Zirkelbach filed suit against DOWL, alleging it incurred $1,218,197.93 resolving problems caused by DOWL's allegedly negligent design plans. DOWL filed a motion for partial summary judgment citing the contractual damages limitation of $50,000. The District Court granted DOWL's motion and Zirkelbach appealed. *Id*. at 10.

On appeal, Zirkelbach argued that the limitation of liability clause was unenforceable as against public policy under Section 28-2-702, of the Montana Code, which provides:

> All contracts that have for their object, directly or indirectly, to exempt anyone from responsibility for the person's own fraud, for willful injury to the person or property of another, or for violation of law, whether willful or negligent, are against the policy of the law.

The Supreme Court rejected the above argument, holding that the limitation of liability clause was valid. The Court noted the sophistication and equal bargaining power of the two business entities, and emphasized the "fundamental tenet of modern contract law is freedom of contract; parties are free to mutually agree to terms governing their private conduct as long as those terms do not conflict with public laws." *Id*. at 11 citing *Winter v. State Farm Mut. Auto. Ins. Co.* (2014) 375 Mont. 351. The Court also cited a virtually identical California statute regarding limitation of liability clauses, in reaching the conclusion that "it would be difficult to imagine a situation where a contract between relatively equal business entitles would be able to meet the required characteristics of a transaction that implicated public interest." *Id*. at 13.

The Court made the additional observation that the limitation of liability clause only limited damages; it did not exempt DOWL from <u>all</u> liability under the Agreement. This was an important consideration as the Court had previously held, in *Keeney Const. v. James Talcott Const. Co., Inc.* (2002) 309 Mont. 226, that section 28-2-702, is not violated when business entities contractually limit liability, so long as they do not eliminate liability altogether. *Id*. at 12.

Finally, the Court rejected Zirkelbach's argument that the limitation of liability clause was an indirect exculpatory clause because the $50,000 amount was nominal in comparison to DOWL's total fee of $665,000. The court found, however, that at the time the parties entered into the contract – originally valued at approximately $123,000 – the $50,000 limitation of liability represented approximately 40% of the contract price. The Court concluded it was "unwilling to allow Zirkelbach to avoid a term of the contract simply because it [had] become more burdensome due to its own failure to renegotiate." *Id*. at 13. This is an interesting holding in that the Court appeared to impose an informal obligation to renegotiate the limitation of liability in conjunction with any contract amendments, lest the non-negotiating party suffer the consequences.

<u>New York</u>

In *Sear-Brown Group v. Jay Builders, Inc.* , 244

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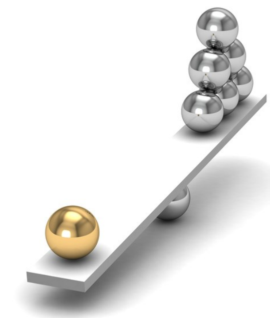
A.D.2d 966, 665 N.Y.S.2d 162 (1997) the Appellate Division of the Supreme Court, Fourth Department in New York addressed an engineering firm's suit against a real estate developer for engineering service fees owing on a residential construction projects. The developer counter-claimed for $1 million alleging negligence and gross negligence against the engineers. The Supreme Court granted summary judgment for the engineering firm limiting its liability on the counterclaims to $304,660 and denied the developer's motion for summary judgment. On appeal, the Appellate Division held that the limitation of liability clause in the engineering firm's contracts did not apply to the counterclaims for negligent misrepresentation and gross negligence, and that there were genuine issues of fact as to whether: (1) the developer justifiably relied upon the firm's pre-contractual representations, and (2) the firm's conduct rose to the level of gross negligence. The Court therefore modified the judgment and, as modified, affirmed it.

Sear-Brown sued Jay Builders, Inc. alleging negligence and gross negligence with respect to Jay's contractual duties on the Stoney Point Landing residential project. On cross motions for summary judgment the engineer's liability was limited to $304,660, the amount it had billed pursuant to the limitation of liability clauses of its contracts.

Jay argued that the trial court erred in granting the motion because limitation of liability clauses are void and unenforceable pursuant to New York's General Obligations Law. However, the Court noted that the General Obligations Law only applies where a party seeks to protect itself from claims for personal injury and physical damage to property. Because in the case before it, Jay was seeking damages solely for economic loss, the clause was in principle enforceable. However, the Court concluded that the clause was not effective as to Jay's counterclaims for negligent misrepresentation and gross negligence absent language included in the agreements to the contrary. 244 A.D.2d at 966-967. Remand was necessary, however, because there were factual issues as to whether Sear-Brown's conduct in fact constituted gross negligence.

<u>South Dakota</u>

The issue of the enforceability of an exculpatory clause was recently reviewed by the Supreme Court of South Dakota in *Domson, Inc. v. Kadrmas Lee & Jackson, Inc. and Dakota Engineering, LLC* (May 21, 2018) 2018 WL 4502292. Domson sued Dakota and Kadrmas Lee & Jackson (KLJ) for professional negligence. Dakota and KLJ asserted that a clause in the contract between Domson and its client, the Oglala Sioux Tribe, insulated them from liability for negligence. The trial court ruled for Dakota and KLJ and after receiving supplemental briefing from the parties as to the enforceability of exculpatory clauses, The Supreme Court of South Dakota affirmed the judgment.



The Tribe hired Dakota and KLJ to design a road reconstruction project on the Pine Ridge Indian Reservation. It was unclear whether Dakota or KLJ prepared the bid documents including the project manual, but Domson submitted a bid and was the apparent low bidder. On July 5, 2012 Domson and the Tribe then entered into a contract for the project with Dakota/KLJ designated the "engineer" and the Tribe's representative.

There appears to have been no dispute that Domson did not substantially complete the project in the time required under the contract and KLJ, as the Tribe's representative, assessed Domson $103,950 in liquidated damages. In January 2015, Domson then brought suit against Dakota and KLJ alleging professional negligence including a failure to reasonably draft, interpret and apply the project's contracted documents, seeking in excess of $1.1 million in damages.

The contract entered into between the Tribe and Domson provided that:

> Neither engineer's authority or responsibility under this Article 9 or under any other provision of the contract documents nor any decision made by engineer in good faith either to exercise or not exercise such authority or responsibility or the undertaking, exercise, or performance of any authority or responsibility by engineer shall create, impose, or give rise to any duty in contract, tort, or otherwise owed by engineer to contractor, or any subcontractor, any supplier, any other individual or entity, or to any surety for or employee or agent of any of them.

The trial court interpreted paragraph 9.09 as insulating KLJ from liability to Domson for negligence, absent a claim that KLJ acted in bad faith. On appeal, Domson argued that the exculpatory clause was a prohibited indemnity provision and was also against the policy of the law against enforceability of an engineer's exculpatory clause. For that proposition, Domson cited *Lyndon Property Insurance Co. v. Duke Levy & Associates,* 475 F.3d 268 (5th Cir. 2007). The Supreme Court noted that while the South Dakota statutes mandated responsibility for injury caused by

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willful acts or want of ordinary skill, nothing in the statute prohibited one party from agreeing by contract to release a third party from liability for ordinary negligence. *Lyndon* was in turn distinguishable because in that case the public entity had attempted to bargain away the engineer's potential liability to a surety that would step in the entity's shoes under the doctrine of equitable subrogation. 475 F.3d at 272. In contrast, Domson was not seeking to stand in the shoes of the Tribe in its suit against Dakota and KLJ.

The Supreme Court did caution, however, that it was not to say that every exculpatory clause insulating a third party from liability for negligence would be enforceable. In the case before it, paragraph 9.09 was valid and enforceable because Domson had not identified that this provision contravened sound public policy under the specific circumstances of the case. Moreover, because Domson had not presented facts to show that Dakota and KLJ's design and drafting fell below the professional standard of care the rules attended to unenforceability of exculpatory clauses for engineers and architects were not implicated.

Conclusion

As the above decisions illustrate, attorneys drafting contracts for design professionals and engineers should careful review the relationship between the parties, the nature of the services to be provided and the degree, the type of conduct (and potential damages) to be addressed by the limitation and the degree of limitation or exculpation that is being sought. Then, the law needs to be carefully reviewed for a particular state's approach to these provisions. The laws that may be relevant to the enforceability calculus can run the gamut from professional licensing and oversight regulations to decisional law regarding adhesion contracts.

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BRING THE CLAIMS PROFESSIONAL WITH YOU BY DON EODICE

Your client's interests may require the personal attendance of the claim professional at more than the just the trial.

In professional liability claims, issues of privilege and confidentiality tend to make the defense attorney the point person in the investigation. Defense counsel meets with the insured(s), contacts the witness(es), attends depositions, observes the plaintiff attorney in action and has knowledge of the venue. While bringing the claim professional into those discussions may unfavorably impact privilege, opportunities for the claim professional to gain necessary firsthand knowledge manifest throughout the litigation. Judges may require a representative of the company with adequate authority to be present at certain proceedings, but that is not enough. The claim professional needs to be present to hear and see the verbal and nonverbal interactions of the parties that you see. Relying just on reporting the recitations of what was said and how people presented themselves, no matter how comprehensive the report, can have an adverse impact for your client.

The Move Inside

In 1978, as a casualty road adjuster, I often met with insureds and claimants face to face. I even recall taking statements from claimants who were represented in their attorney's offices. These meetings provided an early opportunity to judge the credibility and likeability of both parties.

In the 1990's, many insurance carriers consolidated local claim offices into regional and national operations. Office location, cost restrictions, time out of the office, and other logistics have all contributed to the concept of desk adjusting. While the cost synergies of consolidation enabled carriers to remain afloat in a challenging market, the ability of the claim professional to assess the credibility of witnesses, insureds or claimants became limited to a review of documents, written reports and phone calls with defense counsel. Even when ordered by the court to attend litigation proceedingscorporate restrictions on travel often required retaining an independent adjuster to attend in their place. Direct contact responsibilities were affectively relegated to defense counsel and the occasional independent adjuster.

What We Lost

Not too long ago, I attended a mediation in the Federal Court for the Eastern District of Pennsylvania. The magistrate judge spoke to both sides in the court-

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room. I sat there thinking how redundant this will be, but, the plaintiff and my insureds, who were present, probably needed to hear this so I sat there patiently. What the judge said stunned me and has stuck with me for years.

After going over what mediation is all about, she then said, "The truth doesn't matter." Over my years in claims I never expected to hear it from a judge. She said, the manner in which the evidence is presented or refuted is all the jury will hear. Most cases that go to a jury do not have bright line, or "ah ha" evidence for either side. If the case had such evidence, a jury trial is unlikely. As such, evidence may or may not lead to the truth. She said that, without such certainty, the jury will tend look to other factors to help them decide the case. She then went into what, in her experience, is important to a jury.

She stated that a verdict is, in part, dependent on several things. If the jury likes the plaintiff more than they like the defendant, they will find a way to award for the plaintiff. If the jury believes the plaintiff was wronged and that wrong needs to be corrected and a message needs to be sent so it doesn't happen again, they will award larger sums for the plaintiff. Likewise, if they like the defendant more than the plaintiff; if they believe the plaintiff is taking advantage of the defendant; or if they believe the plaintiff is trying to "game" the system, they will award for the defendant.

She said if the jury can't decide who they like more, the plaintiff or the defendant, they will look to which attorney they like more. Which attorney is presenting the evidence in a more cohesive, believable manner. Which attorney "connects" with them more.

The point is that all of this is nonverbal. Even the jury's view of the evidence is dependent, in her view, on nonverbal ques. And yet, the claims professional possibly never met or spoke to anyone that the jury will hear.

How Physical Observations Impact the Evaluation of Exposure

While review of reports, documents and other evidence may be helpful to evaluate exposure, they nonetheless are only written words and fail to adequately communicate vital information about the parties. At least one study quoted in *Psychology Today*, determined that in many cases, only 7% of communication relies on actual words. (Jeff Thompson, Ph. D, 2011).

I saw the impact of how the nonverbal aspect of meeting the plaintiff can impact an evaluation when I was a claims supervisor. We had determined that voluntary mediation provided an opportunity for early resolution to a litigated, and sometimes non-litigated claim. Though our office was in New Jersey, my senior claim representative and I would arrange as many as 15 mediations to occur on a multi-day trip to Connecticut. One of the stipulations was that the plaintiff attorney would produce the plaintiff(s). We usually selected retired judges to mediate the cases. This was useful for both sides, especially where the plaintiff attorney had difficulty controlling the client and the would benefit from hearing the comments of the mediator. On one particular trip, we experienced the impact of meeting the plaintiff and the impact on evaluating the case.

One case involved a minor auto accident and a claim of soft tissue neck and back injuries. Evaluation the claim from the documents received, we had placed a fair range settlement value consistent with the history of cases in that venue with similar injuries. While outrageous demands and offers tend to a construct of which side of the table you are on, we were nonetheless surprised at the recalcitrance, of the usually reasonable plaintiff attorney, to negotiate anything less than a six figure settlement. The comments that the plaintiff made a very credible witness and truly suffered residual injuries were the usual jargon of these type of claims. In short, we heard that before. Both parties agreed to mediate the case prior to instituting litigation.

While my senior claim rep. and I were waiting for the mediator to finish talking to the plaintiffs in another case, we noticed a female waiting in the lobby. She drew our attention when we noticed that while she was talking to the receptionist and others, she had to turn her body instead of turning her neck. Was this an act? It didn't look like one to either of us. Our concerns grew. We watched her during the mediation and the behavior was completely consistent. After the plaintiff left the room with her attorney, the mediator, without any prompting from us, commented on the believability of the claimant's residual complaints. We agreed and got on the phone to the home office for additional authority.

In the second case, the complaints of soft tissue injuries were amplified by claims of lost earnings and loss of consortium. Still, we evaluated a fair range of settlement values consistent with the damages claimed. Then we met the plaintiffs and heard them related their case. This case was in litigation and we had discovered a job application completed by the injured plaintiff after the loss. Like most job applications, there was a question which essentially asked, do you have any physical limitations which would prevent you from performing the essential functions of the position with or without reasonable accommodations, to which she answered no. This was inconsistent with the claims of permanent disability re-

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strictions which were presented as damages. When asked about this and other inconsistencies, the plaintiff exploded. The behavior just clearly demonstrated the lack of credibility which was not in the documents. Our evaluation changed dramatically to a take it or leave it offer at the low end of a fair range, which later was accepted.

Seeing is Believing

To represent the best interests of your client, the defendant, the nonverbal expressions of the insured, the plaintiff, the plaintiff attorney, witnesses and even the judge need to be known by the claim professional. Any evaluation without how any party to the litigation will present to a jury risks an evaluation based on incomplete information. But, even your own personal observations will be filtered through you the prism of experience. Personal attendance by the claim professional is clearly a better option. I'm sure we've all seen judges react unfavorably to arguments from either party, witness antics at depositions, and reactions from opposing counsel which would make for good TV. These are all things the people with control of the litigation (consent clause notwithstanding) and the deep pockets usually do not see, but should see. I know from personal experience seeing a judge blow up on at attorney has a greater impact than reading a report that the judge didn't react well to the plaintiff attorney's argument. As noted earlier, seeing the claimant stiffly holding her back and neck while waiting for the mediation to begin, was far more informative than any report about her continuing disability.

In addition, the claim professionals may need to seek additional authority to settle the case. This usually comes from home office examiners, management, or even senior management. These people may or may not have been previously involved in the case. The dynamics of the mannerism with which the witnesses present themselves and the potential impact on the fair and reasonable settlement and evaluation of potential verdict values, needs to be related in an accurate, clear, concise manner. Like the kid's game of "telephone", the further removed from the firsthand experience of meeting and listening to the witness, the less likely that information will be presented in a way necessary to convince those with the authority to provide that authority. Just hearing that a witness may not be likeable or credible, may only appear as a line on a form to gain additional authority.

The Impact on Professional Liability Claims

With the defense counsel doing most, if not all of the investigation, the claim professional rarely meets with the insured, plaintiff, plaintiff attorney or any witnesses. In addition, there is often not a single event or "occurrence" where complained of behavior is demonstrated. More often it is a decision, policy or practice, often inherited in place possibly for years before the current administration, which allegedly manifested in disparate treatment, disparate result or other alleged wrongful outcome which leads to a claim. The predicate for the basis of decisions or the enforcement of policy and practice can be seen be pretextual or based on fair and impartial business needs.

This was demonstrated in a court ordered mediation I attended where the plaintiff felt usage of unpaid leave to go to Florida every over the Christmas season to warm ailing ankles in the sands on the beach was a legitimate usage of a benefit. The plaintiff viewed the new administrator's denial of unpaid leave and offer to purchase a heating pad, which could be used on the job, as discriminatory.

Who will make more sense to a jury? Who is more believable? Who is more likeable? Does the plaintiff need to be rescued? Was the plaintiff wronged and the jury needs to set it right? These things are difficult if not impossible to tell from documents in a file. Had I not attended it is highly unlikely I would have the full breath of the situation. In this case, while the plaintiff's mannerisms and the way in which he responded to questions clearly left much to be desired, neither would the new administrator's behavior likely not engender any favor from the jury.

Conversely, I have seen many cases where after speaking to the insured, defense counsel has contacted my staff told them to settle this case. Not only is the plaintiff's claim accurate, but the insured will not present well to a jury. Not even defense counsel believed or liked the insured. The insured may even anger the jury which potentially could inflate a verdict.

Conclusion: Attendance Matters

Surprises at any time in the litigation process can be disastrous. The claim professional needs to know how people will present. This will aide in obtaining adequate authority or deciding to defend the case. Personal experience is the best opportunity and chance of success.

Occasions to meet the plaintiff arise throughout the case. This can be at an early intervention, mediation (court ordered or voluntary), depositions, or some other legal proceeding. It is a case by case judgment call on if these should be attended by the claim professional as well as the defense counsel. Judgment should be used to determine if attendance of the claim professional is necessary when less significant testimony

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is being elicited. Also, attendance of the claim professional can be seen a sign of weakness or anxiousness in the negotiations. However, this may be offset by the firsthand experience to of being there. Remember, the claim professional may need to bring the experience back to the office to obtain additional authority or to secure authority to proceed to trial. Relating those firsthand experiences in such a presentation is more powerful and convincing than any presentation of documents or reports.

In representing the bests interests of your client, you must decide how to best communicate the mannerisms of the parties involved to the claim professional. Seeing is believing, and I would suggest it is the best way to make sure the claim professional understands what you are up against. How you suggest, strongly suggest or insist on personal attendance of the claim professional when will impact the result.

Don Eodice is the principal of **Eodice Consulting LLC** where he serves as an expert witness on bad faith and coverage litigation. Don may be reached at don@eodiceconsulting.com.

AN INSPIRATIONAL STORY ABOUT "GETTING BACK UP" BY ROD CATE AND JASON JOBE

If you have attended a PLDF Annual Meeting, I hope you have had an opportunity to meet and experience the positive vibes of one of our more remarkable members, Rod Cate. Rod is a partner at Hand Arendall Harrison Sale, LLC in Mobile, Alabama, where his practice focuses on the defense of medical malpractice and medical products liability claims. Rod is extremely accomplished in this field, even receiving the designation of "Best Lawyers in America" - Medical Malpractice Defense (2018).

Rod has overcome much more adversity than the average person to achieve his successes in life and law. Appropriately, Rod recently authored an inspirational book entitled, "Get Back Up." Based upon his experiences, the book is about overcoming adversity and limitations to meet your all around potential. I have personally read the book and cannot recommend it enough. Given Rod's ties to PLDF, I thought our members would be interested in hearing about his book. I recently caught up with Rod for the following candid Q&A:

Q. Rod, tell us about your book "Get Back Up."

A. It's a motivational memoir. When I was 15 years old, I suffered a broken neck playing high school football. The injury left me paralyzed from the neck down. In the blink of an eye, I went from athlete to quadriplegic. I was fortunate that I was able to walk again but still suffer significant paralysis. The book is about my journey. It is a deep dive in to what it's like to be paralyzed and what I go through on a daily basis. There are many humorous parts to the book, especially when I describe things that happen to me daily. I discuss what it's like to be a physical disabled lawyer. I talk about some of my jury trials and how wonderful life has been for me as a lawyer. Basically, the book is about overcoming adversity and not allowing sometime devastating life events ruin your quest for a great life.

Q. What motivated you to write "Get Back Up?"

A. I have a unique tale to tell. I'm pretty sure no one in the world has broken their neck playing football, overcome quadriplegia, been practicing as a lawyer for 26 years and along the way has lived such a fantastic life. I want to share what I've learned from my experience and hopefully motivate the readers to overcome their adversities on the way to live their best lives. We all

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face adversity. Some adversity is just a bit tougher to overcome than other.

Q. What have you learned from your experiences?

A. Well, the most important is to never quit, ever. We all have one life. I want to make mine the best as possible. I could have felt sorry for myself on so many occasions and just thrown in the towel. One thing the book discusses is how great life can be by just pushing forward. I have a great career, a great family, wonderful friends and have had some unbelievable experiences by just pushing forward and not letting my physical disability get in the way. You have to get to and turn the corner. You don't know for sure what's around the corner. Maybe it's something not so good. To me, it's worth the risk. I'm a big proponent of continually moving forward.

Q. How has your physical disability affected your practice of law?

A. Not at all as far as I know. The great thing about trying cases is there is not a lot of walking around. Typically, I go from counsel table to the podium to address the court, question witnesses or give opening statements and closing arguments to the jury. I do have to be somewhat careful to make sure I have a clear path because, especially in small courtrooms, boxes and cords can prove hazardous. Travel can be challenging. When I was a younger lawyer, I refused to jump in a wheelchair to be pushed from gate to gate. I was too prideful. As I have gotten older, I've learned to check my pride at the ticket counter along with my bags.

Q. What are your thoughts on the PLDF experience?

A. To me, the most important part of life is having great relationships. I've been in the PLDF now for 7 years or so. Through PLDF, I've developed great relationships that go far beyond just being colleagues. I've got friends in PLDF whom I communicate with regularly. The annual meeting is always a blast because it is a time when I can reconnect with other PLDF members that are true friends.

Q. Any parting shots?

A. Yes. I'm a proponent of living a passion-filled life. To me, it's being passionate about the small things in life that drives true happiness. Life doesn't have to be about how much money you make. Spending time with family and friends is my biggest passion. The routine parts of daily life drive true happiness. Having a great sandwich. Taking a great nap. Watching a great movie. There should be no such thing in life characterized as mundane. If there is, it's your own fault.

Rod's book can be purchased on Amazon or by visiting his website, rodcate.com. The book is available in paperback ($8.99) or for the Kindle ($5.99).

COVERAGE FOR CYBER ATTACKS CASE LAW UPDATE—AND HOW PROFESSIONAL LIABILITY COVERAGE MAY BE AFFECTED, BY MICHAEL D. HANDLER

Recent cases addressing insurance coverage for intrusive and expensive cyber breaches provide a glimpse into the current trends for insurers' defense and indemnification of professional-risk insureds. Professional industries of virtually every kind will continue to face electronic security challenges, from sophisticated point-of-payment cyberattacks to inexpensive social engineering "phishing' scams, as the related insurance coverage law continues to develop.

For example, in June 2018 the Fifth Circuit Court of Appeals, in *Spec's Family Partners, Ltd. v. Hanover Insurance Co.*, 739 Fed. App'x. 233 (5th Cir. 2018) permitted a "Directors, Officers and Corporate Liability" insured to seek defense cost reimbursements from its insurance carrier, for an underlying lawsuit regarding amounts the insured's credit card processor demanded after the insured's credit card network was hacked. Although this *Spec's Family Partners* opinion is "unreported", it is foreseeable that if a professional liability ("PL") insured held off on buying a specific cyber-insurance policy before it sustained losses from a cyberattack, the insured may attempt to point to *Spec's Family Partners* as a basis for arguing it should receive defense funding from its PL insurer based on underlying allegations that go beyond clearly-excluded conduct.

Why should this matter to all lawyers, not just "management liability defense" lawyers? Recall that lawyers are also insureds under their legal malpractice policies. Then consider the potential for first-party theft losses within an average law firm. The scenario could be as small as a scammer using a fake email address to impersonate a firm's senior member, who appears to be writing during an off-site cli-

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ent seminar needing gift cards for use in an alleged attendees' drawing. The email tricks a junior employee, who believes this is what their boss needs ASAP, into purchasing and activating the gift cards then emailing the "boss's account" a picture of each gift card's scratch code.

Consider also, the many larger ways that law firms are entrusted with their clients' financial interests. Hypothetically, a law firm's business practice group may handle property acquisitions for an existing client. The law firm may believe that its client's CEO has emailed a request for the law firm to wire money to an acquired business's bank account as a milestone payment, e.g. initial payment upon closing of the acquisition deal. The firm tries to be full-service for its clients, so it wires the money directly instead of dealing through an escrow agent. Two weeks after wiring the money, the firm learns from the client that the expected sale proceeds have *not* been received by the expected recipient. An investigation reveals that the email requesting the sale proceeds to be wired instead of sent by check, was "spoofed" (disguised) and fraudulent. The client then demands the money from the law firm. Was this an authorized or voluntary parting of the client's money to a third party? What if the law firm's footer contains a boilerplate disclaimer stating "We do not accept wiring instructions via email." What then is the impact on the availability of PL insurance coverage?

CGL Coverage Is Usually On the Sidelines, Unless It's an "Inside Job"

Commercial General Liability ("CGL") policies were often casually referred to as "comprehensive" liability policies, but those days are in the past. Insurance companies have offered specialized "cyber" or "data breach" policies for many years now, consistent with the belief that hacking incidents were unique risks for which insureds would benefit from standalone insurance coverage. For some CGL policies, insurers would reinforce these distinctions by using the ISO forms introduced in 2014 to state exclusions from CGL coverage for the access to or disclosure of confidential or personal information.

Case law has developed slowly on whether CGL policies remain non-triggered by hacking incidents. Since February 2014, when a New York trial court considered whether the CGL's "Personal and Advertising Injury" coverage was available for a widespread Sony PlayStation hacking (*Zurich Am. Ins. v. Sony Corp. of Am.*, 2014 WL 8382554, 2014 N.Y. Misc. LEXIS 5141 (N.Y. Sup. Ct. Feb. 21, 2014)), reported case law has only rarely addressed such CGL coverage issues. The Fourth Circuit Court of Appeals last addressed in 2016 a different set of facts from *Sony* and upheld a finding of coverage for "publication", where the insured allegedly posted patient records or otherwise made personal information such as the patients' Social Security numbers available on the internet. *Travelers Indem. Co. of Am. v. Portal Healthcare Sols., LLC*, 35 F.Supp.3d 765, 768 (E.D. Va. 2014), *aff'd*, 644 F. App'x. 245 (4th Cir. 2016).

It is even rarer for a single jurisdiction to weigh in twice within one year on these CGL coverage issues. But recently, the United States District Court for the Middle District of Florida twice concluded (applying South Carolina law in November 2017, then applying Florida law in September 2018) that no CGL coverage is available when an alleged hacking-incident's injuries did not result from the insured's business activities but rather from the actions of third parties. *Innovak Int'l, Inc. v. Hanover Ins. Co.*, 280 F.Supp.3d 1340 (M.D. Fla. 2017); *St. Paul Fire & Marine Ins. Co. v. Rosen Millennium, Inc.*, No. 17-00540, 2018 WL 4732718, 2018 U.S. Dist. LEXIS 173072 (M.D. Fla. 2018). For CGL coverage to apply, this federal court repeatedly held, the insured is required to be the publisher of the private information that was allegedly made publicly accessible. Florida is often regarded as an influential jurisdiction, so this court's opinions may point to an emerging general rule that CGL policies are not expected to respond to losses allegedly caused by third-party hackers. However, an appeal of the *Rosen Millennium* case denying CGL coverage under Florida law was taken to the 11th Circuit Court of Appeals on October 19, 2018.

Relief Requested For Hacking Incidents May Trigger Professional Liability Coverage, According To The Fifth Circuit

Issued in June 2018, the Fifth Circuit Court of Appeals' *Spec's Family Partners* opinion involved a corporation (a liquor store chain)'s losses arising from a long-term hacking of its credit card network. More specifically, the business's credit card processing company demanded millions of dollars to fund fines and reimbursements to card-issuing banks. It allegedly owed these amounts under its Merchant Agreement, and due to its noncompliance with Payment Card Industry (PCI) data security requirements.

The appeals court's conclusion that the management liability / Directors & Officers insurer was not excused from its duty to defend, turned on its interpretation of the PL policy's exclusion for claims arising from the insured's liability under a written or oral contract or agreement. This is an exclusion common to many liability policies, including CGL and PL policies. Despite the insurer's position that the contrac-

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tual liability exclusion applied to the Merchant Agreement, there was at least one claim that potentially fell within the scope of the PL insurance coverage. The demand letters to the insured could be viewed as containing allegations of negligent payment card industry data security violations, and as containing "demands for a type of non-monetary relief not contemplated by the Merchant Agreement."

This recent expansive interpretation of the PL insurer's duty to defend following a credit card hacking incident may motivate PL insureds (and insurers) to reexamine their coverages that may be available for when cyber-mistakes are made. This new opinion contrasts with another federal court's strict application in 2016 of a similar "contractual liability" exclusion, to limit a cyber security policy's duty to indemnify, in *P.F. Chang's China Bistro, Inc. v. Federal Ins. Co.*, 2016 WL 3055111 (D. Ariz. 2016). That case's data breach incident involved theft of 60,000 restaurant customers' credit card numbers. The insured's loss at issue was MasterCard's calculated Fraud Recovery Assessment, which included PCI violation charges. The *P.F. Chang's* court held that both the cybersecurity insurance policy's definition of "Loss" and two of its Exclusions would bar coverage for those contractual obligations that the insured assumed from a third party.

In 2016, the *P.F. Chang's* Court turned to cases analyzing CGL policies' exclusionary language for guidance, because it stated that cybersecurity insurance was relatively new to the market but the fundamental principles of these exclusions were the same across different types of policies. PCI contractual arrangements have also remained substantially consistent over the years, with banks, credit card companies and payment processors requiring agreed contractual arrangements and typically imposing repayment obligations on smaller players. Analogously, because "cloud" computing or service providers generally have more marketplace power than their users of various types and sizes, their cloud-service contracts can include "take it or leave it" indemnity terms whose parameters are difficult to fully anticipate at the time of contracting. Given this, *P.F. Chang's* strictly applying "contractual liability" exclusions (albeit in the strict duty-to-indemnify context) could potentially nullify significant components of the insurance coverage provided by the policies they appear in.

As professional service providers more commonly rely on an electronic transaction economy and on cloud computing, exclusionary provisions may require careful scrutiny within a PL policy, or within a specialized cyber-breach policy as demonstrated by *P.F. Chang's*, to determine which portions of these insureds' losses due to electronic hacking might not be covered. In a typical PL policy, the Definitions of Loss, Claim and Wrongful Act are provisions that can dictate the scope of coverage (and defense) afforded. Further, the PL scope of coverage can be subject to variations in definitions and throughout the policies that are not usually encountered within the standardized CGL coverage grant's "damages" because of property damage or bodily injury. Because PL policies' definitions are generally similar but rarely identical when issued by different insurance companies, these differences may influence a court's determination of which claims and/or categories of losses will obligate the PL insurer to defend.

Case Law On Commercial Crime Policies Is Addressing Social Engineering Fraud

As "social engineering" fraud becomes increasingly common and as unsuspecting employees' compliance with "spoofed" instructions continue to result in losses large and small, more cases nationwide have focused on the availability of insurance coverage under commercial crime policies for these incidents. Where crime policies' "Computer Fraud" coverage provisions generally cover "direct loss" that results from computer fraud, the majority rule and larger trends have continued to support that because computers are used in almost every business transaction, coverage is not provided for *all* monetary transfers that involve fraud. That would convert the insured's crime policy into a "general fraud" policy. *Pestmaster Servs., Inc. v. Travelers Cas. & Sur. Co.*, 2014 WL 3844627 (C.D. Cal. 2014).

In 2016, the Fifth Circuit Court of Appeals issued one of the commonly-cited cases finding no coverage based on the computer fraud provision of a commercial crime policy, based on the absence of a loss "directly" resulting from use of a computer and given the insured's failure to investigate phony wire transfer instructions apparently received from its vendor. *Apache Corp. v. Great American Ins. Co.,* 662 Fed.Appx. 252 (5th Cir. 2016) (applying Texas law). Among the more recent opinions debating what constitutes a "direct loss" from a theft aided by computer, the minority view was taken by the Second Circuit Court of Appeals, to favor "computer fraud" coverage for an accounts-payable employee's wire transfer to a fraudster's bank account based on an email allegedly altered to look like it came from a high-ranking company official. *Medidata Solutions, Inc. v. Federal Insurance Co.,* 268 F.Supp.3d 471 (2017), *aff'd*, 2018 WL 3339245 (2d Cir. July 6, 2018).

Two 2018 opinions in the Ninth Circuit are consistent with the general trend for courts to strictly apply computer-fraud provisions of a crime insurance policy. In April 2018, the Ninth Circuit Court of Appeals held that an employee's issuance of a $700,000 wire transfer to a hacker/spoofer's bank account was exclud-

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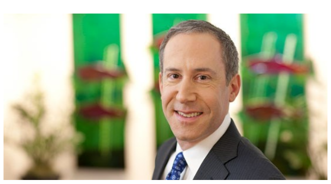
ed from coverage as an "authorized" access to the funds. *Aqua Star (USA) Corp. v. Travelers Cas. and Surety Co.*, 719 Fed.Appx. 701 (9th Cir. 2018). In August 2018, the U.S. District Court for the District of Nevada ruled that as a matter of law, an insured's investigation costs and amounts paid back to its customers (whose credit cards were used by the insured's employees for fraudulent charges) were not direct results of covered employee theft. *CP Food & Beverage, Inc. v. U.S. Fire Ins. Co.*, 2018 WL 3993408 (D. Nev. 2018). If "direct means direct" whenever "direct loss" is required for the application of computer fraud coverage, one possible lesson of this most-recent case is for insureds to obtain their coverage for external social engineering fraud by purchasing a social engineering fraud endorsement.

"Go Phish" – PL Insureds Might Seek Coverage There, If Deterred Elsewhere

Returning to the hypothetical scenario detailed in the first section above regarding PL coverage for wire transfers, different approaches taken in various jurisdictions on language appearing in multiple kinds of policies may make the insurance picture unpredictable. The "big picture" of where each policy fits into an insured's "web" of insurance potentially impacts where coverage may be found, because policyholders (and often, the courts) are reluctant to conclude there will be a non-covered gap in the "web" of insurance. Where there are case law trends to find no coverage for a third-party hacking incident under CGL and/or Crime policies, and where data breach coverages may be strictly bounded to their stated provisions as well, PL insureds may then attempt to seek coverage, or at least reimbursement for their defense costs, under their PL policies .



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THE PURPOSE AND LIMITATIONS OF THE PEER REVIEW PRIVILEGE, BY STUART T. O'NEAL AND NICOLE C. FREILER

All 50 states and the District of Columbia have some version of a peer review privilege. Although they all share the primary purpose of attempting to improve the quality and safety of patient care by encouraging the thorough and honest investigation of medical care and to evaluate ways to improve patient care overall, they differ in the scope of information protected. Most states' peer review privilege protects from discovery documents and information prepared by and/or specifically for a peer review committee or similar entity.

Illinois Courts, like others across the country, have explained that their peer review protection act protects documents that arise from the workings of peer review committees "which are an integral part, but not the result, of the peer-review process." *Toth v. Jensen*, 272 Ill. App. 3d 382, 385, 639 N.E.2d 484, 208 Ill. Dec. 428 (1995). Generally speaking, in Illinois and elsewhere, peer review protection acts protect documents created by or for, as well as the deliberations of, peer review committees, but not documents or information generated prior to the commencement of the peer review process or after the process ends. *Pietro v. Marriott Senior Living Services, Inc.*, 348 Ill. App. 541, 549, 810 N.E.2d 217, 284 Ill. Dec. 564 (2004). At least in Illinois, where documents are created "in the course of internal quality control for the purpose of reducing morbidity or mortality of for improving patient care", they are protected. *Mnookin v. Northwest Cmty. Hosp*., 2018 Ill. App. (1st) 171197-U, 2018 Ill. App. Unpub. LEXIS 948 (Jun. 8, 2018).

In recent years, courts across the country have been grappling with the boundaries of the peer review privilege and, in many instances, have limited peer review protections, creating a narrow evidentiary privilege that is often difficult to defend. The purpose of this article is to describe some of the limitations that have been recognized by Courts and provide proactive strategies for ensuring that peer review documents and information are protected.

A recent Pennsylvania Supreme Court decision is illustrative of this trend. In *Reginelli v. Boggs*, 181 A.3d 293 (2018), the Pennsylvania Supreme Court placed additional limits on the protection offered by Pennsylvania's Peer Review Protection Act ("PRPA"). At issue in *Reginelli*, was a file maintained by Dr. Brenda Walpher regarding Dr. Marcellus Boggs. *Id.* Both Dr. Walpher and Dr. Boggs were employees of UPMC Emergency Medicine, Incorporated (hereinafter referred to as ERMI). *Id*. ERMI, pursuant to a contract with Mongahela Valley Hospital (hereinafter referred to as MVH), provided staffing and administrative services for the MVH Emergency Department. *Id*. During the course of a medical malpractice action that was filed against

Dr. Boggs, both MVH and ERMI claimed that the PRPA's statutory evidentiary privilege protected from disclosure the performance evaluation file that was maintained by Dr. Walpher on Dr. Boggs. Id.

The Pennsylvania Supreme Court held that neither ERMI nor MVH could claim the PRPA evidentiary privilege. According to the Court, ERMI was not a "professional healthcare provider" as that term is defined by Pennsylvania's PRPA. *Id*. at 303. The PRPA defines professional healthcare providers as individuals or organizations who are "approved, licensed, or otherwise regulated to practice or operate in the healthcare field under the laws of the Commonwealth." Id. The Court also found that the performance file at issue was not generated or maintained by MVH's Peer Review Committee; instead, it was generated and maintained solely by Dr. Walpher. *Id*. Thus, the Court held, neither party could assert the privilege with regard to the file. *Id*.

The Court explained that ERMI, which it described as "a business entity that provides hospitals and other healthcare facilities, pursuant to contractual agreements, with staff involved with the provision of emergency medical services," did not fit within the PRPA's definition of "professional healthcare provider" *Id*. The Court explained that "no principled reading of the definition of professional healthcare provider permits any entity to qualify if it is not approved, licensed, or otherwise regulated to practice or operate in the healthcare field under the laws of Pennsylvania. As such, while ERMI is an organization that is comprised of hundreds of professional healthcare providers (namely, physicians), it is not itself a professional healthcare provider because it is unregulated and unlicensed." *Id*. The Pennsylvania Supreme Court concluded that "in the present case, ERMI does not qualify as a professional healthcare provider under the PRPA because it is not approved, licensed, or otherwise regulated to practice or operate in the healthcare field in Pennsylvania, and it did not become one because one of its employees (Dr. Walpher) conducted an evaluation of another of its employees (Dr. Boggs)." *Id*. at 303-304.

With regard to MVH, the Court explained that the PRPA's evidentiary privilege is reserved only for the proceedings and documents of a "review committee." *Id*. at 304. MVH, the Court noted, did not contend that Dr. Walpher was a member of the hospital's peer review committee, and the certified record contained no evidence to support such a finding. Id. The Court explained that "individuals conducting peer review are not defined as a review committee under the PRPA, even if they qualify as another type of review organization. As a result, we must conclude that Dr. Walpher, as an individual, was not a review committee engaging in peer review, and thus, MVH is not entitled to claim the PRPA's evidentiary privilege based upon her work as member of its medical staff." *Id*.

Finally, both ERMI and MVH claimed that a hospital's peer review committee may conduct protected peer review activities through an outside entity pursuant to a contract. Id. at 306. According to the parties, Dr. Walpher, on behalf of ERMI, conducted the review at the request of MVH pursuant to ERMI's contract with MVH. Id. The Court found that MVH and ERMI had failed to preserve this issue for appeal, noting that "for reasons of either strategy or oversight, neither MVH nor ERMI included the contract between them in the record in the trial court proceedings." *Id*. Because it was unable to review the contract between ERMI and MVH, the Court explained that there was no conclusive documentary evidence to establish one way or the other whether MVH contracted with ERMI to conduct peer review on its behalf. *Id.*

In 2000, the Appeals Court of Massachusetts addressed the issue of the application of their State's peer review privilege where peer review functions were performed by an outside consultant. *Grande v. Lahey Clinic Hosp.,* 49 Mass.App.Ct. 77. There, a physician brought a breach of contract action against the hospital and sought to depose the hospital's out-of-state consultant to its peer review committee. *Id*. Although she did not attend the hospital's peer review committee meetings, she did review various materials and records and prepare a report to the committee. *Id*.

The Court reviewed Massachusetts' peer review statute and found that the consultant's activities were privileged peer review activities because "the information she gathered, and her study of the records were all to the end of working up her report for the peer review committee." *Id*. at 80. The Court explained that "[h]ospitals would be discouraged from bringing in outside medical experts to assist in peer review if access to their testimony in connection with their consultative efforts stripped away the confidentiality of their consultative work and thereby the peer review proceedings. Of course, peer review committees could guarantee the confidentiality of the work of a consultant by having the consultant attend the meetings of the peer review committee when the case on which the consultant has assisted is discussed…" *Id*. at 80-81.

As more and more hospitals and other medical facilities are turning to outside entities and consultants to staff and operate various departments within their facilities, it is important that attorneys and their healthcare clients are aware of the limitations of the peer review privilege, and the impact that these outsourcing agreements may have on the application of the privilege. The key issues of which you and your clients should be cognizant are (1) private entities and consultants providing services to a hospital facility pursuant to contractual agreements, may not be considered "professional healthcare providers" for purposes of the peer review privilege; and (2) single individuals performing employee performance evaluations may not be considered "review committees" for purposes of the peer review privilege. However, with careful planning and thoughtful consideration of these limitations, their impact can be minimized and legitimate peer review activities can still be protected.

A necessary first step toward ensuring that peer review activities performed by employees of outside service providers are protected is to ensure that contracts with these outside entities and consultants are carefully drafted to ensure that peer review activities are protected. This may require revising or adding addendums to existing contracts. Contracts with any consultant or outside entity providing staffing and management services within the healthcare facility should explicitly reference peer review, including the identification of individuals from the entity who may be considered members of the peer review committee or who may be called upon to perform peer review activities. More specifically, contracts should state that the consultant or entity being retained by the healthcare facility will provide various services, including peer review activities, and that certain employees (identified by title or name) of the entity will, by operation of the contract itself, serve as members of the hospital's peer review committee. Contracts and relevant by-laws should be revised accordingly to ensure protection moving forward. Whenever possible, all members of the peer review committee, including consultants and employees of outside entities, should participate in peer review committee meetings.

Additionally, hospitals that want to protect employee performance evaluations must ensure that they are conducted in accordance with the hospital's peer review policy, and that the appropriate individuals are participating in those reviews. If employee performance evaluations are to be protected, they must be performed by the peer review committee itself, rather than by the employees' direct supervisor only. Reginelli makes it clear that, at least in Pennsylvania, employee performance evaluations completed by a single supervisory employee will not be protected. However, similar limitations are likely to be found in other states' whose Courts have limited the protection to documents and information generated exclusively for use by or in connection with a peer review committee.

From a litigation standpoint, once a matter has been brought to suit, attorneys must protect peer review documents by ensuring that, where appropriate and necessary to assert the privilege, copies of any relevant contracts are made a part of the record during discovery. Court's throughout the country routinely rely upon waiver to avoid answering difficult questions regarding, *inter alia*, the contours of evidentiary privileges. These contracts should, of course, first be redacted so as not to disclose any confidential or proprietary information. However, the contract must be produced and made a part of the record to preserve the argument that the contracted entity was contracted with to provide peer review services.

As courts continue to limit the protections afforded by the peer review privilege, it is more important than ever for hospitals and attorneys charged with defending them take a proactive approach to the protection of peer review materials. This requires a thoughtful and careful approach to peer review materials that begins long before a case is brought to suit.

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MALPRACTICE CLAIMS AGAINST ACCOUNTANTS WILL FAIL UNLESS SUPPORTED BY EXPERT TESTIMONY ON EVERY ESSENTIAL POINT,

BY PAUL BOYLAN

In *Rhode Island Resource Recovery Corporation v. Monacelli LLP,* 2018 WL 3244388, —A.3d— (July 3, 2018), the Supreme Court of Rhode Island reversed a $5.7 million jury verdict and judgment for accounting malpractice and ruled that the accused accounting firm was not liable. The evidence was insufficient because the plaintiff at trial did not show, by expert testimony, that the claimed losses were proximately caused by the negligence of the auditor and not by one or more other causes. Actual harm caused by the error must be proved to the jury, not assumed by it. The Opinion resolves, in favor of accounting professionals, a novel issue in Rhode Island law. It increases the protection of accountants and all professionals in all malpractice cases. This issue is an open question in many states. The Opinion supports argument that this increased protection should be required in other states.

A. This issue in other states.

The role of experts in proof of proximate causation in accounting malpractice is treated in a number of cases in other states, but is not discussed conceptually in any case yet identified. *See T.L. Wallace Construction, Inc. v. McArthur, Thames*, 2017 WL 2812952, 234 So.3d 312, 330 (Miss. 2017) (expert testimony used to prove proximate causation). *T.L. Wallace*, relying on Mississippi law, describes proximate cause in the context of accounting malpractice as proof that there was a "reasonable" connection between the act or omission and the damage. The jury must find that the negligence was the cause in fact and the legal (or proximate) cause of the damage. The defendant's negligence "need not be the sole cause of an injury," but must be a substantial factor in producing it; *American Mechanical Solutions, L.L.C. v. Northland Process*, 184 F. Supp.3d 1030, 1060-1063 (D. New Mex. 2016) (dicta; expert testimony is required as to causation in accounting malpractice; collecting prior cases as to accounting, law, medicine, and chiropractice; *Buke, LLC v. Cross Country Auto Sales, LLC*, 2014-NMCA 078; 331 P.3d at 955 (N. Mex. Ct. App. 2014) (expert testimony is required to prove accounting malpractice and all other forms of professional negligence cases); In *re CBI Holding Co., Inc.*, 419 B.R. 553, 569 (S.D.N.Y 2009) (discussed in more detail below; accounting malpractice; proximate causation of loss was successfully proved by an expert); *Star Broad. Inc. v. Reed Smith Ltd. Liab. P'ship*, 2009 WL 482833 (E.D.Va.2009) aff'd., 373 Fed. Appx. 407, 2010 WL 1474359 (dicta; under Virginia law expert testimony is usually required to establish proximate causation in all cases of medical, legal, and accounting malpractice affirming grant of summary judgment because expert reports and testimony in legal malpractice case failed to show proximate causation of loss); *Traveler's Cas. And Sur. Co. of America v. Ernst & Young LLP*, 542 F.3d 475, 492 (5th Cir. 2008) (expert testimony was successfully used to prove that plaintiff surety was reasonable to rely on financial information typically used by sureties, and that the incorrect information caused the loss to the surety); *Frank v. Lockwood*, 275 Neb. 735, 743, 749 N.W.2d 443, 451 (2008) (expert used successfully to prove malpractice by accountant as to filing of tax return); *Brown-Wilber, Inc. v. Copeland Buhl & Co.,* N.W.2d 209, 218 (Minn. 2007) construes, in the context of accounting malpractice, a state statute as to expert disclosure which requires that a plaintiff's expert show each element of accounting malpractice including facts showing that the departure from the standard of care was a direct cause of the plaintiff's injuries. The exact level of detail required in the pretrial expert disclosures is not specified; *Board of Trustees of Fire and Police Retiree Health Fund v. Towers, Perrin et al.*, 191 S.W.3d 185, 192 (Tex. Ct. App. 2005) (summary judgment for plaintiff was correctly denied in accounting malpractice action because the plaintiff did not establish proximate causation by use of expert testimony); *Greenstein, Logan & Co. v. Burgess Marketing, Inc.*, 744 S.W.2d 170, 184 (Ct. App. Tex. Waco, 1987) (the plaintiff must establish a causal connection between damages and the accountant's negligent conduct before he can recover; the jury question as to causation was properly framed and the jury award was affirmed because it was viewed as limited to damages the jury found to be proximately caused); *Vernon J. Rockler & Co., Inc. v. Glickman, Isenberg, Lurie & Co.*, 273 N.W.2d 647, 651 (Minn. 1978) (affirms a judgment for the accounting firm because the advice given was not a formal or clear-cut statement by the accountant, and the plaintiff did not in fact rely on the described advice).

B. Expert Testimony As To Reasonable Reliance Proves Proximate Causation.

Successful expert testimony which proves proximate causation of loss in accounting malpractice involves, in several reported cases, proof that the plaintiff reasonably relied on a non-accurate or omissive reports of the accounting firm.

In Re CBI Holding Co. Inc., 419 B.R. 553 (S.D.N.Y 2009), *supra*, illustrates successful expert proof of proximate causation in an accounting malpractice case. In *CBI*, plaintiff's expert witness testified that if the plaintiff company had been told by its accountants that some of its management was falsely inflating earnings, it would have ceased an acquisition strategy, and taken steps to preserve value while trying to attract a buyer. It would not have pursued a public debt offering which caused significant expenses and liabilities at a time when the company was already highly leveraged. The alternative strategies described by the trial expert would have prevented the eventual bankruptcy. If not for the accounting malpractice, the expert testified, a sale of the company was feasible at a price calculated as 22% of revenue. *In Re CBI, supra*, 419 B.R. at 559. (S.D.N.Y 2009).

The experience and knowledge of a party can be sufficient for successful proof of loss causation. *T.L. Wallace, supra*, 234 So.3d at 330 (Miss. 2017). In *T.L. Wallace* the trial testimony of a business owner who engaged the defendant was sufficient to establish loss causation. The owner, who had a fifth-grade education, had managed his multi-million dollar construction company successfully for more than thirty years. He testified that if the accused accounting firm had informed him of the true financial status of his company he would have liquidated assets earlier, would not have given $1 million to charity, would have not paid bonuses to executives, and would have fired the persons responsible for non-detection of deficient internal controls. The Court said "no one was better qualified" than the owner to testify as to what he would have done differently.

C. Proximate Causation Of Loss Is Not Always Easy To Prove.

The facts of the RIRRC case were such that reliable expert testimony as to proximate causation would not have been be easy to develop or to present to a Jury. The principal reason stated for the rule announced in the *RIRRC* Opinion is that the malpractice claims by the Agency tried against the auditor in *RIRRC* were "inevitably complicated" by facts showing that the auditor was one of three outside professionals accused of concurrent malpractice by the Agency as to the topics in dispute. The Agency alleged in concurrently filed cases negligence by (i) that its outside auditor for ten years prior to the defendant, and (ii) that its sole outside long-term investment advisor. As to the same issues or subjects as to which the auditor was alleged negligence. The Agency asserted that the negligence of all three concurrently caused very substantial losses to the Agency from 1999-2008.

The two other accused professionals were, in the eyes of the appellate Court, "possibly culpable" actors "directly relevant" to jury identification of the causes of any loss. The negligence of those two other professionals "would potentially have had a significant impact" on the jury deliberations and specifically "on the damages a jury might find to be caused primarily by the defendant auditor" (emphasis added). The absence of expert testimony as to the auditor on proximate causation forced the jury to decide liability based only on alleged failures of the auditor to report financial abuse as to crucial topics. The jury verdict, in effect, was that because there had been no reports of alleged abuse as to the topics by the auditor, the non-reporting of financial abuse by itself caused the loss alleged as to each topic. That outcome is instead unfair and incorrect because it closely resembles, or is equivalent to, strict liability. That outcome is as a result incorrect and unfair. Liability for malpractice requires, instead, proof of (i) negligence (error or fault), plus (ii) actual or "in fact" causation of the claimed loss, plus (iii) proof of proximate (or legal) causation, plus (iv) proof of the amount of the loss caused by the error. The fact that several actors were accused of simultaneously causing the same alleged losses made it clear to the appellate court that expert testimony as to proximate causation was required.

Reliable expert description of the relative roles of the three professionals in causation would have been essential in the RIRRC case, but reliable expert testimony on those issues would not have been easy to obtain. It is not clear how any expert could reliably opine as to the relative importance of

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multiple causes at various dates.

If for example, the investment advisor violated duties to the Agency starting in 1999, and the prior auditor by negligently did not detect those violations and thereby allowed them to continue starting in 1999 both forms of negligence and at work in 2006 when the defendant auditor is engaged. Reliable expert testimony on as to the relative importance of these causes is difficult if not impossible. What kind of expertise or learning would qualify anyone to be an expert as to when, how and why the defendant auditor became the "primary" cause of a loss? What qualifications, training, or expertise permits admissible expert testimony as to when and why one form of concurrent negligence, as opposed to others, became the dominant cause of certain losses? How are those issues reliably identified? These questions suggest that it is not clear that loss causation in RIRRC was able to be competently and reliably proved

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Editor's Note: We will be having a Wellness Initiative feature as a new addition to the PLDF Quarterly. Patty Beck of the MLM will be taking the lead. It will focus on wellness-related material and will include content such as practice tips, information about the benefits of meditation/mindfulness, techniques for meal planning, and the like.

PRACTICING WELL: UNPLUGGING 101

BY PATTY BECK

In a professional world that encourages and often demands immediate responses to email, how do we strike a balance between providing prompt professional services with the need to step away and have personal time outside of work? For starters, we need to be mindful of the fact that it is "okay" to "unplug" and devote time to our personal lives, especially during weekends, holidays and vacations.

In fact, taking time for ourselves is vital to our professional success as studies show that productivity and quality of work increase when we are rested. The next step is to practice unplugging on a small scale before attempting to unplug for an extended period of time (i.e., a week-long vacation). For example, for one month, spend 15-30 minutes during each workweek away from your computer and email (disable cell phone/device notifications).

During this time, do something you enjoy while making the conscious decision to be present in that moment and not be interrupted by work. This can mean going for an afternoon walk or jog, eating lunch away from your desk, reading a book for pleasure, etc. Once you have experienced that everything will be "okay" even if you are unavailable for a short period of time, start adding more of these brief periods of "me time" to your weekly routine until you eventually feel comfortable taking a full day away from work (pro tip: start with a weekend day where email traffic is likely minimal).

Although there will certainly be times where you need to be plugged in, training yourself how to be unplugged for short periods of time can have noticeable impacts on mental health and professional success. Remember, the key is to start small – most people do not respond well to large or sudden changes, so the slower you go, the more successful you will be.

Tips for Vacations: 1) decide how "unplugged" you plan to be (i.e., completely unplugged, checking email once per day, available by phone for emergencies only, etc.); 2) manage expectations by setting an auto-reply one week in advance of your vacation to alert clients and colleagues of your anticipated absence and availability; 3) arrange for a colleague to cover your files during your absence; and 4) be open with colleagues regarding your "availability" to help foster a workplace environment that encourages taking time to unplug and recharge.

Patty Beck is a Claim Attorney with Minnesota Lawyers Mutual Insurance Company where she manages litigation involving legal malpractice claims, advises attorneys facing existing and potential ethical dilemmas, and resolves complex pre-suit malpractice claims on behalf of MLM insureds. She is Co-Chair of the MSBA's Life & The Law Committee. Prior to joining MLM she worked as a litigator focusing on employment law for a large law firm in Minneapolis, MN.