

Understanding Insurance

The science of determining rates

Carl Younger, President

A common question at our seminar breaks is how insurance rates are set. Our insureds are not asking for an explanation of insurance ratemaking: they are asking why their homeowners, auto or boat policies have increased significantly over the last two years. After reminding our insureds of our record of having only one rate increase over the past six years, we focus on projected expenses, emphasizing the probability of future losses, and the financial success of a company's investments.

Operating Expenses

A simple principle of business is that revenue must cover costs. Costs for an insurance company fall into three main categories: (1) general operating expenses (salaries, rent, etc.); (2) costs to pay claims; (3) and the expenses of handling claims. While general operating expenses can be closely monitored, the costs of claims and the expenses of handling claims are often estimated and are likely to be incurred during a future period.

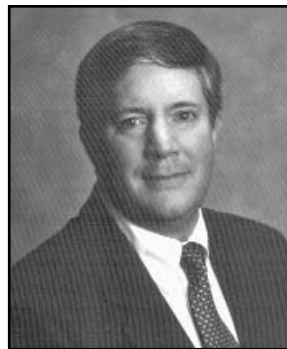
Insurance companies must project expenses for specific claims, as well as create a reserve for other claims. Claims history is used to project what amounts should be held as reserves to pay claims. The number of claims per year (frequency) and the size and distribution of claim payments (severity) are input into a formula that estimates what amounts will be paid to handle and resolve claims. Each line of business (homeowners, auto, legal professional liability) has its own history and formula. A substantial increase in the frequency or severity can affect projections of what existing and future claims may cost - leading to possible increases in rates.

Revenues and Investments

Insurance companies use premiums not only to pay current overhead and claims but also to invest in bonds or stocks projected to produce income. A company could, on a long-term basis, have its aggregate premiums equal its total claims and operating expenses yet be financially successful if earnings from investments were positive. An insurance company uses the time value of money to obtain positive financial returns and reduce the amounts its policyholders might otherwise pay.

Recent History

During the good investment years of the 1990s, insurance companies could earn significant returns in the equity markets and use those returns to stabilize premiums. However, the 21st century has not been so kind: investment losses removed the cushion protecting premiums. In addition, certain events have changed the formula for setting rates, particularly by impacting the perceived "severity" of losses. For many types of insurance, we are seeing the negative impacts of the "Perfect Storm" - of increased costs and reduced investment income.



Carl Younger
President

Why are WE Different?

After this explanation, the question we next hear is, "Why is Lawyers Mutual different?" There are several reasons. We monitor operating expenses closely. Even in difficult periods, we have an exceptional record of claims repair and resolution. We maintain a close relationship with our insureds, seeking early notification of matters that might become claims. We focus on North Carolina and have employees with unique knowledge of the practice of North Carolina law. As a mutual company, we do not borrow money to operate and do not have to earn a higher profit to pay shareholders for the use of their capital and exposure to the risks inherent in the insurance industry. In short, we are unique because of YOU.

This uniqueness is evident as Virginia, Tennessee and Georgia seek a malpractice carrier to replace a company in receivership that cannot guarantee existing claims will be paid. This uniqueness is also evident in the medical malpractice market and the departure of a major commercial carrier from North Carolina. For our Silver Anniversary, we celebrate our uniqueness. We are here today - and will be here tomorrow - because of YOU.

LME TODAY

LAWYERS MUTUAL LIABILITY INSURANCE COMPANY OF NORTH CAROLINA

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Appellate Practice

A fertile field for malpractice claims

Mark Scruggs, Claims Counsel

A recent situation reported to Lawyers Mutual highlights a pitfall found in the Rules of Appellate Procedure - a pitfall that could result in a malpractice claim. The problem stems from a misunderstanding of the interplay (or more correctly the lack of interplay) between Appellate Rule 27(b) dealing with computation of time and Appellate Rule 12(a) governing the time for filing the record on appeal.



Mark Scruggs
Claims Counsel

Appellate Rule 27(b) is identical to Civil Procedure Rule 6(e), a rule of procedure ingrained in most litigation lawyers because it is so often employed. Appellate Rule 27(b) states: "Whenever a party has the right to do some act or take some proceedings within a prescribed period after the service of a notice or other paper upon him and the notice or paper is served upon him by mail, three days shall be added to the prescribed period."

One must be extremely careful, however, when applying this rule to several aspects of appellate practice, including calculating the deadline for filing the record on appeal. In a recent case, the trial court settled the record on appeal under Appellate Rule 11(c). The order settling the record on appeal was filed with the court and mailed to counsel for the appellant.

Appellate Rule 12(a) requires that "[w]ithin 15 days after the record on appeal has been settled . . . the appellant shall file the record on appeal with the clerk of the court to which appeal is taken." Receipt of the order by mail caused appellant's counsel to erroneously calculate the deadline for filing the record on appeal with reference to Appellate Rule 12(a) and Appellate Rule 27(b). Counsel tickled the deadline for filing the record on appeal 18 days after his receipt by mail of the order settling the record on appeal.

Counsel filed the record on appeal in due course, but more than 15 days after settlement of the record on appeal by the trial court. Counsel for the appellee filed a motion with the Court of Appeals to dismiss the appeal, and the motion was granted. Thus, the client's appeal may be lost and a malpractice claim could be the result.

Like so many others, this error is one that lawyers who delve into appellate practice infrequently could easily make, especially given the pervasive use of identical Civil Procedure Rule 6(e) in civil litigation practice. However, Appellate Rule 27(b) conditions the addition of three days upon a party having "the right to do some act or take some proceedings within a prescribed period." In the case of filing the record on appeal, the appellant does not have the right - he has the obligation - to file the record on appeal within 15 days after settlement of the record on appeal. The timely filing of the record on appeal is a jurisdictional requirement and the deadline for filing the record on appeal is governed exclusively by Rule 12(a).

Challenges . . .
Risks . . .
Obstacles . . .

Solutions

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GROUP HEALTH BENEFITS

Have You Confirmed That In Writing?

Revisions to the rules of professional conduct

Louise Paglen, Vice President of Risk Management

The Supreme Court of North Carolina recently approved revisions, effective March 1, 2003, to the Rules of Professional Conduct. Several rules were rewritten to require a person's "informed consent confirmed in writing" before undertaking a representation. In some cases, the writing must be "signed" by the client.

Whereas under the old rules, all the conflicts of one lawyer were imputed to all the other lawyers in a firm, the new rules now allow "screening" under certain circumstances. To fully comprehend the most significant changes to the rules, it is necessary to first understand the terms: "confirmed in writing;" "informed consent;" "signed;" and "screening" as defined in the revised Rule 1.0 - Terminology.

Rule 1.0 - Terminology

The term "confirmed in writing" is used together with "informed consent" in conflict of interest rules: 1.7, 1.8 and 1.9. The revisions to Rule 1.7 and 1.9 deal with the conditions that must be met prior to waiving a conflict of interest involving a current, former or prospective client [hereinafter referred to generally as "client"]. Revisions to Rule 1.8 describe the kinds of disclosures that are required prior to entering into a business transaction with a client or making an aggregated settlement or plea agreement on behalf of two or more clients. The term "screening" is used in the context of imputed conflicts described in Rule 1.10.

"Informed consent" is defined as "the agreement by a person [client] to a proposed course of conduct after the lawyer has communicated adequate information and explanation appropriate to the circumstances." Prior to obtaining informed consent, the lawyer should discuss with the client the facts underlying the situation, including an explanation of the disadvantages and advantages of the proposed course of conduct (e.g. waiving a conflict of interest). The lawyer should also discuss with the client any alternative options. In some cases, it would be appropriate to advise the client to seek independent counsel. Whether or not the communication with the client is sufficient to satisfy the lawyer's professional obligation under the rule, would depend on a number of factors, including whether the client is experienced in legal matters or is represented by independent counsel.

Where the rules require that informed consent be confirmed in writing, the "writing" may take the form of an electronic transmission (such as email or fax), audio or video recording, handwriting, typewriting, printing, photostating or photography. The "writing" may be transmitted either from the lawyer to the client or vice versa. However, the transmittal must take place within a reasonable time after the informed consent is obtained. A "signed" writing may be an electronic process attached to or

logically associated with the writing (such as an email signature or fax transmittal sheet) that is executed with an intent to sign the writing.

"Screening" is defined in Rule 1.0 as the "isolation of a lawyer from any participation in a professional matter" through procedures that are designed to protect confidential information.

Waiving a Conflict of Interest

Prior to adoption of the most recent revisions to the Rules of Professional Conduct, it was not required that a waiver of a conflict of interest be documented in writing. Revisions to Rule 1.7 (Conflict of Interest: Current Clients) and Rule 1.9 (Duties to Former Clients) now require that a client give "informed consent" to waive a conflict of interest and that consent must be "confirmed in writing." Although strongly recommended by Lawyers Mutual, the rules do not require that the client sign the waiver document.

Given the recent rise in malpractice claims premised on an alleged conflict of interest, prudent risk management practices require careful and thoughtful consideration before seeking a waiver. If seeking a waiver would nevertheless be advantageous to the client, the lawyer should carefully set out in writing the circumstances giving rise to the conflict of interest, the disclosures made to the client, including the risks and advantages of consenting to the waiver. The client should then acknowledge having read and understood the disclosures by signing the written waiver, preferably in the presence of a witness. In the event the client later alleges malpractice on the basis of a conflict of interest, this practice will provide excellent documentation supporting the lawyer's compliance with the rules requiring informed consent. Regardless of client consent, some conflicts of interest may not be waived. These include: (1) cases where the client's interests are so adverse that the lawyer will not be able to provide competent representation to each client; (2) a claim by one client against another in the same litigation; or (3) concurrent representation that is prohibited by law.



Louise Paglen
Vice President of Risk
Management

Imputed Conflicts and Lateral Hires

Prior to March 1st, all conflicts of interest, even those of a personal nature, were imputed to all lawyers in a firm. For example, under the old rules if one lawyer in a firm had strong political beliefs that prevented him or her from adequately

Continued on pg. 4

representing a particular client, in the absence of a valid waiver, all of the lawyers in the firm were conflicted out of the representation. Revisions to Rule 1.10 acknowledge that in the majority of cases, an individual lawyer's personal conflict of interest should not be imputed to all other members of the firm.

Rule 1.10 was also relaxed to make it much easier for lawyers to move from one firm to another without encumbering the new firm with all the conflicts of interests from the former firm. Lawyers who become associated with a new firm may have a conflict of interest with a former client (Rule 1.9) that would prohibit the lawyer from undertaking a representation adverse to that client. Under the old rule, the conflict of interest was imputed to all lawyers in the firm. As a result, the firm was required to: (1) obtain waivers from each affected client; or (2) withdraw from representations tainted by the new lawyer's conflict of interest; or (3) refrain from hiring the lawyer due to the conflict. Revisions to Rule 1.10(c) now allow the firm to screen the disqualified lawyer" (the lawyer affected by the conflict under Rule 1.9) from any participation in the matter. The firm must, however, give written notice to any former client affected by the conflict. Although the former client must have an opportunity to

ascertain whether the firm has complied with the provisions of the rule, the former client's consent to the firm's representation is no longer required.

Business Transactions With Clients

Lawyers Mutual has recently experienced an increase in malpractice claims involving lawyers who enter into business transactions with their clients. Revisions to the rules, although intended to protect the client from unfair dealing, if properly followed by attorneys engaging in this risky business, may also help reduce the possibility of a malpractice claim. Pursuant to Rule 1.8(a), before a lawyer enters into a business transaction with a client, the lawyer must advise the client in writing of the desirability of seeking the advice of independent legal counsel with respect to the transaction. In a "writing signed by the client," the client must also give "informed consent," with respect to the "essential terms of the transaction," including the lawyer's role and representation as it relates to the transaction. The new rule, like its earlier version, still requires that the transaction be fair to the client.

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RULES OF PROFESSIONAL CONDUCT REVISIONS

Revised Rule	Subject	Client Consent Required	Writing Required	Client's Signature Required	Comments
1.5(b)	Fee Agreement	√			Communicate with new clients regarding fee and expenses.
1.5(c)	Contingency Fee	√	√	√	Explain calculation method.
1.5(e)	Fee Splitting	√	√		Fee must be in proportion to services.
1.7(b)	Waiver of Conflict – Current Clients	√	√		Some conflicts are nonconsentable.
1.8(a)	Business Transactions with Clients	√	√	√	Must advise to seek independent counsel.
1.8(g)	Aggregate Settlement	√	√	√	Applies to plea agreements involving multiple defendants in criminal cases.
1.9	Waiver of conflict – former clients	√	√		Some conflicts are nonconsentable.
1.10(c)	Imputed Conflicts		√		Personal conflicts are not imputed. Screening permitted for lateral hires.

Aggregate Settlements and Plea Agreements

Revisions to paragraph (g) of Rule 1.8 now require that each client who is a party to an aggregated settlement, or in a criminal case, an aggregated agreement as to a guilty or nolo contendere plea, must provide "informed consent" to the agreement in a writing signed by each client.

Contingency Fee Agreements

Although strongly recommended, the State Bar stopped short of requiring that all fee agreements be in writing. However, under the newly revised Rule 1.5, all contingency fee agreements and fee splitting agreements between lawyers in separate firms must now be documented in writing.

Contingency fee agreements must be signed by the client and must include an explanation of the method used to calculate the fee. The agreement must also "clearly notify the client of any expenses for which the client will be liable, whether or not the client is the prevailing party." At the conclusion of the representation, the lawyer must provide the client with a written accounting that includes any remittance to the client and the method used to determine the amount.

Although the requirements for entering into a contingency fee agreement have been strengthened, the State Bar eliminated the obligation that clients remain liable for court costs and litigation expenses advanced by their lawyer. Under revised Rule 1.8(e), repayment of court costs and litigation expenses may now be contingent on the outcome of the case;

and lawyers representing indigent clients may pay court costs and litigation expenses on their behalf.

Fee Splitting

Under the prior rules, lawyers in separate firms who wanted to associate and share fees were required only to inform the client of the arrangement, and divide the fee in proportion to each lawyer's services. As long as the client did not object to the participation of each lawyer, they were free to divide the fee. Under the revised Rule 1.5(e), the client must agree to the arrangement, "including the share each lawyer will receive," and the agreement must be "confirmed in writing." The division of the fee must still be in proportion to the services performed by each lawyer.

Lawyers Mutual is Available to Help

It may be difficult for lawyers in private practice to find the time to study the changes to the ethics rules or to keep their staff adequately informed. Therefore, as a free service to its insureds, Lawyers Mutual will offer in-house training on risk management topics such as this one. If you would like to request a risk management presentation for the attorneys and/or staff in your firm, please contact Diane Boyette at 1-800-662-8843 to schedule a program designed to meet your needs. Smaller firms are encouraged to invite other law offices to join them for the presentation.

WE Care - BarCARES

We recently highlighted programs of the NC State Bar which direct lawyers to needed mental health and addiction services. The NC Bar Association in conjunction with several local bar associations has gone one step further: BarCARES provides direct confidential counseling services to members and their families at no cost through participating local bar associations. If your local association is a member of BarCARES, do not hesitate to call 1-877-394-2271 if you or a family member needs help. For more information on the program call 1-800-662-7407, extension 302. Please seek help if it is needed. As fellow lawyers and friends, WE Care about you and your family.

Understanding Underwriting...

HOW LONG DOES IT TAKE TO GET MY POLICY?

It takes approximately ten days to process an application and issue a policy.

DO I HAVE TO FILL OUT A NEW APPLICATION EVEN IF THERE ARE NO CHANGES?

Yes, it is required for each applicant to complete a new application each and every year. Your Claims Made Policy is a reissue policy - not a renewal - thus requiring the new application.

LMI TODAY

The contents of this newsletter are intended for general information purposes only and should not be construed as legal advice or legal opinion on any specific facts or circumstances. It is not the intent of this newsletter to establish a standard of due care for any particular situation. Rather, it is our intent to advise our policyholders to act in a manner that might well be above the standard of care in order to minimize a firm's malpractice risk.

Henry A. Mitchell, Jr.
Chairman

Carl Younger
President

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A publication for policyholders of
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