

Professional Malpractice

Recovering Damages in Legal Malpractice Cases

An update on what type of award, and how much, a client can expect

By **Bennett J. Wasserman**

In the quickly evolving field of lawyer malpractice, one area that seems to get less attention than others is compensable damages. The question is: What types of damages can a client legitimately expect to be awarded as a result of his or her lawyer's substandard handling of a matter?

New Jersey courts have been willing to push the envelope in this area, permitting, for example, recovery of attorney fees as compensatory damages to the prevailing plaintiff (*Saffer v. Willoughby*, 143 N.J. 256 (1996)), emotional distress due to loss of liberty (*Snyder v. Baumecker*, 708 F. Supp. 1451, D.N.J. 1989)), and emotional distress where the lawyer botches a client's noneconomic claims (*Kohn v.*

Wasserman is general counsel to legalmalpractice.com. He is editor in chief of the Legal Malpractice Law Review blog and is special professor of law at Hofstra University Law School. He is of counsel to Davis Saperstein & Salomon PC.

Schiappa, 281 N.J. Super. 235 (1995)). Our neighbor Pennsylvania has been less bold.

But, recently, Pennsylvania has seen an important appellate decision relating to how much a legal malpractice plaintiff can recover from a former negligent attorney. New Jersey has fine-tuned its own approach on available damages as well. Because so many New Jersey lawyers now also practice in Pennsylvania, a brief update on both states may be of interest.

Pennsylvania

Unlike New Jersey, which has a single statute of limitations for legal malpractice actions (six years), Pennsylvania continues to have two separate time limits: two years for legal malpractice actions based in tort (called "trespass"), and four years for those actions based on contract (called "assumpsit"). There has been, until now, an important substantive distinction to this procedural difference. For the plaintiff suing in tort, a broader range of compensatory damages is available: virtually all foreseeable damages, including the value

of noneconomic injuries that would have been available in the underlying case or transaction had it not been botched by the negligent lawyer. But if a legal malpractice plaintiff sues only for breach of contract within four years — because, as usually occurs, the plaintiff has missed the two-year statute of limitations for tort — the recoverable damages have been limited to recovery of attorney fees paid to the allegedly negligent lawyer. Any other damages sustained as a result of the negligent lawyer's services were believed to be barred. Those other damages would only be available if the plaintiff had brought a timely trespass (tort) claim. The obvious result was bizarre and, some say, downright unjust.

But, on Nov. 12, 2012, in *Coleman v. Duane Morris*, the Superior Court of Pennsylvania took a closer look. And its soon-to-be-published decision spells a sea change in Pennsylvania's law of recoverable damages in legal malpractice cases.

It all goes back to a case called *Bailey v. Tucker*, 533 Pa. 237 (1993), a malpractice action arising out of a claim of ineffective assistance of counsel in defending an underlying criminal case. The client sued for malpractice. Because of policy reasons, the court imposed more rigorous burdens of proof and preconditions to recovery for tort claims brought by the criminal defendant against negligent defense counsel. But then the court went on to hold that, as to a legal malpractice claim based on breach of contract, pursuant to which the lawyer furnished his services, the "damages will be limited to the

amount actually paid for the services plus statutory interest.”

The *Bailey* decision seemed to make clear that its holding applied only to breach-of-contract claims arising from botched representation in the defense of an underlying *criminal* claim.

(The New York Court of Appeals recently decided a very similar case in *Dombrowski v. Bulson*, 19 N.Y. 3d 347 (2012), stopping the Appellate Division from expanding recoverable damages for noneconomic loss suffered by a criminal defendant as a result of ineffective assistance of counsel.)

In Pennsylvania, many lawyers came to believe that *Bailey* applied to underlying civil matters as well. Indeed, at least one state court and one federal decision so held. And based on those erroneous readings of *Bailey*, the trial court in *Coleman* dismissed the plaintiff’s breach-of-contract legal malpractice claim entirely because, although the attorney’s breach allegedly caused substantial damage, the plaintiffs had not paid any fee. Thus, they were entitled to nothing back. But finally, the appellate court cleared up the confusion. Here’s what happened:

Coleman held ownership interests in BCA Management and BCA Professional Services, which collectively owed over \$2 million in unpaid payroll and employee withholding taxes, for which the plaintiffs were personally liable. In order to relieve themselves of this liability, the plaintiffs sought to sell their interests in BCA. They began negotiating with a buyer and sought legal advice from their attorney and her law firm (who had previously represented them in various matters) regarding a non-binding letter of intent. The letter of intent provided that the plaintiffs would sell their shares in BCA for at least \$2.5 million. The plaintiffs alleged that the attorney agreed to represent them in the transaction, that she agreed to bill BCA for the legal work, and that the buyer would pay the attorney fees after its acquisition of BCA.

The plaintiffs then put together a draft agreement outlining the sale and submitted it to the attorney. The draft agreement provided for the sale of 100 percent of the plaintiffs’ BCA stock in exchange for \$300,000. Further, the plaintiffs would resign their positions with BCA and get

new positions with the buyer. Finally, the draft agreement contained a guaranty that the buyer would pay up to \$2.2 million in unpaid taxes. The defendant attorney made revisions to the draft agreement and gave it to the plaintiffs and to the buyer’s counsel. The plaintiffs alleged that, following this, they were assured by the attorney that the sale would relieve them of their personal tax liability. The defendant attorney’s changes were incorporated into the final stock purchase agreement. The plaintiffs later learned that despite the transfer, they would remain personally liable for the taxes.

At the closing, the plaintiffs and their attorney were advised that the buyer had assigned its rights under the agreement to an alleged subsidiary formed the day before. The plaintiffs asked the attorney about the significance of this assignment, and the attorney allegedly replied that it would not affect the tax liability issue and that the plaintiffs had “gotten everything they wanted, and more” from the deal. After the closing, one of the plaintiffs continued to manage BCA, but he was soon fired. He sued to re-obtain control of BCA after he was made aware of problems at the company by current and former clients. The court awarded him limited power of attorney and ordered him to perform an accounting. The plaintiffs then discovered that BCA’s assets had been plundered by the buyer and that the unpaid taxes were still owing. Eventually, the IRS seized a BCA bank account to pay a small part of the total tax debt.

The plaintiffs brought an action for legal malpractice against the law firm. The suit was based on a breach-of-contract theory, seeking to recover the lost value of the BCA stock and the interest and fees that accrued on the tax debt. They did not sue in negligence because the two-year statute of limitations had already run.

The defendants asserted that the plaintiffs had concealed the true extent of their tax liability and in fact never discussed their tax liability with them. They also claimed that the plaintiffs did not pay them attorney fees and that the plaintiffs’ damages were inconsistent with proof of “actual loss.” The defendants argued that *Bailey v. Tucker* was controlling and limited the plaintiffs’ damages to a reimbursement of

attorney fees paid. Since the plaintiff had paid no fees to the defendant attorney or firm in connection with the sale of the BCA stock, the action should be dismissed on the pleadings since no damages were sustained. The trial court agreed and dismissed the claim on the pleadings. The plaintiffs appealed.

So the issue was now squarely before the court: Is a client who sues a lawyer for legal malpractice based on breach of contract allowed to recover consequential damages, or are damages limited to attorney fees paid to the defendant attorneys? The court ruled clearly and unequivocally:

We conclude that the limitation on damages imposed by the *Bailey* court applies to an action in assumpsit [breach of contract] based on a claim of attorney malpractice in a criminal case, but that limitation does not extend to an action for legal malpractice in assumpsit where the underlying action was, as here, a civil action.

Moreover, the court held that the plaintiffs had entered into the transaction represented by the defendant attorney with the expectation that they would be relieved of their tax liability, which constituted “actual loss”:

Thus, the plaintiffs’ claim for the value of their stock, which they bargained away based on their reliance on defendants’ legal advice, and the interest and penalties that had accrued on the unpaid taxes... would constitute the actual losses sustained by plaintiffs.

The net effect of the *Coleman* appellate decision is more than just a clarification that the *Bailey* decision was never intended to apply to legal malpractice claims arising from botched underlying civil matters. Now that it has been made clear that damages recoverable for breach-of-contract cases brought within the four-year statute of limitations are equally available to damages recoverable in tort actions brought for tort within two years. From

the defense perspective, whatever benefit a two-year statute of limitations provided in defending tort-based claims in legal malpractice cases is of no practical value anymore.

New Jersey

In New Jersey, which is arguably the only state where the plaintiff's cost of successfully prosecuting a legal malpractice action is added to the compensatory damages recovered from the negligent lawyer, we saw some tweaking to that doctrine, which emanates from *Saffer v. Willoughby*. Many clients opt to retain their malpractice attorneys on a contingent fee basis, but that does not mean that the compensatory damages to be awarded to cover the attorney fees as the cost of prosecuting the legal malpractice action will be equal to the amount of the contingent fee that plaintiff agreed to pay his malpractice lawyer. In an unpublished decision, the Appellate Division in *Nix v. Verp* (Feb. 18, 2011), the court made clear that the contractual terms between the malpractice plaintiff and the lawyer prosecuting the malpractice action are not binding on the court when it awards additional compensatory damages to the prevailing plaintiff. Instead, the court will utilize the usual "lodestar" method of calculating fees which it believes to be reasonable. It will then add that figure on to the compensatory damages already awarded to

the plaintiff. Here's how that would work:

1. A contingent fee agreement between the malpractice plaintiff and his malpractice attorney does not apply to applications for attorneys fees under *Saffer*. "The reasonable counsel fees payable to the prevailing party under fee-shifting statute is determined independently of the provisions of the fee agreement between the party and his or her counsel."

2. Trial courts may employ the lodestar method — the number of hours reasonably expended by the attorney, multiplied by a reasonable hourly rate — in calculating counsel fee awards in legal malpractice actions.

3. No compensation is due for non-productive time, such as hours that are excessive, redundant or otherwise unnecessary. Further, the court can reduce the hours claimed by the number of hours spent litigating claims on which the party did not succeed.

4. Determining the reasonableness of hourly rates need not be unnecessarily complex or protracted, but the trial court should satisfy itself that the assigned hourly rates are fair, realistic and accurate, or should make appropriate adjustments.

The importance to contingency fee lawyers handling legal malpractice cases cannot be understated. They must now keep reliable time records of the work they actually perform in representing all legal

malpractice clients, if they hope to recover attorney fees at the end of the successful case. Although this decision is unpublished and has no precedential value, it makes sense to save this decision as a handy guide for future reference.

One caveat, however. The court in *Nix* refers to the erroneous assumption that *Saffer v. Willoughby* is a "fee shifting" scheme. It is not. It is a method by which the New Jersey Supreme Court permits an award of compensatory damages to the injured victim of legal malpractice. If the damages, in the form of attorney fees and costs, that the client is required to pay the malpractice attorney are to be paid under a contingent fee retainer agreement, and the client actually has to pay that amount, we are at a loss to understand why the trial court must go through a lodestar analysis, which typically is applied to hourly fee cases and quantum meruit considerations. What if a lodestar analysis would award more than the contingent fee? Would the court rule otherwise? Would the court rule that the lawyer can collect only the amount of the contingent fee? This dilemma might be resolved if the court had not mixed apples and oranges by confusing fee-shifting modalities as provided in various statutes and rules with an award of compensatory damages. *Saffer v. Willoughby* is *not* a fee-shifting modality. ■