LEGAL MALPRACTICE COVERAGE AND CLAIMS RELATED TO ACTS OF TERRORISM

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I. DO LAW FIRMS NEED TERRORISM COVERAGE AS PART OF THEIR PROFESSIONAL LIABILITY COVERAGE?

The Terrorism Risk Insurance Act of 2002 ("TRIA") requires insurers, including most professional liability insurers, to offer coverage for losses resulting from a defined "act of terrorism." Once an insurer makes the offer to provide terrorism coverage and quotes a premium for that coverage, a policyholder must decide to accept the offer and pay the applicable premium for the terrorism coverage or allow the insurer to exclude coverage for such acts of terrorism. An insurer is not required to offer — and is thus free to exclude — coverage for losses resulting from violent political acts which do not meet the specific definition of an "act of terrorism" under TRIA. For this reason, the policyholder is required to assess the risk that it may face a professional liability claim for a loss caused in part by a TRIA-defined act of terrorism in order to determine its need for the insurance offered. Making such an assessment of necessity requires an understanding of what is (and what is *not*) an "act of terrorism" under TRIA. *See generally* Jarrett, *The Business of Terrorism: The Terrorism Risk Insurance Act of 2002,* 77-OCT Fla.B.J. 63, 64 (2003).

In the context of professional liability insurance for law firms, the terrorism coverage offered provides coverage for a loss that results from an "act of terrorism" *and* that is otherwise covered by the policy. For this reason, in determining whether to purchase terrorism coverage as part of its professional liability risk management, each firm must assess the likelihood that it may sustain liability for a loss that results *both* from an "act of terrorism" *and* its own negligent error, act or omission in the rendition of professional services.

II. WHAT IS AN "ACT OF TERRORISM" UNDER TRIA?

A professional liability insurer might offer or exclude coverage only for losses resulting from an "act of terrorism" as defined in TRIA. TRIA defines an "act of terrorism" as follows:

An "act of terrorism" means:

> *[A]ny act that is certified by the Secretary of the Treasury, in concurrence with the Secretary of State, and the Attorney General of the United States*
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> *(i) to be an act of terrorism;*
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> *(ii) to be a violent act or an act that is dangerous to —*
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> *(I) human life;*
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> *(II) property; or*
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> *(III) infrastructure;*
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> *(iii) to have resulted in damage within the United States, or outside of the United States in the case of —*
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> *(I) an air carrier (as defined in section 40102 of title 49, United States Code) or United States flag vessel (or a vessel based principally in the United States, on which United States income tax is paid and whose insurance coverage is subject to regulation in the United States); or*
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> *(II) the premises of a United States mission; and*
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> *(iv) to have been committed by an individual or individuals acting on behalf of any foreign person or foreign interest, as part of*

an effort to coerce the civilian population of the United States or to influence the policy or affect the conduct of the United States Government by coercion.

III. WHAT ADDITIONAL PROTECTION DOES AN INSURED OBTAIN BY PURCHASING PROFESSIONAL LIABILITY COVERAGE FOR LOSSES RESULTING FROM TRIA-DEFINED "ACTS OF TERRORISM"?

A. *Under TRIA, determination of whether a loss results from an "act of terrorism" is a political, rather than a contractual, question.*

At first glance, it would appear that, notwithstanding the detailed definition in TRIA, the question of what constitutes an "act of terrorism" is a subject fraught with potential dispute giving rise to extended coverage litigation. However, TRIA pre-empts most coverage questions arising out of the definition of "act of terrorism" by conferring upon the Secretary of the Treasury the authority — with the concurrence of the Secretary of State and the Attorney General of the United States — to certify (or not to certify) whether a particular act is a defined "act of terrorism." The decision to certify or not to certify is final and not subject to judicial review. TRIA, H.R. 3210, §102(1)(C).

B. *Political constraints may discourage government officials from characterizing conduct causing losses as an "act of terrorism."*

While it may generally be politically expedient for public officials to characterize acts of violence directed against American citizens as "terrorist" in nature, there may be distinct political concerns which might dissuade the Secretary of Treasury from making a formal determination that given conduct is an "act of terrorism" for purposes of determining insurance coverage for the loss.

1. Triggering insurance exclusions

Where the policyholder elects not to purchase proffered terrorism coverage, the insurer is free to exclude losses resulting from a TRIA-defined "act of terrorism" from its coverage. In this situation, the Secretary of Treasury's determination that a given act of violence is an "act of terrorism" within the meaning of the Act would trigger the terrorism exclusion, thus depriving policyholders of insurance benefits they might otherwise be entitled to.

2. Risk transfer to government

When a policyholder elects to purchase professional liability coverage for losses caused by an "act of terrorism," the insurer's payment of such a loss counts toward the insurer's "deductible" for terrorism losses. After the insurer has met its deductible, the federal government will reimburse the insurer for 90% of losses paid in excess of the deductible up to $100 billion per year, at which point the insurer's liability is capped. These limits on insurers' indemnity obligations only take effect if the cause of the loss is certified as an "act of terrorism" by the Secretary of the Treasury.

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Since the Secretary of the Treasury's determination that given conduct is an "act of terrorism" under TRIA potentially confers benefits on insurance companies at the expense of policyholders and taxpayers, the Secretary may be reluctant to take the political risks attendant to making such a determination. This possibility may lead policyholders to conclude that purchasing a professional liability policy which does not provide coverage for losses resulting from an "act of terrorism" as defined under TRIA exposes them to little additional risk.

C. *Many acts of violence would not constitute an "act of terrorism" under TRIA.*

The detailed definition of an "act of terrorism" under TRIA means that many types of violent and harmful activity may not properly be certified as such by the government officials charged with that responsibility. For example, only acts committed by individuals "acting on behalf of any foreign person or foreign interest" may qualify as an "act of terrorism" under TRIA. Thus, domestic terrorism would not fall within this definition.

> **Example:** A disgruntled citizen angry at the federal government bombs a post office. A notice of appeal mailed by an attorney to court for filing is destroyed, and the attorney is subsequently sued for malpractice for failure to perfect a timely appeal. This domestic act of violence was not carried out on behalf of any foreign person or foreign interests, and as such, it cannot be classified as an "act of terrorism" within the meaning of TRIA. It would not be necessary to purchase coverage for losses from TRIA-defined acts of terrorism for this loss because the loss did not result from a certified *foreign* "act of terrorism."

Similarly — except in cases involving damages to certain air carriers or vessels or to the premises of a United States mission — the conduct must actually have "resulted in damage within the United States." TRIA, H.R. 3210, §102(1)(A). Arguably this requires some form of "physical" damage. On the other hand, loss of use of tangible property which has not been physically damaged often falls within the definition of "property damage" in insurance policies. Thus, a violent act which interferes with the use of tangible property (but does not result in physical damage to it) could conceivably be one which "resulted in damage" as required by TRIA.

Example: A suicide bomber acting on behalf of Al Qaeda commandeers the lobby of the Empire State Building and threatens to blow up both the building and himself. After twenty-four hours of negotiations — during which time the Empire State Building is closed to the public and to tenants — police are eventually able to subdue the would-be bomber without injury to persons or property.

A lawyer who is a tenant of the building misses a court filing deadline because he did not have access to his offices to prepare the necessary papers. If the lawyer is subsequently sued for malpractice for failure to prepare and timely file these papers — and if the lawyer's professional liability excludes coverage for losses caused by a TRIA-defined "act of terrorism" because the lawyer declined to purchase TRIA coverage — a question would be raised as to whether the acts which interfered with the use of tangible property (the lawyer's office) but caused no *physical* damage to the office or building could properly be characterized as an "act of terrorism" which "resulted in damage" to trigger the exclusion.

D. *An "act of terrorism" (whether defined under TRIA or not) must be a proximate cause of the loss before a terrorism exclusion would preclude coverage.*

Where a professional liability policy excludes losses from acts of terrorism (regardless of whether the "act of terrorism" tracks the TRIA definition), the terrorism exclusion would preclude coverage only for a loss which actually results from the act of terrorism. A professional liability claim would be covered even if there was some temporal relationship between an act of terrorism and the resulting

loss giving rise to the claim as long as the act of terrorism was not a proximate cause of the loss.

> **Example:** In *In re Bushnell*, 273 B.R. 359 (D.Vt. 2001), the creditors in a bankruptcy proceeding sought to enlarge their time to file an appeal from a summary judgment entered in favor of the debtor. The order entering summary judgment had been entered on September 8, 2001, and the ten-day period in which to file a notice of appeal expired on September 18. Bankruptcy rules further provide that if no timely notice of appeal has been filed within the ten-day period, a party may, upon a showing of "excusable neglect," seek an additional twenty days in which to file the notice.
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> The creditors sought to file a notice of appeal on September 21, 2001. This was not timely, because the notice should have been filed on or before September 18 (ten days after entry of the order being appealed from). On October 10, the debtor moved to dismiss the appeal, and on October 19, the creditors moved to enlarge the time in which to file the notice of appeal. This motion, too, was untimely, since it should have been filed within twenty days after the expiration of the original deadline in which to file the notice of appeal, *i.e.,* on or before October 8, 2001. Thus, the creditors filed neither a timely notice of appeal within ten days nor a timely motion for an extension of the time to file the appeal within the additional twenty-day period.

The Court granted debtor's the motion to dismiss the appeal. In doing so, the Court rejected the creditors' argument that the terrorist attacks which closed the court on September 11 at noon and all day on September 12 excused the creditors' compliance with the filing deadlines which were jurisdictional:

> [T]here is no evidence that there was any necessary nexus between claimants' counsel's tardiness an these events, or that the events of September 11th had a direct causal impact upon claimants' counsel's failure to act timely, beyond that which one might experience in the context of a personal tragedy. ... [¶] There is no allegation that claimants' counsel's office was closed for an extended period of time due to the calamity, that her clients were unavailable for critical consultation due to unavoidable circumstances related to the attack or that any consequence of the attack directly impeded counsel from filing a simple notice of appeal or motion for extension of time in a timely manner. 273 B.R. at 364-365.

If the creditors in *Bushnell* were to file a malpractice action against their attorney for failure to perfect a timely appeal, the determination that the attorney's failure to file the notice of appeal was *not* proximately caused by the terrorist attacks would presumably negate any coverage defense that the loss was excluded because it resulted from an "act of terrorism."

E. *Law firms may have means of avoiding liability for terrorist-related losses in addition to purchasing insurance coverage.*

A law firm may have means other than purchasing insurance to minimize professional liability risks attendant to an "act of terrorism." Pursuing other loss prevention mechanisms is important even if a law firm has purchased coverage for losses resulting from TRIA-defined "acts of terrorism," particularly if the policy excludes losses resulting from violent acts (such as domestic acts of terrorism) not falling within the TRIA definition.

Courts and court rules may permit lawyers to avoid liability for losses resulting from terrorist activity. For example, if terrorists force closure of the courts, some jurisdictions provide that filing deadlines are extended until the next day the courts are open. *See, e.g.,* Rule 6(a), Federal Rule of Civil Procedure ("when the act to be done is the filing of a paper in court, a day on which weather or other conditions have made the office of the clerk of the district court inaccessible, in which event the period runs until the end of the next day which is not one of the aforementioned days") and Section 12b, California Code of Civil Procedure ("If any city, county, state, or public office, other than a branch office, is closed for the whole of any day, insofar as the business of that office is concerned, that day shall be considered as a holiday for the purpose of computing time ...").

Even where a deadline is jurisdictional (such as the time limit in which to file a notice of appeal), courts may exercise some discretion to excuse technical noncompliance with deadline. The "unique circumstances" doctrine allows a court to permit a filing after the passage of a jurisdictional deadline if it can be shown that an act of terrorism made it impracticable to comply with the deadline.

Example: The federal district court in New York entered judgment against the defendant on August 14, 2001.

> Under Rule 4, Federal Rules of Appellate Procedure, the defendant had thirty days in which to file a notice of appeal with the right to seek an extension for an additional thirty days upon a showing of excusable neglect or good cause. The defendant's time to appeal expired on September 13, 2001. Because of the defense counsel's inability to access its office due to the September 11 attacks, the defendant did not seek an extension of its time in which to file a notice of appeal until October 23, 2001. The court granted the extension even though the motion was not technically timely because of the "unique circumstances" surrounding the World Trade Center attack. *Ishay v. City of New York,* 178 F.Supp.2nd 314 (E.D.N.Y. 2001).

F. ***The risk that an "act of terrorism" may result in professional liability claim is real.***

Given the fact that courts have been lenient in excusing the failure to perform professional obligations in a timely manner where an act of terrorism was a proximate cause of that failure, there might at first blush appear to be little need for a law firm to obtain professional liability coverage without a terrorism exclusion. Nevertheless, after September 11, serious acts of terrorism on United States soil — and the disruption of day-to-day life caused thereby — can no longer be regarded as "unprecedented." For this reason, the possibility exists that in the future, attorneys will be held to a standard of care that not only requires the attorney to foresee the possibility of work interruption due to natural disasters such as floods or earthquakes but also to anticipate their possible inability to fulfill their professional responsibilities because of acts of terrorism. Thus, the risk that an act of terrorism may create a loss which is also proximately caused by an attorney's

negligent act or omission — and the attorney's potential liability for that loss — must be viewed as real.

Terrorist-related activities might result in closure of courts in one location but not elsewhere. An attorney whose office is inaccessible because of an act of terrorism might nonetheless face liability if she misses a filing deadline in another location where the courts remain open. For example, Section 12b, California Code of Civil Procedure, extends deadlines "[i]f any city, county, state, or public office, *other than a branch office,* is closed for the whole of any day, insofar as the business of that office is concerned ..." This statute provides no protection for a missed deadline if only a branch office of the court is closed. *See Bennett v. Suncloud,* 56 Cal.App.4th 91 (1997) (closing of the West branch of the Los Angeles County Superior Court as a result of an earthquake on last day for statute of limitations to run would not excuse tardy filing of complaint unless the plaintiff could also show that the downtown court, where the action could also have been filed, was also closed).

Moreover, an attorney cannot be certain that her failure to meet a deadline — particularly a jurisdictional deadline — will be excused by the court. An attorney thus runs the risk that her inability to access her office and take other steps to timely file papers as a result of an act of terrorism may result in professional liability on her part.

> **Example:** A prisoner sought reconsideration of a motion for summary judgment entered against him in his civil rights action. The prisoner timely filed his motion for reconsideration on September 6, 2001, but the copy served on the defendant was not post-marked until September 12, 2001 (after the deadline had passed for making the motion for reconsideration). Technically the service was not

proper, since a party must generally serve papers "before the time of filing." Rule 25(b), Federal Rules of Civil Procedure. Nevertheless, the Court, referring to "the tragic events of September 11, 2001 and the resulting lags in postal service," accepted the filing and service as timely and ruled on the motion's merits (although it proceeded to deny the motion for reconsideration). *Davidson v. Scully,* 172 F.Supp.2nd 458, 463, n.2 (S.D.N.Y. 2001.

In excusing the apparently late service of the motion for reconsideration, the Court in part alluded to the "plaintiff's *pro se* status." A different result might have obtained if the moving party had been represented by counsel.

IV. WHAT IS PRACTICAL EFFECT OF A TERRORISM EXCLUSION ON THE DUTY TO DEFEND?

A. *A terrorism exclusion may have little impact on an insurer's duty to defend professional liability claims.*

Even where a loss is arguably the result of an "act of terrorism" (whether defined by TRIA or otherwise), a law firm may be entitled to a defense under its professional liability policy even if it did not purchase the proffered terrorism coverage and the policy has a terrorism loss exclusion. In most jurisdictions, the terrorism exclusion would eliminate a duty to defend only if it eliminated *all* potential for coverage. In jurisdictions which look only to the "four corners" of the pleading asserting the claim against the insured to determine the potential for coverage, a terrorism exclusion would eliminate a duty to defend only if the act of terrorism was pled as the *sole* cause of the claimant's loss.

In most instances, the claimant alleging professional negligence will not make reference to other factors — such as an act of terrorism, a snowstorm or an earthquake — which might, in addition to the defendant's negligence, have

contributed to the loss. Thus, a malpractice claimant might allege in her complaint that she suffered a loss because her attorney failed to file a complaint prior to expiration of the statute of limitations, but she would not like likely include allegations regarding the existence of extenuating circumstances (such as a terrorist attack which closed her attorney's office) in her pleading. Particularly in those jurisdictions in which the duty to defend is measured exclusively by the allegations of the four corners of the complaint, an insurer would not be able to deny a defense to an insured attorney even where it might have no ultimate duty to indemnify. Even the policyholder's ability to argue that it should have no liability because its failure to meet a court deadline was occasioned by a terrorist act would probably not defeat the duty to defend, since the possibility would still exist that the court would not accept the "act of terrorism" as a valid excuse and proceed to impose liability on other grounds which would be covered by the attorney's professional liability policy. *See In re Bushnell, supra.*

B. *Coverage issues relating to a terrorism exclusion might give rise to possible conflict of interest between the insurer and the insured.*

Where a policyholder elects to purchase professional liability coverage which excludes losses resulting in part terrorist-related activity (whether that activity is an "act of terrorism" under TRIA or not), a conflict might arise between the insurer and its policyholder where a given claim might not be covered because of the exclusion. In some instances, the policyholder's best chance of avoiding liability is to shift responsibility for the loss from his own misfeasance to the terrorist act. For example, an attorney who has unequivocally failed to meet a jurisdictional deadline may have no viable defense other than to attribute his failure to meet a court deadline to difficulties occasioned by violent activities which have been certified as an "act of terrorism" under TRIA. Where a court accepts the argument that an act of terrorism *may* have contributed to the attorney's misfeasance but does not excuse the attorney from his liability therefor,

raising of the defense may eliminate the attorney's insurance coverage if he has failed to purchase terrorism coverage and his policy excludes coverage for terrorism-related losses. An insured may thus be in a position to successfully argue that an insurer's reservation of rights with respect to claims potentially giving rise to a loss from an "act of terrorism" raises a conflict entitling the insured to independent counsel.

V. CONCLUSION

Losses that result from acts of terrorism can be both substantial and widespread. Law firm clients who have directly sustained these losses may well seek compensation from their attorneys whose errors or omissions contributed to the loss, even if the predominant cause of the loss was an act of terrorism. This fact alone should cause law firms to consider whether their possible involvement in these types of losses warrants obtaining insurance coverage to cover that risk.

The need for law firms to evaluate their requirements for professional liability coverage which includes coverage for losses caused in part by terrorism-related incidents is an ongoing one. Awareness of these issues is particularly important now in light of the ongoing debate over the extension of TRIA after December 31, 2005. To the extent that TRIA is modified — particularly with respect to its definition of "act of terrorism" — law firms must analyze the impact of any such modification on their professional liability coverage, especially if their insurer has excluded losses resulting from a TRIA-defined "act of terrorism."