

A Summary of Exclusion 6 of the B.C. Lawyer's Compulsory Professional Liability Insurance Policy (the "Policy")

Introduction and background

Exclusion 6, the 'business and benefit' exclusion, removes coverage for claims that arise from a lawyer's business activities or losses rather than professional services. Coverage is also excluded for claims that arise from professional services provided to a lawyer's family. Both scenarios present an undue risk to the insurance fund for several reasons. The lawyer's personal interest may well lead to more casual, less thorough, service and clouded judgment, increasing the likelihood of a successful claim. It also increases the risk of paying defence costs because the lawyer is more likely to become the target of a disgruntled party in the matter. Finally, our ability to successfully defend a claim is further compromised by the lawyer's desire to assure a claimant's recovery.

This summary is intended to assist lawyers in understanding how the Exclusion operates in relation to negligence claims, and includes an explanation of its application to trusts. Information is also provided about a due diligence process to disclose activities that may trigger the Exclusion, along with a sample questionnaire.

Coverage for any claim or potential claim is determined by the Policy wording. If you would like our position on the application of the Exclusion to a particular set of circumstances, please contact one of our advance ruling advisors, Surindar Nijjar, Kate McLean, Coran Cooper-Stephenson or Margrett George. Depending on the nature of your question, we may ask you to send us a detailed description of the circumstances, in writing.

Bolded or italicized words are defined in the Policy, and the following abbreviations are used:

- "family" or "family member" refers to spouse (including *common-law* spouse), children, parents or siblings
- "colleagues" refers to law firm partners, associates or associate counsel
- "interest or control" refers to effective management or control or beneficial ownership in an amount greater than 10%

Exclusion 6.1 - the "benefit exclusion"

Exclusion 6.1 of the Policy states that the Policy does not apply to:

- "6. a **claim:**
- 6.1 arising out of an **error** of an **Individual Insured**, the payment of which would benefit, in whole or in part, directly or indirectly, the **Individual Insured** or the **Individual Insured's family** or **law firm**, provided that this Exclusion 6.1 does not apply to any benefit derived solely from the ownership of an **organization;**"

As a result, you will not have coverage for a claim the payment of which would personally benefit you, your family¹, or your law firm.

¹ Since the Exclusion relating to *common-law spouse*, parents and siblings was introduced for the first time in the 1991 Policy, this provision was "grandfathered" so that the Exclusion would not apply to claims brought by a *common-law spouse*, the parents or the siblings of the lawyer if the services giving rise to the claim occurred before January 1, 1991 (see Exclusion 6.3 of the Policy).

Examples of how the exclusion applies are as follows:

- You act for your father in a personal injury action leading to a settlement. Your father talks to his neighbours months later and develops “settler’s remorse”. He sues you alleging professional negligence in the handling of his claim resulting in an improvident settlement. This claim would not be covered as payment of it would directly benefit your father;
- Your spouse borrows funds from a business associate and you prepare and register a mortgage over the matrimonial home to secure the debt. The mortgage goes into default and there is insufficient equity to repay the debt. The business associate sues your spouse for the shortfall, and you, claiming she relied on you qua lawyer to provide appropriate security for the loan. There would be no coverage for this claim as the payment of it would directly benefit your spouse by discharging your spouse’s obligation to repay the loan. It would also benefit you on the basis that a financial gain to your spouse would be to your indirect advantage.

The exclusion most often arises when you act for yourself or a family member on a personal matter, although it may arise when you act for a client unrelated to you². Further, although in-law, step and other relationships fall outside the Policy’s definition of ‘family’, the exclusion may still be triggered. For example, if you act for your brother-in-law on a matter, payment of any claim may well directly or indirectly benefit your sister.

Exclusion 6.2 - the “business exclusion”

Exclusion 6.2 of the Policy states that the Policy does not apply to:

6. a **claim**:
 - 6.2 by or in any way connected to any **organization** in which:
 - 6.2.1 the **Individual Insured**;
 - 6.2.2 the **Individual Insured’s family**; or
 - 6.2.3 the partners, associates or associate counsel of the **Individual Insured** or of the **Individual Insured’s law firm**;

individually or collectively, directly or indirectly, had at the time of the **error** or thereafter, effective management or control of the **organization** or beneficial ownership of the **organization** in an amount greater than ten percent (10%), provided that with respect to any payment resulting from a **claim** that falls within Part B of this policy, this Exclusion 6.2 applies only to exclude the **ineligible portion** of such payment.”

As a result, you will not have coverage for a claim that is by or in any way connected to³ any *organization*⁴ that is partially owned, indirectly or directly, or managed or controlled by you,

² For example, if you are acting for a business that owes you, your family or your law firm a debt (not legal fees), payment of a claim to the business will constitute a “benefit” if the business, otherwise not viable, is now able to repay the debt.

³ It is not necessary that the *organization* be the claimant. More often than not, it is a third party, such as an investor, financial institution or joint venture, who is advancing a claim against both the *organization* in which the lawyer has interest or control and the lawyer.

your family or your colleagues, either alone or together. Whether you have “indirect” or “beneficial” ownership of an *organization* depends on the actual circumstances of ownership at the time the services were provided and the claim is advanced. Examples of indirect and beneficial ownership that would trigger the exclusion are:

- You and your spouse own all the shares of Holding Co, which owns 50% of the shares of ABC Co, which in turn owns 25% of the shares of DEF Co. Any claim arising from your provision of legal services to ABC Co or DEF Co would not be covered;
- You and your sister are the sole contingent beneficiaries of FamTrust Co, a trust set up by your father who has rolled all the shares of ABC Co into it. Any claim arising from your provision of legal services to ABC Co would not be covered.

Whether you, your family or your colleagues exercise “effective management or control” also depends on the particular circumstances present at the time the services were rendered and the claim is advanced. In investigating effective management or control, the Insurer will consider a number of factors, for example:

- whether you, your family member or your colleague (referred to as “you”) is an officer or director of, or employer in, the *organization*, and if you are a director, how many other directors the organization has;
- whether the *organization*’s other directors look to you for guidance and generally accept the advice given;
- whether your shareholdings, alone or in conjunction with that of others under your influence, or your financial contributions, are sufficient to elect a majority of the Board of Directors or maintain de facto control of the *organization*; and
- whether you have day to day management of the *organization*’s affairs.

Optional business innocent insured coverage (“BIIC”) may be purchased from the Law Society. BIIC provides coverage to innocent lawyers who may be vicariously liable for another lawyer’s acts, but have no insurance under the negligence provisions of the Policy because of the operation of Exclusion 6.2. BIIC **does not** provide any insurance coverage for Exclusion 6.1, the benefit exclusion.

Application to trusts

Although the definition of ‘organization’ is very broad, it does not include trusts. As a result, you are free to provide legal services to your partner’s family trust, for instance, without concern that your partner’s relationship with the trust itself might trigger Exclusion 6.2. However, Exclusion 6.2 may still apply if, for instance, there is another organization related to the trust that is owned, controlled or managed by you, your family or your colleagues. Further, Exclusion 6.1 may apply. For example, 6.1 will be triggered if you provide legal services to or act as trustee in relation to your own family trust. Although neither Exclusion will apply if you provide, either directly or through your firm, legal services in relation to an arms-length trust of which you are also a trustee, providing both types of services does increase the risk of claims. More information on this risk is provided in the second part of [Executors, trustees and other fiduciaries](#).

⁴ Broadly defined in the Policy to mean “any business, business venture, joint venture, proprietorship, partnership, limited partnership, cooperative, society, syndicate, corporation, association or any legal or commercial entity”.

Due diligence

Firms may wish to implement a due diligence process to try and discover whether or not any of the lawyers at their firm (including partners, associates and associate counsel) are providing legal services in circumstances that would trigger the application of Exclusion 6, if a claim or potential claim arose. To assist, we have developed a questionnaire that firms may wish to incorporate into whatever due diligence process they use. The questionnaire is intended as an aid only, and may not succeed in disclosing all potentially offending activities. If any offending activities are disclosed, your firm will need to decide whether or not to continue providing the services, given that coverage will not be available. Use of the questionnaire by a firm will have no bearing on whether or not any claim or potential claim is covered under the Policy. A copy of the questionnaire is attached.

Summary

On personal matters – matters that do not involve an *organization* – if your family members require legal advice or services for personal matters, you should not act. Your colleagues, however, may.

On business matters – matters that involve an *organization* – consider if the legal advice or services required involves an *organization* in which beneficial ownership in an amount greater than 10% or effective management or control is, or may be, held, directly or indirectly by you, your family or your law firm colleagues, alone or together. If you or any other lawyer or lawyers at your firm have the offending interest or control, then no one at the firm should act. If your family has the offending interest or control⁵, another lawyer at your firm can act, but you should not.

If you as the lawyer handling the matter have coverage, then your firm will have coverage. If you fall within the Exclusion, you will not have coverage, and neither will your firm⁶. Neither defence nor indemnity coverage will be available. Protect yourself. Have one of your colleagues provide legal services for you or your family on personal matters, or retain outside counsel. On business matters in which no one at your firm can act, retain outside counsel. And appreciate that even if the Exclusion does not apply, there are still risks in acting for family on personal or business matters. Read '[About to act for family or friends? \(Resist, it's just too risky\)](#)' before you agree to act.

⁵ Note that if your family, together with you or your law firm colleagues, has an offending interest or control, another lawyer at your firm can still act (but not you) provided that neither you nor your law firm colleagues, either alone or together, have an offending interest or control.

⁶ Condition 6.3 of the Policy extends limited coverage for a lawyer's former partners (although not the lawyer) in circumstances where, for example, the lawyer acts for an *organization* and later moves in-house, acquiring beneficial ownership in an amount greater than 10% or effective management or control of the *organization*.

B.C. Lawyers' Compulsory Professional Liability Insurance Policy
Questionnaire

Exclusion 6 of the Policy excludes coverage for a claim against you in two circumstances:

1. If payment of the claim would personally benefit you, your **family**, or our firm (6.1);
2. If the claim is by or in any way connected to any **organization** that is partially owned, indirectly or directly, or managed or controlled by you, your **family**, or any other lawyers at our firm, either alone or together (6.2).

To help us avoid finding ourselves facing a claim for which there is no coverage under the policy, would you please answer the following questions. If you answer 'yes' to any question, please provide details on a separate page. Bolded words are defined as follows:

“Organization means: any business, business venture, joint venture, proprietorship, partnership, limited partnership, cooperative, society, syndicate, corporation, association or any legal or commercial entity.”

“Family means: spouse (including **common-law spouse**), children, parents or siblings.”

“Common-law spouse means: a person not married to the lawyer, who has lived with the lawyer in a marriage-like relationship, including a similar relationship between persons of the same gender, for a period of not less than one year.”

1. Are you providing any legal services for your own personal benefit, or to your **family**, or to our firm (other than services relating to a client's payment of our legal fees)?

Yes/no (please circle one).

2. To the best of your knowledge and understanding, is any other lawyer at our firm providing legal services for that lawyer's own personal benefit, or to that lawyer's **family**, or to our firm (other than services relating to a client's payment of our legal fees)?

Yes/no (please circle one).

3. To the best of your knowledge and understanding, are you providing legal services to any **organization** in which you, your **family** or any other lawyer at our firm, separately or together, has or had effective management or control or beneficial ownership in an amount greater than 10%?

Yes/no (please circle one).

4. To the best of your knowledge and understanding, is any other lawyer at our firm providing legal services to any **organization** in which that lawyer, that lawyer's **family** or any other lawyer at our firm, separately or together, has or had effective management or control or beneficial ownership in an amount greater than 10%?

Yes/no (please circle one).

Submitted by: _____ Date: _____