

## Legal expense insurance

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*Though perhaps not as inevitable as death and taxes, the chances of being involved in a law suit is ever-present – for businesses and individuals. So, it's not surprising the insurance industry has found a way of responding to the expense of being involved in a lawsuit: legal expense insurance.*

1. There are two basic types of legal expense insurance:  
Before-the-Event insurance (typically referred to as Legal Fees Insurance in Québec, and Legal Protection Insurance in Europe) and
2. After-the-Event insurance (which is sometimes called “Adverse Costs Protection” or, more generically, as “litigation insurance”).

Before-the-Event insurance is more common in Canada than After-the-Event insurance. But, After-the-Event insurance has grown faster than anticipated, according to Simon Gibson, VP and National Practice Leader at Aon Risk Solutions.



Background

Legal expense insurance [has been around since World War I](#). Barbara Haynes, CEO of DAS Canada, says that world-wide, the market for legal expense insurance is about € 9 billion, with most of it in Europe. Legal expense insurance has been [widely available in Canada since the mid-1990s](#), but it has really taken off since 2010, when DAS entered the Canadian market. DAS ([Deutscher Automobil Schutz](#)) is a subsidiary of ERGO, which is part of Munich Re.

Haynes estimates that when DAS arrived in Canada the market for Before-the-Event insurance was Cdn \$3-4 million. In the short time since [DAS Canada](#) has been offering it, it has grown to about Cdn \$50 million, according to Haynes. And, based on the per capita spend in Europe, Haynes estimates that Before-the-Event represents a Cdn \$500 million opportunity here.

“I see it a little like travel or D&O was 15 year ago,” explains Haynes. “It’s a niche product that has to be sold, rather than bought. In other words, there isn’t a government or bank saying you’ve got to have it. But, as awareness grows, I think it’s going to become more commonplace,” she says.

Given how litigious society has become and given the high cost of legal fees, the Canadian Bar Association and others involved with access to justice see Before-the-Event insurance as a way for regular Canadians to be able to afford to protect themselves and to enforce their legal rights and claims. As the Barreau du Québec puts it, [“This small investment \(in legal fees insurance\) can pay large dividends](#) because it allows you to stay informed about your rights and obligations and, if necessary, to defend your rights!” In 2014 DAS Canada reported that 63% of survey respondents indicated that the cost of seeking legal advice is the main reason they wouldn’t meet with a lawyer to discuss a legal situation they face, and half of those surveyed don’t feel they have the resources to hire a lawyer. So, the cost of legal services is clearly a barrier to access to justice.

Before-the-Event insurance is by far the more well-known type of legal expense insurance. One reason for this may be that After-the-Event insurance is relatively new here in Canada. For example, DAS has only been offering it here since 2013.

### **Before the Event (BTE) Insurance**

As its name implies, BTE insurance responds to unforeseen legal events that crop up. Like other types of insurance, “you buy it ‘in case something happens’,” says Haynes.

BTE is available for individuals and businesses. Haynes says that on the commercial side, customers tend to be small to medium-size enterprises – the kind of business that doesn’t have in-house counsel.

So long as the type of case is covered, the insured’s expenses are covered, whether they’re bringing the action or defending a suit brought against them. The legal expenses covered include:

- the insured’s lawyer’s fees,

- disbursements (including expert witness fees),
- court costs, and
- the opposing side's legal costs a court may order the insured to pay (these are often referred to as adverse costs).

BTE does not cover the cost of damages the insured might have to pay if unsuccessful.

### **Elements of Coverage for Typical BTE Policies**

The types of legal matters covered by BTE is surprisingly broad. For example, [DAS's commercial BTE policies typically cover:](#)

- Employment disputes
- Contract disputes
- Tax Disputes (audits and appeals)
- Violations of certain statutes, for example, anti-spam laws
- Suspension or cancellation of business-related licenses
- Property issues, for example, to pursue claims related to physical damage and trespass
- Defense in certain criminal prosecutions, for example, for breaches of occupational health and safety legislation

For individuals, [DAS's BTE typically covers:](#)

- Employment disputes
- Contract disputes
- Tax Disputes (audits and appeals)
- Bodily injury
- Property protection
- Highway Traffic Act infractions and protection of one's driver's licence
- Landlord-tenant disputes
- Defending one's self against criminal prosecution at work

One way insurers combat adverse selection is by imposing a waiting period on coverage of certain types of claims. For example, the policy may require a 60-90 day waiting period on employment or contract disputes.

In addition to paying legal expenses on covered perils, most BTE policies also provide insureds with over-the-phone legal advice on any legal question. "Most policies come with legal advice on every topic. So, even though things like divorce and wills and estates aren't legal actions covered by most BTE policies, you can speak with a lawyer about such issues. They will speak to you quite extensively, but they won't give you an actual legal opinion or review documents. It's general legal advice on your issue," says Haynes. And, she notes that when DAS provides its BTE to a group or association, if members of that group tend to have special legal concerns, DAS tries to put members in touch with lawyers with special expertise in that area.

Haynes sees the telephone legal advice as an important feature of BTE. “We see the phone-in legal advice as a grass roots type of coverage. If you can solve the problem by getting legal advice early on, that can be really helpful. It’s really about risk-management. And, if the customer phones in to ask about a legal matter, if it can’t be resolved through such advice, they may find out they have an insured claim,” she says.

### **Who Provides the Legal Services?**

Under DAS BTE policies, for example, when an insured’s legal claim is covered by BTE, the insured doesn’t get to choose their lawyer; the insured is assigned a DAS Panel Lawyer. Panel lawyers are not lawyers that work in-house at DAS – they are independent but they have entered into an agreement with the insurer to provide services. Some insurers offer the option for the insured to choose their own lawyer, but for that privilege they usually charge an additional premium and cap how much they will pay toward the lawyer’s hourly rate, says Aon’s Simon.

“In some parts of Europe there is legislation that requires the free choice of lawyers. In Canada there’s no such legislation so what we have done is set up a panel of law firms across the country. They’ve got specialization in the areas we cover and we enter into a business agreement with them. There are service standards and fee tariffs and then we assign the lawyer to the insured and the lawyer proceeds with the matter,” explains Haynes. “The insured ends up getting the right kind of lawyer with the right specialty and the benefit of our negotiated prices,” she says.

In terms of lawyer-client privilege, Haynes explains that the DAS policy wording is such that the privilege is considered tri-partite. It means the insured has lawyer-client privilege with the assigned lawyer, but DAS has the right to certain information. “Generally speaking we’re not delving heavily into the circumstances of the particular claim,” Haynes says.

### **Initiating – and Continuing – a Claim**

Most BTE policies do not pay legal expenses the insured might have incurred before notifying the insurer, nor will they cover legal disputes that existed before coverage takes hold. So, insureds who think they might have a claim begin by phoning the telephone legal advice line to discuss the matter. If the lawyer on the legal advice line doesn’t think the insured has a claimable issue, the lawyer will provide general advice and recommend next steps. If the lawyer believes the insured’s issue is eligible under the policy, the file is forwarded to the insurer’s claims department

BTE generally only covers legal expenses if the case has a reasonable prospect of success. DAS, for example, does not apply the “prospects of success” test to criminal defense matters covered by BTE because, according to Haynes, “you don’t really know which way it’s going to go until it’s over and everyone is innocent until proven guilty.”

“For civil matters, it has to be more likely than not that a case will be successful for us to assign a lawyer and proceed with litigation. We don’t want somebody embarking on

something that doesn't have a cat in hell's chance of being successful," says Haynes. "It's also important for insureds to understand that just because a claim is covered, it doesn't mean that the matter will necessarily proceed to trial. Given the cost, time, stress, and uncertainty of going to court, the majority of disputes are settled by out-of-court negotiation," she adds.

If the insurer concludes the prospects of success do not warrant proceeding with the case and the insured disagrees, the insured can seek a second opinion. If the lawyer giving the second opinion believes the insured has a reasonable prospect of success, the consultation with the second lawyer may be covered, according to Gibson of Aon.

### **BTE Premiums and Coverage Limits**

Because legal fees are high and they can add up quickly, typically BTE coverage limits range from \$100,000 to \$200,000 per claim, but higher limits are available. And, if a covered legal claim that began in one year continues over subsequent years, it continues to be covered until it is resolved. Premiums depend on coverage limits and whether the policy is purchased on a stand-alone basis or if it's built into another policy. "If a small business is purchasing a policy on a stand-alone basis, it's generally a bit more expensive," explains Haynes. "The reason for that is we've seen more frequency (of claims) if somebody buys the policy separately. For such policies, you could be looking at a premium of \$1,000-\$1,200 for \$200,000 of coverage."

Though Haynes notes that not many cases end up approaching the limits of indemnity, if a matter does, the insured may be able to arrange with the lawyer to continue to work at a discounted rate. And, if the insurer is pretty confident the insured will prevail in the matter, the insurer may agree to cover costs in excess of the limits of indemnity in the hopes of getting cost recovery, according to Haynes.

### **Purchasing BTE**

In Canada, BTE insurance is usually purchased from a broker rather than directly. Though it can be purchased on a stand-alone basis, it's generally purchased with other coverage. For example, [Square One homeowners' policies](#) make legal expense protection available as part of their national home insurance offering and [Peace Hills Insurance began offering DAS's coverage](#) on homeowner, condo, and tenant policies Alberta in November 2017. As well, BTE coverage is often available through professional associations and organizations as a member benefit.

The issue of adverse selection is one of the reasons stand-alone policies are not as common. "If a client is buying BTE on a stand-alone basis, more often than not they've had some litigation experience before. If that's the case, that's reflected in the premium," says Gibson. He says Aon typically sells BTE insurance as part of a package of insurance or as part of an program for an industry or class of business.

“The great thing about BTE is that it doesn’t discriminate based on what type of company you are or the type of profession you are in – the elements of cover provided under the insurance will typically have value and will respond to an appropriate risk. It’s up to the broker to unearth that exposure or highlight the risks and how the policy would respond. Likewise, with a property trespass dispute – for example, someone frequently occupying a landowner’s parking spaces – most wouldn’t know they can take proactive steps of getting an injunction or cease and desist order,” Gibson explains. “Once you uncover for them some of the risks that the policy would cover, it becomes a pretty easy sell.”

## **Underwriting and Claims Management**

Like any other insurance, in terms of underwriting BTE, insurers focus on frequency of claims and claim severity. Aon’s Gibson says that “If the potential insured had two or more legal disputes in the past three years, the underwriter will try to unearth what their litigation exposure looks like. To get a picture of the risk, they’ll look at what types of cases they were, what the outcome was, and how much was spent on the litigation. The two key variables in underwriting a BTE policy are the payroll and gross revenue of a company or organization, or their operating budget if we’re looking at a municipality. That information will help you gage the two key elements of exposure on BTE: employment disputes and contract disputes,” he says.

But, according to Haynes, though there’s some disparity in terms of claim frequency by different groups (for example, contractors tend to be more prone to having contract disputes), the disparity between insureds is not as pronounced with BTE insurance as it is with other types of property insurance. Claims management is more important when it comes to BTE, according to Haynes. Determination of “prospects of success” is key, as is ensuring the quality of panel lawyers.

I asked both Haynes and Gibson whether insurers are keeping an eye on the potential for increased harassment or discrimination suits against employers in light of the “#metoo” movement. Haynes says that at this point, that seems more of a potential issue in the U.S. and that it might come up under the criminal defense coverage. Gibson says he thinks that the issue may not end up having a big impact on insurers because they “have comfort in the fact that for these civil disputes, there is the caveat that there has to be reasonable prospects of success. So, they’re not going to be defending every suit. They’ve got that assessment built in. Also, for the policyholder, they have the final say on whether the policy extends to certain individuals. If they had a certain individual they didn’t want to defend if it’s a criminal charge, they can decide the policy isn’t extended to them. This is something they can declare at the point of claim,” he says.

## **Québec’s Legal Fees Insurance**

Insurance to cover the cost of legal fees has been available in Québec since at least the 1990s. The Barreau du Québec (the Québec law society) has been a strong advocate for it since it was introduced.

Legal fees insurance is similar to BTE, though it generally has much lower limits. It's available for individuals and small businesses and it covers the insured's legal expenses, including disbursements. The insurance is meant to cover "day-to-day" situations, including employment disputes, contract disputes, workers' compensation claims, landlord-tenant issues, and so on.

There are some noteworthy differences between the typical Québec legal fees insurance and BTE, including the following:

Covers some non-dispute matters – Québec legal fees insurance usually provides up to \$1,000 for costs incurred in estate or personal protection matters.

Doesn't cover opponent's legal fees – Because it's extremely rare for Québec courts to order a losing party to pay the legal fees of the other party, legal fees insurance usually does not cover such costs.

Insureds choose their lawyer – under Québec legal fees insurance policies, insureds are allowed to hire the lawyer of their choice. The insured then submits the invoice to the insurer for reimbursement.

Coverage limits are quite low – Québec legal fees insurance typically covers up to three matters per year and the maximum cost per case is \$5,000 (with a total annual payout limited to \$15,000-\$25,000). Because the limits of coverage are considerably lower than typical BTE policies, the premiums for legal fees insurance are also considerably lower.

### **After the Event (ATE) Insurance**

ATE insurance – in contrast to Before-the-Event insurance – is designed to protect the insured in situations where a claim has already arisen. It protects the insured (the plaintiff) in the event the plaintiff loses the case. According to Dominique Zipper, Manager, After the Event Insurance at DAS Canada, losing means the plaintiff is awarded zero dollars or is awarded less than the defendant's last offer to settle.

If the plaintiff (the insured) loses, ATE pays:

- disbursements the insured's lawyer incurs in pursuing the action, and
- adverse costs the court may order the insured to pay.

If the plaintiff wins, typically they're awarded damages and costs. In that case, the disbursements incurred by the insured in pursuit of the case are paid out of the damages the plaintiff was awarded. But if the insured loses, the ATE insurance pays the disbursements and adverse costs, if awarded.

DAS's Haynes admits that given the uncertainty and length of time lawsuits take, "ATE is a challenging class of business from a cash-flow perspective and capital, but it's been offered for a long time."

## **Cases ATE Insurance is Available For**

ATE insurance is generally only available for cases taken on a contingency basis. According to Zipper, the reason ATE is limited to contingency cases is because the insurance is basically underwriting the lawyer's judgment, so the insurance company wants the lawyer to have a vested interest in the litigation proceeding. In essence, the willingness of the lawyer to take the case on a contingency basis amounts to the lawyer determining the matter has a reasonable prospect of success. As Zipper notes, lawyers do not spend time on cases with low prospects of success.

The most widely available ATE insurance is for personal injury. Interestingly, though most would consider medical malpractice a type of personal injury, some insurers (DAS Canada, for example) specifically exclude medical malpractice cases, as the loss experience differs from other types of personal injury cases. According to Zipper, one reason DAS excludes medical malpractice is that the Canadian Medical Practitioners Association (CMPA) aggressively defends its members because of the reputation risk to the doctor and the hospital. She also says it's very difficult to get a settlement in medical malpractice cases and it takes a long time. Also, the loss experience is not the same as for other types of personal injury.

ATE insurance is available in Canada for civil litigation, ranging from personal injury, medical malpractice, class actions, mass torts, and a variety of complex, one-off commercial litigation cases. Aon, who acts as a broker for DAS, uses Axis and Lloyds for ATE coverage for medical malpractice cases as well as civil litigation, according to Gibson. It's also possible to get ATE policies for clients who are defendants, though it's rare, acknowledges Gibson.

## **How Clients Obtain ATE Coverage**

ATE insurance is available to clients only through lawyers. With respect to DAS ATE personal injury coverage, for example, it is only available through lawyers who have entered into a delegated authority agreement with DAS. Normally the client must agree to ATE insurance within six months of signing the contingency agreement with the lawyer. Insurers sometimes allow insureds to be signed up after that, but Aon's Simon says the client usually has to have signed up for the insurance more than 180 days before their case goes to trial. "If you're less than 180 days from trial, it's a pretty good bet you're going to proceed to trial and that's when the risk is heightened," explains Simon. "Before that stage, the prospects of success might have been 75%, but when you go to trial, the prospects might drop to, say, 50/50," he says.

In signing up a client for ATE insurance, DAS expects the lawyer to confirm that they believe the case has greater than a 51% chance of success. And, during the course of the litigation, if the prospect of success drops below that, the lawyer must let DAS know. If the prospects drop below the threshold, Zipper says DAS suspends coverage. She says that if coverage is suspended, DAS is on the hook for costs incurred up to that point because it doesn't want to leave the law firm at a loss, but the plaintiff is on the hook for costs



incurred after the suspension. If, at a later stage, the prospect of success returns to above the 51% threshold, DAS reinstates coverage.

When DAS first introduced ATE coverage in Canada, they spent a fair bit of time educating lawyers about the benefits of the coverage. But, as word about ATE spread, lawyers started taking notice. Zipper says that DAS Canada now has about 130 law firms with delegated authority.

“I’ve seen a shift in the last six months,” says Gibson. “We’ve actually started to receive an increased number of inquiries from law firms, rather than the other way around. That’s a tip of the cap to DAS – they’re almost synonymous with this kind of insurance in Canada and that reputation has filtered through,” he says. “DAS often fields the call and then they advise the lawyers about what brokers are actively selling their products. So, we get calls from lawyers referred to us through DAS and we also get calls from lawyers who are just Googling ‘After the Event’ insurance or they come to us by way of our website or by referral,” he says.

“And, at industry events – like the Trial Lawyers’ Association conferences – the conversation has gone from ‘what is this insurance?’ to ‘I understand what this insurance is and I’d like to hear a bit more about it.’ And most recently I’ve had lawyers say to me ‘I know about this insurance and our firm should be doing something about it.’ We’re definitely finding increased due diligence by the law firms,” Gibson says.

Some law firms see the ability to offer their clients ATE insurance as something that gives them a competitive advantage. Zipper also believes one of the main reasons lawyers are interested in having delegated authority to offer ATE is because they see such insurance as a risk management tool. She notes that the lawyer isn’t earning anything by offering this insurance, but it’s a professional negligence avoidance tool for them. They’re potentially providing their client peace of mind that they won’t be liable for potential costs if the plaintiff loses and the lawyer will recover their disbursements, she says.

Though insurers will give a lawyer or law firm delegated authority for a single case, usually the delegation extends to all future cases the lawyer takes on. Under the delegated authority, the law firm has the authority to bind risk on behalf of the insurer. Canadian insurers often offer to bind the firm’s entire book of cases as far back as five years. In the UK, where the ATE insurance market is quite mature, insurers only insure new cases that come in, they no longer write law firms’ older book of business. So, as the market matures here, it’s likely Canadian insurers will follow suit, but for the time being, insurers are offering this as incentive to get law firms on board.

### **Premiums and Commissions**

Because ATE insurance follows the personal injury business model, just as the lawyer’s fee is contingent on success, the premium is contingent too. ATE premiums are:

- deferred until the conclusion of the action, and

- only paid if the plaintiff prevails in the lawsuit.

If the plaintiff loses the case, the insurer waives the premium but the insurance responds, paying the disbursements and adverse costs, if any. Zipper explains that the rationale for this treatment is that when plaintiffs go to see a personal injury lawyer they don't have to pay any money up front. And, because personal injury lawyers advertise "you don't pay unless you win", clients expect to not have to fork over any money until the very end, when their lawyer takes a cut. So, the insurer only takes the ATE premium if the plaintiff gets money.

Premiums for DAS ATE ranges from \$1,000-\$2,000 for Cdn \$100,000 of coverage. Interestingly, until 2015 DAS had different premium rates for ATE coverage on motor vehicle accidents than for all other personal injury cases. But, according to Zipper, they found little difference in payment experience, so they no longer differentiate between the two types. Aon's Gibson, who places ATE offered by a variety of carriers and for a variety of types of cases, says premiums range from about Cdn \$1,000 to hundreds of thousands for complex cases (for example, class action suits).

Given the relatively low cost and the fact that the premium is deferred, it seems hard to believe that any plaintiff would decline such insurance, but it happens. "We tend to think of personal injury awards as being big, but they're not always that big," says Haynes. "If you're awarded damages of \$30,000, the premium becomes a bigger percent of the award and so some plaintiffs simply think, 'I'll take my chances'," she says.

As further evidence that ATE is modelled on the personal injury lawyer's business model, brokers who get personal injury lawyers to accept delegated authority usually only collect a commission at the conclusion of the case and only if the insured prevails. In other words, the broker doesn't get a commission unless the insurer collects a premium.

Gibson notes that though in most cases the broker's commission is contingent, there are some variations. "For medical malpractice, commercial litigation, or class action cases, for example, we have the ability to offer different options of payment. It might be a flat fee up front that's non-contingent. If the insured is paying on that basis, they typically have a reduction in the premium. The rationale for the reduced premium is that the insurance company is getting an amount regardless of if the insured wins or loses," he says.

### **Underwriting ATE Policies**

On ATE policies, underwriting focuses on the skills and qualifications of the lawyers that are given delegated authority. Zipper explains that DAS is putting its risk in the hands of the lawyer whose book of files it is insuring. They're underwriting the lawyer's legal judgment and so the insurer looks at things like: How often do the lawyers go to trial? How many cases have they lost? How many cases have been abandoned? The goal is not to go to trial that often, but to have the legal judgement to proceed if you need to, she says. DAS works with some law firms that have a reputation as being "settlement firms", some that are considered "trial firms", and some that are mixed. But, she stresses that most files

should not be going to trial because the court system is overburdened and there aren't enough judges to go around. Zipper, who used to be a litigator, notes that if the lawyers are doing their job, most cases should settle.

DAS also looks at the law firm's business model. Zipper says they don't want a firm that has so many cases per lawyer that lawyers don't have a personal relationship with their clients. When that's the case, it's more likely plaintiffs will abandon their cases and when that happens, DAS doesn't earn premium. Though the insurer doesn't pay claims on abandoned cases either, administratively it's not great when cases are abandoned because it leads to less predictability for the insurer.

During the course of litigation, the insurer monitors how the case is moving along and lawyers are expected to periodically report to the insurer. Zipper says that DAS monitors updates from lawyers, as predictability of a portfolio's loss experience helps DAS determine its future premium earning pattern.

## **Conclusion**

Many people think other types of insurance, for example commercial policies, provide sufficient protection to insureds in the event of a legal action, but there are lots of gaps. Legal expense insurance fills many of those gaps. And, to the extent there may be overlap, for example, with some D&O policies or employment practices liability insurance, those policies often have fairly high deductibles. Since BTE doesn't have any deductibles, insureds will still benefit from BTE coverage alongside their other policies.

Concerns about the cost of legal expenses is real, and well founded. In a [2015 Ipsos poll conducted on behalf of DAS](#), 73% of Canadian small business owners indicated that legal disputes would have a tangible financial impact on their business. Three in 10 Canadian small business owners indicated they were somewhat worried about being sued, but only 12% of Canadian small business owners felt they have sufficient insurance coverage if sued. Perhaps the most interesting statistic the survey revealed is that nearly six in 10 Canadian small business owners said they would purchase BTE if offered such coverage.

Given that ATE is still relatively new in Canada, most agree that there's room for growth. Unlike in countries like the UK, where the market is mature and there aren't many law firms that haven't entered into delegated authority agreements, there are still plenty of Canadian law firms that have not yet gotten on board.

A recent Ontario superior court case may also prompt growth in the ATE market. In that case the court held that if an insured prevails and the court awards the insured costs, the [ATE premium is a recoverable disbursement](#). The court basically held that the cost of ATE is a reasonable cost a plaintiff might incur to support the cost of litigation. This decision should encourage plaintiffs to take out ATE insurance, given that they might be able to recover the cost of the premium.

And finally, Aon's Gibson thinks there's also room to expand the types of cases that might be covered by ATE. For example, he thinks there may be increased interest in ATE insurance for civil litigation that's not contingency fee based.

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