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PROFESSIONALLY SPEAKING

NEWS & INSIGHTS

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Wilson Elser's newsletter features articles written by the firm's Professional Liability & Services Practice attorneys.

Professionally Speaking explores current topics of interest to general counsel, claims professionals and risk managers for various professional liability lines, including accountants, lawyers, design professionals, insurance brokers and others.

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You've Been Served… Tips for Accountants Handling Subpoenas

By Rebecca Gelozin

A subpoena is a common legal document that can be served on an accountant or firm whether they are a party to a case or a target of an investigation. Accountants are among the most subpoenaed professions. What should you do if you have been served?
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How Should Accountants Respond to Subpoenas?

By Rebecca Gelozin

In this video, Rebecca Gelozin discusses what accountants should do when subpoenaed
Watch the Video

Editors

Carole Buckner
Of Counsel
San Diego, CA
619.321.6205
carole.buckner@wilsonelser.com

William McDevitt
Partner
Philadelphia, PA
215.606.3979
william.mcdevitt@wilsonelser.com

Daniel Tranen
Partner
St. Louis, MO
314.930.2862
daniel.tranen@wilsonelser.com

Contributors

Carole Buckner
Of Counsel
San Diego, CA
619.321.6205
carole.buckner@wilsonelser.com

Joseph Francoeur
Partner
New York, NY
646.823.7791
joseph.francoeur@wilsonelser.com

Rebecca Gelozin
Partner
White Plains, NY
203.260.3902
rebecca.gelozin@wilsonelser.com

Eve Mouzouris
Of Counsel
New York, NY
516.519.2297
eve.soldatos@wilsonelser.com

Daniel Tranen
Partner
St. Louis, MO
314.930.2862
daniel.tranen@wilsonelser.com

Learn more about Wilson Elser's Professional Liability & Services Practice, visit our website.

Is an Attorney Liable in a Cybersecurity Incident Resulting in a Loss to a Non-Client?

By **Joseph Francoeur and Eve Mouzouris**

Cybersecurity threats to law firms are on the rise. Data breach lawsuits have been trending upwards and show no signs of slowing down. Considering the highly sensitive information they handle, it may come as no surprise that law firms are prime targets for cyberattacks. However, what is surprising is how these attacks can give rise to lawsuits and grievance complaints from non-clients against attorneys.

Typically, a non-client cannot sue an attorney for professional negligence or malpractice because the attorney's legal duties are restricted to their client (i.e., lack of privity). The lack of privity defense is used to protect attorneys, but cyber threats are wreaking havoc on this protection. This is especially true in "wire transfer" scams, where an email account is hacked by a cyber scammer who intercepts email communications involving a transfer of funds (litigation settlement, real estate purchase, corporate transaction) and provides fraudulent wiring instructions. We have seen a rise in claims for contribution made by the non-client against the attorney, who failed to call and confirm the accuracy of the wire instructions.

Despite the growing number of such claims, there is an absence of case law dealing with privity as a defense. This likely occurs for two reasons. First, "duty" is not a required element of a contribution claim, which makes privity irrelevant. Second, such cases are likely being settled due to the lack of any viable defense for failing to verbally confirm instructions before sending a wire. Worse yet, many malpractice policies now exclude claims for wire fraud, leaving attorneys who haven't procured a cyber policy exposed to liability and left without insurance coverage to deal with the damages.

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Nevertheless, the historical protection of privity is not entirely gone. In fact, New York courts are protecting lawyers when a non-client brings a legal malpractice claim against the attorney involved, but not the party responsible for verifying the wiring instructions. As detailed in the recent cases below, these claims are being dismissed for lack of privity.

In *Contour Mortgage Corp. v. Reverse Mortgage Solutions, Inc. et al.*, 605335/2022 (Sup. Ct. Nassau Cty. May 21, 2024), the attorneys representing the purchaser's mortgage lender emailed all parties to obtain the final payoff letter just prior to the closing. The seller's attorney emailed the real payoff instructions to the lender's attorney. However, on the day of the closing, a fraudulent email was sent impersonating the seller's attorney, which contained fake payoff instructions. The lender's attorney failed to verbally confirm the wire instructions before sending the wire, and over $350,000 was wired to the cyber scammer. The non-client lender brought a legal malpractice action against the seller's attorney, alleging that the firm breached the standard of care when it provided false, erroneous, and fraudulent information in the payoff letter. The Court granted the defendant seller's attorney's motion to dismiss, holding that no privity existed between the parties. The Court held that the seller's attorney was not retained by and had no relationship with the purchaser's mortgage lender. Therefore, any claim for legal malpractice was "meritless." The court emphasized that the seller's attorney "was not the entity responsible for wiring or confirming receipt of any funds at all."

In *First American Title Insurance Company v. Liberty Land Abstract Inc. et al.*, 600326-22 (Sup. Ct. Nassau Cty. July 25, 2022), the title insurance company's title agent agreed to serve as the title closer, settlement agent, and escrow agent in connection with a real estate transaction. At the closing, the seller's attorney provided the title agent with a payoff statement for the seller's mortgage. The title agent made a phone call to verify the information in the payoff letter but called the number

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on the false wire instruction instead of independently verifying the number before calling. Relying on the false instruction, the title agent issued a wire for over $422,000 to the cyber scammer. The purchaser filed a claim under its policy on the basis that the seller's mortgage was not paid off. The non-client title insurance company then brought a lawsuit against the seller's attorney, alleging common law indemnification, negligence, and professional malpractice. The court granted the seller's attorney's motion to dismiss, holding that the seller's attorney did not share a special or near-privity relationship with the title agent or the title insurance company, which would have otherwise given rise to an obligation or duty. Additionally, the court noted that the complaint contained no information alleging that the seller's attorney represented that they would "verify the accuracy of that payoff statement."

CONCLUSION

Attorneys who fail to confirm wire instructions properly may find themselves defending claims for contribution brought by non-clients. These claims are not likely to be afforded the protection of a lack of privity. Attorneys without a cyber policy may face these exposures without the benefit of an insured defense and indemnity. Attorneys should take care to always properly vet wire instructions – each and every time they send a wire. More importantly, attorneys must closely examine their insurance policies to determine whether they may be left out in the cold without coverage for these novel yet increasingly rampant claims.

For additional information, contact:

Joseph Francoeur
Partner
New York, NY
646.823.7791
joseph.francoeur@wilsonelser.com

Eve Mouzouris
Of Counsel
New York, NY
516.519.2297
eve.soldatos@wilsonelser.com

When Liability Appears Bleak, Pivot to Causation and Damages!

By **Daniel Tranen**

An old adage about legal strategy goes something like this: *when your case is weak on the law, pound the facts. When your case is weak on the facts, pound the law. And when your case is weak on the facts and the law, pound the table.*

We often are confronted with professional liability claims or cases where the defense on liability is weak and where the claimant can clearly articulate a set of damages and alleges negligence, i.e., the lawyer plainly missed the deadline and the underlying case was dismissed; the audited financial statements are clearly wrong, and someone lost a lot of money; or the insurance broker failed to procure the policy that they agreed to procure so the policyholder had to pay the claim out of their own pocket. When confronted with these types of claims or lawsuits, and when they include these devastating facts, we are inclined to throw up our hands and pay the claim or the settlement, often for the full value of the claimed loss. From a defense perspective, the facts seem to indicate that the case is a loser.

NOT SO FAST.

The question of negligence does not end with establishing a breach of duty and the existence of an injury. The claimant also must prove the combined elements of causation and damages to win the case. And sometimes, even with an obvious and indisputable mistake, that element – that the mistake caused the injury – can effectively be challenged.

In the first scenario listed above, even though the lawyer missed the deadline and the underlying case was dismissed, we still must determine if the underlying case could have been successful. If the merits of the underlying case can be effectively challenged, then the lawyer's mistake did not cause any actual loss to the plaintiff.

As an example, I defended a lawyer years ago who failed to timely file papers seeking a visa for a foreign national client to remain in the country, and she was deported. However, even though there was no question that the lawyer failed to do what was required, the case was thrown out by a Cook County, Illinois, judge because I established that the foreign national did not qualify for the visa sought or any other visa allowing her to remain in the United States, even if the visa papers were timely filed (the lawyer never took any payment for the work because of the mistake).

Similarly, an accountant who fails to properly audit financial documents such that there are clear errors

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in those documents will not be liable for accounting malpractice if the third party receiving the faulty documents cannot link any damages to its actual reliance on them. In other words, if the conduct that led to the damages was not based upon reliance on the financial records, and instead, the damages are based upon the poor performance of the company, a defense to the accounting malpractice claim may exist notwithstanding the clear breach of duty by the accountant.

For example, a bank may receive audited documents containing errors. Still, if the bank receives them after it has already loaned the money to the borrower for whom the audited financial documents were prepared, and the borrower defaults, there may be no causal link between the faulty financial documents and the bank's loss. Yes, the bank can say that it received financial documents audited by the accountant, and yes, the bank can point out that the borrower defaulted. But if the bank loaned the money *before* it reviewed the faulty documents, or if its employees never actually reviewed the faulty financial documents, then it did not rely on those erroneous documents when it loaned the money. And so, in this case, despite the accountant's clear error, there is no causation between the creation, and even the delivery, of the faulty financial documents and the bank's injury, which actually flows from the poor performance of the borrower and not any act or omission by the accountant.

In a typical scenario, an insurance broker who fails to procure insurance for a client can be liable for that failure. However, if the policy the broker was supposed to procure would not have covered the casualty anyway, based upon some exclusion or policy condition, then the failure to procure does not cause the policyholder to be damaged, notwithstanding the broker's error. Again, there might be clear evidence of negligence on the broker's part, but that negligent act must be the cause of the actual injury. Sometimes, the plaintiff or claimant simply cannot link the bad act of the insurance broker to the claimed damages, which must flow from the absence of the policy that the broker was to procure.

Thus, the next time you have a claim or lawsuit where the breach of duty is obvious, don't give up hope and immediately pay the demand. Analyze the combined elements of causation and damages. This is particularly important because claimants and plaintiffs tend to ignore these elements when they see an obvious breach of duty, and they've incurred an injury. However, the existence of an error and an injury by themselves is not enough to win a lawsuit. The injury must proximately flow from the professional's negligence to be compensable.

For additional information, contact:

Daniel Tranen
Partner
St. Louis, MO
314.930.2862
daniel.tranen@wilsonelser.com

Duties of Lawyers Advising Organizations Regarding Legal Risks to Constituents

By **Carole J. Buckner**

ABA Formal Ethics Opinion 514, released on January 8, 2025, provides important guidance concerning the ethical obligations of lawyers advising organizations regarding future conduct that may create legal risk for the organization's constituents. The Opinion notes the "complexity of the modern regulatory environment" and the "fine distinctions upon which the legality of a course of conduct may turn," as well as the possibility that a lawyer providing advice does not always possess all relevant information. A client organization's "constituents" can include officers, directors, managers, and, in some cases, the organization's shareholders. These are individuals with whom the organization's lawyer may interact but for whom the lawyer may not provide individual legal representation.

Traditional professional responsibility rules provide that a lawyer advising an organization represents only the organization and not its constituents. It is possible, however, that a lawyer may jointly represent the interests of the organization's constituents, subject to conflict of interest limitations and/or waivers. In cases where the lawyer does not represent the entity's constituents, the lawyer's ethical obligation is to the organization only, even though a lawyer's advice to an organization may be delivered through individual constituents. The Opinion stresses the importance of lawyers educating constituents about the scope of their representation and clarifying that their obligation is to the entity and not its individual constituents in most cases.

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When a lawyer is solely representing the organization, particularly in cases where the lawyer's relationship commonly includes communicating with constituents acting on behalf of the organization, the question arises as to what extent the lawyer must consider the interests of those constituents.

This question becomes particularly important when the organization engages in a course of conduct potentially exposing both the organization and its constituents to legal risk. In such a scenario, the organization client may decide to accept the legal uncertainty and related risk inherent in the conduct. At the same time, those risks may also impact the constituent, who is perhaps unable to comprehend the scope of the risk due to a lack of legal counsel.

One example discussed in the Opinion is when a lawyer advises the organization regarding representations to the government or a private entity, with a constituent signing the representations. The interests of the individual constituent and the entity may not align to the extent that those representations might create particular risks for the constituent. While the organization may intend to take a more aggressive position best serving the entity, that position may not be in the best interests of the individual constituent signing off on the representations. Importantly, given the lawyer's representation of the organization, the entity may invoke an advice of counsel defense unavailable to the unrepresented constituent.

ADVICE TO ORGANIZATIONS ABOUT RISK TO CONSTITUENTS

According to the Opinion, a lawyer is obligated to advise an organization regarding the legal ramifications of proposed conduct on the organization and may, depending on the gravity and extent of the risk, need to inform the organization of potential legal risks for its constituents, including employees, officers, and directors.

The Opinion also acknowledges that such analysis may involve increased expense. As such, an organization may not wish to solicit legal advice on the risks of proposed conduct on its constituents. The lawyer may concur with the organization in this regard and, with the organization's informed consent, refrain from providing advice.

RESPONSIBILITY TO NON-CLIENT CONSTITUENTS

When the constituent is a non-client, there is a risk that the individual will not understand that the organization's lawyer does not represent the constituent individually, and the constituent may fail to realize that their actions may have personal consequences. Although there is no one-size-fits-all disclosure, the Opinion suggests that the lawyer may want to disclose to constituents that they may incur personal legal risk if they act on behalf of the organization. As well, the lawyer should make clear that they are only advising the organization and not individual constituents and constituents should seek advice from their own counsel. This is particularly important when the lawyer knows or should know that the constituent's legal interests are at risk.

For additional information, contact:

Carole Buckner
Of Counsel
San Diego, CA
714.227.8183
carole.buckner@wilsonelser.com

You've Been Served…Tips for Accountants Handling Subpoenas

By **Rebecca Gelozin**

Accountants are among the most subpoenaed professions; accordingly, it should come as no surprise that there will likely come a time in an accountant's career when a process server or federal agent walks into the office, hands over documents and says "you've been served." Once the shock wears off, remember, it's just a subpoena – but now what?

Subpoenas can:

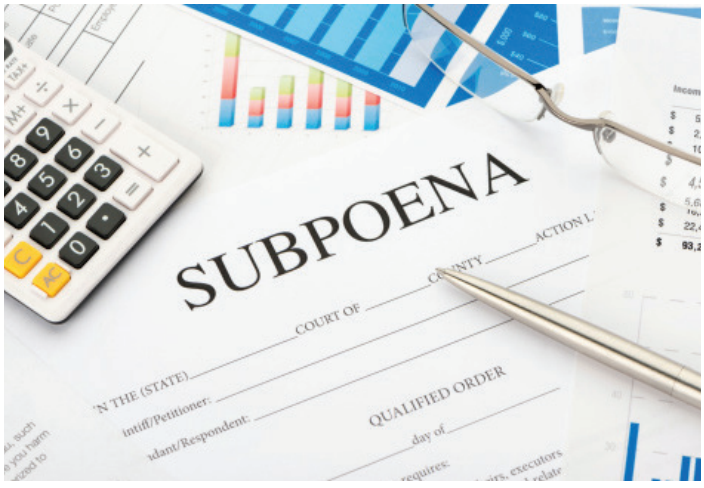
- Come in several forms: a discovery subpoena, a trial subpoena or a government agency subpoena.
- Be generated from civil litigation, criminal prosecutions or government investigations.
- Call for documents, testimony or both.
- Subpoenas generally are served because the issuing party does not have access to the documents or information the accountant maintains; however, subpoenas can be issued to confirm the veracity of documents or information already in the subpoenaing party's possession. Subpoenas can call for tax returns, accounting workpapers, communications with clients or all of the above. Whatever type of subpoena is received, it is important to recognize that each comes with a mountain of risk and should be reviewed carefully, and any responses should be positioned to protect the interests of the client and the accountant.

Upon receipt of a subpoena, the accountant should engage a knowledgeable attorney familiar with the accounting profession and its regulatory, ethical and legal obligations to assist in crafting a response. In addition, the accountant should review any existing errors & omissions policies to determine if specific subpoena assistance coverage is included, and consider contacting their broker or carrier, if appropriate

There is the possibility that the information produced by an accountant in response to a subpoena could form the basis of a subsequent claim of malpractice. Therefore, in response to every request for information or subpoena, an accountant should examine the engagement in question to assess the possibility of a lawsuit.

COMMON SUBPOENA ISSUES

Subpoenas served on accountants most commonly arise from civil litigation involving a client or former client. Whether the matter is a divorce between longtime clients or a business dispute involving a corporate client, civil subpoenas often are served on the parties' accountants to secure financial records and information about the client. However, many lawyers who serve subpoenas do not realize that, pursuant to I.R.C. 7216, tax return information is protected from disclosure in response to a civil subpoena. Accordingly, when a subpoena requests tax returns and related information, an accountant



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should advise the issuing attorney that an executed 7216 authorization form needs to be secured from the taxpayer authorizing such disclosure.

If the subpoena arises from a criminal matter, it is most likely a "grand jury" subpoena issued by a state district attorney's office or a U.S. Attorney's Office. The regulations implementing I.R.C. 7216 contain exceptions to allow for production of materials in response to grand jury subpoenas regardless of client consent.

In addition, I.R.C. 7525 provides for a limited tax practitioner privilege, and some states have passed evidentiary accountant-client protections similar to attorney-client privileges that raise additional complexities in responding to a subpoena.

SHOULD YOU TELL YOUR CLIENT?

Another question often raised by subpoenaed accountants is whether to inform the client that its records have been subpoenaed. Generally, there is no legal obligation on subpoena recipients to maintain the confidentiality of the existence of a subpoena. However, occasionally a subpoena is accompanied by a court order requiring confidentiality, which must be respected.

In other situations, especially with criminal or investigatory subpoenas, the subpoenaing agency "requests" that the accountant keep the existence of the subpoena confidential. These requests generally do not have the force of law, but there may be compelling reasons to comply. However, whatever the reason, confidentiality must be weighed against the accountant's duties to its client or former client.

COSTS OF RESPONDING

Ideally, every engagement should have an engagement letter that contains a provision whereby the costs incurred by the accountant for responding to subpoenas will be reimbursed by the client. Specifically, such provision should include attorney fees. Most clients recognize that if they are involved in litigation or another activity that causes their accountant to incur costs, the accountant should be able to bill them for the professional time spent dealing with the requests and the legal fees incurred to ensure proper compliance with the subpoena. To avoid disputes with clients, the accountant should consider providing for such fees in the engagement letter.

In some states, ancillary compensation is set by statute, in others it is limited to photocopying or similar expenses. In most cases, the actual costs incurred (expenses, lost professional time, attorney fees) are significantly greater than the usual compensation for services rendered.

CONCLUSION

Responding to subpoenas can present numerous risks to the unwary accountant. Divulging certain information at the wrong time in the wrong circumstances to the wrong parties can be a crime, an ethical violation or a breach of an accountant's duties to the client, leading to potential liability. Moreover, divulging information, properly or improperly, may provide a potential plaintiff with the ammunition to bring a malpractice claim against the accountant. Consequently, the best course when served with a subpoena is to contact legal counsel and notify the insurance carrier.

For additional information, contact:

Rebecca Gelozin
Partner
White Plains, NY
203.260.3902
rebecca.gelozin@wilsonelser.com

How Should Accountants Respond to Subpoenas?

In this video, **Rebecca Gelozin** discusses what accountants should do when subpoenaed.