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Professional Malpractice

Holding Lawyers Accountable for Bad Settlements

Will New Jersey follow Pennsylvania's lead and re-establish better client protection?

By Bennett J. Wasserman

How do you know when you have a good settlement? The folklore of the courthouse used to be: "If everyone walks away a little unhappy." That time-tested wisdom took a bizarre twist when the New Jersey Supreme Court decided *Puder v. Buechel*, 183 N.J. 428 (2005), which some say stands for the proposition that when a client settles a case, he waives the right to sue his attorney for malpractice in a subsequent action.

Prior to *Puder*, the New Jersey Supreme Court's decision in *Zeigelheim v. Apollo*, 128 N.J. 250 (1992), protected clients against attorney negligence, even when the underlying case settled. The *Puder* decision shifted that protection away from the client in favor of the lawyer whose negligence brought about the unsatisfactory settlement.

Three recent cases in New Jersey have started to erode *Puder* and reassert the *Ziegelheim* beachhead that once protected victims of attorney malpractice. Do these cases signify a move back to the days of *Ziegelheim* and the protection it afforded those clients victimized by shoddy lawyering?

Pennsylvania faced a similar problem, when, in 1991, the state high court decided *Muhammad v. Straussburger,* 526 Pa. 541 (1991), which shields attorneys from legal malpractice claims sounding in negligence or contract where they involve cases of completed settlements. Since then, the state's trial and appellate courts have successfully contained the *Muhammad* decision's destructive effect on a client's right to receive quality legal representation in settling a case. An examination of these decisions can shed some light on how New Jersey ought to address its own *Puder* problem.

In *Muhammad,* a 6-week-old infant died from complications of general anesthesia administered during a routine circumcision. An initial offer to settle was made for $23,000. The parents advised their lawyer that they would agree to accept it. At a later pretrial conference an offer of $26,500 was extended, at the suggestion of the court. That settlement figure was then accepted. Soon thereafter, and before the settlement was paid, the clients informed their attorneys that they were not satisfied with the amount. The defendants moved to enforce the settlement, which was granted. A legal malpractice action against their attorneys followed. While the Supreme Court disagreed with the defendant lawyer that the suit could not be barred by collateral estoppel, it then went on to affirm the dismissal of the legal malpractice suit on the basis of a longstanding public policy which encourages settlements unless the client can specifically plead and show that the lawyer fraudulently induced the settlement.

In 1993, an appellate court in Pennsylvania took the first step away from the *Muhammad* rule, in *Collas v. Garnick*, 425 Pa. Super. 8 (1993). There, a passenger sued her lawyer for malpractice for advising her to sign a general release settling her motor vehicle personal injury claims against the driver and owner of the vehicle with which she had collided. Her injuries were apparently exacerbated by the failure of the seat belt she was wearing and she contemplated suing the designer and manufacturer of the seat-belt system as well. She settled the motor vehicle case by signing a general release that discharged not only the defendant driver and owner but "all other parties, known or unknown, who might be liable for the damages sustained." The client then proceeded to sue the seat-belt manufacturer. That case was dismissed as being barred by the prior release. The client

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then sued her lawyer, alleging that the lawyer gave incorrect advice and negligently interpreted the language of the release.

Citing New Jersey's *Ziegelheim,* the *Collas* court said that if the defendant lawyer "was unfamiliar with the effect of a general release, he had a duty to conduct the necessary research to enable him to advise his clients regarding the effect of the contract about which the clients had requested advice." The court found that *Muhammad* "has no application to the facts of this case" because the clients there complained only about their dissatisfaction with the amount of their settlement. Here, however, Collas did not allege that the settlement was inadequate but that their lawyer negligently gave them bad advice about the written release they had been asked to sign. Thus, the lesson to be learned from this case is that the lawyer's negligence preceded the settlement, and was the proximate cause of the settlement.

The next salvo was *White v. Kreithen*, 435 Pa. Super. 115 (1994), when the appellate court denied a motion to dismiss a legal malpractice claim brought by a client in an underlying medical malpractice case on the grounds that the lawyer had been negligent in preparing the case, thereby requiring the client to take it over pro se and accept a court-encouraged settlement of $150,000. The lawyer had previously evaluated the case as between $250,000 to $500,000. As though it frowned with disapproval on the "broad policy rationales employed by the Supreme Court and the unqualified articulation of its 'simply stated' holding," the appellate court ruled that *Muhammad* did not control because the lawyer did not participate in the settlement — his prior negligent representation only sabotaged the client's chances of eventually getting an adequate settlement. Here too, the lesson to be learned is that it was the lawyer's negligence during the pretrial phase of the case that made it impossible for the client to receive an adequate settlement within the range that even the negligent lawyer had estimated.

The federal courts were next to diminish the holding of *Muhammad*.

In *Builder's Square, Inc. v. Saraco*, 868 F. Supp. 748 (E.D. Pa. 1994), an insurer's designated defense counsel did not tell the insured that the plaintiff was prepared to settle a product liability claim for the insured's $1 million policy limit. The defense lawyer, without consulting the insured, rejected the settlement demand. A year later, on the eve of trial, the defense lawyer then advised the insured of the prior settlement offer. By then, the underlying plaintiff had discovered that her medical condition was more serious than originally believed. The settlement demand was then increased to $7 million. New counsel then substituted into the case and proceeded to trial, which resulted in a $4.25 million settlement. The insured had to contribute $3.25 million — $2 million of which came from its own resources. In the settlement agreement with the underlying plaintiffs, the insured explicitly reserved all claims against its prior designated defense counsel. When the insured sued for failing to pursue the earlier settlement opportunities, the designated defense counsel raised *Muhammad* as a grounds for dismissal.

The *Saraco* court made it clear that the facts of the case did not resemble those in *Muhammad* and refused to bar the malpractice claim against the designated defense counsel. First, this was not an action by a client who later became dissatisfied with a settlement agreement consummated by the attorney with the client's assent. It was an action by a client dissatisfied with his attorney for failing to communicate settlement offers and depriving the client of the opportunity to settle a case on more favorable terms than those that were later available. The insured expressly reserved its right to sue the designated defense counsel. The court observed that while "[s]uch a reservation does not itself create rights…, [i]t does underscore, however, that plaintiff has not had a change of heart about the action of an attorney to which it had assented." Once again, the lesson to be learned is to pinpoint the lawyer's negligence before the settlement and draw the causal link between that negligence and the adverse settlement, particularly where a beneficial result could otherwise have been achieved.

The next federal case to weaken *Muhammad* was *Wassall v. DeCaro,* 91 F.3d 443 (3d Cir. 1996). In *Wassall*, the Third Circuit reversed a District Court dismissal of a legal malpractice case based on the *Muhammad* rule. In the underlying defamation case, the defendant lawyer's representation of plaintiffs "was shoddy at best." He had so seriously damaged any hope of recovery or settlement that the clients "did not wish to suffer with defendants any longer and [wanted] to put a merciful end to two and a half years of malpractice … ." The list of malpractice allegations was long, to be sure. The underlying court dismissed for lack of prosecution. Afterwards, the plaintiffs sued the lawyers for malpractice. The District Court dismissed, believing that the plaintiffs' agreement to permit the underlying court to dismiss for lack of prosecution constituted a settlement under *Muhammad,* thus barring the subsequent malpractice action. In an insightful opinion, the Third Circuit reversed, and predicted that if this case were before the Pennsylvania Supreme Court, it would find that even the policies enunciated in *Muhammad* would allow the present action for legal malpractice to proceed. The court reviewed each of the state appellate decisions and catalogued three categories of cases where *Muhammad* would not bar a subsequent legal malpractice action:

> (1) if the attorney sued did not settle the case; (2) if the malpractice plaintiff is forced to settle because of the attorney's negligence; or (3) if the malpractice plaintiff does not try to question, retrospectively, the amount of the settlement the attorney negotiated.

Here, the court reasoned, the plain-

tiff's assent to the dismissal in the underlying case should not bar their subsequent malpractice action. "Plaintiffs 'wanted out' of the case, not for what they were getting in a settlement, but because [their lawyer] had so shabbily represented them that they merely wanted an end to the legal travail [he] had inflicted upon them." But here's where the court's analysis was so insightful that it was almost visionary in terms of what followed:

> The policies expressed in *Muhammad*, of preserving resources and allowing access to the courts by other litigants, are served by *allowing* the present action for malpractice. Plaintiff's allegations, if proven, show an enormous waste of the court's time by an unprepared attorney. Where the attorney's conduct in this regard "forces" a client to accept a dismissal of the case, allowing a subsequent malpractice action serves as a systemic deterrent for this behavior and thus promotes the policies articulated in *Muhammad*.
>
> An attorney who has neglected his role as a steward hopelessly delaying, and perhaps prohibiting the system from properly resolving his client's case, should not be able to seek safe haven in a dismissal that resulted because the client could not risk allowing the attorney further to neglect his role. Under these conditions, we are convinced that the Pennsylvania Supreme Court would not shield [the lawyer] from liability under the guise of encouraging settlements in general.

About six months after the Third Circuit's decision in *Wassal*, the Pennsylvania Supreme Court, in *McMahon v. Shea*, 547 Pa. 124 (1997), finally settled the turmoil that its decision in *Muhammad* had wrought. *McMahon* was a legal malpractice case arising out of the drafting and execution of a property settlement agreement in a divorce action. The client alleged that the attorney was negligent in preparing a settlement agreement dealing with payment of alimony that would be incorporated but not merged into the final divorce decree. After entry of the divorce decree, the wife remarried. The husband petitioned to terminate the alimony payments, but was denied on the grounds that the agreement survived the divorce decree. The husband was required to continue to pay alimony until the youngest child turned 21 or had finished college. The trial court dismissed the malpractice complaint based on *Muhammad*. The appellate court reversed and found that *Muhammad* did not apply "where the attorneys' alleged negligence does not lie in the judgment regarding the amount to be accepted or paid in a settlement, but rather lies in the failure to advise a client of well-established principles of law and the impact of a written agreement. *Muhammad* could not be interpreted to "blindly protect lawyers who carelessly advise clients incorrectly about their substantive rights."

The Pennsylvania Supreme Court recognized that this was the opportunity to act. Blaming an "unwarranted expansion of *Muhammad*" on lower courts that had held "that the rule of *Muhammad* was 'well nigh absolute,'" the Court acknowledged that "this interpretation is erroneous.… [T]he policy which encourages settlements of law suits does not operate to relieve a lawyer from a duty to inform his or her client of all relevant considerations before the client enters and signs a complex legal agreement." Thus, as to settlement agreements, *Muhammad* was no longer the bright-line rule that it had become and that had caused the knee-jerk response to boot otherwise meritorious post-settlement legal malpractice cases. Instead, the Court drew on its pre-*Muhammad* 1989 holding in *Rizzo v. Haines*, 520 Pa. 484, 555 A.2d 58 (1989), and acknowledged that the "fact that the legal document at issue had the effect of settling a case should not exempt [an attorney] from liability." Wrote the Court:

> Prior to *Muhammad*, we held that the 'necessity for an attorney's use of ordinary skill and knowledge extends to the conduct of settlement negotiations.' [citation omitted] We further stated that 'an attorney may not shield himself from liability in failing to exercise the requisite degree of professional skill in settling the case by asserting that he was merely following a certain strategy or exercising professional judgment. Rather, the importance of settlement to the client and society mandates that an attorney utilize ordinary skill and knowledge.'

Lower courts got the message. Not only did *McMahon* limit *Muhammad* to its facts, the new rule has been clearly articulated in *Red Bell Brewing Co., v. Buchanan Ingersoll, P.C.,* 2005 WL 180775 (2001):

> In cases wherein a dissatisfied litigant merely wishes to second guess his or her decision to settle due to speculation that he or she may have been able to secure a larger amount of money, i.e. "get a better deal" the *Muhammad* rule applies so as to bar that litigant from suing his counsel for negligence. If, however, a settlement agreement is legally deficient or if an attorney fails to explain the effect of a legal document, the client may seek redress from counsel by filing a malpractice action sounding in negligence.

The now circumscribed rule of *Muhammad*, and the concomitant resuscitation of a client's right to insist on competent representation from its lawyer was most recently vindicated in *Schnader Harrison Segal & Lewis, LLP*

v. Popowich, 2005 WL 2680017 (2005), which arose from a divorce settlement. Allowing a post-settlement malpractice action to proceed, the court wrote:

> Unlike the plaintiffs in *Muhammad,* [the client] did not simply change his mind about the monetary amount of the settlement. Instead, he is claiming that his attorney breached a contractual duty or a duty of care in crafting the settlement agreement itself.

After years of turmoil, the Pennsylvania Supreme Court set the record straight. *Muhammad* applies to bar only those legal malpractice cases where the sole basis of the client's complaint is the adequacy of the settlement. In other words, a malpractice case would be barred only where the client has had a change of heart after the settlement and wants more money or a "second bight of the apple." If there is any allegation of attorney negligence at any point in the underlying case, including the drafting of the final settlement agreement, the attorney is not immune from liability.

In New Jersey, it appears that there may be an inkling of hope that like the *Muhammad* phenomenon, the analogous *Puder* problem may also be destined for an equally sensible resolution.

Three recent New Jersey cases — one federal and two state — may have begun the process of scaling back *Puder*'s Draconian holding, and have allowed malpractice claims to proceed, even when the underlying case has settled.

Keltic Financial Partners, LP v. Krovatin, 2007 WL 1038496 (D.N.J. 2007), involved a complicated financing transaction that ultimately settled. The plaintiffs to the malpractice action sued several attorneys involved in the transaction, alleging they committed malpractice in a variety of ways. The defendants all relied on *Puder* for the proposition that "a client should not be permitted to settle a case for less than it is worth… and then seek to recoup the difference in a malpractice action against [the] attorney." Although the District Court granted summary judgment, it explicitly found that *Puder* did not apply. First, the plaintiffs alleged that the malpractice arose not as a result of an improper settlement, but in the context of the underlying loan transaction itself, and the litigation that ensued. Thus, the settlement of the action did not preclude a malpractice claim based on those services allegedly negligently rendered. Moreover, the District Court found that the circumstances of this case would undermine a fundamental principle encouraging settlement because it would have required the plaintiffs to litigate their case to its conclusion in order to preserve their malpractice claims. Even *Puder* did not contemplate such a result.

Although the *Keltic Financial* court distinguished *Puder* and differentiated it from the facts before it, the District Court dismissed the malpractice claims under the entire controversy doctrine, finding that the transactions giving rise to the malpractice claim shared a causal nexus and thus were required to be brought in one action.

Prospect Rehabilitation Services, Inc. v. Squitieri, 392 N.J. Super. 157 (App. Div. 2007), involved settlement of a dispute involving a nursing home seeking to recover certain overpayment of rent and construction advances. The trial court dismissed several of the underlying counts on partial summary judgment. Although the plaintiffs appealed, they decided to settle their remaining claims prior to the other defendants moving for partial summary judgment on the same grounds. After settlement, the plaintiff sued its attorney for various shortcomings, including failing to assert certain Medicare dental claims and failure to propound discovery. Plaintiff also claimed that it settled the case for less than it was worth because of counsel's errors.

The Appellate Division reversed the dismissal of the malpractice claim by distinguishing *Puder*, on which the defendant attorney primarily relied. Plaintiff relied on *Ziegelheim* to support its claim that a malpractice action is not barred merely because the underlying case settles. The trial court granted partial summary judgment by adopting defendant's reasoning and reliance on *Puder* by holding that plaintiff's "calculated decision" to settle as they did barred their malpractice claims. The Appellate Division held that the case before it was "factually and legally distinguishable from *Puder* and does not have the 'fairness and the public policy [considerations] favoring settlements' or the equities that pervaded that case." First, no one from the plaintiff ever represented that the settlement entered into was "fair." Moreover, plaintiff did not settle prior to rulings by the trial court (as in *Puder*, which settled prior to a ruling on the motion to enforce the original settlement). In sum, the Appellate Division reversed the trial court's *Puder*-based grant of summary judgment by finding sufficient difference between the facts before it and the specific facts of *Puder*. Doing so allowed the Appellate Division to scale back *Puder*'s effect and permit the malpractice claim to proceed.

Angerame v. Arnold, 2007 WL 2847561 (N.J. Super. 2007), was decided by the Appellate Division on October 3, 2007. The case involved a malpractice claim asserted against an attorney who had represented the purchaser of a home with certain defects that he claimed were not properly disclosed. The purchaser had commenced the initial litigation against the sellers, real estate brokers, title guarantee company, home inspection company and the purchasers homeowners' insurance company. The lawsuit settled approximately six months after it began. Several months after resolving the initial lawsuit, the purchaser then sued his attorney for malpractice, claiming that the lawyer knew of certain defects, but failed to disclose them, and/or failed to negotiate a reduced price on the home.

The trial court dismissed the malpractice claim on the grounds of judi-

cial estoppel – because the plaintiff had blamed the defendants in the original action, his newly placed blame on counsel was inconsistent with his prior litigation position and was thus estopped. In an effort to save his malpractice claims, plaintiff distinguished *Puder* by claiming that "he never placed on the record any statement that he felt the settlement in that case was in complete satisfaction of his losses or one that was fair and reasonable." The Appellate Division, without discussing *Puder* at all, upheld dismissal of the malpractice claim by finding that the plaintiff had taken inconsistent litigation positions and that the defendants in the original action were "alternative tortfeasors, meaning that once plaintiff recovered from the sellers [with whom he settled], he cannot recover from the [attorneys]." Because the underlying case settled and plaintiff's position was thus not judicially advanced, it was not judicially estopped – the Appellate Division held that plaintiff could not take a position inconsistent with the position asserted in a litigation earlier. Because plaintiff blamed the original defendants for the defects to the home, he could not subsequently blame another – his counsel – for those same defects. Thus, the malpractice claim was barred.

In a footnote, the Appellate Division noted the difference between the *Angerame* case and *Puder*, in that "here plaintiff did not represent to the first court that the settlement was fair and equitable." However, the Appellate Division's ruling was based entirely on non-*Puder* or *Zeigelheim* rationale.

Thus, in the three instances in which courts have discussed *Puder*, they have done so, much like their Pennsylvania counterparts, in what appears to be an effort to scale back *Puder*'s scope and effect or to dodge it entirely. Where possible, the courts have distinguished *Puder* factually, but they also have looked to the differences between *Zeigelheim* and *Puder* to limit *Puder* to its specific facts. Taken together, the recent decisions show that merely settling an underlying case may not insulate a lawyer from a malpractice claim, even when the client represents that the settlement is fair.

While these three post-*Puder* New Jersey cases suggest that New Jersey has just started down the same path that Pennsylvania had to travel in order to contain the damage caused by its *Muhammad* decision, it is still much too early to tell where it will end. *Puder* could have been decided on the basis of causation and the Court would have reached the same result, but the New Jersey Supreme Court declined to do so. Instead, the Court based its decision on "the public policy favoring settlements … ." If the Court had looked at the Pennsylvania experience and how that very same policy got so distorted, it could have prevented the collateral damage that *Puder* has thus far caused to the client's right to receive competent legal representation — a principle that before *Puder* had been even more sacrosanct in New Jersey.

Rather than confronting the Supreme Court with the issue of which public policy is more important — the policy favoring settlements or the policy protecting clients from substandard lawyering — the New Jersey courts after *Puder* have sought to contain *Puder's* damage through case-sensitive factual and legal distinctions. The lesson to be derived from these post-*Puder* cases may be the very same one already learned in Pennsylvania after *Muhammad*. It's a bit too early to know whether New Jersey will heed that lesson. New Jersey still has a way to go to restore the vitality of *Ziegelheim*, but at least Pennsylvania's experience provides it with a good road map on how to circumvent around the risks of the minefield that *Puder* has placed in its path. By following Pennsylvania's lead, hopefully it won't take as long in New Jersey to re-establish the principle that the quality of lawyering is far more important than the quantity of settlements. ■