Study J-111 February 2, 2000

Memorandum 2000-14

Statute of Limitations for Legal Malpractice

In 1999, the Commission requested and received authority to study the statute of limitations for legal malpractice. The topic was suggested by Andrew Wistrich (United States Magistrate Judge for the Central District of California), who co-authored a major article analyzing the statute, which can serve as a background study for the Commission. Ochoa & Wistrich, *Limitation of Legal Malpractice Actions: Defining Actual Injury and the Problem of Simultaneous Litigation*, 24 Sw. U. L. Rev. 1 (1994) (Exhibit pp. 1-79). This memorandum introduces the topic, which has been the subject of extensive litigation in recent years.

CODE OF CIVIL PROCEDURE SECTION 340.6

The governing statute is Code of Civil Procedure Section 340.6, which provides:

> 340.6. (a) An action against an attorney for a wrongful act or omission, other than for actual fraud, arising in the performance of professional services shall be commenced within one year after the plaintiff discovers, or through the use of reasonable diligence should have discovered, the facts constituting the wrongful act or omission, or four years from the date of the wrongful act or omission, or whichever occurs first. In no event shall the time for commencement of legal action exceed four years except that the period shall be tolled during the time that any of the following exist:
>
> (1) The plaintiff has not sustained actual injury;
>
> (2) The attorney continues to represent the plaintiff regarding the specific subject matter in which the alleged wrongful act or omission occurred;
>
> (3) The attorney willfully conceals the facts constituting the wrongful act or omission when such facts are known to the attorney, except that this subdivision shall toll only the four-year limitation; and
>
> (4) The plaintiff is under a legal or physical disability which restricts the plaintiff's ability to commence legal action.

> (b) In an action based upon an instrument in writing, the effective date of which depends upon some act or event of the future, the period of limitations provided for by this section shall commence to run upon the occurrence of such act or event.

Section 340.6 codifies the discovery doctrine, under which the limitations period does not begin to run until the client "discovers, or through the use of reasonable diligence should have discovered" the attorney's malpractice. The client must commence the action within one year from the date of discovery. To preclude endless potential exposure, however, the statute also requires the client to bring the action within four years from the date of the wrongful act or omission.

These alternate limitations periods (one-year-from-discovery and four-years-from-occurrence) are tolled so long as the allegedly negligent attorney continues to represent the client "regarding the specific subject matter in which the alleged wrongful act or omission occurred." Even after the client replaces the attorney, the limitations periods are tolled until the client suffers actual injury. "Rather than forcing a client to file a malpractice action whenever the attorney falls below the standard of competent counsel, the statute allows the client to wait until the attorney's mistakes cause some palpable harm …." *Laird v. Blacker*, 2 Cal. 4th 606, 626, 828 P.2d 691, 7 Cal. Rptr. 2d 550 (1992) (Mosk, J., dissenting).

Much litigation has centered on this actual injury requirement. The Supreme Court has addressed it no less than four times in the past decade. See *Jordache Enterprises, Inc. v. Brobeck, Phleger & Harrison*, 18 Cal. 4th 739, 958 P.2d 1062, 76 Cal. Rptr. 2d 749 (1998); *Adams v. Paul*, 11 Cal. 4th 581, 904 P.2d 1205, 46 Cal. Rptr. 2d 594 (1995); *ITT Small Business Finance Corp. v. Niles*, 9 Cal. 4th 245, 885 P.2d 965, 36 Cal. Rptr. 2d 552 (1994); *Laird v. Blacker*, 2 Cal. 4th 606, 828 P.2d 691, 7 Cal. Rptr. 2d 550 (1992).

A key problem is determining when actual injury occurs. Suppose, for instance, that the malpractice consists of failing to file a lawsuit until after the statute of limitations expires. Does the injury occur when the limitations period expires? When the client incurs attorney's fees relating to the potential limitations defense? When the defendant asserts the limitations defense? When the defendant prevails at trial on the basis of the limitations defense? When the defendant prevails on appeal? The courts have grappled with questions such as these, but have found it difficult to provide clear guidance reflecting sound policy.

The attached article by Professor Tyler Ochoa (Whittier Law School) and Judge Wistrich analyzes the actual injury requirement at length, focusing on what they call the problem of simultaneous litigation. The authors explain:

> If the alleged malpractice occurs in the course of litigation, then the outcome of the malpractice action is usually dependent on the outcome of the underlying proceeding. Moreover, even when the alleged malpractice occurs in a transactional setting, often the client does not discover the alleged malpractice until litigation arises concerning the subject matter of the transaction. In both classes of cases, if the limitation period for the legal malpractice action expires before the underlying litigation is concluded, *then the client who wishes to preserve his or her legal malpractice claim is forced to litigate two lawsuits simultaneously*.

(Exhibit pp. 2-3 (emphasis added).) Simultaneous litigation of a malpractice claim and an underlying claim raises a number of problems.

Problems Arising From Simultaneous Litigation

In assessing the impact of simultaneous litigation, the "most important consideration is that the client's legal position in the underlying action may be compromised by the proceedings in the malpractice action." (*Id.* at 20.) For example, where the malpractice consists of missing the statute of limitations, the malpractice claim may alert the defendant in the underlying action to assert a limitations defense. Even if the defendant is already aware of the defense, the client must take inconsistent positions in the two lawsuits. In the underlying action, the client has to show that the limitations defense is invalid. In the malpractice case, the client must show that the underlying suit was untimely. The result may be inconsistent verdicts or application of collateral estoppel in a manner harmful to the client. (*Id.* at 20-21.)

Simultaneous litigation could also result in a waiver of the attorney-client or work-product privilege. To establish malpractice, the client may need to disclose confidential communications with the attorney defendant. But such disclosure may waive the attorney-client privilege, giving the opposing party in the underlying action access to information that would otherwise be privileged. "Again, the waiver might result in a defeat of the client's position in the underlying litigation, to the prejudice of both the client and the former attorney." (*Id.* at 21.)

Another problem is that litigating two lawsuits simultaneously may be a hardship on the client. (*Id.* at 21-22.) It is difficult enough to bear the expense and emotional strain of litigating one lawsuit. Litigating two cases at once may be prohibitive for some clients.

Finally, the outcome of the underlying action will often render the legal malpractice action unnecessary. "It makes little sense to clog court dockets and expend limited judicial time and resources in litigating malpractice actions which may be avoided completely by a favorable result in the pending proceeding." (*Id.* at 22-23.) "To force malpractice plaintiffs to file their actions before they know the outcome of the case upon which their claim is based does not promote judicial economy." *Laird*, 2 Cal. 4th at 626 (Mosk, J., dissenting).

Competing Policies

The complications of simultaneous litigation must be balanced against the policies underlying statutes of limitation: the interest in litigating claims while evidence is fresh and readily available, and the policy of guaranteeing repose with respect to conduct in the distant past. (Exhibit pp. 14-15.) If assertion of a malpractice claim is delayed while the underlying action is pending, evidence may deteriorate. Memories may fade, documents may be lost or destroyed, witnesses may die or disappear. In addition, the attorney may be oblivious to the potential malpractice claim and proceed accordingly. "Permitting the client to commence a malpractice action after such a lengthy delay would severely undermine the policy of guaranteeing repose." (*Id.* at 23.)

Where the client gives the attorney prompt notice of the potential malpractice claim, however, these concerns are less pressing. Once an attorney is placed on notice, the attorney "may take steps to preserve evidence by collecting and retaining important documents and maintaining contact with or obtaining statements from potential witnesses." (*Id.*) The policy of repose is also mitigated, because the attorney knows of the potential liability and can take it into account in making decisions.

Proposed Solution

Thus, Professor Ochoa and Judge Wistrich advocate application of the doctrine of equitable tolling in the context of legal malpractice. Under this doctrine, the statute of limitations on a potential claim will be tolled during the pendency of a related claim, so long as three elements are met: (1) timely notice to the potential defendant, (2) lack of prejudice to the defendant in gathering

evidence to defend against the potential claim, and (3) good faith and reasonable conduct on the part of the potential plaintiff. (*Id.* at 51.) Professor Ochoa and Judge Wistrich explain:

> [C]ourts must weigh the desirability of guaranteeing repose and minimizing deterioration of evidence against the desirability of avoiding the problems which may result from simultaneous litigation of the malpractice claim and the underlying action. Despite the lack of a clearly defined legal basis for applying the doctrine of equitable tolling, these competing policies can best be balanced by defining "actual injury" in a manner consistent with that doctrine, *thereby tolling the commencement of the limitation period for the malpractice action until an adverse judgment or other appealable order is entered against the client at the trial court level in the underlying action*, provided that the other requirements of the doctrine are satisfied.

(*Id.* at 79 (emphasis added).) In other words, where a malpractice claim relates to underlying litigation (either because the malpractice occurred during the litigation or because the malpractice led to or may affect the litigation), Professor Ochoa and Judge Wistrich would interpret the actual injury requirement of Section 340.6 to incorporate the equitable tolling doctrine. Under this view, if the client gives the attorney notice of the potential malpractice claim, affords the attorney adequate opportunities to gather evidence relating to that claim, and acts in good faith, actual injury does not occur, and thus the limitations period on the malpractice claim is tolled, until the underlying litigation has been resolved in the trial court.

JUDICIAL DECISIONS

Although there are strong policy justifications for the equitable tolling doctrine, judicial decisions (including Supreme Court decisions issued after the attached article was written) do not support its use in applying Section 340.6. These decisions are of obvious importance in evaluating whether to revise the statute. To some extent, they also shed insight on the policy considerations presented by simultaneous litigation.

Express Rejection of Equitable Tolling

In the recent case of *Gordon v. Law Offices of Aguirre & Meyer*, 70 Cal. App. 4th 972, 83 Cal. Rptr. 2d 119 (1999), the court expressly held that the statute "is not subject to equitable tolling …." The court explained that "whether the doctrine of

equitable tolling applies to section 340.6 is a matter of statutory construction." *Id.* at 120. Section 340.6 states that "in no event" shall the limitations period exceed four years except where one of the statutorily enumerated grounds for tolling applies. Thus, "the Legislature *expressly intended to disallow tolling under any circumstances not enumerated in the statute*." *Id.* at 124, *quoting Laird* , 2 Cal. 4th 606, 618 828 P.2d 691, 7 Cal. Rptr. 2d 550 (1992) (emphasis in *Gordon*).

As a matter of statutory construction, this argument may have some merit, but it has no bearing in determining whether equitable tolling is good public policy in the context of legal malpractice. The court merely stated its view of what the law is, not what the law should be and why.

Supreme Court Decisions Predating *Jordache*

Unlike the court in *Gordon*, the Supreme Court has repeatedly expounded on the policy implications of simultaneous litigation. While it has not rejected the equitable tolling doctrine in so many words, it has nonetheless made clear that equitable tolling does not apply in legal malpractice cases.

At first, the Court's approach was similar to the bright-line, termination-at-the-trial-level test that Prof. Ochoa and Judge Wistrich advocate. In *Laird*, the Court considered whether the limitations period of Section 340.6 "is tolled during the time the client appeals from the underlying judgment on which the claim of malpractice is based." 2 Cal. 4th at 608. The Court concluded that "the limitations period of section 340.6 commences when a client *suffers an adverse judgment or order of dismissal in the underlying action* on which the malpractice action is based." *Id.* at 609 (emphasis added). Justice Mosk dissented, maintaining for a number of reasons that the limitations period should be tolled until the appeal is resolved. *Id.* at 621-28 (Mosk, J., dissenting).

The Court's next case interpreting the statute involved malpractice in the preparation of loan documentation. Again, the Court focused on termination of the underlying action, concluding that "in transactional legal malpractice cases, when the adequacy of the documentation is the subject of dispute, an action for attorney malpractice accrues *on entry of adverse judgment, settlement, or dismissal of the underlying action*." *ITT Small Business Finance Corp. v. Niles*, 9 Cal. 4th 245, 258, 885 P.2d 965, 36 Cal. Rptr. 2d 552 (1994) (emphasis added). The Court based its decision in part on a policy analysis similar to that of Prof. Ochoa and Judge Wistrich:

> [T]here was no danger in the present case that tolling the malpractice statute of limitations until conclusion of the adversary

> proceeding would undermine the statute's goals of preserving evidence and notifying defendants. [The client] notified [the attorney] that he should contact his malpractice insurer as soon as [the client] realized it would have to defend the documentation prepared by [the attorney] in the adversary proceeding. Finally, it would be a waste of judicial resources to require both the adversary proceeding and the attorney malpractice action to be litigated simultaneously. Had [the client] prevailed in the adversary proceeding, the malpractice action would have been unnecessary.

Id. at 257. Justice Mosk concurred, reiterating his view that tolling should continue until the underlying action is fully resolved. *Id.* at 258 (Mosk, J., concurring). Justice Kennard dissented on the ground that "actual injury may be sustained well before the resolution of a third party action by adverse judgment or settlement." *Id.* at 260 (Kennard, J., dissenting). In her view, "it defies common sense to hold … that a client has not sustained 'actual injury' even though the client has paid thousands, perhaps hundreds of thousands, of dollars because the attorney's malpractice has compelled the client to prosecute or defend third party litigation." *Id.* at 259 (Kennard, J., dissenting).

The Court reversed course and was even more badly splintered in the next decision, in which an attorney failed to file the client's claim within the statute of limitations. The issue was "when, in the event of such a failure or misadvice as to the applicable limitations period, the plaintiff sustains 'actual injury' for purposes of tolling the statue of limitations in a subsequent suit for professional negligence." *Adams v. Paul*, 11 Cal. 4th 581, 585, 904 P.2d 1205, 46 Cal. Rptr. 2d 594 (1995). Three justices determined that in light of the many variables in such cases, the determination of when actual injury occurs is "generally a question of fact." *Id.* at 588. Thus, the case would have to be remanded for determination of "the point at which the fact of damage became palpable and definite even if the amount remained uncertain, taking into consideration all relevant circumstances." *Id.* at 593. Justice Kennard concurred, emphasizing certain points and stating certain qualifications. Chief Justice Lucas, joined by Justices Mosk and George dissented, adhering to the termination-at-the-trial-level test. "I would hold that in a legal malpractice action typified by the facts here — in which the client attempted to avoid dismissal of an underlying action on statute of limitations grounds by litigating the merits of the statutory defense — 'actual injury' occurs *at the time of disposition of the client's underlying lawsuit, whether by dismissal, settlement or entry of adverse judgment*." *Id.* at 605 (Lucas, J., dissenting)

(emphasis added). His policy analysis closely tracks that of Prof. Ochoa and Judge Wistrich:

> Had plaintiff filed her malpractice action prior to dismissal of her underlying action following settlement, she would have been forced to take inconsistent positions with regard to the statute of limitations issue: In the malpractice action, she would have argued that she was damaged by [her attorney's] misadvice which resulted in the untimely filing of her wrongful death lawsuit, while in the underlying action itself, she maintained that the estate should be estopped from asserting the defense in the first place. Such a scenario not only results in a waste of judicial resources [cite omitted], but also creates the potential for inconsistent judgments.

Id.

***Jordache*: Case-By-Case Factual Determination of Actual Injury**

The Court's most recent decision construing the actual injury requirement of Section 340.6 is *Jordache Enterprises, Inc. v. Brobeck, Phleger & Harrison*, 18 Cal. 4th 739, 958 P.2d 1062, 76 Cal. Rptr. 2d 749 (1998), in which a law firm failed to advise its client regarding insurance coverage. Justice Chin authored the majority opinion, which was joined by four other justices, including Justice Kennard, who also wrote a short concurrence.

The Court squarely endorsed four principles: "(1) determining actual injury is predominantly a factual inquiry; (2) actual injury may occur without any prior adjudication, judgment, or settlement; (3) nominal damages, speculative harm, and the mere threat of future harm are not actual injury; and (4) the relevant consideration is the fact of damage, not the amount." *Id.* at 743. In reaching these conclusions, the Court stressed that Section 340.6 was intended to codify *Budd v. Nixon*, 6 Cal. 3d 195, 491 P.2d 433, 98 Cal. Rptr. 849 (1971). The Court expressly overruled *ITT* , commenting that the "broad, categorical rule" advanced in that decision "cannot be reconciled with the particularized factual inquiry required to determine actual injury under section 340.6 …." 18 Cal. 4th at 763. The Court also embraced the analysis of *Adams*, *see id.* at 762, which interpreted *Laird* to mean merely that actual harm occurs *no later than* termination of the underlying action at the trial level, 11 Cal. 4th at 591 n.4.

The Court thus rejected the termination-at-the-trial-level test, stating that "the determination of when attorney error has caused actual injury under section 340.6, subdivision (a)(1), cannot depend on facile, 'bright line' rules." 18 Cal. 4th at 764. Instead, "only the facts and circumstances of each case, analyzed in light

of the alleged negligence and its consequences as revealed by the evidence, can establish when the plaintiff sustained actual injury under section 340.6." *Id.*

On the facts before it, the Court determined that the client sustained actual injury "*before* settlement of the insurance coverage litigation." *Id.* at 764-65 (emphasis added). The malpractice "allowed the insurers to raise an objectively viable defense to coverage under the policies," increasing the client's costs to litigate its coverage claims and reducing the settlement value of those claims." *Id.* at 743. Because the client provided its own defense rather than tendering the defense to its insurer, it "not only lost a primary benefit of liability insurance," but also "lost profitable alternative uses for the substantial sums it paid in defense costs." *Id.* at 744.

In reaching this result, the Court explicitly considered the problems inherent in simultaneous litigation, which Prof. Ochoa and Judge Wistrich describe in their article: forcing the client to take inconsistent positions, compelling waiver of the attorney-client privilege, requiring the client to bear the burden of litigating two cases at once, and undermining judicial economy. *Id.* at 757-58. The Court dismissed these considerations, stating that "[w]hatever the merits of these policies in other settings, the legislative scheme embodied in section 340.6 allocates their relative weight in legal malpractice actions. *Id.* at 757. Moreover, "existing law provides the means for courts to deal with potential problems that may arise from the filing of a legal malpractice action when related litigation is pending." *Id.* at 758. "The case management tools available to trial courts, including the inherent authority to stay an action when appropriate and the ability to issue protective orders when necessary, can overcome the problems of simultaneous litigation if they do occur." *Id.* As Prof. Ochoa and Judge Wistrich point out, however, the alternative of staying a malpractice action until judgment is entered in the underlying action "is unsatisfactory", because the court may deny the stay due to pressure to control its docket. Even if the stay is granted, the mere filing of the malpractice action may alert opposing counsel in the underlying action to a possible defense and impose unnecessary litigation costs on parties and the legal system. (Exhibit pp. 65-66.)

George and Mosk Dissents

Both Chief Justice George and Justice Mosk vigorously dissented in *Jordache*, pointing out that the Court's opinion deviated from precedent, particularly *ITT*. *Id.* at 766-67 (Chief Justice George, dissenting); *id.* at 767-68 (Justice Mosk, dissenting). Each of them expressed serious policy concerns about the Court's

approach, including some concerns not raised by Prof. Ochoa and Judge Wistrich.

According to Chief Justice George, important policy considerations are best served by a rule that actual injury occurs on disposition of the underlying litigation, whether by settlement, dismissal or adverse judgment. *Id.* at 767 (Chief Justice George, dissenting). He explained:

> Those policy considerations include the comparative ease of application of that rule, its consistency with the policy favoring narrow construction of statutes of limitation, and the theoretical and practical advisability of entertaining one lawsuit at a time. [Cite omitted.] Additionally, a rule that measures the running of the statute of limitations from an early date — before the underlying litigation or controversy has been resolved — inevitably will require (or at least encourage) the early filing of legal malpractice actions that might otherwise not be brought, and may lead former clients, as malpractice plaintiffs, to pursue their legal malpractice action more vigorously than their underlying action against the third party, for reasons other than the relative merits of the two actions and the relative culpability of the respective tortfeasors. For example, the former client may conclude that a wealthy law firm is a less sympathetic defendant than a less affluent third party.

Id. at 767 (Chief Justice George, dissenting).

Similarly, Justice Mosk reiterated his support for the bright-line approach of *ITT*, observing that the majority "reject that 'bright line' rule in favor of an uncertain case-by-case approach that will require plaintiffs to sue their lawyers for harm that may be causally unrelated to the lawyers' act or omission." *Id.* at 768 (Mosk, J., dissenting). He declared that the "illogic of the majority's approach is patent." *Id.* For although

> the lawyers' omission exposed plaintiff to the *possibility* that its insurers might have a viable defense, such defense was neither certain to be raised nor certain to succeed. The causal connection between the lawyers' omission and plaintiff's damages was established only when plaintiff settled its lawsuit with insurers.

Id. at 768-69 (Mosk, J., dissenting) (emphasis in original).

Justice Mosk further remarked that the "impracticality of the majority's approach is also apparent." In particular,

> [i]n the absence of a bright line rule, clients will be constrained to bring actions against their lawyers even before they could prove

> any compensable injury — resulting in potentially unnecessary waste of judicial time and resources. Moreover, clients wishing to preserve their legal malpractice claims may be forced to litigate two suits simultaneously, thus raising obvious additional legal and practical problems.

Id. at 769 (Mosk, J., dissenting)

ANALYSIS AND RECOMMENDATION

Determining how the statute of limitations should apply to legal malpractice claims is challenging. It is hard to anticipate all of the different settings in which malpractice can arise and identify all of the relevant considerations. Unlike the Supreme Court, however, the Commission has the luxury of focusing on what the law *should be*, not what the law *is*. Whereas the Court dismissed policy concerns relating to simultaneous litigation on the ground that the Legislature already balanced the competing interests and codified the case-by-case approach of *Budd*, the Commission may examine the policies at stake unconstrained by rules of statutory construction.

At this preliminary stage of this study, the case-by-case approach recently adopted by the Supreme Court in *Jordache* strikes the staff as unworkable, confusing, costly for litigants, and difficult for courts to administer. Ideally, a statute of limitations should state a clear, easy-to-follow rule, not one that requires guesswork and forces the client and attorney to incur substantial sums debating about whether the malpractice suit was timely, rather than addressing the merits of the malpractice claim. Although categorically addressing the myriad malpractice situations may entail difficulties, imperfect guidance may be better than little to none.

The idea behind the actual injury requirement of Section 340.6 is to allow the client to delay suit until elements of malpractice are established. *Jordache*, 18 Cal. 4th at 751. The elements of malpractice include not only damages, but also causation. The client should be able to delay suit until *both* of these components are satisfied. Thus, even if the client sustains harm (e.g., legal expenses), the limitations period should remain tolled until it is clear that the malpractice caused the damages. *Jordache Enterprises, Inc. v. Brobeck, Phleger & Harrison*, 56 Cal. Rptr. 2d 661, 667-69 (1996), *rev'd*, 18 Cal. 4th 739, 958 P.2d 1062, 76 Cal. Rptr. 2d 749 (1998). This means waiting until the underlying litigation is resolved, at

least at the trial court level. *Id.*; *see also Jordache*, 18 Cal. 4th at 769-70 (Mosk, J., dissenting).

As the Supreme Court pointed out in *Jordache*, most lawsuits settle and thus "litigation related to a legal malpractice claim is unlikely to conclude with a judicial determination establishing either the attorney's error or a causal nexus between damages and the error." 18 Cal. 4th at 755. Nonetheless, once a settlement is reached the effect of an attorney's conduct may be much less speculative than beforehand, particularly because the settlement can be structured with the malpractice claim in mind.

For these reasons, as well as those presented in the attached article and in the policy analyses of Chief Justice George and Justice Mosk, **the staff tentatively recommends revising Section 340.6 to expressly incorporate equitable tolling.** If the Commission concurs, we would prepare a draft proposal along these lines for the Commission's next meeting. As usual, the staff will raise issues for the Commission's consideration as this study progresses, and present and analyze possible alternative approaches (e.g., whether equitable tolling should continue until underlying action is resolved at the appellate level, or only until the trial court renders its decision).

ADDITIONAL ISSUE

The Supreme Court very recently decided yet another case involving the statute of limitations for legal malpractice. *Samuels v. Mix*, 2 Cal. 4th 1, 989 P.2d 701, 91 Cal. Rptr. 2d 273 (1999). This time the issue did not relate to the actual injury requirement. Rather, the question was which party bears the burden of proving when the client discovered, or through the use of reasonable diligence should have discovered, the facts constituting the alleged malpractice.

The staff will discuss and analyze this decision in its next memorandum for the Commission.

Respectfully submitted,

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LIMITATION OF LEGAL MALPRACTICE ACTIONS: DEFINING ACTUAL INJURY AND THE PROBLEM OF SIMULTANEOUS LITIGATION

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* The authors have requested that the initial citation to the California Supreme Court cases also include a citation to the official reporter for the benefit of the practitioners. All short citations are to the Regional Reporter.

INTRODUCTION

The limitation period for legal malpractice actions in California is tolled during the time that "[t]he plaintiff has not sustained actual injury . . . ."[1] Defining the point at which "actual injury" occurs, however, has proven to be an extremely troublesome question. Since 1990 there have been fifteen reported opinions which have considered the "actual injury" exception in a number of different circumstances, with widely varying results. Much of the disagreement has focused on the meaning of the California Supreme Court's 1992 opinion in *Laird v. Blacker*,[2] which settled one aspect of the question but failed to achieve its apparent goal of setting forth a standard which could be applied in a consistent manner to a broad range of situations. To resolve the disagreement among the Courts of Appeal regarding *Laird*, the California Supreme Court granted review in *ITT Small Business Finance Corp. v. Niles*,[3] which was argued before the court on October 6, 1994.[4]

The difficulty of defining "actual injury" is compounded by the unusual nature of legal malpractice actions. If the alleged malpractice occurs in the course of litigation, then the outcome of the malpractice action is usually dependent on the outcome of the underlying pro-

1. CAL. CIV. PROC. CODE § 340.6(a)(1) (West 1982).

2. 2 Cal. 4th 606, 828 P.2d 691 (Cal.), *cert. denied*, 113 S. Ct. 658 (1992).

3. 23 Cal. Rptr. 2d 728 (Ct. App. 1993), *review granted*, 865 P.2d 632 (1994).

4. The California Supreme Court recently granted review in four other cases which address the question of when actual injury occurs. *See* Adams v. Paul, 31 Cal. Rptr. 2d 846 (Ct. App.), *review granted*, No. 5041623 (Sept. 29, 1994); Baykin v. Cobin, 30 Cal. Rptr. 2d 428 (Ct. App.), *review granted*, 878 P.2d 1275 (1994) (accountant malpractice); Weir v. Superior Court, No. F020375 (Ct. App.) (Unpublished opinion), *review granted*, No. 5040166 (July 18, 1994); Moss v. Mavridis & Assoc., No. B063743 (Cal. App.) (Unpublished opinion), *review granted*, No. 5039876 (June 20, 1994).

ceeding. Moreover, even when the alleged malpractice occurs in a transactional setting, often the client does not discover the alleged malpractice until litigation arises concerning the subject matter of the transaction. In both classes of cases, if the limitation period for the legal malpractice action expires before the underlying litigation is concluded, then the client who wishes to preserve his or her legal malpractice claim is forced to litigate two lawsuits simultaneously. Simultaneous litigation can raise a host of legal and practical problems, including collateral estoppel, inconsistent outcomes, and waiver of attorney-client privilege. Thus, any solution to the problem of defining "actual injury" for purposes of tolling the limitation period in legal malpractice actions must take into account the possibility that simultaneous litigation, with its attendant problems, may occur.

In this article, we will first review the development of the "actual injury" tolling provision in California, from its judicial adoption in 1971 to its legislative adoption in 1977. Second, we will explore the policies underlying the legal malpractice statute of limitation and the countervailing policies that may make delayed accrual or tolling desirable in situations involving simultaneous litigation. Third, we will examine case law applying the "actual injury" tolling provision to various fact situations and analyze potential legal solutions to the problem of defining "actual injury," including the doctrine of equitable tolling. Finally, we will demonstrate how the doctrine of equitable tolling could be applied to the facts in *ITT Small Business Finance Corp. v. Niles* and recommend adoption of the equitable tolling doctrine as a standard for resolving future cases concerning the "actual injury" tolling provision in legal malpractice actions.

I. BACKGROUND

A. *Judicial Adoption of Discovery Rule and Actual Harm Requirement*

Before the enactment of California Code of Civil Procedure section 340.6, the limitation period applicable to legal malpractice actions was two years.[5] The applicable statute, however, contained "no statutory language which could be construed to specify the time of accrual

5. Code of Civil Procedure § 339 provides a two-year limitation period for "[a]n action upon a contract, *obligation* or *liability* not founded upon an instrument of writing." CAL. CIV. PROC. CODE § 339(1) (West 1982) (emphasis added). This section was held applicable to actions for legal malpractice in Alter v. Michael, 413 P.2d 153 (Cal. 1966).

of an action for legal malpractice,"[6] that is, the time at which the two-year period would commence to run. Consequently, it was left to the courts to select a rule of accrual to apply to actions for legal malpractice.[7] The two most common alternatives are the wrongful act rule, which measures the limitation period from the date of the wrongful act or omission,[8] and the discovery rule, which measures the limitation period from the time that the plaintiff either actually discovered the injury and its negligent cause, or could have discovered the injury and its cause through the exercise of reasonable diligence.[9]

In 1936, the California Supreme Court "held that in an action for medical malpractice the period of limitations did not begin until discovery."[10] By 1971, California courts had adopted "a general rule that in actions for professional or fiduciary malpractice, the cause of action does not accrue until the plaintiff discovers, or should discover, the negligence."[11] Despite this general rule, however, prior to 1971 it was consistently held that "in actions for legal malpractice the statute [of limitation] commences to run from the date the negligent act occurs."[12]

In *Neel v. Magana, Olney, Levy, Cathcart & Gelfand*,[13] the California Supreme Court undertook to review "the rule that a cause of action for malpractice by an attorney arises, and the limitation period

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6. Neel v. Magana, Olney, Levy, Cathcart & Gelfand, 6 Cal.3d 176, 191, 491 P.2d 421, 430 (Cal. 1971). Code of Civil Procedure § 312, which applies to all of the statutes of limitation in Title II of the Code, states only that "[c]ivil actions . . . can only be commenced within the periods prescribed in this title, after the cause of action shall have accrued," and "does not define that point at which the cause of action accrues." *Id.* at 430 n.30.

7. *See id.* at 431 ("Legislative silence in the present case may indicate that the Legislature has chosen to defer to judicial experience and to repose with the judiciary the rendition of rules for the accrual of causes of action.").

8. *See, e.g.*, Myers v. Eastwood Care Ctr., Inc., 31 Cal.3d 628, 634, 645 P.2d 1218, 1221 (Cal. 1982) ("As a general rule a cause of action arises when the wrongful act was committed and not at the time of discovery; the statute commences to run even though a plaintiff is ignorant that he has a cause of action.") (citation omitted).

9. *See, e.g.*, Sanchez v. South Hoover Hosp., 18 Cal. 3d 93, 96-97, 553 P.2d 1129, 1132 (Cal. 1976) (holding that the discovery rule applies to actions for medical malpractice).

10. *Neel*, 491 P.2d at 426 (citing Huysman v. Kirsch, 6 Cal. 2d 203, 312-13 n.7, 57 P.2d 908 (Cal. 1936)).

11. *Id.* at 427 (citing United States Liability Ins. Co. v. Haidinger-Hayes, Inc., 1 Cal. 3d 586, 596, 463 P.2d 770 (Cal. 1970)).

12. Griffith v. Zavalaris, 30 Cal. Rptr. 517, 519 (Ct. App. 1963). *Accord Haidinger-Hayes Inc.*, 463 P.2d at 776; Heyer v. Flaig, 70 Cal. 2d 223, 231, 233 n.7, 449 P.2d 161, 166 n.7 (Cal. 1969); Alter v. Michael, 64 Cal. 2d 480, 483, 413 P.2d 153, 155 (Cal. 1966); Lattin v. Gillette, 95 Cal. 317, 320-21, 30 P. 545 (Cal. 1892) (dictum); Yandell v. Baker, 65 Cal. Rptr. 606, 608 (Ct. App. 1968); Eckert v. Schaal, 58 Cal. Rptr. 817, 820 (Ct. App. 1967).

13. 491 P.2d 421 (Cal. 1971).

commences, at the time of the negligent act."[14] The court attributed the origin of the rule to an erroneous headnote appended to one of its previous decisions,[15] and noted that the rule was inconsistent with the use of the discovery rule in all other cases of professional malpractice.[16] After reexamining the justification for applying the discovery rule in professional malpractice cases generally,[17] and concluding that "[t]hese reasons for delayed accrual of action for malpractice apply as much to the legal profession as to others,"[18] the court held that "in an action for professional malpractice against an attorney, the cause of action does not accrue until the plaintiff knows, or should know, all material facts essential to show the elements of that cause of action."[19]

In *Budd v. Nixen*,[20] a companion case to *Neel*, the court considered the application of the discovery rule to "a situation in which the client contends that although he discovered his attorney's negligence,

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14. *Id.* at 422.

15. In Hays v. Ewing, 70 Cal. 127, 11 P. 602 (Cal. 1886), the plaintiff commenced an action on June 16, 1884, alleging defendant's negligence in a collection suit which was dismissed on November 19, 1881. The court stated that "so far as [this action] is based on any neglect of the defendant prior to the judgment of November, 1881, [it] was barred by section 339 of the Code of Civil Procedure." *Id.* at 602. Although this language could be read to hold only that the action accrued on or before the date the underlying action was dismissed, the publisher's headnote to the case states that "a cause of action against an attorney for neglect of duty . . . is barred at the expiration of two years *after the neglect occurred.*" *Id.* at 602 n.1 (emphasis added). In *Neel*, the court concluded that "this unwarranted headnote generated the peculiar rule that only in legal malpractice cases does the statute of limitations begin to run before damage and before discovery." 491 P.2d at 425. *See also id.* at 426-28 (describing reliance on headnote of *Hays v. Ewing* in subsequent cases). However, the *Neel* court's criticism of this headnote is unjustified and is somewhat misleading, because in 1886 it was well established in other jurisdictions that "[w]here an attorney is sued for malpractice, the cause of action arises from the time when such malpractice occurred, and that without any reference to the circumstance whether the client then knew the fact or not." *Lattin*, 30 P. at 549 (quoting H. WOOD, A TREATISE ON THE LIMITATION OF ACTIONS AT LAW AND IN EQUITY § 122 (1883)).

16. *Neel*, 491 P.2d at 427-28 n.19.

17. Three reasons were given for the departure in such cases from what the court described as the "ordinary" rule that the cause of action accrues "upon the occurrence of the last element essential to the cause of action." *Id.* at 428. First, because the professional possesses specialized knowledge and skill, "the client may not recognize the negligence of the professional when he sees it," and hiring a second professional to oversee the work of the first would be "an expensive and impractical duplication." *Id.* Second, "not only may the client fail to recognize negligence when he sees it, but often he will lack any opportunity to see it," because much of the work of the professional is performed "out of the client's view." *Id.* Third, because the professional and the client have a fiduciary relationship, the discovery rule "vindicates the fiduciary duty of full disclosure; it prevents the fiduciary from obtaining immunity for an initial breach of duty by a subsequent breach of the obligation of disclosure." *Id.* at 429.

18. *Id.* at 429.

19. *Id.* at 430.

20. 6 Cal. 3d 195, 491 P.2d 433 (Cal. 1971).

he had not, at that time, suffered consequential damages."[21] In *Budd*, the attorney, Nixen, filed an answer on Budd's behalf, but failed to allege that Budd was not individually liable for his actions as president of a corporation.[22] On September 15, 1964, while the case was under submission, Budd retained a new attorney and discovered the alleged negligence.[23] Budd's new attorney filed an opposition to the proposed findings of fact, but the court entered judgment against Budd on November 4, 1965.[24] Budd's subsequent appeal was dismissed as untimely, and on September 11, 1967, less than two years after judgment was entered but more than two years after he discovered the alleged negligence, Budd filed a malpractice action against Nixen.[25]

The court held that "a cause of action for legal malpractice does not accrue until the client suffers damage."[26] The court explained its reasoning as follows:

> If the allegedly negligent conduct does not cause damage, it generates no cause of action in tort. The mere breach of a professional duty, causing only nominal damages, speculative harm, or the threat of future harm—not yet realized—does not suffice to create a cause of action for negligence. Hence, until the client suffers appreciable harm as a consequence of his attorney's negligence, the client cannot establish a cause of action for malpractice. . . . "It follows that the statute of limitations does not begin to run against a negligence action until some damage has occurred."[27]

The court cautioned, however, that "[t]he cause of action arises . . . before the client sustains all, or even the greater part, of the damages occasioned by his attorney's negligence. Any appreciable and actual harm flowing from the attorney's negligent conduct establishes a cause of action upon which the client may sue."[28]

Applying this standard, the court held that it was a question of fact whether Budd had incurred damages when "he was compelled to 'incur and pay attorney's fees and legal costs and expenditures,' " or whether he "did not suffer damage until the formal entry of judgment . . . against him."[29] The court indicated that the cause of action would be barred if, more than two years before the action was filed, Budd

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21. *Id.* at 435.
22. *Id.*
23. *Id.*
24. *Id.*
25. *Id.*
26. *Id.* at 434.
27. *Id.* at 436 (citations and footnotes omitted).
28. *Id.*
29. *Id.* at 437.

either (1) paid fees to the defendant which "in consequence of defendant's negligence . . . exceeded the reasonable value of defendant's legal services"; or (2) paid fees to his second attorney "for his efforts to extricate plaintiff from the effect of defendant's negligence."[30] However, "[i]f plaintiff's action in tort had not earlier accrued, it at least matured on entry of judgment because he clearly then became obligated to pay a considerable sum to the [third party] or to post a bond on appeal."[31]

The effect of *Neel* and *Budd* was to postpone accrual of a cause of action for legal malpractice until the client both (1) discovered, or should have discovered, the facts essential to show the elements of his cause of action, and (2) sustained at least some damage as a result of the alleged malpractice. Once both conditions were satisfied, the client had two years within which to commence the action. However, neither *Neel* nor *Budd* considered the possibility that the limitation period for the legal malpractice action might expire before the underlying lawsuit was concluded.

B. *Enactment of Section 340.6*

In adopting the discovery rule of accrual for legal malpractice actions, the California Supreme Court acknowledged in *Neel* that "the instant ruling will impose an increased burden upon the legal profession. An attorney's error may not work damage or achieve discovery for many years after the act, and the extension of liability into the future poses a disturbing prospect."[32] The court also recognized "the possible desirability of the imposition of some outer limit upon the delayed accrual of actions for legal malpractice,"[33] and suggested that an absolute limit, similar to the four-year absolute limit which then existed for actions for medical malpractice,[34] "may be desirable in actions for legal malpractice."[35]

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30. *Id.*

31. *Id.*

32. Neel v. Magana, Olney, Levy, Cathcart & Gelfand, 6 Cal. 3d 176, 192, 491 P.2d 421, 431 (Cal. 1971).

33. *Id.* at 431-32.

34. *See* Historical Note to CAL. CIV. PROC. CODE § 340.5 (West 1982). The absolute limitation period for medical malpractice actions is now three years. *Id.* § 340.5.

35. *Neel*, 491 P.2d at 432.

The Legislature responded to this suggestion by enacting Code of Civil Procedure section 340.6 in 1977.[36] That section provides in relevant part:

> (a) An action against an attorney for a wrongful act or omission, other than for actual fraud, arising in the performance of professional services, shall be commenced within one year after the plaintiff discovers, or through the use of reasonable diligence should have discovered, the facts constituting the wrongful act or omission, or four years from the date of the wrongful act or omission, whichever occurs first. In no event shall the time for commencement of legal action exceed four years except that the period shall be tolled during the time that any of the following exist:
>
> (1) The plaintiff has not sustained actual injury;
>
> * * *
>
> (b) In an action based upon an instrument in writing, the effective date of which depends upon some act or event of the future, the period of limitations provided for by this section shall commence to run upon the occurrence of such act or event.[37]

Although the phrase "except that *the period* shall be tolled" might be considered ambiguous, it has been held that subdivision (a)(1) tolls both the one-year and four-year periods of the statute.[38]

One effect of section 340.6 was to codify the discovery rule of *Neel* and *Budd*.[39] However, the legislative history of the bill which enacted section 340.6 reveals that the language of the "actual injury" requirement was amended twice during the debate on the bill. As originally introduced, the bill did not contain the tolling provision but simply provided that "the time for the commencement of action shall

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36. Act of September 17, 1977, ch. 863, § 1, 1977 Cal. Stat. 2908-09 (effective January 1, 1978).

37. CAL. CIV. PROC. CODE § 340.6 (West 1982). The limitation period is also tolled while the attorney continues to represent the plaintiff regarding the matter in which the alleged negligence occurred; if the attorney willfully conceals the alleged negligence from the plaintiff; and while the plaintiff is under a legal or physical disability which restricts his or her ability to commence legal action. *Id.* § 340.6(a)(2)-(4).

38. Bennett v. McCall, 23 Cal. Rptr. 2d 268, 270 (Ct. App. 1993) (citing Johnson v. Haberman & Kassoy, 247 Cal. Rptr. 614, 617 (Ct. App. 1988), and Gurkewitz v. Haberman, 187 Cal. Rptr. 14, 20 (Ct. App. 1982)). In *Gurkewitz*, the court noted that subdivision (a)(3) contains the proviso "except that this subdivision shall toll only the four-year limitation," which suggests that the other subdivisions tolled both the one-year and four-year periods. 187 Cal. Rptr. at 19. The *Gurkewitz* court also noted that the legislative counsel's digest of the final form of the statute summarized the effect of the tolling provisions as follows: "*These periods* would be tolled during the time that the plaintiff has not sustained actual injury . . . ." *Id.*.

39. Laird v. Blacker, 2 Cal. 4th 606, 611, 828 P.2d 691 (Cal.), *cert. denied*, 113 S. Ct. 658 (1992).

be three years after the date of the negligent act or one year after the plaintiff discovers, or through the use of reasonable diligence should have discovered, the damage."[40] The bill was revised to start the one-year period upon discovery of "the facts constituting the wrongful act or omission," and to provide that the limitation period was tolled during the time that "[t]he plaintiff has not sustained *significant* injury."[41] When the final language of the tolling provision was adopted, however, the phrase "significant injury" was replaced with the phrase "actual injury."[42] One court explained the reason for the change as follows:

> The change was motivated by pragmatic reasons rather than [by] favoritism for lawyers. For a statute of limitations to effectively preclude litigation of stale claims, the inquiry of damage should not invariably raise an issue of fact subjecting the lawyer to uncertainty and the expense of litigating both the merits of the claim and [the] statute defense. . . . The California approach reduces the hazard of its statute creating factual issues for litigation by focusing upon the *fact* of damage rather than upon the *amount*.[43]

However, the use of the phrase "actual injury" also can be viewed as a legislative recognition that an inchoate or potential injury may be avoided if the underlying litigation is terminated in the client's favor, and therefore that no "actual" injury exists until there has been a judicial determination or settlement adverse to the client in the underlying litigation.[44]

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40. A.B. 298, 1977-78 Reg. Sess. (as introduced January 25, 1977), *reprinted in part in Gurkewitz*, 187 Cal. Rptr. at 19.

41. A.B. 298, 1977-78 Reg. Sess. (as amended May 9, 1977) (emphasis added).

42. CAL. CIV. PROC. CODE § 340.6(a)(1) (West 1982); A.B. 298, 1977-78 Reg. Sess. (as amended May 17, 1977).

43. Finlayson v. Sanbrook, 13 Cal. Rptr. 2d 406, 410 (Ct. App. 1992) (quoting 2 RONALD E. MALLEN & JEFFREY M. SMITH, LEGAL MALPRACTICE § 18.11, at 105 (3d ed. 1989) [hereinafter LEGAL MALPRACTICE]. Mallen's views regarding § 340.6 have been considered authoritative because the legislative history "indicates that the members of the Assembly Judiciary Committee considered and reviewed the article . . . wherein Mr. Mallen proposes a legal malpractice statute of limitations," and because "[t]he bill as eventually enacted retains much of the wording as Mallen's proposed statute." Southland Mechanical Constructors Corp. v. Nixen, 173 Cal. Rptr. 917, 922 (Ct. App. 1981), *disapproved in part on other grounds*, Laird v. Blacker, 2 Cal. 4th 606, 828 P.2d 691 (Cal.), *cert. denied*, 113 S. Ct. 658 (1992); *see also Laird*, 828 P.2d at 696 (citing LEGAL MALPRACTICE, *supra*, § 18.11); Krusesky v. Baugh, 188 Cal. Rptr. 57, 59 (Ct. App. 1982) (citing Ronald E. Mallen, *An Examination of a Statute of Limitations For Lawyers*, 53 CAL. ST. B.J. 166 (1978)); Gurkewitz v. Haberman, 187 Cal. Rptr. 14, 19 n.3 (Ct. App. 1982) (citing Ronald E. Mallen, *A Statute of Limitaitons for Lawyers*, 52 CAL. ST. B.J. 22,22).

44. For example, if an attorney negligently drafts an agreement in an ambiguous manner, the effect of the agreement on the client's rights and obligations may be unclear. However, the potential injury to the client's interests will not ripen into "actual" injury until the other party to

C. *California Cases Construing "Actual Injury" Provision*

Following the enactment of Code of Civil Procedure section 340.6, a disagreement arose in the courts of appeal regarding the proper construction of the "actual injury" tolling provision. Some courts held that "the harm suffered must be irremediable before the statute of limitations begins to run in a legal malpractice suit,"[45] and therefore that "actual" harm did not occur "until the new lawyer's attempts to rectify the malpractice through judicial action proved unavailing."[46] Under this reasoning, "a trial court judgment which is adverse to a client because of his attorney's alleged malpractice does not cause irremediable harm until any appeal filed in that case likewise has been decided against the client."[47] Other courts, however, have held that "when the client is a losing plaintiff in the underlying action, an appeal of the dismissal of the action does not affect the date of actual harm under section 340.6 . . . ."[48]

In *Laird v. Blacker*,[49] the California Supreme Court resolved the disagreement among the courts of appeal regarding the effect of an appeal in the underlying litigation. In *Laird*, the underlying action

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the agreement takes a position contrary to the client's understanding of the agreement and the other party's interpretation is sustained by a court.

45. Robinson v. McGinn, 240 Cal. Rptr. 423, 429 (Ct. App. 1987). *Accord* Bell v. Hummel & Pappas, 186 Cal. Rptr. 688, 694 (Ct. App. 1982); Southland Mechanical Constructors Corp. v. Nixen, 173 Cal. Rptr. 917, 925 (Ct. App. 1981). The "irremediable" standard had its origin in Heyer v. Flaig, 70 Cal. 2d 223, 449 P.2d 161 (Cal. 1969), which preceded the adoption of the discovery rule for legal malpractice actions. In *Heyer*, the court held that because the intended beneficiaries of a will could not possess any legal interest in the estate until the testatrix died, the beneficiaries' third-party action against the decedent's attorney for malpractice in negligently drafting the will did not accrue until "the testatrix' death when the negligent failure to perfect the requested testamentary scheme becomes irremediable and the impact of the injury occurs." *Id.* at 162.

46. *Robinson*, 240 Cal. Rptr. at 428; *see also Bell*, 186 Cal. Rptr. at 694 (holding that actual harm did not occur until "the new attorney failed in his attempt to rectify the previous mistake," because "[i]t was not until then that his [plaintiff's] claims were lost and the full impact of the wrongful acts settled leaving damage that was for all practical purposes irremediable.") (citation omitted).

47. Worton v. Worton, 286 Cal. Rptr. 410, 419 n.1 (Ct. App. 1991) (Johnson, J., concurring). *See also Robinson*, 240 Cal. Rptr. at 426 (stating that appellant did not sustain actual harm "until he exhausted his administrative appeal remedy and this appeal was finally decided against him").

48. Laird v. Blacker, 2 Cal. 4th 606, 828 P.2d 691, 703 (Cal. 1992) (citing Troche v. Daley, 266 Cal. Rptr. 34, 39 (Ct. App. 1990)) ("Troche's attempts to appeal the dismissal of the federal action do not affect the date she suffered actual harm."), *cert. denied*, 113 S. Ct. 658 (1992). *See also Worton*, 286 Cal. Rptr. at 418 ("The availability of an appeal from a judgment in a civil action does not make 'irremediable' the harm the client sustained upon entry of judgment for purposes of tolling the statute of limitation for legal malpractice.") (citations omitted).

49. 828 P.2d at 691.

was dismissed for lack of prosecution on October 20, 1981.[50] On December 7, 1981, plaintiff dismissed her attorneys and filed an appeal *in propria persona*.[51] On September 15, 1982, she voluntarily dismissed her appeal after settling with the defendant for $1,000.[52] Eight months later, on May 17, 1983, she filed a malpractice action against her former attorneys.[53] The court held that "the limitations period of section 340.6 commences when the client suffers an adverse judgment or order of dismissal in the underlying action on which the malpractice action is based,"[54] rather than when an appeal of right is dismissed,[55] or when the opinion on appeal becomes final. The court emphasized the potential for manipulation of the limitation period by clients, and the effect that tolling the limitation period during an appeal would have on the policies of promoting repose and avoiding deterioration of evidence:

> [T]olling the statute during an appeal would place the statute of limitations for legal malpractice in the power of the client who could cause the statute to be tolled indefinitely and, hence, thwart the purpose of the statute of limitations which is to require diligent prosecution of known claims thereby providing necessary finality and predictability in legal affairs, and ensuring that claims will be resolved while the evidence bearing on the issues is reasonably available and fresh.[56]

In addition, the court disapproved in part those decisions which had held that damages must be "irremediable" before the statute of limitation would begin to run.[57] Justice Mosk dissented, advocating a construction of "actual injury" that would "toll the limitations period for

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50. *Id.* at 692.

51. *Id.*

52. *Id.*

53. *Id.*

54. *Id.*

55. *Id.* at 696 (rejecting plaintiff's argument that her damages were only speculative until her appeal was dismissed).

56. *Id.* at 695 (quoting Worton v. Worton, 286 Cal. Rptr. 410, 418 (Ct. App. 1991) (citations omitted). *See also id.* at 698:

> (The policy behind the limited tolling periods in the statute is clear. If we nonetheless hold that the statute is tolled pending an appeal, we allow clients, with knowledge that they have suffered actual injury, unilaterally to control the commencement of the statute of limitations and hence undermine the legislative goal of resolving cases while the evidence is fresh, witnesses are available and memories have not faded.)

57. *Id.* at 696-97 (disapproving in part, Robinson v. McGinn, 240 Cal. Rptr. 423 (Ct. App. 1987), Bell v. Hummel & Pappas, 186 Cal. Rptr. 688 (Ct. App. 1982), Southland Mechanical Constructors Corp. v. Nixen, 173 Cal. Rptr. 917 (Ct. App. 1981), and Heyer v. Flaig, 70 Cal. 2d 223, 449 P.2d 161 (Cal. 1969)).

filing legal malpractice actions when, as here, a client takes an appeal of right from the underlying judgment and is awaiting its outcome."[58]

Laird was an unusual case in one respect: the alleged negligence of the attorney, failure to prosecute, resulted in an adverse consequence for the client only when the underlying action was dismissed.[59] The judgment of dismissal was therefore the earliest point at which "actual injury" could be said to occur.[60] In many cases, however, the alleged negligence is discovered while the litigation is still pending, and the client immediately expends resources, such as time and attorneys' fees, in attempting to defend the legal action taken by their attorney or to correct the problem before a judgment is entered. In this situation, the question is whether "actual injury" occurs (a) when the opposing party first asserts a legal right against the client; (b) when the client spends money in defending the position taken by his or her former attorney; or (c) upon entry of judgment against the client.

Both option (b) and option (c) find support in the opinion in *Laird*. On the one hand, *Laird* states flatly that "the statute of limitations for legal malpractice actions commences on entry of adverse judgment or final order of dismissal."[61] On the other hand, *Laird* also states that the plaintiff "sustained actual injury when the trial court dismissed her underlying action *and she was compelled to incur legal costs and expenditures in pursuing an appeal.*"[62] In addition, the court in *Laird* relied heavily on the opinion in *Budd v. Nixen*,[63] in which the court held that it was a question of fact whether the plaintiff suffered damage upon entry of judgment or when "he was compelled to 'incur and pay attorney's fees and legal costs and expenditures.' "[64]

Because of this ambiguity in *Laird*, subsequent California cases have been sharply divided on the question of when "actual injury" occurs. Some cases have viewed *Laird* as establishing a "bright line" rule that "the statute of limitations for legal malpractice actions commences upon entry of adverse judgment or final order of dismissal."[65]

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58. *Id.* at 700 (Mosk, J., dissenting).

59. *See id.* at 696.

60. *See id.*

61. *Id.* at 696. The court further stated that "the limitations period of section 340.6 commences when a client suffers an adverse judgment or order of dismissal in the underlying action on which the malpractice action is based." *Id.* at 692.

62. *Id.* at 696 (emphasis added).

63. 6 Cal. 3d 195, 491 P.2d 433 (Cal. 1971). *See supra* notes 19-30 and accompanying text.

64. *Budd*, 491 P.2d at 437.

65. Pleasant v. Celli, 22 Cal. Rptr. 2d 663, 666 (Ct. App. 1993) (quoting Laird v. Blacker, 2 Cal. 4th 606, 828 P.2d 691 (Cal. 1992)). *See also* ITT Small Business Fin. Corp. v. Niles, 23 Cal. Rptr. 2d 728, 730-31 (Ct. App. 1993) (stating that the date of "settlement at trial court level . . . is

However, the majority of the cases decided since *Laird* have held, based on *Laird's* reliance on *Budd v. Nixen*, that "[a] client suffers damage when he is compelled, as a result of the attorney's error, to incur or pay attorney fees."[66] And in cases in which the underlying action was not pending at the time the alleged negligence was discovered, some courts have held that "actual injury" occurs even earlier, upon the occurrence of an event that eventually resulted in the client's loss of a legal right or remedy, even though the loss was not yet confirmed by entry of judgment or dismissal in the underlying action.[67] Cases in the latter two categories follow the view that the language of *Laird* must be considered in the context of the narrow question presented,[68] and therefore that *Laird* "cannot reasonably be construed to have addressed the point whether events other than entry of an adverse judgment can satisfy the criteria of actual injury . . . ."[69]

In resolving this conflict in the decisions of the courts of appeal, it is useful to examine the policies underlying the legal malpractice statute of limitation and the problems associated with simultaneous litigation;[70] decisions from other states in legal malpractice cases;[71] and

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the functional equivalent of the trial court dismissal in *Laird*"), *review granted*, 865 P.2d 632 (1994); Sirott v. Latts, 8 Cal. Rptr. 2d 206, 211 (Ct. App. 1992) (Johnson, J., dissenting) (arguing that client did not suffer actual injury until settlement of underlying action at trial court level); *cf.* Baykin v. Cobin, 30 Cal. Rptr. 2d 428, 430 (Ct. App.) (accountant malpractice), *review granted*, 878 P.2d 1175 (1994).

66. *Sirott*, 8 Cal. Rptr. 2d at 209. *Accord* Bennett v. McCall, 23 Cal. Rptr. 2d 268, 270 (Ct. App. 1993); Kovacevich v. McKinney & Wainwright, 19 Cal. Rptr. 2d 692, 696 (Ct. App. 1993); *see also* Adams v. Paul, 31 Cal. Rptr. 2d 846, 849 (Ct. App.), *review granted*, No. 5041623 (Sept. 29, 1994).

67. *See* Foxborough v. Van Atta, 31 Cal. Rptr. 2d 2d 525, 530 (Ct. App. 1994) (holding that "Foxborough sustained actual injury when it lost the night Van Atta was to secure indefinitely."); Finlayson v. Sanbrook, 13 Cal. Rptr. 2d 406, 409, 411 (Ct. App. 1992) (holding that where alleged negligence consists of missing deadline under statute of limitation, actual injury occurs upon expiration of limitation period on underlying action); Johnson v. Simonelli, 282 Cal. Rptr. 205, 208 (Ct. App. 1991) (holding that where seller's attorney drafted agreement which allegedly contained inadequate security for promissory note, actual injury occurred when buyer defaulted, notwithstanding pending action by seller against buyer to recover balance due on note). *See also* Schrader v. Scott, 11 Cal. Rptr. 2d 433, 435, 438-39 (Ct. App. 1992) (holding that in an action for accountant malpractice, appreciable harm occurred no later than date client received notice of final adjustment and deficiency, even though administrative appeals were still pending, but suggesting that injury occurred when client originally acted on erroneous tax advice); McKeown v. First Interstate Bank of Cal., 240 Cal. Rptr. 127, 130 (Ct. App. 1987) (holding in action for breach of fiduciary duty based on negligent tax advice that appreciable harm occurred when client received notice of deficiency, rather than when tax court judgment became final).

68. "The question before us is: what constitutes 'actual injury'—the judgment against plaintiff, or the finality of the appeal therefrom?" *Laird*, 828 P.2d at 692.

69. *Bennett*, 23 Cal. Rptr. 2d at 271 (quoting Hensley v. Caietti, 16 Cal. Rptr. 2d 837, 842 (Ct. App. 1993)).

70. *See infra* text accompanying notes 70-115.

decisions in other situations involving potential simultaneous litigation.[72]

II. Policy Analysis

A. *Policies Underlying Limitation*

One of the principal policies underlying statutes of limitation is the policy of avoiding deterioration of evidence.

> It is fundamental that the primary purpose of statutes of limitation is to prevent the assertion of stale claims by plaintiffs who have failed to file their action until evidence is no longer fresh and witnesses are no longer available. . . . The statutes, accordingly, serve a distinct public purpose, preventing the assertion of demands which through the unexcused lapse of time, have been rendered difficult or impossible to defend.[73]

Statutes of limitation serve this purpose in two ways. First, they encourage plaintiffs to commence litigation promptly, thereby placing the defendant on notice of a potential claim and affording him or her the opportunity to preserve evidence, by collecting documents and, if necessary, locating and deposing witnesses.[74] Second, they help to prevent stale claims from being presented to the trier of fact by facilitating the disposition of such claims on procedural grounds at an early point in the proceedings.[75] However, statutes of limitation are a rather blunt instrument for serving this purpose. In many instances, memories may fade, witnesses may disappear or documents may be lost before the limitation period expires. In other cases the claim may be barred even though there has not been any significant loss of evi-

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71. *See infra* text accompanying notes 116-208.

72. *See infra* text accompanying notes 209-52.

73. Addison v. State, 21 Cal. 3d 313, 317, 578 P.2d 941, 942-43 (Cal. 1978).

74. *See* Davies v. Krasna, 14 Cal. 3d 502, 512, 535 P.2d 1161, 1168 (Cal. 1975) ("The fundamental purpose of such statutes [of limitation] is to protect . . . defendants by affording them an opportunity to gather evidence while facts are still fresh."); Elkins v. Derby, 12 Cal. 3d 410, 412, 525 P.2d 81, 83 (Cal. 1974) ("[T]he fundamental purpose of the limitations statute . . . is to insure timely notice to an adverse party so that he can assemble a defense when the facts are still fresh.").

75. *See* Barrington v. A.H. Robins Co., 39 Cal. 3d 146, 152, 702 P.2d 563, 566 (Cal. 1985) ("[S]tatutes [of limitation] were enacted to promote the trial of the case before evidence is lost or destroyed, and before witnesses become unavailable or their memories dim."); Kaiser Found. Hosps. v. Workers' Compensation Appeals Bd., 39 Cal. 3d 57, 62, 702 P.2d 197, 200 (Cal. 1985) ("The purpose of any limitations statute is to require diligent prosecution of known claims thereby . . . ensuring that claims will be resolved while the evidence bearing on the issues is reasonably available and fresh.") (internal quotes omitted).

dence.[76] In still other cases, the claim may be barred even though the overall quality of the evidence actually has improved with the passage of time.[77]

The absolute nature of statutes of limitation finds its justification in a somewhat different policy: the policy of guaranteeing repose, or peace of mind.[78] This policy is grounded in the notion that, at some point, potential defendants are entitled to a "fresh start," unencumbered by the threat of liability for misdeeds committed in the distant past. Statutes of limitation serve this policy by relieving potential defendants of the continuing threat of liability, "thereby providing necessary finality and predictability in legal affairs."[79] In order for this policy to be effective, however, it is important that the limitation system facilitate the early disposition of claims, at the pleading or summary judgment stage. If the defendant must be subjected to a trial before his or her limitation defense can be determined, much of the benefit of repose will be lost.

Balanced against these policies, however, is the "strong public policy that seeks to dispose of litigation on the merits rather than on procedural grounds."[80] Based on the principle that "[f]or every wrong there is a remedy,"[81] this policy favors permitting plaintiffs to present their cases to the trier of fact regardless of any delay in commencing the action.

The balance between the policy of deciding cases on their merits and the policies favoring limitation is most easily struck when the plaintiff has been aware of a potential claim for a long period of time and nonetheless failed to commence an action promptly. In such a case, it is fair to grant the defendant repose and to deny the plaintiff

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76. In addition, the plaintiff generally has an additional three years after commencement of the action within which to serve the summons and complaint upon the defendant, unless the time is shortened by applicable fast-track rules. CAL. CIV. PROC. CODE § 583.210 (West Supp. 1994).

77. *See, e.g.*, Pierce v. Johns-Manville Sales Corp., 464 A.2d 1020, 1025-26 (Md. 1983) (noting that "evidence relating to the central issue in a latent disease case—the existence of the disease, its proximate cause, and the resulting damage—tends to develop rather than disappear as time progresses").

78. *See, e.g.*, Valley Circle Estates v. VTN Consol., Inc., 33 Cal. 3d 604, 615, 659 P.2d 1160, 1167 (Cal. 1983) ("In general, a statute of limitations is enacted as a matter of public policy to afford repose by giving security and stability to human affairs.") (citation omitted); Wyatt v. Union Mortgage Co., 24 Cal. 3d 773, 787, 598 P.2d 45, 53 (Cal. 1975) ("Statutes of limitation have, as their general purpose, to provide repose and to protect persons against the burden of having to defend against stale claims.").

79. *Kaiser Found. Hosps.*, 702 P.2d at 200.

80. Barrington v. A.H. Robins Co., 39 Cal. 3d 57, 62, 702 P.2d 563, 566 (Cal. 1985) (internal quotes omitted).

81. CAL. CIV. CODE § 3523 (West 1970).

his or her day in court because the plaintiff initially acquiesced in the status quo.[82] Moreover, if the defendant was unaware of the potential claim, then he or she will have been unable to preserve evidence to defend against a long-delayed claim, whereas the plaintiff will have had the opportunity to preserve evidence supporting the claim.

The balance is more difficult to achieve, however, in those cases in which the plaintiff fails to discover the facts on which his or her claim is based within the limitation period, despite the exercise of reasonable diligence. In such cases, the defendant may still expect repose because of the apparent acquiescence of the plaintiff, but the plaintiff has not been able to gain an unfair advantage in the preservation of evidence, and it seems unfair to hold the plaintiff solely responsible for delay which could not reasonably have been avoided. The harshness of barring a valuable claim where the plaintiff is blameless has resulted in the gradual adoption of the discovery rule of accrual in an increasingly wide range of civil actions.[83]

The discovery rule provides that the limitation period does not commence until the plaintiff discovers, or in the exercise of reasonable diligence should have discovered, the injury and its negligent cause.[84] Unrestricted application of the discovery rule, however, severely undermines the policies of repose and avoiding deterioration of evidence, because an injury may not occur, or may not be discovered, for many years after the alleged wrongful act or omission.[85] Typically the legislative response to concerns about open-ended liability has been to enact statutes of repose, which specify an absolute period of time from occurrence of the alleged wrongful act within which certain categories of claims must be brought, regardless of whether or when the plaintiff

82. This principle is also firmly rooted in American jurisprudence. Among the maxims of jurisprudence enacted in the 1872 Civil Code are the following: "He who consents to an act is not wronged by it," *id.* § 3515; "Acquiescence in error takes away the right of objecting to it," *id.* § 3516; and "The law helps the vigilant, before those who sleep on their rights," *id.* § 3527.

83. For a history of the development of the discovery rule in California, see Stephen V. O'Neal, Comment, *Accrual of Statutes of Limitations: California's Discovery Exceptions Swallow the Rule*, 68 CAL. L. REV. 106 (1980).

84. *See, e.g.*, CAL. CIV. PROC. CODE § 340.5 (West 1982) (medical malpractice); *Id.* § 340.2(a) (exposure to asbestos); Jolly v. Eli Lilly & Co., 44 Cal. 3d 1103, 1109, 751 P.2d 923, 927 (Cal. 1988) (personal injury); Neel v. Magana, Olney, Levy, Cathcart & Gelfand, 6 Cal. 3d 176, 190, 491 P.2d 421, 430 (Cal. 1971) (legal malpractice).

85. *Neel*, 491 P.2d at 431. *See, e.g.*, Lemmerman v. Fealk, 507 N.W.2d 226 (Mich. Ct. App. 1993) (holding that 54-year-old plaintiff could commence an action for sexual abuse which allegedly occurred from the time she was three until she reached puberty, where the plaintiff alleged that due to psychological trauma she had repressed memories of the abuse until shortly before the suit was commenced).

should have discovered the injury.[86] Often these statutes contain a two-tier structure, barring claims that are not asserted within a relatively short period of time after discovery, as well as those that are not asserted within a longer period of time after commission of the allegedly wrongful act giving rise to liability.[87] In some cases, the Legislature has acted to restrict the impact of the discovery rule because of a perceived "crisis" in the availability and cost of liability insurance.[88]

Similar concerns prompted the enactment of section 340.6 in 1977.[89] Section 340.6, however, is not a true statute of repose. Although the statute purports to set a four-year outside limit on actions for legal malpractice, the four-year period is extended indefinitely "during the time that . . . [t]he plaintiff has not sustained actual injury . . . ."[90] The adoption of this tolling provision demonstrates the Legislature's unwillingness to allow the policies favoring limitation to override the policy favoring adjudication of disputes on their merits.[91] Although tolling the limitation period until "actual injury" occurs might appear to be inconsistent with the apparent statutory goal of reducing malpractice liability exposure for attorneys, it can be viewed as promoting this purpose indirectly. Preserving causes of action from the bar of limitation until actual injury has occurred, may serve to reduce unnecessary litigation by encouraging clients who have discovered allegedly negligent conduct to wait and see if the conduct causes

86. *See, e.g.*, CAL. CIV. PROC. CODE § 337.15 (West 1982) (enacting 10 year statute of repose governing injuries to property arising out of any latent deficiency in the planning or construction of an improvement to real property).

87. *See, e.g., id.* § 340.5 (requiring actions for medical malpractice to be commenced within three years after date of injury or within one year after plaintiff discovers or should have discovered the injury).

88. *See* 1975-76 Cal. Assembly J., 2d Extraordinary Sess. 2-3 (May 19, 1975) (proclamation of the Governor convening the Legislature in extraordinary session and asking Legislature to consider, *inter alia*, "setting a reasonable statute of limitations for the filing of [medical] malpractice claims").

89. *See* Southland Mechanical Constructors Corp. v. Nixen, 173 Cal. Rptr. 917, 923 (Ct. App. 1981) ("[I]n several of the committee reports it is stated that the purpose of Assembly Bill No. 298 was to reduce the costs of legal malpractice insurance."), *disapproved in part on other grounds*, Laird v. Blacker, 2 Cal. 4th 606, 828 P.2d 691 (Cal.), *cert. denied*, 113 S. Ct. 658 (1992); *see also* Mallen, *supra* note 42, 52 CAL. ST. B.J. at 22 (describing increase in premiums for legal malpractice liability insurance and decline in the number of companies providing such insurance).

90. CAL. CIV. PROC. CODE § 340.6(a)(1) (West 1982).

91. "[I]t would be unfair to cut off a cause of action by a statute of limitation before a remedy existed." Mallen, *supra* note 42, 52 CAL. ST. B.J. at 24 n.17. As noted above, the text of § 340.6 was based in large part on Mallen's proposed statute. *See supra* note 42. *Compare* Mallen, *supra* note 42, 52 CAL. ST. B.J. at 24 *with* CAL. CIV. PROC. CODE § 340.6(a) (West 1982).

injury before commencing suit.[92] Because malpractice liability insurance covers the cost of defending lawsuits in addition to paying judgments or settlements, the intended purpose of the "actual injury" tolling provision may have been to achieve a net reduction in liability insurance premiums by discouraging the premature filing of potential actions in which no damage ultimately occurs, despite preserving of other potential actions for a longer period of time.

This purpose has important consequences for the judicial construction of the statutory phrase "actual injury." There is a tendency for courts to strictly construe "actual injury" to mean *any* adverse consequence for the client, even when that adverse consequence may be corrected or avoided in the litigation in which the alleged malpractice occurred.[93] This approach was severely criticized by the dissenting Justice in *Sirott v. Latts*:[94]

> [I]t seems reasonable to forecast this rule will only encourage clients and their advisors to adopt a "hair trigger" approach to their lawyers' possible malpractice. Don't wait to see whether the problem can be cured or minimized at the trial level. Don't even wait to see if what might be viewed as bad advice actually turns out to have made you a net winner. File that malpractice lawsuit and file it *now*. Otherwise the statute of limitations clock will tick away and you'll be without recourse if your efforts to prevent or minimize the harm ultimately fail. . . . [T]hese "hair trigger" lawsuits are bad for lawyers because there probably will be many more malpractice suits filed. It is only reasonable to anticipate [that] clients and their advisors will feel compelled to file early and often in order to preserve their rights while they learn whether they can avoid any problems

92. *See* Laird v. Blacker, 2 Cal. 4th 606, 626, 828 P.2d 691, 704 (Cal. 1992) (Mosk, J., dissenting); *see also* Mallen, *supra* note 42, 52 CAL. ST. B.J. at 24 ("Thus, the plaintiff should not be required to sue until he sustains significant damage. To do otherwise is to outlaw causes of action before remedies may exist, *or to promote unnecessary litigation*.") (emphasis added). Mallen cites three cases as "illustrative of the actions brought prematurely while other litigation was pending which would determine whether the attorney was negligent or caused damage." *Id.* at 24 n.18.

93. For example, in Finlayson v. Sanbrook, 13 Cal. Rptr. 2d 406, 407 (Ct. App. 1992), the court held that when the alleged malpractice consisted of missing the statute of limitation in the underlying action, "actual injury" occurred on the date the limitation period in the underlying case expired.

94. 8 Cal. Rptr. 2d 206, 212-13 (Ct. App. 1992). In *Sirott*, the attorney advised the client not to purchase medical malpractice tail insurance, asserting that the $50,000 premium was unconstitutional. *Id.* at 208. The client followed the attorney's advice and was subsequently sued for medical malpractice; however, the cost of defending the action did not exceed $50,000 until the client settled the case. *Id.*. The majority held that "actual injury" occurred when the client incurred attorney fees in defending the medical malpractice action, even though the client had not suffered a net loss from his attorney's advice at that time. *Id.*

> their lawyers' potential malpractice may have caused . . . . Thus, it seems rational to forecast [that] lawyers will find themselves forced to defend against many cases which would not have been filed if the clients were only allowed to wait to see if they really suffered a net loss because of the lawyer's mistake.[95]

Viewed from this perspective, defining "actual injury" as occurring when the client's legal right arguably might have been impaired or lost, or even when the client's legal position has been challenged by an adverse party, is premature, because it encourages the client "to file a precautionary legal malpractice suit in anticipation of losing on an issue that may never arise, or, if it does arise, may be resolved against the [opposing party] in the underlying suit."[96] Therefore, the policy of reducing the sum of defense costs and judgment or settlement costs, and thereby reducing malpractice insurance premiums may be better served by defining "actual injury" as occurring when the client can be reasonably certain that the attorney's conduct has adversely affected the outcome of the underlying action, rather than that point at which a potential legal problem arises.

B. Policies Concerning Simultaneous Litigation

When the alleged malpractice occurs in the course of litigation, or when litigation arises concerning the transaction in which malpractice allegedly occurred, then additional considerations come into play when interpreting the "actual injury" standard. If "actual injury" is deemed to occur at an early point in the underlying action, the possibility exists that the one-year limitation period will expire before the underlying action is resolved. Under such a rule, the client who wishes to preserve his or her cause of action must commence the malpractice action while the underlying action is still pending. Litigating two lawsuits simultaneously, however, can raise a number of practical and legal problems.

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95. *Id.* at 212-13 (Johnson, J., dissenting) (other emphases omitted).

96. Pleasant v. Celli, 22 Cal. Rptr. 2d 663, 668 (Ct. App. 1993). In *Pleasant*, a missed-statute-of-limitation case, the court disagreed with *Finlayson*, holding that:

> the actual harm to Pleasant continued to be merely prospective until (1) the medical defendants recognized a potential statute of limitations defense, (2) asserted the defense, (3) fought Pleasant's tolling and other arguments through demurrer and summary judgment, and (4) succeeded in having Pleasant's case dismissed. Until that point, . . . Celli's breach of professional duty caused only an unrealized threat of future harm.

Id. This result is more consistent with the purpose of the "actual injury" provision because it is likely that the malpractice action would never have been filed had the client prevailed in the underlying action. *Id.*

The most important consideration is that the client's legal position in the underlying action may be compromised by the proceedings in the malpractice action. For example, suppose the alleged malpractice consists of filing the underlying action after the relevant statute of limitation has run, and that the client discovers the former attorney's alleged malpractice when he or she retains a new attorney. If "actual injury" has already occurred at that point, then the limitation period for the legal malpractice action will expire one year later. Yet at that point, the defendant in the underlying action may not have raised the limitation defense, and the possibility exists that the defendant will never raise the limitation defense, or that the court will hold that it was waived.[97] If the client must file a legal malpractice action to preserve his or her rights, the client runs the risk that making the attorney's error public by filing a malpractice action will alert the defendant in the underlying action to the potential limitation defense.[98] Moreover, even if the defendant is already aware of the potential limitation defense, the malpractice action forces the client to take inconsistent positions in the two lawsuits:

> In the underlying suit where they are attempting to cure the lawyer's mistake, the clients must attempt to convince the court that what their lawyers did or advised was not error (or at least not erroneous enough to deny the clients their legal rights). Simultaneously in the legal malpractice case, these same clients must attempt to prove that what their lawyers did or advised indeed was error.[99]

The consequences of taking inconsistent positions can be disastrous for both the client and the former attorney. For example, an admission in the malpractice action that the attorney's error waived the client's legal right could be used to impeach the client in the underlying lawsuit, resulting in the defeat of the client's position and increasing the damages to which the former attorney might be subject.[100] In addition, if both cases proceed simultaneously, there is a possibility that

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97. "Is a plaintiff harmed by her attorney's failure to file a timely lawsuit, even if it never occurs to the defendants in the underlying suit to assert a statute of limitations defense? Under *Finlayson*, the answer would be 'yes.' " *Pleasant*, 22 Cal. Rptr. 2d at 667 (criticizing *Finlayson*, 13 Cal. Rptr. 2d at 411).

98. "Taken to its extreme, *Finlayson* would oblige a plaintiff to sue a former attorney upon discovering that the attorney filed the complaint late . . . even if the defendants do not realize the suit against them is untimely." *Pleasant*, 22 Cal. Rptr. 2d at 667.

99. Sirott v. Latts, 8 Cal. Rptr. 2d 206, 213 (Ct. App. 1992) (Johnson, J., dissenting). *See also Pleasant*, 22 Cal. Rptr. 2d at 667; ITT Small Business Fin. Corp. v. Niles, 23 Cal. Rptr. 2d 728, 732-33 (Ct. App. 1993), *review granted*, 865 P.2d 632 (1994).

100. *Pleasant*, 22 Cal. Rptr. 2d at 667 (citing United States Nat'l Bank of Or. v. Davies, 548 P.2d 966, 970 (Or. 1976)).

inconsistent verdicts could result from the same set of facts.[101] "More likely, clients may end up 'winning' a finding in the legal malpractice lawsuit which will constitute collateral estoppel against their position in the underlying lawsuit—or vice versa."[102]

Litigating a malpractice action at the same time as the underlying lawsuit also could result in a waiver of the attorney-client or work-product privilege. For example, suppose that the client has disclosed potentially damaging information to the attorney in confidence. By placing the former attorney's conduct at issue in the malpractice action, the client necessarily waives the attorney-client privilege to the extent necessary to show the information available to the attorney at the time he or she acted. Those communications, however, would otherwise be privileged in the underlying action. By waiving the privilege in the malpractice action, the client may expose those confidential communications to the scrutiny of the opposing party in the underlying proceeding. Again, the waiver might result in a defeat of the client's position in the underlying litigation, to the prejudice of both the client and the former attorney.[103]

An additional consideration is that it is often impractical for the client to engage in simultaneous litigation to protect his or her rights. This is particularly true in cases in which the client is an individual or a small business. In such a case, it is likely that the expense of litigating the underlying action is already burdensome. To compel the client to retain additional counsel to file a malpractice action and to expend time and resources responding to motions and discovery requests in the malpractice action before the outcome of the underlying suit is

101. *ITT Small Business Fin. Corp.*, 23 Cal. Rptr. 2d at 733; *Sirott*, 8 Cal. Rptr. 2d at 213 (Johnson, J., dissenting). For example, in an action for negligent drafting of a contract, the trier of fact in the underlying action might find that the contract was ambiguous and should be construed against the client, whereas the trier of fact in the malpractice action might find that the contract was not ambiguous, leaving the client with no recovery. Conversely, the trier of fact in the underlying action might find that the contract was sufficiently definite while the trier of fact in the malpractice action might find that the contract was negligently unclear, giving the client a double recovery which would amount to unjust enrichment at the former attorney's expense.

102. *Sirott*, 8 Cal. Rptr. 2d at 213 (Johnson, J., dissenting).

103. If the attorney continues to represent the client in the underlying litigation, the simultaneous prosecution of a malpractice claim also threatens to disrupt the ongoing attorney-client relationship. This problem is addressed by the provision tolling the limitation period during the time that the attorney continues to represent the plaintiff regarding the matter in which the alleged negligence occurred. CAL. CIV. PROC. CODE § 340.6(a)(2) (West 1982). Accordingly, the "actual injury" tolling provision comes into play only when the client discharges the allegedly negligent attorney before the underlying litigation is concluded.

known may cause severe financial hardship.[104] If the client who cannot afford counsel chooses to proceed without an attorney, he or she is likely to be overwhelmed by the legal complexity of one lawsuit, let alone two.[105] In either case, the emotional stress of being involved in litigation will be compounded by an additional lawsuit.

In the case of a institutional litigant, impracticality may take an entirely different form. For example, an insurance company may have a large number of matters pending at any one time. The soundness of its lawyers' legal advice is implicitly called into question in every case in which the insured challenges the insurer's legal position. The sheer number of cases makes it impractical for the insurer to have to commence an action against its attorney every time it is called upon to defend its legal position.[106] This consideration suggests that "actual injury" should be defined in a manner that allows the client to separate those cases in which an attorney's legal work is merely challenged from those cases in which it is reasonably probable that the attorney's legal work is, in fact, deficient.[107]

The final consideration is judicial economy. In many cases, the outcome of the underlying proceeding will render the legal malpractice action unnecessary.[108] If the client is successful in the underlying lawsuit, notwithstanding the alleged malpractice of his or her former attorney, then the malpractice suit may become moot for lack of damages.[109] Indeed, even if the attorney's alleged malpractice increased the cost of litigating the underlying action, if the client ultimately prevails then he or she may decide that the remaining damages do not justify the expense and hardship of bringing a second lawsuit. It makes little sense to clog court dockets and expend limited judicial

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104. *Cf.* Lambert v. Commonwealth Land Title Ins. Co., 53 Cal. 3d 1072, 1078, 811 P.2d 737, 740 (Cal. 1991) ("[T]he unexpected burden of defending an action may itself make it impractical to immediately bear the additional cost and hardship of prosecuting a collateral action against an insurer."). For a discussion of *Lambert*, see text accompanying notes 238-245 & 249-251.

105. *See* Laird v. Blacker, 2 Cal. 4th 606, 626, 828 P.2d 691, 704 (Cal.) (Mosk, J., dissenting), *cert. denied*, 113 S. Ct. 658 (1992).

106. The same is true in the case of a finance company. "[I]t would be impractical for a lender to commence action against its attorney every time one of its debtors challenged the validity of the lender's legal position and thus the soundness of its lawyers' legal work. This would be a substantial and unwelcome addition to the already overwhelming caseload our courts must handle." ITT Small Business Fin. Corp. v. Niles, 23 Cal. Rptr. 2d 728, 732 (Ct. App. 1993), *review granted*, 865 P.2d 632 (1994).

107. *Id.*

108. *ITT Small Business Fin. Corp.*, 23 Cal. Rptr. 2d at 733.

109. *Laird*, 828 P.2d at 704 (Mosk, J., dissenting).

time and resources in litigating malpractice actions which may be avoided completely by a favorable result in the pending proceeding.[110]

C. *Balancing the Policies*

All of the considerations which come into play when simultaneous litigation may occur suggest that the limitation period for legal malpractice claims should be tolled until the underlying action is finally resolved. These considerations however, must be balanced against the policies underlying statutes of limitation. In theory, the underlying lawsuit could be reviewed by the California Court of Appeal, the California Supreme Court and the U.S. Supreme Court. If a remand is required, a retrial and further appeals could ensue. The underlying action could take years to resolve, during which time the former attorney may be completely unaware of the client's potential malpractice claim and may have arranged his or her affairs accordingly. Permitting the client to commence a malpractice action after such a lengthy delay would severely undermine the policy of guaranteeing repose.

The length of the potential delay also implicates the policy of avoiding deterioration of evidence. The longer the limitation period for the malpractice claim is tolled, the greater are the chances that memories will fade, that relevant documents will be lost or destroyed, and that witnesses will disappear or die. In addition, if the attorney is unaware of the potential malpractice claim, then the client gains an unfair advantage in the ability to preserve relevant evidence. This policy, therefore, favors a definition of "actual injury" that falls at the earliest possible point in the underlying litigation. It also suggests, however, that some of the unfair prejudice to the defendant can be mitigated or cured if notice is given to the former attorney at an early point in the underlying litigation. Once the attorney is placed on notice, he or she may take steps to preserve evidence by collecting and retaining important documents and maintaining contact with or obtaining statements from potential witnesses.

Achieving the proper balance between these opposing considerations depends in part on the finality of the underlying action. While the problems of simultaneous litigation carry considerable weight before a judgment is entered at the trial level in the underlying action, those problems are substantially reduced after a judgment is entered at the trial level. Before judgment, almost every dispute in which one

110. Sirott v. Latts, 8 Cal. Rptr. 2d 206, 213-14 (Ct. App. 1992) (Johnson, J., dissenting).

of the parties acted upon the advice of counsel raises a potential malpractice claim. After judgment, however, there has been a judicial determination against one party which makes it more probable that the attorney for that party may have erred in some manner. Although this determination is not always dispositive of the issue of malpractice and may be subject to reversal on appeal, it represents a relatively clear "bright-line" which can conveniently be used to eliminate the large number of malpractice claims which otherwise would be filed merely to protect the client's claim against the attorney in the event of an adverse decision.[111] Conversely, because only a small percentage of actions are actually appealed, and of those, only a small percentage are reversed on appeal, it is likely that the number of "unnecessary" malpractice actions filed solely to preserve the cause of action pending an appeal will be relatively small.[112]

The risk that taking an inconsistent position will prejudice the client is also greatly reduced after an adverse judgment has been entered because it is unlikely that the client's position in the newly filed malpractice lawsuit could be raised for the first time on appeal in the underlying action, and because the client's position in the underlying litigation already has been rejected at the trial court level.[113] Finally, the burden of litigating an appeal is usually considerably less than the burden of litigating in the trial court. During pretrial and trial, the client's personal participation is needed in responding to discovery requests, developing evidence and giving testimony, none of which occurs at the appellate level. In addition, the financial burden of an appeal is usually spread out over a long period of time, because of lengthy delays between filing the notice of appeal and briefing, and between briefing and oral argument. On balance, therefore, the rele-

111. *Cf.* Pleasant v. Celli, 22 Cal. Rptr. 2d 663, 667-68 (Ct. App. 1993) (discussing the importance of a judicial determination adverse to the client in establishing actual injury).

112. "[S]ince most appeals result in affirmances, deferral of the malpractice action is [usually] a postponement, not an avoidance." *Laird*, 828 P.2d at 698. In 1991-92, for example, 23% of contested dispositions in civil cases in California Superior Court were appealed. Judicial Council of California, 1993 Annual Report, Vol. 2: Judicial Statistics for Fiscal Year 1991-92 [hereinafter *1993 Annual Report*] at 26. The reversal rate in civil appeals disposed of by written opinion was 22%. *Id.* at 28. Multiplying these percentages yields an overall reversal rate of 5% of contested civil dispositions. Moreover, assuming that the vast majority of appeals disposed of without written opinion were affirmances, the reversal rate on appeal drops to 15.7% (935 reversals in 5,962 appeals), which, multiplied by 23%, yields an overall reversal rate of 3.6% of contested civil dispositions.

113. The danger of taking inconsistent positions is further reduced after final judgment has been entered in the trial court because it reduces the likelihood that the client will have to take inconsistent positions before the same trial judge. *Sirott*, 8 Cal. Rptr. 2d at 213 nn. 2-3 (Johnson, J., dissenting).

vant policies favor tolling the limitation period on the malpractice claim until entry of judgment in the underlying action. The remaining problems associated with having two actions pending simultaneously can be resolved by requesting that the trial court stay the malpractice action while the appeal in the underlying action is pending,[114] or by requesting that the trial court exclude evidence concerning the malpractice action from consideration in the underlying action.[115] The court can then balance the need of the former attorney to preserve evidence through discovery against the additional burden that the second action will place on the client.[116]

The foregoing analysis assumes that the underlying action is pending at the time the alleged malpractice is discovered. In some cases, however, although it can be anticipated that litigation regarding the underlying subject matter will occur, there is no action pending at the time the alleged negligence is discovered. For example, suppose a client discovers the alleged malpractice of his or her attorney in failing to file an action within the statute of limitation, and immediately files the action in an attempt to cure the attorney's alleged negligence. In such a case, all of the policies that weigh against simultaneous litigation of the malpractice claim and the underlying action apply. There is, however, an additional factor to be considered: by controlling the timing of the not-yet-commenced underlying action, the client may be able to deliberately extend the limitation period for bringing the malpractice action, and thereby gain an unfair advantage in the preservation of evidence.[117] The importance of this consideration depends on the client's good faith in commencing the underlying action. If the client commences the underlying action promptly upon discovering the alleged negligence, it is fair to characterize the underlying action

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114. *See infra* text accompanying notes 310-15.

115. *See infra* note 231.

116. In cases in which a stay is appropriate, care should be taken to specify precisely when the stay will terminate, in order to avoid additional litigation regarding the duration of stay. *See, e.g.*, Rosenthal v. Wilner, 243 Cal. Rptr. 472, 474-76 (Ct. App. 1988) (action stayed "pending resolution of the . . . appeal" in the underlying action; holding that stay remained in place until petition for certiorari to United States Supreme Court was denied, rather than upon filing of remittitur four months earlier).

117. *See* Finlayson v. Sanbrook, 13 Cal. Rptr. 2d 406, 411 (Ct. App. 1992). The court stated

> Although *Laird* repeatedly asserted without qualification that "actual injury" for purposes of section 340.6 occurs when a client suffers an adverse judgment or order of dismissal in the underlying action, we believe that the rule must be qualified to those situations in which there exists a timely filed underlying action. . . . [Otherwise] the limitations period could be indefinitely extended simply by filing a time-barred action however late and then waiting until an adverse judgment is rendered.

Id.

as a good-faith attempt to avoid or mitigate the consequences of the alleged negligence. In such a case it is reasonable to allow the client the benefit of whatever tolling rule is applicable in those cases in which the alleged negligence was discovered while the underlying action was pending.[118] However, if the commencement of the underlying action is unreasonably delayed after the client discovers the alleged negligence, then it is more reasonable to conclude that the underlying action was brought solely in an attempt to circumvent the statute of limitation on the malpractice claim, and tolling should be denied.[119]

III. LEGAL ANALYSIS

A. Legal Malpractice Cases in Other States

Courts in thirty states and the District of Columbia have expressed the view that a cause of action for legal malpractice does not accrue, and the statute of limitation does not begin to run, until the plaintiff has suffered some damage.[120] Many of these jurisdictions have adopted the view that damage is an essential element of the cause of action which must be "discovered" under the discovery rule of accrual.[121] However, some states, like California, consider damage to be independent of discovery.[122] Four other states[123] have adopted

118. This solution is somewhat similar to the doctrine of equitable tolling, which provides that when a plaintiff has several legal remedies and pursues one reasonably and in good faith, the statute of limitation as to the other remedies is tolled if the defendant is not prejudiced thereby. Elkins v. Derby, 12 Cal. 3d 410, 414, 525 P.2d 81, 83-84 (Cal. 1974). *See infra* discussion accompanying notes 232-54.

119. The one-year limitation period provides a useful rule of thumb for determining whether commencement of the underlying action has been "unreasonably delayed." The amount of time elapsed after discovery and before commencement of the underlying action may be counted against the one-year limitation period to provide an additional incentive for the plaintiff to act diligently. *See infra* text accompanying notes 353-54.

120. The 30 states are: Alabama, Alaska, Arizona, California, Colorado, Florida, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Missouri, Nevada, New Jersey, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Tennessee, Texas, Washington and Wisconsin. *See generally* Francis M. Dougherty, Annotation, *When Statute of Limitations Begins to Run Upon Action Against Attorney for Malpractice*, 32 A.L.R. 4th 260 (1984 & Supp. 1993); Ronald E. Mallen, *Limitations and the Need for "Damages" in Legal Malpractice Actions*, 60 DEF. COUNS. J. 234, 235-37 & n.6 (1993); LEGAL MALPRACTICE, *supra* note 42, § 18.11 at 29-32 & n.2.

121. *See, e.g.*, Knight v. Furlow, 553 A.2d 1232, 1234 (D.C. Ct. App. 1989); Massachusetts Elec. Co. v. Fletcher, Tilton & Whipple, 475 N.E.2d 390, 391 (Mass. Sup. Ct. 1985); Grunwald v. Bronkesh, 621 A.2d 459, 464 (N.J. 1993); Hennekens v. Hoerl, 465 N.W.2d 812, 819 (Wis. 1991).

122. *See, e.g.*, Chicoine v. Bignall, 835 P.2d 1293, 1294-98 (Idaho 1992) (discussing the "some damage" rule and rejecting the discovery rule); Sabes & Richman, Inc. v. Muenzer, 431 N.W.2d 916, 918-19 (Minn. Ct. App. 1988) (same).

the discovery rule for legal malpractice actions or for other professional malpractice actions, but they have not specifically discussed the requirement of damage in the legal malpractice context. Two states which have adopted the discovery rule have rejected the view that damage is a required element which must be discovered,[124] and the courts of Pennsylvania are divided over whether damage is required.[125] Seven states[126] adhere to the rule that a cause of action for legal malpractice accrues when the alleged negligent act or omission occurs, while the remaining six states[127] have not addressed the issue.

In those states in which damage is required, the cases can be grouped into two categories: alleged negligence committed during the course of litigation, and alleged negligence in advising clients or drafting documents in a transactional setting.

1. Malpractice in Litigation Setting

When the alleged malpractice occurs during the course of litigation, the majority of jurisdictions have held that injury occurs, and the cause of action accrues, upon entry of an adverse judgment at the trial court level.[128] There is no consistent rationale given for this outcome; often the result is reached simply by assertion.[129] Some courts have emphasized the monetary injury to the client, explaining that when a judgment is entered, a client must either pay the judgment or post a

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123. Delaware, South Carolina, West Virginia and Wyoming.

124. *See* Peschel v. Jones, 760 P.2d 51, 55-56 (Mont. 1988); Rosnick v. Marks, 357 N.W.2d 186 (Neb. 1984).

125. *Compare* Boerger v. Levin, 812 F. Supp. 564, 565 & n.2 (E.D. Pa. 1993) (citing cases requiring "proof of actual loss") *with* Garcia v. Community Legal Servs. Corp., 524 A.2d 980, 986 (Pa. Super. Ct. 1987) (rejecting damage rule; "the limitation period begins to run when the alleged breach of duty occurs, . . . [or] until the injured party should reasonably have learned of this breach."), *appeal denied*, 538 A.2d 876 (Pa. 1988).

126. Arkansas, Connecticut, Georgia, Mississippi, New York, South Dakota and Virginia. In many of these states, however, the harshness of the wrongful act rule is mitigated by the rule tolling the limitation period while the allegedly negligent attorney continues to represent the plaintiff. *See generally* LEGAL MALPRACTICE, *supra* note 42, § 18.13.

127. Hawaii, Maine, New Hampshire, Rhode Island, Utah and Vermont.

128. *See, e.g.*, Michael v. Beasley, 583 So. 2d 245, 252 (Ala. 1991); Wettanen v. Cowper, 749 P.2d 362, 365 (Alaska 1988); Treasure Valley Bank v. Killen & Pittenger, 732 P.2d 326, 328 (Idaho 1987) (on confirmation of bankruptcy plan); Zupan v. Berman, 491 N.E.2d 1349, 1352, (Ill. Ct. App. 1986); Watson v. Dorsey, 290 A.2d 530, 533 (Md. Ct. App. 1972); Hayden v. Green, 420 N.W.2d 201, 206 (Mich. Ct. App.) (Hood, J., dissenting), *dissenting opinion adopted*, 429 N.W.2d 604 (Mich. 1988); Nationwide Mutual Ins. Co. v. Winslow, 382 S.E.2d 872, 873-74 (N.C. Ct. App. 1989); Price v. Becker, 812 S.W.2d 597, 598 (Tenn. Ct. App. 1991); Richardson v. Denend, 795 P.2d 1192, 1195 (Wash. Ct. App. 1990), *review denied*, 803 P.2d 1309 (Wash. 1991).

129. *See, e.g.*, *Michael*, 583 So. 2d at 252; *Price*, 812 S.W.2d at 598.

bond and incur costs and attorney's fees in pursuing an appeal.[130] This rationale suggests that injury might occur before judgment is entered if "damage in the form of legal fees is incurred to ameliorate the impact of [the alleged] negligence";[131] however, this rule generally applies in the litigation context only when the client contends that the action would have been settled prior to judgment but for the attorney's negligence.[132] In other cases in which attorney's fees have been held to constitute injury in the litigation context, a previous judgment[133] or other judicial determination of liability[134] had already occurred.

Other courts have reasoned that an adverse judgment at the trial court level generally places the client on notice that he or she has been harmed.[135] This rationale suggests that damage can occur earlier if a client obtains actual knowledge of the alleged negligence at an earlier

130. *See, e.g.*, *Wettanen*, 749 P.2d at 365; *Hayden*, 420 N.W.2d at 206 (Hood, J., dissenting), *dissenting opinion adopted*, 429 N.W.2d at 604; St. Paul Fire & Marine Ins. Co. v. Speerstra, 666 P.2d 255, 258 (Or. Ct. App.), *review denied*, 670 P.2d 1036 (Or. 1983).

131. Jacobson v. Shine, 859 P.2d 911, 913 (Colo. Ct. App. 1993) (dictum) (holding that plaintiff incurred legal fees and injury occurred no later than date bankruptcy judge denied plaintiff's claim).

132. *See, e.g.*, Breakers of Ft. Lauderdale, Ltd. v. Cassell, 528 So. 2d 985, 986 (Fla. Dist. Ct. App. 1988) (holding that a cause of action for litigation malpractice is tolled until the appeal is final and does not apply to negligent failure to settle, which accrues when attorney's fees are incurred); *cf.* Bollam v. Fireman's Fund Ins. Co., 730 P.2d 542, 542, 547 (Or. 1986) (stating that action against liability insurer for negligent failure to settle accrues when client incurs attorney's fees to defend underlying action rather than when client settles underlying action).

133. *See, e.g.*, *Jacobson*, 859 P.2d at 913 (holding that plaintiff incurred legal fees and injury occurred no later than date bankruptcy judge denied plaintiff's claim); Braud v. New England Ins. Co., 576 So. 2d 466, 469, 470 (La. 1991) (client sustained actual harm when default judgment obtained by attorney was attacked by opposing party, causing client to incur and pay attorney's fees and costs); Massachusetts Elec. Co. v. Fletcher, Tilton & Whipple, 475 N.E.2d 390, 392 (Mass. 1985) (client sustained harm when action commenced by insurer seeking reimbursement of amount paid in settlement of underlying claim because "it was then clear that the electric companies would incur legal expenses in the defense of a claim that was based in part on the alleged negligent conduct of their attorneys").

134. Northwestern Nat'l Ins. Co. v. Osborne, 610 F. Supp. 126, 128, 130 (E.D. Ky. 1985) (holding that injury occurred when independent counsel first rendered billable services on June 7, 1982, after interlocutory order of default entered against client on March 5, 1981); Cantu v. St. Paul Cos., 514 N.E.2d 666, 668-69 (Mass. 1987) (holding that injury occurred when client retained independent counsel to advise him after jury verdict was returned, but before judgment was entered).

135. "[T]he damages, if any, resulting from the errors or omission of an attorney allegedly occurring during the course of litigation, are embodied in the judgment of a court. . . . We conclude, therefore, that upon entry of judgment, a client, as a matter of law, possesses knowledge of all the facts which may give rise to his or her cause of action for negligent representation." Richardson v. Denend, 795 P.2d 1192, 1195 (Wash. Ct. App. 1990), *review denied*, 803 P.2d 1309 (Wash. 1991). *See also* LEGAL MALPRACTICE, *supra* note 42, § 18.11, at 45.

point in time.[136] Generally, however, courts will delay accrual until judgment is formally entered, even if the adverse decision is announced earlier.[137] Likewise, if the parties enter into a settlement agreement, the limitation period is usually tolled until judgment is formally entered,[138] unless the settlement agreement is made enforceable without court approval.[139]

One exception to the majority rule that a cause of action for litigation malpractice accrues upon (or is tolled until) entry of judgment in the underlying action is when the alleged malpractice consists of missing the statute of limitation for filing the underlying action. In that situation the clear majority of courts hold that injury occurs on the date that the limitation period for the underlying action expires, even though the limitation period on the malpractice claim may be tolled until the neglect is discovered.[140] These courts reason that "the argument that the tortfeasor might not raise the statute of limitations

136. *See, e.g.*, Fischer v. Browne, 586 S.W.2d 733, 735, 737 (Mo. Ct. App. 1979) (holding that damage occurred when judge determined and ruled upon motion for summary judgment and communicated that decision to the parties, rather than date on which judgment was formally entered, and suggesting that damage arguably occurred "as soon as the motions for summary judgment were filed").

137. *See, e.g.*, Johnson v. Cornett, 474 N.E.2d 518, 519 (Ind. Ct. App. 1985) (holding that cause of action accrued on date dissolution decree was signed rather than date dissolution order was announced); Barnard v. Lannan, 829 P.2d 723, 725 (Or. Ct. App. 1992) (holding that cause of action accrued when judgment of dismissal was entered rather than on date of order of dismissal, because the order "was interlocutory, non-appealable and subject to modification or reversal by the trial court").

138. *See, e.g.*, Poole v. Lowe, 615 A.2d 589, 593 (D.C. 1992) (holding that cause of action for entering settlement without approval of client accrued on date settlement was approved by commissioner, rather than date settlement was agreed to, despite the fact that client had actual knowledge that agreement had been entered into before settlement was approved, because injury became "objectively verifiable"); Anderson v. Anderson, 399 N.E.2d 391, 401-02 (Ind. Ct. App. 1979) (action for legal malpractice dismissed as premature where dissolution decree did not dispose of parties' property and property settlement agreement was not final until approved by court).

139. *See* Sutton v. Mytich, 555 N.E.2d 93, 96-97 (Ill. App. Ct. 1990) (holding that limitation period commenced upon entry of judgment because the settlement agreement "was not enforceable until approved by the trial court," but suggesting in dictum that "if the agreement could have been enforced by either party without entry of judgment," then action would have accrued when settlement agreement was executed).

140. *See, e.g.*, Basinger v. Sullivan, 540 N.E.2d 91, 93-94 (Ind. Ct. App. 1989); Olivier v. Poirer, 563 So. 2d 1227, 1229 (La. Ct. App. 1990); Thorpe v. DeMent, 317 S.E.2d 692, 695-96, (N.C. Ct. App.), *aff'd*, 322 S.E.2d 777 (N.C. 1984); Cutcher v. Chapman, 594 N.E.2d 640, 640-41 (Ohio Ct. App. 1991); Garcia v. Community Legal Servs. Corp., 524 A.2d 980, 986 (Pa. Super. Ct. 1987) (alleging injury occurred on date statute expired, but limitation period for malpractice action was tolled until constructive discovery occurred; suggesting in dicta that limitation period for other litigation malpractice may be tolled until appeal resolved), *appeal denied*, 538 A.2d 876 (Pa. 1988); Banton v. Marks, 623 S.W.2d 113, 116 (Tenn. Ct. App. 1981). *Contra* Bowman v. Abramson, 545 F. Supp. 227, 228 (E.D. Pa. 1982) (dismissing as premature action for legal mal-

[in the underlying action] 'is too speculative and unrealistic for serious consideration.' "[141] These decisions, however, ignore the fact that the date on which the statute of limitation expires may be unclear and may legitimately be the subject of litigation. For example, a client may have a good-faith argument that the limitation period in the underlying action was tolled, and that the action was therefore timely filed.[142] Indeed, in two cases in which the client prevailed at the trial court level, notwithstanding the late filing of the action, it was held that the limitation period was tolled until the trial court judgment in the underlying action was reversed on appeal.[143] These cases are logically inconsistent with the notion that the client is injured as soon as the limitation period on the underlying action expires. The better reasoned rule is that as long as the client acts reasonably and in good faith in deciding when to file the underlying action, the malpractice action should be tolled until judgment is entered dismissing the plaintiff's claim.[144]

In contrast to the majority rule that injury occurs when judgment is entered in the underlying action, courts in several states have held that a cause of action for litigation malpractice is tolled until all appeals have been resolved in the underlying action.[145] Some of these

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practice based on failure to file within limitation period because cause of action would not accrue until appeals exhausted in underlying action).

141. Roberts v. Heilgeist, 465 N.E.2d 658, 661 (Ill. App. Ct. 1984) (quoting King v. Jones, 483 P.2d 815, 818 (Or. 1971)) ("In essence, it would require a plaintiff to bring suit in the hope that the tortfeasor, or his attorney, would be negligent in failing to raise the statute of limitations defense.").

142. *See, e.g.*, Finlayson v. Sanbrook, 13 Cal. Rptr. 2d 406, 408 n.3 (Ct. App. 1992) (noting that plaintiff's counsel believed that the underlying action would be held timely based on authority which was overruled by the California Supreme Court after the underlying action was filed).

143. *See* Brewer v. Davis, 593 So. 2d 67, 68-69 (Ala. 1991) (where judgment was entered on jury verdict favorable to plaintiffs, plaintiffs sustained no loss or injury until Alabama Supreme Court reversed the trial court's judgment); Chicoine v. Bignall, 835 P.2d 1293, 1298 (Idaho 1992) (action for legal malpractice for failure to timely file motion for new trial did not accrue until Idaho Supreme Court reversed trial court order granting a new trial, because "[s]o long as the trial court's order stood, Chicoine was entitled to a new trial despite the untimeliness of the motion").

144. *See infra* text accompanying notes 338-54.

145. *See* Bowman v. Abramson, 545 F. Supp. 227, 228, 231 (E.D. Pa. 1982); Amfac Distrib. Corp. v. Miller, 673 P.2d 795, 796 (Ariz. Ct. App.), *aff'd as supplemented*, 673 P.2d 792, 793-94 (Ariz. 1983); Peat, Marwick, Mitchell & Co. v. Lane, 565 So. 2d 1323, 1325-26 (Fla. 1990) (accountant malpractice) (citing with approval seven Florida appellate decisions involving legal malpractice); Neylan v. Moser, 400 N.W.2d 538, 542 (Iowa 1987); Dearborn Animal Clinic v. Wilson, 806 P.2d 997, 1006 (Kan. 1991) (dictum) (stating that "the [rule] which generally will be applicable . . . is that the statute of limitations does not begin to run until the underlying litigation is finally determined," but not applying rule in transactional malpractice case); Hibbard v.

courts reason that "[u]ntil the underlying . . . cases are decided adversely to the plaintiff the case against his former attorneys is hypothetical and his damages are speculative."[146] The reasoning in these cases has been criticized for failing to recognize the monetary injury to a client that occurs when a judgment is entered against the client at the trial court level.[147] Other cases emphasize the practical benefit of tolling the malpractice action until the underlying case is concluded, reasoning that a favorable outcome in the underlying action may render the malpractice action unnecessary.[148] While this consideration may justify tolling the malpractice action until a judgment is entered at the trial court level,[149] it ignores the fact that after a judgment is entered, "the effort [to avoid or mitigate damages] usually is unsuccessful since the vast majority of appeals are affirmed."[150] Still other

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Taylor, 837 S.W.2d 500, 502 (Ky. 1992); K.J.B., Inc. v. Drakulich, 811 P.2d 1305, 1306 (Nev. 1991); Semenza v. Nevada Medical Ins. Co., 765 P.2d 184, 186 (Nev. 1988); Hughes v. Mahaney & Higgins, 821 S.W.2d 154, 157 (Tex. 1991).

146. *Bowman*, 545 F. Supp. at 228. *See also Amfac Distrib. Corp.*, 673 P.2d at 796 ("Where there has been no final adjudication of the client's case in which the malpractice allegedly occurred, the element of injury or damage remains speculative and remote . . . . "); *Semenza*, 765 P.2d at 186.

147. Thus, in Chambers v. Dillow, 713 S.W.2d 896, 898-99 (Tenn. 1986), the court said:

> Plaintiff was liable for the court costs of his dismissed lawsuit, he had suffered a lengthy delay in the progress of his case, even if it be assumed it was subject to revival, and at a minimum had lost the interest on the use of an anticipated money recovery. Also he was immediately faced with the necessity to incur additional attorney's fees, all as a direct result of Frost's negligence.

See also Wettanen v. Cowper, 749 P.2d 362, 365 (Alaska 1988) (client "suffered actual harm upon the entry of judgment . . . [and] by having to retain new counsel and to pay costs associated with appealing the trial court's denial of his motion to set aside the amended partial judgment"); Hayden v. Green, 420 N.W.2d 201, 206 (Mich. Ct. App.) (Hood, J., dissenting) (client incurred time and expense in prosecuting appeal and paid court reporter to prepare transcript), *rev'd and dissenting opinion adopted*, 429 N.W.2d 604 (Mich. 1988). *But see Amfac Distrib. Corp.*, 673 P.2d at 798 (although Amfac suffered out-of-pocket loss at time judgment was entered, loss was contingent on outcome of appeal because costs could be recovered if appeal was successful).

148. *See, e.g.*, *Bowman*, 545 F. Supp. at 228 ("Should the Superior Court reverse the trial court and allow the medical malpractice cases to proceed, the law suit here will become moot."); Washington v. Georges, 837 S.W.2d 146, 148 (Tex. Ct. App. 1992) (limitation period is tolled "to give the legal system a chance to resolve the case in the client's favor before commencing limitations on his right to sue the lawyer."); Drake v. Simons, 583 So. 2d 1074, 1075 (Fla. Dist. Ct. App. 1991) (stating that the threshold question is:

> If the lower court's ruling, which was adverse to the client, was reversed on appeal, would the client still have a legal cause of action for malpractice? Where the response to this question is in the negative, the statute of limitations begins to run at the time an appellate decision is rendered . . . .).

Semenza, 765 P.2d at 186 ("[T]his court will not countenance interlocutory-type actions for legal malpractice brought to trial while an appeal of the underlying case is still pending.").

149. *See supra* text accompanying notes 109-14.

150. LEGAL MALPRACTICE, *supra* note 42, § 18.11, at 46 (citing Laird v. Blacker, 828 P.2d 691, *cert. denied*, 113 S. Ct. 658 (1992)). *But see* Stroud v. Ryan, 763 S.W.2d 76, 78 (Ark. 1989) (although limitation period accrued when default judgment was entered in trial court, limitation

cases have justified tolling the malpractice action because of the risk that the client will be forced to take inconsistent positions in the underlying case and the malpractice action.[151] This rationale also has been criticized on the grounds that courts should recognize that "it is sometimes necessary for parties to maintain alternative, inconsistent and even mutually exclusive positions in the course of litigation."[152]

2. Malpractice in Transactional Setting

a. In General

Unlike malpractice which occurs during litigation, transactional malpractice occurs before any underlying litigation is commenced. However, transactional malpractice often is not discovered until an action is filed concerning the underlying transaction, or at least until a dispute arises concerning the parties' rights and obligations. Consequently, there are a number of possible events which could be deemed to constitute injury resulting from transactional malpractice for purposes of accrual of the statute of limitation. Injury could be deemed to occur (a) when the transaction is entered into by the client, or when the client acts upon the attorney's advice;[153] (b) when the other party to the transaction takes some action inconsistent with the client's as-

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period was tolled during period that default judgment was vacated by court of appeals until it was reinstated by Arkansas Supreme Court); Fliegel v. Davis, 699 P.2d 674, 675-76 (Or. Ct. App. 1985) (where court of appeals reversed judgment against client, malpractice action did not accrue until Oregon Supreme Court reversed court of appeals opinion and reinstated original judgment).

151. *See, e.g.*, Peat, Marwick, Mitchell & Co. v. Lane, 565 So. 2d 1323, 1326 (Fla. 1990) ("To require a party to assert these two legally inconsistent positions in order to maintain a cause of action for professional malpractice is illogical and unjustified.") (accountant malpractice); Dearborn Animal Clinic v. Wilson, 806 P.2d 997, 1006 (Kan. 1991) (quoting United States Nat'l Bank of Or. v. Davies, 548 P.2d 966, 970 (Or. 1976)); Hughes v. Mahaney & Higgins, 821 S.W.2d 154, 156-57 (Tex. 1991).

152. Braud v. New England Ins. Co., 576 So. 2d 466, 469-70 (La. 1991) (citing, inter alia, FED. R. CIV. P. 8(e)(2)) ("A party may also state as many separate claims or defenses as he has regardless of consistency . . . ."). It should be noted, however, that California does not have a statute or rule comparable to Federal Rule 8(e)(2) or to the Louisiana statutes cited in the opinion.

153. *See, e.g.*, Arizona Management Corp. v. Kallof, 688 P.2d 710, 713 (Ariz. Ct. App. 1984) (injury or damaging effect occurred on the date agreement was entered into); Grunwald v. Bronkesh, 621 A.2d 459, 464-65 (N.J. 1993) (dictum) ("Legally-cognizable damages occur when a plaintiff detrimentally relies on the negligent advice of an attorney."); Binstock v. Tschider, 374 N.W.2d 81, 85 (N.D. 1985) (plaintiff injured when option to purchase land created by execution of documents drafted by attorney); Hennekens v. Hoerl, 465 N.W.2d 812, 818 (Wis. 1991) (plaintiff suffered actual damage "when [he] received negligently drafted legal documents," or on date performance was due); *cf.* Jaquith v. Ferris, 687 P.2d 1083, 1086 (Or. 1986) (realtor's negligence, but relying on legal malpractice cases: "Plaintiff's contractual obligation itself constituted harm.").

serted rights;[154] (c) when a dispute arises concerning the rights and obligations of the parties, or when an action is filed by either party to the transaction;[155] (d) when a client incurs attorneys' fees in defending his or her legal position;[156] (e) upon entry of judgment adverse to the client at the trial court level;[157] or (f) after the adverse judgment has been sustained on appeal.[158]

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154. *See, e.g.*, Leighton Ave. Office Plaza, Ltd. v. Campbell, 584 So. 2d 1340, 1343 (Ala. 1991) (action for failure to record interest in limited partnership; injury occurred when office building was sold without consent); Myers v. Wood, 850 P.2d 672, 673 (Ariz. Ct. App. 1992) (contract for sale of business; injury occurred when buyer defaulted); Zitrin v. Glaser, 621 So. 2d 748, 749-50 (Fla. Dist. Ct. App. 1993) (per Moe, J., with Stone, J., concurring on other grounds) (action for negligent drafting of employment agreement; injury occurred when employee left employment rather than when contract entered into); Bonz v. Sudweeks, 808 P.2d 876, 877 (Idaho 1991) (action for negligent failure to release lis pendens; damage occurred when third-party investor declined to invest in property); Dearborn Animal Clinic v. Wilson, 806 P.2d 997, 1006 (Kan. 1991) ("Further monetary damage was incurred . . . when Holenbeck ceased making any payments to Central . . . ."); Sabes & Richman, Inc. v. Muenzer, 431 N.W.2d 916, 918 (Minn. Ct. App. 1988) (action for failure to register copyright; injury occurred when third party distributed similar work); Grunwald v. Brankesh, 621 A.2d 459, 467 ("[W]e conclude that damage occurred when Resorts refused to close on the property after Grunwald had bypassed another offer.").

155. *See, e.g.*, *Leighton Ave.*, 584 So. 2d at 1343 (action for negligence in closing sale of office building; injury occurred when limited partners filed complaint against partnership); Rayne State Bank & Trust Co. v. National Union Fire Ins. Co., 483 So. 2d 987, 996 (La. 1986) (action for negligent drafting of mortgages; damage was speculative until debtor filed adversary proceeding in bankruptcy to have mortgages declared invalid).

156. Palisades Nat'l Bank v. Williams, 816 P.2d 961, 963 (Colo. Ct. App. 1991) (client suffers injury when "damage in the form of legal fees is incurred to ameliorate the impact of [the alleged] negligence."); Griggs v. Nash, 775 P.2d 120, 125 (Idaho 1989) (client suffered damage when incurred attorney fees in defending claims filed by third party); Dearborn Animal Clinic v. Wilson, 806 P.2d 997, 1006 (Kan. 1991) ("[T]he plaintiffs clearly suffered monetary damage when they had to retain counsel to enforce their interpretation of the contract . . . ."); Dixon v. Shafton, 649 S.W.2d 435, 438 (Mo. 1983) (plaintiffs suffered some damage no later than date on which they retained independent counsel); *Grunwald*, 621 A.2d at 465 ("[A] client may suffer damages, in the form of attorney's fees, before a court has announced its decision in the underlying action."); Jaquith v. Ferris, 687 P.2d 1083, 1086 (Or. 1984) (realtor's malpractice; "The legal costs plaintiff assumed to resist her contractual duty to convey likewise constituted harm."); Magnuson v. Lake, 717 P.2d 1216, 1219-20 (Or. Ct. App. 1986) (applying *Jaquith* to legal malpractice action).

157. Spivey v. Trader, 620 So. 2d 212, 215 (Fla. Dist. Ct. App. 1993) (action for negligent advice regarding incorporation; damage occurred, at the earliest, at time judgment entered in personal injury action subjecting property of corporation to execution).

158. Doyle v. Linn, 547 P.2d 257, 259 (Colo. Ct. App. 1975) (surveyor's negligence; "The mere assertion of a claim of adverse title does not in and of itself constitute damage. . . . Here plaintiffs suffered no damages until the adverse claim of the government was determined to be valid [on appeal]."); Peat, Marwick, Mitchell & Co. v. Lane, 565 So. 2d 1323, 1325-26 (Fla. 1990) (accountant malpractice; "[A] cause of action for legal malpractice does not accrue until the underlying legal proceeding has been completed on appellate review . . . ."); *Dearborn Animal Clinic*, 806 P.2d at 1006 (dictum) ("[T]he better rule, and the one which generally will be applicable . . . is that the statute of limitations does not begin to run until the underlying litigation is finally determined"; but declining to apply rule in action for negligent drafting of purchase agreement).

Upon further analysis, however, the six possible dates of injury can be boiled down to three views of when injury occurs. The first view is that injury occurs upon the effective date of the transaction or agreement. In many cases, this date is the same as the date on which the transaction is closed or the agreement executed.[159] In many other cases, however, performance is not due until some date in the future. In such a case, although the agreement may have been negligently drafted, generally the client is not injured until the other party fails to perform in accordance with the client's understanding of the substance of the transaction.[160] For example, a negligently drafted security agreement does not cause injury to the client until the other party defaults, because if the other party carries out its contractual obligations, there is no need to resort to security.[161] Similarly, negligence in drafting an option agreement generally will not cause injury until the option is either exercised or lapses.[162] Finally, the failure to include a covenant not to compete in an employment contract usually will not cause injury until the employee leaves to go elsewhere.[163] The view that injury occurs upon the effective date of the transaction rests on the rationale that:

> "the judicial process does not create liabilities or destroy rights, but only declares what is present through the process of determining the facts and applying the law. Thus, a right, remedy or interest is usu-

159. *See, e.g.*, Arizona Management Corp. v. Kallof, 688 P.2d 710, 713 (Ariz. Ct. App. 1984); *Jaquith*, 687 P.2d at 1085 (realtor's negligence).

160. California has expressly recognized this principle in subsection (b) of Code of Civil Procedure § 340.6, which provides: "In an action based upon an instrument in writing, the effective date of which depends on some act or event of the future, the period of limitations provided for by this section shall commence to run upon the occurrence of such act or event." CAL. CIV. PROC. CODE § 340.6(b) (West 1982). One commentator has opined that this subsection is a "vestige" of the original draft of A.B. 298 which was rendered unnecessary by the subsequent amendment adding the "actual injury" tolling provision to subsection (a). *See* Mallen, *supra* note 42, 53 CAL. ST. B.J. at 168.

161. *See, e.g.*, Myers v. Wood, 850 P.2d 672, 673 (Ariz. Ct. App. 1992); *accord* Johnson v. Simonelli, 282 Cal. Rptr. 305, 308 (Ct. App. 1991).

162. *See, e.g.*, Grunwald v. Bronkesh, 621 A.2d 459, 467 (N.J. 1993) (injury occurred when third party declined to exercise option). At least one court has taken the opposite view. *See* Binstock v. Tschider, 374 N.W.2d 81, 85 (N.D. 1985) (client was injured when option was created, rather than at time option was executed, because option diminished value of land). However, this case can justifiably be criticized on the ground that if the other party had not exercised the option, the asserted "loss" would never have been realized.

163. *See, e.g.*, Zitrin v. Glaser, 621 So. 2d 748, 749-50 (Fla. Dist. Ct. App. 1993) (injury occurred when employee left employment rather than when contract entered into) (per Moe, J., with Stone, J., concurring on other grounds). It is possible, however, that an injury could occur earlier if an employee threatened to leave and used the lack of a covenant not to compete to extract concessions from his or her employer.

> ally lost, or a liability is imposed at the time of a lawyer's error, even though a court does not so declare until a later date."[164]

This view has been criticized on the ground that the loss or liability is not "actual" unless and until the other party brings an action to enforce the rights assertedly created by the negligently drafted agreement and prevails.[165]

The second view is that injury occurs whenever the plaintiff incurs attorneys' fees or any other kind of monetary injury, however small, in defending his or her legal position.[166] The cases supporting this view include cases holding that the cause of action does not accrue until an action is brought against the client, because the rationale of those cases is that it is reasonably certain that the client will have to incur attorneys' fees once an action is filed.[167] These cases rest on the rationale that once attorneys' fees have been incurred, the *fact* of injury has become certain, and "[u]ncertainty as to the total *extent* of the damage does not delay accrual of the claim itself."[168]

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164. LEGAL MALPRACTICE, *supra* note 42, § 18.11, at 42. *See, e.g.*, Arizona Management Corp. v. Kallof, 688 P.2d 710, 713 (Ariz. Ct. App. 1984) ("[T]he fact that the validity of the lease agreement was not judicially established until the appellate process had been exhausted does not change the fact that appellant was damaged at the time he lost rights because of the alleged negligently drafted . . . agreement."); *Grunwald*, 621 A.2d at 465 ("We recognize . . . that inherent in a system permitting appeals is the possibility that damages may be extinguished or altered retroactively. . . . That circumstance, however, does not alter the time when the underlying injury or harm occurs . . . ."); Hennekens v. Hoerl, 465 N.W.2d 812, 816 (Wis. 1991) ("[I]njury to a legal interest or loss of a legal right constitutes actual damage before such an injury or loss produces monetary loss.").

165. *See, e.g., Hennekens*, 465 N.W.2d at 826 (Steinmetz, J., dissenting); *see also* Peat, Marwick, Mitchell & Co. v. Lane, 565 So. 2d 1323, 1326 (Fla. 1990) ("[U]ntil their tax court action was final, the Lanes did not have an action for malpractice."); Rayne State Bank & Trust Co. v. National Union Fire Ins. Co., 483 So. 2d 987, 995 (La. 1986) ("Since the mortgages were not necessarily invalid, and had never been declared invalid, it cannot be concluded that Rayne State Bank was damaged . . . at the time the mortgages were executed.").

166. *See* cases cited *supra* note 154.

167. *See, e.g.*, Rayne State Bank & Trust Co. v. National Union Fire Ins. Co., 483 So. 2d 987, 996 (La. 1986) (damage occurred when adversary proceeding filed against client because client was forced to defend action). In another case, the court held that damage occurred on the date a complaint was filed, despite the fact that the client was "not legally obligated to defend" the action until they learned of the complaint six days later. Leighton Ave. Office Plaza, Ltd. v. Campbell, 584 So. 2d 1340, 1343 (Ala. 1991). The difference in dates did not affect the outcome, and the date of filing seems to have been chosen primarily because it was objectively ascertainable.

168. Palisades Nat'l Bank v. Williams, 816 P.2d 961, 964 (Colo. Ct. App. 1991) (emphasis added). *See also* Dixon v. Shafton, 649 S.W.2d 435, 439 (Mo. 1983) ("In many actions the extent of damage may be dependent on uncertain future events . . . [;] Such uncertainties have never been held to preclude the filing of suit and, . . . have not delayed the accrual of the plaintiff's claim for purposes of the statute of limitations."); LEGAL MALPRACTICE, *supra* note 42, § 18.11, at 36-38 & nn.15-22.

The third view is that injury does not occur, and the cause of action does not accrue, "until the underlying legal proceeding has been completed on appellate review because, until that time, one cannot determine if there was actionable error by the attorney."[169] This view rests in part on the policy that "[t]o require a party to assert . . . two legally inconsistent positions in order to maintain a cause of action for professional malpractice is illogical and unjustified."[170] The court also noted that a favorable judgment in the tax court would have rendered the malpractice action moot.[171] One commentator has suggested that the leading case supporting this view may be construed as resting on the discovery rule rather than the lack of injury.[172] Although certain language in the opinion is susceptible of such an interpretation,[173] the policies of avoiding unnecessary litigation and not forcing the client to take inconsistent positions are better served by tolling the limitation period at least until entry of judgment, even if the client has previously discovered the alleged negligent act or omission.

Other courts also have recognized that judicial economy and the risk of forcing the client to take inconsistent positions may justify tolling the statute of limitation past the point at which injury might otherwise be deemed to have occurred. In *United States National Bank of Oregon v. Davies*,[174] for example, the court stated:

> There is no doubt that decedent's necessity to defend the [underlying] action caused him damage more than two years prior to the commencement of the present action. It is not so clear, however, that at that time it could yet be determined that [the] expense of

169. *Lane*, 565 So. 2d at 1325 (accountant malpractice; citing legal malpractice cases). Applying *Lane*, one case held that a cause of action for legal malpractice accrued no earlier than entry of judgment at the trial court level, where the client appealed the judgment but voluntarily dismissed the appeal five months later. Spivey v. Trader, 620 So. 2d 212, 213, 215 (Fla. Dist. Ct. App. 1993). Another Florida case has expressed the view that *Lane* is limited to litigation malpractice. Zitrin v. Glaser, 621 So. 2d 748, 749 (Fla. Dist. Ct. App. 1993). *Zitrin* is questionable because the opinion was subscribed to by only one judge, with another judge concurring but expressing the view that *Lane* was not so limited. *See id.* at 750 (Stone, J., concurring). In addition, the alleged malpractice in *Lane* (negligent tax advice) clearly occurred well before any litigation had been commenced. *Lane*, 565 So.2d at 1324-25.

170. *Lane*, 565 So. 2d at 1326. *See also supra* text accompanying notes 95-100.

171. *Lane*, 565 So. 2d at 1324, 1325 (approving and quoting court of appeals decision).

172. *See* LEGAL MALPRACTICE, *supra* note 42, § 18.11, at 50 & nn.85-86.

173. The opinion distinguishes another case on the ground that "the client understood and believed his representation had not been proper" at an earlier point, and states: "Until the tax court determination, both the Lanes and Peat Marwick believed that the accounting advice was correct . . . ." *Lane*, 565 So. 2d at 1326, 1327. However, the court goes on to state that "consequently, there was no injury," rather than "consequently, the injury had not yet been discovered." *Id.* at 1326.

174. 548 P.2d 966 (Or. 1976).

> defense *was caused by* negligent advice by defendants. In many situations, the closeness of the legal questions involved would make it impossible to ascertain until the ultimate determination of the case whether it was brought as the result of the attorney's bad advice or whether it was the result of a misapprehension on the part of the party who sued as to his legal rights. In the present instance, if decedent had won the case brought against him, he would not normally be in a position to claim that negligent advice on the part of the present defendants was a cause of his expense of defense.
>
> Plaintiff's decedent could have played it safe by filing an action against defendants immediately upon his being sued, in the event it subsequently appeared defendant's negligent advice was the cause of the action brought against him. However, it does not seem wise to encourage the filing of such provisional actions. More important, it could prove disastrous to a plaintiff's defense of the action brought against him and, thus, perhaps disastrous to his former legal advisor as well. In the present case, plaintiff's decedent would have been defending one suit or action, claiming he had acted in conformance with the law, while simultaneously maintaining an action against defendants, claiming that he had not acted in conformance with the law because of faulty advice from defendants. Such an inconsistent position would have given rise to impeachment of decedent in his defense of the action brought against him, which certainly is not desirable from either of the present parties' point of view.[175]

Despite having recognized these policies, the court failed to take them to their logical conclusion, that is, that the cause of action should be tolled at least until entry of judgment in the underlying action.[176] Instead, the court concluded that "common sense dictates that a 'later event' (the appearance of the decedent's probable liability) should take place before the statute commences to run."[177] This statement allowed later courts to conclude that the policies discussed in *Davies*

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175. *Id.* at 969, 970.

176. *Cf.* Dearborn Animal Clinic v. Wilson, 806 P.2d 997, 1005-06 (Kan. 1991) (quoting *Davies*). The *Dearborn Animal Clinic* concluded:

> In a legal malpractice action in which there is underlying litigation which may be determinative of the alleged negligence of the attorney, the better rule, and the one which generally will be applicable . . . , is that the statute of limitations does not begin to run until the underlying litigation is finally determined.

Id.

177. *Davies*, 548 P.2d at 970. *See also* Niedermeyer v. Dusenbery, 549 P.2d 1111, 1112 (Or. 1976) (restating *Davies*' holding as:

> even though damage was inflicted and harm incurred when the plaintiff was forced to assume the expense of hiring counsel to defend the claim . . . , the statute should not commence to run until such time as it appeared reasonably probable that the cost of litigation was caused by the defendant's negligence.)

apply only when the client has not yet discovered the alleged negligence.[178] This standard is insufficient to vindicate the policies discussed in *Davies*, which are applicable even if the client has discovered the alleged negligence, so long as the client's decision to attempt to mitigate damages by pursuing the underlying action is reasonable.[179]

b. Negligent Advice Regarding Taxes[180]

Two of the most common forms of transactional malpractice are negligent advice regarding the tax consequences of a transaction and negligent preparation of tax returns.[181] This situation is problematic because the error and the injury may be widely separated in time. Although liability for taxes or penalties may be incurred at the time a transaction is entered into, or at the time an incorrect return is filed, the client generally does not suffer any monetary loss unless and until the Internal Revenue Service determines the amount of any taxes and penalties owing and takes steps to collect the amount of the deficiency. Much of the confusion in this area has resulted from unfamiliarity with, and imprecise language concerning, IRS procedures. It is therefore useful to preface a discussion of these cases with an overview of the tax collection process.

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178. *See, e.g.*, Jaquith v. Ferris, 687 P.2d 1083, 1085 (Or. 1984) (realtor's negligence; "Unlike the plaintiff in *Davies*, she makes no claim that some aspect of [the underlying] suit triggered, for the first time, her knowledge of the improper land value or her realtor's possible negligence."); Magnuson v. Lake, 717 P.2d 1216, 1219 (Or. Ct. App. 1986) ("*Davies* held that a plaintiff may not be aware of an attorney's negligence until the resolution of a lawsuit which depends on the legality of an attorney's advice."); *Dearborn Animal Clinic*, 806 P.2d at 1006 (distinguishing general rule tolling action until underlying litigation is finally determined; "the statute begins to run at the time that is reasonably ascertainable that the injury was caused by the attorney's malpractice even though the underlying action may not have been finally resolved.").

179. *Compare* Lambert v. Commonwealth Land Title Ins. Co., 811 P.2d 737, 739 (Cal. 1991) (action for breach of duty to defend is equitably tolled until underlying action is terminated by final judgment) *with* Bollam v. Fireman's Fund Ins. Co., 730 P.2d 542, 547 (Or. 1986) (action for damages against liability insurer for negligent management of claim accrued when insured incurred attorney fees rather than when underlying action settled; distinguishing *Davies*).

180. For a discussion of California cases involving negligent tax advice and a proposed tolling rule for such cases, see *infra* section IV.C.3.

181. Such cases frequently involve alleged professional malpractice by accountants in addition to, or instead of, attorneys. In this situation, however, many cases have recognized that the determination of when injury occurs is the same for both attorneys and accountants. *See, e.g.*, Peat, Marwick, Mitchell & Co. v. Lane, 565 So. 2d 1323, 1325 (Fla. 1990) (accountant malpractice, but relying on legal malpractice cases: "We find that the basic principles for all professional malpractice actions should be the same . . . ."); Brower v. Davidson, Deckert, Schutter & Glassman, 686 S.W.2d 1, 2-3 (Mo. Ct. App. 1985) (malpractice cause of action against accountant and attorneys, single date of accrual); Godfrey v. Bick & Monte, 713 P.2d 655, 656-57 (Or. Ct. App.), *review denied*, 719 P.2d 874 (Or. 1986) (same).

After a tax return is filed, the IRS selects certain returns for an examination, or audit.[182] If the examiner determines there is a deficiency, the taxpayer has the option of agreeing or disagreeing with the examiner's findings. If the taxpayer agrees, the deficiency is immediately assessed and the amount owing is billed to the taxpayer.[183] If the taxpayer disagrees, the taxpayer is sent a preliminary notice of deficiency, also known as a 30-day letter, giving the taxpayer 30 days within which to file a protest and request consideration by the Appeals Office.[184] If the taxpayer does not respond within 30 days, or if a settlement cannot be reached, then the IRS sends the taxpayer a statutory notice of deficiency, also known as a 90-day letter.[185] The statutory notice of deficiency gives the taxpayer 90 days to file a petition in the United States Tax Court for redetermination of the deficiency.[186] If a petition is filed within the 90-day period, the IRS is prohibited from assessing or collecting the deficiency until the decision of the Tax Court has become final.[187] Because Tax Court review may be obtained without prior payment of the deficiency alleged to be due, "the overwhelming number of tax cases, some 95 percent, are instituted in the Tax Court."[188] The Tax Court is not confined to reviewing the administrative record; instead, it tries factual and legal

182. MICHAEL I. SALTZMAN, IRS PRACTICE AND PROCEDURE ¶ 8.01, at 8-1 to 8-5 (2d ed. 1991); PUB. NO. 556, EXAMINATION OF RETURNS, APPEAL RIGHTS, AND CLAIMS FOR REFUND 1 (Nov. 1990) [hereinafter IRS PUB. NO. 556].

183. SALTZMAN, *supra* note 179, ¶ 8.01, at 8-5; IRS PUB. NO. 556, *supra* note 179, at 2.

184. SALTZMAN, *supra* note 179, ¶ 8.01, at 8-5 to 8-6, ¶ 8.08, at 8-84 to 8-86, 8-91; IRS PUB. NO. 556, *supra* note 179, at 2-3. Although it is standard practice for the IRS to send a 30-day letter, this preliminary notice is not required by statute, and it is sometimes bypassed altogether. *Cf.* SALTZMAN, *supra*, note 179, ¶ 9.03[3] at 9-15 & n.35. The 30-day letter is therefore a poor benchmark for determining when injury occurs.

185. SALTZMAN, *supra* note 179, ¶ 8.01, at 8-6, ¶ 8.08, at 8-91; ¶¶ 9.03[3]-[4], at 9-16 to 9-20; IRS PUB. NO. 556, *supra* note 179, at 2. The 90-day letter is known as a *statutory* notice of deficiency because, subject to limited exceptions, it is required by statute to be sent before the IRS can assess or collect any deficiency. 26 U.S.C. §§ 6212, 6213(a) (1988 & Supp. V 1993).

186. 26 U.S.C. § 6213(a) (1988 & Supp. V 1993); SALTZMAN, *supra* note 179, ¶ 10.01, at 10-3, ¶ 10.03 [2][a], at 10-13 to 10-14; IRS PUB. NO. 556, *supra* note 179, at 2. The period is 150 days if the notice is addressed to a taxpayer outside the United States. 26 U.S.C. § 6213(a). Because the 90-day letter is "a notice to taxpayers that the IRS intends to assess a tax deficiency," Russell v. United States, 774 F. Supp. 1210, 1214 (W.D. Mo. 1991), it may correctly (if confusingly) be referred to as a notice of proposed assessment. However, it is not correct to refer to a notice of deficiency as an assessment or as a notice of assessment.

187. 26 U.S.C. § 6213(a) (1988 & Supp. V 1993); SALTZMAN, *supra* note 179, ¶ 1.05[2][b], at 1-32, ¶ 10.03[2][c], at 10-21. The IRS may be enjoined from assessing or collecting a deficiency during this period. 26 U.S.C. § 6213(a); SALTZMAN, *supra* note 179, ¶ 10.03[2][c], at 10-21. The decision of the Tax Court becomes final upon expiration of the time allowed for filing a notice of appeal or upon exhaustion of appellate review. 26 U.S.C. §§ 6214(d), 7481(a) (1988).

188. SALTZMAN, *supra* note 179, ¶ 1.05[2][b], at 1-33, (citing INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY ANNUAL REPORT 1988, at 38-39.)

issues de novo.[189] Decisions of the Tax Court are subject to appellate review by the United States Courts of Appeals.[190]

If the taxpayer does not timely file a petition with the Tax Court, the deficiency may be assessed immediately, and the taxpayer must pay the full amount of the assessed tax.[191] The taxpayer may then file a claim with the IRS for a refund of the amount overpaid.[192] If the claim is rejected, or is not acted upon within six months, the taxpayer may commence an action for a refund, either in a United States District Court or in the United States Claims Court.[193] As in a Tax Court proceeding, and unlike judicial review of actions by most other administrative agencies, an action for a refund "involves a de novo determination of the correct tax and is not a review of the administrative processing of the case."[194] Decisions of the district court may be appealed to the appropriate United States Court of Appeals, while decisions of the Claims Court may be appealed to the United States Court of Appeals for the Federal Circuit.[195]

Considerable confusion has been caused in cases involving negligent tax advice because some courts have incorrectly referred to a notice of deficiency as an "assessment" or have failed to distinguish between the two procedures.[196] Thus, some cases which refer to an

189. SALTZMAN, *supra* note 179, ¶ 1.05[2][b]-[c], at 1-35 to 1-36.

190. 26 U.S.C. § 7482 (1988 & Supp. V 1993); SALTZMAN, *supra* note 179, ¶ 1.05[3], at 1-39 to 1-40.

191. 26 U.S.C. § 6213(c) (1988 & Supp. V 1993); SALTZMAN, *supra* note 179, ¶ 10.01, at 10-3.

192. SALTZMAN, *supra* note 179, ¶ 8.08, at 8-93; IRS PUB. NO. 556, *supra* note 179, at 5.

193. 26 U.S.C. §§ 7422(a), 7432(a) (1988 & Supp. V 1993); SALTZMAN, *supra* note 179, ¶ 1.05[2][a], at 1-31, ¶ 8.01 at 8-6.

194. SALTZMAN, *supra* note 179, ¶ 1.05[2][a], at 1-31; *see also* ¶ 1.05[c], at 1-36.

195. 28 U.S.C. § 1291 (1988) (district courts); 28 U.S.C. § 1295 (1988 & Supp. V 1993) (Court of Federal Claims); SALTZMAN, *supra* note 179, ¶ 1.05[2][a], at 1-31 to 1-32.

196. *See, e.g.*, Graham v. Harlin, Parker & Rudloff, 664 S.W.2d 945, 946 (Ky. Ct. App. 1983) (stating that IRS "assessed a deficiency" but noting that plaintiff petitioned for redetermination in Tax Court within 90 days); Feldman v. Granger, 257 A.2d 421, 422, 425 (Md. 1969) (stating that IRS "assessed a deficiency" but noting that plaintiff contested the deficiency in Tax Court and referring to "notice of the tax deficiency" and "notice of the tax deficiency assessment"); Leonhart v. Atkinson, 289 A.2d 1, 3 & n.1, 5 (Md. 1972) (stating in text that "a substantial deficiency [was] assessed" but noting in text that plaintiffs "challenged this assessment in United States Tax Court" and referring to "notice of the tax deficiency" and "notice of the tax deficiency assessment"); May v. First Nat'l Bank of Grand Forks, 427 N.W.2d 285, 288-89 (Minn. Ct. App. 1988) (stating that IRS "issued deficiency notices" in February 1986, but later stating that IRS "assessed an actual tax deficiency" in that month); Chisholm v. Scott, 526 P.2d 1300, 1301-02 (N.M. 1974) (referring to accrual event as "notice of deficiency assessment," "assessment" and "notice by mail"); Snipes v. Jackson, 316 S.E.2d 659, 660 (N.C. Ct. App.) (action accrued when plaintiff "was notified of the tax assessment," but sequence of events suggesting assessment was notice of deficiency), *appeal dismissed and review denied*, 321 S.E.2d 899 (N.C. 1984); Wall v. Lewis, 366 N.W.2d 471, 472-73 & n.1 (N.D. 1985) (referring to "deficiency notices" as "notifica-

"assessment" as the date of injury are more properly read as holding that the limitation period commences when a notice of deficiency is received.[197] Even after correcting for these problems, however, there are no less than five different views as to when "injury" occurs and a cause of action for malpractice for negligent tax advice accrues. The first view is that injury occurs as soon as the taxpayer incurs attorneys' or accountants' fees in responding to the IRS.[198] This view is based on the premise that the fees are an element of damages in the taxpayer's malpractice suit against his or her attorneys or accountants. It can be criticized however, for failing to recognize that "administrative appeal and certainly litigation usually involve professional representation and cost, and the taxpayer will normally incur this cost no matter what the outcome."[199] Thus, such fees can only be attributed to the alleged negligence only if it can be shown that plaintiff would not have been selected for an audit if the alleged negligence had not occurred. Since there are many different reasons why a return is selected for an audit, many of which may be unrelated to the alleged malpractice, commencing the limitation period when fees are incurred is unwise.

The second view is that injury occurs, and the cause of action accrues, when the taxpayer first learns that the IRS intends to contest the amount of tax owing. This is usually deemed to occur when the preliminary notice of deficiency is received,[200] but one court has sug-

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tion of additional tax assessment" and a "deficiency assessment"); Mills v. Garlow, 768 P.2d 554, 556 (Wyo. 1989) (correctly referring to "statutory notice of deficiency," but citing cases regarding "assessment" in support of holding).

197. *See, e.g.*, *Feldman*, 257 A.2d at 425 (stating that statute of limitation began to run "from the date of this assessment of the tax deficiency," but specifying date of statutory notice of deficiency); *Leonhart*, 289 A.2d at 5 ("[T]he statute of limitations began to run when notice of the tax deficiency assessment was received."); *Chisholm*, 526 P.2d at 1302 ("[T]he statute may not be deemed to have run until four years after notice had been given by the IRS."); *Wall*, 366 N.W.2d at 473 (stating that "actual damage has been incurred no later than when the IRS has imposed a tax assessment" but relying on "the date the IRS issued its tax deficiency notices in determining date of injury").

198. *See, e.g.*, Harvey v. Dixie Graphics, Inc., 593 So. 2d 351, 353-55 (La. 1992) (limitation period commenced to run when plaintiff "incurred substantial accountant's and attorney's fees" in connection with IRS audit) Godfrey v. Bick & Monte, 713 P.2d 655, 657 (Or. Ct. App.) ("Plaintiff had been damaged more than two years before commencement of the action when he incurred attorney and accounting fees in his attempt to resolve his IRS problems."), *review denied*, 719 P.2d 874 (Or. 1986).

199. SALTZMAN, *supra* note 179, ¶ 8.08, at 8-93.

200. Isaacson, Stolper & Co. v. Artisan's Savings Bank, 330 A.2d 130, 131, 134 (Del. 1974) (stating "statute of limitations began to run when plaintiff first received notification from IRS of its 'statutory deficiency,' " but giving date of 30-day preliminary notice of deficiency rather than date of 90-day statutory notice of deficiency); Seebacher v. Fitzgerald, Hodgman, Cawthorne & King, 449 N.W.2d 673, 676 (Mich. Ct. App. 1989) (holding statute ran "when [plaintiff] received the IRS notice" rather than on date of assessment); Brower v. Davidson, Deckert, Schutter &

gested that it can occur earlier, during the audit process.[201] This vi uses the initial notice of deficiency as a surrogate for discovery of t alleged negligence.[202] It has been criticized because of the preli nary nature of the 30-day notice:

> [T]he preliminary findings of the examiner are merely proposed findings, subject to review and negotiation prior to any determination of a deficiency, unless the taxpayer agrees with such findings or fails to pursue the internal review provided by the IRS. . . . It would seem, therefore, given the provisional nature of the examining officer's proposed deficiency, that a reasonable taxpayer would not know or have reason to know that he had a cause of action against his accountant until such time as the [statutory] notice of deficiency issues or, alternatively, when the taxpayer has indicated his agreement with the IRS. . . .
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> . . . .
>
> Although we do not know how many adjustments proposed by IRS examiners are reversed or altered upon further review, we think it is a better policy to discourage the filing of lawsuits until such time as the likelihood of accountant error is established by the IRS at some point beyond the initial examiner's preliminary conclusions. We anticipate that this approach would also comport with the response of the average taxpayer to an examiner's proposed adjustments.[203]

In accordance with this criticism, a plurality of decisions follo the third view, which holds that actual injury occurs when the tax payer receives the statutory notice of deficiency.[204] These decision

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Glassman, 686 S.W.2d 1, 3 (Mo. Ct. App. 1985) (holding that statute of limitation commenced t run upon receipt of IRS agent's report rather than date of statutory notice of deficiency o settlement in Tax Court); *see also* Ford's, Inc. v. Russell Brown & Co., 773 S.W.2d 90, 92 (Ark 1989) (dictum) (even if discovery rule applied, statute would run from date plaintiffs "were firs notified of a deficiency" following an audit, rather than date of subsequent settlement and as sessment of tax).

201. *See* Gambino v. Cardamone, 414 N.W.2d 896, 899 (Mich. Ct. App. 1987) (discovery o claim occurred no sooner than date plaintiff was first contacted by IRS in connection with audi and no later than date of assessment).

202. *See* Ackerman v. Price Waterhouse, 591 N.Y.S.2d 936, 942-43 (Sup. Ct. 1992) (describing and distinguishing cases relying on 30-day notice as a benchmark), *aff'd mem.*, 604 N.Y.S.2d 721 (N.Y. App. Div. 1993).

203. Mills v. Garlow, 768 P.2d 554, 557-58 (Wyo. 1989); *see also Ackerman*, 591 N.Y.S.2d at 943:

> Any 30-day notices could have done no more than to alert plaintiffs that the legal dispute had come to the IRS's attention . . . . However, by the time of issuance of any 90-day notices, the plaintiffs would have been under a clear obligation to formulate their own independent view and to consider securing individual counsel.

204. *See* cases cited *supra* note 193; *see also* Adell v. Sommers, Schwartz, Silver & Schwartz, 428 N.W.2d 26, 31 (Mich. Ct. App. 1988) ("[P]laintiff should have discovered his damages . . . when he was notified by the IRS of the tax deficiency."); *Ackerman*, 591 N.Y.S.2d at 943-44

attribute a dual significance to the statutory notice of deficiency: first, it is regarded as sufficient to place the taxpayer on inquiry notice regarding the possibility of malpractice;[205] and second, it is a point far enough advanced in the process that it is nearly certain that the taxpayer will incur some damage, however uncertain the amount.[206] These decisions overlook the fact that the statutory notice of deficiency is not in itself an enforceable obligation. If the IRS does not assess the tax and penalties in a timely manner, or if the taxpayer successfully petitions for redetermination of the deficiency in Tax Court, the taxpayer may not suffer any damage. In addition, these decisions do not give sufficient consideration to the problems of simultaneous litigation. If a petition is filed in Tax Court, or if the taxpayer pays the deficiency and sues for a refund, the underlying action could be adversely affected by the malpractice action.

In response to the former objection, several courts have adopted a fourth view, which holds that a cause of action does not arise until the IRS assesses a deficiency.[207] The rationale for this view was first set forth by the Texas Supreme Court:

("This court adopts the 90-day notice as a better test than the assessment date, for it places any taxpayer on notice of the need to consult an attorney to consider either payment or an alternative Tax Court action."); Hoover v. Gregory, 835 S.W.2d 668, 674 (Tex. Ct. App. 1992) ("[W]e conclude that upon receipt of the Notices of Deficiency, each appellant knew or should have known that there was a risk of harm . . . that the IRS was assessing a deficiency against them."); *cf. Mills*, 768 P.2d at 557-58 (limitation period "begins to run when the taxpayer receives the statutory notice of deficiency, § 6212, or at the equivalent time when the taxpayer registers his agreement with the IRS by signing the agreement form 870").

205. *See, e.g., Ackerman*, 591 N.Y.S.2d at 943 ("[B]y the time of issuance of any 90-day notices, the plaintiffs would have been under a clear obligation to formulate their own independent view and to consider securing individual counsel."); Feldman v. Granger, 257 A.2d 421, 425 (Md. 1969) ("[W]e are of the opinion that any reasonable and prudent man . . . should have known at that time, that he had sustained legal harm as of that date, if not before.").

206. *See, e.g., Hoover*, 835 S.W.2d at 673 (Plaintiff's legal interest was "exposed to a specific and concrete risk of harm which had theretofore remained only a logical possible consequence of defendant's conduct.") (emphasis omitted); *Mills*, 768 P.2d at 558 ("Statutory notice of deficiency will not begin until such time as the likelihood of . . . error is established by the IRS at some point beyond the examiner's preliminary conclusions.").

207. *See, e.g.*, Thomas v. Cleary, 768 P.2d 1090, 1094 (Alaska Ct. App. 1989) ("Only when the tax deficiency is assessed will the tort of which the Clearys complained ripen."); Streib v. Veigel, 706 P.2d 63, 67 (Idaho 1985) ("[N]o damage was suffered until the tax return was challenged and an assessment made."); Bick v. Peat Marwick & Main, 799 P.2d 94, 101 (Kan. Ct. App. 1990) ("Assessment of the negligence penalty is the essential factor completing the wrong."); Atkins v. Crosland, 417 S.W.2d 150, 153 (Tex. 1967) ("[T]he plaintiff's cause of action did not arise until the tax deficiency was assessed."); *cf.* Wall v. Lewis, 366 N.W.2d 471, 473 (N.D. 1985) ("[A]ctual damage has been incurred no later than when the IRS has imposed a tax assessment thereby creating an enforceable obligation against the client." In *Wall*, however, the court held that injury occurred when notices of deficiency were issued).

> Prior to assessment the plaintiff had not been injured. That is, assessment was the factor essential to consummate the wrong—only then was the tort complained of completed. If a deficiency had never been assessed, the plaintiff would not have been harmed and therefore would have had no cause of action.[208]

This view has been criticized for permitting liability for negligent tax advice to extend far into the future. Courts following the "assessment" view point out that a deficiency must be assessed within three years from the date the tax return is filed.[209] However, this argument fails to recognize that the IRS and the taxpayer may agree to extend the three-year limitation period, and that the three-year period is tolled if a petition is filed in Tax Court.[210] Indeed, no case following the "assessment" view has considered whether the limitation period would continue to be postponed if a petition were filed in Tax Court, thereby delaying the date of assessment until the Tax Court decision became final. However, it has been recognized that because the deficiency may be assessed immediately if the taxpayer and the IRS agree to settle the case, the limitation period begins to run at any time during the process whenever the IRS and the taxpayer reach agreement.[211]

The fifth view, currently followed in only one state, is that if the taxpayer continues to disagree with the IRS, a cause of action for malpractice does not accrue "until the tax court action [is] final," or "until the underlying legal proceeding has been completed on appellate review."[212] This view is based primarily on the inequity of requiring a

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208. *Atkins*, 417 S.W.2d at 153. *But see Hoover*, 835 S.W.2d at 672-74 (construing *Atkins* as establishing a discovery rule of accrual rather than as requiring assessment as a precondition to accrual).

209. 26 U.S.C. § 6501(a) (1988); *see, e.g.*, *Streib*, 706 P.2d at 68; *Atkins*, 417 S.W.2d at 154; *Mills*, 768 P.2d at 557.

210. 26 U.S.C. §§ 6501(c)(4), 6503(a)(1) (1988); *see* Ackerman v. Price Waterhouse, 591 N.Y.S.2d 936, 944 (Sup. Ct. 1992) ("The use of the later assessment date is found to be inappropriate since the payment obligation is subject to an automatic stay if a Tax Court action is brought."), *aff'd mem.*, 604 N.Y.S.2d 721 (App. Div. 1993).

211. *Mills*, 768 P.2d at 557-58 (limitation period commences "when the taxpayer registers his agreement with the IRS by signing the agreement form 870," because "[a]n agreement by the taxpayer with the proposed adjustment at any point in this procedure results in a binding determination of tax liability upon which enforcement actions may immediately commence."); Wynn v. Estate of Holmes, 815 P.2d 1231, 1233-34 (Okla. Ct. App. 1991) (limitation period commenced when plaintiffs received a "deficiency assessment" from IRS after case settled; assessment also erroneously called a "deficiency notice").

212. Peat, Marwick, Mitchell & Co. v. Lane, 565 So. 2d 1323, 1325-26 (Fla. 1990). Although the facts of the case did not involve appellate review subsequent to the Tax Court settlement, the Florida Supreme Court approved of lower court decisions tolling legal malpractice actions until appellate review was completed. *Id.* at 1325.

taxpayer to maintain legally inconsistent positions in the malpractice action and the underlying Tax Court proceeding. However, the majority of cases involving Tax Court and District Court review of IRS tax determinations have concluded that the limitation period is not tolled until such review is completed.[213]

B. Limitation in Other Simultaneous Litigation Situations

1. Malicious Prosecution

An action for malicious prosecution must be filed within one year of the accrual of the cause of action.[214] In theory, there is no reason why a cause of action for malicious prosecution should not accrue at the time the underlying action is filed. At that point, a wrongful act has been committed, initiation of an action with malice and without probable cause, and an injury is, or shortly will be, suffered which includes the time, expense and emotional burden of defending a lawsuit. However, if the statute of limitation commenced to run at that point, or at the point at which the defendant retained an attorney to defend the underlying action, in most cases the malicious prosecution claim would need to be filed before the underlying action was terminated. Under these conditions, malicious prosecution would be asserted as a counterclaim in virtually every lawsuit. The substantive law wisely recognizes that this would result in a large number of unnecessary claims being filed, because the outcome of the underlying action may negate an essential element of the cause of action, lack of probable cause. To avoid this undesirable result, the substantive law provides that one of the elements that the plaintiff must plead and prove is that the underlying action "was pursued to a legal termination in [the] plaintiff's favor."[215] For purposes of accrual of the one-year statute of limitation, therefore, the question becomes: at what point is the un-

213. *See, e.g.*, Feldman v. Granger, 257 A.2d 421, 424-26 (Md. 1969) (rejecting argument that "the limitation period should not start to run until the plaintiff has exhausted all available administrative remedies"); Wall v. Lewis, 366 N.W.2d 471, 472-73 (N.D. 1985) (rejecting argument that injury did not occur until federal district court dismissed action for refund, but holding that a question of fact existed as to whether discovery occurred before that time); Hoover v. Gregory, 835 S.W.2d 668, 674-76 (Tex. Ct. App. 1992) (refusing to extend Texas rule tolling legal malpractice actions until outcome of appeals to accountant malpractice action not involving litigation malpractice).

214. Malicious prosecution is considered an injury to the person (similar to libel or slander) and therefore falls within Code of Civil Procedure § 340(3). *See* CAL. CIV. PROC. CODE § 340(3) (West 1982); Feld v. Western Land & Dev. Co., 4 Cal. Rptr. 2d 23, 26 (Ct. App. 1992); Rare Coin Galleries, Inc. v. A-Mark Coin Co., 248 Cal. Rptr. 341, 344 (Ct. App. 1988); Soble v. Kallman, 129 Cal. Rptr. 373, 374 (Ct. App. 1976).

215. Bertero v. National Gen. Corp., 13 Cal. 3d 43, 50, 529 P.2d 608, 613 (Cal. 1974).

derlying action "sufficiently terminated to authorize counter-action by the aggrieved party[?]"[216]

When no appeal is taken, "a cause of action for malicious prosecution accrues at the time judgment on the underlying action is entered in the trial court," rather than upon expiration of the time within which the opposing party could have appealed.[217] The effect of an appeal of the underlying action, however, is less certain. One court has held that an action for malicious prosecution cannot be maintained while an appeal in the underlying action is pending, and that an action filed during that time must be dismissed as premature.[218] "[T]he unstated assumption [is that] a cause of action for malicious prosecution does not accrue until an appeal from the underlying action is resolved."[219] The majority of cases, however, hold that the limitation period is tolled from the date the notice of appeal is filed "until the conclusion of the appellate process, at which time it commences to run again."[220] These cases take the view that an action filed while an appeal is pending should be stayed until the appeal is decided, rather than dismissed as premature.[221]

There are at least two possible criticisms of the rule tolling the limitation period until the conclusion of the appellate process in malicious prosecution cases. To start with, counting the relatively brief period between the entry of judgment in the trial court and the filing of the notice of appeal against the limitation period is unduly complicated and merely sets a trap for the unwary. A better rule would be to toll the limitation period until the appeal is concluded in those cases where an appeal is taken. The other criticism is more fundamental: the policies of promoting repose and avoiding deterioration of evidence may be undermined by the potential lengthy delay of the appellate process. This criticism, however, does not survive scrutiny. Because the plaintiff in the malicious prosecution action must have

216. *Soble*, 129 Cal. Rptr. at 375.

217. *Id.* at 374 (citing Anderson v. Coleman, 56 Cal. 124, 126 (1880)).

218. Friedman v. Stadum, 217 Cal. Rptr. 585, 587-88 (Ct. App. 1985).

219. Feld v. Western Land & Dev. Co., 4 Cal. Rptr. 2d 23, 27 (discussing *Friedman*).

220. Rare Coin Galleries, Inc. v. A-Mark Coin Co., 248 Cal. Rptr. 341, 344 (citing Gibbs v. Haight, Dickson, Brown & Bonesteel, 228 Cal. Rptr. 398, 402 (Ct. App. 1986)); *accord Feld*, 4 Cal. Rptr. 2d at 26. Although *Gibbs* concluded that "the appeal process was exhausted with the denial of the petition for hearing [by the California Supreme Court]," 228 Cal. Rptr. at 402, subsequent cases have held that tolling ceases upon issuance of the remittitur, *Rare Coin Galleries*, 248 Cal. Rptr. at 346; *Feld*, 4 Cal. Rptr. 2d at 26, or, in federal court, upon issuance of the mandate, Korody-Colyer Corp. v. General Motors Corp., 256 Cal. Rptr. 658, 659 (Ct. App. 1989).

221. *Feld*, 4 Cal. Rptr. 2d at 27.

received a favorable judgment at the trial court level in the underlying action, any delay pending the outcome of an appeal is attributable solely to the opposing party who filed the appeal, who will become the defendant in the malicious prosecution action.[222] Since the opposing party necessarily has notice of a potential malicious prosecution claim, by filing the appeal it may be deemed to have impliedly consented to toll the statute of limitation pending the outcome.

In drawing an analogy to malicious prosecution for purposes of analyzing the limitation of legal malpractice cases, the most important aspect is that the statute of limitation does not begin to run until a judgment has been entered at the trial court level, even though an "injury" may be said to have occurred when the underlying action was originally filed or when the defendant first incurred attorneys' fees in defending the underlying action. While this rule of accrual is a consequence of the substantive law, rather than a strictly procedural rule, it reflects a policy determination that delayed accrual or tolling will prevent the filing of a large number of actions which may be rendered moot by the outcome of the underlying action. The same consideration holds true for legal malpractice. In many cases, a favorable outcome in the underlying action will negate the existence of a malpractice cause of action,[223] and in many other cases, a favorable outcome will render the malpractice action worthless as a practical matter. Only in a small number of cases will a malpractice action still be viable despite a favorable outcome in the underlying action.[224]

2. Indemnity

Another type of action that depends on the outcome of an underlying proceeding is an action for indemnity. In an indemnity action, the indemnitee seeks reimbursement from the indemnitor for all or part of the damages which the indemnitee was required to pay to the plaintiff in the underlying action. The claim for reimbursement arises either from an express or implied contract or by operation of law.

222. It is true that a party who was unsuccessful at the trial court level might bring a malicious prosecution claim after the judgment was reversed on appeal. In that case, however, the cause of action would not accrue until the appellate decision was rendered, because until then there has not been a termination in favor of that party.

223. *See, e.g.*, ITT Small Business Fin. Corp. v. Niles, 23 Cal. Rptr. 2d 728, 733 (Ct. App. 1993) ("Had ITT prevailed in the adversary proceeding the legal malpractice action would have been unnecessary."), *review granted*, 865 P.2d 632 (1994).

224. *See* Laird v. Blacker, 2 Cal. 4th 606, 626, 828 P.2d 691, 704 (Cal.) (Mosk, J., dissenting) ("The majority's analysis defies rationality with its fictional scenario of a client who files a malpractice action against an attorney after winning the underlying lawsuit; this would be a rare situation indeed."), *cert. denied*, 113 S. Ct. 658 (1992).

"It is well settled that a cause of action for implied indemnity does not accrue or come into existence until the indemnitee has suffered *actual loss* through payment."[225] This rule applies regardless of whether the underlying action is terminated by settlement or by judgment,[226] or whether an appeal is taken in the underlying action.[227] The theory behind this rule is that the indemnitee does not suffer "actual loss" either at the time the potential liability to the third party arises, or when it becomes legally obligated to pay either by settlement or by the entry of judgment against it. Instead, "actual loss" occurs only when the obligation is satisfied by payment.[228] The rule reflects a concern about the possibility of inconsistent results.[229]

One advantage of the rule of accrual in indemnity actions is that it is a "bright-line" rule: since the date on which payment occurs is easily ascertained, the limitation issue can often be disposed of at the pleading or summary judgment stage. On the other hand, this rule can be criticized for placing too much emphasis on the policies which disfavor simultaneous litigation of claims. It is true that judicial economy may be better served by this rule in cases in which the indemnity arises from an express contract that is not the subject of the underlying action, such as a contract for liability insurance. In such cases, the issues in the indemnity action may be avoided altogether if the indemnitee prevails in the underlying action. More frequently, however, the issue of indemnity is inextricably interwoven with the underlying action, such as in actions for partial or comparative indemnity among alleged joint tortfeasors. In such cases, judicial economy would be

225. E.L. White, Inc. v. City of Huntington Beach, 21 Cal. 3d 497, 506, 579 P.2d 505, 510 (Cal. 1978) (emphasis added) (citing Sunset-Sternau Food Co. v. Bonzi, 60 Cal. 2d 834, 843, 389 P.2d 133, 139-40 (Cal. 1964)). *Accord* People *ex rel* Dep't of Trans. v. Superior Court, 26 Cal. 3d 744, 751, 608 P.2d 673 (Cal. 1980).

226. "The claim accrues at the time the indemnity claimant suffers loss or damages, that is, at the time of payment of the underlying claim, payment of a judgment thereon, or payment of a settlement thereof by the party seeking indemnity." *People ex rel. Dep't of Trans.*, 608 P.2d at 678 (quoting Maurice T. Brunner, *When Statute of Limitations Commences to Run Against Claim for Contribution or Indemnity Based on Tort*, 57 A.L.R.3d 867, 884 (1974)).

227. *See, e.g., Sunset-Sternau Food Co.*, 36 Cal. Rptr. at 733, 748 (cause of action accrued when plaintiff satisfied judgment following unsuccessful appeal).

228. "The implied promise of indemnity and reimbursement applies only to the actual loss and not to the liability incurred. Thus, the cause of action does not arise until the agent has actually paid the obligation." *Id.* at 843 (citations omitted).

229. "Indeed, if the agent could sue the principal for reimbursement prior to satisfying the outstanding obligation, he would either collect funds before incurring any expenditures and thus become unjustly enriched or would recover for a potential liability which might never mature." *Id.* at 843–44.

better served by requiring the indemnity claim to be litigated concurrently with the underlying action:

> [T]he practical advantage of requiring that actions for indemnity be brought by way of cross-complaint is the consolidation of related evidence and matters of proof in a single judicial proceeding. . . . The cross-complaint serves the purpose of permitting a complete determination of the dispute among all parties, thus avoiding circuity of proceedings. Combining these causes in a single trial is an efficient utilization of limited judicial resources.[230]

For this reason, in 1981 the Legislature amended section 901 of the Government Code to provide that for purposes of filing a claim against a public entity, "the date upon which a cause of action for equitable indemnity or partial equitable indemnity accrues shall be the date upon which a defendant is served with the complaint giving rise to the defendant's claim for [indemnity]."[231] At the same time, however, the Legislature rejected a proposal to amend the Code of Civil Procedure to provide the same rule of accrual for indemnity claims generally.[232]

The rule delaying accrual of indemnity actions until payment also places too little emphasis on the policies of promoting repose and avoiding deterioration of evidence. It allows an indemnitee to gain an unfair advantage in preserving evidence by delaying payment as long as possible. Indeed, the indemnitee may unilaterally delay accrual of the cause of action by appealing the underlying action to the California Court of Appeal, the California Supreme Court, and the United States Supreme Court. In that event, an indemnitor could potentially find itself facing an action after years of delay. While it is true that an appeal may render the indemnity action unnecessary, the chances of a favorable outcome are greatly reduced after judgment has been entered against the indemnitee at the trial court level. Thus, the policies of promoting repose and avoiding deterioration of evidence would be better served by requiring that notice be given to the indemnitor at an earlier stage in the proceedings, either upon commencement of the underlying action against the indemnitee, or at least upon entry of judgment at the trial court level.

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230. Valley Circle Estates v. VTN Consol., Inc., 33 Cal.3d 604, 614, 659 P.2d 1160, 1167 (Cal. 1983) (citations omitted).

231. CAL. GOV'T CODE § 901 (West Supp. 1994).

232. *See* 1981-82 Cal. Assembly J. 3980 (May 26, 1981) (setting forth text of proposed Code of Civil Procedure § 360.7); 1981-82 Cal. Sen. J. 5718 (Aug. 31, 1981) (deleting proposed § 360.7 from final bill).

Unlike the analogy between malicious prosecution and legal malpractice the analogy between indemnity and legal malpractice provides little guidance. Claims for legal malpractice are neither as easily separable from the underlying action as are indemnity actions based on an express contract, nor are they as intertwined with the underlying action as are indemnity claims among joint tortfeasors. Of these two extremes, however, legal malpractice actions are certainly closer in character to the former. Like a claim against a liability insurer, a malpractice claim involves matters which are collateral to the underlying claim, but which may be avoided altogether by a favorable outcome. This similarity suggests that judicial economy would be better served by tolling or delaying accrual of the limitation period for legal malpractice actions until the underlying action is resolved.

Another consideration is that the risk of taking inconsistent positions may be greater in legal malpractice cases than in cases of indemnity. In the joint tortfeasor case, for example, it is quite consistent for a defendant both to deny liability and to assert that another defendant is wholly or partially liable. It is also not uncommon for a defendant to deny liability and simultaneously to assert a cross-claim against a liability insurer or indemnitor. Although these positions may be mutually exclusive, they are not necessarily inconsistent; rather, the indemnitee's position in the underlying action is properly viewed as an alternative or contingent claim. Moreover, evidence that a party was insured by another is not admissible against the insured to prove negligence or other wrongdoing.[233] By contrast, a legal malpractice claim is not merely contingent on the outcome of the underlying action; in many cases, the legal position taken by the former attorney is the focus of the underlying action. In such a case, the hazards of arguing both sides of a single legal issue are evident.[234]

233. CAL. EVID. CODE § 1155 (West 1966).

234. The liability insurance example suggests that the problem of simultaneous litigation in malpractice cases could be addressed by enacting a rule of evidence (or making a case-by-case determination) that nothing in the malpractice action may be used against the client in the underlying action. *Cf. Id.* § 352 ("The court in its discretion may exclude evidence if its probative value is substantially outweighed by the probability that its admission will . . . (b) create substantial danger of undue prejudice, of confusing the issues, or of misleading the jury."). While certainly such a rule would mitigate or eliminate some of the risks to clients, it does nothing to reduce the number of potentially unnecessary legal malpractice actions which would be filed to preserve the cause of action pending the outcome of the underlying action.

3. Equitable Tolling

In applying statutes of limitation in simultaneous litigation contexts outside the legal malpractice area, "courts have adhered to a general policy which favors relieving [a] plaintiff from the bar of a limitations statute when, possessing several legal remedies he, reasonably and in good faith, pursues one designed to lessen the extent of his injuries or damage."[235] This policy has been implemented through the doctrine of equitable tolling.[236] "The 'equitable tolling' doctrine is a judicially created doctrine designed to prevent unjust and technical forfeitures of the right to a trial on the merits when the purpose of the statute of limitations—timely notice to the defendant of the plaintiff's claims—has been satisfied."[237]

Three elements must be present in order for the doctrine of equitable tolling to suspend the running of the statute of limitation: (1) timely notice to the defendant in filing the first claim; (2) lack of prejudice to the defendant in gathering evidence to defend against the second claim; and (3) good faith and reasonable conduct on the part of the plaintiff.[238] The timely notice requirement means that "the first claim must alert the defendant in the second claim of the need to begin investigating the facts which form the basis of the second claim."[239] To meet this requirement, several courts have held or suggested that "the defendant in the first claim [must be] the same one being sued in the second."[240] The California Supreme Court, how-

235. Addison v. State, 21 Cal.3d 313, 317, 578 P.2d 941, 943 (Cal. 1978); *see also* Elkins v. Derby, 12 Cal.3d 410, 414, 525 P.2d 81, 84 (Cal. 1974); Collier v. City of Pasadena, 191 Cal. Rptr. 681, 684 (Ct. App. 1983).

236. *Addison*, 578 P.2d at 943-44. For a history of the development of the equitable tolling doctrine, see *Collier*, 191 Cal. Rptr. at 684-85; *see also* Appalachian Ins. Co. v. McDonnell Douglas Corp., 262 Cal. Rptr. 716, 738-40 (Ct. App. 1989).

237. *Appalachian Ins. Co.*, 262 Cal. Rptr. at 738-39; *see also Elkins*, 115 Cal. Rptr. at 647 ("[T]his and other courts as well as legislators have liberally applied tolling rules or their fundamental equivalents to situations in which the plaintiff has satisfied the notification purpose of a limitations statute."); *Collier*, 191 Cal. Rptr. at 684-85 ("[T]he primary purpose of the statute of limitations is normally satisfied when the defendant receives timely notification of the first of two proceedings.").

238. *Addison*, 578 P.2d at 943-44; *see also* Mitchell v. Frank R. Howard Memorial Hosp., 8 Cal. Rptr. 2d 521, 528 (Ct. App. 1992); *Collier*, 191 Cal. Rptr. at 685.

239. *Collier*, 191 Cal. Rptr. at 685; *see also* Thompson v. California Fair Plan Ass'n, 270 Cal. Rptr. 590, 592 (Ct. App. 1990). It also has been stated that "the first claim must have been filed within the statutory period." *Collier*, 191 Cal. Rptr. at 685. While this requirement will generally hold true, as discussed below it should not be applied in legal malpractice cases in which the alleged wrongful omission is the attorney's failure to file the underlying action within the applicable limitation period. *See infra* text accompanying notes 338-441.

240. *Collier*, 191 Cal. Rptr. at 685; *see* Garabedian v. Skochko, 283 Cal. Rptr. 802, 808 (Ct. App. 1991) (citing Dowell v. County of Contra Costa, 219 Cal. Rptr. 341, 345 (Ct. App. 1985))

ever, has held otherwise. In *Lambert v. Commonwealth Land Title Ins. Co.*,[241] the court held that the limitation period for an action against an insurer for breach of the duty to defend "is equitably tolled until the underlying action is terminated by final judgment."[242] The court held that the requirement of notice was satisfied even though the insurer was not a party in the underlying action.[243] Similarly, in both *Tu-Vu Drive-In Corp. v. Davies*[244] and *County of Santa Clara v. Hayes Co.*,[245]:

> [T]he plaintiff first pursued a remedy against one defendant which, if successful, would reduce the damages which had to be sought from a second defendant . . . . In both instances, the California Supreme Court held the statute of limitations for the second action was tolled during the pendency of the first, even though the second action was brought against an entirely different defendant.[246]

The second element requires that the facts of the two claims be sufficiently similar that the investigation of the first claim will put the defendant in a position to defend the second claim. "The critical question is whether notice of the first claim affords the defendant the opportunity to identify the sources of evidence which might be needed to defend against the second claim."[247] Thus, in *Lambert*, the court held that the insurer would not be prejudiced by tolling the limitation period for a breach of the duty to defend because the insurer "will be aware that it must take the steps necessary to prepare and preserve a defense to an action by its insured."[248]

(holding that "the doctrine of equitable tolling does not apply merely because defendant *B* has obtained timely knowledge of a claim against defendant *A* for which defendant *B* knows or believes he may share liability").

241. 53 Cal.3d 1075, 811 P.2d 737 (Cal. 1991).

242. *Id.*

243. *Id.* at 741: The court stated:

> By tendering defense of a third party action to an insurer, the insured will have put the insurer on notice that it may be required under the policy to defend the action. Thus, the insured [sic, should be insurer] will be aware that it must take the steps necessary to prepare and preserve a defense to an action by its insured.

Id.

244. 66 Cal.2d 435, 426 P.2d 505 (Cal. 1967).

245. 43 Cal.2d 615, 275 P.2d 456 (Cal. 1954).

246. Collier v. City of Pasadena, 191 Cal. Rptr. 681, 686 n.7 (Ct. App. 1983) (discussing *Tu-Vu* and *Hayes*). Notice requirement satisfied where notice to one defendant results in timely collection of evidence needed by second defendant. (dictum).

247. *Id.* at 686; *see* Addison v. State, 21 Cal.3d 313, 319, 578 P.2d 941, 944 (Cal. 1978) (finding no prejudice to defendants was shown where defendants "had the opportunity to begin gathering their evidence and preparing their defense" during the pendency of the underlying action).

248. 811 P.2d at 741. The opinion actually reads: "Thus, the insured [sic] will be aware that it must take the steps necessary to prepare and preserve a defense to an action by its insured." *Id.* In the context of a suit by an insured against an insurer for breach of the duty to defend, it is

The third element, good faith and reasonable conduct on the part of the plaintiff, is satisfied "when the plaintiff has several alternative remedies and makes a good faith, reasonable decision to pursue one remedy in order to eliminate the need to pursue the other."[249] Thus

> "statutes of limitation ha[ve] been tolled when a plaintiff filed a case which promised to lessen the damages or other harm that might have to be remedied through a second case. The statute for the second case was tolled while the plaintiff pursued the first, presumably to further the public purpose of minimizing harm."[250]

This element also requires that the plaintiff exercise reasonable diligence in pursuing the first remedy. Thus

> "equitable tolling is not available to a plaintiff whose conduct evidences an intent to delay disposition of a case without good cause; and it is certainly not available to a plaintiff who engages in the procedural tactic of moving the case from one forum to another in the hopes of obtaining a more favorable ruling."[251]

The doctrine of equitable tolling serves to balance the policies underlying statutes of limitation against the policies which favor litigation of disputes on their merits and which disfavor simultaneous litigation of related but separate lawsuits. First, it vindicates the policy which favors litigation of disputes on their merits by avoiding forfeitures, while at the same time it ensures that the policies of repose and of avoiding deterioration of evidence are satisfied by requiring timely notice and lack of prejudice to defendants.[252] Second, "it avoids the hardship upon plaintiffs of being compelled to pursue simultaneously several duplicative actions upon the same set of facts."[253] This consideration was considered dispositive in *Lambert:*

> It is harsh to require an insured—often a private homeowner—to defend the underlying action, at the homeowner's own expense, and *simultaneously* to prosecute—again at the homeowner's own expense—a separate action against the title company for failure to defend. "[T]he unexpected burden of defending an action may it-

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clear that the quoted sentence contains a typographical error and that the subject of the sentence should read "insurer."

249. Mitchell v. Frank R. Howard Memorial Hosp., 8 Cal. Rptr. 2d 521, 529 (Ct. App. 1992).

250. *Collier*, 191 Cal. Rptr. at 684.

251. *Mitchell*, 8 Cal. Rptr. 2d at 529.

252. Addison v. State, 21 Cal.3d 313, 319, 578 P.2d 941, 944 (Cal. 1978); *Collier*, 191 Cal. Rptr. at 686 & n.8.

253. *Collier*, 191 Cal. Rptr. at 687; *Addison*, 578 P.2d at 944 ("We discern no reason of policy which would require plaintiffs to file simultaneously two separate actions based upon the same facts . . . since 'duplicative proceedings are surely inefficient, awkward and laborious.' ").

> self make it impractical to immediately bear the additional cost and hardship of prosecuting a collateral action against an insurer."[254]

Third, the doctrine promotes judicial economy to the extent that the disposition in the underlying action "may render the proceeding in the second [action] unnecessary or easier and cheaper to resolve."[255] Finally, the doctrine avoids the risk of forcing plaintiffs to take inconsistent positions in two different actions.[256]

> We also believe that respect for our legal system . . . is hardly enhanced by a[n] incongruent procedural structure which causes an injured party to simultaneously allege before different tribunals propositions which are mutually inconsistent. Absent a tolling rule, this is precisely the strategy to which a party unsure of his remedy must resort to in order to protect his right to recovery.[257]

IV. APPLYING EQUITABLE TOLLING TO LEGAL MALPRACTICE ACTIONS

A. *ITT Small Business Finance Corp. v. Niles*

In December 1984, ITT retained Niles to act as its attorney in connection with preparation of certain loan documents and the closing of a $200,000 loan to California Solution, Inc.[258] The loan documents contained a security agreement granting ITT a security interest in certain assets of California Solution, liens on three pieces of real property and a pledge of stock as collateral. On February 16, 1988, California Solution filed for bankruptcy. Two years later, on February 14, 1990, California Solution commenced an adversary proceeding in bankruptcy court against ITT, claiming that the loan documentation which Niles had drafted on ITT's behalf was inadequate. Five months later, on July 11, 1990, ITT sent a letter to Niles informing him that ITT expected him to indemnify ITT for any loss suffered in the adversary proceeding and advising Niles to contact his malpractice insurer. During the next two years, ITT vigorously contested the allegations that the loan documentation was insufficient. Finally, on January 28, 1992, ITT entered into a settlement agreement with California Solution for

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254. 811 P.2d at 740.

255. *Collier*, 191 Cal. Rptr. at 687; *see also* Elkins v. Derby, 12 Cal.3d 410, 412, 525 P.2d 81, 86 (Cal. 1974).

256. *Elkins*, 525 P.2d at 88.

257. *Id.*

258. The statement of facts in this paragraph is adapted from the Court of Appeal opinion in ITT Small Business Fin. Corp. v. Niles, 23 Cal. Rptr. 2d 728, 729 (Ct. App. 1993), *review granted*, 865 P.2d 632 (1994).

an amount less than the full value of its security. Two months later, on March 16, 1992, ITT filed a legal malpractice action against Niles.

The trial court granted summary judgment in favor of Niles on the grounds that the statute of limitation barred the malpractice action, and ITT appealed. The Second District Court of Appeal reversed. In an opinion written by Justice Johnson, the court held that:

> ITT did not suffer actual injury until January 28, 1992, when it was forced to accept an adverse settlement with California Solution, Inc. at the trial court level in the adversary proceedings. Until that moment it was entirely possible ITT could have prevailed in those proceedings by establishing the loan documentation was sufficient and then suffered no actual injury.[259]

The court relied in part on the statement in *Laird v. Blacker* that "the limitations period commences when a client suffers an adverse judgment or order of dismissal in the underlying action on which the malpractice action is based."[260] The court also rejected Niles' argument that "ITT suffered actual injury when forced to incur legal fees in order to defend itself in the adversary proceeding."[261] In so holding, the court brought itself squarely into conflict with other court of appeal cases holding that "[a] client suffers damage when he is compelled, as a result of the attorney's error, to incur or pay attorney fees."[262] The *ITT* opinion also conflicts with another court of appeal case which held in similar circumstances that the client suffered actual injury when the debtor first defaulted on the loan.[263] Justice Johnson's attempts to distinguish these conflicting cases are unpersuasive at best[264] and erroneous at worst.[265]

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259. *Id.* at 731.

260. 2 Cal.4th 606, 609, 828 P.2d 691, 692 (Cal. 1992).

261. *ITT Small Business Fin. Corp.*, 23 Cal. Rptr. 2d at 731.

262. Sirott v. Latts, 8 Cal. Rptr. 2d 206, 209 (Ct. App. 1992); *accord* Bennett v. McCall, 23 Cal. Rptr. 2d 268, 270 (Ct. App. 1993); Kovacevich v. McKinney & Wainwright, 19 Cal. Rptr. 2d 692, 696 (Ct. App. 1993).

263. *See* Johnson v. Simonelli, 282 Cal. Rptr. 206, 208-09 (Ct. App. 1991). The corresponding date in the *ITT* case would be February 16, 1988, the date California Solution filed for bankruptcy. *But see* Slavin v. Trout, 23 Cal. Rptr. 2d 219, 222-24 (Ct. App. 1993) (action for negligent appraisal; rejecting *Johnson's* conclusion that statute of limitation commences to run upon default because "[t]he lender's resort to the property does not occur until later and it is at that point the lender suffers appreciable harm").

264. The *ITT* opinion distinguishes *Johnson v. Simonelli* on the ground that "[i]n *Johnson* it was clear [that] the attorneys' behavior left their client with inadequate security," whereas "*ITT* litigated the adequacy of the security issue for years before it was clearly determined [that] Niles' behavior left it without ample security." 23 Cal. Rptr. 2d at 731-32. However, the opinion in *Johnson* specifically acknowledged the possibility that the security might have been found to be adequate in the underlying litigation and rejected the argument that this uncertainty should toll the limitation period. 282 Cal. Rptr. at 208. "Hence, at the time of default on the note if the

In rejecting the argument that the attorneys' fees incurred by ITT constituted "actual injury," Justice Johnson reasoned that:

> the whole question of whether ITT was damaged at all was contingent on the outcome of adversary proceedings, [because] [u]ntil that time the attorney fees it was paying were the result of California Solution's *claim* [that] ITT's documentation was insufficient[,] not Niles' actual failure to prepare adequate documentation. Those same fees would have been incurred even if ITT "won" the settlement conference and obtained its full security or full payment of the debt. Only after ITT "lost" that settlement conference could it be said the firm sustained "actual damages" which in fact were attributable to the alleged negligence of its former lawyer, Niles."[266]

This argument recognizes that because legal questions are rarely clear-cut, causation of damages often will be difficult or impossible to determine until the outcome of the underlying action.[267] However, it was clear no later than July 11, 1990, that ITT suspected that Niles had committed malpractice and therefore also suspected that the attorneys' fees it was incurring were possibly caused by the malpractice. Indeed, those attorneys' fees constituted one of the elements of damages claimed by ITT in the malpractice action.[268] Under general tort limitation principles, ITT's suspicion would be sufficient to start the

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security was adequate, plaintiff had no cause of action; if the security was inadequate, actual injury occurred and the statute of limitation commenced running." *Id.* Similarly, the *ITT* opinion distinguishes *Kovacevich* on the ground that the legal fees in that case "were incurred after the client accepted the adverse position in which the former lawyer's actions had placed him." 23 Cal. Rptr. 2d at 732 n.2. Although the opinion in *Kovacevich* is not inconsistent with this supposition, there is nothing in the opinion to indicate that such was the case or that the court's holding was limited to circumstances in which liability was clear.

265. The *ITT* opinion distinguishes *Sirott* on the ground that "[t]here the legal fees which represented the 'actual injury' were incurred *after* the arbitration award was confirmed which established the lawyer had committed malpractice in advising [that] his client's insurance coverage survived." 23 Cal. Rptr. 2d at 731. This statement is wrong: *Sirott* expressly states that "[p]laintiff incurred attorney fees in defending the medical malpractice action not later than January 20, 1987," whereas the arbitration award was rendered on August 7, 1987, and "was confirmed by judgment entered January 7, 1988." 8 Cal. Rptr. 2d at 209. It is interesting to note that both *Sirott* and *ITT* were decided by the same three-judge panel, and that Justice Johnson, the author of *ITT*, was the dissenting justice in *Sirott*.

266. 23 Cal. Rptr. 2d at 732.

267. *See* United States Nat'l Bank of Or. v. Davies, 548 P.2d 966, 969 (Or. 1976).

268. *Cf.* Budd v. Nixen, 6 Cal.3d 195, 202, 491 P.2d 433, 437 (Cal. 1971) ("[P]laintiff would have had a viable claim, as tort damages, for the fees he paid Deissler, his second attorney, to the extent that such fees compensated that attorney for his efforts to extricate plaintiff from the effect of defendant's negligence.") *superceded by* CAL. CIV. PROC. CODE § 340.6 (West 1982) as stated in Laird v. Blacker, 279 Cal. Rptr. 700, 711 (Ct. App. 1991), *aff'd*, 828 P.2d 691 (Cal. 1992).

limitation period running.[269] Moreover, it is possible in theory for a client to have a claim for damages to recover attorneys fees even if it receives a favorable judgment in the underlying action.[270] It is therefore a legal fiction to pretend that the attorneys' fees incurred by ITT in defending the loan documents drafted by its former attorney did not constitute "actual injury" at the time they were incurred, but did constitute "actual injury" in retrospect after negligence (and therefore causation) was confirmed.

Nonetheless, there are compelling policy reasons supporting the view that "actual injury" should not be deemed to occur until the underlying action has been terminated at the trial court level.[271] As the *ITT* court explained:

> First, it would be impractical for a lender to commence an action against its attorney every time one of its debtors challenged the validity of the lender's legal position and thus the soundness of its lawyers' legal work. This would be a substantial and unwelcome addition to the already overwhelming case load our courts must handle. . . . [I]t is more practical to wait until the debtor establishes that the lender's legal position indeed is weak and the security is found to be inadequate, before commencing the statute of limitations on the attorney malpractice cause of action.
>
> Second, it would be unreasonable to compel ITT to commence the malpractice action at the same time it was litigating the adversary proceeding. ITT would have to defend Niles' performance as its lawyer in the "adversary proceedings" while simultaneously arguing this same performance constituted professional negligence in its legal malpractice action. In a smaller jurisdiction this could entail defending the work of the attorney in the morning, while in the afternoon making the complete opposite argument, both times in front of the same judge. In a larger jurisdiction, where different judges would hear each matter, this could result in different outcomes based on the same set of facts . . . .
>
> Finally, it is a waste of judicial time as well as private resources to require both matters to be litigated when the outcome in one

269. *See, e.g.*, Jolly v. Eli Lilly & Co., 44 Cal.3d 1103, 1110, 751 P.2d 923, 927 (Cal. 1988) ("Under the discovery rule, the statute of limitations begins to run when the plaintiff *suspects* or *should suspect* that her injury was caused by wrongdoing.") (emphasis added).

270. For example, suppose an attorney files an action for personal injury more than one year after the date of the accident. Even if the client is able to defeat a motion for summary judgment on limitation grounds (for example, by invoking a delayed discovery rule), the client might still have a claim for damages to recover the attorney's fees spent litigating the limitation issue if the client proves that the motion would not have been brought if the action had been filed within one year, and that an ordinary attorney acting reasonably would have done so.

271. *See supra* Part II and accompanying text.

> may render the other unnecessary. Had ITT prevailed in the adversary proceeding the legal malpractice action would have been unnecessary. Even when the client loses the underlying action, as was the case at hand, it makes sense to litigate the malpractice action second. Normally many of the issues relevant in the malpractice action will have been decided in the underlying action thus shortening the malpractice case.[272]

Of course, these same considerations were raised in *Laird v. Blacker* to justify tolling the limitation period until any *appeals* were resolved in the underlying action,[273] and were rejected by the majority. However, all of these considerations bear considerably greater weight before a judgment is entered in the underlying action.[274] In addition, there is evidence to suggest that the statutory requirement that "actual injury" must occur before the limitation period commences to run was intended to reduce unnecessary litigation by encouraging clients who have discovered allegedly negligent conduct to wait and see if the conduct adversely affects the outcome of the underlying action before filing suit.[275]

It is possible to resolve the problem of defining "actual injury" in the *ITT* case in a manner consistent with the policies underlying the statute of limitation by applying the doctrine of equitable tolling. All three elements of the doctrine are present in *ITT*. First, ITT provided timely notice to the defendant, Niles, shortly after the underlying action was commenced against it.[276] ITT's letter of July 11, 1990, specifically placed Niles on notice that he might be called upon to defend a legal malpractice action if ITT was not successful in defending his work in the underlying action.[277] Second, Niles was not prejudiced in gathering evidence because "notice of the first claim afford[ed] the defendant the opportunity to identify the sources of evidence which

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272. *ITT Small Business Fin. Corp.*, 23 Cal. Rptr. 2d at 732-33 (footnote omitted); *see also* Pleasant v. Celli, 22 Cal. Rptr. 2d 663, 667-68 (Ct. App. 1993); Sirott v. Latts, 8 Cal. Rptr. 2d 206, 213 (Johnson, J., dissenting).

273. 7 Cal. Rptr. 2d 550, 563 (Mosk, J., dissenting), *cert. denied*, 113 S. Ct. 658 (1992).

274. *See supra* notes 109-14.

275. *See supra* notes 90-94.

276. ITT's letter of July 11, 1990, was timely because it was sent within one year of the time that the underlying action was commenced against ITT, which was the earliest point at which ITT could be said to have discovered the alleged negligence.

277. *Compare* Lambert v. Commonwealth Land Title Ins. Co., 53 Cal.3d 1075, 1079, 811 P.2d 737, 741 (Cal. 1991)

> (By tendering defense of a third party action to an insurer, the insured will have put the insurer on notice that it may be required under the policy to defend the action. Thus, the [insurer] will be aware that it must take the steps necessary to prepare and preserve a defense to an action by its insured.)

might be needed to defend against the second claim."[278] Third, the facts demonstrate good faith and reasonable conduct on the part of ITT. ITT was faced with two alternative remedies and made "a good faith, reasonable decision to pursue one remedy in order to eliminate the need to pursue the other,"[279] or at least "to lessen the extent of [its] injuries or damage."[280] Had ITT been successful in defending the adequacy of the loan documentation prepared by Niles, the legal malpractice action would have been rendered unnecessary.[281] That ITT was ultimately unsuccessful does not change the fact that it made a reasonable, good faith effort to mitigate its damages by contesting the adversary proceeding.[282]

Applying the doctrine of equitable tolling to legal malpractice cases, such as *ITT*, also promotes the policies underlying the doctrine. First, "it satisfies the policy underlying the statute of limitations" by providing timely notice and the opportunity to preserve evidence "without ignoring the competing policy of avoiding technical and unjust forfeitures."[283] Second, it eliminates the hardship of requiring a plaintiff to litigate two actions simultaneously[284] as well as avoiding the risks associated with forcing a plaintiff to take inconsistent positions in two different proceedings.[285] Finally, it promotes judicial economy to the extent that the disposition of the underlying action "may render the proceeding in the second [action] unnecessary or easier and cheaper to resolve."[286] This final policy makes the justification for equitable tolling in legal malpractice actions even stronger than in *Lambert*, because in duty-to-defend cases the insurer has a duty if the underlying action is even *arguably* within the policy coverage, and re-

278. Collier v. City of Pasadena, 191 Cal. Rptr. 681, 686 (Ct. App. 1983); *compare Lambert*, 811 P.2d at 741 (no prejudice to insurer in tolling limitation period for breach of duty to defend until judgment is entered in underlying action); Addison v. State, 21 Cal.3d 313, 319, 578 P.2d 941, 944 (Cal. 1978) (no prejudice where defendants "had the opportunity to begin gathering their evidence and preparing their defense" during the pendency of the underlying action).

279. Mitchell v. Frank R. Howard Memorial Hosp., 8 Cal. Rptr. 2d 521, 529 (Ct. App. 1992).

280. *Addison*, 578 P.2d at 943.

281. *ITT Small Bus. Fin. Corp.*, 23 Cal. Rptr. 2d at 733.

282. *See* County of Santa Clara v. Hayes Co., 43 Cal.2d 615, 619, 275 P.2d 456, 458 (Cal. 1954) ("It would be anomalous if by the very act of attempting to prevent damage from defendant's wrong, it should lose the benefit of the rule tolling the statute while its action was barred."); *Collier*, 191 Cal. Rptr. at 684 (statute of limitation is equitably tolled when "the plaintiff first pursue[s] a remedy against one defendant which, if successful, would reduce the damages which had to be sought from a second defendant").

283. *Addison*, 578 P.2d at 944.

284. *Lambert*, 811 P.2d at 740.

285. Elkins v. Derby, 12 Cal.3d 410, 412-13, 525 P.2d 81, 83 (Cal. 1974).

286. Collier v. City of Pasadena, 191 Cal. Rptr. 681, 687 (Ct. App. 1983); *see also Elkins*, 525 P.2d at 88.

gardless of whether the insured is ultimately found liable, whereas in the malpractice context, a successful result in the underlying action will generally render the malpractice action unnecessary.

B. *Objections to Equitable Tolling*

The most serious objection to applying the doctrine of equitable tolling to legal malpractice actions such as *ITT Small Business Finance Corp. v. Niles* concerns the legal basis for applying the doctrine. Code of Civil Procedure section 340.6 provides that "*[i]n no event* shall the time for commencement of legal action exceed four years except that the period shall be tolled during the time that any of the following exist."[287] This language suggests an intent to disallow tolling for any reason other than those specified in the statute.[288] There are three possible answers to this argument. First, it can be argued that the policies underlying the equitable tolling doctrine are merely being used to inform the court's construction of "actual injury," thereby employing the legal fiction that although a contingent or speculative "injury" may occur when attorneys' fees are incurred in defending the underlying action, "actual injury" does not occur until negligence, and therefore causation, have been confirmed by a judgment in the underlying action.[289]

Second, it has been held that subdivision (a)(4) of section 340.6[290] incorporates by reference all of the general tolling provisions of Chapter 4, Title 2, Part II of the Code of Civil Procedure,[291] and at least one court has held that the equitable tolling doctrine is implicit in section 355 of the Code of Civil Procedure, which is contained in Chapter 4. In *Bollinger v. National Fire Ins. Co.*,[292] the California Supreme Court, in an opinion by Justice Traynor, noted that section 355 was "copied from section 84 of the New York Code of Procedure, which in

287. CAL. CIV. PROC. CODE § 340.6(a) (West 1982) (emphasis added).

288. *See, e.g.*, Bledstein v. Superior Court, 208 Cal. Rptr. 428, 433 (Ct. App. 1984).

289. *Cf.* Worton v. Worton, 286 Cal. Rptr. 410, 419 & n.1 (Ct. App. 1991) (Johnson, J., concurring) (arguing that while the underlying action is pending, damages are "speculative" and are not "actual and appreciable"). "Alternatively, this could be viewed as an application of California's 'equitable tolling doctrine.' " *Id.*

290. Subdivision (a)(4) tolls the limitation period while "[t]he plaintiff is under a legal or physical disability which restricts the plaintiff's ability to commence legal action." CAL. CIV. PROC. CODE § 340.6(a)(4) (West 1982).

291. *Bledstein*, 208 Cal. Rptr. at 433-35.

292. 25 Cal.2d 399, 154 P.2d 399 (Cal. 1944), *superceded in part on other grounds by* CAL. CIV. PROC. CODE § 581(c) (West 1976 & Supp. 1984), *as stated in* ABC v. Walter Reade-Sterling Inc., 117 Cal. Rptr. 617, 619 (Ct. App. 1974).

turn was based on section 4 of the English Limitation Act of 1623."[293] The court also noted that "[t]he wording of section 355 is reminiscent of the old English statutes that specified situations instead of formulating general rules,"[294] and that "[i]f construed literally as applying only in the event of reversals on appeal, section 355 would not give the protection that the English statute afforded to a plaintiff who had unsuccessfully pursued his right in a previous suit."[295] The court reasoned that "[e]ven the English statute . . . had to be supplemented by judicial construction and applied beyond its literal language to accomplish its purpose,"[296] and concluded that "statutes that have their roots in the English statute should be construed with similar liberality,"[297] because "[t]he basic policy that underlies section 355 calls for relief in such a case."[298]

Third, as an alternative legal basis for applying equitable tolling in the *Bollinger* case, Justice Traynor asserted:

> In any event this court is not powerless to formulate rules of procedure where justice demands it. Indeed, it has shown itself ready to adapt rules of procedure to serve the ends of justice where technical forfeitures would unjustifiably prevent a trial on the merits. . . . [For example,] where amendment is sought after the statute of limitations has run, the amended complaint will be deemed filed as of the date of the original complaint so long as recovery is sought upon the same general set of facts . . . . Statutes of limitation are not so rigid as they are sometimes regarded. . . . It is established that the running of the statute of limitations may be suspended by causes not mentioned in the statute itself. . . . It is [therefore] sufficient to hold that the equitable considerations that justify relief in this case are applicable . . . .[299]

This broad assertion of judicial power raises troubling questions and is inconsistent with the more prevalent view that "[s]tatutes of limitation are products of legislative authority and control."[300] Nonetheless, subsequent cases applying the equitable tolling doctrine have contin-

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293. *Bollinger*, 154 P.2d at 404.

294. *Id.* at 405.

295. *Id.* at 404-05.

296. *Id.*

297. *Id.* (citing Gaines v. City of N.Y., 109 N.E. 594, 596 (N.Y. 1915) (Cardozo, J.)).

298. *Bollinger*, 154 P.2d at 410. *See also* Addison v. State, 578 P.2d 941, 943 (Cal. 1978) (stating that *Bollinger* "allowed the action, based on the broad policy implicit in Code of Civil Procedure section 355"); Appalachian Ins. Co. v. McDonnell Douglas Corp., 262 Cal. Rptr. 716, 739 (Ct. App. 1989).

299. *Bollinger*, 154 P.2d at 405.

300. Valley Circle Estates v. VTN Consol., Inc., 33 Cal.3d 604, 615, 659 P.2d 1160, 1167 (Cal. 1983) (quoting Zastrow v. Zastrow, 132 Cal. Rptr. 536, 539 (Ct. App. 1976)).

ued to espouse a broad view of judicial power. For example, in *Addison v. State of California*,[301] the California Supreme Court said: "The rule announced in *Bollinger* is a general equitable one which operates independently of the literal wording of the Code of Civil Procedure."[302] More recently, in *Lambert v. Commonwealth Land Title Insurance Co.*,[303] the California Supreme Court relied on a combination of the latter two rationales: "Because the Legislature cannot 'predict all of the circumstances that come within the purposes of the tolling exceptions,' it is 'appropriate for courts to construe the statutory tolling scheme and implicit tolling exceptions to effect the ostensible legislative purpose.' "[304]

In the case of section 340.6, the apparent legislative purpose was to reduce liability insurance premiums for lawyers by reducing their potential exposure to malpractice liability.[305] However, the Legislature demonstrated an unwillingness to forego the policy favoring resolution of disputes on their merits by enacting provisions tolling the statute until "actual injury" occurs and by incorporating the general tolling provisions of Chapter 4 by reference.[306] These conflicting purposes can best be harmonized by construing "actual injury" in a way that reduces unnecessary litigation by allowing clients who have discovered allegedly negligent conduct to wait and see whether the conduct affects the outcome of the underlying action before bringing suit. In this manner, the total number of malpractice suits filed against attorneys will be reduced, thereby achieving the legislative goal. Thus, despite the questionable foundation of the equitable tolling doctrine, application of the doctrine serves the purposes underlying the statute rather than defeating them. Therefore the court need not be troubled by resorting to general equitable principles to support its position.[307]

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301. 21 Cal.3d 313, 578 P.2d 941 (Cal. 1978).

302. *Id.* at 943.

303. 53 Cal.3d 1072, 811 P.2d 737 (Cal. 1991).

304. *Id.* at 448 (quoting Lewis v. Superior Court, 220 Cal. Rptr. 594, 596 (Ct. App. 1985)).

305. *See supra* notes 86-94.

306. CAL. CIV. PROC. CODE § 340.6(a)(1), (a)(4) (West 1982); Bledstein v. Superior Court, 208 Cal. Rptr. 428, 433-35 (Ct. App. 1984).

307. The use of the equitable tolling doctrine to help define when "actual injury" occurs in legal malpractice actions should be distinguished from the more general situation in which an action which was erroneously filed in an incorrect forum may be deemed to toll the limitation period for an identical action which is subsequently filed in the correct forum. Although equitable tolling may be appropriate in the latter situation, the policies supporting tolling in such a case are very different from those supporting tolling until "actual injury" occurs. Perhaps for this reason, in 1988 the California Supreme Court depublished a broadly worded Court of Appeal opinion which held that the doctrine of equitable tolling applied to a legal malpractice action which was first erroneously filed in federal court and later re-filed in state court. Afroozmehr v.

Another objection to applying the doctrine of equitable tolling to legal malpractice actions similar to *ITT* is that if such a construction of "actual injury" is to be adopted, it should be limited to actions involving litigation malpractice, rather than transactional malpractice.[308] As noted above, courts in other states have reached very different results in determining when the limitation period commences in actions involving litigation malpractice on the one hand and transactional malpractice on the other,[309] although none of these decisions has set forth a reasoned rationale for the disparity in outcomes. Two commentators have suggested the following justification for making this distinction:

> The predicate for analysis is the recognition that the judicial process does not create liabilities or destroy rights, but only declares what is present through the process of determining the facts and applying the law . . . . A distinguishable situation is where the error that causes the damage occurs within the judicial proceeding itself. Then, the judicial process does not declare the rights and liabilities of the parties, but rather is the situs of the client's injury to a cause of action or a defense. Since subsequent events usually determine the economic consequence of the error, the time of the injury is when the judicial action is completed, typically upon entry of an order or judgment.[310]

This analysis is flawed in three respects. First, entering into a transaction does not necessarily fix the legal rights or liabilities of the parties. For example, a court may decide to avoid the clear meaning of a negligently drafted agreement by applying the doctrine of unconscionability. Second, "subsequent events usually determine the economic consequence of the error" in transactional situations as well as in circumstances involving litigation. For example, whether or not the economic consequence of a drafting error is large or small depends on the actions of the other party to the transaction as well as the outcome of

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Asherson, 247 Cal. Rptr. 296, 297, 301-03 (Ct. App.), *review denied and ordered not published*, No. S006278 (Cal. Aug. 11, 1988).

308. *See, e.g.*, Amfac Distrib. Corp. v. Miller, 673 P.2d 792, 793 (Ariz. 1983) ("The issue before us is when a cause of action accrues for legal malpractice which occurs during the course of litigation."); Arizona Management Corp. v. Kallof, 688 P.2d 710, 714 (Ariz. Ct. App. 1984) ("*AMFAC* was expressly limited to situations where *malpractice occurs during the course of litigation.*") (emphasis in original); Hughes v. Mahaney & Higgins, 821 S.W.2d 154, 157 (Tex. 1991) (tolling rule applies "when an attorney commits malpractice in the prosecution or defense of a claim that results in litigation"); Hoover v. Gregory, 835 S.W.2d 668, 675 (Tex. App. 1992) ("We interpret *Hughes* narrowly as controlling in legal malpractice cases when a malpractice suit is brought against an attorney in the course of litigating the complainant's underlying claim.").

309. *See supra* notes 126-177 and accompanying text.

310. LEGAL MALPRACTICE, *supra* note 42, § 18.11, at 42, 45 (footnotes omitted).

any litigation which arises concerning the transaction. Third, even if one takes the view that rights and liabilities are fixed when the negligent action is initially taken, this rationale applies to negligent acts in litigation as well as transactional negligence. For example, if an attorney inadvertently waives a defense by failing to plead it in the answer, or fails to serve a defendant within the time permitted by law, the "injury" to the client is as complete as an injury which arises from a negligently drafted agreement, yet the proposed distinction would toll the limitation in the former situation but not in the latter. This incongruity is avoided by an analysis that recognizes that the basis for tolling the limitation period lies in the policies concerning simultaneous litigation, and that these policies are equally applicable to situations where the underlying litigation arises from transactional malpractice as they are when the malpractice occurs in the underlying litigation itself.

A third possible objection to applying the doctrine of equitable tolling to legal malpractice actions is the difficulty of defining the point at which tolling ceases. It could be argued that because the risks to the client associated with simultaneous litigation cannot be eliminated until all appellate review is exhausted, the equitable tolling rule proposed here must likewise be continued until all appellate review is exhausted,[311] a result which the California Supreme Court has already rejected.[312] This argument ignores the equitable nature of the doctrine. Because the doctrine is founded on reasons of public policy, it should be applied only to the extent that it continues to serve those policies. As pointed out above, the justifications for tolling are strongest before a judgment is entered at the trial court level, and are relatively less important thereafter.[313] In particular, because only a small percentage of actions are ultimately reversed on appeal,[314] it is a reasonable compromise between competing policies to adopt a tolling rule that ceases upon entry of judgment at the trial court level, thereby satisfactorily accounting for 95% of contested cases, while leaving the remaining actions to be handled on a case-by-case basis.[315]

311. *Cf.* County of Santa Clara v. Hayes Co., 43 Cal.3d 615, 275 P.2d 456, 458 (Cal. 1954) (statute of limitation tolled "until the date it was finally determined to be invalid by the decision of this court").

312. *See* Laird v. Blacker, 2 Cal.4th 606, 609, 828 P.2d 691, 692 (Cal.) (limitation period commences upon entry of adverse judgment or order of dismissal at trial court level and not upon finality of the appeal therefrom), *cert. denied*, 113 S. Ct. 658 (1992).

313. *See supra* Part II.C.

314. *See supra* note 110.

315. If a judgment adverse to the client is entered at the trial court level but is subsequently reversed, either by the trial court on reconsideration or by an intermediate appellate court, the

A final objection to applying the doctrine of equitable tolling to legal malpractice actions is that there are procedural alternatives to tolling which can accomplish the same goals. The most frequently mentioned alternative is that the plaintiff should file the malpractice action within one year of discovery and then seek a stay of the malpractice action while the underlying action is litigated until its conclusion.[316] The cases suggesting this approach, however, mention it primarily as an alternative to tolling the limitation period pending the outcome of an appeal in the underlying action, rather than as an alternative to tolling the limitation period until judgment is entered at the trial court level.[317] As noted above, the policy reasons for tolling the limitation period are strongest before a judgment is entered.[318] In addition, the alternative of staying the malpractice action until a judgment is entered in the underlying action is unsatisfactory for several reasons. First, in some situations the very existence of the malpractice action may prejudice the client (and the former attorney) by alerting the opposing party to a possible defense or legal position that will cause the client to lose the underlying action, thereby increasing the measure of damages in the malpractice action. Second, even the minimum action of filing a lawsuit and seeking a stay imposes costs on both the parties and the legal system which in some cases would be avoided altogether if tolling were permitted.[319] Avoiding unnecessary

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policies underlying the equitable tolling doctrine will once again outweigh the competing policies unless and until the adverse judgment is reinstated by a higher court. *See* Stroud v. Ryan, 763 S.W.2d 76 (Ark. 1989); Fliegel v. Davis, 699 P.2d 674, 675-76 (Or. Ct. App. 1985). *But see* Safine v. Sinott, 19 Cal. Rptr. 2d 52, 53-55 (Ct. App. 1993) (client injured when he paid money into escrow pursuant to erroneous judgment, despite subsequent entry of corrected judgment at trial court level; rejecting argument that action was tolled until corrected judgment was reversed on appeal for lack of jurisdiction).

316. *See, e.g.*, Knight v. Furlow, 553 A.2d 1232, 1236 (D.C. App. 1989); Grunwald v. Bronkesh, 621 A.2d 459, 466-67 (N.J. 1993); Zimmie v. Calfee, Halter & Griswold, 538 N.E.2d 398, 402 (Ohio 1989); *cf.* LEGAL MALPRACTICE, *supra* note 42, § 18.11, at 53 ("Judicial relief is available . . . to abate a pending legal malpractice action.").

317. *Knight*, 553 A.2d at 1236 (stating that "in some circumstances . . . trial of the malpractice action should be stayed *pending the appeal*") (emphasis added); *Grunwald*, 621 A.2d at 466-67 ("Staying the malpractice action *pending completion of the appellate process* on the underlying claim . . . prevents duplicative litigation and saves plaintiffs the discomfort of maintaining inconsistent positions.") (emphasis added); *Zimmie*, 538 N.E.2d at 402 (noting that "the trial court could have been requested to stay this malpractice action until there was a *final judgment from the appellate courts*. . .") (emphasis added).

318. *See supra* Part II.C.

319. These costs are greatly increased if the stay is contested. *See, e.g.*, Rosenthal v. Wilner, 243 Cal. Rptr. 472, 474-76 (Ct. App. 1988) (following successful petition for writ of mandate, action for appellate malpractice stayed "pending resolution of the . . . appeal" in the underlying action; second appeal was required to determine whether the stay terminated upon issuance of the remittitur, or upon later denial of a writ of certiorari by the United States Supreme Court).

malpractice actions is good for both the former attorney and the client: the former attorney avoids a public accusation that may injure his or her business, and the client avoids the emotional and financial hardship of bringing a second action.[320] Third, in this era of fast-track calendars and single-judge assignments, judges are often reluctant to grant a stay because their judicial performance is evaluated in part by the number of unresolved matters on their dockets.[321] If discovery in the malpractice action proceeds, notwithstanding the pendency of the underlying action, it will impose costs on the parties and the judicial system which might have been avoided if tolling had been permitted. These considerations, like those underlying the tolling rule itself, are strongest before a judgment is entered in the underlying action.

A second alternative, which is sometimes mentioned, is that the client should attempt to secure a waiver of the statute of limitation from the former attorney before proceeding with the underlying action.[322] The theory is that an attorney will readily agree to such a waiver to avoid having a potentially unnecessary malpractice action commenced against him or her.[323] While this alternative has much to recommend it, it is inferior to the equitable tolling doctrine for three reasons. First, having to seek a waiver distracts the client from the principal focus of salvaging the underlying litigation. Second, if the attorney believes the client has a weak case, he or she may make a strategic decision to decline the waiver, in the hope that the cost of litigating two actions simultaneously will force the client to settle the malpractice action on more favorable terms. Third, where the purpose of the statute of limitation has been served by timely notice to the defendant, the client ought to be able to make the choice between

320. Indeed, in some cases the defendant attorney may request that the malpractice action be stayed. *See Rosenthal*, 243 Cal. Rptr. at 474 (action stayed following successful petition for writ of mandate by defendants).

321. *Cf. Rosenthal*, 243 Cal. Rptr. at 474 (superior court denied motion to stay action for appellate malpractice pending determination of appeal in underlying action; stay granted following successful petition for writ of mandate by defendants).

322. *See, e.g.*, Northwestern Nat'l Ins. Co. v. Osborne, 610 F. Supp. 126, 129 (E.D. Ky. 1985) The court stated: "this situation is easily avoided by the client's going to the allegedly negligent attorney and obtaining a waiver or extension of the statute of limitations until such time as it may be seen if the underlying litigation can be favorably concluded." *Id.*

323. *Id.* at 129-30 (client "could seek a waiver of the statute from the allegedly negligent attorney, who if he declines to grant it, has only himself to blame for an unnecessary suit against him"); LEGAL MALPRACTICE, *supra* note 42, § 18.11, at 53 ("[E]xperience has shown that most lawyers are willing to enter into an agreement tolling the statute of limitations . . . . Usually, lawyers prefer such an alternative to that of being named in a lawsuit that must be defended at cost to themselves or their insurers.").

his alternative remedies without being pressured by the attorney who allegedly placed the client in a difficult position.

C. *Other Legal Malpractice Actions*

1. Failure to File Within Limitation Period

Two California cases have expressed opposite views on the issue of when "actual injury" occurs when the attorney misses the statute of limitation for filing the underlying action. In *Finlayson v. Sanbrook*,[324] the plaintiff retained the defendant in 1981 to file a worker's compensation claim and to pursue "any and all claims arising out of his asbestos-related illness."[325] The defendant failed to file a third-party civil action against the manufacturers and suppliers of asbestos, and the statute of limitation on such an action expired in 1982.[326] In 1983, the plaintiff retained new counsel and filed both the third-party action and a legal malpractice action. Summary judgment against the plaintiff on statute of limitation grounds was not entered in the third-party action until May 26, 1988.[327] In February 1989, the trial court in the malpractice action denied the plaintiff's motion to extend the five-year statute for bringing an action to trial.[328] Therefore, on February 9, 1989, plaintiff voluntarily dismissed his malpractice action and filed a new action, alleging that the date of "actual injury" was May 26, 1988.[329] The Court of Appeal held that the client suffered "actual injury" in 1982, when the statute of limitations expired on the underlying claim, because "the fact of damage is apparent when a right or remedy is lost due to an attorney's failure to file within a statutory limitation."[330] The court asserted that its conclusion was consistent with *Laird v. Blacker*, saying:

> Although *Laird* repeatedly asserted without qualification that "actual injury" . . . occurs when a client suffers an adverse judgment or order of dismissal in the underlying action, we believe that the rule must be qualified to those situations in which there exists a timely filed underlying action. If the *Laird* rule demanded an adverse judgment in missed statute cases, the limitations period could

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324. 13 Cal. Rptr. 2d 406 (Ct. App. 1992).
325. *Id.* at 407.
326. *Id.* at 407 & n.2.
327. *Id.* at 408.
328. *Id.* at 407.
329. *Id.* at 408.
330. *Id.* at 409.

> be indefinitely extended simply by filing a time-barred action however late and then waiting until an adverse judgment is rendered.[331]

The opposite result was reached in the factually similar case of *Pleasant v. Celli*.[332] In *Pleasant*, the plaintiff's daughter died on September 19, 1981, allegedly as the result of medical malpractice.[333] Plaintiff retained the defendant in October 1981 to bring a medical malpractice action; however, defendant did not file the case until November 24, 1982, approximately two months after the one-year statute of limitation had expired.[334] After plaintiff retained new counsel, the medical defendants demurred to the complaint on limitation grounds.[335] When he was notified of the demurrer, defendant told plaintiff's new counsel that he did not have malpractice insurance, and "[h]e requested that Pleasant contest the arguments asserted by the medical defendants."[336] Plaintiff did so, but summary judgment was entered in the underlying action on limitation grounds in December of 1985, and the plaintiff filed a malpractice action on June 17, 1986.[337] The Court of Appeal held that *Laird v. Blacker* created a "bright-line" rule that "the plaintiff's cause of action for malpractice does not accrue until the trial court dismisses the plaintiff's underlying case or enters an adverse judgment against the plaintiff."[338] The court criticized the *Finlayson* decision, asking:

> Is a plaintiff harmed by her attorney's failure to file a timely lawsuit, even if it never occurs to the defendants in the underlying suit to assert a statute of limitations defense? Under *Finlayson*, the answer would be "yes." Taken to its extreme, *Finlayson* would oblige a plaintiff to sue a former attorney upon discovering that the attorney filed the complaint late . . . even if the defendants do not realize the suit is untimely.[339]

The court also stated that "in many cases it is impossible to determine whether a client has been harmed by his attorney until the ultimate

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331. Finlayson v. Sanbrook, 13 Cal. Rptr. 2d 406, 411 (Ct. App. 1992).

332. 22 Cal. Rptr. 2d 663 (Ct. App. 1993).

333. *Id.* at 664.

334. *Id. See* CAL. CIV. PROC. CODE § 340.5 (West 1982) (action for professional negligence against health care provider must be brought within one year after the plaintiff discovers the injury).

335. Pleasant v. Celli, 22 Cal. Rptr. 2d 663, 664-65.

336. *Id.* at 665.

337. *Id.*

338. *Id.* at 666, 668.

339. *Id.* at 667 (ellipsis in original).

determination of the underlying suit, due to the closeness of the legal issues,"[340] and explained:

> This is a case in which the wrong and the harm were not concurrent. Celli committed his wrong the day the statute of limitations expired. However, the actual harm to Pleasant continued to be merely prospective until (1) the medical defendants recognized a potential statute of limitations defense, (2) asserted the defense, (3) fought Pleasant's tolling and other arguments through demurrer and summary judgment, and (4) succeeded in having Pleasant's case dismissed. Until that point, when the "fact" of damage was judicially determined, Celli's breach of professional duty caused only an unrealized threat of future harm.[341]

The court did not discuss the possibility that "actual injury" occurred at point (3), when Pleasant incurred attorneys' fees in defending the timeliness of her medical malpractice action.[342]

Both *Pleasant* and *Finlayson* can be better understood in terms of the doctrine of equitable tolling. In *Pleasant*, all three elements of the doctrine were present. First, the defendant received timely notice of his potential liability when he was contacted by plaintiff's new counsel promptly after the alleged negligence was discovered. While it has been stated that "the timely notice requirement essentially means that the first claim must have been filed within the statutory period,"[343] this statement means that when notice is accomplished by filing an action against the same defendant, the first action must be filed within the statutory period *for the second action* in order to toll the second action.[344] A requirement that the first action be timely filed makes no sense when the timing of the first action is within the control of the

340. *Id.* (citing United States Nat'l Bank of Oregon v. Davies, 548 P.2d 966, 969 (Or. 1976)).

341. *Id.* at 668.

342. An intermediate position was taken in Adams v. Paul, 31 Cal. Rptr.2d 84 (Ct. App.), *review granted*, No. 5041623 (Sept. 29, 1994), in which the court stated:

> We think both cases assume too much. *Finlayson* assumes that the statute of limitations deadline will always be obvious, even though there may be a hotly contested tolling issue. . . . *Pleasant*, on the other hand, assumes that only a judicial determination of the fact of damage will suffice.

Id. at 849. The *Adam* court concluded that "Adams sustained actual damage as a result of Paul's negligence in April 1990 when she was forced to oppose the estate's summary judgement motion [in the underlying action]." *Id.*

343. Collier v. City of Pasadena, 191 Cal. Rptr. 681, 685 (Ct. App. 1983).

344. Thus, in *Collier* the court concluded that "[t]he timely notice requirement was satisfied when Collier filed his *workers' compensation claim*" because it was "easily within the six months allowed for initiating *disability pension claims*." 191 Cal. Rptr. at 687 (emphasis added). Of course, in many cases the distinction is unimportant because the first action and the second action involve the same claims filed at different times. *See, e.g.*, Addison v. State, 21 Cal.3d 317, 319, 578 P.2d 941, 942 (Cal. 1978); Appalachian Ins. Co. v. McDonnell Douglas Corp., 262 Cal. Rptr. 716, 741 (Ct. App. 1989).

defendant rather than the plaintiff and where the failure to file is the basis for liability in the second action.[345] In this context, the "timely notice" requirement should be interpreted to mean that the client notified the former attorney of his or her potential liability promptly after discovery of the alleged negligence.[346] Second, the former attorney was not prejudiced in the opportunity to prepare a defense because notice of the first action alerted him to the possibility that he might be liable for malpractice.[347] Third, the plaintiff and her counsel acted reasonably and in good faith in pursuing the underlying action. Indeed, they were urged to do so by the former attorney himself.[348] Obviously the case for equitable tolling is strongest where the delay in bringing the second action can be attributed in large part to the defendant.[349]

In *Finlayson*, by contrast, while the first two elements of the equitable tolling doctrine were satisfied, it is arguable that the third element was not. Certainly the initiation of the first malpractice action in 1983 placed the former attorney on notice of his potential liability and afforded him an opportunity to preserve evidence while awaiting the outcome of the underlying action. After having filed a malpractice action, however, the plaintiff took no further steps to pursue discovery or to have the malpractice action stayed while the underlying action was being litigated, and more than five years later the trial court denied the plaintiff's motion to extend the five-year period for bringing the malpractice action to trial.[350] The court viewed the voluntary dismissal of the first malpractice action and the filing of the second malpractice action as an improper attempt to extend the limitation

345. *Cf.* Bollinger v. National Fire Ins. Co., 25 Cal.2d 399, 407, 154 P.2d 399, 404 (Cal. 1944) (" '[I]t is clear to us that the defendant's conduct furnished the occasion for the delay and that it cannot take advantage of a situation which was of its own creation.' ") (citation omitted).

346. *Cf.* Lambert v. Commonwealth Land Title Ins. Co., 53 Cal.3d 1072, 1079, 811 P.2d 737, 741 (Cal. 1991) ("By tendering defense of a third party action to an insurer, the insured will have put the insured on notice that it may be required under the policy to defend the action.").

347. "When notified of this defense by Pleasant's new counsel, . . . Celli informed Pleasant's attorney that he lacked malpractice insurance." Pleasant v. Celli, 22 Cal. Rptr. 2d 663, 665 (Ct. App. 1993).

348. *Id.* at 665.

349. For example, in *Bollinger* the defendant "requested and obtained from plaintiff and the court numerous continuances and extensions of time" before moving for a nonsuit on grounds that the first action was prematurely filed. *Bollinger*, 154 P.2d at 401. The court concluded that "[b]ut for the unreasonable delay in bringing the [first] action to trial, the limitation period would not have expired and ample time would have remained to file a new action." *Id.* at 405.

350. The first malpractice action was filed in 1983, but the plaintiff's motion to extend the five-year period for bringing the action to trial was not denied until sometime shortly before February 1989. Finlayson v. Sanbrook, 13 Cal. Rptr. 2d 406, 407 (Ct. App. 1992).

period.[351] In addition, although summary judgment was granted in the underlying action on May 26, 1988, the plaintiff did not file his second malpractice action until more than eight months later.[352] Other courts have agreed that "equitable tolling is not available to a plaintiff whose conduct evidences an intent to delay disposition of the case without good cause."[353] However, another court, while acknowledging the argument that "a failure to act could sometimes unfairly mislead a defendant" into believing the plaintiff was foregoing his second claim,[354] questioned the reasoning underlying such a conclusion:

> [A] plaintiff's inaction on the second claim—as opposed to affirmative conduct—can seldom be said to have misled the defendant in a way that would negate equitable tolling on that claim. Complete inactivity on the second claim, in fact, is what "equitable tolling" is all about. This doctrine excuses the plaintiff from even filing a claim to say nothing of relieving him of the responsibility for constantly monitoring the . . . disposition of his claim.[355]

Following this reasoning, the client's conduct in *Finlayson* could be viewed as a good-faith attempt to place the former attorney on notice and to preserve his malpractice cause of action while he attempted to avoid or mitigate the consequences of his attorney's negligence by pursuing the underlying action.[356] His efforts to do so were thwarted when the underlying action took more than five years to resolve and the trial court denied his motion to extend the five-year period for bringing the malpractice action to trial. Moreover, had the plaintiff failed to bring the underlying action, the attorney might have argued in the malpractice action that the plaintiff could have mitigated his damages by bringing the underlying action anyway, since the defendant might have waived the limitation defense or a tolling exception might have been applied. Although, in retrospect, the plaintiff should have sought a stay of his malpractice action in the first instance, or appealed the denial of his motion to extend the five-year period,

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351. "If the *Laird* rule demanded an adverse judgment in missed statute cases, the limitations period could be indefinitely extended simply by filing a time-barred action however late and then waiting until an adverse judgment is rendered." *Finlayson*, 13 Cal. Rptr. 2d at 411.

352. *Id.* at 408. It should be noted, however, that the opinion does not indicate when the plaintiff moved to extend the five-year period for bringing the first malpractice action to trial.

353. Mitchell v. Frank R. Howard Memorial Hosp., 8 Cal. Rptr. 2d 521, 529 (Ct. App. 1992).

354. Collier v. City of Pasadena, 191 Cal. Rptr. 681, 691 (Ct. App. 1983).

355. *Id.* at 691.

356. There is no reason to believe that the plaintiff pursued the underlying action in bad faith. The opinion indicates that the plaintiff's new counsel believed that the underlying action might be deemed timely despite the late filing, based on a 1979 Court of Appeal opinion. That opinion, however, was overruled by the California Supreme Court after the underlying action was commenced. *Finlayson*, 13 Cal. Rptr. at 408 n.3.

under the circumstances his failure to do so and the voluntary dismissal and re-filing of his malpractice action should not be construed as bad faith.[357]

Another possible distinction between *Pleasant* and *Finlayson* is that in *Pleasant* the underlying action was already pending at the time the plaintiff discovered the alleged negligence, whereas in *Finlayson* the plaintiff discovered the alleged negligence before the underlying action was filed. This distinction, however, is not a sufficient reason to allow equitable tolling in one case and to deny it in the other. Instead, the time that elapses after discovery and before the filing of the underlying action should be counted against the one-year limitation period. Thus, if the plaintiff waits eleven months after discovering the alleged negligence to file the underlying action, he or she will have only one month to file a malpractice action after judgment is entered in the underlying action.[358] Under this rule, the plaintiff has a reasonable time within which to commence the underlying action if doing so might avoid or mitigate the damages in the malpractice action, but he or she is also "penalized for waiting too long after discovery" to file the underlying action.[359]

2. Negligent Advice Regarding Settlement

Laird v. Blacker holds that the limitation period for legal malpractice actions "commences when a client suffers an adverse judgment or order of dismissal in the underlying action on which the malpractice action is based."[360] This holding is consistent with equitably tolling the limitation period until an adverse judgment is entered in the underlying action. However, problems may arise in determining when equitable tolling should cease if the plaintiff settles the underlying action, rather than litigating until final judgment. For

357. *Cf.* Appalachian Ins. Co. v. McDonnell Douglas Corp., 262 Cal. Rptr. 716, 740-41 (Ct. App. 1989) (holding that equitable tolling applied where plaintiff voluntarily dismissed his first action after removal to federal court and re-filed in state court).

358. *See* Prudential-LMI Commercial Ins. v. Superior Court, 51 Cal.3d 674, 692-93, 798 P.2d 1230, 1242 (Cal. 1990) (holding that limitation period in statutory insurance policy begins to run upon discovery of loss but is equitably tolled from the time an insured gives notice of the damage to the insurer until coverage is denied).

359. *Id.* at 399. This analysis assumes that timely notice is given to the former attorney at the time the underlying action is commenced. If there is a substantial delay in giving notice to the attorney after the underlying action is filed, or if the plaintiff fails to give notice within one year after discovering the alleged negligence, then the elements of timely notice or good faith or both will be lacking, and equitable tolling should be denied.

360. 2 Cal.4th 606, 609, 828 P.2d 691, 692 (Cal.), *cert. denied*, 113 S. Ct. 658 (1992).

example, in *Hensley v. Caietti*,[361] a marital dissolution action, the parties negotiated a stipulated settlement at a settlement conference on September 28, 1989.[362] The court approved the stipulation, informed the parties that "the settlement was effective immediately," and directed the husband's counsel to prepare the judgment.[363] However, entry of judgment was delayed more than two months because the plaintiff discharged her counsel before the proposed judgment was agreed upon.[364] The trial court found that Hensley sustained "actual injury" when she entered into the stipulated settlement agreement.[365] On appeal, Hensley "argue[d] that she did not sustain actual injury until the effective date of the ensuing judgment."[366]

The court held that "[n]egligent legal advice which induces a client to enter into a binding contract resolving marital property and support issues results in actual injury at the point of entry."[367] The court rejected the argument that actual injury did not occur until judgment was entered, saying:

> That leaves the question whether the consideration that some or all of the provisions of a marital settlement agreement are subsequently incorporated in a judgment "delays" actual injury until the judgment takes effect. We discern no reason why that should be the case. . . . The consideration that the injury attributable to entry into the contract may be remediable by the attack on the contract does not render the injury harmless.[368]

The *Hensley* court's resolution of this question is unsatisfactory because it ignores the practical benefits of a bright-line rule that "actual injury" occurs, or equitable tolling ceases, upon entry of judgment in the underlying action. The date on which a judgment is entered can easily be ascertained from the record in the underlying action, of which the court may take judicial notice.[369] The date on which the settlement occurred, however, may be uncertain: the parties may

361. 16 Cal. Rptr. 2d 837 (Ct. App. 1993).
362. *Id.* at 838.
363. *Id.*
364. *Id.* at 838-39.
365. *Id.* at 839, 842.
366. *Id.* at 842.
367. *Id.* at 843; *see also* Turley v. Wooldridge, 281 Cal. Rptr. 441, 445 (Ct. App. 1991) (holding that appreciable harm occurred when marital settlement agreement was signed by the parties, where the agreement provided that "the effectiveness of the agreement relating to the transfers of property were not made contingent upon approval by the court and the provisions of the agreement were not to be merged in the anticipated Interlocutory Judgment of Dissolution of Marriage").
368. *Hensley*, 16 Cal. Rptr. 2d at 843.
369. *See* CAL. EVID. CODE § 452(d) (West 1966).

have orally agreed to settle on one date, reduced the details to writing on another date, signed the written agreement on a third date, and received court approval on a fourth date. Thus, using the date of settlement creates a trap for the unwary, whereas the "entry of judgment" rule fosters greater certainty and helps to avoid unnecessary litigation.[370]

There are other situations in which there is a judicial determination adverse to the client before entry of judgment or an order of dismissal occurs. For example, if a preliminary injunction is entered against the client due to his or her attorney's negligence, then clearly there has been a judicial determination that adversely affects the client, even if a permanent injunction is ultimately denied by the trial court. The conclusion that an "actual injury" has occurred is supported by the additional fact that entry of a preliminary injunction is immediately appealable even though there has not yet been a final judgment.[371] In situations such as this, an order which is immediately appealable serves the same function as the "entry of adverse judgment or final order of dismissal" in *Laird*. Although many of the policy considerations supporting delayed accrual or equitable tolling may still be present, these policies are outweighed by the policies of repose and avoiding deterioration of evidence after there has been a determination at the trial court level.[372] Therefore, the best solution is to hold that "actual injury" occurs whenever there is an order or judgment adverse to the client which is immediately appealable.[373] This solution also resolves any potential conflict over when "entry of judgment" occurs. Because a jury verdict or an announcement of judicial decision is not appealable until a judgment is formally entered, the limitation

370. This analysis assumes that the other elements of the equitable tolling doctrine are satisfied. In *Hensley*, however, although the plaintiff and her former attorney had a "terrible argument" regarding the settlement agreement, there is nothing to indicate that the former attorney was given notice of his potential liability for malpractice in the event that the client was unable to mitigate the effects of his alleged negligence at the trial court level. *Hensley*, 16 Cal. Rptr. 2d at 838.

371. *See* CAL. CIV. PROC. CODE § 904.1(a)(6) (West Supp. 1994) (appeal may be taken "[f]rom an order granting or dissolving an injunction, or refusing to grant or dissolve an injunction").

372. *See supra* Part II.C.

373. *Cf.* Turley v. Wooldridge, 281 Cal. Rptr. 441, 445 n.2 (Ct. App. 1991) ("actual injury" with regard to spousal support occurred no later than entry of interlocutory judgment of dissolution, rather than date of entry of final judgment of dissolution).

period should be deemed to commence on the latter date rather than the former.[374]

3. Negligent Advice Regarding Taxes

Another situation in which it can be anticipated that litigation regarding the underlying subject matter may occur is when the alleged malpractice consists of negligent tax advice.[375] Although many of the cases involve negligent advice by fiduciaries other than attorneys, such as accountants or banks, the same principles and considerations that govern "actual injury" in legal malpractice cases are applicable.[376]

The facts of *McKeown v. First Interstate Bank of California*[377] are illustrative. In *McKeown*, the plaintiffs alleged that they entered into a loan agreement on the basis of negligent tax advice by the defendant. The loan payments were made between 1972 and 1975. The plaintiffs were audited in 1973 and were preliminarily advised of their tax liability on the loan payments to be made in 1974. Plaintiffs incurred accountants' fees in connection with the audit, and they were represented by an attorney in administrative proceedings between 1974 and 1976. In December 1976, the IRS sent plaintiffs a notice of deficiency regarding their 1972 taxes. In January 1977, plaintiffs retained an attorney to challenge the deficiency in Tax Court. On November 23, 1977, the IRS sent a notice of deficiency regarding their 1973 through 1975 taxes. The Tax Court entered judgment against plaintiffs on February 26, 1980, and taxes were assessed in accordance with the judgment on June 9, 1980. Plaintiffs filed an action against the bank for breach of fiduciary duty on February 24, 1982. The applicable limitation period was four years.[378] The court held that "notification of the tax deficiency in December 1976 constituted harm sufficient to trigger the running of the statute."[379] In the alternative,

374. *See, e.g.*, Johnson v. Cornett, 474 N.E.2d 518, 519-20 (Ind. Ct. App. 1985) (holding that limitation period commenced on date dissolution decree was signed by the court rather than on date court announced its decision).

375. For an overview of Internal Revenue Service tax collection procedure, see *supra* text accompanying notes 179-192.

376. *See supra* note 178.

377. 240 Cal. Rptr. 127 (Ct. App. 1987). The facts in this paragraph are drawn from the opinion. *Id.* at 129.

378. CAL. CIV. PROC. CODE § 343 (West 1982) ("An action for relief not hereinbefore provided for must be commenced within four years after the cause of action shall have accrued."); *McKeown*, 240 Cal. Rptr. at 129.

379. *McKeown*, 240 Cal. Rptr. at 130; *see* Moonie v. Lynch, 64 Cal. Rptr. 55, 57 (Ct. App. 1967) (cause of action for negligent preparation of tax return by accountant accrued when "the government assessed, or to plaintiff's knowledge was about to assess, a penalty"); *but see* United States v. Gutterman, 701 F.2d 104, 106 (9th Cir. 1983) (action for legal malpractice) (plaintiff

the court held that the plaintiffs "suffered appreciable harm at least as early as January 1977," when they "paid attorneys fees . . . for representation in the tax court proceeding."[380] The court rejected the plaintiffs' contention "that they suffered no appreciable harm until the tax court judgment against them became final in late February 1980."[381]

In analyzing when the statute of limitation should commence in malpractice cases involving negligent tax advice, it is important to distinguish situations in which the taxpayer accepts the IRS's determination of tax liability and permits assessment and collection of the additional tax and penalty from cases in which the taxpayer files a petition for redetermination in Tax Court or commences a suit for a refund in District Court.[382] In the former situation, any problems associated with simultaneous litigation cease to exist once the taxpayer acquiesces in the IRS's determination. In such a case, although it may be assumed that discovery has occurred when the statutory notice of deficiency is received, the limitation period should nonetheless continue to be tolled until assessment occurs.[383] The basis for this position is that "actual injury" does not occur until "an enforceable obligation has come into existence."[384] One commentator has explained the significance of the act of assessment as follows:

> Assessment of a tax is significant for two reasons. First, assessment not only establishes a taxpayer's liability for the amount of any tax

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"first suffered actual and appreciable harm, at the latest, in August 1972 when the IRS assessed the tax penalty"); *see also* Boykin v. Cobin, 30 Cal. Rptr.2d 448, 429 (Ct. App.) (accepting plaintiff's position that "their causes of action did not accrue until the Internal Revenue Service issued its notice of deficiency assessing penalties for negligence and "fraud."), *review granted*, 878 P.2d 1275 (1994)).

380. *McKeown*, 240 Cal. Rptr. at 129 (citing Budd v. Nixen, 491 P.2d 433, 436 (Cal. 1971)).

381. *Id. See also* United States v. Gutterman, 701 F.2d 104, 106 (9th Cir. 1983) (rejecting argument that a malpractice claim for negligent tax advice does not accrue until a court judgment in a collection suit by the government, where plaintiff neither filed a petition in Tax Court nor paid the tax and filed suit for a refund in District Court); Schrader v. Scott, 11 Cal. Rptr. 2d 433, 435-39 (Ct. App. 1992) (limitation period for accountant malpractice commenced when plaintiffs received notice of final adjustment of deficiency from the IRS and was not tolled until administrative appeals were concluded).

382. A taxpayer may also commence a suit for a refund in the United States Claims Court. *See supra* note 190 and accompanying text. For convenience, this discussion will refer only to suits for refund in District Court; however, this discussion is equally applicable to suits for refund in Claims Court.

383. In *Boykin*, 30 Cal. Rptr.2d at 428, the court referred to the critical document as both a "notice of deficiency assessing penalties for negligence and fraud," and "the final audit report, also referred to as the notice of deficiency . . . . *Id.* at 429. It is evident from these statements that the court failed to distinguish between a preliminary notice of deficiency, a statutory notice of deficiency, and an assessment. *See supra* notes 193-94 and accompanying text.

384. *Gutterman*, 701 F.2d at 106.

> due and unpaid, but also the Service's entitlement to collect and retain the amount as a tax. Until an assessment is made, the Service cannot collect a tax administratively, because both the lien and levy provisions require the making of a demand for payment, which in turn assumes the making of an assessment. . . . Second, assessment of a tax is the administrative act that divides . . . examination and administrative settlement procedures from collection procedures . . .[385]

When the taxpayer challenges the IRS's determination in Tax Court or in District Court, however, then all of the considerations which support equitable tolling of the limitation period until entry of judgment in the underlying action continue to apply. First, as with legal malpractice, the outcome of the underlying action may make the negligence action unnecessary. If the trial court determines that no taxes or penalties are owed, usually there is either no malpractice or no injury on which a malpractice claim can be based. Judicial economy is therefore best served by tolling the limitation period until a judgment has been entered.[386] Second, it is an error to assume that attorneys' fees necessarily constitute actual injury, because the taxpayer's return may have been selected for an audit even in the absence of the alleged negligence, and because in many cases the client may have instructed the accountant or the attorney to take an aggressive legal position. Therefore, because the client can reasonably expect to spend money on attorneys' fees in defending his position, it cannot be said with certainty that the alleged negligence has caused any injury until a judgment has been entered.[387] Third, many of the dangers of simultaneous litigation, including the possibility that the client's position in the negligence action will be used against him or her in the underlying proceeding, are equally present in the negligent

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385. SALTZMAN, *supra* note 179, ¶ 10.01, at 10-2.

386. *Cf.* Ackerman v. Price Waterhouse, 591 N.Y.S.2d 936, 941 (Sup. Ct. 1992) ("[T]he *Atkins* test encourages potential plaintiffs to wait to sue an accountant until subjected to a demonstrable wrong and injury. Accordingly, it protects federal tax preparers from the prejudice of needless litigation expense on suits which must later be abandoned because no damage ensued, after occasioning an entirely wasted investment of court resources."), *aff'd*, 604 N.Y.S.2d 721 (1993).

387. *See supra* text accompanying notes 195-96. "Even a taxpayer whose return is ultimately vindicated by the audit is nonetheless put through an ordeal and may suffer the 'harm' of having to spend money to hire professional help. Such 'harm', while real, cannot be said to have been caused by anything other than the IRS decision to examine the return." *Boykin*, 30 Cal. Rptr.2d at 431.

tax advice situation.[388] In addition, unlike most judicial review of administrative action, both Tax Court actions and actions for refund in District Court involve de novo determination of the correct tax rather than "substantial evidence" review of the agency's action.[389] Thus, a judgment in Tax Court or in District Court is analogous to a judgment at the trial court level in the underlying litigation, rather than to an appeal of a trial court determination.[390] Therefore, if an action is commenced either in Tax Court or in District Court promptly after the client discovers the alleged negligence, and if the other elements of the equitable tolling doctrine are satisfied, actual injury should not be deemed to occur, and the limitation period should be tolled, until judgment is entered in the underlying action.[391]

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388. *See, e.g.*, Peat, Marwick, Mitchell & Co. v. Lane, 565 So. 2d 1323, 1326 (Fla. 1990) (injustice of requiring a party to assert legally inconsistent positions in Tax Court and in negligence action justifies tolling limitation period until Tax Court entered judgment against taxpayer).

389. *See supra* notes 186, 191 and accompanying text.

390. By contrast, in cases involving review of administrative action generally, the limitation period should be tolled only until the client has exhausted his or her administrative remedies, an action analogous to a trial court judgment, rather than until the administrative action has been upheld on judicial review, an action more analogous to an appeal. *See* Worton v. Worton, 286 Cal. Rptr. 410 (Ct. App. 1991).

> "The administrative appeal discussed in [*Robinson*] resulted in a final administrative adjudication of plaintiff's right to receive a disability pension. The equivalent final adjudication in [the] present case occurred upon entry of the judgment of dissolution .... Stated differently, the administrative appeal referred to in *Robinson* is not an appeal in the sense of a post-judgment remedy in a civil action, but is merely the last step in the administrative procedure necessary to secure a final adjudication at the administrative level."

Id. at 417-18; *see also* Robinson v. McGinn, 240 Cal. Rptr. 423, 428 (Ct. App. 1987), *disapproved on other grounds*, Laird v. Blacker, 828 P.2d 691, 697-98 (Cal.), *cert. denied*, 113 S. Ct. 658 (1992).

391. Another transactional negligence situation which arises frequently is an action by intended beneficiaries of a will against an attorney for alleged malpractice in drafting the will. In Heyer v. Flaig, 449 P.2d 161, 162 (Cal. 1969), the California Supreme Court held that the limitation period for such claims accrued upon the testator's death, "when the negligent failure to perfect the requested testamentary scheme becomes irremediable and the impact of the injury occurs." The decision rested on two grounds. First, because the attorney's duty "effectively to fulfill the desired testamentary scheme continued until the testatrix's death," the wrongful act occurred not only when the attorney drafted the will, but when he failed to take corrective action prior to the testatrix's death. *Id.* at 166. Second, because an intended beneficiary does not acquire any legal interest under a will until the testator dies, there can be no injury and no cause of action at least until death occurs. *Id.* These considerations make this type of action somewhat different from other types of transactional malpractice. In addition, although *Heyer* predated the adoption of the discovery rule for legal malpractice actions in California, it has been suggested that subsection (b) of Code of Civil Procedure § 340.6 was specifically intended to toll the limitation period in this type of case. *See* CAL. CIV. PROC. CODE § 340.6(b); Mallen, *supra* note 42, 53 CAL. ST. B.J. at 168. Accordingly, this article does not undertake to analyze such claims in detail. However, in principle there is no reason why the same considerations justifying equitable tolling in legal malpractice actions generally should not apply where litigation regarding the will is commenced promptly after discovery of the alleged negligence.

CONCLUSION

Despite the California Supreme Court's 1992 opinion in *Laird v. Blacker*, courts have continued to struggle with the question of when "actual injury" occurs in legal malpractice cases. To answer that question, courts must weigh the desirability of guaranteeing repose and minimizing deterioration of evidence against the desirability of avoiding the problems which may result from simultaneous litigation of the malpractice claim and the underlying action. Despite the lack of a clearly defined legal basis for applying the doctrine of equitable tolling, these competing policies can best be balanced by defining "actual injury" in a manner consistent with that doctrine, thereby tolling the commencement of the limitation period for the malpractice action until an adverse judgment or other appealable order is entered against the client at the trial court level in the underlying action, provided the other requirements of the doctrine are satisfied. The facts in *ITT Small Business Finance Corp. v. Niles* are particularly well-suited to application of the equitable tolling doctrine, and the case therefore provides the California Supreme Court with an auspicious opportunity to announce a standard that will bring much-needed clarity to this difficult question of statutory interpretation.