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Attorney Malpractice: New York's Measure of Damages--Benefit-of-the-Bargain? A Rose by Any Other Name

Jacob L. Todres

ATTORNEY MALPRACTICE: NEW YORK'S MEASURE OF DAMAGES—BENEFIT-OF-THE-BARGAIN? A ROSE BY ANY OTHER NAME . . .

JACOB L. TODRES[†]

Recently I had occasion to examine the New York measure of damages in tax malpractice situations.[1] During this work I was struck by the realization that with respect to such malpractice causes of action there does not appear to be a clear, well-defined articulation of the applicable measure of damages in New York. This was especially perplexing because in both breach of contract and fraud situations, the measure of damages is well defined. For breach of contract, an injured party may recover "benefit-of-the-bargain" damages,[2] while a defrauded party is entitled to recover "out-of-pocket" damages.[3] Both of these measures of damages are clearly established by the Court of Appeals,[4] and the labels are rather attractive and elegant. In tax malpractice, and in attorney malpractice in general, there simply is no analog.

To the extent there is any attempt to generalize the measure of damages in negligence situations, which includes tax malpractice, the courts state that the injured party is to be made "whole."[5] Unfortunately, this seems to be a goal rather than a

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[†] Professor of Law, St. John's University School of Law. The author gratefully acknowledges invaluable suggestions by Andrew J. Simons, Vice Dean Emeritus, St John's University School of Law, and the excellent research assistance and suggestions of Rae Kahle Buse, class of 2012.

[1] Jacob L. Todres, *New York's Law of Tax Malpractice Damages: Balanced or Biased?* 86 ST. JOHN'S L. REV. 143 (2012).

[2] *See, e.g.*, Martin v. Julius Dierck Equip. Co., 43 N.Y.2d 583, 374 N.E.2d 97, 403 N.Y.S.2d 185 (1978).

[3] *See, e.g.*, Lama Holding Co. v. Smith Barney Inc., 88 N.Y.2d 413, 668 N.E.2d 1370, 646 N.Y.S.2d 76 (1996).

[4] *See supra* notes 2–3.

[5] *See, e.g.*, *Martin*, 43 N.Y.2d at 589, 374 N.E.2d at 100, 403 N.Y.S.2d at 188. *See also* Scalp & Blade, Inc. v. Advest, Inc., 309 A.D.2d 219, 225, 765 N.Y.S.2d 92, 97 (4th Dep't 2003).

measure of damages. The problem is that there is no fixed definition of what it means to be made "whole." It depends entirely on how "whole" is defined. "To be made whole" has different meanings in different contexts. Thus, to be made whole has been applied with respect to damages from personal injury,[6] breach of contract,[7] negligence or strict products liability,[8] and breach of fiduciary duty by an executor[9] and by an escrow agent,[10] despite the fact that the measure of damages may be different in each situation. The Fourth Department was very perceptive when, with respect to a complaint that alleged causes of action for breach of fiduciary duty, negligence, breach of contract and fraud, it stated: "While the precise measure of damages may vary under each of those theories, there can be no doubt that, under all of them, the 'object of compensatory damages' is the same, i.e., to make the plaintiff 'whole.' "[11]

While it might be asymmetrical and a bit intellectually troubling that there is no attractive and pithy catch phrase describing the negligence measure of damages, as there is for fraud and breach of contract damages, I do not wish to address the entire negligence area. Negligence seems to be very broad and to include many disparate segments. For instance, it includes personal injuries by automobiles and other means, medical malpractice, damage to property, malpractice by all types of professionals, etc. Many of these areas have developed unique rules to deal with their unique circumstances. I assume the existence of these many different adaptations prevent the broad negligence area from being susceptible to one simple, catchy description. I certainly am unable to suggest one. However, I wish to focus solely on one segment of the negligence

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[6] *See, e.g.*, Buchner v. Pines Hotel, Inc., 87 A.D.2d 691, 693, 448 N.Y.S.2d 870, 872 (3d Dep't 1982), *aff'd*, 58 N.Y.2d 1019, 448 N.E.2d 1347, 462 N.Y.S.2d 436 (1983); Carr v. Third Colony Corp., 2001 N.Y. Slip Op. 40400(U), 2001 WL 1606662, at *10 (N.Y. Civ. Ct. Kings Cnty. Nov. 9, 2001).

[7] *See* Lehman Bros., Inc. v. Piper Jaffray & Co., 2008 WL 5129084 (Sup. Ct. N.Y. Cnty. May, 20, 2008).

[8] *See Martin*, 43 N.Y.2d at 589, 374 N.E.2d at 100, 403 N.Y.S.2d at 188.

[9] *In re* Rothko, 43 N.Y.2d 305, 322, 372 N.E.2d 291, 298, 401 N.Y.S.2d 449, 456 (1977).

[10] Nat'l Union Fire Ins. Co. Pittsburgh, Pa. v. Proskauer Rose Goetz & Mendelsohn, 165 Misc. 2d 539, 546, 634 N.Y.S.2d 609, 615 (Sup. Ct. N.Y. Cnty. 1994), *aff'd*, 227 A.D.2d 106, 642 N.Y.S.2d 505 (1st Dep't 1996).

[11] Scalp & Blade, Inc. v. Advest, Inc., 309 A.D.2d 219, 225, 765 N.Y.S.2d 92, 97 (4th Dep't 2003) (citations omitted).

area. It is the thesis of this Article that the traditional measure of damages in New York in all attorney malpractice situations, including tax malpractice, is essentially the same as the breach of contract measure of damages, that is, benefit-of-the-bargain damages. This is based primarily upon the definition of each measure of damages. It is also buttressed by cases that indicate that in attorney malpractice situations the damages recoverable are the same regardless of whether the cause of action is framed in tort, that is, negligence, or breach of contract.[12]

This thesis is probably not very novel. In *Solon v. Domino*,[13] the Southern District trial judge directly sidestepped addressing this issue: "[t]abling the legal question whether benefit-of-the-bargain damages are recoverable in a negligence action under New York law."[14] Presumably, this was in response to the plaintiffs' suggestion that benefit-of-the-bargain damages were the appropriate remedy in that tax malpractice situation.[15]

Before proceeding, I wish to emphasize that my thesis is that New York's *traditional* measure of damages in attorney malpractice cases is essentially the same as the benefit-of-the-bargain measure of damages of contract law. In recent years, courts in New York seem to have strayed from the traditional measure of damages in tax malpractice situations. Instead, they seem to have applied the fraud, out-of-pocket measure of damages.[16] In a recent article,[17] I argued extensively that this deviation is wrong and seems to have occurred inadvertently rather than in a principled manner. Later cases involving negligently rendered incorrect tax advice simply followed the holding in a prior case[18] involving incorrect tax advice without

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[12] *See, e.g.*, Campagnola v. Mulholland, Minion & Roe, 76 N.Y.2d 38, 42, 555 N.E.2d 611, 613, 556 N.Y.S.2d 239, 241 (1990); Santulli v. Englert, Reilly & McHugh, P.C., 164 A.D.2d 149, 152, 563 N.Y.S.2d 548, 550 (3d Dep't 1990) (Casey, J., concurring in part and dissenting in part), *modified*, 78 N.Y.2d 700, 586 N.E.2d 1014, 579 N.Y.S.2d 324 (1992).

[13] No. 08 Civ. 2837 (SCR), 2009 U.S. Dist. LEXIS 51405 (S.D.N.Y. Feb. 25, 2009).

[14] *Id.* at *9.

[15] *Id.* at *7–9. *Solin* treated the case as if the defendant were a professional advisor—that is, an attorney or accountant. In fact, the defendant was a financial advisor and it is unclear whether New York law recognizes malpractice claims against financial advisors. *Id.* at *2, *11–12.

[16] Todres, *supra* note 1.

[17] *Id.*

[18] Alpert v. Shea Gould Climenko & Casey, 160 A.D.2d 67, 559 N.Y.S.2d 312 (1st Dep't 1990).

focusing on the fact that the prior case involved only fraud causes of action, which have a much narrower measure of damages than the traditional negligence measure of damages in these situations.[19]

The benefit-of-the-bargain measure of damages for breach of contract seems to be long established and quite well understood. In an early case[20] in which the New York Court of Appeals was contrasting contract damages and fraudulent misrepresentation damages, it described breach of contract damages as follows:

> The measure of damages which flows from a breach of contract is the difference between the value of what has been received under the contract and the value of what would have been received if the contract had been performed according to its terms. Damages there are not limited to indemnity for loss suffered through the *making* of the contract. The injured party is entitled to the benefit of his bargain as written and is entitled to damages for the loss caused by failure to perform the stipulated bargain. That loss may include the profits which he would have derived from performance of the contract. [21]

In a more recent case,[22] the New York Court of Appeals essentially reiterated this earlier formulation:

> [A] cause of action for breach of warranty is a contractual remedy[—]a remedy which seeks to provide the parties with the benefit of their bargain. It is, in essence, a remedy designed to enforce the agreement, express or implied, of the parties and to

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[19] Under New York's "out-of-pocket" measure of damages for fraud, a defrauded plaintiff may recover only the difference between the amount paid and what was actually received in return. Reno v. Bull, 226 N.Y. 546, 553, 124 N.E. 144, 146 (1919). No recovery is available for any element of lost profit. *Id.* Nor is any cognizance taken of what was promised. In negligence, under New York's traditional measure of damages, a plaintiff may recover the difference between his present pecuniary position and what his position would have been without the negligence, including lost profit. Flynn v. Judge, 149 A.D. 278, 280, 133 N.Y.S. 794, 796 (2d Dep't 1912). *See infra* text accompanying notes 24–33. It is most surprising and counterintuitive that greater damages are awarded in negligence, involving an inadvertent error, than in fraud, involving intentional, egregious conduct. This demands attention and change! For a more detailed review of the fraud and negligence measures of damages, see *infra* notes 25–39 and accompanying text.

[20] Sager v. Friedman, 270 N.Y. 472, 1 N.E.2d 971 (1936).

[21] *Id.* at 481, 1 N.E.2d at 974.

[22] Martin v. Julius Dierck Equip. Co., 43 N.Y.2d 583, 374 N.E.2d 97, 403 N.Y.S.2d 185 (1978).

> place them, should one of the parties fail to perform in accordance with the agreement, in the same position they would have been had the agreement been performed.[23]

Many similar formulations abound in the lower courts.[24]

To summarize, contractual benefit-of-the-bargain damages are designed to place the injured party in the same position she or he would have been if the agreement had been performed. And these damages include any profits lost as a result of the breach.

While I have been unable to trace the traditional attorney malpractice measure of damages to an early Court of Appeals case, I have traced it back one hundred years to the Second Department in *Flynn v. Judge*.[25] In *Flynn* the plaintiffs sued their attorney alleging that his negligent advice caused them to be removed as executors and trustees of their father's estate and therefore caused them the loss of the commission income from these positions.[26] In reviewing the trial court's dismissal of the plaintiffs' causes of action, the Second Department stated:

> [T]he measure of damages is the difference in the pecuniary position of the client from what it should have been had the attorney acted without negligence.[27]

The court then quoted the following:

> 'In actions against attorneys for negligence or wrongs, the debt lost and cost sustained through their negligence furnish, when the action can be maintained, the obvious measure of damages,

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[23] *Id.* at 589, 374 N.E.2d at 99–100, 403 N.Y.S.2d at 188. *See also* Brushton-Moira Cent. Sch. Dist. v. Fred H. Thomas Assocs., 91 N.Y.2d 256, 261, 692 N.E.2d 551, 553, 669 N.Y.S.2d 520, 522 (1998) ("Damages are intended to return the parties to the point at which the breach arose and to place the nonbreaching party in as good a position as it would have been had the contract been performed.").

[24] *See, e.g.*, Schwartz v. Pierce, 57 A.D.3d 1348, 1351–52, 870 N.Y.S.2d 161, 165 (3d Dep't 2008) (quoting *Brushton-Moira Cent. Sch. Dist.*, 91 N.Y.2d at 261, 692 N.E.2d at 553, 669 N.Y.S.2d at 522); Mañas v. VMS Assocs., 53 A.D.3d 451, 454, 863 N.Y.S.2d 4, 7 (1st Dep't 2008) (quoting *Brushton-Moira Cent. Sch. Dist.*, 91 N.Y.2d at 261, 692 N.E.2d at 553, 669 N.Y.S.2d at 522); Scalp & Blade, Inc. v. Advest, Inc., 309 A.D.2d 219, 225, 765 N.Y.S.2d 92, 97 (4th Dep't 2003) (quoting Campagnola v. Mulholland, Minion & Roe, 76 N.Y.2d 38, 42, 555 N.E.2d 611, 613, 556 N.Y.S.2d 239, 241 (1990)); Cayuga Harvester, Inc. v. Allis-Chalmers Corp., 95 A.D.2d 5, 22, 465 N.Y.S.2d 606, 618 (4th Dep't 1983) (quoting *Sager*, 270 N.Y. at 481, 1 N.E.2d at 974 (1936)).

[25] 149 A.D. 278, 133 N.Y.S. 794 (2d Dep't 1912).

[26] *Id.* at 279, 133 N.Y.S. at 795–96. Plaintiffs alleged that they also incurred certain other losses. *Id.* at 279, 133 N.Y.S. at 796.

[27] *Id.* at 280, 133 N.Y.S. at 796.

> where this measure definitely exists. In other cases the plaintiff is entitled to be in the same position as if the attorney had done his duty.'[28]

Recently, the Court of Appeals addressed the proper measure of damages in an attorney malpractice situation in *Campagnola v. Mulholland, Minion & Roe*.[29] The issue before the court in *Campagnola* was the amount of damages recoverable by an injured plaintiff from his negligent attorney who was retained to prosecute an action for personal injuries.[30] The retainer agreement provided for a contingent fee to the attorney based on any recovery obtained. Due to the attorney's negligence in failing to give notice to the plaintiff's insurance company, a potential recovery of the $100,000 face amount of the insurance policy was lost. The issue the court had to decide was whether the maximum recoverable damage award was the full $100,000 or whether the $100,000 was to be reduced by the contingent fee percentage—one-third—that would have been payable to the attorney under the contingent fee arrangement.[31] In addressing the measure of damages, the court stated that "[t]he object of compensatory damages is to make the injured client whole. Where the injury suffered is the loss of a cause of action, the measure of damages is generally the value of the claim lost."[32]

While the majority's opinion seems generally consistent with *Flynn's* measure of damages, it is ambiguous about what it means to make the injured client "whole." The concurring opinion by Judge Kaye is much more explicit:

> In lawyer malpractice cases, as in all negligence cases, the focus in damages inquiries must be on the injured plaintiff—not on whether damages will unduly harm the wrongdoer defendant—the objective being to put the injured plaintiff in as good a position as she would have been in had there been no breach of duty.[33]

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[28] *Id.* (quoting EDWARD P. WEEKS & CHARLES T. BOONE, A TREATISE ON ATTORNEYS AND COUNSELORS AT LAW § 319 (2d ed. 1892)).

[29] 76 N.Y.2d 38, 555 N.E.2d 611, 556 N.Y.S.2d 239 (1990).

[30] *Id.* at 40–41, 555 N.E.2d at 611–12, 556 N.Y.S.2d at 239–40.

[31] *Id.* at 40–41, 555 N.E.2d at 612, 556 N.Y.S.2d at 240. The court held that the full $100,000 was recoverable. *Id.* at 41, 555 N.E.2d at 612–13, 556 N.Y.S.2d at 240–41.

[32] *Id.* at 42, 555 N.E.2d at 613, 556 N.Y.S.2d at 241.

[33] *Id.* at 45–46, 555 N.E.2d at 615, 556 N.Y.S.2d at 243 (Kaye, J., concurring).

As augmented by Judge Kaye's concurrence, the *Campagnola* measure of damages seems to be the same measure of damages as articulated in *Flynn*. A subsequent lower court opinion further clarifies this:

> [D]amages for malpractice are also limited to pecuniary loss—i.e., the difference between the actual result achieved and that which should have been accomplished, and the financial loss thereby sustained.[34]

Additionally, the well-known New York requirement that in a malpractice action against an attorney there often needs to be a trial within a trial[35] is simply a direct application of the *Flynn* traditional measure of damages. The "trial" of the underlying lost or botched cause of action within the malpractice trial is simply the method utilized to establish what the negligent attorney should have accomplished, which is the reference point in defining the extent of the recoverable injury suffered by the injured plaintiff.

The traditional *Flynn* measure of damages in attorney malpractice situations is that the injured plaintiff is entitled to recover the difference between his present pecuniary position and what it would have been had the negligent attorney acted without negligence.[36] When this is compared with contract benefit-of-the-bargain damages it seems to be essentially the same. In benefit-of-the-bargain damages the injured party is entitled to the difference between the value of what was received under the contract and the value of what would have been received if the contract had been performed according to its terms.[37] In both situations the damages are the difference between what should have been received (that is, non-negligent representation by the attorney or full performance of the

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[34] Sanders v. Rosen, 159 Misc. 2d 563, 572, 605 N.Y.S.2d 805, 810 (Sup. Ct. N.Y. Cnty. 1993). *See also* Lewis v. Alper, 15 A.D.2d 795, 796, 224 N.Y.S.2d 996, 998 (2d Dep't 1962) (Hopkins, J. concurring) (discussing how provable damages are "the difference in the plaintiffs' pecuniary position from what it should have been had the defendant acted without negligence").

[35] *See e.g.*, McKenna v. Forsyth & Forsyth, 280 A.D.2d 79, 82, 720 N.Y.S.2d 654, 656–57 (4th Dep't 2001); 3 Cottage Place LLC v. Cohen, Tauber, Spievack & Wagner, LLP, 2008 N.Y. Slip. Op. 30538, 2008 N.Y. Misc. LEXIS 8343 at *10–11 (Sup. Ct. N.Y. Cnty. Sept. 25, 2008); Alva v. Hurley, Fox, Selig, Caprari & Kelleher, 156 Misc. 2d 550, 555, 593 N.Y.S.2d 728, 731 (Sup. Ct. Rock. Cnty. 1993).

[36] Flynn v. Judge, 149 A.D. 278, 280, 133 N.Y.S. 794, 796 (2d Dep't 1912).

[37] Martin v. Julius Dierck Equip. Co., 43 N.Y.2d 583, 589, 374 N.E.2d 97, 99–100, 403 N.Y.S.2d 185, 188 (1978).

contract) and what was actually received. These seem identical but for terminology differences needed to describe the different contexts—negligent representation of a client versus non-performance of a contractual obligation.

It should be noted that in attorney malpractice situations there are two different relevant potential causes of action. The first is the traditional negligence cause of action that has been assumed herein. A second cause of action could be framed in terms of breach of contract, that is, that by his negligent representation, the attorney breached his contract to represent the client in an expected workmanlike, non-negligent manner. While both causes of action seem viable, there are a number of cases that hold the recovery is the same, and the cause of action is essentially for negligence.[38] This is consistent with some rather longstanding New York authority that in a civil action, whether in tort or contract, the damages should be the same, apart from the possibility of punitive damages in appropriate tort situations.[39]

In conclusion, since the New York measure of damages in attorney malpractice situations appears to be the same as in breach of contract situations, it would be refreshingly appropriate for them to be referred to by the same name—that is, benefit-of-the-bargain damages. In both situations the law seeks to make an injured plaintiff whole by awarding her or him the difference between their present financial situation and what it would have been had the other party—the attorney or the other contracting person—performed as required.

There seem to be two possible objections to simply extending the "benefit-of-the-bargain" label to attorney malpractice situations. The first arises from an abundance of caution that jurists typically display. Though the basic measure of damages seems to be the same, there is no certainty that they are absolutely identical. Some difference between the two may lurk in some crack or crevice of the complexities that may arise in each area. Why go out on a limb and suggest the rules are identical?

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[38] *See supra* note 12.

[39] *See* Baker v. Drake, 53 N.Y. 211, 220 (1873); Vooth v. McEachen, 181 N.Y. 28, 31, 73 N.E. 488, 489 (1905). Both of these cases were recently followed by the Court of Appeals in *Campagnola v. Mulholland, Minion & Roe*, 76 N.Y.2d 38, 42, 555 N.E.2d 611, 613, 556 N.Y.S.2d 239, 241 (1990).

The second objection is based upon a fundamental principle embodied in New York law. The Court of Appeals has recognized that "[t]he unique relationship between an attorney and client, founded in principle upon the elements of trust and confidence on the part of the client and of undivided loyalty and devotion on the part of the attorney, remains one of the most sensitive and confidential relationships in our society."[40] Based on this rationale the Court of Appeals held that traditional contract principles will not always apply in attorney client disputes.[41] Because of this policy, perhaps the courts would not wish to extend the contract "benefit-of-the-bargain" terminology to attorney malpractice situations, lest the special status of the attorney-client relationship be blurred or diminished thereby.

In response to these concerns I suggest that the attorney malpractice measure of damages area would still benefit from having an appropriately descriptive, pithy catch-phrase. If not "benefit-of-the bargain," I suggest that the measure of damages be referred to as "expectancy" damages," that is, the difference between the client's current pecuniary position and what it would have been had the required legal services been rendered, in an appropriate, non-negligent manner.

[40] Demov, Morris, Levin & Shein v. Glantz, 53 N.Y.2d 553, 556, 428 N.E.2d 387, 389, 444 N.Y.S.2d 55, 57 (1981).

[41] *Campagnola*, 76 N.Y.2d at 43–44, 555 N.E.2d at 613–14, 556 N.Y.S.2d at 241–42.