

“In Fact” Language Does Not Require Judicial Determination of Illegal Profiteering

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The Seventh Circuit recently concluded that coverage for an action by a former client against a law firm seeking to recover payments for legal services under a void contract is barred by the personal profit exclusion contained in the law firm's professional liability policy. *Brown & Lacounte, L.L.P. v. Westport Ins. Corp.*, No. 02-1425, 2002 U.S. App. LEXIS 21241 (7th Cir. Oct. 10, 2002). In so holding, the court found that the professional liability insurer was not required to prove the law firm's illegal profiteering as a prerequisite to denying coverage under the personal profit exclusion, which contained an "in fact" requirement.

An Indian tribe sued a law firm seeking the return of payments it made under a void legal services contract. The tribe maintained that legal services contract was void because the law firm failed to obtain the U.S. Secretary of the Interior's approval for the contract. The law firm sought coverage and a defense under its professional liability policy for the tribe's action, and the insurer denied coverage based on the personal profit exclusion. The exclusion provided that there was no coverage for claims "based upon, arising out of, attributable to, or directly or indirectly resulting from...any insured having gained in fact any personal profit or advantage to which he or she was not legally entitled." Coverage litigation ensued.

The Seventh Circuit found that the tribe's allegations against the law firm "comprise just the sort of claim barred by the policy's personal profit exclusion." In so holding, the court rejected the law firm's argument that the personal profit exclusion applies only to individual insured lawyers of the firm and not the firm itself because the exclusion refers to personal profit or advantage "to which *he or she* was not legally entitled." The court reasoned that because the term "insured" includes the law firm, "the most natural and reasonable interpretation" of the personal profit exclusion is that the law firm is included with the meaning of "any insured."

The court also rejected the law firm's argument that the insurer could not invoke the exclusion to deny coverage without first litigating the underlying allegations and proving that the law firm illegally profited. The court first reasoned that the law firm's interpretation would render the exclusion meaningless because the insurer "could never use it to exclude a claim until it defended the underlying action." Second, the court observed that policy interpretation involves questions of law and not fact. Therefore, the court found that there is no reason why it could not decide the application of the personal profit exclusion before the underlying allegations were proved. In so holding, the court distinguished *Alstrin v. St. Paul Mercury Ins. Co.*, 179 F. Supp.

2d 376 (D. Del. 2002), and similar cases holding that mere allegations of receiving illegal profits were insufficient to trigger the personal profit exclusion. The court reasoned that those cases purportedly focused on whether there was "sufficient evidence in the underlying complaint to show the profits received were illegal." Because the allegations in the Indian tribe's complaint "unequivocally" allege that the law firm reaped an illegal profit, the court found that the exclusion barred coverage.

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