

Under Pennsylvania Law, "Arising Out of" Means "Causally Connected"

April 2007

The United States District Court for the Western District of Pennsylvania, applying Pennsylvania law, has held that a contractual liability exclusion in a legal malpractice policy barred coverage only for those allegations against an attorney that arose entirely out of a real estate contract and not for other allegations involving the same transaction. *Milgrub v. Cont'l Cas. Co.*, 2007 WL 625039 (W.D. Pa. Feb. 22, 2007).

The attorney entered into a contract to sell residential real estate property that he owned. After the sale, the buyers brought a suit against the attorney contending that he acted as both the seller and as their counsel in the transaction. The buyers alleged, among other things, that the attorney breached his fiduciary duties and committed professional negligence during the transaction.

The attorney tendered the suit to the insurer under a lawyers professional liability policy. The policy contained an exclusion barring coverage for any claim "based on or arising out of the Insured's alleged liability under any oral or written contract or agreement" unless such liability "would have attached . . . in the absence of" the contract or agreement. The insurer denied coverage for the lawsuit, asserting that the claim against the attorney "arose out of" the real estate contract. Coverage litigation ensued.

Prior to deciding the coverage issue, the court made two observations. First, it asserted that, under Pennsylvania law, the phrase "arising out of" is "very broad and vague" and therefore must "be construed strictly against the insurer and liberally in favor of the insured." Construing the phrase in this manner, the court found that it means "causally connected with, not proximately caused by." Second, the court reasoned that an attorney-client retainer agreement did not fall within the contractual liability exclusion or else the exclusion could "swallow the entire Policy."

The court found that the contractual liability exclusion applied to bar coverage for the claim of professional negligence, which included the failure to secure a waiver of the alleged conflict of interest and provide effective representation. According to the court, the attorney could not possibly be liable for this claim "but for his participation in the land-sale contract" because the claim stemmed "entirely from the allegation that [the attorney] simultaneously sold his house and acted as the buyers' attorney."

With respect to the allegations of breach of fiduciary duty, however, the court found that the attorney could be liable for certain of the allegations irrespective of the "alleged conflict of interest engendered by [the] real-estate contract." In particular, the court concluded that the buyers could establish liability for the attorney's: (1) alleged failure to disclose negative conditions about the property to the buyers; and (2) alleged demand that the buyers close on the property without seeking recourse or compensation to repair discovered defects, without having to demonstrate a conflict of interest. As a result, the court held that the contractual liability exclusion did not bar coverage for all of the allegations against the attorney.