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NEWSLETTER

Other Decisions of Note

June 2007

No Coverage for Counterclaim Seeking Injunctive and Declaratory Relief or for Set-Off Affirmative Defense

The Eastern District of Louisiana, applying Louisiana law, has held that an E&O policy issued to an insurance agent does not provide coverage for fees and costs associated with defending against a counterclaim for declaratory and injunctive relief because that relief does not constitute damages an insured is legally obligated to pay. *Moore v. State Farm Mut. Auto. Ins. Co.*, 2007 WL 1343338 (E.D. La. May 4, 2007).

The insuring agreement provided that the insurer will "pay on behalf of the Insured all sums which the Insured shall become legally obligated to pay as damages because of any claim . . . arising out of . . . [a]ny negligent act, error or omission in rendering or failing to render professional services for others in the Insured's capacity as an Insurance Agent." The court reasoned that because the suit sought only injunctive and declaratory relief, the insured could not become legally obligated to pay damages since no damages were at issue in the case. It also rejected the policyholder's argument that the counterclaim should be covered since the party asserting it alleged that "the amount in controversy" exceeded $75,000. According to the court, the "attempt to value the injunctive relief sought does not transform its counterclaim into one for damages." The court also rejected the policyholder's argument that a statutory affirmative defense allowing a set-off of damages triggered coverage because "[a]t most, [the counterclaim plaintiff] may be entitled to a set-off up to, but not exceeding, the amount of the Plaintiffs' claims."

Court Interprets Securities-Based Claims Exclusion in Fiduciary Liability Policy

The United States District Court for the Southern District of New York, applying Michigan law, has held that a policy exclusion for securities-based claims in a fiduciary liability policy does not bar coverage for actions alleging violations of ERISA related to an insured's employee benefit plans even though separate lawsuits had been filed against the insured companies alleging violations of the Securities Exchange Act of 1934. *In re Tower Automotive*, 2007 WL 1149231 (S.D.N.Y. Apr. 17, 2007).

The exclusion at issue provided that no coverage would be available "for any Securities-Based Claim if such Securities-Based Claim, or *any other written demand or civil or administrative proceeding against an Insured, seeks* . . . relief for any purchaser or holder of securities issued by [the insured] who is not a Plan participant or beneficiary based upon, arising from, or in consequence of any Wrongful Acts." The insurer argued that the italicized language operated to bar coverage for ERISA actions—which the parties agreed were Securities-

Based Claims—once the Securities Exchange Act actions were filed. The court disagreed, finding that the italicized language was ambiguous and that the insurer's argument ran counter to the notion that coverage for securities claims is a fundamental element of fiduciary liability policies. Rather, reading the exclusion in light of the entire policy, the court concluded that the exclusion would apply only if the company "sought coverage for a claim—including written documents—brought by non-participants."

District Court Holds Exclusion for Claims "Arising from" Contract Precludes Coverage

The United States District Court for the Eastern District of Missouri, applying Missouri and New Jersey law, has granted summary judgment in favor of a D&O liability insurer, holding that coverage was precluded by an exclusion in the policy applicable to claims arising from the policyholder's obligations under a written contract. *Spirtas Co. v. Fed. Ins. Co.*, 2007 U.S. Dist. LEXIS 27418 (E.D. Mo. Mar. 7, 2007).

A subcontractor was insured under a D&O liability policy that excluded coverage for any claim "based upon, arising from, or in consequence of any actual or alleged liability of an Insured Organization under any written or oral contract or agreement," but allowed coverage if the insured "would have been liable in the absence of the contract or agreement." One year after the policyholder entered into a subcontract agreement with a general contractor, the general contractor brought suit against the policyholder, seeking a declaratory judgment and alleging breach of contract, conversion, breach of trust, and unjust enrichment. The insurer denied coverage and the policyholder filed suit. Both parties sought summary judgment.

In ruling for the insurer, the court recognized that, while exclusions are strictly construed, the phrase "arising from" in the exclusion was interpreted broadly under both Missouri and New Jersey law to mean "'originating from,' 'having its origins in,' 'growing out of,' or 'flowing from.'" The court concluded that all of the claims fell within the terms of the exclusion. While the court noted that claims for conversion, breach of trust and unjust enrichment were not contingent on an oral or written contract, the court emphasized that each of the general contractor's claims "arise[s] from" the alleged liability of the policyholder under the subcontract agreement and the policyholder would not be liable under any of the theories of recovery absent the contractual agreement.

Fraud Exclusion Excuses Insurer from Duty to Defend Under Professional Liability Policy

The Court of Appeals of Maryland has held that a fraud exclusion excused an insurer from its duty to defend under a professional liability policy. *Moscarillo v. Prof'l Risk Mgmt. Servs., Inc.*, 2007 WL 1109216 (Md. Apr. 16, 2007). The exclusion barred coverage for "[a]ny claim arising out of or in connection with any dishonest, fraudulent, criminal, maliciously or deliberately wrongful acts or omissions, or violation of law committed by an Insured." The policyholder, a psychiatrist, was accused in underlying litigation of fraudulently diagnosing a patient to help her obtain disability benefits. After the insurer denied coverage based on the fraud exclusion, the insured instituted a declaratory judgment action seeking to establish that the insurer had to reimburse the defense costs he had incurred. In affirming summary judgment for the insurer, the court interpreted the policy to require the insurer to defend the psychiatrist where there was a claim for negligence but not "where the pleadings . . . alleged only fraudulent conduct." The court then considered whether any claim in the

underlying litigation could potentially fall within policy's coverage. The psychiatrist argued that extrinsic evidence indicated that he had committed malpractice. The court, however, refused to find a duty to defend because the psychiatrist's position would require the court to re-characterize the underlying complaint, which alleged only intentional torts of fraud and conspiracy, not malpractice. The court also rejected the psychiatrist's argument that the exclusion required a finding of fraud, reasoning that the plain language of the exclusion applied and contained no such requirement.

Declaratory Judgment Action Not Ripe Where Court Approval of Settlement Agreement Pending

The United States District Court for the Western District of Missouri has held that an insurer's declaratory judgment action regarding its duty to indemnify the insured under a claims made policy for a class action settlement was not ripe where the settlement remained subject to final court approval in the underlying action. *Executive Risk Indem., Inc. v. Asurion Protection Servs., LLC*, 2007 WL 1378376 (W.D. Mo. May 7, 2007). The insurer accepted the insured's defense under a reservation of rights, but when the insured requested the insurer contribute to a proposed settlement agreement, the insurer filed a declaratory judgment action. After the action was filed, the parties in the underlying litigation finalized the settlement agreement, pending court approval. In ruling on the insured's motion to dismiss the declaratory judgment action, the court first noted the prohibition on rendering advisory opinions and observed that the settlement ultimately might not receive judicial approval. Nevertheless, the court stated that the underlying court considering the settlement appeared to be moving quickly to resolve the matter, and so it denied the insured's motion to dismiss and issued a stay pending final action on the underlyingsettlement.