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NEWSLETTER

E&O Policy Provides Coverage Where Alleged Conduct Involving Procurement of Insurance Could Be Considered Negligent

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The United States District Court for the District of Oregon, applying Oregon law, has held that an E&O policy provides coverage for a lawsuit against an insured municipality and its city manager alleging that they improperly obtained health insurance for retired employees. *City of Medford v. Argonaut Ins. Group*, 2007 WL 4570713 (D. Or. Dec. 26, 2007). The court rejected the insurer's argument that the alleged conduct was intentional and also rejected the insurer's arguments that certain policy provisions precluded coverage.

The insured municipality and city manager sought coverage under an E&O policy for a lawsuit by former city employees who claimed that the city improperly obtained health insurance coverage that did not cover retirees. The complaint alleged violations of a state law and of a city ordinance due to the insureds' "intentional conduct of not providing the opportunity for any Plaintiff to participate in its health care insurance program upon their retirement." The complaint also alleged civil rights violations and willful violations of state and federal age discrimination laws. The coverage action ensued, and the insurer and the insureds filed cross-motions for partial summary judgment on the insurer's duty to defend.

The E&O policy included an employee benefits liability form and an employment practices liability form, both of which the court considered and found to provide coverage. The employee benefits liability form provided coverage for claims "caused by the negligent act, error or omission of the insured . . . in the administration of the insured's employee benefits program." The insurer argued that "the decision to obtain health insurance that did not extend to retired employees was purposeful and deliberate, not negligent." The municipality and city manager responded that the complaint alleged that the city manager failed to follow the advice of the city attorney regarding the proper interpretation of a state statute governing employee benefits. They also argued that the failure to follow legal advice could be negligent and was an error in judgment that should be covered under an E&O policy. The court agreed, contrasting the allegations with *Baylor Heating & Air Conditioning, Inc. v. Federated Mutual Insurance Co.*, 987 F.2d 415, 419 (7th Cir. 1993), in which the Seventh Circuit interpreted a similar policy and held that an insured who had acted upon the advice of counsel had acted intentionally. The court noted that unlike the situation in *Baylor*, the insureds allegedly had acted *against* the advice of counsel, and the court concluded that the insureds' decision could be considered a

"negligent act, error or omission" under the policy. The court acknowledged that "the decision to go against the advice of counsel could also be considered intentional" but held that "the ambiguity should be construed against the insurer."

The insurer further argued that the city's decision to obtain health insurance that did not cover retirees was not administration of an employee benefits program as defined by the policy. The policy defined "administration" as follows:

a. Giving counsel to employees with respect to the employee benefits programs;
b. Interpreting the employee benefits program;
c. Handling of records in connection with the employee benefits programs;
d. Effecting enrollment, termination or cancellation of employees under the employee benefit programs, ...

The insurer cited *Maryland Casualty Co. v. Economy Bookbinding Corp. Pension Plan & Trust*, 621 F. Supp. 410, 414 (D.N.J. 1985), in which the court held that a similar policy covered only "liability incurred in relatively routine, ministerial acts" and not "liability incurred in the decision-making and monitoring involved in managing [a] [p]lan's investments." The court, however, disagreed with *Maryland Casualty's* "narrow interpretation of the word 'administration,'" emphasizing that the policy did not restrict the definition to ministerial acts. Accordingly, the court rejected the insurer's argument and held that the insureds' decision effected "enrollment, termination or cancellation of employees under the employee benefit programs."

The court also rejected the insurer's argument that the alleged wrongful conduct did not occur within the policy period. The insurer maintained that the claim stemmed from the city's purchase of health insurance coverage that did not extend to retirees, a purchase that occurred before the E&O policy took effect. The municipality and city manager countered that the benefits at issue were established by city ordinances that went into effect during the policy period. The court agreed with the insureds, determining that the choice of health coverage occurred during the policy period. In doing so, the court emphasized that the complaint alleged that the city could have obtained health insurance coverage during the policy period that extended to retirees but chose not to do so.

The court next considered the employment practices liability form, which provided coverage for "wrongful employment acts." The definition of "wrongful employment act" included "[e]mployment discrimination." The court indicated that coverage existed under the employment practices liability form, pointing out that the underlying plaintiffs alleged age discrimination under state and federal law.

The insurer argued that coverage was barred by a policy exclusion for claims "flowing from or originating out of the failure to secure or maintain proper insurance or bonds" because the claims depended on the allegation that the insureds failed to maintain proper insurance for retirees. However, the court concluded that

this exclusion did not apply because the complaint "allege[d] discrimination based on age, and s[ought] damages stemming from the City's alleged age-related disparate treatment of the plaintiffs."

The insurer also argued that coverage was barred by an exclusion for claims "flowing from or originating out of any violation of any of the duties or responsibilities required of the insured as an employer by the following laws or similar provisions of any other laws, rules, or regulations." The policy listed a number of federal statutes, including COBRA and ERISA. The insurer maintained that the state statute that the insureds were alleged to have violated was analogous to both COBRA and ERISA. The court, however, held that this state statute was "not so similar to the listed statutes as to fall within this exclusion." Therefore, the court granted the motion of the city manager and municipality for partial summary judgment and denied the insurer's motion.