

Appeals Court Vacates Stay of Insurer's Declaratory Action

August 2010

The United States Court of Appeals for the Seventh Circuit, applying Indiana law, has reversed a stay of an insurer's declaratory judgment action seeking a determination that the insured breached the cooperation clause in the policy. *Mut. Assurance Co., Inc. v. Hellman*, No. 08-2887 (7th Cir. Jun. 21, 2010). In so holding, the appellate court determined that the insurer was entitled to establish evidence of actual prejudice despite the ongoing underlying proceedings in state court.

The insurer provided professional liability insurance coverage to the insured, who operated a medical office. In 2004, the insured, facing several federal charges, left the country and disappeared. Following his disappearance, hundreds of malpractice claims were filed against the insured. The policies provided defense and indemnity coverage to the insured subject to a cooperation clause, which required the insured to "fully cooperate with [the insurer] and defense counsel in the investigation, handling, and defense of the legal proceeding." Based upon the insured's disappearance, the insurer filed suit in federal court seeking a declaration that the insured breached the cooperation clause, thus relieving the insurer of its duties to defend and indemnify. The district court stayed the declaratory judgment action on comity and fairness grounds, pending resolution of the parallel proceedings in state court. The insurer appealed.

Finding that the district court abused its discretion, the appellate court vacated the stay and remanded the declaratory judgment action for further proceedings. In so determining, the court noted that the existence of parallel proceedings in state court is not in and of itself sufficient to warrant a stay. Rather, the court must inquire about the prospect that "the declaratory action may present factual questions that the state court also has been asked to decide." The appellate court further rejected the district court's conclusion that the insurer could not demonstrate actual prejudice from the lack of cooperation without interfering with factual determinations in the pending underlying actions in state court. The appellate court held that it was "not willing to assume that the only way [the insurer] can prove its case is through an excursion into factual questions that the state courts have been, or will be, asked to address." Moreover, the court emphasized the significance to the insurer of having a single ruling pertaining to the impact of the insured's behavior on the coverage determination.