

# Counterclaims Seeking Declaration of Rights and Attorneys' Fees Give Rise to 'Loss' Under D&O Coverage Form

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The United States District Court for the Western District of Missouri, applying Missouri law, has held that counterclaims seeking declarations regarding the rights of insured entities and the recovery of attorneys' fees give rise to "loss" and "defensible incidents" under D&O and Legal Defense Coverage Forms in commercial multi-peril and church package policies. *Church Mutual Ins. Co. v. The Exec. Board of the Mo. Baptist Conv'n*, 2005 WL 1532948 (W.D. Mo. June 24, 2005). The court also found that the insurer was estopped from denying coverage under the Legal Defense Coverage Forms because it had made an initial payment of defense expenses before refusing to provide coverage.

The plaintiff insurer issued commercial multi-peril, umbrella liability and church package policies to a number of Baptist churches in Missouri. The insurer also issued commercial multi-peril and umbrella liability policies to an unincorporated association of affiliated Baptist churches that functioned as the state's denomination. These multi-peril and church package policies generally included a Legal Defense Coverage Forms and/or a Directors, Officers and Trustees Liability Coverage Form (D&O Form). The Legal Defense Coverage Forms generally provided that the insurer will "pay 'defense costs,' incurred by the insured, that result from a 'suit' to which this insurance applies . . . only if . . . [t]he 'suit' results from a 'defensible incident.'" A "defensible incident" is defined as "any acts, omissions or failures of the insured."

The D&O Forms generally provided that the insurer will pay "those sums that any of your 'Directors, Officers or Trustees' become legally obligated to pay for 'loss' arising from any claim or claims because of injury arising out of a 'wrongful act.'" In addition, the D&O Form provided that the insurer has "the right and duty to defend the insured against any 'suit' seeking payment for 'loss' and to pay for the 'defense expense.'" Under this form, "loss" was defined as "damages, judgments, settlements and defense expenses."

The insured entities filed a class action against five non-profit Baptist organizations that had previously been members of the association of affiliated churches. At one time, the non-profit organizations' articles of incorporation provided that each organization's trustees would be elected or appointed by the association of churches. The dispute arose after the organizations amended their articles of incorporation to remove the association's involvement from the election of their trustees. As part of this underlying suit, the organizations

filed counterclaims against the insured entities, which generally sought declarations that: (1) the non-profit organizations had legally amended and filed their restated articles of incorporation, (2) the insured entities were not members of the non-profit organizations, (3) the insured entities did not have the "right" to elect the trustees of the various organizations and (4) the insured associations had no rights to the property of the organizations. Although they did not seek monetary damages, the underlying counterclaimants sought attorneys' fees and costs in the event their counterclaims were successful. The insurer initially issued a \$5,000 payment for defense expenses to the association of churches, but later denied coverage for any additional defense costs. The insurer also never provided a defense to any of the other insured entities for the counterclaims.

In this coverage action, the insurer sought a declaration that the allegations contained in the counterclaims did not trigger any duty to defend the insured entities because the counterclaims sought no money damages and alleged no "conduct or wrongful act that could potentially trigger coverage." The insured entities filed counterclaims in the coverage litigation seeking a declaration as to their right to a defense and damages for breach of contract and bad faith refusal to defend.

The district court rejected the insurer's argument that there was no duty to defend the insured entities against the underlying counterclaims under both the Legal Defense Coverage Forms and the D&O Forms. With respect to the D&O Forms, the court concluded that the declarations sought by the non-profit organizations in their counterclaims constituted "loss" under the policies – in the form of "judgments" and "defense expenses." In addition, the court noted that under *Hyatt Corp. v. Occidental Fire & Casualty Co.*, 801 S.W.2d 382 (Mo. Ct. App. 1990), the award of attorneys' fees and costs "is indistinguishable from a damages award for [insurance] coverage purposes."

With respect to the Legal Defense Coverage Forms, the court found that the counterclaims formed a "suit" arising from a "defensible incident," as it was "obvious" that the counterclaims were "premised on acts or omissions of the [association]," which fell under the definition of "defensible incident." The court further noted that the insurer was estopped from denying coverage under the Legal Defense Coverage Forms because it "has already admitted the applicability of this provision to the subject claims and paid a portion of the defense costs pursuant thereto." The court concluded that this payment was an "[i]mplicit" acknowledgement that "the counterclaims at issue constitute a 'suit' to which the insurance policy applies."

The court, however, rejected the insured entities' claim for bad faith refusal to provide a defense. The court stated that "[g]iven the policy language, and the nature of the [counter]claims . . . the Court finds that [the insurer] did have a reasonable basis for denying the counterclaimants a defense and indemnity under the policy issued to [the association]."

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