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NEWSLETTER

Other Decisions of Note

July 2005

Free Extended Reporting Period Does Not Extend Coverage to Claims Made After Expiration of Legal Malpractice Policy

In an unreported decision, a federal district court, applying Colorado law, has denied an insured's motion for summary judgment, holding that a free 60-day "mini-tail" for reporting claims does not extend coverage to claims made after expiration of the policy period under a claims-made legal malpractice policy. *Bornstein v. Westport Ins. Corp.*, 2005 WL 1459738 (D. Colo. June 21, 2005). The insurer issued the policy to an attorney with a provision warning that coverage might not be available for claims made against the attorney after expiration of the policy period "unless you purchase an Extended Reporting Period or 'tail' endorsement." The policy was marketed to the attorney by a flyer stating that the policy included "a free 60-day *mini-tail* for reporting claims." The court rejected the attorney's argument that the free "mini-tail" extended coverage to a claim made against the attorney after expiration of the policy, concluding that the brochure only provided an extended period for reporting claims and did not mention the making of a claim.

Insurer's Right to Control Defense Includes Right to Select Defense Counsel

The United States District Court for the Eastern District of California has granted summary judgment for an insurer, holding that the insurer's right to control the defense it provides to a policyholder under a professional liability policy includes the right to select defense counsel. *Carolina Cas. Ins. Co. v. Bolling, Walter & Gawthrop*, 2005 WL 1367096 (E.D. Cal. May 31, 2005). The insurer issued a lawyer's professional liability policy to the defendant law firm. The policy stated that "[t]he insurer shall have the right and duty to defend any Claim to which this insurance applies." A former client of the defendant law firm filed a malpractice action against the firm and an individual lawyer. The firm tendered the claim to the insurer but requested that the firm be allowed to defend itself in the underlying action and charge its hourly rate against the policy deductible. The insurer rejected this request and indicated its preference for retaining counsel to defend the action, but the law firm continued to conduct its own defense. The insurer filed this action seeking a declaration that it has the right to select defense counsel or, alternatively, that it is not obligated to defend or indemnify the insured. The court held that "the right and duty to defend affords an insurer the right to control the defense." The court further held that "while the Policy does not expressly state that [the insurer] has the right to select defense counsel, the right to control the defense generally includes the right to select defense counsel." In so holding, the court expressly rejected the law firm's contention that it had a right to defend itself up to the amount of the deductible, noting that this argument "defies a common sense reading of the insurance contract."

Retaliation Allegations Not Related to Discrimination Allegations for Purpose of Prior Acts Exclusion

In an unpublished decision, the United States District Court for the District of Puerto Rico has held that even though the prior acts exclusion in an EPL policy precluded coverage for allegations of discrimination that took place before the prior acts date, the exclusion did not apply to allegations of retaliatory firing by the same plaintiff in the same case. *San Miguel v. Necso Redondo*, S.E., 2005 WL 1397447 (D.P.R. June 9, 2005). The prior acts exclusion at issue stated that "[l]oss(es) arising out of the same or related Wrongful Act(s) shall be deemed to arise from the first such same or related Wrongful Act." However, the court did not provide any analysis as to why it rejected the insurer's argument that the two sets of allegations were related.

California Court Holds Insurer Not Entitled Unilaterally to Rescind Policy and Must Advance Defense Costs Pending Court Ruling on Rescission

In an unpublished minute order, the Superior Court of California for San Diego County has granted plaintiffs' motion for summary adjudication, declaring that a primary insurer that issued a D&O policy that was later rescinded unilaterally was obligated to provide a defense to its insureds until a court issued a ruling on the validity of the insurer's rescission of the policy. *Cole v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, No. GIC821682 (Cal. Super. Ct. May 23, 2005). The insurer argued that it was not obligated to provide a defense because the policy was void from its inception and had been properly rescinded in compliance with the requirements of California's rescission statutes. The court rejected this argument, holding "[t]he essential facts are undisputed, and based on the policy language, and the fact that no court has yet ruled on [the insurer's] rescission claims or its policy defense, [the insurer] has a duty, since 5/02, to pay Plaintiffs' reasonable defense expenditures in [the underlying actions]." The court also held that the insurer "has a duty to pay Plaintiffs' reasonable defense expenditures in the [underlying actions] until there is a final decision by this Court that [the insurer] is entitled to rescind its policy."

Federal Court in Connecticut Refuses to Dismiss Equitable Subrogation Action

The United States District Court for the District of Connecticut has denied an insurer's motion to dismiss an equitable subrogation action brought by another insurer to recover the costs incurred in defending a lawyer under a reservation of rights in two lawsuits related to a first lawsuit that was filed and reported during the defendant insurer's policy period. *Westport Insurance v. St. Paul Fire & Marine Insurance Company*, 2005 WL 1412131 (D. Conn. June 14, 2005). The first insurer issued a claims-made policy to an attorney. The policy provided that the first insurer would "consider all claims or suits for covered loss caused by a wrongful act, or a series of related wrongful acts, to have been made or brought on the date that the first of those claims or suits is first made or brought." The second insurer issued a claims-made and reported professional liability policy to the lawyer for the subsequent policy period. Three lawsuits were filed against the lawyer for malpractice relating to a single matter—one during the first insurer's policy period and two during the second insurer's policy period. The first insurer refused to participate in the defense of the two lawsuits filed during the second insurer's policy period and the second insurer provided a defense in those suits subject to a reservation of rights. In denying the first insurer's motion to dismiss the resulting equitable subrogation action, the court rejected the first insurer's contention that the amount of the second insurer's recovery should be limited to the settlement amount in the underlying action, noting that "[t]o hold otherwise would inappropriately create incentives for insurers in situations where two policies are in effect to decline coverage,

because their maximum liability in a subrogation action would be limited." The court also rejected the first insurer's contention that the second insurer was a volunteer and thus not entitled to equitable subrogation. The court noted the lack of controlling Connecticut case law on the issue and, applying *Erie*, held that "this Court believes that the Connecticut Supreme Court would permit subrogation actions where an insurer pays a loss for which it reasonably may be liable, even if its obligation under the policy is in dispute."

Ninth Circuit Finds No Coverage for Employees' Unpaid Wages Under Liability Policy

In an unpublished decision, the United States Court of Appeals for the Ninth Circuit has determined that a policyholder was not entitled to reimbursement for defense fees or indemnity payments in connection with a claim alleging that the policyholder violated California labor laws and failed to pay overtime wages. *Big 5 Corp. v. Gulf Underwriters Ins. Co.*, 2005 WL 1529709 (9th Cir. June 30, 2005). Applying California law, the court determined that, because the underlying claimant employees sought unpaid overtime wages, the claim constituted an employment claim as defined by the liability policy at issue. The court then determined that, because this was an employment claim, the underlying claimants satisfied the policy's definition of "directors and officers," which included "employees" for purposes of such claims. Finally, the court noted that the policy plainly excluded coverage for claims by directors and officers for "any claim for wages," and, accordingly, held that there was no coverage for defense costs or settlement payments made in connection with the underlying action.

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