

ALERT

Prior Knowledge of Potential Malpractice Claim Precludes Coverage under Lawyers Professional Liability Policy

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The United States District Court for the Eastern District of Michigan, applying Michigan law, granted an insurer's motion for summary judgment holding that a prior knowledge condition in the policy's insuring agreement barred coverage for an underlying legal malpractice claim. *McKeen v. Continental Cas. Co.*, 2011 WL 3839803 (E.D. Mich. Aug. 30, 2011). The court also granted the insurer's motion for summary judgment on the policyholder's bad faith claims. Wiley Rein LLP represented the insurer in this matter.

The policyholder sought coverage under a lawyers professional liability policy for a legal malpractice suit that arose from its representation of a client in a medical malpractice and wrongful death action. Prior to the inception of the policy, the trial court in the medical malpractice action had dismissed the case as a sanction for the policyholder's failure to comply with discovery orders, and the Michigan Court of Appeals affirmed the trial court's dismissal and denied the policyholder's motion for reconsideration.

The insurer denied coverage for the subsequent legal malpractice claim filed by the client based on the prior knowledge condition in the policy's insuring agreement. Specifically, the policy afforded coverage only if no Insured "had a basis to believe that any such act or omission [on which the claim is based], or related act or omission, might reasonably be expected to be the basis of a claim." The policyholder then filed a lawsuit against the insurer seeking coverage and alleging bad faith.

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Ruling on the parties' motions for summary judgment, the court held that the policy afforded no coverage for the legal malpractice claim because the prior knowledge condition to coverage was not satisfied. The court determined that the prior knowledge provision was unambiguous and that, in light of the adverse events in the medical malpractice suit that occurred prior to the inception of the policy, the policyholder had a reasonable basis to expect that a claim might be made against it. The court held that the policyholder's subjective belief that the client would not bring a legal malpractice claim was "irrelevant." In this regard, the court found that the policyholder's subjective belief that it was not facing a claim was unreasonable as a matter of law in light of the undisputed facts.

The court also granted the insurer's motion for summary judgment on the policyholder's bad faith claim. First, the court ruled that the policyholder did not state a claim for bad faith breach of an insurance policy under Michigan law because the policyholder alleged no duty separate and distinct from the policy that the insurer had allegedly breached. In addition, the court held that the policyholder was not entitled to penalty interest under Michigan statute for failure to timely pay the claim because coverage was reasonably in dispute.