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ALERT

Facts Outside Complaint Required Insurer to Assume Duty to Defend; Corporation Entitled to Indemnification for Settlement Despite Applicability of Exclusion to Individual

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Applying Massachusetts law, a federal district court has held that an insurer could not rely solely on the allegations set forth in an administrative charge of discrimination to deny a defense where the insurer had knowledge of facts from other sources that established a potential for coverage. The court also held that the insurer was obligated to indemnify the insured entity for its settlement of a claim involving allegations of sexual harassment by a former officer even though the policy's intentional acts exclusion precluded coverage for that individual insured. *Manganella v. Evanston Ins. Co.*, 2011 WL 5118898 (D. Mass. Oct. 28, 2011).

The former president of a clothing boutique and the boutique sought coverage under an employment liability policy for a charge of discrimination filed with the state commission against discrimination by the boutique's former human resources manager. In the charge, the manager alleged that she had worked for the boutique from 1997 to 2006 and that the president had subjected her to nearly constant physical and verbal sexual harassment "throughout her employment." The policy included a retroactive date of April 28, 1999, limiting coverage to claims arising out of acts committed after that date. The insurer refused to provide a defense on the grounds that the charge alleged harassment of the manager beginning with the start of her employment in 1997 and therefore before the policy's retroactive date. The boutique subsequently settled with the claimant for $300,000.

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In a prior coverage opinion in this case — which was reported in the December 2010 edition of *Executive Summary* — the court found that the insurer had information calling into question whether the alleged harassment in fact had begun before the retroactive date. Specifically, the insurer had an affidavit provided by the manager in connection with a prior claim on November 13, 1998, which stated that she never witnessed or heard from anyone associated with the company that the president had committed any acts of sexual harassment. According to the court, "[a]t a minimum," the insurer "had a duty to investigate the inconsistency between its own records and the [commission] charge before choosing the version of facts that justified a denial of coverage, while ignoring another under which coverage attached." The court therefore held that the denial of a defense based on the retroactive date was improper at that point.

The boutique subsequently moved for summary judgment on its claim for reimbursement of the settlement amount. The court held that because the insurer had breached its duty to provide a defense, it had the burden to prove that the claim was not within the policy's coverage, and that the insurer failed to meet this burden because the evidence presented on the issue was "in equipoise." The court further held that while a prior finding of intentional misconduct by the former president triggered the policy's intentional acts exclusion with respect to him, the exclusion did not apply to the boutique because the boutique only faced vicarious, and not direct, liability. Accordingly, the court concluded that the insurer was obligated to indemnify the boutique for its settlement of the claim.