

Leaving Law Firms in the Lurch: The Insured versus Insured Exclusion Applied to the Modern Law Firm

The Illinois Appellate Court, First District recently applied the insured versus insured exclusion in the context of a defamation claim by a former employee of a law firm against her firm. While the case appears to be a straight forward application of the exclusion, the ruling has significant future repercussions. In particular, the broad interpretation afforded this insured versus insured exclusion leaves law firms greatly exposed when confronted with a claim made by a partner or an associate in the firm.

In Andreou and Casson, Ltd. v. Liberty Insurance Underwriters, Inc., No. 1-05-2754, 2007 WL 2769252 (Ill. App. Ct., 1st Dist., September 24, 2007), the Court considered an appeal by plaintiffs Andreou and Casson, Ltd. *et al.* (“A&C”) from the trial court’s grant of defendant Liberty’s motion for summary judgment. This lawsuit, an insurance coverage action stemming from the underlying defamation action and a denial of A&C’s tender to its carrier Liberty, was filed for purposes of obtaining a declaration that Liberty owed A&C a duty to defend.

Dana Kurtz filed the underlying defamation action against A&C, claiming breaches of fiduciary duties, fraud, disparagement, defamation, and humiliation. She alleged that as a partner with the firm, she had been improperly ousted and that the firm had “publicly disparaged her professionalism and integrity,” such as by making false representations to clients and falsely alleging that she had removed files from the law firm. Kurtz also alleged that A&C breached the partnership agreement by failing to change the firm name to incorporate her name. The trial court found that contrary to A&C’s argument, Kurtz was a partner in the law firm. It also concluded that A&C breached the partnership agreement.¹

The Liberty Policy issued to A&C was an Illinois lawyers professional liability policy that covered wrongful acts, *i.e.*, “any actual or alleged act, error omission, or personal injury which arises out of the rendering or failure to render professional legal services.” The Policy covered insureds, defined as:

“b. if the named insured is a partnership ... such partnership ... and each lawyer who is a partner thereof including any incorporated partner and each shareholder of any such incorporated partner;

* * *

d. each lawyer employed by the named insured;”

The Policy contained the following exclusion: “The policy does not apply to any claim made by one or more insured against another insured....”

¹ The parties eventually reached an undisclosed settlement.

The issue before the Appellate Court was whether the insured versus insured exclusion excused Liberty from any duty to defend. Relying on the trial court's finding that Kurtz was a partner in A&C, the Court concluded that the insured versus insured exclusion clearly applied. The Court thus affirmed the trial court's summary judgment.

While the decision here was likely a foregone conclusion in light of the trial court's ruling that Kurtz was a partner in the law firm, the Court's interpretation of the insured versus insured exclusion has more far reaching implications. The insured versus insured exclusion had not been previously applied in the context of an action against a law firm, thereby making this a case of first impression.

The broad interpretation given the exclusion leaves law firms without coverage under a professional liability policy when faced with a lawsuit brought by a partner in the firm, or by virtue of subsection (d), an associate in the firm. This could include discrimination or harassment, tort, and even breach of contract claims.

Additionally, while the Court considered the insured versus insured exception, it could just as easily have excused any duty to defend based on the Liberty Policy's definition of "wrongful acts." In particular, the Court could have found that the underlying complaint did not satisfy the professional legal services rendered provision.

The message being delivered to law firms by the Illinois Appellate Court appears to be that when confronted with breach of contract or tort claims filed by partners or associates of the firm, the appropriate recourse is something other than their professional liability policies. Accordingly, law firms should be sure to procure and turn to their general liability insurance policies so as to avoid being sent into the proverbial battle without a shield.

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