

# Prior Knowledge Exclusion Bars Coverage Where Accusations Against Insured Provided Notice of Forthcoming Malpractice Suit

---

January 2007

The United States Court of Appeals for the Fourth Circuit, applying Maryland law, has held in an unpublished opinion that a court petition seeking to remove an accountant as personal representative of an estate put the accountant on notice of a potential malpractice claim and that, as a result, coverage was barred under an accounting malpractice policy's prior knowledge exclusion. *Westport Ins. Corp. v. Albert*, 2006 WL 3522500 (4th Cir. Dec. 6, 2006).

The insurer issued two consecutive professional malpractice policies to an accountant. The policies, which covered claims made and reported for the policy periods of January 1, 2001 to January 1, 2002 and January 1, 2002 to January 1, 2003, excluded from coverage "any act, error, omission, circumstance, or 'personal injury' occurring prior to the effective date of this 'policy' if any insured at the effective date knew or could have reasonably foreseen that such act, error, omission, circumstance or 'personal injury' might be the basis of a 'claim.'"

The accountant served as the personal representative to a woman's estate. The accountant had previously set up an annuity to provide the woman with income while transferring funds to her beneficiary in a way that avoided taxes. In November 2001, after the woman's death, the beneficiary filed a petition to remove the accountant as the estate's personal representative. The filing, which the accountant received on December 3, 2001, alleged that the accountant had breached his fiduciary duty and had mismanaged estate property. The accountant did not tender that suit to the insurer. In January 2002, the beneficiary filed a malpractice suit against the accountant, who gave notice to the insurer in February 2002. The insurer sought a declaratory judgment that neither the 2001 nor the 2002 policy covered the malpractice suit.

The Fourth Circuit first noted that, under Maryland law, the prior knowledge exclusion would apply if the November 2001 suit "would have put an objectively reasonable accountant on notice that a malpractice suit was forthcoming." The court held that an objectively reasonable accountant would have reached such a conclusion here when faced with the 2001 suit alleging breach of fiduciary duty.

With respect to the prior policy, the court held that the accountant was barred from seeking coverage under that policy since he did not timely raise the argument in the pleadings below. The court also noted that, even

if the argument could be asserted, coverage was barred under the 2001 policy since the accountant did not provide notice during that policy period. The accountant pointed to a Maryland law requiring prejudice in order for an insurer to deny coverage based on late notice. The court rejected that argument, explaining that the "law, however, applies only to 'claims made' policies and not 'claims made and reported policies.'"