

Coverage for Lawyer's Malpractice Claims Barred by Misappropriation and Dishonesty Exclusions

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The Supreme Court of Nebraska has held that misappropriation and dishonesty exclusions in a lawyers professional liability policy barred an attorney's former clients from executing legal malpractice judgments against the insurer that issued the policy. *Fokken v. Steichen*, 2008 WL 62539 (Neb. Jan. 4, 2008).

Several of the attorney's former clients accused him of settling their tort claims without their approval by signing their signatures on release agreements and settlement checks without their authorization. The former clients also asserted that they had not received any of the settlement proceeds from the attorney. Furthermore, the former clients alleged that the attorney (1) failed to communicate with them regarding the defendants' settlement offers; (2) accepted the settlement offers on their behalf without obtaining their consent; (3) allowed their tort claims to be dismissed with prejudice after the statute of limitations had expired; and (4) breached fiduciary duties owed to them. The former clients won malpractice judgments against the attorney and then instituted garnishment proceedings against the attorney's insurer, and the parties cross-moved for summary judgment.

In granting the insurer's motion for summary judgment, the court first observed that the former clients' garnishment claims against the policy proceeds depended on whether the insurer would have been obligated to indemnify the attorney for the malpractice judgments in the first place because "the claim of a judgment creditor garnishor against a garnishee can rise no higher than the claim of the garnishor's judgment debtor against the garnishee." The court next considered the former clients' argument that "where an insurance company is notified of a pending suit against an insured and has a full opportunity to defend the action, the judgment against the insured, if obtained without fraud or collusion, will be conclusive against the insurance company." The court rejected this contention, explaining that the insurer was not challenging the malpractice judgments but was instead contending that the judgments were not covered by the policy.

The court then considered the effect of the misappropriation exclusion, which barred coverage for "any CLAIM arising out of conversion, misappropriation or improper commingling of funds." The former clients contended that their malpractice claims against the attorney were not barred by the exclusion because they were based

on the attorney's failure to communicate regarding the settlement and dismissal of their actions after the statute of limitations had expired. The former clients conceded that the attorney may have committed acts of conversion, misappropriation or commingling of funds but argued that those acts were not the proximate cause of their damages. The court, however, relying on *O'Toole v. Brown*, 422 N.W.2d 350 (Neb. 1988), interpreted the "arising out of" language in the exclusion to require no more than a causal connection. Having found such a causal connection between the attorney's acts of conversion, misappropriation and commingling of funds in signing the settlement checks and retaining the settlement funds and the former clients' claims to recover the settlement funds, the court concluded that the exclusion barred coverage for those claims.

The court then turned to the application of the dishonesty exclusion, which barred coverage for "any CLAIM that results in a final adjudication against any INSURED that an INSURED has committed any criminal, dishonest, fraudulent or malicious acts, errors, omissions or PERSONAL INJURIES." The former clients argued that the trial court had based the malpractice judgments against the attorney on the attorney's failure to obtain their consent to settle the tort claims, not upon an act of dishonesty. The court, however, interpreted the trial court's decision to include a finding that the attorney had signed the former clients' names on the settlement checks without their authorization. The court held that this finding constituted a final adjudication of dishonesty that precluded coverage for the balance of the malpractice judgments.