

# Massachusetts District Court Determines No Coverage for Attorney's Failure to Pay Tax Fines Because Tax Returns Were Filed Prior to Policy's Retroactive Date



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The United States District Court for the District of Massachusetts, applying Massachusetts law, has held that an attorney's failure to pay tax fines promptly arose out of his earlier failure to file tax returns timely, which occurred prior to the retroactive date of his lawyer's professional liability policy. *Ferguson v. General Star Indemnity Co.*, 2008 WL 4696900 (D. Mass. Sept. 18, 2008).

The insurer issued a claims made lawyer's professional liability policy effective September 13, 2000, that contained a "Retroactive Date" of September 12, 1997. The policy specified that it did "not apply to [Claims] arising out of negligent act(s), error(s), or omission(s) which took place prior to the Retroactive Date[.]"

The insured attorney represented the executrix of an estate. The attorney failed to file an estate tax return that was due on October 27, 1994. He did not file the requisite estate tax return until July 5, 1996. The attorney did not remit the resultant penalties and interest until March 1998 for federal taxes and July 2001 for state taxes. The executrix ultimately paid \$241,600 in penalties and interest related to the attorney's errors. The executrix sued the attorney and his law firm for malpractice and negligence in August 2001. The insurer denied coverage and refused to provide a defense, noting that the events giving rise to the claim appeared to have occurred prior to the policy's September 12, 1997, retroactive date. A subsequent judgment was entered against the attorney for negligence for \$224,046.41. The attorney assigned his rights against the insurer to the executrix, who then filed suit against the insurer.

In the coverage litigation, the insurer argued that the claim arose out of acts that took place prior to the policy's retroactive date (*i.e.*, the initial filing of the tax returns). The insurer also argued that the "known loss doctrine" precluded coverage under the policy because the attorney was aware of the facts that gave rise to the underlying claim at the time he submitted his application for insurance.

The executrix responded that the attorney committed malpractice after the retroactive date by acting as "an

obstacle" to the payment of fines and penalties and giving false assurances that he would "take care of" delinquency notices received from the Internal Revenue Service. She also argued that the attorney was not aware of the fact that he had committed malpractice at the time he submitted the policy application.

On cross motions for summary judgment, the court first examined the language of the retroactive date exclusion, noting that the phrase "arising out of" must be read expansively. With this standard in mind, the court indicated that the plaintiff had, "at most, alleged a 'continuous scheme' which began before the policy went into effect and continued uninterrupted." The court then rejected the argument that the attorney's post-retroactive date conduct regarding the fines and penalties gave rise to a covered claim, holding that "[t]he fact that a scheme continued into the policy period does not alter the fact that the injuries 'arose out of' events which predated coverage."

While the court found the retroactive date issue dispositive, it nonetheless addressed the insurer's "known loss" arguments. According to the court, that argument would not have prevailed at summary judgment, as there were questions of fact about the date on which the attorney realized he had committed malpractice. However, this issue was moot given the insurer's successful summary judgment argument regarding the policy's retroactive date.