

"Business Enterprise" Exclusion Bars Coverage for Suit Against Law Firm

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Applying Virginia law, a federal court has held that an insurer had no duty to defend a law firm and one of its partners in a suit brought by a group of investors who were shareholders in a technology company because the firm's professional liability policy excluded coverage for claims arising out of a "business enterprise." *Minn. Lawyers Mut. Ins. Co. v. Antonelli, Terry, Stout & Kraus*, 2010 WL 4853300 (E.D. Va. N ov. 18, 2010).

The company, which had developed patents for wireless messaging technology, initially retained the law firm to provide patent prosecution services. The partner became an investor in the company and gradually became involved in advising the company and its other investors on business decisions. When the technology company faced financial difficulties and declared bankruptcy, the partner convinced the other investors to assign their rights to the company's patents to a patent holding company partly owned by the partner to avoid the technology company's creditors. After the holding company won a large settlement for infringement of one of the patents, the investors sued the partner and the law firm, alleging that the partner had defrauded the investors by stealing the patents. The firm requested that its insurer defend the suit, and the insurer denied coverage.

In the coverage litigation that followed, the insurer moved for summary judgment, arguing that it had no duty to defend the underlying suit because it was not a claim "resulting from the rendering or failing to render professional services while engaged in the private practice of law." In this regard, the policy issued to the law firm defined "professional services" for which there was coverage as "legal or notary services for others, including, but not limited to services as administrator, conservator or guardian; executor or personal representative; trustee, escrow agent [or] title insurance agent." The insurer contended that the partner was not providing professional services to the investors because he was their business associate. The court rejected this argument, pointing out that the investors' complaint repeatedly alleged that the partner had provided legal advice to them about how to protect the technology company's patents from its creditors. According to the court, the partner's actions therefore qualified as "professional services" within the scope of the policy.

Nonetheless, the court concluded that the insurer had no duty defend because coverage was barred by the policy's "business enterprise" exclusion. The exclusion applied to "any claim arising out of professional services rendered by any insured in connection with any business enterprise: (a) owned in whole or in part;

(b) controlled directly or indirectly; or (c) managed, by any insured, and where the claimed damages resulted from conflicts of interest with the interest of any client or former client or with the interest of any person claiming an interest in the same or related business enterprise." According to the court, there were four conditions to trigger the exclusion, each of which was met here. First, the underlying suit was a claim that arose out of the partner's provision of legal services to the investors. Second, the partner had rendered those legal services "in connection with" several "business enterprises," which included the partner's advice to the investors to protect the technology company's patents from creditors. Third, the court noted that the partner and a co-partner at the firm both had an "ownership" interest in a secured creditor of the technology company, and the partner also had an "ownership," "control," or "management" interest in the patent holding company. Finally, the court determined that the investors' damages arose out of a conflict of interest between the partner and the investors, who claimed an interest in the business enterprise that consisted of the scheme to keep the patents out of the hands of creditors.