

No Duty to Defend Where Insured's Actions Clearly Fell Within Business Enterprise Exclusion

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The Intermediate Court of Appeals of Hawaii has held that a professional liability insurer did not owe a duty to defend a real estate broker because the insured's alleged acts and omissions clearly fell within the policy's business enterprise exclusion. *Keown v. Tudor Ins. Co.*, 2012 WL 6552918 (Haw. Ct. App. Dec. 13, 2012).

The insured real estate broker was one of several unpaid directors at a local school. The school operated on land it subleased from another non-profit entity that also supervised a Buddhist temple on the same property. An opportunity arose to purchase the land, and the school and non-profit entity agreed to purchase it jointly. The insured broker handled many of the details of the arrangement, including drafting the sale agreement. The parties agreed to close the sale, even though they were unable to reach an agreement on the co-tenancy structure of the property, and the deed conveyed an undivided one-half interest each to the school and the non-profit entity. Without telling his clients, the broker also recorded a mortgage for himself as mortgagee on the school's interest to secure a loan he had made to the school to finance the purchase.

After the sale, the non-profit entity filed suit against the school and the broker, seeking a partition of the property and making a claim against the broker for negligence. The complaint alleged, among other things, that the broker had breached his duty of care by causing a dispute over the division of the property and by recording his mortgage without disclosure. The broker tendered the complaint to his professional liability insurer, but the insurer denied coverage based on several provisions in the policy, including the business enterprise exclusion. The exclusion barred coverage for "actions against the Insured arising out of or connected with the performance or failure to perform services for any person or entity . . . controlled by" an Insured, "in which any Insured is a director," or "which is affiliated with any Insured through common ownership, control, or financial interest."

The broker retained counsel to defend the litigation, which was eventually settled. The broker then filed suit for declaratory relief against the insurer, seeking coverage for defense and indemnity costs incurred in the negligence action. The trial court granted summary judgment in favor of the insurer, and the broker appealed.

The Intermediate Court of Appeals affirmed, noting that, although insurers have a broad duty to defend under liability policies, the terms of policy exclusions should be interpreted according to their plain, ordinary meaning. The court found that the policy's business enterprise exclusion was broadly worded, and that the broker's actions clearly fell within the exclusion because the broker had acted on behalf of both the school and the non-profit entity in the real estate transaction while also serving as a director on the school's board. Thus, the subsequent lawsuit was an action "connected with" or "arising out of" services the broker performed for an entity for which he served as a director. The court also noted that the fact that the broker received no compensation for his services further suggested that he was acting as an interested director in the transaction and not merely as a broker.

In addition, the court held that the broker's actions fell under a separate clause of the business enterprise exclusion, which precluded coverage for actions arising out of services performed for an entity with which the insured shared a financial interest. By securing his loan to the school with a mortgage on the school's interest in the property, the broker and the school had obtained a common financial interest. The court found that this common financial interest was closely connected to the underlying action because the non-profit entity's complaint was based in part on the broker's failure to disclose his mortgage. The court rejected the broker's argument that giving effect to the policy's exclusionary clauses was contrary to the reasonable expectations of a layperson. The court reasoned that the broker should have known that his professional insurance would not cover a lawsuit arising out of his personal business activities.