

Prior Knowledge Exclusion Precludes Coverage for Accountant's Professional Liability

June 2005

The United States District Court for the District of Maryland, applying Maryland law, has held that the prior knowledge exclusion in a professional liability policy precluded coverage for a claim for professional malpractice where the insured accountant became aware of allegations that could have formed the basis of the claim prior to the effective date of the claims-made policy. *Westport Ins. Corp. v. Albert*, 2005 WL 1308534 (D. Md. May 31, 2005).

The insurer issued two claims-made professional liability policies to an accounting firm, one for 2001 and one for 2002. The 2002 policy contained a prior knowledge exclusion that provided that the policy would not apply to "any 'claim' . . . resulting from . . . 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.'"

In 1996, a woman executed a will naming a member of the accounting firm as the "personal representative" of her estate. In November 2001, after the woman's death, the primary beneficiary of the will filed a probate action against the accountant seeking to remove the accountant as "personal representative." The petition for removal in the probate action alleged that the accountant was a "malfeasant" who mismanaged estate property, provided inadequate accounting statements and breached his fiduciary duties by failing to distribute funds as required by the will. In January 2002, the beneficiary filed a malpractice action against the accountant and the firm containing similar allegations. The insurer filed this action seeking a declaration that neither policy provided coverage for either the probate or malpractice action. The insureds did not dispute the insurer's assertion that neither policy provided coverage for the probate action and that there was no coverage for the malpractice action under the 2001 policy. The only issue before the court was thus whether the 2002 policy's prior knowledge exclusion barred coverage for the malpractice action.

With respect to that issue, the district court held that the exclusion applied. The court first determined that the "act, error, omission, circumstance, or 'personal injury'" giving rise to the malpractice action occurred prior to the inception date of the 2002 policy. According to the court, the same acts giving rise to the malpractice action also gave rise to the probate action, and those acts occurred prior to November 29, 2001, when the

probate action was filed.

The court next addressed whether, after reviewing the allegations contained in the complaint for the probate action in November 2001, a reasonable person would have foreseen that those allegations "might be the basis of a 'claim.'" According to the court, "Maryland courts have applied an objective standard to prior knowledge exclusions . . . when determining whether an insured had knowledge of a potential claim." In applying this objective standard, the court concluded that "no person who received the allegations set forth in [two petitions in the probate action] . . . could plausibly contend that he did not have a reasonable basis to foresee a claim against him on the basis of the contents of those pleadings."

The court rejected the insureds' argument that "reasonableness" was a fact that could not be disposed of at the summary judgment stage, concluding instead that these facts presented reasonable foreseeability as a matter of law. The court also rejected the insureds' assertion that the probate action could not serve to place the accountant on notice of a possible future claim for damages because it was not a claim for damages itself. In rejecting this second assertion, the court stated that while the probate action may not have given the accountant "knowledge" that an action for damages was forthcoming, it nonetheless provided him with enough information to reasonably conclude that an action for damages might be filed.

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