

# Reasonable Person Standard Is Appropriate to Assess Prior Knowledge

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The United States District Court for the Western District of Missouri, applying Missouri law, has granted an insurer's motion for summary judgment, ruling that the prior knowledge provision of the policy excluded coverage. *First Bancshares, Inc. v. St. Paul Mercury Ins. Co.*, 2011 WL 4352551 (W.D. Mo. Sep. 16, 2011). The court determined that the reasonable person standard, not the insured's subjective intent, should apply in assessing prior knowledge.

The insured purchased an insurance policy from its insurer for the period covering July 1, 2007 to July 10, 2010. A subsidiary of the insured was also named as an insured under the policy. The policy afforded coverage against any claims of an "Employment Practices Act," which included claims for wrongful discharge of a former employee. However, the policy contained a provision that provided that such coverage did not extend to "any claim arising from any such fact, circumstance or situation to the extent the claim is against an Insured who knew of such fact, circumstance or situation prior to the issuance of the proposed policy" (the Prior Knowledge Provision).

On April 12, 2007, an employee was terminated by the subsidiary. On April 29, 2007, the employee filed an application for unemployment benefits with the Missouri Division of Employment Security (the Division), which she ultimately lost. On October 14, 2009, the employee filed suit against the insureds for wrongful termination. Subsequently, the insureds sought coverage under the policy, and the carrier denied coverage based on the Prior Knowledge Provision. The insured then filed a coverage action.

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The insurer moved for summary judgment based on the Prior Knowledge Provision, asserting that the proceedings before the Division in which the employee applied for unemployment benefits gave rise to prior knowledge because in the initial application and on appeal the employee claimed she was retaliated against for being a “whistleblower.” In considering the insurer’s argument, the court agreed with the carrier that determination of whether the Prior Knowledge Provision applied was a two step process. The first question is whether the insureds knew of facts, circumstances, or situations that could reasonably give rise to a claim. The second inquiry is whether the employee’s state suit against the insureds arose from facts, circumstances or situations known to the insureds. With respect to the first question, the court noted that “arising out of” is construed broadly under Missouri law and that the insured did not dispute that the claimant’s suit arose out of a proceeding of which the insured was aware. Thus, the issue was whether the insured should have reasonably believed the underlying application for employment benefits would give rise to a claim.

In that regard, the insurer contended that a reasonable person standard should control the determination whether the proceedings before the Division implicated the Prior Knowledge Provision. The insureds argued that the proceedings were resolved in their favor and that the employee never gave any indication of any threat of a lawsuit. However, the court determined that Missouri law supported the insurer’s contention, and found that the facts in the record demonstrated that the facts, circumstances or situations surrounding the proceedings in the Division would have lead a reasonable person to anticipate a claim. Accordingly, the court granted the insurer’s summary judgment motion.