

Client Alert

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Mere Possibility That Claim is Based on Negligence is Enough to Avoid Liability Policy's 'Contract' Exclusion

A Connecticut appellate court held recently that a contract exclusion in a public entity errors and omissions liability insurance policy did not relieve the insurer's duty to defend when there was at least a possibility of coverage based on the allegations against the insured. The court reasoned that the fact finder could determine that the underlying negligent misrepresentation claim may not have arisen out of contract, thereby putting the claim beyond the scope of the policy's contract exclusion.

Background

In 2005, the insured—the town of Monroe (Monroe)—purchased a “Public Entity Errors and Omissions Liability Policy” (the E&O Policy) from insurer Discover Property and Casualty Insurance Company (Discover). A year later, Bellsite Development, LLC (Bellsite) brought an action alleging that Monroe had agreed to help develop and manage a wireless telecommunications tower but then abandoned the agreement. The complaint alleged claims of breach of contract, promissory estoppel, and negligent misrepresentation.

Monroe tendered the claim to Discover and requested a defense and indemnity, but the insurer denied coverage, forcing Monroe to retain counsel. The jury awarded Bellsite a \$700,000 verdict. Monroe appealed the verdict, and the appellate court reversed, directing judgment in favor of Monroe on all counts.

In 2015, Monroe brought a coverage action seeking a declaratory judgment that Discover had a duty to defend the underlying action and asserting damages arising from Discover's alleged breach of duty. Monroe moved for summary judgment on its coverage claims. Discover cross-moved, alleging that Monroe could not prevail as a matter of law because the E&O Policy specifically excluded coverage for contractual claims. The court granted Discover's motion, reasoning that the allegation in the underlying complaint amounted to a finding of a procurement contract, and the negligent misrepresentation claim arose from that contract. The court concluded, therefore, that because the contractual exclusion clause barred coverage for contract-based claims and damages, Discover did not have a duty to defend. Monroe appealed.

The Court's Decision

The appellate court's decision turned on a finding that the underlying negligent misrepresentation claim was separate and distinct from the contractual claim. Central to the court's analysis was whether coverage for the negligent misrepresentation claim was negated by the E&O Policy's contractual exclusion. The court determined that a contract could be found to exist, with the alleged negligent misrepresentation arising out of that contract. But, the court also determined that there was a possibility that the negligent misrepresentation could exist independent of any contract. Consequently, even though the phrase “arose out of” was to be construed broadly, a possibility nevertheless existed that the negligent misrepresentation did not arise out of the contract and, thus, it would not be negated by the E&O Policy's contract exclusion.

Insurance Implications

The *Town of Monroe* decision serves as a reminder that policy provisions that work to limit or preclude coverage will be construed narrowly and in favor of the policyholder. As the decision demonstrates, this principle applies even when the limiting language contains words or phrases that typically are afforded expansive constructions. For that reason, among others, policyholders should give careful consideration to every claim alleged against them to determine whether any of the claims create a possibility of coverage. The case cite is *Town of Monroe v. Discover Prop. & Cas. Ins. Co.*, No. AC 38332, 2016 Conn. App. LEXIS 443 (Conn. App. Ct. Dec. 1, 2016).

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