

Eastern District of Kentucky
FILED

OCT 29 2003

AT LEXINGTON
LESLIE G WHITMER
CLERK U S DISTRICT COURT

UNITED STATE DISTRICT COURT
EASTERN DISTRICT OF KENTUCKY
FRANKFORT

CIVIL ACTION NO. 97-18-JMH

NORTHFIELD INSURANCE COMPANY, et al.,

PLAINTIFFS,

v.

JUDGMENT

FRANKLIN COUNTY, KENTUCKY, et al.,

DEFENDANTS.

* * * * *

In accordance with the Order of even date and entered contemporaneously herewith,

IT IS HEREBY ORDERED:

(1) that there exists no obligation on the part of KALF under the KALF policies to provide any indemnification for the claims made in *Jennifer Vest, et al., v. Franklin County, et al.*, Case No. 94-CI-01870, in the Scott Circuit Court;

(2) that there exists no obligation on the part of Northfield Insurance Company under policy number AA101077 and Certain Underwriters at Lloyd's, London, under policy number G512135 to provide indemnification for or against the claims made in *Jennifer Vest, et al., v. Franklin County, et al.*, Case No. 94-CI-01870, in the Scott Circuit Court;

(3) That this action be, and the same hereby is, **DISMISSED AND STRICKEN FROM THE ACTIVE DOCKET;**

(4) That all pending motions be, and the same hereby are, **DENIED AS MOOT;** and

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10/31/03

(5) That all scheduled proceedings be, and the same hereby are, CONTINUED GENERALLY.

This is the 29th day of October, 2003.

Joseph M. Hood
JOSEPH M. HOOD, JUDGE

Date of Entry and Service:

NOTICE IS HEREBY GIVEN OF THE
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ON 10-30-03
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UNITED STATE DISTRICT COURT
EASTERN DISTRICT OF KENTUCKY
FRANKFORT

OCT 29 2003

AT LEXINGTON
LESLIE G WHITMER
CLERK U S DISTRICT COURT

CIVIL ACTION NO. 97-18-JMH

NORTHFIELD INSURANCE COMPANY, *et al.*, PLAINTIFFS,

v. MEMORANDUM OPINION AND ORDER

FRANKLIN COUNTY, KENTUCKY, *et al.*, DEFENDANTS.

* * * * *

This action is before the Court on several motions, including Plaintiffs' motion for summary judgment [Record No. 113]. Defendant Franklin County, Kentucky ("Franklin County") has also filed a motion for summary judgment against Defendant Kentucky Association of Counties All Lines Fund ("KALF") [Record No. 119] and for partial summary judgment against Plaintiffs [Record No. 144]. Finally, Defendant KALF has filed their own motion for summary judgment [Record No. 121]. Arguments were heard on these motions on August 11, 2003. The Court being sufficiently advised, these matters are ripe for decision.

I. FACTUAL BACKGROUND

This case is an insurance contract dispute between several insurance companies, namely Plaintiffs Northfield Insurance Company ("Northfield") and Certain Underwriters at Lloyds of London ("Lloyds") and Defendant Kentucky Association of Counties All Lines Fund ("KALF"), and Defendant Franklin

County, Kentucky.¹

A. UNDERLYING FACTUAL SCENARIO AND CLAIMS

Sometime beginning in or about 1987 and continuing until at least August, 1994, Hunter Hay, the County Jailer for Franklin County, Kentucky (hereinafter "County Jailer"), began raping, sodomizing and otherwise physically and mentally abusing female jail employees under his supervision. During the latter portion of this same period, the County Jailer also wrongfully demoted a male jail employee who refused to let the Jailer sleep with his wife and fired two male jail employees who participated in a Kentucky State Police investigation of his conduct at the jail.

Franklin County, through its executive officials, knew that the County Jailer was engaging in conduct in violation of the Kentucky Civil Rights Act ("KARA") throughout most of this same period. Specifically, as early as 1989, female jail employees complained to Robert Arnold, Franklin County Judge Executive (the County's Chief Executive Officer) about the County Jailer's sexual misconduct against them. By 1994, at least four and perhaps as many as twelve female jail employees

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Defendant KALF is a corporation created pursuant to the Kentucky Interlocal Corporation Act, KRS 165.120, and provides liability insurance for counties and other political subdivisions of the state of Kentucky, as well as certain agents and employees thereof.

had complained to Judge Executive Arnold about sexual harassment by the County Jailer. County Judge Executive Arnold, however, neither initiated an investigation into these allegations nor took any other action against the County Jailer until July 1994, when jail employees confronted him and threatened to report the Jailer's conduct directly to the Kentucky State Police. County Judge Executive Arnold then agreed to assist certain of the employees in contacting the State Police, who initiated a substantial investigation into the Jailer's conduct, including but not limited to the Underlying Claimants' allegations of pervasive sexual abuse at the jail. As a result of this investigation and the Underlying Claimants' testimony before a grand jury and at trial, the Commonwealth of Kentucky indicted, convicted and sentenced the County Jailer on more than 15 criminal counts, including rape, sodomy, attempted rape, sexual assault and violations of the Kentucky Whistleblowers Act ("KWA").

On December 15, 1994, nine employees or former employees of the Franklin County Correctional Facility (the "Vest plaintiffs") filed a civil action in Franklin County Circuit Court against Franklin County, former Franklin County Jailer Hunter Hay, and Franklin County Judge/Executive Robert Arnold, styled as *Jennifer Vest, et al., v. Franklin County, et al.*, Case No. 94-CI-01870. In the *Vest* action, the plaintiffs

alleged that Hay, while acting as Franklin County Jailer, committed acts of sexual harassment and retaliated against certain of the plaintiffs for their attempts to oppose Hay's conduct. Those plaintiffs alleged that defendant Franklin County was liable in damages under the KCRA and the KWA because County officials failed to take adequate steps to prevent or stop harassment and retaliation by Hay.

Defendant Franklin County requested that KALF defend the County, Arnold, and Hay in that matter and indemnify them for any ensuing liability. KALF provided a defense to Franklin County, Arnold and Hay under a reservation of rights. KALF then notified Northfield and Certain Underwriters that it expected them to indemnify KALF if it was required to indemnify Franklin County. Franklin County eventually paid settlements totaling \$537,961.57 to four of the nine Vest plaintiffs through Offers of Judgment. Jim Boyd, Franklin County Attorney, has stated that the County fully informed KALF of the County's intent to make the settlement offers.

On July 11, 1997, the trial court found Franklin County liable as a matter of law for the County Jailer's sexually harassing and retaliatory conduct and granted the Underlying Claimants motion for summary judgment on quid pro quo and hostile work environment claims. As a necessary predicate to finding the County liable on the hostile work environment

claims, the trial court concluded that the County's discovery and deposition testimony established beyond dispute that County officials had direct knowledge of the Jailer's prohibited conduct and failed to timely take action to stop it. The trial court therefore ruled as a matter of law that the County was deemed to have authorized the Jailer's conduct and thus rendered such conduct within the scope of his duties on behalf of the County for purposes of the KARA. On October 3, 1997, a jury returned a verdict against Franklin County totaling \$5,077,178, of which \$4,999,286 was awarded to four female plaintiffs on their sexual harassment, retaliation and constructive discharge claims. With regard to the male employee's claims, the jury awarded him \$8,892 in lost wages and further found that the County violated the KWA in an "oppressive, malicious or fraudulent" manner and thus awarded him punitive damages in the amount of \$75,000.

B. KALF Insurance Policies

Franklin County is a member of the Kentucky Association of Counties ("KACO"), a nonprofit corporation formed in 1974 to represent individual County members' collective interests before the Kentucky Legislature and in other endeavors. In 1987, KACO expanded its services to its member Counties to offer a self-insurance program sponsored and administered by KACO to help meet the needs of its member Counties in an

otherwise difficult insurance market. To that end, KACO founded KALF through a bond issuance and required member Counties to execute a program administration agreement that set forth the parties' respective rights and responsibilities under this self-insurance program. KALF issued Kentucky Association of Counties All Lines Fund Coverage Agreement No. 0045 to Franklin County for successive periods from July 1, 1988 to July 1, 1996. Both Franklin County and KALF treated the KALF Policies as the operative insurance agreement between KALF and Franklin County for the entire period between July 1, 1988 and July 1, 1996.

There are seven KALF policies at issue in this case, each described as "Coverage Agreement 0045." The KALF policies were issued for the following policy periods: July 1, 1989, to June 30, 1990 (hereinafter, the "89/90 Policy"); July 1, 1990, to June 30, 1991 (hereinafter, the "90/91 Policy"); July 1, 1991 to June 30, 1992 (hereinafter, the "91/92 Policy"); July 1, 1992, to June 30, 1993 (hereinafter, the "92/93 Policy"); July 1, 1993, to June 30, 1994 (hereinafter, the "93/94 Policy"); July 1, 1994, to June 30, 1995 (hereinafter, the "94/95 Policy"); and July 1, 1995, to June 30, 1996 (hereinafter, the "95/96 Policy"). The relevant provisions of those policies are discussed below.

1. General Coverage Provisions

The policies in effect for the periods from July 1, 1989 through June 30, 1992 contain the following general provision regarding coverage:

- A. KALF will pay on behalf of the member all sums which the member shall become legally obligated to pay as damages because of the commitment of a tort during the Coverages Period shown on Page 1 of this Coverage Agreement by the member or its employee or agent, except as excluded hereinafter, and up to the limits of liability stated herein.

The protection provided the member under this Coverage A shall be extended to apply to any employee of the member so long as the employee was acting within the scope of his or her duties as such at the time of the commitment of the alleged tort.

...

- C. KALF shall pay on behalf of any employee for claims brought against such individuals for torts committed by such persons or for alleged violations of such person's fiduciary duties in their public official capacity during the Coverage Period...except as restricted hereinafter.

[89/90 Policy, Article II at 2-3, JA 0001-0027; 90/91 Policy, Article II at 2-3, JA 0028-0056; 91/92 Policy, Article II at 2-4, JA 0057-87]. Article II, Section D provides that KALF has the right and duty to investigate claims and to defend suits seeking damages for claims against those covered by the

policy. *Id.* However, Section D also provides that where intentional torts are alleged, KALF has only the duty to defend the claim or suit but no liability for judgments resulting from intentional torts. *Id.*

The policies in effect for the periods from July 1, 1992 through July 1, 1995 contain the following general provision regarding coverage:

- A. KALF, at its election, will pay either as reimbursement to the member or on behalf of the member all sums which the member shall become legally obligated to pay as damages because of the commitment of a tort during the Coverage Period shown on Page 1 of this Coverage Agreement by the member or its employee except as excluded hereinafter, and up to the limits of liability stated herein.

The protection provided the member under this Coverage A shall be extended to apply to any employee of the member so long as the employee was acting within the scope of his or her duties as such at the time of the commitment of the alleged tort....

- C. KALF shall pay on behalf of any employee for claims brought against such individuals for torts committed by such persons or for alleged violations of such person's fiduciary duties in their public official capacity during the Coverage Period...except as restricted hereinafter.
- D. KALF shall have the right and duty to investigate any claim and to

defend any suit seeking damages for such claim against a member, or any other person to whom KALF has assumed a duty under Sections A and C of this Article, even if any of the allegations of the suit are groundless, false or fraudulent, and shall make such investigation and settlement of any claim or suit as it deems expedient. In the event the claim included allegations of an intentional tort, KALF shall still have the duty to defend such claim or suit but shall not be liable for that portion of any judgment [sic] due to the claim having been found to be the result of an intentional tort. KALF has no obligation to pay any punitive damages assessed on account of a member's or an employee's intentional acts or act expected to cause injury or damage or punitive damages assessed due to deliberate indifference or gross negligence of the member or its employee.

[92/93 Policy, Article II at 3-4, JA 0088-0106; 93/94 Policy, Article II at 5-7, JA at 107-0141; 94/95 Policy, Article II at 5-7, JA 0142-0174.]

2. Exclusions

The policies in effect for the periods from July 1, 1989 through June 30, 1992 contain the following coverage exclusions:

A. Under the coverage provided under Article II, Sections A, C & D does not apply:

1. To a claim arising out of the willful violation of a penal

statute or ordinance committed by or with the knowledge or consent of the member;

2. To a claim resulting from an intentional tort or act intended to cause injury or damages;...

B. Under the coverage provided under Article II, Section C, coverage does not apply if the person(s) against whom the claim is made was not acting in good faith and within the scope of his or her official functions and duties when the alleged tort or violation of fiduciary duty was caused by the willful or wanton misconduct of such person(s) or was an intentional tort.

[89/90 Policy, Article V at 5, JA at 0001-0027; 90/91 Policy, Article V at 5-6, JA 0028-0056; 91/92 Policy, Article V at 5-6, JA 0057-87.]

The policies in effect from July 1, 1992 through July 1, 1995, provide that:

- A. Coverage under this Agreement does not apply to:
 1. To a claim arising out of the willful or intentional violation of a statute, ordinance or constitutional provision;
 2. To a claim resulting from an intentional tort or an act intended to cause injury or damages;...

Under the coverage provided under Article II coverage does not apply if the

person(s) against whom the claim is made was not acting in good faith and within the scope of his or her official functions and duties when the alleged tort or violation of fiduciary duty was caused by the willful or wanton misconduct of such person(s) or was an intentional tort.

[92/93 Policy, Article V at 6, JA at 0088-0106; 93/94 Policy, Article V at 9, JA at 0107-0141; 94/95 Policy, Article V at 9, JA at 0142-0174.]

3. Definition of Intentional Tort

Within the 89/90, 90/91, and 91/92 policies, an intentional tort is defined follows:

A tort which was committed with knowledge that committing the act was wrong or knowingly failing to correct a wrongful act after its discovery.

[89/90, 90/91 and 91/92 Policies at 1, Article I, JA at 0003, 0031 & 0060].

Within the 92/93, 93/94, and 94/95 policies, an intentional tort is defined as follows:

E. Intentional tort means a tort which was committed with knowledge that committing the act was wrong or expected to produce a wrongful act or knowingly failing to correct a wrongful act after discovery. Intentional tort additionally means any action or inaction by the member or its employees in violation of any ordinance, regulation, statute or constitutional provision. Intentional tort shall also include...any action taken by a member or a member's employee in

violation of a party's constitutional or civil rights or in a retaliation for a person or persons exercising their constitutional rights to free speech or association.

[92/93 Policy at 1, Article I, JA at 0088-0106; 93/94 Policy at 3, Article I, JA at 0107; 94/95 Policy at 3, Article I, JA 0142-0174.]

An intentional tort is defined by the policy as:

...a tort which was committed with knowledge that committing the act was wrong or knowingly failing to correct a wrongful act after its discovery.

[89/90 Policy, Article I at 1, JA at 0001-0027; 90/91 Policy, Article I at 1, JA at 0028-0056; 91/92 Policy, Article I at 1, JA 0057-87.]

4. FURTHER TERMS AND CONDITIONS OF COVERAGE

The KALF policies also impose certain obligations on its members with regard to admissions of liability, assumption of obligations, and payments, as follow:

The following additional terms and conditions shall apply to this Coverage Agreement:

...

D. If a claim is brought against the member the member shall:

...

3.	Neither	admit	any
	liability,	make	any
	payment,	assume	any

obligation, nor incur any expense related to such claim or suit, except with the prior written consent of KALF;

...

5. Neither voluntarily make any payment, assume any obligation nor incur any expense, other than for first aid to others at the time of the accident, except at its own cost.

E. No action shall lie against KALF unless, as a condition precedent thereto, there shall have been full compliance with all of the terms of this Coverage Agreement....

[89/90 Policy, Article VI at 8-9; JA 0001-0027; 90/91 Policy, Article VI at 8-9, JA 0028-0056; 91/92 Policy, Article VI at 5-6, JA 0057-0087; 92/93 Policy, Article VI at 9-10, JA 0088-0106; 93/94 Policy, Article VI at 13, JA 0107-0141; 94/95 Policy, Article VI at 12-14, JA 0142-0174.]

C. EXCESS LIABILITY INSURANCE POLICIES

KALF in turn obtained coverage from Plaintiffs for certain of its potential liabilities to its member counties, including Franklin County. Plaintiffs collectively issued six excess liability insurance policies providing Public Entity All Lines Aggregate Insurance to KALF for the benefit of its members, including Franklin County, for the period June 30, 1988 through June 30, 1995. Plaintiff Underwriters subscribed

in several and proportional share to provide a specific percentage of the limits of the certain insurance policies to the tune of 75-100%. Plaintiff Northfield subscribed in several and proportional share to provide a specific percentage of the limits of the certain insurance policies ranging from 25-100%.

Plaintiffs' Policies provide excess Comprehensive General Liability coverage with a \$1 million dollar limit per occurrence and in the aggregate and excess Public Officials Errors and Omissions liability coverage subject to a \$1 million limit per occurrence and per member aggregate. For each policy period, KALF/Franklin County is liable for the first \$250,000 per occurrence or per claim. As a result, Plaintiffs' Policies actually provide a percentage of \$750,000 in limits over the KALF/Franklin County self-insured retention of \$250,000. Because Plaintiffs' Policies potentially respond to claims asserted by all participating members of the KALF pooling arrangement, the Plaintiffs' Policies identify KALF as the nominal Assured and identify by endorsement the individual county members for whose benefit the Plaintiffs' Policies apply. The terms and conditions of Plaintiffs' Policies thus apply to the conduct of the participating KALF members such as Franklin County, as KALF has no employees, owns no property and otherwise has no insurable interests. Plaintiff

Northfield also issued separate excess policies to apply over and above the limits of the Plaintiffs' Policies to KALF for the benefit of certain of its members (including Franklin County). The Northfield Excess Policies expressly incorporate by reference the terms and conditions of the Plaintiffs' Policies to which they are excess and from which they follow.

1. ERRORS AND OMISSIONS POLICIES

With regard to coverage under the errors and omissions policies, it is provided as follows:

If during the Policy Period, any Claim is first made against the Assured for a wrongful Act, Underwriters [and Northfield] will indemnify the Assured, for all Loss incurred by the Assured by reason of any Wrongful Act as hereinafter denied.

[JA at 1365, 1421, 1491.]

The definition of "wrongful act" is:

...any actual or alleged error or misstatement, omission, acts of neglect or breach of duty including misfeasance, malfeasance, and nonfeasance by the Assured. "Wrongful Act" includes actual or alleged violations of the United States Constitution or any State constitution, or any law affording protection for civil rights, provided coverage is otherwise afforded hereunder for such Wrongful Act.

[Id.]

Section IV, Errors and Omissions Exclusion B provides that Plaintiffs have no duty to indemnify any claim "brought

about or contributed to by fraud, dishonesty or criminal act of any Assured." [JA at 1366; 1422; 1492.] An "Assured" is defined as:

...the Named Assured but also: any official, trustee, Director, Officer, Partner, Volunteer or employee of the Named Assured while acting within the scope of his duties as such.

[JA at 1359; 1406; 1474.]

Further, Exclusion I bars coverage for any claim for "bodily injury or property damage," i.e., "physical injury to any person (including death) and any mental anguish or mental suffering associated with or arising from such physical injury." [JA at 1421; 1491.]

2. COMPREHENSIVE GENERAL LIABILITY COVERAGE

The comprehensive general liability section provides as follows:

Underwriters hereby agree, subject to the limitations, terms and conditions hereunder mentioned, to indemnify the Assured for all sums which the Assured shall be obligated to pay by reason of the liability imposed upon the Assured by law or assumed by the Assured under contract or agreement, for damage direct or consequential, and expenses...on account of personal injuries...suffered or alleged to have been suffered by an person or persons (excepting employees of the Assured injured in the course of their employment)..."

[JA at 1414, 1482.] Assured is defined as the "Named Assured but also: any official, trustee, Director, Officer, Partner,

Volunteer or employee of the Named Assured while acting within the scope of his duties as such." [JA at 1359, 1406, 1474.]

Exclusion (k) to Section II states that the policies do not apply "to any claim arising out of discrimination related to employment or wrongful termination of any person." [JA at 1417, 1486.] Exclusion (j) to Section II of each of Plaintiff's policies states that coverage does not apply to "any claim resulting from the sexual or physical abuse or molestation of any person by the Assured or any...employee of the Assured." [JA at 1417, 1486.]

D. Procedural History of this Matter

On March 24, 1997, Plaintiff Northfield filed this declaratory judgment action requesting that the Court declare that Northfield has no duty to indemnify KALF under Northfield Policy No. 101077 (policy period from June 30, 1992, to June 30, 1995) with respect to any liability which Franklin County incurred arising out of the Vest action. On September 30, 1997, plaintiffs Northfield and Certain Underwriters filed their first amended complaint for declaratory relief seeking the same relief sought in Northfield's original complaint, but adding Certain Underwriters as a plaintiff and seeking a declaration of noncoverage under an additional Certain Underwriters Policy G512135 (Policy period June 30, 1992, to June 30, 1995).

On December 26, 1997, Defendant KALF filed an answer to plaintiffs' first amended complaint, which included a counterclaim against Northfield and Certain Underwriters and a crossclaim against co-defendant Franklin County. In its crossclaim, KALF requests that the Court either declare that KALF has no duty under one of its Coverage Agreement 0045 policies (Policy Period July 1, 1994, to July 1, 1995) to indemnify Franklin County for liability it incurred in the Vest action or that if the County is entitled to coverage under KALF's policy, that KALF's coverage obligation is limited to \$250,000.00 with plaintiffs Northfield/Certain Underwriters liable for the County's liability in excess of that amount.

The Court subsequently granted leave for defendant Franklin County to amend its answer and counterclaim. In that amended paper, Franklin County requests that the Court declare the parties' rights under additional insurance policies that Northfield and Certain Underwriters issued to KALF and that KALF issued to Franklin County during the years 1989 through 1996.

II. APPLICABLE STANDARD OF REVIEW

Under Fed. R. Civ. P. 56(c), summary judgment is appropriate "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the

affidavits, if any, show that there is no issue as to any material fact, and that the moving party is entitled to judgment as a matter of law." The moving party may discharge its burden by showing "that there is an absence of evidence to support the nonmoving party's case." *Celotex Corp. v. Catrett*, 477 U.S. 317, 325 (1986). The nonmoving party, which in this case is the plaintiff, "cannot rest on [her] pleadings," and must show the Court that "there is a genuine issue for trial." *Hall v. Tollett*, 128 F.3d 418, 422 (6th Cir. 1997). In considering a motion for summary judgment the court must construe the facts in the light most favorable to the nonmoving party. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 255 (1986).

III. DISCUSSION

A. CHOICE OF LAW

Federal courts sitting in diversity must apply the choice-of-law rules of the forum state, and this Court notes that the Kentucky Supreme Court has adopted the "most-significant-relationship" test, as set forth in THE RESTATEMENT OF CONFLICT OF LAWS 2d, to determine which state's law to apply in contract disputes. *Cole v. Miletic*, 133 F.3d 433, 437 (6th Cir. 1998); *Lewis v. American Family Ins. Group*, 555 S.W.2d 579, 581-82 (Ky. 1977); RESTATEMENT OF CONFLICT OF LAWS 2d, § 188 (1971). This test attempts to determine which state has the

most significant relationship to the transaction and the parties based on, among other things, the following criteria: (a) the place of contracting; (b) the place of negotiation; (c) the place of performance; (d) the location of the subject matter of the contract; and (e) the domicile, residence, nationality, place of incorporation and place of business of the parties. RESTATEMENT OF CONFLICT OF LAWS 2d, § 188. Even considering this test, it should be noted that the application of Kentucky law is favored by the Courts of the Commonwealth when it is the forum whenever it is justifiable. *Adam v. J.B. Hunt Transport, Inc.*, 130 F.3d 219, 231 (6th Cir. 1997).

Applying these choice-of-law principles to the instant facts establishes that Kentucky law should apply in determining the rights of the parties under the terms of the Policies. In the instant matter, the relevant policies were requested, delivered, and premiums paid within the Commonwealth of Kentucky, the subject matter of the policies (i.e., Franklin County's liabilities) located in Kentucky, and any contacts with jurisdictions other than the Commonwealth of Kentucky are, by comparison, few and not substantial. Accordingly, Kentucky law governs this Court's interpretation and application of Plaintiffs' Policies with respect to the claims at issue in this Motion.

B. INTERPRETING THE CONTRACTS

Pursuant to Kentucky law, the "terms of an insurance policy are to be given their ordinary meanings as persons with ordinary and usual understanding would construe them," and they are to be enforced as written. *Sunny Ridge Enterprises, Inc. v. Fireman's Fund Ins. Co., Inc.*, 132 F. Supp. 2d 525 (E.D. Ky. 2001); *Foster v. Kentucky Housing Corp.*, 850 F. Supp. 558, 561 (E.D. Ky. 1994); see *Peoples Bank & Trust Co. of Madison County v. Aetna Cas. & Sur. Co.*, 113 F.3d 629, 636 (6th Cir. 1996) (in the absence of an ambiguity an "[insurance] contract is to be read according to its plain meaning, its true character and purpose, and the intent of the policies"); *Masler v. State Farm Mut. Auto. Ins. Co.*, 894 S.W.2d 633, 636 (Ky. 1995) ("the terms of an insurance policy are held to be enforceable as written..."). Moreover, "[c]ourts in Kentucky are required to examine insurance policies as complete instruments to determine the extent of the coverage offered." *United States Fid. & Guar. Co. v. Star Fire Coals, Inc.*, 856 F.2d 31, 33 (6th Cir. 1988).

While ambiguities in the language of the policy will generally be construed in favor of the insured and against the drafter, the Court must give the policy a reasonable interpretation, and there is no requirement that every doubt be resolved against the insurer. *Stone v. Kentucky Farm*

Bureau Mut. Ins. Co., 34 S.W.3d 809 (Ky. App. 2000); *State Auto Mut. Ins. Co. v. Ellis*, 700 S.W.2d 801 (1985); *Wolford v. Wolford*, 662 S.W.2d 835 (Ky. 1984). Courts applying Kentucky law are also admonished as follows:

The rule of strict construction against an insurance company certainly does not mean that every doubt must be resolved against it and does not interfere with the rule that the policy must receive a reasonable interpretation consistent with the parties' object and intent or narrowly expressed in the plain meaning and/or language of the contract. Neither should a non-existent ambiguity be utilized to resolve a policy against the company. We consider that courts should not rewrite an insurance contract to enlarge the risk to the insurer.

Meyers v. Kentucky Med. Ins. Co., 982 S.W.2d 203, 208 (Ky. Ct. App. 1997) (quoting *St. Paul Fire & Marine, Ins. Co. v. Powell-Walton-Milward*, 870 S.W.2d 223, 226 (Ky. 1994)); see *Foster*, 850 F. Supp. at 561 ("every doubt will not always be construed against the insurer"). Finally, unambiguous and clearly drafted policy exclusions, which are reasonable, "are enforceable under Kentucky law." *Id.* at 210 (citation and internal quotations omitted).

1. KALF POLICIES

Defendant KALF argues that the agreement at issue was not ambiguous with regard to the nature of the coverage provided, the duty to defend, or exclusions from coverage. In

particular, KALF asserts that Exclusion A(2) of Article V of its policies unambiguously provides that its policies do not apply to "a claim resulting from an intentional tort or an act intended to cause injury or damages...[,]" as defined in the policies, and that this exclusion applies to the matter at hand. Further, KALF argues that its policies very clearly state that settlement offers were to be made only with its "prior written consent" under those Article VI provisions forbidding admissions of liability, payments, and assumptions of liability related to claims or suits with the written consent of KALF. The Court agrees.

As discussed above, the state trial court found Franklin County liable as a matter of law for the County Jailer's sexually harassing and retaliatory conduct and granted a motion for summary judgment on quid pro quo and hostile work environment claims. Necessarily, the trial court had already concluded that the County's discovery and deposition testimony established that County officials had direct knowledge of the Jailer's prohibited conduct and failed to take timely action to stop it. Franklin County's failure to act in the face of this knowledge fits neatly into the exception carved out in Article V of the policies, as "intentional torts" are variously defined in Article I as those wrongs "committed with knowledge that committing the act was wrong or knowingly

failing to correct a wrongful act after its discovery...[,]”
“action or inaction by the member or its employees in violation of any ordinance, regulation, statute or constitutional provision...[,]” or an “action taken by a member or a member’s employee in violation of a party’s constitutional or civil rights or in a retaliation for a person or persons exercising their constitutional rights to free speech or association.” This Court finds as a matter of law, founded on the conclusions of the state trial court, that Franklin County at best “knowingly failed to correct a wrongful act after its discovery” and at worst “committed [the wrong] with knowledge that...[it] was wrong...” Certainly, the trial court concluded that the actions and inactions of the member and its agents violated statutory prohibitions on harassment and the Vest plaintiff’s civil rights.

Franklin County makes the argument that even if it had knowledge that sexual harassment was occurring at the jail and it failed to take prompt and effective action to prevent such harassment, this would not mean that the County’s failure to take action (as a result of omissions of then-County Judge Execute Robert Arnold) was a “knowing” failure calculated to intentionally cause injury to the Vest plaintiffs. Defendant Franklin County opines that absent such an intent to cause injury, courts hold that an “intentional act” exclusion does

not preclude coverage for an employer's liability that is connected to wrongful acts of supervisors, citing *United States Fidelity & Guaranty Company v. Toward*, where the district court rejected an insurer's contention that there was no coverage for a school which had allegedly failed to adequately supervise teachers who had molested students. *United States Fidelity & Guaranty Company v. Toward*, 734 F. Supp. 465, 468 (S.D. Fla. 1990). The district court disagreed with the insurance company's argument that if a tortfeasor's underlying act, itself, is not covered under a policy, that there automatically can be no coverage for another insured's failure to prevent the tortfeasor's wrongful acts. However, that case is distinguishable from the present matter for it involved a situation where the underlying act itself had been addressed in a state criminal action but not a state civil action. Here, the actions, inaction, and type of liability of Franklin County has been considered and adjudicated in a state civil case.

Similarly, Franklin County's reliance on *Seminole Point Hospital Corp. v. Aetna Casualty & Surety Co.* is misplaced. *Seminole Point Hospital Corp. v. Aetna Casualty & Surety Co.*, 675 F. Supp. 44, 47 (D.N.H. 1987). In that matter, former employees of a corporation sued the company alleging that its officers engaged in sexual harassment and that the corporation

knew of the conduct but negligently failed to prevent or stop it. The insurer denied coverage on the grounds of exclusions which precluded coverage for injury intentionally caused or aggravated by the insured or for damages arising out of the discharge or discrimination against any employee in violation of law. In holding that the insurer's intentional acts exclusion did not preclude coverage for damages arising out of the corporation's negligent failure to prevent wrongful conduct by its officers, the district court rejected the insurer's position that the company's failure to adequately supervise the employees or otherwise prevent the sexual harassment necessarily precluded insurance coverage for such liability as a matter of law. Again, this Court notes that the present matter is distinguishable because "knowledge" is the linchpin of an "intentional tort" as defined by the policies. That fact of that "knowledge" has been adjudicated by the state trial court and ascribed to Franklin County takes the counties actions out of the realm of negligence as discussed in *Seminole Point Hospital*, and the issue of knowledge will not be relitigated here.²

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For similar reasons, Franklin County's reliance on *James Graham Brown Foundation, Inc. v. St. Paul Fire & Marine Insurance Company* is misplaced. *James Graham Brown Foundation, Inc. v. St. Paul Fire & Marine Insurance Company*, 814 S.W.2d 273 (Ky. 1991). In that case, the Kentucky Supreme Court ruled that a corporation which was liable for pollution

Notwithstanding that Judge Arnold has testified that he did not have a positive feeling that Hunter Hay had made sexual advances toward jail employees or had otherwise acted improperly until two jail employees met with Arnold in 1994 and agreed to pursue charges against Hay, the state trial court has already established that Franklin County had knowledge of certain wrongs and was thus party to a "knowing failure" to correct Hunter Hay's sexual harassment at the Franklin County Jail. This Court agrees with KALF that, as a result, the actions of Franklin County, by and through Arnold, fall outside of the coverage provisions. Whether or not these acts could otherwise constitute "misjudgment and simple neglect on the part of Franklin County Judge Executive Robert Arnold," as KALF contends, is no longer a viable issue at this late stage.

Additionally, with regard to Offer of Judgment settlement agreements reached with the other Vest plaintiffs, the

cleanup costs was entitled to insurance coverage even though the insurer had argued that the act of placing the pollutants in the ground was intentional and thus precluded coverage. The Court rejected the insurer's position and instead held that a policyholder who is liable for the intentional act of another is entitled to coverage unless the insured specifically intended both the act which caused the injury and the resultant injury. In the instant matter and under the relevant policies, "intention" turns on knowledge that may be ascribed to Franklin County by virtue of information received by Arnold from the victims of Hay. As described above, that knowledge has already been established.

evidence indicates that Franklin County notified KALF of its intent to enter into settlement agreements, but there is no evidence of any written consent as required by the contract. This provision is clear and unambiguous, and, notwithstanding Franklin County's arguments about the sensibility of these settlement agreements, it bars any recovery under the policies by Franklin County for amounts paid or to be paid under those agreements. The Court cannot ignore the fact that the information provided to KALF by Franklin County does not and cannot substitute for the type of consent from KALF necessary under the policy.³ In short, Franklin County may not recover from KALF under any of the policies issued.

2. EXCESS POLICIES

The Excess Policies expressly incorporate by reference the terms and conditions of the Plaintiffs' Policies to which they are excess and from which they follow. Accordingly, as the incidents and damages are excluded from coverage by KALF's policies, as described above, it is clear that Plaintiffs bear no obligation to indemnify KALF or Franklin County in this

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Franklin County also argues that, even if the County had not informed KALF, the insurer still has a duty to indemnify the County for those settlements since KALF has disclaimed any duty to provide coverage at all relevant times. Considering that the Court has determined that KALF correctly disclaimed coverage for the liability of Franklin County in this matter, this argument is now moot.

matter.

Nonetheless, the Court notes that the excess policies themselves include language that would exclude this situation from coverage. Plaintiffs argue that the scope of liability adjudicated in the Vest matter, as well as the County Jailer's criminal convictions for rape, sodomy, sexual assault and violations of the KWA establish that the Vest plaintiff's claims and injuries were "brought about and contributed to by [the] criminal act" of "an Assured" and are, thus, excluded from errors and omissions policy coverage. At the very least, argue Plaintiffs, the County Jailer was an "employee" of the Assured Franklin County and that the claims and injuries adjudicated in the state trial court against Franklin County depend from those criminal acts. Plaintiffs also argue that principles of collateral estoppel preclude any argument by Defendant Franklin County that the County Jailer was not "acting within the scope of his duties as such" and, thus, does not qualify as an "Assured" under Plaintiffs' policies. In any event, Exclusion I to Section IV expressly bars coverage for any claim for "bodily injury or property damage" and would preclude any recovery on the policies for those portions of the jury award representing the Vest plaintiffs' "mental anguish or mental injury" arising from physical injury precipitated by the unlawful and forcible sexual misconduct of

the County Jailer.

With regard to the Comprehensive General Liability coverage to Defendants under Section II of the Policies, each of the policies unambiguously states that coverage does not apply "to any claim resulting from the sexual or physical abuse or molestation of any person by the Assured or any volunteer worker or employee of the Assured." [JA at 1417; 1486.] Hay, an Assured as well as an employee of Assured Franklin County, sexually abused and/or molested each of the six female Vest plaintiffs. As the civil claims against the County Jailer and Franklin County "resulted from the sexual or physical abuse or molestation" by an Assured or an employee of an Assured as defined by Plaintiffs' Policies, this exclusion bars coverage for the amounts paid to settle the claims of the six female Vest plaintiffs.

Other exclusions provide that the policies do not apply "to any claim arising out of discrimination related to employment or wrongful termination of any person." [JA at 1417, 1486.] Each of the nine Underlying Claimants asserted that Franklin County engaged in employment discrimination against them and/or wrongfully terminated them in violation of the KCRA through the County Jailer's and County's sexual harassment and/or violation of the KWA. Accordingly, insofar as any of the settlement payments or jury award results from

or reflects damages for such claims, they, too, would be excluded from coverage.

Finally, the policies exclude coverage for claims due to "personal injury...which the Assured intended or expected or reasonably could have expected," including bodily injury, mental anguish, shock, sickness, discrimination, humiliation, and assault and battery. [JA at 1358, 1417, 1486.] No doubt, Hay intended, expected or reasonably could have expected his victims to suffer such personal injuries as a result of his conduct. More importantly, as Franklin County was adjudged directly liable for the Hay's conduct, it cannot escape the application of this exclusion by asserting that, as a political body, it did not have a subjective intent or expectation of harm with respect to the Underlying Claimants. It was determined in the Vest matter that Franklin County officials had contemporaneous knowledge that female jail employees were being subjected to some type of sexual harassment and abuse yet did not act to investigate such claims or take any appropriate action as mandated by the KCRA and its own sexual harassment policy. Accordingly, the County's failure to act was deemed to be actionable under the KCRA as if it had taken the action itself, and no part of Franklin County's settlement with some of the Vest plaintiffs that constitutes "personal injury" qualifies for coverage as

an "occurrence" under Plaintiffs' Policies because one or more of Plaintiffs' Assureds expected or intended the harm for which coverage is sought.

C. EXCLUSIONS AND DEFINITION OF INTENTIONAL TORT FOUND IN THE KALF COVERAGE AGREEMENTS ARE NEITHER ILLEGAL NOR IN VIOLATION OF KY. REV. STAT. 367.170 OR 304.12-010

In the First Amended Cross-Claim, Franklin county asserts that KALF is precluded from enforcing certain provisions of Coverage Agreement 0045, including that provision excluding coverage for claims resulting from an intentional tort or an act intended to cause injury or damage and the definition of "intentional tort" on the grounds that such provisions are illegal and violate Ky. REV. STAT. 367.170 and 304.12-010. KALF, in its motion for summary judgment, argues that the provisions are not illegal or in violation of Kentucky statute.

KY. REV. STAT. 367.170 declares any "unfair, false, misleading or deceptive acts or practices in the conduct of any trade or commerce" to be unlawful. KY. REV. STAT. 367.170(1). "[U]nfair shall be construed to mean unconscionable." KY. REV. STAT. 367.170(2). KY. REV. STAT. 304.12-010 prohibits any person from engaging in "an unfair method of competition or any unfair or deceptive act or practice in the business of insurance."

Franklin County argues that KALF's January 9, 1988, sales

proposal provided to the Franklin County Fiscal Court is evidence that KALF's conduct was unfair, misleading and deceptive. KALF offered to provide General Liability coverage for civil rights liability, Public Officials coverage (including wrongful termination and acts in error or omission), and Law Enforcement coverage (including mental distress and violation of civil rights). It is the position of Franklin County that KALF then issued policies that attempted to omit the coverages marketed to the County and utterly failed to provide any definitions of the scope of the Public Officials and Law enforcement coverages.

In support of their theory, Franklin County offers the testimony of Del Beard, an expert witness employed with Insurance Schools, Inc. Specifically he reports that KALF's sales proposals deceptively claimed to provide coverage for inherently intentional torts such as malicious prosecution, assault and battery, wrongful discharge, any act in error or omitted, humiliation, and violation of civil rights, and yet made no mention of any intentional torts exclusion. He further opined that KALF failed to explain key terms such as occurrence, exclusions, and policy limits. He further argues that the wording of certain key terms, such as the definition of "intentional torts" and "occurrence" and the structure of the policies produced a contract that is misleading and

virtually incomprehensible to the average insured.

While Franklin County Attorney James Boyd has explained that KALF representatives never explained the terms or coverages of the policy and that the County believed that they had insurance to cover them for whatever happened, he has also testified that he was never consulted by the Fiscal Court concerning the County's insurance needs and has never read the KALF policy. Judge Arnold has testified that he more than likely relied upon Boyd, the Magistrates, and the County Treasurer for the working knowledge of the County's insurance coverage and claims, for advice, and for knowledge of what was contained in the KALF agreements.

The Court is loathe to conclude that the actions of KALF constitute unfair, false, misleading or deceptive acts or practices or that they may be defined as unconscionable in the absence of any evidence to suggest that Franklin County, through its public officials, questioned or even read the contents of the policies. Without impugning Beard's testimony, the Court declines to charge KALF with Franklin County's apparent failure to peruse its own insurance coverage documentation. This claim shall be dismissed with prejudice.

D. CONCLUSION

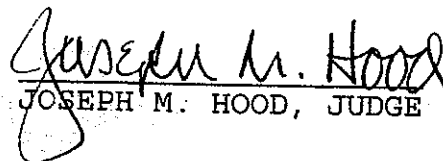
For all of the reasons stated above, KALF's motion for summary judgment shall be granted, Plaintiffs' motion for

summary judgment shall be granted, and Defendant Franklin County's motions for summary judgment and partial summary judgment shall be denied.

Accordingly, IT IS ORDERED:

- (1) that Defendant KALF's motion for summary judgment [Record No 121] be, and the same hereby is, GRANTED;
- (2) that Plaintiffs' motion for summary judgment [Record No. 113] be, and the same hereby is, GRANTED; and
- (3) that Defendant Franklin County's motions for summary judgment [Record No. 119] and partial summary judgment [Record No. 144] be, and the same hereby are, DENIED;
- (4) that all crossclaims and counterclaims by Defendant Franklin County pending against Plaintiffs and Defendant KALF be, and the same hereby are, DISMISSED WITH PREJUDICE;
- (5) that Plaintiffs' request for declaratory relief [Record No. 29] be, and the same hereby is, GRANTED; and
- (6) that Defendant KALF's request for declaratory relief [Record No. 40] be, and the same hereby is GRANTED IN PART and DENIED IN PART.

This is the 29th day of October, 2003.


JOSEPH M. HOOD, JUDGE

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