ARONBERG GOLDGEHN

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Insurance Coverage Update

Restitution of Administrative Fee Is Not Covered Damages

The U.S. District Court for the Southern District of Illinois has determined that a suit for the return of an administrative fee is not a suit for "damages". The court held that the insurer, represented by Aronberg Goldgehn in the declaratory judgment action, had no duty to defend or indemnify a municipality against a class action suit in which the plaintiff attacked the constitutionality of a city ordinance requiring payment of a fee to release an impounded vehicle. *Atlantic Specialty Ins. Co. v. City of Carbondale, et al.,* 2020 WL 4436307 (SD Ill., August 3, 2020).

The coverage action rose from a class action lawsuit filed against the City of Carbondale (the "City") in which the underlying claimant, on behalf of himself and the putative class, sought the refund of a fee he asserted the City wrongfully collected. The claimant alleged that the City administratively seized and impounded his vehicle and charged him a $400 administrative towing fee pursuant to a City ordinance. The claimant sought a judicial declaration that the ordinance was unconstitutional, and requested that the City be ordered to disgorge the administrative fees taken from him and the class members.

The City tendered the class action suit to its liability insurer under a policy that included, among other coverages, Public Officials Errors and Omissions Liability ("E&O") coverage and Law Enforcement Liability ("LEL") coverage. The City ultimately agreed that the E&O and LEL coverages were the only potentially applicable coverage parts of the policy, and the court therefore only addressed the issues under those two coverage parts.

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The E&O and LEL Insuring Agreements both provided that the insurer would pay those sums that the City became legally obligated to pay as "damages" for a "claim" resulting from a "wrongful act". Both coverage parts defined "damages" to include money damages, but specifically excluded non-monetary relief and "payment, restitution, return or disgorgement of any fees, profits, commissions, charges," or "funds allegedly wrongfully or unjustly held or obtained."

The insurer disclaimed coverage for the lawsuit because the relief requested – non-monetary declaratory relief and disgorgement of the administrative fees – did not constitute "damages". The insurer then sought a declaratory judgment that it had no duty to defend or indemnify for the suit.

Applying Illinois law and substantial precedent from the Seventh Circuit U.S. Court of Appeals, the *City of Carbondale* court agreed with the insurer's disclaimer. The court held that the claimant did not seek "damages", the policy's Insuring Agreements therefore were not triggered, and the insurer had no duty to defend or indemnify. In reaching that conclusion, the court discussed the long line of Seventh Circuit and Illinois cases finding that restitution or disgorgement of monies to which an insured is not legally entitled does not constitute covered damages or loss under an insurance policy. The court included in its discussion the often-cited Seventh Circuit decisions in *Level 3 Communications v. Federal Ins. Co*., 272 F.3d 908 (7th Cir. 2001) and *Ryerson, Inc. v. Federal Ins. Co*., 676 F.3d 610 (7th Cir. 2012). The court also relied on the Illinois Appellate Court's decision in *Local 705 Int.'l Bhd. of Teamsters Health and Welfare Fund v. Five Star Managers, LLC*, 735 N.E.2d 679 (Ill. App. 2000), upon which the Seventh Circuit relied in *Level 3*. These decisions, and others from Illinois and many other jurisdictions, make clear that the return of money unjustly obtained does not constitute covered loss or damages under a liability insurance policy. As in those cases, the *City of Carbondale* court found that the claimant in the underlying lawsuit sought the return of fees the City allegedly wrongfully charged, and the suit involved the potential restoration of ill-gotten gains.

The court also rejected the City's argument that a declaration in the coverage action would determine an ultimate fact in the underlying suit, a situation that Illinois courts disfavor. Under Illinois law, it is generally inappropriate for a court considering a declaratory judgment action to declare issues of ultimate fact that could bind the parties to the underlying action. *Maryland Casualty Co. v. Peppers*, 355 N.E.2d 24 (Ill. 1976). The City argued that the court's declaratory judgment could determine whether the amount charged the claimant was a "fee" or a "fine", which the City contended was a disputed issue in the underlying case. The court rejected that argument because, regardless of whether the money is ultimately found to be a fine or a fee, both constitute a "charge" or "funds allegedly wrongful or unjustly held or obtained", and consequently would fall within exceptions to the policy's "damages" definition. Therefore, the court's coverage determination would not impact an ultimate factual issue in the underlying lawsuit.

Comment

Insurers and insureds frequently debate and litigate questions as to whether suits seeking the return of funds constitute suits for covered "damages" or "loss". The *City of Carbondale* case is another example

of courts employing the reasoning of *Level 3* and its progeny in finding that suits for restitution or disgorgement of ill-gotten gains, or moneys to which an insured is not legally entitled, do not give rise to covered claims.

If you have any questions about this Update, please contact the author listed below or the Aronberg Goldgehn attorney with whom you normally consult:

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