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Lawyer Insights

Common issues, tips for navigating related insurance claims (Part 2)

Understanding the scope of related-claim provisions and how they work can minimize surprises should a claim arise.

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***Editor's note**:* This is the second of a two-part series discussing the significance of "related" claims under directors and officer (D&O) and other claims-made liability policies.

Part one of this series explained the importance of "related" claims and surveyed two recent federal cases that examined relatedness. This article delves into why these decisions are important by examining the landscape of relatedness decisions and highlighting several key points for policyholders to keep in mind as they navigate this intricate and fact-specific legal domain.

When it comes to "relatedness," results may vary.

Relatedness is a multi-faceted issue, the outcome of which can turn on one or many variables. This article will focus on three common variables:

- Policy language;
- Variations in state law; and
- Divergent facts.

The outcome of a relatedness analysis can be unpredictable, turning on the facts of each case, and can benefit insurers and policyholders, depending on the circumstances.

There's more than one way to define related.

The way related claims or acts are defined can vary greatly from one policy to the next. In *American Southwest*, **discussed in part one of this series**, the policy defined "interrelated claim" as, "all claims arising out of a single act or omission or arising out of interrelated acts or omissions in the rendering of professional service."

But other insurers provide markedly different standards for assessing relatedness. "Related Wrongful Act(s)" can be defined as, "the same, related or continuous, or Wrongful Act(s) which arise from a common nucleus of facts."

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Another policy may define “Interrelated Wrongful Acts” as, “any Wrongful Acts which have as a common nexus any fact, circumstance, situation, event, transaction or series of facts, circumstances, situations, events or transactions.” Other insurers may use different variations, but they all aim to achieve the same goal, which is to incorporate the concept of “relatedness” into a particular policy form.

When faced with multiple claims spaced months or years apart, insurers often attempt to limit or eliminate coverage by arguing that a later claim “related back” to an earlier claim outside the current policy period. If another insurer issued that earlier policy, the current insurer may point the finger to escape liability altogether. But even if there is continuity of insurers across all policy years, pushing claims into earlier years may still limit coverage if the other policy had lower limits, higher retention, sublimits or more restrictive coverage terms.

The case of *Hanover Insurance Co. v. R.W. Dunteman Co.* is one example where related claims eliminate coverage entirely. In *Hanover*, the Seventh Circuit found that, under Illinois law, when a claimant added new allegations and new defendants to an amended complaint, that claim related back to the original complaint, which was excluded from coverage under an earlier policy because of the insured’s failure to give timely notice.

The Seventh Circuit analyzed the D&O policy’s definition of “Related Claims” and “Related Wrongful Acts.” The underlying dispute concerned the reduction of a shareholder’s ownership interest, which led to the filing of an original complaint during a 2017 policy period and amended complaint during a 2018 policy period. The court determined that the original complaint and the amended complaint concerned both “Related Wrongful Acts” and “Related Claims.” As for the new allegations, the court found that they were “logically connected” and, as a result, alleged “Related Wrongful Acts” as defined by the policy.

Similarly, with respect to adding new defendants, the court found that, under the policy’s related-claims provision, the theories alleged against the new defendants were “based upon” or “related to” the claims made in the original complaint. Since the insureds had failed to provide timely notice of the claim under the 2017 policy, and because the subsequent amended complaints were considered related to the claim under the 2017 policy, the court found that the insurer was justified in denying coverage.

Zurich American Insurance Co. v. UIP Cos. yielded a similar result under similar facts, although under different policy language. The court determined that an email sent during a 2017 policy period about the potential buyout of an ownership interest constituted a claim triggering the D&O policy’s notice requirements but that the insured had failed to give timely notice. This email preceded three lawsuits filed during the 2018 policy period seeking compensation for the same ownership interest.

The court concluded the three 2018 lawsuits related to the initial claim under the 2017 policy, because they all arose from the same wrongful act and shared a “common nexus” as defined by the policy. As a result, the insurer properly denied coverage for the three related lawsuits based on the policyholder’s failure to provide timely notice of the original claim.

The case of *Alexbay LLC v. QBE Insurance Corp.* tells a similar story. There, the court granted summary judgment for an insurer that had denied coverage for a lawsuit because it was a related claim that predated the coverage period of the D&O insurance policy.

The underlying lawsuit challenged the conveyance of company shares to Alexbay LLC, which the court determined was the same “common nexus of facts [or] circumstances” underlying an earlier lawsuit in a

previous coverage period. Since the lawsuit was deemed first made during a previous policy period, the insurer was not required to provide coverage.

These are just some examples of how courts have applied the language of related-claims provisions to eliminate coverage. Other cases rule against relatedness, or in favor of coverage, under similar policy language due to other factors, like different governing law or facts discussed below.

State law variations

Aside from divergent policy language, whether claims are related can also turn on applicable state law. Because insurance is regulated by the states, each state has created a body of case law governing how policies should be interpreted and disputes under those policies should be resolved. While many principles are uniform nationwide, many issues — including how to assess "relatedness" under claims-made policies — vary widely between different states.

For instance, some courts have found that "related" claim provisions located in the "Conditions" section of a policy, rather than the "Exclusions" section, show that such provisions were intended to be a condition that the policyholder must meet to trigger coverage under the policy. But other courts find that simply labeling a related-claims provision as a condition will not allow an insurer to escape its burden of proof if the provision acts as an exclusion and works to limit or eliminate coverage.

In *Borough of Moosic v. Darwn National Assurance Co.*, the Third Circuit determined that a related-claim provision found in the insuring agreement operated to "limit coverage" and therefore should be treated as an exclusion even if it were not labeled as one in the policy. As a result, the court held that the insurer raising the "related" claim defense to limit or exclude overage was relying on an exclusion and carried the burden of proving the exclusion applied.

Some states have also developed common-law standards to assess "relatedness," which may be applied regardless of variations in policy language. New York, for example, applies a "sufficient factual nexus" test to establish that a prior claim is interrelated with a subsequent claim. As stated in *Weaver v. Axis Surplus*, a sufficient factual nexus is found where the Claims "are neither factually nor legally distinct, but instead arise from common facts" and where the "logically connected facts and circumstances demonstrate a factual nexus' among the Claims."

Oklahoma has developed another standard. In *Axis Surplus Insurance v. Johnson*, the U.S. District Court for the Northern District of Oklahoma ruled that relatedness turned on whether the relationship between two claims was "so attenuated . . . that an objectively reasonable insured could not have expected that they would be treated as a single [related] claim."

Other states, like Delaware, have departed from common-law relatedness standards in favor of more traditional policy interpretation. All these variations in state law stand to impact related-claim analysis depending on which state's law governs a particular dispute.

Divergent facts

As seen in the cases highlighted in this series, while policy language and state law are important factors, the determination of whether claims are related often comes down to a factual inquiry unique to the specific circumstances giving rise to the claim. In *American Southwest*, for example, the Tenth Circuit

determined the botched audits were related because the same auditor made the same error three separate times.

Yet, applying the same "logically" or "casually" connected analysis, the court in *OutsideIn* held that while both claims at issue stemmed from the same architectural firm's involvement in the project around the same time, they were unrelated because there was no evidence that the firm acted with a common purpose in the claims. While both insurer and policyholder can argue that the policy language and state law are in their favor, the analysis often turns on the facts of the case at hand. As seen in the case law, the fact-intensive nature of related claims means the outcome can be unpredictable.

Relatedness can benefit both sides.

Although many decisions discussed above favored insurers, policyholders can also benefit from "relatedness" of claims. For instance, each claim is typically subject to its own retention that must be satisfied before the insurer will being reimbursing losses. But if multiple claims are related, they constitute a single claim and will only be subject to a single retention, which can be worth tens if not hundreds of thousands (or millions) of dollars in savings. Policyholders similarly may be able to pull otherwise uncovered lawsuits into a particular policy that has no sublimit, greater limits, different insuring agreements, or less restrictive exclusions.

The multiple-retention issue was examined in the Tenth Circuit's ruling in *Brecek & Young Advisors v. Lloyds of London*, which determined under New York law that 26 individual claimants' claims in one arbitration constituted interrelated wrongful acts and thus should not be subject to $50,000 retentions for each claim. The ruling was significant, as the dispute over relatedness was the difference between a $1.3 million retention or a single $50,000 retention. In reversing the lower court's summary judgment ruling on "relatedness," the court concluded that, since all claims "were connected by common facts, circumstances, decisions, and policies," the claims arose from interrelated wrongful acts and should not be subject to individual retentions.

A policyholder similarly benefited in *Carolina Casualty Insurance Co. v. Omeros Corp*., by pulling a subsequent related claim within a policy's scope of coverage. In that case, the U.S. District Court for the Western District of Washington agreed with a policyholder that, even though a claim was made and reported after the applicable policy period, the insurer should still have to pay since the claim related to an earlier claim that had been made and reported within the policy period. The court concluded that the claims were related wrongful acts and, as a result, all claims should be considered a single claim. The court granted summary judgment for the policyholder and required the insurer to treat the separate claims as one claim, which had been made on the date of the earliest claim, which successfully brought the second claim into coverage under the policy.

Policyholders should consider "relatedness" when a new claim is made and determine whether it is beneficial for that claim to relate back to an earlier claim or policy. For example, a claim may relate back to an earlier policy period with a more favorable retention, higher limits or better policy language. Because related-claim can both increase and decrease recovery, insures may construe its policy differently across claims, depending on whether relatedness would benefit the policyholder or the insurer. This has led to insurers being on both sides the issue when interpreting identical policy terms. So policyholders should investigate these conflicting positions if they find themselves in a dispute over the meaning and scope of a related-claim provision.

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Relatedness and risk management

The related-claim decisions and factors discussed above provide guidance to policyholders in navigating the challenging and often unpredictable world of related claims, which can arise in many ways.

First, policyholders should strive to understand all applicable related-claim provisions when negotiating their policies, rather than after a claim arises. Is the policy clear? How are the related-claim provisions intended to operate and does the policy language support that intent? Do any provisions warrant further discussion and, if needed, amendment by endorsement? As the *Eleventh Circuit in Health First, Inc. v. Capitol Specialty Ins. Corp.*, noted when enforcing one particularly broad set of related-claims provisions, the policyholder is often "stuck with the policies it paid for." Understanding how related-claim provisions work along with policy conditions, exclusions and other provisions can ensure that policyholders obtain appropriate protection in exchange for their premium dollars.

Second, policyholders must understand that of the examples above are merely illustrative and that disputes involving multiple claims show up in other ways and implicate other policy provisions. A "prior notice" exclusion is one such example that can be used punitively to limit coverage using "related" claim concepts. In *Emmis Communications Corp. v. Illinois National Insurance Co.*, an insurer denied coverage under a D&O policy's prior notice exclusion based on a notice provided under a previous policy from a separate insurer. The insurer argued that, since the claim filed under the current policy "related" to the previous claim and the current policy required only "any shared factual allegation" to establish relatedness, it appropriately denied coverage. The court disagreed and determined the claims were not related enough to make the prior notice exclusion applicable. As Emmis shows, related claims can arise in various ways, including in prior notice exclusions and other potential limitations on coverage.

Because of the considerable variations in related claims provisions, policyholders must consider the effect of related-claim provisions early on, whether that be during the initial placement of insurance or later renewals, non-renewals, cancellations or runoffs. Understanding the scope of related-claim provisions and how they work along with policy conditions, exclusions and other provisions, as well as state law, can minimize any surprises should a claim arise.

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