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FEATURE STORIES

Insurance Coverage under D&O and Professional Liability Policies: Watch Your Insurance Company's Fuzzy Math

By R. Mark Keenan and Craig M. Hirsch

Trouble hits. Ten actions by 10 claimants separately allege that a director or senior executive at your company caused each claimant a loss of \$1 million. Despite the separate claims, it appears that the allegations all arise from a single act, or perhaps related acts, of alleged malfeasance. The actions name the executive as well as your corporation as defendants. The policy provides for a \$1 million retention or deductible—the amount of money your corporation pays per loss before the insurance company begins to cover your claim.

You file a claim with your insurance company under an insurance policy that states:

Claims involving the same wrongful act or interrelated wrongful acts of one or more insureds shall be considered a single loss and only one retention shall be applied to each such single loss.

Perhaps you even have a simpler form. At least one insurance company has had a form that provides that, "Interrelated Wrongful Acts means *all* causally connected wrongful acts" (emphasis added).

Since each claimant's action derives its origins from a common plan perpetrated by the senior executive, the policy's interrelated wrongful acts provisions seems to combine all underlying claims into a single loss. Thus, after paying the retention, you expect the insurance company to cover \$9 million (i.e., a \$10 million loss less the retention) depending on the policy limits.

That's how it works...in theory. All claims featuring the same wrongful acts will become a "single loss" and obligate the policyholder to pay a single retention or deductible. After that, the insurance company must step to the plate, cover the remaining loss, and exhaust its policy limits if necessary.

Insurance Companies' Subjective View

But here's the rub: when the policy features a substantial retention, the insurance company will often characterize each underlying claim as an individual loss regardless of the factual nexus or interrelatedness between the policyholder's wrongful acts. Thus, the insurance company will claim that the policyholder must satisfy a retention on each claim before triggering coverage. Now your corporation must pay 10 separate retentions totaling \$10 million, leaving the loss actually covered by the insurance company at? You guessed it—zero.

Can insurance companies get away with this subjective policy interpretation?

They shouldn't. Remember, most courts find policy provisions ambiguous when two plausible interpretations exist and the general rule states that latent ambiguities are resolved *contra proferentum*, i.e., against the insurance company who drafted the policy. As noted by the *Tenth Circuit in Strauth v. National Union Fire Ins. Co.*, policyholders, not insurance companies, often get the benefit of the doubt:

Many of the courts that take a pro-insured approach when faced with policies which do not define "interrelated" cite, as a major reason for taking such an approach, the maxim that ambiguities in insurance policies "must be interpreted in favor of the insured.

Further, in construing a policyholder's reasonable expectations, New York courts tend to identify the root causes of loss in a manner which maximizes insurance coverage. In other words, courts have found a single occurrence when a policyholder has large deductibles or retentions and large per occurrence limits. (See *Champion Int'l Corp. v Continental Cas. Co.*) Consequently, when the policyholder has no deductible or low per-occurrence limits, the courts have determined multiple occurrences. (See *Arthur A. Johnson Corp. v. Indemnity Ins. Co. of North America*, 7 N.Y.2d 222 [1959].)

Interrelated Wrongful Acts Mean a "Common Nexus" of Facts

A recent decision by the Second Circuit involved a policy defining "interrelated wrongful acts" as "any and all Wrongful Acts that have as a common nexus any fact, circumstance, situation, event, transaction, cause or series of causally or logically connected facts, circumstances, situations, events, transactions, or causes." Here, the two underlying claims filed against the policyholder both alleged the same cause of action—antitrust violations—and similar facts. In a dispute between two insurance companies, the Second Circuit affirmed the District Court's finding that both claims emanated from interrelated wrongful acts because they were "neither factually nor legally distinct" under the policy definition.

Unfortunately, many policies fail to define "related" or "interrelated" wrongful acts making the courts the ultimate arbiters of the connection between multiple claims. However, some courts will apply a common sense or dictionary meaning to the terms when interpreting the insurance policy, a reading that typically favors the policyholder. In *Continental Casualty Co. v. Wendt*, the 11th Circuit held that, "The words 'relate' or 'related' are commonly understood terms in everyday usage. They are defined in the dictionary as meaning a 'logical or causal connection between two events.'"

A Single Loss for Two Insureds

Another question arises under the interrelated wrongful acts provision: what if two insureds—such as a group of directors, or both the company and a senior officer—are found jointly and severally liable in an underlying claim with each contributing a payment to satisfy the judgment which is less than the applicable deductible? The underlying complaint asserts distinct causes of actions against each insured, prompting the insurance company to cry two losses and two deductibles, and that the wrongful acts are not interrelated.

While always a fact-sensitive inquiry, chances are that when dealing with a single legal proceeding with insureds covered by the same policy, and an ultimate finding of liability that any or all of the insureds must satisfy, the wrongful acts which produced the underlying claim are interrelated and one deductible applies. The insurance company's focus on the delineation between causes of actions would be misplaced. The focus of the policy provision is on "acts," not theories, and courts have ruled that the operative question is whether the conduct of each insured—based upon the allegations and evidentiary findings in the underlying claim—is interrelated. Distinctions between the causes of action asserted against each insured should not be determinative.

All acts with a related causal connection should elicit a single loss and a single retention no matter the number of causes of actions or individual claims. A plain reading of the sample provision from the top of the article can

support no other interpretation. The interrelationship of how insureds allegedly behaved is what governs whether the retention has been exhausted.

Conclusion

The shrewd policyholder will beat the insurance company at its own game. Request a policy definition of interrelated that combines all potential claims arising out of same or interrelated acts into a single loss, especially if you have a significant deductible or retention. The language should focus on the facts and allegations, not the number of claims or causes of action. Don't allow any syntactical wiggle room. When you commit or allegedly commit a series wrongful acts within the same course of conduct, your policy should mechanically combine all claims seeking damages based on this conduct.

You purchased an insurance policy with the expectation of coverage in troubled waters. Don't let the insurance company abandon ship. 🚢

ABOUT THE AUTHORS

R. Mark Keenan is a senior shareholder in the New York office of Anderson Kill & Olick, P.C. and chair of the firm's financial institutions group. Mr. Keenan is a leading lawyer in the fields of insurance coverage, securities law and litigation. Mr. Keenan regularly represents policyholders in insurance coverage disputes involving broker/dealers, hedge funds, investment advisors and other financial institutions.

Craig M. Hirsch is an attorney in the New York office of Anderson Kill & Olick, P.C. and a member of Anderson Kill's financial services group. Mr. Hirsch practices in the fields of insurance recovery litigation with an emphasis on D&O liability and professional liability coverage, products liability and commercial litigation.

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Warren, McVeigh & Griffin, Inc. | Griffin Communications, Inc.
Independent Risk Management Consultants and Publishers
1420 Bristol Street North, Suite 220, Newport Beach, CA 92660
Telephone 949-752-1058 | Fax 949-955-1929 | Customer Service 800-205-6218
www.riskvue.com | www.griffincom.com