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Seventh Circuit Decision Sends Warning to "Claims Made" D&O Insurance Policyholders

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By: Brian S. Scarbrough, Maura E. Smyles

Policyholders with claims made D&O liability insurance – or any other type of claims made liability insurance – should take care to closely review both the terms of the notice requirements within their policies and those pertaining to treatment of related wrongful acts or related claims. Where such provisions use broad language to aggregate wrongful acts and related claims, treating them all as a single claim, it is especially important to be diligent in reporting all potential claims as soon as they arise. Failure to do so could result in large and unexpected out-of-pocket costs, as the no-coverage determination for the original claim could bar coverage for related claims for years to come.

The U.S. Court of Appeals for the Seventh Circuit in *Hanover Ins. Co. v. R.W. Dunteman Co.*, 2022 WL 13769371, --- F.4th --- (7th Cir. Oct. 24, 2022), recently interpreted Illinois law on the aggregation provisions in a claims made D&O liability insurance policy. The court concluded that an initial complaint seeking relief only against the company and a later amended complaint that introduced individual defendants and new allegations of serious wrongdoing constituted the same claim. This led to a finding of no coverage for the policyholders due to untimely notice of the initial complaint to the insurer.

Because many claims made policies include similar aggregation and claims notice provisions, policyholders should pay close attention to how coverage was lost here due to untimely notice and how to guard against that risk in the future.

Background on Claims Made Policies

A claims made insurance policy, including a directors and officers liability ("D&O") insurance policy, provides coverage for losses resulting from claims made against policyholders during the relevant policy period. Such policies often further specify when a claim must be reported or noticed to the insurer, typically requiring such notice during the relevant policy period or within a set amount of time after the policy period expires. Policy provisions vary on notice and should be carefully consulted. But under such policies, timely notice of a claim by a policyholder to its insurer can be critical.

The Insurance Coverage Lawsuit

The federal insurance coverage litigation arose from an underlying dispute between family members over ownership interests in the family's Illinois-based construction businesses, Du-Kane Asphalt and Crush-Crete.

A. Underlying State Court Litigation

Following the death of family matriarch Jane Dunteman, her estate sued in state court, claiming that Jane's shares were wrongfully diluted prior to her death. The initial complaint, filed in August 2017, sought a declaratory judgment against only Du-Kane Asphalt as to the size of Jane's ownership interest in the company at the time of her death.

Nearly a year later, in July 2018, the estate filed an amended complaint that broadened its factual allegations and added Crush-Crete and the Dunteman brothers as co-defendants. Specifically, the estate alleged that the Dunteman brothers, as directors and officers of Du-Kane Asphalt, were responsible for the wrongful reduction in Jane's ownership interest. The amended complaint also added counts against Du-Kane Asphalt and Crush-Crete for minority shareholder oppression and against the individual Dunteman brothers for breach of fiduciary duty, fraud, and conspiracy.

At that point, in 2018, the defendants first notified their insurer about the lawsuit and sought coverage.

B. Insurance Policy: Relevant Provisions

All six codefendants—Du-Kane Asphalt, Crush-Crete and the four individual Dunteman brothers—were insured under the same claims made D&O policies, consecutively issued in 2017 and 2018 by Hanover. The policies required a claim to be first made during the policy period and also required the insureds to report all claims to Hanover "as soon as practicable," or no later than 90 days after the expiration of the applicable policy period.

Of significance here, the 2017 policy contained two aggregation provisions that impacted whether the insured timely made notice.

- First, the policy treated all "Related Wrongful Acts" as one wrongful act, collectively "deemed to have occurred at the time the first of such Related Wrongful Acts occurred." The policy defined Related Wrongful Acts as those that are "logically or causally connected by reason of any common fact, circumstance, situation, transaction, casualty, event, result, injury or decision."

- Second, the policy treated "Related Claims" as a single claim that was made in the policy period of the earliest of such claims. The policy defined Related Claims as "all Claims based upon, arising from or in any way related to the same facts, circumstances, situations, transactions, results, damage or events or the same series of facts, circumstances, situations, transactions, results, damage or events.

In short, according to the Court, all related wrongful acts were aggregated and deemed to have occurred at the time of the earliest act, while all related claims were aggregated and deemed to have been made at the time of the earliest claim.

C. Insurance Notice

In 2018, after the estate moved to file an amended complaint, the policyholders for the first time notified Hanover. They sought coverage under the 2018 policy based on the new allegations made in the amended complaint. Hanover denied coverage because it determined that the claim was first made in 2017, before the then-current 2018 policy period, and the insureds had failed to provide notice of the claim within the time period provided in the 2017 policy.

The case was submitted on cross-motions for judgment on the pleadings. The district court entered judgment for Hanover, and the policyholders appealed. The Seventh Circuit ultimately affirmed the lower court's grant of judgment on the pleadings for Hanover.

Seventh Circuit's Reasoning

The parties disputed several key points on appeal, including: whether the original complaint constituted a reportable claim, whether the addition of new defendants in the amended complaint meant that those parties could report in the then-current policy period, and whether the new allegations contained in the amended complaint were related to those in the original complaint such that they commenced a new claim reportable under the policy. These disputed points serve as practical guidance to policyholders on why claims should be reported right away under claims made insurance policies, even those that may be regarded at the time as minor or nuisance claims.

Reportable Claim: When the original complaint was filed in state court in 2017, it simply sought a declaratory judgment against Du-Kane Asphalt. The policyholders insisted that this action alone did not constitute a reportable claim because it did not allege any "wrongful act" by Du-Kane Asphalt. The Seventh Circuit concluded that the original complaint was a reportable claim and "fit comfortably" within the policy's broad definition of a "wrongful act." The Court added that the fact that the original complaint sought only declaratory relief and could not have resulted in a compensable loss for the insureds, did not affect the analysis. Under the terms of the policy, the notice requirement did not turn on the specific remedies that the plaintiffs requested.

New Defendants: The Seventh Circuit previously stated, in Community Foundation for *Jewish Education v. Federal Ins. Co.,* 16 F. App'x 462, 467 (7th Cir. 2001), that an amended complaint against a new party would constitute "a new proceeding with respect to the insured," reasoning that "[i]f the insured is brought into the litigation for the first time through the amended complaint, that claim is obviously new to that entity; thus it is a claim first made."[2] The policyholders argued that this precedent required a finding of coverage for the company that was added through the amended complaint, and thus became a party during the relevant policy period. Hanover disagreed that *Community Foundation* controlled, given that that the original defendant (Du-Kane Asphalt) and

the new co-defendants (Crush-Crete and the individual Dunteman brothers) were all insured under a single policy.

The Court ultimately declined to give controlling weight to *Community Foundation*. Applying Illinois law, the Court emphasized that the essential purpose of the notice requirement would be undermined if later iterations of a complaint could excuse a policyholder's failure to timely report the lawsuit when it was first filed against one of the policyholders.

New Allegations: The policyholders argued that the claims made in the amended complaint and those made in the original complaint were unrelated, and thus could not be properly aggregated under the policy's "Related Claims" provision. They pointed to the new causes of action contained in the amended complaint and emphasized distinctions between the facts, legal theories, parties, and time periods in which the alleged events occurred. Hanover disagreed, insisting that even if the Court were to conclude that the amended complaint constituted a new claim, the two claims should at least be treated as "Related Claims" that were deemed first made during the 2017 policy period with the filing of the original complaint.

The Seventh Circuit concluded that the new allegations in the amended complaint did not commence a new claim. "At the very least," the court reasoned, "the allegations in the original and . . . amended complaints are 'logically . . . connected' because they collectively concern the insureds' wrongful reduction of Jane's ownership interest in the family business." The Court also cited as support for its conclusion the fact that amendments to a complaint do not commence a new civil action, even when they introduce new causes of action.

Takeaways for Policyholders

The Seventh Circuit's broad construction of claim relatedness provisions sends a warning to policyholders under any claims made insurance policies, including D&O liability policies: provide prompt notice of even seemingly minor claims—including those that appear to fit well within the policy deductible or retention—to avoid the risk of losing coverage for any and all related claims that evolve during the course of litigation against any parties insured under the same policy.

Whether multiple claims or wrongful acts are related is a heavily litigated coverage area with decisions coming out both for and against policyholders. To avoid this uncertainty, policyholders should give serious consideration to how aggregation and relatedness provisions in claims made insurance policies could both restrict (as it did here) or expand (as the concurring opinion in this case discussed) coverage. And that assessment in turn should be taken into account when deciding to make notice of an initial claim.

For their part, directors and officers who are insured under the same D&O policies as the company itself should work closely with management to ensure that all claims against the company or any other insured party are being timely reported to the insurer. If an initial claim against one policyholder – such as the company – goes unreported, it could be too late to seek coverage once

subsequent developments in litigation add allegations against additional policyholders – such as individual directors and officers.

The decision isn't all bad news for policyholders, though. As Judge Hamilton pointed out in his concurring opinion, the reasoning actually "cuts both ways." If a policyholder *does* provide timely notice of a very minor claim against only one policyholder, then the logic of the opinion dictates that future developments in the litigation will also be covered as related claims, even when they greatly expand the scope of liability or the policyholders at issue. As such, the extent to which the enforcement of broad claim relatedness provisions expands or restricts the coverage owed to policyholders depends on the extent to which policyholders heed this warning and invest in robust risk management for tracking and reporting claims.

It is nearly impossible to anticipate the precise level of risk associated with a particular claim at the outset. Discovery, or other developments in the case, might lead to additional defendants, causes of action, or requested forms or relief. As a policyholder, the best way to manage that uncertainty is to closely monitor all claims and report them to your insurer as soon as possible.

Footnotes

[1] Brian Scarbrough is a partner and co-chair of the Insurance Recovery and Counseling Group in Jenner & Block LLP's Washington DC office. Maura Smyles is a Law Clerk in the same office.

[2] *Community Foundation for Jewish Education v. Federal Ins. Co.*, 16 F. App'x 462, 467 (7th Cir. 2001).

Related Attorneys

Brian S. Scarbrough
Partner
bscarbrough@jenner.com
+1 202 637 6306

Maura E. Smyles
Associate
msmyles@jenner.com
+1 202 639 6864

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