

# Client Alert: Recent Developments Construing “Claims” in the Context of Insurance Coverage for Government Investigations

## Publications

June 22, 2023

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Government investigations are costly, requiring companies and individuals to expend significant financial resources to comply with, or challenge, the government’s requests. In these situations, where a company or an individual faces a government subpoena, civil investigative demand, indictment, or otherwise finds themselves subject to a government investigation, what are the latest legal developments concerning whether their directors and officers (D&O) liability insurance policy will treat the investigation as a “claim” that triggers potential coverage under the policy?

The threshold questions that historically have guided this analysis are (and continue to be): **first**, what is the definition of the term “claim” in the particular policy at issue, and **second**, what does the specific investigation at issue look like in terms of available communications and documents from the government?

## **Recent Guidance from the Fourth Circuit**

While coverage may be available, companies should first identify what the “investigation” looks like. A subpoena may qualify as a claim, while a search warrant may not, at least in the 4th Circuit.

Recently, the Fourth Circuit offered fresh guidance as to whether a search warrant constitutes a “claim” that triggers potential coverage under a law firm’s professional liability insurance policy. In *Brown Goldstein Levy LLP v. Fed. Ins. Co.*, No. 22-1023, 2023 WL 3513693 (4th Cir. 2023), the court ruled that a law firm’s liability insurance would *not* cover expenses incurred during a government investigation involving a search warrant and a conflict letter directed to one of the firm’s partners.<sup>[1]</sup> In 2014, the government notified a partner at Brown Goldstein Levy LLP (BGL).<sup>[2]</sup> In 2019, the government notified the partner P that his representation of several clients, including one under investigation for its connection to a federal racketeering case, presented multiple nonwaivable conflicts and subsequently obtained a search warrant for Brown Goldstein's offices, believing that the partner was connected to criminal conduct.<sup>[3]</sup>

After successfully defending the charges, BGL sued their insurer when it refused to cover costs related to the search warrant litigation and defense costs for the investigation of the subject partner. [4] Unconvinced that the government’s conflict letter and search warrant constituted a “claim,” the Fourth Circuit dismissed BGL’s claims against its insurer.<sup>[5]</sup>

The insuring agreement in the relevant liability insurance policy stated that the Insurer “shall pay Loss on behalf of an insured on account of any claim first made against such Insured during the Policy Period for a Wrongful Act committed by the Insured.” The policy further defined the term “claim” to include:

- (a) a written demand or written request for monetary damages or non-monetary relief;
- (b) a written demand for arbitration;
- (c) a civil proceeding commenced by the service of a complaint or similar pleading; or
- (d) a formal civil administrative or civil regulatory proceeding (including a disciplinary or grievance proceeding before a court or bar association) commenced by the filing of a notice of charges or similar document or by the entry of a formal order of investigation or similar document against an Insured for a Wrongful Act, including any appeal therefrom.<sup>[6]</sup>

The court proceeded to examine BGL’s claim under subpart (a) of the policy’s definition of the term “claim”—specifically, whether the search warrant could be considered “a written demand or written request for monetary damages or non-monetary relief ... against an Insured for a Wrongful Act.” Concluding that it could not be so considered, the court reasoned that because a search warrant does not “demand[] compliance,” it was therefore not a “written demand” for nonmonetary relief against an Insured under the policy. The court further distinguished between subpoenas and search warrants, noting that the former by comparison *does* command the recipient to comply.<sup>[7]</sup>

As for the conflict letters issued to the partner at issue, the court likewise found that these were *not* demands, but rather notices informing him of his ethical obligations. The court dismissed BGL’s suit against its insurer, signaling to policyholders that courts in the Fourth Circuit would strictly adhere to policy language and a narrow interpretation of written demands and requests in the context of interpreting what constitutes a “claim” for insurance coverage purposes for a government investigation.

### **Other Circuit Approaches**

Because circuits vary in their approach to this issue, companies and individuals facing government investigations are advised to take note of the applicable law, in addition to the particular policy language and specific circumstances of the investigation. Government investigations often begin with subpoenas directed to the company or to an individual(s) within the company, and as

demonstrated below, existing caselaw is quite mixed concerning coverage for government subpoenas.

In *Patriarch Partners, LLC v. Axis Insurance Company*, a New York district court found, and the Second Circuit affirmed, that a subpoena *did* constitute a claim under Patriarch Partners' excess D&O liability insurance policies.<sup>[8]</sup> In 2012, the U.S. Securities and Exchange Commission issued a subpoena ordering Patriarch Partners, a private equity investment firm, to produce all emails and messages from certain executives.<sup>[9]</sup> The SEC then launched an enforcement action against the company, and Patriarch Partners, having depleted the first \$20 million of its primary and excess D&O liability insurance in response to the investigation and enforcement action, sought coverage for the remaining defense costs from the last excess insurer in its D&O liability insurance tower.<sup>[10]</sup>

The relevant excess D&O liability insurance policy defined the term "claim" to include, in relevant part, a "written demand for monetary damages or non-monetary relief (including but not limited to injunctive relief) or a written request to toll or waive the statute of limitations" or an "investigation of an insured alleging a Wrongful Act."<sup>[11]</sup> The district court found that the initial subpoena and later investigation and enforcement action were within the definition of "claim" for purposes of triggering potential coverage under the policy.<sup>[12]</sup> Consistent with prior Second Circuit holdings on this issue, the district court held that a "demand" for "non-monetary relief" includes a subpoena seeking the production of documents.<sup>[13]</sup> Likewise, an investigation and enforcement action by the SEC clearly falls under an "Investigation" of an insured.<sup>[14]</sup> The Second Circuit affirmed in favor of Patriarch.

As the *Patriarch Partners* case demonstrates in comparison to the *BGL LLP* case, it is important for companies and individuals to take note of the particular language in each policy—specifically, the definition of the term "claim." Unlike the policy at issue in *Patriarch Partners*, the policy at issue in *BGL LLP* did not define a "claim" to include an "investigation of an insured alleging a Wrongful Act," which is a much broader catch-all clause compared to the more restrictive language contained in BGL's policy.

The standard in other circuits is even more restrictive, finding that a subpoena or a notice of investigation does not constitute a "claim" unless it also includes an allegation of wrongdoing.<sup>[15]</sup>

In *MusclePharm Corporation v. Liberty Insurance Underwriters, Inc.*, 712 Fed. App'x. 745, 753 (10th Cir. 2017), the SEC issued a subpoena ordering MusclePharm, a company that sells sports nutrition products, to produce documents in support of the SEC's "inquiry" into the company with the disclaimer that "[t]he investigation...should not be construed as an indication by the Commission or its staff that any violation of the law has occurred."<sup>[16]</sup> The insuring agreement in the relevant excess D&O liability insurance policy required: 1) a claim, 2) made during the policy period, 3) lodged against an insured person or organization, and 4) for a wrongful act.<sup>[17]</sup> The policy further defined the term "claim" to include a written demand for monetary or non-monetary relief against

the Insured, a formal administrative or regulatory proceeding against the Insured, or a formal criminal, administrative, or regulatory investigation against the Insured when the Insured receives a Wells Notice or target letter in connection with such investigation.<sup>[18]</sup> Because the subpoena issued to MusclePharm did not allege a “wrongful act” or target a specific insured person, the Tenth Circuit held that the SEC was merely gathering information, rather than seeking “relief” as would be required to trigger potential coverage under the policy.<sup>[19]</sup>

Likewise, in *Ctr. for Blood Rsch., Inc. v. Coregis Ins. Co.*, 305 F.3d 38, 42 (1st Cir. 2002), the First Circuit held that a subpoena seeking the production of documents from the Center for Blood Research did not constitute a “claim,” as defined in the relevant policy, because the Center for Blood Research was merely a “custodian of records,” not a target of an investigation.<sup>[20]</sup>

However, a district court in Illinois has gone the opposite direction from the Tenth and First Circuits with respect to the necessity of a wrongful act for purposes of a “claim” in the context of an investigation. In *Astellas US Holding, Inc. v. Starr Indemnity and Liability Company*, No. 17 CV 8220, 2018 WL 2431969, \*5 (N.D. Ill. 2018), the court found that a subpoena itself need not explicitly allege a “wrongful act.”<sup>[21]</sup> Because the relevant policy only required that a “claim” be made “for any wrongful act,” it was enough for the purported targets to allege as part of their insurance claim that the government issued the subpoena *for* a wrongful act.<sup>[22]</sup>

## **Choice of Law and Forum Selection Considerations**

When placing or renewing an insurance policy, policyholders should be aware of how these differences in the definition of “claim” may interact with any choice of law analysis with respect to coverage disputes. Because the differences across jurisdictions can lead to varying interpretations, policyholders should consider adding a specific forum selection clause to the policy up front to make potential litigation more predictable. If there is not an opportunity to do so as part of the policy negotiations, once a claim comes in, the parties will need to undertake a choice of law analysis to determine which state’s law will apply and should take note of how different “claims” can be treated differently depending on the jurisdiction. A choice of law analysis for an insurance policy typically involves weighing factors such as where the claim was made, where the policyholders’ principal place of business and/or place of incorporation are located, where the policy was negotiated, and where the last act required to complete the policy (such as the delivery of the policy or payment of premium) was performed.

## **Monitoring the Investigation from a Coverage Perspective**

In the event an investigation forms the basis for a noticed claim (or potential claim) policyholders should additionally work with their insurers to keep them apprised as to how the investigation is progressing and where the investigation appears to be headed. The initiating documents may or may not reflect the actual or eventual focus of the investigation and can result in shifting coverage

determinations depending on the operative definition of the term “claim” in the relevant policy. Taking proactive steps like this can better position policyholders for coverage and reduce unnecessary disputes with their insurers.

## **Looking Ahead**

Moving forward, it is critical for companies and individuals to evaluate their existing insurance coverage to be familiar with the language in the insuring agreement and in the definition of the term “claim” that will guide the analysis of potential coverage for an investigation. Should a company or an individual become involved in an investigation, it is important that they first understand the government’s request, next determine the applicable jurisdiction, and finally review their insurance policies to determine how a “claim” is defined and will be interpreted under the policy and applicable law. As we have seen, not all investigations and “claims” are treated the same across jurisdictions: the potential availability of insurance coverage will depend on the type of initiating document (a conflict letter vs. a subpoena vs. a search warrant vs. something else) and in some jurisdictions, whether wrongdoing is expressly alleged and against whom.

Whether companies and individuals can access insurance coverage for various types of government investigations remains an ever changing area of law worthy of continuing attention from policyholders and their counsel.

## **Footnotes**

[1] *Brown Goldstein Levy LLP v. Fed. Ins. Co.*, No. 22-1023, 2023 WL 3513693 (4th Cir. 2023).

[2] *Id.* at \*1.

[3] *Id.*

[4] *Id.*

[5] *Id.* at \*6.

[6] *Id.* at \*2.

[7] *Id.* at \*5.

[8] *Patriarch Partners, LLC v. AXIS Ins. Co.*, No. 16-CV-2277 (VEC), 2017 WL 4233078, \*4 (S.D.N.Y. 2017), *aff'd*, 758 F. App'x 14 (2d Cir. 2018).

[9] *Patriarch Partners, LLC v. AXIS Ins. Co.*, 758 F. App'x 14, 19 (2d Cir. 2018).

[10] *Id.*

[11] *Patriarch Partners, LLC v. AXIS Ins. Co.*, 2017 WL 4233078, at \*1.

[12] *Id.*

[13] *Id.* at \*4.

[14] *Id.* at \*5.

[15] See *MusclePharm Corporation v. Liberty Insurance Underwriters, Inc.*, 712 Fed. App'x. 745, 753 (10th Cir. 2017); *Ctr. for Blood Rsch., Inc. v. Coregis Ins. Co.*, 305 F.3d 38, 42 (1st Cir. 2002).

[16] *MusclePharm Corporation v. Liberty Insurance Underwriters, Inc.*, 712 Fed. App'x. at 750.

[17] *Id.* at 753.

[18] *Id.* at 749-50.

[19] *Id.* at 756.

[20] *Ctr. for Blood Rsch., Inc. v. Coregis Ins. Co.*, 305 F.3d at 42 (defining the term “claim” in relevant part to include “any judicial or administrative proceeding in which an insured(s) may be subjected to a binding adjudication of liability for damages or other relief.”

[21] *Astellas US Holding, Inc. v. Starr Indem. & Liab. Co.*, No. 17 CV 8220, 2018 WL 2431969, \*5 (N.D. Ill. 2018).

[22] *Id.*

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