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RELATED ACTS & INTERRELATED WRONGFUL ACTS – SIX DEGREES OF SEPARATION

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One of the most heavily-litigated issues between insurers and policyholders involves the issue of whether, in the context of claims-made and reported policies, two claims are "related" or "interrelated." The significance of this issue cannot be understated. It can arise in the context of two separate lawsuits being filed against the insured during a single policy period, thereby raising the issue of whether both lawsuits are limited to a single claim limit or two claim limits, or in the context of two separate claims, or lawsuits, that span two, consecutive claims-made policy periods.

If a lawsuit is filed against the Insured during Policy A's policy period and a second lawsuit is filed during the policy period of the very next policy, Policy B, and the two lawsuits are deemed to be "interrelated" or "related" pursuant to the provisions in the policies, the insured may be left with no coverage for the second lawsuit filed during the term of Policy B because the insurer will assert that (1) Policy A has been exhausted through payments of the first "related" lawsuit filed during the Policy A policy period, and no limits remain to cover the second, "related" lawsuit, (2) because of their "relatedness," the second lawsuit (or claim) is deemed to have been first made against the insured during Policy A's policy period, and any coverage that might apply to the second lawsuit must be determined pursuant to the terms and provisions of Policy A, which may be quite different from those in Policy B, or (3) because of their "relatedness," any notice of the second lawsuit is "late" and ousts the second lawsuit from coverage.

All three of these outcomes are unacceptable to policyholders, who contend that treating two separate lawsuits filed (or "claims made" against the insured) during two

[1] The analysis included herein represents contributions from all four authors, and the content of this paper and the observations expressed herein are not to be attributed to any one of them, individually, or collectively, and are also not to be attributed to their respective law firms or the clients of those law firms.

separate policy periods as “related” and, therefore, a single claim is inconsistent with a policyholder’s reasonable expectations of coverage, and also is incompatible with the very purpose of a claims-made and reported policy to cover claims that are “made” against the insured during the policy period. “Pushing back” a second lawsuit, or claim against the insured, into a prior – possibly now exhausted – policy based on some vague notion of “relatedness” or “interrelatedness”, terms that are typically undefined in the claims-made policies, is not contemplated by a policy form that is described as a policy covering claims “made” against the insured during the policy period.

Insurers contend that treating two separate lawsuits, though filed by different parties and involving different (or the same) causes of action, as a single, “related” or “interrelated” claim is consistent with the intent of claims-made policies to operate more narrowly than occurrence-based policies, and that the insured is only entitled to one policy limit per claim – not more than one. Without the “related” or “interrelated” policy provisions, a policyholder could, conceivably, obtain two claim or policy limits from two consecutive policies for the very same wrongful act or series of wrongful acts just because they were contained in lawsuits filed, or “made,” against the policyholder one year apart.

Most claims-made and reported policies contain provisions “deeming” claims involving the same “wrongful acts” to have been made on the earliest date on which any wrongful act or “related” wrongful act was reported under the policy during which the wrongful or related wrongful act was reported, or “any other policy providing coverage”:

> *"All Claims involving the same Wrongful Act or Related Wrongful Acts of one or more Insureds will be considered a Single Claim, and will be deemed to have been made on . . . the earliest date on which any such Wrongful Act or Related Wrongful Act was reported under this Policy . . . or any other policy providing coverage."*

Another “deemer” clause for “related wrongful acts” states:

> *“Claims alleging, based upon, arising out of or attributable to the same or related wrongful acts shall be treated as a single claim regardless of whether made against one or more than one of you. All such claims, whenever made, shall be considered first made during the policy period or any extended reporting period in which the earliest claim arising out of such wrongful acts was first made, and all such claims shall be subject to the same limits of liability.”*

And yet another:

> *“All Claims arising out of the same Wrongful Act and all Interrelated Wrongful Acts of the Insureds shall be deemed to be one Claim, and such Claim shall be deemed to be first made on the date of the earliest of such Claims is first made, regardless of whether such date is before or during*

the Policy Period. All Loss resulting from a single Claim shall be deemed to be a single Loss."

A common definition of "interrelated wrongful acts" states:

"Wrongful Acts which are based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any of the same or related or series of related facts, circumstances, situations, transactions or events."

This definition of "interrelated wrongful acts" appears in a policy that does not define the term "related," used in the definition, nor the phrase "circumstances, situations, transactions or events," leaving the courts to come up with their own tests and analyses to determine what constitutes a "related" or "interrelated" wrongful act (is a "related" wrongful act different from an "interrelated" wrongful act, for example?).[2]

As demonstrated in the case studies contained herein, many courts have struggled with identifying whether two claims, or two lawsuits, are "related" or "interrelated," and whether the second lawsuit (or an initial lawsuit followed by a regulatory investigation one year later) should be deemed to have been made during an earlier policy period, when the "related" first lawsuit was brought against the insured. Often, the second lawsuit, or claim, was brought by different plaintiffs, alleging different causes of action, seeking different relief, and may even involve a regulatory agency when the first lawsuit was brought by private plaintiffs.[3] Despite these facts, many courts have found two such suits to be sufficiently "related" due to a "common nexus" of facts, or "substantially similar" facts, or after the application of the "sufficient factual nexus" test or the "operative facts" test adopted by the court in *Emmis Communications Corp. v. Illinois National Ins. Co.,* 323 F. Supp. 3d 1012 (S.D. Ind. 2018), *aff'd,* 937 F.3d 836 (7th Cir. Aug. 21, 2019), discussed more fully below.

Case Studies of Various Situations Involving Potentially Interrelated Wrongful Acts, Related Wrongful Acts and Six Degrees of Separation

[2] One court, for example, has held that the terms "same," "essentially the same," and "related" as "so elastic, "so lacking in concrete content, that they import into the contract substantial ambiguities." *See, e.g., Community Health Center of Buffalo, Inc. v. RSUI Indemnity Co.,* 2012 U.S. Dist. LEXIS 28934, at *9-10 (W.D.N.Y. 2012).

[3] *See Am. Cas. Co. of Reading, P.A. v. Gelb*, 18 N.Y.S.3d 30,32 (App. Div. 2015) (rejecting argument that two claims were interrelated where the two proceedings, "while arising from the merger, are wholly different, with different parties, different allegations, and different causes of action.")

CASE STUDY NUMBER 1

Interrelated Wrongful Acts and Fraudulent Business Schemes

I. INTRODUCTION

While the vast majority of business transactions conducted daily worldwide are legitimate and at arms-length, it is also an unfortunate reality that many are not. News reports are filled with stories of Ponzi schemes, pyramid schemes and other fraudulent investing scams. The victims of these schemes are often preyed upon by a network of actors – bankers, lawyers, accountants, brokers, etc. - connected towards a common purpose and enterprise. The scheme often involves a common *modus operandi* but spanning large periods of time, multiple transactions in varied locations and of course, multiple victims each with unique losses in terms of their nature and amount.

State and federal courts nationwide are filled with lawsuits arising out of these fraudulent investment schemes. And of course, many of the defendants in those suits are insured under some sort of D&O or E&O liability policy, policies which no doubt contain some version of an "interrelated wrongful acts" provision, for example:

> *"All Claims involving the same Wrongful Act or Related Wrongful Acts of one or more Insureds will be considered a Single Claim, and will be deemed to have been made on . . . the earliest date on which any such Wrongful Act or Related Wrongful Act was reported under this Policy . . . or any other policy providing coverage."*

A common definition of "interrelated wrongful acts" might include:

> *"Wrongful Acts which are based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any of the same or related or series of related facts, circumstances, situations, transactions or events."*

The usual consequence of deeming a series of seemingly disparate wrongful acts as "interrelated" is that each claim arising out of such acts are treated as a single claim, meaning only policy limit applies to that claim. The policies at issue are typically claims-made policies that typically provide coverage only for claims first made during the given policy period. If disparate wrongful acts are deemed to be "interrelated," these provisions allow insurers to treat all such claims made against an insured as a single claim first made on the earliest date any such claim is made – typically narrowing the claim to a single policy period. This may impact either coverage under the policy at issue (i.e., push the coverage “back” to the policy that was on the risk at the time of the first wrongful act) or the limits of the policy itself (if all claims were made during the policy period.) Thus, a policyholder insured under a policy with a $500,000 per claim

limit could find itself limited to that one claim limit to satisfy hundreds, if not thousands, of claims arising out of the same scheme, claims brought by disparate victims alleging uniquely different damages. It should therefore come as no surprise that this issue has spawned a wide body of litigation over the interpretation of such "interrelated wrongful acts" provisions in the context of these fraudulent schemes. This discussion will provide a brief overview of some of those rulings, with emphasis on a fairly recent California federal court decision focusing on those issues.

II. GENERAL OVERVIEW

As with any discussion of how courts treat a given coverage issue, there are multiple factors that must be taken into account, including the language of the specific policy at issue and the facts of the case as applied to that language. And of course, courts have reached different results on seemingly similar facts and policy language. It is therefore somewhat of a challenge to arrive at a singular "black letter" statement of law that applies across the board to these so-called fraudulent business scheme cases. Nonetheless, there are some common principles courts have employed.

When terms such as “related” or “interrelated” are left undefined in the policy, they are commonly understood and used to broadly encompass both logical and causal connections (see, e.g., *Bay Cities Paving & Grading, Inc. v. Lawyers’ Mut. Ins. Co.* (1993) 5 Cal.4th 854.) In applying this principle to fraudulent business scheme cases, courts have found relatedness where "[e]ach underlying claim was based on a “common business decision.” (*Associated Industries Insurance Company v. Brad Williams, LLC,* 2018 U.S. Dist. LEXIS 84721 (S.D. Miss., No. Div. 2018.) The existence of a common business decision (a *modus operandi*) is often enough to tip the scales in favor of a finding of relatedness, i.e., when an insured is accused of defrauding separate claimants in separate instances using the same basic scheme. Some courts have found a common *modus operandi* to be a strong factor in finding relatedness. For example, in *Am. Commerce Ins. Brokers, Inc. v. Minn. Mut. Fire & Cas. Co.,* 551 N.W.2d 224 (Minn. 1996) an employee of the insured embezzled nearly $200,000 from the company over a one year period using the same method each time. The insured submitted a claim under its Employee Dishonesty coverage, which contained an "interrelated wrongful acts" limitation. The Minnesota Supreme Court applied the provision, noting "[w]e cannot so restrict the plain and ordinary meaning of the word 'related' such that acts of embezzlement which follow each other in time, take place at the same business, and are committed by the same employee are not 'related' as that word is commonly used. Rather, the phrase 'series of related acts' is intended to encompass a continuous embezzlement scheme in which the dishonest employee converts funds from an employer by a common scheme on a constant basis."

Thus, courts have found interrelatedness where the claims were based on the same misleading statement (*Zunenshine v. Exec. Risk Indem., Inc.,* No. 97 Civ. 5525(MBM), 1998 WL 483475, at *5 (S.D.N.Y. Aug. 17, 1998), aff'd, 182 F.3d 902 (2d Cir.1999); the same agreement to sell stocks (*Home Ins. Co. of Ill. (N.H.) v. Spectrum Info. Techs., Inc.,* 930 F.Supp. 825, 850 (E.D.N.Y.1996); the same omissions in the same proxy literature (*Ameriwood Indus. Int'l Corp. v. Am. Cas. Co. of Reading, Pa.,*

840 F.Supp. 1143, 1152 (W.D.Mich.1993); and the same development of an industrial park and one party's attempts to interfere with the development (*Bensalem Twp. v. Int'l Surplus Lines Ins. Co.,* Civ. A. No. 91-5315, 1992 WL 142024, at *2 (E.D.Pa. June 15, 1992), *rev'd on other grounds*, 38 F.3d 1303 (3d Cir.1994.))

The court in *W.C. and A.N. Miller Development Co. v. Continental Casualty Co.,* 814 F. 3d 171 (4th Cir. 2015) distinguished claims related due to a "common scheme" from claims that were unrelated by a mere "common motive." In that case, the insured was sued in 2006 and again in 2010, both suits arising out of the same transaction. The court concluded that the conduct alleged in the lawsuits shared a common nexus of fact and were therefore interrelated wrongful acts. The two lawsuits were held to be linked by a multitude of common facts, a common transaction, and common circumstances. Thus the court held "[t]hese elements logically and causally connect the two lawsuits. . . . "an alleged scheme involving the same claimant, the same fee commission, the same contract, and the same real estate transaction." The court rejected the insured's attempts to avoid this "straightforward conclusion" by characterizing the allegations in the two lawsuits as alleging merely a "common motive" which is insufficient to establish the interrelatedness of the 2006 and 2010 lawsuits.

In *Morden v. XL Specialty Ins.,* 903 F. 3d 1145 (10th Cir. 2018), the insured was the subject of an SEC investigation prior to the policy, followed by a later-filed securities suit. The insured, an investment adviser, was involved in four separate investments alleged to have been gone bad. These four investments were different in nature. They involved investment opportunities in a software company, a real estate lender, a shell company and a literal gold mine. In addition, each of the investors were different. However, the court observed that the investments "share[d] common threads." In all four, "[c]lients were promised too much, not warned of risks, and not informed of conflicts of interest of their advisers, who had undisclosed stakes in the ventures." First, the court noted that the test for relatedness is "quite broad." Next, it noted that the wrongful acts were committed "by the same entity, against the same victims, using the same techniques (understating risk, overstating upside potential, and concealing financial interests of the advisers)." Because the SEC action and subsequent civil complaint alleged a common "scheme," the Tenth Circuit held they were related.

The United States District Court *Nobilis Health Corp. v. Great American Ins. Co*., H-17-2386 (S.D. Tex. 2018) reached a similar result. In Nobilis, the insured was a publicly-traded healthcare corporation. Near the end of the policy period, an anonymous blogger posted an article on a website claiming that the company was overvalued. As a result of that posting, the company's stock dropped. While the policy was still in place, a class of stockholders filed suit against Nobilis alleging, among other things, that it overstated its revenues. The case was voluntarily dismissed. Noblis was sued in another class action following the expiration of the policy, alleging that it overstated its net income and lacked effective internal financial controls. Finally, a third class action was filed against Nobilis alleging Nobilis's financial statements "provided the investing public with a misleading view of Nobilis' revenues, expenses, and general business operations." Great American denied coverage for the second and third class

action suits as being made after the policy period. The court found in the insured's favor, noting that "Related Wrongful Acts" is "broadly defined" and that [a]ll three lawsuits contain allegations that Nobilis' financial statements were misstated, false, misleading, and/or inaccurate." The court noted that the carrier "focus[ed] on minute differences" such as the fact that the later class actions made additional allegations regarding accounting errors. Ultimately the court held the clause applied to "any common fact" and found the common allegations to be sufficient to trigger the clause. Interestingly enough, this was actually a victory for the policyholder in that as a result of the court's ruling, all of the lawsuits, even those filed after the policy period, were deemed related and thus one claim, all which were covered under the policy. This case illustrates the "shifting sands" policyholders and their insurers may find themselves on when confronted with an "interrelated wrongful acts" conundrum.

In *Gregory v Home Insurance Co.,* 876 F. 2d 602 (7th Cir 1989) the insured was sued in a class action arising out of an offering for sale of episodes in a videotape series. Investors brought claims against an attorney alleging that he misrepresented the status of videotapes as securities; and the tax consequences of investment in videotapes.

The court found these acts sufficiently related to constitute a single claim under the policy. With respect to the claims involving the tax advice rendered by the insured, the court held "[it] is easy to decide that all the class claims arising from Mr. Gilbert's mistaken advice on the investment program's tax advantages are treated as a single claim under Paragraph IV of the policy, and therefore are subject to the $500,000 limit." As for the securities violation allegations, the court examined the three documents drafted by the insured in connection with the offering and found there to be "no question that these documents and Gilbert's acts in drafting them are 'related.'" It was clear to the court that the documents were "interdependent components of a single plan." The court further found that the insured's advising the investors of the tax and security law consequences of its offering, specifically his alleged failure to tell them that its offering was a security and should be registered, was also a related act, "by any plain and ordinary meaning of 'related.'"

Finally, the Ninth Circuit found that although two suits "were filed by two different sets of plaintiffs in two different fora under two different legal theories, the common basis for those suits was the WFS business practice of permitting independent dealers to mark up WFS loans." Thus, the relationship between the two claims was not so "attenuated or unusual" to prevent the insurer from treating them as the same claim (*WFS Financial, Inc. v. Progressive Cas. Ins. Co., Inc.,* 232 Fed.Appx. 624 (9th Cir. 2007.)

As can be seen from the above, courts in a wide variety of jurisdictions and as the state and federal level apply a somewhat broad definition of "relatedness" that is often used to connect seemingly disparate claims, suits, facts and damages where there is a common scheme and *modus operandi* to each. This brings us to a California federal court decision that weaved together many of these themes - *Liberty Ins.*

Underwriters, Inc. v. Davies Lemmis Raphaely Law Corp., 162 F. Supp. 3d 1068 (C.D. Cal. 2016) ("Davies.")

III. The Davies Decision

In Davies, the insureds were a transactional real estate firm that represented clients involved in purchasing, selling, transferring, and/or syndicating ownership, leasing, and financing of commercial properties. The firm served as counsel for a licensed California real estate broker that facilitated real estate investment partnerships. They were insured under three successive professional "claims-made-and-reported" liability policies issued by Liberty. Each of the policies defined "wrongful act" as "any actual or alleged act, error, omission or personal injury which arises out of the rendering or failure to render professional legal services." With regard to multiple claims, the policies stated:

> *"Claims alleging, based upon, arising out of or attributable to the same or related wrongful acts shall be treated as a single claim regardless of whether made against one or more than one of you. All such claims, whenever made, shall be considered first made during the policy period or any extended reporting period in which the earliest claim arising out of such wrongful acts was first made, and all such claims shall be subject to the same limits of liability."*

Between 2011 and 2013, seven cases were filed against the insureds and its real estate broker related to 23 transactions which occurred between December 2003 and November 2009. Each of those actions involved a similar alleged scheme - in the course of negotiating a property acquisition transaction, the defendants made a false representation to plaintiff-investors that the sellers would pay all commissions relating to the transaction, when in reality the purchase price of the property was marked up to include a commission payment. The plaintiffs in the underlying actions alleged that they relied upon these misrepresentations in choosing to invest.

All of the underlying actions alleged that the insured participated in the drafting of the offering memoranda and other documents relating to the proposed investment and had knowledge of the alleged misrepresentations and materials omissions but failed to disclose them. With the exception of one action, each of the plaintiffs alleged that they had an attorney-client relationship with the insured and that the insured failed to properly disclose actual or potential conflicts or properly represent the interests of the plaintiff-clients. All of the underlying actions included the same causes of action.

Each property acquisition at issue was completed on a different date, purchased from a separate seller, and on different terms from each other acquisition. The purchase agreements were negotiated at different times with 21 different sellers represented by 21 different law firms. Each of the underlying actions were filed by the same law firm representing these various investor-plaintiffs.

The issue was whether the underlying actions should be considered a single claim for purposes of the 2010-2011 policy's per-claim limit. Ultimately the court found that the seven claims were a single claim, related to the first suit filed in 2011.

The court first noted that California courts have found multiple claims to be sufficiently related where the underlying actions are in service of a "single plan" (*McWethy v. California Ins. Guarantee Ass'n,* No. G035992, 2006 Cal. App. Unpub. LEXIS 5785, 2006 WL 1793640, at *1 (Cal. Ct. App. June 30, 2006 - an attorney hired to prepare a client's will and trusts fraudulently made himself beneficiary and trustee of the trust, and distributed large amounts of stock to himself and his daughter after the client's death; court found that separate allegations relating to (1) exercising undue influence on the client before his death and (2) fraudulent receipt and sale of the stocks should be treated as a single claim as the wrongful acts were considered "both logically and causally related to each other as part of a single plan to obtain . . . a large share of [the estate]." The court noted that that all injuries ultimately arose from defendant's violations of his fiduciary duty to the single deceased client; *Flowers v. Camico Mut. Ins. Co.,* No. A134890, 2013 Cal. App. Unpub. LEXIS 4091, 2013 WL 2571271, at *2 (Cal. Ct. App. June 12, 2013) - an accounting firm failed to protect and guard against an embezzlement scheme perpetrated by its Chief Financial Officer; court found that the firm's acts, errors, and omission were "related", reasoning that "in every instance, the allegations against the Firm remain[ed] the same, that is, the Firm repeatedly failed to detect and guard against Hillyer's embezzlement scheme, which resulted in the same injury to the plaintiffs, namely, the loss of their funds."

Notably, both of these cases cited by the Davies court involved harm to a single victim, albeit through a series disparate acts. Nevertheless, the court noted 9th Circuit decisions finding that claims were sufficiently related even where "the suits were filed by two different sets of plaintiffs in two different fora under two different legal theories" (citing *WFS Fin., Inc. v. Progressive Cas. Ins. Co., supra,* and *XL Specialty Ins. Co. v. Perry,* No. CV 11-02078-RGK JCGx, 2012 U.S. Dist. LEXIS 109341, 2012 WL 3095331, at *8 (C.D. Cal. June 27, 2012) - underlying actions from multiple plaintiffs deemed to be related where the allegations were based on defendant-company's consistent policy of recklessly issuing high-risk mortgages.) The court similarly noted decisions in other jurisdictions holding that "[c]laims may be related even if they allege different types of causes of action and arise from different acts" where there is "a 'single course of conduct' that serves as the basis for the various causes of action." (*In re DBSI, Inc.,* No. 08-12687 PJW, 2011 Bankr. LEXIS 2727, 2011 WL 3022177, at *4 (Bankr. D. Del. July 22, 2011); see also *Kilcher v. Cont'l Cas. Co.,* 747 F.3d 983, 989 (8th Cir. 2014) ("a court may consider several factors in concluding whether dishonest acts are part of a 'series of related acts,' including whether the acts are connected by time, place, opportunity, pattern, and, most importantly, method or modus operandi."); *Cont'l Cas. Co. v. Wendt*, 205 F.3d 1258, 1264 (11th Cir. 2000) - a "single course of conduct" "aimed at a single particular goal" establishes relatedness.)

Following this analysis, the court held:

"In this case, while the Underlying Actions have been brought by different plaintiffs, they all arise from a single course of conduct, a unified policy of making alleged affirmative misrepresentations to investors in order to induce them to invest in commercial real estate acquisitions facilitated by AMC.

. . .

The Underlying Actions all allege the same misrepresentations and omissions by Defendants in the same form relating to similar or identical investments and properties. In deciding to invest in AMC's commercial property transactions, the plaintiffs in the Underlying Actions all uniformly relied on written memoranda and other documents prepared by DLR which contained alleged misleading statements and omissions regarding inflated purchase prices and hidden commissions." (Davies at 1078.)

The court distinguished these facts from those found in *Financial Management Advisors, LLC v. Am. Int'l Specialty Lines Ins. Co.,* 506 F.3d 922, 925 (9th Cir. 2007) where the Ninth Circuit found that fraudulent misrepresentation claims brought by "unrelated investors, with unique investment objectives [who] were advised at separate meetings on separate dates, according to their unique financial positions" were not sufficiently related as to constitute a single claim. In contrast, in Davies, the underlying actions were all ultimately based on the same alleged uniform policies and/or reckless actions of the insured and its client. At the end of the day, the Davies court strictly followed the "causal-or-logical connection" approach adopted by the California Supreme Court in Bay Cities, supra.

The Ninth Circuit affirmed this ruling in an unpublished decision on December 26, 2017, held that "[w]hile the underlying actions are not causally related, they are logically related to each other by the “common purpose or plan”—a scheme to incentivize investments by signifying that sellers would pay commissions, while hiding the fact that the price of the investment included the commissions. . . . The district court did not err in concluding that this common plan satisfied the related conduct language in the policy."

The Davies case thus represents yet another in a series of decisions in which courts have found relatedness based on a common plan, scheme or *modus operandi*, regardless of the number of suits, claims, plaintiffs and disparate damages alleged.

IV. CONCLUSION

Claims-made policies are purposefully intended to provide a more narrow scope of coverage than occurrence-based policies so that insurers can more predictably measure the windows under which their policies may be implicated. Claims-made insurance allows for a close match between premium dollars and claims. Shortly after the expiration of a claims-made policy, an insurer can close its books and determine its

profit or loss. Interrelated wrongful acts provisions preserve the essential workings of claims-made policies, and allow insurers to rightfully deny coverage for claims that are not actually first made during a given policy period.

The court's reasoning in *Davies* may seem logically counterintuitive to the notion that separate wrongful acts that produce separate harms are "related." However, the focus on a common scheme is often all that is required from a legal standpoint. Courts have discussed the difference between a "common motive" (a common purpose amongst disparate acts often different in scope and time) and a "common scheme" (often involving the same claimant, contract, transaction, or outcome) when attempting to determine relatedness. When the only connection between the acts is the furthering of some general business practice or intent, courts are less likely to relate multiple acts based on this common motive. Alternatively, a common scheme is more likely to result in a "common fact, circumstance, situation, transaction, or event" between multiple acts and result in a logical or causal connection that runs throughout the events.

CASE STUDY NUMBER 2

WHAT HAPPENS WHEN A COMPLEX SET OF FACTS, INCLUDING MULTIPLE SECURITIES LAWSUITS AND SIMILAR ACTIONS, RESULTS IN A DISAGREEMENT AMONG INSURANCE COMPANIES OVER THE EXISTENCE OF "INTERRELATED WRONGFUL ACTS"?

WHEN A COURT FINDS POLICY WORDING TO BE "ABSURD" AND "NONSENSICAL"

Emmis Communications Corp. v. Illinois National Ins. Co., 323 F. Supp. 3d 1012 (S.D. Ind. 2018), *aff'd,* 937 F.3d 836 (7th Cir. Aug. 21, 2019).

The *Emmis* decision illustrates the limits of the "interrelated wrongful acts" exclusion and arguments for their application offered by insurers. The decision is noteworthy not only for its recognition of the boundaries of such exclusions, but also for its unusual appellate history.

I. Factual Background

As the district court recognized, the facts of *Emmis* are "voluminous." The significance of this *Emmis* decision regarding relatedness turns on an understanding of those facts, which are summarized below.

A. The 2010 Go-Private Attempt

In 1999, Emmis issued Preferred Stock with certain rights and protections under Emmis's Articles of Incorporation. Ten years later, in 2010, when the value of Emmis's common stock had dropped, its CEO and largest shareholder Jeff Smulyan proposed a go-private transaction (the "2010 Go-Private Attempt"). Smulyan formed a company, JS

Acquisition, LLC ("JSA"), to acquire all of Emmis's common stock. Alden Global Distressed Opportunities Master Fund ("Alden"), a minority holder of Emmis Preferred Stock, agreed to finance the 2010 Go-Private Attempt.

Under the proposed terms of the 2010 Go-Private Attempt, JSA would purchase the Common Stock at a premium and the Preferred Stock would be converted into subordinated debt. Although the Emmis Board of Directors approved these terms, a group of Preferred Stock holders threatened to block the transaction. JSA negotiated an agreement with the Preferred Stock holders to remove their objections. However, Alden withdrew its commitment to finance the transaction. As a result, the 2010 Go-Private Attempt failed.

Litigation followed.

1. Shareholder Suits: Before the transaction collapsed, Emmis shareholders filed seven separate putative class actions alleging that the proposed terms "undervalued the shares of Emmis and the approval of it constituted a breach of fiduciary duty" by Emmis's directors. 323 F. Supp. 3d at 1017.

   The Shareholder Suits were reported under Emmis's D&O policy issued by Chubb for the policy period October 1, 2009 to October 1, 2010 (the "Chubb Policy"). Chubb accepted coverage. All Shareholder Suits were dismissed after the 2010 Go-Private Attempt failed.

2. The JSA Suit and Alden Action: In September 2010, JSA sued Alden for breach of its agreement to finance the Go-Private Attempt (the "JSA Suit").

   Alden (a Preferred Stock holder) responded in February 2011 with a derivate action against Emmis's Board of Directors (the "Alden Action"). Alden claimed that Emmis's Board had breached its fiduciary duties to agreeing to financially support the JSA Suit.

   Emmis reported the Alden Action to its D&O insurers for the period October 1, 2010 to October 1, 2011. Chubb, one of the insurers for this policy period, accepted coverage for the Alden Action. Chubb determined that "the Alden Action and the Shareholder Suits were Related Claims because they both 'emanated from the proposed buyout by JSA – *i.e.*, the 2010 Go-Private Attempt.'" *Id.*at 1018.

B. The Preferred Stock Transactions

In June 2011, Emmis (flush with cash after selling some radio stations) embarked on a successful effort to gain control over its Preferred Stock. This was accomplished through a series of transactions, including Amendments to the Articles of Incorporation,

which affected the rights of the Preferred Stock holders. The shareholders approved the amendments as recommended by the Board.

More litigation ensued.

Several Preferred Shareholders sued Emmis and its officers and directors (the "*COF Suit*"). The *COF Suit* alleged that the transactions resulting in Emmis gaining control over the Preferred Stock violated federal securities laws, Indiana corporate law and were breaches of fiduciary duty. The original and amended complaints in the *COF Suit* alleged that gaining control of the Preferred Stock was the result of Smulyan's frustration with the failed 2010 Go-Private Attempt.

Emmis's broker, Marsh, reported the *COF Suit* under Emmis's D&O policy issued by Illinois National Insurance Co. ("INIC") for the period October 1, 2022 through October 1, 2012. Marsh also reported the *COF Suit* under the 2009-10 and 2010-11 D&O Policies referenced above, including the 2009-10 Chubb Policy that covered the *Shareholder Suits* and *Alden Action*. Chubb and INIC both denied coverage.

II. Coverage for the COF Suit

Emmis successfully defended the *COF Suit* and then sued INIC to recover its defense costs.

A. INIC Policy Provisions

INIC argued that coverage was barred for the *COF Suit* under each of the three subsections of its Policy's "Specific Investigation/Claim/Litigation Event or Act Exclusion." That exclusion barred coverage for

> (i) any of the Claim(s), notices, events, investigations or actions listed under EVENT(S) below (hereinafter "Event(s)"); or (ii) the prosecution, adjudication, settlement, disposition, resolution or defense of: (a) Event(s); or (b) any Claim(s) arising from the Event(s); or (iii) any Claim alleging, arising out of, based upon, attributable to or in any way related directly or indirectly, in part or in whole, to an Interrelated Wrongful Act (as that term is defined below)."

The INIC Policy defined "EVENT" to include "all notice of claim or circumstances as reported under" the Chubb Policy.

The Policy defined "Interrelated Wrongful Act" as "(i) the same or related facts, circumstances, situations, transactions or events alleged in any of the Event(s), and/or (ii) any Wrongful Act(s) that are the same or that are related to those that were alleged in any of the Event(s)." *Id.* "

A "Wrongful Act" was defined as:

(1) any actual or alleged breach of duty, neglect, error, misstatement, misleading statement, omission or act or any actual or alleged Employment Practices Violation or Third–Party EPL Violation ... or
(2) with respect to an Organization, any actual or alleged breach of duty, neglect, error, misstatement, misleading statement, omission or act by such Organization, but solely in regard to a Securities Claim

B. District Court Rejects INIC's Arguments

The court rejected all of INIC's arguments. For purposes of this paper, we focus on the court's rejection of one argument, *i.e*., that the *COF Suit* and the *Shareholder Suits* or the *Alden Action* were "Interrelated Wrongful Acts" and therefore barred under subpart (iii) of the exclusion.

When Emmis notified Chubb, its policy had expired by this time, and Chubb denied coverage for the second lawsuit on the ground that the suit **was not related** to the earlier suits arising from the first, failed "go private" effort. Emmis also notified its current D&O insurer, INIC, which denied coverage for the second suit on the basis that the 2012 suit **was related** to the earlier suits filed in 2010. INIC's primary basis for denying coverage was an exclusion for "Interrelated Wrongful Act[s]," which, as stated above, were defined as "the same or related facts, circumstances, situations, transactions or events alleged in any of the Event(s)." *Id.* at *7. INIC asserted that, in the 2012 complaint, the aggrieved shareholders described Emmis' efforts to take the company private in 2010 and also noted that the 2012 effort was designed to achieve the same goal as the 2010 effort. *Id.* at *6, 11-12. Asserting that the allegations in the 2012 and earlier actions were therefore "logically connected," INIC argued that the 2012 lawsuit arose out of the "facts, circumstances, situations, transactions or events" at issue in the 2010 complaints.

The District Court acknowledged that there were "overlapping factual allegations" between the *COF Suit* and the *Shareholder Suits*. The court reasoned that if the provision "were to be applied literally, it would mean that any shared factual allegation would be sufficient to trigger the exclusion, including the allegation that Emmis is a publicly-traded corporation, or even simply that Emmis does business in Indiana." *Id.* at 1026. The court thus determined that it "would be nonsensical" and "absurd" to read the provision in such a way that would make coverage dependent on the whim of the plaintiff's attorney who drafted the complaint in the lawsuit." *Id.*

Instead, the Court found that subpart (iii) "must be read to exclude only those claims that share operative facts with the *Shareholder Suits* and/or the *Alden Action*; that is, facts that form the basis of the causes of action asserted in the lawsuit. *Id.* The Court found that Emmis's alleged frustration with the failed 2010 Go-Private Attempt and alleged desire to punish the Preferred Stock holders were not relevant to the claims asserted in the *COF Suit*. The Court rejected a "broad application" of subpart (iii). The Court concluded as follows:

> The Shareholder Suits were filed to stop the 2010 Go–Private Attempt, which involved an attempt by JSA to purchase all of Emmis's Common Stock and convert its Preferred Stock into subordinated debt instruments. The Alden Action involved the decision of Emmis to finance a lawsuit related to the 2010 Go–Private Attempt. Section (iii) excludes claims in which someone seeks to hold the insureds liable for the actions or omissions that were at issue in the Shareholder Suits and/or the Alden Action or any actions or omissions that are logically connected to them. The COF Suit simply did not seek to do that. The only connection between the COF Suit and the other suits is that the 2010 Go–Private Attempt is mentioned in the COF Suit as part of the historical context of the relationship between Emmis and its shareholders. That is not enough to bring the COF Suit under Section (iii) and exclude it from coverage.

Id. at 1029.

III. Appellate Proceedings: Seventh Circuit Reverses Then Affirms

On appeal, the Seventh Circuit initially issued a three-page opinion reversing the District Court. The Seventh Circuit found that the subpart of the exclusion barring coverage for claims "as reported" under the Chubb Policy was unambiguous and barred coverage for the *COF Suit.* The Seventh Circuit did not address the District Court's interpretation of the "Interrelated Wrongful Acts" exclusion.

Plaintiffs, joined by *amici curiae*, sought rehearing both by the panel and *en banc*. In what can only be described as a stunning reversal (and that appears to be unprecedented in the Seventh Circuit), the panel granted rehearing, withdrew its original opinion and summarily affirmed the judgment of the district court without opinion.

IV. Take-aways

- No matter how broad the exclusion, exclusions must be narrowly construed.
- Literal application of an "Interrelated Wrongful Acts" exclusion is inconsistent not only with narrow construction of the exclusion, but also with a common-sense application of the policy language.
- Overlapping facts that are not operative facts do not make separate claims or suits "Interrelated Wrongful Acts."
- The parties and court must focus on the claims asserted and the substance of the overlapping allegation, not merely the fact that such overlapping allegations exist.

CASE STUDY NUMBER 3

The Recent *NCAA* Decision

For various colleges, divisions and conferences, decision making is ongoing as to whether football will be played this fall -- or played at all -- as a result of the COVID-19 pandemic. While 2020 collegiate "fall ball" is still in question, whether the National Collegiate Athletic Association ("NCAA") is entitled to $25 million in excess liability coverage for class claims involving alleged violations of the Sherman Act is not – at least for now.

In a July 2020 decision, the Court of Appeals of Indiana in *National Collegiate Athletic Association v. Ace American Insurance, et al.*[4] recently sided with a group of excess insurers holding that they are not required to provide coverage for an underlying lawsuit (the *Jenkins*[5] suit) for claims involving rules used by member colleges and universities to provide financial assistance to student-athletes. The Court of Appeals applied a "Related Wrongful Acts" Exclusion to exclude coverage for the *Jenkins* lawsuit, which covered the same claims as a prior lawsuit (the *White*[6] lawsuit) previously fought by the NCAA.

By way of background, the underlying *Jenkins* lawsuit was filed on March 17, 2014, as a class action by which class plaintiffs (Division I football and basketball players) sought to enjoin the NCAA (and other defendants) from imposing any restrictions on the amount of money or other benefits that may be offered student-athletes by the association schools or anyone else. The *Jenkins* plaintiffs contested, as illegal under the Sherman Act, all NCAA rules that prohibit, cap, or otherwise limit the remuneration that players may receive for their athletic services, including specific NCAA Bylaws 12 (amateurism; prohibiting boosters, etc.), 13 (recruiting), 15 and 16.

In 2012, the NCAA purchased a series of primary and follow form excess liability policies to cover a two-year term. The NCAA made a claim and reported *Jenkins* to the various Insurers pursuant to the terms of the policies in effect at that time. The primary policy provided that the policy would pay on behalf of the NCAA "loss" arising from a "Claim" first made during the policy period and reported to the Insurer for any "actual or alleged 'Wrongful Act'" of the NCAA. "Wrongful Acts" was defined, in relevant part, to include any actual or alleged act, error, omission, misstatement, misleading statement, neglect or breach of duty for "violation of the Sherman Antitrust Act or similar federal, state or local statutes or rule." The primary policy was further subject to a Related Wrongful Acts Exclusion, which stated, in relevant part:

> IV. Exclusions
> The Insurer shall not be liable to make any payment for Loss in connection with a Claim made against the Insured:
>
> * * *

[4] No. 19A-PL-1313, 2020 Ind. App. LEXIS 298 (Ct. App. July 15, 2020).

[5] Cite

[6] *White v. NCAA*, Case No. CV06-0999 (C.D. Cal.).

> C. alleging, arising out of, based upon or attributable to the facts alleged, or to the same or Related Wrongful Act alleged or contained, in any Claim which has been reported, or in any circumstance of which notice has been given before the inception date of this policy, under any other management liability insurance policy, directors and officers liability insurance policy or any similar insurance policy of which this policy is a renewal or replacement or which it may succeed in time.

The primary policy defined "Related Wrongful Act" as:

> Wrongful Acts which are the same, related or continuous, or Wrongful Acts which arise from a common nucleus of facts. Claims can allege Related Wrongful Acts regardless of whether such Claims involve the same or different claimants, Insureds or legal causes of action.[7]

In response to *Jenkins*, the NCAA filed an insurance claim seeking coverage to fund its defense. The primary insurer denied coverage, citing the Related Wrongful Acts Exclusion, and finding that the *Jenkins* lawsuit involved the same Wrongful Acts as those in the earlier *White* action. Specifically, the primary insurer reasoned that both actions challenged the limitation on the amount of financial aid provided to Division I football and basketball players and asserted that the NCAA unlawfully agreed with other entities to cap the financial aid provided to student-athletes. Thus, the actions involved the same, related or continuous Wrongful Acts and/or Wrongful Acts which arise from a common nucleus of facts. Accordingly, *Jenkins* was deemed to have been first made in February 2006 when the *White* lawsuit was filed. The excess insurers relied on the primary insurer's denial to also bar coverage under the 2012-14 excess policies.

In response, the NCAA filed a Complaint for declaratory judgment and damages against the Insurers and the parties subsequently filed cross-motions for partial summary judgment on the NCAA's coverage claim. After a hearing, the trial court ruled in favor of the Insurers, finding (as quoted by the appellate court):

> The NCAA repeatedly draws overly fine distinctions regarding the related actions and deconstructs the language about different class action definitions and causes of actions, etc. The [c]ourt finds these analyses unavailing. The Related Wrongful Acts and prior notice provisions are unambiguous, the underlying claims are clearly all against one wrongful act,

[7] The primary policy also contained a "Notice/Claim Reporting Provision" that, as the appellate court noted, "aligns notice as to an initial and any subsequent 'same or … related" Wrongful Act.

> that is, the enforcement of Bylaws 15 and 16, first made in the White action, and coverage is barred under the policies.

The NCAA appealed that ruling and now faces the Court of Appeals affirmation of that ruling. Following are some of the key facts that the appellate court relied on to reach its ruling below.

White v. NCAA

The plaintiffs in *White* asserted an anti-trust complaint that challenged the NCAA's "Bylaw 15." At the time, Bylaw 15 set the cap on financial aid and provided that every student-athlete's scholarship must be limited to the cost of attending the university. The rule defined "cost of attendance" exclusively to mean tuition, fees, room and board, and required textbooks. The plaintiffs argued that the Bylaw's definition was less than the *actual* cost of attendance because it excluded incidental costs such as transportation or supplies, and it barred schools from providing health or accident insurance to athletes. Thus, the plaintiffs asserted the difference between the Bylaw's "cost of attendance" and the *actual* cost of attendance, collectively, as their damages.

The plaintiffs argued that the scheme of limiting each school's potential to offer aid and incentives was anti-competitive and violated the Sherman Act. They argued that, absent these regulations, "schools competing against one another to attract student-athletes… would increase the amount of financial aid available so that full athletic scholarships would, in fact, cover the full cost of attendance." The NCAA settled *White* in 2008, agreeing to expand "cost of attendance" to include certain incidentals, to enable universities to provide insurance for athletes, and to open a $218 million opportunity fund for student-athletes with financial need. Throughout this litigation, the NCAA's fees and liability were covered by its then-existing liability insurance.

Jenkins v. NCAA

Jenkins commenced several years later as a similar action by student-athletes that essentially broadened *White*'s anti-trust theory. Where *White* focused on Bylaw 15, *Jenkins* attacked "all NCAA rules that prohibit, cap, or otherwise limit the remuneration that players may receive." The complaint described the NCAA's arrangement as a set of "**cartel agreements** with the avowed purpose and effect of placing a ceiling on the compensation that may be paid to those players for their services." Also, rather than money damages, the *Jenkins* plaintiffs sought declaratory and injunctive relief, seeking to enjoin the NCAA from enforcing any restrictions on what money or benefits could be offered to student-athletes.

Arguments on Appeal

On appeal, the NCAA disputed the application of the Related Wrongful Acts Exclusion and argued that such a literal and broad application of the exclusion "would

negate virtually all coverage" and defeat the purpose for which the NCAA obtained the policies. Alternatively, the NCAA also argued that even if the exclusion was not ambiguous, the *Jenkins* and *White* claims were unrelated and not factually connected, but involved separate allegations of wrongdoing. Interestingly, the NCAA sought to support its argument that the exclusion was overbroad and imprecise by likening it to Indiana's precedents on application of pollution exclusions and advocating for the court to apply jurisprudence regarding environmental pollution to the policy language at issue. Relying on precedent in the environmental pollution context, the NCAA claimed that the exclusionary language at issue was overbroad, ambiguous, and failed to give policyholders objective guidance in its application. In defining "related" as "associated; connected," the NCAA argued that every Wrongful Act is "related" to every other Wrongful Act" as every act by the NCAA is associated or connected because the NCAA committed them all.

The court found the NCAA's reliance on the environmental pollution precedent "without merit to the situation" before it, rejecting the arguments and noting that well-established Indiana law is clear that case law interpreting policy language in one policy is inapplicable to different language in different policies and the NCAA's reliance on such case law was "misplaced." The Court found that both suits were attacks on the same framework of the NCAA policy (*i.e*., the cap on student-athlete remuneration). Moreover, it noted that plaintiffs in *Jenkins* specifically cited the *White* settlement in their complaint, arguing that it had failed to curb the anti-competitive restrictions at issue. The court opined that *Jenkins* was simply a broader iteration of the same claim in *White*, against the same alleged anti-competitive agreement, and the Wrongful Acts in both cases stemmed from a common nucleus of facts – the scholarship scheme imposed on student-athletes.

Given that the policy clearly provided for coverage on a claims-made basis, and that the policy provided for a Related Wrongful Acts exclusion, the court upheld the denial of coverage under the 2012-2014 policies. In doing so, the Court further pointed out that relating *Jenkins* back to the earlier 2006 policy did not result in a situation of "no coverage" for the NCAA, it merely placed coverage under the original policy in which the claim was first made.

With respect to the ambiguity argument raised, the appellate court cited to *Gregory v. Home Ins. Co.*[8] noting that a policy is not made ambiguous simply because the parties disagree on how it applies to a given situation, and the court's finding that the term "relate" was not ambiguous. Distinguishing the case of *Am. Home Assurance Co. v. Allen*,[9] which in analyzing the terms "interrelated wrongful acts" found the term "interrelated" to be ambiguous, the Court held the Related Wrongful Act exclusion was not ambiguous or overbroad. The Court's finding of no ambiguity will certainly be relied on by insurers in subsequent coverage claims just as the Court's distinguishing of precedent finding the term "interrelated" as ambiguous will, likewise, be relied on by policyholders in pursuit of covered claims.

[8] 876 F.2d 602 (7th Cir. 1989).

[9] 814 N.E.2d 662 (Ind. Ct. App. 2004).

It remains to be seen whether the NCAA will appeal this ruling further – and whether student-athletes will be showcasing their services in “fall ball” this year.