

Settlement Agreement Extends to Later Claims Covered by Scope of Release

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The United States District Court for the Eastern District of Virginia, applying Texas law, has held that a settlement agreement resolving coverage litigation released the insurer's obligation for defense costs for certain claims tendered for coverage under a subsequent policy. *Nat'l Heritage Found., Inc. v. Phil. Indem. Ins. Co.*, 2012 WL 5331570 (E.D. Va. Oct. 25, 2012).

A corporation overseeing the investment and distribution of charitable funds on behalf of donors was sued in 2005 for mismanagement of funds. The corporation's insurer denied defense and indemnity coverage for the suit, and the insured corporation filed for bankruptcy in 2009, assertedly as a result of the insurer's refusal to provide coverage for the suit. The corporation filed suit against the insurer for denial of coverage and sought consequential damages, including the corporation's bankruptcy costs. The insurer and the corporation settled the coverage litigation for \$18 million and executed a settlement and release. The release provided that the corporation released the insurer "from all claims, demands, causes of action, and damages asserted in, arising out of, or connected with" the 2005 lawsuit. The corporation then sought coverage for four matters under a directors and officers liability policy issued by the same insurer to the corporation in 2008, and the insurer contended that the earlier release applied.

The court held that the release for the settlement of the 2005 lawsuit applied broadly to any claim "arising out of" or "connected with" the 2005 lawsuit. The court further held that the release extended to claims that would not have occurred but for the 2005 lawsuit, including the insured's bankruptcy. The court then concluded that indemnification for two claims brought in the insured's bankruptcy proceeding was not encompassed within the terms of the release because they did not arise out of the 2005 lawsuit as they were not causally related to the bankruptcy. The court reasoned that these two claims—alleging fraudulent inducement to invest with the insured and breach of fiduciary duty—were not causally connected to the 2005 lawsuit and subsequent bankruptcy because they could have been brought even if the insured had not filed for bankruptcy. The court, however, held that the defense costs incurred in defending these suits were covered by the release for the 2005 lawsuit because the insured sought these defense costs as damages in its 2005 lawsuit.

Second, the court held that defense costs for defending against a late-filed proof of claim in the bankruptcy proceeding were causally related to the bankruptcy, and thus fell within the scope of the release, because these defense costs were incurred in dismissing the proof of claim "pursuant to the bankruptcy rules that bar

tardy notice of claims.”

Finally, the court held that the release applied to defense costs associated with the appeal of the corporation's bankruptcy plan “because these defense costs exist only as a result of the bankruptcy proceeding” and were therefore casually connected to the consequential damages sought in the 2005 lawsuit for the insured's bankruptcy.