

Notice-Prejudice Rule Inapplicable to Claims-Made Policy Under Delaware Law; Claims Not Related

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The Connecticut Superior Court predicted that the Delaware Supreme Court would hold that an insurer that issued a claims-made policy is not required to show prejudice to assert a late notice defense. *Southridge Capital Mgmt., LLC v. Twin City Fire Ins. Co.*, 2006 WL 2730312 (Conn. Super. Ct. Sept. 8, 2006). It also held that five cases for which insureds sought coverage did not relate back to a case filed prior to the applicable policy period.

A now-defunct insurer issued an investment company and D&O liability policy to a private investment advisory firm. In applying for the policy, the firm disclosed an action filed against it in 1998. That suit alleged that the entities related to the insureds "sold short" after converting debentures received as compensation for financing into stock. The application for the policy included a question about pending claims or litigation and stated, "it is agreed that if the [policyholder] has knowledge of any such fact or circumstance or if such pending or prior claim or suit exists, then any claim or suit arising therefrom shall be excluded from coverage under the proposed policy." The policy required notice as soon as practicable and no later than 60 days after the claim was first made.

The policyholder sought coverage for five lawsuits filed against it in 2001. The lawsuits arose out of private equity transactions by the firm. The lawsuits generally alleged that the firm financed other companies in return for stock in the companies, and that the firm then manipulated the price of the other companies' stock by "short selling" in order to profit from the alleged manipulation of the stock price. The insurer denied coverage for four of the underlying actions on the grounds that they were related to the pre-policy period 1998 action disclosed in the policy application but advanced some of the defense costs incurred in the fifth action. The firm filed the instant action seeking a declaration as to its rights under the policy.

On cross-motions for summary judgment regarding coverage under the policy, the court first addressed the relationship of the underlying actions to the 1998 action disclosed on the policy application. The court concluded that the issues presented were issues of first impression under Delaware law. With respect to the related claims provisions in the policies, the court held that the insurer did not establish that the underlying

actions for which the plaintiffs sought coverage related back to the pre-policy period action disclosed in the application process. After analyzing cases discussing "relatedness," such as *Continental Cas. Co. v. Wendt*, 205 F.3d 1258 (1st Cir. 2000) and *Lehigh Valley Health Network v. Executive Risk Indemnity, Inc.*, 2001 WL 21505 (E.D. Pa. 2001), which applied similar language yet reached varying results, the court concluded that "[i]t is likely impossible to reconcile all of the results... such that each is consistent with a single set of principles." The court explained, however, that "courts have analyzed the 'relatedness' of claims, in situations where policy language is similar if not identical to that here, in an effort to make the process as objective as possible" by focusing on factors such as whether (1) the parties are the same, (2) the claims all arise from the same transaction or transactions, (3) the alleged wrongful acts are contemporaneous and (4) there is a common scheme or plan.

Analyzing these factors, the court noted that the later actions were brought by different claimants, the 1998 action was withdrawn before the alleged wrongful acts in the other actions were allegedly committed, the defendants in the 1998 action were different than those in the later actions and the specific allegations regarding the financing arrangements varied from action to action. Based on these differences, the court concluded that it did "not believe that the underlying actions are all related closely enough to [the 1998 action] such that they should all be deemed to be a single claim."

Regarding late notice, the court first concluded that the Delaware Supreme Court would not require an insurer to establish prejudice before denying coverage based on late notice. The court reasoned that a Delaware trial court had so concluded, that the Delaware Supreme Court had previously recognized fundamental differences between claims-made policies and occurrence-based policies and that the weight of case law from other jurisdictions establishes that prejudice is immaterial to the question of late notice in the claims-made context.

Applying the notice provision in the policy, the court concluded that coverage was unavailable for four out of the five underlying actions because of late notice. The court also rejected the policyholder's argument that the insurer waived the late notice issue, concluding that "[g]eneral reservations of positions regarding coverage do not constitute waivers of defenses as to coverage, because waiver requires the intentional relinquishment of a known right."