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Insured Takeaways From 10th Circ. Interrelated Claims Ruling

By **Michael Stockalper** (January 19, 2024, 4:55 PM EST)

The U.S. Court of Appeals for the Tenth Circuit's recent broad application of Oklahoma law on "interrelated acts" and "interrelated claims" creates concerning precedent for policyholders seeking to maximize coverage under a professional liability policy with per claim limits.

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In this regard, careful preloss planning and policy modifications may prevent unexpected coverage gaps and avoid surprise exposure. In addition, post-loss strategic planning may prove critical to maximize recovery depending on the applicable state law.

Background on Interrelated Acts and Interrelated Claims Policy Language

Interrelated acts and interrelated claims provisions may bear on the scope of available coverage in a variety of ways.

For example, in claims-made policies, where the policy covers only claims that are first made against the insured during the policy period, a claim against the insured found to be interrelated to a claim in a different policy period may affect whether coverage applies at all.[1]

Additionally, interrelated claims or interrelated acts provisions may also bear on available limits or deductibles, to the extent that a policy is subject to per claim limits or has a per claim deductible.

In that sense, if two or more claims are deemed interrelated, then a policy with larger aggregate limits may only provide coverage under a single per claim limit, resulting in less recovery for the insured.

On the other hand, if the insured is only required to pay a per claim deductible, then interrelated claims will lessen the insured's costs in obtaining coverage.

Historically, courts were more inclined to adopt pro-insured interpretations of the term "interrelated," particularly where left undefined in the policy. In such situations, courts often simply defaulted to the maxim that ambiguities in insurance policies must be interpreted in favor of the insured.[2]

Perhaps due to this judicial proclivity, modern policies now almost always define the phrases "interrelated acts," "interrelated claims" and "interrelated wrongful acts" with more particularity.[3] This has resulted in clearer direction in terms of policy interpretation, but also sometimes less favorable results for insureds.

Now typically, whether a series of acts or claims will be interrelated becomes inherently a fact-specific inquiry, which gives courts wide discretion to apply law to facts.

To that end, one would imagine that in close cases a "tie goes to the insured" axiomatic approach would carry through to maximize coverage and avoid forfeiture of policy benefits.

However, this is not necessarily so, as observed in the subject case for this article: American Southwest Mortgage Corp. v. Continental Casualty Co. in the Tenth Circuit.[4]

Multiple Audits, Multiple Years — Interrelated Acts?

In American Southwest, two lending companies lost millions after relying on inaccurate reporting from an auditing company — the insured — which failed to detect that the borrower falsely represented it had collateralized loans.

The court held that the auditor's three separate audit reports of the borrower mortgage company's finances in 2014, 2015 and 2016, predicated on a failure to review source documentation to detect company fraud, amounted to interrelated acts under a professional liability policy.

As such, the court **found** in October that only $1 million in per claim limits were available under the auditor's policy, since interrelated acts could support only one claim, notwithstanding that the policy had up to $3 million in aggregate limits and the audits were conducted in three separate years.

The court further held that multiple claims arising from any single audit year were interrelated claims to also limit per claim recovery to a single limit, irrespective of the number or type of claimants — here, two different lenders.

The Policy Language

The Continental Casualty policy language at issue defined "[i]nterrelated acts or omissions" as "all acts or omissions in the rendering of professional services that are logically or causally connected by any common fact, circumstance, situation, transaction, event, advice or decision."

In looking solely at whether the audits were logically connected — as this was, to the court, a dispositive analysis — the court held that each audit report was logically related because the same common facts and circumstances tied the recurring negligent acts together. Namely, there "was one Auditor — one who performed the same service for the same clients three times."[5]

Each time, the auditor made the same error and perpetuated the same fraud scheme. The court distinguished seemingly applicable prior authority authored by now U.S. Supreme Court Justice Neil Gorsuch, where the Tenth Circuit held that an insured's negligence in structuring a corporate stock sale was not interrelated with its misrepresentations associated with the release of a deed of trust.[6]

In addition, the policy defined "interrelated claims" as "all claims arising out of a single act or omission or arising out of interrelated acts or omissions in the rendering of professional services."

In that regard, the court found that the claims all arose out of the same audit for each given year and were thus interrelated as well, even though there were two separate lending companies relying on the audits.

The court was unconvinced that because each lender was owed a separate duty of care, this had any bearing on the fact that the conduct at issue related to the same audit.

The court determined that despite the $3 million in aggregate limits, only $1 million in per claim limits were available.

The Takeaway

This decision is concerning for policyholders insofar as one would think that an auditor performing discrete audits in separate years would constitute separate and unrelated acts.

In that regard, the court could easily have made available multiple per claim limits either within a single audit year or, at a minimum, across multiple audit years.

For instance, in RLI Insurance Co. v. OutsideIn Architecture LLC, the U.S. District Court for the Middle District of Florida construed similar logically or causally connected policy language in September.

The court held that a demand letter against an architect threatening to expose the architect for permit violations regarding upcoming demolition work was not interrelated with an eventual lawsuit

based on a worker's death during the demolition phase at the same project site.[7]

Given the factual situation before it, the Tenth Circuit could have come to a similar conclusion, if anything, drawing upon the factual differences from audit year to audit year.

Given this decision, companies with a similar exposure seeking to maximize per claim limits may want to explore options to negotiate manuscript policy language, if available, to limit the application of an interrelated acts provision, or perhaps to define terms slightly differently — e.g., to remove the "logically related" language.

However, considerations should also be taken into account in terms of how such policy modifications could affect other aspects of coverage, such as applicable per claim deductibles or self-insured retentions.

Notably, the lack of potential for interrelated acts relative to a per claim self-insured retention could increase an insured's out-of-pocket expenses before accessing coverage.

In the alternative, policyholders should always consider a thorough examination of choice-of-law issues to determine if another more favorable state's law may apply.

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[1] See e.g. Zurich American Ins. Co. v. UIP Companies LLC , No. 19-vc-1818, 2021, WL 602901 (D.D.C. Feb. 16, 2021) (held that an insurer properly denied coverage under claims-made policy for related lawsuits based on policyholder's failure to give timely notice of the original claim — a demand email sent during the 2017 policy period, which was adjudged related to lawsuits filed during the 2018 policy period).

[2] See e.g. Home Ins. Co. of Illinois (New Hampshire) v. Spectrum Information Technologies, Inc. , 930 F.Supp. 825, 848 (E.D. N.Y. 1996) (finding that where the term "interrelated" was undefined required a construction in favor of the insured); Atlantic Permanent Fed. Sav. & Loan Ass'n v. American Cas. Co. of Reading, Pa. , 839 F.2d 212, 219-20 (4th Cir.1988) (holding that several different acts were interrelated and explaining that "Virginia law requires us to construe all ambiguities in insurance contracts against the insurer and in favor of coverage").

[3] See Stauth v. National Union Fire Ins. Co. of Pittsburgh , Nos. 97-6437, 97-6438, 1999 WL 420401 (10th Cir. June 24, 1999) (discussing insurers' efforts to further define the phrase).

[4] American Southwest Mortgage Corp. v. Continental Casualty Co. , 84 F.4th 910 (10th Cir. 2023) (Oklahoma law). https://law.justia.com/cases/federal/appellate-courts/ca10/22-6071/22-6071-2023-10-16.html

[5] Id. at 915.

[6] See Professional Solutions Insurance Co. v. Mohrlang , No. 09–1286, 2010 WL 325903 (10th Cir. Jan. 29, 2010). https://law.justia.com/cases/federal/appellate-courts/ca10/09-1286/09-1286-2011-03-14.html.

[7] See RLI Ins. Co. v. OutsideIn Architecture LLC , No: 8:20-cv-2395-CEH-AEP, 2023 WL 5840590 (M.D. Fla. Sept. 11, 2023)
