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True or False? Claims-Made Policies Cover the Cost of Complying with Subpoenas

By Nicholas R. Maxwell

Ever since insurance companies began routinely selling claims-made insurance coverage in the 1980s, policyholders and their insurance companies have argued over what constitutes the "claim" needed to trigger the policy's insuring agreement. This dispute arises frequently in today's business world, as more and more D&O and E&O policyholders are forced to defend against investigations by government regulatory agencies. While the Trump administration's promises of regulatory relief may portend some easing on this front, the long-term trend probably points toward continued vigorous enforcement.

Given the seriousness of such investigations and the glacial pace at which they often proceed, policyholders can end up incurring millions of dollars in legal fees before formal legal proceedings even begin. One of the most frequent and expensive mechanisms with which policyholders must comply are mandatory subpoenas from government regulators.

It is typical insurance industry practice to deny coverage for legal fees incurred responding to a subpoena. This practice has led to a slow but steady stream of new judicial decisions on the subject. By keeping abreast of this case law, policyholders can anticipate the likelihood of coverage for complying with a particular subpoena, and negotiate the most favorable policy language in future renewals.

The single most important factor in assessing coverage is, of course, the policy language. While claims-made policies for many years actually did not define "claim,"[1] the vast majority of D&O and E&O policies now define the term. Assuming there is not a formal proceeding triggering other subparts of a typical definition of "claim," the policyholder generally must show that it has received a "written demand" for "nonmonetary relief," and that the demand alleged a "wrongful act" by the policyholder. A wrongful act is typically defined to mean an actual or alleged act, error or omission committed in the course of the policyholder's business.

Did the Subpoena Demand Nonmonetary Relief?

Whether there was a written demand is generally not controversial, but different courts have taken sharply divergent positions on whether the demand seeks the necessary "relief." In *Minuteman Int'l, Inc. v. Great Am. Ins. Co.*, for example, the Securities and Exchange Commission issued multiple subpoenas to the policyholder, demanding testimony and document production, and the poli-

Nicholas R. Maxwell is an attorney at Anderson Kill whose practice concentrates in corporate and commercial litigation, insurance recovery, exclusively on behalf of policyholders, and in environmental and employment law. He is admitted to the New York and New Jersey Bars.
(212) 278-1161 | nmaxwell@andersonkill.com

cyholder incurred legal fees complying with the subpoenas.[2] The court emphasized that if the policyholder had not complied, the SEC could have brought suit to enforce the subpoenas and secure the testimony and documents, which the court deemed a form of relief. Accordingly, the court held that the "subpoenas were demands for relief in that they were demands for something due."

In *Diamond Glass Cos. v. Twin City Fire Ins. Co.*, the court addressed the same claim language as in *Minuteman Int'l*, in a situation where the policyholder had received multiple grand jury subpoenas to provide documents and testimony.[3] Explicitly declining to follow *Minuteman Int'l*, the court held that requiring the insurance company to cover the policyholder's compliance with the mandatory subpoena, "notwithstanding the absence of any assertion of civil or criminal liability against Diamond or any of its directors or officers …[,] would be absurd."

Minuteman Int'l and *Diamond Glass* show how unpredictable courts can be on coverage for compliance with mandatory government-issued subpoenas, yet other cases show that there is still some rhyme or reason to the way courts reach their decisions in such highly fact-specific cases. In *Ctr. for Blood Research, Inc. v. Coregis Ins. Co.*, for example, the policy included an endorsement providing potential coverage for "nonmonetary claims" that otherwise would not fall within the claim definition.[4] However, the relevant definition of claim from the endorsement was limited to "any judicial or administrative proceeding in which any INSURED(S) may be subjected to a binding adjudication of liability for damages or other relief." Despite the policyholder's receipt of and compliance with a mandatory subpoena, as in *Minuteman Int'l* and many other cases finding coverage,[5] the subpoena clearly did not constitute a "judicial or administrative proceeding" in which the policyholder could be held liable; accordingly, the court ruled against the policyholder.

Courts seem to be beginning to recognize that in today's world, D&O and E&O policyholders can incur significant cost before ever being indicted or subjected to civil enforcement proceedings. Corporate policyholders cannot reasonably protect their interests without capable counsel to comply with government-issued subpoenas. Moreover, competent representation in the early stages can inure to the insurance company's benefit by convincing the regulators not to commence an action or seek an indictment. Nonetheless, insurance companies still argue that proceedings prior to an indictment/enforcement action, no matter how involved and lengthy, are not claims. Accordingly, policyholders must analyze the specific language of their subpoena, and the circumstances surrounding its issuance, to demonstrate to a court that the government has sought the relief necessary to meet the relevant definition.

Did the Subpoena Allege a Wrongful Act?

Certain courts have held, and insurance companies often argue, that even if a mandatory government-issued subpoena demands specific relief, that alone does not make it a claim. Indeed, subpoenas can sit anywhere on the spectrum from clearly alleging unlawful conduct by the recipient, to seeking information solely in order to pursue a third party. The degree of connection between the policyholder and the government's investigation can be key.

In *Agilis Benefit Servs., LLC v. Travelers Cas. & Sur. Co. of Am.*, for example, the insurance company argued that mandatory subpoenas from a U.S. attorney were "mere requests for information," and on their face did not actually accuse the policyholder of wrongdoing.[6] The court, noting that the subpoenas identified the policyholders as "parties of interest" and referenced "contraband," rejected the insurance company's argument and reiterated that "a government investigation is a serious matter."

The court in *ACE Am. Ins. Co. v. Ascend One Corp.* also took into account the subpoena as well as related circumstances to determine whether the government had alleged the requisite wrongful acts by the policyholder.[7] The court emphasized the typical enforcement function of the government agency issuing the subpoena and the fact that the subpoena was captioned "In re: [policyholder]" to hold in the policyholder's favor.

Courts will also sometimes look to circumstances outside the subpoena itself to divine whether the policyholder is being accused of wrongdoing or is a mere bystander enlisted to further the government's investigation of a third

party.[8] Policyholders must analyze how most strategically to tell their story when seeking coverage for the costs reasonably incurred in complying with government-issued subpoenas.

What States' Laws Might Govern a Potential Insurance Coverage Dispute?

As shown by the case law discussed above, courts have not reached a consensus on what is and is not a claim, and most jurisdictions do not even have an appellate decision setting forth general principles. Nonetheless, if multiple states' laws are potentially in play, it could be in the policyholder's best interest to avoid one particular jurisdiction or seek out another. Policyholders must also be intimately familiar with the underlying facts of the cases on which they rely, even when citing cases from other jurisdictions.

Conclusion

Policyholders have much to gain by closely assessing the key indicators of coverage for subpoena compliance costs, both from their policy language and from the language of the subpoena itself and surrounding circumstances. With millions of dollars in legal fees potentially on the line, the devil is in the details.

ENDNOTES

[1] See, *e.g.*, *Polychron v. Crum & Forster Ins. Cos.*, 916 F.2d 461 (8th Cir. 1990).

[2] No. 03-cv-6067, 2004 U.S. Dist. LEXIS 4660, at *5-6 (N.D. Ill. Mar. 18, 2004).

[3] No. 06-cv-13105, 2008 U.S. Dist. LEXIS 86752 (S.D.N.Y. Aug. 18, 2008).

[4] 305 F.3d 38 (1st Cir. 2002).

[5] See, *e.g.*, *Syracuse Univ. v. National Union Fire Ins. Co. of Pittsburgh, Pa.*, No. 2012EF63, 2013 N.Y. Misc. LEXIS 2753 (Sup. Ct. Mar. 7, 2013), aff'd, 112 A.D.3d 1379 (4th Dep't 2013); *Protection Strategies, Inc. v. Starr Indem. & Liab. Co.*, No. 13-cv-00763, 2013 U.S. Dist. LEXIS 187451 (E.D. Va. Sept. 10, 2013); *Dan Nelson Auto. Grp., Inc. v. Universal Underwriters Grp.*, No. 05-cv-4044, 2008 U.S. Dist. LEXIS 4987 (D.S.D. Jan. 15, 2008); *Richardson Elecs., Ltd. v. Fed. Ins. Co.*, 120 F. Supp. 2d 698 (N.D. Ill. 2000).

[6] No. 08-cv-213, 2010 U.S. Dist. LEXIS 144499, at *40 (E.D. Tex. Feb. 24, 2010).

[7] 570 F. Supp. 2d 789 (D. Md. 2008).

[8] *Ascend One Corp.*, 570 F. Supp. 2d at 797.