Strategies for Defending the Insurance Agent/Broker E&O Claim, and Application

I. Introduction

Defending the insurance agent/broker E&O claim can present both a number of challenges and opportunities. On the negative side of the ledger, the fact is that while it remains a recognized obligation on the part of the insured to read his/her policy in most if not all jurisdictions in the U.S., the prevailing view is that the failure to read policy documents does not present a bar to claims for negligent failure to procure, or failure to advise. The failure on the part of the insured to read his/her policy can be raised as a defense based on a comparative fault analysis. But only in a handful of remaining states can it be cited as an absolute bar to the making of such claims. Additionally, in the vast majority of jurisdictions an agent/broker is not viewed as a fiduciary, owing a duty to advise the insured as to what types of insurance to purchase, at what limits, absent a “special relationship” or “special

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As we look forward to the start of Spring, I want to take a moment to thank everyone in the Professional Liability Insurance Committee ("PLIC") for their participation. This has thus far been a terrific year, and we look forward to keeping the momentum going into the Spring.

In November, the Committee provided its contribution to the ABA Tort Trial & Insurance Practice Section ("TIPS") Journal Annual Survey on the Law, contributing a section addressing developments in 2017 in the area of professional liability and directors and officers liability. This Annual Survey edition of the TIPS Journal is an impressive, law review level collection of articles, and the content submitted with regard to professional liability and D&O.

Also in November, PLIC issued its Fall 2017 Newsletter. The Fall Newsletter included articles on successful mediations in securities class actions, the six most critical concepts that drive the process of a successful mediation, and the insurer perspective on mediation.

In January, PLIC co-sponsored a D&O Insurance Cyber Liability Forum held at the St. John’s University School of Law New York City campus. The event featured a discussion of officers’ and directors’ liability and coverage issues, and the resolution of same following a hypothetical cyber-attack and data breach. Speakers included Jay Kramer, a partner at Lewis Brisbois who had formerly been Special Counsel for the FBI in its Office of General Counsel and currently heads up the Lewis Brisbois Cyber Incident Response Team. Additional speakers included Christopher Liu, Head of Cyber Risk for the AIG Financial Institutions Group, Adeola Adele, Director of Integrated Cyber Solutions and Thought Leadership at Willis Towers Watson, and Rich Sheridan, Senior Vice President and Chief Claims Officer at Berkley Cyber Risk Solutions. Attendance exceeded our expectations, and there was substantial interaction between the panels and the audience throughout. Just altogether a terrific event.

In February, during our monthly conference call, we were treated to a presentation from Marygrace Schaeffer of DecisionQuest on how to understand and craft trial presentations that appeal specifically to the Millennial Juror. In March, we are planning to have Thomson Reuters present on e-discovery processes and procedures, and what can be done to deal with the massive growth of electronically stored information and the need for discovery of social media in a comprehensive, yet targeted and cost-effective manner. This presentation will be held on March 13th, at 11:00 AM Eastern Time.
In May, we’re looking forward to a tremendous slate of programs at the TIPS Section Conference in Los Angeles. For those of you attending, we are planning to host a dinner for members of our Committee. If you are planning to attend, please reach out to me (at pbiging@goldbergsegalla.com) to let me know so I can make the appropriate reservations.

Thank you all again for your active participation in PLIC. I look forward to working with you all to keep the momentum going with the committee throughout the rest of the year, and getting a chance to break bread with you at the TIPS Section Conference in May.

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Issue Preclusion in Shareholder Derivative Litigation

The Delaware Supreme Court, once again addressing questions of issue preclusion in the context of shareholder derivative litigation, has rejected suggestions by the Chancery Court that giving preclusive effect to initial, unsuccessful efforts to litigate demand futility violates the Due Process rights of shareholders attempting to bring a subsequent action elsewhere. California State Teachers’ Retirement System, et al. v. Aida M. Alvarez, et al. and Wal-Mart Stores, Inc., No. 295, 2016 (Del. Jan. 25, 2018), 2018 WL 547768. According to the Court, such issue preclusion does not necessarily violate Due Process rights, at least where the various plaintiffs have a common interest and legal representation is adequate in the initial action.

The Chancery Court Proceedings

This matter arose out of a series of derivative actions filed both in Arkansas and Delaware against a large corporation. Multiple actions were consolidated in federal district court in Arkansas, and those actions were ultimately dismissed due to failure to allege demand futility. The actions filed in Delaware were likewise consolidated but proceeded more slowly, due in part to the fact that plaintiffs initially filed a books and records demand that had led to a Section 220 Delaware General Corporation Law proceeding alleging deficiencies in the defendant corporation’s production. By the time that action was resolved and a consolidated derivative complaint was filed in Delaware, the Arkansas action had been dismissed. The defendants accordingly moved to dismiss the Delaware action based on collateral estoppel with respect to demand futility. The Chancery Court granted that motion and the plaintiffs appealed.

On appeal, the Delaware Supreme Court ultimately issued a remand order, which asked the Chancery Court to address the following question:

In a situation where dismissal by the federal court in Arkansas of a stockholder plaintiff’s derivative action for failure to plead demand futility is held by the Delaware Court of Chancery to preclude subsequent stockholders from pursuing derivative litigation, have the subsequent stockholders’ Due Process rights been violated? See Smith v. Bayer Corp., 564 U.S. 299 (2011).

On remand, the Chancery Court observed that its prior decision was based in part on consideration of the Due Process issue, noting case law nationally generally supported the notion that Due Process rights of the subsequent shareholders were...
The following is the Professional Liability Insurance Committee’s first Industry Spotlight piece. The honor goes to Carrie Graziani who is a Manager, Specialty Claims for Hanover Insurance Company’s Management Liability group in Itasca, Illinois.

**How did you first become involved in working in the insurance industry?**
After law school, I had a brief stint at a plaintiff’s class action law firm. I quickly found that plaintiff’s work was not for me and got an associate position with a local insurance defense and coverage firm. I really enjoyed the challenge of coverage litigation and continued as an insurance side coverage attorney, moving to a second firm and continued that path. I had an opportunity to go in house with a carrier and handle D&O and EPL and took it for the change in career paths. I use my coverage background on a daily basis and still enjoy the challenge of deciding sophisticated coverage issues.

**2. How did you end up gravitating to D&O/Management Liability Claims?**
I gravitated toward D&O/Management Liability because of the challenge of dealing with businesses and guiding business decisions. I think that with D&O, especially private company and non-profit D&O, our Insureds may have small businesses with sophisticated issues. I like helping them maneuver through ensuing litigation and truly helping them to understand the issues. Additionally, with business decisions, there is typically not a black and white right or wrong. More often than not, it’s a gray area, which makes it challenging and interesting. No two cases are the same or create the same issues.

**3. What types of insureds and claims do you see in Hanover’s D&O/Management Liability book and are there particular trends you see as developing issues of concern?**
Hanover Insurance Company writes middle market and small company private D&O and non-profit D&O. Typically, our policies are package policies with D&O, EPL, crime, fiduciary and cyber. We see a myriad of claims in all of those books, but our
biggest source of claims is EPL. Due to the recent newsworthy sexual harassment claims, as well as the more recent changes to the ADA, we have seen a significant uptick in those areas. I believe that Management Liability’s biggest exposure is EPL. More Plaintiffs firms are taking on EPL issues and we have seen much bigger demands and the use of the news as pressure to get bigger dollars.

4. What do you envision as becoming more prevalent issues in the D&O/Management Liability area over the next 5 years?
I think we will continue to see an interest and interplay between cyber coverage/claims and other coverage parts, including in the D&O/Management Liability space. I am not sure how cyber will play out in the next 5 years, but I do think that there could be industry changes in this growing and amorphous area and it could affect the other coverages or become a part of other coverages, changing the dynamics we are used to today. We are already seeing how cyber has changed Crime and D&O, but I think it could be more influential in other Management Liability coverage areas as well.

5. What do you see as absolutely critical to appropriate management of the tripartite relationship?
Communication is essential. Communication with Insureds to understand their role and participation is key. Sometimes, the breakdown of that piece can cause an Insured to think there is some untoward strategy, when it really is just a lack of understanding. Additionally, communication with counsel about the defense of the case only also is a factor. It is essential to leave counsel out of any coverage discussion, even when it comes to strategy on settlement. I think blurring the lines on coverage issues and strategy issues can get a carrier into trouble.

6. The word is that you’re a big NHL fan. What’s your prediction for the Blackhawks this year?
I am a true hockey fan, and a Blackhawks fan. I hate to say but I don’t think it is their year. The playoffs are looking to be pretty questionable at this point, which will be the first in some time. I think a lot of Hawks fans have started using the old Cubs’ adage, “maybe next year”!
Mitigating Losses through Agent E&O Policies – Tips for Title Insurers and Their Counsel

1. Introduction

For some time now, many title insurers have used independent agents to provide title, closing, and escrow services in connection with real estate transactions. These agents include title companies, escrow companies, closing service vendors, and attorneys in private practice. When a claim is made under a title insurance policy for a title defect, or a claim is otherwise asserted against a title insurer for problems or irregularities relating to the transaction or title, sometimes the problem is or may be the fault of the agent.

When the agent is or may be at fault, the title insurer is faced with the decision of whether to assert an indemnity claim against the agent to recoup or mitigate its loss. This decision is often a sensitive issue, as title insurers typically enjoy good, longstanding business relationships with their agents and do not wish to frustrate those relationships or develop a reputation for suing or asserting claims against their agents. But sometimes, particularly when the loss is large or the conduct at issue is egregious, the title insurer decides the circumstances warrant pursuing a claim.

Practically speaking, however, the typical goal of the title insurer is to recoup or mitigate its loss not necessarily by seeking indemnity from the agent, but instead by triggering exposure under the agent’s errors and omissions (“E&O”) insurance policy. The agent itself may not be collectible, or easily collectible, and recovery or contribution from the agent’s E&O policy is the most efficient way to mitigate the loss.

This article discusses some basic concepts and practical tips for title insurers and their counsel when attempting to mitigate their losses by triggering exposure under an agent’s E&O policy. There are several precautionary steps a title insurer can take prior to a loss to increase the chances of triggering exposure under an agent’s E&O policy (such as requiring each agent to have certain types and amounts of E&O coverage), which are beyond the scope of this article. Instead, this article is limited to addressing certain post loss steps for title insurers to take that will increase the chances of successfully mitigating the loss by obtaining recovery or contribution from an agent’s E&O policy.

J. Scott Slater, Esquire

J. Scott Slater is a founding member of Slater Grant in Wesley Chapel, Florida. Scott defends professionals who have been accused of committing malpractice, breaching fiduciary duties, or violating ethical obligations.
2. Draft the Claim with the E&O Policy in Mind

Before sending a demand or filing a suit against an agent, the title insurer needs to be mindful of the coverages and—perhaps more importantly—the exclusions in the agent’s E&O policy. The goal is to draft the claim in such a way as to maximize both the liability of the agent for the underlying problem and coverage under the E&O policy. Sometimes the title insurer is at the mercy of the underlying plaintiff: If that plaintiff has asserted the claim in such a way as to give the E&O carrier readily identifiable policy defenses, there may not be much that can be done to rectify the situation. But if that has not happened, a title insurer should not hastily draft an indemnity claim against the agent without considering likely E&O policy defenses. Doing so can risk describing the claim in such a way as to destroy coverage, which could put the title insurer in the ultimate position of having the agent itself as the only source of recovery.

2.1 Obtain the E&O policy

In order to carefully prepare a demand or suit against the agent with the E&O policy in mind, it obviously helps to have the E&O policy in hand. If the title insurer does not already have a copy of the agent’s E&O policy as part of its risk management practices, it needs to make efforts to get a copy.

A prudent practice is to send formal correspondence to the agent that generally describes the underlying claim or issue that presents a risk of loss for the title insurer, generally asserts that the agent is or may be responsible for the problem, demands that the agent notify its E&O carrier, and demands the name of the carrier and a copy of the applicable insurance policy to be provided by a date certain. Some states have statutes that provide a procedure for such a demand and require both the insured and the liability insurer to provide this and other information (such as potential coverage defenses) within a certain time frame, such as 30 days.²

2.2 Try to avoid implicating coverage defenses and exclusions

If the title insurer is able to obtain a copy of the applicable E&O policy, then it should read it carefully for the scope of coverage and exclusions. If the title insurer is unable to obtain a copy of the policy, then it should still consult resources—and perhaps sample E&O policies for other similar agents—that can educate the title insurer and its counsel on typical coverage limitations and exclusions in E&O policies. Although the specifics of E&O policies vary, many of them that are issued to agents who work with title companies have similar terms and conditions.³

Below is a brief discussion of some of the most common coverage defenses and exclusions in agent E&O policies.
2.1.1 Fraud or intentional acts

Title insurers should expect that most E&O policies for agents will have an exclusion for fraud, intentional misconduct, and criminal behavior. Such an exclusion typically has language similar to this:

**Criminal, Dishonest or Fraudulent Wrongful Acts or Knowing Violations of the Rights or Laws.** We won’t cover loss that results from any criminal, dishonest, or fraudulent wrongful act or any knowing violation of rights or laws committed by: The protected person, or Anyone with the consent or knowledge of the protected person.

Examples of such conduct by an agent are loan fraud, embezzlement of escrowed funds, and intentionally ignoring certain title issues in order to benefit the agent or his client. Sometimes it is difficult to avoid, but if it is possible to describe the claim against the agent as being one in negligence or some other non-intentional tort, then that will increase the chances of avoiding this policy exclusion.

If the agent’s employee clearly engaged in a fraudulent or other intentional act, a common, prudent strategy to potentially avoid the fraud/intentional conduct exclusion is to assert claims against the agent company for negligence independent of the agent employee’s conduct (such as negligent supervision or hiring, or other negligence).

2.1.2 Breaching contract with, or instructions from, title insurer

Another common E&O policy exclusion is for breach of a contract or agreement. The key to avoiding this exclusion is for the title insurer to allege conduct of the agent that is a common-law or statutory tort or breach of duty independent from the agent’s obligations in its contract with the title insurer. Otherwise, an E&O carrier will likely be successful in avoiding exposure under the policy.

Similarly, E&O policies may exclude acts relating to an agent’s violation of a title insurer’s underwriting instructions or standards. Again, the key is avoiding allegations sounding in the agent’s failure to comply with an agreement or understanding with title insurer; instead, the allegations should focus on the agent’s independent negligence or tortious conduct.

2.1.3 Property “flipping”

E&O policies sometimes have an exclusion for claims related to “flip transactions”—where a property is purchased and then soon resold or “flipped” for a profit. These
provisions are sometimes very broad and exclude coverage for any claim arising out of or related to such a transaction, regardless of the circumstances. With this type of provision, there is not much the title insurer can do to avoid the exclusion—the only analysis is whether a flip transaction is involved. However, other policies exclude only claims involving “improper” participation or conduct of the agent in a flip transaction. For these policies, coverage can be triggered by avoiding allegations that the agent knowingly or wrongfully participated in the transaction.

2.1.4 Known title defects

Many E&O policies exclude coverage for title defects known to the agent at the time the title insurance is issued. Even if the agent mistakenly determines the issue is not a title defect, the exclusion can apply if it turns out the issue is, in fact, a title defect. In other words, the fact that the agent’s conduct is mere negligence does not matter; if the defect was known, the exclusion applies.

Therefore, if the title insurer does not know for sure that the agent was aware of the title defect prior to the title insurance being issued, the indemnity claim against the agent should avoid allegations that the agent knew about and failed to properly report or address the issue. Instead, the claim should sound in a failure to discover the defect, or at least should remain silent on the knowledge issue until the facts can be sorted out.

2.1.5 Personal profits or advantage

Another common exclusion applies to claims “based upon or arising out of [the agent’s] gaining any profit or advantage to which [the agent] is not legally entitled.” The title insurer’s indemnity claim against the agent should therefore avoid assertions that the agent’s conduct resulted in improper personal gain to the agent. Such assertions may add dramatic effect to the claim, but they risk negating E&O coverage. This is true even if the personal gain is not illegal, and the agent did not intend to improperly gain from the conduct.

3. Notify the E&O Carrier of the Claim Early and Often

3.1 Why to notify the carrier

Because the title insurer’s ultimate goal is to reach the agent’s E&O coverage, merely asserting a claim against the agent is not enough. The agent’s E&O carrier must be put on notice, and a claim against the E&O policy must be asserted. A title insurer is wise to not rely upon the agent itself to give the E&O carrier timely and sufficient notice; instead, the insurer itself should attempt to put the carrier on notice.
through its own efforts, in addition to demanding that the agent notify the carrier. Notice is that important. This is for three primary reasons.

3.1.1 Claims-made-and-reported policies

First, whether and when the E&O carrier is notified of the claim against the agent can be the difference between coverage and no coverage. Many agent E&O policies are of the "claims-made-and-reported" variety. This means that, during the policy period, the claim must be made by the title insurer against the agent and the agent must report the claim to the E&O carrier. Even if the title insurer asserted a claim during the policy period, an E&O carrier can escape exposure if the claim is not reported to the carrier during the policy period. Prompt notice to the agent’s E&O carrier is therefore crucial.

3.1.2 Prejudice

Second, if an E&O carrier is not timely and sufficiently notified of a claim against the agent, the E&O carrier can assert a defense to coverage based on alleged prejudice. Regardless of what type of policy is at issue (occurrence, claims-made, or claims-made-and-reported), the carrier can argue that late or insufficient notice has caused it to not be able to properly investigate, defend, and potentially settle the claim.

3.1.3 Voluntary payer

The third primary reason for notifying the E&O carrier of the claim against the agent is to avoid the “voluntary payer” defense. If the title insurer has paid a loss caused by the agent without first notifying and involving the agent’s E&O carrier, the carrier can argue that the title insurer did not assert an applicable policy defense—or some other defense—and thus became a volunteer in paying the loss. Stated differently, if there are valid defenses to the underlying claim against the title insurer, then the title insurer’s loss was not proximately caused by the agent; it was caused by the insurer not properly defending itself. Courts have recognized this as a valid defense to a title insurer’s indemnity claim against an agent.

Given the availability of the voluntary payer defense, title insurers are well-advised to notify the E&O carrier of the claim against the agent as early as possible, and then ask the agent and carrier if they believe any policy defenses (or other defenses) exist. The title insurer should seek to obtain a consensus amongst the three parties about the title insurers’ defenses. The title insurer should also notify and involve the E&O carrier and the agent in any settlement discussions with the underlying insured. The key is to give the E&O carrier and the agent every opportunity to “speak up” if they believe the title insurer should be handling the underlying claim differently.
3.2 How to notify the carrier

The title insurer should notify the agent of the claim and demand the agent notify its E&O carrier. But as stated above, the title insurer should not stop there. The agent may not promptly notify the carrier, and that has resulted in title insurer’s losing the opportunity to recover against the E&O policy. Although some policies require that the agent itself notify the E&O carrier in order to constitute proper notice, the title insurer should nevertheless ensure that it make its own independent efforts to notify the carrier as well. The more notice, the less opportunity for the carrier to claim prejudice or some other notice-based defense.

The title insurer should notify the agent’s E&O carrier through its own efforts by way of letters, emails, and other written correspondence. It should not rely on telephone conversations or voicemail. There needs to be written documentation. A letter by certified mail, return receipt requested, is preferable for the initial notification. If the title insurer has the E&O policy (see discussion above re: obtaining the policy), it should be sure to send at least the initial notification to the address and in the manner provided for in the policy.

There may be considerations that would warrant a title insurer—soon after its insured asserts a claim against it—filing suit against the agent and, if the jurisdiction allows, the E&O carrier directly. This is another means of notifying the E&O carrier, but should ideally be done in conjunction with written correspondence. Such a suit could be in the form of a third party claim in the underlying insured’s action against the title insurer, or in a separate action, depending on what the jurisdiction allows.

3.3 When to notify the carrier

For the reasons discussed above, a title insurer with an indemnity claim against an agent should notify the agent’s E&O carrier as soon as possible after the claim becomes known. This is the initial notice. Also, notification and communication with the carrier should continue thereafter when appropriate, including for the reasons discussed regarding the voluntary payer defense. Again, the goal is to keep the E&O carrier informed of important events regarding the underlying insured’s claim.

Additionally, there is at least one situation where the title insurer should ensure the agent’s E&O carrier is notified after the initial notification of important events regarding the title insurer’s indemnity claim. This is where the E&O carrier denies coverage pre-suit, but reserves the right to reevaluate the claim if a suit is filed and requests that the agent notify it if suit is later filed. In this situation, a court has held that coverage was voided under the E&O policy’s cooperation clause where the agent did not notify the carrier as requested (it did not do so until the lawsuit was
Therefore, a prudent title insurer will give an initial notice to an agent’s E&O carrier when the claim first becomes known, and then a second notice if and when the title insurer sues the agent. The title insurer should not rely on the agent to give the required notice.

4. Join Any Agent-Carrier Declaratory Judgment Actions

When a claim is asserted or threatened against an agent, and the E&O carrier disputes coverage under the policy, sometimes the agent or the carrier will initiate a declaratory judgment action to have a court resolve the coverage issue. When this happens, another helpful strategy for title insurers is to join the declaratory judgment action as a party. The title insurer and its counsel may be able to strengthen or supplement the arguments in favor of coverage, thereby increasing the chances of having the agent’s E&O coverage as a source of recovery.

Depending on the jurisdiction, the title insurer should normally have no problem demonstrating a right to join the declaratory judgment action. Indeed, some jurisdictions view the title insurer as a necessary party to the action, where the insurer has made it clear that it intends to hold the agent liable for any loss that it suffers due to the agent’s actions.

5. Be Mindful of the Statute of Limitations

A final note is that a title insurer with an indemnity claim against an agent—as any other plaintiff—should always be mindful of the statute of limitations and when the claim accrues. Some jurisdictions hold that the statute of limitations on such a claim does not begin to run until the title insurer pays a loss allegedly caused by the agent, not from the earlier time when the title insurer first learns that a problem has arisen that was potentially caused by the agent. However, title insurers should not take the risk and should seek to either file suit against the agent, or obtain a tolling agreement, no later than the earliest deadline for indemnity, contract, or tort claims in the applicable jurisdiction, assuming the clock begins to run from the date the transaction at issue closed. Being overly cautious here is worth it.

Additionally, title insurers should keep in mind that some of their agents—such as practicing attorneys and other “professionals”—may have shorter statutes of limitations in the applicable jurisdiction than other agents, such as title companies.

6. Conclusion

Claims and losses are inevitable in title insurance. Sometimes, title insurers are forced to make the difficult and sensitive decision of whether to seek indemnity from
their agents where the problem was caused by them. If the decision is made to go forward with such a claim, there are certain steps title insurers can take to increase the chances of a recovery against the agent’s E&O policy, which include the ones addressed above: draft the claim with the E&O policy in mind, notify the E&O carrier of the claim early and often, join any agent-carrier declaratory judgment actions, and be mindful of the statute of limitations.

Endnotes

1 The general term “agent” will be used throughout this article to refer to these independent agents.

2 E.g., section 627.4137, Florida Statutes.

3 Title insurers should keep in mind that agents who are attorneys will likely have professional liability policies that may be different from other, non-attorney agents. A discussion of the nuances of attorney professional liability policies is beyond the scope of this article.


6 Trumbull Ins. Co. v. Braunstein & Todisco, LLC, 2004 WL 1616441 (Conn.Super.) (unpublished) (duty to defend upheld despite exclusion for “any dishonest, fraudulent, criminal, intentional or malicious act, error, omission, or Personal Injury or deliberate misrepresentation”, when agent failed to inform underwriter of unrecorded contract to purchase insured property, but no fraud alleged).

7 Title Industry Assurance Co., R.R.G. v. Chicago Abstract Title Agency, 2015 WL 5675544 (E.D.Ill. 2015) (unpublished) (title agency was sued by two lenders and a title insurer for losses they suffered because an employee of the agency stole money from the company’s escrow account; court held that the carrier was required to defend the title agency, because the complaint alleged more types of conduct by the agent than the simple assertion of theft, such as negligent supervision of the escrow accounts); but see Chicago Title Ins. Co. v. Northland Ins. Co., 31 So.3d 214 (Fla. 4th DCA 2010) (exclusion for “damages arising out of the comingling, conversion, misappropriation or defalcation of funds or other property” was found to negate coverage when title agent delivered money to an attorney for a mortgage payoff and attorney stole the money, causing a policy loss; court drew no distinction between stealing of money by the title agent and the attorney, who was unaffiliated with the agent).

8 Northland Insurance Co. v. Stewart Title Co., 327 F.3d 448 (6th Cir. 2003) (Stewart Title sought indemnification from Northland for, among other things, agent’s breach of the underwriting agreement and other tortious conduct, including negligence; however, because duty breached in the asserted negligence was a duty created by the contract, there was no coverage under E&O policy).

9 Id.

10 Trumbull Ins. Co. v. Braunstein & Todisco, LLC, 2004 WL 1616441 (Conn.Super.) (unpublished) (E&O carrier relied on exclusion for any claim “arising out of any intentional breach of underwriting authority,” but court found complaint did not allege agent violated instructions, nor did it disclose what the agent’s underwriting authority was).

11 Those Certain Underwriters at Lloyd’s London v. GMC Land Services of Florida, Inc., 315 Fed.Appx. 785, 2009 WL 426096 (11th Cir. 2009) (broad exclusion for any claim involving a property flip was found to exclude claim, regardless of nature of agent’s conduct).

12 United Fire & Casualty Co. v. Realty Title Co., 2007 WL 428068 (W.D.Mo.) (E&O carrier found obligated to defend insured agent in lawsuit claiming that agent failed to detect loan fraud ring, including property flipping, despite a specific exclusion for “actual or alleged improper participation by any insured in any ‘flip transaction’”; use of term “improper” means not all participation negates coverage; here, mere negligence was alleged, not knowing participation).
13 United Fire & Casualty Co. v. Fidelity Title Ins. Co., 258 F.3d 714 (8th Cir. 2001) (E&O carrier successfully invoked an exclusion for “claims arising from defects in title of which the [agent] had knowledge at the date of issuance of such title insurance”; it was immaterial that the agent mistakenly believed the mortgage at issue did not constitute a defect in title).


15 National Title Agency, LLC v. United Nat’l Ins. Co., 2016 WL 1092485 (D Utah 2016) (personal-profits exclusion was broadly construed to negate coverage for claim that agent allowed the garnishment of its escrow account for agency company debts; exclusion was not limited to illegal gain).

16 First American Title Ins. Co. v. Continental Cas. Co., 709 F.3d 1170 (5th Cir. 2013) (no E&O coverage where error had occurred within policy term, and First American had made demand on agent to report the claim to E&O carrier, but agent failed to report claim during policy term).

17 E.g., Fidelity National Title Ins. Co. of Tennessee v. Kidd, 99 N.C.App 737, 394 S.E.2d 225 (N.C.App. 1990) (“If we determine, taking the evidence in the light most favorable to National, that the matters raised by the insureds were excluded from coverage, then National provided a defense and settlement funds to the insureds voluntarily, and the trial court correctly granted defendants’ motion for summary judgment. If National was not obligated to defend the insureds, then any negligence of the defendants could not have proximately caused National any harm.”); Title Ins. Co. of Minnesota v. Christian, 267 S.C. 71, 226 S.E.2d 240 (1976) (where title insurer sought to recover from attorneys who had prepared the defective title evidence, insurer’s summary judgment motion was denied where attorneys put forth a litany of policy defenses which the insurer overlooked or ignored, including that the commitment had expired, that the insured lender had actual knowledge of the missed prior lien, and that there was no evidence that the lender had funded the loan); Stewart Title Guar. Co. v. Virginia Commonwealth Title Co., 64 F.3d 659, 1995 WL 501354, 1995 U.S.App. LEXIS 23947 (4th Cir. 1995) (title insurer paid a claim based on a forged mortgage, but because insurer could not prove that the mortgage was, in fact, forged and thus unenforceable, the agent was not liable to the insurer).


19 Louisiana, for example, has a direct action statute. Id.

20 First American Title Ins. Co. v. Nat’l Union Fire Ins. Co. of Pittsburgh, Pa., 695 So.2d 475 (Fla. 3d DCA 1997).


22 E.g., American Title Ins. Co. v. First Commercial Title, Inc., 967 F.2d 583 (9th Cir. 1992).
circumstances.” But the terrain has shifted on this as well. Cases addressing when a special relationship or special circumstances exist giving rise to a duty to advise have evidenced an increasing willingness on the part of the courts to accept as a foundation of its analysis that insurance policies are inherently complicated, and that agents/brokers are often retained precisely for their expertise in assisting their customers in identifying insurance risks specific to their circumstances or business operations, and helping them tailor their insurance to protect them against same.

On the plus side of the ledger, courts continue to recognize that brokers are not guarantors of the risks faced by their customers, who are much better equipped to understand the value of their holdings, the impact a particular type of loss could realistically be anticipated to have on their business operations, their risk tolerance, and what they can afford and would be willing to pay to protect themselves against risk. In light of this, it is generally recognized that it would be unfair to charge agents/brokers with the responsibility to provide advice and guidance absent a truly special relationship or special circumstances. Further, it is not simply the obligation of the insured whose coverage fails to respond to a loss in whole or in part to point to the alleged failings of the agent/broker in order to establish liability on the agent/broker’s part for the uninsured loss. It remains the responsibility of the insured in proving its entitlement to relief to show that, but for the alleged negligence on the part of the agent/broker, the loss would have been covered under the policy in question. And to the extent the plaintiff had no coverage in place whatsoever, it is the burden of the insured to prove that insurance coverage for the loss would have been available, and if offered the insured would have been willing and able to pay for same.

Assuming proximate causation can be generally established, other arguments can be made to limit the value of the claims. For example, if an argument could be made that the claim would have been covered but for the agent/broker’s negligence, but the claim would have been treated as multiple claims with multiple deductibles, this can be an effective way to substantially limit the recoverable damages. As another example, if the coverage the insured claims should have been purchased would have actually been purchased, it may be valid to argue that the policy would have been far more expensive. The additional premiums would have to be subtracted from the value of the claim, as there would have been no coverage save for the purchase of this coverage and the payment of these premiums. If the plaintiff insured is claiming that the coverage should have been purchased at the outset of the parties’ relationship and the relationship goes back several years, the saved premiums over that entire period can arguably be applied to reduce the recovery. As still another example, it is possible that an expert or an underwriter at the carrier involved in providing the policy missing an endorsement adding coverage the
insured claims he/she asked the agent/broker to procure may be able to show that any such coverage would not have been offered without being capped at a certain limit, or that it would not have been offered or available given the risk involved, the insured's loss history, or the specific circumstances of the insured's situation that would have been taken into account during the underwriting of the risk.

While these defense arguments can be used in many cases to effectively blunt agent/broker E&O claims, it is important to note that they have to be deployed thoughtfully and with care. Sometimes the agent/broker will have a viable argument that notwithstanding the poor advice given with regard to the placement of coverage, or the inclusion of policy language via endorsement, the insured is nonetheless wholly unable to establish a credible link between the agent/broker's negligence and the damages asserted. However, while it can seem reasonable to point to a lack of clarity in connecting the dots, point to the insured's burden to prove proximate causation, and declare that for this reason the insured's E&O claim must fail, proof of loss can sometimes be complicated by the nature of the loss, and courts will take this into consideration. What might seem a sure fire proximate causation defense argument may not necessarily yield an early dispositive ruling.

A recent California appellate court decision highlights the arguments available to the broker to combat agent/broker E&O claims, and how these issues can play out in real time. Some other recent decisions provide further evidence of how these issues and arguments can play out, and the increasingly expansive view of the potential range of parties who were impacted by the agent/broker’s alleged negligence who may be viewed as having standing to sue the agent/broker. The following is an analysis of the California appellate court decision, and the lessons that can be drawn from it, followed by a brief summary of some other recent agent/broker E&O decisions of note, and conclusions that can be drawn from these decisions.

II. Case Study – The Agent/Broker’s Defenses as Applied

In *Performance Team Freight System, Inc. v. Arthur J. Gallagher & Co.*, the insurance broker Arthur J. Gallagher (“Gallagher”) was sued for professional negligence and breach of contract by its customer, a company engaged in the business of providing trucking and warehousing services (“Performance Team”), after a claim for over $1.4 million under crime insurance coverage was challenged by its insurers, and the claim was ultimately settled for just $500,000. The claim was made after it was determined that drivers hauling customer merchandise were systematically opening packages, stealing portions of the merchandise, and then re-sealing the packages before delivery. The nature of the thefts made it hard to confirm everyone who might have been involved in the scheme. Accordingly, while a number of drivers were
terminated after the investigation, they were not terminated on the grounds that they had been implicated in the thefts. And it was impossible to track each piece of stolen merchandise to the specific driver believed to have stolen it. The drivers involved in the scheme apparently were all making use of a fencing operation, and the issue only came to light after stolen merchandise had been fenced.

The drivers involved were independent contractors, and the fidelity and crime coverage in issue provided that only thefts by “employees” would be covered. However, a policy endorsement negotiated by Gallagher defined employees in such a way that they could be deemed employees for the purposes of the coverage.

After commencing a lawsuit against the insurers asserting, *inter alia*, claims for declaratory relief and breach of contract, Performance Team ultimately settled their claim for the deeply discounted $500,000 figure. In its suit against Gallagher, Performance Team alleged that they were compelled to settle for far less than the actual value of the stolen merchandise because of Gallagher’s negligence in procuring coverage, and specifically its alleged negligence in regards to the crafting of the language defining in what circumstances independent contractors would be deemed employees. Specifically, while the endorsement defined “employees” to include independent contractors in the regular service of Performance Team’s ordinary course of business, it limited such coverage to those contractors performing services for Performance Team pursuant to a written contract between a “natural person independent contractor” and Performance Team for such services.

The problem that developed was that in the course of investigating and considering the claims, the insurers raised questions about whether coverage would apply only with respect to thefts by drivers who each had individual written contracts with Performance Team. Not all did. Additionally, the insurers questioned whether some portion of the thefts might have occurred after delivery, as there was no definitive evidence that the thefts occurred prior thereto. They had also raised questions about whether there was sufficient evidence to determine the drivers involved in the thefts had all conspired and colluded with others, thus making it a single claim with a single deductible, or multiple claims.

As noted above, after settling with its insurers, Performance Team sued Gallagher, claiming it was compelled to settle for such a discounted amount because of Gallagher’s negligence in regards to the inclusion of the endorsement on the policy concerning covered “employees.” After taking discovery, Gallagher moved for summary judgment. The theory presented was that Gallagher could not prove “causation” because Performance Team had not identified which drivers involved in the thefts fell outside the policy’s definition of employees. Thus, it was argued,
they could not prove what portion, if any, of the reduced payment was caused by this. Additionally, Gallagher argued that Performance Team could not establish that, but for Gallagher’s alleged negligence, Performance Team’s claim would have been fully covered. The argument in this regard was based on the fact that there were other issues that had not been resolved, including whether there definitively was collusion among the drivers, or not, and thus whether one or more deductibles would have applied. Lastly, and relatedly, Gallagher argued that Performance Team had failed to prove actual damages flowing from Gallagher’s alleged negligence. Gallagher’s argument in this regard prevailed at the trial court, and Performance Team’s claims were dismissed on summary judgment.

On appeal, the judgment was reversed. As grounds for reverseal, the appellate court pointed out that:

Performance Team’s complaint was not limited to the theory that Gallagher was negligent in negotiating and agreeing to Endorsement No. 6 because it was too narrow. The complaint also alleged Gallagher’s breach was in failing to procure “full and complete crime coverage” for the risk of driver theft and by failing to advise Performance Team there was a gap in the company’s crime coverage. This theory is that Gallagher breached its duty by failing to ensure that Performance Team’s crime coverage would encompass theft by any of the independent contractors driving for Performance Team, irrespective of whether the driver was a “natural person” or whether there was a written independent contractor agreement. Under this theory, had Gallagher procured such coverage, it would have been unnecessary for Performance Team to show the insurer anything other than that truck drivers performing services for Performance Team committed the thefts. Endorsement No. 6 gave Federal an opportunity to challenge coverage based on the status of the drivers. Performance Team argues that had Gallagher procured the “full and complete” coverage for driver theft the company wanted, Federal simply could not have argued there was no coverage for the theft losses because of the nature of the drivers’ employment, or because of a lack of proof of driver status.²

As to the argument raised with respect to the fact that there were other reasons having nothing to do with the “employee” endorsement that were raised concerning the claim, the appellate court noted that Performance Team had offered evidence that it had identified the drivers, by name, that it believed had committed the thefts
and provided this evidence to the lead insurer. Performance Team also attested, by counsel, that they had provided Federal with detailed supporting documentation which identified each specific item of merchandise that the client claimed was missing from their shipments. While Performance Team never specifically accused any drivers of stealing, the appellate court found this to provide sufficient evidence to establish the existence of a material issue of fact precluding summary judgment.

With regard to the collusion issue, the court noted that while Performance Team had no evidence of communications between the drivers about planning and executing the thefts, it had presented strong circumstantial evidence that there was a common conspiracy. This evidence included the fact that all of the drivers implicated were making pick-ups at specific client warehouse locations, that they all were tied to the same merchandise shortages involving opened and re-sealed cartons, and that they all moved the merchandise through the same fencing operation.

Lastly, the court noted that the fact that Federal had challenged coverage on multiple bases did not, ipso facto, negate Performance Team’s assertion that but for Gallagher’s negligence, it would have been able to secure a better settlement or recovery against Federal at trial. The uncertainty created by the application of the definition of who were “employees” within the meaning of the endorsement, and thus what portion of the claims might be covered, was, by itself, a significant reason why Federal did not accept coverage.

On the damages argument, because the court concluded that Performance Team’s claims could not be dismissed on summary judgment on the evidence before it, the court found that the arguments Gallagher had raised were not sufficient to dismiss the claim based on an alleged inability to prove Performance Team’s actual damages. In so doing, the court noted that it was insufficient for Gallagher to simply point to the fact that Federal had multiple reasons for challenging coverage. On summary judgment, it was Gallagher’s burden to show that no damages could be proven because of this.

III. Lessons to be Learned

The significance of this decision is how it highlights some of the challenges facing brokers today, insofar as they provide more sophisticated services. In this case, Gallagher stepped in to try to help its client resolve an issue that had arisen about when thefts by independent contractors might be covered. In so doing, it went beyond purchasing an “off the shelf” product. And in so doing, it opened itself up to risk in failing to consider all of the potential theft scenarios that could arise, and how
the language defining who were to be deemed “employees” or not could potentially lead to coverage disputes.

The case is also significant in how it highlights a variety of useful defense arguments available to brokers facing E&O claims, and what can be done by Plaintiffs’ counsel to try to fend off these arguments. In this instance, Gallagher ultimately failed to obtain summary judgment, but the issues its counsel identified, and the manner in which they were presented evidenced some very intelligent lawyering. The fact is that, notwithstanding the very real and legitimate concerns raised by the issue regarding which implicated drivers were and weren’t properly deemed covered “employees”, there were a number of other coverage issues raised by Federal in the course of investigating the claim. At the end of the day, it is the plaintiff’s burden to prove the damages proximately caused by the broker’s alleged negligence. This case strongly suggests that a court, viewing a set of complicated facts such as these, will not be satisfied to come to the conclusion that the broker may have acted negligently in procuring coverage, but because it’s complicated to follow the threads leading from this negligent conduct to the injuries incurred as a result, the only rational solution is to let the broker off the hook. Proximate cause is a critical issue. But complexity, alone, in determining how the broker’s negligence impacted the customer’s lack of coverage or other harm will not be sufficient to avoid liability. On summary judgment, it will be the broker’s responsibility to show how the harm cannot be attributed to the broker’s negligence, in whole or in part.

IV. Miscellaneous

Quickly surveying some additional miscellaneous holdings in agent/broker E&O cases in 2017, it is noted that, in *O.P.H. of Las Vegas, Inc. v. Oregon Mut. Ins. Co.*, the court held that, absent special circumstances, a broker does not owe a duty to monitor the insured’s payment of insurance premiums. In *J & A Freight Systems, Inc. v. Travelers Property & Casualty Co. of America*, while acknowledging a duty on the part of an insured to know the import and meaning of its insurance policy, the court denied a motion to dismiss the insured’s negligent misrepresentation claim based on same. The court held that an insured’s duty to know the contents of his policy does not present an absolute bar to causes of action brought by an insured against an insurance agent or broker, as opposed to causes of action by an insured against an insurer. And in *Moje v. Federal Hockey League LLC*, the court held that a minor league hockey player who was blinded during a game might have standing to pursue a claim against the broker who procured liability coverage for the league in his capacity as a “proposed insured” to whom the broker owed a duty of reasonable care. This continues the trend towards courts being ever
more open to the concept of a broker owing a duty of care flowing out beyond the customer it is dealing with directly.

V. Conclusion
As has been the case in recent years, agent/broker E&O decisions in 2017 continue to evidence a trend of courts being more receptive generally to finding bases for identifying a duty to advise, or at very least being unwilling to dispose of duty to advise claims on summary judgment. That said, whether within the realm of the “duty to advise” claim or otherwise, there are numerous viable arguments in the thoughtful defense lawyer’s/claims attorney’s arsenal upon which to build strong defenses to the various claims that can typically be brought against a broker when insufficient coverage is available to respond to an insured’s loss. As we move deeper into the digital age, with all the risks that are presented by the reduced interaction between human beings on both the broker side and the underwriting side, and we continue to see courts become ever more accepting of the premise that insurance is a complicated field through which the broker is seen as and expected to provide specialized expertise and guidance, it is important to continue to keep a close eye on the trends, consider how the issues and arguments are likely to play out, and take careful note of what can and must be done to build out the defense case.

Endnotes
2 Id. at *7.
deemed sufficiently protected, despite their status as non-parties to the first litigation, because courts were willing to conclude the competing shareholders were in privity, at least where the initial shareholder’s counsel provided adequate representation. See *In re Wal-Mart Stores, Inc. Delaware Derivative Litigation*, C.A. No. 7455-CB (consol.), supp. op. (Del. Ch. July 25, 2017), 167 A.3d 513 (Del. Ch. 2017). However, the Chancery Court then noted the peculiarities of derivative litigation in this context, in that Delaware courts have repeatedly admonished shareholders to “use the tools at hand,” i.e., to obtain corporate books and records under Section 220, before bringing a derivative action, which is in considerable tension with plaintiff counsel’s financial incentive to be the first to file an action in a “race to the courthouse.” As a result, the Chancery Court noted the first filed actions were more prone to dismissal for demand failure, as they were less likely to have the benefit of “adequate due diligence.” Thus, the subsequent shareholder would lose out on collateral estoppel grounds, despite a better prepared complaint, arguably giving rise to a Due Process concern noted by the Delaware Supreme Court.

In an apparent effort to resolve this tension, the Chancery Court advocated adopting an approach suggested in dicta last year in *In re EZCORP Inc. Consulting Agreement Derivative Litigation*, 130 A.3d 934 (Del. Ch. 2016). Specifically, that preclusive effect should only be given to prior derivative actions that have survived motions to dismiss pursuant to Rule 23.1. While acknowledging that this result could lead to “seriatim lawsuits litigating demand futility,” the Chancery Court noted such subsequent lawsuits would typically be based on “a more refined complaint with more particularized allegations or more tailored legal theories after doing additional homework, such as obtaining corporate books and records through a Section 220 proceeding.” According to the court, this approach “should go a long way in addressing the ‘fast-filer’ problem and ensure better protection of due process rights” for shareholder plaintiffs.

**The Supreme Court Opinion**

On appeal once again, the Delaware Supreme Court was not persuaded. First, it noted because the Arkansas decision was rendered by a United States District Court, federal law governed the Due Process analysis. The Court then observed that three federal circuit courts have previously determined that Due Process rights of subsequent plaintiffs are protected where their interests were aligned with the prior plaintiffs and where those prior plaintiffs had adequate representation.

With respect to whether the two groups of plaintiffs shared common interests, the Court explained that both groups of plaintiffs were in privity, as each group was seeking to assert the same set of rights, i.e., those of the corporation, and not their own individual...
rights as shareholders. Thus, plaintiffs in separate derivative actions nonetheless share a commonality of interest sufficient to avoid offense to notions of Due Process.

The Court then focused on the adequacy of representation, stating that federal law generally deemed representation “adequate” where (1) the interests of the party and non-party are aligned, (2) the initial party understood that it was acting in a representative capacity or otherwise took care to protect the interests of the non-party, and, at least in some instances, (3) notice is provided to the non-party. It also indicated that an analysis of quality of the representation and confirmation of a lack of any conflicts was also appropriate to the adequacy evaluation.

With respect to the first of the federal requirements, the Court stated that its privity analysis confirmed the relevant alignment of interests. Regarding representative capacity, it concluded that the record demonstrated both groups of plaintiffs were aware of the competing actions and the likelihood of one action being held preclusive as to the other. As for notice, the Court concluded that federal courts dispensed with this requirement with respect to derivative actions.

Turning to adequacy, the Court addressed the fact that the Arkansas plaintiffs had not made a books and records demand before filing their complaint. It observed Arkansas counsel had access to certain relevant corporate documents in the public domain via a newspaper article and that counsel had made the determination that these documents were sufficient to make the case. In other words, while counsel considered the option, it ultimately did not think a Section 220 demand was necessary. Just because that determination ultimately proved to be wrong, the Court stated, was not sufficient to deem counsel inadequate, though the Court stressed that determination was based on the specific facts at hand. As for potential conflicts, the Court found no evidence the initial plaintiffs advanced their interests at the expense of the later plaintiffs.

Accordingly, having found that the two groups of plaintiffs’ interests were aligned and that the initial plaintiffs were adequately represented, the Court held that there was no Due Process violation in according preclusive effect to the initial ruling.

*       *      *

Corporate Coverage Analysis: When the Chancery Court advocated a retreat from the preclusive effect of certain first filed actions, D&O insurance carriers took notice, as it was a sure recipe for additional litigation and thus additional exposure to their policies. Thus, the Delaware Supreme Court’s recent reaffirmation of the probity of such preclusive effect is a welcomed outcome for insurers and insureds alike, as it prevents the proverbial second bite at the apple in the context of derivative litigation.
## Calendar

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<td>April 5-6, 2018</td>
<td><strong>Motor Vehicle Products Liability Conference</strong>  &lt;br&gt; Contact: Felisha A. Stewart – 312/988-5672</td>
<td>Arizona Biltmore Resort &amp; Spa Phoenix, AZ</td>
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<td>April 6-7, 2018</td>
<td><strong>Toxic Torts &amp; Environmental Law Conference</strong>  &lt;br&gt; Contact: Felisha A. Stewart – 312/988-5672</td>
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<td>April 14-18, 2018</td>
<td><strong>TIPS National Trial Academy</strong>  &lt;br&gt; Contact: Donald Quarles – 312/988-5708</td>
<td>Peppermill Resort &amp; Spa Casino Reno, NV</td>
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<td>May 2-6, 2018</td>
<td><strong>TIPS Section Conference</strong>  &lt;br&gt; Contact: Felisha A. Stewart – 312/988-5672  &lt;br&gt; Speaker Contact: Donald Quarles – 312/988-5708</td>
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<td>May 9-11, 2018</td>
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<td>August 2-5, 2018</td>
<td><strong>ABA Annual Meeting</strong>  &lt;br&gt; Contact: Felisha A. Stewart – 312/988-5672  &lt;br&gt; Speaker Contact: Donald Quarles – 312/988-5708</td>
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<td>October 10-14, 2018</td>
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