Alert
February 2, 2015

Global Insurance Alert
News Concerning Professional Liability Issues

COZEN O'CONNOR

Eighth Circuit Deems Legal Threats a "Claim;" Regulation Requiring Prejudice Inapplicable

On January 9, 2015, the U.S. Court of Appeals for the 8th Circuit handed down *Philadelphia Consolidated Holdings Corp. v. LSi-Lowery Systems, Inc.*, which decided whether a technology company's claim was covered under its professional liability policy. In *LSi-Lowery*, the court decided three issues of current importance for "claims made" policies. First, emails showing an expectation the insured would be sued meant that a "claim" had been made even though damages were not expressly demanded. Second, when it was made, the claim involved a "wrongful act," even though it related to breach of a contract (an excluded circumstance). Third, a regulation mandating a finding of prejudice in order to prevail on "late notice" did not apply because there was no coverage under the policy in the first instance.

Threat of Legal Proceedings Constitutes a Claim

The insured, LSi, had undertaken to provide technology consulting services to its client, Hodell, who quickly became dissatisfied and sued LSi in November 2008. PCHC, which had issued a policy for the 2008-09 period during which the lawsuit was filed, as well as the preceding period, denied coverage on the ground that the claim had not been "first made and reported," as required, during any policy period.

The court observed that complaints by Hodell had begun on March 13, 2007, and continued as summarized in the following timeline of the customer's emails:

2007

March 13 Hodell states system is unstable and affecting its "… bottom line each day …"

March 14 LSi acknowledges: "if we do not get Hodell happy, we can expect a legal issue."

April 11 Hodell warns that if they throw the system out, "they will for sure get legal."

April 23 First PCHC policy incepts

April 25 Hodell inquires "who will pay for the damages?"

June 25 Hodell demands that LSi correct everything "or reimburse" it for the "expense."

July 24 Hodell's attorneys advise LSi Hodell will "… pursue all legal and equitable remedies …" if breach of agreement is not cured.

2008

April 23 Second PCHC policy incepts

November 21 Hodell files suit against LSi

December 8 LSi first notifies PCHC of Hodell's claims against it

Both policies defined a claim to include a "demand for money." LSi contended that Hodell had made no "specific demand for money" until it filed suit. The 8th Circuit disagreed, reasoning that the emails demonstrated both Hodell's intent to sue if necessary and LSi's anticipation of being sued. This established that a claim had been made prior to the April 2008 inception date of the policy under which the claim was first reported.

Richard C. Mason

Member

rmason@cozen.com
Phone: (215) 665-2717
Fax: (215) 665-2013

Related Practice Areas

- Insurance Coverage
- Professional Liability Insurance Coverage

Industry Sectors

- Insurance

Wrongful Act Inferred Where Claim Concerned the Same Errors and Omissions as the Ensuing Negligence Action

LSi next argued that it was not required to give notice prior to the lawsuit because Hodell's complaints asserted breach of contract, which did not implicate the policy, given that contract claims were excluded. The court again disagreed, holding that Hodell had made it clear it intended to pursue "all" possible legal remedies, not just breach of contract. Also, the acts and omissions alleged in the complaint mirrored those in Hodell's prior emails.

Missouri Regulation Mandating a Finding of "Prejudice" Deemed Inapplicable

Lastly, LSi asserted that PCHC could not prevail unless it proved it was prejudiced by untimely notice, invoking a Missouri regulation providing: "No insurer shall deny any claim based upon the insured's failure to submit a written notice of loss within a specified time … unless this failure operates to prejudice the rights of the insurer." The court concluded, however, that this regulation pertained to provisions that were akin to an exclusion, and did not apply where "… there was no coverage … in the first instance …" because the insuring agreement applied only to claims first made and reported during the policy period.

Significance of Decision

The *LSi-Lowery* decision is important for three reasons. The decision confirms that a claim may arise even when a demand against the insured does not specify the sum demanded. Secondly, the decision construed the Wrongful Acts provision as geared to the acts and omissions, rather than the legal theories, that were the subject of the customer's accusations. When an insured omits to take the simple step of notifying its insurer, it risks the consequences if it turns out that a later-filed complaint alleges facts relating to earlier communications from the disgruntled customer. Lastly, the court declined to apply a regulation, which plainly was not intended to apply to "claims made" policies, where the insurer was not invoking a "late notice" defense, but rather disclaiming coverage under the insuring agreement. This last holding is particularly notable, given the existence of similar "notice-prejudice" statutes in a number of other states.

To discuss any questions you may have regarding the issues discussed in this Alert, or how they may apply to your particular circumstances, please contact Richard C. Mason at (832) 214-3909 or rmason@cozen.com.