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Illinois – Seventh Circuit Holds That Lawsuit Against Insured Cannot Include Multiple "Claims"

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On June 19, 2020, the Seventh Circuit Court of Appeals affirmed a district court's decision finding that a damages argument advanced under new legal theories and factual allegations does not amount to a "claim" under the claims-based insurance policy issued over a decade after the commencement of the underlying lawsuit. In 2003, Peoples National Bank was sued by the Newmans for breach of contract, and later conversion and breach of fiduciary duty. The underlying lawsuit arose out of letter-of-credit proceeds relating to the Newmans' operation of Taco John's restaurant franchises and a misallocation of those proceeds. In 2013, the court found Peoples liable for breach of contract, and in 2015, summary judgment was granted for the Newmans on the two other counts.

Between those two decisions, Peoples National Bank obtained a claims-made policy with Federal Insurance that ran from April 15, 2014 to April 15, 2017. In 2016, the damages aspect of the underlying lawsuit went to trial, and the Newmans advanced an argument based on a "Pledge Agreement" between the parties. These facts and theories were not presented in the liability portion of litigation. Peoples tendered the issue to Federal asserting that the damages argument based on these new facts and theories was a "claim" made during the policy period that triggered Federal's duty to defend and indemnify Peoples. When Federal denied coverage because 1) the damages argument was not a "claim" under the policy, and 2) even if it was, it would fall outside of the coverage period, because the lawsuit was filed in 2003, Peoples brought suit seeking to recover its loss from the damages argument. The district court granted summary judgment in favor of Federal. Prior to Peoples filing an appeal of that decision, the state appellate court vacated the underlying damages award. Because of this decision, on appeal Peoples only sought to recover for loss of defending against the Newmans' damages argument.

The court looked to the type of insurance policy issued and the policy terms to determine whether the damages assertion, brought thirteen years into the lawsuit, could potentially trigger coverage under the policy. The policy at issue is a claims-made policy, and the court compared the risks associated with those in an occurrence-based policy. A claims-based policy focuses on claims that could be made during the policy period, and an occurrence-based policy covers the risk of an injury occurring during the policy period. With an occurrence based policy, a claim could be brought outside of the policy period extending the insurer's risk beyond the expiration of the policy. With a claims-based policy, like the one between Peoples and Federal, the risk to the insurer exists only during the policy period.

The court then turned to the definition of "claim" provided in the policy. The policy defined "claim" as "a written demand for monetary or non-monetary relief, including injunctive relief" or "a civil proceeding commenced by the service of a complaint or similar pleading," including "any appeal therefrom." The court pointed to the use of the conjunction "or" as connecting each of the sections of the list, and indicating that the definitions could not operate simultaneously. Peoples argued that the written closing argument for damages fell under the "written demand for monetary or non-monetary relief" definition of "claim." The court disagreed, and held that under the policy, "a 'claim' taking the form of 'a civil proceeding commenced by the service of a complaint' spans the entire civil action, not just the legal theories and factual allegations in the complaint that commenced that action."

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The court explained that Peoples' interpretation is unreasonable, because it would contravene and subvert the purpose of the policy by allowing "claims" within other "claims." Under Peoples' reasoning, "a written demand for monetary or non-monetary relief" would "engulf" the civil proceeding part of the definition making the civil proceedings definition meaningless. The court found that the civil proceeding definition "comfortably holds independent meaning." The court determined that where "a complaint commences a civil proceeding against the insured, no other claim may form within that claim." The same logic applies to the written demand for monetary and non-monetary definition. The court explained that its holding recognized the plain language and grammar present in the policy and the purpose and risks associated with a claims-based policy. The court found that the damages argument presented was an assertion made within the "claim" commenced in 2003, and could not be a "claim" in and of itself. The appellate court affirmed the district courts grant of summary judgment to Federal, and held that Federal had no duty to defend or indemnify Peoples against the damages argument.

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