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How Del. 'Arising Out Of' Ruling May Affect Insurance Cases

By **Keith McKenna and Maria Brinkmann** (October 20, 2023, 6:13 PM EDT)


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In the recent decision in Ace American Insurance Co. v. Guaranteed Rate Inc.,[1] the Delaware Supreme Court firmly rejected insurer Chubb's broad interpretation of the words "arising out of" in a professional services exclusion.

In doing so, the court confirmed that long-standing, fundamental principles of insurance policy interpretation in the context of policy exclusions remain intact.

Specifically, in affirming the Superior Court of Delaware's decision, the Supreme Court reiterated that "exclusion[s] must be interpreted narrowly and in favor of coverage,"[2] and, in that context, the phrase "'arising out of' requires 'some meaningful linkage between the two conditions imposed in the contract.'"[3]

Although Ace v. GRI deals with a professional services exclusion, the court's thorough analysis of the phrase "arising out of" extends its application to a wide range of exclusions employing similar prefatory language, significantly increasing the decision's import in insurance coverage litigations.

Ace involved a policyholder, Guaranteed Rate Inc., which was a mortgage loan servicing provider and an approved lender in the federal government's Direct Endorsement mortgage insurance program.

This federal program permitted Guaranteed Rate to endorse single-family residential mortgage loans for insurance and guaranty by the Federal Housing Administration and the U.S. Department of Veterans Affairs.[4] In tandem with its endorsement, Guaranteed Rate was required to certify to the government that each loan and GRI's loan program met FHA and VA rules.

In 2017, a former Guaranteed Rate employee brought a qui tam action against GRI, alleging that Guaranteed Rate violated the False Claims Act by falsely certifying to the government that the loans it endorsed were eligible for government insurance.

In connection with the qui tam, the U.S. Attorney's Office for the Northern District of New York and the U.S. Department of Justice issued a civil investigative demand to Guaranteed Rate, notifying it that the government was investigating allegations that Guaranteed Rate violated the FCA by originating and underwriting federally insured mortgage loans that it falsely certified had met loan-approval requirements.

Guaranteed Rate sought insurance coverage for the CID and the government's subsequent settlement demand under a management liability policy that Guaranteed Rate purchased from Chubb.

Chubb denied coverage on the grounds that (1) the CID was not a "claim" under the policy, and (2) the settlement payment made in connection with the CID triggered the policy's professional services exclusion, which bars coverage for claims "alleging, based upon, arising out of, or attributable to any Insured's rendering or failure to render professional services."

Guaranteed Rate filed an action in Delaware Superior Court seeking to obtain insurance coverage.

In two decisions, the Superior Court rejected both of Chubb's coverage defenses. The court held that the CID constituted a claim based on the reasoning in Conduent State Healthcare LLC v. AIG Specialty Insurance Co.,[5] which involved similar facts and policy language.[6]

Separately, the court held that the professional services exclusion, when interpreted narrowly and in favor of coverage, did not bar coverage for the CID and related settlement payment.[7] Chubb appealed the Superior Court's rulings on its professional services exclusion defense.

On appeal, the Delaware Supreme Court noted that the parties agreed on what constituted GRI's rendering of professional services and that Guaranteed Rate was not providing professional services if it engaged in wrongful conduct that violated the FCA.[8] Their dispute centered on "whether the FCA claims arose out of GRI's loan originating and underwriting services," and thus triggered the policy's professional services exclusion.[9]

The court began its analysis with a discussion of IberiaBank Corp. v. Illinois Union Insurance Co.[10] In 2020, Chubb took the completely opposite position, successfully arguing that FCA charges did not qualify as professional services under professional liability policies, and thus, were excluded from coverage.

Indeed, in IberiaBank, the U.S. District Court for the Eastern District of Louisiana agreed with Chubb's assertion that "submitting false certifications to the federal government was separate from IberiaBank's professional services — loan underwriting for clients — and therefore were not covered losses under the policies."[11] Referencing IberiaBank, the Delaware Supreme Court noted that, while not pertinent as a matter of judicial estoppel, IberiaBank "bears on how Chubb (ACE) has interpreted 'professional services' under similar policies in similar circumstances."[12]

Turning to Chubb's contrary argument in the present case — that the FCA claims against Guaranteed Rate qualify as claims "arising out of" Guaranteed Rate's professional services — the court considered the damages alleged by the government in the FCA claims and the nature of those claims, which Guaranteed Rate settled.

The court found it significant that Guaranteed Rate settled FCA claims alleging that Guaranteed Rate defrauded the government by falsely certifying that loans met certain insurance requirements, claims that the court determined were unrelated to Guaranteed Rate's performance of professional services. Therefore, concluding that GRI's "alleged misconduct arose out of the false certifications, not the professional services Guaranteed Rate provided to borrowers," the court held that the policy afforded coverage for the FCA claims.[13]

In reaching its conclusion, the court flatly rejected Chubb's argument that "[b]ut for the deficiencies in

[GRI's] underwriting ... the FCA claims would not exist."[14] Although the court acknowledged that Delaware courts interpret the words "arising out of" in insurance policies "liberally," it reiterated that the phrase also demands "some meaningful linkage between the two conditions imposed in the contract."[15]

The court reasoned that in contrast to the cases relied upon by Chubb, "where the harm arose from negligent conditions or the use of a product," the underlying FCA claims at issue here were not based on the failure to perform professional services.[16] Thus, emphasizing the "difference between the subject of the FCA claims — false certifications — and the underlying conduct used to demonstrate the falsity of the claims — underwriting loans," the court found the requisite "meaningful linkage ... absent."[17]

The court also recognized that Chubb's proffered interpretation of "arising out of" "effectively extends coverage of the exclusion to just about anything remotely connected to the professional service," and adopting such interpretation would gut coverage for "many acts only incidentally related to professional services ... if the act would not have arisen but for the rendering of professional services."[18]

As underscored by the court, this result is untenable under Delaware law, which requires that the linkage be "meaningful, not tangential."[19]

In sum, Ace v. GRI definitively rejects insurers' attempted broad interpretation of the phrase "arising out of" in the context of policy exclusions, and upholds the well-established insurance policy interpretation rule that exclusions must be construed narrowly and in favor of coverage.

This ruling helps to clarify that although the words "arising out of" are generally read broadly in the context of provisions granting insurance coverage, when exclusionary language is at issue, those words require a meaningful linkage between the two conditions imposed by the insurance policy, not merely a tangential or "but for" causal link.

In the wake of Ace v. GRI, insurers likely will try to argue that its application is limited to coverage disputes involving "professional services" exclusions. But that attempt is likely to fail.

Delaware courts have faithfully applied a meaningful linkage in other contexts when insurance policies use the phrase "arising out of," or similar phrases like "resulting from," "in consequence of," or "in any way involving."

For example, in Sycamore Partners Management LP v. Endurance American Insurance Co., the Delaware Superior Court determined in 2021 that there was no meaningful linkage sufficient to trigger any of the provisions the insurer raised as defenses to coverage, including the policy's interrelated claims provision, prior notice exclusion, and prior and pending litigation exclusion.[20]

Similarly, in Options Clearing Corp. v. U.S. Specialty Insurance Co.,[21] the court applied a meaningful linkage test to the subject policy's event and prior notice exclusions, resulting in a finding of coverage, with the court's 2021 holding that a meaningful linkage cannot be established merely because "two claims ... mention some of the same facts."[22]

Notably, this court supported its conclusion in part on the grounds that the "Delaware Supreme Court has instructed lower courts to implement 'meaningful linkage' in a coverage context broadly, where possible, to find coverage."[23]

While Ace v. GRI demonstrates more specifically how courts should execute this instruction when analyzing the applicability of a professional services exclusion, the ruling has wide-ranging application in coverage disputes involving any exclusions that employ "arising out of" or similar prefatory language.

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[1] ACE American Insurance Co. v. Guaranteed Rate, Inc., Case No. 360, 2022, 2023 WL 5965619 (Del. Sept. 14, 2023).

[2] id. at *4.

[3] Id. at *6 (quoting Pac. Ins. Co. v. Liberty Mut. Ins. Co., 956 A.2d 1246, 1256-57 (Del. 2008)).

[4] 2023 WL 5965619, at *1.

[5] Conduent State Healthcare, LLC v. AIG Specialty Insurance Co., 2019 WL 2612829 (Del. Super. June 24, 2019).

[6] Guaranteed Rate, Inc. v. ACE Am. Ins. Co., 2021 WL 3662269, at *5 (Del. Super. Aug. 18, 2021), reargument denied, 2021 WL 4726608 (Del. Super. Oct. 11, 2021), cert. denied, 2021 WL 5370794 (Del. Super. Nov. 16, 2021), and appeal refused, 266 A.3d 212 (Del. 2021).

[7] Id. at *4; Guaranteed Rate, Inc. v. ACE Am. Ins. Co., 2022 WL 4088596, at *2 (Del. Super. Aug. 24, 2022).

[8] 2023 WL 5965619, at *4.

[9] Id.

[10] 2019 WL 585288 (E.D. La. Feb. 13, 2019), aff'd, 953 F.3d 339 (5th Cir. 2020).

[11] 2023 WL 5965619, at *5.

[12] Id.

[13] Id. at *6.

[14] Id. (emphasis in original).

[15] Id. at *6.

[16] Id.

[17] Id. at *7.

[18] Id. at *8.

[19] Id.

[20] Sycamore Partners Management, L.P. v. Endurance American Insurance Co., 2021 WL 4130631 (Del. Super. Sept. 10, 2021).

[21] Options Clearing Corp. v. U.S. Specialty Insurance Co., 2021 WL 5577251 (Del. Super. Nov. 30, 2021).

[22] 2023 WL 5965619 at *8.

[23] Id.