



By
Alan Rutkin

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A February decision from the U. S. Court of Appeals for the 4th Circuit in *Republic Franklin Insurance Co. v. Albe-marle County School Board* offers important insight as to what actually constitutes an insurable “loss.”

The school board, which held the policy, and its bus drivers ran into a dispute. The bus drivers claimed they were owed unpaid wages and certain other damages. The school board turned to its insurer. But the insurer said that salary decisions were not “wrongful acts” and the loss was not insured under the policy.

that wrongful act. Such loss could only arise if the failure to fulfill the pre-existing duty to pay wages caused ‘damages’ apart from the back wages not paid.”

In other words, the insured committed a wrongful act by not paying the workers’ wages. But the obligation to pay the wages did not result from either the claim or the wrongful act. The obligation to pay the wages was a pre-existing obligation that arose from the work that was done.

Thinking about it, the decision makes a world of sense. When the drivers worked without pay the policyholder incurred a debt. The policyholder’s failure to pay a debt should not transform a financial obligation into an insured loss.

Importantly, this reasoning should extend beyond wage-and-hour disputes and into other insurance issues that arise from financial wrongdoing.

For example, we are seeing investors claiming losses of principal. These investors may well be alleging “wrongful acts” as defined in the policy. They may also (or instead) be alleging acts that are excluded under the policy, but the focus here is on the loss. If the entity is forced to return investors’ money, that should not be an insurable loss.

Similarly, if the claim is brought by an individual employee who is forced to return money to the corporation, the money returned cannot be an insured loss.

Insurance, like math, is best understood with simple examples. Assume that you bought a service but refused to pay because you considered the service unsatisfactory. A court disagreed, found the service satisfactory, and held you liable. Surely, your obligation to pay for the service would not be insurable.

This same principle should hold true in a variety of financial disputes. BR

Claim Tossed Under the Bus

Insight: There’s a difference between an insured loss and an incurred debt.

The trial court agreed with the insurer, holding that the school board did not commit “wrongful acts” under the policy because the board had a pre-existing duty to pay.

The appellate court took a different approach and found that the decisions were “wrongful acts,” but the loss question was more complicated.

The policy required the insurer to “pay for all ‘loss’ resulting from a ‘claim’ for a ‘wrongful act’ to which this insurance applies.” The policy defined “loss” as “any amount which an insured is legally obligated to pay as damages.”

Given this policy language, the court reasoned that “a breach of a pre-existing duty to pay is a wrongful act but...the resulting obligation to pay back wages may not be a loss resulting from

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