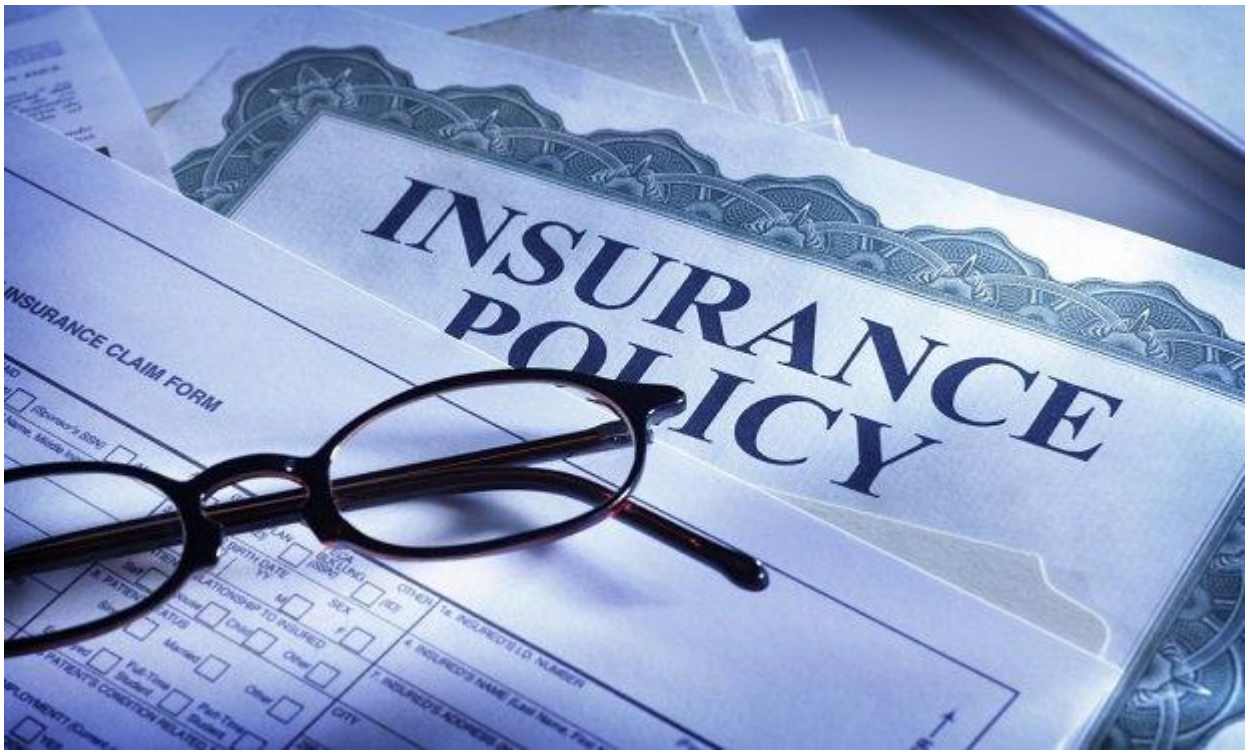
The 'any insured' exclusion: When an insurer is still exposed

What happens when a policy contains a general severability clause within an exclusion itself?

By **Marc R. Kamin** | August 24, 2021



(//images.propertycasualty360.com/contrib/content/uploads/sites/414/2021/08/Insurance-policy-iStockphoto.jpg) How can the prior knowledge clause and the non-imputation clause co-exist? And more specifically, what implications, if any, does this clause have on the prior knowledge clause immediately preceding it? (Photo: iStock)

No one likes uncertainty, particularly those in the insurance industry. Insurers and underwriters should therefore be wary of general severability (or non-imputation) clauses that have the potential to strip any meaning from an exclusion that would otherwise serve to exclude coverage for all insureds.

To avoid any uncertainty, a severability clause, if one must exist, should reference a specific provision or condition of the policy and one that is not expressly in conflict with the severability provision itself. Exclusions applying to "any insured" unambiguously exclude coverage for *all*, including innocent insureds. Therefore, most courts generally uphold that interpretation (https://www.propertycasualty360.com/2021/07/12/are-courts-ignoring-policy-interpretation-rules-in-covid-decisions-414-205774/) even in the face of a severability provision found elsewhere in the policy. What happens, however, when the policy contains a general severability clause, or the clause is found *within* the exclusion itself?

Can the prior knowledge and non-imputation clauses co-exist?

Imagine this: Your insureds, a corporate entity and its three officers, have just been sued for breach of fiduciary duty and fraud related to dubious acts that pre-date the D&O policy (https://www.propertycasualty360.com/2021/05/03/is-diversity-the-next-big-do-risk/) period. The allegations alone indicate prior knowledge by one of the three officers, all of whom, along with the insured entity, have claimed coverage. "Obviously excluded," you think to yourself after reading the first paragraph of the clear prior knowledge exclusion, which excludes from coverage any claim based on any act, error, or omission, of which, as of the inception date of the policy period, *any insured* knew and had reason to believe might give rise to a claim. Continuing to read the policy while also beginning to craft the declination letter in your mind, you reach the final paragraph of the same prior knowledge exclusion: "Knowledge possessed by an insured shall not be imputed to any other insured to determine if coverage is available."

How can these two clauses — the prior knowledge clause and the non-imputation clause — co-exist? And more specifically, what implications, if any, does this clause have on the prior knowledge clause immediately preceding it?

The policyholder will likely argue that the two clauses, read together, give rise to some ambiguity that the court should construe against the insurer, thus preserving coverage for innocent insureds. (Determining whether an insured is an *innocent* insured is likely to involve a fact-intensive inquiry and, depending on the language of the exclusion, employ a mixed subjective/objective analysis based largely — if not entirely — on circumstantial evidence rather than any proverbial "smoking gun.")

So long as an agent, director, officer or manager is deemed to have had pertinent knowledge, coverage should be excluded from the insured entity.

So, what about the two innocent insured officers? If the court concludes that an ambiguity exists that should be construed against the insurer, and the two innocent insured officers are found liable, the insurer will likely be on the hook for the portion of fault allocated to them, assuming a just allocation can even be made, up to the applicable policy limit. And, if the jury suspects or somehow learns that an insurer is covering the damages of certain insured defendants and thus that a victim is more likely to be made whole again, the jury may apportion all fault to those innocent insureds for whom coverage is available, exposing the insurer to the same risk that would exist without the prior knowledge exclusion.

To avoid this uncertainty and potential exposure, insurers and underwriters should ensure that their policies do not contain general non-imputation or severability provisions and, if a non-imputation or severability provision must exist, it is not embedded within or susceptible to application to an otherwise unambiguous "any insured" or "all insured" exclusion with which it may conflict. For example, a severability clause corresponding specifically to misrepresentations made in the *application* for insurance and for which the insurer may rescind may serve to prevent the carrier from rescinding the policy in its entirety. Still, the application-specific severability clause would not interfere with the carrier's reliance on a simple any-insured prior knowledge exclusion to exclude completely coverage for risks that were known by at least one of the insureds.

Again, most courts generally uphold an “any insured” exclusion as applying to all insureds, even if a severability clause is found elsewhere in the policy. But, by omitting general non-imputation provisions from a policy and from otherwise clear “any insured” exclusions, insurers can avoid — if not litigation (https://www.propertycasualty360.com/claims/litigation/) altogether — the time- and cost-intensive discovery necessary to identify innocent insureds and can further avoid questions regarding the allocation of fault, *i.e.*, policy proceeds, that would be required in affording coverage to only innocent insureds.

Marc Kamin (https://stewartsmithlaw.com/attorneys/marc-kamin/) is a partner with Stewart Smith, a Pennsylvania-based law firm specializing in insurance coverage work and litigation. He can be reached at 484.589.5506 and MKamin@StewartSmithLaw.com (mailto:MKamin@StewartSmithLaw.com).

Related:

- **Which is better: Deny coverage or defend under a reservation of rights? (https://www.propertycasualty360.com/2021/03/18/denying-coverage-vs-defending-under-a-reservation-of-rights-which-is-better/)**
- **Impact of the cross suits exclusion (https://www.propertycasualty360.com/2021/01/13/the-impact-of-the-cross-suits-exclusion/)**
- **Policy interpretation error clarified by Illinois Supreme Court** (https://www.propertycasualty360.com/2020/12/18/illinois-supreme-court-corrects-error-of-policy-interpretation-414-193379/)