IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MONTANA
HELENA DIVISION

VICTOR J. DONOVAN and RITA M. DONOVAN, RICHARD A. HILL and BETTI C. HILL, GEORGE L. STEVENS and GERTRUDE STEVENS, Plaintiffs, vs. CATLIN SPECIALTY INSURANCE COMPANY, Defendant.	CV-14-06-H-RKS **ORDER GRANTING DEFENDANT'S MOTION FOR SUMMARY JUDGMENT**

I. Synopsis

Plaintiffs are investors who sued their investment brokerage in an underlying action. Catlin insured the brokerage in the underlying action. Plaintiffs now allege Catlin violated the Montana Unfair Trade Practices Act in the underlying action by consolidating Plaintiffs' claims with others and applying a single policy limit to the consolidated claims, thereby reducing Plaintiffs' potential recovery.

Catlin is entitled to summary judgment on that claim. The insurance contract between Catlin and the investment brokerage provided for the consolidation of similar claims. That provision is valid under the applicable New York law. The provision and the relevant law provided Catlin with a reasonable basis to consolidate the claims.

Catlin also moved for summary judgment on an issue of potentially recoverable damages. Because Catlin is granted summary judgment on the UTPA claim, the damages issue may be moot. Ruling on that motion is reserved pending the parties' submission of status reports to clarify what, if any, issues remain pending.

II. Jurisdiction

Plaintiffs filed this lawsuit in Montana's First Judicial District, Lewis and Clark County. Doc. 1-1. Defendants removed the case to federal court on the basis of diversity jurisdiction. Doc. 1-2; 28 U.S.C. § 1332. The parties are completely diverse, as Plaintiffs are Montana residents and Defendant is a company incorporated under the laws of the State of Delaware, with its principal place of business in the State of Georgia. The parties consented to the jurisdiction of a magistrate judge. Doc. 3.

III. Status

Now pending are two Motions for Summary Judgment, both filed by Catlin. The first motion seeks judgment that Catlin's assertion of a $2 million policy limit did not constitute a breach of Montana's Uniform Trade Practices Act. Doc. 20. The second motion seeks a ruling that the only potential damages Plaintiffs may recover in this case are those arising from Catlin's alleged bad-faith conduct, not damages they sought to recover in the underlying claim against the insured. Doc. 25.

Both motions are fully briefed and supported by Defendant's statements of undisputed fact and Plaintiffs' statements of disputed fact. Docs. 21, 22, 26, 27, 29, 30, 31, 32.

IV. Standards

Summary judgment

The court shall grant summary judgment if there is no genuine issue of material fact and the movant is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(a). The party moving for summary judgment has the initial burden of showing there is no genuine issue of material fact. *Adickes v. S.H. Kress & Co.*, 398 U.S. 144, 157 (1970). If the moving party makes a prima facie showing that summary judgment is appropriate, the burden shifts to the opposing party to show the existence of a genuine issue of material fact. *Id*. On summary judgment, all

inferences should be drawn in the light most favorable to the party opposing summary judgment. *Id*. at 159.

A fact is material if it might affect the outcome of the suit under the governing law. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). The materiality determination rests on substantive law. *Id*. A dispute about a material fact is genuine "if the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Id.*

V. Facts

Plaintiffs purchased securities through Independent Financial Group. The securities turned out to be part of a ponzi scheme, and Plaintiffs did not get the distributions that they allege their brokers guaranteed. Doc. 7 (Complaint); Doc. 29 at 8.

Independent Financial Group was insured by Catlin, and notified Catlin of Plaintiffs' potential claims in April 2009. Catlin issued a Reservation of Rights letter in June 2009. Plaintiffs sued Independent Financial Group and individual brokers with the company in July 2009, alleging investment broker professional malpractice and other claims.[1] Catlin issued a second Reservation of Rights letter to Independent Financial Group in December 2009. Catlin disputed Independent

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Financial Group's liability as well as coverage for the claims under the policy. Catlin also maintained that 17 pending claims, including Plaintiffs' claims, were "interrelated wrongful acts," so if there was coverage, it was only for a single occurrence and subject to a policy limit of $2 million. Doc. 7. Defendants contend – and Plaintiffs do not dispute – that all of the consolidated claims were based on allegations relate to the claimants' purchase of fraudulent "Tenant-In-Common" interests in DBSI. See Defendants' Preliminary Pretrial Statement, Doc. 10 at 5. Defendants maintain that the claims are interrelated because they arise from Independent Financial Group's single, and allegedly insufficient, due diligence investigation into DBSI. Doc 10 at 5.

Before the case resolved, defense costs consumed the $2 million policy limit that Catlin contended was applicable, and Catlin withdrew from the case. Independent Financial Group and Plaintiffs settled without Catlin's input. Doc. 5 at 7.

Independent Financial Group is not a party to this action. Plaintiffs do not allege that they have been assigned claims against Catlin by Independent Financial Group.

Plaintiffs allege that Catlin acted in bad faith by providing $2 million for all 17 claims, rather than the policy's $8 million aggregate limit. Doc. 7. Plaintiffs

argue that Defendants' position constituted failure to promptly settle Plaintiffs' claims after liability had become reasonably clear, in violation of the Montana Unlawful Trade Practices Act. Doc. 7 at 7. Plaintiffs allege this "bad faith" caused them $3 million in actual damages, and contend that punitive damages should also be imposed. Doc. 7.

Catlin contends that its coverage position in the underlying suit was correct, or at lease not in bad faith because it had a reasonable legal basis. Doc. 9 at 2.

VI. Analysis

A. Good faith basis

Plaintiffs argue that by the time of the December 2010 mediation, it was reasonably clear that Independent Financial Group was liable to Plaintiffs, and that the claims against Independent Financial Group were not interrelated acts as the policy used the term. Doc. 11 at 8.

Plaintiffs' claims are premised on Montana's Unfair Trade Practices Act, Mont. Code Ann. § 33-18-201.[2] Doc. 11 at 9. That statute provides, in part:

> A person may not . . . do any of the following :
>
> (1) misrepresent pertinent facts or insurance policy provisions relating to coverages at issue;

[2]By statute, Montana law provides an independent cause of action for a third-party claimant alleging an insurer has violated certain subsections of this statute, including those at issue here. Mont. Code Ann. 33-18-242(1)

> (6) neglect to attempt in good faith to effectuate prompt, fair, and equitable settlements of claims in which liability has become reasonably clear.

In the underlying action, Plaintiffs alleged Independent Financial Group violated Financial Industry Regulatory Authority (FINRA) by failing to recommend investments to Plaintiffs in accordance with each Plaintiff's investor profile. Doc. 7 at 5.[3] Plaintiffs argue that the claims were not "interrelated wrongful acts" because each claim arises from a different investor with a unique investor profile, and is based on numerous transactions that occurred over a span of years. Doc. 7 at 6.

An insurer may not be held liable for an alleged violation of § 33-18-201 if the insurer had a reasonable basis in law or in fact for contesting the claim or the amount of the claim. Mont. Code Ann. § 33-18-242(5). An insurer asserting this affirmative defense has the burden of establishing it by a preponderance of the evidence. *Redies v. Attorneys Liab. Protec. Soc.*, 150 P.3d 930, 937 (Mont. 2007). In a summary judgment proceeding where the insurer's asserted basis for contesting a claim is grounded on a legal conclusion, and no issues of fact remain

[3]The FINRA suitability rule (Rule 2111) required IFG to make recommendations in accordance with each investor's age, other investments, financial status and needs, tax status, investment objectives, investment experience investment time horizon, liquidity needs, risk tolerance, and any other information the investor disclosed. See Defendant's Statement of Undisputed Facts, Doc. 27 at 5; Plaintiffs' Statement of Disputed Facts, Doc. 32 at 7-8.

in dispute, it is for the court to determine whether the precedent sufficiently provides a defense to the bad-faith action. *Watters v. Guar. Nat. Ins. Co.*, 3 P.3d 626, 639 (Mont. 2000) *overruled on other grounds by Shilhanek v. D-2 Trucking, Inc.*, 70 P.3d 721 (Mont. 2003).

Catlin contends that they had a reasonable basis in law for contesting both the claim and the amount of the claim. Defendants argue that specific liabilities alleged in the underlying claims were not covered by the insurance policy, and that the claims were interrelated acts, with a single $2 million policy limit. Doc. 21.

i. New York law provides the "legal landscape."

Catlin's insurance contract with Independent Financial Group included a provision that laws of the State of New York would govern "issues pertaining to meaning, interpretation and effect" of the policy. Catlin argues that the reasonableness of their coverage positions therefore depends on New York law.[4] Doc. 21 at 4.

Plaintiffs argue that the choice-of-law provision should not apply in this case because the provision was part of a contract between Catlin and Independent Financial Group: Plaintiffs did not agree to the provision. Plaintiffs argue that the

[4]Defendants do not dispute the applicability of the Montana Unfair Trade Practices Act to this law. Rather, their argument is that the analysis should focus on whether their claims-handling practice had a good-faith basis under New York law during the relevant period. Doc. 38 at 11.

provision should be disregarded because the conduct at issue occurred in Montana and application of New York law would contravene public policy. Doc. 29 at 11 (citing *Modroo v. Nationwide Mut. Fire Ins. Co.*, 191 P.3d 389, 400 (Mont. 2008).

Federal courts sitting in diversity apply the law of the forum state to a choice of law determination. *Ticknor v. Choice Hotels International, Inc.,* 265 F.3d 931, 937 (9th Cir.2001). Accordingly, the Court applies Montana's choice of law rules to determine which state law governs the interpretation of the contract.

Montana will generally respect a contractual choice-of-law provision unless three factors are met: (1) if, but for the choice-of-law provision, Montana law would apply(2) if Montana has a materially greater interest in the particular issue than the state chosen by the parties; and (3) if applying the state law chosen by the parties would contravene a fundamental policy of Montana. *Modroo v. Nationwide Mut. Fire Ins. Co.*, 191 P.3d 389, 400 (Mont. 2008) (applying *Restatement (Second) of Conflict of Laws § 187 (2)(b)).*

Here, the *Modroo* criteria are not satisfied. The choice-of-law provision was part of a contract between Catlin and Independent Financial Group. Montana law would not apply to a provision of a contract between two out-of-state parties that was not performed in Montana and Montana does not have a materially greater interest than New York in the disputed between the insured and the insurer.

Plaintiffs' argument that the choice-of-law provision contravenes a fundamental Montana policy, even if true, would not justify disregarding the provision because the two preceding *Modroo* factors are not satisfied.

The choice-of-law provision in the contract between Catlin and Independent Financial Group is valid. New York law provides the "legal landscape" that must be considered to determine if Catlin had a reasonable basis to dispute the existence or amount of coverage.

ii. Under New York law, the "Interrelated Wrongful Acts" is valid.

The insurance policy provides:

Interrelated Wrongful Acts means any Wrongful Acts that are:

1. Similar, repeated or continuous; or

2. Connected by reason of any common fact, circumstance, situation, transaction, casualty, decision or policy or one or more series of acts, circumstances, situations, transactions, casualties, events, decisions or policies.

Doc. 7-1 at 8 (policy).

"Wrongful Act" means "a negligent act or omission . . . committed by an Insured in the rendering of a Professional Services."

Doc. 7-1 at 10.

The Interrelated Wrongful Acts provision is valid under New York law. In

Quanta Lines Insurance Co. v. Investors Capital Corp., 2009 WL 4884096, *14-15 (S.D.N.Y.), a federal district court applying New York law approved application of the exact provision at issue here under similar facts. Plaintiffs provide no authority to suggest any court has found the provision invalid under New York law.

iii. The "Interrelated Wrongful Acts" provision provided Catlin with a reasonable basis to consolidate plaintiffs' claims with others.

In *Quanta Lines Insurance* the federal court, applying New York law to an identical "Interrelated Wrongful Acts" provision, held that separate demands alleging an insured fraudulently sold unregistered securities shared a "sufficient factual nexus" and therefore were "interrelated wrongful acts" under the policy at issue. *14-15. Courts in other jurisdictions have also upheld equivalent provision on substantially identical facts. *Capital Growth Financial LLC v. Quanta Specialty Lines Insurance Co.*, 2008 WL 2949492 (S.D. Fla. 2008); *Bracek & Young Advisors, Inc. v. Lloyds of London Syndicate 2003*, 2012 WL 5569242 (D. Neb. 2012).

The claims Catlin consolidated arose from allegations that related to a single entity's fraudulent securities and from Independent Financial Group's single investigation into that entity. Precedential cases provided a reasonable basis for Catlin to assert that the claims could be consolidated with others under a single

policy limit. That satisfies the criteria for Unfair Trade Practices Act's safe harbor provision, Mont. Code Ann. § 33-18-242(5). Montana law does not require insurers to hand over a blank check for every claim. It simply provides that an insurer must have a reasonable basis to contest the existence or amount of coverage. Catlin and Independent Financial Group formed a contract for insurance that included a choice-of-law provision and a broad Interrelated Wrongful Acts provision. Catlin has cited on-point cases in which similar or identical provisions were held to be applicable in similar or identical circumstances. Catlin has met its burden to establish a reasonable basis for consolidating Plaintiffs' with others.

Plaintiffs have advanced no persuasive reason that the contract provisions should not be enforceable between the insurer and the insured. Moreover, Plaintiffs have not show that they, as a third party, are entitled to damages for Catlin's application of the provisions with respect to Independent Financial Group's claim.

Based on the undisputed facts, Catlin is entitled to summary judgment.

B. The motion for summary judgment regarding damages is moot.

The parties appear to agree that only damages arising from any bad faith conduct in the underlying litigation are recoverable in this action, and that Plaintiffs cannot "double recover" the same damages they already recovered in the

underlying action. Docs. 26 at 7, 31 at 10. The parties appear to dispute whether Plaintiffs can now recover damages that were *alleged* but not *recovered* in the underlying action. Docs. 26, 37.

The summary judgment ruling in Defendant's favor on the bad-faith claim, discussed above, may render moot the damages issued presented in doc. 25. Ruling on the damages issue will be reserved, subject to the parties' status reports (discussed below).

C. Remaining issues

This Order grants summary judgment to Catlin as to Plaintiffs' claim that Catlin violated the Unfair Trade Practices Act by consolidating their claims with others under a single $2 million policy limit. Though Catlin's motion, doc. 20, is described as motion for partial summary judgment, this ruling appears to dispose of the entire case.

Each party should file a status report describing what claims they believe remain pending and whether Catlin's motion for summary judgment as to underlying claim damages (doc. 25).

It is ORDERED:

1. Defendant's Motion for Summary Judgment, Doc. 20, is **GRANTED**.

2. Ruling on Defendant's Motion for Partial Summary Judgment, Doc. 25, is **RESERVED.**

3. Each party is ORDERED to file a status report as described in this order on or before September 5, 2014.

Dated the 25th day of August, 2014.

Keith Strong
United States Magistrate Judge