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Avoiding The MDL For Insurance Coverage Disputes

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Law360, New York (July 06, 2010, 11:46 AM ET) -- When similar lawsuits, involving common factual allegations, are pending in multiple federal districts, the Judicial Panel on Multidistrict Litigation (the “Panel”) is empowered to transfer all such lawsuits to any one federal court for coordinated and consolidated pretrial proceedings. The Panel transfers cases that contain common facts and, thus, will conduct common discovery.

The Panel is a group of seven federal judges designated by the Chief Justice of the United States and authorized by 28 U.S.C. § 1407 to determine which cases qualify for multidistrict litigation (“MDL”) treatment. Under 28 U.S.C. § 1407, the Panel may transfer cases “for pre-trial purposes” upon a finding that the transfers will result in the convenience of the parties and witnesses and will promote the just and efficient conduct of the cases.

In addition to securities fraud, antitrust and other federal law actions, the MDL procedure has often been used in mass tort cases to coordinate and consolidate discovery of common facts.

Recent examples include numerous lawsuits claiming injury allegedly caused by installation of defective Chinese-made drywall (In re: Chinese-Manufactured Drywall Products Liability Litigation, MDL No. 2047 (J.P.M.L. June 15, 2009)) (“Chinese Drywall MDL”) and claims of injury allegedly related to formaldehyde off-gassing from trailers supplied by [FEMA](#) as temporary shelter for people displaced by Hurricanes Katrina and Rita. Such mass disasters often generate insurance coverage disputes, and recent proceedings in the Chinese Drywall MDL suggest a possible trend by plaintiffs’ counsel in the underlying matters of attempting to bring insurance coverage actions into the underlying MDL.

Recently, the Chinese Drywall MDL has been the battleground for a fight among underlying plaintiffs, insureds and insurers as to whether insurance coverage actions should be transferred there. Numerous attempts have been made to transfer insurance coverage declaratory judgment actions to

the Chinese Drywall MDL.

The underlying plaintiffs have argued that the insurance coverage actions involve “common facts” because the insurance coverage analysis must consider the facts of the underlying disputes. The plaintiffs seeking transfer have also argued that insurance policies often have “common” language and that transfer is warranted to ensure consistent application of policy terms and to promote settlement.

Appearing to agree with the underlying plaintiffs’ perspective, the judge presiding over the Chinese Drywall MDL, Judge Eldon E. Fallon, invited transfer of insurance disputes, stating: “the insurance issues ... are better and more efficiently dealt with if they are transferred to the MDL.”

Opposing transfer, insurers have argued that the Chinese Drywall MDL does not make sense for the overlaid insurance coverage disputes. Despite superficial appearances, the facts in dispute are not truly common: the facts at issue in the MDL provide a backdrop for the insurance coverage lawsuits, but in the insurance context, these “underlying” facts typically will be undisputed. Instead, discovery in the insurance coverage actions will focus on the specific insurance policies at issue and the specific facts of a particular underlying loss or complaint.

Second, the parties to insurance coverage declaratory judgment matters seek speedy resolutions. A quick resolution of the parties’ rights and obligations relating to an insurer’s duty to defend or indemnify can eliminate uncertainty and benefit both the insurer and the policyholder. With the underlying plaintiffs and some policyholders seeking consolidation and the insurers opposed, the battle lines were drawn in the Chinese Drywall MDL to test this new trend.

History of the Chinese Drywall MDL

On June 15, 2009, the Panel established the Chinese Drywall MDL by transferring 10 actions to the Eastern District of Louisiana. The original consolidated lawsuits generally involve individual or putative class action plaintiffs seeking relief arising from Chinese Drywall installed in the plaintiffs’ homes.

According to the transfer order, these products liability lawsuits “share[d] factual questions concerning drywall manufactured in China, imported to and distributed in the United States, and used in the construction of houses.”

Early Attempts to Incorporate Insurance Disputes to the Chinese Drywall MDL

Although none of the consolidated actions is an insurance coverage dispute, almost immediately attempts began to expand the Chinese Drywall MDL to include insurance disputes. The Panel rejected the first few attempts.

First, on Dec. 2, 2009, the Panel rejected transfer of an insurer’s declaratory judgment action in *Gen. Fid. Ins. Co. v. Katherine L. Foster et al.* (S.D. Fla. C.A. No. 9:09-80743).

Accepting the insurer’s position, the Panel observed that “[p]laintiffs in the majority of the actions in the Chinese Drywall MDL are individuals who seek relief related to property damage or personal injuries arising from drywall manufactured in China and installed in their homes,” whereas “[t]he plaintiff insurance company in the declaratory judgment action before the Panel seeks to determine its

rights and obligations under a commercial general liability policy.”

Holding that the insurance coverage declaratory judgment action did not share sufficient questions of fact with the products liability actions to meet the requirements of 28 U.S.C. § 1407, the Panel vacated the order to conditionally transfer the insurance coverage matter to the Chinese Drywall MDL.

Similarly, on Feb. 5, 2010, in *Builders Mutual Ins. Co. v. Dragas Mgmt. Corp et al.* (E.D. Va. C.A. No. 2:09-185), the Panel again denied a motion to transfer an insurance coverage lawsuit because the interpretation of insurance policies does not “share sufficient questions of fact ... related to property damage or personal injuries arising from drywall manufactured in China and installed in their homes.”

As part of its ruling, the Panel stated: “given that this declaratory judgment action is not related to any action pending in [the Chinese Drywall MDL], transfer would not serve the convenience of the parties and witnesses or promote the just and efficient conduct of the litigation.”

However, in its third decision, the Panel appeared to open the floodgates to the transfer of insurance coverage actions to the Chinese Drywall MDL. On April 5, 2010, the Panel ordered the transfer of *Owners Insurance Co., et al. v. The Mitchell Co. Inc., et al.* (M.D. Ga. C.A. No. 5:09-373) to the MDL.

It is not apparent on the face of the Panel’s April 5 order why the Mitchell Company lawsuit was carved out for special treatment, and the Panel did not indicate any intent to overrule its prior decisions denying transfer. However, the order does note that “the claims in this insurance declaratory judgment action are related to products liability claims in an action that the Panel transferred to [the Chinese Drywall MDL] with its original transfer order in this docket.”

Seizing on the Panel’s order in Mitchell Company, the Plaintiffs’ Steering Committee in the Chinese Drywall MDL sent the Panel an ex parte letter, dated April 9, 2010, listing the captions of 23 additional insurance coverage disputes pending in six different federal jurisdictions, and labeling these insurance coverage disputes “tag along” lawsuits which should all be transferred based on the Mitchell Company order.

The Panel did not initially respond to this request, even declining to docket the letter. However, after five weeks, the Panel responded with an order conditionally transferring four of the 23 actions, but subject to further briefing and consideration. That briefing is ongoing.

The Panel remained silent with respect to the other 19 actions listed in the letter. Perhaps flummoxed by the Panel’s silence on the remaining actions, the Plaintiffs’ Liaison Counsel and Plaintiffs’ Lead Counsel filed a Motion for Designation of Potential Tag-Along Actions dated May 28, 2010, more formally seeking transfer of 17 of the 23 insurance coverage lawsuits previously listed.

In the meantime, yet another transfer motion in *Chartis Specialty Ins. Co., et al. v. Banner Supply Co., et al.* (M.D. Fla. C.A. No. 8:10-330) was being presented to the Panel for its May 27, 2010 hearing date. Numerous insurers intervened in the briefing of the Banner Supply matter to set forth the legal and common sense arguments against pulling insurance coverage issues into the underlying products liability MDL.

On June 15, 2010, the Panel responded with an order in *Taylor Woodrow Communities at Vasari LLC*

v. Mid-Cont. Cas. Co. (S.D. Fla. C.A. No. 2:09-823); Chartis Specialty Ins. Co., et al. v. Banner Supply Co., et al (M.D. Fla. C.A. No. 8:10-330); and Gen. Fid. Ins. Co. v. Katherine L. Foster et al., (S.D. Fla. C.A. No. 9:09-80743). This order is its most comprehensive and important holding on this issue to date.

The order denies transfer of these three insurance coverage declaratory judgments. Specifically referencing the many insurer briefs, the Panel held that insurance coverage declaratory judgment actions do not meet the requirements for transfer set forth in 28 U.S.C. § 1407 where “the cases present strictly legal questions which require little or no centralized discovery.”

Although the Panel stressed that transfer of insurance coverage actions must be decided, case-by-case, on the facts of each lawsuit, the Panel concluded more generally that insurance coverage lawsuits do not share common questions of fact with the products liability lawsuits and sufficient conveniences or other benefits such as serving judicial efficiency do not justify transfer.

In short, the fact that insurance declaratory judgment actions and the underlying proceedings “do have a common factual backdrop involving the general circumstances of imported Chinese Drywall and the damage it is alleged to have caused,” is not sufficient to warrant transfer under 28 U.S.C. § 1407.

The Panel found, instead, that “[e]ach of the insurance coverage questions in these cases is likely to be decided by an application of the complaint to the policy language under the applicable state law.”

The Panel deemed that “the most important consideration” in denying transfer is whether “the insurance coverage actions require and rely on the same factual discovery as the underlying tort actions.” Commenting on the plaintiffs’ suggestion that insurance actions should be transferred to promote settlement, the Panel made clear that such considerations, while, perhaps “a sometime by-product,” were “not a statutory rationale.”

Just two days after the Panel’s recent June 15 order, the Plaintiffs’ Steering Committee withdrew its tag-along motion because “the Panel’s reasoning would apply here, making additional efforts by those involved moot.” Thus, it appears that the efforts to effect a wholesale transfer of insurance coverage actions to the Chinese Drywall MDL are over.

Roadmap for Insurers in Future MDL Actions

The Panel’s decisions relating to the transfer of insurance coverage actions to the Chinese Drywall MDL provide a roadmap to other insurance companies in future MDL actions to avoid transfer and consolidation of insurance coverage lawsuits when the underlying matters are in an MDL.

The major lesson learned from the Chinese Drywall MDL is that the strict application of 28 U.S.C. § 1407(a) to insurance coverage actions counsels against wholesale consolidation of such actions with the underlying proceedings. Pursuant to Section 1407(a), transfer of "civil actions involving one or more common questions of fact" are permitted for pretrial purposes, when such a transfer serves "the convenience of the parties and witnesses and promote[s] the just and efficient conduct of such actions."

However, as the Panel recognized in its June 15 order, the issues for resolution in insurance coverage declaratory judgment actions typically are predominantly legal – the application of contract language to the facts of the claim – and any disputed facts and discovery generally implicate facts that are

unique to the insurance coverage relationship, namely, the specific insurance policies and their formation and the details of the claim.

Further, the disputed legal issues are usually state questions. As a result, judges in states having jurisdiction over the disputes can normally be presumed to have more familiarity with the state law to be applied than an MDL judge who may be venued in a state having no connection to the parties, the contracts or the subject matter of the insurance contract dispute.

To avoid transfer, parties can also compare the discovery sought in the MDL with the discovery in the insurance declaratory judgment action to demonstrate that discovery in the MDL action focuses on the underlying facts, not the insurance claim.

Finally, cases that would inconvenience the parties and witnesses as well as not be in the interest of justice will not be transferred under the Panel's recent holding. In many instances, all of the core relevant discovery in an insurance coverage action will be located in the jurisdiction where the district court case is pending, bearing no relationship whatsoever to the MDL action jurisdiction.

Even if the parties seeking transfer are unsuccessful under Section 1407, those opposing transfer should be prepared for a "back door" approach. In several Chinese Drywall matters, underlying plaintiffs have also sought transfer to the MDL by using the general venue provisions of 28 U.S.C. § 1404(a).

Transfer under this provision is only permitted "to any other district or division where [the lawsuit] might have been brought." Thus, this tactic should not prevail in most cases, because the court where the MDL action is located will likely not be a federal district in which the declaratory judgment action could have been brought either as a matter of personal jurisdiction or federal venue requirements.

Although the MDL may sometimes present an efficient and effective means to resolve complex disputes, it is clear in the Chinese Drywall MDL that any related insurance coverage issues can most efficiently be resolved in separate lawsuits focused on each unique insurance dispute. Insurers effectively presented these arguments to the Panel, and the Panel listened, appropriately applying 28 U.S.C. § 1407 and creating a roadmap for similar issues that may arise in the future.

--By Catherine M. Colinvaux and Seth V. Jackson, [Zelle Hofmann Voelbel & Mason LLP](#)

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