

Client Alert

October 2016

Imprecise Policy Language Results in Coverage for FDIC Action Against Directors and Officers of Defunct Bank

The United States Court of Appeals for the Ninth Circuit held in *St. Paul Mercury Ins. Co. v. Federal Deposit Ins. Corp.*, No. 14-56830 (9th Cir. Oct. 19, 2016), that an action by the FDIC against a defunct bank's former directors and officers did not trigger the "insured versus insured" exclusion in the bank's D&O policy because it was ambiguous as to whether the FDIC action was "on behalf of" the bank and, thus, within the scope of the exclusion.

Background

In November 2009, the Office of the Comptroller of the Currency closed Pacific Coast National Bank and appointed the FDIC as receiver. In November 2012, the FDIC sued numerous former directors and officers of the defunct bank, alleging tortious conduct, including breaches of fiduciary duty and gross negligence, in connection with the bank's lending practices.

The bank and its directors and officers were insured under a management liability policy issued by Travelers Companies, Inc. (Travelers), the parent of St. Paul Mercury Insurance Company. Travelers filed suit in federal court against the insured directors and officers and the FDIC seeking a declaratory judgment that the policy's "insured versus insured" exclusion barred coverage for the FDIC's claims. The exclusion purported to bar coverage for claims against an insured "by or on behalf of any Insured or Company in any capacity." Travelers argued the exclusion applied because the FDIC, as receiver, asserted claims against the directors "on behalf" of the bank, also an insured under the policy. The court rejected Travelers' argument and granted summary judgment to the FDIC, finding that the phrase "on behalf of," as used in the exclusion, was ambiguous.

Appeal

The Ninth Circuit affirmed. The court found ambiguity as to whether the FDIC's suit was "on behalf of" the bank where the FDIC represented multiple interests in its role as receiver, only one of which was as the bank's successor-in-interest. The court further found that Travelers could have simply excluded coverage for FDIC actions, but chose not to do so. The court found this to be indicative of Travelers' intent to cover FDIC actions here, given Travelers' use of a "regulatory exclusion" endorsement to specifically exclude coverage for FDIC actions in other policies. This also conflicted with what the court said was the bank's reasonable expectation of coverage. Likewise, the absence of such an exclusion in Pacific Coast's policy was further support of ambiguity. Finally, the court noted that identical policy language had previously been found to be ambiguous by the Eleventh Circuit in a similar FDIC proceeding, which the Ninth Circuit refused to disregard in the absence of any indicia that the other circuit's construction was "clearly erroneous."

Implications

The Ninth Circuit's decision illustrates the breadth of coverage available to banks for FDIC actions, and potentially other regulatory claims, in the absence of express regulatory exclusions. The decision likewise confirms the narrow scope of the "insured versus insured" exclusion and how that exclusion was not intended to apply in the case of regulatory enforcement actions, even where the action is brought "on behalf" of the insured entity.

The decision also illustrates the importance of understanding how courts in other jurisdictions have interpreted similar policy provisions as well as how insurers have treated similar risks in other policies and product lines. This is particularly important in the case of policy ambiguities, where courts often will look for guidance beyond the four corners of the policy. Qualified coverage counsel can help identify this extrinsic information and present arguments that help explain otherwise ambiguous policy language.

Contacts

Walter J. Andrews
wandrews@hunton.com

Lawrence J. Bracken II
lbracken@hunton.com

Michael S. Levine
mlevine@hunton.com

Matthew T. McLellan
mclellanm@hunton.com

Syed S. Ahmad
sahmad@hunton.com

John C. Eichman
jeichman@hunton.com

Sergio F. Oehninger
soehninger@hunton.com