

Exclusion for "Liability Assumed Under Contract" Does Not Exclude All Breach of Contract Claims

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The United States District Court for the Eastern District of Pennsylvania, applying Pennsylvania law, has denied summary judgment for an insurer and granted summary judgment for an insured, holding that an exclusion for "liability assumed under contract" does not preclude coverage for an insured bank's alleged wrongful failure to extend credit to a customer. *Cincinnati Ins. Co. v. Stonebridge Fin. Corp.*, 2011 WL 2549975 (E.D. Pa. June 23, 2011).

The insured bank issued two loan commitment agreements in which the insured agreed to extend credit of approximately \$5 million to a customer. The customer sued the bank, alleging that it failed to show up at the closing and thereby breached its obligation to extend credit to the customer. The insured submitted the underlying action to its E&O insurer. The E&O policy provided specified coverage for loss from any claim for "any actual or alleged error, misstatement, misleading statement, act, omission, neglect or breach of duty committed . . . by . . . [the insured] in the performance of 'professional services.'" "Professional services" means "activities allowed under the law and regulations governing financial institutions which are performed for or on behalf of any client or customer of [the insured]." The policy included a contractual liability exclusion, which precluded coverage for "legal liability assumed by any of the 'policy insureds' under the terms, conditions, or warranties of any oral or written agreement, or by virtue of any waiver or release from liability of any third party." The policy also included a Financial Institution Coverage endorsement providing coverage for "any claim or claims arising out of any 'wrongful lending act' related to an extension of credit or refused extension of credit to a 'borrower.'" The E&O insurer agreed to defend the underlying suit under a reservation of rights and subsequently sought a declaratory judgment that coverage was barred by the contractual liability exclusion.

The court held that the contractual liability exclusion did not preclude coverage for the underlying action. The court rejected the insurer's reliance on case law denying coverage for breach of contract claims under comprehensive general liability (CGL) policies, noting that "E&O policies differ substantially from CGL policies" and that E&O policies "provide coverage for liability resulting from covered acts, errors or omissions in performance of professional services." The court also rejected the insurer's argument that public policy considerations prohibit providing coverage for breach of contract claims. Further, the court held that the

contractual liability exclusion at issue for "liability assumed under contract" applies "only to instances where the insured agrees to 'assume' the tort liability of a third party, such as in indemnification and hold harmless agreement." The court also noted that when the policy is read to include the Financial Institution Coverage endorsement, which provided coverage for "claims arising out of any 'wrongful lending act' . . .," the insured "reasonably expected the [p]olicy to cover 'all lender liability practices,' whether asserted in negligence or breach of contract."

Having concluded that the contractual liability exclusion does not apply, the court held that the insured's alleged conduct falls within the definition of "professional services." The court stated that "courts consider an insured's conduct a 'professional service' if it: (1) arises out of the insured's day-to-day business operations; (2) involves specialized knowledge or skill; or (3) implicates a special risk inherent in the practice of the insured profession." The court held that the insured's alleged conduct of failing to extend credit under an agreement it believed had expired fell within all three of the above categories.

Finally, the court rejected the insurer's contention that the duty to indemnify was not ripe because the underlying litigation was still pending. The court held that Pennsylvania law allows a court to determine whether the insurer has a duty to indemnify in the event of liability. Accordingly, the court held that the insurer had a duty to defend the insured and to indemnify the insured in the event the insured eventually is found liable.