

I v. I Exclusion Does Not Bar Coverage for ERISA Breach of Fiduciary Duty Claims Where Fund Trustee Was Plaintiff in Underlying Action

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A federal district court, applying New York law, has held that the insured v. insured exclusion in a Trustee and Fiduciary Liability Policy did not apply to bar coverage for a suit brought by the chairman of the board of trustees and two plan participants. *Bodewes v. ULICO Cas. Co.*, 2004 WL 2168396 (W.D.N.Y. Sept. 25, 2004).

An insurer issued a Trustee and Fiduciary Liability Policy to a union pension fund. The policy provided coverage for "any Loss...[that the Insureds] shall become legally obligated to pay...by reason of any Wrongful Act...committed or alleged to have been committed by the Insureds...while acting in any capacity directly connected with such Trust...." The policy defined "Insureds" as "the Trustees (including Past and Future) of the Trust...while acting in their capacity as such." The policy also contained an insured v. insured exclusion that "specifically excludes any claim or allegation which, directly or indirectly, in whole or in part, arises out of any assertions, allegations, causes of action or demands whatsoever by or on behalf of an Insured or Insureds under this certificate against another Insured or Insureds hereunder."

Prior to the expiration of the policy period, an official of the pension fund notified the insurer that an investigation had revealed that claims would likely be made under the policy based on the fund's declining financial viability. Subsequently, the chairman of the board of trustees of the plan and two fund participants brought an ERISA action seeking equitable relief and damages based on alleged breaches of fiduciary duties by eight current and former trustees of the pension fund. The complaint further set forth claims against the pension fund's former actuarial firm. The claims against the actuarial firm were settled, and the chairman withdrew as a plaintiff.

The insurer denied coverage based on, *inter alia*, the insured v. insured exclusion in the policy, maintaining that the participation of the chairman as a plaintiff triggered application of this exclusion. The defendant trustees in the underlying action filed third-party claims against the insurer seeking defense and indemnification under the policy, which were severed from the underlying action to be tried separately.

The district court held that the policy provided coverage for the underlying action, notwithstanding the fact that the chairman was a plaintiff. The court, citing cases such as *Level 3 Communications, Inc. v. Federal Ins. Co.*, 168 F.3d 956 (7th Cir. 1999), asserted that the primary purpose of the insured v. insured exclusion is the prevention of collusive suits whereby companies seek to recoup losses suffered through poor business judgment by asserting claims against D&O policies. The court stated that reliance on such cases "is neither entirely accurate nor entirely helpful" and that "no case has been found or cited in which an insurer has successfully excluded coverage for a claim of breach of ERISA fiduciary duties based on and 'Insured v. Insured' exclusion in a trustee liability policy."

Following *QBE International Ins. Ltd. v. Clark*, 2003 WL 22433117 (N.D.Ill. Oct. 24, 2003), in which the court rejected the application of the insured v. insured exclusion to claims brought against the trustees of a failed workers compensation trust by its liquidator because such application would bar claims of both the trust and participants, the district court held that applying the exclusion would "have the effect of expanding the scope of the 'insured v. insured' exclusion, in contravention of the well-settled principle of New York law that exclusion clauses must be narrowly construed." The court also noted that "it is beyond dispute" that the ERISA statute authorized both the participants and the chairman to bring the underlying action and that the "interests of the parties to that action are 'genuinely adverse.'" The court held that applying the exclusion in such circumstances "'would thwart the intentions and purposes of the contracting parties.'"

The district court also rejected the insurer's argument that the presence of the chairman as a plaintiff and the operation of the insured v. insured exclusion barred any coverage for the claims of the participants. The court specifically distinguished the case on which the carrier relied, *PowerSports, Inc. v. Royal & Sunalliance Ins. Co.*, 307 F. Supp.2d 1355 (S.D. Fla. 2004), because that case involved underlying litigation initiated solely by an insured. In contrast, the court noted that here two of the three original—and the only remaining—plaintiffs were plan participants with a clear statutory right to prosecute their claims against the trustees. Overall, the court held that "adopting the interpretation of the 'Insured v. Insured' exclusion urged by [the insurer] would render superfluous the bargained-for provision of coverage for claims made against the trustees in the underlying action."

The court also rejected the insurer's reliance on the "insufficient contributions" exclusion in the policy as a basis for denying coverage, holding that the breach of fiduciary duty claims in the underlying action "are independent of any liability related to the failure of the pension fund to collect sufficient employer contributions." Similarly, the court granted the pension fund's motion to strike the other affirmative defenses asserted in the insurer's answer, which included insufficient notice, failure to satisfy conditions precedent to coverage and known risk.

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