

ALERT

Insolvency Exclusion Bars Coverage for Claims Due to Underfunded Employee Benefit Plans

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A federal district court, applying Pennsylvania law, has held that the insolvency exclusion in an insurance agency's professional liability policy excused the insurer from the duty to defend the agency in lawsuits alleging that it had caused employee benefit plans that it created to be underfunded. *ACE Capital Limited v. Morgan Waldon Ins. Management, LLC*, Civil Action No. 11-128, 2011 WL 5914275 (W. D. Pa. Nov. 28, 2011).

The insurance agency designed and created employee benefit plans for the employees of unions. After some of the plans ran into financial trouble, several of the unions filed suit against the insurance agency, alleging that it had wrongfully caused the employee benefit plans to be underfunded and therefore unable to pay all of the benefits promised to the union employees. The agency tendered the lawsuits to its insurer, which agreed to defend the agency, subject to a reservation of rights. The insurer then filed a declaratory judgment action against the insurance agency and the unions, seeking a determination that it did not have a duty to defend or indemnify the agency in the lawsuits.

Faced with cross-motions for summary judgment, the court ruled in favor of the insurer based on the policy's insolvency exclusion. The insolvency exclusion provided that the insurer "will not defend any Claim or pay any Damages or Claim Expenses based upon, arising out of, directly or indirectly relating to or in any way involving . . . [i] nsolvency, bankruptcy, liquidation, receivership, rehabilitation or financial inability of the following, including but not limited to the failure, inability or unwillingness to pay Claims, losses or benefits due to the insolvency or bankruptcy of" the listed entities, which included an "[e]mployee benefit plan" and a "[s]elf-insured program." After

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reviewing cases interpreting other insolvency exclusions, the court concluded the exclusion at issue was unambiguous and its broad wording precluded any duty to defend the insurance agency in the unions' lawsuits because the allegations in the suits "related to" the insolvency of the employee benefit plans. The court noted that the exclusion applied even though the insurance agency's alleged mistakes in underfunding the plans occurred prior to the insolvencies. The court also held that the "underlying purpose" of the exclusion could not be used to create an ambiguity. Finally, the court rejected the insurance agency's arguments that application of the insolvency exclusion would defeat its reasonable expectations and would render the policy's coverage illusory. Accordingly, the court granted the insurer summary judgment.