

ALERT

California State Law Does Not Bar Defense for Federal Prosecution

May 13, 2013

An intermediate appellate court in California has held that Section 533.5(b) of the state insurance code does not apply to preclude insurance coverage for criminal actions brought by federal prosecutors. *Mt. Hawley Ins. Co. v. Lopez*, 2013 WL 1818627 (Cal. Ct. App. May 1, 2013).

A United States Attorney brought federal charges against an insured physician, alleging that he had transplanted a liver into a patient who was not next in line on the “waiting list” in violation of applicable federal regulations. The insurer refused to provide a defense, contending that Section 533.5(b) precluded it from doing so. This provision of the insurance code states:

No policy of insurance shall provide, or be construed to provide, any duty to defend . . . any claim in any criminal action or proceeding or in any action or proceeding brought pursuant to [California’s unfair competition law] in which recovery of a fine, penalty, or restitution is sought by the Attorney General, any district attorney, any city prosecutor, or any county counsel, notwithstanding whether the exclusion or exception regarding the duty to defend this type of claim is expressly stated in the policy.

Citing to the federal appellate court’s opinion in *Bodell v. Walbrook Ins. Co.*, 119 F.3d 1411 (9th Cir. 1997), the insured argued that the proscription on coverage set out in the statute applied only to prosecutions by the state and local authorities. The state appellate court agreed, holding that Section 533.5(b) did not apply to criminal actions prosecuted by the federal government. In reaching this conclusion, the court rejected the insurer’s argument that the statute

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was limited to prosecutions by the four identified state and local authorities only with respect to civil actions brought under the state's unfair competition laws and that coverage for all other criminal actions was prohibited, regardless of the prosecuting authority. The court also pointed out that "there is no public policy in California against insurers contracting to provide a defense to insureds facing criminal charges" and that to conclude otherwise would make individuals reluctant to serve on boards of directors out of fear of having to fund their own defense costs.