

ALERT

No Duty to Defend Where Employee Participated in Scheme to Siphon Millions of Dollars of Class Action Settlement Proceeds

July 16, 2013

The United States District Court for the Eastern District of Pennsylvania has held that an insurer has no further duty to defend a negligence suit against an insured class action settlement administrator because the actions of one of its employees in approving fraudulent claims fell within the policy's sublimit for misappropriation, misuse, theft or embezzlement of funds. *Camico Mut. Ins. Co. v. Heffler, Radetich & Saitta, LLP*, 2013 WL 3481527 (E.D. Pa. June 27, 2013).

The employee of the insured administrator participated in a scheme to siphon several million dollars of settlement proceeds to his co-conspirators and subsequently pled guilty to mail fraud and wire fraud. Following the discovery of the scheme, members of one of the settlement classes sued the administrator for damages resulting from the employee's actions. The administrator's insurer had funded the defense against the class-members' claims but sought a declaratory judgment that the policy's \$100,000 sublimit for claims "arising from, related to or in connection with any Insured's misappropriation, misuse, theft or embezzlement of funds" should apply and relieve it of any further coverage obligation.

The court granted summary judgment to the insurer and allowed it to recoup the costs it had paid beyond the sublimit, finding that the employee's conduct fell within each of the terms of the exclusion. The court found it irrelevant whether the employee was the ringleader of the scheme or had directly received any or all of the stolen money. At the very least, the court held, the employee had aided and abetted the commission of misappropriation, misuse, theft or embezzlement.

Practice Areas

D&O and Financial Institution Liability
E&O for Lawyers, Accountants and Other Professionals
Insurance
Professional Liability Defense

With respect to the insured's argument that the sublimit should not apply because the employee was not an insured under the policy, the court noted that the policy provided coverage for former employees "but only while performing Professional Services on or after the Retroactive Date." The administrator argued that the employee had worked for the company only prior to the relevant policy year and that his criminal acts were not performed for the company's benefit. The court rejected this argument, determining that the former employee's acts were covered because they were performed after the retroactive date. Moreover, the court held that the policyholder's interpretation would render the language of the sublimit redundant. The court determined instead that, because the employee had engaged in misappropriation, misuse, theft or embezzlement in connection with his work for the administrator, he was performing professional services for the benefit of the company when he committed the acts at issue.

The court also rejected the administrator's argument that the insurer could not deny coverage for negligence claims asserted against an innocent insured that were related to a criminal act committed by another insured. The court noted that the policy contained a specific provision allowing coverage for innocent insureds in certain circumstances but that it specifically did not apply to the exclusion for misappropriation, misuse, theft or embezzlement. The court also emphasized the breadth of the exclusion, in particular the use of the term "any Insured" and the phrase "related to," which does not require any causal connection.

Finally, the court granted summary judgment to the insurer on the administrator's claim for bad faith because the insurer's reliance on the sublimit was reasonable and appropriate and therefore could not constitute bad faith.