

PETERS & NYE LLP

Attorneys at Law

14 Executive Court, Suite 2
South Barrington, Illinois 60010
Phone: 847-423-0350 Fax: 847-381-1693

www.petersye.com

U.S. Bank N.A. v. Indian Harbor Ins. Co., 2014 U.S. Dist. LEXIS 91335 (D. Minn. July 3, 2014)

Case Update: Minnesota District Court, applying Delaware law, holds that payment of restitution in settlement of a claim is covered under professional liability policies

On July 3, 2014, a Minnesota District Court issued a decision in *U.S. Bank N.A. v. Indian Harbor Ins. Co.*, 2014 U.S. Dist. LEXIS 91335 (D. Minn. July 3, 2014) rejecting the Insurers' arguments that the settlement of class actions by bank customers for overdraft fees assessed by U.S. Bank were restitutionary, and therefore uninsurable. Applying Delaware law, the District Court held that Delaware law does not prohibit insurance for restitution when the underlying allegations of ill-gotten gains were not finally adjudicated.

The Insured, U.S. Bank, was sued in three class actions for overcharging overdraft fees to its customers by re-ordering customers' debit-card transactions from highest amount to lowest amount, instead of chronologically, resulting in more overdraft fees for its customers. The class actions asserted common law and statutory causes of action seeking the return of the excess overdraft fees collected by U.S. Bank. In 2013, U.S. Bank settled the class actions for \$55 million.

U.S. Bank had purchased a primary professional liability insurance policy from ACE American and an excess policy from Indian Harbor. U.S. Bank sought coverage from ACE American and Indian Harbor (the "Insurers") for defense costs and settlement amount above the retention. The Insurers denied U.S. Bank's claim, arguing that the settlement was not a covered "loss" under the insurance policies. The Policies defined "Loss" as "the total amount which [U.S. Bank] becomes legally obligated to pay on account of each Claim . . . made against [U.S. Bank] for Wrongful Acts . . . including, but not limited to, damages, judgments, settlements, costs, pre-judgment and post-judgment interest and Defense Costs." The Insurers filed a Motion for Judgment on the Pleadings, arguing that the following provisions limited the Loss definition to preclude coverage for the settlement:

1. The "**Uninsurable Provision**": excluding "[m]atters which are uninsurable under the law pursuant to which this Policy is construed";
2. The "**Extension-of-Credit Provision**": excluding "principal, interest, or other monies either paid, accrued, or due as a result of any loan, lease or extension of credit by [U.S. Bank]."

The Insurers principally argued that the Policy did not cover the settlement under the Uninsurable Provision because the settlement is restitutionary and restitution is uninsurable as a matter of law. The Court rejected this argument for several reasons. First, the Uninsurable Provision only carves out from the definition of "Loss" those "[m]atters which are uninsurable



Exclusively Dedicated to the Insurance Industry

under the law pursuant to which this Policy is construed”. The Court interpreted this Provision as referring to the law as it currently exists. Because no Delaware authority has held that restitution is uninsurable as a matter of law and Delaware courts have held that public policy did not prohibit insurance coverage in similar contexts such as for punitive damages and civil penalties, the Court held that the settlement payment is a “Loss”.

The Court refused to address the issue of the insurability of a restitutionary settlement as a matter of first impression and speculate as to how a Delaware court would rule on this issue. The insurers had asked the Court to follow the law of other states that forbid such coverage, while the Insured argued that Delaware courts do not readily void insurance coverage based on public policy considerations. The Court found that no reason compelling enough was presented for it to hold, as a matter of first impression, that restitutionary settlements are uninsurable under Delaware law.

The Court’s reasoning also employed an analysis that crafted an extension of coverage from a Policy exclusion. Because Delaware law requires that the definition of “Loss” must be interpreted consistently with all Policy provisions, the Court based its second ground for holding that the restitutionary settlement is insurable on its interpretation of the Policy’s Ill-Gotten Gains Exclusion, which excludes from coverage money to which the Insured is “not legally entitled” only “as determined by a final adjudication in the underlying action”. Viewing “money to which the Insured is not legally entitled” as including a restitution payment, the Court held that the parties contemplated the possibility of coverage for restitutionary settlements because they expressly excluded restitution resulting only from a final adjudication. The Court reasoned that the insurer’s arguments would result in nullifying the final adjudication requirement of the exclusion. While the Court agreed with the general proposition that restitution is uninsurable as held in the line of cases starting with the Seventh Circuit’s decision in *Level 3 Communications, Inc. Federal Insurance Co.*, these decisions did not affect the Court’s decision because they involved policies that did not contain the “final adjudication” language. The Court stressed that the Insurers and Insured, knowing of the *Level 3* decision, still decided to cover a restitutionary settlement absent a final adjudication as evidence by the Ill-Gotten Gains Exclusion.

Lastly, the Insurers argued that the Extension-of-Credit Provision bars the settlement, as the settlement stemmed from U.S. Bank’s overdraft policy and that overdraft protection constitutes an extension of credit to its customers. The Extension-of-Credit Provision bars money paid as “a result of any loan, lease or extension of credit by [U.S. Bank].” The Court first held that the Insurers’ interpretation of the Extension-of-Credit was overbroad in that the Provision was designed to prevent coverage for losses by U.S. Bank for losses due to unpaid loans, which are not at issue in the case. Second, the Court stated that the Insurers’ reading of the Provision would bar coverage of any professional liability claim relating to U.S. Bank’s lending operations — an interpretation which could not have been intended by the parties. Third, the Court noted that the Insurers’ interpretation of the Extension-of-Credit Provision assumes that the settlement was based on an extension of credit, when the class actions alleged that overdraft fees were charged while the customer accounts still had positive balances, and before any overdraft protection was extended. Thus, the Court found the Insurers’ argument that the Extension-of-Credit Provision limits the settlement was misplaced.



Exclusively Dedicated to the Insurance Industry