

Court Applies Criminal/Intentional Acts Exclusion to Bar Coverage for Negligence and Breach of Contract Claims

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The United States District Court for the District of Minnesota, applying Minnesota law, has held that a policy's criminal/intentional acts exclusion bars coverage for a money judgment based solely on the underlying plaintiff's negligence and breach of contract claims where the substantive conduct alleged was criminal and undeniably connected to the conduct for which the judgment was entered. *Scottsdale Ins. Co. v. Riverbank*, 2011 WL 3920296 (D. Minn. Sept. 7, 2011).

The insured company, the company's CEO and the CEO's husband were sued in connection with the CEO's and her husband's receipt of \$600,000 under the terms of a mortgage loan agreement. In addition to alleging that the CEO and her husband failed to satisfy their first mortgage and failed to record the second mortgage on the property in question, the plaintiff also brought a negligence claim against the insured company and a breach of contract claim against the husband. The plaintiff won summary judgment on both of these claims and was awarded a \$636,742.77 judgment. After criminal charges were brought against the CEO of the company, she pled guilty to theft by false representation in connection with the loan transaction at issue. In the subsequent coverage action, the insurer argued that the policy did not provide coverage for the underlying judgment because, among other things, the policy's criminal/intentional acts exclusion precluded coverage for losses "alleging, based upon, arising out of, attributable to, directly or indirectly resulting from, in consequence of, or in any way involving" criminal, fraudulent or dishonest acts.

Agreeing with the argument that the policy's criminal/intentional acts exclusion barred coverage, the court first noted that the policy's "Innocent Insureds" provision provided that the knowledge of the CEO or CFO of the insured company shall be imputed on the company. Because the underlying complaint focused on the CEO's role in leading the alleged fraudulent activity, the court then reasoned that the gravamen of the underlying suit was the CEO's intentional criminal activity. The court explained that even though the insured company was deemed only negligent, the actions leading to that finding were performed by its CEO and resulted from the actions for which she was criminally charged, pled guilty and was sentenced. Accordingly, the court determined that the underlying plaintiff's injuries resulted from the CEO's intentional criminal actions, and, thus, concluded that the policy's criminal/intentional act exclusion applied to bar coverage. In so doing, the court also noted that excluding coverage for criminal acts is supported by public policy. The court also rejected the

insureds' argument that the "illusory coverage doctrine" was applicable.