

# Fourth Circuit Holds That Personal-Profit and Conversion Exclusions Do Not Preclude Coverage for Underlying Fraud Suit

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Applying Maryland law, the United States Court of Appeals for the Fourth Circuit has held that, where an underlying complaint seeks restitution but does not allege that the policyholder itself gained any profit or advantage, an E&O insurer may not disclaim coverage on the basis of a personal-profit exclusion. *Cornerstone Title & Escrow, Inc. v. Evanston Ins. Co.*, 2014 WL 631098 (4th Cir. Feb. 4, 2014). The court also held that an exclusion for claims “based upon or arising out of” conversion did not apply where the policyholder allegedly improperly delivered a check, but the payee did not receive the check.

A state attorney general sued the policyholder, a title insurer, and ten co-defendants, seeking restitution and alleging that the defendants defrauded homeowners on the brink of foreclosure through sale-leaseback agreements whereby homeowners sold their houses to the co-defendants only for them to rent the houses back to the homeowners at inflated rates. The policyholder allegedly provided settlement services for the sale-leaseback transactions and failed to deliver the sale proceed checks to the homeowners. The attorney general sought to hold the policyholder responsible for the co-defendants' acts as well as its own, eventually garnering a settlement wherein the policyholder paid \$100,100 in restitution. After the insurer denied coverage for the underlying claim, the policyholder filed suit against the insurer, alleging breach of its duties to defend and indemnify the insured.

The trial court had held that two policy exclusions precluded coverage: (1) an exclusion for claims “based upon or arising out of” the policyholder's gaining any profit or advantage to which the policyholder was not legally entitled; and (2) an exclusion for claims “based upon or arising out of the actual or alleged ... conversion ... [of] any escrow funds, monies, monetary proceeds, or any other assets, securities, negotiable instruments ... irrespective of which individual, party, or entity actually or allegedly committed or caused in whole or part the [excluded act].”

On appeal, the Fourth Circuit reversed the district court, holding that neither exclusion defeated coverage. The court held that the personal-profit exclusion did not apply because, although the underlying complaint alleged that the other co-defendants wrongfully profited from their conduct and sought restitution from the defendants collectively, it did not allege that any profit or advantage inured specifically to the policyholder's

benefit. Further, the court noted that, given that the underlying complaint alleged claims based on the failure to make required statutory disclosures, the attorney general could have prevailed against the policyholder independent of any claims stemming from the defendants' unlawful receipt of profit or advantage.

The court further held that the conversion exclusion did not apply because, under Maryland law, a claim against a third-party based on improper delivery of a check does not amount to conversion unless the payee receives the check. The court found that, in the instant case, the policyholder misdirected the settlement checks before the payee homeowners received the checks, and therefore such actions could not amount to conversion. The court further noted that, because the underlying complaint sought to hold the insured responsible for failing to make required disclosures, prematurely recording deeds, and making misleading statements, the underlying complaint made claims that were not based upon or arising out of conversion.