

Professional Services, Broad Fund Exclusions in Binder Bar Coverage

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The U.S. District Court for the Western District of Pennsylvania has ruled that an insurance binder for a prospective D&O policy and investment advisor policy did not provide coverage for a lawsuit alleging wrongdoing with respect to the management of private funds because the binder stated that the ultimate policies would include a "Professional Services Exclusion—Complete" with respect to the D&O coverage and a manuscript "Broad Private Fund Exclusion" with respect to the investment advisor coverage. *MDL Capital Mgmt., Inc. v. Federal Ins. Co.*, 2006 WL 2974165 (W.D. Pa. Oct. 16, 2006). Wiley Rein & Fielding LLP represented the prevailing insurer in this action.

The insurer issued a conditional binder to MDL Capital Management, Inc. for specified D&O and investment advisor coverage. The binder referenced a professional services exclusion for the D&O policy and a "Broad Private Fund Exclusion" in the investment advisor policy. Before a policy issued, MDL and certain of its officers were sued for alleged mismanagement of one of the private funds identified in the conditional binder. The insurer denied coverage based on the exclusions identified in the binder. MDL filed suit against the insurer thereafter.

The court first addressed the availability of D&O coverage under the conditional binder. The court noted that the binder indicated that a "Professional Services Exclusion—Complete" would be included in this policy. The endorsement form referenced in the binder excluded coverage for "Loss on account of any Claim based upon, arising from or in consequence of the rendering of or failure to render professional services, including but not limited to the following services: ... investment advisor..." The court concluded that the underlying action's allegations were based on the company's investment advisor services. The court therefore held that the exclusion applied based on its plain and unambiguous terms. In doing so, the court rejected MDL's argument that application of a professional services exclusion with respect to a D&O policy results in illusory coverage.

The court then addressed the availability of investment advisor coverage. The binder indicated there was to be a manuscript exclusion: "Broad Private Fund Exclusion—MDL Broad Market Fixed Income Fund, MDL Core Fund and MDL Active Duration Fund, Ltd. (endorsement wording to be developed)." Even in the absence of exclusion wording, the court stressed that the exclusion could have only one reasonable reading: it barred coverage for claims arising out of all professional services as an investment advisor to the specified funds, including the underlying litigation.

The court rejected MDL's argument that the reasonable expectations doctrine required the court to give effect to their putative belief that the exclusion only barred coverage for the funds themselves, and not for liability arising out of their management, based upon MDL's "subjective" and "uncommunicated" understanding. The court held that the reasonable expectations doctrine could not apply because the language was unambiguous and because MDL was "sophisticated" and "used a broker to purchase [the] liability insurance policies."