

Court of Appeals Affirms That “In Fact” Requirement Was Triggered by Jury’s Guilty Verdict

April 18, 2013

Applying Illinois and Florida law, the United States Court of Appeals for the Fourth Circuit has affirmed that a jury’s guilty verdict in a criminal proceeding triggers the “in fact” element of a D&O policy’s dishonesty and personal profit exclusions, allowing the insurer unilaterally to cease advancing defense costs. *Farkas v. Nat’l Union Fire Ins. Co. of Pittsburgh, Pa.*, 2013 WL 1459248 (4th Cir. Apr. 11, 2013). In a short per curiam opinion without additional legal analysis, the court adopted the district court’s “thorough” opinion in *Farkas v. Nat’l Union Fire Ins. Co. of Pittsburgh, Pa.*, 861 F. Supp. 2d 716 (E.D. Va. 2012), originally discussed in the May 2012 issue of *Executive Summary* and summarized briefly below.

The insured, the chairman of a bankrupt mortgage corporation, was indicted on various criminal counts for bank, wire and securities fraud. The mortgage corporation’s D&O insurer agreed that the criminal proceeding constituted a claim under the policy, but reserved its right to limit or deny coverage based on policy exclusions for claims “in fact” arising out of fraud or wrongful personal profit. Pursuant to an order of the bankruptcy court, the insurer advanced approximately \$1 million for the chairman’s defense costs and then awaited court approval to advance additional amounts. The jury found the chairman guilty on all counts, and the insurer informed the chairman that the verdict triggered the “in fact” element of the policy’s dishonesty and personal profits exclusions, such that it would no longer advance defense costs.

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In the ensuing coverage dispute, the court first held that the jury’s verdict clearly triggered the “in fact” requirement of the personal profit and dishonesty exclusions, rejecting the chairman’s argument that the phrase was ambiguous and holding that the insurer properly could refuse to advance further defense costs.

The court further held that the insurer could recoup the defense costs previously advanced, rejecting the insured’s argument that the carrier was obligated to advance *all* defense costs incurred prior to the jury’s verdict and *then* seek reimbursement on the basis that the dishonesty and personal profit exclusions barred coverage. Noting that this was not a case where the carrier had “dragged its feet before advancing costs,” the court held that forcing the carrier to pay out amounts for which it could immediately seek recoupment was not appropriate either under the terms of the policy or as a practical matter.

The opinion is available [here](#).