

New York's Highest Court Addresses Coverage Under Fiduciary Liability Policy

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In its recent decision in *Federal Ins. Co. v International Bus. Machs. Corp.*, 2012 NY Slip Op 1320 (N.Y. Feb. 21, 2012), the New York Court of Appeals - New York's highest court - had occasion to consider whether an underlying ERISA lawsuit fell within the scope of coverage afforded under an excess fiduciary liability policy, and in particular, what it means to be acting in one's capacity as a fiduciary.

Federal issued to IBM an Executive Protection Excess Insurance Policy, providing follow-form excess coverage over a fiduciary liability policy issued by Zurich. IBM and the IBM Personal Pension Plan were named as defendants in a class action lawsuit alleging that various amendments made to its employees' benefit plans violated ERISA laws pertaining to age discrimination. IBM settled the underlying suit, which settlement included a payment to plaintiffs of their attorneys' fees in prosecuting the lawsuit. IBM, in turn, sought coverage for the payment of these fees under the Federal policy, claiming that the primary Zurich policy, with limits of liability of \$25 million, had exhausted.

Federal sought a judicial declaration that coverage was unavailable for the underlying suit as it did not fall within the Zurich policy's definition of "wrongful act," which was amended by endorsement to include:

1. any breach of the responsibilities, obligations or duties by an Insured which are imposed upon a fiduciary of a Benefit Program by the Employee Retirement Income Security Act of 1974, as amended, or by the common or statutory law of the United States, or ERISA equivalent laws in any jurisdiction anywhere in the world;
2. any other matter claimed against an Insured solely because of such Insured's service as a fiduciary of any Benefit Program;
3. any negligent act, error or omission in the administration of any Benefit Program.

Federal argued that the underlying ERISA class action did not fall within this definition of "wrongful act" because the suit was not brought against IBM in its capacity as a fiduciary but rather in its capacity as a plan settlor or sponsor. While the trial court rejected Federal's argument, this ruling was reversed on appeal by a New York intermediate court, which agreed that "[t]he age discrimination provisions of ERISA, which IBM allegedly violated by enacting the amendments, are not responsibilities, obligations, or duties imposed upon a fiduciary of a Benefit Program by ERISA. Rather, they are obligations imposed on settlors of ERISA benefit plans."

On further appeal, the Court of Appeals agreed with the Appellate Division that the changes IBM made to the benefit plans were made in its capacity as a plan settlor rather than in a fiduciary capacity. The Court further agreed that the definition of "wrongful act" limited coverage to instances where the insured is acting in a fiduciary capacity. As the Court explained, "[w]e conclude that the average insured would reasonably interpret the disputed language in the definition of 'Wrongful Act' to mean that coverage is limited to acts of an insured undertaken in its capacity as an ERISA fiduciary."

In reaching its conclusion, the Court rejected several arguments asserted by IBM. Most notably, IBM argued that because the term “fiduciary” was not defined in the Zurich policy, it must be given a “plain, ordinary meaning” that the average policyholder would understand rather than the definition contained in the ERISA statute. Specifically, IBM argued that the term “fiduciary” should be construed as one who acts for the benefit of another and owes that party the duties of good faith – duties that IBM owed to underlying plaintiffs as the plan sponsor. Under this interpretation of the term “fiduciary,” explained the Court, “IBM’s actions would be covered by virtue of the fact that it was an insured and a plan fiduciary that allegedly violated certain ERISA provisions, regardless of the fact that, if the allegations are correct, it undoubtedly did so in its capacity as a plan settlor and not in its capacity as an ERISA fiduciary.” The Court rejected this broad construction of the term “fiduciary,” explaining that it would result in a “strained and implausible” interpretation of the policy. As the Court explained, because “the first prong of the ‘Wrongful Act’ definition refers not only to duties imposed by ERISA (or foreign equivalents) but also to duties imposed by common law and statutory law,” IBM’s proposed definition of fiduciary would result in the policy extending coverage to “almost every lawsuit imaginable, a result we find to be unreasonable.”

The Court also considered IBM’s argument that under Federal’s interpretation of the policy, the first and second prongs of the definition of “Wrongful Act” would have an identical meaning. The Court rejected this argument, explaining that the first prong related to violations of ERISA or other common or statutory law, whereas the second prong related to any fiduciary breach. As the Court explained, “[p]rong two would extend coverage to an insured’s claims arising from liability incurred solely due to the insured’s position as a fiduciary. For instance, if the insured is named in an action solely due to its status as a fiduciary, even where the action does not allege that the insured actually breached any fiduciary duties, and the action results in a settlement or a judgment against the insured, it is possible that Zurich and Federal would be liable for funds spent to settle the suit or pay the judgment.”

Finally, the Court rejected IBM’s reliance on the fact that Federal subsequently revised its own policies to make more explicit the concept that coverage is limited to instances where insureds are acting in their *capacities* as fiduciaries. The Court rejected IBM’s reliance on other language contained in subsequently issued policies, explaining:

It is simply not the case that because the challenged provision could have been worded differently, it is ambiguous and must be construed in IBM’s favor. There are often many ways of effectively conveying the same meaning and the question is not simply whether the insurer could have phrased the provision differently. Rather, the issue is, in light of the reasonable expectations of the average policy holder, whether the provision, as written, is sufficiently clear and precise such that there is no room for reasonable disagreement about the scope of coverage.

The Court agreed that the Zurich policy was sufficiently clear and precise in its scope. Thus, the Court of Appeals affirmed the decision of the Appellate Division, concluding that IBM was not entitled to coverage under Federal’s policy since the underlying suit did not allege a “wrongful act” as that term was defined by the Zurich policy.

Labels: [Fiduciary](#), [Wrongful Act](#)