COVINGTON

COVINGTON & BURLING LLP

E-ALERT | Financial Institutions & Insurance

October 18, 2013

FDIC CAUTIONS FINANCIAL INSTITUTIONS AND THEIR DIRECTORS REGARDING RECENT INCREASE IN EXCLUSIONS CONTAINED IN D&O INSURANCE POLICIES

The FDIC last week issued a Financial Institution Letter advising financial institutions and their directors and officers of the increased use of exclusionary terms or provisions in D&O policies, and the resulting increased risk of uninsured personal civil liability for directors and officers. (FIL-47-2013, October 10, 2013).

The FDIC Letter urges the directors of financial institutions to make well-informed choices about D&O coverage, including consideration of costs and benefits, exclusions and other restrictive terms in proposed policies, and the implications for personal financial liability for directors and officers.

D&O insurance is a critical asset for financial institutions and their directors and officers, and the FDIC Letter expressly affirms that the purchase of D&O insurance serves a valid business purpose. The FDIC's Letter is also a timely reminder that the D&O insurance market is in constant flux and that — in addition to seeking advice from insurance brokers — directors should consider seeking advice from experienced coverage counsel to gain a better understanding of the potential impact of restrictive provisions in proposed policies.

The FDIC's Letter did not identify any particular exclusionary language that troubled the regulator, but it may have been prompted by developments such as a recent decision by a federal court in Georgia holding that an exclusion usually found in D&O policies but lacking a standard carve-out barred coverage for a suit brought by the FDIC in its capacity as receiver against the former directors and officers of a failed bank. *St. Paul Mercury Insurance Co. v. Miller, et al.*, 2:12-CV-0225-RWS (August 19, 2013). In that case, the FDIC was directly interested because the unavailability of coverage might reduce the FDIC's recovery, if any, in the matter. (The *St. Paul Mercury* ruling itself was the subject of another Covington & Burling E-Alert.)

The FDIC may also be warning indirectly about insurers' increasing efforts to impose a so-called "regulatory exclusion," which expressly precludes coverage for claims brought by any governmental, quasi-governmental, or self-regulatory agency. Another drafting practice that may have concerned the FDIC is the retention of seemingly ordinary boiler-plate provisions in excess D&O policies that insurers and some courts have interpreted restrictively, resulting in the policyholder inadvertently forfeiting excess policy proceeds by giving an underlying carrier a discount off of limits in settlement of a coverage dispute. *See, e.g., JP Morgan Chase & Co. v. Indian Harbor Ins. Co.*, 947 N.Y.S.2d 17 (App. Div. 2012) , *leave to appeal denied*, 20 N.Y.3d 858 (2013).

Finally, the Letter reiterates the FDIC's long-standing position that insured depository institutions and depository institution holding companies are prohibited from purchasing insurance for civil money penalties assessed against directors and officers by any federal banking agency. The Letter advises that this prohibition applies even in cases where the insured directors and officers reimburse the corporation for the cost of such coverage. However, the FDIC Letter does not mention personal umbrella coverage purchased directly by a director and officer independently of the regulated entity.

Covington has long advised corporate clients and their directors and officers about the placement of D&O insurance and the presentation of D&O insurance claims, both within the financial services industry and more broadly. To inquire about our provision of such services, please contact one of the lawyers listed below.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our financial institutions and insurance practice groups:

Bruce C. Bennett	+1.212.841.1060	bbennett@cov.com
John Dugan	+1.202.662.5051	jdugan@cov.com
David Goodwin	+1.415.591.7074	dgoodwin@cov.com
William Skinner	+1.202.662.5470	wskinner@cov.com
D. Jean Veta	+1.202.662.5294	jveta@cov.com
Bert Wells	+1.212.841.1074	bwells@cov.com