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NY Panel Rejects Insurers' Defenses In $140M JP Morgan Suit

By **Josh Liberatore**

Law360 (March 18, 2022, 7:02 PM EDT) -- A New York appeals panel rejected several remaining defenses asserted by insurers still hoping to avoid covering a J.P. Morgan Securities Inc. predecessor for a $140 million payment to the U.S. Securities & Exchange Commission, finding that the insurers can't rely on exclusions or public policy considerations.

In an order entered Thursday, a four-judge appeals panel for the New York Supreme Court ruled that primary insurer Vigilant Insurance Co. and several excess insurers can't get out of covering their policyholder for part of a $250 million settlement with the SEC resolving accusations that Bear Stearns, which was acquired by J.P. Morgan in 2008, helped its hedge fund clients profit through illegal late trading and deceptive market timing.

The ruling comes after the state's high court **in November** found that the settlement wasn't an uninsurable penalty, reversing the appellate court's prior ruling against coverage in a litigation that stretches back to 2009.

The high court remanded the case to the appellate court for judgment regarding the insurer's remaining anti-coverage defenses. The appeals court struck those arguments down, ruling that the insurers can't rely on public policy considerations or on two exclusions — one for "personal profit or advantage" and another for "prior knowledge" — to get out of covering the settlement.

The appellate court rejected the insurers' contention that they don't have to cover the settlement because public policy prohibits indemnification of losses that were caused by intentionally harmful conduct.

The record "does not show that Bear Stearns intended to harm mutual fund investors by its facilitation of these trading strategies" or that the firm "knew that its actions would 'directly and immediately' harm the investors," the panel said.

J.P. Morgan's coverage suit dates back to 2009, when it sued Vigilant and excess insurers including Travelers Indemnity Co., Federal Insurance Co., National Union Fire Insurance Co. and Liberty Mutual Insurance Co.

Bear Stearns, which didn't admit or deny misconduct, asked for its insurers to cover only $140 million out of the $250 million total settlement — the amount that reflects customers' improper profits, according to court records.

In November, the New York Court of Appeals decided to overturn the Appellate Division, First Department's September 2018 reversal of the state trial court's August 2017 order directing the insurers to cover the $140 million payment.

The high court had to decide whether the SEC-ordered disgorgement was a penalty imposed by law, which would have made it an uncovered loss. A majority of the court found that the SEC payment was restitution, not punitive, and so wasn't a "penalty" within the reasonable meaning of the policy language.

The high court asked the appellate court to take another look at the case and decide whether the insurers had any other valid coverage defenses.

On Thursday, the appellate court shot those arguments down, including a pair of exclusions cited by the insurers.

An exclusion barring coverage for "any personal profit or advantage to which (Bear Stearns) was not legally entitled" doesn't apply to the claim for the disgorgement payment, the panel said, because the SEC payment "represents third-party gains, rather than a benefit or advantage to Bear Stearns."

Some policies also contained exclusions for "prior knowledge," according to court records. But the panel said there's "no evidence" that any high-ranking Bear Stearns employee had early enough knowledge of the allegedly deceptive trading scheme to trigger that exclusion.

The panel did give a win to the excess insurers, finding that J.P. Morgan isn't entitled to prejudgment interest.

That's because the "contractual attachment provision permitted those insurers to wait out good faith coverage disputes between the insured and the underlying insurer without risk of breaching their performance obligations," the panel said.

"Only upon actual payment by the underlying insurer did the excess insurers' performance obligations become due," the panel added.

Counsel for Liberty Mutual declined to comment Friday.

Counsel for the remaining parties didn't immediately respond to requests for comment Friday.

Judges Rolando T. Acosta, Dianne T. Renwick, Troy K. Webber and Cynthia S. Kern sat on the panel for the appeals court.

J.P. Morgan is represented by Steven E. Obus and Seth B. Schafler of Proskauer Rose LLP.

Vigilant and Federal Insurance Co. are represented by Daniel M. Sullivan, James M. McGuire and Gregory Dubinsky of Holwell Shuster & Goldberg LLP and by Joseph G. Finnerty III, Megan Shea Harwick, Eric S. Connuck and Marc A. Silverman of DLA Piper.

Travelers Indemnity Co. is represented by Marsha J. Indych and David F. Aberneth of Faegre Drinker Biddle & Reath LLP.

Liberty Mutual is represented by Scott Schechter, Andrew E. Oldis and Matthew Mawby of Kaufman Borgeest & Ryan LLP.

National Union Fire Insurance Co. of Pittsburgh is represented by Kevin J. Windels of D'Amato & Lynch LLP.

The case is J.P. Morgan Securities Inc. et al. v. Vigilant Insurance Company et al., case numbers 2018-00580 and 2018-303, in the Supreme Court of the State of New York Appellate Division, for the First Judicial Department.

--Additional reporting by Shawn Rice. Editing by Nick Petruncio.

Update: This story has been updated to include the decision by counsel for Liberty Mutual to decline comment.
