

# Sixth Circuit Holds Settlement for Fraudulent Transfers Insurable Under Ohio Law

[Blog](#) Hunton Insurance Recovery Blog

## Hunton Andrews Kurth LLP

**USA** | February 13 2024

D&O, E&O, and other professional liability insurers often raise the insurability, or rather “uninsurability” loss defense. Consistent with our prior analysis of the ways the Ohio district court erred in assessing insurability, the Sixth Circuit’s recent decision in *Huntington National Bank v. AIG* outlines how courts should evaluate insurability defenses, particularly in the absence of public policy rendering a loss uninsurable.

### Background

*Huntington National Bank v. AIG* involved an alleged fraudulent transaction between Huntington National Bank (“Huntington”) and a purported computer-services business. The computer-services business sought financial assistance from companies, including Huntington, to obtain computer equipment. Over time, Huntington became suspicious of the computer-serve business’s operations, and the bank’s regional head of security launched an investigation. During the investigation, Huntington’s head of security learned about Brian Watson—the chairman and chief executive of the business—and his history of fraud. But, despite this discovery, the head of security did not share any information with the Huntington employees managing the business’s account. The computer-service business eventually paid off its debt to the bank, but later in the year, the FBI raided the computer-services business’s offices. After the raid, both the computer-services business and its purported vendor were bankrupt. A trustee was appointed to represent the companies in bankruptcy proceedings.

The trustee “felt an injustice occurred” and accused Huntington of putting “its desire to be repaid ahead of its concerns that Watson was committing a Ponzi scheme and, by doing so, perpetuated the Ponzi scheme to its benefit and other lenders’ detriment.” The trustee sued Huntington, alleging fraudulent transfers and seeking recovery of the transfers from the bank. The trustee and Huntington ultimately reached a settlement for \$32 million.

### Huntington’s Insurance Claim

Huntington provided notice of the claim under its bankers professional liability insurance policy and sent the insurer a letter demanding repayment. The policy’s definition of “Loss” had several carve outs, including one for “matters that may be deemed uninsurable under the law pursuant to which this policy shall be construed.” Relying on this carveout, the insurer denied coverage for the settlement. It argued that the settlement was not a “Loss” under the policy because the settlement reflected transfers not accepted by Huntington in good faith, and disgorgement payments are uninsurable under Ohio law. Huntington subsequently initiated a coverage action, alleging breach of contract and bad faith.

### The District Court Grants Summary Judgment for the Insurer

In deciding the insurer’s summary judgment motion, the United States District Court for the Southern District of Ohio explained that the insurer—as the drafter of the policy—had the burden of proving that the settlement payment was an uninsurable loss under governing Ohio law. But, instead of analyzing whether the insurer had met this high burden, the district court engaged in its own analysis of whether the settlement was insurable.

The district court instead faulted *Huntington* for not *disproving* the insurer’s uninsurability defense. Specifically, the court concluded that Huntington “offer[ed] no persuasive authority to support” that the transfers reflected in the settlement—which the insurer characterized as disgorgement—were insurable under Ohio law. The court effectively shifted the burden of proof to Huntington, the policyholder, to negate the insurable loss exclusion by proving the absence of public policy prohibiting coverage for the settlement. The court also explicitly stated that “while no Ohio court has addressed whether disgorgement is insurable, the Court finds that Ohio courts are unlikely to permit insurance coverage for wrongfully obtained money.” As a result, the district court upheld the insurer’s coverage denial, and, in doing so, ignored the commonly understood insurance principle that a loss is deemed insurable unless there is a clearly articulated pronouncement under the applicable state law to the contrary.

### **The Sixth Circuit**

The Sixth Circuit reversed the grant of summary judgment for the insurer on the issue of insurability. The Sixth Circuit first recognized that the district court rightly held that the insurer has the burden of proving a loss is uninsurable. The court stated that the “uninsurable under the law” language in the definition of “Loss” was an exclusion to coverage, regardless of the location of the language in the policy (there, in a definition as opposed to the policy section titled “exclusions”). As such, the insurer had the burden to prove the loss was uninsurable.

With respect to the public-policy analysis that insurer’s must undertake to support an uninsurability defense, the Sixth Circuit emphasized that “Ohio courts should look to pronouncements from the legislature as the proper policymaker and avoid declarations of public policy without legislative support.” Accordingly, in its analysis, the Sixth Circuit looked to Ohio courts analyzing Ohio statutes to determine the insurability of losses.

It noted that only two categories of claims are uninsurable under Ohio law as a matter of public policy—claims seeking coverage for punitive damages and claims seeking coverage for losses due to certain intentional torts. Based on this established Ohio precedent, the Sixth Circuit determined that in order for a loss to be uninsurable under Ohio law, the damages sought must be based on an intent to injure, malice, ill will, or some other similar culpability. The Sixth Circuit agreed with Huntington that the settlement payment was insurable because the settlement was not akin to punitive damages and was not intended to punish an intentional bad act. Thus, it held that the settlement payment was insurable under Ohio law and remanded to the district court for further proceedings.

### **Conclusion**

The Sixth Circuit’s decision highlights the importance of analyzing definitions of “Loss” and choice-of-law provisions at renewal. Uninsurable loss defenses are matters of state law. Thus, the existence or absence of pronouncements from a state’s legislature and its highest courts can either support or negate uninsurable defenses. Businesses should consider what law applies according to a policy and what losses are deemed uninsurable under the governing state’s law to mitigate the risk of uncovered losses, especially as insurers continue to increasingly rely on insurability and public policy defenses, even when not supported by the law governing the policy.

We previously outlined the ways the Ohio district court departed from black letter insurance principles in forcing a policyholder to disprove a defense for which the insurer held the burden of proof. The Sixth Circuit’s correct application of those principles ensures that policyholders will be given the benefit of the insurance bargain and re-

affirms the well-established principle that insurers have the burden to prove exclusions, regardless of their location in the policy.

Hunton Andrews Kurth LLP - Andrea DeField, Geoffrey B. Fehling and Jae Lynn Huckaba

Powered by

**LEXOLOGY.**