Bond Case Briefs

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MBIA Inc. v. Certain Underwriters at Lloyd's, London

United States District Court, S.D. New York - July 16, 2014 - Slip Copy - 2014 WL 3533985

MBIA purchased a Primary Financial Institutions Professional Indemnity Policy and an Excess Financial Institutions Professional Indemnity Policy (together, the "Policies") from a syndicate of insurers, including Lloyds, London (the "Underwriters").

In July 2008, MBIA was named as a defendant in a number of lawsuits by several public entities and others who had purchased bond insurance from MBIA (collectively, the "Bond Cases"). In these suits plaintiffs alleged that MBIA committed negligence, among other things, in the sale and underwriting of financial guarantee insurance for the plaintiffs' public finance bonds as well as wrongful acts in the bidding for and sale of municipal derivatives to plaintiffs.

In March, 2010, MBIA was named as a defendant in *City of Phoenix v. Ambac Financial Group, Inc., et al.* ("Phoenix") based on improper credit ratings resulting in unfair insurance premiums. MBIA sought coverage for the Bond Cases as a single Claim under the Policies.

In July 2008, lawsuits were filed against MBIA alleging that MBIA and others allocated the municipal derivatives market among themselves and rigged the bidding system through which plaintiffs purchased municipal derivatives and assigned plaintiffs lower interest rates, charged them higher fees, and subjected them to unnecessarily high risks (collectively, "Derivatives Cases"). MBIA submitted all of the Derivative Cases as a single Claim under the Policies.

In February 2009, MBIA separated its subsidiaries in order to provide municipal and state issuers frozen out of the public finance market with financial guarantee policies, while attracting capital investment to the benefit of the holding company and all policyholders (the series of transactions that implemented this change is referred to as the "Transformation").

Subsequent lawsuits alleged that MBIA's Transformation was improper because it deprived plaintiffs of the benefits of the financial guarantee insurance MBIA sold to the plaintiffs and lowered the credit rating of MBIA Insurance (collectively, "Transformation Cases"): Plaintiffs alleged that this had the effect of decreasing the value of the structured finance instruments MBIA guaranteed. Moreover, plaintiffs alleged that following the Transformation, MBIA lacked the necessary assets to perform its obligations under the structured finance guarantee policies and MBIA favored its public finance bond insurance clients over its structured finance clients. MBIA submitted all of the Transformation Cases as a single Claim under the Policies.

Although certain of the cases against MBIA have settled, Underwriters refused to advance MBIA money for their defense costs or settlement, arguing that the Policies only require the Underwriters to make payment after the final disposition of all related or identical underlying claims. Thus, Underwriters took the position that MBIA was not yet entitled to reimbursement. MBIA sued the Underwriters for breach of contract and declaratory judgment.

The District Court held that:

- As MBIA had submitted the Bond, Derivatives, and Transformation Cases as single Claims, the Underwriters had no obligation to pay any Loss until final disposition of all underlying actions constituting a Claim;
- Underwriters could not invoke the professional services exclusion in the Policy as a coverage defense in the Transformation Claim;
- MBIA's Transformation did not fall within the Financial Guarantee Exclusion provision of the Policy; and
- The Underwriters must make payment to MBIA on the Transformation Claim under the Policy.