**UNITED STATES DISTRICT COURT**
**FOR THE DISTRICT OF PUERTO RICO**

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| FEDERAL DEPOSIT INSURANCE CORPORATION, AS RECEIVER OF WESTERNBANK PUERTO RICO,<br><br>plaintiff intervenor,<br><br>v.<br><br>FRANK C. STIPES GARCÍA, *et al*., | CIVIL ACTION NO. 11-02271 (GAG)<br><br>RE: DECLARATORY JUDGMENT |

**THE D&OS'[1] REPLY IN SUPPORT OF THEIR**
**MOTION TO CLARIFY THE COURT'S ADVANCEMENT ORDER[2]**

In resolving the D&Os' Motion to Clarify the Court's Advancement Order (D.E. 881) (the "Motion"), and making it clear that the D&Os are entitled to advancement of defense costs from the 09-10 Policies,[3] the Court should focus on four indisputable facts: (1) each of the 09-10 Policies is a claims-made policy, "as opposed to an 'occurrence policy,'" which renders each of the Insurers "responsible for claims made during the term of the policy;"[4] (2) the FDIC-R's claims against the D&Os (the "Non-Inyx Claims") were "made during the term" of the 09-10 Policies; (3) the D&Os gave timely notice to the Insurers[5] pursuant to the 09-10 Policies—the **only** condition precedent to advancement; and (4) the Court found there to be a "remote possibility" of coverage under *all of the policies at issue*, an order that the First Circuit affirmed.

[1] The "D&Os" are Frank C. Stipes García, Juan C. Frontera García, Héctor Del Río Torres, William Vidal Carvajal, César Ruiz, and Pedro R. Domínguez.
[2] The "Advancement Order" refers to the Court's July 3rd Order at D.E. 211.
[3] The 09-10 Policies are the policies covering the period from December 31, 2009 to December 31, 2010, and can be found at D.E. 1021-3.
[4] *F.D.I.C. v. St. Paul Fire & Marine Ins. Co.*, 993 F.2d 155, 158 (8th Cir. 1993).
[5] The "Excess Insurers" include XL Specialty Insurance Company, Liberty Mutual Insurance Company, and ACE Insurance Company. "AIG" is AIG Insurance Company—Puerto Rico. Collectively, AIG and the Excess Insurers will be referred to as the "Insurers."

This is not a close question. The Advancement Order's finding of a "remote possibility" of coverage under *any of the policies at issue* meant that the D&Os are entitled to advancement under *every policy at issue*, including the 09-10 Policies, because the policies for each year are identical (as the Insurers admit). Moreover, the Court rejected the Insurers' sole basis for opposing advancement (the "insured v. insured" exclusion) two years ago. The Insurers cannot now oppose advancement with arguments they didn't make then. They couldn't even have made new arguments (and didn't even try) on a timely motion for reconsideration two years ago (which they filed, and lost, before they took their appeal, and lost). Accordingly, the Court should grant the D&Os' Motion, and make it clear that the D&Os are entitled to advancement of defense costs under the 09-10 Policies.

The Court need not be distracted by the Insurers' arguments, because the brief analysis set forth above resolves the Motion. If it wishes to go further, those arguments are as follows:[6]

**(1)** That the Advancement Motion "did not specify that relief was sought only under the 2009-2010 tower" (Excess Insurer Opp. at 3-5), even though AIG acknowledged that we specifically requested advancement under the 09-10 Policies, by stating under oath that "Plaintiff D&Os are seeking coverage for the FDIC Lawsuit under the ***2009-10 Policy***"[7];

**(2)** That the "D&Os improperly seek a ruling under the 'inapplicable' remote possibility test" (AIG Opp. at 2), even though the Court already rejected this argument in holding that the "remote possibility test" governs the Insurers' advancement obligations, a holding that the First Circuit affirmed;

**(3)** That there is "no coverage" under the 09-10 Policies—the same assertion the Insurers made two years ago—except this time they base it on a new, untimely argument that they waived two years ago as a matter of law;

**(4)** That their untimely (and waived) argument can deny advancement under the 09-10 Policies, because *they have* "decided" that the FDIC's claims "relate" back to prior claims under the 06-07

[6] The Excess Insurers Opposition can be found at D.E. 958, and the AIG Opposition can be found at D.E. 959.
[7] *See* AIG's Opposition to the Advancement Motion, D.E. 185, at n. 8 (emphasis added) (citing Affidavit of M. Marrero at ¶ 5).

Policies, even though the "remote possibility" test applies to ***all coverage arguments***, including purported "interrelatedness" arguments, and there is at least a "remote possibility" that the FDIC's claims, based on purported "grossly negligent" loan approvals, are unrelated to securities fraud claims private plaintiffs made four years earlier, based on purported misrepresentations about a loan's impairment; and

**(5)** That the Court should defer ruling until it has decided the Excess Insurers' summary judgment motion, even though (a) the D&Os need, and are entitled to, the advancement of defense costs *right now, in preparing for trial*, and (b) the Insurers' advancement obligation is separate and distinct from their indemnity obligation.

We briefly demonstrate below that each of the Insurers' arguments is without merit. To keep the Insurers from shirking their advancement obligation on the eve of trial (when the 06-07 Policies will be exhausted, if not sooner), the Court should grant the D&Os' Motion.

**1. The D&Os' Advancement Motion expressly sought advancement under the 09-10 Policies, and AIG—speaking for all the Insurers—expressly admitted, under oath, that the D&Os were seeking advancement under the 09-10 Policies**

The Excess Insurers falsely assert that the Advancement Motion did not implicate the 09-10 Policies, which, they claim, gave them the right to put on blindfolds and "assume that your Honor did not specify the 2009-10 Policies because nothing in the motion papers before you requested a ruling specifying the 2009-10 Policies were applicable." Excess Insurers Opp. at 5. This disingenuous argument is false on its face, not to mention contrary to their advancement obligation.

***First***, the D&Os triggered the Insurers' advancement obligation when they gave the Insurers timely notice of claims that the FDIC "made" under the 09-10 Policies—the only condition precedent to advancement.[8] *See* 09-10 Policies, D.E. 1021-3, at §7(a); *DiLuglio v. New England Ins. Co.*, 959 F.2d 355, 358 (1st Cir. 1992) (Under a claims-made policy, "the pivotal event for insurance coverage purposes becomes the date the claim is *made* . . . ."). After

[8] The D&Os' letters that gave timely notice to the Insurers can be found at D.E. 1021-4.

receiving timely notice, the Insurers could avoid advancement only if there was "no possibility" of coverage under the 09-10 Policies. The Insurers argued that the "insured v. insured" exclusion negated "all possibility" of coverage, absolving them of the advancement obligation. The Insurers ***did not*** make any other argument in trying to avoid their advancement obligation under the 09-10 Policies. The Court's published opinion leaves no doubt about what was argued. *See W Holding Co., Inc. v. Chartis Ins. Co. - Puerto Rico*, 2012 WL 5379039, *3 (D.P.R. 2012) (stating that to avoid advancement, AIG "seems only to rely on the Insured v. Insured Exclusion as justification for impossibility"). Thus, if the Insurers should have "assumed" anything, they should have assumed that the 09-10 Policies *were the policies at issue on the Advancement Motion and the Order that granted it*, not the 06-07 Policies, which were already depleted by about one-third. In obedience to the Advancement Order, they should have advanced defense costs from the 09-10 Policies.[9]

***Second***, the assertion that the D&Os never asked for advancement under the 09-10 Policies is false. In the Advancement Motion, the D&Os defined the policies at issue to include the 09-10 Policies. *See* D.E. 147 at n. 2 (defining the policies at issue to include the 09-10 Policies). When AIG responded—on behalf of the Insurers—it admitted, under oath, that the "D&Os are seeking coverage for the FDIC Lawsuit under the 2009-10 Policy." *See* D.E. 185 at n. 8; *see also* sworn declaration of M. Marrero, D.E. 185-1 at ¶ 5.

**2. The "remote possibility" test governs advancement of defense costs, and the Insurers cannot now assert "coverage defenses" they did not assert two years ago**

For the first time ever, the Insurers argue that there is "no coverage" under the 09-10 Policies, because of Section 7(b) (a "Subsequent Notice Provision") and Section 4(d) (a "Prior Notice Exclusion") in the primary policy. *See* Excess Insurers Opp. at 11 and 15. The Insurers

[9] That said, if there's one thing we know from the Insurers' course of conduct, it's that obedience to the Advancement Order never was high on their "to do" list. In fact, one suspects it was put on their "not to do" list.

claim these arguments are not waived, despite their having not made them two years ago, or at anytime since.[10] This is incorrect.

The "remote possibility" test applies to *all* positions an Insurer takes to avoid advancement, including "interrelatedness" positions. There is no doubt that this test applies to the Excess Insurers' "interrelatedness" position under Section 4(d) of the primary policy—which is a type of exclusion. *E.g., Ryan v. Nat'l Union Fire Ins. Co. of Pittsburgh,* 692 F.3d 162, 168 (2d Cir. 2012) (affirming district court finding of a "possibility" that "interrelatedness" provision did not apply); *accord Brown v. AIG*, 339 F. Supp. 2d 336, 347 (D. Mass. 2004) (finding that an almost identical Prior Notice Exclusion did not preclude advancement, because "at least some of the wrongful acts alleged by the Trustee present a "reasonable potential for coverage").

The "remote possibility" test also applies to AIG's "interrelatedness" position under Section 7(b). AIG argues that Section 7(b) is not an exclusion, but some other thing that is "immune" from the "remote possibility" test. AIG cites no case in support, which is no surprise, because none exists. Nor has AIG offered any basis for its contention that Section 7(b) is anything other than an argument for negating coverage under the 09-10 policy, i.e., an exclusion. The "remote possibility" test applies to ***all denial of coverage arguments***, including "interrelatedness" arguments. It is not limited to arguments based on self-identified

[10] The Excess Insurers ignore the fact that none of these arguments were made on the Advancement Motion, the motion for reconsideration, the appeal, or at anytime since. The Insurers, once again, took unilateral steps to prejudice their insureds and obstruct the D&Os' defense of the FDIC-R's lawsuit, until a crisis was imminent and the D&Os were forced to seek the Court's assistance. Lawyers playing tactical games might think this clever, but it is nothing more than bad-faith obstinance. All the Insurers evidently think they can pocket their exclusion arguments for later use when it's convenient for them, and the Excess Insurers evidently were tasked with making the frivolous argument that the Advancement Motion was directed only at AIG. *See* Excess Insurers' Opp. at 3-4. But that motion sought advancement from *all of the policies*, and a decision as to *any policy* would be (and was) effective as to *all policies*, because the primary policies are identical and the excess policies "follow form." Thus, if the Excess Insurers believed an exclusion, or other policy provision, could have negated all coverage and thereby prevented advancement under the "remote possibility" test, the time to make those arguments was two years ago, not now.

"exclusions."[11] Because the "remote possibility" test applies to all provisions purporting to exclude, deny or negate coverage, the Insurers waived the right to make these "relatedness" arguments to prevent the advancement of defense costs, by never making them on the Advancement Motion. *See In re Caribbean Carrier Holding Panama, Inc.*, 2011 WL 1261191 (Bankr. D.P.R. 2011) (A party waives arguments not raised in opposition to a motion).

**3. Even if the Insurers were able to assert waived coverage defenses, there is a "remote possibility" that the FDIC's claims against the D&Os are unrelated to the prior claims**

Even if the Court were to entertain the Insurers' waived coverage defenses—two years after they failed to make them—their arguments are without merit. The Insurers claim that the FDIC's Non-Inyx Claims are "interrelated" with prior securities claims arising from borrower fraud (1) that *different, private plaintiffs* filed in 2006, (2) alleging that *different directors* failed to discover the borrower fraud, (3) relating to a *different loan* than the loans the D&Os are being sued for here, (4) originated by a *different lending division*, (5) governed by a *different policy*, and (6) operated by *different officers*, (7) which caused *different losses* (the "Inyx Lawsuits"). At a minimum, there is at least a "remote possibility" that the FDIC's Claims against the D&Os are "unrelated" to the Inyx Lawsuits.

In fact, one judge already found that the FDIC's Non-Inyx Claims "have limited relevance" to the Inyx Lawsuits. *Hildenbrand v. W Holding, et al.*, No. 3:07-cv-01886 (D.P.R.) [D.E. 330, at 9-10]. As a matter of logic, the Non-Inyx Claims, which a magistrate judge already found to have "limited relevance" to the Inyx loan *for purposes of discovery* (the loosest standard of all), cannot now be found "substantially related" to it for purposes of coverage (a much

[11] AIG also argues that its unilateral "relatedness decision," which it was not empowered to make, actually "saves W Holding $2,000,000" in retention amounts. We take the Insurers' feigned generosity in the same spirit in which they gave it. Retention amounts do not apply to non-indemnifiable losses, and as the Excess Insurers admit, "Westernbank no longer exists." D.E. 896 at 1. A non-existent Westernbank cannot indemnify the D&Os.

stricter standard). Therefore, even if this argument had not been waived, the Insurers could *not possibly* meet their burden of demonstrating "no possibility" of coverage under the 09-10 Policies because the FDIC Non-Inyx Claims are not substantially related with the Inyx Lawsuits.

Despite (or perhaps because of) these obvious, indisputable material differences, the Insurers choose to argue in generalities, claiming some sort of overarching "common plan" between these disparate claims, by disparate plaintiffs, which were "claims made" in different policy years.[12] *See* Excess Insurers Opp. at 11. They argue that a purportedly "reckless growth strategy" by Westernbank ties together these disparate clams. *Id.* This argument cannot prevail, because, as one court put it, "the mere existence of an aggressive loan policy" ***cannot*** tie together "disparate acts and omissions made by five directors in connection with the issuance of loans to over 200 unrelated borrowers . . . ." *Eureka Fed. Sav. & Loan Ass'n v. Am. Cas. Co. of Reading, Pa.*, 873 F.2d 229, 235 (9th Cir. 1989) (The allegedly related claims concerned numerous loans originated by *the same division* and governed by *the same policies*, which still was not enough); *accord FDIC v. Mmahat*, 907 F.2d 546, 554 (5th Cir. 1990) (rejecting argument that a "common

[12] The Excess Insurers' argument that "the D&Os cannot 'split' the FDIC Complaint into multiple Claims" is a distortion of fact and a misstatement of law. *See* Excess Insurers' Opposition at 8. The Excess Insurers previously acknowledged the undisputed fact that "[o]n December 17, 2010, the FDIC issued a letter asserting *claim**s*** against former Westernbank directors and officers." *See* Memorandum of Law in Support of Insurer Defendants' Joint Motion to Dismiss, D.E. 197 at 5 (emphasis added). Moreover, the FDIC's demand letter made claims under the 09-10 Policies, and, as a matter of law, consisted of multiple claims. *See, e.g., Pereira v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 525 F. Supp. 2d 370, 377 (S.D.N.Y. 2007), *aff'd sub nom., Pereira v. Gulf Ins. Co.*, 330 Fed. Appx. 5 (2d Cir. 2009) (finding each demand for damages to be a separate claim); *Cont'l Cas. Co. v. Orr*, 2008 WL 2704236 (D. Neb. 2008) ("the term 'claim' is not synonymous with "complaint," and a single lawsuit may contain multiple claims."); *Home Ins. Co. of Illinois (New Hampshire) v. Spectrum Info. Tech., Inc.*, 930 F. Supp. 825, 846-47 (E.D.N.Y. 1996) (A "'suit' may contain several discrete 'claims.'") (citation omitted); *AT&T Corp. v. Faraday Capital Ltd.*, 918 A.2d 1104, 1108 (Del. 2007) (same); *Bay Cities Paving & Grading v. Lawyers' Mutual Ins. Co.*, 5 Cal. 4th 854, 859 (Cal. 1993) ("We agree with the Court of Appeal's view that including multiple claims within a single action does not render them a single claim . . . . [T]he 'cause of action' is based upon the harm suffered, as opposed to the particular theory asserted by the litigant," and "one *injury* gives rise to only one claim for relief.'") (citation omitted); Scott Seaman & Jason Schulze, *Allocation of Losses in Complex Insurance Coverage Claims* § 14:2 at 14-8 (2d ed. 2006) (Where there are numerous acts or omissions and different time periods and claimants, courts often find multiple claims."). The Excess Insurers' reliance on *Fed. Ins. Co. v. Raytheon Co.*, 426 F.3d 491, 501 (1st Cir. 2005) is misplaced. The insured therein *conceded* that the lawsuit at issue presented a single claim. *See id*. at 502, n. 10. Absent that concession, the court might have accepted the dissent's position that each different liability theory was a different claim, which is the "more common definition," and "the definition which best addresses the parties' reasonable expectations . . . ." *Id*. at 502.

plan," consisting of a desire to "generate fees," made claims interrelated, because "a single motive does not make a single act."); *FSLIC v. Burdette*, 718 F. Supp. 649, 660 (E.D. Tenn. 1989) (rejecting insurer's theory "that all twenty-five loans and participations are tied together by a common thread.").

A "common plan" based on a purportedly "reckless growth strategy" cannot tie together unrelated claims for the simple reason that it would cause every subsequent claim to be "related" to any prior claim, which would render illusory the promise of coverage in subsequent insurance policies. Banks, like all other businesses, are in the business of growing their business. If the Insurers could exclude any subsequent claim based on a purported "growth strategy" that hindsight allows one to claim was "reckless," it would allow insurers to "preclude coverage for *any* claim against [the insureds] based on how it provides business services . . . ." *ACE Am. Ins. Co. v. Ascend One Corp*., 570 F. Supp. 2d 789, 800 (D. Md. 2008) (finding subsequent claim unrelated). Thus, there is at least a "remote possibility" that the FDIC's Non-Inyx Claims do not relate back to the Inyx Lawsuits.

**4. The D&Os are entitled to advancement now, and it would violate the 09-10 Policies to defer ruling until summary judgment**

The Excess Insurers claim the D&Os are not prejudiced by their stonewalling and accounting gambits because they are advancing defense costs now, and argue that "the Court should deny the D&Os' motion and resolve the issues of coverage on the merits as presented in the pending motions for summary judgment . . . ." Excess Insurers Opp. at 8. First of all, the Insurers' duties to advance and to indemnify (or ultimately cover claims) are separate duties that "require[] separate analysis." *Employers Mut. Cas. Co. v. PIC Contractors, Inc.*, 24 F. Supp. 2d 212, 215 (D.R.I. 1998). The analysis for an Insurers' obligation to advance costs under the 09-10 Policies is whether is a remote possibility of coverage based on "a liberal interpretation of the

pleadings, that the insured is protected by the policy issued, regardless of the final outcome of the case." *Metlife Capital Corp. v. Westchester Fire Ins. Co.*, 224 F. Supp. 2d 374, 388 (D.P.R. 2002). This Court performed (and completed) its "advancement analysis" two years ago, when it ordered the Insurers to advance defense costs under all of the policies at issue. Consistent with their obstinate obstruction of their insureds' efforts to defend themselves, the Insurers attempted an end run of the Advancement Order through an accounting gambit, ledgering defense costs from the already dwindled 06-07 Policies and sitting on their hands until the close of discovery, hoping to run out the clock. This is improper, and highly prejudicial. If the Court were to roll up the advancement issue with the summary judgment motions, it could leave the D&Os with no funds to defend themselves, let alone settle this case.[13]

Moreover, deferring ruling on this Motion would violate the policies. As the First Circuit correctly pointed out, the 09-10 Policies state that the Insurers "must advance defense costs . . . . ***prior to the final disposition of a claim***." *W Holding Co.*, 2014 WL 1280246 (1st Cir. 2014) (emphasis added). Summary judgment is a "final disposition," and for the Court to defer ruling on this motion until it decides the Insurers' summary judgment motions would contradict the plain language of 09-10 Policy and deny the D&Os their fundamental right to advancement.

## CONCLUSION

Two years ago the Insurers had the opportunity, and were required, to assert any "relatedness" argument that might have limited advancement by negating coverage under the 09-10 Policies. Instead of making any such argument, they kept silent, apparently believing they could unilaterally decide to ledger all defense costs against the almost-depleted 06-07 Policies.

[13] The Excess Insurers assert that there are "substantial funds" remaining in the 06-07 Policies, but that is far from true. Notwithstanding the fact that there is less than $10 million left under second to last excess layer, and the fact that the final excess layer has refused to pay a dime to anyone, by the time this Motion is briefed, extensive summary judgment briefing will have been required, depositions remain incomplete, and the parties will soon begin expert discovery. The 06-07 Policies will be completely dissipated in short order.

That gambit was improper, and the Insurers waived the right to assert a "relatedness" argument now. At bottom, the D&Os gave the Insurers timely notice of the FDIC's clams, which are "claims made" under the 09-10 Policies. That timely notice triggered the D&Os' right to advancement, unless the Insurers could establish "no possibility" of coverage. The Insurers failed to establish "no possibility" of coverage. Instead, this Court found the requisite "remote possibility" of coverage, in an Advancement Order that the First Circuit affirmed. Accordingly, there is no question that the D&Os are entitled to advancement from the 09-10 Policies, and the Advancement Order should be clarified to leave no doubt.

**RESPECTFULLY SUBMITTED** in San Juan, Puerto Rico, on May 5, 2014.

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**CERTIFICATE OF SERVICE**

I CERTIFY that on May 5, 2014, I electronically filed this document with the Clerk of the Court using CM/ECF. I also certify that this document is being served today on all counsel of record either by transmission of Notices of Electronic Filing generated by CM/ECF or by U.S. Mail.

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