

## CLIENT MEMORANDUM

# FDIC Issues Advisory Statement Regarding D&O Insurance Policies, Exclusions and Indemnification for Civil Money Penalties

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## AUTHORS

**Mitchell J. Auslander** | **Christopher J. St. Jeanos** | **Megan Y. Hogan**

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On October 10, 2013, the Federal Deposit Insurance Corporation (the “FDIC”) issued the attached advisory statement in response to its concern that there has been an increase in exclusionary terms contained in directors and officers liability insurance policies issued to depository institutions. The statement reminds directors and officers of banks (1) to make sure they understand the scope and significance of exclusions in their D&O insurance policies; and (2) that a bank’s purchase of insurance indemnifying against civil money penalties (“CMPs”) is prohibited.

With respect to the first reminder, the FDIC acknowledges that directors and officers are exposed to personal financial liability for damages arising out of civil suits relating to their decisions and actions when indemnification is not available due to exclusions in insurance policies. The agency goes as far as to state that the inclusion of additional exclusionary provisions “may affect the recruitment and retention of well-qualified individuals.” Although the FDIC does not cite to specific exclusionary language, it can be inferred that the FDIC is referring primarily to regulatory exclusions that exclude coverage for claims brought by any governmental, quasi-governmental or self-regulatory entity, including the FDIC.

It is unique to the banking industry that the FDIC, under certain circumstances, may be appointed conservator or receiver of a failing or struggling federal or state depository institution and thus put in the position of bringing post-closure claims against the failed bank. If a D&O liability insurance policy includes a regulatory exclusion, directors and officers may not be indemnified for claims brought against them by the FDIC. As suggested in the statement, it is therefore important for

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directors and officers to be fully aware during renewal with their insurance carriers of both the current terms of their policies and the proposed addition of terms.

As to the second reminder, perhaps as a hedge against its expressed concern regarding the scope of D&O coverage, the FDIC reiterates that CMPs cannot be paid with insurance money. A CMP may be assessed for the violation of any law or regulation, as well as for a violation of any condition imposed in writing by a banking agency in connection with any written agreement between a bank and the federal agency. In its statement, the FDIC reminds directors that the FDIC regulations prohibit banks from purchasing insurance that could be used to pay or reimburse an institution-affiliated party ("IAP") for the cost of any CMP assessed against such person in an administrative proceeding or a civil action commenced by any federal banking agency. The statement also makes clear that the FDIC regulations do not include an exception for cases in which an IAP reimburses the depository institution for the designated cost of the CMP coverage. As a result, banks are now officially on notice that they should not purchase insurance that would pay or reimburse for CMPs regardless of whether the bank itself or individual directors and officers pay for the CMP protection.

D&O insurance coverage for all industries is constantly changing. Directors and officers should review their D&O policies and be cognizant of exclusions within the policies and exclusionary language in policy endorsements. To the extent an insurer states its intention to add exclusions during future renewal discussions, as always, discuss the potential implications of such exclusions and policy language alternatives with your brokers or legal professionals.

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If you have any questions regarding this memorandum, please contact Mitchell J. Auslander (212 728-8201, [mauslander@willkie.com](mailto:mauslander@willkie.com)), Christopher J. St. Jeanos (212 728-8730, [cstjeanos@willkie.com](mailto:cstjeanos@willkie.com)), Megan Y. Hogan (212-728-8942, [mhogan@willkie.com](mailto:mhogan@willkie.com)) or the Willkie attorney with whom you regularly work.

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