

Prison Break: Insurer Seeks to Escape Coverage for Suit Tied to “El Chapo”

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In an appeal to the Ninth Circuit, a private equity firm has asked the court to reverse an order finding there was no coverage for a suit alleging it concealed that a facility it sold was run by Joaquín “El Chapo” Guzmán. AKN Holdings had purchased a manufacturing facility in Reynosa, Mexico, from Thermo Fisher, unaware that the facility “was overrun” by the drug cartel of “El Chapo.” After discovering the concealment, AKN Holdings sued Thermo Fisher and, while that suit was pending, in turn sold the facility to FINSA, also without disclosing the cartel activities or its pending lawsuit.

FINSA filed suit against AKN Holdings, alleging breach of contract for failing to disclose the drug activities. AKN Holdings tendered the suit to its insurer, Great American, which denied coverage, and in the subsequent coverage action, moved to dismiss AKN Holdings’ claims based on the policy’s contract exclusion. The district court granted the motion to dismiss, finding there was no coverage under the contract exclusion because the FINSA suit arose out of lease, purchase and guaranty agreements executed in connection with the sale.

On June 4, 2021, AKN Holdings appealed the order, but its brief was silent as to the El Chapo and cartel allegations, instead arguing that the FINSA suit alleged it concealed other facts and that the claims were for fraud, rather than breach of contract. AKN Holdings argued that the FINSA suit claims constituted “wrongful acts” under the policy and that the tort claims were not subject to the contract exclusion. Great American recited the drug cartel facts in its response brief, filed January 10, 2022, and noted that under California law, the phrase “arising out of” is construed broadly. The brief argues that all of the claims arise out of the purchase, lease and guaranty agreements, absent which, “FINSA would not have suffered any loss and no recovery could be had against AKN Holdings premised on fraud or any legal theory. The FINSA Action is accordingly ‘based upon,’ ‘arises from,’ or ‘is in any way related to’ AKN Holdings’ ‘actual or alleged breach of a written contract or agreement,’ such that coverage is precluded by the policy’s contract exclusion.”

The case style is *AKN Holdings, LLC v. Great American E&S Insurance Company*, No. 21-55590, United States Court of Appeals for the Ninth Circuit and was reported by Law 360.

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