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Attorneys for Defendant

IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF OREGON  
EUGENE DIVISION

UMPQUA BANK, an Oregon chartered  
commercial bank,

CV No.: 10-6423-AA

Plaintiff,

vs.

PROGRESSIVE CASUALTY  
INSURANCE COMPANY, an Ohio  
corporation,

**DEFENDANT PROGRESSIVE  
CASUALTY INSURANCE  
COMPANY'S ANSWER TO  
PLAINTIFF UMPQUA BANK'S  
COMPLAINT AND  
COUNTERCLAIMS**

Defendant.

Progressive Casualty Insurance Company ("Progressive") responds to the Complaint  
herein as follows:

**ANSWER**

1. Paragraph 1 contains legal conclusions to which no response is required. To the extent that a response is required, Progressive admits, on information and belief, the jurisdictional allegations set forth in paragraph 1.

2. Paragraph 2 contains legal conclusions to which no response is required. To the extent that a response is required, Progressive admits, on information and belief, the allegations addressing venue set forth in paragraph 2.

3. Progressive admits, on information and belief, the allegations set forth in paragraph 3.

4. Progressive admits the allegations set forth in paragraph 4, except it denies that it is an unincorporated subsidiary of Progressive Corporation. Progressive avers that it is a separately incorporated entity under the laws of the State of Ohio. Progressive is a subsidiary of Drive Insurance Holdings, Inc., which is a subsidiary of the Progressive Corporation.

5. Progressive admits that it issued Policy No. 10028871-05 (the "Progressive Policy") and refers to that document (attached hereto as "Exhibit A") for its full and complete contents. To the extent that the allegations contained in paragraph 5 purport to describe or characterize the contents of the Policy, that document speaks for itself and no response is required. To the extent a response is required, those allegations are denied. All other allegations contained in paragraph 5 are denied.

6. To the extent that the allegations contained in paragraph 6 purport to describe, characterize or selectively quote from the contents of the Progressive Policy, those allegations are denied. Progressive respectfully refers to the Policy in its entirety, which speaks for itself. All other allegations contained in paragraph 6 are denied.

7. Progressive admits that, in June 2009, Kevin Padrick, purportedly as trustee of the Summit Accommodators Liquidating Trust, filed a civil action against Umpqua in the Circuit Court for the State of Oregon, County of Multnomah (the "Oregon Court"), Case No. 0906-08488 (the "Padrick Action"). To the extent that the allegations contained in paragraph 7 purport

to describe or characterize the contents of the operative (second amended) complaint in the Padrick Action (the "Padrick Complaint," attached hereto as "Exhibit B"), that document speaks for itself and no response is required. All other allegations contained in paragraph 7 are denied.

8. Progressive admits that, in September 2009, Danae Miller and 56 other parties filed a civil action against Umpqua in the Oregon Court, Case No. 0909-12729 (the "Miller Action"). Progressive also admits that the Oregon Court consolidated the Padrick and Miller Actions into the "Consolidated Cases." To the extent that the allegations contained in paragraph 8 purport to describe or characterize the contents of the operative (fourth amended) complaint in the Miller Action (the "Miller Complaint," attached hereto as "Exhibit C"), that document speaks for itself and no response is required. All other allegations contained in paragraph 8 are denied.

9. Paragraph 9 contains legal conclusions to which no response is required or given. Progressive admits that Umpqua informed Progressive of the Padrick and Miller Actions in June 2009 and September 2009, respectively. Progressive also admits that it reserved all of its rights with respect to the Padrick and Miller Actions, and that it indemnified Umpqua for certain defense costs related thereto. All other allegations contained in paragraph 9 are denied.

10. Progressive admits the allegations set forth in paragraph 10 and avers that the terms of the agreement reached on September 21, 2010 were reduced to a writing signed by the parties to the Consolidated Cases. Progressive was not a party to the Consolidated Cases.

11. Progressive admits the allegations set forth in paragraph 11 and avers that the terms of the agreement reached on September 21, 2010 were reduced to a writing signed by the parties to the Consolidated Cases. Progressive was not a party to the Consolidated Cases.

12. Progressive denies the allegations set forth in paragraph 12 as stated. Progressive avers that, subject to a full reservation of rights, it advanced to Umpqua 40.8 percent of the settlement amount for which Umpqua became liable as part of the settlement of the Consolidated Cases (the "Progressive Advancement"). Progressive further avers, upon information and belief,

that Umpqua funded the remainder of the settlement amount for which Umpqua became liable as a part of the settlement of the Consolidated Cases.

13. Progressive admits, on information and belief, the allegations set forth in paragraph 13.

14. Progressive incorporates and reasserts its answers to paragraphs 1 through 13 as if fully set forth herein.

15. Paragraph 15 contains legal conclusions to which no response is required. To the extent that a response is required, those allegations are denied. To the extent that the allegations contained in paragraph 15 purport to describe or characterize the contents of the Progressive Policy, that document speaks for itself and no response is required. All other allegations contained in paragraph 15 are denied.

16. Paragraph 16 contains legal conclusions to which no response is required. To the extent that a response is required, those allegations are denied. To the extent that the allegations contained in paragraph 16 purport to describe or characterize the contents of the Progressive Policy, that document speaks for itself and no response is required. All other allegations contained in paragraph 16 are denied.

17. Paragraph 17 contains legal conclusions to which no response is required. To the extent that a response is required, those allegations are denied. To the extent that the allegations contained in paragraph 17 purport to describe or characterize the contents of the Progressive Policy, that document speaks for itself and no response is required. All other allegations contained in paragraph 17 are denied.

18. Paragraph 18 contains legal conclusions to which no response is required. To the extent that a response is required, those allegations are denied. All other allegations contained in paragraph 18 are denied.

19. Paragraph 19 contains legal conclusions to which no response is required. To the extent that a response is required, those allegations are denied. All other allegations contained in paragraph 19 are denied.

20. Paragraph 20 contains legal conclusions to which no response is required. To the extent that a response is required, those allegations are denied. To the extent that the allegations contained in paragraph 20 purport to describe or characterize the contents of the Progressive Policy, that document speaks for itself and no response is required. All other allegations contained in paragraph 20 are denied.

21. Paragraph 21 contains legal conclusions to which no response is required. To the extent that a response is required, those allegations are denied. All other allegations contained in paragraph 21 are denied.

22. Paragraph 22 contains legal conclusions to which no response is required. To the extent that a response is required, those allegations are denied. All other allegations contained in paragraph 22 are denied.

23. All allegations not expressly admitted are hereby denied.

#### **AFFIRMATIVE DEFENSES**

Progressive alleges that plaintiff is not entitled to judgment based upon the following affirmative defenses, without taking on the burden of proof as to any such matter that would otherwise rest with plaintiff.

#### **FIRST AFFIRMATIVE DEFENSE**

24. The complaint fails to state a claim upon which relief may be granted.

#### **SECOND AFFIRMATIVE DEFENSE**

25. Umpqua has waived any right to the relief sought.

#### **THIRD AFFIRMATIVE DEFENSE**

26. Umpqua is estopped from claiming the relief sought.

#### **FOURTH AFFIRMATIVE DEFENSE**

27. Umpqua is barred from relief on the grounds that it has failed to comply with the terms of the Progressive Policy.

**FIFTH AFFIRMATIVE DEFENSE**

28. Umpqua is barred, in whole or in part, from the relief sought because of the provisions, terms, exclusion, and conditions of the Progressive Policy, including, but not limited to Policy Section V (Illegal Profit/Payment Exclusion) (subsections (1) and (3)) and as a matter of public policy.

**SIXTH AFFIRMATIVE DEFENSE**

29. Umpqua has failed to mitigate its alleged damages or losses.

**SEVENTH AFFIRMATIVE DEFENSE**

30. Umpqua's claim for damages or losses, if any, must be setoff or reduced by the value of all consideration given or transferred to Umpqua under the terms of the September 21, 2010 Settlement Agreement, including, without limitation, the value of all property, security, and assignments transferred to Umpqua pursuant to paragraph 2 thereof, as well as any other recovery, or right to recovery, that Umpqua may have or had.

**EIGHTH AFFIRMATIVE DEFENSE**

31. Progressive explicitly reserves the right to supplement or amend its affirmative defenses as additional facts become known during its investigation and discovery.

**COUNTERCLAIMS**

Progressive alleges that plaintiff is not entitled to judgment based upon the following counterclaims, and that Progressive is entitled to affirmative relief.

**NATURE OF COUNTERCLAIMS**

32. Progressive seeks to recover from Umpqua the Progressive Advancement plus pre-judgment interest on that amount accruing from the date on which Progressive advanced the Progressive Advancement.

33. The basis for this counterclaim is that there is no coverage under the Progressive Policy for the settlement of the Consolidated Cases. As a result, and in light of Progressive's

express reservation of the right to recoup the Progressive Advancement, Progressive is entitled to the relief sought herein.

34. Progressive also seeks a declaration that there is no coverage under the Progressive Policy for any part of the settlement of the Consolidated Cases.

### **JURISDICTION**

35. The Court has jurisdiction over this counterclaim pursuant to 28 U.S.C. § 1332 and 28 U.S.C. §§ 2201 and 2202. Both parties to this counterclaim are of diverse citizenship and the amount in controversy exceeds \$75,000 exclusive of interest, fees, and other costs.

### **PARTIES**

36. Progressive is an insurance company organized as a corporation under the laws of the State of Ohio, with its principal place of business in Mayfield Village, Ohio.

37. Upon information and belief, Umpqua is a commercial bank organized under the laws of the State of Oregon, with its principal place of business in Roseburg, Douglas County, Oregon.

### **THE UNDERLYING CIVIL ACTIONS**

38. In June 2009, Kevin Padrick (“Padrick”), purportedly as trustee of the liquidating trust created to administer the assets of the bankruptcy estate of Summit Accommodators, Inc. (“Summit”), filed the Padrick Action.

39. A true and correct copy of the Second Amended Padrick Complaint is attached hereto as Exhibit B.

40. Summit was in the business of facilitating 1031 exchanges. Generally, a “1031 exchange” is a transaction in which a taxpayer defers capital gains taxes by exchanging “like-kind property” pursuant to Section 1031 of the Internal Revenue Code.

41. In its role as a 1031 intermediary, Summit would hold 1031 exchange funds for the benefit of its clients (“Exchange Funds”).

42. The Padrick Complaint alleges that, in or about 1995, two of Summit’s principals began embezzling from the Exchange Funds by transferring money from Summit to Inland

Capital Corp. (“Inland”). Rather than hold the Exchange Funds for the benefit of Summit’s clients, Inland allegedly lent the money to Summit’s principals and related parties for their personal benefit (the “Insider Loans”).

43. The Insider Loans are alleged to have caused Summit to suffer liquidity problems because Summit did not have sufficient funds to cover its outstanding obligations to clients. As a result, Summit’s principals allegedly started a Ponzi scheme, using money from new clients to pay old clients.

44. The Padrick Complaint alleged that Umpqua and its senior managers were aware of and aided and abetted this Ponzi scheme as follows:

The principals used the embezzled funds for their own personal benefit and for the benefit of their friends and family members. The highest level of management at Umpqua Bank – including Umpqua’s CEP Ray Davis and its then President Dave Edson – became fully aware of this Ponzi scheme and the principals’ embezzlement, as well as the substantial financial risks that the principals’ misconduct created for Summit and its clients. Yet, Davis, Edson and other Umpqua officials continued to actively encourage and materially assist the Summit principals in their tortious conduct, including by encouraging them to use Umpqua’s banking services as a depository for the continued flow of embezzled funds, by making substantial loans to Summit’s principals and/or for the real estate investments that were part of the Ponzi scheme, and by actively assisting the Principals in generating new customers and victims of the Ponzi scheme – even referring to their relationship as an “alliance.” Umpqua did so because it reaped huge financial rewards from Summit’s business.

Second Amended Complaint by Kevin D. Padrick at ¶ 1.

45. Padrick asserted a single cause of action for conspiracy/aiding and abetting. To this end, Padrick alleged that Umpqua and Summit’s principals “acted in concert in accomplishing the tortious conduct described” in the Padrick Complaint. Padrick further alleged that Umpqua “knew that the [p]rincipals’ conduct was tortious and/or had a general awareness of the [p]rincipals’ tortious scheme” and Umpqua “substantially assisted and encouraged the [p]rincipals in their tortious conduct.”

46. Padrick further alleged that “Umpqua acted with malice and/or has shown a reckless and outrageous indifference to a highly unreasonable risk of harm and has acted with

conscious indifference to the welfare of others.” As relief, Padrick sought between \$25 million and \$30 million, plus costs and disbursements and other just and equitable relief.

47. In or about September 2009, Danae Miller and various other clients and creditors of Summit filed the Miller Action against Umpqua in the Circuit Court of Oregon for Multnomah County.

48. The Fourth Amended Complaint in the Miller Action (the “Miller Complaint”) is attached hereto as Exhibit C.

49. The allegations of the Miller Complaint largely follow the allegations in the Padrick Action, and assert claims for aiding and abetting fraud and conversion, and for breaches of fiduciary duty.

50. The Padrick Action and Miller Action were consolidated and are referenced to herein as the Consolidated Cases.

#### **THE PROGRESSIVE POLICY**

51. Attached hereto as Exhibit A is a true and correct copy of the Progressive Policy.

52. Subject to all of its terms, conditions and exclusions, the Progressive Policy affords certain claims-made coverage for the Policy Period from May 20, 2009 through May 20, 2011.

53. The illegal profit/payment exclusion of the Progressive Policy Policy (Section V) provides:

The Insurer shall not be liable to make any payment for Loss, other than Defense Costs, in connection with any Claim arising out of or in any way involving:

1. any Insured gaining, in fact, any profit, remuneration, or financial advantage to which the Insured was not legally entitled;
2. payment by the Company of inadequate or excessive consideration in connection with its purchase of Company securities; or
3. conflicts of interest, engaging in self-dealing, or acting in bad faith.

(Progressive Policy, Section V)

54. Umpqua is alleged to have had knowledge of Summit's tortious activities, yet continued to provide Summit material assistance while benefiting financially therefrom. Accordingly, coverage is precluded under Subsection (1) of the illegal profit/payment exclusion.

55. Subsection (3) of the illegal profit/payment exclusion bars coverage for the settlement because the Padrick and Miller complaints allege that Umpqua acted in bad faith by aiding and abetting the Summit Ponzi scheme.

56. Alternatively, Subsection (3) of the illegal profit/payment exclusion bars coverage for the settlement because Umpqua is alleged to have acted, in effect, in bad faith by aiding and abetting the Summit Ponzi scheme.

57. Policy Section IV, Definitions, excludes from the Policy's definition of Loss "any matters which are uninsurable under the law pursuant to which this **Policy** should be construed." Coverage for the Settlement also is barred by public policy to the extent that Umpqua's conduct is uninsurable.

#### **SETTLEMENT AND PROGRESSIVE'S RESERVATION OF RIGHTS**

58. The parties to the Consolidated Cases conducted a mediation on September 20 and 21, 2010. Pursuant to the terms of the settlement negotiated at the mediation, Umpqua was required to make a payment to the plaintiffs in the Consolidated Cases.

59. Umpqua demanded that Progressive fund that portion of the settlement of the Consolidated Cases for which Umpqua was liable. Progressive advanced to Umpqua a portion of that amount, referred to herein as the Progressive Advancement. The Progressive Advancement was made subject to a full reservation of Progressive's rights, including its right to seek reimbursement from Umpqua.

#### **FIRST COUNTERCLAIM**

##### **(Restitution or Recoupment from Umpqua)**

60. Progressive repeats, realleges, and incorporates by reference the allegations in paragraphs 32 through 59, above.

61. The Progressive Policy provides no coverage for the Settlement.

62. Progressive advanced the Progressive Advancement towards the settlement of the Consolidated Cases subject to a full and complete reservation of rights.

63. With full knowledge of the reservation of rights, Umpqua proceeded with the settlement and accepted the Progressive Advancement.

64. Because the Progressive Policy provides no coverage for the settlement of the Consolidated Cases, Progressive had no obligation to make the Progressive Advancement.

65. Progressive is entitled to a judgment in its favor that Umpqua must repay the Progressive Advancement. Progressive is further entitled to a judgment in its favor that Umpqua must pay prejudgment interest on the Progressive Advance, running from the date on which the advance was made.

## **SECOND COUNTERCLAIM**

### **(Declaration of No Coverage)**

66. Progressive repeats, realleges, and incorporates by reference the allegations in paragraphs 32 through 65, above.

67. Coverage for the Settlement of the Consolidated Action is precluded by Policy terms, conditions and exclusions, including but not limited to, Policy Section V (Illegal Profit/Payment Exclusion) subsections (1) and (3). Coverage also may be precluded as matter of public policy.

68. Accordingly, Progressive is entitled to a declaration that there is no coverage for the settlement of the Consolidated Actions.

## **PRAYER FOR RELIEF**

WHEREFORE, Progressive prays that this Honorable Court order, adjudge and decree the following relief:

- A. An award to Progressive in the amount of the Progressive Advancement with pre- and post-judgment interest thereon;

- B. A declaration that there is no coverage under the Progressive Policy for the settlement of the Consolidated Cases;
- C. An award of costs and disbursements;
- D. Such other and further relief as the Court deems just, necessary and proper.

DATED this 7th day of February, 2011.

MARKOWITZ, HERBOLD, GLADE  
& MEHLHAF, P.C.

By: 

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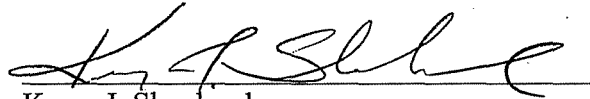
**ATTORNEY CERTIFICATE OF SERVICE**

I hereby certify that on February 7, 2011, I have made service of the foregoing **DEFENDANT PROGRESSIVE CASUALTY INSURANCE COMPANY'S ANSWER TO PLAINTIFF UMPQUA BANK'S COMPLAINT AND COUNTERCLAIMS** on the party listed below in the manner indicated:

Seth H. Rowe / Michael E. Farnell  
Parsons Farnell & Grein, LLP  
1030 SW Morrison Street  
Portland, OR 97205

- U.S. Mail
- Facsimile
- Hand Delivery
- Overnight Courier
- Email
- Electronically via USDC CM/ECF system

DATED this 7th day of February, 2011.



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