wiley

NEWSLETTER

Notice of Prior Suit Against Company Does Not Constitute Adequate Notice of Later Suit Against Directors and Officers

January 2008

A Florida appellate court has held that a D&O policy issued to a company does not afford coverage for shareholder lawsuits against directors and officers of the company (the "Shareholder Suit") filed after the policy expired even though the company had tendered during the policy period a lawsuit filed against the company over a failed merger as well as a state insurance investigation into the company's reserve levels (the "Prior Proceedings") because the Prior Proceedings did not provide the insurer with sufficient notice that the earlier matters could lead to shareholder suits against the company's directors and officers. *National Union Fire Ins. Co. of Pittsburgh, P.A. v. Underwriters at Lloyd's, London*, 2007 WL 4179675 (Fla. Ct. App. Nov. 28, 2007).

The insurer issued a claims-made D&O policy to a company that was also an insurer. The policy contained a provision addressing notice of potential claims, which stated that:

"If during the Policy Period the Assureds first become aware of a specific Wrongful Act, and if the Assureds during the Policy Period give written notice to Underwriters as soon as practicable of:

- The specific Wrongful Act, and
- The consequences which have resulted or may result therefrom, and
- The circumstances by which the Assureds first became aware thereof,

then any Claim made subsequently arising out of such Wrongful Act shall be deemed for the purposes of this Policy to have been made at the time such notice was first given."

The insured company had entered into a merger agreement after disclosing that it was under-reserved, in violation of state law, by $100 million. When it became apparent that the company was actually under-reserved by a far greater amount, the Florida Department of Insurance filed a complaint seeking a receivership for the company, and the merger partner sued to rescind the merger agreement. The company provided notice of the Prior Proceedings to its D&O insurance carrier during the relevant policy period by

sending the insurer a copy of the receivership pleadings and the complaint from the lawsuit. The insurer declined coverage on the ground that the policy only afforded coverage to the company's officers and directors, and the Prior Proceedings named only the company as a defendant.

The Shareholder Suit, which alleged that the company's officers and directors violated federal securities laws by making misrepresentations about its reserves, was filed and tendered to the insurer after the end of the policy period. The insurer denied coverage on the grounds that the Shareholder Suit was filed after the policy period expired and did not involve the same wrongful acts alleged in the Prior Proceedings.

The court held that the complaints in the Prior Proceedings, both filed against the insured company, did not place the insurer on notice of a potential shareholder class action against the company's officers and directors. The court reasoned that, even assuming that the Shareholder Suit arose out of the same wrongful acts alleged in the Prior Proceedings, the pleadings from those matters "did not adequately describe the consequences that resulted from [the company's] wrongful acts." In particular, there "was no reference in these materials to intimate a potential claim that might be brought against [the company's] directors and officers by its shareholders for securities law violations." According to the court, "an insurance company cannot reasonably be expected to speculate that litigation in connection with a failed merger, or an insurance department's concern about under-reserved [sic], would lead to a shareholder's class action against directors and officers for securities law violations."