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NEWSLETTER

District Court: "Other Insurance" Provisions Mutually Repugnant and "Loss" Does Not Require That Insureds Pay Settlement

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The United States District Court for the District of Connecticut, applying Virginia law, has denied a D&O insurer's motion for summary judgment, holding that two "other insurance" provisions were mutually repugnant. *Macey v. Carolina Cas. Ins. Co.*, 2012 WL 6125200 (D. Conn. Dec. 10, 2012). The court also held that the D&O policy's definition of "Loss" did not require that the insureds pay an underlying settlement as long as the insureds incurred legal liability.

An insurer issued a D&O policy to a company that had been formed through a corporate merger and stock sale (the merged entity). As part of the merger transaction, certain prior owners and directors of the merged entity (the Legacy Shareholders) became directors of the surviving entity, but only for purposes of approving the corporate reorganization. They then resigned from the board in order to close the merger and were replaced by directors chosen by the entity that purchased the majority of the surviving entity's stock (the purchasing entity). Approximately one year later, the Legacy Shareholders sued the directors who had replaced them for taking subsequent actions that divested the Legacy Shareholders of the minority ownership interests they had retained after the merger and stock sale, naming the individual directors, the merged entity and the purchasing entity as defendants. The defendant directors sought coverage under the merged entity's D&O policy, as well as the purchasing company's officers, directors and managers insurance policy The parties eventually settled the underlying suit for $3 million, with the purchasing entity's insurer paying $1.5 million plus the defense costs, and the purchasing entity paying the remainder of the settlement.

The merged entity's D&O insurer denied coverage for the Legacy Shareholders suit based on the "insured vs. insured" exclusion, the "other insurance" provision, and the argument that the Legacy Shareholders did not suffer "loss" under the policy. In a prior holding, after the individual directors filed suit against the merged entity's D&O insurer, the United States Court of Appeals for the Second Circuit reversed a ruling by the district court in favor of the merged entity's D&O insurer based on the "insured vs. insured provision," remanding the case to the district court. *See* July 9, 2010 article. On remand, the court held that the competing "other insurance" provisions were mutually repugnant because each of the "other insurance" provisions in the two policies were triggered. On this basis, it held that they should be disregarded.

The court also denied summary judgment concerning the D&O insurer's "no loss" argument. The insurer contended that, because the purchasing entity and its carrier funded the defense of the underlying litigation and its settlement, the insureds had not incurred "loss," which was defined to include "damages, judgments [and] settlements . . ." The D&O insurer contended that summary judgment was appropriate because (1) the individual directors did not have to pay any of the underlying settlement or defense costs out of their pocket, and (2) any recovery by the individual directors should be equitably barred as it would result in either a windfall or double recovery for the directors. The court held that, "[n]otwithstanding the fact that the [D&O policy] expressly excludes eight items from the contractual definition of 'Loss,' nowhere does it indicate that the 'damages, judgments, settlements' must have been initially paid by the insured" and that the "insured's legal liability by itself triggers coverage." The court also held that, because the directors agreed to assign any proceeds of this coverage litigation to the purchasing entity, there was no risk of double recovery.