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NEWSLETTER

I v. I Exclusion Precludes Coverage for Suit Filed by Former Director

June 2005

The United States Court of Appeals for the Eleventh Circuit has upheld a district court's grant of summary judgment for an insurer on the grounds that the I v. I exclusion in the policy precludes coverage for a securities class action initiated by a former director. *Sphinx Int'l, Inc. v. Nat'l Union Fire Ins. Co.*, 2005 WL 1389234 (11th Cir. June 14, 2005). In affirming the district court's grant of summary judgment, the court held, *inter alia*, that the lack of collusion between the underlying litigants did not foreclose the application of the plain language of the exclusion and that the exclusion precluded coverage for the entire underlying action, not simply that portion of the action attributable to the insured plaintiff.

A former director of the insured entity brought a securities class action against the insured entity and several of its directors. Thereafter, the former director solicited and recruited other shareholders to join in the litigation. The insured entity sought coverage for the securities class action under a D&O policy. The insurer denied coverage based on the I v. I exclusion, which barred coverage for claims against the insured entity brought:

By or at the behest of the Company, or any affiliate of the company or any Director or Officer, or by any security holder of the Company, whether directly or derivatively, unless such Claim is instigated and continued totally independent of, and totally without the solicitation of, or assistance of, or active participation of, or intervention of any Director or Officer or the Company.

In response, the insureds filed coverage litigation.

In reviewing the district court's grant of summary judgment to the insurer, the court of appeals rejected the insured entity's three main arguments in holding that the I v. I exclusion barred coverage for the securities class action. First, the insured entity claimed that the exclusion did not apply because the former director who initiated the securities litigation was not a "duly" elected or appointed director and thus did not fall within the scope of coverage under the policy as a "director." The insured entity argued that the former director was not "duly" elected because he had only held a position for a short period of time before the insured entity discovered that he was subject to a covenant not to compete and had misrepresented his experience. The

court of appeals upheld the district court's reliance on the dictionary definition of "duly" and its reasoning that a director is "duly" appointed if he is appointed "through regular and proper channels of corporate governance," commenting that "[t]he district court's reasoning is spot on." The court of appeals ultimately concluded that "the plain meaning of 'duly' clearly indicates that [the former director] was a 'duly' elected officer and director because it is undisputed that the procedures by which he was elected were conducted in a due manner, time, and degree."

The court of appeals also upheld that district court's rejection of the insured entity's argument that the insurer must prove collusion between the underlying parties to invoke the I v. I exclusion. In so holding, the court of appeals opined that a split of authority exists in other courts as to whether the I v. I exclusion is limited in applicability to collusive suits but concluded that, "while there is a conflict, it's fought outside Florida" because Florida's plain meaning jurisprudence does not permit a court to "look behind unambiguous policies in search of countervailing rationales." The court determined that the I v. I exclusion in the policy at issue was unambiguous and concluded that "because the D&O policy's language is unambiguous, we apply it as written." Therefore, no showing of collusion was needed.

Finally, the court of appeals rejected the insured entity's argument that the I v. I exclusion should only apply to preclude coverage for that part of the underlying action directly attributable to the former director. The insured entity attempted to rely on *Level 3 Communications v. Federal Insurance Co.*, 168 F.3d 956 (7th Cir.1999), in support of this argument, noting that the Seventh Circuit in *Level 3 Communications* applied the I v. I exclusion only to those portions of an underlying settlement attributable to the former director. The court of appeals rejected the insured entity's reliance on that decision, reasoning that "the former-director plaintiff in *Level 3 Communications* was merely a passive shareholder who joined a larger suit" whereas the former director in this case "brought the lawsuit and recruited every other plaintiff." The court of appeals also reasoned that the policy language at issue in *Level 3 Communications* only precluded suits "brought or maintained by or on behalf of any Insured" while the policy at issue in the instant case was much broader. The court of appeals concluded that "[w]hile the language in *Level 3 Communications* gave the court some wiggle room, the language in our case is plain and clear, compelling our conclusion that [the insurer] need not cover [the insured entity] for [the former director's] lawsuit."

For more information, please contact us at 202.719.7130.