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Delaware Superior Court Ruling Should Prompt Review of D&O Coverage by Investors Involved in Company Management

Directors and officers (D&O) liability insurance generally protects directors and officers against legal expenses and personal liability for acts and omissions taken in their capacity as directors and officers of the insured company. In *Goggin v. National Union Fire Insurance Company of Pittsburgh, PA* (November 30, 2018), the Delaware Superior Court held that a D&O insurance contract at issue excluded coverage where claims against directors arose out of acts in their capacities as both directors of and investors in the company.

The case involved two directors of U.S. Coal Corporation who were also investors in the company. The underlying claims related to alleged breaches of fiduciary duties that were asserted by the trustee in U.S. Coal's bankruptcy proceeding. During the relevant period, U.S. Coal maintained D&O coverage under a policy issued by National Union. Although the D&O policy covered liabilities and expenses arising out of acts and omissions by the investor-directors, National Union ultimately denied coverage to the directors on the basis that the alleged fiduciary duty claims did not "arise out of" alleged wrongdoing *solely* in the directors' capacity as U.S. Coal directors. The court agreed and held that National Union properly applied the insurance contract's "capacity" exclusion for claims arising out of "any actual or alleged act or omission of an Individual Insured serving in any capacity, other than as [a director or officer] of a Company". The decision applied a "but for" test in assessing the applicability of the capacity exclusion. If the claim would not have existed "but for" the directors' conduct as investors, the claim is not based on the director's conduct *solely* as a director of the insured entity and the "capacity" exclusion applies to deny coverage. Of course, the opposite would also be true. In applying the court's pesky "but for" or "sole capacity" analysis, no fiduciary duty claim could have been asserted against the investors in U.S. Coal who did not also have fiduciary duties as directors.

The decision rests substantially on the facts underlying the alleged breaches of fiduciary duty and the specific language of the insurance policy at issue. However, taken as a whole, it should be a warning to investors who are also involved in management of a portfolio company that a careful review of D&O policies by experienced advisers is important to understanding whether such investors will be protected against the claims they anticipate and to assisting portfolio companies negotiate exceptions to exclusionary language in policies that would deny anticipated coverage. Such a review is especially important for investor-directors who provide troubled company financing or who act in multiple other capacities with an insured company (e.g., member-manager, management consultant, lender, financial adviser, restructuring manager, etc.).

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