Insurance Coverage For COVID-19 Claims Under D&O Policies

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To date, much of the insurance industry's focus on the Coronavirus (COVID-19) pandemic has been on business interruption coverage under commercial property insurance policies. There have been numerous lawsuits filed alleging that COVID-19 and/or other attendant circumstances trigger the insuring agreements of these policies. That question, whether COVID-19 constitutes a "direct physical loss of or damage to property," as property policies generally require, will likely be the single most litigated issue in connection with COVID-19 claims in the foreseeable future. This makes sense given the immediate and far-reaching economic implications faced by the industry.

In the long-term, however, carriers should expect a myriad of claims under personal, commercial, and professional lines. Of the professional lines likely to be affected, and for which lawsuits have already been filed under, are directors & officers liability policies (D&O). D&O coverage typically provides defense and liability costs to directors and officers of organizations for claims made against them while acting in their official capacity. While no two policies are the same, a typical D&O policy may cover three types of losses, referred to as Sides A, B, and C. Side A covers a director's or officer's direct losses, *i.e.*, those not indemnified by the organization. Side B covers losses relating to claims made against the directors and officers for which the organization has indemnified them, *i.e.*, the organization gets reimbursed when it indemnifies its directors or officers or advances legal costs on their behalf. Side C covers losses incurred based on claims against the organization itself (often referred to as "entity" coverage). D&O coverage is nearly always written on a claims-made basis.

As businesses and the economy continue to reopen and employees go back to work in shared spaces, there could be a surge of claims alleging directors and officers (or any management-level employee) engaged in "wrongful acts" that exposed individuals to COVID-19. An increase of claims and lawsuits alleging that companies and their officers and directors contributed to drop in stock price or other negative financial consequences related to COVID-19 should also be expected. In all of these instances, the specific language of a D&O policy should be examined in conjunction with the applicable state's law in considering whether such claims are within the scope of coverage. After that, the next step is to examine policy exclusions. This article provides an overview of both, as well as a sampling of current issues in litigation.

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Is the Lawsuit Within the Scope of Coverage?

A typical D&O policy's insuring agreement covers "insured persons" for "loss" which they are legally obligated to pay resulting from a "claim" first made during the policy period (or any extended reporting period, which this article does not discuss) for a "wrongful act." Some policies also specifically include insuring agreement provisions for indemnification (Side B), and coverage for the organization (Side C).

The term "insured persons" may include: (1) directors and officers; (2) natural persons who were, now are, or shall become members of a management or advisory committee of the organization; and (3) natural persons who were, now are, or shall become employees of the organization.

"Loss" may be defined to mean defense costs, but it may also be defined more broadly to include the total amount of monetary damages which the insured becomes legally obligated to pay on account of a "claim" for a "wrongful act." The definition may include or specifically exclude punitive or exemplary damages, and the definition often may not include taxes, criminal or civil penalties imposed by law, restitution, or disgorgement. *See, e.g., Level 3 Communications, Inc. v. Fed. Ins. Co.*, 272 F.3d 908, 910 (7th Cir. 2001) (applying Illinois law) (finding that "loss" does not include ill-gotten gain); *Pan Pac. Retail Properties, Inc. v. Gulf Ins. Co.*, 471 F.3d 961, 971 (9th Cir. 2006) (applying California law) (recognizing that one cannot insure against the risk of being ordered to return money or property that has been wrongfully acquired).

The manner in which a "wrongful act" is defined also varies by policy. A typical definition follows:

Wrongful act means any actual or alleged error, misstatement, misleading statement, act, omission, neglect or breach of duty committed, attempted or allegedly committed or attempted on or after the Retroactive Date, if any, set forth in the Policy and prior to the end of the **policy period** by:

1. Any of the **insured persons** in the discharge of their duties solely in their capacity as **insured persons** of the **organization**;
2. Any of the **insured persons** of the **organization** in the discharge of their duties solely by reason of their status as such; or
3. The **organization**.

Again, any policy under which a claim is made must be specifically examined because these definitions will vary. Moreover, there will be a host of other issues to unravel with respect to whether a claim or lawsuit meets the insuring agreement of a D&O policy, including, non-exhaustively, considerations concerning reporting periods and whether requested remedies constitute insurable losses.

Do Policy Exclusions Apply?

The following are some examples of exclusions that, depending on specific factual allegations, may be included in a D&O policy and could be raised by insurers as a basis for a denial of coverage.

- **Exclusions for Bodily Injury/Personal Injury and/or Property Damage**

These exclusions generally preclude coverage under a D&O policy with respect to a claim for actual or alleged: (1) "bodily injury" (which usually includes sickness, disease, or death of any person, mental anguish or emotional distress) (*See, e.g., Waller v. Truck Ins. Exch., Inc.*, 900 P.2d 619 (Cal. 1995), *as modified on denial of reh'g* (Oct. 26, 1995)); (2) "property damage" (including, but not limited to, physical injury, loss of or loss of use or currency or any negotiable or non-negotiable instruments or contracts representing money); and/or (3) for the list of enumerated offenses set out in a policy's definition of "personal injury" (or "personal and advertising injury").

Claims for "bodily injury" will likely be the focus here. For a "bodily injury" exclusion to preclude coverage, there must be some nexus between the injury and the alleged "wrongful act." *See, e.g., Philadelphia Indem. Ins. Co. v. Maryland Yacht Club, Inc.*, 742 A.2d 79 (Md. Spec. App. 1999) (refusing to apply exclusion for "bodily injury" because nexus between the alleged wrongful termination and the injury was too attenuated); *Fireman's Fund Ins. Co. v. U. of Georgia Athletic Ass'n, Inc.*, 654 S.E.2d 207, 213–14 (Ga. App. 2007) (holding that for the "bodily injury" exclusion to bar coverage, the nexus between the claimant's bodily injury and the claims against the insured cannot be too attenuated; thus, where no conduct by the insured is related to the claimant's bodily injury, the "bodily injury" exclusion does not preclude coverage).

- **Pollution Exclusions**

There is a limited amount of case law interpreting pollution exclusions in the context of D&O coverage. Nonetheless, depending on the facts and the language of a particular policy, these exclusions could form the basis for denials under D&O policies for claims made in connection with COVID-19. *See High Voltage Engr. Corp. v. Fed. Ins. Co.*, 981 F.2d 596, 601-02 (1st Cir. 1992) (Massachusetts law) (ruling that a pollution exclusion in an executive liability and indemnity policy barred coverage for claims of unfair and deceptive trade practices made against directors of an insured company stemming from the alleged disposal of hazardous waste because the court determined that the directors' "wrongful acts" were related to the disposal of hazardous wastes); *see also Natl. Union Fire Ins. Co. of Pittsburgh, PA v. U.S. Liquids, Inc.*, 88 Fed. Appx. 725 (5th Cir. 2004) (unpublished) (applying Texas law, holding that securities fraud suit and related derivative action against insured waste management company and its executives alleging losses from nondisclosure of improper waste disposal practices fell within broad pollution exclusion in directors, officers, and corporate liability

policy applicable to any loss "arising out of" actual discharge of pollutants "including … damage to the [insured] or its [shareholders]."); cf. *Sealed Air Corp. v. Royal Indem. Co.*, 961 A.2d 1195 (N.J. Super. App. Div. 2008) (holding that securities fraud claims against insureds, to recover for false and misleading representations and omissions pertaining to evaluation of contingent pollution liabilities remaining with a subsidiary to be spun off, were not based on and did not arise out of or involve the actual, alleged, or threatened discharge, release, escape, seepage, migration, or disposal of pollutants; thus, pollution exclusion of D&O policy did not apply because the complaint was rooted in securities fraud and misrepresentation, not pollution from asbestos, and the pollution was too attenuated from the damages sought). Again, a particular state's law and precedent construing pollution exclusions should influence application of these exclusionary provisions.

- **Conduct Exclusions**

A conduct exclusion precludes coverage for claims against an insured based upon, attributable to, or arising in fact out of any dishonest, malicious, fraudulent or deliberately criminal act or any willful violation of any statute or regulation. Some conduct exclusions require that the violation be established by a final, non-appealable adjudication. *See, e.g., Imperato v. Navigators Ins. Co.*, 777 Fed. Appx. 341 (11th Cir. 2019) (fraudulent acts exclusion). A key assessment will be whether the insured is alleged to have engaged in intentional or negligent conduct. *See, e. g., Horace Mann Ins. Co. v. Tennessee Mun. League*, 1994 WL 108921 (Tenn. Ct. App. 1994).

- **Insured vs. Insured Exclusions**

These exclusions are standard in D&O policies and they are designed to bar coverage for claims between insureds since D&O policies are intended to provide coverage for third-party claims. *See Level 3 Communications, Inc. v. Fed. Ins. Co.*, 168 F.3d 956, 957 (7th Cir. 1999) (Nebraska law); *Miller v. St. Paul Mercury Ins. Co.*, 683 F.3d 871, 874 (7th Cir. 2012), *order clarified* (Aug. 3, 2012), *judgment entered*, 10-3839, 2012 WL 12930871 (7th Cir. June 29, 2012) (Illinois law) (finding these exclusions "control the cost of D&O insurance by removing from coverage both 'collusive suits—such as suits in which a corporation sues its officers or directors in an effort to recoup the consequences of their business mistakes, thus turning liability insurance into business-loss insurance'—as well as 'suits arising out of those particularly bitter disputes that erupt when members of a corporate, as of a personal, family have a falling out and fall to quarreling.'").

Particular attention should be focused on any exceptions to these exclusions, which may add coverage back for certain claims. *See, e.g., Intelligent Digital Systems, LLC v. Beazley Ins. Co., Inc.*, 906 F. Supp. 2d 80 (E.D. N.Y. 2012) (under New York law, recognizing, but not applying, an "employment-related" exception); *Julio & Sons Co. v. Travelers Cas. & Sur. Co. of Am.*, 684 F. Supp. 2d 330 (S.D.N.Y. 2010) (under Texas law, recognizing, but not applying, exception for shareholder

derivative actions); *Link Snacks, Inc. v. Fed. Ins. Co.*, 664 F. Supp. 2d 944 (W.D. Wis. 2009) (applying Wisconsin law) (wrongful termination exception).

- **Exclusions for Violations of Securities Laws**

Public companies could be subject to claims by investors asking whether steps could have been taken to avoid economic losses in value due to COVID-19. Additionally, directors and officers may be exposed to derivative suits alleging a failure to properly manage the effects of the COVID-19 pandemic on revenues and profits. Whether or not these exclusions ultimately apply depends on the allegations of a lawsuit and language of the exclusion because these exclusions generally are not limited to a specific category of securities transactions and bar coverage not only for claims based on actual violations of the enumerated federal and state securities laws, but also claims based on alleged violations of those laws. *See In re SRC Holding Corp.*, 545 F.3d 661 (8th Cir. 2008) (under Minnesota law, holding that exclusion under D&O policy issued to securities underwriter and broker providing policy would not cover "any Claim based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged violation" of federal or state securities laws or regulations, was not by its plain terms limited solely to claims based on, arising out of or in any way involving violations occurring in connection with sale of corporate underwriter/broker's own stock, but prevented underwriter/broker from asserting claim under policy for indemnity or defense of investors' claims against it for alleged violation of securities laws in connection with its underwriting and sale of bonds of unrelated entity).

- **Antitrust Exclusions**

D&O policies may further include antitrust exclusions, which preclude coverage for any loss (including attorney's fees) incurred in connection with antitrust claims. These exclusions may broadly preclude coverage under other types of competition laws, including, for example, trade restraint, unfair competition, and unfair trade practices laws. *See, infra, McQueen and Ballinger et al. v. Amazon.com, Inc.*, N.D. Cal., No. 4:20-cv-02782, complaint 4/21/20.

- **Miscellaneous Other Exclusions**

Certain other exclusions in D&O policies could come into play with respect to COVID-19, including, among others, exclusions for breach of contract, prior acts, personal profit or gain, and trade secret misappropriation. As noted above, application of these exclusionary provisions will generally depend on the specific policy language and facts alleged on case-by-case basis. Carriers should also expect cyber-related claims to be at issue, and coverage extensions or stand-alone cyber policies with D&O coverage extensions ought to be reviewed in conjunction with any complaints and the applicable state's law.

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A D&O policy will also typically have an "Other Insurance" provision that provides that if other valid and collectible insurance applies (often GL) then the D&O policy is excess and does not defend unless the other policy is exhausted. Litigation involving these provisions could be at issue amongst carriers to determine whether carriers are co-primary, or if one primary policy is actually excess to another.

A Sampling of Current Issues in Litigation

So far, the lawsuits filed by policyholders seeking coverage under D&O policies include actions alleging price-fixing or price-gouging, direct and derivative securities claims arising out of COVID-19 financial reporting obligations, regulatory investigations in connection with SEC reporting and disclosure requirements, and unfair trade practice claims.

For example, a putative class has been filed in the Northern District of California that contends that Amazon has taken advantage of the COVID-19 pandemic by using its high market share and ability to control the prices charged by third parties for whom it delivers products to engage in price gouging. Counts include violation of the California Unfair Competition law, negligence, and unjust enrichment. On its face, there is an argument that the action presents a "claim" for "loss" arising from a "wrongful act." Likely issues include whether the relief in effect constitutes restitution or disgorgement, whether there is fraud or the willful violation of a statute, and whether Amazon gained profit or remuneration to which it was not entitled, and possibly even whether the California statute is an antitrust law. *See McQueen and Ballinger et al. v. Amazon.com, Inc.*, Case No. 4:20-cv-02782 (N.D. Cal.) (filed April 21, 2020).

Another example is an action that was filed against Norwegian Cruise Lines and its CEO. It alleges that he sold stock while knowing that COVID-19 was going to have a severe impact on the cruise line industry and knowing that employees were being instructed to make false representations to prospective customers. Once again, a "claim" for alleged "loss" based upon a "wrongful act" has seemingly been asserted, but there will likely be a number of potential issues including any securities law exclusion, whether the relief sought would be restitution or disgorgement, and issues about deliberate violations of law. *See Douglas v. Norwegian Cruise Lines et al.*, Case No. 1:20-cv-21107 (S.D. Fla.) (filed Mar. 12, 2020).

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Coverage determinations regarding claims related to COVID-19 will be made by courts based on the facts of each claim, the policy at issue, and the applicable state's law. Therefore, in determining whether there is coverage for a particular lawsuit, the policy's definitions of "wrongful act," "loss," "claim," and "insured persons," and the applicability of the policy's exclusions, should be closely analyzed under the applicable state's law in the context of a particular claim or

lawsuit.