

Complaint's Allegations that Directors and Officers Provided Assistance Insufficient to Support Motion for Summary Judgment on Insured V. Insured Exclusion

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The United States District Court for the Northern District of Illinois has held that allegations in a shareholder derivative complaint that the plaintiffs obtained information from past and present directors and officers of the company are insufficient to support a motion for summary judgment on the insured v. insured exclusion. *Welch v. Agricultural Excess & Surplus Ins. Co.*, No. 00-C-5725, 2001 U.S. Dist. LEXIS 15608 (N.D. Ill. Sept. 28, 2001). The court also analogized the duty to advance defense costs to the duty to defend, but held that the insureds were not entitled to summary judgment on the advancement of defense costs because they failed to establish that they had executed the requisite written promise to reimburse the insurer in the event there was no coverage.

The insureds in this action were directors and officers of a company created through a merger in March 1999. The principals of a predecessor entity became the directors and officers of the new company. Thereafter, in May 1999, the newly formed company procured directors and officers liability insurance. The policy issued contained an insured v. insured exclusion that barred coverage for "any Claim made against the Directors or Officers . . . by any security holder of the Company whether directly or derivatively unless such securities holder bringing such Claim is acting totally independent of, and totally without the solicitation of or assistance of, or participation of, or intervention of, any Director or Officer, or the Company, or any affiliate of the Company." The policy also provided for the advancement of defense costs upon the condition that the insureds sign a written undertaking, promising to repay any costs advanced if the insurer is not liable under the policy.

In September 1999, shareholders of the insured company brought a derivative action against the company and its directors and officers. The complaint contained specific allegations describing misrepresentations by the directors and officers prior to the creation of the insured company and misconduct that occurred after the insured company came into existence. Moreover, the plaintiffs specifically alleged that the information contained in the complaint came from discussions with and information provided by past and present directors and officers. The insurer denied coverage for the claim, and the insureds brought this action. Both

parties moved for summary judgment.

The court denied without prejudice the insurer's motion for summary judgment on the insured v. insured exclusion. Because the only evidence regarding the assistance of the directors and officers was the unsupported allegations in the underlying complaint, the court found that the insurer had not presented undisputed evidence in support of its motion. It indicated that the insurer would be required to present affidavits, deposition testimony or other competent evidence in order to prevail.

The insurer also argued that the gravamen of the underlying litigation was conduct that predated the existence of the company, so the asserted wrongful acts did not occur in the directors' and officers' insured capacity. It also maintained that, because the policy did not contain a duty to defend, the court was not required to read the complaint broadly in favor of coverage. The insureds countered that the complaint contained generalized allegations of wrongdoing in an insured capacity, so the insurer was obligated to advance defense costs.

The court found that while duty to defend cases were not directly controlling, "they appear to be instructive in interpreting the obligation to advance costs of litigation." It emphasized two ways in which the duty to advance was broader than the duty to indemnify. First, the insureds could be required to repay amounts advanced if there was no coverage. Thus, the court reasoned, the policy contemplated the advancement of fees for which the insurer might not have ultimate liability. Second, the "very nature" of the advancement obligation "accepts the contingency that liability may or may not be found." In light of these considerations and the requirement of construing ambiguity against the insurer, the court concluded that the "duty of defense cases appear applicable." As a result, because some of the complaint's allegations could encompass conduct in the insured's insured capacity, it rejected the insurer's arguments. The opinion does not address whether the policy contained allocation provisions.

The insureds did not secure summary judgment, however, because they failed to establish that they had executed the written undertakings required by the policy as a condition to advancement of defense costs.