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D&O Insurance Tips For Coronavirus-Related Claims

By **Catherine Doyle and Jan Larson** (April 6, 2020, 12:48 PM EDT)

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The unprecedented impact of the COVID-19 crisis continues to send shockwaves throughout the business community. While governments and health organizations react in real time to the spread of the virus under ever-changing conditions, company executives also face difficult decisions in how to respond responsibly to these novel challenges.

Among other business decisions in a time of extreme volatility, corporate directors and officers must balance the health of the company — its stock price and bottom line — and the health and safety of its employees and customers. With securities markets on a continuous roller coaster over fears of the virus and resulting economic shutdowns, the spotlight may soon shine on whether the directors and officers in charge communicated accurately about and responded appropriately to the crisis.

Shareholder complaints against public companies seeking damages for lost stock value already have been filed alleging that company directors and officers made misleading public disclosures. As such claims continue to propagate, companies will soon look to directors and officers liability insurance to cover defense costs incurred and any later potential liability. Whether D&O liability insurance may prove a source of relief for these types of claims will depend upon the specific language and exclusions in each policy, which policyholders should carefully review.

Economic analysts agree that the impact of COVID-19 on the economy is likely to be catastrophic, at least in the near term. Weekly unemployment claims and stock market drops have already reached record levels. Projections by commentators and government spokespersons alike continue to shift and contribute to economic unease as the full extent of the crisis is continually evolving and not yet known.

Other factors impacting the economic climate include government actions at the federal and state level such as shelter-in-place and quarantine orders, job layoffs and losses from business shutdowns, global supply chain disruptions, ongoing and evolving efforts to protect the health of employees and customers, and reduced capacity as remaining employees experience illnesses or turn to caretaking responsibilities outside of work. Meanwhile, the U.S. Securities and Exchange Commission has issued guidance to public companies to make disclosures regarding the impact of COVID-19.

This minefield of business risks, combined with the need to communicate to the public about the changing risk vectors, leaves corporate executives charged with navigating required responses and disclosures vulnerable to claims of mismanagement and misrepresentation. While companies scramble to implement COVID-19 response plans and to notify their shareholders and consumers about their state of preparedness and responses to the pandemic, these decisions and communications are fraught with risk.

The overall market volatility, combined with scrutiny over what these communications say, or do not say, opens the door to litigation claiming that public disclosures either did not adequately inform investors of risks or affirmatively made misrepresentations that influenced the price of the company's stock. Company executives are likely to turn to their D&O liability insurers as a safeguard against the anticipated influx of claims.

Company executives have already been identified as named defendants in at least two recent putative shareholder class actions.

Douglas v. Norwegian Cruise Lines, filed in the U.S. District Court for the Southern District of Florida, named as individual defendants Norwegian Cruise Lines' director, president and CEO, as well as the executive vice president and chief financial officer. Among other allegations regarding sales tactics and misleading safety assurances made directly to customers, the complaint pointed to statements in Norwegian's 10-K filing — which had been signed by the individual defendants — attesting to Norwegian's safety practices and preparedness for health incidents such as COVID-19.

McDermid v. Inovio Pharmaceuticals Inc., filed in the U.S. District Court for the Eastern District of Pennsylvania, likewise named the company's CEO as a defendant. Whereas the Norwegian allegations amount to a failure to adequately disclose risks, the Inovio claims include alleged affirmative attempts to use the pandemic as an opportunity to artificially inflate the price of the company's stock.

According to the complaint, the individually named defendant CEO stated on Fox Business News that the company had developed a COVID-19 vaccine that it would begin testing in the U.S. within months. The company's stock price temporarily soared and then rapidly declined upon further investigation into the purported vaccine's readiness.

As the progression of COVID-19 and its resulting economic impact are still in flux, other public companies filing periodic SEC reports and making public disclosures in the middle of this evolving landscape may be targeted in the near future with lawsuits similar to those already filed.

D&O liability insurance typically protects individual corporate executives from alleged or actual wrongful acts of themselves and the insured company. Typical claims that may be covered by D&O liability insurance include alleged breach of fiduciary duty (including as the subject of a shareholder derivative action), alleged failure to comply with securities laws, and alleged mismanagement, misrepresentation and otherwise negligent performance related to a variety of corporate duties. In many ways, the perils brought by the COVID-19 crisis fall squarely within the purpose of D&O liability insurance.

With that said, like all lines of insurance, D&O liability insurance policies are subject to various exclusions that may foreclose coverage, and each policy is unique in the exclusions it includes and the precise wording thereof. It will be important for corporate policyholders to identify any exclusions that specifically reference viruses, as well as to review more general exclusions and other limitations that an insurer might try to rely on to avoid coverage for COVID-19-related claims.

One starting place is to determine whether the company's D&O liability insurance policy includes a pollution exclusion. These types of exclusions, where included in a D&O liability policy, typically seek to exclude coverage for claims related to the alleged or actual discharge, dispersal, release, escape, seepage, migration or disposal of pollutants, along with requests or requirements related to testing, monitoring, containment, clean up or removal of pollutants.

The term "pollutants" is usually subject to a specific definition, the scope of which should be evaluated. The definition of "pollutants" may in some instances explicitly mention viruses or other communicable diseases, while in other instances utilized generalized terms like irritants or contaminants with some combination of descriptors such as solid, liquid, gaseous, biological and thermal. In the context of D&O liability policies, many pollution exclusions are also subject to explicit carveouts for securities claims.

Another common exclusion found in D&O liability insurance policies is the insured-versus-insured exclusion (or narrowed to an entity-versus-insured exclusion) — designed in large part to prevent the transfer of risk of certain internal business disputes, for example where one director sues another or where the company sues a director, from the company to the insurer.

In a shareholder derivative action, the shareholder plaintiffs essentially stand in the shoes of the company to sue its directors and officers for their alleged breach of fiduciary duty. In most D&O liability policies, the insured-versus-insured exclusion is often amended by various exceptions, or narrowed to an entity-versus-insured exclusion, that will permit coverage in specific situations, and accordingly, should be the subject of special review.

D&O liability insurance policies also usually contain wrongful-conduct exclusions and unentitled-profit-or-advantage exclusions. The former may exclude coverage for acts that involve fraudulent conduct, criminal conduct and other willful or intentional wrongdoing, while the latter may exclude coverage for acts that constitute the gaining of financial profit or other advantage to which there is no legal entitlement.

Careful review of the language of these exclusions is warranted, as some may contain beneficial provisions requiring that the conduct or acts be established by way of a final adjudication in an underlying action before the insurer may rely upon the conduct or acts as a basis to assert the exclusion as a bar to coverage.

As COVID-19-related claims are likely to intersect multiple types of insurance, including but perhaps not limited to, commercial property coverage (including business interruption coverage), commercial general liability coverage, and worker's compensation coverage, corporate policyholders should also include review of any exclusions in a D&O liability insurance policy that might otherwise be covered under these other types of insurance.

For example, D&O liability policies often exclude coverage for claims for bodily injury and property damage that would ordinarily be covered under a commercial general liability insurance policy. These bodily injury and property damage exclusions, however, vary in their scope and breadth and are sometimes subject to explicit carveouts for securities claims.

In addition to the types of exclusions noted here, corporate policyholders should also consider whether their D&O liability insurance policy contains other relevant potential limitations, including those with regard to claims for disgorgement or restitution. In some instances, a D&O liability policy will explicitly address whether such claims are covered or excluded as part of the definition of the term "loss."

The existence of coverage for these types of claims may also be jurisdiction-specific, to the extent there is a policy limitation for matters deemed uninsurable as a matter of law. The question of whether an alleged disgorgement or restitution has been established may also turn on the presence or absence of admissions or judicial findings made to date in a particular matter.

We urge all corporate policyholders that may be subject to COVID-19 claims as a result of corporate statements, disclosures and responses in connection with this crisis to review their D&O liability insurance policies and evaluate available potential coverage, paying particular attention to policy exclusions and other limitations and coordinating with experienced coverage counsel as needed.

In addition, when negotiating renewals or obtaining new insurance coverage across all types of insurance, including D&O liability insurance, we suggest that corporate policyholders keep abreast of efforts by the insurance industry to add new policy exclusions and other limitations in response to COVID-19.

Going forward, corporate policyholders should also anticipate that the D&O liability insurance market, in addition to other insurance markets, may react to this pandemic by shifting their underwriting focus to add the evaluation of risks presented by COVID-19 and public health epidemics more generally, including scrutiny of supply chain vulnerabilities and the ability to adapt to remote work.

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