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Top 10 steps when faced with a D&O insurance denial letter

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A director or officer being sued or investigated for allegations of mismanagement is facing one of his or her worse nightmares. His reputation is at stake (often fuelled by a stream of adverse news articles in the local press) and, because a director's or officer's liability even for 'corporate decisions' is a personal liability, such a claim can be a financial nightmare as well. The situation is made all the worse when the director receives notification that the D&O insurer may be denying coverage. This article will lay out the top 10 steps for a director to take to put him back in control.

Step 1: Don't panic

If you have been sued or investigated as a director or officer, your company's D&O carrier has sent a coverage analysis letter back to the company's risk manager or general counsel. The carrier has no obligation to send a copy to you even though you are being sued and even though the letter might state that there is no coverage. So, first thing first: get the letter. Second, if the letter is denying or reserving rights on coverage, know this response is not all that

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uncommon. Indeed, in our experience the vast majority of initial responses from your friendly neighborhood D&O claims department is anything but a "don't worry, you're covered, no problem" response. The reason for this lies in the way D&O claims are alleged. The wording of the complaint almost always results in 'potential coverage issues'. Nevertheless, *usually* there is nothing to fear.

Step 2: Understand that not every denial letter is a real denial letter

The most common response from a D&O carrier is a 'reservations of rights' letter. This letter will generally indicate that coverage is initially being provided under your policy but that such coverage may be removed in the future if certain things occur. While this sounds scary, in most instances it is nothing to lose sleep over. The most common 'reservation' arises from the fact that claims against directors and officers almost always include allegations of fraud, intentional conduct or some other form of dishonesty. D&O policies, as well as public policy, preclude coverage for intentional wrongdoing. However, in all modern D&O forms in the market today, the so-called 'fraud' exclusion is subject to a final adjudication against the director that he actually committed the fraud, and even in that instance, the exclusion will not apply to other directors who did not know of the fraud. Form wording can be different from policy to policy (not just in the fraud exclusion but generally) so it is best to consult with an expert on the exact wording of your policy (see Step 5). Then again, you might actually be looking at the wrong insurance policy.

Step 3: Look at your other insurance policies

It is not uncommon for a D&O carrier to either deny coverage or reserve its rights on coverage because there might be another insurance policy that should be the policy to cover the claim. The most common example of this is when there is a series of 'related' D&O claims, the first of which was initiated before the inception of the D&O policy in question. A D&O policy has a number of 'related back' provisions that, in essence, say that all 'related' claims are deemed to be one claim that was 'first made' at the time of the first claim in the series. Fortunately, the D&O policy in existence at the time of the first claim in the series usually has a 'related forward' provision that would, in essence, say it will cover all the claims in the series even ones that were initiated against the director after the policy expired. Other common clauses pointing the finger at other insurance policies include: bodily injury/property damage (go to General Liability policy), pollution (go to environmental policy), ERISA (go to Fiduciary Liability policy) and, a bit more problematic, the general 'Other Insurance' clause. Of course, at this point, it might be a good idea to actually read the policy.

Step 4: Read the policy

An insurance policy is, after all, a contract. And like all contracts it has terms and conditions which might benefit one party or the other. The job of an underwriter is to determine the right mixture of terms, conditions and premium that provides a benefit to the buyer and at the same time safeguard the interests of the carrier. While we always recommend reading the insurance policy *before* there is a claim, if this hasn't occurred, it is a good idea to do so now. This also might be a good time to read the company's by-laws on director indemnification and obtain a commitment from the general counsel that your legal fees, settlements and adverse judgments will be paid by the company, especially in the event the D&O insurer doesn't pick up the tab. Of course, like all contracts, insurance

policies can be technical and D&O policies more so because they are designed for corporate buyers who have access to expertise.

Step 5: Talk with an independent industry expert that you hire

If you have followed steps 1-4, you may already have an opinion as to whether you have a real problem or not. However, either way, it is best to personally retain an insurance expert to review your situation. He may confirm your conclusions or point out things you did not see. In the event that the denial or reservations letter is a 'real' denial (see Step 2), he can assist you in managing the situation. Preferably the individual should be someone with a D&O insurance *carrier* background, whether in underwriting or claims. Remember, your company's fundamental obligation is to its own interests rather than yours, so don't be afraid to hire your own expert.

Step 6: Talk to the coverage lawyer

Upon receipt of a D&O claim denial or reservations letter, the company will retain outside counsel to review and, if necessary, negotiate with the insurance carrier over coverage. Even though hired by the company, you have a right to speak to the individual since *you* are the one being sued. If the situation becomes serious, you should contemplate hiring your own coverage counsel.

Step 7: Talk to the insurance broker

Because D&O is a specialised field in insurance, the major insurance brokerage firms assign individuals who *only* do this type of insurance. Many times these individuals have *decades* of experience in D&O brokerage and claims. The major brokerage firms also have a 'policyholder advocacy' department whose sole job is to help out in claims (at no cost).

Step 8: Talk to the underwriter (not just the claims department)

It is disturbing how often this step is ignored. The underwriter is the person you made the deal with. Presumably, they have an understanding of their *intent*, perhaps regardless of the 'plain meaning' of the words in the policy. Don't be afraid to get them involved right from the beginning and if the individual underwriter your broker dealt with does not seem interested in helping, go up the ladder until you find someone who is. (If you never find anyone, this is a good reason to move coverage.)

Step 9: Look at what other business you have with the carrier

A D&O claim negotiation should not be isolated from the rest of the relationship. What other business do you or your company have with the carrier? How long is the relationship? How much total premium? What is your company's personal 'loss ratio'? Even business with the carrier *outside insurance policies* can play a role.

Step 10: Negotiate the 'win-win' solution

Often a challenging claims scenario can be resolved by looking at the bigger picture or by moving other pieces around the chessboard. At the end of the day, most carriers just want to make sure they will *eventually* get their money back through future premiums and/or other business. Understand the goals of the insurance carrier and they are more apt to understand your goals. ■