Wiley Rein & Fielding

January 2004

The Executive Summary

Developments Affecting Professional Liability Insurers

Court Refuses to Apply I v. I Exclusion Where Officers Who Provided Information to Plaintiffs Did Not Do So to Obtain an "Economic Benefit"

The United States District Court for the Northern District of California, applying California law, has held that a D&O insurer could not deny coverage based on the I v. I exclusion even though two officers of the company had provided information to the underlying plaintiffs because the officers had not sought to obtain an "economic benefit" by providing the information. *Harris, et al. v. Gulf Ins. Co.*, 2003 WL 23110387 (N.D. Cal. Dec. 15, 2003).

The insurer issued a D&O policy that provided coverage for claims made against directors and officers for "Wrongful Acts." The policy defined "Wrongful Act" as "any error, misstatement, misleading statement, act, omission, neglect, or breach of duty committed or attempted, or allegedly committed or attempted, by one or more Directors or Officers, individually or collectively, in their respective capacities as such." The policy also contained an I v. I exclusion barring coverage for actions "brought or maintained by or on behalf of…any security holder of the Insured Company whether directly or derivatively except…a Claim that is brought and maintained by security holders who are acting totally independently of, and totally without the solicitation, assistance, participation, or intervention of any Director or Officer of the Insured Company."

The company and a number of its directors and officers were named as defendants in class action securities lawsuits. After the insurer discovered from reviewing the consolidated amended complaint that two officers of the company, who were not named in the securities lawsuit, had provided information to the plaintiffs in the underlying action, it stopped advancing defense expenses based on the I v. I exclusion. Two individual defendants in the securities litigation then filed a declaratory judgment action challenging the applicability of the I v. I exclusion.

The court held that the I v. I exclusion did not apply in these circumstances. Relying on *MacKinnon v. Truck Insurance Co.*, 31 Cal. 4th 635 (2003), the court opined that "insurance coverage is interpreted broadly so as to afford the greatest possible protection to the insured, whereas exclusionary clauses are interpreted narrowly against the insurer." The court pointed to the definition of "Wrongful Act" and reasoned that "[t]his coverage language is quite broad, establishing a

continued on page 9

Also in This Issue

E&O Policies Cover School Board-Policyholder in Sexual Abuse Case

In an unreported decision, a New York appellate court has determined that E&O policies issued to a school board provide coverage for allegations of negligent hiring and supervision of an employee who engaged in intentional sexual abuse even though the policies did not afford coverage for intentional sexual abuse. *ACE Fire Underwriters Ins. Co. v. Orange-Ulster Bd. of Coop. Educ. Servs.*, 2003 WL 22810333 (N.Y. App. Div. Nov. 24, 2003).

Two insurers issued E&O policies to a county school board. A third-party claimant sued the school board alleging claims of negligent hiring and supervision arising out of the sexual abuse of a student. The insurers sought to deny coverage on the grounds that intentional sexual abuse was not covered under the policies.

The appellate court, relying on the prior decision of the New York Court of Appeals in *Watkins Glen Central School District v. National Union Fire Insurance Co.*, 286 A.D.2d 48 (N.Y. 2001), held that coverage was available. The court first noted that E&O policies are designed to provide coverage for liability arising out of a policyholder's negligent actions "inherent in the practice of that particular profession or business." The court then stated, without explanation, that the allegations of negligent hiring and supervision fell "squarely within the errors and omissions policies issued," and therefore, the policies afforded coverage to the school board. ✦

Prior Notice Exclusion Bars Coverage Where Notice of Claim Given under Prior Policy

In an unreported decision, a federal district court in Texas, applying Texas law, has determined that a policyholder was not entitled to coverage under a claims-made replacement D&O policy because it provided notice of the same claim under the prior D&O policy. *United Investors Realty Trust v. Hartford Spec. Co.*, No. 3:01-CV-2083-N (N.D. Tex. Sept. 12, 2003).

The first insurer issued a D&O policy to a real estate investment trust. Six months into the policy period, a second insurer acquired the first insurer's assets, including the right to reissue policies. On July 15, 2000, by agreement of the trust, the second insurer issued a replacement D&O policy. The replacement policy contained a prior notice exclusion that barred coverage for "any Claim, Wrongful Act, or circumstance if notice is given under any directors and officers liability…policy, the term of which incepted prior to the Inception Date of this Policy."

On June 22, 2000, prior to issuance of the replacement policy, a third-party claimant sent a letter to the trust alleging that the directors and officers of the trust breached their fiduciary duties. The trust forwarded the letter to the first insurer, which acknowledged the letter and accepted the defense of the underlying action. The first insurer subsequently was placed into court-ordered rehabilitation, which affected its ability to satisfy its defense obligations. The policyholder then tendered the claim to the second insurer. Coverage litigation ensued.

Examining the application of the prior notice exclusion, the court noted that the first insurer's policy clearly incepted before the second insurer's policy. The court explained that whether notice was tendered to the first insurer depended on the meaning of the term "under" in the exclusion. Using the plain and ordinary meaning of "under" in this specific context, the court stated that "under" means "in accordance with." The court, therefore, concluded that the trust's June 22, 2000 letter constituted notice "in accordance with" the first insurer's policy. In so holding, the court rejected the trust's argument that for notice to be given "under" a policy, it must be given in a manner capable of "effecting" coverage. The court reasoned that the trust's approach "does too much violence to the words of the policy" because it would "dramatically rewrite the notice provision into a prior coverage position." Accordingly, the court held that coverage was barred by the prior notice exclusion in the second insurer's policy. ✦

For more information, please contact us at 202.719.7130

Selling Viatical Agreements Does Not Constitute the "Business of Insurance" under Insurance Agency's E&O Policy

A Texas appellate court has held that a professional liability policy issued to an insurance agency did not provide coverage for litigation based on the sale of viatical agreements because the litigation did not arise out of the "business of insurance." *Employers Reinsurance Corp. v. Threkeld & Co. Ins. Agency*, 2003 WL 22724617 (Tex. App. Nov. 19, 2003).

An insurance company issued a professional liability policy to an insurance agency that provided coverage for "any negligent act, error or omission…arising out of the conduct of the business of the Insured in rendering services for others as a general insurance agent, insurance agent or insurance broker…." The agency was sued by investors in viatical agreements that it marketed. A viatical agreement is an arrangement whereby a person, usually terminally ill, is immediately paid a sum less than the expected death benefit of his or her life insurance in exchange for transferring his or her rights to the policy benefits upon death. The underlying plaintiffs alleged that the agency acted fraudulently and negligently by marketing agreements that turned out to be worthless because the underlying life insurance policies were cancelled on the grounds that they were fraudulently obtained. Coverage litigation followed.

The appeals court held that coverage was not available because "a viatical settlement is not an insurance policy, and the business of selling fractional interests in insurance policies is no part of the 'business of insurance.'"

The appeals court held that coverage was not available because "a viatical settlement is not an insurance policy, and the business of selling fractional interests in insurance policies is no part of the 'business of insurance.'" The court reasoned, among other things, that the agency did not "receive and collect consideration for insurance" when it paid premiums on behalf of the terminally ill person in facilitating the transfer of the underlying policies to the investors. The court also explained that the agency was not "representing an insurer" when it brokered the transfer of the underlying insurance policies to the investors it solicited. Since the viatical agreements are not part of the "business of insurance," the court held that the insuring agreement unambiguously did not provide coverage. ✦

Arbitration Panel Has Authority to Award Policyholder Amount in Excess of Arbitration Claim

The United States District Court for the Northern District of Illinois, applying federal and Illinois law, has held that an arbitration panel did not exceed its authority when it awarded a policyholder a greater amount than it had requested in its Statement of Claim. *Robertson-Ceco Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pennsylvania*, 2003 WL 22757755 (N.D. Ill. Nov. 19, 2003).

The policyholder company was insured under a D&O policy. After the policyholder's majority shareholder, a second company, sought to purchase the outstanding shares of the policyholder, several shareholder suits were filed against the policyholder. The policyholder settled the lawsuits by agreeing to pay a premium for the shares. It then submitted a claim to the D&O insurer for $4.2 million, which it asserted was the difference between what it paid for the shares and what it would have paid in the absence of litigation. The insurer refused to pay on the ground that the claim was outside the scope of the policy. The policyholder then submitted the claim to arbitration as required in the policy.

In its Statement of Claim filed in the arbitration, the policyholder claimed $4.2 million in damages, but noted that it might have cost as much as $6.75 million (the

continued on page 4

For more information, please contact us at 202.719.7130

Texas Appellate Court Applies "Eight Corners" Rule

A Texas appellate court has held that an insurer was not required to defend a policyholder where the factual allegations in the petition did not come within the scope of coverage of an E&O insurance policy. *Landmark Chevrolet Corp. v. Universal Underwriters Ins. Co.*, 2003 WL 22809055 (Tex. Ct. App. Nov. 26, 2003).

The insurer had issued an E&O policy to two car dealerships. The policy provided that the insurer had a duty to defend the dealerships against, among other things, alleged violations of state or federal "truth-in-lending or truth-in-leasing law[s]." Former customers sued the dealerships, alleging that the dealerships had unlawfully charged a "consumer services fee" in exchange for a "worthless" coupon book. The underlying petitions alleged fraud and violations of the Texas Deceptive Trade Practices Act. The insurer declined to defend the dealerships in the litigation on the ground that the plaintiffs had not alleged violations of truth-in-lending laws. The dealerships then brought a declaratory judgment action.

The appellate court held in favor of the insurer. The "eight corners rule," the court noted, requires the court to "compar[e] the factual allegations in the four corners of the pleadings with the language in the four corners of the insurance policy," while focusing on the origin of the damages, as opposed to the legal theories alleged, and giving "a liberal interpretation" to the allegations. Thus, the insurer's duty to defend only arises if "the factual allegations in the pleadings…when fairly and reasonably construed, state a cause of action potentially covered by the policy." The court then explained that "[e]ven giving the pleadings the required liberal construction, they do not allege facts indicating that the…plaintiffs are seeking damages for a violation of federal or state truth-in-lending or truth-in-leasing law." The court found that the plaintiffs had not alleged that the dealerships were "creditors" or that the cars were purchased on credit, as required under the Federal Truth-in-Lending Act, or that the automobiles were to be paid for in deferred installments, as required under Texas' Motor Vehicle Installment Sales Act. The court also refused to permit the consideration of extrinsic evidence, explaining that the Texas Supreme Court has "never recognized an exception to the 'eight corners rule,'" and that the Court of Appeals itself has "specifically considered, and rejected, such an exception." ✦

Arbitration Panel Has Authority to Award Policyholder Amount in Excess of Arbitration Claim

continued from page 3

difference between the initial tender offer and the amount actually paid per share) to obtain releases from the plaintiff-shareholders. After full arbitration proceedings, the arbitration panel awarded the policyholder $7,446,103.

The insurer then challenged the award under Section 10(d) of the Federal Arbitration Act, which provides for the review and vacation of an arbitration award where "the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made." The insurer argued that the company's Statement of Claim placed "a cap" on the amount the arbitration panel could award.

The district court disagreed with the insurer, holding that "[a]rbitrators are free to fashion any award that is just, equitable, and within the scope of the agreement of the parties…. [I]mposing a cap on an arbitration award based on the initial pleadings runs counter to the rules establishing arbitrator discretion in fashioning a remedy [such as the American Arbitration Association's Commercial Arbitration Rule § R-45]. Such a cap is also counter to practice in the federal courts, where damages may exceed the amount in the initial pleading." As no transcript of the arbitration proceeding existed, the court "assumed" that the award was supported by evidence presented in the hearings.

The district court also found that the panel had not deprived the insurer of the ability to defend itself against a larger, "re-computated" award because such an award had been "put forth as a possibility" at the time when the company described the potential size of its damages in its Statement of Claim. In addition, the court found that the panel had not gone "outside the arbitration agreement to add new categories of damages," but had merely "recalculated the amount for the same claim of damages." The district court also held that the policyholder could maintain its count for "vexatious and unreasonable conduct" based on its allegation that the insurer had refused to pay covered losses without a legitimate basis and had attempted to delay payment "for as long as possible." ✦

For more information, please contact us at 202.719.7130

"Non-Insurance Contracts" and "Securities Broker/Dealer" Exclusions Held Ambiguous as Applied to Viatical Agreements

A federal district court in Georgia, applying Georgia law, has held that "non-insurance contracts" and "securities" exclusions in an E&O policy issued to a life insurance salesman did not unambiguously bar coverage for the sale of a viatical settlement agreement and that, as a result, a jury could consider parol evidence about the exclusions. *Utica Mutual Ins. Co. v. Costa,* 2003 WL 22945649 (M.D. Ga. Dec. 10, 2003).

The insurer issued an E&O policy to a life insurance salesman who sold viatical settlements. The policy issued to the life insurance salesman excluded coverage for "non-insurance contracts," which included "[a]ny investment advice given or alleged to have been given relating to the performance or lack of performance of any investment or resulting from valuations in the value of any investments including, but not limited to…any non-insurance contract." The policy also excluded "[s]ervices" as a "security broker" or "security dealer." Various investors filed suit against the insured for negligence, breach of fiduciary duty and fraud. Coverage litigation followed.

The federal district court found that the exclusions as applied to viatical agreements were ambiguous. The court explained that a reasonable insured could understand that a viatical agreement did not constitute a non-insurance contract because of the "close connection" between viatical investments and life insurance. The court also found that the "securities broker/dealer" exclusion was ambiguous because, at the time, "it was unclear whether viatical settlements were securities under Georgia law." Accordingly, the court allowed parol evidence to show that viatical agreements were covered under the policy. The court emphasized the fact that in the past the insurer had notified the life insurance salesman that certain activities were not covered under the policy, but it had failed to notify him that activities relating to viatical settlement agreements would not be covered. ✦

Intentional Acts Exclusion Bars Coverage for Fraud; Insurer Did Not Waive Exclusion by Omitting from Initial Denial

In an unreported decision, a federal district court in New York, applying New York law, has held that the intentional acts exclusion in a professional liability policy issued to a securities broker/dealer bars coverage for the fraudulent sale of worthless investments. *Westport Resources Invest. Servs., Inc. v. Chubb Custom Ins. Co.*, 2003 WL 22966305 (S.D.N.Y. Dec. 16, 2003). The court also held that the insurer did not waive its right to rely on the exclusion by failing to raise it in its denial of coverage letter.

The insurer issued a claims-made professional liability policy to a securities brokerage firm and its representatives. The policy excluded coverage for intentional acts "brought about or contributed to" by "any knowing, intentional, fraudulent, or dishonest Wrongful Act by an Insured." The exclusion also contained a "safe harbor" provision, which stated that the exclusion "shall only apply to an Insured if it is established in fact that the Insured participated in or acquiesced in the knowing, intentional, fraudulent, or dishonest act, the willful or intentional violation, or the gaining of profit, remuneration or advantage…."

One of the insured's registered representatives convinced some of the firm's clients to invest in an investment vehicle, which was separate from the company's business. The representative was later convicted of fraud because the investments were worthless. The clients then began arbitration proceedings against the brokerage firm arguing that the company negligently supervised the representative.

The insurer denied coverage for the arbitration based on the fact that the representative's scheme was initiated before the retroactive date in the policy. The insurer also reserved on other potentially applicable policy terms, but did not specifically resume on the intentional acts exclusion. Coverage litigation ensued.

The court held that the intentional acts exclusion barred coverage. It rejected the brokerage firm's argument that coverage was available because the claim against it was for negligence, explaining that the intentional acts exclusion applied to fraud by an insured, including the representative,

continued on page 7

For more information, please contact us at 202.719.7130

Insurer Has a Duty to Defend Law Firm in Suits by Two Other Firms Regarding Referral Fee Arrangement

A federal district court in the Southern District of New York, applying New York law, has held that an insurer had a duty to defend a law firm in connection with two suits brought by two other law firms alleging breach of contract, fraud and breach of fiduciary duty concerning referral fee arrangements. *Napoli, Kaiser & Bern, LLP, v. Westport Ins. Co.*, 2003 WL 22953171 (S.D.N.Y. Dec. 15, 2003).

An insurer issued a claims-made professional liability policy to a law firm. The coverage provision stated "[t]he Claim must arise by reason of an act, error, omission or Personal Injury… Coverage shall apply to any such Claims arising out of services rendered or which should have been rendered by any Insured, and arising out of the conduct of the Insured's profession as a lawyer…." The policy contained an exclusion for "any Claim arising out of any dishonest, fraudulent, or malicious acts, errors, omissions, or deliberate misrepresentations."

In November 2001, two law firms filed suit against the policyholder law firm. The plaintiff law firms had referred thousands of diet drug litigation clients to the policyholder law firm, which was already representing numerous clients in the same matter. The policyholder law firm accepted the representation of the referred clients, and in return, agreed to share with the plaintiff law firms a specified percentage of the fees earned for the referred cases. The plaintiff law firms alleged that the policyholder firm obtained higher settlements for its direct clients, and misrepresented settlement terms to obtain approval from referred clients. As a result, the plaintiff law firms argued that they were entitled to higher fees than those received for the referred clients. The two complaints alleged breach of contract, fraud and breach of fiduciary duty to the plaintiff law firms and referred clients. After the insurer determined that it had no duty to defend because the underlying complaints alleged fraud, the policyholder law firm filed suit.

The court held that the insurer had a duty to defend. Although the court recognized that the fraud claims were excluded by the policy, the court concluded that the breach of fiduciary duty claims fell squarely within the four corners of the policy issued. As a result, the court found that a duty to defend existed, noting that if a single claim potentially falls within the coverage of a policy, the insurer has a duty to defend the entire action. In reaching this decision, the court ignored the insurer's arguments concerning the legal merits of the fiduciary duty claims, focusing on the fact that, so long as there was a possibility that the defendant firm faced liability on the claim, the insurer had a duty to defend. Additionally, the court rejected the insurer's argument that the "gravaman" of the underlying complaints was fraud, explaining that a breach of fiduciary duty claim could be based on negligent conduct. The court explained that the underlying complaints did not allege that the breach was intentional, but rather alleged facts that if proven could support a claim for negligence, which the court found is potentially covered under the four corners of the policy.

The court rejected the insurer's argument that the underlying suit was based on a commercial dispute and did not "aris[e] out of the conduct of the insured as an attorney."

The court also rejected the insurer's argument that the underlying suit was based on a commercial dispute and did not "aris[e] out of the conduct of the insured as an attorney." In so holding, the court distinguished the present case from cases involving fee disputes. The court reasoned that the plaintiff law firms' claims stemmed from the policyholder firm's alleged failure to manage its cases in a professional manner, and that the lowered fees were simply a consequence of these actions. The court found that although it was arguable that the claims "arise out of" referral agreements, not unique to the practice of law, the language of the policy on this point was ambiguous, and therefore must be resolved against the insurer.

Finally, the court rejected the insurer's argument that an exclusion for fraud in the policy relieved it of the duty to defend. The court applied the same analysis to the scope of the exclusion issue that it applied to the scope of coverage question, noting that the exclusion did not apply to all conduct alleged in the plaintiffs' complaints. The court therefore held that the insurer had a duty to defend and that the insurer was required to reimburse the defendant firm for legal fees already incurred. It also held that the insurer was entitled to discovery and a trial on whether the amount of fees incurred was reasonable. ✦

For more information, please contact us at 202.719.7130

Insurer Has Duty to Defend Attorney in Suit Alleging Negligent Failure to Obtain Bankruptcy Discharge of Attorney's Pre-Petition Fees

An Illinois appellate court has held that an insurer had a duty to defend an attorney, insured under a legal malpractice policy, in a lawsuit alleging that the attorney negligently failed to obtain discharge of his pre-petition fees in connection with the representation of a client in a bankruptcy proceeding. *Cont'l. Cas. Co. v. Law Offices of Melvin James Kaplan*, 2003 WL 22861281 (Ill. App. Ct. Dec. 3, 2003).

The insurer issued a professional liability policy to an attorney that provided coverage for all sums the attorney "shall become legally obligated to pay as damages and claim expenses because of a claim that is first made…against the [insured] and reported in writing to the [insurer] during the policy period by reason of an act or omission in the performance of legal services…." The policy defined legal services as "those services performed by an insured for others as a lawyer." The policy excluded from the definition of damages "legal fees, costs and expenses paid or incurred or charged by…[the insured]."

A former client of the attorney filed a class action complaint based on the attorney's representation of the client in a chapter 7 bankruptcy proceeding. The client alleged that prior to the filing of a bankruptcy petition on the client's behalf, the attorney required the client to sign a retainer agreement for the payment of fees in installments and that a portion of the fees collected by the attorney was for services rendered prior to the bankruptcy submission, which the client alleged violated the Bankruptcy Code. The client's three count complaint alleged: (1) that the attorney violated the automatic stay provisions of the Bankruptcy Code by collecting fees after the filing of the bankruptcy petition for services rendered pre-petition, (2) that the attorney was negligent in failing to obtain a discharge of his pre-petition fees, and (3) that the client was entitled to an award of actual and punitive damages based on the attorney's violation of the Bankruptcy Code's statutory injunction on the collection of pre-petition debt after discharge.

The appellate court initially noted that the policy in question was a "Lawyer's Professional Liability" policy and, therefore, the risks undertaken by the insurer included "those inherent in the practice of law." The court concluded that the first and third counts of the client's complaint were not covered under the policy because they arose out of the attorney's actions as a creditor collecting on a debt, and not out of any act or omission of the attorney in rendering legal services. However, the court held that the policy provided coverage for the second count, alleging that the attorney had failed to obtain a pre-petition discharge of the client's fee obligation to the attorney. The court reasoned that simply because the amount of damages under this claim would be analyzed in terms of the fees collected by the attorney pre-petition did not mean that the injury was in fact caused by the fees charged and therefore excluded from coverage. Instead, the court held that the damage was caused by the attorney's alleged negligence in rendering legal services and was potentially within the coverage afforded by the policy. ✦

Intentional Acts Exclusion Bars Coverage for Fraud; Insurer Did Not Waive Exclusion by Omitting from Initial Denial

continued from page 5

not the insured. The court reasoned that the "safe harbor" did not impose coverage because the representative was convicted of criminal fraud, and the safe harbor did not apply to claims "arising out of or resulting from, in whole or in part, an Insured's commission of…any…criminal act."

The court also held that the insurer did not waive the defense based on the intentional acts exclusion by failing to rely on the exclusion when it initially denied coverage. The court explained that waiver can not be used to create coverage where none exists. Relying on *Albert J. Schiff Associates, Inc. v. Flack,* 417 N.E.2d 84 (N.Y. 1980), the court stated "where the issue is the existence or non-existence of coverage (*e.g.*, the insuring clause and exclusions), the doctrine of waiver is simply inapplicable." ✦

For more information, please contact us at 202.719.7130

New York Public Policy Mandates Right to Purchase Extended Reporting Period Coverage

In an unreported decision, a New York trial court, applying New York law, has held that even though a policyholder did not have a right under two claims-made professional liability policies to purchase extended reporting period (ERP) coverage upon the policyholder's decision not to renew, New York public policy required that the policyholder have such a right. *Segal Co. v. Certain Underwriters at Lloyd's, London*, No. 601110/03 (N.Y. Sup. Ct. Nov. 18, 2003).

The insurer had issued primary and excess polices in the excess and surplus lines market to a benefits consulting firm. The primary policy's extended reporting period endorsement provided that the firm could purchase ERP coverage in "the event of cancellation or non-renewal of the insurance by [the insurer]." The excess policy followed form to the primary policy. Several months before the policies expired, the firm's broker informed the firm that it would be unable to replace the firm's coverage "due to recent adverse loss experience." The firm responded that it would exercise its right to purchase the ERP for both the primary and excess policies. The insurer then offered to renew the primary and excess policies under different terms, but the firm refused and elected to purchase ERP coverage. The insurer argued that the firm did not have such a right since the firm, and not the insurer, had declined to renew the policy. Litigation concerning the firm's right to elect ERP coverage commenced.

The court first held that the insurer's renewal proposal did not trigger the firm's contractual right to purchase ERP coverage because the primary policy, and thus the follow-form excess policy, provided that "the quotation of different premiums, deductibles, limits of liability, or policy language in a renewal offer does not constitute a refusal to renew." Consequently, since the insurer had not cancelled or failed to offer renewal policies, the firm did not have a right under the language of the policies to purchase ERP coverage.

Nevertheless, the court concluded that New York public policy required that the firm have a right to purchase ERP coverage under both policies. In so holding, the court relied upon a New York Insurance Department regulation—11 NYCRR § 73.3(c)(1)—that requires that all claims-made policies allow the policyholder to purchase ERP coverage upon termination or non-renewal, even where caused by the policyholder. Citing a New York statute providing that all policies that fail to comply with New York's insurance laws "shall be enforceable as if [they] conformed with such requirements or prohibitions," the court held that the firm had a right to purchase ERP coverage under the primary and excess policies. The court rejected the insurer's arguments that the insurance regulations did not apply because the insurer was a foreign insurer not authorized to do business in New York and the policies were issued in the excess and surplus lines market, explaining that the insurer "not being authorized to do business in New York has nothing whatsoever to do with the right of New York to regulate industries affecting its residents." ✦

WRF Announces New Insurance Partners

The Insurance Group is pleased to announce that William Smith and David Topol, both of counsel with the firm, have been elected to the partnership, effective January 1, 2004.

William E. Smith
202.719.7350
wsmith@wrf.com

William Smith serves in the litigation and insurance practices. He represents clients in complex civil litigation matters and has substantial experience representing professional liability and general liability insurance carriers in coverage actions. Mr. Smith is a former in-house litigation counsel for a global telecommunications company where he handled domestic and international commercial litigation and arbitration matters. He received his J.D., *magna cum laude*, from the University of Michigan Law School.

David H. Topol
202.719.7214
dtopol@wrf.com

David H. Topol serves in the firm's insurance, litigation and appellate practices. He represents insurance carriers in connection with a variety of professional liability policies, including banking, mutual fund, investment adviser and directors and officers policies. Recently, he authored the "Professional Liability Chapter" of *Holmes' Appleman on Insurance*, 2d, (Fall 2003). Mr. Topol is a former Trial Attorney with the U.S. Department of Justice, Environmental Enforcement Section. He also served as a law clerk to the Honorable A. Raymond Randolph, U.S. Court of Appeals for the D.C. Circuit. Mr. Topol received his J.D. from Yale Law School.

Court Refuses to Apply I v. I Exclusion Where Officers Who Provided Information to Plaintiffs Did Not Do So to Obtain an "Economic Benefit"

continued from page 1

reasonable expectation that the insured will be covered for making misleading statements."

The court then held that the I v. I exclusion did not "conspicuously, plainly and clearly" apprise the officers that coverage was unavailable, notwithstanding the insurer's argument that the exclusion applied since other officers had provided "assistance." In so holding, the court rejected the insurer's effort to rely on a dictionary definition of "assistance," explaining that California law disfavors resorting to a dictionary definition in lieu of relying on how the policy language at issue would be interpreted by a reasonable layperson. The court reasoned that the insurer's interpretation would lead to absurd results, such as loss of coverage if a director of the company was subpoenaed to testify in the underlying action or was duped into making a statement advantageous to the underlying plaintiffs. The court also reasoned that adopting the insurer's interpretation of the exclusion would "tread dangerously close to violating the public policy of the State of California." Specifically, the court stated that the insurer admitted at oral argument that its interpretation of the policy language could provide an incentive for policyholder companies and directors to agree to suppress evidence, which is against public policy. Finally, the court held that adopting the insurer's interpretation of the exclusion would render coverage under the policy illusory because coverage or non-coverage would turn on chance events outside of a director's or officer's control.

Ultimately, the court held that "the [I v. I] exclusion bars coverage for securities fraud claims only if a director or officer actively and voluntarily provided substantial aid or help to a securities fraud plaintiff with the intent to aid the prosecution of the lawsuit in order to obtain economic benefit." Applying this standard, the court held that, although the stipulated facts indicated that two officers of the company had provided information that allowed the consolidated amended complaint to survive a motion to dismiss, there was no evidence the officers had acted to obtain an "economic benefit". ✦

For more information, please contact us at 202.719.7130

Sign up to receive *The Executive Summary* and other WRF newsletters by email!

Please visit www.wrf.com/newsletters.asp

Contributors

Joseph A. Bailey III	202.719.4554	jbailey@wrf.com
Nicholas A. Bonarrigo*	202.719.7410	nbonarrigo@wrf.com
Mary E. Borja	202.719.4252	mborja@wrf.com
Thomas W. Brunner	202.719.7225	tbrunner@wrf.com
Jason P. Cronic	202.719.7175	jcronic@wrf.com
Stephanie M. Denton	202.719.4612	sdenton@wrf.com
Cara Tseng Duffield	202.719.7407	cduffield@wrf.com
Valerie E. Green	202.719.7516	vgreen@wrf.com
Paul J. Haase	202.719.3434	phaase@wrf.com
Dale E. Hausman	202.719.7005	dhausman@wrf.com
Kimberly M. Melvin	202.719.7403	kmelvin@wrf.com
Karalee C. Morell	202.719.7520	kmorell@wrf.com
Leslie A. Platt	202.719.3174	lplatt@wrf.com
William E. Smith	202.719.7350	wsmith@wrf.com
Daniel J. Standish	202.719.7130	dstandish@wrf.com
Sandra Tvarian Stevens	202.719.3229	sstevens@wrf.com
David H. Topol	202.719.7214	dtopol@wrf.com
Jonathan S. Woodruff*	202.719.7426	jwoodruff@wrf.com

*District of Columbia Bar membership pending. Supervised by the principals of the firm.

1776 K Street NW ✦ Washington, DC 20006 ✦ (ph) 202.719.7000 ✦ (fax) 202.719.7049

7925 Jones Branch Drive ✦ Suite 6200 ✦ McLean, VA 22102 ✦ (ph) 703.905.2800 ✦ (fax) 703.905.2820

For back issues of WRF Newsletters, please visit www.wrf.com/publications/newsletter.asp