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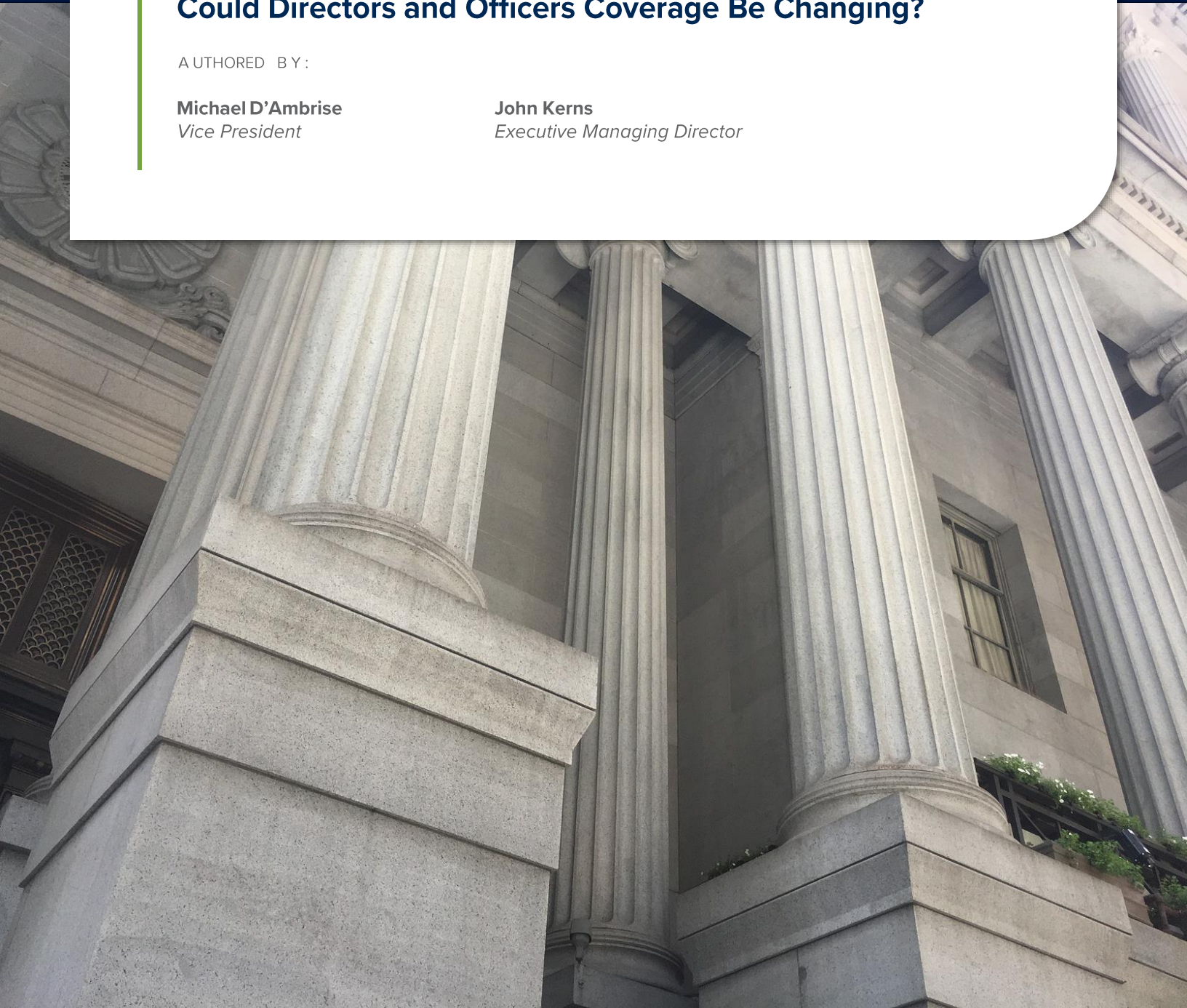
# New Supreme Court of Delaware Decision

## Could Directors and Officers Coverage Be Changing?

AUTHORED BY:

**Michael D'Ambrise**  
*Vice President*

**John Kerns**  
*Executive Managing Director*





# What Did the Supreme Court of Delaware Say?

While the COVID-19 pandemic may still be front and center, state courts continued working and rendering crucial decisions. The Supreme Court of Delaware recently rendered a decision that could have a significant effect on both venue and the meaning of fraud coverage. With so many corporations being incorporated in Delaware, there could be a national impact.

In March 2021, the Supreme Court of Delaware issued a ruling in *RSUI Indemnity Company v. Murdock*.<sup>1</sup> This specific dispute arose from events that occurred in 2013. David Murdock, Dole's Chief Executive Officer, took the company private via a merger that allowed Murdock to acquire all of Dole's stock. Following this privatization, stockholders filed multiple lawsuits alleging a breach of fiduciary duty against Murdock and Dole's Chief Operating Officer and General Counsel, Michael Carter. Stockholders alleged that Murdock and Carter drove down the stock price through multiple fraudulent acts. The Delaware Court of Chancery found that Murdock and Carter breached their fiduciary duties and engaged in fraudulent acts. Prior to settlement in that case, a federal securities class action was filed based on the findings of the Court of Chancery—both cases were settled.

Dole sought coverage under their Directors and Officers (D&O) Policy for defense and settlement costs following these events. Because the Court of Chancery found that Murdock and Carter engaged in fraudulent acts, several of Dole's insurers, including RSUI Indemnity Company, filed suit to determine whether they had an obligation to provide coverage for the federal case.

After the Delaware Superior Court found in favor of Dole, RSUI Indemnity Company appealed to the Supreme Court of Delaware. RSUI claimed that California law should apply to the case and that even if Delaware law did apply, Delaware does not allow coverage of claims involving fraud as a matter of public policy.

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1. *RsuI Indem. Co. v. Murdock*, 248 A.3d 887 (Del. 2021)

# A California Dispute, But Delaware's More Favorable Law Applies

Because the D&O Policy did not have a choice of law provision, the court needed to determine which state's laws would apply. When looking to determine whether California or Delaware law applied in this case, the court looked at a variety of factors. The court acknowledges that the corporation has many contacts with the state of California that were factored into the analysis. In the end, the court held that "[w]hen the insured risk is the directors' and officers' 'honesty and fidelity' to the corporation"—and we would add to its stockholders and investors—and the choice of law is between headquarters or the state of incorporation, the state of incorporation has the most significant interest."<sup>2</sup> This means that in a directors and officers coverage case where the company implicated is incorporated in Delaware, Delaware law is likely to apply.



Because many companies are incorporated in the state of Delaware, its law could have a significant impact in the other 49 states where disputes may arise. While Delaware may prove to be a more favorable jurisdiction for coverage when allegations of fraud are involved, other considerations such as the insurability of punitive damages may also be more favorable if coverage is being considered under Delaware law. Although awards of punitive damages in D&O cases are not exactly pervasive, they do exist.

## Fraud Coverage in Delaware: What Does it Mean?

After deciding that Delaware is the correct forum for this case, the court turned to whether the public policy in Delaware would preclude coverage for claims involving fraud. In doing so, the court held that "The question here then is: does our State have a public policy against the insurability of losses occasioned by fraud so strong as to vitiate the parties' freedom of contract? We hold that it does not. To the contrary, when the Delaware General Assembly enacted Section 145 authorizing corporations to afford their directors and officers broad indemnification and advancement rights and to purchase D&O insurance 'against any liability' asserted against their directors and officers 'whether or not the corporation would have the power to indemnify such person against such

liability under this section,' it expressed the opposite of the policy RSUI asks us to adopt."<sup>3</sup> The court's holding in this instance shows it believes that Delaware's public policy favors parties' freedom of contract and that sophisticated parties should be able to enter into contracts without interference from the state; however, this does not mean that all fraud would be covered. The court also noted that "the Policy's exclusion of losses 'based upon, arising out of or attributable to . . . any deliberately . . . fraudulent act' but only if 'established by a final and non-appealable adjudication,' implies that fraud that does not fall within the exclusion because it has not been finally adjudicated will otherwise be covered"<sup>4</sup>

2. <https://www.greenbiz.com/article/why-supply-chain-disruptions-may-slow-down-clean-energy-deployments>

3. <https://www.rystadenergy.com/newsevents/news/press-releases/solar-powers-supply-chain-crisis-makes-15c-climate-target-a-major-challenge/>

4. <https://www.swissre.com/reinsurance/property-and-casualty/reinsurance/engineering-reinsurance/inflation-can-be-bad-news-for-engineering.html>



The significance of this part of the ruling could be overstated. While the court does make clear that carriers can be responsible for defending a fraud claim, it also makes clear that this coverage is still subject to what is often referred to as the “conduct exclusion”: a common policy exclusion that bars coverage for deliberate fraud, typically after a court has rendered a non-appealable judgment that such deliberate fraud has occurred. This could mean possible coverage that would cease if a state’s highest court or the United States Supreme Court affirmed that deliberate fraud did, in fact, occur. Thus, the Supreme Court of Delaware’s ruling seems in line with current case law and policy language on fraud but could result in more change down the line for businesses to note.

## Implications in Purchasing D&O Insurance

We view the Supreme Court of Delaware’s decision as a positive precedent. The court’s decision and ultimate ruling in favor of Dole supports what many boards of directors rely upon when purchasing D&O insurance: when allegations or findings of fraud have been established, it is not until it is proven through non-appealable, final adjudication at the highest court level that coverage would be barred. The conduct exclusion is understandable in that D&O carriers do not want to be insuring matters that may otherwise grate against public policy. If D&O insurance carriers were to modify the conduct exclusion to apply much earlier in the claim or litigation process, a mere email evidencing an admission of fraud could be used to bar coverage. This would be problematic when considering the length and expense major shareholder claims incur. While “choice of law” is not necessarily established in most standard D&O policy forms, “state of incorporation” for companies incorporated in Delaware may be good coverage practice based upon this ruling.

Companies seeking to mitigate risks presented by the threat of securities litigation can do so with D&O liability coverage. As the legal community monitors for securities filings around the country that could have a Delaware implication, publicly traded companies should process the effects of these cases and consider the scope of their policies to help ensure that such litigation will be addressed.

**Brown & Brown’s Executive Liability team offers innovative solutions to companies seeking to limit this type of litigation risk with insurance coverage programs.**



## About the Authors

### **Michael D'Ambrise**, *Vice President*

Michael P. D'Ambrise is a Vice President in the Brown & Brown's Executive Liability practice in New York. He has a Bachelor of Arts degree with high honors in History/Political Science and Spanish from Rutgers University and a J.D. from Fordham Law School. Michael is a member of the New York and New Jersey State Bars and the bar of the United States District Court for New Jersey. He is a former claims analyst who specializes in Executive Liability coverages.

### **John Kerns**, *Executive Managing Director*

John Kerns is an Executive Managing Director and leads the National Financial Services practice out of the New York City office. John has more than 20 years of experience within the Executive Liability marketplace. John holds a B.A. degree in English Literature from The Catholic University of America.



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