AKO FINANCIAL SERVICES ALERT

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D&O Insurance: Don't Let The Insurance Companies Control Your Life

By R. Mark Keenan

Directors and Officers ("D&O") insurance is one of the most critical insurance protections for any financial institution—and in particular, its Board of Directors. In turn, advancement of defense costs, on a monthly or quarterly basis, is one of the most practical protections provided to any director or officer in such a policy. If a director has to wait until the litigation is completed before he or she can obtain reimbursement for legal fees—it may be too little, too late.

Allegations of Misrepresentation

Recently, however, insurance companies have been attempting to block advancement of defense costs based solely upon their allegation that the policyholder made a misrepresentation in the policy application (which you as an outside director did not see, review or sign).

Can the D&O insurance companies negate such payments based upon mere allegations and assertions alone?

The few courts that have specifically addressed the issue have held that an insurance company must first advance defense costs to its Director and Officer policyholders—and must continue to do so until a *final adjudication* of rescission is reached—by a court of law.

> **"...insurance companies were telling the Court... we can unilaterally decide the policyholder's rights..."**

Nevertheless, insurance companies have persisted in their pursuit to unilaterally decide important issues of coverage. In the fallout regarding Adelphia Communications, former directors of Adelphia sought reimbursement of the legal fees incurred in hundreds of civil suits that had been brought against them. Adelphia's D&O insurers said no, "we won't pay" because they had sent a letter "rescinding" the policy due to allegations that the directors had committed wrongdoings.

This firm, representing one of the directors, immediately filed a motion before the court, *Associated Electric & Gas Insurance Services, Ltd., et al. v. John J. Rigas, et al.* (2004 WL 540451 (E.D.Pa.) March 17, 2004) seeking advancement of the directors legal fees pending resolution by the court of any rescission claim.

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R.Mark Keenan is a senior shareholder in the New York office of Anderson Kill & Olick and Co-Chair of Anderson Kill's Financial Services Group. Mark is a leading lawyer in the fields of insurance coverage, securities law and litigation. Mark has also provided risk management services involving policy and claim analysis, factual investigations of loss, preparation of damage calculations, claims negotiations, creditor committee representation in foreign insolvencies, due diligence investigations in mergers and acquisitions and many other facets of risk management services. Mark can be reached at mkeenan@andersonkill.com or (212) 278-1888.

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We hope you find this issue of the Financial Services Alert informative. We invite you to contact the Group Chairs, R. Mark Keenan, at (212) 278-1888 or mkeenan@andersonkill.com or David M. Schlecker, at (212) 278-1730 or dschlecker@andersonkill.com with your questions or concerns.

In opposition, the Adelphia insurance companies argued that they were entitled to refuse payment of advance defense costs based upon their "rescission" of the insurance policy and that under the law, they can unilaterally rescind a policy without a judicial determination.

In other words, the insurance companies were telling the Court "we don't need you" we can unilaterally decide the policyholders' rights—without the Court.

Needless to say, we argued that if an insurance company were permitted to deny obligations to advance defense costs based upon mere assertion of misrepresentations alone (as compared to court adjudication) the requirement to advance defense costs would be rendered illusory. An insurance company could simply negate its duty to advance defense costs through its own self serving allegations.

Innocent Until Proven Guilty

Moreover, there is a simple but rather basic notion in our system of justice. Namely, that you are presumed innocent until proven guilty. Shouldn't a policyholder be presumed to be innocent until he or she is proven guilty? Shouldn't the policyholder have the right to expect that his or her own insurance company would be the first to promote the policyholder's presumed innocence rather than convicting him without court process?

Just recently, Federal Judge Baylson ruled in favor of the Adelphia directors holding that these important public policy considerations including the "presumption of innocence" and that each party should be entitled to their "day in court," require performance under the insurance policy unless and until a court of law rescinds it. The court noted "it would be possible" for D&O insurance companies to explicitly reserve "to themselves" the "unfettered discretion whether to advance defense costs—but that language does not appear in these policies." The court noted why: "No doubt, as a matter of business common sense, the Carriers might be reluctant to issue a policy with such a draconian power, because they might find it different to sell..."

In sum, the court held that "Insurance carriers do not function as courts of law," and required advancement of defense costs.

As this author noted in the *Wall Street Journal* article covering the case, "This is still the United States of America . . . when there is a dispute you have to [await] a court determination." (*Wall Street Journal*, March 24, 2004, Page C5).

Don't let your insurance company unilaterally determine your rights. ■

R. Mark Keenan was quoted in the March 24, 2004 issue of the Wall Street Journal in an article entitled "Directors' Armor: Adelphia Ruling Shows Legal Bills Must Be Covered." Mark led the Anderson Kill team in a major victory for D&O policyholders over insurance companies. To view the decision, article or press release, please visit our website at www.andersonkill.com or contact Mark for more information.

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