The Impact of Delaware's Sudden Dominance in D&O Coverage Disputes

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Long dominant in business and corporate governance litigation, the Delaware state courts have recently garnered significant attention for their decisions in director & officer liability insurance coverage disputes. In the past few years, the Delaware Superior Court has issued a number of pro-corporate policyholder rulings that are distinctly more favorable to insureds compared to decisions in other jurisdictions on the same or similar issues. The result has been an increased level of D&O insurance coverage litigation generally, and in Delaware in particular. This paper addresses several of the most significant decisions issued to date on critical issues, including choice of law, public policy limitations on coverage, the scope of Securities Claim coverage, related wrongful act issues, and allocation between covered and uncovered loss.

I. Delaware Choice of Law and Forum Related Issues

In the absence of a choice of law clause, the choice of law rules in most states require the forum court to determine which state has the most significant relationship with the insurance coverage dispute. More often than not, the most significant relationship test results in application of the insurance law of the state where the named insured corporation has its primary business location, particularly if the policy itself is issued and delivered to the insured in that jurisdiction. *See, e.g., Certain Underwriters at Lloyd's, London v. Foster Wheeler Corp.*, 36 A.D.3d 17 (N.Y. App. Div. 1st Dep't 2006), aff'd, 9 N.Y.3d 928 (2007) (under "center of gravity" test, applicable law is the location of the insured's principal place of business where insurance policies cover risks in multiple states).

The Delaware Supreme Court likewise applies the most significant relationship test to decide choice of law for insurance policies. *See Certain Underwriters at Lloyd's, London v.*

Chemtura Corp., 160 A.3d 457 (Del. 2017); *Travelers Indem. Co. v. CNH Indus. Am., LLC*, No. 420, 2018 WL 3434562 (Del. July 16, 2018) (TABLE). However, in a little-noticed decision in 2010, Delaware Superior Court Judge Fred Silverman, in a discussion that appears to be *dicta*, expressed why he thought Delaware law should apply to an insurance coverage dispute under a D&O policy issued to a company headquartered in Virginia but incorporated in Delaware. *See Mills Limited P'ship v. Liberty Mut. Ins. Co.*, No. 09C-11-174, 2010 Del. Super. LEXIS 563, 2010 WL 8250837 (Del. Super. Ct. Nov. 5, 2010). The coverage issue in *Mills* was an exhaustion question arising out of the settlement of a securities fraud claim. The court had actually found that a Virginia court would apply the same coverage standard as a Delaware court, and noted that "if the laws would produce the same decision, there is no real conflict and a choice of law analysis would be superfluous." *Id*. at * 11 (citing *Great Am. Opportunities, Inc. v. Cherrydale Fundraising, LLC*, No. 3718, 2010 Del. Ch. LEXIS 15 (Del. Ch. Jan. 29, 2010). The court nevertheless addressed choice of law. The court noted that an optional arbitration clause in the policy provided that any arbitrators would "give due consideration" to the law of the insured's state of incorporation, and concluded that the parties "probably expected Delaware law to apply." *Id*. at *14. The court noted that "a fundamental policy of contract law is protecting the parties' expectations." *Id.* at *11. The court then cited the Restatement (Second) Conflicts of Law and listed the contacts set forth in §188 as considerations for determining applicable law when an insured risk involves multiple jurisdictions and is not "located" in a particular state. Those contacts included the places of contracting and of negotiation of the contract, but the court made no mention of a factual record or analysis in that regard. Instead, the court stated, without citing any precedential authority:

> When the insured risk is the directors' and officers' "honesty and fidelity" to the corporation, and the choice of law is between headquarters or the state of incorporation, the state of incorporation has the most significant relationship.

Id. at *17-18.

The *Mills* decision drew little attention at the time.

In 2018, however, Judge Eric Davis of the Delaware Superior Court, in *Arch Insurance Co. v. Murdock*, 2018 Del. Super. LEXIS 96; 2018 WL 112911 (Del. Super. Ct. March 1, 2018) ("*Arch v. Murdock 2018*"), adopted and applied the *Mills* analysis in holding that the law of Delaware, rather than California, governed the construction of a D&O policy issued in California to Dole Food Company, Inc. The matter in dispute was coverage for a settlement of a Delaware Chancery Court action arising out of Dole CEO and controlling stockholder David Murdock's acquisition of 100% of Dole's publicly-traded stock. Dole was a Delaware corporation whose headquarters was in California. The primary defendants, Murdock and Dole's former general counsel, were located in California, and the insurers presented evidence that the relevant conduct of the parties had taken place in California, the policies were issued and delivered in California, and the policies contained California amendatory endorsements to conform the policies to California's insurance regulatory requirements. The policies contained no choice of law provision and no ADR clause like that in *Mills*. The court nevertheless applied Delaware law.

The court acknowledged that "[i]n complex insurance cases with risks in multiple states such as this one, Delaware courts have generally held that the most significant factor for the conflict-of-law analysis is the principal place of business of the insured because it is 'the situs which link[s] all the parties together,'" citing cases including *Liggett Group, Inc. v. Affiliated FM Ins. Co.,* 788 A.2d 134 (Del. Super Ct. 2001). *See Arch v. Murdock 2018*, 2018 Del. Super. LEXIS 96, at *22. *Liggett* contained an in-depth choice of law analysis applying the law of the

state of the insured's headquarters to a general liability policy insuring risks in multiple states. Judge Davis observed that *Liggett* "is a very well-reasoned opinion and strong authority on the issue of choice of law in complex insurance coverage situations." *Id.* at *24. But the court found *Mills* to be the "better authority" for a D&O policy, citing Judge Silverman's dicta that the state of incorporation has the "most significant relationship" to a D&O policy, which insures directors' and officers' "honesty and fidelity" to the corporation. *Id.*

The Delaware Supreme Court rejected the Dole D&O insurers' application for certification of Judge Davis's decision for interlocutory appeal. The coverage litigation has since been resolved, but one of the insurer parties reserved the right to appeal the choice of law ruling (and others) to the Delaware Supreme Court. The insurer's opening brief was filed under seal on July 7, 2020. The case caption is *RSUI Indemnity Company v. David H. Murdock, et al.*, No. 154,2020, in the Supreme Court of Delaware.

The Delaware Superior Court made several other controversial rulings in *Arch v. Murdock*, two of which are discussed later in this paper. But the impact of the choice of law decision to date has been significant. Since the court's March 1, 2018 decision, at least two courts have expressly adopted and applied the choice of law principle discussed in *Mills* and applied in *Arch v. Murdock I*, one characterizing the principle as a "consistent" holding of Delaware courts. *See Pfizer, Inc. v Arch Ins. Co.*, No. N18C-010310, 2019 WL 3306043, 2019 Del. Super. LEXIS 345 at *19 (Del. Super. Ct. July 23, 2019) ("[A]pplying Delaware law here accords with this Court's consistent application of Delaware law to resolve disputes over insurance coverage of directors' and officers' liability."); *Calamos Asset Mgmt. v. Travelers Cas. & Sur. Co. of Am*, No. 18-1510, 2020 U.S. Dist LEXIS 111895 (D. Del. June 25, 2020). Other Delaware Superior Court judges have acknowledged the principle in *dicta*. *See IDT Corp. v.*

U.S. Specialty Ins. Co., 2019 Del. Super. LEXIS 55*; 2019 WL 413692 (Del. Super. Ct. Jan. 31, 2019) (noting there was no conflict of laws in the case and that a Delaware court should therefore "avoid a choice-of-law analysis altogether," but then noting "one more thing"—"Delaware courts have consistently held" (citing only *Mills*) that Delaware law should apply to a Delaware corporation's D&O policy); *Ferrellgas Partners, L.P. v. Zurich Am. Ins. Co*., 2020 Del. Super. LEXIS 41, at *8; 2020 WL 363677 (Del. Super. Ct. Jan. 21, 2020) (finding no need to choose between Texas and Delaware law, but asserting that Delaware courts "consistently" have held (citing *IDT* and *Mills*) that Delaware law applies to D&O insurance disputes with Delaware corporations.).

It remains to be seen whether *Mills* and *Arch v. Murdock I* approach will be upheld by the Delaware Supreme Court or followed by other jurisdictions. Indeed, a New York trial court recently rejected the *Mills* analysis in connection with a series of D&O coverage disputes arising out of the American Realty Capital accounting fraud. In *XL Specialty Insurance Co. et al. v. AR Capital, LLC, et al*, No. 650018/2019 (Sup. Ct., NY Cty., NY) the court applied New York law over Delaware law to a D&O policy issued to a Delaware-incorporated insured, AR Capital, LLC, with a principal place of business in New York. *See* Transcript of Hearing at 45-49, attached to Decision + Order on Motion (Jan. 31, 2020), *XL Specialty Ins. Co. et al. v. AR Capital, LLC, et al*, No. 650018/2019 (Sup. Ct., NY Cty., NY). The insureds had asserted counterclaims against excess D&O insurers for breach of contract and bad faith and argued for application of Delaware law based on *Mills* in opposing a motion to dismiss those claims. The New York court rejected that argument, distinguishing the choice of law analysis in an insurance coverage case from that in an "internal affairs doctrine" case – such as breach of fiduciary or other duties to shareholders by corporate officers – "where you look at the state of

incorporation." *Id.* at 8. Specifically, the court ruled that a contract choice of law analysis should apply, even if the underlying claim for which the insured seeks coverage is an "internal affairs" matter.

> This case is not about whether the defendants breached their fiduciary duties to the shareholders of their WREIT [sic]. It's about -- that claim is already settled. The question here is about insurance coverage and interpretation of the insurance contract.

Id. at 46. Consistent with New York's "center of gravity" test, the court ruled that the insured's "state of domicile should be the driving force" in the choice of law analysis. *See* Transcript at 46.

The American Realty Capital insurance dispute resulted in other Delaware Superior Court rulings on *forum non conveniens*, personal jurisdiction and comity, all of which have taken on greater significance in light of the *Mills* and *Arch v. Murdock 2018* decisions. The issues arose because of a race to the courthouse in which the insurers filed in New York and the insureds filed in Delaware a day later.

First, the Delaware Superior Court rejected the insurer's motion to dismiss the second filed Delaware action on *forum non conveniens* grounds. The court found that the Delaware and New York cases would be deemed contemporaneously filed, with no "first-to-file" preference. The court applied a *forum non conveniens* analysis and held that the insurer defendants failed to establish they would suffer "overwhelming hardship" if required to litigate in Delaware and that the so-called *Cryo-Maid* factors (balancing of the parties' interests)[1] did not "tip in favor of"

[1] *See Gen. Foods Corp. v. Cryo-Maid, Inc*., 198 A.2d 681 (Del. 1984). One of the *Cryo-Maid* factors is whether Delaware substantive law would apply to the case. The defendant insurers argued that New York law would apply, but the plaintiff insureds' asserted there was no conflict between the relevant laws of the two states. The court made no ruling on choice of law and treated it as a neutral factor. *Id.* at *16-17.

staying the Delaware litigation in deference to the New York forum. *See AR Capital, LLC v. XL Specialty Ins*. Co., 2019 Del. Super. LEXIS 216, at *20, 2019 WL 1932061 (Del. Super. Ct. April 25, 2019), *reh'g denied* 2019 Super. LEXIS 288 (May 29, 2019).

Meanwhile, the New York trial court denied the insureds' motion to dismiss the New York case in favor of the Delaware forum, based on New York's strong interest in the dispute and application of the "first filed" rule. On appeal, the First Department affirmed the decision. *See XL Specialty Ins. Co. v. AR Capital, LLC*, 181 A.D.3d 546 (NY App. Div. 1st Dep't 2020).

Second, the Delaware Superior Court addressed personal jurisdiction with respect to certain Difference in Conditions ("DIC") insurers that had been sued in Delaware but were not involved in the New York litigation. The DIC insurers sought dismissal for lack of personal jurisdiction because their policies had been issued to a different named insured headquartered in New York and incorporated in Maryland, and that insured had no place of business in Delaware. The court granted the jurisdiction motion as to the DIC insurers, holding that under recent United States Supreme Court case law, in order for the court to exercise general personal jurisdiction over the DIC insurers, they would either have to be incorporated or have their principal place of business in Delaware, which they did not. *Id.* at *8. The court ruled that personal jurisdiction also was lacking, and found inadequate the insureds' allegations that the DIC insurers are licensed to do business and in fact transact business in Delaware, and that they write insurance policies covering Delaware citizens. *Id.* at *13. Those connections, according to the court, were "outside the context of this lawsuit," and the cause of action asserted against the DIC insurers did not arise from their conduct in Delaware. *Id.*

The AR Capital coverage litigation proceeded simultaneously in two jurisdictions for over a year and a half, with the parties coordinating discovery between the two cases. However, on a second round of dismissal motions filed in the Delaware action, the insurers again asked the Delaware Superior Court to dismiss or stay the Delaware litigation in deference to the New York action. Although the Delaware court again rejected the *forum non conveniens* argument, it decided to stay the litigation on principles of comity. This was based on the substantive rulings that had been reached in the New York litigation by the trial court, and affirmed by the Appellate Division, that New York was a logical forum and New York had a legitimate interest in the litigation,. *See AR Capital, LLC v. XL Specialty Ins. Co.,*, No. N19C-01-024, 2020 WL 4907990 (Del. Super. Ct. Aug. 3, 2020).

II. Coverage for Settlement Reached After Trial Court Decision Finding Fraud

The *Arch v. Murdock* case also raised a unique question regarding the primary D&O policy's conduct exclusion and the insurability of fraudulent conduct under Delaware law. As noted above, the underlying claim against Murdock and others arose out of Murdock's taking Dole private in a November 2013. The price and other terms of the transaction were approved by a special committee of the Dole board and a narrow majority of disinterested stockholders. *See In re Dole Food Co. Stockholder Litig*., No. 8703, No. 9079, 2015 Del Ch. LEXIS* 223 (Del. Ch. August 27, 2015) (the "Chancery Court Decision"), at *73-80. Dole stockholders sued Murdock and others in Delaware Chancery Court, alleging breaches of fiduciary duty that had artificially deflated the market value of Dole's stock and had allowed Murdock to acquire the stock at an unfair price. *See id.* at *2-7. After a full bench trial, Vice Chancellor Travis Laster found that Murdock, the General Counsel, and Murdock's holding company DFC Holdings were jointly liable for breach of their duties of loyalty to the selling stockholders, specifically

finding and repeatedly characterizing Murdock's and the General Counsel's as conduct as "fraud." *See, e.g.*, *id.* at *155 ("Murdock and Carter's pre-proposal efforts to drive down the market price and their fraud during the negotiations reduced the ultimate deal price by 16.9%."); *see also Arch Ins. Co. v. Murdock*, 2018 Del. Super. LEXIS 96 *; 2018 WL 112911 (Del. Super. Ct. March 1, 2018) ("*Arch v. Murdock 2018*"), at *17 ("Vice Chancellor Laster specifically found that 'Murdock and Carter's conduct throughout the Committee process . . . demonstrated that their actions were not innocent or inadvertent, but rather intentional and in bad faith.'"). Vice Chancellor Laster found that Murdock and the two other responsible defendants were liable to Dole stockholders in the amount of over $148 million. *See Dole* Chancery Court Decision, 2015 Del Ch. LEXIS* 223, at *158.

Shortly after the Chancery Court Decision was issued, before the issuance of a final order and without the Dole D&O Insurers' written consent, the *In re Dole* parties reached a settlement in which Murdock agreed to pay 100% of the Chancery Court's award against him and the other defendants (the "Dole Settlement"). Murdock then sought coverage for the Dole Settlement from the Dole D&O insurers. In the subsequent *Arch v. Murdock* insurance coverage action, the insurers asserted – among other defenses to coverage for the Dole Settlement – both the primary policy's conduct exclusion and the uninsurability of fraud as a matter of public policy.

The D&O primary policy's conduct exclusion stated that the policy would provide no coverage for any Loss on account of a Claim;

> based upon, arising out of or attributable to … [a]ny profit … or financial advantage to which the Insured was not legally entitled; or [a]ny willful violation of nay statute or any deliberately … fraudulent act, error or omission by the Insured, ***if established by a final and non-appealable adjudication adverse to such Insured in the underlying action.***

Arch v. Murdock I, at *8 (emphasis added). The Superior Court granted the insureds' motion to dismiss the insurers' claim based on the exclusion. *See Arch Ins. Co. v. Murdock*, 2016 Del. Super. LEXIS 645, 2016 WL 7414218 (Del Super. Ct. Dec. 21, 2016) ("*Arch v. Murdock 2016*"). The court did not question that the underlying court's findings of fraud and deliberate conduct, and indeed ultimately ruled that the insureds were collaterally estopped from denying those findings. *See Arch v. Murdock 2018,* 2018 Del. Super. LEXIS 96, at *18. The court also acknowledged that the underlying settlement and the subsequent Chancery Court order approving were "carefully crafted to mitigate the findings of" the Chancery Court Decision, possibly for the purpose of "maintain[ing] insurance coverage." *Id.* at *20. But the court found that the conduct exclusion did not bar coverage for the settlement, because "the [Chancery Court Decision] was not a final and non-appealable decision," *Id.* at *21.

The Superior Court's written opinion did not comment on the primary case law relied on by the insurers in their briefing: *In re IBP, Inc. S'holders Litig. v. Tyson Foods, Inc.,* 793 A.2d 396 (Del. Ch. 2002) ("*IBP*"), *appeal dismissed in part sub nom. Tyson Foods, Inc. v. Aetos Corp.*, 809 A.2d 575 (Del. 2002) ("*Tyson*"), and *aff'd Tyson Foods, Inc. v. Aetos Corp.*, 818 A.2d 145 (Del. 2003). In *IBP*, a party who entered and obtained court approval of a case after a post-trial decision returned to the court and moved to vacate the interlocutory order. Then-Vice Chancellor Strine rejected the motion, ruling that under Chancery Court rules, the interlocutory order *became* a final and non-appealable judgment as a result of the court's approval of the settlement. *IBP,* 793.A.2d at 400. The Delaware Supreme Court affirmed Vice Chancellor's Strine's ruling, explaining that when parties settle and waive any right to appeal, an interlocutory ruling "achieves finality" and becomes a "final and non-appealable adjudication." *Tyson*, 809 A.2d at 580.

The *Arch v. Murdock* court nevertheless found that the "plain, unambiguous language" of the conduct exclusion did not apply because (i) the Chancery Decision did not constitute a final and non-appealable adjudication, and (ii) the Chancery Court's "Settlement Order and Final Judgment did not make findings regarding fraudulent acts by an insured." *Arch v. Murdock 2016*, 2016 Del. Super. LEXIS 245, at *21.

The Delaware Supreme Court's treatment of this issue on appeal will be worth watching, for reasons beyond the Superior Court's failure to address the *IBP* and *Tyson* decisions. A year later in the same case, the *Arch v. Murdock* court held that the same Chancery Court Decision was "finally adjudicated" for purposes of collateral estoppel. *See Arch v. Murdock 2018,* 2018 Del. Super. LEXIS 96 *at *17-18.* The court cited the *Tyson* decision that it did had not addressed in the *April v. Murdock 2016* decision on the conduct exclusion. *Id.* at *16. For collateral estoppel purposes, the court found that the Chancery Court Decision "is sufficiently definite to be a final judgment on the merits," *id.* at *18, and ruled that "the Court will employ collateral estoppel against the Insureds on factual issues determined in the [Chancery Court Decision] to the extent those factual issues are relevant to issues in this civil action." *Id.* at *18-19. The court distinguished its holding from its earlier one on the conduct exclusion, quoting its own dicta from that earlier decision that there is a "big difference between [a collateral estoppel finding and] finding that contractually you agreed to a final non-appealable order. . . ." *See id.* at *16 n.91, *quoting Arch v. Murdock 2016*, 2016 Del. Super. LEXIS 96 at *15-16.

The collateral estoppel issue was before the *Arch v. Murdock* court because the insurers were seeking summary judgment on their defense that allowing Murdock to obtain insurance reimbursement for his payment in the Dole Settlement would violate Delaware public policy, as it would allow a Delaware director or officer to profit from conduct that a Delaware Chancery

Court had found to be a fraud against Dole's stockholders. The court rejected that defense in the same decision. The court acknowledged that it could not enforce an insurance provision that is contrary to Delaware public policy, but stated that Delaware courts may not "void an otherwise valid contract provision 'in the absence of clear indicia that such a policy actually exists.'" *See Arch v. Murdock 2018,* 2018 Del. Super. LEXIS 96, at *26-27, *citing Whalen v. On-Deck, Inc*., 514 A.2d 1072, 1074 (Del. 1986). The court stated that it could not find a Delaware decision holding that a corporation cannot obtain directors and officers insurance that covers breach of loyalty based on fraud. *See id.* at *27. The court cited *Whalen*, noting that the Delaware Supreme Court held that there was no Delaware public policy against insurance coverage for punitive damages. *See id.* The court also observed that § 145(g) of the Delaware General Corporation Law gives corporations the power to purchase insurance coverage for directors and officers "against any liability that could be asserted against him. *See id*. Finally, though acknowledging that "it may strain public policy to allow a director to collect insurance on a fraud," the court denied the insurers' motion, holding that Delaware public policy did not "clearly prohibit the Insurers from indemnifying the Insureds' fraud." *Id*. at *28.

The *Arch v. Murdock* decision on coverage for fraud is a striking example of the potential impact of the same court's decision on application of Delaware law to a D&O policy. The insurers sought application of the law of California, which includes a statutory provision barring insurance coverage for willful misconduct. S*ee* California Ins. Code § 533. Application of that California statute to the *Arch v. Murdock* coverage dispute might well have changed the outcome.

The Dole Settlement also raised the question whether Murdock's payment of additional consideration for the Dole shares he purchased constituted insurable "Loss". The court granted

the insureds' summary judgment motion on that issue, finding that the Dole Settlement fell within the primary policy's definition of Loss, which expressly included "settlement amounts." *Arch Ins. Co. v. Murdock*, 2019 Del. Super LEXIS 227, at *24, 2019 WL 2005750 (Del. Super. Ct. May 7, 2019) (*Arch v. Murdock III*). Although the policy's Loss definition expressly did not include "amounts representing the increase in the consideration paid … by the Policyholder in connection with its purchase of any securities," the court found that language did not apply because Murdock, rather than Dole (the policyholder), paid the Dole Settlement. *Id*. The court made no specific finding regarding whether Delaware public policy barred coverage for the Dole Settlement as disgorgement or restitution, but in light of his earlier decision on public policy and its reliance on the Delaware Supreme Court's *Whalen v. On-Deck, Inc*. decision in *Arch v. Murdock 2018*, the court's views on that specific issue were evident. A Delaware Superior Court had already ruled in 2015 that a restitutionary settlement was covered under a similarly worded D&O policy because of the policy's inclusion of "settlements" in is definition of Loss and a final adjudication condition in its illegal profit exclusion. *See Gallup, Inc. v. Greenwich Ins. Co*., 2015 Del. Super., LEXIS 129, 2015 WL 1201518 (Del. Super Ct., February 25, 2015).

The *Arch v. Murdock* decisions on the conduct exclusion and Delaware public policy on insuring fraud are on appeal in *RSUI Indemnity Company v. David H. Murdock, et al.*, No. 154,2020, in the Supreme Court of Delaware.

III. Coverage For a Shareholder Appraisal Action

Under most public company D&O policies, entity coverage is available only for a "Securities Claim." In 2019, Delaware courts issued two rulings regarding what constitutes a D&O insurance "securities claim." The first of these rulings found, as a matter of first impression, that a shareholder appraisal action pursuant to 8 Del. C. § 262 constitutes a

"Securities Claim," which the D&O policy at issue in that case defined as "any actual or alleged violation of any federal, state or local statute, regulation, or rule or common law regulating securities . . . ." *Solera Holdings, Inc. v. XL Specialty Ins. Co.*, 213 A.3d 1249, 1254 (Del. Super. Ct. 2019).[2]

By way of background, section 262 of the Delaware General Corporation Laws confers upon any stockholder holding shares at the time of certain types of mergers or consolidations the right to demand an appraisal by the Delaware Court of Chancery of the fair value of the shares. See 8 Del. C. § 262. *See also Verition Partners Master Fund, Ltd. v. Aruba Networks, Inc.,* 210 A.3d 128 (Del. 2019) (discussing valuation standards applicable to a section 262 appraisal action). No allegations of wrongdoing are required to plead an appraisal action.

The underlying claim in *Solera Holdings* was an appraisal action brought against Solera, the insured, following a merger between Solera and another company. *See id*. at 1252. The underlying plaintiffs claimed that the fair market value of their shares at the time of the merger was greater than the agreed merger price. The appraisal action did not allege any claims against Solera other than a request for an appraisal. *See id.* Solera requested coverage from its D&O insurer, which denied coverage on the basis that an appraisal action is not a claim for a "violation" of any law, as required by the policy definition of "Securities Claim," because "a 'violation' of law must involve wrongdoing, and allegations of wrongdoing are not required in an appraisal action." *Id*. at 1253. The D&O policy did not define the term "violation." *See id*. at 1255.

[2] The Superior Court's ruling in *Solera Holdings* is currently pending on appeal before the Delaware Supreme Court.

In response, Solera argued that the term "violation" does not require any wrongdoing; it merely requires an alleged violation of a legal standard. *See id*. at 1255. Accordingly, Solera argued, the appraisal action alleges a violation of law because an appraisal action "inherently alleges a violation of the statutory obligation to provide shareholders fair value for their shares when they are cashed out of their position." *Id*. at 1255.

Agreeing with Solera, the Delaware Superior Court held that a shareholder appraisal action against an insured entity is a "Securities Claim" because it alleges a violation of a law or rule regulating securities. *See id*. at 1255-56. The stockholders have a legal right to receive fair market value for their shares, reasoned the court, and the basis for an appraisal action is an allegation that the stockholders did not receive fair market value. *See id*. at 1256. In so ruling, the court rejected the insurers' argument that an appraisal action is not a Securities Claim because the appraisal action did not allege violations of law involving wrongdoing. As the court explained, the plain and ordinary meaning of the term "violation" is not limited to wrongdoing – a violation is, "among other things, a breach of the law and the contravention of a right or duty." *Id*. at 1256. The court also noted that if the insurer "intended to limit coverage to claims alleging wrongdoing, the Policy could have used limiting language." *Id*. at 1256.

The *Solera Holdings* court also held that the appraisal action sought "Loss," even though the only relief sought in the appraisal action was the fair market value of the shares and pre-judgment interest. The D&O policy at issue defined "Loss" to include "damages, judgments, settlements, pre-judgment and post-judgment interest or other amounts . . . that [Solera] is legally obligated to pay." *Id*. at 1256-57. Although the parties agreed that the fair market value of the shares did not constitute covered "Loss," the underlying claimants also sought pre-judgment interest. *See id*. at 1256. The court rejected the insurer's argument that pre-judgment interest

only constitutes "Loss" if it is awarded on covered damages, noting that the insurer did not cite any supporting case law and could have drafted the policy to limit coverage for pre-judgment interest awarded on covered damages if it had so desired. *See id*. at 1257. Although it found that pre-judgment interest constitutes "Loss," the court nevertheless denied Solera's motion for summary judgment regarding coverage for the pre-judgment interest due to factual issues and concerns that other policy exclusions could eliminate coverage. *See id.*

IV. "Securities Claim" Coverage For Claims Under Laws That Do Not "Regulate" Securities

In the second case addressing the meaning of "Securities Claims" in a D&O Policy, the Delaware Superior Court ruled in favor of the policyholder that the "Securities Claim" coverage for the company under a D&O Policy extended to breach of fiduciary duty, unlawful payment of dividends and fraudulent transfer counts asserted against it. On appeal, the Delaware Supreme Court reversed, holding that "Securities Claim" as defined by the policy did not include a claim against an insured for alleged common law and violations of state and federal laws that do not specifically "regulate securities." *See In re Verizon Ins. Coverage Appeals*, 222 A.3d 566 (Del. 2019), *reh'g denied* (Nov. 18, 2019).

This coverage dispute arose out of Verizon's 2006 spin-off of its print and electronic directories business into a newly formed subsidiary, Idearc Inc. Verizon transferred the directories business to Idearc in exchange for 146 million shares of Idearc common stock, $7.1 billion in Idearc debt, and $2.5 billion in cash. Verizon distributed the common stock to its shareholders. Idearc then launched as an independent, publicly traded company with $9.1 billion in debt. In 2009, Idearc filed for Chapter 11 bankruptcy. U.S. Bank, the Litigation Trustee, filed suit against Verizon and certain of its officers, alleging that they had loaded Idearc with

excessive debt. The Litigation Trustee's complaint alleged counts for (i) breach of fiduciary duty; (ii) payment of an unlawful dividend in violation of the Delaware Code; and (iii) fraudulent transfer under the U.S. bankruptcy code and the Texas Uniform Fraudulent Transfer Act. The Trustee sought to recover approximately $14 billion in damages.

Verizon incurred more than $48 million in defense costs, which it sought to recover from its insurers under its D&O policies. The insurers denied coverage on the basis that the trustee action did not constitute a "Securities Claim," defined in relevant part to mean a claim "alleging a violation of any federal, state, local, or foreign regulation, rule or statute regulating securities (including, but not limited to, the purchase or sale or offer or solicitation of an offer to purchase or sell securities)." Verizon then filed a coverage action against the insurers in Delaware Superior Court.

In the coverage litigation, the parties cross-moved for summary judgment on whether the U.S. Bank action was a "Securities Claim." The insurers argued that the "rules" and "regulations" referenced in the definition should be understood to refer to federal securities laws and state Blue Sky laws. By contrast, Verizon argued that the insurers' interpretation was too narrow and the word "rule" should be read to encompass judicial rules of law or common law rules that "must be followed to properly engage in a securities transaction." The Superior Court held that the definition of "Securities Claim" was ambiguous, and that the doctrine of *contra proferentem* required it to adopt Verizon's interpretation of "Securities Claim." As it stated: "Nothing in the policies' definitions of securities claims purports to exclude common-law rules or to limit coverage to only those claims alleging violations of enumerated state or federal securities statutes and regulations." *Verizon Commc'ns Inc. v. Illinois Nat'l Ins. Co.*, No. CVN14C06048WCCCCLD, 2017 WL 1149118, at *10 (Del. Super. Ct. Mar. 2, 2017).

On appeal, the Delaware Supreme Court disagreed and reversed. The Supreme Court determined that the "Securities Claim" definition was unambiguous and the Trustee's action did not assert a "Securities Claim" within the meaning of the policies. *See In re Verizon Ins. Coverage Appeals*, 222 A.3d at 580. The Supreme Court concluded that "regulations, rules, or statutes," as used in the definition of "Securities Claim" "must be directed specifically towards securities laws for 'regulating securities' to have meaning." *Id.* at 575. The Supreme Court also observed that none of the legal causes of action in the trustee suit were "specifically directed" towards securities laws or even necessarily involved securities. The Supreme Court rejected Verizon's argument that the "Securities Claim" definition encompassed claims for any unlawful conduct committed during a securities-related transaction, finding that Verizon's interpretation would cast "too broad a net." *Id.* at 579. It therefore held that Verizon was not entitled to coverage for its defense costs. The Supreme Court reversed and ordered the Superior Court to enter judgment in favor of the insurers. In November 2019, the court denied Verizon's request for a rehearing.

V. Related Wrongful Acts and Related Claims Issues

The Delaware Superior Court recently has adopted an interpretation of common wording in D&O Policies regarding "Related Wrongful Acts" that differs significantly from other jurisdictions. In interpreting policy language regarding whether Wrongful Acts and Claims are related and the application of the Prior Notice and Prior and Pending Litigation exclusions, the Delaware Superior Court requires a showing that claims are "fundamentally identical" in order to be considered related. *See Pfizer*, *Inc. v Arch Ins. Co.*, No. N18C-01-310, 2019 Del. Super. LEXIS 345, 2019 WL 3306043 (Del. Super. Ct. July 23, 2019).

The underlying lawsuit in *Pfizer* was a securities class action captioned *Morabito v. Pfizer, Inc.* Pfizer's D&O insurer denied coverage for the *Morabito* suit based on two exclusions: (1) a "Related Wrongful Acts" exclusion that excluded coverage for Claims "alleging, arising out of, based upon or attributable to the facts alleged, or to the same or related Wrongful Acts alleged or contained in any Claim which has been reported . . ." under a prior policy; and (2) two "Specific Litigation Exclusions" that excluded coverage for Claims "alleging, arising out of, based upon, attributable, or in any way related directly or indirectly" to the underlying facts, circumstances, acts or omissions alleged in an earlier lawsuit captioned *Garber v. Pharmacia*, and Interrelated Wrongful Acts. *Id*. at *5-*6. The insurer argued that there was no coverage for the *Morabito* suit because it was related to the *Garber* suit, which had been brought during a prior policy period.

In interpreting the policies, the *Pfizer* court cited *United Westlabs, Inc. v. Greenwich Ins. Co.*, No. 09C-12-048, 2011 WL 2623932 (Del. Super. Ct. July 1, 2011), which the court stated examined an "indistinguishable" definition of Interrelated Wrongful Acts. In *United Westlabs*, the court initially stated that it need not determine whether Delaware or California law governed the policy, because the laws between the two states did not differ. The court then rejected the insured's argument that two sets of wrongful acts were unrelated because they were based on separate injuries and events and separated over two year time period. As a factual matter, the court found that the two sets of wrongful acts in that case were "fundamentally identical" for the purpose of holding (in the insurer's favor) that the matters were considered a single claim in the same policy period because they involved the same subject and common facts, circumstances, transactions, events and occurrences, notwithstanding the addition of other parties to the later filed counterclaim. *Id.* at *11.

In a footnote, the *Pfizer* court also cited *Medical Depot, Inc. v. RSUI Indem. Co.*, No. N18C-01-310, 2016 WL 5539879 (Del. Super. Ct. Sept. 29, 2016). *Id.* at *9 & n. 82. In *Medical Depot*, the court held that two actions were not related and therefore not considered a single Claim, where one was an individual wrongful death and products liability case for injuries caused by a body sling, and the second was a class action under California's unfair trade practices statute seeking redress for having purchased the sling, but did not allege physical injury. Without citation, the court stated that the two suits were not "fundamentally identical" and therefore the class action did not relate back to the personal injury suit.

Based on these precedents, the *Pfizer* court more broadly held that under Delaware law, "similar 'relatedness' or 'arising out of' policy language is interpreted as precluding coverage only where two underlying actions are 'fundamentally identical." *Id.* at *7. *See also id.* at *9. It then concluded that the *Morabito* and *Garber* suits were not "fundamentally identical." Although the suits shared some similarities, the court found there were notable differences. First, although both were securities fraud class actions, the *Morabito* suit was brought by the shareholders of Pfizer and the Garber suit was brought by shareholders of Pharmacia before it was acquired by Pfizer. Second, although both suits alleged that the defendant had made false representations and omissions regarding health risks allegedly caused by the drug Celebrex, the *Morabito* suit involved alleged cardiovascular risks and the *Garber* suit involved gastrointestinal risks. *See id*. at *10. Additionally, the *Morabito* suit alleged false representations regarding a second drug, Bextra. *See id*. As the court concluded, "[i]n short, while there may be some thematic similarities, the Underlying Actions are truly, in all relevant respects, different." *Id*. at *10. In so ruling, the court found significant that these suits "involved entirely distinct misrepresentations of very different health risks associated with Celebrex." *Id*.

A year later, the *Pfizer* court issued a second decision, applying the "fundamentally identical" standard to a prior notice exclusion. *See Pfizer, Inc. v. U.S. Specialty Ins. Co.*, No. N18C-01-310, 2020 WL 5088075 (Del. Super. Ct. August 28, 2020). Based on its earlier decision, the court held that the prior notice exclusion did not apply because the *Morabito* and *Garber* actions were not "fundamentally identical."

VI. Allocation and the Larger Settlement Rule

The *Arch v. Murdock* court issued yet another controversial decision just before the case was finally settled in 2020, in this instance on allocation. For purposes of trial, the D&O insurers argued that the Dole Settlement would have to be allocated in accordance with the primary policy's allocation clause. Among other things, they asserted, defense cost payments had been made by underlying insurers for uninsured defendants, and there were insurable capacity issues with respect to Murdock and the other defendants in the Chancery Court Decision. *See* Transcript of Oral Argument, *Arch Ins. Co. v. Murdock*, No. N16C-01-104 (Del. Super Ct. Aug. 27, 2019). The primary policy contained the following allocation clause:

> If in any Claim, the Insureds who are afforded coverage for such Claim incur Loss jointly with others (including other Insureds) who are not afforded coverage for such Claim, or incur an amount consisting of both Loss covered by this Policy and loss not covered by this Policy because such Claim includes both covered and uncovered matters, then the Insureds and the Insurer agree to use their best efforts to determine a fair and proper allocation of covered Loss. The Insurer's obligation shall relate only to those sums allocated to matters and Insureds which are afforded coverage. In making such determination, the parties shall take into account the relative legal and financial exposures of the Insureds in connection with the defense and/or settlement of the Claim.

See Arch Ins. Co. v. Murdock, No. N16C-01-104, 2020 Del. Super. LEXIS 156, at *6-7 (Super. Ct. Jan. 17, 2020) ("*Arch v. Murdock IV*").

The insureds, on the other hand, sought a summary judgment ruling that any allocation of Loss under the D&O policies would be governed by the "larger settlement rule," and that the insurers would be unable to establish that any uncovered liability had increased the amount of the Dole Settlement. *See Arch v. Murdock IV*, 2020 Del. Super. LEXIS 156, at *12-*13.

The court granted the insureds' motion to apply the larger settlement rule, finding that the Allocation Clause did not apply to the circumstances of the Dole Settlement.

Judge Davis first acknowledged that no Delaware court had ever applied the rule. *See id*. at *18. He cited cases from the Ninth and Seventh Circuits as the source of the rule: *Safeway Stores, Inc. v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, 64 F.3d 1282, 1287 (9th Cir. 1995); *Nordstrom, Inc. v. Chubb & Sons, Inc*., 54 F.3d 1424, 1433 (9th Cir. 1995); *Caterpillar, Inc. v. Great Am. Ins. Co.*, 62 F.3d 955 (7th Cir. 1995); and *Harbor Ins. Co. v. Continental Bank Corp.*, 922 F.2d 357, 368 (7th Cir. 1990). *Id*. *17-18. The judge observed that the rationale for the rule, as he perceived it, was consistent with the coverage provided by the primary D&O policy, which when read "as a whole" was intended to provide the insured with "a complete indemnity for Loss regardless of who else might be at fault for similar actions." *Id.* at *18-19.

The court analyzed the Dole allocation clause but read the "relative legal and financial exposures" standard to apply only in the specific context of the insurers' and insureds' agreement "to use their best efforts to determine a fair and proper allocation of covered Loss." The court read the provision to mean that if the parties were unable to agree on allocation despite those efforts, the stated standard would no longer apply and the larger settlement rule would take over. *See id*. at *20-21. The insurers would not be deprived of their "economic deal" under the policy, the court reasoned, because they would still have the protection of subrogation. *Id.* at *21.

The *Arch v. Murdock IV* decision is troubling for D&O insurers, as it arguably renders clauses like the Dole allocation clause meaningless. The larger settlement rule developed at a time when D&O policies did not include an allocation requirement. The rule was viewed as largely favorable to insureds, and insurers adopted allocation clauses to provide for specific standards like relative exposure. *See* 23-146 Appleman on Insurance Law & Practice Archive § 146.5[E][1]. If *Arch v. Murdock IV* stands as good law in Delaware, the ability of the parties to reach agreement on allocation between covered and uncovered loss will be negatively impacted.

The larger settlement decision in *Arch v. Murdock IV* is under appeal in *RSUI Indemnity Company v. David H. Murdock, et al.*, No. 154,2020, in the Supreme Court of Delaware.