



Issue 16

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### In this issue . . .

We look at Side-A Only Coverage for Directors and Officers Liability Insurance.

### The D&O Policy: A Quick Refresher

The standard D&O policy has two coverage parts, Side-A and Side-B. Side-A covers the Directors and Officers individually, while Side-B reimburses the company for money it has paid to or on behalf of its Directors and Officers to indemnify them for damages they may be liable for as a result of alleged wrongful acts. This somewhat circuitous arrangement is because most corporate by-laws require such indemnification. Accordingly, most D&O claims are paid under the corporate reimbursement section. This is why Side-A retentions are usually minimal and Side-B retentions are much more substantial.

So why have a "Side-A" coverage part if, in most cases, the company indemnifies the Directors and Officers? In the event that the company is unable to or is prevented from, making a reimbursement, Side-A is necessary. Inability to pay might be caused by corporate bankruptcy; an example that might cause prevention is a shareholder derivative lawsuit whereby shareholders sue the Directors and Officers on behalf of the company. Most states prohibit corporate indemnification for this type of action.

### What is Side-A Only Coverage?

It is a separate policy that covers only the Directors and Officers. There is no Side-B corporate reim-

bursement. It is also called "non-indemnifiable acts" coverage.

### Isn't That What Side-A is for in a Standard Policy?

Yes, but there are at least two potential problems that the standard two-part policy is not equipped to handle. The first involves corporate bankruptcy, where the judicial waters are very muddy. Some bankruptcy courts have taken the position that the mere presence of Side-B coverage in a D&O policy is enough to make the policy a potential asset of the bankruptcy estate, and so they have "frozen" the whole policy, including Side-A coverage. And if entity coverage has been added to the policy it is very likely that this will happen. Freezing the whole policy puts it out of the reach of the D&Os just when they may need it most.

The second problem is one of (unforeseen) limit exhaustion. For example, adding entity coverage or Employment Practices Liability (EPL) to a D&O policy may put added pressure on the limit. A bad EPL claim could wipe out the insurance program, leaving the D&Os with nothing to protect them. Also, if a derivative suit is filed in tandem with a class action lawsuit and the class action claim is settled first, there may not be enough limit left to pay for the derivative suit.

### Note To Readers

*We have just updated our mailing list, however this is a continuous process. If you (i) saw this newsletter but do not receive your own copy and would like to, (ii) know of someone who would like to receive a copy, or (iii) know of someone who should be taken off the list, please let us know at [info@cug.com](mailto:info@cug.com) Thank You.*

## Side-A Only Solution?

In both these situations, having a Side-A Only policy in an excess / DIC\* position would be very helpful. Side-A Only policies should be outside the reach of even the most creative bankruptcy courts. These policies would be largely unaffected by EPL claim complications, and would be there to respond to a derivative claim following a class action pay-out by the standard two-part insurance program.

The loss scenarios described may be remote, and buying a Side-A Only policy may provide more protection than is deemed necessary. But it is worth considering.

- ◆ If you have any questions on Side-A Only policies, please contact any of our D&O underwriters.
- ◆ The next edition of "Prior & Pending" will look at some of the issues when the scope of the D&O policy is expanded. If you would like a copy, please contact [info@cug.com](mailto:info@cug.com)
- ◆ Visit our web site at [www.cug.com](http://www.cug.com) for our forms and applications and more information about our company.

\* *Difference in Conditions. In this context it means that the Side-A Only policy would not only sit over the standard policies to respond to excess claims, but would drop down to become primary coverage for Side-A claims if the standard two-part policies did not or could not respond.*

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