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Is Your D&O Insurance the Strongest?

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The Tenth Circuit Court of Appeals recently affirmed a decision finding that MusclePharm and its board of directors did not have coverage under their D&O policy for legal expenses incurred in responding to an informal SEC investigation. Unfortunately, MusclePharm failed to procure readily available coverage in the D&O insurance market that would have provided protection for just this circumstance.

MusclePharm sought coverage of more than \$3 million in legal fees incurred responding to the SEC investigation. MusclePharm then appealed the Colorado district court's grant of summary judgment in favor of the insurer to the Tenth Circuit Court of Appeals. On October 17, 2017, the Court of Appeals upheld the district court's finding of no coverage in *MusclePharm Corp. v. Liberty Ins. Underwriters, Inc.*, 2017 WL 4675701 (10th Cir. 2017). The district court had found that the D&O policy at issue did not provide coverage for certain "informal" regulatory investigation expenses, such as when the SEC issues subpoenas to individuals for production of documents or depositions.

The D&O policy was purchased in 2013, and contained a relatively restrictive definition of "claim" that covered "formal investigation" defense expenses only after the SEC issued a "Wells Notice," which alerts a company "that the SEC's Enforcement Division is close to recommending to the full Commission an action against the recipient and provides the recipient the opportunity to set forth his version of the law or facts." *Id.*, n.3. Prior to receiving the Wells Notice, the SEC issued no less than 21 subpoenas demanding documents and requesting depositions of various executives and board members, which may seem like a "formal investigation" to many.

Take-away

The D&O insurance market has been "soft" since at least the early 2000s creating vigorous competition among insurers and resulting in steady premiums, high liability limits, flexible terms and provisions, and an overabundance of underwriters. Consequently, D&O insurers have had to enhance their coverages to attract policyholders. Part of the enhanced coverage routinely offered includes expanded "claim" definitions that cover payment of defense expenses associated with "informal" regulatory investigations.

Organizations should take the time to review their D&O programs at each policy renewal to ensure they are obtaining the best available coverage in the market. Relying on brokers alone is not enough; many brokers specifically disclaim any responsibility for providing recommendations that

could be viewed as legal advice. If your organization has not reviewed the scope of coverage provided by your current D&O policy or evaluated the many options available in today's D&O market, your company and your board members could be left with feeble protection.

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