

SIDE-A COVERAGE FOR PRIVATE COMPANIES AND NON-PROFIT ORGANIZATIONS



Directors and officers (D&O) litigation against private and non-profit organizations has increased 450% in the past decade – raising serious consequences for their directors and officers.

As the reality of today's litigation environment has come into greater focus, many private company directors and officers have been seeking coverage once considered solely the domain of public company executives: Side-A Excess D&O Insurance, with Difference In Conditions (DIC) coverage.

In an era marked by higher volume and increased severity of claims, the primary D&O policy limits at private companies may be spread too thin. After protecting the company's balance sheet in litigation, there may not be ample coverage left for individual directors and officers.

DRIVING FORCES

What's moved the needle so dramatically in D&O litigation against private companies? Claims emanate from many sources, but three have proven especially potent:

- Tightened regulations and stricter enforcement
- Financial distress/bankruptcy
- Mergers and acquisitions



Coverage Highlights

Side-A Excess D&O Insurance supplements the company's D&O insurance program with coverage dedicated solely to individual directors and officers.

Side-A SelectSM, our market-leading, lead Side-A DIC insurance offering, provides a number of benefits to meet today's challenges, including:

- **Re-defined critical policy terms and conditions** to make broad Side-A cover more explicit, and bolstering DIC triggers to include "if for any reason" in addition to an enumerated list
- **Optional enhancements** highlighted on the declarations page, including multinational capabilities, Side-A Match Edge[®] (SAME), and:
 - **Per Claim Limit structure:** alternative structure to reinstatements to best leverage AIG's claims expertise
 - **Dedicated Individual Limits:** depending on number of board members included, typically available at \$1 million additional limit per director (inside and outside) of the company (additional premium applies) that provides separate personal liability protection above entire Side-A tower
 - **Updated pre-claim inquiry cover:** based on when the Pre-Claim Inquiry is "reported," not when it is "received," and eliminates (in response to the Yates Memo) a requirement that the organization's inquiry has to be in response to an enforcement body investigation or part of the organization's derivative investigation
- **One exclusion:** improved conduct exclusion—a "for" exclusion rather than absolute, defense costs carveback, independent director carveback to fraud exclusion, and "portion of Loss" and "the underlying action" wording; no pollution or BI/PD exclusion
- **Broadened definition of loss:** with tax liability cover for taxes assessed against the organization for which a director or officer is legally liable; no clean-up costs limitations regarding pollution liability
- **Broader civil fines and penalties cover:** with affirmation that if a fine or penalty cannot be determined as civil or criminal, such fine or penalty will be treated as civil until a contrary determination is made
- **Defense costs definition amendment** so that a director or officer can engage their own counsel without demonstrating need based on conflict of interest
- **Expanded plaintiff attorney fees cover,** beyond non-monetary settlements to also cover if awarded solely against a director or officer, or if the named entity is financially insolvent and directors and/or officers are held personally liable due to judicial award or court-approved settlement

Claims Scenarios



Financial Insolvency Leads to Non-Indemnifiable Loss For Executives

A bankruptcy trustee filed action against the board of directors and insured executives of an energy company, alleging improper transfer of nearly \$100 million prior to the company's insolvency. The trustee alleged fraud against several of the defendants arising out of their participation in the transfer of the funds and alleged negligence and breach of fiduciary duty against the remaining defendants arising out of their failure to prevent the transfer.

Coverage under the Side-A policy was triggered given that the company's underlying \$10 million in ABC policy limits were exhausted by numerous legal actions and the organization's inability to indemnify the defendants due to its insolvency. The entire \$5 million Side-A policy limit was exhausted through defense and settlement payments.



Minority Investor Claim Triggers Insured vs. Insured Exclusion

An early investor in a Silicon Valley start-up company filed suit against the company's former CEO for fraud and breach of fiduciary duty arising out of the defendant's alleged gross mismanagement of the company. Based on the nature of the allegations in the complaint, the company refused to indemnify its former CEO. The claim was submitted to the primary ABC carrier, but the plaintiff in this case held a board seat at the company and qualified as an insured under this policy, triggering the Insured vs. Insured exclusion. The claim was ultimately covered under the Side-A policy based on the DIC feature in the form, with total loss exceeding \$3 million.



Professional Services Exclusion Triggers Difference in Conditions Provision

A former insured executive of a consulting company was alleged to have engaged in a scheme to defraud and obtain money and property through false and fraudulent conduct, including the issuance of false invoices for professional services rendered. A federal criminal indictment was served against the executive.

The claim was submitted to the company's ABC carrier, but coverage was not available under this policy based upon the professional services exclusion in that form. Given the basis of the denial under the primary policy, coupled with the company's refusal to indemnify the executive, the Side-A policy dropped down to pay the executive's defense costs based on the DIC feature in the form. Total defense costs incurred exceeded \$2 million.



Reputational Issues Lead to Non-Profit Organization's Refusal to Indemnify Officials Implicated in Scandal

Senior executives at a large non-profit organization were indicted for their alleged roles in a criminal conspiracy involving the misuse of federal funds. Based on the criminal nature of these allegations, the non-profit organization refused to indemnify these executives and the organization did not purchase sufficient limits on their primary D&O tower to cover all of the legal fees incurred in the defense of the criminal cases. These fees were covered under the Side-A policy, with total incurred loss in excess of \$2 million.

For more information on Side-A coverage for private companies and non-profit organizations, please contact your underwriter or Keith Freid at keith.freid@aig.com.

The scenarios described herein are offered only as examples. Coverage depends on the actual facts of each case and the terms, conditions and exclusions of each individual policy. Anyone interested in the above product(s) should request a copy of the policy itself for a description of the scope and limitations of coverage.

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