

# Cover me in fraud: Delaware Supreme Court finds fraud is insurable

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MARCH 18, 2021

The Delaware Supreme Court has held that fraudulent conduct by corporate officers and directors is insurable in Delaware. This consequential decision, *RSUI Indemnity Company v. Murdock*, No. 154, 2020, 2021 WL 803867 (Del. Mar. 3, 2021), is inconsistent with the public policy of many other states, and likely will have an immediate effect on Delaware-based corporations involved in litigation and the plaintiffs suing them.

## THE INSURANCE POLICY

Dole Food Company Inc. (“Dole”) and its directors and officers were insureds under a corporate liability insurance policy, with secondary insurers, including RSUI Indemnity Company (“RSUI”), providing excess coverage. The policy had an expansive definition of covered losses, which on its face did not exclude all losses occasioned by fraud.

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The insurers agreed to “pay on behalf of the Insured Individual all Loss ... arising from any Claim for a Wrongful Act first made against ... such Insured Individual ... [and] pay on behalf of the Policyholder all Loss arising from any Securities Claim first made against the Policyholder for a Wrongful Act.”

“Wrongful Act” was defined in the policy to include “actual or alleged error, misstatement, misleading statement, act, omission, neglect or breach of duty.” And “Loss means all monetary amounts which the Insureds become legally entitled to pay on account of a Claim, including damages, settlement amounts and judgments ... [and] Defense Costs.”

While the policy excluded losses “based upon, arising out of or attributable to ... any deliberately ... fraudulent act,” the policy required that this determination of fraud be “established by a final

and non-appealable adjudication adverse to such Insured in the underlying action.”

## THE FRAUD

David H. Murdock, a director of Dole and its chief executive officer, took the company private years ago in a transaction where Mr. Murdock acquired all of Dole’s stock not already owned by him, and cashed out the Dole stockholders.

Two state court shareholder lawsuits subsequently were filed and consolidated against Dole, Mr. Murdock and C. Michael Carter, the company’s president, chief operating officer and general counsel — a plenary action and an appraisal proceeding — alleging, among other claims, that the defendants manipulated the value of Dole’s stock and breached their fiduciary duties owed to shareholders in connection with the merger.

A federal securities class action later was filed against Dole, Mr. Murdock and Mr. Carter, predicated upon alleged violations of the Securities Exchange Act.

The Delaware Court of Chancery, presiding over the consolidated state court actions, conducted a nine-day trial and determined that Mr. Carter had “engaged in fraud” and “intentionally tried to mislead the [Special] Committee for Murdock’s benefit,” and that Mr. Murdock also “engaged in fraud” and had “breached his duty of loyalty by orchestrating an unfair, self-interested transaction.”

The court concluded that “Murdock and Carter’s ... efforts to drive down the market price and their fraud during the negotiations reduced the ultimate deal price by 16.9%” and found the two jointly and severally liable for \$148,190,590.18 — or \$2.74 per share — in damages.

Dole and its officers and directors thereafter settled all three litigations with the shareholders, including the federal securities case. Certain of the excess policy insurers, including RSUI, filed suit seeking a declaratory judgment that they had no obligation to fund the settlement.

Dole and Mr. Murdock counterclaimed and sought to enforce the insurance policy up to its full policy limits. All of the plaintiff excess policy insurers, except for RSUI, voluntarily dismissed their claims.

## THE DECISION

In the *Dole* decision, a landmark ruling, the highest court in Delaware held that Delaware public policy does not prohibit Delaware corporations from securing insurance for directors and officers in order to cover breach of loyalty claims based on corporate fraud.

The Court grounded its decision on Delaware statutory authority (8 Del. C. § 145) authorizing corporations to purchase insurance “against any liability” asserted against their directors and officers “whether or not the corporation would have the power to indemnify such person against such liability under this section.”

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This statute also permits corporations to indemnify their directors and officers for expenses incurred if the person “acted in good faith and in a manner the person reasonably believed to be in or not opposed to the best interests of the corporation ...” Read together, the Court observed that Delaware corporations have the authority to obtain directors and officers insurance for liabilities arising from bad-faith conduct.

In so holding, the Supreme Court of Delaware reaffirmed “the right of sophisticated parties to enter into insurance contracts as they deem fit ‘in the absence of clear indicia that ... [a countervailing public] policy exists,’” and rejected RSU’s argument that insurance coverage should not be available for intentional wrongdoing.

The Court stated that the well-established common law principle, that an insured should not be allowed to profit from the consequences of her own wrongdoing, is inapplicable where there is no contrary public policy or where, as here, the public policy weighs in favor of the insurability of losses caused by breach of the duty of loyalty and fraud.

The Court found that the allegations of fraud in the underlying litigation “fit comfortably” within the terms of the liability policy and the scope of coverage, particularly since the litigants settled prior to the determination of fraud being “established by a final and non-appealable adjudication.” The Court accordingly affirmed the judgment in favor of *Dole* and the individual defendants.

## TAKEAWAYS

Delaware courts long have been friendly to corporations organized under Delaware law, and the *Dole* decision is certainly corporation-friendly. Although *Dole* was based in California and the insurance policy was issued there, the Court based its decision on Delaware law, where *Dole* was organized. California law would have been much less hospitable to *Dole* than the Delaware Supreme Court’s interpretation of Delaware law.

The decision emphasized that the policy exclusion regarding fraud required a final and unappealable order, meaning that settlements were covered. The result provides incentives for parties to settle and adds to the risk of litigating to the highest appellate court. The decision should make it more difficult for insurers to refuse to cover litigation expenses or to stay uninvolved in settlement negotiations or mediations.

A blanket prohibition against insuring for losses arising from false or misleading representations or breaches of the duty of loyalty by a corporation’s directors and officers (even when based on fraud) could potentially leave injured plaintiffs and other victims without a means of recovery.

In addition to greatly benefiting Delaware-organized companies, the *Dole* decision helps plaintiffs seeking fraud-based damages from Delaware corporations, to the extent insurance coverage is implicated, as there is now greater assurance that judgments can be satisfied by deep-pocketed insurance companies.

The decision also suggests that insurance companies will be compelled to defend and cover fraudulent conveyance actions and judgments involving Delaware companies in the bankruptcy context, including actions based on actual intent fraudulent conveyance.

Given the Court’s stated rationale, and the decision’s reliance on the specific terms of the insurance policy at issue, there is little reason to believe that this decision will be extended to cases not involving directors and officers or to fraud disputes governed by the law of other states.

Additionally, insurance companies may revise the fraud exclusions in their future policies in order to circumvent the *Dole* ruling. Nevertheless, there are countless insurance liability policies in place now, and the *Dole* decision is very important and will have a meaningful impact on these policies, Delaware companies and the litigants suing them.

*This article was published on Westlaw Today on March 18, 2021.*

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