

# Insights

## **Q & A on Directors & Officers Insurance: Coverage for Liability due to COVID-19**

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The coronavirus of 2019 (COVID-19) has affected all businesses in one way or another. For public and privately held companies, a big question arises: what liability does the company have? If an employee, customer, shareholder, or third-party sues the company or the company's officers and directors because of COVID-19, who is responsible, and will the Directors & Officers (D & O) insurance cover the claim?

### **What does a D & O insurance policy generally cover?**

A company's D & O insurance policy protects the business's management personnel, such as members of the company's board of directors, the company's executive management team, and its officers, from claims related to or arising from the decisions they make while fulfilling their duties to the company.

### **What types of claims fall under a D & O insurance policy?**

Generally, when an action is brought against a company's management personnel, officers, or directors, or the claim most often arises from either negligence or breach of fiduciary duties, specifically breach of the duty of care, owed to the company. A negligence claim usually alleges that someone failed to act when there was a duty to act or acted in a manner inconsistent with the duty of care owed.

Officers and directors owe fiduciary duties to the company, and usually to one another, to act, fairly, honestly, and openly, and to exercise their business judgment in the best interests of the company. The duties of care and loyalty mean the officer or director must put company interests ahead of personal interests. Officers and directors also owe a duty to follow applicable laws when acting for the company. Some states define these fiduciary duties more or less broadly.

In addition, each D & O insurance policy differs. It is important to review the specifics of the policy. Some policies are broadly stated, and some will have specific exclusions for particular situations.

### **Why are claims for breach of fiduciary duties brought against a company's management personnel?**

Directors and officers of a company owe the company fiduciary duties such as the duty of loyalty and the duty of care. In the context of COVID-19, a claim for breach of fiduciary duty would most likely arise from a director's or officer's breach of the duty of care owed to the company. For example, decisions a company makes about how to conduct its business, whether close the business, and so on must be made with these duties in mind.

## **What does it mean to exercise business judgment?**

Exercising business judgment means making a decision for the business in good faith and the degree of care that a reasonable person would use in similar circumstances. In a case alleging negligence or breach of fiduciary duty related to COVID-19, a court might look at the decisions that directors and officers made with regard to continuing or ceasing business operations, altering business operations, entering into contracts, or implementing extra precautions. The court would examine the decision-making process and whether management, officers, or directors acted reasonably, in good faith, and in the best interests of the company.

## **How can directors and officers demonstrate business judgment?**

Directors and officers of a company can demonstrate that they exercised good business judgment in a variety of ways:

- Hold a meeting (including virtual or telephonic meetings). A specially called meeting of the board of directors should follow the requirements for special meetings. If the company does not have provisions in its bylaws or operating agreement for virtual meetings or actions by written resolutions, it should adopt them as soon as possible.
- Meetings should have minutes that provide some detail about the information considered and the action taken.
- A company should develop and implement a written response plan with senior management, officers and directors. The board should consider and approve the plan and clearly delegate responsibility for implementing the plan.
- The board of directors should monitor the company's situation and response plan, and make adjustments as the situation warrants, considering the current situation and applicable national, state and local requirements.
- The board should consider whether company policies and procedures need to be altered (even on a temporary basis), and communicate changes to management personnel, employees and other stakeholders as appropriate.
- A company should consider designating one person as the COVID-19 point of contact, and direct inquiries to and responses through this person. Good crisis management techniques should be applied.

There are many ways for senior managers, directors and officers to demonstrate that a business decision was made after they exercised their business judgment. Where it is clear a decision was made, and the company can demonstrate how it reached that decision and acted based on that decision, D & O insurance will generally cover negligence or breach of fiduciary duties claims. Courts most often defer to the business judgment of a company's officers, directors and senior management, when it is shown that business judgment was used and applied reasonably under the circumstances.

## **When will D & O insurance not cover a negligence or breach of fiduciary duty claim?**

D & O insurance is meant to protect directors and officers of a company from the business decisions they make as situations arise. The reason for this is that directors and officers of companies have to make difficult business decisions, which often must be made quickly.



That is exactly what has occurred with COVID-19 and its rapid spread. D & O insurance will generally cover the decisions directors and officers make during this public health emergency to protect those directors and officers who exercise sound business judgment.

Neither insurance companies nor courts expect companies or those who act for them to respond perfectly. Looking back at decisions through the lens of 20/20 hindsight is not the test of whether good business judgment was exercised. But where a company's directors and officers fail to make a business decision and fail to exercise their business judgment in good faith or act unreasonably, courts may hold them accountable and the D & O policy may not provide coverage for the claim.

If you have any questions about your D & O insurance policy, or business decisions related to COVID-19, please contact **Judy L. Woods** or any other member of the **Krieg Devault LLP Litigation Team**.