

Mother's Participation in Lawsuit As Insured Person Sinks Daughters' Claims

Coverage for a lawsuit brought by an Insured Person, a former Director of the defendant company, and non-Insureds, her daughters, was barred by the Insured v. Insured exclusion of a D&O Policy in a recent ruling by the Eighth Circuit, *Jerry's Enterprises, Inc. v. U.S. Specialty Ins. Co.*, No. 15-3324, 2017 WL 104468 (8th Cir. Jan. 11, 2017).

Jerry Paulson founded Jerry's Enterprises, Inc. ("JEI"), a chain of grocery stores operating in Minnesota, Wisconsin and Florida. He gifted shares in JEI to his three daughters, including Cheryl Sullivan, and to his grandchildren, including Sullivan's daughters Kelly and Monica. Upon his death in 2013, Paulson's estate plan appointed his daughters to the JEI Board of Directors. Under the plan, they would remain as directors until such time as their shares and the shares of his grandchildren were redeemed. Sullivan served as a director for approximately four months, during which time she raised concerns with the directors of JEI regarding the valuation of her shares. Shortly after cashing out her shares, she and her daughters sued JEI, claiming they were forced to redeem their shares for less than they were worth.

The D&O policy issued to JEI included an IvI exclusion precluding from coverage any Claim that is "brought by or on behalf of, or in the name or right of . . . any Insured Person, unless such Claim is: (1) brought and maintained independently of, and without the solicitation, assistance or active participation of, the Insured Organization or any Insured Person . . ." Insured Person included "any past, present, or future director, officer, managing member, officer or Employee of the Insured

Organization," and Claim was defined as "any civil proceeding commenced by service of a complaint or similar pleading."

The policy also included an allocation provision which specified that:

If Loss covered by this Policy and loss not covered by this Policy are both incurred in connection with a single Claim, either because the Claim includes both covered and uncovered matters, or because the Claim is made both against Insureds and against others not included within the definition of Insured, the Insureds and the Insurer agree to use their best efforts to determine a fair and proper allocation of all such amounts

The insurer denied coverage based on the IvI exclusion. In the subsequent coverage litigation, the district court judge granted the insurer summary judgment based on the exclusion. On appeal, JEI conceded that Cheryl Sullivan was an Insured Person due to her status as a past director of JEI. However, the company argued that the founder's granddaughters were never employees, and thus, were not Insured Persons under the policy. So, the court should have applied the allocation provision to allow coverage for the granddaughters' claims.

The Eighth Circuit disagreed, affirming the lower court decision, since the language of the exclusion did not leave room "to apply the clause to some parts of a lawsuit but not others." Furthermore, the Eighth Circuit noted that all of the claims in

the lawsuit were brought by all three plaintiffs jointly; meaning Sullivan's claims could not be separated from her daughters'. While acknowledging that tension existed between the lvi Exclusion and the allocation provision, the court concluded "loss associated with the Sullivan lawsuit is not covered under the insurance policy due to the presence of a former director – Sullivan – as an active participant."

Comment:

Policyholder advocates will likely bemoan the Eighth Circuit's refusal to apply the allocation clause, arguing the claims of the Sullivan daughters, who were not insureds under the policy, should not have been barred. However, the court properly applied the maxim of contract law that specific contract language controls over general language. The language of the lvi exclusion spoke specifically to Claims brought with the

participation of Insured Persons, whereas the allocation provision spoke generally to Claims that included both covered and uncovered matters. Insurers should take solace in this decision where the court interpreted the exclusion's language in a straightforward manner and applied the exclusion to the Claim as a whole.

If you have any questions about this Update, please contact the author listed below or the Aronberg Goldgehn attorney with whom you normally consult:

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