

A-SIDE D&O FAQ

1. WHY DO COMPANIES BUY A-SIDE COVERAGE?

Companies buy A-Side Directors & Officers (D&O) coverage to protect their executives against non-indemnifiable claims – claims where the company cannot legally provide protection or is financially unable to do so.

2. IS A-SIDE COVERAGE GENERALLY PURCHASED BY ITSELF OR WITH OTHER D&O COVERAGE?

Typically, A-Side D&O coverage is purchased as part of a larger traditional D&O package, which also includes protection for executives against indemnifiable losses (B-Side cover) and coverage for the company itself (C-Side coverage). A-Side usually sits excess of the other coverages.

3. WHEN MIGHT A COMPANY BE LEGALLY PROHIBITED FROM INDEMNIFYING AN EXECUTIVE?

A company's ability to indemnify or hold harmless its executives is controlled by the law of the state where the company is based or incorporated. This is true whether the company is publicly traded or privately held. State law generally grants a company broad license to indemnify its directors and officers after a threshold test is passed. The typical test requires the company to determine that the individuals acted in good faith and in the best interests of the company at the time they undertook the alleged acts. Most states, however, expressly restrict a company's ability to indemnify its executives for settlements or court awards of derivative claims.

4. WHAT IS A DERIVATIVE CLAIM?

Derivative claims allege breach of fiduciary duty or a conflict of interest by executives. They are usually brought in state court by a current shareholder in the name of the company. They are derived (hence the name) from the right of corporations to seek legal redress through the courts; the individual shareholder bringing suit does so derivatively on behalf of the company. The goal is to return the firm to the condition it would have been in but for the alleged breach or conflict. Settlements or court awards are therefore paid to the company itself. Here's the tricky part: if the company were to indemnify the executives for court awards or settlements that would otherwise go to the company itself, there would be no net gain to the company and the purpose of the suit would be thwarted. (This is sometimes referred to as the potential "circularity problem" in indemnifying executives for derivative claims.)



5. WHAT IS A "BROAD FORM" A-SIDE D&O POLICY? WHAT DOES "DIC" MEAN?

While an A-Side D&O policy provides narrower coverage than the traditional D&O insurance package because it doesn't include B- or C-Side coverage, it generally contains fewer exclusions. Such A-Side protection is referred to as "broad form" coverage. When a company buys the whole package, the A-Side policy usually sits excess of traditional D&O coverage and is often written on a difference-in-conditions (DIC) basis. This allows the A-Side policy to drop down and pay when the traditional policies don't because of their additional exclusions.

6. WHAT ARE DROP-DOWN PROVISIONS? WHEN MIGHT THEY APPLY?

Excess coverage can be written so that it drops down and pays claims that are covered under the excess A-Side policy but not the underlying or lower layers of insurance. This applies when the excess coverage is broader (and is on a DIC basis) but may also apply when an underlying traditional D&O carrier wrongfully denies coverage for a claim or is itself financially unable to pay the claim, or if the firm itself allegedly wrongfully refuses to indemnify its executives.

7. ARE A-SIDE D&O POLICIES LESS LIKELY TO BE TRIGGERED THAN TRADITIONAL D&O POLICIES?

Yes. Most U.S. D&O claims are indemnifiable, which means that they do not trigger A-Side policies. This is why most companies purchase A-Side coverage as additional or excess insurance over a broader D&O program. Note, however, that the ability of a company to indemnify its executives may not be transferrable for executives at international operations and subsidiaries.

8. WHAT ARE THE ECONOMICS OF BUYING A-SIDE D&O COVERAGE? IT'S MUCH CHEAPER, RIGHT?

Unfortunately not. Although the coverage is less likely to be triggered than B- or C-Side coverage, there are generally fewer exclusions and the policy may be written excess on a DIC basis, meaning that it may pay first. In these cases it functions as – and is therefore often priced as if it were – primary coverage.

9. WHICH INSURANCE CARRIERS WRITE SPECIALIZED OR STAND-ALONE A-SIDE D&O COVERAGE?

Most D&O carriers write stand-alone A-Side coverage. As mentioned, the traditional D&O insurance policy includes embedded A-Side coverage, so, technically every standard D&O carrier offers it. However, over the past 10 years, many D&O carriers began to offer a specialized, or stand-alone, A-Side policy as well. Prior to this, such specialized coverage was offered solely by some firms in Bermuda and London.

10. ARE ALL A-SIDE D&O POLICIES THE SAME? ARE ALL A-SIDE D&O INSURANCE CARRIERS ALIKE?

While all A-Side D&O policies provide coverage for non-indemnifiable claims against the company's executives, all policy forms are different: they are not all broad-form or DIC. Perhaps even more importantly, not all D&O carriers have experience handling and paying claims under A-Side D&O policies. Such unfamiliarity could prove costly, leaving executives personally holding the bag in A-Side claims.

For more on A-Side coverage, see our A-Side Purchasing Studies and our ER Alert, "Anatomy of a Derivative Claim" (March 2005).

CONTACTS

Atlanta, GA

Charles Maxell
404 224 5123
charles.maxell@willis.com

Denver, CO

Jim Iacino
303 218 4039
jim.iacino@willis.com

Radnor, PA

Matt Schott
610 254 5642
matt.schott@willis.com

Boston, MA

David Goldstein
617 351 7498
david.goldstein@willis.com

Los Angeles, CA

Chris Crawford
213 607 6294
chris.crawford@willis.com

San Francisco, CA

Michael Mahoney
415 291 1535
mike.mahoney@willis.com

Chicago, IL

Brian Gauen
312 621 4855
brian.gauen@willis.com

New York, NY

Steve Pincus
212 915 7940
steve.pincus@willis.com