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SPECIAL SECTION: FCPA

Yes, Your D&O Policies Cover FCPA Defense

Save your company millions by positioning it to recover insurance proceeds

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You are general counsel of a global manufacturing company and sit down at your desk one morning to find that your company has received letters from the U.S. Department of Justice and the Securities and Exchange Commission. A whistleblower alerted the agencies that improper payments had been made to foreign officials by employees of your company's foreign subsidiary. The agencies are conducting an investigation into whether these payments violate the Foreign Corrupt Practices Act (FCPA) and federal securities laws. The agencies want your company to enter into a tolling agreement and voluntarily produce documents as part of the investigation. They also want to interview various directors and officers of your company.

The steps you take next could save your company and its shareholders millions of dollars by positioning your company to recover insurance proceeds for the costs of responding to the government's inquiries and the follow-on civil litigation that may ensue once news of the FCPA investigation is made public.

First Steps

Initially, provide prompt notice of the FCPA investigation to your D&O insurance company. The best way to give notice is through your insurance broker, who should make sure that all insurance companies that issued insurance policies in all potentially applicable policy periods are put on notice. As part of the notice, the broker should provide copies of the letters you received from the government concerning the FCPA investigation and should work to comply with reasonable requests for information made by your insurance companies.

> ***Put your company in the best position to recover insurance proceeds for the costs of responding to the government's inquiries.***

Government FCPA investigations and follow-on civil litigation can continue for several years. To the extent reasonable, keep the insurance companies informed of defense counsel arrangements and the status of the FCPA investigation and the civil litigation. Provide regular updates of litigation filings to avoid the insurance companies making improper arguments concerning cooperation. Propose that the insurance companies enter into confidentiality agreements to facilitate information sharing, particularly where nonpublic information is at issue. Consider scheduling periodic calls with insurance company representatives to provide status updates concerning civil litigation as well, and to give insurance company representatives the opportunity to ask questions of defense counsel concerning the defense of the litigation pertaining to alleged FCPA violations.

Provide advance notice of potential civil litigation settlements to those insurance companies whose limits may be tapped by a settlement, and invite those insurance companies to attend an upcoming mediation where a settlement might be reached. Your policy may require written consent to enter into a settlement agreement as a condition of coverage, but consent cannot be unreasonably withheld, especially where the insurance company has associated with the policyholder in settlement negotiations.

Also, consider providing your insurance companies with prompt notice of any potential settlements resulting from the government's FCPA inquiry, even though, in reality, the company may have very little choice when it comes to entering into a consent order. Frequently, D&O insurance companies argue that there is no coverage for settlements that involve supposed "disgorgement" of so-called "improperly" obtained profits. While cases have reached differing results, to the extent that anyone other than the organization itself profited from the "improperly" obtained funds addressed by the settlement – for example, if the "improper" profits actually benefitted the organization's customers, as in *J.P. Morgan Sec. Inc. v. Vigilant Ins. Co.*, 21 N.Y.3d 324 (N.Y. 2013) – such amounts should be covered.

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Be Prepared to Provide Defense Invoices

Your primary policy may contain a consent clause concerning defense counsel arrangements for your company and for individual directors and officers. Although it is often the case that several firms are preapproved by the insurance company to represent your company in securities litigation, the insurance company should not withhold consent concerning the reasonable retention of defense counsel for the company or for directors and officers. Bear in mind, however, that insurance companies often improperly challenge the reasonableness of defense counsel's rates.

In civil litigation where both the company and individual directors and officers are named as defendants – or where the company is named as a nominal defendant, as in derivative actions – the individual director or officer should be entitled to retain their own defense counsel separate from the company when there is a potential conflict of interest between the company and an individual director or officer. For example, a potential conflict of interest between the company and individual directors and officers may arise after a motion to dismiss has been denied because the company may be more inclined to pursue any potential claims against the directors and officers at that time.

With respect to an investigation, individual directors and officers who are interviewed or subpoenaed as part of a government FCPA inquiry are entitled to retain their own defense counsel regardless of whether there is a potential conflict of interest. However, it is usually good practice to alert the insurance company to defense counsel retentions so as to keep the insurance company informed.

Be Aware of Coverage Issues

Policyholders frequently find themselves in a difficult position when it comes to disclosing defense counsel's invoices to their insurance companies. Insurance companies often add not-agreed-upon and unreasonable conditions to coverage not found in the insurance policy. Policyholders must be alert to such improper gamesmanship when it comes to the advancement of defense costs.

Defense counsel generally should avoid putting attorney-client privileged information in their invoices, since an aggressive plaintiff's counsel may argue that the attorney-client privilege has been waived when attorney-client communications in defense invoices are disclosed to a D&O insurance company. Plaintiffs have been known to aggressively press this issue even though there are good arguments against the position. For one, it can be argued that an insurance company and its policyholder have a common interest in the defense of the underlying litigation that mitigates waiver of the attorney-client privilege when attorney-client communications in defense-cost invoices are provided to the insurance company. In addition, generally, attorney work product is only waived when it is disclosed to an adversary or a conduit to an adversary.

Ultimately, when the company is facing high-stakes litigation, the possibility of waiver and whether and how to provide invoices to your D&O insurance company must be weighed in the context of the defense.

Obtain Consent For Defense Counsel

Insurance companies often raise several purported coverage issues in the context of a claim for costs pertaining to an FCPA investigation and follow-on civil litigation. Many insurance companies argue over whether notice of an investigation constitutes a "notice of circumstance" that might lead to a "claim" or a "notice of claim" that triggers coverage under the policy. (A "notice of circumstance" can be used to anchor a future "claim" made during a subsequent policy period into an earlier policy period.)

The definition of "claim" or "securities claim" may include any "formal or informal administrative or regulatory proceeding or inquiry commenced by the filing of a notice of charges, formal or informal investigative order or similar document." See *MBIA Inc. v. Federal Ins. Co.*, 652 F. 3d 152, 155 (2d Cir. 2011). By contrast, your policy may define these terms as a more formal "administrative or regulatory proceeding" instituted against the company. See *Office Depot, Inc. v. Nat'l Union Fire Ins. Co.*, 453 Fed. Appx. 871, 875 (11th Cir. 2011). Some policies may contain exclusions for investigations involving only the company.

The scope of coverage for investigation costs in a D&O policy may include an individual director or officer's costs in responding to a government interview request or government subpoena. However, even where the policy purports to exclude the company's costs incurred in responding to an investigation, a portion of the company's costs very likely are "reasonably related" to the representation of its directors and officers, and there is a good argument that any company costs that are "reasonably related" to the representation of individual directors and officers should be covered because they are "reasonably related" to a covered claim.

In the context of an FCPA claim, insurance companies often assert the personal profit or financial advantage exclusion and the deliberate criminal or fraudulent acts exclusion. Many D&O insurance policies require that there be a non-appealable final adjudication in the underlying litigation in order for these exclusions to apply, in which case even settlements do not trigger the exclusion. Thus, although this exclusion may potentially come into play if a case is litigated to a final resolution, the insurance companies must advance defense costs until that time.

Your company will steadfastly and aggressively defend a government inquiry into alleged FCPA violations. Government inquiries often lead to substantial defense costs as well as follow-on civil litigation in the form of shareholder derivative suits and class actions alleging violations of securities laws and breach of fiduciary duty, among other things. Like an investigation, civil litigation can last years and lead to substantial defense costs. A key part of your company's defense strategy should include positioning the company to recover these defense costs from the insurance assets already purchased by your company.