

No Coverage for Lean Buyout Lawsuit: Securities Exclusion Applies to Claims Alleging Improper Share Valuation

A U.S. District Court in Florida showed a limited appetite for a policyholder's attempt to beef up its claim for coverage, and held that a broad policy exclusion bars coverage despite allegations and causes of action not strictly limited to the excluded conduct.

In *Colorado Boxed Beef Co., Inc. v. Evanston Ins. Co.*, No 18-cv-1237, 2019 WL 77376 (M.D. Fla. Jan. 3, 2019), policyholders of a for-profit management liability policy sued seeking coverage for an underlying suit that alleged the directors and officers of the insured company bought company shares through improper means. The underlying suit alleged the D&O's made misrepresentations and omissions of material facts in connection with their purchase of the shares, specifically regarding factors that drove down the stock price.

The policy at issue contained a standard insuring agreement, providing coverage for loss that the insured persons become legally obligated to pay on account of any claim for a wrongful act taking place before or during the policy period. The policy also contained an exclusion precluding coverage for claims based upon, arising out of or in any way involving the actual, alleged or attempted purchase or sale, or offer or solicitation of an offer to purchase or sell, any debt or equity securities (the "Securities Exclusion").

The insurer moved to dismiss based on the Securities Exclusion. The court examined the underlying complaint, which sought to revoke, rescind, or award damages for the sale of company stock to the D&O's. The underlying plaintiffs focused on the misrepresentations and omissions in connection with the D&O's share purchase and included a Stock Purchase Agreement ("SPA") as an exhibit to the underlying complaint. The underlying complaint alleged various misdeeds, such as self-dealing and corporate usurpation, to support causes of actions seeking declaratory, equitable, or legal relief related to the SPA.

The D&O's argued that they were entitled to coverage because the underlying complaint alleged conduct that both preceded and continued after the SPA, and one of the individuals seeking coverage was not party to the SPA. In other words, the D&O's claimed the underlying complaint encompassed more than the purchase and sale of securities, dealing with various alleged corporate fiduciary breaches. They pointed to underlying allegations of self-dealing and usurpation of corporate opportunity to argue that they faced claims for wrongful acts not involving the purchase and sale of securities.

The court rejected the D&O's arguments in full and held that the Securities Exclusion precluded coverage. Rather than form bases for

independent claims, the allegations regarding misconduct outside of the SPA were “part and parcel of the fraudulent inducement and purchase of the (suing) Sellers’ shares in the company.” The allegations that the D&O’s argued constituted wrongful acts not involving securities were “the very acts by which the securities fraud is alleged to have been accomplished.” The possibility that the conduct might create a separate or additional cause of action could not change what the court viewed as the essential nature of the underlying complaint: a scheme to undervalue the company, cheat the sale price, and coerce the underlying plaintiffs into accepting an artificially low value for their shares. Since that was “relating in any way to . . . and arising out of” the stock sale, the court ruled in favor of the insurer.

Comment

Be it scattershot approaches or complaints drafted for audiences beyond the court, extraneous or superlative facts often mire a seemingly straightforward coverage determination. In *Colorado Boxed Beef Co.*, the court declined to recast the underlying

complaint’s fundamental claims. The claimants sought to rescind, reform, or recover damages based on an allegedly fraudulent stock purchase transaction that undervalued a former shareholder’s stake in the company.

The means by which the transaction was fraudulent varied, and very well could have supported additional causes of action for breach of fiduciary duty or other business torts. But the underlying plaintiffs did not go that far. And the court refused to read the underlying lawsuit as something it was not. Instead, it used sound and organized logic to conclude that the exclusion applied because the claim related to, and arose out of, the sale of stock no matter the breadth of the alleged conduct or the possible causes of action that conduct might support

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