

Policyholder wins cover in Canadian D&O case

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Court ruling limits scope of pollution exclusion

TORONTO—The first Canadian appeals court decision to examine how a pollution exclusion in a directors and officers policy applies to a securities claim has gone firmly in favor of the policyholder. Risk managers, though, must be vigilant, as insurers responding to the decision are expected to tighten their policy language to ensure that pollution exclusions limit coverage as intended.

The coverage dispute in *Boliden Ltd. vs. Liberty Mutual Insurance Co.* began with an April 1998 environmental disaster when a tailings dam collapsed, releasing toxic waste and contaminating the surrounding land at a zinc mine in southern Spain that was owned by a subsidiary of the mining company. Shareholders sued Boliden and its directors and officers in Ontario and British Columbia later that year for alleged misrepresentations in its 1997 initial public offering on the Toronto Stock Exchange.

Boliden, which was based in Toronto and later moved its headquarters to Stockholm, Sweden, advised Liberty Mutual of the securities class actions and sought indemnification under its D&O policy. The insurer, however, denied the claim for any part of the loss, including more than \$3 million in defense costs of the directors and officers, relying on the pollution exclusion in the policy, court papers say.

In April, the Ontario Court of Appeal rejected Liberty Mutual's claim that the pollution exclusion in the D&O policy should be read as excluding all losses arising from a claim that relates to or involves a pollution loss. The court agreed with a lower court's determination that the clause excluded pollution-related losses, not pollution-related claims, and applying the exclusion clause required considering whether the alleged wrongful acts or omissions by the directors and officers gave rise to both pollution losses and nonpollution-related losses.

The Boliden ruling is important because it is the first time a Canadian appeals court has ruled on a D&O policy pollution exclusion in a securities case and helps provide clarity and consistency on D&O coverage issues, said Murn Meyrick, senior vp, corporate counsel for Toronto-based Executive Risk Services Ltd. "It's lovely to have our courts giving us some direction," she said. "This is a well-reasoned decision."

The claim was actually related to securities litigation and clearly was a claim of lost shareholder value, said Patrick Bourk, a Toronto-based senior associate at Integro (Canada) Ltd. responsible for Canadian legal affairs. "That is the real nature of the claim. It just happens to be couched in a pollution-related matter," he said.

The lower court correctly ruled the insurer should indemnify Boliden for 80% of the defense costs under an endorsement to the D&O policy, the Court of Appeal ruled. The motion judge also correctly determined that

Executive Risk Insurance provides coverage for Directors, Officers and Trustee's Liability and Fiduciary Liability on behalf of certain Lloyds of London underwriting syndicates.



the exclusion clause should be strictly and narrowly interpreted against the insurer and any ambiguities should be decided in favor of the policyholder, the court ruled.

"That's a very well-established principle of Canadian insurance law," said Mark Gelowitz, a partner in the litigation department of Osler, Hoskin & Harcourt L.L.P. in Toronto.

The company and lawyers for both parties did not return requests for comment. "We don't comment on matters in active litigation," a Liberty Mutual spokeswoman said in an e-mail.

Although the ruling was a victory for the policyholder, risk managers should read their policies carefully because different wording may have resulted in a different decision, said Brian Rosenbaum, a member of the legal and research practice of the financial services group of Aon Reed Stenhouse Inc. in Toronto.

In the competitive D&O market, many insurers have attempted to distinguish themselves by broadening coverage, brokers and insurers say. The pollution exclusion used to be very broad, but insurers have included securities coverage for directors and officers as the market has softened, they say.

"A lot of insurers in these times, because the market is so competitive, are prepared to offer that, when in the past they wouldn't have," Mr. Bourk said.

In light of the decision, though, insurers are likely to consider tightening their policy language because they may not have anticipated that they granted this type of broad coverage, Ms. Meyrick said.

"The lesson learned by insurance carriers is that they may ultimately clean up that language or try to make it less ambiguous," Mr. Rosenbaum said.

Pollution exclusions featuring the terms "directly or indirectly" likely would be added by insurers to D&O policies with greater frequency, said Eric Dolden, an insurance attorney with Vancouver, British Columbia-based Dolden Wallace Folick L.L.P.

Risk managers "should look very carefully if the word 'indirectly' is used, because it can broaden the potential scope of the exclusions," Mr. Dolden said.

Risk managers should consider negotiating an exception for securities claims related to a pollution incident or purchasing a Side A difference-in-conditions policy to cover such matters when the primary policy will not, Mr. Rosenbaum said. Buyers must decide if they want the enhanced coverage and if they are willing to pay for it, but the soft market makes this a good time to seek the coverage, he said.

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Boliden highlights the value of a DIC policy, which could drop down in situations when the primary insurer denies coverage and could be used to fight a primary insurer, Mr. Bourk said. Risk managers "may take it more under advisement than they have before," he said.

Boliden Ltd. vs. Liberty Mutual Insurance Co., Court of Appeal for Ontario, 2008 ONCA 288, April 17, 2008.

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