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RECHTSANWÄLTE

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D&O insurance

Federal Court of Justice:

„Seriousness“ is no precondition for insured event in D&O insurance

On 13 April 2016, the Federal Court of Justice (“**BGH**”) clarified several long-discussed aspects of the D&O insurance, by two almost identical decisions (IV ZR 304/13 und IV ZR 51/14):

- The insured person (director, manager), against whom its own company asserts a compensation due to breach of duty, may assign the right of recourse vis-à-vis the D&O insurer to the aggrieved company, cf. sec. 108 para. 2 Insurance Contract Act (“**VVG**”).

  Consequently, the aggrieved company asserts a direct claim for compensation against D&O insurers. The liability claim must be examined as part of the assessment of the insurance claim.

- “Seriousness” of the claim of the insured person by the company is no precondition for the insured event under the D&O insurance. Hence, the D&O insurer cannot successfully argue that the aggrieved company has never intended to assert the liability claim against the insured person (director, manager) in court or by way of enforcement measures.

1. FACTS

The facts of the two BGH decisions were as follows:

The manager of a limited liability company breached his company duties. The company then claimed compensation from its manager in writing arising from sec. 43 para. 2 Limited Liability Companies Act. Shortly after the written claim, the manager assigned its indemnification claim against the D&O insurer to the company.

The company claimed compensation from the D&O insurer.

The District Court dismissed the claim at first instance arguing that the agreed Special Terms and Conditions of the policy prohibit the assignment of the indemnification claim by the manager (insured person). The prohibition to assign claims as agreed in the Special Terms and Conditions of the policy does not breach sec. 108 para. 2 VVG and is therefore effective. The aggrieved company is not a "third party" under sec. 108 para. 2 VVG.

On appeal, the Higher Regional Court dismissed the aggrieved company's claim against the D&O insurer based on a different argument: The aggrieved company has never "seriously" claimed compensation from its own manager. Particularly, there had never been the intention to assert the liability claim against the own manager in court or by enforcement measures into the manager's private assets. Hence, there is no liability claim of the aggrieved company against the manager due to lack of "seriousness" of the claim for compensation. Consequently, there is no insurance claim against the D&O insurer.

With the two decisions of 13 April 2016, the Federal Court of Justice clarified that both arguments are incorrect.

2. ASSIGNMENT OF INDEMNIFICATION CLAIM AGAINST D&O INSURER PERMISSIBLE

The company's manager is a "third party" in the meaning of sec. 108 para. 2 Insurance Contract Act. If a D&O-policy exists, the manager (as insured person) may assign its indemnification claim to the aggrieved company. The aggrieved company will then have a direct claim against the D&O-insurer, provided that the liability and the insurance claim exist. The Federal Court of Justice stated that with the new version of sec. 108 para. 2 VVG the legislator intended that - in such cases as those two decided by the Federal Court of Justice - the aggrieved company would not have to undertake a liability lawsuit

against its own manager, by which the manager would inevitably be “damaged” or even “burnt”.

3. „SERIOUSNESS“ OF CLAIM NOT REQUIRED

In addition, the BGH clearly stated that „seriousness“ of the assertion of the claim against the own manager (or director) is no precondition for a liability claim of the aggrieved company against its manager. This would even apply if the assertion of the claim against the insured person was only made in order to assert the claim against the D&O insurer.

The BGH further explained that the creditor of a liability claim is free to decide whether and to what extent it asserts the claim against the damaging party and which assets of the damaging party it accesses – eventually by enforcement measures. Especially in the event of high claims, as it is often the case in D&O insurance, the damaging party will not possess sufficient private assets to pay the respective damage claims by its own resources.

Against this background, it is legitimate and legally permissible if the aggrieved company asserts the claim against its own manager and then makes the manager assign the indemnification claim against the D&O insurer to the company. It is within the discretion of the aggrieved party how it requests compensation for the damage. Preferably, the aggrieved company may assert the claim against the liability insurer. Usually it is the insurer who is the more credible debtor and has promised performance in these circumstances.

The BGH points out that

> *„the coverage claim of liability insurance does not require a prior individual claim against the policy holder or its advance performance to the aggrieved party.“*

Also, the purpose of the liability insurance is not limited to the compensation of the potential financial damage of the damaging party resulting from its liability.

> *„The private liability insurance is rather subject to social commitment and thus has to protect the aggrieved party and secure its indemnification – for example in case the damaging party does not possess sufficient private resources.”*

The statute's intention is to ensure that the impacted party benefits at the end form the indemnification as per secs. 108 to 110 VVG.

Considering the interests of all parties, the interpretation of sec. 108 para. 2 VVG including the contract terms does not prohibit

> *that the aggrieved party asserts damage claims, particularly – or even exclusively – with the intention to gain insurer's liability performance as stipulated by the legislator.*

Based on the argument that the aggrieved party only intends to gain access to the insurer's liability payment, the seriousness of its claim for indemnification may not be denied for legal reasons, states the BGH. According to the BGH, there are no deviations from the general liability insurance resulting from the special constellation of the D&O insurance.

The Appeal Court had interpreted the „seriousness" as unwritten requirement in the terms of the insurance contract, so the BGH. The BGH further clarifies that the interpretation of insurance terms is depending on their wording. The wording has to be interpreted from a reasonable policy holder's point of view. The policy holder will not understand the insurance terms in that way that the purpose of the claim has also targeted the access of the personal assets of the damaging party. There is nothing to suggest so within the insurance terms.

4. ASSIGNMENT OF THE INDEMNIFICATION CLAIM NO INDICATION FOR COLLUSIVE CONDUCT

At the end of the two judgments, the BGH also states that such process (written claim against its own manager, assignment of indemnification claim, direct claim against the insurer) is neither contrary to public (sec. 138 German Civil Code "BGB") nor contrary to good faith (sec. 242 BGB). Such conduct does not imply any collusive interaction between the aggrieved company and its manager leading to the exclusion of insurance cover. Such collusive conduct would only be given if the company referred to claims resulting from sec. 43 para. 2 Limited Liability Companies Act ("GmbHG") which in fact had not incurred at all or not in the alleged amount and if the aggrieved company and the manager were aware of this fact.

In particular, the insurer's allegation that it only wanted to protect itself against such collusive interaction (ultimately fraudulent conduct of the policy holder and the insured person) is not applicable. No disadvantages derive from the assignment for the procedural situation. The insurer may protect itself in the same way as without assignment.

5. CONCLUSION

It is permissible that the manager director against whom claims are asserted assigns its indemnification claim against a D&O insurer to the aggrieved company and the company then directly asserts the claim for payment against the D&O insurer. This procedure is also permissible if the aggrieved company never intended to access the manager's assets.

The objections regularly brought forward by D&O insurer's (this approach constituted a collusive combination/ a fraudulent conduct, this approach was misleading, solely one claim should be constructed against the D&O insurer etc.) have legally no prospect of success as of now.

We therefore assume that direct assertions of liability claims against D&O insurers will increase in the future. Some preconditions must also be considered and the insured person's rights must remain.

In case you have any further queries, please do not hesitate to contact us:

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