WILHELM

RECHTSANWÄLTE

Dr. Fabian Herdter, LL.M. Eur. Versicherungspraxis, August 2013

D&O insurance

Policyholder's duty to disclose information versus policyholder's interests in commercial and industrial confidentiality

1. INTRODUCTION

After the occurrence of an insured event, D&O insurers often insist on the duty to disclose information and to provide documents in order to force the policyholder to disclose full information. This concerns even such information that is not relevant for the insured event and which should not be disclosed to the public or to competitors. Insurers may request, for example, sensible information concerning business strategy, products, distribution structure etc. In many D&O cases, insurers request disclosure of the minutes of executive and general meetings (including attachments) which may contain sensible information as well.

In this context the question raises how executives can meet their corporate confidentiality obligations without breaching the duty to disclose information towards the insurer.

2. POLICYHOLDER'S DUTY TO DISCLOSE INFORMATION AND TO PROVIDE DOCUMENTS

In case an insured event occurs in D&O insurance by making a claim ("claims made"), the insurer, in general, has a legitimate interest in obtaining information about the insured event. This results from the fact that the policyholder manages the insured risk and therefore has superior knowledge compared to the insurer.

German statutory law takes account of this situation by implementing the policyholder's duty to disclose information and to provide documents pursuant to sec. 31 Insurance Contract Act (VVG). Such duties also form part of various insurance terms.[1]

2.1 Scope of sec. 31 para. 1 VVG

Sec. 31 para. 1 VVG governs the policyholder's statutory duty to disclose information. The regulation however fails to adopt sanctions for violating it (*lex imperfecta*). As a result, the insurer is only entitled to insist on the breach of the policyholder's duty to disclose information if the parties agreed upon a contractual duty in the insurance contract giving rise to contractual sanctions for violating the (policyholder's) duty to disclose information. If there is no such clause or if the contract only contains a general hint as to the statutory duty in sec. 31 VVG, a breach of the duty to disclose information can rarely result in negative consequences for the policyholder.

In detail, sec. 31 para. 1 VVG differentiates between the policyholder's statutory duty to disclose information according to sec. 31 para. 1 s. 1 VVG and the policyholder's statutory duty to release documents to the insurer according to sec. 31 para. 1 s. 2 VVG. The policyholder's duty to release documents describes a separate statutory duty.[2] It does not form part of the policyholder's duty to disclose information.

2.2 Duty to dislose information according to sec. 31 para. 1 s. 1 VVG

In accordance with sec. 31 para. 1 s. 1 VVG, after the occurrence of an insured event, the insurer may demand that the policyholder discloses all the information necessary to establish the occurrence of the insured event or the extent of the insurer's liability.

It is thus required that the requested information is *necessary* to establish the insured event or the extent of the insurer's liability. The appraisal of what is necessary falls – according to prevailing jurisdiction – into the insurer's sphere and will in general to be

---

[1] For example clause 7.3.2.2 AVB-AVG (version of May 2013) in D&O-insurance.

[2] Cp. *Möller* in Bruck-Möller, VVG, 8th edition, sec. 34 note 28; *Brömmelmeyer* in Bruck-Möller, VVG, 9th edition, volume I, sec. 31 no. 80.

determined from the insurer's subjective perspective.[3] As a consequence, the extent of information required is solely at the disposition of the insurer.[4] Due to the amount of information requested, especially in D&O cases, this results in considerable difficulties.

In contrast, according to dissenting opinion, the insurer's subjective view for the appraisal of the term "*necessary*" cannot be the determining factor. The term "necessary" also has to be understood in an objective and normative way.[5] Beyond, it is argued that the policy holder only has to fulfill reasonable requests for information, so that the insurer has to prove in dispute that the information requested is actually required and had or may have had influence on its settlement practice.[6]

2.3 Duty to release documents according to sec. 31 para. 1 s. 2 VVG

The duty to release documents is found in sec. 31 para. 1 s. 2 VVG.

Pursuant to sec. 31 para. 1 s. 2 VVG, the insurer can require the disclosure of documents to the extent that can *reasonably* be expected from the policyholder. In particular, the disclosure can be unreasonable if the document is in the possession of a third party that refuses to disclose the document, if the disclosure is not economical reasonable in terms of time and money, or if the disclosure has become impossible for other reasons.[7]

In our opinion, the duty to release documents could be further qualified to be "unreasonable" if the policy holder would be forced to breach statutory confidentiality obligations towards its own company.

---

[3] Cp. BGH NJW 1967, 1226; BGH VersR 2006, 258 (259); BGH VersR 2000, 222 (223); more restrictive OLG Köln VersR 2011, 339.

[4] Cp. *Schwintowski* in Schwintowski/Brömmelmeyer, VVG, sec. 31 no. 28.

[5] Cp. MüKo-*Wandt*, VVG, sec 31 No. 31; *Schwintowski* in Schwintowski/ Brömmelmeyer, VVG, sec. 31 no. 29.

[6] Cp. *Brömmelmeyer* in Bruck-Möller, VVG, 9th edition, sec. 31 no. 28.

[7] Cp. MüKo-*Wandt*, VVG, sec. 31 no. 102.

3. CONFIDENTIALITY OBLIGATIONS

Confidentiality obligations for executives can be found in various regulations.

Sec. 93 para. 1 s. 3 AktG (German Stock Corporation Act) applies for board members of German stock companies.

Under this provision, directors have to keep any information and secrets of the company strictly confidential, in particular business or trade secrets that have become known to board members while working on behalf of the board. For the supervisory board this provision applies similarly in accordance with sec. 116 s.1 and 2 AktG / sec. 93 para. 1 s. 3 AktG.

The confidentiality obligation comprises all secrets of the company. Secrets of the company are facts known only to a strictly limited circle of persons (and thus not obvious). It must be essential that these facts are to be kept secret according to the explicit or assumed needs of the company and that there is a justified (economical) interest of the company in the maintenance of confidentiality.[8] Facts to be kept secret are, for example, production projects, manufacturing procedures, inventions, designs, calculations, sales planning, financial planning, customer lists, etc.

Company secrets also concern information on M&A negotiations as well as results and contents of executive board and supervisory board meetings.[9]

According to sec. 93 para 2 AktG, a breach of the confidentiality duty may lead to a compensation claim of the company against the board member who violates the duty. In addition, the breach is liable to prosecution according to sec. 404 para. 1 AktG.[10] The supervisory board may further revoke the appointment of the board member for exceptional reasons (sec. 84 para 3 s. 1 AktG).

Besides these confidentiality obligations (under corporate law), further confidentiality obligations may arise for board members, for example under data protection law pur-

[8] Cp. MüKo-*Spindler*, AktG, 3rd edition 2008, sec. 93 no. 100.

[9] Examples found in MüKo-*Spindler*, AktG, 3rd edition. 2008, sec. 93 no. 100.

[10] Cp. sec. 85 GmbHG for executives, members of the supervisory board, or liquidators of a GmbH.

suant to secs. 27 et seqs BDSG (Federal Data Protection Act), under capital market law pursuant to sec. 14 para. 1 No. 2 WpHG (Securities Trading Act), or under competition law pursuant to sec. 17 UWG (Act against Unfair Competition).

4. DUTY TO DISCLOSE VERSUS CONFIDENTIALITY OBLIGATION

After notification of the insured event under the D&O insurance, board members often have to decide on how to deal with the confidentiality interests of the company against the policyholder's duties to disclose information and evidence to the insurer. Board members, on the one hand, should not violate these disclose requirements towards the insurer in order to uphold insurance cover (for the board member itself and for the company). Board members, on the other hand, should not violate statutory confidentiality obligations towards the company in order to avoid being held responsible due to breach of duty. In many cases, these obligations diverge and are contrary to each other.

Against this background, the question raises whether in such situation the disclosure of confidential documents could be considered as unreasonable within the meaning of sec. 31 para 1 s. 2 VVG.

4.1 Insurer's own confidentiality not sufficient

Insurers often argue that existing confidentiality interests of the policyholder could principally not lead to any unreasonableness of the insurer's demand to disclosure confidential documents (in respect of sec. 31 para 1 s.2 VVG), as the insurer is sworn to secrecy according to sec. 203 No. 6 and sec. 4 StGB (German Penal Code).

This is only true in part since the scope of sec. 203, No. 6 StGB only applies for members of companies in private health, accident, or life insurance. Liability insurance – such as the D&O insurance – does not fall within the scope of application of sec. 203, No. 6 StGB.

Though an insurer whose employees disclose confidential information of the policyholder would possibly become liable towards the damaged company, such claims would be difficult to establish and prove and thus difficult to realize. For the policyholder it is usually hard to understand which employees of the insurer have access to the documents provided, how those documents are stored (by electronic record and / or reference file) and what happens after settlement of the claim with the documents.

4.2 Possible solutions

There are basically two solutions to handle this issue in order to define the term "unreasonableness" in the meaning of sec. 31 para. 1 s. 2 VVG.

4.2.1 Policyholder does not have any duty to provide confidential documents

The policyholder might argue that the disclosure of documents which are subject to statutory confidentiality obligations according to above mentioned regulations, is unreasonable in terms of insurance law and thus not due. This could apply even more if the documents are not connected to the insured event noticed to the insurer.

This view is supported by the fact that the insurer – at the time of entering into the insurance contract – is aware of the statutory confidentiality obligations the board members of the policy holder have to meet. The confidentiality obligations are accordingly part of the premium calculation. The bodies acting on behalf of the policyholder can only provide such information and documents they are entitled to disclose. What is impossible is not owed.

The problem resulting from such argument is that the insurer would then probably deny cover due to breach of duty. Thus, the policyholder would risk insurance (defense) cover of all its board members claimed against under the D&O insurance. As a consequence of this approach, the board member (who lost its defense cover) might claim against the (policy holding) company under employment contract and with reference to contractual or fiduciary duty of loyalty and trust granted by the company.

Even in case the insurer does not deny cover due to breach of obligation, there would still be a risk for the policyholder that the insurer denies maturity of cover. The insurer could argue that – contrary to sec. 14 VVG – the insurer is not able to execute the necessary enquiries as long as the policyholder fails to provide the allegedly relevant documents.

As a consequence, in day-to-day-practice, a total denial of documents based on the argument of confidentiality appears to be not effective.

4.2.2 Policyholder discloses documents by referring to the standard of information rights according to sec. 810 German Civil Code (BGB)

A solution could be achieved by referring to the criterion of "reasonableness of the disclosure of documents" in sec. 810 BGB (German Civil Code).

Sec. 810 BGB obliges the company in case of dispute to give board member access to relevant business documents.[11] The amount of disclosed information depends on the reasonable interest of the person seeking disclosure. The board member gets access to relevant documents so that his defense against the claim does not fail for difficulties of proof. The board member must be given the opportunity to prove that he applied the diligence of a prudent and conscientious manager.[12]

The access for the manager to relevant business documents, however, ends where the link between the requested data and the legal position in question is no longer tangible. If the information request is only intended for “fishing” evidence, as the board member (who bears the burden of proof) only hopes to find out whatsoever hint to some wrongful doing on the company side, this does not constitute a reasonable interest.[13] Assuming that the board member requests access to documents concerning business and trade secrets, the company’s confidentiality interest should then be balanced against the evidence needs of the board member considering all the circumstances of the case, and it could finally be justified to exclude, for example, parts of the document from the request.[14]

In applying these principles to the relationship company / insurer, a reasonable solution for both parties could be achieved in upholding the company’s duty to disclose the requested documents, but – at the same time – in restricting that duty so that the company is free to black out or to render unrecognisable those parts of the documents (subject to confidentiality) which are in no way related to the insured event.

---

[11] Cp. BGHZ 152, 280 (285); MüKo-*Spindler*, AktG, 3rd edition. 2008, sec. 93 AktG No. 170.

[12] Cp. Müko-*Spindler*, AktG, 3rd 2008, sec. 93 No. 170. If the company denies the retired board member this right, this leads to proof or demonstration facilities for the benefit of the retired board member

[13] Cp. *Marburger* in Staudinger, 2009, sec. 810 BGB No. 10 with further references.

[14] Cp. *Marburger* in Staudinger, 2009, before sections 809-811 BGB No. 5.

In return, according to sec. 31 para. 1 s. 1 VVG, the insurer would be entitled to obtain detailed information of the company about why certain documents are subject to confidentiality. The policyholder would then have to explain, at least would have to give an overview of what is the content of certain documents and why these documents are not relevant for the insured event and therefore were blackened. Based on this information, the insurer would then have to explain why he requires the blackened information in order to review the occurrence of the insured event or the extent of the insurer's liability.

Such procedure could ensure that reasonable statutory confidentiality interests of the company are respected as well as the insurer' s interest in obtaining all relevant information in respect of the alleged breach of duty.

5. SUMMARY

The company's duty to disclose information towards the insurer in insured versus insured cases is not unrestricted to the extent that statutory duties of confidentiality remain unconsidered.

In consideration of the diverging interests of the company and the insurer a reasonable solution for both parties could be achieved by defining the criterion of "reasonableness" pursuant to sec.31 para. 1 s. 2 VVG by referring to the standard of information rights of board members as specified in sec. 810 BGB (German Civil Code).

Dr. Fabian Herdter, LL.M. Eur.
Lawyer
Master of European and International Business Laws

Wilhelm
Partnerschaft von Rechtsanwälten
Reichsstraße 43
40217 Düsseldorf

Telephone: + 49 (0)211 687746 - 50
Telefax: + 49 (0)211 687746 - 20

www.wilhelm-rae.de
fabian.herdter@wilhelm-rae.de

AG Essen: PR 1597