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[District Court Holds No D&O Insurance Coverage For Attorneys' Fees And Costs Incurred In Voluntary Response To SEC Investigation](#)

In *Office Depot, Inc. v. National Union Fire Insurance Co. of Pittsburgh, Pa.*, No. 09-80554-CIV-MARRA, 2010 WL 4065416 (S.D. Fla. Oct. 15, 2010), the [United States District Court for the Southern District of Florida](#) recently concluded that Office Depot, Inc. (“Office Depot” or the “Company”) could not recover \$23 million in attorneys’ fees and costs incurred in voluntarily responding to a [Securities & Exchange Commission](#) (“SEC”) investigation and in conducting an internal investigation and audit. The court held that these fees and costs did not fall within the policy’s definition of loss “arising from” a covered “Securities Claim” made against the Company or a covered “Claim” made against one of its officers, directors or employees. Companies with policy language similar to that in *Office Depot* thus take a calculated risk, when committing resources towards voluntary cooperation with the SEC or an internal investigation, that insurance coverage for the attorneys’ fees or costs incurred will not be available.

The SEC Investigation and the Whistleblower Complaint

In June 2007, Office Depot was reported in the financial press as hearing improperly disclosed material information regarding projected profits and sales to financial analysts, implicating SEC [Regulation FD](#). In July, the SEC sent Office Depot a letter of inquiry, seeking the Company’s communications with financial analysts. That same month, a purported whistleblower alleged improper recognition of vendor rebate program funds. In response to the whistleblower complaint, Office Depot conducted an internal investigation and audit. In November 2007, the SEC expanded its inquiry to include the recognition of vendor rebate program funds. Office Depot voluntarily cooperated with the SEC’s inquiry by providing documents and making its employees and officers available for sworn testimony without the issuance of subpoenas. The Company provided notice of the SEC’s inquiry letter to its directors and officers (“D&O”) insurers. In January 2008, the SEC issued a formal “order directing private investigation” and issued a series of subpoenas to Office Depot employees, including several persons who previously testified voluntarily. The SEC also issued “Wells notices” to Office Depot officers. In December 2009, Office Depot reached a settlement with the SEC. See Securities Exchange Act of 1934, [Rel. No. 63152](#) (Oct. 21, 2010).

The Insurance Policy and the Claim

National Union Fire Insurance Co. insured Office Depot for loss arising from a “Securities Claim” made

against it. The policy also provided coverage for Insured Persons (officers, directors or employees). A “Securities Claim,” as defined by the Policy, excepted administrative and regulatory proceedings against and investigations of the Company. But, the policy carved back the exception if an administrative or regulatory proceeding was commenced and maintained against the Company during the time it was maintained against an Insured Person. Office Depot asserted that this carve-back provided coverage because the terms “administrative and regulatory proceedings” were undefined in the policy.

The policy defined a “Claim” as a civil, criminal, administrative or regulatory proceeding against the Company, commenced by service of a complaint or a notice of charges. As to Insured Persons, the policy included investigations “(i) once such Insured Person is identified in writing by such investigating authority as a person against whom a civil, criminal, administrative, regulatory or arbitration proceeding for monetary, non-monetary or injunctive relief may be commenced; or (ii) in the case of an investigation by the SEC or a similar state or foreign government authority, after the service of a subpoena upon such Insured Person.”

“Loss” to which the Policy applied included “damages, settlements, judgments (including pre/post-judgment interest on a covered judgment),” and “Defense Costs” were defined as “reasonable and necessary fees, costs and expenses consented to by the Insurer . . . resulting solely from the investigation, adjustment, defense and/or appeal of a Claim against an Insured.”

The only “Defense Costs” for which National Union acknowledged coverage were attorneys’ fees and costs incurred by the employees and officers served with SEC subpoenas and Wells notices. These fees and costs totaled \$1,125,102, and because the policy retention was \$2.5 million, National Union did not make any payment on the claim.

The Court’s Decision

Office Depot filed a declaratory judgment action against National Union and the excess insurer. The parties filed cross-motions for summary judgment. On October 15, 2010, the court ruled in favor of the insurers. Applying Florida law, the court held the Policy language was clear and unambiguous. The court explained that the expenses incurred by Office Depot in voluntarily responding to the SEC investigation do not constitute a loss arising from a “Securities Claim” as investigations are expressly excepted from the definition of a “Securities Claim.” The SEC investigation did not fall within the “carve back” restoration of coverage for an “administrative or regulatory proceeding against an Organization,” because if the parties had intended the “carve back” clause to include an investigation, it would have so stated.

The court rejected Office Depot’s argument that the SEC investigation was a “Claim” because the SEC’s investigation was informal and there was no complaint or notice of charges filed. It also rejected Office Depot’s attempt to expand coverage by urging an expansive reading of the “relation back” clause found in

the “Notice/Claim Reporting Provisions.” The court explained that those Provisions merely defined when a claim is considered “made,” and were not intended to expand coverage.

Finally, the court concluded that Office Depot’s investigation expenses were not a covered “Loss” under the Policy. The Court explained that the Policy extends coverage for “Loss” “arising from” a “Securities Claim” or “Claim” against an Insured Person. Since neither term covers SEC investigations such as the one here, there was no coverage. The court noted that Office Depot is essentially seeking to recover the cost of investigating a “potential claim,” when the Policy definition of covered “Defense Costs” encompasses only the cost of investigating an actual “Claim.”

Impact of the Court’s Decision

The court’s interpretation of this D&O insurance policy leaves companies at risk of incurring substantial attorneys’ fees and costs in order to provide early cooperation with an SEC inquiry without ever obtaining coverage for the amounts spent. The company is effectively penalized for cooperating before subpoenas are issued. Voluntary cooperation with the SEC is, in most cases, still advisable. However, companies with policy language similar to that of Office Depot must bear in mind that the financial burden of cooperation is likely to fall squarely on the company’s shoulders.

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