

Liberty Needn't Cover Client's \$3M Expenses In SEC Probe, *Law360*, ft. Kevin Mattessich

Kevin M. Mattessich, co-managing partner in the New York City office at Kaufman Dolowich & Voluck, LLP, was quoted in *Law360* in an article written by Rick Archer.

Law360, New York (October 17, 2017, 4:07 PM EDT) — The Tenth Circuit found Tuesday that a U.S. Securities and Exchange Commission announcement of an investigation is not an allegation or request for relief, and thus doesn't trigger coverage under a sports nutrition company's policy with Liberty Insurance Underwriters Inc., even though the client shelled out \$3 million responding to the probe.

MusclePharm Corp. had claimed Liberty, a unit of Liberty Mutual, owed it coverage for the money it spent responding to the probe they were first informed of in 2013, but in an unpublished opinion, the panel said coverage was not triggered because the SEC did not allege wrongdoing until two years later in a Wells notice.

"Prior to that time, the SEC had not alleged a 'wrongful act' nor had it targeted a specific insured person," Circuit Court Judge Mary Beck Briscoe, writing the opinion for the panel, said.

MusclePharm, a Denver-based sports nutrition company, had argued that when the SEC initiated an investigation in 2013 into whether CEO Brad Pyatt and other executives failed to report certain benefits and perks, it did so by issuing a formal order, giving it a name and case number, and granting the SEC's staff members authority to subpoena witnesses, take evidence and compel documents — all of which equate to a formal regulatory proceeding.

That should have triggered a claim under the "Order of Formal Investigation" section of its Liberty directors and officers policy, a fact the insurer ignored, MusclePharm said.

Liberty countered that its policy expressly stated that a formal regulatory investigation only becomes a claim when the company receives Wells notices from the SEC signaling an enforcement action is underway, which didn't happen until February 2015. Therefore, the policy doesn't cover any costs predating that point in time, the insurer said.

Last August, U.S. District Judge Robert E. Blackburn sided with Liberty, agreeing with the insurer that the SEC order and other requests issued prior to the Wells notices did not allege a wrongful act on the part of MusclePharm or any of its executives.

MusclePharm appealed, contending that Judge Blackburn's decision misconstrued both the language of its D&O policy and controlling law. According to the company, the SEC subpoenas equated to a demand for nonmonetary relief covered by the policy, and the district judge misconstrued the word "alleged" in the policy's definition of a wrongful act to require a clear assertion of actual wrongdoing.

However, the panel said the 2013 SEC order is not an allegation under either the policy or the common definition, as the order expressly stated that it "should not be construed as an indication by the commission or its staff that any violation of the law has occurred, nor as a reflection upon any person, entity or security."

“Thus, the SEC sought to determine, through documents and testimony, whether there would ultimately be any basis for seeking monetary and/or nonmonetary relief from MusclePharm,” Judge Briscoe said. “By this action, the SEC was not seeking relief, but was only gathering information.”

“The court just took a very common-sense approach to the language of the policy,” Liberty counsel Kevin Mattessich said.

MusclePharm counsel Jerold Oshinsky declined to comment Tuesday, saying he had not had the opportunity to review the decision.

MusclePharm ultimately settled with the SEC in September 2015 over charges of unreported perks and related-party transactions. The company and the executives together agreed to pay \$910,000 in penalties and employ an independent monitor for 12 months.

Circuit Court Judges Mary Beck Briscoe, Harris L. Hartz and Robert E. Bacharach sat on the panel for the Tenth Circuit.

MusclePharm is represented by Jerold Oshinsky of Kasowitz Benson Torres & Friedman LLP and by Richard B. Benenson of Brownstein Hyatt Farber Schreck LLP.

Liberty is represented by Kevin M. Mattessich and Jeffrey S. Matty of Kaufman Dolowich & Voluck LLP.

The case is MusclePharm Corp. v. Liberty Insurance Underwriters Inc., case number 16-1462, in the U.S. Court of Appeals for the Tenth Circuit.