

D&O Update: Supreme Court Reverses Dismissal Order in Zicam Securities Litigation



By John Orr

On March 22, 2011, the United States Supreme Court ("USSC") issued its opinion in securities litigation involving Matrixx Initiatives Inc., makers of the cold remedy, Zicam (*Matrixx Initiatives, Inc. v. Siracusano*, No. 09-1156, Mar. 22, 2011). In ruling that the lower court erred in dismissing Matrixx from the litigation, the USSC concluded that whether it was reasonable for plaintiff investors to have acted upon previously undisclosed reports of possible adverse effects of Zicam, was a matter to be decided at trial. The USSC decision may create ripples through the halls of public pharmaceutical and life sciences companies, as executives there continue to grapple with how far a company must go in disclosing product-related risk factors.

In its complaint, shareholders of Matrixx alleged the company should have disclosed that Zicam may cause anosmia, a condition associated with a loss of smell. The district court granted the company's motion to dismiss, concluding that the number of anosmia cases of which Matrixx executives were aware was not statistically significant. In upholding the 9th Circuit's reversal of that decision, the USSC rejected a bright-line test that would require an allegation of statistical significance to satisfy the scienter and materiality requirements of the federal securities laws.

D&O Market Impact: Whether D&O insurance underwriters will now view public pharmaceutical and life sciences companies as greater risks to securities claims remains to be seen. Only time will tell whether the plaintiffs' bar will attempt to exploit the *Matrixx* decision by asserting more cases against these companies on theories associated with inadequate public disclosures.

Policy Language Considerations: The *Matrixx* decision should serve as a reminder for companies to review policy wording as it pertains to disclosure-based D&O claims. For example, exclusions for claims alleging fraud and known violations of law should not trigger unless, at a minimum, there is a final and unappealable adjudication of such conduct. Moreover, the clause known as "Severability in the Application for Insurance," which should protect insureds with no actual knowledge of materially false public disclosures from policy rescission, should be as protective as possible. Additionally, companies, particularly those in the healthcare, pharmaceutical, nutraceutical and life sciences sectors, should be mindful of absolute bodily injury exclusions that unexpectedly could trigger in D&O litigation relating to adverse health risks of products.

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