



H.S. Grace & Company, Inc.

D&O Policy: Effect of Change of Control Provision And Cancellation of Employee Stock Options

Allegations

A well-established and successful high-technology company's stock had a significant price run-up. Soon thereafter, the company sold a significant business unit and cancelled the stock options of the transferring employees. At the time of cancellation, virtually all of the transferring employees' stock options were significantly in-the-money. The affected employees sued. The company claimed that there was no relevant change in control provision; therefore, there was no requirement to vest the options. However, during the course of the dispute, the company made and expected to make additional "settlement" payments to certain transferring employees. Subsequent to the payments, the company attempted recovery under its D&O policy. The carrier declined coverage claiming that the parent company benefited by cancelling the in-the-money options; specifically the gain was subject to a policy exclusion.

Analysis

As the carrier and the insured had differing views on whether a gain resulted from the cancellation of the options, the carrier engaged H.S. Grace & Company, Inc. (HSG) to examine the arguments. HSG's analysis confirmed that the insured did gain by cancelling the options, demonstrated the amount of the gain, and pointed out that the sale of the division may not have been consummated in absence of terminating the subject stock options.

Among the advisors on HSG's team was the former treasurer of AT&T and a professor and former head of the Accounting Department at Baruch College.

Result

HSG's analysis enabled the carrier to take a strong position in its negotiations with the insured due to the soundness of its case, resulting in a favorable settlement for the carrier.

H.S. Grace & Company, Inc. is a team of senior executives who diagnose and resolve critical corporate problems in business governance, operations, finance and control. With more than 1,000 years of experience, our goal is to help companies enhance shareholder value, protect reputation and their long-term ability to succeed, avoid and manage litigation, and navigate major changes such as mergers and acquisitions or bankruptcies. We often serve as consulting and testifying experts, identifying and analyzing critical business issues.

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