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Fourth Circuit Court of Appeals Holds Bump-Up Exclusion Precludes Coverage

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In *Towers Watson & Co. v. National Union Fire Insurance Co. of Pittsburgh, PA*, No. 24-1302, 2025 U.S. App. LEXIS 12963 (4th Cir. May 28, 2025), the Fourth Circuit Court of Appeals affirmed the decision of the United States District Court for the Eastern District of Virgina, holding that an insurance policy's bump-up exclusion precluded coverage for the parties' settlement, including the portion that ultimately went toward attorneys' fees.

By way of background, Towers Watson and Willis Ground Holdings entered into a merger agreement, which was the first part of a larger, two-phase transaction. In relevant part, the Towers Watson shareholders received the right to 2.649 shares of Willis stock for each Towers Watson share, along with a special dividend. Over the next few years, former Towers Watson shareholders filed separate class actions asserting federal securities law and Delaware state law claims. The shareholders' claims stemmed from allegations that Tower Watson's former chairman and CEO negotiated the merger agreement under an undisclosed conflict of interest which resulted in a below-market valuation of Tower Watson shares to ensure the merger's success. The parties ultimately settled, and this coverage dispute followed.

Towers Watson held a primary D&O liability policy with National Union, along with six layers of excess coverage from other insurers, which were largely "follow form" to the primary policy (the "Policy"). The Policy provided coverage for the "Loss of any Organization . . . arising from any Securities Claim made against such Organization for any Wrongful Act of such Organization," and the "Loss of an Organization that arises from any [] Claim . . . made against any Insured Person . . . for any Wrongful Act of such Insured Person." The Policy contained a "bump-up" exclusion which generally bars coverage for losses stemming from judgments or settlements reached in connection with claims that seek an increase in the consideration paid for a security.

The Fourth Circuit determined that two conditions must be satisfied before the bump-up exclusion is triggered: 1) there must be a "Claim" alleging that the consideration paid for an acquisition was inadequate; and 2) the settlement of such claim must represent an effective increase in the "price or consideration" shareholders received for that acquisition.

After establishing the first condition was clearly satisfied, the Fourth Circuit addressed the second condition, namely the terms "represent" and "effectively increased." Because the Policy did not define either term, the Court looked at the terms' dictionary definitions to determine whether the second condition was satisfied. The Fourth Circuit found that, when read together, the terms indicate that it must look at the "real result" of the settlements, rather than the theoretical one. With that, the Court determined the shareholders, claiming their shares were devalued in the merger process, sought to rectify that shortfall. Which, the Court found, was effectively an increase in the consideration paid for their shares. Thus, the Fourth Circuit found the second condition was satisfied and the bump-up exclusion applied, so Towers Watson was not entitled to indemnification for the settlements.

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Towers Watson raised three arguments the Fourth Circuit ultimately found unavailing. Towers Watson first argued the district court's analysis of the bump-up exclusion collapsed its two distinct elements into one by only looking at the allegations and not what the settlement itself represented. The Court disagreed, pointing to the district court's opinion which contained separate sections addressing the elements, and the Court's ability to independently assess the issue. Next, Towers Watson argued settlements of alleged violations of § 14(a) of the Securities Exchange Act are immune from the application of bump-up provisions. The Court noted that it was not tasked with deciding whether the complaints came within § 14, but whether the loss falls within the scope of the bump-up exclusion. Finally, Towers Watson argued the damages were meant only to remedy the devaluation, not represent an increase in their compensation. The Fourth Circuit found that to argue such would ignore the shareholders' allegations, the purpose of the expert report, and the practical effect of the damages.

The Fourth Circuit further affirmed the district court's finding that the settlement money designated to attorneys' fees fell within the ambit of the bump-up exclusion by way of the common fund doctrine such that the bump-up exclusion bars indemnity for the entirety of the settlement awards, including the portion that went towards attorneys' fees. The settlements required Willis to pay $90 million into a common fund entirely for the benefit Towers Watson shareholders, who's authorized representatives then asked the courts to award attorneys' fees and costs out of that common fund. The Fourth Circuit agreed with the district court that regardless of how the additional consideration was distributed once paid to the beneficiaries, it constituted *in toto* an increase in consideration paid for the merger. As such, the bump-up exclusion bars indemnity for the whole settlement award, including the portion that went toward attorneys' fees.

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