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Alert

New Jersey Supreme Court Enforces Capacity Exclusion In D&O Insurance Policy

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The New Jersey Supreme Court held, as a matter of first impression in New Jersey, that an insurer's capacity exclusion in a Directors and Officers liability insurance policy precludes coverage for an insured director who was acting in a dual capacity with an affiliated, but non-insured, entity. Coughlin Midlige and Garland, LLP represented its client, Berkley Insurance Company, before the NJ Supreme Court to obtain this ruling. In addition to enforcing clear exclusionary language, the Court also favorably addressed the reach of the New Jersey doctrines of forfeiture and estoppel under *Firemen's Fund Ins. Co. v. Security Ins. Co.* and *Griggs v. Bertram,* respectively The case, which was decided on May 11, 2026, is entitled *Mist Pharmaceuticals LLC v. Berkley Insurance Company*, A-34-24, and can be read here.

In *Mist Pharmaceuticals*, Berkley issued a D&O Policy to Mist Pharmaceuticals that included a Capacity Exclusion, which barred coverage for any "loss in connection with a claim made against any insured. . . in any way involving any wrongful act of an insured person serving in their capacity as. . . a member. . . of any other entity other than an insured entity." The insured person at issue was a director with the insured entity but was also an officer and director of a non-insured entity. The underlying claim involved a dispute between the insured person and a co-shareholder in the non-insured entity, with allegations that the insured person engaged in self-dealing utilizing Mist Pharmaceuticals as a vehicle for that self-dealing.

Based upon the policy language in the Berkley D&O Policy, the Court distinguished the case from the exclusion addressed in the Court's prior *Flomerfelt* decision and refused to require a causal nexus between excluded activity and the harm alleged in the underlying claim. Rather, the Court concluded that the exclusionary language in the Berkley D&O Policy was more analogous to the language at issue in the Court's ruling in *Norman International*. Underscoring the importance of policy language, the Court held that because the exclusion applied if the allegations in the underlying actions "in any way involved" the wrongful acts of an insured person for an uninsured entity, it did not require any causal relationship between excluded activity and the alleged harm. Specifically, the Court held that in light of the exclusionary language in the Berkley Policy, claims premised on a director's or officer's misconduct in a "dual capacity" for insured and uninsured entities was not covered.

To avoid application of the exclusion, the insured had argued that Berkley had forfeited the right to rely on it or was it estopped from doing so based upon the New Jersey Supreme Court's *Firemen's Fund* and *Griggs* decisions. The Court made clear that the *Firemen's Fund* decision only applies in the situation in which the insurer had already breached its obligations under a policy and had acted in bad faith. Because such circumstances were not present in the *Mist Pharmaceuticals* matter, the Court held there was no forfeiture of any coverage defenses. Moreover, because Berkley had reserved its rights to rely upon the Capacity Exclusion and advised its insured of its intention to disclaim coverage or the possibility that coverage would be denied or questioned, the *Griggs* decision did not apply either. Given the multiple reservation of rights letters sent by Berkley to its insured, the Court held that Mist Pharmaceuticals could not establish that it justifiably relied upon any commitment by Berkley to cover the claims at issue.

The Court's decision in *Mist Pharmaceuticals* is significant for insurers handling New Jersey claims. It evinces the New Jersey Supreme Court's willingness to apply clear policy language and enforce broad prefatory language, even when contained in an exclusion. It also, as a matter of first impression, applied the Capacity Exclusion to a "dual capacity" situation. Moreover, the Court's clarification of when its *Firemen's Fund* and *Griggs* decisions apply provides additional guidance to insurers regarding the type of conduct that must be established for an insurer to forfeit or be estopped from asserting a coverage defense.

Adam M. Smith argued the appeal on behalf of Berkley.