

3 TIPS FOR COMPANIES EVALUATING INSURANCE COVERAGE IN MERGERS AND ACQUISITIONS

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Insurance policies are a significant asset that must be considered in any merger or acquisition. As companies are acquiring or merging with another company in 2015, there are three insurance-related tips for companies to keep in mind.

1. Value insurance policies

As companies consider whether to acquire another company and its liabilities, it is crucial to value the insurance policies that may cover these liabilities. An acquiring company should request the target company's insurance policies (both historic and current), loss history reports and pleadings and motions from any litigation involving the target company early in the transaction process. A target company may be entitled to coverage under its own insurance program or programs of additional companies that are or were part of the target company's current or prior corporate history. A target company may also be entitled to indemnity and/or insurance coverage from other companies by contract. The acquiring company also should consider discussing insurance-related issues with the target company's internal and outside counsel, risk managers, compliance officers, and insurance brokers in order to answer questions and obtain critical information. After collecting all relevant insurance policies and information, an acquiring company should chart and analyze the policies and answer the following questions:

- What are the types of insurance policies?
- Are the insurance policies occurrence based or claims made? If there are claims made policies, have any claims or notice of claims been made? Are tail policies needed on claims made policies in order to cover post-closing claims regarding pre-merger activities?
- Are the limits of the insurance policies still available or have the policies been commuted?
- Have the limits of the insurance policies been exhausted?
- Is any coverage with insolvent insurance companies or insurance companies whose financial strength is questionable? If the insurer is insolvent, what is the bar date for the filing of claims?
- Identify whether there are fronting policies, retrospective premium programs or high deductibles. Do retrospective premium programs remain open or have they been closed?

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The acquiring company should then assess the possible insurance recovery for each present and future claim by evaluating which policy or policies would cover the liabilities or confirm that the claim would be uninsured. The acquiring company may use this information to decide which liabilities to accept or require the target company to retain.

2. Ensure policies transfer

Insurance policies often contain anti-assignment clauses which prohibit the assignment of the policies themselves, or rights under the policies, without the consent of the insurer. As a general matter, a constituent company's rights to insurance coverage automatically vest in the surviving company by operation of the relevant state merger statute without implicating the anti-assignment provisions in insurance policies. In the absence of a statutory merger, courts are divided regarding whether anti-assignment provisions are enforceable. Before the California Supreme Court's decision in *Henkel Corp. v. Hartford Acc. and Indem. Co.*, 62 P.3d 69 (Cal. 2003), it was generally accepted by both insurers and policyholders that insurance rights for occurrences taking place prior to a transfer of business assets and/or liabilities were freely transferable without consent of the insurer, despite the existence of an anti-assignment provision requiring insurer consent. The rationale for this rule is that a transfer of post-loss rights does not increase the risk underwritten by the insurer. The occurrence insured against took place, the insurer's obligations are fixed and the assignment does not increase the insurer's obligations; it only changes the recipient of the insurance proceeds. *Henkel* held that post-loss insurance rights could not be transferred without insurer consent where the "claims had not been reduced to a sum of money due or to become due under the policy." However, the majority rule remains that post-loss assignments of insurance rights are permitted without consent of the insurer notwithstanding the existence of an anti-assignment clause. It is critical that parties to a transaction research the question of which state's law applies to an assignment of rights under insurance policies.

3. Consider representation and warranties coverage

Representations and warranties insurance (RWI) covers losses arising from unintentional and/or unknown breaches of representations and warranties made in an acquisition or merger agreement. A buy-side RWI policy provides buyers with coverage in the event of a breach of seller's representations and warranties. Sellers use RWI to reduce or eliminate the amount of sale proceeds held back by the buyer or placed into an escrow account. Parties should consider that RWI is issued on a claims-made basis; RWI does not cover breaches actually known to exist prior to the inception of the policy (although buy-side RWI should cover undisclosed breaches known by the seller); RWI may be structured to cover specific representations and warranties within the agreement or it may provide blanket coverage; and most insurers sell RWI to parties involved in corporate transactions valued between \$25 million and \$2 billion.