

CHAPTER 8

Liability and Property Insurance

In the present litigious environment, insurance and its relationship to an acquisition are becoming more significant. The purchaser should be prepared to review all insurance documents of the target company, with particular emphasis on comprehensive general liability insurance policies (both primary and umbrella), any contractual endorsements (which often contain exclusions), and directors' and officers' liability policies. It is recommended that an insurance professional collaborate with counsel in conducting this review. This insurance professional may be the risk manager for the purchaser or, if not applicable, the purchaser's insurance broker. The specific substantive issues regarding coverage for environmental liabilities is beyond the scope of this outline (for further discussion of environmental laws, see Chapter 9). If the target company has been or is currently subject to an environmental claim, the purchaser should determine whether the target has given adequate notice to all insurers that might have liability with respect to such claim. In reviewing the target's policies, counsel should give careful attention to policies in effect during the 1970s, because they may not have the more restrictive exclusions (such as pollution) that present policies have, and thus may have significant pollution coverage, if applicable.

A. Documents Customarily Reviewed [for the target company and for any material subsidiaries or joint-ventures that do not share coverage with the target]

- ___ 1. Current and prior insurance policies of the target company and all exclusions and endorsements
- ___ 2. Applications for all policies
- ___ 3. Correspondence with insurance brokers and carriers regarding coverage or claims, including, particularly, notice of claims or possible claims
- ___ 4. Responses from insurers rejecting or accepting current and past claims
- ___ 5. Schedule of insurance coverages by year to identify gaps or "holes" in the coverage
- ___ 6. Schedule of the target's loss experiences per insurance year
- ___ 7. Schedule of insurance reserves relating to the target
- ___ 8. Contracts relating to coverage by any captive insurance companies of the target or participation in any insurance pools
- ___ 9. Title insurance policies covering the target's real properties

B. Procedures to Be Followed

- ___ 1. Identify any recurring loss or liability experiences of the target company for which the target's carriers have declined coverage.
- ___ 2. Determine whether insurance is on "occurrence" form or "claims-made" form. A claims-made policy will respond only to claims that are first

asserted against the insured during the period the policy is in force. An occurrence policy will respond to claims in which the occurrence happened during the policy period. Almost all directors' and officers' liability policies and many professional liability and "Errors and Omissions" policies are on a claims-made basis. Before 1986 almost all comprehensive general liability and product liability policies were on the occurrence form. Since 1986 smaller companies have often been able to get occurrence coverage, whereas companies with significant long-term exposure claims (litigation or claims not arising until many years after initial exposure) have found it very difficult, if not impossible, to obtain occurrence coverage.

___ 3. Determine whether any gaps in coverage have been created by shifts between claims-made and occurrence coverage or by changes in contractual exclusions of certain risks.

___ 4. Determine whether the insurer and the insured concur regarding whether actual exposure,¹ manifestation,² injury-in-fact³, or the continuous-trigger theory of coverage⁴ has been agreed upon between the parties.

___ 5. Identify whether the excess policy is an umbrella policy or just excess following the form of the primary policy.

___ 6. Identify whether the target company has a policy of requiring independent contractors performing construction or service activities on company sites to add the company as an additional insured on their insurance policies. Also determine whether the target company is in compliance with any contractual obligations to add any other party as an additional insured.

___ 7. Identify whether recent experience shows a significant increase or decrease in insurance-related litigation and identify whether the magnitude of settlements or verdicts relative to such claims is increasing or decreasing.

___ 8. Determine whether the target company's auditor has taken any position on the adequacy of the company's insurance coverages and insurance reserves and whether the reserves have recently been revised.

___ 9. Identify the extent to which the target company is or has been self-insuring and the consequences of such self-insurance.

___ 10. Confirm that the target company's insurance carriers are still solvent and that the company has received no bankruptcy or insolvency notifications. If such filings have been received, identify the extent and significance of such lack of coverage, including, particularly, excess insurers' responses and whether there has been any "drop down" coverage.⁵

___ 11. Confirm that the target company has overseas coverage, particularly in Europe, if it is selling products there since Europe is now adopting strict liability.

___ 12. Confirm that, to the extent that the purchaser may elect for the target to continue its own coverage after the acquisition, the target's insurers will not exercise a right, if any, to cancel the policies.

C. Comment

A useful starting point is to review the target company's insurance coverages with the company's risk manager or, if none, its insurance broker. Thereafter, purchaser's counsel, with assistance from purchaser's insurance advisers, should review all of the target company's insurance policies, including all deductibles, endorsements, and exclusions. It is often helpful to create a bar chart indicating coverage by area and year. The chart can show the layers of coverage as well as the exclusions and significant endorsements for each layer. It also can identify significant deductibles and whether aggregates have been exceeded, which may result either in termination of coverage or in coverage commencing after satisfaction of the applicable deductible. Counsel should identify whether there is full coverage for each layer or whether only a certain percentage of the layer is insured.

Counsel should review insurance applications made by the target company. Failure to provide accurate and complete information on an insurance application may be grounds for the insurer to reject coverage. This is particularly relevant in directors' and officers' liability coverage, in connection with which the officer signing the application, usually the chief executive officer, is required to identify any claims that either have been asserted or are likely to be asserted against the company. In today's more sophisticated products liability environment,⁶ similar applications are required for new products liability and comprehensive general liability policies and sometimes for renewals of those policies. Counsel should also review the company's notification of claims and the insurers' responses. The insured's notifications to both primary and excess carriers should be in accordance with the requirements of the policies. If the target has deferred giving notice of a claim, the purchaser may wish to consider whether such notice should be given before the acquisition if the target's policy is to be discontinued. Special attention should be paid to denial of claims or reservation of rights by insurers.

NOTES

1. *Insurance Company of North America v. Forty-Eight Insulations*, 633 F.2d 1212 (6th Cir. 1980), reh'g granted, 657 F.2d 814 (6th Cir. 1981), cert. denied, 454 U.S. 1109 (1981).
2. *Eagle-Picher Industries Inc. v. Liberty Mutual Insurance Co.*, 682 F.2d 12 (1st Cir. 1982).
3. *American Home Products Corp. v. Liberty Mutual Insurance*, 748 F.2d 760 (2d Cir 1984).
4. *Keene Corp. v. Insurance Co. of North America*, 667 F.2d 1034 (D.C. Cir. 1981), cert. denied, 455 U.S. 1007 (1982).
5. See *McGuire v. Davis Truck Service, Inc.*, 518 So. 2d 1171 (La. App. 1988); *Transco Exploration Co. v. Pacific Employers Insurance Co.* 869 F.2d 862 (5th Cir. 1989).

6. Shapiro v. American Home Assoc. Co., 584 F. Supp. 1245 (D. Mass. 1984).
See generally Misery Loves Company: Spreading the Costs of CERCLA Cleanup,
42 VAND. L. REV. 1469 (1989).