ARE YOU CONFIDENT?
FINPRO COVERAGE CONSIDERATIONS: MERGERS AND ACQUISITIONS AND STRADDLE CLAIMS

Mergers and acquisitions (M&A) can be profitable, but also complicated — raising the possibility that the personal assets of directors and officers may be at risk if they are accused of wrongful acts during an M&A transaction. Directors and officers liability insurance (D&O) policies can address claims arising before and after the transaction is completed.

But what if a D&O claim includes a series of alleged wrongful acts over time — occurring both before and after the transaction? Are directors and officers covered?

An M&A transaction — whether it is an acquisition of assets or of entities, or a disposition of assets or entities, by a sale, spinoff, or merger — can have significant implications for D&O coverage. Because an organization's structure can change in the course of a transaction, a D&O runoff policy may kick in to provide coverage for claims made prior to the date of change in structure. Runoff occurs when there is a change in control of the company or the company ceases to exist; runoff insurance provides coverage for claims that arise out of wrongful acts that allegedly occurred prior to the date of the change in control. Claims arising out of acts after the transaction generally fall under a D&O go-forward policy.

However, when a D&O claim includes a series of alleged wrongful acts, some occurring before and some after the transaction, it may cause confusion about how directors and officers are covered. These are known as "straddle claims."

It's critical for organizations to understand and address straddle claims in both the D&O runoff and D&O go-forward policies. This can help ensure that directors and officers are covered and minimize potential D&O coverage issues.

THREE APPROACHES

Depending on the specific deal and the commercial approach of insurers, there are three potential approaches to addressing straddle claims:

THE "STRADDLE" APPROACH

Specific policy wording in the wrongful acts sections of runoff and go-forward policies can address straddle claims. This is done by adding:

1. Language that states that the prior acts exclusion on the go-forward policy only applies to that part of loss attributable to wrongful acts occurring prior to the transaction date.
2. Identical wording to the post-transaction wrongful acts exclusion on the runoff policy to clarify that it will exclude coverage for that part of loss attributable to wrongful acts taking place after the transaction date.

If a claim alleges related acts that started before the transaction date and continued afterward, the resulting loss would still need to be allocated between the go-forward policy and the runoff policy. At least two policy limits will be available under this approach, although at least two retentions will also apply.

THE "PUSH" APPROACH

Specific policy wording is added to one of the two policies explicitly to pick up a potential straddle claim. Typically added to the D&O runoff policy, the language usually states that related wrongful acts – even if they happened over time – will be deemed to have been committed or attempted on the date of the earliest one.

If the insurer responsible for the D&O runoff policy is not comfortable picking up straddle claims, it may be possible to include them in the D&O go-forward policy. In that case, the insured entity controlling the D&O go-forward policy would need to be comfortable sharing its limits for past acts. Only one policy limit will be available for matters arising out of pre-transaction wrongful acts, and one retention will apply.

NO STRADDLE CLAIM LANGUAGE

Be prepared for situations where there is no specific policy wording about straddle claims in either the D&O runoff or D&O go-forward policies. In this instance, insurers typically place standard prior acts exclusions on the go-forward D&O policy.

This approach works best when the same primary insurer is on both policies. The insurer will likely cover the claim under one policy or the other.

But that may not always be the case. If there's a claim, an insurer may say that both the runoff endorsement and the prior acts exclusion have overly broad lead-in language (such as "arising out of," "based upon," or "attributable to") and therefore neither policy may respond. It is best to tailor the wording of the policies in advance to avoid such disputes.

When assessing these options, it is important to make sure they are aligned as much as possible with the indemnification provisions in the sale and purchase agreement (SPA). Talk to your insurance advisors before the SPA is finalized, so you can better understand how your D&O insurance works in the event of an M&A transaction.

For more information, please contact your Marsh representative or:

SARAH D. KATZ DOWNEY
US FINPRO D&O Product Leader
+1 212 345 3122
sarah.d.downey@marsh.com

CAROLE LYNN (CL) PROFERES
US FINPRO Product and Industry Leader
+1 215 246 1105
carolelynn.l.proferes@marsh.com