

# Dickstein Shapiro Morin & Oshinsky LLP



**KIRK PASICH** is a founding partner of the Los Angeles office of Dickstein Shapiro Morin & Oshinsky LLP. He was named by *American Lawyer* as one of the top 45 lawyers in the country under the age of 45; by *California Law Business* to its "Legal Dream Team" as one of California's top 25 litigators; by *Chambers USA: America's Leading Business Lawyers* as "the market leader for policyholder representation in California" and "the policyholder attorney most likely to come up with a new argument or perspective concerning policy language" and by *Lawdragon* as one of the "500 Leading Lawyers in America" (one of only 10 insurance coverage lawyers so named). Mr. Pasich conducts an active trial and appellate practice. He has procured jury verdicts in bad faith

cases that have been ranked among the 10 largest verdicts of the year in California. He is the author of more than 400 articles on insurance and the author, co-author, or editor of several books, including *The ABA Manual for Complex Insurance Coverage Litigation* (Aspen 2003), *Casualty and Liability Insurance* (Matthew Bender 2000, 2003), *Directors and Officers: Liabilities and Protections* (LexisNexis 2003), *West's California Litigation Forms: Civil Procedure Before Trial* (2000), and *The Year 2000 and Beyond* (CCH 2000).

**(ZAW300) TWST: Would you give us an overview of Dickstein Shapiro Morin & Oshinsky?**

**Mr. Pasich:** We are a national firm with offices in Washington, DC, New York, and Los Angeles. Our firm has a variety of what we call core practice areas, one of which is insurance coverage. And we represent insureds only in coverage disputes. So whenever there is a dispute between an insurance company and a policyholder, we are on the policyholder side. We've one of the largest, if not the largest, insurance coverage practices in the country. More than 70 of our lawyers spend at least 95% of their time on insurance coverage matters, and we have done everything from directors and officers litigation to environmental, asbestos products, disasters such as Hurricane Katrina, employment practices, and mergers and acquisition coverage issues, which is the topic of our discussion at the conference.

**TWST: How long have you been involved in the insurance industry, and what are some of your specific strengths and skill sets?**

**Mr. Pasich:** I started doing insurance coverage work for policyholders in 1982. That's been the focus of my practice for more than 20 years. I and others at Dickstein do everything from counseling clients in connection with the purchase or renewal of insurance to advising them on insurance issues and risk management issues that come up in deals and transactions, to litigating all the way through jury trials and appeals. I've tried quite a few jury cases and our firm has tried a lot of jury cases for policyholders. We are also very active on the appellate front. We are responsible for some of the most pro-insured decisions nationally at the appellate level in quite a few states, and in a number of federal courts. So we do pretty much everything for which an insured might need legal services.

**TWST: What are some of the cases that you've worked on?**

**Mr. Pasich:** I worked on a case called AIU Insurance Co. v. Superior Court, which is one of the groundbreaking California Supreme Court decisions, that ruled that the costs of cleaning up environmental contamination can be covered by general liability insurance. Most recently, I represented Pacific Enterprises, which is part of Sempra Energy, in a case in which we obtained a \$24 million judgment for Pacific under a crime insurance policy with respect to money that had been taken in a money laundering case by the President of a subsidiary. I was one of the counsel in the Armstrong World Industries case, which is probably the most favorable decision to policyholders on insurance coverage for asbestos. And I also represent almost all of the entertainment industry, at least on the motion picture and record company side, in coverage disputes.

**TWST: Is there anything on the regulatory, judicial or legislative agenda that is set to influence insurance issues as we look forward?**

**Mr. Pasich:** I think there are several things of real interest on the legislative agenda. One is the renewal of the federal terrorism insurance act. That will be decided in the course of the next couple of months, and that has real implications for the price and availability of terrorism insurance. Another is the possibility of Congress passing a bill, at least, for the President to consider on asbestos reform. The third thing I expect to see is major federal legislation regarding the effects of Hurricane Katrina. I suspect we'll see something addressing insurance coverage for natural disasters.

**TWST: You are set to speak at the upcoming Wall Street Transcript Due Diligence Conference. Would you please discuss some of the topics that you'll be focusing on at the conference?**

**Mr. Pasich:** In this new world of Sarbanes-Oxley with enterprise risk management, it is more important than ever, in mergers and acquisitions, for those companies involved as the acquired company or target and the acquiring company or successor or survivor to be aware of insurance issues. We've been doing insurance coverage work with respect to mergers and acquisitions both as part of our own firm's merger and acquisition practice, and on a consulting or a co-counsel basis with other firms that do mergers and acquisitions. There are two reasons for that. First, a lot of folks involved in mergers and acquisitions are not intimately familiar with some of the insurance issues and that means that some very important issues sometimes get overlooked in mergers and acquisitions. Second, a lot of the firms involved in mergers and acquisitions, somewhere in their group of clients, represent insurance companies or companies related to insurance companies. As a result, they may be precluded on conflict of interest grounds from taking an aggressive position on behalf of the companies involved against insurance companies. Or, because of their representation of insurance companies, they may not have a practice group familiar with issues from the insured's perspective.

So it is combinations of some ethical considerations and some knowledge base issues that frequently lead to insurance issues being overlooked. For example, it's not usual for a company acquiring another company or its assets to say, "Well, let's make sure we acquire the rights and insurance policies." One way to do that is by putting into a merger document an assignment of the insurance policies. The problem with that is almost every insurance policy has a non-assignment clause, a clause that says the insured cannot assign its interest in the policy without the insurance company's consent. So, if someone were to do a deal and it was important to acquire the insurance coverage from a target company, and they did it by having an assignment, they would likely find that the assignment wouldn't work. As a result, a piece of the deal perhaps would not come about simply because someone didn't comply with the assignment clause.

Now, the reality is that insurance companies often refuse to consent to an assignment in that kind of setting or at least refuse without additional premium. But that doesn't mean that there's no way to address the issue. In many cases, depending on the governing law, you don't even need to ask for an assignment because the coverage is deemed to "follow" the liability. In other words, if the acquiring company becomes liable for something that the target company did, the target company's insurance very well may protect the acquiring company anyway. It's a technical point, but it could be extremely important when you look at so-called long-term exposures like asbestos or environmental or drugs where people may have been exposed not just years ago but decades ago and are now suing. So that is one example.

One of the other things I would touch on is the importance of making sure that you understand the current status of the insurance at the time the deal is being done. Let's take another example. A company that has environmental problems or significant product exposures may enter into a settlement with its insurance companies, and get a big payment from the insurance companies in exchange for releasing coverage under a policy. So, for example, let's say an insured has over a 20-year or 30-year period, \$200 million worth of

insurance coverage, and it has a whole bunch of claims pending. The insured might say to the insurance companies, "You know what, I'll take 50 cents on the dollar. You write me a check for a \$100 million and I'll say that you've no responsibility for the \$200 million in claims." A year later, that company is acquired by a buyer. The buyer says, "Hey, show me what your insurance coverage looks like" and gets a listing of the policies. The buyer believes, "We've got these product exposures, but we have \$200 million in insurance coverage as listed right here." It turns out that that's not accurate. One, because \$100 million has already been paid, and two, the company being acquired has released the insurance companies from any duties to pay for those product claims. So what the buyer gets is insurance that is half as much as they thought, and it doesn't apply to the products claims. That could be a \$100 million issue in a single transaction or it could be worth even more than that. Those are the kinds of things we are going to be talking about.

**TWST: Do companies pay enough attention, when they're making an acquisition, to the state of the insurance coverage?**

**Mr. Pasich:** Sometimes companies do. I think those that are well advised or that have excellent risk management capabilities focus on these issues. The problem is that there is a mix of issues involved. Some of them are issues that a risk manager can deal with, some are issues that an insurance broker can deal with, some are issues that deal counsel can address. But frequently when you look at the combination of insurance terminology, regulatory issues, Sarbanes-Oxley requirements, historical insurance coverage and how that coverage has changed over the years, and the fact that insurance has its own body of law, its own statutory regulations, its own administrative regulations, there's simply an expertise level required for insurance that's sometimes isn't seen in a deal. There are common insurance issues and it is important to be able to drill down through them and understand them. So, if you get into a technical issue, you may not have in your traditional sources the capabilities that you would want. Furthermore, some of the issues can be addressed in a very straightforward fashion by language changes in the merger or acquisition agreement. In fact, many insurance issues can be addressed by changes to three or four provisions in an overall merger and acquisition agreement to protect everybody. The key is, of course, making sure that that language is in the deal.

**TWST: Who is the best adviser to conduct this type of due diligence? Is it the attorney, is it an insurance adviser or someone else?**

**Mr. Pasich:** Well, there is a selection. If you have a deal counsel who really knows insurance, that can work. It may be a combination of inside risk management and financial personnel with a broker, because sometimes you want to purchase new coverage on a going-forward basis to fill gaps. But I believe that there is a definite role for insurance coverage counsel. Even if it's not significant in terms of dollars expended, there is an important role for coverage counsel to play in these kinds of circumstances. And in the overall price tag of a deal, coverage counsel tends to be very inexpensive because they are looking for certain things. The only time where coverage counsel really has a potentially time-consuming role is if it's critical to analyze all the historic insurance coverage, look at the potential risks and liabilities that exist, and assess how

they are covered. But frankly, in that circumstance, if you need coverage counsel to have a significant role, then it's money well spent because if they don't do it, it doesn't get done.

**TWST: How is D&O insurance treated during the mergers? Does the new company take over the policy or are the Directors left on their own?**

**Mr. Pasich:** The answer is, "it depends." Most policies have what are called "change of control" provisions. These limit or terminate coverage if there is a change of control. And what these clauses typically say is if you consolidate with or merge or sell most of your assets to somebody else, that policy continues only as the covered events that took place before the transaction itself. What that means is that the transaction itself may result in the elimination of ongoing coverage. That means that you need to address how to cover the Directors and officers including former Directors and officers, on a going-forward basis, and that usually requires some new insurance coverage or an endorsement of the existing insurance coverage. And it's important to consider that in the deal documents; you need to put whatever requirements you want to have in there to ensure that it happens.

**TWST: Typically, what is the time frame that Directors need to be covered after the merger?**

**Mr. Pasich:** We know that too often mergers give rise to purported derivative actions or class action claims. Sometimes those claims are made quite quickly, but sometimes they come a few years later. Therefore, the answer for how long Directors and officers need to be protected is also, "It depends." I wish I could be more precise than that, but this coverage typically applies at the time a claim is made. So if one were to say that someone could sue a Director for four years after the transaction, then you need to make sure they are covered for four years. If it's two years, two, and if it's 10 years, 10, whatever the state law or federal law permits in terms of how long after the event someone can sue — that's the period of time you want coverage for.

**TWST: In running through your checklists, what are the items that seem to be most neglected by companies as far as insurance coverage? Is it liability insurance?**

**Mr. Pasich:** It varies. In this day and age, a lot of people pay attention to D&O insurance. So I would say it's probably historic liability insurance coverages that may not get the appropriate level of attention. And, by this, I mean the coverages going back in time, not just the coverage in effect at the time. I also think companies need to check other forms of coverage that are "claims made" coverage, where coverage applies when the claim is made. Many of these policies require that the claim be reported in the same policy period in which it is made to get coverage. These policies include Errors & Omissions, which is very important in the entertainment industry, intellectual property coverage, and fiduciary coverages. A company needs to make sure that claims have been timely reported, or will be, and needs to make sure that those coverages stay in place after the transaction. So, depending on what line of business the company is in, a company can overlook various coverages or can overlook various steps that are necessary to get coverage for claims under existing policies.

**TWST: Can you remedy the lack of coverages after the fact?**

**Mr. Pasich:** You can remedy them in a couple of ways. If you haven't done the deal yet, you can always go to the market or you can put in language in the deal document that gives you the ability to maximize the possibility of coverage. If you have done the deal and you haven't protected yourself on the insurance side, you can go out and acquire new insurance. If you have some lawsuits that you did not know about, you might even be able to get insurance for those. There is something called litigation risk insurance that can protect you on an after-the-fact basis. It's not as readily available as traditional coverages. The market isn't as broad and the pricing isn't as favorable typically. But there are some alternatives out there if the only other choice is going bare without any coverage.

**TWST: As you look at the environment, where do you see insurance fitting in, with regard to M&A due diligence?**

**Mr. Pasich:** I think companies will be more sensitive to the notion of looking at insurance, and so that will help. I think it's important to drill down through the potential coverage issues in a deal to determine whether you simply need to do drafting changes in the agreement or whether you need to actually spend time inventorying and analyzing the insurance and the risks that are out there. I think in the Sarbanes-Oxley world, where we are starting to see a lot of Chief Risk Officer positions created, the scrutiny and attention to insurance issues will increase. And I think it's necessary that it increases.

**TWST: With regard to an asymmetrical event, such as a terrorist incident or a large natural disaster such as Hurricane Katrina, what are the pre-existing coverages that acquirors need to examine concerning the companies that they are purchasing?**

**Mr. Pasich:** I think there are a number of things. With the possibility of terrorism attacks, you want to look at what terrorism coverage they have in place now, and you also want to make sure you assess where they do business and what measures they have that might minimize the cost of insurance or make it easier to get insurance. For things like Hurricane Katrina and other natural disasters, you have to take a look at what the deductibles are in your programs, whether they are dollar deductibles or percentage deductibles, for example, and you have to take a look at some things that may call for a detailed review of the policies. One example is with respect to hurricanes and floods. Some policies have exclusions or limitations on coverage based on whether any of the insured property is located in a 100-year or 500-year flood plain. Those are some concepts found in insurance policies that relate to how areas are recognized in terms of their flood history and affect the coverage available. So, for example, you might have \$100 million of flood insurance, but it could be greater or less if you're in one of the 100-year or 500-year plains. Those are the kinds of things where you have to look at details. You have to know where the properties are, and whether there are any historical classifications that might affect coverage. So you have to know something about the property and something about the policies — you have to know where to look and what to ask. Frankly, I wouldn't expect most corporate counsel to be familiar with those nuances because it is really an insurance specialty. If you look at those, you can figure out what the existing insurance is and you can determine how likely you are

to be able to get the kind of insurance you want at the levels you want on a going-forward basis. Those are the kinds of nuances that are important, particularly when you are looking at coverage for potential catastrophes.

**TWST: Can you offer any insurance-related due diligence recommendations to CEOs who are contemplating a potential acquisition?**

**Mr. Pasich:** I think the first and most important thing they can do is focus on this and make sure whatever the representation is, whether it is deal counsel, a broker, a consultant or coverage counsel, that they are being represented by folks who have experience in the M&A world with insurance issues in particular. That would be, I think, 90% of the battle.

Other than that, I do think there are some basic things that CEOs want to do, such as get a listing of all insurance policies in effect at the time (policy number, company, amount, deductibles, and policy period), find out whether any amounts have been paid under those policies because that may reduce how much coverage you

have, and then try to do the same thing on the coverages that may be important historically, like general liability coverage with the excess and umbrella, and go back and get a reconstruction of that coverage so you know the value of the asset. Insurance is an asset like anything else. It can be worth tens or hundreds of millions of dollars and it warrants the same level of attention and consideration that any other asset worth that kind of money gets in a deal.

**TWST: Thank you. (RT)**

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