Is Your Policy Panacea or Placebo?
The In-House Lawyers’ Guide to Safe and Effective Use of Insurance Coverage

Wednesday, October 28, 2015

Presented by: Carl Blumenstein, Partner
Scenario – Mergers & Acquisitions
Scenario – M&A

- Big Fish Corp. acquires assets and liabilities of Guppy Co., including Guppy’s CGL policies.
- Plaintiff sues for a pre-acquisition liability and Big Fish tenders to Guppy’s CGL insurer.
- Insurer denies coverage because it did not consent to assignment of the policy, as required by express policy term.
What result?
Scenario – M&A

(2003) 29 Cal.4th 934
Policyholder victory!

California Supreme Court adopts majority rule:
Anti-assignment clauses in CGL policies are not enforceable when policy is assigned after covered injury has occurred.

*Fluor Corp. v. Superior Court* (Aug. 2015)
2015 WL 4938295
Scenario—D&O—Rescission
Scenario—D&O—Rescission

- Due to misstatements in 10-Q, publicly traded company restated quarterly results. This led to federal securities class action and derivative liability lawsuits against company, Ds&Os.

- Although misstatements pre-dated policy inception date, they were not disclosed in policy application, signed by CFO.
Scenario—D&O—Rescission

- May a D&O insurer rescind coverage for innocent officers and directors where the CFO made material misrepresentations in application for policy?
Scenario—D&O—Rescission

Answer: You bet.


- *Ins. Code 650:* “[Rescission for misrepresentation] shall apply to all insureds under the contract, including additional insureds, unless the contract provides otherwise.”

- Policy language in Homestore policy not sufficient to come within exception.

**Practice note** — You can be proactive and negotiate more favorable “severability clause” at time of policy purchase.
Scenario—D&O—Rescission
Scenario—Product Defect
Scenario—Product Defect

- Component Manufacturer ships tens of thousands of its state-of-the-art widgets.
- Major Customer advises that the widgets are flawed, its product assembly is off-line, its costs are rapidly mounting as a result.
- Customer presses Manufacturer for immediate action, including compensation.
- Manufacturer has E & O insurance.
E & O Insurance – Product Defect

The key tension:
Policy Requirements vs. Customer Relationship
E & O Insurance – Product Defect

- Notice to insurer
  - Ensure internal report to legal/risk management
  - Is it a “claim”?
  - **Beware:** “Claims” must be timely reported

- What about the customer relationship?
E & O Insurance – Product Defect

- Is there a “defect” covered by policy? Should company admit “defect”?
  
  **Beware:** Policy prohibits admission

- What about the customer relationship?
E & O Insurance – Product Defect

- Who negotiates with customer?
  **Beware:** Insurer’s right to defend
- What about the customer relationship?
E & O Insurance – Product Defect

- Should you compensate the customer?
  **Beware:** “voluntary payments” clause
- What about the customer relationship?
Scenario—Data Breach—Claims by Others

© D. Fletcher for CloudTweaks.com
Scenario—Data Breach—Claims by Others

- Health care system suffers data breach exposing health records of thousands of patients.
- Records were accessible, not encrypted, no security.
- When lawsuit filed, insurer denies coverage.
Scenario—Data Breach—Claims by Others

What result?
Scenario—Data Breach—Claims by Others

Policy Exclusion
No coverage if insured fails “to take reasonable steps to use, design, maintain, and upgrade your system security”

Scenario—Data Breach—Claims by Others

Practice notes:

- Dynamic liability landscape—sundry claims, claimants
- Policy terms not settled, considerable variation
- Beware (!) of terms, exclusions
- Recommend: Consider manuscript coverage tailored to your company’s operations, exposures
Scenario—Data Breach—Company Expenses
Scenario—Data Breach—Company Expenses

Potential causes of harm — “risks”

- Virus
- Hacker
- System malfunction
- Theft of laptop
- Employee malfeasance
- Vendors/business partners
- Unique causes for your company/industry?
Scenario—Data Breach—Company Expenses

Cyber

There is an urgent need to act on cyber risks, including threats that originate across borders. Better global governance would be a significant step toward efforts to mitigate risks. A report by the ESADEgeo-Center for Global Economy and Geopolitics and Zurich reviews the challenges to this approach and offers innovative solutions.

ANATOMY of a HACK

> View now
Assess your vulnerability — in the office, at home and on the move

> Learn more
The impact of global privacy laws on cyber risk mitigation

> Learn more
A summary of the 2015 report on global cyber governance

> Read the report
An overview of the inadequacies of cyber governance and the challenges and opportunities presented by a new framework.

Cyber governance: A holistic and global approach

Related industries and products

> Technology

> Security and Privacy
Scenario—Data Breach—Company Expenses

What coverage MAY be provided???

- Restoration and repair of network/data
- Legal, consultant/forensic services
- Business interruption
- Mitigate negative publicity
- Lost funds
- Pay for extortion
- Unique needs for your business/industry?
Scenario—Data Breach—Company Expenses

- Cyber threats are real
- Insurers are motivated to sell insurance

.....Panacea or Placebo?
Scenario—Data Breach—Company Expenses

Practice Notes:

- Understand your business and the risks
- Obtain appropriate limits
- Specify preferred vendors
- Read policy language, exclusions
- Manuscript policy terms
Scenario—Clinical Trials
Clinical Trial Insurance

- **Purpose:** Insure liabilities arising from human clinical trials of drugs, medical devices
- Specialized policies
- Usually separate policy from GL, product liability, professional (E&O) liability (be aware of coverage “gaps”)
- Not much case law on these policies
Clinical Trial Insurance

- Global implications: Foreign nations may require local insurance, specified limits
- Risk management should coordinate with clinical research organization (CRO) and site management organization (SMO)
- Cautions: Application; timely notice of claims-made form; coverage gaps; exclusions
Maximizing the value of your insurance assets
Top Ten Eight Tips for Safe and Effective Use of Your Insurance Policies
#8 on Top Ten Eight List

Accuracy in the policy application

- Process/personnel to obtain accurate, complete facts
- Insurers will rescind based on misstatements
Always best to negotiate on the front end

- Be thoughtful about risks, coverage needs, retentions, business needs
- Especially unique, evolving coverages
- Consider manuscripted policies
- Consult with knowledgeable broker, counsel
#6 on Top Ten Eight List

Know Your Policies

- Prepare checklist (or have broker/risk manager do so)
- Types of coverage, covered risks, reporting requirements, limits, deductibles
- **Remember**: Additional insured on policies of others—How to track these?
#5 on Top Ten Eight List

Give timely notice of claims

- Establish internal communications
- Educate business people to report claims and circumstances
- Quarterly review
- Calendar policy expirations
#4 on Top Ten Eight List

Be alert to changes in risks/business

- Mergers/acquisitions
- Operations in new states/countries
- New product lines
#3 on Top Ten Eight List

“Right Attitude”

- Be persistent on claims
- Be creative
- Realistic client expectations
- Be prepared to compromise (if appropriate)
#2 on Top Ten Eight List

Know where to get help

- Insurance brokers
- Risk management
- Defense counsel
- Coverage counsel
#1 on Top Ten Eight List

“Read the Policy”
Questions?
For More Information Contact...

Carl Blumenstein
415.438.7219
cblumenstein@nossaman.com