

# Your Coverage Advisor

## Your 2021 Newsletter from Brouse McDowell



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The past year has been a busy one for Brouse McDowell's insurance recovery practitioners. An evolving workplace model and ongoing fall-out from the COVID-19 pandemic have continued to impact the insurance market, including the types and frequency of insurance claims. More than ever, policyholders are seeking our counsel to assist them in selecting and purchasing insurance coverage that will shift the risks of their enterprise and function in the manner contemplated at the time of purchase.

The importance of understanding the coverage being purchased before a loss or injury occurs has been highlighted, in no small part, by the experience many companies have had with insurance claims related to COVID-19. The news is flooded with stories of policyholders whose claims have been unexpectedly denied by their insurers. Of course, business interruption coverage for COVID-related losses is still a hotly litigated issue, in both federal and state courts nationwide. Our insureds also continue to demand that insurers honor their obligations under other types of policy coverages—communicable disease, environmental, and event cancellation. Until state supreme courts decide many of these issues, however, coverage for COVID-19 losses is likely to continue to be contested.

Brouse has also seen several of its clients shift their business models to permit, or even require, regular remote work. This fact, and the evolving nature of cyber risk, highlighted in this newsletter, have made procuring sufficient cyber insurance coverage more

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Insurance Coverage Newsletter  
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critical than ever. For some, though, obtaining comprehensive cyber coverage at reasonable premiums has been a challenge. This is also true in other markets, including directors & officers and property & casualty.

Rising risk awareness, the pandemic, increasing natural disasters, stock market volatility, and an unprecedented number of insurance claims have created a “hard” insurance market. This impacts policyholders in several ways. In underwriting, insurers are likely to raise premiums, reduce the number of policies they issue, refuse to insure certain risks, and narrow the scope of coverage.

With respect to claims, insurers are likely to deny claims with more frequency and are less likely to negotiate reasonable resolutions of disputed claims with their insureds.

Brouse McDowell has been assisting our clients with their insurance coverage needs for decades—in both soft and hard markets—from working with insurance brokers to understand and negotiate policy terms, to advocating zealously for our clients when claims are wrongfully denied. In this issue, we discuss some things on the horizon, as well as issues facing our corporate clients with increasing frequency. ■

## Publications & Media Mention Highlights

**Stacy RC Berliner** and **P. Wesley Lambert** noted in *Law360's* article “Three Insurance Appeals To Watch At State High Courts in March.”

**Stacy RC Berliner** and **Amanda M. Leffler** presented for the northeast Ohio Chapter of RIMS on “Shifting Risk: Drafting Contractual Insurance and Indemnity Provisions to Provide the Protection you Contemplated.”

**Andrew W. Miller** spoke at an OSBA CLE program titled “National Developments in Insurance Coverage: A Year in Review.”

**Amanda M. Leffler** and **P. Wesley Lambert** noted in *Westlaw* and *Law360* regarding first-of-its-kind in Northern District of Ohio Zoom jury trial resulting in a successful verdict for client.

**Joseph K. Cole** wrote a blog “COVID Coverage Cases Turn on Policy Language.”

**Brandi L. Doniere** and **Amanda M. Leffler** presented at Strafford Publication's Virtual CLE titled “GC's Role in Remote Work Legal Issues: Data Governance, Privacy, Automating Documentation, Employee Communication.”

**Anastasia J. Wade** wrote a blog “Reimburse Your Insurer? Look to the Recent Decision by the Nevada Supreme Court.”

**Jarman J. Smith** wrote a blog “Recent Cyberattacks Complicate Cyber Insurance Industry and Coverage.”

**Joseph K. Cole** noted in *Law360's* article “Policyholder Attys Eye Ohio Justice's Role In COVID-19 Fight.”

**Paul A. Rose** noted in *Law360's* article “Drug Co. Owed Defense In Opioid Suits, Ohio Justices Told.”

**Joseph K. Cole** and **Lisa M. Whitacre** wrote an article for the *Cleveland Metropolitan Bar Journal* titled “Managing Supply-Chain Risks Through Insurance.”

# Cyberattacks in 2021 Demonstrate Importance of Cyber-Risk-Insurance for 2022



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As cyber-related incidents continue to grow in number, we are advising companies to place even more emphasis on Cyber Risk Coverage for 2022. The volume of new clients seeking out representative breach counsel regarding cyber-attacks grew immensely in 2021. As a result, Brouse has been called to action in an expanded capacity. From this firsthand experience, we have observed the need for many businesses and organizations to prioritize cyber-risk insurance coverage to contain their liability in the event of a cyber-incident. Along with prioritization comes scrutinization of the policies and the coverage being provided. As companies and policyholders alike increase their awareness of digital threats and their knowledge of coverage-related issues, the cyber-risk insurance industry is being called upon to provide not only an increase in coverage, but also adequate, or even new coverage, in historically weak areas to help ease liability concerns resulting from an alarming number of cyberattacks that wreaked havoc throughout 2021.

## Cyber-Risk Insurance Essential to Addressing Cyberattacks

We can expect another increase in cyber-related attacks this year. Cyber-related impact events such as ransomware and data breaches continue to remain our number one focus as we head into 2022. Looking back at 2021, the Identity Theft Resource Center reported that the number of

data breaches in 2021 surpassed 2020's figure even with three months remaining in the year.<sup>1</sup> As the tactics of cybercriminals continue to evolve and become more sophisticated, we can anticipate that the number of data breaches in 2022 will be even higher than the numbers in 2021. So how can organizations best protect against cyber risks in the year ahead? By prioritizing cybersecurity companywide, including compliance and incident response planning, along with obtaining a comprehensive cyber-risk insurance policy, companies will be ahead of the curve when it comes to mitigating damages of an inevitable attack.

Cyber-risk insurance can be thought of as a collection of coverages that protect your company from a variety of incidents, including data breaches, ransomware attacks, digital destruction, and the resulting damages of the foregoing. A comprehensive cyber-risk policy will likely include more than a few separately identified coverage options, but there are four essential coverages that we would advise all companies to carry to protect your interests during a cyber incident.

## Extortion Coverage

Extortion coverage operates as ransomware recovery support. It can provide monetary reimbursement if your organization is forced to pay a ransom to regain access to compromised systems and/or for the return of stolen data.

<sup>1</sup>See <https://www.propertycasualty360.com/2021/12/29/cyber-insurance-in-2022-a-year-for-collaboration/>.

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If properly obtained, this coverage may also cover the cost of hiring professionals, such as competent legal counsel, to negotiate with the cybercriminals on your behalf. In 2021, the average ransomware payment increased by 82%. A ransom demand can be crippling for many businesses and can provide a swift ending to many small businesses. With an increase in attacks in 2021, it's more important than ever to build up your defenses in anticipation of a cyber event. Now is the time to ask your professional team to do a complete cyber-risk audit to uncover any gaps in your cybersecurity protocols.

### **Business Interruption Coverage**

Business interruption coverage is designed to compensate you for the loss of income that results from the downtime your organization may face after a cyber incident. If your system or network was paralyzed, corrupted, or otherwise made inaccessible as a result of a cyberattack, your business could come to an abrupt halt. And when operations are down, lost revenue is a certainty. Business interruption coverage can cover expenses you incur related to your efforts in restoring your operations.

### **Data Loss/Data Restoration Coverage**

Data restoration coverage is designed to cover the costs of replacing or restoring compromised data resulting from a virus, ransomware, or another form of cyber incident. Most businesses would like to act with urgency to quickly and fully recover their data after a cyberattack. Doing so can reduce downtime and can help restore trust in your business.

### **Incident Response Coverage**

Incident response coverage covers expenses related to the various expert services that your organization may need to remediate the effects

of a cyber incident, to restore security protocols and prevent future security issues. For instance, a data breach can require a thorough investigation by a computer forensics team to determine the breach cause and prevent future occurrences. You will also need to enlist the services of competent cyber legal counsel and—depending on the level of breach—you may need a public relations firm, and consumer ID monitoring and notification specialists.

### **How Brouse Can Help**

Ransomware and other cyber-related incidents will likely remain the number one threat to companies in 2022. Organizations must be prepared to do everything they can to mitigate the damage of an inevitable attack. We advise having cyber legal counsel conduct a review of your existing policies and protocols in place to ensure compliance with all data privacy laws and regulations, revise and update those that need attention, review existing insurance and fill any gaps to obtain appropriate levels of cyber-risk insurance to further reduce exposure to cyber-related risks. Cyber-risk insurance is complex, and it may leave many confused as to what adequate coverage looks like. Failing to obtain the right coverage could leave your organization exposed to substantial risks in the event of a cyber incident. It is important to have assistance from competent professionals as you analyze your security and seek to obtain cyber coverage. Brouse McDowell's Insurance Recovery and Cybersecurity & Data Privacy teams can provide the guidance and tools you need to defend against cyberattacks, protect consumer information and obtain proper cyber-risk insurance coverage. Please contact us for more information and to learn how we can partner with you. ■





## Tips for Managing Supply Chain Risks



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Anyone who has purchased, or tried to purchase, a new vehicle, a bicycle for their child's birthday (speaking from personal experience), certain electronics or appliances, or other high demand products or services has likely experienced the effects of global supply chain disruptions causing businesses both big and small to struggle to meet demand or even continue operating. The reasons for these disruptions are complex and multi-faceted, but there is little doubt that the global pandemic has and continues to play a significant role. Some predictions however, anticipate that supply chain disruptions will continue for the next year or more and could outlast the global pandemic.

So how does a business manage supply chain risks? One tool is insurance. Below are four tips for maximizing insurance as a strategy for managing supply chain risks.

**(Continued on page 6)**

## Tips for Managing Supply Chain Risks (Continued from page 5)

### Know and Understand Your Policies

A policyholder may have a number of different types of policies that cover different losses, including:

- **Business interruption (BI) coverage that covers a policyholder's lost profits if the policyholder's operations are interrupted due to a covered peril. BI insurance provides coverage for lost earnings and may also cover expenses like rent, utilities, and employee wages.**
- **Extra Expense Coverage that covers certain additional expenses in excess of normal operational costs that a policyholder may incur, enabling the policyholder to continue operations while its property is repaired or replaced after a covered loss.**
- **Contingent Business Interruption (CBI) insurance helps cover a policyholder's financial losses related to disruptions of a covered supplier, partner, manufacturer, or major customer that negatively impacts a policyholder's ability to operate.**
- **Supply chain coverage is a specialty "all risk" insurance designed to protect policyholders from a failure in their supply chain.**
- **Other specialty insurance and manuscript policies – there are other specialty insurance products available in the market, and many businesses, particularly larger businesses, negotiate manuscript policies that are tailored to meet their specific needs.**

The specific terms, exclusions, and endorsements in these policies vary greatly. For example, BI and extra expense coverage often, but not always, require physical loss or damage to covered property. These policies typically cover the policyholder's property (as opposed to a supplier or customer) and therefore will not cover losses arising out of physical loss or damage of a supplier's property or facility. CBI insurance, which would cover a

supplier or customer, may also require physical loss or damage; however, many CBI policies, particularly foreign ones, do not have such a requirement.

**For policyholders seeking coverage because of disruptions related to COVID-19 and related government shutdown orders, policies without a physical loss or damage requirement are more likely to provide coverage.**

Whether there is coverage under policies with a physical loss or damage requirement is dependent on whether a "physical loss" has occurred. Courts across the country have struggled with that question reaching differing results. The Ohio Supreme Court is expected to address the issue this year in *Neuro-Communication Servs., Inc. v. Cincinnati Ins. Co.*, No. 2021-0130. Another important consideration is whether the policies have a virus/bacteria exclusion and whether the policies include or exclude communicable disease coverage. Knowing which policies you currently have and understanding what they cover is critical.

### Know and Understand Your Supply Chain and Identify Potential Coverage Gaps

Understanding the ins and outs of your supply chain is also critical in managing the risks

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## Tips for Managing Supply Chain Risks (Continued from page 6)

associated with it. A small business transacting locally or even within the continental United States is less likely to run into the same sorts of risks as organizations with complex supply chains, international suppliers, or suppliers in politically unstable areas, and those differences help determine whether CBI, supply chain, or other specialty coverage makes sense for your business.

Where more complex coverage is warranted, it is important to take a hard look at your supply chain. Here are a few questions to consider:

- **Should just the first tier of suppliers or the entire supply chain be covered?**
- **Are there certain products or materials where no viable alternative supplier is available?**
- **Are there suppliers or customers that are critical to the continued operations of your business?**
- **Are there unique risks associated with your business that justify obtaining a manuscript policy specifically tailored to those risks?**

These considerations must be balanced with the cost of obtaining additional coverage. The takeaway is that there isn't a one size fits all approach when it comes to managing your supply chains risks.

### Identify Current Disruptions

Navigating an existing disruption can be harrowing, though pinpointing the precise location and, sometimes, like in today's supply chain, multiple locations of the disruption can reveal coverage triggered under one or more existing policies. For example, your business may experience disruptions related to a government order requiring a first-tier supplier to shut down while at the same time, a second-tier supplier may be experiencing staffing shortages and production delays. On top of that, necessary materials or parts may be delayed at sea. Fully understanding each of these unique disruptions in the whole of your organization's supply chain will be invaluable in assessing potential coverage.

### Document all Potentially Covered Losses

Get in the habit of documenting all losses, including those you believe are covered and those you're not so sure about. As the pandemic and supply chain disruptions continue to wreak havoc, economic risks and the legal landscape continue to evolve. Whether a claim is covered depends on the specific terms, exclusions, and endorsements of your policies, all of which are interpreted by our courts in light of the circumstances of the claim. What you assume is an uncovered loss, could, in fact, be covered by one or more policies. ■

## 2022 Ohio Supreme Court Update



By Lucas M. Blower  
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The way most general liability insurance policies are structured is that they start off with a very broad coverage grant, applying to all damages that the insured becomes legally obligated to pay because of bodily injury or property damage caused by an occurrence. An occurrence, in turn, is defined broadly as an "accident, including continuous or repeated exposure to substantially the same general harmful conditions."

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After this broad coverage grant, the policy will usually include a battery of exclusions that narrow the coverage.

So, following this broad structure, a typical insurance policy will give with one hand (the coverage grant) and take away with the other (the exclusions). And because the coverage grants are traditionally so broad, for most first-party and third-party risks, the question of coverage comes down to the exclusions—that is, whether the other hand took away what was given in the coverage grant.

But now, in a pair of insurance cases pending before the Ohio Supreme Court, insurers are attempting to subvert this usual structure. Instead of focusing on whether the exclusions apply, they argue that the risk does not fall in the broad coverage grant in the first place. It does not matter, according to these insurers, whether the exclusions took away coverage because as they argue, it was never given in the first place.

In *Motorists Mutual Ins. Co. v. Ironics, Inc.*, the policyholder sold defective tube scale to its customer. Tube scale is a product used to make glass bottles. Because the tube scale was defective, the resulting glass bottles were unusable. The policyholder's customer demanded to be reimbursed for the damage. The policyholder, in turn, tendered the claim to its insurer, who denied the claim.

Now, most liability policies have an exclusion for damages to “your product”—meaning the insured's product. This makes sense, since liability policies in general cover damage to third-party property, not the policyholder's property. (Those sorts of losses are covered by first-party insurance, which is subject to its own slate of exceptions.)

In *Ironics*, though, the policyholder has a strong argument that the exclusion for damages

to “your product” did not apply. This is because the ultimate damage was not to the policyholder's product—the tube scale—but to its customers product—the glass bottles.

The insurers in *Ironics* disagreed with this interpretation of the exclusion, arguing that it applied to the glass bottles because they were integrated products, such that the glass bottles were inseparable from the tube scale. But the insurers also went further, questioning the premise of whether the loss was insured in the first place.

According to the insurers, regardless of whether the “your work” exclusion applied, the loss was not covered because it was not “fortuitous.”

The Ohio Supreme Court first invoked the “doctrine of fortuity” in *Westfield Ins. Co. v. Custom Agri Sys., Inc.*, 133 Ohio St.3d 476, 2012-Ohio-4172, 979 N.E.2d 269, a case holding that liability insurance does not generally cover damages for claims of alleged defective construction and workmanship to the insured's own work. The Ohio Supreme Court held that—to count as “property damage” caused by an “occurrence”—the damage had to be fortuitous.

But it was not clear from *Custom Agri* what the so-called fortuity doctrine added to the traditional analysis. It was always the case that general liability policies applied only to accidental damage. So, it was never clear what a fortuity element added. It seems incoherent to say that a loss could be accidental but not fortuitous. But, if this is what the Ohio Supreme Court was holding—i.e., that there were non-fortuitous accidents—how were policyholders supposed to tell the difference? And what basis was there in the policy language to distinguish between different types of accidents, fortuitous on one side and non-fortuitous on the other, when the language of the coverage grant applied to all accidents?

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## 2022 Ohio Supreme Court Update (Continued from page 8)

These distinctions were never fully addressed in *Custom Agri* or in subsequent cases. Predictably, then, in later cases, such as *Ironics*, insurers seized on the “fortuity” doctrine, arguing to expand it to preclude coverage for even more types of accidental losses. The whole project, though, is only possible if insurers are permitted to introduce new concepts such as an ill-defined “fortuity doctrine,” in the coverage grant, where they don’t belong.

What’s more, once the insurers got a taste for adding restrictions into the coverage grant, they did not stop with the fortuity. In *Acuity v. Masters Pharmaceutical*, for example, another case pending before the Ohio Supreme Court, the insurers are arguing the term “legally obligated” in the coverage grant applies only to tort liability.

The policyholders in *Acuity* are manufacturers and distributors of opiates. The insureds were sued by local and state governments claiming they had to pay increased costs for medical and police services, among others, as a result of the opiate epidemic. The governments are seeking to recover against the manufacturers and distributors based on their role in setting off the epidemic.

The policyholders tendered the government’s claims to their insurers, which denied the claims for a number of different reasons. Most relevant here, the insurers argued that the claims were not covered because the governments’ claims were for economic damages, not direct tort liability for bodily injuries. As such, according to the insurers, the losses were not covered because the terms “legally obligated to pay as damages” in the coverage grant “clarifies that [to be covered] the insured’s obligation must arise from the breach of a non-contractual duty.” (Appellant’s Reply Br. 6.) So according to the insurers, the coverage grant is restricted to traditional tort liabilities.

As an initial matter, it is not clear that this supposed tort restriction on the coverage grant would have any bearing on the policyholder’s claims in *Acuity*. After all, the governments are not suing the policyholders for breach of contract. They are suing in tort. So even if the insured’s purported tort restriction existed, it wouldn’t preclude coverage in *Acuity*.

More importantly though, for our purposes, there is no tort restriction in the coverage grant. The policy applies to damages that the insured is “legally obligated to pay as damages.” The

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## Appointments & Promotions

**Stacy RC Berliner** named Co-Chair of the firm’s Insurance Recovery Practice in January 2021.

**Stacy RC Berliner** named Co-Chair of the Insurance Law Section of the Cleveland Metropolitan Bar Association.

**Joseph K. Cole** selected to serve on the Screening Committee of the Ohio State Bar Association Council of Delegates for 2021-2022.

insurers argue that this phrase applies only to non-contractual duties. But they provide no compelling reason for this proposed restriction. The language does not say “legally obligated *in tort*.” As such, it applies to *all* legal obligations. And it should not be a matter of great controversy that contractual obligations are, in fact, legal obligations (though the insurers’ confusion on this point is perhaps more telling than they realize).

Both of these cases—*Ironics* and *Acuity*—demonstrate a coordinated effort amongst insurers to restrict the coverage grant beyond what is warranted by the language in the policy. Policyholders and the courts should resist these efforts. Every policy gives coverage in one hand and takes it back in the other. But the takebacks should happen in the text of the policy. And if the insurers didn’t take back coverage in their exclusions, the courts shouldn’t do it for them. ■

## Utilizing Representations and Warranties Insurance in M&A Transactions and Related Financing



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Merger and acquisition (M&A) transaction participants are increasingly using representations and warranties (R&W) insurance to provide coverage for breaches of R&W in purchase agreements. In the last few years, R&W insurance has become a commonplace insurance product and a mainstay component of private M&A transactions north of \$50 million.

We spoke with insurance broker Hylant’s T.J. Noonan, Managing Director, Transactional Risk, who specializes in placing R&W insurance. According to Noonan, current policy limits range from \$3 million up to \$1 billion. Typically, this equates to deal sizes of \$20 million to \$10 billion, with deals between \$50 million and \$500 million being the most common. Noonan confirmed 2021 underwriting activity for M&A transactions for less than \$30 million. In these deals, buyers obtain a higher proportion of

coverage to the deal value (i.e., greater than 10%), with minimum out-of-pocket costs for a buyer ranging from \$160,000 to \$200,000, for a \$3 million limit.

An R&W insurance policy protects an insured against financial loss—including defense costs—resulting from breaches of such R&W, and in certain cases covers indemnification in the purchase agreement. This type of insurance can be used by public and private entities, in both change of control situations and non-

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## Utilizing Representations and Warranties Insurance in M&A Transactions and Related Financing (Continued from page 10)

control minority investments. In addition to the standard exclusions discussed below, R&W insurance does not cover breaches in covenants in the purchase agreement.

### Policies Can be “Seller Side” or “Buyer Side”

R&W insurance can be purchased as either “Seller Side” or “Buyer Side” coverage.

Seller Side policies serve as a liability policy providing coverage to the seller for its liability for claims for breach of R&W in the purchase agreement made to the buyer. This type of policy would pay the seller as named insured, *not the buyer*. By comparison, a “Buyer Side” policy is a form of first-party coverage that allows the buyer to be compensated directly by the insurer. A common added variation to “Buyer Side” policies also protects the seller by preventing the insurance company from seeking recovery from the seller except in cases of fraud. We highly recommend this variation be explored for our clients that are sellers.

When Hylant assists its clients in obtaining R&W insurance, the named insured is often the buyer in the transaction, with lenders providing

acquisition financing as additional insureds. By having the buyer and lender as named insured and additional insured, respectively, they can be paid directly from the insurer. This mitigates any collectability issues or controversy presented, which is desirable in distressed transactions or transactions with more than a single selling shareholder. In the event of a breach of any R&W in the transaction, after accounting for the retention, the insured would receive a payment to offset their loss up to the maximum policy limits.

### Introducing R&W Insurance in the Deal

Sellers utilizing an investment banker led competitive bid or auction process often stipulate R&W insurance as a bid qualification and a means they are proposing to avoid an escrow. By comparison, buyers seek R&W insurance when indemnity is limited or absent, or when escrow is not able to be obtained. Since indemnity provisions are often the most negotiated section in purchase agreements, R&W insurance provides a mechanism for parties to bridge the gap by shifting risk of breaches in R&W made by the seller and the collectability of indemnity to an insurer in

## R&W INSURANCE BENEFITS

BUYERS	SELLERS	LENDERS
<ul style="list-style-type: none"> <li>■ Adds protection to indemnity cap and survival periods</li> <li>■ Provides recourse in absence of seller indemnity</li> <li>■ Preserves key relationships</li> <li>■ Ensures collectability</li> <li>■ Enhances competitive bids</li> <li>■ Offers protection to deal financing creditors</li> </ul>	<ul style="list-style-type: none"> <li>■ Provides backstop or replaces negotiated indemnity</li> <li>■ Eliminates or reduces escrow</li> <li>■ Allows minority sellers to avoid joint and several liability</li> <li>■ Provides peace of mind for family and individual sellers</li> <li>■ Enhances disclosure schedules</li> </ul>	<ul style="list-style-type: none"> <li>■ Offers longer term than reps and warranties in purchase agreement</li> <li>■ Allows lenders to be additional insureds; and collectability is direct from insurer</li> <li>■ Enhances underwriting</li> <li>■ Mitigates risk presented by escrow or absence of conditions precedent</li> <li>■ Facilitates prepayments in specific circumstances</li> </ul>

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## Utilizing Representations and Warranties Insurance in M&A Transactions and Related Financing (Continued from page 11)

exchange for a policy premium by providing the buyer, as the named insured, the ability to collect from the insurer. Banks and other lenders providing credit are increasingly requiring R&W insurance as a condition of term sheets and a means to shift risk. The following table provides a summary of the benefits available to buyers, sellers, and lenders.

### Policies are Deal-Specific

R&W insurance is unique in that it is fully customizable and negotiated on a deal-specific basis. Policy limits typically range between 10-20% of the enterprise value of the transaction with retentions set at 1% to 3%. Premiums typically range from 3.5-5% of the policy limits. Because of the time-intensive underwriting, insurers are less motivated by deals below policy limits of \$3 million and charge underwriting fees of \$15,000 to \$40,000.

Insurance capacity for the R&W product is robust comparable to other areas in the insurance market. Capacity in this relatively new market continues to be positively affected by insurers attempting to enter this market.

### Recognizing Limits of Risk Transfer

Buyers need to recognize that R&W insurance, while a means to transfer risk from the buyer's balance sheet, does not provide as broad of coverage as a seller escrow of the same size. For example, R&W insurance does not provide coverage for covenants and special indemnities provided in transactions or information disclosed in due diligence. Buyers also need to account for premiums, retention, and underwriting fees for R&W insurance that the buyer will pay as part of their deal models.

Likewise, each insurer's policy will be different, and it is important to read and know the differences before procuring the product and to tailor those to the policyholder's needs and the circumstances surrounding the deal. Many R&W policies contain the following exclusions:

### R&W INSURANCE: STANDARD POLICY EXCLUSIONS

- Asbestos/PCB
- Healthcare Billing and Coding
- Criminal Fines and Penalties
- Net Operating Losses
- Insured's Actual Knowledge at Binding of Coverage
- Pension Underfunding/Withdrawal Liability
- Medicare/Medicaid Reimbursement Risks
- Post-closing Purchase Price Adjustments
- Transfer Pricing

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## Utilizing Representations and Warranties Insurance in M&A Transactions and Related Financing (Continued from page 12)

Hylant's Noonan explained that industry norm is that retentions are cut by 50% after year one. This is primarily driven by the fact that 66% of claims (greater than \$1 million) are reported within the first year, according to *AIG's Claims Intelligence Series*. See *AIG Claims Intelligence Series: M&A: A rising tide of large claims*, at page 4 (available at [www.aig.com/business/insurance/mergers-and-acquisitions/mergers-and-acquisitions-claims-reports](http://www.aig.com/business/insurance/mergers-and-acquisitions/mergers-and-acquisitions-claims-reports) (visited Feb. 18, 2022)). Because this is a customizable product, policies often have a step down of the retention after the expiration of any indemnities provided by the seller under the purchase agreement.

Underwriters are also known to provide coverage for pre-sale tax indemnities covered in the purchase agreement. Certain fundamental representations may be able to obtain nil retention if made as part of the transaction related to authority to conduct the transaction, ownership of shares, and no brokers other than as listed on disclosure schedules.

### Underwriting Process

The underwriting process is becoming increasingly more stringent. Required information serving as the foundation for the underwriting process includes:

- **draft purchase agreement,**
- **offering memorandum,**
- **any documents describing target's business,**
- **a copy of recent financial statements, and**
- **existing due diligence reports and data room information.**

Insurers will also expect to participate in conference calls with the insured's deal team. Typically, audited financial statements and a quality of earnings report from a qualified external CPA are required before binding of coverage by underwriters. This last requirement can take eight (8) weeks or more.

Due diligence trends related to enforcement of matters on regulators' radar, past litigation history, environmental concerns, and long-term liabilities are always key concepts that underwriters are keen to address. According to Noonan, employment-related claims such as independent contractor vs. employee classification continue to receive increased focus from underwriters.

### How Brouse Attorneys Can Help

Because of the unique nature of the underwriting of this risk, it is important for purchasers of R&W insurance to have a trusted adviser helping them to negotiate terms of the policy and to ensure it is customized to meet their objectives. Brouse attorneys are experienced in negotiating terms of R&W insurance and in serving as liaison with insurers for companies involved in transactions. Our insurance team is accustomed to augmenting our firm's deal lawyers to facilitate obtaining insurance, negotiating on exclusions, the closing of deals, and working with our clients' deal lawyers at other firms to ensure the best coverage possible is obtained. Should you need help with M&A insurance due diligence, please do not hesitate to reach out. ■

# Maximizing Coverage for Government Investigations



By Stacy RC Berliner  
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The Biden administration and government agencies have indicated that in 2022 companies will see an increase in investigations, regulatory oversight, and enforcement actions by the U.S. Securities and Exchange Commission (SEC) and Department of Justice (DOJ). Specifically, government agencies have stated that they intend to take an aggressive approach regarding anti-corruption and compliance, failure of entities to maintain adequate cybersecurity practices and controls, regulation and compliance surrounding cryptocurrencies, environmental investigations and enforcement, and climate disclosures and risk.

Typically, the government's first step is an investigation, which involves letters requesting information, subpoenas, civil investigative demands (CIDs), or formal orders of investigation. Investigations require engaging experienced counsel, reviewing and producing documents, preparing and conducting witness interviews and testimony, and responding to numerous inquiries. They can be disruptive and expensive. That's why it is imperative that companies re-examine their insurance policies and take steps to maximize coverage.

Coverage often depends on whether subpoenas, CIDs or other documents issued as part of governmental investigations, constitute a "claim" alleging a "wrongful act" as defined by your D&O, E&O, or professional liability policies.

## **Do I Have a Claim That Can be Covered?**

What constitutes a claim can vary greatly between policies. Some policies only cover

"regulatory investigations commenced by formal orders of investigation," while others expressly exclude "investigations of an organization." These narrow definitions are problematic to obtaining coverage if the government agency merely issues a letter requesting information – albeit one the company cannot ignore. Other policies, which define a claim to include "investigations of the Insured related to a Wrongful Act" or for costs associated with responding to "informal information requests", are more likely to provide coverage.

## **Does the Government's Investigative Document Allege a Wrongful Act?**

A wrongful act is typically defined broadly to include an actual or alleged breach of a duty, neglect, error, misstatement, misleading statement, omission, or act by the policyholder. Insurers argue that a subpoena or CID does not and cannot "allege" a wrongful act, but merely ask for documents or testimony.

**(Continued on page 15)**

## Maximizing Coverage for Government Investigations (Continued from page 14)

Some courts have agreed with insurers. See, e.g., *MusclePharm Corporation v. Liberty Insurance Underwriters, Inc.*, 712 Fed.Appx. 745, 754 (10th Cir. 2017). However, other courts examine the subpoena or CID more carefully to determine whether it, or the letter accompanying it, alleges violations of law or statute. The Delaware Superior Court held that a CID which stated the government was investigating possible Medicaid fraud and activities, **does** allege a Wrongful Act. *Conduent State Healthcare, LLC v. AIG Specialty Ins. Co.*, No. CVN 18C12074 MMJCCLD, 2019 WL 2612829, at \*6 (Del. Super. Ct. June 24, 2019). Increasingly, SEC subpoenas, tolling agreements, and CIDs include language where the government expressly states that there is

a possible violation of various federal criminal statutes and, thereby giving policyholder's the argument that the document does allege a Wrongful Act and coverage should be afforded.

Coverage often turns upon the specific definitions in your policy, the types of documents issued by a government agency, types of proceedings initiated by the government, and geographic locations of the dispute. With an increase in investigations on the horizon, companies should waste no time in re-examining policy terms and attempting to negotiate more favorable terms if necessary.

If an investigation begins, timing and tenacity could mean the difference between a covered and uncovered claim. Policyholders should take steps to maximize their coverage for these investigations. ■

## Steps to Maximize Coverage for Government Investigations

- 1. Upon notice of a government investigation or receipt of a subpoena, CID, or similar document: contact the person responsible for insurance—risk manager, general counsel, broker, or outside counsel—to examine and evaluate claims of coverage. With the ever-changing law, complexity of investigation, and differing policy language, be cautious that coverage is often misunderstood; bad advice can cost you.**
- 2. Gather all applicable policies – D&O, E&O, EPLI, and professional liability policies.**
- 3. Review all policies. Analyze what constitutes a claim; what constitutes a Wrongful Act; and who qualifies as an Insured.**
- 4. Strictly follow the notice requirements. When in doubt, provide notice. Some claims require immediate notice. Some policies may require notice when the insured has knowledge of potential claims, Wrongful Acts, or related acts. Demand an immediate defense in the notice letter.**
- 5. Actively pursue coverage.**
  - Respond to all mischaracterizations of fact and coverage.
  - Keep the insurer apprised of the investigation.
- 6. Engage insurance recovery counsel, if needed, to enforce your rights under the policy(ies).**

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## Accolades

**The Insurance Recovery Practice** was recognized for the second year in a row by *Chambers USA 2021* in Band 1 for Insurance: Policyholder (Ohio) and **Stacy RC Berliner, Lucas M. Blower, Amanda M. Leffler, Andrew W. Miller,** and **Paul A. Rose** were ranked as leading practitioners.

**The Insurance Recovery Practice** was recognized by *U.S. News – Best Lawyers’ “Best Law Firms” 2022* in Tier 1 for Insurance Law (Akron, Cleveland, and Fort Myers) and Tier 1 for Insurance Litigation (Akron).

Recognized by *The Best Lawyers in America 2022* – **Christopher J. Carney, Clair E. Dickinson, Amanda M. Leffler, Joseph P. Thacker,** and **Richard S. Walinski** for Commercial Litigation; **Stacy RC Berliner, Lucas M. Blower, Amanda M. Leffler, Paul A. Rose,** and **Joseph P. Thacker** for Insurance Law.

**Joseph K. Cole** and **Nicholas J. Kopcho** noted as “Ones to Watch” by *The Best Lawyers in America 2022* for Insurance Law.

Recognized by *Ohio Super Lawyers 2022* – **Stacy RC Berliner, Lucas M. Blower, Amanda M. Leffler,** and **Paul A. Rose** for Insurance Coverage; **Christopher J. Carney, Kerri L. Keller, Nicholas J. Kopcho, P. Wesley Lambert,** and **Richard S. Walinski** for Business Litigation.

Recognized as Rising Stars by *Ohio Super Lawyers 2022* – **Alexandra V. Dattilo** for General Litigation and **Nicholas J. Kopcho** for Business Litigation.

**Joseph K. Cole** received the UToledo Emerging Leader Award from the University of Toledo College of Law.

**David Sporar** recognized by *Who’s Who in America* for 2021.

Save the date for our upcoming  
**Insurance Coverage Conference**  
on Thursday, October 20, 2022.