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# Digging deep, seeking leverage



Auditing a potential acquisition's insurance coverage is an essential task for any prospective purchaser

**By Meg Fletcher**

**F**erretting out a potential acquisition's liability exposures and insurance coverages may determine whether a merger boosts assets or drains them, experts say.

A comprehensive audit of a potential acquisition's insurance coverage "is an essential part of due diligence for any prospective purchaser or merger," said Sheila Mulrennan, the president of IAG Ltd. in New York.

The 20-member Insurance Archaeology Group, which she founded in 1985, has documented more than \$200 bil-

lion in prepaid insurance assets on behalf of clients.

IAG's clients include insurers that request its services on behalf of policyholder clients or themselves. Researchers often examine the records of insurers and agent/brokers to reconstruct policyholders' decades-old coverages.

"To do insurance archaeology often requires the skills of a detective, an historian, a claims specialist, a diplomat and an excavator," Ms. Mulrennan said.

Reconstructing policies requires negotiating access to records, interviewing former employees, reviewing accounting records, examining brokers'

slips and sometimes searching government archives.

Michele Pierro, IAG executive vp, described one quest that took her to a onetime salt mine where a company had stored its oldest records. "To get there, we had to take an outdoor platform elevator," she said. "We were lowered down into an underground city where 150 years of records were shrink-wrapped against damage from water" as well as other critters that sometimes share researchers' interest in old paper—vermin, birds and bats—she said.

In another project, Ms. Mulrennan

has had to don a protective white suit, gloves and shoes to review some radon-contaminated records.

"You can't see the contamination but you can hear the Geiger counter clicking wildly," as it measured the amount of radioactive gas to ensure that it did not exceed safe levels, she said.

Typically, "I think almost everyone attempts to organize and assemble all the relevant insurance policy information, but they may not go back as far as they could, or should," Ms. Mulrennan said.

Such research is especially important if claims involve product manufacturing that result in toxic torts such as asbestos as well as environmental contamination and cleanup, which are all problems that may emerge years after the damage occurs or a merger becomes reality.

Under U.S. Superfund law—the Comprehensive Environmental Response, Compensation and Liability Act of 1980—a wide range of parties can be held jointly and severally liable for expensive environmental cleanup for pollution that may have occurred years before.

"Under the standards of strict product liability, a plaintiff need not prove that a manufacturer was negligent or at fault, but only that a product was defectively designed or manufactured or that the manufacturer did not warn against foreseeable dangers," Ms. Mulrennan said. A purchasing corporation may be liable for the seller's liabilities in some circumstances, including consolidations and mergers, she said.

This has become especially important because the plaintiffs' bar has broadened the class of defendants in such lawsuits from the manufacturers of a toxic product such as asbestos to include other manufacturers that used the product as a component, Ms. Mulrennan said.

Research into prior insurance coverage is important for several reasons.

For example, companies that grow by acquisitions may have some protection against potential liabilities due to some U.S. courts recognizing the transferability of insurance assets—and protections—from sellers to buyers.

In addition, companies with insurance coverage under pre-1986 versions of commercial general liability policies may still have viable coverage, she said.

"Under a standard CGL policy, if a claim is filed against a policyholder 30, 40 or even 50 years after property damage or bodily injury occurs—as often happens in the cases of environmental pollution—a policy that was in effect during the time of continuing exposure or damage is still effective decades later," Ms. Mulrennan said in a statement.

Old CGL policies tend to provide broad coverage terms with no restrictions or exclusions that relate to pollution or contamination and no aggregate limits, she said. In addition, such policies are generally prepaid and rarely involve claims-handling service charges



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**SHEILA MULRENNAN**  
IAG LTD.

or additional premiums. They also generally provide unlimited coverage for defense costs in addition to policy limits, she said.

If a company is purchasing a subsidiary or division, the historic claims audit needs to be "particularly comprehensive," Ms. Mulrennan said. "If you have subsidiaries competing for coverage, it's important to know how much of the limits are left."

Once a company's historic insurance policies are reconstructed, it is important to keep key records available and accessible in a user-friendly environment, she said. IAG suggests that a company use customized software to store records, chart corporate histories and corresponding insurance programs, and help companies and outside attorneys conduct related research.

The timing of an audit is crucial and should be done, ideally, prior to a pur-

chase, Ms. Mulrennan said.

"The only time you have leverage is before the deal is done," she said. In addition, a prospective seller may be induced to perform the audit itself in an effort to quantify its saleable assets.

If a legal crisis emerges after a company is purchased, it is important to begin such research as soon as possible, she said. Records can be lost at any point.

Consolidation among both storage firms and insurance-related companies has had a mixed impact on insurance archaeology.

Previously, most companies had detailed lists of the contents of each box of documents. With the merging of computerized records, information is sketchier now and "it's much harder to figure out what is in a box," she said.

In addition, companies seeking to reconstruct their coverage histories previously could rely heavily on the brokers that had sold them the policies, Ms. Mulrennan said. More recent consolidation among brokers means that tracking the brokers can be almost as challenging as finding the policies, she said.

"Overall, consolidation has made London-related records more organized and accessible," as a result of centralization, she said. "In a few cases, though, the records may be harder to find or unavailable."

In addition, the trend toward distressed London companies establishing bar dates for claims "is making it much more pressing for U.S. companies to pursue potential coverage now," Ms. Mulrennan said. Otherwise, they may not be able to file claims in the future, she said. ■