Insurance Considerations When Entering Corporate Transactions: Will You Still Be Able To Access Historical Insurance Assets After The Closing?

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Companies that are considering engaging in any form of corporate or other transaction—such as a merger, asset sale, stock sale, corporate dissolution, or conversion to limited liability company or partnership—need to analyze carefully whether that transaction may affect their ability to access their historical insurance rights. While many of the corporate and business transactions explicitly address the impact of the transaction on insurance policies in effect at the time of the closing, the transactional documents often fail to address the fate of the historical insurance assets (i.e., insurance policies that have already expired). Even when the transactional documents are clear that the historical insurance rights are to be transferred as part of the transaction, the transacting parties need to be aware of arguments that the insurers will bring to bear in their attempts to use the transaction as an opportunity to avoid their coverage obligations. Specifically, insurers routinely argue that so-called “anti-assignment” or “consent to assignment” provisions in their insurance policies relieve them of their insurance obligations when an assignment of insurance rights has taken place without their consent.

This dispute has become particularly pronounced in cases in which the insurers have been faced with massive demands for coverage for asbestos, silica, environmental, or other delayed-manifestation claims in which the bodily injury or property damage began to take place prior to, but did not manifest until after, the transaction in question. In such disputes, insurers often contend that anti-assignment conditions preclude the policyholder from transferring its insurance rights to a third party without the insurers’ consent, even where the transaction provides that the third party will assume the liabilities to which the insurance rights have been assigned (hereinafter, the “Insurer Position”). In response, the entity to which the insurance rights have been assigned (hereinafter, the “Successor Insured”) typically asserts that anti-assignment conditions cannot be used by insurers to avoid providing coverage for occurrences that already took place prior to the transfer, because the occurrences gave the assigning policyholder “chooses in action” under the policies that were freely transferable, with or without the insurers’ consent (hereinafter, the “Successor Insured Position”).

Courts have resolved this dispute in different ways. A number of courts have adopted the Successor Insured Position that, while an insurer cannot be required to insure a third party for new occurrences that relate solely to the third party’s conduct after the transfer in question, a policyholder is free to assign or otherwise transfer its insurance rights relating to occurrences that began prior to the transfer in question without having to obtain the insurer’s consent. On the other hand, other courts, including most notably the California Supreme Court in In re Hartford Acc’t & Indem. Co., have adopted the Insurer Position and held that an anti-assignment condition precluded the policyholder from transferring its insurance rights without the insurer’s consent, including its liability insurance rights for bodily injury that had already happened prior to, but was not discovered until after, the transaction. As a result, the insurers in Henkel and these other cases were able to avoid paying substantial amounts in coverage to the Successor Insured to which the policyholder had attempted to assign coverage. Based on Henkel and similar decisions, insurers are now more aggressively relying on anti-assignment conditions in insurance policies as a basis for denying coverage where the entity seeking coverage is a successor to the policyholder, whether by way of merger, stock sale, dissolution, or asset sale.1

From the Successor Insured’s perspective, this insurer effort arguably threatens to undermine the efficiency of corporate transactions while benefiting the insurers alone. On this view, insurers are seeking enormous windfalls through the elimination of their coverage obligations pursuant to historical policies, for which they collected substantial premiums, by way of a covert campaign of anti-assignment under other subsequent circumstances having nothing to do with the scope of the risk insured under the policies. According to these Successor Insurers, courts should reject the Henkel decision and remain committed to the position that anti-assignment conditions do not preclude the transfer of liability insurance rights for losses that took place prior to the transfer in question. As discussed in more detail below, this position provides that, whether the corporate transaction resulting in the transfer of insurance rights is a merger, stock sale, dissolution, or asset sale, the insurer’s consent is not required to transfer such insurance rights even where the transfer took place “by operation of law.” The same argument has often been made where the occurrence has taken place prior to, but was not discovered until after, the transaction.2

I. Merger

All fifty states have adopted some form of merger statute.3 Merger statutes generally provide that the surviving corporation, upon the effective date of the merger: (i) assumes all of the rights, privileges, powers, and immunities of the non-surviving corporation (provided they are not inconsistent with the articles of incorporation of the surviving corporation and that if the merger is with a foreign corporation they are consistent with the laws of the domestic jurisdiction), and (ii) is subject to and assumes the prior duties and liabilities of the non-surviving corporation.4

Consistent with such merger statutes, courts have held that a merger results in the transfer of the non-surviving corporation’s rights and obligations under its insurance policies to the surviving corporation.5

Further, such a transfer does not violate any anti-assignment provision in such policies.6

II. Stock Sale

The conveyance of all of a corporation’s stock generally transfers ownership of the corporate entity as a whole, with the corporation generally retaining all of its assets unless certain assets are expressly excluded from the transaction.7 Hence, because the sale of a policyholder’s stock alone ordinarily does not involve an “assignment” of insurance policies, an insurer’s consent typically would not be required.8

III. Dissolution Of Corporate Pocholder

When a corporate policyholder is dissolved and its assets transferred to a third party (typically its shareholders), insurers frequently contend that this transfer of insurance assets requires their consent under the “Assignment” conditions in their policies. Successor Insurers will ordinarily be able to refe the insurers’ position, relying on two principal grounds.

First, in cases involving the transfer of insurance rights in the context of a corporate dissolution, courts have held that an anti-assignment condition does not apply to transfer of insurance assets relating to pre-transfer losses, even where those losses are ongoing, but not discovered until after the transfer.9

Second, certain dissolutions arguably constitute “de facto” mergers for which an insurer’s consent is not required in order to transfer insurance assets. Courts addressing dissolutions have concluded that, where a company purchases all of the stock of another company and then subsequently dissolves its new subsidiary, transferring all of the subsidiary’s assets and liabilities to it, a “de facto” merger may have occurred.10

IV. Asset Sale

Bolstered by the Henkel decision, insurers are now asserting more aggressively that the anti-assignment condition in their policies preclude the transfer of historical insurance rights without their consent. Specifically, even though a purchaser may have agreed to extend to obtain all of the assets, including historical insurance rights, of a seller, insurers contend that their anti-assignment conditions block the transfer of insurance rights and to defeat the buyer’s and the seller’s intent. This conclusion, and the Henkel decision upon which it is based, is the subject of substantial cottage litigation.

A. Cases Addressing Whether the Transfer of Insurance Rights for Coverage for Pre-Transfer Events Requires an Insurer’s Consent

A number of courts addressing the issue have held that anti-assignment conditions do not preclude a transferee from obtaining coverage under the transferee’s policies for the liabilities arising out of pre-transfer events. These courts have reasoned that, because the event causing the liability already took place prior to the transfer, the transfer of the insurance rights relating to this liability does not materially increase the risk to the insurer.11 Similarly, courts applying New York law have found that rights to insurance may be assigned without the insurer’s consent where the event from which the liability arises took place prior to the assignment.12

In addition, courts in other jurisdictions that have considered the issue agree that insurance benefits may be transferred without the insurer’s consent despite the presence of an anti-assignment condition, where the injury or damage in question took place prior to the transfer.13

B. Cases Specifically Involving Injury or Damage Not Discovered Until After the Transfer

A number of courts, including cases decided under New York and Illinois law, have held that assignment conditions do not preclude the transfer of liability insurance rights relating to bodily injuries that took place prior to, but were not discovered until after, the transfer.14

Beyond such cases, a number of courts in other jurisdictions have also held that anti-assignment conditions do not bar the transfer of liability insurance rights relating to losses that took place after the closing, but were not discovered until after, the transfer.15

In the context of asbestos-related bankruptcy plans, several courts have confirmed that a number of courts in other jurisdictions have also held that anti-assignment conditions do not bar the transfer of liability insurance rights relating to losses that took place after the closing, but were not discovered until after, the transfer.16

In the context of asbestos-related bankruptcy plans, several courts have confirmed that insurers often proffer a series of arguments to support their position that insur- ance rights may not be transferred in the face of an anti-assignment provision without their consent, including the following arguments. Specifically, insurers frequently argue:

1. That a policyholder has not suffered a “loss” under the policy until the insurer has breached its indemnity obligation, and therefore that no “loss” could have taken place prior to the execution of the asset purchase agreement where the bodily injury or property damage was not discovered until after that time;

2. That insurance rights can only be transferred “by operation of law”;

3. That various cases should be read to support the conclusion that the anti-assignment conditions apply to the transfer of historical insurance assets; and

4. That the decisions in Henkel and related cases represent the better reasoned view.

Policyholders and Successor Insurers will want to refer to these cases in their insurer arguments depending on the factual circumstances surrounding the asset sale in question.

V. Conclusion

After successfully defeating their cov- erage obligations in Henkel, insurers have been more aggressively raising the anti-assignment condition to attack policyholder- ers’ claims for insurance coverage for losses of bodily injury and property damage, such as environmental, asbestos, silica, and other delayed-manifestation claims. To counter these arguments by insurers, Suc- cessor Insurers may rely on decisional law holding that anti-assignment conditions do not preclude the transfer of insurance rights relating to bodily injury or property damage that took place prior to the transfer. These cases can be effectively undermined by insurers’ arguments, concluding that a policy- holder may transfer to a third party its liability insurance rights without its insurer’s consent. Successor Insurers may claim that a corporate transaction in which the insurance rights were transferred was a merger, stock sale, dissolution, or asset sale, even where the injury or damage at issue did not manifest until years after the transaction.

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