Risk Management Issues in Bankruptcy and Receivership

June 13, 2012

Goals for Today

- What is Risk?
- What is Risk Management?
- What are some of the Insurance implications of Bankruptcy
- What are some of the Implications of Risk Management on Trustee/Receiver activities?
- Obtain 3 Continuing Education Credits
- Have Fun!

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Who am I?

- David Adler, ARM
  - President - Strategic Risk Advisors
  - Senior Advisor – Hanover Stone Partners
  - Treasurer – Spencer Educational Foundation, Inc.
- Practicing Risk Manager – 35 years
- Education
  - MBA – Risk Management & Insurance – Georgia State
  - BBA – Finance – University of Georgia
  - ARM – Insurance Institute of America

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What is Risk?

- Risk = Uncertainty
- Pure Risk = Risk of Loss or No Loss
- Speculative Risk = Potential for Gain or Loss
  - Lottery
  - Business Risk

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What is Risk Management?

- World's Oldest Profession

  When you build a new house, you must place a guard-rail (parapet) around your roof. Do not allow a dangerous situation to remain in your house, since someone can fall [from an unenclosed roof and bring blood upon thy house].

  Deuteronomy 22:8

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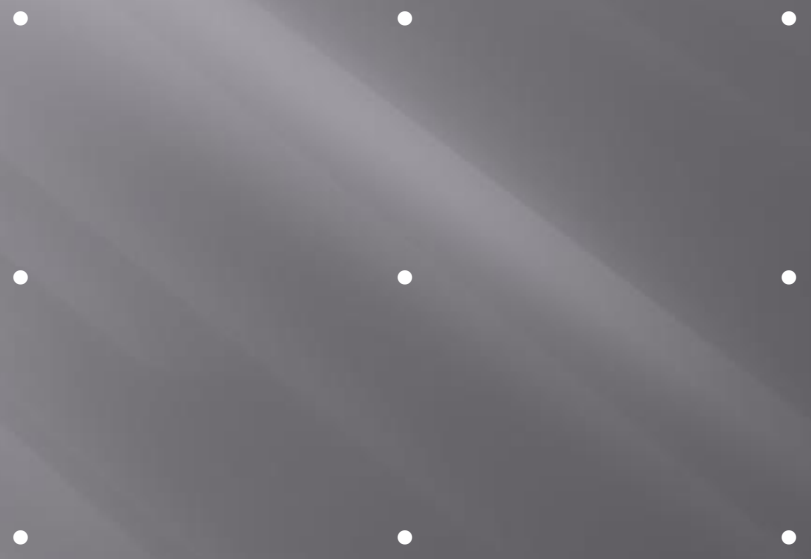
Risk Management Aptitude Test



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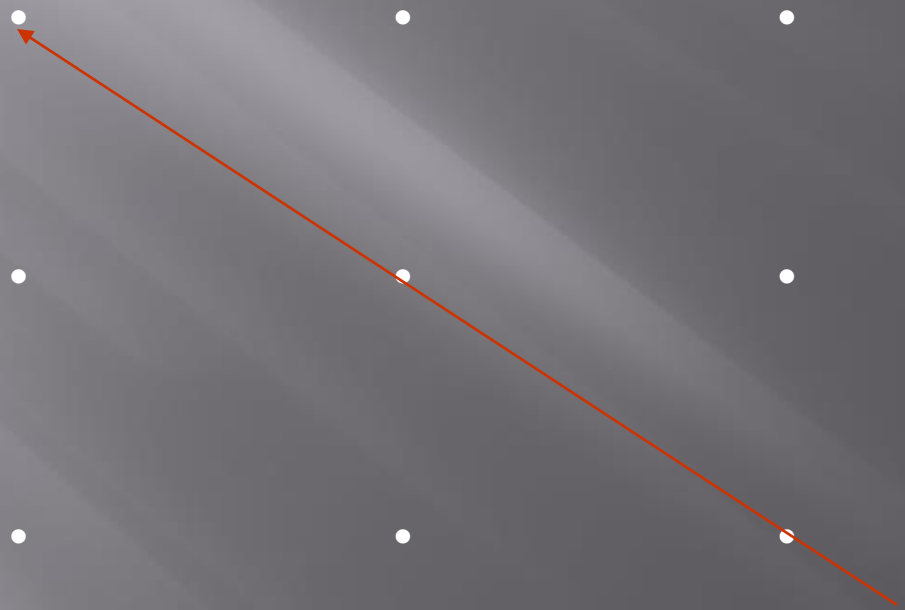
Risk Management Aptitude Test



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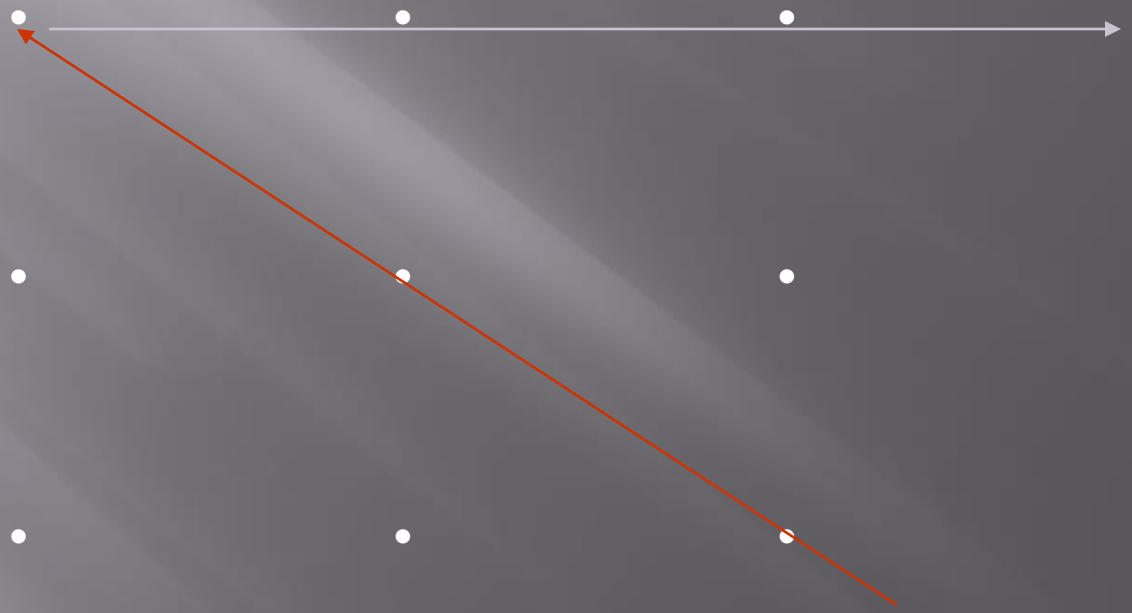

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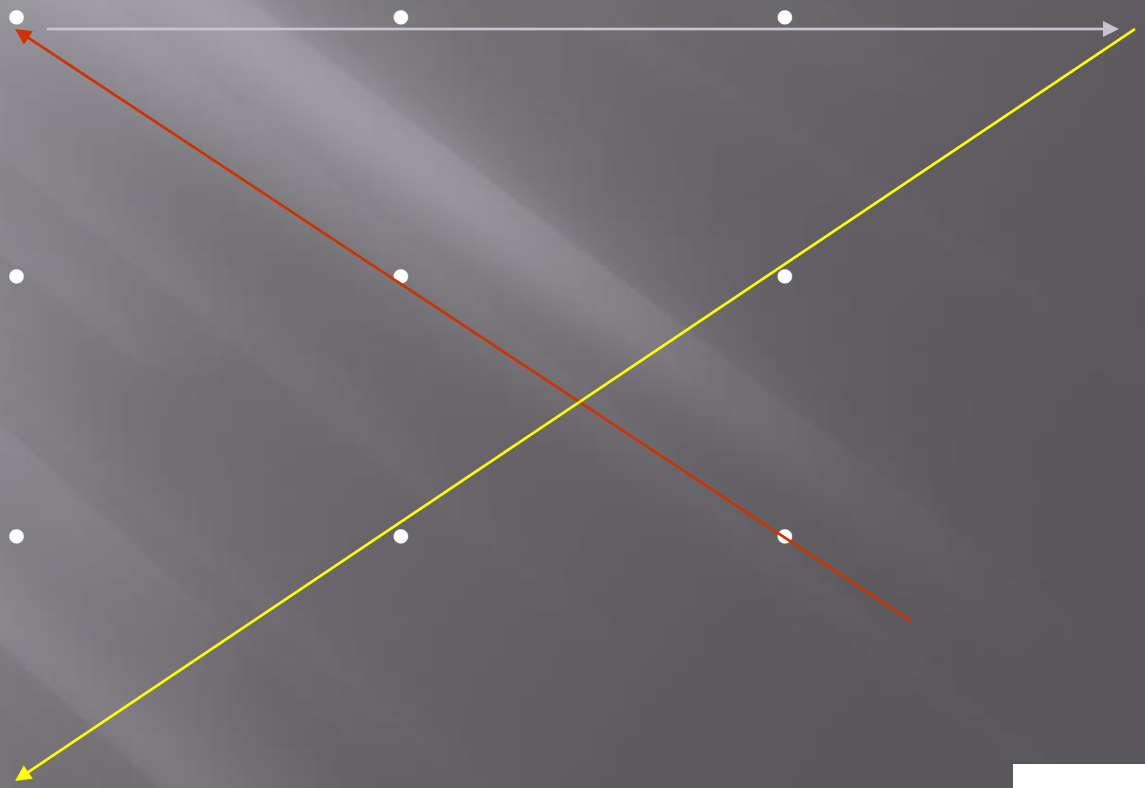

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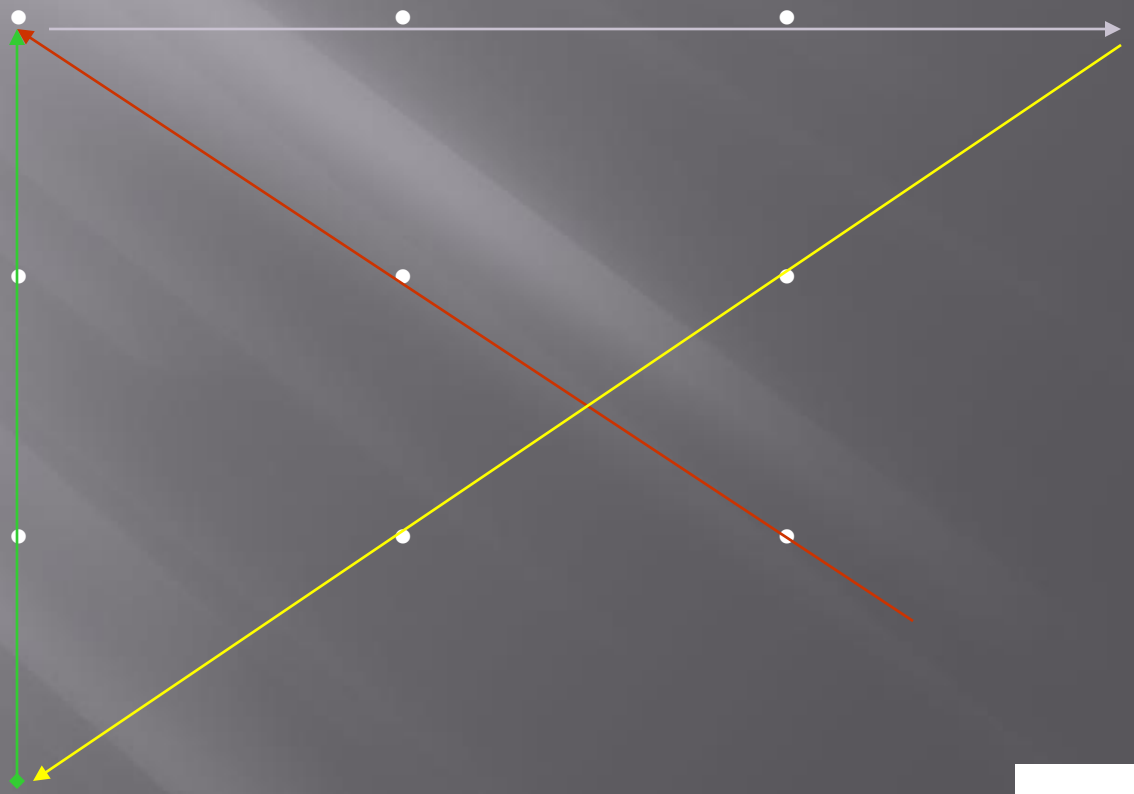

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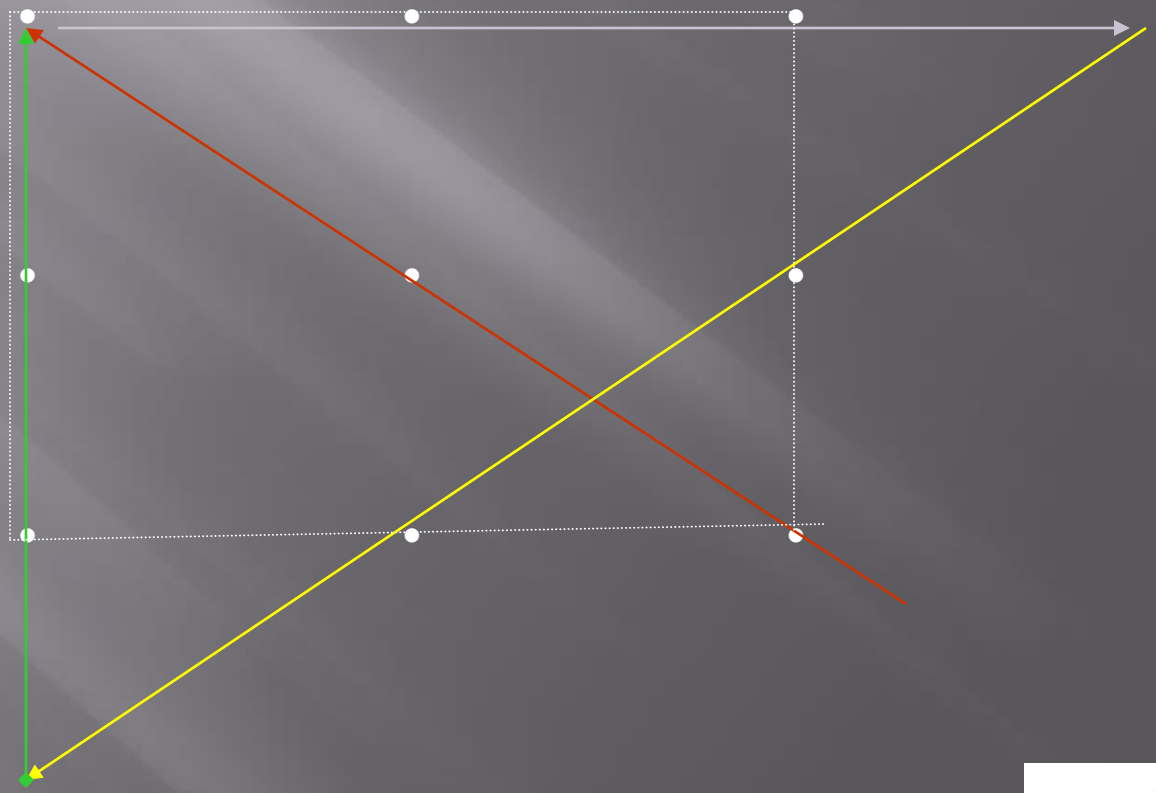

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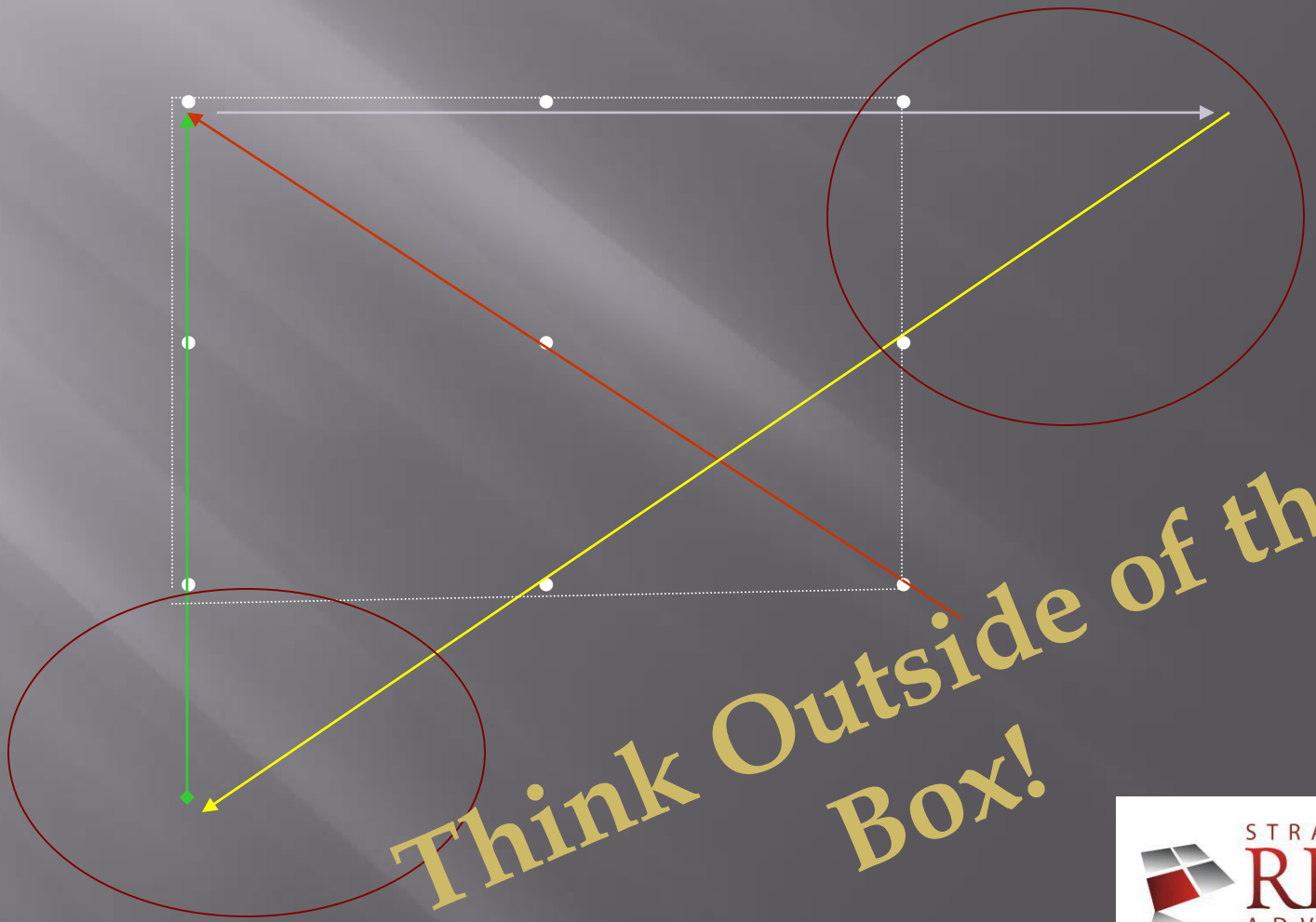

Think Outside of the Box!

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What is Risk Management?

- Evolution from Insurance Buyer
  - Insurance Buyer
  - Insurance Manager
  - Risk Manager

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What is Risk Management

- Risk Management Process
  - Identification
  - Evaluation
    - Critical
    - Important
    - Unimportant
  - Alternatives
  - Implementation
  - Re-evaluation and Review

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What is Risk Management

- Risk Management Alternatives/Tools
  - Transfer (Contractual)
  - Insure
  - Assume
  - Retain
  - Avoid

Don't tell me why I can not do something –
Tell me how I can!

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What is Risk Management

- Risk Management is

  The Specialty of Being a Generalist

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Trustee/Receiver Activities

- Definition of Receiver:
  - A person or entity placed in the custodial responsibility for the property of others, including tangible and intangible assets and rights
- Types of Receiver appointments include:
  - Appointed by a government regulator pursuant to a statute
  - Privately appointed
  - Court appointed

-Wikipedia

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Trustee/Receiver Activities

- Duties of a Receiver:
  - Secure the assets of the company and/or entity
  - Realize the assets of the company and/or entity
  - Manage the affairs of the company in order to discharge the debt owing

The Receiver may run the company in order to maximize the value of the company's assets, sell the company as a whole, or sell part of the company and close unprofitable divisions

- Wikipedia

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Trustee/Receiver Activities

- Contractual Exposure
  - Often very little time to review contractual commitments
  - What legal obligations have been assumed?
    - Fiduciary
    - Liability/Indemnity
    - Individual versus Entity exposure
  - No two deals are alike!

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Potential Project Pitfalls

- Property/Liability
  - Insurable Interest?
- Condition of Property
  - Protective Safeguards
  - Deferred Maintenance
  - Site Inspections critical!
- Building Address correct/complete?

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Potential Project Pitfalls

- Property Values
  - ACV vs Replacement Cost
  - Currently Updated or Artificially Depressed?
  - Coinsurance Requirements
  - Lender Requirements
- Flood/Quake Exposure
  - NFIP Flood Zone Determination
    - Single Determination/Multi-Building property
  - Deductible
    - Flat $
    - % Total Values
    - % Values per Building

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Potential Project Pitfalls

- Environmental Exposures
  - Asbestos
  - Underground/aboveground storage tanks
  - Mold/Fungus
  - Possible Illegal Drug Challenges
  - Phase I/Phase II Reviews?

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Potential Project Pitfalls

- Catastrophe (Cat) Risks
  - Weather Related
  - Cal Quake
  - RMS 11 Impact
- Automobile Exposure
  - Owned/Non-owned
  - Security/Maintenance Vehicles

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Potential Project Pitfalls

- Directors & Officers Liability
  - Possibly single largest bankruptcy asset
  - Whose asset is it?
  - Coverage Rescission challenges
  - Intentional Acts Exclusion

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Risk Management Aptitude Test

- Complete the following pattern:

O T T F ____ ____ ____

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Risk Management Aptitude Test

- Complete the following pattern:

O T T F F S S

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Insurance Coverage Issues

- Our focus is on Policyholder Insolvency
- Most policies include language that bankruptcy or insolvency of the insured does not affect the responsibility of the insurer.
- Several coverage hurdles may still exist, and require close management in order to protect insured's interest

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Insurance Coverage Issues

- Tender of Claim
  - Timely reporting critical
  - In some states, delay in reporting claim is cause for denial without showing prejudice.
  - Potential "constructive notice" if the agent becomes aware
  - Obligation of the insured to cooperate
- Change in Control Provisions
  - Obligation to report – whose, maybe yours?

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Insurance Coverage Issues

- Deductibles/Self Insured Retentions
  - What is the difference in Deductible and SIR?
  - Insurance policies with deductible almost always places insurer with responsibility regardless of ability to recover
  - Must insurer pay claims when the insured does not or can not fund their SIR?
    - Payment of SIR a policy condition?

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Insurance Coverage Issues

- Impact of the Bankruptcy Stay
  - Section 362 of the U. S. Bankruptcy Code provides for an automatic universal stay of any litigation that would affect the "property of the estate".
  - Insurance policies are generally considered property of the estate.
    - Stay may stop cancellation of the policy
    - Courts will often lift stay for failure to pay premiums
  - Proceeds of the insurance policy not necessarily assets of the estate – just the policy
  - Court approval for claim payments

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Insurance Coverage Issues Director's & Officer's Liability

- Directors & Officers Liability
  - Increasing Frequency/Severity of Claims
  - Changing Insurance Market
  - Coverage Rescission Issues
  - Intentional Acts Exclusion

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Insurance Coverage Issues Director's & Officer's Liability

- Directors & Officers Liability

Executive Edge

CHARTIS

11. APPLICATION AND UNDERWRITING

A. Application And Reliance

The **Insurer** has relied upon the accuracy and completeness of the statements, warranties and representations contained in the **Application**. All such statements, warranties and representations are the basis for this policy and are to be considered as incorporated into this policy.

B. Renewal Application Procedure

A written renewal application form is not required in order to receive a renewal quote from the **Insurer**, although the **Insurer** reserves the right to require specific information upon renewal.

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Insurance Coverage Issues Director's & Officer's Liability

- Directors & Officers Liability

C. Insured Person Coverage Non-Rescindable

Under no circumstances shall the coverage provided by this policy for **Loss** under Insuring Agreement A. *Insured Person Coverage* be deemed void, whether by rescission or otherwise, once the premium has been paid.

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Insurance Coverage Issues
Director's & Officer's Liability

D. Severability Of The Application

The **Application** shall be construed as a separate application for coverage by each **Insured Person**. With respect to the **Application**, no knowledge possessed by any **Organization** or any **Insured Person** shall be imputed to any other **Insured Person**.

If the statements, warranties and representations in the **Application** were not accurate and complete and materially affected either the acceptance of the risk or the hazard assumed by the **Insurer** under the policy, then the **Insurer** shall have the right to void coverage under this policy, *ab initio*, with respect to:

(1) **Loss** under Insuring Agreement B. *Indemnification Of Insured Person Coverage* for the indemnification of any **Insured Person** who knew, as of the inception date of the **Policy Period**, the facts that were not accurately and completely disclosed; and

(2) **Loss** under Insuring Agreement C. *Organization Coverage* if any **Insured Person** who is or was a chief executive officer or chief financial officer of the **Named Entity** knew, as of the inception date of the **Policy Period**, the facts that were not accurately and completely disclosed.

The foregoing applies even if the **Insured Person** did not know that such incomplete or inaccurate disclosure had been provided to the **Insurer** or included within the **Application**.

Specimen

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Insurance Coverage Issues Director's & Officer's Liability

- Director's & Officer's Liability
  - Insured versus Insured
  - Is the Receiver/Trustee the same as the "Entity"

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Insurance Coverage Issues Director's & Officer's Liability

- Director's & Officer's Liability
  - Insured Person = "any past, present, or future duly elected director or duly elected or appointed officer of the Organization"
  - Organization = "the Parent Organization and/or any subsidiary"
  - Receiver/Trustee is not included in either definition!
  - With banks, special rules apply to FDIC

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Insurance Coverage Issues Director's & Officer's Liability

- Director's & Officer's Liability
  - Some carriers contend that the Receiver/Trustee "steps into the shoes" of the Organization
  - Some courts have upheld that the Receiver/Trustee represents more interests than merely the estate –
    - Creditors
    - Employees
    - Shareholders

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Insurance Coverage Issues Director's & Officer's Liability

- Director's & Officer's Liability
  - **CAUTION**:
    - Some carriers are now trying to attach "Regulatory Exclusions" to their D&O policies.

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Shift in Property/REO Exposure

- Historically Multi-Family
- Move into new property types
  - Retail
  - Light Commercial
  - Office
  - Trend towards Hospitality
- Not All Affected Properties are Distressed!
  - Class A Office
  - High Occupancy
  - Upside-down Debt

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Current and Emerging Issues

- Receiver/Trustee is a

FIDUCIARY

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Current and Emerging Issues

19. The Receiver shall obtain insurance, if needed, in addition to existing pre-paid coverage, for the Mortgaged Realty and/or the Personal Property Collateral in such amounts, with such companies and to insure against such risks as the Receiver deems necessary or desirable. The Receiver may also finance any of the premiums associated with such insurance with the express written consent of Plaintiff but without any need for prior Court approval. Immediately upon the entry of this Order, the Receiver is entitled to contact the insurance agent or agents retained by Borman and to obtain from such agent(s) information concerning insurance on the Mortgaged Realty, the Personal Property Collateral or any other property related to the foregoing.

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Current and Emerging Issues

25. and its affiliates, agents, representatives, property managers, members, and employees shall turn over to the Receiver, within five (5) business days from the date and time of the entry of this Order, in electronic form, if available, and if not available in electronic form, in paper form, any and all records and information they may have concerning the Mortgaged Realty, Personal Property Collateral, Rents, Other Cash Collateral and any other property related to the foregoing including, without limitation, all books, records, correspondence, and other information related to (a) any leases and other agreements to which the Mortgaged Realty or Personal Property Collateral is or may be subject; (b) any amounts received from the tenants or owners of the Mortgaged Realty; (c) all accounts payable and accounts receivable pertaining to the Mortgaged Realty and/or the Personal Property Collateral; (d) all accounts at financial institutions for income related to the Mortgaged Realty, the Personal Property Collateral, the Rents, Other Cash Collateral or any other property related to the foregoing; (e) all liens or other encumbrances on the Mortgaged Realty, Personal Property Collateral, Rents, Other Cash Collateral and/or any other property related to the foregoing; (f) real and personal property taxes; (g) insurance of all types, including liability and casualty, related to the Mortgaged Realty or the Personal Property Collateral; (h) all operating statements for the years 2006 through 2011 inclusive; (i) copies of all maintenance and service

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Current and Emerging Issues

- As the Receiver/Trustee one must consider emerging and previously unmanaged exposures
- Financial distress affects traditional exposure/claims activity
  - Workers' Compensation
  - CyberLiability/Information Security
  - Employment Practices Liability

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Current and Emerging Risk Management Issues

- Employment Practices Liability
  - The new "Unemployment"
  - Harassment
  - Failure to Promote
  - Failure to Hire
  - Wrongful Separation
  - Wage & Hour

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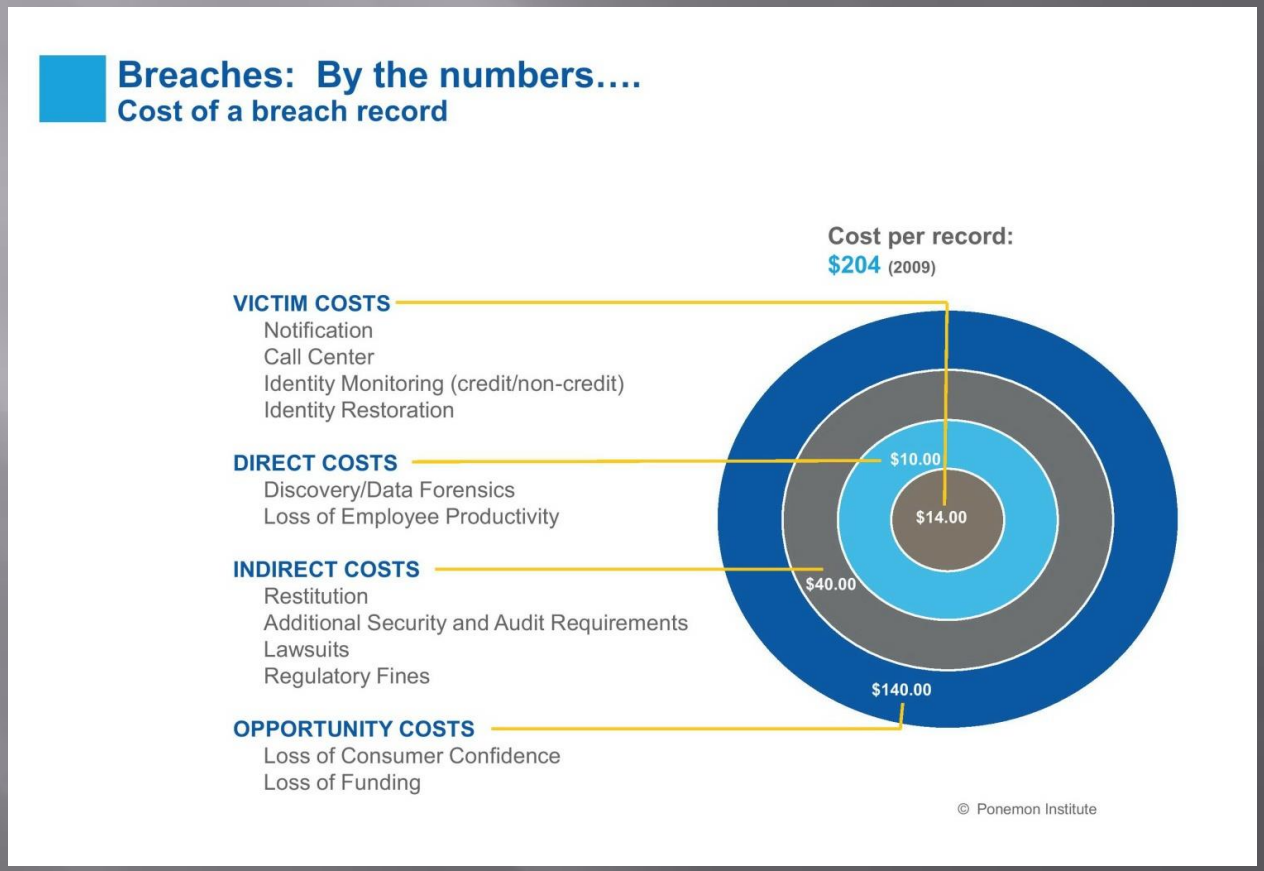
Current and Emerging Risk Management Issues

- Cyber and Information Security



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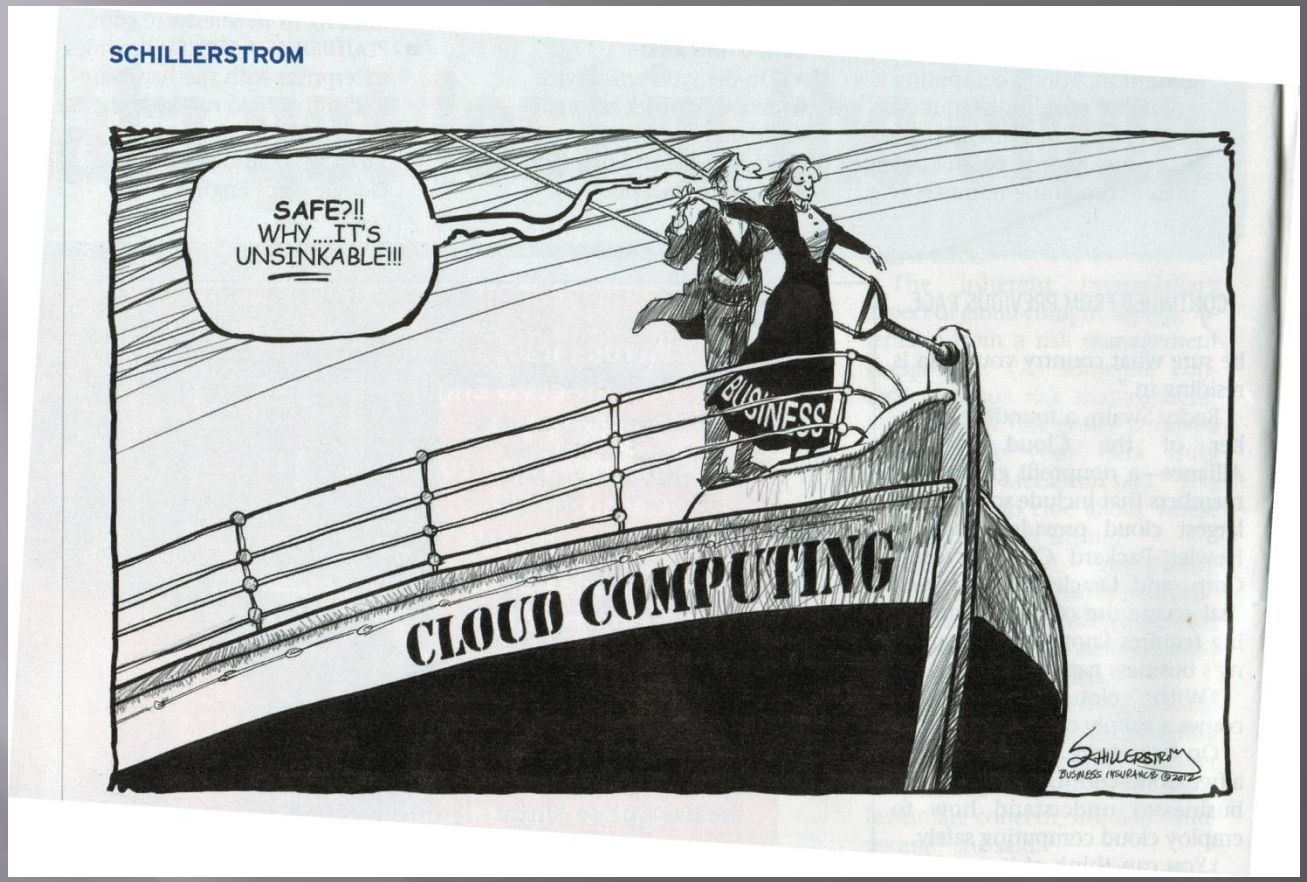

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Current and Emerging Risk Management Issues

- Telecommuting
  - Workers Compensation
  - Wage & Hour
- Mobile Devices
- Social Media
  - Social Networking Policies

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Current and Emerging Risk Management Issues

- Other Issues:
  - Insurance Company Insolvency
  - Global Economy
  - Supply Chain Disruptions
  - Insurance Company Consolidations

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Summary

The most important message to take away from this seminar is:

The Receiver/Trustee has a Fiduciary responsibility to many interested parties. Therefore, it must act in it's fiduciary capacity as a professional manager of the business entity in a prudent manner

Who Is Strategic Risk Advisors?

- Formed in 2009
- Primary focus includes:
  - Insurance Management
  - Claims Management
  - Employee Benefits & Retirement
  - Workers Compensation
  - Special Projects

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Who Is Strategic Risk Advisors?

- Some of our clients include

PORTMAN HOLDINGS

Lucror Resouces

About Hanover Stone Partners

Hanover Stone Partners LLC

Objective. Creative. Comprehensive.

Our experience, our expertise and our enthusiasm work collaboratively, to achieve one primary objective, to **drive down the enterprise's overall *cost of risk***. That is our single mission, our benchmark, our performance measurement and how we are rewarded. Our value proposition is simply to deliver **better solutions, by more experienced professionals, more efficiently**.

Strategic Risk Advisors is proud to be associated with Hanover Stone Partners

A Thought …

If we always do

What we have always done,

We will always get

What we always got.

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Contact Information

Strategic Risk Advisors, LLC
100 Inland Drive
Atlanta, GA 30342

P: 404-276-RISK (7475)
F: 404-478-6864
dadler@strategicrisk.net
www.strategicrisk.net

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