



MERGERS AND ACQUISITIONS

Warranty & Indemnity Insurance in Irish M&A Transactions

by **Seanna Mulrean**

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The strategic use of Warranty & Indemnity Insurance in M&A transactions in Ireland is growing in popularity, particularly when there is a cross border element.

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W&I Insurance is less costly and more compatible with overall deal processes and timetables than when it was originally pioneered in the 1970s. As a result, it's now a more attractive means of dealing with many of the key hurdles associated with the structuring and negotiating of M&A transactions. This article examines the key features and benefits of using W&I insurance.

What is Warranty & Indemnity (W&I) Insurance?

W&I insurance provides cover for losses incurred as a result of breach of the warranties or certain indemnities in an M&A transaction.

The most common type of policy is the buyer side policy under which a buyer is insured for any losses it suffers as a result of a breach of warranty.

While less common, a sell side policy insures the seller giving the warranties, for any losses suffered as a result of the buyer bringing a valid claim against it, for a breach of warranty or a covered indemnity.

Why use it?

The following are among the most common reasons for parties using W&I insurance:

- It protects a buyer or a seller from financial loss resulting from a breach of warranty made by the seller in a sale agreement.
- It removes the need for mechanisms commonly used to deal with risks arising from breach of warranty or indemnity, such as the retention of monies in escrow for a period of time post completion, or where part of the consideration is to be deferred and set off against warranty claims, thus making sales proceeds immediately available to the seller.
- It removes the concern about a seller's solvency and ability to meet warranty or indemnity obligations in the future.
- It is particularly effective when used to enhance a warranty cap, where negotiations with the seller are difficult or to fill a warranty gap left by existing private equity vendors who refuse to provide warranties.
- It can differentiate your bid in an auction process. In a competitive bid context it can enable a buyer to offer to buy the target without or with minimal seller liability, thus making the buyer's bid more attractive to the seller.
- It avoids the need to sue management who may be continuing with the business.

Key Features

Premiums for W&I insurance will depend on the specifics of the deal but are usually in the region of 1% to

1.8% of the limit purchased.

Insurers will also usually require the insured to bear the first portion of any warranty claim by way of an excess or "retention". Recent trends have shown these excesses to be in the region of 0.5% to 1.5% of the policy coverage. Other costs of obtaining W&I Insurance include the broker's fees or commission, the underwriter's due diligence fees, and insurance premium taxes (if applicable).

In addition to the excess, general exclusions will apply, and these usually include the following:

- Fraud and deliberate non-disclosure on the part of the insured.
- Any forward looking warranties, for example the ability to collect debts after completion.
- Liabilities arising out of anything disclosed or otherwise within the knowledge of the insured party; findings in the due diligence reports, if the insurer has had access to such reports; or issues covered by specific indemnities in the share purchase agreement, unless these are covered separately.

Practicalities

The process of putting W&I Insurance in place typically takes between two to four weeks.

The underwriting process involves a review of the transaction documents, the negotiation of the policy terms, and on buy side deals, due diligence by the insurer's advisors.

Insurers will generally require discussions with the insured and their advisors usually by way of conference call during which the underwriters will ask questions in order to get comfortable with the due diligence process (in the case of a buyer side policy) or the disclosure process (on the sellers side).

Felix Sloman, a broker with JLT Specialty's M&A group offers the following key tip:

Insurance should be considered early on. As a seller, if a draft sale agreement is released to bidders that contains a material warranty cap, it can be difficult to then lower this when the concept of insurance is introduced. It is far better to consult with experienced legal counsel or a specialist insurance broker from the outset to ensure the best outcome.

As more underwriters enter the Irish market, we anticipate competition to follow, which will make W&I insurance an even more viable option to parties to M&A transactions. Along with the recent upturn in M&A activity, this means that W&I Insurance is likely to become a more regular feature of Irish transactions rather than the exception.

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