

RISK MANAGEMENT BULLET

Representations and Warranties Insurance An effective means of improving transactions

As a business professional involved with merger and acquisition transactions, you are well aware of the investment of intellectual capital that goes into negotiating and structuring a deal as well as the loss of capital that inevitably follows if a deal falls apart. You'll probably also agree that the representations and warranties made in the purchase & sale agreement are among the most hotly debated portions of any transaction. Subtle changes in this language can shift risks dramatically and potentially scuttle a deal. Coverage is available now that can allow these risks to be transferred away from the parties to the transaction and improve the deal for both sides.

Mergers and acquisitions generally require the seller to indemnify the buyer for breaches of the representations and warranties that are made in the purchase and sale agreement. Depending on the parties involved and the nature of the representations and warranties, the seller may be required to escrow monies, which may represent a percentage of the purchase price or of the amount of indemnification. From the seller's perspective, this requires them to maintain substantial illiquid capital following an exit. From the buyer's perspective, an indemnity with no escrow or insurance provides only limited comfort, as there is no guarantee that they will be able to collect losses if a breach occurs.

Representations and Warranties Insurance (RWI) coverage can help protect against some of these exposures and can be written on either a "seller basis" or a "buyer basis". Selling entities and shareholders can obtain valuable protection against claims alleging breaches of the reps and warranties made in the contract. Most private company D&O policies and other coverages won't respond to many of these types of claims for a variety of reasons and would leave the sellers exposed. Additionally, the inclusion of RWI coverage in a transaction may alleviate some of the need for escrow holdbacks and allow the seller to collect more of the purchase price at closing than would otherwise be the case. Buyers can obtain coverage for indemnification that is not paid by the seller as well as for a portion of their legal expenses. There is a great deal of flexibility in the structure of the product, including the potential for structuring coverage periods to match the expirations of the various representations and warranties in the agreement.

The Mergers & Acquisitions practice group of The Simkiss Companies can be an invaluable addition to the due diligence team of any transaction, helping to identify risks and suggest solutions (both insurance and non-insurance) to treat them. Our staff includes a wide range of elite professional designations, including CPA, MBA, CPCU, CLU, ChFC, etc. as well as in-house counsel, making us uniquely qualified to add value to an infinite range of transactions. We welcome the opportunity to share these services with you or your associates at any time.