WARRANTY & INDEMNITY (W&I)

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Warranty & Indemnity insurance (W&I) can be purchased by either a buyer or a seller and protects the policyholder for loss arising from a breach of the warranties and claims under indemnification provisions (including tax indemnity/covenant), contained in a sale and purchase agreement (SPA).

It typically covers the full suite of warranties, subject to policy exclusions, to insure against loss or liability arising from unknown or undisclosed matters and indemnities.

Each W&I policy is tailored to meet the specific needs of a transaction and is intended to work in parallel with the negotiations, supporting (not substituting) a robust due diligence process.

> "W&I can manage financial risk for both buyers and sellers; smoothing the deal negotiation process and protecting ongoing commercial relationships"

Buyers

- Provides an advantage in competitive auction processes by replacing recourse against the seller with a W&I policy
- Enhances protection for warranty breaches surrounding financial and time seller limitations, as well as certainty of payment
- Protects the relationship with the sellers post completion who may rollover and become part of the new management team

Sellers

- Provides a clean exit as the sellers can ring-fence liabilities under the W&I policy and removes the need for escrows or other mechanisms
- Enhances the amount and speed of the distribution of sales proceeds, as well as the speed of deal negotiations and the certainty of the transaction completing
- Protects sellers who have not been actively involved in the management of the target business

Costs & Policy

- The policy is a non-renewable, one-off cost with the premium paid upon completion of the transaction
- They are multiyear policies in line with the exposures being addressed; typically 2-7 years and incept when the deal signs
- Premiums are calculated on the policy limit purchased, industry sector and jurisdiction of the target company, as well as the governing law of the purchase agreement. They typically range between 0.6-0.8% for real estate transactions and 0.7-1.5% for operational transactions, however certain industry sectors and/or territories, can increase to 2-4%

CASE STUDY

An owner-managed business is being acquired by an industry buyer owned by an international private equity firm. The buyer and their private equity owners want to protect the relationship with the new management team being acquired, whilst the sellers wish to minimise any long term liabilities following the sale, especially as one of the co-founders (and major shareholder) is leaving the business.

As the leaving co-founder wants to receive all of their share of the sale proceeds immediately and not wait until the expiration of the warranties being given in the sale and purchase agreement, nor set up an escrow arrangement, W&I Insurance is suggested.

The W&I policy would allow the seller limitations under the sale and purchase agreement to be reduced to 0.5% of the transaction value, instead of the original suggested 20% and also remove the need for an escrow.

Simultaneously, it would provide the buyer with the additional financial protection they would require given the new low seller limitations in place and also if a breach of warranty claim were to arise post completion, the W&I policy is the path of recourse for the buyer, not the new management team recently acquired. A Buyer W&I policy was arranged during the on-going deal negotiations over a 2 week period and paid for by the sellers, even though the policyholder was the buyer.