



Cooley

attorney advertisement

Copyright © Cooley LLP, 3175 Hanover Street, Palo Alto, CA 94304. The content of this packet is an introduction to Cooley LLP's capabilities and is not intended, by itself, to provide legal advice or create an attorney-client relationship. Prior results do not guarantee future outcome.

Trending Issues in Negotiation of Indemnification Provisions

UT Law 2016 Mergers and
Acquisitions Institute

October 21, 2016

Panelists:

Craig A. Menden, Cooley LLP, Palo Alto

Mark S. Solomon, Andrews Kurth LLP, Dallas
Elizabeth C. Brandon, Barnes & Thornburg,
Dallas

Jessica C. Pearlman, Partner, K&L Gates,
Seattle

Tom D. Harris, Haynes & Boone, Dallas



K&L GATES

K&L Gates LLP

Overview of Representation & Warranty Insurance

Jessica Pearlman

jessica.pearlman@klgates.com

Rep & Warranty Insurance Summary

- **Typical coverage of rep & warranty insurance (“RWI”):**
 - RWI generally covers breaches of sellers’ reps and warranties in a definitive acquisition agreement

- **Potential benefits of RWI:**
 - Enhance auction bid or bridge negotiation gaps (price, length of claim period)
 - Reduce seller escrow amounts and overall indemnity exposure
 - Ease process by streamlining negotiation/documentation of agreement

Rep & Warranty Insurance Summary

- **Growth of RWI**
 - RWI introduced in US in late 1990s, but initially used sporadically
 - RWI usage has grown dramatically since 2012
 - Pre-2012, market wary of collectability of claims and viewed RWI as prohibitively expensive and time consuming to obtain
 - ~2012, perception shifted
 - lower premiums and increased demand
 - allowed insurers to expand capacity, enable more flexible and expedient underwriting, and simplify claims process (claims paid in ordinary course)

- **Impact on auctions**
 - Pre-2015, early users of RWI had a competitive bidding advantage and could often preempt auctions with favorable terms
 - From 2015, bidders may be at competitive disadvantage without RWI (or offer of RWI-like indemnity terms, self-insuring the risk)

Rep & Warranty Insurance Summary

- **Exclusions**
 - Known breaches of reps (“actual knowledge of actual breach” by identified deal team members of the insured)
 - Vary by deal (and specialty policies may cover exclusions), but often include:
 - Environmental issues (absent clean Phase I reports)
 - Employee classification / FLSA issues
 - Certain state tax issues
 - Specific issues identified in underwriting
 - Other matters usually not covered include any adjustments to purchase price, breaches of seller covenants, punitive damages

Rep & Warranty Insurance Summary

- **Typical context**
 - PE seller (seller seeks quick/unconditional return of capital to LPs)
 - Middle market between \$100-\$500MM of enterprise value (“EV”)
 - Not yet efficient for <~\$5MM of risk, but trending downward
 - Risk amounts >\$50MM may require syndication, which reduces certainty of coverage and thus utility of RWI in bid process
- **Pricing fairly consistent, assuming clean underwriting:**
 - Total cost: ~50 basis points of EV (for policy for 10% of EV)
 - Premium typically ~4% of policy limit plus minor underwriting costs
- **“No seller indemnity” deals**
 - Can utilize RWI to provide a public company style deal with no seller indemnity (“NSI”)
 - NSI policies available, but at higher price (+~25-75 BPs)
 - Buyers/insurers leery of removing seller’s incentive to get reps right

Find the full text of this and thousands of other resources from leading experts in dozens of legal practice areas in the [UT Law CLE eLibrary \(utcle.org/elibrary\)](http://utcle.org/elibrary)

Title search: Trending Issues in Negotiation of Indemnification Provisions

Also available as part of the eCourse
[2016 Mergers and Acquisitions eConference](#)

First appeared as part of the conference materials for the
12th Annual Mergers and Acquisitions Institute session
"Trending Issues in Negotiation of Indemnification Provisions"