IronPro®

Transactional Liability Insurance

Access Experience. Get Results.

IRONSHORE

your safe harbour®

Risk Transfer Solutions as Unique as the Deal Itself

Insurance for Companies Involved with Mergers & Acquisitions

With the financial strength of a large company and the quick response time associated with a smaller more nimble firm, Ironshore is uniquely positioned to be a market leader in providing insurance solutions to parties facing the great risks and uncertainties associated with merger and acquisition transactions.

- Representations and Warranties Insurance
- Litigation Containment Insurance
- Tax Opinion Indemnity Insurance

Thoughtful Solutions to the Unthinkable

Through combined talent, products, global capabilities and financial strength, the IronPro division of Ironshore offers holistic risk management solutions for domestic, foreign or cross-border business transactions that are motivated by strategic buyers or financial sponsors. At IronPro, we've lived it - not as theorists, but on the front lines. As such, our team has an unmatched understanding of the characteristics of the changing risks and knows how to develop the strategies and the products for effective mitigation of transactional liability exposures.

Underwriting Expertise and Financial Strength

Our dedicated team of Transactional Liability underwriting professionals is directed by Greg Flood. Together, we bring more than a decade of experience to underwriting the risks associated with divestitures, restructuring and M&A transactions – at any point along the continuum. Having appropriate underwriting authority allows the group to provide skillful and consistent decision-making and to solve complex problems quickly. With deep market expertise matched by outstanding credentials in international affairs, law, economics, finance and business, we bring an unparalleled ability to tailor comprehensive solutions and facilitate the transaction. As part of Ironshore Inc, our insurance solutions are backed by the financial strength of Ironshore Insurance Ltd., rated A (Excellent) by A.M. Best Company with a Financial Size Category of Class XIV.

Expert Claim and Litigation Management

In the event a Transactional Liability claim does arise, insureds want seasoned professionals with proven expertise working for them. IronPro's Transactional Liability claims division is second to none. With leadership from Mike Mitrovic, no other insurance firm has a better understanding or practiced approach to expeditious claims management and fair resolution in this high-profile, complex arena.

The M&A Landscape

To survive in a global economy, companies are looking to get bigger and rebuild their platforms so as to achieve economies of scale. This has spawned a frenzy of mergers, acquisitions, divestitures and restructuring transactions worldwide. Now, in the wake of the ever broadening effects of the credit crunch in the United States, we have rolled headlong into a period characterized by a fair degree of uncertainty. Every transaction is met with increased caution and involves greater risk. With so much at stake, executives need to make sure that the deals they make stay on track.

Net Liabilities and their Impact on Transactions

Merger and acquisition deals involving public companies or private equity firms fail for many reasons, including, among other things, the inability of the parties to agree on price and the failure to accurately assess the value of the assets and liabilities of the acquisition target. Any examination of liabilities should include exposure to litigation. In assessing this exposure, those doing due diligence focus on net liabilities – the amount of gross liability minus any amounts that are contractually the responsibility of an insurance company or some other third party.

Losses can be net to the company because they are in excess of available insurance limits – as is sometimes the case for high-severity, low-frequency claims, such as security claims. Losses can also be net to the company because they are beneath the company's self-insured retention – as is often the case for high-frequency, low-exposure claims, such as employment claims. Finally, some losses are simply not covered by insurance. These three types of exposure will form the bulk of the acquisition target's net liability, and risk managers and brokers can help identify such exposures.

Once such exposures are identified, they can threaten a deal. Legal actions initiated against the purchaser utilizing a "successor liability theory" can, in many instances, have a chilling effect on an otherwise commercially advantageous transaction. By transferring risk, the Ironshore Transactional Liability Insurance products can solve problems that might not otherwise be addressed within a required time frame and accelerate the speed with which a transaction can be completed.

For example:

- Differing appetites for risk
- Differing perceptions of the ultimate financial exposure associated with a risk
- Disagreements over allocation of financial risk for a given exposure
- Unfamiliarity by one party with the legal, political or regulatory jurisdiction of an industry

With timing often critical and concerns ranging from indemnity obligations to tax exposure or litigation, transferring the risks you can insure mitigates these issues. In addition, transferring all or part of the financial responsibility for a contingency or deal point can provide the parties to a transaction with greater post-transaction flexibility. The delays and complications associated, for example, with posting escrow or providing an indemnity are avoided, and additional post-transaction financing can be expedited by assuaging the concerns of potential lenders.

Representations & Warranties Insurance

The terms of a merger or acquisition are typically set forth in a Sale and Purchase Agreement ("the SPA"). As net liabilities, including litigation exposure, are identified in the course of due diligence and the buyer attempts to determine the scope of the exposure, understandings are reached between the parties as to whether, and to what extent, the buyer or seller is responsible for the liability. The SPA contains provisions memorializing these understandings. Often, the SPA calls for the seller to indemnify the buyer for some or all of the liability. Sometimes, the seller is asked to post a sum of money in escrow to provide security for its agreement to indemnify. These provisions in the SPA are called Representations and Warranties (R&Ws) or Warranties and Indemnities in the United Kingdom. If either the scope or duration of the indemnity or the amount of security provided in connection with the indemnity becomes a point of contention, this can delay, or even derail, the consummation of a transaction. Representations and Warranties Insurance can mitigate these risks.

R&W Insurance at Work

A Representation and Warranties Insurance policy issued to the buyer indemnifies the buyer for breaches of representations and warranties given by the seller in the SPA. If the seller wants to limit the scope of its indemnity obligation or the buyer wants the seller to put more money in escrow to secure its indemnification obligation than the seller deems reasonable, Representations and Warranties Insurance can close the gap, allowing the parties to more quickly resolve such issues and close the transaction.

Representations and Warranties Insurance can also be issued to the seller to bridge the gap between the amount that the purchaser wants the seller to indemnify and what the seller is willing or able to do. For example, private equity firms seeking to sell portfolio companies are typically reluctant to issue lengthy commitments to indemnify the buyer because they want to distribute the sale proceeds to their investors as soon as possible and move on to the next investment. Representations and Warranties Insurance can help the private equity firm make such portfolio companies more attractive to potential buyers.

EXAMPLE

Both parties to a transaction agree to all of the terms of an acquisition, except for the duration of the indemnity supporting certain Representations and Warranties. The seller offers a 12-month indemnity while the buyer insists on 24 months. A representations and warranties policy can bridge the gap by insuring breaches of the representations and warranties discovered after 12 months and prior to 24 months from the date of the sale.

These policies can also resolve disputes over the amount of indemnification a seller is willing to provide.

EXAMPLE

Both parties agree to all of the terms of an acquisition, except for the amount of the indemnity supporting the seller's representation for its contributions to a multiemployer-defined employee benefit plan, which it intends to withdraw from post-merger ("withdrawal liability"). The seller offers a $10,000,000 indemnity to support its representations for withdrawal liability, but the buyer is demanding $20,000,000. A $10,000,000 Representations and Warranties policy can be purchased to close the gap.

Often, the parties can agree on the amount of indemnity to be provided but are at odds regarding the extent to which the indemnity should be secured.

EXAMPLE

The seller may be a Debtor in Possession that has been reorganized in bankruptcy and is selling a subsidiary. The seller and the buyer agree to all the terms, including the amount of indemnity supporting certain representations and warranties in the SPA. They agree that the amount of the indemnity should be limited to $10,000,000; however, they do not agree on the security supporting the indemnity. The buyer wants the full amount of $10,000,000 secured with funds held in escrow while the seller is willing to agree to only $2,000,000. A Representations and Warranties Insurance policy featuring an $8,000,000 limit in excess of the $2,000,000 indemnity that the seller agrees to secure can bridge the gap.

Comparing this product to a more traditional insurance product is a bit like comparing a custom-made suit to one bought "off the rack." These policies are, by their nature, custom-tailored to the transaction at issue, and only underwriters with a wealth of experience in this area should be considered. Further, large bureaucratic companies are likely to find it difficult to provide such tailor-made insurance solutions within a tight time frame, given their need to secure multiple approvals even after the underwriting process is complete – Ironshore is uniquely positioned to act promptly and provide the necessary expertise.
Very often, as will be explained in greater detail below, the act of underwriting these risks provides a service for the parties in and of itself. Once the exposure is examined by the seasoned professionals at Ironshore, their analysis will help the parties make their own judgments regarding the value of the risk.

R&W Insurance Coverage Highlights

IronPro manuscripts each policy to meet the insured's specific needs – the policy is tailored to the exposure.

- Capacity Up to $20 million of capacity is available for any single transaction. Additional coverage structured on a case-by-case basis. Deductible 1% to 3% of the transaction value.
- Premium 2% to 6% of the amount of insurance purchased.
- Policy period generally matches the survival period for the R&W set forth in the acquisition agreement. On a buyer-side policy, coverage can extend beyond the survival period for R&W included in the agreement.

Buyer's Value Proposition

- Enhance protection for breaches of R&W
- Extend duration of R&W
- Ease indemnity collection concerns
- Distinguish themselves from competing bidders
- Protect key relationships

Seller's Value Proposition

- Reduce contingent liabilities
- Distribute sale proceeds to reward investors or pay down existing debt
- Protect passive sellers from unintentional breach of R&W
- Eliminate obstacles to completing the sale, which expedites the sale and potentially increases the return

Litigation Containment Insurance

When the due diligence process reveals a litigation exposure and the parties cannot agree on the scope of indemnification to be provided by the seller principally because they are having difficulty determining the extent of the exposure, Ironshore has a unique product to address the problem – the Litigation Containment Insurance policy.

Ironshore underwriters have the ability to seek the advice and expertise of claims staff with years of experience in determining the expected resolution value of litigation. Ironshore can write a policy that caps the exposure to outstanding litigation, thereby allowing the parties to a merger to have certainty with regard to the amount of the exposure. The Litigation Containment Insurance policy is designed to buy out litigation exposures that are underinsured or uninsured. This can involve a large loss that threatens to exceed the amount of insurance available; a portfolio of high-frequency, low-severity claims that are within a company's self-insured retention; or a claim that is simply uncovered by insurance. Where a merger is effected by the purchase of assets and the buyer is concerned about the imposition of successor liability for the seller's litigation exposure, this product provides a solution. It responds in the event a buyer is dragged into, or charged with, the cost of litigation outstanding against the seller.

Ironshore is one of the only facilities in the United States that can provide tailored litigation containment insurance on a timely basis.

The Litigation Containment Insurance policy operates to transfer exposure to existing third-party claims against the seller to a third-party insurer, thereby limiting the exposure to the price of the policy. This allows the parties to a transaction to quantify a risk whose value had previously been unknown – perhaps eliminating a point of contention in the merger or acquisition negotiations. The policy can be used to contain almost any type of exposure that can be reasonably quantified, including securities litigation, employment practices claims, errors and omissions and professional liability claims, ERISA claims, contractual disputes, claims involving intellectual property and products liability.

The mere act of placing a value on an exposure whose value is unknown can provide a great service to the parties in a merger transaction. Each Litigation Containment Insurance policy is tailored to meet the needs of each party to a merger transaction. Every transaction is unique, and every Litigation Containment Insurance policy must be unique. Therefore, underwriting such policies requires great time and effort. Ironshore is one of the only facilities in the United States that can provide such insurance solutions on a timely basis while still tailoring its product to the needs of specific clients.

Tax Opinion Indemnity Insurance

A Tax Opinion Indemnity Insurance policy is designed to cover costs arising from a successful challenge by the Internal Revenue Service or state tax authorities (collectively "tax authorities") to a specific tax position taken by a company. Such a challenge could involve additional tax payments, interest, penalties and defense costs.

A corporation might, for example, consider purchasing Tax Opinion Insurance if its tax return includes a substantial deduction for an item that could be viewed as questionable and ultimately disallowed by the tax authorities, even though the corporation's outside accountant is willing to issue a written opinion supporting the deduction. In this situation, Tax Opinion Insurance would cover the costs associated with the corporation's tax position, except any additional tax due.

While the accountant preparing an opinion regarding the tax implications of a merger transaction may well have Errors and Omissions Insurance, such insurance is not adequate to meet the need of the parties to a merger transaction. The event that triggers coverage with a Tax Opinion Indemnity Insurance policy, unlike an Errors and Omissions' policy, is a final decision by the tax authorities that the proposed tax treatment was inappropriate, not the finding that the accountant was negligent. Often, the opinion of the buyer's or seller's accountants with regard to the tax consequences of a complex transaction can be filled with enough caveats as to limit the opinion's utility. Further, the tax code is so complex that the mere fact that an accountant was incorrect in predicting what the tax authorities would decide does not necessarily make the accountant negligent or even incorrect in his or her opinion. It could simply be that the tax code is subject to more than one interpretation and there is no binding legal authority deciding the particular issue one way or the other. Therefore, Tax Opinion Indemnity Insurance is needed to alleviate the uncertainties associated with the tax treatment of merger transactions that potentially leave the door open for tax adjustment down the road.

Today, many transactions are completed before the tax authorities can adjudicate the actual tax liability associated with the transaction. Seeking a private letter ruling to enhance certainty is often impossible. The tax authorities may not be able to issue a private opinion letter in the time frame needed because the issue is too fact-specific, they have no firm rule or policy regarding the particular issue or simply because bureaucratic inertia prevents a timely response. In these situations a Tax Opinion Indemnity Insurance policy can limit the exposure associated with adverse tax rulings.

Tax Opinion Indemnity Insurance Coverage Highlights

IronPro manuscripts each policy to meet the insured's specific needs.

- Up to $20 million of capacity is available for any single transaction.
- Premiums, limits and retentions and even policy period are determined on a per policy basis in light of the structure of the transaction and according to the specific needs of the parties.

Tax Opinion Indemnity Insurance at Work

EXAMPLE

Whether securities issued in connection with a merger transaction, such as a loan by shareholders, are characterized as debt or equity is a very fact-intensive inquiry. Tax authorities often will not issue private letter rulings about this issue. How this issue is decided can, among other things, affect whether, and to what extent, dividends paid by such securities are taxed and whether deductions or credits apply.

EXAMPLE

When the target company is restructured so as to achieve significant tax benefits, often the company must show that the main purpose of the restructuring had an overriding commercial purpose and was not simply tax avoidance. Otherwise, the taxing authorities will deny the tax benefits. Tax opinions regarding such issues can be insured, thereby providing the certainty necessary to allow the transaction to move forward.

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