



REPRESENTATIONS & WARRANTIES INSURANCE COVERAGE OVERVIEW



McGRIFF, SEIBELS & WILLIAMS, INC.

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POLICY BASICS

Policy Limits:
Typically 10% to 20% of enterprise value

Retention: 1-3% of enterprise value

Policy Period: Typically six years for fundamental and tax reps and three years for general reps

Premium: One-time payment of 2% to 4% of policy limits

Coverage: Protects against financial losses (including defense costs) from breaches of representations and warranties that are unknown to the buyer at the time coverage is bound.

STRUCTURE AND STRATEGIC CONSIDERATIONS

Buy-Side Policy Overview



Examples of Uses for R&W Insurance

Strategic

Enhance bid in auction by proposing a structure that reduces seller's post-closing risk while preserving protection for buyer

Protect key relationships with executives, rollover shareholders, and customers

Risk Management

Provide recourse when no seller indemnity is available

Increase maximum indemnity and extend survival period

Ease collection concerns

Satisfy lenders' requirement for additional security on transaction

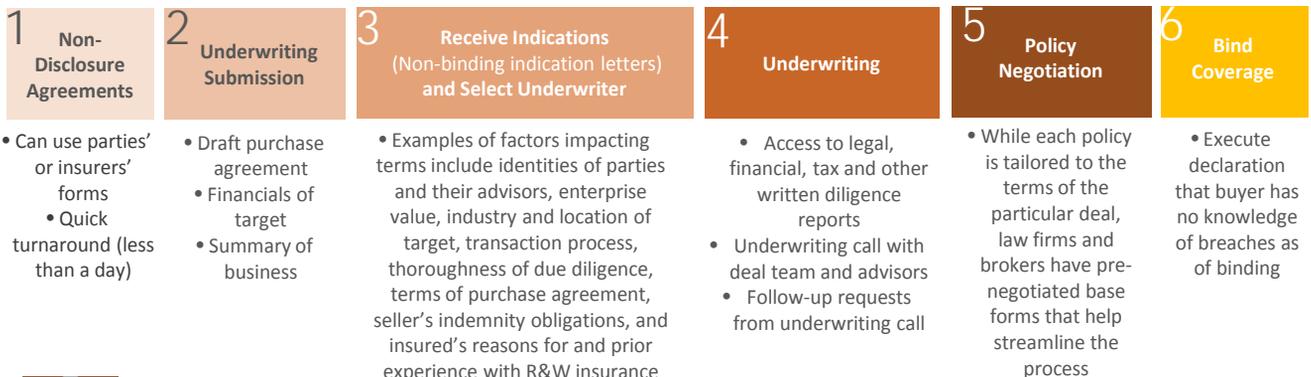
Insured: Buyer

Objective: To cover financial loss suffered as a result of a breach of seller's representations and warranties

Structure: Seller's indemnity capped at a lower amount and policy sits excess of the cap / retention (which can be split between buyer and seller)

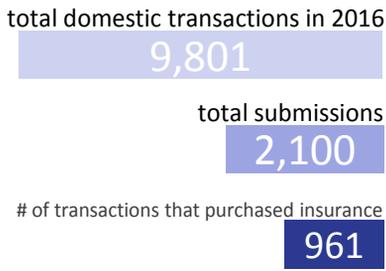
First- and Third-Party Coverage: Depending on the breach, policy can provide first- or third-party coverage

UNDERWRITING PROCESS



REPRESENTATIONS & WARRANTIES INSURANCE MARKET AND CLAIMS UPDATE

MARKET LANDSCAPE



Market Participation*

- AIG
- Allied World
- Ambridge
- Beazley
- Berkshire Hathaway
- Berkley
- BlueChip
- Concord
- CFC
- Chubb
- Euclid
- Ethos
- Everest
- Great American
- Hartford
- Ironshore
- RLI
- Tokio Marine
- HCC
- QBE
- Vale
- XL Catlin

*Includes insurers underwriting directly and MGAs/MGUs underwriting on behalf of insurers

EVOLUTION OF R&W INSURANCE

HISTORICAL R&W MARKET

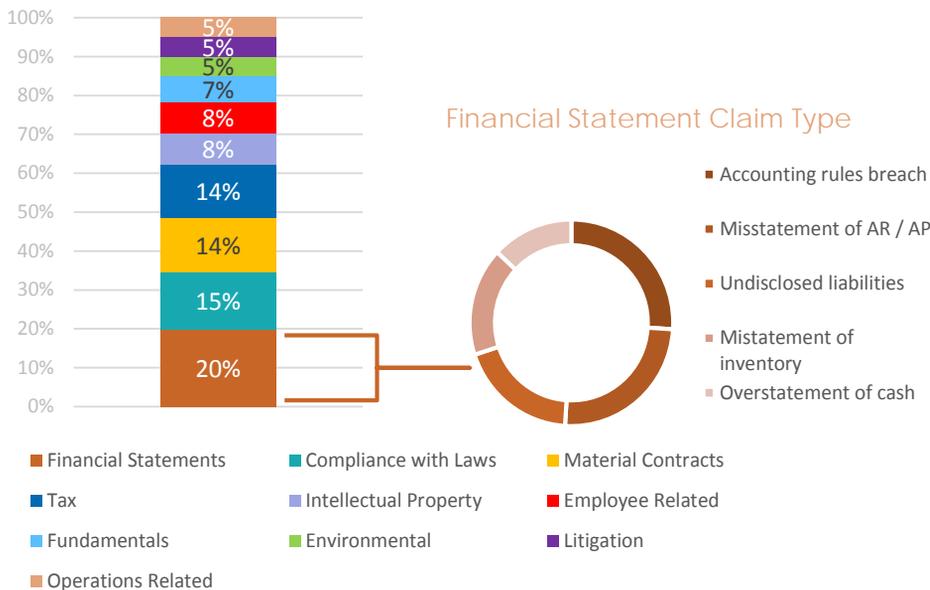
- Limited coverage (more subject-matter exclusions)
- Stricter requirements for retention levels and structures
- Limited market participation and competition
- Usually only available where enterprise value >\$50M
- Lengthy and rigorous underwriting process
- Used mostly on private-equity transactions

CURRENT R&W MARKET

- Expanding coverage (exclusions more often limited to known and undiligenced matters)
- Flexibility on retention levels and structures
- Increasing market competition and capacity
- Available in smaller deals (e.g. enterprise value of \$10mm)
- A more efficient underwriting and placement process based on nimble and deal-specific underwriting
- Used regularly by strategic as well as private-equity buyers

CLAIMS UPDATE

RWI Reported Claims by Breach Type (2015 claims data)



Other Claim Trends

- **Likelihood** / Even though deals of \$100mm or less accounted for 45% of all transactions, they made up only 17% of R&W claims from 2011-2015. Alternatively, deals greater than \$1bn account for 7% of all transactions but 23% of claims.
- **Timing** / 51% of R&W claims were reported within the first year of the policy, 41% within the second year, and 8% after the second year.
- **Severity** / 55% of AIG's claims from 2011 – 2015 resulted in claims >\$1mm. Of the claims greater than \$1mm but less than \$10mm, the average amount was \$3.5mm.

NOTE: While more claims information is becoming available, total industry claims data is limited in scope compared to more established insurance products. We expect more data to be accessible to the industry within the next several years as the product matures.



REPRESENTATIONS & WARRANTIES INSURANCE MARKET UPDATE

The transactional insurance marketplace continues to develop and mature. Just three years ago there were about five underwriters offering Representations & Warranties (R&W) insurance; now there are more than 20. The resulting competition has driven an expanded appetite for small deals and increased capacity for large deals. It has also incentivized creative underwriting and product development into market segments where R&W insurance had previously been unavailable.

Market appetite for smaller deals continues to increase / Historically R&W insurance had limited utility for deals under about \$50 million in enterprise value. Now deal parties are utilizing R&W insurance in small deals – even where enterprise value is less than \$10 million. Minimum premiums result in insureds purchasing at least \$3 million to \$5 million in policy limits, and minimum retentions often result in insureds retaining a higher percentage of enterprise value in small deals than they might in a larger one. Nonetheless, R&W insurance is an increasingly useful tool in closing deals for which it would not have been available (or would not have been cost-effective) just a short time ago.

Market capacity continues to increase for larger deals / Market capacity has increased to well more than \$1 billion limits available for any one deal. More underwriters now have the experience and credibility to lead large towers, and new markets to the R&W insurance space are driving increasingly competitive pricing for follow-form excess capacity.

New industry buyers lead to expanding coverage / Some markets are now willing to underwrite R&W insurance in industries where appetite was previously very limited. For example, R&W insurance placements in healthcare and financial industry deals are becoming more common. Similarly, markets have grown more willing to underwrite to risks that previously would have resulted in categorical exclusions. For example, FLSA / wage & hour matters can often be diligenced and underwritten, with some state-specific exceptions; healthcare matters fall into this category; even deals involving mortgage-related and other financial-services businesses can occasionally be underwritten; and underwriters are becoming more sophisticated in underwriting and covering cyber and data-security risks that might previously have triggered exclusions.

Tax coverage / More markets are underwriting tax risks, and sometimes offering package discounts for bundling R&W and tax insurance with a single market. For years a small handful of underwriters led tax placements, but now more than ten markets tout tax-insurance capacity. The competition driven by the influx of tax underwriters has generally decreased pricing for tax insurance, and, as with R&W insurance, appetite has expanded with the increased competition.



Contact:

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