Warranty & Indemnity Insurance – Real Estate

INTRODUCTION

W&I insurance is a generic name for insurances providing cover for losses arising from a breach of warranty or in certain cases under an indemnity. The insurance often provides advantages for both the buyer and the seller in M&A transactions as the seller’s liability to cover breaches under the SPA is transferred to an insurer. Through a W&I insurance, the seller may limit its monetary liabilities while still providing commercial warranties and without affecting the buyer’s possibility to claim for reimbursements.

WHY SHOULD A W&I INSURANCE BE CONSIDERED?

- A “clean exit” for the seller – by strategic use of a W&I insurance, the seller’s liability under the SPA for breaches of warranties are covered through the insurance policy.
- Financial incentives – as the W&I insurance replaces the financial security for warranty breaches, an escrow can be avoided meaning a higher cost efficiency which may contribute to the transaction value by 1% - 2% while the seller gains instant access to the proceeds.
- Well-established counterpart – uncertainties regarding a seller’s ability to reimburse the buyer due to insolvency or liquidations can be avoided in the event of a claim as the insurer assumes the warranties in the transaction.
- Relationship-building – facilitates negotiation tools between seller and buyer and eases a continued relationship, especially when the management of the company remains after the transaction is completed.
- In Real Estate transactions it is sometimes possible to place insurance without a retention/deductible, provided that each claim reaches a predetermined threshold level (de minimis).
- Simplifies the claims process in case of breaches if there are several sellers in a transaction as a claim only has to be made against one insurer.
- Provides improvements and/or differentiation of a bid in an auction process as the seller will be “off the hook”.

COSTS

Subject to signed NDAs, Aon will approach the insurance market to seek indicative terms, Non-Binding Indications (NBI), on a cost-free basis. Following these approaches, and giving consideration to their reputations and the competitive terms offered, you will, with Aon’s assistance, be able to select the insurer who is best positioned to provide a W&I insurance in respect of the specific transaction. Prior to commencing into underwriting, the insurer requires a signed “Expense Agreement”.

<table>
<thead>
<tr>
<th>STEPS</th>
<th>COSTS</th>
<th>COMMENTS</th>
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</thead>
<tbody>
<tr>
<td>NBI stage</td>
<td>Nil</td>
<td>Aon provides a report which summarizes the NBI’s and recommends an insurer which is best suited for the transaction</td>
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<tr>
<td>Insurer is engaged but no W&amp;I insurance is placed</td>
<td>EUR10K - EUR20K</td>
<td>Cost regards the insurer’s external legal fees – these are normally waived if a W&amp;I insurance is placed</td>
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<tr>
<td>If a W&amp;I insurance is placed</td>
<td>0.7% - 1.4% of insured limit</td>
<td>The price is based on Nordic real estate transactions</td>
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The premium in Nordic transactions is usually between 0.7% - 1.4% of the purchased limit. The aggregate limit is normally between 10% and 30% of the transaction value and reflects the seller’s liability in the SPA.
W&I INSURANCE CONTENT & COMMON EXCLUSIONS

WHAT THE INSURANCE COVERS

- Fundamental warranties
- Operational/Business warranties
- Tax warranties – for example declarations, payment of taxes and tax revisions
- Environmental warranties – for example permits and compliance
- Seller’s fraudulent acts – when the buyer is the policyholder

COMMON EXCLUSIONS

- Matters known to the insured
- Fraud of the insured
- Forward looking statements – such as budgetary forecasts
- Pension underfunding
- Construction defects, conditions of assets
- Fines and penalties (to the extent they are uninsurable)
- Bribery, corruption and sanctions. Bribery exclusions can be removed in respect of more benign territories and where the target has appropriate policies and procedures in place
- Pollution/contamination clean up
- Transfer pricing

TIMING

NBI-stage (indications regarding pricing and insurability of the warranties): 3-5 days
Risk assessment and W&I insurance placement: 4-7 days
Total: 7-12 days

W&I QUICK FACTS

- W&I Insurances are used in 25%-30% of all Swedish transactions
- The premium costs for W&I insurances have dropped more than 50% during the last years
- The amount of insurers has risen from 3 in 2007 to over 15 insurers
- Total capacity (insured limit / transaction) for Nordic transactions >EUR750m

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