Insurance Options for Offering Documents

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EXECUTIVE SUMMARY
This report details the insurance implications in respect of the issuance of Shareholder Circulars, Prospectus / Offering or Rights Offering Documents (Shareholder Documents) by publicly traded companies.

A public offering imposes liabilities on the company, its directors and its officers as they prepare and make statements to investors.

Companies have several options on how to deal with these offering liabilities; they could extend their Directors’ & Officers’ Liability Insurance (D&O) policy, retain the risk, or buy a stand-alone specialist policy (sometimes referred to as a Public Offering of Securities Insurance (POSI) or IPO-insurance). More and more, companies and more specifically, the management of the companies, are electing to buy the stand alone cover.

This summary addresses the insurance options available to deal with these exposures.

SHAREHOLDER DOCUMENT LIABILITIES – COMPANY OPTIONS
Below are the three options clients have when evaluating how to deal with the exposures incurred in such documents.

D&O Insurance
The first point to make is that most companies’ existing D&O policies do not automatically respond to claims arising out of such Shareholder Documents; most policies have a standard exclusion for such liabilities within their terms and conditions. However, D&O policies can be extended to include this cover often for an additional premium.

Before electing to cater for the offering exposures under a D&O policy, directors need to consider:
- there will only be one aggregate limit of insurance for the wrongful acts of the directors and the offering exposure – therefore directors are putting the limit of protection they have at a greater risk
- D&O insurers will charge an additional annual premium for the extension which would need to be included in the renewal for up to six years
- it is not likely that D&O pricing (and thus the extension) will remain at the current low levels
- at renewal, insurers may elect not to offer the extended cover for the offering or the cost would be prohibitive

Hence, the company and its directors must consider if they are comfortable that claims arising out of such Shareholder Documents could potentially erode their aggregate D&O limits.
Retention of Risk

The company may decide it do not wish to insure the exposures incurred in the statements made in the Shareholder Document. Whilst we understand that this approach will very much depend on the directors’ perception of risk, Aon does not recommend this approach.

One of the main reasons is that this could negatively impact the availability of the company’s ongoing D&O insurance. Insurers will consider very carefully any D&O claims made to see if they relate in any way to the statements made in such shareholder documents.

Stand Alone Insurance for Shareholder Document

Alternatively, the insurance market can offer a specialist product that would cover all the exposures incurred in a Shareholder Document in a stand-alone package.

This policy allows directors to ‘ring fence’ any potential liabilities arising out of the transaction, with separate limits for the policy period.

Aon recommends that clients seriously consider the purchase of such a stand-alone insurance policy to completely ring fence the exposures arising from such shareholder documents.

STAND-ALONE INSURANCE

Stand-alone offering document / prospectus policies cover exposures incurred under statements made to shareholders in such documents. This product derives from POSI insurance (Prospectus Liability); a policy that picks up liabilities arising from statements made in initial public offering (IPO) documents.

Aon has noted that clients are increasingly using POSI insurance rather than retaining the risk or extending their D&O. This seems to be a reflection of changing attitudes in the face of shifting corporate governance, shareholder attitudes and the current economic climate.

As with most insurance, the decision to purchase coverage is determined by circumstances and the risk attitude of the company in question.

Coverage

Stand-alone policies provide ‘wrap-around’ cover for the company, directors, officers and employees (if applicable) for liabilities arising out of Shareholder Documents.

The policy covers:
- Shareholder actions relating to the statements made in the Circular
- Claims arising from statements made during road-show presentations etc.
- Contractual indemnity provided by directors to issuing underwriters
- Legal Expenses coverage in respect of any regulatory investigations
- Shareholder derivative investigation costs
- Crisis Management expenses
- Typically a six year non-cancellable policy period

Coverage is offered for:
- the directors and officers and any relevant employees (if have liability)
- the company
- directors’ indemnity to the issuing underwriter
- selling and/or controlling shareholders (if applicable)
Benefits

There are advantages to a stand-alone policy, especially when comparing the purchase of this cover, against the inclusion within the D&O policy.

Benefits include *inter alia*:

- Cover is in place for the full six year period of liability
- Policy has a 'one off' premium which can be attributed as a transaction cost
- Policy covers all exposures not just 'wrongful acts'
- Cover for the entity is included as standard
- Claims against the Shareholder Document will not erode annual D&O limits
- Company doesn’t have to buy increased D&O limits for the policy period

**RECOMMENDED INSURANCE LIMITS**

Insurers who provide POSI insurance recommend that clients should consider limits of at least 10%-15% of the capital being raised. Obviously, it can be argued that secondary offering exposures are less than an “initial” offering and as such perhaps lower levels may be considered.

The final decision on the acceptable level of insurance will depend on the company; but factors such as the current economic climate and risk appetite will factor.

**CAPACITY AND COST FOR STAND ALONE INSURANCE**

We have found clients are increasingly buying insurance for these types of risk; reflecting a changing risk attitude in the face of shifting corporate governance and shareholder attitudes.

There is significant capacity available for this type of specialist insurance, but the biggest limitation in obtaining larger limits is likely to be pricing. We estimate that in total there may be up to USD 500m of insurance capacity if required for the right deal.

The cost of this insurance is very dependent on the risk profile of the company and the circumstances around the issuance of the shareholder documents.

Costs vary depending on the specific details of the risk but typically, coverage costs between 0.1% and 0.6% of the limit of insurance bought. Higher pricing may apply for certain risks, e.g. jurisdictions where insurers are less familiar with the listing rules. We would hesitate to provide more refined pricing estimates without first having discussions with insurers who have had a chance to review all the relevant information.

**CONCLUSION**

For the reasons discussed above, we recommend that clients give serious consideration for the purchase of a separate insurance policy to cover the liabilities arising from the issuance of Shareholder Documents.

We trust that this is of assistance but please contact us with any questions you may have.

Best regards,

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