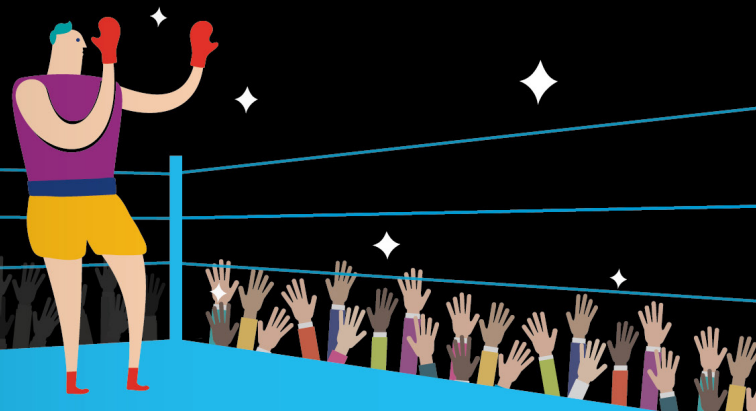


W&I claims: Who's in your corner?



The Warranty and Indemnity (W&I) insurance market has exploded globally over recent years. From its beginnings at the start of the millennium to its now commonplace use in M&A transactions, W&I insurance mitigates the sellers' and buyers' risks, protecting their interests as well as those of their lenders and shareholders. Insured parties rely on the security of an A+ rated insurer standing behind the warranties should one be breached.

Claims activity has significantly increased to nearly one in five policies¹, along with the increase in the number of W&I policies over the last two decades. However, W&I policies are unique to the transaction and claims tend to be complex, so a standardised claims process in the event of a warranty breach has not yet been developed. As a result, there is not much information available to policyholders about best practices for submitting a claim.

Mayer Brown, as a leading advisor in the W&I market, works closely with insureds and insurers drawing on the firm's transactional and insurance expertise to steady a course through the claims process. Lockton's global transactional risks team places in excess of 500 policies a year and works alongside their claims team to advise clients on how to resolve complex W&I insurance claims.

Jane Childs (Mayer Brown) and **Harry Blakelock (Lockton)** share their thoughts on what to expect from the W&I claims process and how to maximise its speed and effectiveness.

What does the claims process involve?

HB: At a high level, the same principles apply to a W&I claim as to any other claim: timely notification and close liaison with insurers, so as not to prejudice positions, and provision of relevant supporting documentation. However, each W&I policy is unique, providing coverage for risks that are specific to a transaction and the particular underlying acquisition agreement.

Essentially, all parties are working towards a common understanding of what has happened, so cooperation and a constructive dialogue between the insured and the insurer in the event of a claim is paramount from the outset. Helping the insurer's claims team to understand the nature of the issues is in both parties' interests.

JC: Even though the range of insured warranties is becoming more immediately recognisable, the underlying facts of a breach (and how they interact with those warranties) are as variable as the deals themselves. There are some distinct differences and additional complexities with the W&I claims process which should be borne in mind.

¹ 'M&A Insurance – The new normal?', AIG Claims Intelligence Series, 20th January 2019, <https://www.aig.com/content/dam/aig/america-canada/us/documents/insights/aig-manda-claimsintelligence-2018-w-and-i.pdf>.

Addressing the needs of the agreement and the policy, which may well be quite different

JC: Insureds will need to consider the contractual notification provisions in both the agreement and the policy, as notification deadlines will likely vary between them. Insureds should also ensure that the content of the notification meets the requirements of each contract respectively, and that notification is provided on a timely basis in both cases.

The importance of compliance with notification clauses under an agreement was recently highlighted in *Teoco UK Ltd vs Aircom*². The Court of Appeal confirmed that a buyer was unable to recover damages for breach of tax warranties because its notification letter failed to set out with sufficient clarity “reasonable details of the claim” in compliance with the provisions of the agreement.

As Harry mentioned above, the main aim of a claims process is for all parties to reach a common understanding in order to resolve it. In Mayer Brown’s experience, W&I insurers ideally like to see three key points addressed in a claims notification:

1. An explanation of which representations and/or warranties in the SPA are allegedly breached;
2. The evidence which is being relied on to demonstrate why and how the representations and/or warranties were allegedly breached; and
3. Evidence of the loss caused by the alleged breach.

Where a potential breach of warranty involves a claim by or dispute with a third party, insurers will need to be involved at an early stage.

Insurers often require that insureds obtain their consent before incurring any defence costs that will be claimed under the policy, or before any settlement is reached. It can often be beneficial for insurers to liaise with defence counsel directly, to help them understand the issues involved in the dispute with the third party. Therefore, insureds should anticipate that insurers may also want to hold update calls with your defence lawyers.

The supporting documents that can help an insurer’s claims team to review a new claim faster include:

- the final version of the agreement;
- confirmation of the Closing Date;
- the issued Policy;
- the final version of the Disclosure letter or Disclosure Schedule;
- final versions of any additional tax agreements and other relevant transaction documents;
- the underwriting Q&A/proposal forms;
- due diligence reports;
- all documentation related to the alleged breach e.g. a letter from a tax authority setting out the basis of a tax liability; the accountant’s advice confirming there are no grounds on which to challenge the tax demand; an (independent) auditor’s explanation of the impact of the warranty breach on the purchase price;
- correspondence between the buyer and seller pertaining to the alleged breaches; and
- information supporting the suffering of, and quantum of, the alleged loss.

The W&I broker will help the insured to provide much of this information to the claims team.

HB: Insureds are typically required to notify insurers as soon as practical even when perhaps the full suite of information is not yet forthcoming. They need to pull together as much information as is readily available to support the insurance claim when it is first made.

This initial process and dialogue is where an experienced claims broker can add real value. They help sharpen the focus of the insurer’s response and follow-up enquiries, to ensure they are relevant to the breach and loss issues. They can also help insureds think more broadly about what information or documentation might exist – or could be obtained – to advance the claims review.

² Details of judgment approved can be found at <http://www.bailii.org/ew/cases/EWCA/Civ/2018/23.html>.

Be prepared to share (possibly quite a lot)

HB: Given the inherent complexity of W&I claims, it is not unusual for insurers to ask for further details and explanations so they can better understand the factual issues relating to the breach, what has been established to date and what still might need investigation, and particularly to fully appreciate causation, quantum and loss.

JC: It is key that the insurer's claims team has a full picture of the information that was disclosed between the transactional parties when the risk was placed. With these details, the team can assess the adequacy of that disclosure, its relevance to the warranties that are alleged to have been breached, and the knowledge of the insured in relation to the issues causing the breach of warranty.

All of this means that the amount of supporting documentation that all parties might need to provide over the course of a W&I claim could be voluminous. Understandably, the greater the number of warranties that are breached, the longer the relevant time period, and the greater the number of entities and countries and advisers involved, the broader the range of documentation that is likely to need to be considered.

In more established insurance markets such as the professional liability and financial lines markets, Mayer Brown works with clients who are accustomed to providing this level of detailed information, and a healthy practice of transparency has developed around the insurance issues being considered. Insurers and policyholders alike want to target the enquiries at an early stage to focus on the issues that will materially impact the coverage determination, as well as liability and loss.

Our clients in these markets have come to appreciate that the insurers' questions are not driven by a suspicion that false or incomplete information is being provided. Rather, the insurer, not unlike the client when they engaged in the sale and purchase transaction at the outset, simply needs to be satisfied through its own due diligence that a covered warranty breach has occurred and that the appropriate level of indemnity is being provided.

Buyers and sellers have their stakeholders to whom they are accountable for the underlying transaction and insurers have their stakeholders to account to as well. Aside from the policyholders themselves, these include the regulator, shareholders and reinsurers, all of whom expect to see insureds treated fairly as well as an established audit trail which supports the outcome of the claim.

How insurance brokers can help in the claims process

HB: Insurers in the W&I market fall into two categories: (i) company markets, and (ii) Managing General Agents (MGAs). Company markets are typically large corporations who use the strength of their balance sheet to take on risks; they will also usually have an established and experienced claims team.

MGAs, on the other hand, are W&I experts underwriting policies on behalf of multiple capacity providers who take on the financial risk. In the event of a claim under a W&I policy, Lockton frequently assist the insured to liaise with representatives of both the MGA and the capacity providers sitting behind them. The actual claims decision-makers vary between MGAs depending on the arrangements they each have with their capacity providers. It is key that the insurance broker knows who these decision-makers are, to ensure they are all being kept up-to-date in order to respond to the claim.

With a clear and formal claims process yet to evolve in the W&I space, the guidance of a broker with an established claims team is vital. The broker's role is key, assisting and advising clients through the procedure of getting the right information to the insurer as well as assisting with the different investigative and review phases of the process, and managing expectations regarding the likely outcome.

A W&I broker's claims team has the legal and insurance expertise to handle complex disputes, with market know-how that enables them to argue a client's case to get the best possible settlement from the insurer. An in-house claims team also brings the added benefit of proximity to the policyholder, their risks and their deal from the moment the policy is taken out. If a breach of warranty does occur, a buyer can feel secure that the team handling their claim already knows the details of their case inside out.

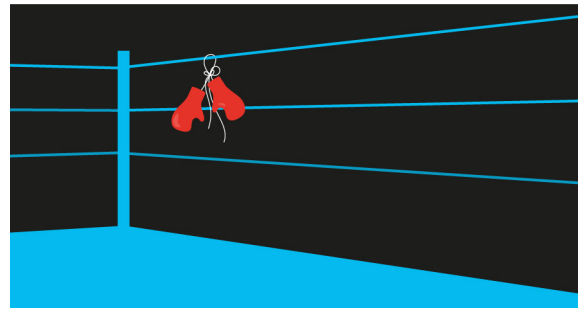
When difficult claims arise, it is invaluable to have a broker's insight into what motivates insurers, as well as the commercial muscle of their market relationships and premium spend. It is ordinarily in both parties' favour to avoid the lengthy and often costly processes of arbitration and/or litigation so a close working relationship between the W&I broker, their claims team, the W&I underwriter and the insurer's claims team is vital, to manage and resolve any issues.

Concluding remarks

Given the idiosyncrasies of W&I claims to date, a future where they follow a standardised process is currently uncertain. Complex, often high-value and commercially sensitive matters are rarely solved with an off-the-peg solution. Having the support of experienced professionals can help, but policyholders need to be prepared to:

- Share the details of the complexities of the warranties and the circumstances of the alleged breach with insurers; and
- Appreciate that the process of claims managers gaining a full understanding of the issues may require the provision of a volume of documentation, and take some time.

As ever, the key to a respectful and successful relationship is continuous and open communication between the parties, to reach a common goal: determining the insurance claim with the benefit of the best evidence available to support that claim and to get to the right outcome.



Harry Blakelock Senior Vice President | Lockton

www.linkedin.com/in/harry-blakelock-4568a216/

E harry.blakelock@uk.lockton.com

T +44 (0)20 7933 2671

M +44 (0)75 0095 9451

Jane Childs Partner | Mayer Brown

www.linkedin.com/in/jane-childs-5a311221/

E jchilds@mayerbrown.com

T +44 (0)20 7398 4622