

# Legal Update

## Four Key Takeaways from FSN Capital's Recent €50 Million Warranty & Indemnity Insurance Claim

A consortium of 12 insurance underwriters led by Liberty GTS recently paid a €50 million claim under a warranty and indemnity liability (W&I) insurance policy issued in connection with FSN Capital's acquisition of Gram Equipment.<sup>1</sup> This is one of the largest, publicly announced claims paid under a W&I policy in recent memory. A few key points about W&I policies and claims in general can be derived from publicly available information about this claim,<sup>2</sup> and we briefly describe these points below.

As background, according to FSN Capital, it filed its insurance claim in June 2018, shortly after its acquisition of Gram Equipment in early 2018. The insurance claim alleged that the seller breached several of the warranties in the share purchase agreement, including warranties related to accounting material and the seller's duty of disclosure. Following an investigation, the insurers agreed to pay the full €50 million limit under the W&I insurance policy.

A few key points to note:

1. **Financial Statement Representations:** Some of the representations that appear to underlie these claims are related to financial statements; representations on this subject are some of the more common ones at issue in claims under W&I policies.

While publicly available information does not indicate the scope or breadth of the representations at issue, in our work on behalf of W&I insurers, we often see a wide variation in these types of representations. Certain formulations of these representations may be more difficult to cover under a W&I policy, especially without sufficient diligence. They include:

- a. Representations that cover the adequacy and completeness of "books and records," when such term is undefined or broadly defined;
  - b. Representations that cover the sufficiency of internal controls and/or procedures to uncover fraud or errors in financial statements or records; and
  - c. Representations regarding off-balance-sheet or other "off the books" arrangements.
2. **"Full Disclosure"-Type Representations:** Reports indicate that the claim also included breaches of representations regarding seller's "duty of loyal disclosure." Information on the governing law of the share purchase agreement and W&I policy was not publicly available—in this transaction, the seller was a Swedish

company and the target company appears to have operations in Denmark, the United States and Singapore. While we offer no comment on how this type of representation may be construed under the laws of different jurisdictions, one general takeaway on this point is the importance of the breadth of representations regarding full disclosure and reliance on information provided. In reviewing transaction documents, one should consider the scope of knowledge-savings clauses (i.e., sandbagging provisions) in indemnities and whether the definition of fraud includes a reliance component. The extent to which provisions like these are incorporated in W&I policies could greatly impact the insured's ability to recover under a W&I policy.

- 3. Importance of Audited Financial Statements:** Reports on this claim also state that the buyer became aware of the issues in question during the preparation of annual financial statements, when independent statutory auditors performed an audit. According to the buyer's claim, accounting "irregularities" had a material impact on the target's EBITDA and resulted in insured losses. As a result, another key takeaway for W&I underwriters and their counsel is determining whether audits of target company financials have regularly occurred and, even if so, whether the audits have been conducted by reputable accounting firms and whether those firms have found any irregularities, internal controls deficiencies and/or restatements of financial statements. Another key point in diligence is the scope of financial advisor diligence, which may not include a review or assessment of things such as internal controls.

- 4. Other Claims:** One last point to note, for context: According to the buyer, the insurance payout did not fully compensate the buyer for its losses in this matter, and it is pursuing legal claims against the seller and senior management of the target. According to reports, at least some of the other transaction-related claims relate to the post-closing purchase price adjustment. While allegations must, obviously, be proven by an adjudicator of fact, it's reasonable to infer that there may be numerous facts and circumstances that are unreported and/or tangential to this W&I claim that may have had an impact of the resolution of the claim with the W&I insurers. As a result, as a disclaimer, we note that this case may not be typical of claims generally or claims based on representations of this nature.

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## Endnotes

<sup>1</sup> <https://fsncapital.com/news/fsn-capital-gram-insurance-limit-paid/>

<sup>2</sup> Mayer Brown did not play a role in underwriting the W&I policy or in the related transaction or claim/dispute.

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