So far, it seems that 2014's dynamic Mergers & Acquisitions market is charging into 2015.

It was undoubtedly an exceptional year for deal making with Thomson Reuters reporting a 47% increase in the total value of worldwide M&A in its annual Mergers & Acquisitions Review for 2014.

Purchase price multiples reached 2007 levels which, according to the Wall Street Journal were driven by high levels of leverage, with debt being available at well over five times EBITDA.

ON THE UP

In tandem with the significant increase in M&A deals, there was a substantial rise in the usage of M&A Insurance to help facilitate these transactions.

Transactional Insurance policies provide assistance in the completion of a transaction, with the key products being Warranty & Indemnity (W&I), Tax Liability and Contingency coverage.

These solutions cater for a multitude of issues, ranging from a breach of the warranties or a claim under the tax indemnity set out in the SPA, to more specific tax, regulatory, litigation or other contingent liabilities that are either ongoing or potential.

“\n\n“The evolution of these products, with the flexibility of the cover available and the competitively priced premiums, led to a huge increase of interest from the M&A market in 2014 and we expect this to continue in 2015” says James M Wilson, Head of Transaction Solutions at Protean Risk, a specialist broker of Transactional Insurance products.

2015 has already been labelled as the year in which M&A activity will be dominated by smaller and mid-market deals, and with the significant amount of liquidity and more flexible debt packages available, growth in the M&A market will accelerate.

The private equity sector will continue to drive activity this year and the number of deals will increase given the amount of “dry powder” available and very favourable financing.

USE IT OR LOSE IT

Even though last year was branded as a phenomenal year, surprisingly the number of deals in the UK that made it over the finishing line was at the lowest level since the global financial crisis.

Transactional Insurance can help prevent this by facilitating the closing of a transaction through overcoming deal impasses, improving or securing financing arrangements, and as an effective risk management tool providing balance sheet protection.

This will be invaluable for M&A advisers in 2015, in which abundant cash reserves, recovering markets and competing buyers chasing high-quality deals will lead to even more competition.

Transactional Insurance products can be used as a strategic tool to gain a competitive advantage in an environment where auction processes are becoming commonplace, with Sellers seeking clean exits and insisting on low Seller caps. Thus, there is an increasing need for the parties to use W&I as part of the normal transaction process.

M&A Professionals expect 2015 to be an extremely active year, however uncertainties in the deal making environment will give rise to an increase in the application of M&A Insurance.

2015 has already been labelled as the year in which M&A activity will be dominated by smaller and mid-market deals, and with the significant amount of liquidity and more flexible debt packages available, growth in the M&A market will accelerate.

The private equity sector will continue to drive activity this year and the number of deals will increase given the amount of “dry powder” available and very favourable financing.

USE IT OR LOSE IT

Even though last year was branded as a phenomenal year, surprisingly the number of deals in the UK that made it over the finishing line was at the lowest level since the global financial crisis.

Transactional Insurance can help prevent this by facilitating the closing of a transaction through overcoming deal impasses, improving or securing financing arrangements, and as an effective risk management tool providing balance sheet protection.

This will be invaluable for M&A advisers in 2015, in which abundant cash reserves, recovering markets and competing buyers chasing high-quality deals will lead to even more competition.

Transactional Insurance products can be used as a strategic tool to gain a competitive advantage in an environment where auction processes are becoming commonplace, with Sellers seeking clean exits and insisting on low Seller caps. Thus, there is an increasing need for the parties to use W&I as part of the normal transaction process.

M&A Professionals expect 2015 to be an extremely active year, however uncertainties in the deal making environment will give rise to an increase in the application of M&A Insurance.
“As warranties can often be the most deliberated aspects during negotiations, tactical use of W&I insurance can successfully facilitate the transaction process” says Emma Danks, Partner at Taylor Wessing, who specialises in private equity.

Buyers use the insurance to gain additional financial protection above an agreed warranty cap (or replace a cap if none is offered), or to sit behind the Seller’s cap should there be doubts about the ability to bring a claim against the Seller. Sellers traditionally use the insurance to gain access to the deal proceeds that would otherwise be tied up in escrow to back their warranty cap obligations.

The W&I policy allows for a clean exit by the Seller with limited recourse against them. It gives the Buyer certainty in the event an issue arises that amounts to a breach of warranties and importantly, frees up capital that can be retained by the Sellers to enhance returns elsewhere or used by the Buyer in the business going forward.

“W&I insurance is used to take issues off the table for my clients during an auction process, putting a cost effective policy in place as opposed to negatively impacting the required purchase price” states Matthew Gooch, Managing Director and Head of European Banking at William Blair.

RELAX ABOUT TAX
Another item that will continue to take centre stage for M&A in 2015 is Tax, so understanding these issues as early as possible in the deal process is crucial and will often have a significant effect on deal value. The increase in scrutiny from tax authorities globally, and the introduction of more complex tax rules have created an uncertain climate, as any tax inconsistency coming under the spotlight could prevent the completion of a transaction or pose issues post close. This is particularly salient in cross-border deals, which are expected to increase this year.

A growing trend to address this uncertainty has been to turn to insurance, which can be utilised by either the Buyer or Seller to protect them from a tax exposure representing a risk to the target business. A W&I policy will usually cover tax liabilities that are unknown at the time of completion, as these may give eventual rise to claims under the tax warranties and covenant.

As the knowledge and experience in the insurance market has evolved, it has also become possible for underwriters to cover specific and known tax issues identified during the due diligence process. These risks include, but are not limited to, residency issues, employment tax and group reorganisations, which can be insured in a bespoke, tailored policy.

“A tax policy can be used in situations where a transaction party is unwilling or unable to tolerate uncertainty due to the magnitude of the financial exposure relative to the size of the transaction, or a buyer has not identified any specific tax issue but wants to prudently minimize risk relating to the Seller’s pre-closing tax issues” says Jeff Doran, Managing Director of Ambridge Europe, a specialist underwriter of Transactional Insurance products.

READY, SET, GO
As we look ahead in 2015 and the year the deal makers are expecting evolves, Transactional Insurance too will develop, both in popularity and dynamism. Through tackling some of the transaction hurdles of the past and alleviating uncertainties when negotiating a deal, insurance can help limit the reasons for the failed transactions of previous years. Dealmakers recognise that successful deals require superior strategies, comprehensive DD and well developed execution plans.

By being adaptable to deal deadlines, flexible in coverage and mitigating the concerns of parties when structuring a deal, Transactional Insurance is most definitely poised for the 2015 road ahead.

For more information on Transactional Insurance, please contact:
James M. Wilson
Head of Transaction Solutions
T: +44 (0)20 3763 5355
M: +44 (0)7720 361 151
E: jameswilson@proteanrisk.com

www.proteanrisk.com/transaction-solutions