

COVID-19 – Transaction Liability Considerations Reps & Warranties Insurance

What Can USI do?

COVID-19 exclusions. Are Representations and Warranties (R&W) Insurers applying?

- **Some are imposing COVID-19 exclusions on a blanket basis**, while others are more industry dependent. Booking, Entertainment, Airlines, Cruise/Casinos and Hotels (BEACH) industries being most impacted.
- **Many are not, for the moment.** All markets will flag COVID-19 as a key underwriting diligence issue or as a heightened risk that may need an exclusion (depending on the diligence provided during the U/W process).
- **Beware of “Loss” definition.** Some insurers are narrowing their definition of Loss to limit or exclude COVID-19 matters vs. adding an outright exclusion.

Many exclusion wordings attempt to be “absolute.” Seek to work with the insurers to eliminate or narrow such limitations. **Examples:**

- Eliminate broad “arising from, related to or in any way involving...” preamble language; **seek “for” preamble.**
- Limit any exclusion to COVID-19-related supply chain interruption or other operational specific impact (**as opposed to all COVID-19-related matters**).

Transactions Where Diligence is Underway but Not Signed

- We expect to see extensions of exclusivity agreements to better digest COVID-19 impact.
- **Diligence efforts will be notably hampered or impossible (in near term)** due to shelter-in-place directives, availability of personnel, restriction of physical visits and modified production schedules.
- Where insurance terms are provided, we expect more contingent exclusions relating to open diligence that can not be completed because of COVID-19 related obstacles (i.e. closed facilities, unavailable data, need for face-to-face meetings).
- Buyer and seller will need to determine how the liability for these excluded areas will be addressed - if diligence is not satisfactory enough to remove the proposed exclusion(s).

Signed Transactions That Have Yet to Close

- **Firms are examining the MAC or MAE (Material Adverse Change or Effect)** within the purchase agreements to evaluate whether the clause is triggered.
 - If triggered, this could allow terms and pricing to be amended or possibly terminated.
- **Underwriters – more focused on COVID-19 issues** in their bringdown calls prior to closing; looking to better ascertain the depth and breadth of changes in the underlying business before closing.
- Expect delays in closing dates due to pending regulatory approvals or financing delays.

COVID-19's Effect on New M&A Activity/R&W Placements

- A **slowdown** of M&A activity for the next quarter until firms can better ascertain the economic effects of COVID-19, including the impact on a target’s business.
- **Most believe activity will resume relatively quickly** as crisis dissipates, unleashing pent-up demand. There is too much capital and a low interest rate environment to be an overly extended slow down in M&A activity.
- Any acquisition activity in near term will likely be in the sectors that are less impacted by COVID-19 and/or based on more opportunistic strategies (i.e. the target company is in dire need of capital).
- **Outlook: Future diligence practices will focus on business continuity plans, supplier sourcing, nimbleness of HR and remote IT functions (remote workforce issues, network practices, etc.).**

Please contact your USI representative for further information or to address any questions.