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.