Representations and Warranties

Case Study 1 – the VC clean exit

Buyer: Large multinational corporation

Seller: Mid size technology company with split ownership between management and 6 different VC houses with varying levels of ownership and no board representation

Purchase price: $160m

Escrow: $24m, 2 year duration for most warranties and 7 years for Tax and IP

Issue: Despite the large negotiated escrow, the Buyer was insistent on joint and several liability above and beyond the $24m, 2 year negotiated cap. The Management team and one VC house were prepared to move forward on that basis. The other VCs refused to agree to the deal beyond the negotiated $24m/2 year agreed escrow.

Solution: We negotiated a policy that provided protection to the VC houses that sat excess of the $24m/2 year cap for a total of $116m of coverage. This started to run once the original $24m had been fully eroded. The policy ran for a period of seven years covering all warranties. All the VC were insured but the management team, who were comfortable with their warranties remained uninsured.

The process took 6 weeks from beginning to end and the overall premium was 2.1% of the limit of indemnity purchased. The price was so competitive largely due to the high point of attachment and Management's willingness to remain uncovered.

Case Study 2 – Sleep easy cover on a trade sale

Buyer: Timber production company

Seller: Timber production company

Purchase price: $50m

Escrow: $ Various

Issue: Both purchaser and vendor were content with the majority of warranties and with a central basket for those warranties. However, several warranties, most notably Environmental and Process Patent warranties were the subject of debate. The mechanism was a primary escrow basket for all warranties for the first two years that covered the general and special warranties. Once two years passed that basket was released and the second basket (only for the special warranties) continued for another 5 years. However, if in the first two years the special warranties were called, they would erode the first basket and only then could the second basket be eroded.

Solution: We structured a policy that allowed coverage for all warranties up to the full limit of both baskets. The process took about a month from beginning to end for a limit of $10m; the overall premium was 3.5% of the limit purchased.