



Developing Business:

words | Ian Le Breton

Transaction Insurance

Regular readers may remember that in past articles, I have written about several aspects of the insurance industry — in particular the growing importance of new insurance business to Gibraltar. After all Gibraltar's insurance industry has expanded from just 13 licensed insurers at the turn of the century to over 60 today. That's a lot of new business and a lot of new employment.

I have set out in the past why Gibraltar is such an important insurance centre. As we know, Gibraltar's financial services sector, including insurance, is very well regulated and the benign fiscal regime makes doing business here very tax efficient. Tie in these advantages with the speed of licensing, the ability to passport services across the EU, a highly trained, professional workforce and a legal system based on English law and the overall offering is unbeatable.

I learned long ago that our insurance

industry was certainly not limited to the traditional motor policies and "personal lines" — although these are very well catered for locally. Gibraltar is better known internationally for providing innovative insurance solutions that are increasingly in demand in an ever more sophisticated financial world.

Take, for instance, transactional insurance business. It is a segment of the wider insurance market that demonstrates huge promise — and therefore is excellent news for Gibraltar. The principles are not difficult

to grasp and yet, for reasons I shall explain, the market has yet to reach its full potential.

Geoff Trew, managing director of Sovereign Insurance Services at Ocean Village, told me once that almost any risk can be insured — provided one is prepared to pay the premium. His team works closely with leading transaction insurance practitioner Protean Risk whose head of Transaction Solutions, James Wilson, has also endeavoured to keep me up to speed in this fast growing field.

It may seem obvious but transactional

insurance seeks to offer protection to those involved in any sort of deal, arrangement or other financial transaction. If it were so easy, why has the market failed thus far to achieve its full potential? There are several reasons for this; read on.

In the past, insuring "transactions" was simply not commonly done. Few people outside the industry knew of its existence, premiums were expensive and the coverage being offered was too restrictive. Combine these factors with limited knowledge and experience from insurers and the often lengthy lead times involved and, perhaps, one can understand the limited appeal.

Fast-forward to 2014 and things have changed markedly. Demand and thus usage has risen significantly with the result that coverage has expanded drastically whilst premiums have reduced considerably. There is far more knowledge and experience to be found within the underwriting community and turnaround can now be measured in hours. So I thought it might be an opportune time to look at the sector.

Work undertaken in the mergers and acquisition market — normally abbreviated to "M&A" — is particularly suited to transactional insurance. There is a difference between these two types of transaction although increasingly the distinction between a "merger" and an "acquisition" has become blurred. Legally, a merger is the coming together of two companies into one entity. On the other hand, an acquisition involves one firm absorbing another and establishing itself as the new owner. Either way, some form of insurance could be considered whilst the transaction is in progress.

The global financial crisis over the last few years has of course had a dramatic effect on the level of M&A activity, which is only now seeing more positive signs of life. Indeed many would blame some of the more spectacular — and in hindsight ill judged — deals for exacerbating, if not in fact causing, the crisis in the first place.

In recent months, the UK financial press has been dominated by what would have been the largest ever takeover of a UK company. The US pharmaceutical giant Pfizer was seeking to purchase its Anglo-Swedish competitor AstraZeneca in an eye-popping £69 billion deal. The deal fell through because AstraZeneca (and, of course, its shareholders) rejected the offer as seriously undervaluing the business. Ultimately then, it was a question of market economics but at the time, as readers will recall, there was a big political brouhaha.

The proposed transaction failed but no doubt the advisers were well paid on all sides and this will have cost a great deal. This story broke at the same time that I was getting interested in transactional insurance and I wondered how much insurance protection might have been written. We shall never know the final bill but we can at least consider the types of "products" that might have been employed to manage the risk. Broadly there are three basic lines.

Warranty and Indemnity (W&I) insurance provides cover for either the buyer or seller in a transaction (or conceivably both sides).

The underlying insurance policy provides protection in cases where a breach of warranty occurs or a claim under an indemnity is made as set out in any Sales Purchase Agreement.

Taxation liability is another "product" that is designed to reduce or eliminate tax exposure. For example, this might arise where underlying legal advice has been provided supporting a particular tax treatment that may be subject to a future challenge by tax authorities.

Finally, contingency insurance is designed to cover a wide variety of legal or other "con-

tingent" costs. These risks need not necessarily relate to a specific transaction. An example could be where a commercial property owner is concerned that his tenants might be evicted because of a challenge by a public authority for breaching zoning regulations. Should they be forced to leave, the buyer might see his "contingent liability" turned into a real one as the rent roll plummets. All of this can be insured.

Aside from M&A work, other areas where transactional insurance might be considered would include restructurings and workouts, financing or investments, liquidations and licensing agreements. In other words, transactional insurance could be included in a large part of the legal and corporate advisory work undertaken by Gibraltar firms and for which we have become respected globally.

My good friend James Wilson believes that this market segment presents huge potential. Insuring transactions is clearly increasing in popularity but even so, less than 5% of all worldwide transactions are currently insured. Imagine finding a market where fully 19 out of any 20 possible commercial targets are currently available. It is not difficult then to understand the excitement being generated by this part of the insurance business.

James went on to tell me that the majority of claims — approximately six out of every ten — that are made by such transactional insurance policy holders results from tax or financial valuation. When dealing with corporate M&A, transactional insurance enables parties to transfer risk — and these may relate to both known and unknown threats.

A well thought out transactional insurance policy will facilitate a potential deal as well as providing tangible financial protection for the parties involved. Private equity purchasers were traditionally the main customers for this product. However it is clear that more corporates are now purchasing such protection, so it is to be hoped that the current 5% market take up can only increase — to the benefit of all concerned.

As a keen proponent of any potential upside for Gibraltar firms this is clearly an area that I'd like to see local firms develop. There is definitely potential out there and, as the economic recovery becomes a reality in several key markets, the level of corporate activity in particular is likely to increase. Using transactional insurance serves a very useful purpose in facilitating such deals. I expect local industry players will become more involved in this exciting business, to the benefit not only of themselves but all of us in Gibraltar. ■



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