

## Multiple-Based Damage Claims Under Representation & Warranty Insurance

### PENpoints

*A recent claim against a representations and warranties insurance policy exemplifies an insured's positive claims experience and how such policies may allow a buyer to recover multiple-based damages.*

Private equity funds are increasingly using representations and warranties (R&W) insurance and related products (such as tax, specific litigation and other contingent liability insurance) in connection with acquisitions as they become more familiar with the product and its advantages.<sup>1</sup> Acquirors considering R&W insurance frequently raise concerns about the claims process and claims experience. A recent claim against a policy issued by Concord Specialty Risk (Concord) both provides an example of an insured's positive claims experience and highlights the possibility for a buyer to recover multiple-based damages under R&W insurance.

### R&W Insurance Advantages

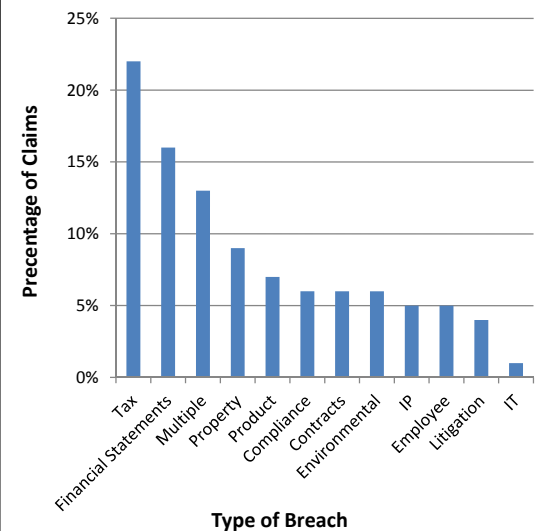
Under an acquisition-oriented R&W policy, the insurance company agrees to insure the buyer against loss arising out of breaches of the seller's representations and warranties. The insurer's assumption of representation and warranty risk can result in better contract terms for both buyer and seller. For example, the seller may agree to make broader representations and warranties if buyer's primary recourse for breach is against the insurance policy, and the buyer may agree to a lower cap on seller's post-closing indemnification exposure as it will have recourse against the insurance policy. In addition, R&W insurance often simplifies negotiations between buyer and seller, resulting in a more amicable, cost-effective and efficient process.

### Claims Experience

As repeat participants in a competitive insurance market, established R&W insurers have an incentive to act reasonably when responding to a claim. In order to continue to attract business, an insurer seeks to enhance its reputation as a reliable counterparty that pays valid claims under its policies. As a result, an insurer is subject to market pressures that do not similarly influence a one-time seller when facing an indemnification claim under an acquisition agreement.

### PENstats

#### R&W Insurance Claims: Types of Alleged Breaches (Global)



Source: AIG July 2013 Claims Review

A Kirkland client's recent acquisition experience is instructive. Buyer acquired target using R&W insurance issued by Concord. After closing, buyer discovered that seller had breached its financial statements representation, leading to an inflated EBITDA figure and, therefore, purchase price (which had been calculated as an EBITDA multiple). Buyer made a claim under the policy for the breach, seeking damages based in part on the purchase price multiple of the EBITDA misstatement. Buyer and Concord settled the claim for an amount that was based in part on the multiple of misstated EBITDA, which buyer felt appropriately reflected the damages it suffered as a result of the financial statement misrepresentation.

### INSIDE KIRKLANDPEN

*Upcoming Events . . . . . 3*

### Multiple-Based Damages

During an acquisition agreement negotiation, the parties frequently heavily negotiate buyer's right to recover consequential, special and indirect damages and damages based on a multiple. Some sellers insist that buyer waive the right to recover such damages, and some buyers are unwilling to proceed if the contract limits buyer's right to indemnification for any and all damages recoverable at law. When a contract includes categorical damage waivers (including consequential and multiple-based damages), a buyer may not be fully compensated for the decreased value of its investment arising out of a breach of a seller's representations and warranties. Indeed, buyers often assert that excluding multiple-based damages in a transaction where buyer

has priced the target based on an earnings multiple can deprive it of protection against breaches of the representations and warranties most important to its pricing decision (e.g., financial statements and customer relationships).

In the case cited above, R&W insurance allowed buyer to protect itself against a breach of such "pricing" representations and warranties and receive appropriate compensation for its purchase price overpayment, while avoiding a difficult discussion with seller over damage limitations. In deals where the disagreement between buyer and seller on the issue of categorical damage exclusions appears intractable, R&W insurance may help facilitate a satisfactory resolution.

---

1 One major carrier recently reported a 40 percent increase in 2012 R&W insurance over 2011. Jay Rittberg, "M&A Insurance Heats Up Despite Lower Deal Volumes," *Advisen Management Liability Journal*, September 2012, at 11, 11.

---

If you have any questions about the matters addressed in this *KirklandPEN*, please contact the following Kirkland authors or your regular Kirkland contact.

**Dr. Markus P. Bolsinger LL.M.**

<http://www.kirkland.com/mbolsinger>

+1 212-446-4938

**Jeremy S. Liss, P.C.**

<http://www.kirkland.com/jliss>

+1 312-862-2286

**Michael J. Snow**

<http://www.kirkland.com/msnow>

+1 312-862-7124

**PENnotes****Securities Filings 2013: Practical Guidance in a Changing Environment  
Chicago, November 14-15, 2013**

This program will analyze in detail the principal forms used for filings with the SEC under the Securities Act of 1933 and the Securities Exchange Act of 1934, with particular emphasis on the mechanics of and timing for assembling particular filings. Each segment of the program will incorporate practical drafting and disclosure tips. Ethics credit and recent legislation and SEC rule changes affecting disclosure obligations, in particular those resulting from the JOBS Act, will be woven within the topics covered. Kirkland partner Gerald T. Nowak will speak at the event. Click [here](#) for more information.

**Structuring and Negotiating LBOs: Advance Topics  
Chicago, November 21, 2013**

This roundtable breakfast discussion on representation and warranty insurance will take place on November 21 at Kirkland's Chicago office. This will be the first in a series on advanced topics relating to private equity transactions and is intended for experienced private equity professionals who are responsible for overseeing or executing transactions. Registration details to come.

**PLI Chicago Tax Strategies for Corporate Acquisitions, Dispositions, Spin-Offs, Joint Ventures, Financings, Reorganizations & Restructurings 2013  
Chicago, November 19-21, 2013**

This program will focus on the tax issues presented by the entire spectrum of modern major corporate transactions. Kirkland partner Jack Levin will participate on the topic titled "Structuring Leveraged Buyouts," partner Todd Maynes will present on the topic titled "Tax Strategies for Financially Troubled Businesses and Other Loss Companies," and partner Jeffrey Sheffield will participate in the panel titled "Current Issues in Divisive Strategies - Spin-Offs and Synthetic Spin-Offs." Click [here](#) for more information.

**Beijing**

Kirkland & Ellis International LLP  
29th Floor, China World Office 2  
No. 1 Jian Guo Men Wai Avenue  
Beijing 100004  
P.R. China  
+8610 5737 9300  
+8610 5737 9301 fax

**Chicago**

Kirkland & Ellis LLP  
300 North LaSalle  
Chicago, IL 60654  
+1 (312) 862-2000  
+1 (312) 862-2200 fax

**Hong Kong**

Kirkland & Ellis  
26th Floor, Gloucester Tower  
The Landmark  
15 Queen's Road Central  
Hong Kong  
+852-3761-3300  
+852-3761-3301 fax

**London**

Kirkland & Ellis International LLP  
30 St Mary Axe  
London, EC3A 8AF  
United Kingdom  
+44 20 7469 2000  
+44 20 7469 2001 fax

**Los Angeles**

Kirkland & Ellis LLP  
333 South Hope Street  
Los Angeles, CA 90071  
+1 (213) 680-8400  
+1 (213) 680-8500 fax

**Munich**

Kirkland & Ellis International LLP  
Maximilianstrasse 11  
80539 Munich  
Germany  
+49 89 2030 6000  
+49 89 2030 6100 fax

**New York**

Kirkland & Ellis LLP  
601 Lexington Avenue  
New York, NY 10022  
+1 (212) 446-4800  
+1 (212) 446-4900 fax

**Palo Alto**

Kirkland & Ellis LLP  
3330 Hillview Avenue  
Palo Alto, CA 94304  
+1 (650) 859-7000  
+1 (650) 859-7500 fax

**San Francisco**

Kirkland & Ellis LLP  
555 California Street  
San Francisco, CA 94104  
+1 (415) 439-1400  
+1 (415) 439-1500 fax

**Shanghai**

Kirkland & Ellis International LLP  
11th Floor, HSBC Building  
Shanghai IFC  
8 Century Avenue  
Pudong New District  
Shanghai 200120  
P.R. China  
+8621 3857 6300  
+8621 3857 6301 fax

**Washington, D.C.**

Kirkland & Ellis LLP  
655 Fifteenth Street, N.W.  
Washington, D.C. 20005  
+1 (202) 879-5000  
+1 (202) 879-5200 fax

# Private Equity Practice at Kirkland & Ellis

Kirkland & Ellis' nearly 400 private equity attorneys have handled leveraged buyouts, growth equity transactions, recapitalizations, going-private transactions and the formation of private equity, venture capital and hedge funds on behalf of more than 300 private equity firms around the world.

Kirkland has been widely recognized for its preeminent private equity practice. The Firm was named "Private Equity Group of the Year" in 2012 and 2013 by *Law360* and was commended as being the most active private equity law firm of the last decade in *The PitchBook Decade Report*. In addition, Kirkland was awarded "Best M&A Firm in the United States" at *World Finance's* 2012 Legal Awards and was honored as the "Private Equity Team of the Year" at the 2011 *IFLR Americas Awards*.

The Firm was ranked as the #1 law firm for both Global and U.S. Buyouts by deal volume in Mergermarket's *League Tables of Legal Advisors to Global M&A for Full Year 2011 and 2012*, and has consistently received top rankings among law firms in Private Equity by Chambers & Partners, *The Legal 500*, the Practical Law Company and *IFLR*, among others.

*The Lawyer* magazine has recognized Kirkland as one of its "Transatlantic Elite" every year since 2008, having noted that the firm is "leading the transatlantic market for the provision of top-end transactional services ... on the basis of a stellar client base, regular roles on top deals, market-leading finances and the cream of the legal market talent."

## KIRKLANDPEN

## KIRKLAND & ELLIS

### EDITORS

**Jack S. Levin, P.C.**  
**Margaret A. Gibson, P.C.**  
**Norbert B. Knapke II**

### SUBSCRIPTIONS

To subscribe to *KirklandPEN*, please email  
[kirklandpen@kirkland.com](mailto:kirklandpen@kirkland.com)  
+1 (312) 862-3356

This publication is distributed with the understanding that the author, publisher and distributor of this publication and/or any linked publication are not rendering legal, accounting, or other professional advice or opinions on specific facts or matters and, accordingly, assume no liability whatsoever in connection with its use. Pursuant to applicable rules of professional conduct, portions of this publication may constitute Attorney Advertising.

© 2013 KIRKLAND & ELLIS LLP. All rights reserved.

[www.kirkland.com](http://www.kirkland.com)