Howden M&A

The unsung role of insurance in M&A

Infrastructure Assets

HOWDEN

Inaccurate assessments of financial information, flawed competitive analysis or business culture clashes … there are many ways M&A can go wrong, eroding the value of your investment.

Here's our short guide to avoiding your infrastructure deal getting headlines for the wrong reasons.

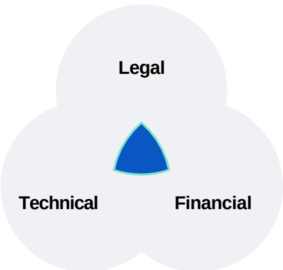
1

Think about insurance before due diligence scoping, not afterwards

You can tell a lot about how a target is run by looking at its insurance policies, their precise wordings and the ensuing policy activity. Of course, movements in historical premiums and claims activity can be revealing, and often bear further expert examination.

By conducting an insurance audit concurrently with other due diligence activities, you can get a rounded, independent view of the target asset.

Insurance policy usage touches on all the key aspects of due diligence can reveal a lot of important detail in legal, technical and financial due diligence.



> The insurance markets understand that fulsome due diligence cannot be undertaken on every individual asset within an infrastructure portfolio. Howden M&A can help you determine appropriate sample sizes before approaching insurers.

2

Well-scoped due diligence can help you manage higher risk scenarios that would otherwise be excluded

Infrastructure deals often face a number of scenarios that warranty & indemnity insurers typically exclude from coverage, leaving the buying entity to bear the risk alone.

The best way to avoid this scenario is to ensure that the due diligence scope includes financial, technical and/or legal assessments of the following areas:

- Feed-in tariffs
- Operation & maintenance contracts
- Health & safety
- Grants & subsidies
- Cyber & data protection
- Bribery, corruption and money laundering where the target business operates in a high-risk jurisdiction
- Contractor/employee reclassification.

Including these areas in the due diligence scope, along with any other areas that are of material importance to the target in question, will avoid the need to revise or re-scope due diligence exercises, thereby enabling the most fulsome coverage to be negotiated within the transaction timetable.

3

Understand environmental liabilities before they become expensive problems

Environmental liabilities can attach to any infrastructure acquisition. It is vitally important to understand the liabilities you face, and which of them are covered by the insurance that has been put in place by the construction company or target.

Broadly speaking, environmental risks consist of:

Construction risks arising from activities during the development phase including run-off of contaminated storm water, generation of dust, spillage of hazardous chemicals or exacerbation of contamination that previously laid dormant.

Historical soil and groundwater pollution, especially where the asset sits on former industrial or previously contaminated land.

Operational risks, which can cause pollution by discharging or releasing hazardous substances. This may be a current, live issue or a historical liability.

Protection is often a matter of the policy design and specific wordings, and should be reviewed in detail. Where gaps are identified, standalone environmental insurance can bridge the gap.

> Investors should give careful consideration to the extent of environmental protection in place via the target's insurances.

4

Avoid unpalatable indemnities in the transaction documentation

Where transactions involve large swathes of land and real estate acquired over time, legal due diligence may uncover issues such as:

- Boundary encroachments
- Planning breaches
- Lack of access rights
- Breaches of restrictive covenants
- Inability to verify the chain of title
- Third party rights
- Lack of planning and zoning permits.

When the above situations arise during the sale process, title and legal indemnity insurance can provide a solution to resolve the impasse promptly.

> Insurance can help you avoid delays or renegotiations, keeping the transaction moving.

5

Spotting future costs and assessing incoming liabilities

The target's programme of insurance should be examined closely to assess:

- Does it meet fully the requirements of key project contracts such as PPAs, O&Ms, EPC agreements or Project/Concession agreements?
- Are there any discrepancies between the EML study and the insurance purchased?
- Does the programme comply with local insurance regulations?

It is also important to assess factors that can increase future insurance costs.

These can include changing technologies, the availability of spare parts, shifts in the asset output over the project lifecycle, fluctuating rebuild costs, trends in the insurance market and inflation.

> Be aware of factors that can increase future insurance costs, as these can be significant.

6

Additional advice for complex or overseas transactions

Where the investor is acquiring an overseas entity, a complex group or a group that holds subsidiaries in overseas jurisdictions, the risk of a title to shares claim is often far greater.

As such, sellers often wish to cap their liability for fundamental warranties, particularly those speaking to the ownership of the shares.

When working in less familiar jurisdictions, or on deals with a complex history of share ownership, it can be comforting for both sides to have insurance in place for this risk that provides cover in excess of the typical warranty and indemnity policy limits (often 20-30% of the purchase price), right up to the full deal value.

> Multi-jurisdiction deals can be particularly challenging from a title to shares perspective, as claims to ownership can arise unexpectedly and derail the deal.

Speak to Howden

Howden M&A is a leading full-service M&A insurance broker with offices throughout Europe and APAC. We are supported by an Infrastructure Assets practice made up of leading professionals with decades of experience that have, together, acted for/on numerous infrastructure deals/projects.

We welcome your questions about M&A in the infrastructure sector.

Howden M&A has specialist teams dedicated to insurance due diligence, warranty and indemnity insurance, environmental liability, real estate and title risks, tax liability and contingent risks.

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