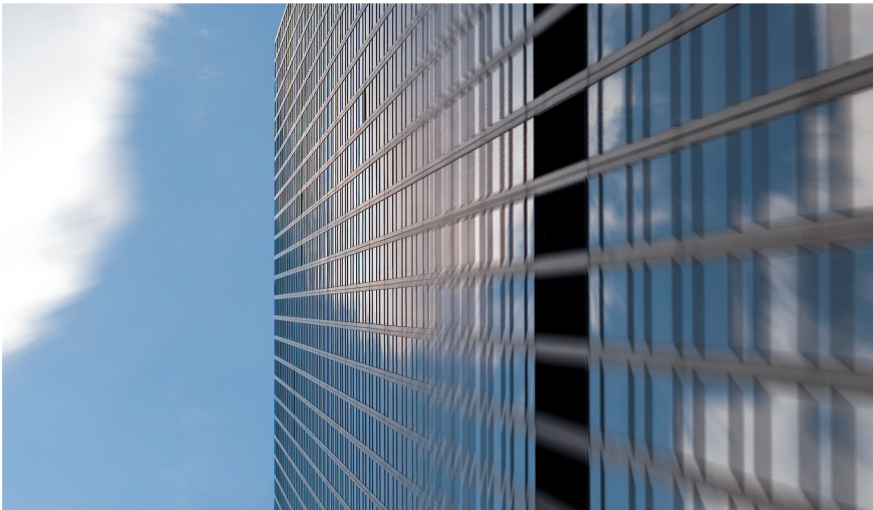


# PRIVATE EQUITY MANAGEMENT AND PROFESSIONAL LIABILITY

Willis has worked in partnership with selected underwriters to design an exclusive product which addresses the key management liabilities which arise from the operation of a private equity or venture capital fund, from the initial structuring of the fund to its last exit and subsequent final distribution.

The partnership approach has delivered a highly effective product designed to address the client's requirement on a platform that works for all parties. The combination of our knowledge, experience and pioneering mentality has resulted in a bespoke cutting-edge product for a unique industry.

Private Equity and Venture Capital (PE/VC) funds face a unique exposure in the area of management liability. These risks appeared to be minimised in an era of ever-increasing returns and outperforming funds. However, the changing economic landscape, combined with an increased focus on corporate governance, may serve to accelerate the rate of claims against funds (and the individuals therein) from a variety of sources, irrespective of the reputational nature of the industry.



The area of management liability within the structure of a fund is highly specialised. Standard Directors' & Officers' (D&O) policies have been shown to have gaps in coverage leaving individuals with unnecessary levels of exposure, especially when compared with the protection available in the market today.

Claims brought will still require a legal defence. The Private Equity Management & Professional Liability (PEL) policy will respond in respect of recovering legal expenses for both valid and invalid claims within the parameters of the policy. Willis believes that the sector is misunderstood by the insurance market and is therefore not fully represented during discussions with underwriters in delivering additional breadth of wordings.

## POTENTIAL EXPOSURES

- Claims by Limited Partners (LPs) alleging misleading offering documents or mismanagement of the fund.
- Poor due diligence.
- Corporate Governance issues in both the PE / VC companies and their portfolio companies.
- Insolvency of a portfolio company.
- Alleged negligence by the PE / VC companies to the management team of a portfolio company.
- Employment-related issues in the management of portfolio companies.
- Minority shareholders of portfolio companies, especially at exit stage.
- Indemnification provisions in portfolio companies.
- Exits from investments, especially Professional.

Professional Indemnity (PI) exposure associated with advice on investment banking issues:

- Internal crime / fraud.
- Administrative errors in distribution of proceeds including "in-kind" distribution.

## **BESPOKE COVERAGE**

Willis has been successful in negotiating broad insurance cover which goes beyond standard policy coverage typically available in the market:

- Blanket cover for all PE / VC representatives on portfolio company boards.
- No restriction in terms of industry sector.
- Coverage for claims brought by the portfolio company where acting wholly independently of the PE / VC company.
- No requirement for positive net worth of portfolio company.
- No requirement for portfolio company to purchase D&O.
- No “non-aggregation of limits” clause.
- No “Financial Institutions” exclusion.
- No recourse to Fund for indemnity.
- Automatic inclusion of new funds below a threshold of 150% of the value of last fund.
- No exclusion for claims brought by insured person(s) or the company against other insured person/s.

## **“BLENDED POLICIES”**

Willis predominantly recommends a “blended policy” to fulfil the needs of PE / VC funds.

Advantages of this approach:

- In a General Partnership structure the D&O and PI exposures are more difficult to separate. In the Willis policy insurers provide coverage across both these areas.
- Cost effectiveness through the purchasing of reduced overall capacity
- Separate policies tend to produce a disproportionate premium allocation to the PI policy.

## **CLAIMS SCENARIO (I)**

A Private Equity fund planned their exit strategy via the Initial Public Offering (IPO) route. At that time, the fund owned a large proportion of the issued share capital with a number of smaller investors owning the remaining shares. During the IPO, an action was brought against the fund by a minor shareholder. The minor shareholder claimed that the IPO structure was designed specifically to maximise value for the fund and left the smaller investors disadvantaged.

## **CLAIMS SCENARIO (II)**

The Private Equity fund breached the investment parameters defined within the Private Placement Memorandum (PPM) after an investment within a certain geographical region. Subsequently, the target company underperformed significantly leaving the investors looking for recourse. When it was discovered that the fund were in breach of the PPM, LP's wasted no time in bringing an action against the private equity fund.

Other claims in this sector include:

- Non-completion of deals.
- Vendor disputes.
- Lack of additional funding.
- Claims surrounding management change.
- Refinancing creating conflicts of interest.
- Portfolio company purchaser claim.
- Creditor claims for insolvent exits.

For more information contact your local Willis Associate, or call the London M&A Practice on: +44 (0)20 3124 6000.