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PROSPECTUS LIABILITY INSURANCE

When a company seeks to raise capital through the offer of securities to the public, or seeks an admission to trade securities, a prospectus or listing particulars will be issued, detailing in-depth financial information about the company and its future objectives and strategies.

If capital is being raised in the UK, the issuing directors must be satisfied they have complied with the requirements laid down by the Financial Services Markets Act (2000), the listing rules and the London Stock Exchange's admission and disclosure standards.

The capital raising may be through simultaneous offerings on one or more stock exchanges, in which case care must be taken to comply with the relevant laws and regulations of the territory in which each of the stock exchanges is domiciled. In all jurisdictions signatories to the prospectus have a personal responsibility for the accuracy of the contents.

Liabilities may be incurred if the prospectus contains errors or omissions which are relied upon by investors in making their decision to purchase the company's securities. These liabilities, which potentially represent the greatest risk exposure that the directors (and the company) may incur in the corporate life of the company, can be insured through the purchase of a Prospectus Liability policy [variously known as Initial Public Offering insurance (IPO) or Public Offering of Securities Insurance (POSI)].

Prospectus Liability Insurance is transaction-specific and addresses the following risks:

- Shareholder actions alleging misstatements in the prospectus upon which investment decisions were made.
- Shareholder actions alleging failure to disclose material information in the prospectus.
- Legal expenses in respect of regulatory investigations.
- Shareholder derivative actions.
- Crisis management expenses.
- Long-term contractual liabilities arising from the offer or listing.
- Claims for misrepresentation in the lead up to the offering (roadshow activity).
- Breach of warranty in the placing agreement / underwriting agreement.
- Secondary offerings made on similar terms to an initial public offering.

WHO IS COVERED BY PROSPECTUS LIABILITY INSURANCE?

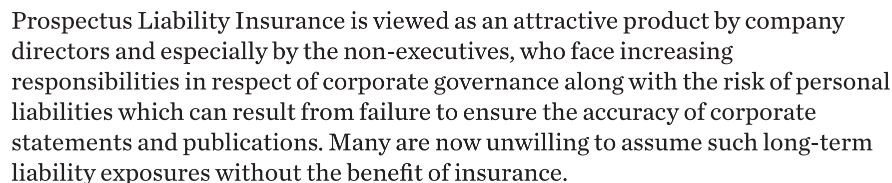
The company, its directors (including non-executive directors) and officers and employees for a securities claim.

Additional interested parties to the prospectus may also be covered:

- The issuing underwriter.
- Selling shareholders.
- Controlling shareholders.
- Advisors to the transaction.

USE OF PROSPECTUS LIABILITY INSURANCE

Cover has been available for some time in the insurance market, and has been substantially utilised by companies undertaking initial and secondary offerings of shares, rights issues, bond offerings or private placements. Cover will also be of interest to companies involved in other forms of transactions where a prospectus may be issued, such as a debt-for-equity swap.



Prospectus Liability Insurance is viewed as an attractive product by company directors and especially by the non-executives, who face increasing responsibilities in respect of corporate governance along with the risk of personal liabilities which can result from failure to ensure the accuracy of corporate statements and publications. Many are now unwilling to assume such long-term liability exposures without the benefit of insurance.

ADVANTAGES OF PROSPECTUS LIABILITY OVER DIRECTORS' & OFFICERS' LIABILITY INSURANCE

- A Prospectus Liability policy ensures that a ring-fenced limit of cover is in place for specific prospectus exposures (which can be higher than annual Directors' & Officers' Liability policy limits).
- Policy covers the strict liability exposures relating to the prospectus.
- The one-off premium can be attributed as a transaction cost of the listing.
- Cover is provided for claims arising from issue of the prospectus and the policy period covers the statute of liability for those claims (six years in the UK, three years in the US).
- Directors' & Officers' Liability cover does not provide cover for prospectus liabilities as standard.
- The purchaser does not face a renewal risk of insurance premiums shifting upwards or market capacity not being available in future years.
- The insured does not have to buy extended levels of Directors' & Officers' Liability cover in relation to prospectus risks.
- Any claims made against the Prospectus Liability policy will not erode aggregate cover limits purchased under the company's Directors' & Officers' Liability cover.
- The Prospectus Liability policy remains in place in the event the company is taken over or merges with another.
- The policy may help attract directors who are joining the board for the offering.

WHAT LIMITS ARE PURCHASED?

Limits purchased will vary depending on the risk appetite of individual companies, the circumstances and size of each individual offering and in which jurisdictions the offering takes place. There is enough insurance market capacity to provide substantial limits for policies covering the full period of the statute of limitations.

COST OF INSURANCE

The premium is usually calculated as a percentage of the overall limit of cover. Key factors which will affect pricing are whether the share listing is being undertaken on a main or specialist exchange and whether it is multijurisdictional, the number of interested parties being covered and the amount being raised.

There are a number of carriers offering bespoke policies in a competitive insurance marketplace which helps keep premiums at an attractive level for the buyer.

INFORMATION REQUIRED TO OBTAIN A QUOTATION

In order to underwrite prospectus exposures insurers will require the following:

- Copy prospectus / listing particulars.
- Percentage of securities to be offered pursuant to US laws and regulations.
- Value of securities being offered.
- Copy of placing / underwriting agreement.
- Proposal form.

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

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