The Debrief

Highlights from the Debevoise Emerging Markets Legal Symposium

December 13, 2018

On 19 November 2018, Debevoise hosted its inaugural Emerging Markets Legal Symposium in London. Lawyers and key industry stakeholders discussed topical issues arising from recent trends in global M&A transactions, with particular focus on current trends in emerging markets transactions and the consequences for deal structuring and negotiations. Panel topics included the use of non-traditional deal structures, the continuing rise in the use of warranty & indemnity insurance in M&A transactions, the growth of impact investing by private equity funds, trends in key terms of shareholder agreements, risk allocation developments in purchase agreements, latest trends in pricing mechanisms in M&A transactions, and current tax structuring developments and challenges.

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Key takeaways from the day's events are highlighted below.

- **Impact Investing**. Mainstream investors are becoming increasingly active in impact investing as the industry grows and investors gain confidence in impact management and measurement. In addition, recent regulatory developments in the United States and Europe have eased concerns that impact investments could violate the fiduciary duty to maximize profits. Indeed, the Global Impact Investing Network noted in its most recent annual survey that more than $58 billion was committed to impact investments deals in 2017, a 58% increase from the previous year. As more investments are being made, the due diligence process is evolving beyond typical risk management assessments, and transaction documentation now often includes clauses driven by investors' specific reporting criteria, such as impact undertakings and reporting covenants.

- **Pricing Mechanisms**. While in the United States, completion accounts remain the standard mechanism for determining price in M&A deals, emerging markets lean toward locked-box structures. (In the UK, both approaches are found.) Increasingly, sellers in locked box transactions are seeking some compensation for the delay in receiving the purchase price given the shift in economic risk before the contract is signed, even though the seller receives the purchase price only after completion. This is typically reflected in the sales and purchase agreement as a specified percentage of

the purchase price (i.e. interest) or a daily profit charge, in either case accruing from the locked box date through completion.

- **Warranty & Indemnity Insurance**. The buyer's recourse for losses resulting from breaches of warranties by the seller or for specific indemnities in the acquisition agreement and the allocation of such risks between the buyer and the seller has traditionally been a matter of intense—and sometimes heated—negotiation. Sources of recovery have included escrows or guarantees by sellers, which lead to further negotiations around credit-worthiness, quantum, duration and other terms, and such options are not always attractive or available—especially to private equity sellers. In European and U.S. transactions, there has been marked increase by both buyers and sellers of Warranty & Indemnity (W&I) insurance as an alternative recovery source. W&I insurance permits sellers to distribute more proceeds faster, while reducing the pressure in negotiations around the warranties and the buyer's recourse for breaches and ensuring a creditworthy source of recovery for buyer's claims. Whilst the W&I insurance policy terms (e.g., pricing, retention and exclusions) still vary by market, the proliferation in the use of W&I insurance in Europe and the U.S. has led to the development of relatively standardized terms and exclusions. In emerging market transactions, W&I policies are currently used relatively infrequently. But given the growing acceptance of these policies in developed market transactions and the increasing sophistication and effort of insurance carriers in promoting these products, it is likely simply a matter of time before W&I insurance begins making an impact in emerging markets as well.

- **Developments and Challenges in Tax Structuring**. Private equity funds and other investment platforms are constantly looking for tax efficient structures to ensure that their investors are not worse off than they would have been investing directly and to mitigate potential double taxation as much as possible. However, in structuring funds and investment platforms, careful consideration should be given to the ever-evolving tax landscape, with a particular focus on the changes that may result from the implementation by participating countries of the action points of the "base erosion and profits shifting (BEPS)" project developed by the OECD.

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