Specific Tax Risk Insurance Policy

A Specific Tax Risk Insurance Policy is a bespoke insurance solution designed to provide financial cover in the event of an identified tax risk crystallising into an actual liability by transferring the identified tax risk to the insurance market.
**Snapshot**

Specific Tax Risk Insurance Policies have become a popular and cost-effective tool for funds, corporates and individuals to manage tax risks. The product can be placed in a transactional context by the buyer, the seller or the target, but it can also be placed on a standalone basis, such as insuring tax risks concerning forward looking cash repatriation and internal restructuring issues.

In particular, the product can be a valuable tool during mergers and acquisitions when the parties have identified a tax risk but neither party is willing or able to retain the risk. It can be used as a defensive strategy, replacing the need for a seller escrow, contractual indemnities or preventing price chips arising from due diligence.

Howden M&A has a dedicated tax team which can help clients to structure, market and negotiate Specific Tax Risk Insurance Policies, drawing on over 50 years of specialist tax experience across the team.

**Policy parameters**

**Policy limit** – The policy will provide cover for:
- The estimated tax exposure of the identified tax risk(s)
- Interest and penalties
- Defence costs
- Incremental costs should the proceeds under the Specific Tax Risk Insurance Policy be themselves taxable (‘Gross Up’).

**Premium** – This is calculated as a percentage of the policy limit (known as ‘Rate on Line’). The Rate on Line applied is typically around 1.5%-2.5% in the UK and 2%-5% in Europe, depending on a number of factors (see ‘Insurable risks’ below).

*For example, a £10m Policy Limit within a 2% Rate on Line will cost £200k.*

**Retention/Excess/Deductible** – The insurer might require an element of the loss to be borne by the insured party, usually where there is a higher risk of detection by the tax authorities. However, this is usually limited to defence costs only.

**Policy period** – A Specific Tax Risk Insurance Policy will be designed to cover the applicable statute of limitations in the jurisdiction of the insured, usually 7 years. It can sometimes be extended to 10 years.

**Underwriting fees** – Before an insurer begins underwriting the risk, the client must enter into an expense agreement to cover the underwriting fee. The quantum of the underwriting fee depends on the value, complexity and jurisdiction of the identified tax risk.

The underwriting fee might be payable in addition to the premium or, in certain instances, waived upon the policy binding.

**Insurance Premium Tax** – Certain jurisdictions will charge insurance premium tax (‘IPT’) on the payment of a premium. This is an additional cost to the premium of the policy. The rate of IPT is dependent on the jurisdiction of the insured.

**External advice** – Insurers will expect to see advice from an external advisor of the client which analyses the technical merits of the tax risk. This is always provided to the insurers on a non-reliance basis.

Specific Tax Risk Policies are complimentary to external advice and cannot be used as a substitute.

**Insurable risks**

Whether a tax risk is insurable and the Rate on Line will depend on a variety of factors, including:

- The jurisdiction of the tax authority and the insured
- The probability of risk discovery
- The competitive tension between insurers
- The availability and quality of advice including the technical analysis and defence arguments
Howden M&A's Services

Illustrative Process and Timeline

Specific Tax Risk Insurance Policies can be placed with an A-rated insurer within the time frame you require. Although this is typically around 10 days.

Please see below for an indicative process and how Howden M&A can assist the client through the process.

| Day X                | • Initial discussions with Howden M&A’s tax specialists to discuss the risks. This includes reviewing tax due diligence reports, external analysis and information
|                     | • Howden makes recommendations to the client regarding insurability
| Day X+1             | • Howden submits the tax risks to the insurance market for non-binding indications (‘NBI’) of terms
| Day X+3             | • Howden receives NBI terms from the insurers and produces a report for the client summarising the NBI offers, our recommendations and other specific remarks

Costs will only be incurred at this stage onwards

| Day Y                | • The client selects an insurer and enters into an expense agreement
| Day Y+2              | • Insurer begins both underwriting and drafting of the insurance policy simultaneously
|                     | • Client provides further information requested by the insurer. This is just to verify the assumptions in the NBI terms
|                     | • Howden assists the client to negotiate the policy wording and the coverage position with the insurer
| Day Y+5              | • The final policy is issued and incepted

| Policy Period        | • During the policy period, if the client notifies the insurer for a claim under the policy, our in-house claims specialist and the tax team can assist the client with the claims process

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