



Warranty and Indemnity Insurances in Korea

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I. W&I Insurance Trend in Korea

A warranty and indemnity (“W&I”) insurance policy covers a seller’s liability arising from a breach of representations and warranties in an underlying sales and purchase agreement (“SPA”) in M&A transactions. Since its introduction in the U.S. market in the late 1990s, W&I insurances have had a rapid growth in Korea after first being used in M&A auctions and PE transactions from 2016, and are now widely undertaken in large-scale transactions as they provide buyers with a straightforward claim process of the insurer without any concern of the sellers’ solvency while allowing sellers to have a ‘clean exit’.

Following such increase in the W&I insurance transaction volume, there has also been an upward trend in the volume of W&I insurance claims made by the buyers and related disputes in Korea, which has necessitated legal considerations for the role of W&I insurance in any given M&A transaction at its early stage. In this Shin & Kim newsletter, we have endeavored to outline the main features of and key considerations for procuring a W&I insurance.¹

II. Main Features

The overarching features of a W&I insurance are (i) it covers unknown risks, and (ii) sellers’ ‘clean exit’ is secured without the buyer’s or the insurer’s right of indemnity against the seller except in highly special circumstances such as the seller’s fraud.

The W&I insurance does not ordinarily cover any risks known to the buyer (which is commonly referred to as “known risks”), and the coverage is limited to losses or damages arising from a breach of the representations and warranties by a seller due to any circumstances not discovered by due diligence undertaken by the buyer. As such, any risks identified through a due diligence exercise should be appropriately addressed by the buyer by (i) reflecting the identified issues into valuation of the target, or (ii) including special indemnity provisions and/or conditions precedent to closing in the SPA to resolve or mitigate such risks.

If the buyer decides to take out a W&I insurance, the SPA will contain a provision stating that the seller shall not be liable

for any losses or damages arising from its breach of the representations and warranties, except in case of the seller's fraud. As the W&I insurance offers a 'clean exit' to the seller (the insurer has no recourse to the seller except in case of the seller's fraud), the transacting parties are able to swiftly negotiate and finalize representations and warranties to be given in an SPA, enhancing the parties' ability to secure and close the M&A transaction (as any issues associated with the compensation for damages due to a breach of the representations and warranties by the seller will be resolved between the insurer and the buyer).

III. W&I Insurance Coverage

1. Limit of Liability

Any limit on liability under the W&I insurance policy will be determined by the insurer and the buyer taking into consideration: (i) the size of the transaction, (ii) the likelihood of any breach of the relevant representations and warranties, (iii) any characteristics of the industry to which the target belongs, and (iv) the insurance premium amount. From our experience, the liability limit for W&I insurance policies for Korean transactions ranges between 10% and 20% of the transaction price, which may be higher for smaller transactions.

One thing worth highlighting to buyers (who are also insureds under W&I insurance policies) is that the limit on the insurer's liability under the W&I insurance is separate from the limit on seller's liability under the relevant SPA, meaning any liability cap, basket, threshold or de minimis that apply to the seller's liability under the SPA will not apply under the W&I insurance policies which will have their own liability limit thresholds.

2. Premium

The insurance premium amounts for Korean deals range between 1.5% to 3% of the policy limits, depending on various factors taken into account by the insurer such as the size of the transaction and the characteristics of the industry to which the target belongs.

The insurance premium should in principle be borne by the buyer who is the policyholder, but the parties to the SPA can negotiate to share such costs.

3. Survival Period

A survival period during which an insured party can make a claim under a W&I insurance policy is typically three years for general representations and warranties and seven years for fundamental and/or tax-related representations and warranties.

Similar to the limit on liability, the survival period under the W&I insurance is different from the survival period provided under the SPA in most cases, and regardless of the survival periods provided under the SPA, the buyer will be entitled to make insurance claims during the survival period set out under the W&I insurance policy.

4. Exclusions

The W&I insurances do not cover any known risks (any risks known to the buyer), environmental (pollution) liabilities, product liabilities, underfunded pensions, assessments or predictions of future events, transfer pricing between related parties, or denial of unfair act and calculation in connection with tax liabilities, among others.

Further, depending on the negotiations with the insurer of the W&I insurance, it is possible that certain deal specific exclusions are included in the W&I insurance cover.

IV. Subscription Process

The process of procuring W&I insurance involves (i) seeking an insurer through an insurance broker, (ii) receiving a non-binding indication (“**NBI**”, a preliminary quotation for pricing and coverage) from the selected insurer through the insurance broker, (iii) completing an underwriting process, (iv) obtaining the insurance policy (i.e., placement of the W&I insurance policy) and (v) paying the insurance premium.

As insurance brokers play a crucial role in procuring insurers and their NBIs, it is important to seek assistance from a competent insurance broker who is able to find an insurer that offers competitive products to satisfy the buyer’s needs. Shin & Kim maintains a very close relationship and extensive experience in working with various local and foreign insurance brokers. We can help our clients select an insurer who is most suitable for the specific nature of the transaction.

V. W&I Insurance Claims

As noted above, we have seen an increase in the number of W&I insurance claims as the volume of W&I insurance policy issuances has surged in recent years.

According to the market study published by the insurance companies and insurance brokers, (i) approximately 20% of the W&I insured transactions result in insurance claims, and (ii) between 60% to 70% of those claims relate to the seller’s breach of the representations and warranties relating to financial statements, taxes, legal compliances and material contracts. Given the foregoing, it is of paramount importance to appoint the right legal counsel from an early stage of the transaction who has ample experience in W&I insurance and able to prepare for and navigate a W&I insurance claim.

VI. Key Considerations

The scope of negotiations of representations and warranties between the parties to an M&A transaction are notably

different depending on whether or not a W&I insurance will be obtained by the buyer. The buyer in particular should be aware that it must not only negotiate separately with the insurer on coverage exclusion, but also carry out a tailored due diligence exercises having regard to the terms of the applicable W&I insurance policy. Given the importance of W&I insurance in M&A transactions, retaining a competent legal counsel who is familiar with both the underwriting process and terms and conditions of a W&I insurance policy early on in the transaction will help to ensure that the transaction is successful.

Shin & Kim's W&I insurance team's caliber as a W&I insurance advisor is unparalleled due to the sheer volume of W&I insurance policy transactions it has advised on as well as the number of W&I insurers and buyers it has represented since the introduction of W&I insurances in the Korean M&A market. We are recognized as the undisputed leading W&I insurance advisor in Korea. From selection of the insurance broker, W&I insurance underwriting, negotiation and execution of insurance policy and filing any W&I insurance claim, Shin and Kim provides a one-stop shop service in guiding the clients through all of the W&I process and remain at the forefront of key market trends in the industry.

¹ [Also refer to "Main Features and Issues of W&I Insurance in M&A Transactions" \(in Korean\) by Chae-won Kang, BFL No. 105 \(January 2021\), Seoul National University Financial Law Center.](#)

[\[Korean version\]](#) M&A 거래에서 W&I 보험(진술 및 보장 보험)의 활용 방안

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