Specific Contingency Insurance

Case studies

Potential impact of a change in law on capital investment

A US company has prepared to enter into a longterm contract with a foreign entity. Fulfillment of this contract will require that the US company make a significant capital investment in plant and equipment. The contract contains a provision that allows the foreign entity to cancel the contract in the event of certain changes in the law. The US company is unwilling to execute the contract unless it can gain protection against a loss of its capital investment resulting from cancellation of the contract due to a change in the law. The US company may obtain a Specific Contingency Insurance policy to respond to losses incurred in the event there is a change in the applicable law.

Potential impact of a change in law on future income of a target business

Given the political environment, the potential purchaser of a package of certain loans is concerned about the impact on the future income stream emanating from the purchased assets in the event that there is a change in law that eliminates the ability to charge certain recurring fees on the loans. The potential purchaser is unwilling to proceed without some form of an indemnity for this loss of income. The seller is not prepared to offer any form of indemnity. A Specific Contingency Insurance policy may be procured by the purchaser to respond to any losses incurred in the event of the applicable change in law.

Potential challenge to a position taken regarding amounts due under a contract

An investor is in the process of considering a significant strategic investment in a financially distressed company. The company recently terminated a material contract and has taken the position that there are no further amounts due under the terms of the contract. While the counterparty to the contract has not made a demand for payment, the investor is concerned that the publicity surrounding the cash infusion may lead such counterparty to file a claim for contractual damages. As a condition to receiving the investment, the company may obtain a Specific Contingency Insurance policy to respond to any claims for contractual damages by the counterparty to the recently terminated contract.

Potential mismatch between two indemnities

A licensee uses intellectual property licensed from a licensor in a product that it sells to a customer. The customer requires an indemnity from the licensee for

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any patent infringement claims that are made against it by any third parties as a result of its use of the licensor's embedded intellectual property. Given the existence of the indemnity in its favor from the licensor (which has significant financial resources), the licensee willingly provided the requested indemnity. During due diligence in connection with a loan required by the licensee, lawyers for potential lenders determine that certain parts of the indemnity given to the customer are broader than the indemnity given to the licensee by the licensor. Given the limited financial resources of the licensee, the lender is not prepared to take the risk that the licensee may not be able to recover all amounts paid under the indemnity it has given in favor of the customer from the licensor. As a condition to closing on the loan, the licensee purchases a Specific Contingency Insurance policy to respond to any losses incurred as a result of a claim from the customer that is not in turn recovered from the licensor. The lender is added to the policy as a loss payee.

Potential liability preventing fund liquidation

One of a private equity fund's portfolio investments became insolvent 18 months after being acquired by the fund. In contentious bankruptcy proceedings, the private equity fund and its general partner were named in protracted litigation as the controlling persons of the portfolio company. The litigation was settled and releases were exchanged between most parties. However, there were parties to the litigation that could not be found and did not sign releases. The fund's general partner is unwilling to permit liquidation of the fund because of concerns about claims being made against the fund by the nonreleasing parties with respect to the matters for which all other parties have provided a release. A Specific Contingency Insurance policy may be obtained by the general partner to respond to claims brought by the non-releasing parties relating to the litigation, allowing the fund to liquidate.

Potential challenge to compliance with zoning laws

Lawyers conducting due diligence for the buyer of a group of buildings have highlighted the fact that several key tenants of the buildings conduct businesses that may fall outside of the type of activity for which the buildings are zoned. As several of these tenants are paying above-market rents, the buyer is concerned about the impact of a reduction in rent stream if one or more of the tenants are no longer able to conduct their businesses in the buildings because of a challenge by the relevant authorities. The owner of the buildings may obtain a Specific Contingency Insurance policy, which is assignable to the buyer at closing, to respond to any losses incurred as a result of any challenge by the relevant authorities.

Potential claims made by dissenting shareholders

An overleveraged company is in the process of restructuring its debt in a manner that will result in substantial dilution of equity to the existing shareholders. For various reasons, the restructuring is being concluded without the approval of the relevant bankruptcy court. The shareholders/debtholders of the company that have agreed to the terms of the restructuring require an indemnity in the event that they are sued by shareholders/debtholders who did not vote in favor of the restructuring. The restructuring entity is unable to provide such an indemnity. A Specific Contingency Insurance policy may be obtained to respond to any claims by any dissenting or abstaining shareholders/debtholders against any shareholder/debtholder that voted in favor of the restructuring.

Threatened action

A competitor of a manufacturer issued correspondence alleging that the company's main product infringed on that competitors intellectual property. In several rounds of correspondence between advisers for the company and the competitor, the company robustly rejected any allegations of infringement. The competitor has not been heard from since the company sent out its most detailed response over three years ago. The company is now attempting to raise private funding and the proposed funder has concerns that the competitor will revive its allegations in the form of a lawsuit. A Specific Contingency Insurance policy may be issued to respond to losses incurred by the company as a result of any infringement action brought by the competitor.

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