Tax indemnity insurance.

M&A... Navigating the tax issues

Tax indemnity insurance is a specialist product designed to indemnify the insured for any additional tax that becomes due following a business sale or restructure.

At present, this insurance is most relevant in mergers and acquisitions where the parties are unable to satisfactorily allocate the tax risks between themselves.

This can result in deadlock so a key selling point of the product is its ability to facilitate the completion of transactions that might otherwise flounder.

Case studies

Inadvertent failure to make election

During the due diligence process for a pending acquisition, it was discovered that the target company inadvertently did not make a required tax election. The regulations of the relevant taxing authority provided that relief for such an inadvertent error might be sought; however, the timeframe for receiving the relief would have prejudiced the deal timetable.

If the election was denied, the target company could suffer significant addition tax liabilities. Tax advisors to both the proposed target and buyer agreed that given the facts, the risk of relief being denied was low but not nil. The buyer was neither willing to assume the risk nor willing to agree to delay the transaction until the relief was received. A seven year tax indemnity policy was put in place to provide cover in the event additional tax liabilities did become due.

Degrouping relief

As part of a restructuring process and focus on core operations, it was decided to split the operations of a company into two separate entities. Steps were taken so that the demerger would be tax-neutral. However, the directors and financing banks were concerned that an unexpected challenge to the tax planning could potentially result in a significant tax exposure.

This exposure impinged on the ability of the group to realise the benefits of a restructuring strategy, including the sale of one of the demerged entities and as such, tax insurance was sought and a tax indemnity policy was put in place. By doing this, the risk of a challenge to the applicability of de grouping relief under TCGA1972, s179 was transferred to an insurer.

Discounted loan notes

As part of an agreement for the sale of a company,a buyer also agreed to purchase loan notes issued by the target company to the seller. The loan notes were acquired at a discount and it was considered that there might be a tax charge as a result of an actual or deemed release once the buyer and target became connected.

The buyer identified that there was a risk of a tax charge arising: under the deemed release provision in FA 1996, Sch 9, para 4A; and /or on the actual release of the dept, despite the fact that the parties were connected for the purposes of the loan relationship rules.

A tax indemnity insurance policy was obtained by the buyer of the discounted loan notes, insuring it against each of these specific risks.

MARKEL®

Tax Indemnity Insurance
A step by step guide to mitigating uncertainty in taxation transactions

Assessing your client's eligibility for tax indemnity insurance in order to mitigate their risk of additional tax that could become payable in the event of an adverse ruling or settlement of any dispute with the tax authorities and, where applicable, the cost of defending any litigation that may be involved.

Contact Markel Tax
An initial assessment call with our experienced tax and insurance experts can very quickly determine whether tax indemnity insurance is feasible.

Submission
In order to evaluate the risk, we will need:
- An overview of the tax issue with details of the proposed transaction or restructuring scheme
- Copies of any correspondence with the tax authorities about the issue
- Copies of any relevant legal or accounting opinions
- A copy, if applicable, of the vendor's indemnity in a purchase and sale agreement

Initial indication
We will provide indicative terms, including the premium cost, the level of any excess and, if appropriate, the insurer's due diligence costs.

Placement with specialist insurers
Where terms are accepted, instructions will be given to complete placement. This involves the provision of bespoke terms and policy wording. Premiums become payable when cover begins and the finalised documentation is released.

Premiums
Premiums for tax indemnity insurance are determined case by case because every transaction raises unique issues.
Factors in setting premiums include:
- The nature of the transaction causing the tax issue
- The taxpayer's particular circumstances, representations made and insurance limit required
- Relative strength and legal basis of the tax position taken
- The structure of the insurance programme

You can rest assured that the insurance policy your client is purchasing is backed by an A rated insurer.

If you have a client facing a tax risk who might be able to benefit from the peace of mind that this tax indemnity insurance would offer, please contact us on 0345 223 2727 and we will be happy to assist you.

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