Marsh

Transactional Risk Global Tax Bulletin 2024

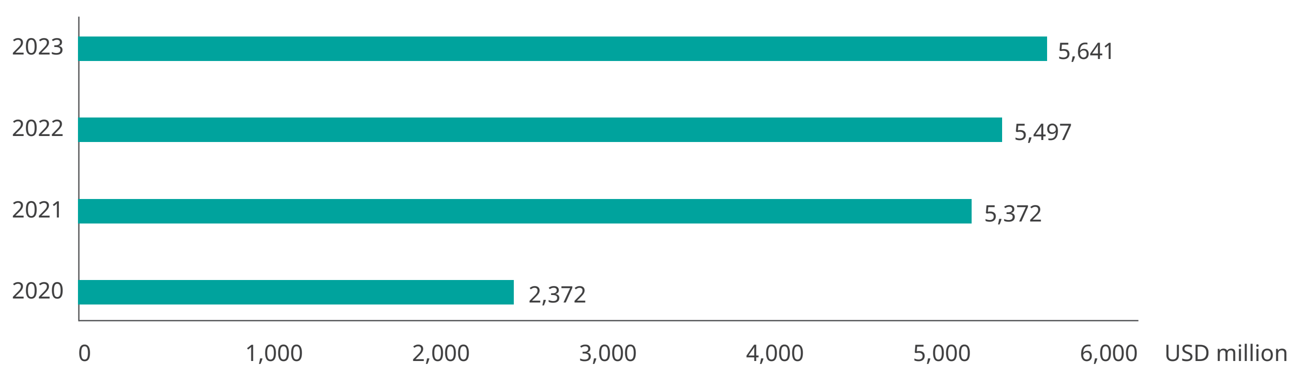
Introduction

Welcome to the *Transactional Risk Global Tax Bulletin 2024*. This report provides a global overview of the current state of the tax insurance market, which is experiencing significant growth and is comparatively mature in the Western Hemisphere. This report explores key trends and developments, and growth opportunities in tax insurance across regions including the US, Canada, Latin America, the UK, Europe, and Asia Pacific (APAC).

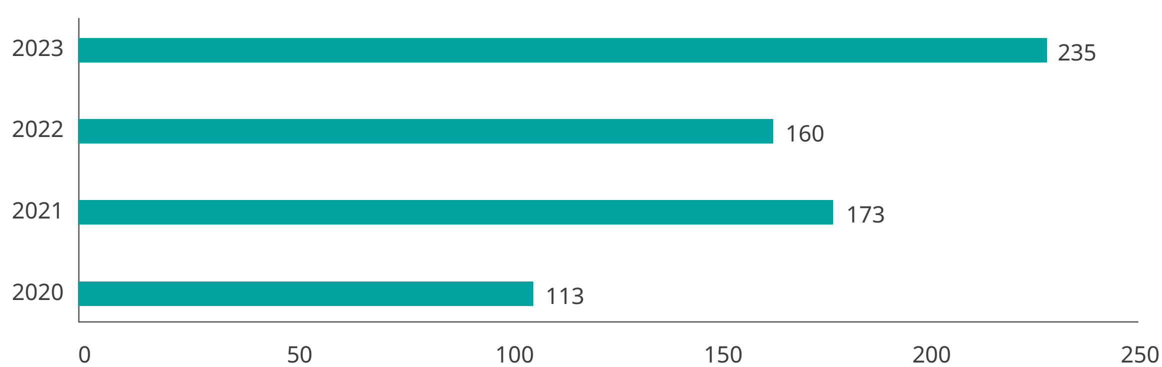
The report examines the increasing use of tax insurance in various industry sectors and explains the factors behind declining premium rates. It provides valuable insights into the global tax insurance market, enabling businesses, lawyers, tax advisors, and insurers to better understand and make informed decisions regarding tax risk mitigation.

Marsh Global Tax Overview

Global Amount of Tax Risks/Limits (in USD million)



Global Number of Bound Tax Policies



United States, Canada, and Latin America

The tax insurance market in the Americas is growing rapidly, is a comparatively mature market, and has been seeing claims activity. The US market can be divided into three sectors:

- **M&A based**: Representations and warranties insurance (called warranties and indemnities insurance in Europe and Asia) includes coverage for unknown tax risks and breaches of tax representations in purchase agreements. However, tax insurance can step in and mitigate "known" or identified tax risks where insurers have an appetite for that category of risks, such as pass-through status and possible inadvertent terminations of S corporation status, pre-acquisition restructurings, availability of tax attributes like net operating losses and tax credits, debt equity characterizations, worthless stock deductions, successor liability, tax treaty withholding tax issues, tax-free spinoffs, and other common tax issues. While M&A activity has decreased since its peak in 2020-2021, there has been an increase in activity in the second part of 2024, leading to a year-over-year increase in tax insurance placements arising from M&A activity.
- **Renewable energy industry**: The development of the US renewable energy market is fuelled by a variety of transferrable "green energy" US federal tax credits, with the Section 48 investment tax credit and the Section 45 production tax credit being the most prevalent. As a result of legislation passed in 2022 (see below), these credits can be sold to unrelated US taxpayers, usually at a discount, and potentially used to offset the purchaser's US federal income tax liability. There is also strong interest in obtaining tax insurance for carbon sequestration tax credits and advanced manufacturing credits (Sections 45Q and 45X, respectively). Because many sponsors/developers of projects provide indemnities to investors in these credits — commonly called tax equity investors — tax insurance has traditionally been used to mitigate the risks associated with these indemnities by providing a backstop if there is a successful IRS challenge to the credits. Historically, these credits were monetized by US taxpayers only through complex partnership and leasing structures. Today, however, these credits can be transferred to unrelated taxpayers through the Section 6418 transfer rules, which were enacted as part of the Inflation Reduction Act, which became law in August of 2022. These tax insurance policies may be viewed as providing a credit enhancement to sellers of tax credits that have indemnities to buyers where developers/sponsors are not well capitalized. Marsh can place buy-side policies or buyer/seller policies regarding the credit's anticipated tax benefit, which policies are both designed to respond in the event of a successful IRS challenge.
- **Strategic tax placements:** There has been strong growth in the number of tax insurance policies purchased by multinational corporations, family offices, private equity firms, and the investment management sector. These tax insurance policies aim to mitigate significant, complex tax risks on the insured's balance sheet in areas of the tax law where the tax position is viewed as sound, but not free from doubt. Complex business entities use these policies to better enable financial decisions when there is a possibility of large tax contingencies if the IRS were to challenge the tax position being insured. With the onset of complex international tax rules like Pillar 2, this part of the tax insurance business is likely to experience strong growth in the next decade.

Since the start of 2020, Marsh USA has bound more than US$11 billion in tax insurance limits, with between 50% and 80% of those policies each year unrelated to M&A activity. Additionally, Marsh USA led the transactional risk marketplace in the number of tax insurance submissions to the underwriting market for the past two years, including breaking the all-time record for the number of tax insurance submissions to the marketplace in 2023. In 2024, as of this writing, Marsh USA is on pace to exceed its 2023 submission level.

In terms of insurance limits, Marsh has placed policies with limits as large as $US1 billion and as small as a few million dollars. Drawing on the growth of the Marsh McLennan Agency network, we serve both the middle market and Fortune 500 clients.

For US tax risks, premium rates-on-line (ROLs), typically range, as a percentage of the limit insured, from below 2% to as high as 5%, depending on underwriters' perception of the tax risk being insured. If the IRS or a state/local tax authority is challenging the position, or if the position is in litigation, ROLs can be considerably higher. The cost for a policy is a one-time payment for the duration of the policy, typically between 7 and 10 years.

We also frequently place coverage for Canadian tax risks. Despite the fact that a number of tax risks that are insured are subject to certain reportable transaction rules (being reportable to the Canada Revenue Agency), the insurance market for tax risks in Canada remains robust. We expect the number of insured tax risks to increase, as Canada recently implemented a renewable energy tax credit regime similar to the US renewable energy tax credit regime. It is likely that Canadian taxpayers will use tax insurance policies to support the monetization of these credits similar to the US market; indeed, we have already started to observe tax credit activity in the Canadian tax insurance underwriting market.

We anticipate moderate growth in the number of tax insurance policies addressing tax issues arising in Latin American jurisdictions including Mexico, Chile, Argentina, Colombia, and Brazil. Given the higher baseline ROLs for policies addressing tax risks in these jurisdictions, we recommend that taxpayers with tax risks in these jurisdictions seek insurance for such risks before the tax authorities begin audits or otherwise challenge the intended tax treatment, as an existing audit or investigation may prevent the insurability of the risk in these jurisdictions.

United Kingdom

The London tax insurance market is a unique global market. Since 2020, placement of tax insurance into the London insurance market has increased significantly, driven in large part by the expansion of insurer appetite for a wider range of risks and jurisdictions. There has also been a significant drop in rates, arising from increased insurer competition as multiple carriers entered this product line.

Historically, tax insurance was largely used in the context of M&A transactions; for example, insuring historical tax risks pertaining to a target company. Today, however, it is frequently used in non-M&A situations, such as internal restructurings, refinancings, wind-ups, availability of tax assets, and balance sheet items to provide greater financial confidence in the relevant situation.

For example, the expansion of insurer appetite can be seen in the coverage of "change of tax law" risks. It is quite common practice for insurers to exclude any future "change of law" from tax insurance policies; however, in today's environment of innovation, some insurers have re-assessed how they can provide certainty of treatment of future tax liabilities resulting from a "change of tax law". We have also seen significantly expanded jurisdictional appetite, with insurers proactively seeking opportunities across regions such as Latin America, the Middle East, Asia and Africa, which historically were difficult areas to find coverage.

As the tax insurance market has grown, we have secured increasingly larger policy limits - with multiple placements with limits of liability in excess of US$1 billion, using both specialised tax insurance capacity and other non-traditional capacity.

Since 2020, we have seen significant growth in the number of tax policies purchased, with 44 placed in 2023 alone by Marsh's London-based broker team, with total limits exceeding US$2 billion.

As insurer appetite continues to expand, and awareness of the product increases, we expect its use to continue to grow, as it has over the preceding five years.

Continental Europe

The European tax insurance market followed the global trend of increased activity with a slight delay, and thereafter have caught up quickly. Countries such as Sweden and Denmark took the lead in establishing tax insurance markets, followed by Germany, Spain, Italy, France, and Poland.

Tax insurance is now well-established in Continental Europe and considered a standard tool for a wide array of clients, lawyers, and tax advisors. Compared to 2020, the number of policies successfully placed in Europe has quadrupled, and the amount of limits covered by the insurance has nearly increased tenfold.

An increasing number of clients, with the support of their lawyers and tax advisors, are using tax insurance to protect against known tax risks, both in context of M&A transactions and to mitigate tax risks arising from day-to-day operations and internal restructuring. The percentage of policies purchased outside an M&A context was approximately 25% in 2020, and steadily grew to approximately 45% in 2023, similar to the trends observed in the US and UK marketplaces.

Global insurers have identified Europe as a growth market and invested in local underwriting teams. While the majority of policies were underwritten from London as recently as 2020, most insurers now have specialized tax insurance teams across Europe, allowing them to underwrite more complex risks and take into account specific national circumstances.

For Marsh, proximity to clients in European hubs has been the key to growth. To cater to the diversity of Europe and assist our clients where they are, Marsh has built a team of tax experts in the Nordic region, Germany, France, Spain, Italy, and Poland, and now has the largest tax insurance broking team in Europe.

Increased expertise among insurers and brokers, coupled with a steadily growing number of placed policies, has helped to improve both coverage options and pricing. While the ROL varies significantly depending on the nature of the risk and relevant jurisdiction, ROLs show a downward trend: The average ROL in Europe decreased from near 3% in 2020 to approximately 2.5% in 2023. In 2023 and 2024, several policies were placed with ROLs well below 2%.

This general trend has continued to date in 2024, with both the number of policies and the insured limits continuing to rise while coverage has broadened and become increasingly affordable.

Asia Pacific Region

The number of tax insurance policies placed by Marsh in the APAC region in 2023 doubled compared to 2020, and the total limit deployed by insurers on policies placed increased five-fold over the same period. In 2023, Marsh placed policies covering tax risks in APAC with a total limit of approximately US$1 billion. Demand for tax insurance has continued to rise throughout 2024 and we expect greater uptake going forward.

India is the most mature tax insurance market in APAC, and insurance is routinely used to cover risks related to international tax treaty benefits, especially in M&A transactions where the buyer is the withholding agent for any capital gains tax to be paid by the sellers. Marsh has placed tax insurance programs in India covering exposures up to approximately US$300 million for each policy.

While India accounts for most the tax policies placed in APAC, the use of the product has expanded across the region in recent years — as Marsh has placed insurance covering tax risks in Australia, China, Indonesia, Japan, South Korea, Singapore, and Vietnam.

The increased demand for tax insurance in the region has been driven primarily by:

1. Increased awareness of the product among clients, who are using the insurance to protect their balance sheet and to transfer tax exposures to insurers. Advisors have been advocating for the product and proposing it to clients as an alternative means of mitigating tax risks. Tax insurance is most commonly being used in the M&A setting, as an alternative to purchase price adjustments, funds being put in escrow, or specific indemnities, which can enable sellers to achieve a "clean exit" and give buyers greater financial protection. There has also been an increase in the use of tax insurance to address tax risks outside of M&A, primarily for group restructuring and "business-as-usual" tax exposures.
2. Insurers are now writing tax risks in jurisdictions that were previously not within their remit, with an appetite for a variety of risks. This includes risks that have been historically challenging to insure, such as tax positions that are heavily dependent on factual circumstances, for example, loss utilization rules, valuation, and transfer pricing.

There has been a significant increase in the number of insurers writing tax risks in APAC, with the high level of competition in the market leading to a generally favorable pricing environment for insureds. For APAC tax risks, Marsh is currently observing that premium rates-on-line are generally within the range of 2% to 5%, depending on the jurisdictions involved.

Conclusion

The tax insurance market is experiencing significant growth globally. The US, Canada, Latin America, UK, Europe, and APAC are all witnessing increased demand for tax insurance.

Tax insurance is being used in various sectors, including M&A, renewable energy, and balance sheet protection for multinational corporations to mitigate known and unknown tax risks. Insurers have expanded their appetite for tax risks and established local underwriting teams to address specific national circumstances.

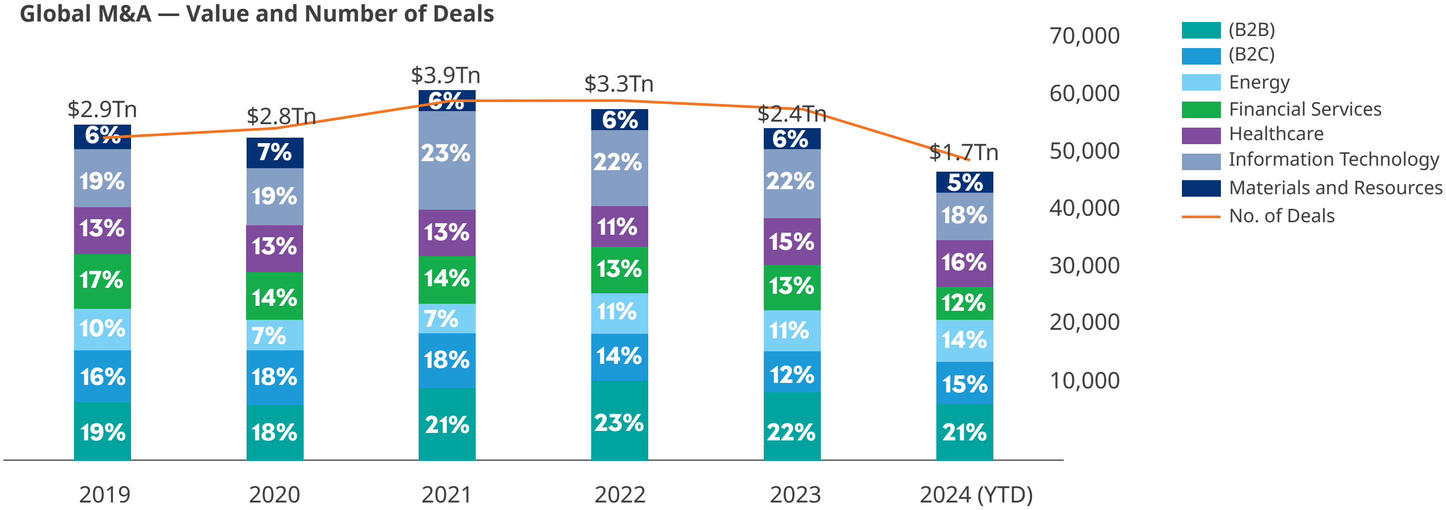
Premium rates generally have been declining in many regions, making tax insurance more affordable for policyholders. The popularity and growth of tax insurance are expected to continue globally, driven by increased awareness among clients and advisors, as well as insurers' willingness to underwrite a variety of risks.

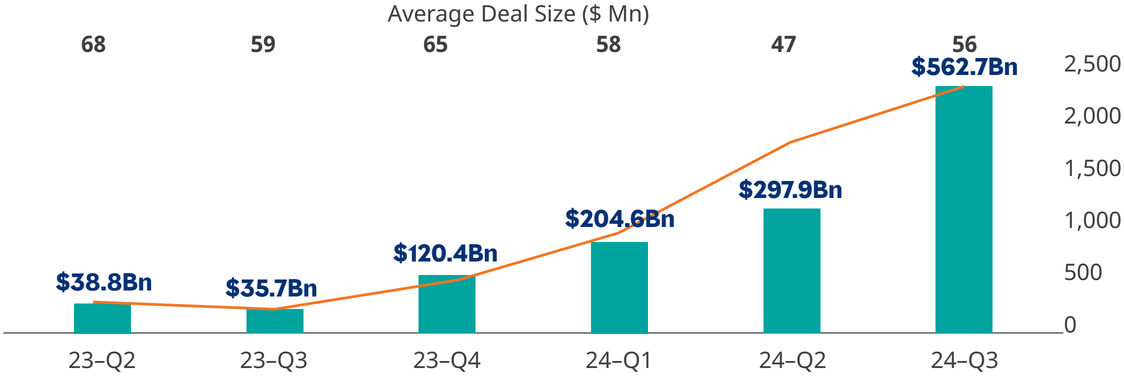
As a leader in this space, Marsh is well-positioned to assist organizations in navigating the complexities of tax risks and providing tailored tax insurance solutions. Through our expertise and global network, we can help clients effectively manage tax-related uncertainties and safeguard their business interests.

To learn more about the benefits of tax insurance and how it can support your organization's risk management strategy, we encourage you to reach out to your Marsh representative today.

Global M&A Market Value and Number of Deals

Global M&A — Value and Number of Deals





Source: Pitchbook

Why Marsh?

Marsh's Transactional Risk Practice is the world's leading provider of transactional risk insurance advisory services for M&A transactions, including representations and warranties insurance, tax indemnity insurance, and contingent liability insurance. In 2023, Marsh placed more than 2,000 transactional risk insurance policies on nearly 1,200 unique transactions globally on behalf of our clients, representing over $49 billion in limits of liability. Marsh employs over 120 dedicated transactional risk professionals located in strategic centers of excellence across 25 offices, with regional broking hubs in New York, San Francisco, Atlanta, Chicago, Toronto, London, Stockholm, Singapore, and Sydney. Our specialists possess deep experience, with backgrounds in taxation, corporate law, investment banking, and accounting policy, allowing us to understand the critical risks you may face during and after a transaction. We offer high-level access to all leading transactional risk insurance markets, enabling us to deliver the most comprehensive and cost-effective solutions to meet your needs.

For more information about Marsh's tax insurance solutions, visit marsh.com, or contact your local Marsh representative.

Craig Schioppo
Global Transactional Risk Leader
craig.schioppo@marsh.com

Mark McTigue
Managing Director, Tax Insurance
Co-Leader North America
mark.mctigue@marsh.com

Antony Joyce
Managing Director, Tax Insurance
Co-Leader North America
antony.joyce@marsh.com

Dr. Leon Steenkamp
Head of Tax Insurance, UK
leon.steenkamp@marsh.com

Leon Mixios
Head of Specific Risks, UK
leon.mixios@marsh.com

Eugene Lim
Head of Tax Insurance, Asia
eugene.lim@marsh.com

Kane Sim
Chief Client Officer —
Private Equity and M&A, Pacific
kane.sim@marsh.com

Alexander Skuratovski
Head of Tax Insurance, Europe
alexander.skuratovski@marsh.com

Dr. Bogdan Hansen
Tax Broker, Germany
bogdan.hansen@marsh.com

Laura Grosscurt
Tax Broker, Benelux
laura.grosscurt@marsh.com

Mara Sánchez-Ávila Ezquerra
Tax Broker, Spain
mara.sanchez-avila@marsh.com

Francesco Junior Nobili
Tax Broker, Italy
francescojunior.nobili@marsh.com

Clyde Fiawoo
Tax Broker, France
clyde.fiawoo@marsh.com

Krzysztof Dyba
Tax Broker, CEE and Eastern Mediterranean
krzysztof.dyba@marsh.com

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