

Real Estate Funds

Building a Risk-Resilient Portfolio

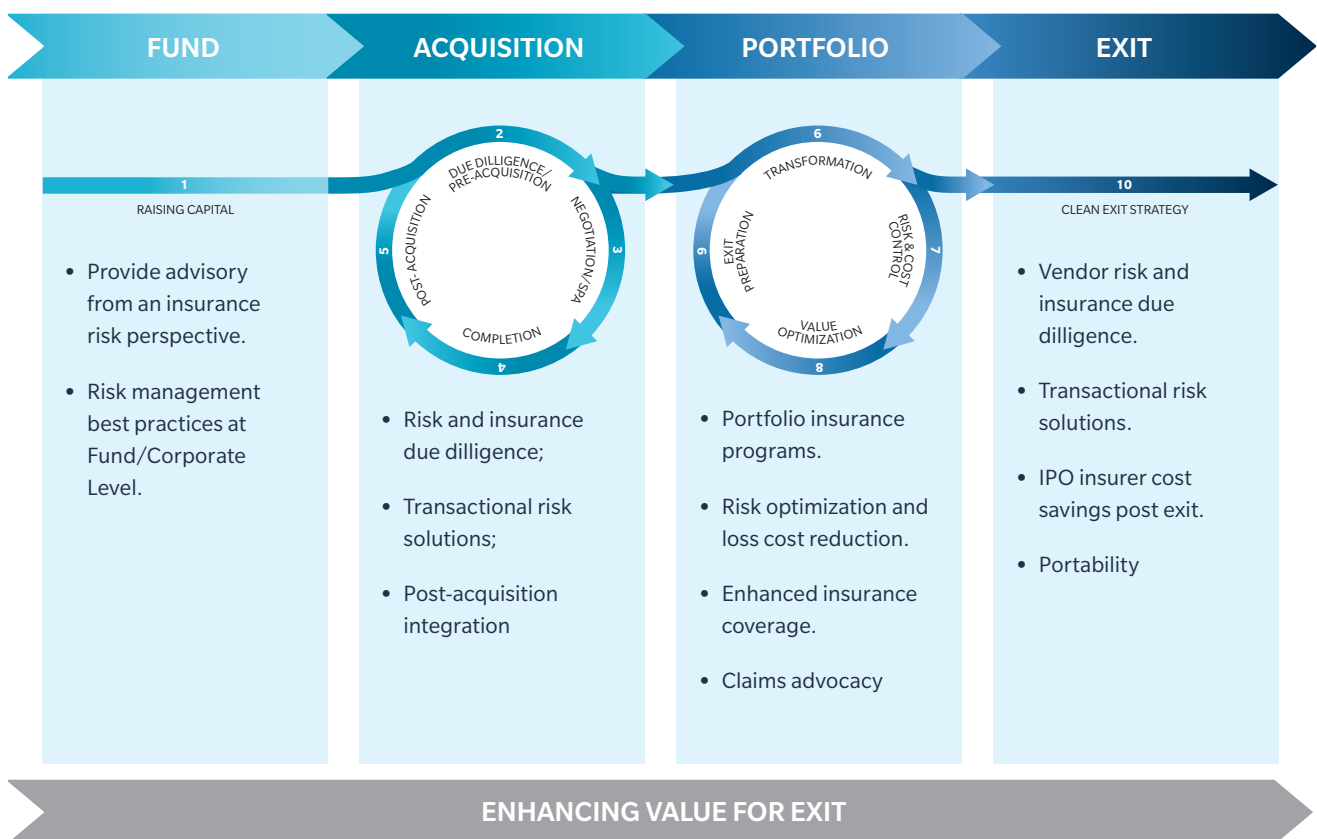


The Real Estate industry in Asia faces a myriad of different needs: providing homes and offices for the growing middle-class, social-infrastructure such as schools and aged-care homes for societies, and even data centers to support the growing use of technology. With Asian economies set to grow at unprecedented speeds, the demand for real estate is bound to increase.

The risk profiles of stakeholders like equity investors, corporates and lenders change throughout the life cycle of a real estate asset – from construction to operations and divestment. Their key risks revolve around preserving and enhancing asset value, reducing volatility of revenue streams, and redeploying of capital.

At Marsh, we understand the needs of our Private Equity Real Estate clients. Our team comprises specialists from both the Private Equity and Real Estate sectors. We understand the workings of real estate deals in private equity, and can provide cradle-to-grave support for each of your property investment, ensuring optimal outcomes and best returns for you and your partners.

Cradle-to-Grave Support for a Real Estate Fund



Due Diligence & Lenders Advisory

Equity Investors

For equity investors such as real estate funds and strategic corporates, Marsh can serve as risk advisors who will conduct pre-acquisition insurance due diligence (DD) on the target. This DD review will help investors understand the potential financial impact of the Target’s risks and insurance issues, and allow the investor to formulate a winning bid. This also allows the investor to ensure that their interests, and that of their limited partners and management teams, are well-protected.

PRE-ACQUISITION DUE DILIGENCE SCOPE	POTENTIAL IMPACT TO TRANSACTION
Uncover Red Flags (e.g. underinsurance, breach of contractual requirements, uninsured exposures).	<ul style="list-style-type: none"> Deal breakers. Representation and warranties in the SPA. Post-closing cost of risk.
Cost of risk analysis.	<ul style="list-style-type: none"> Valuation models. Price negotiations.
Analysis of key tenancy contracts in real estate transactions.	Seller's indemnities.
Claims.	Post-closing cost of risk.

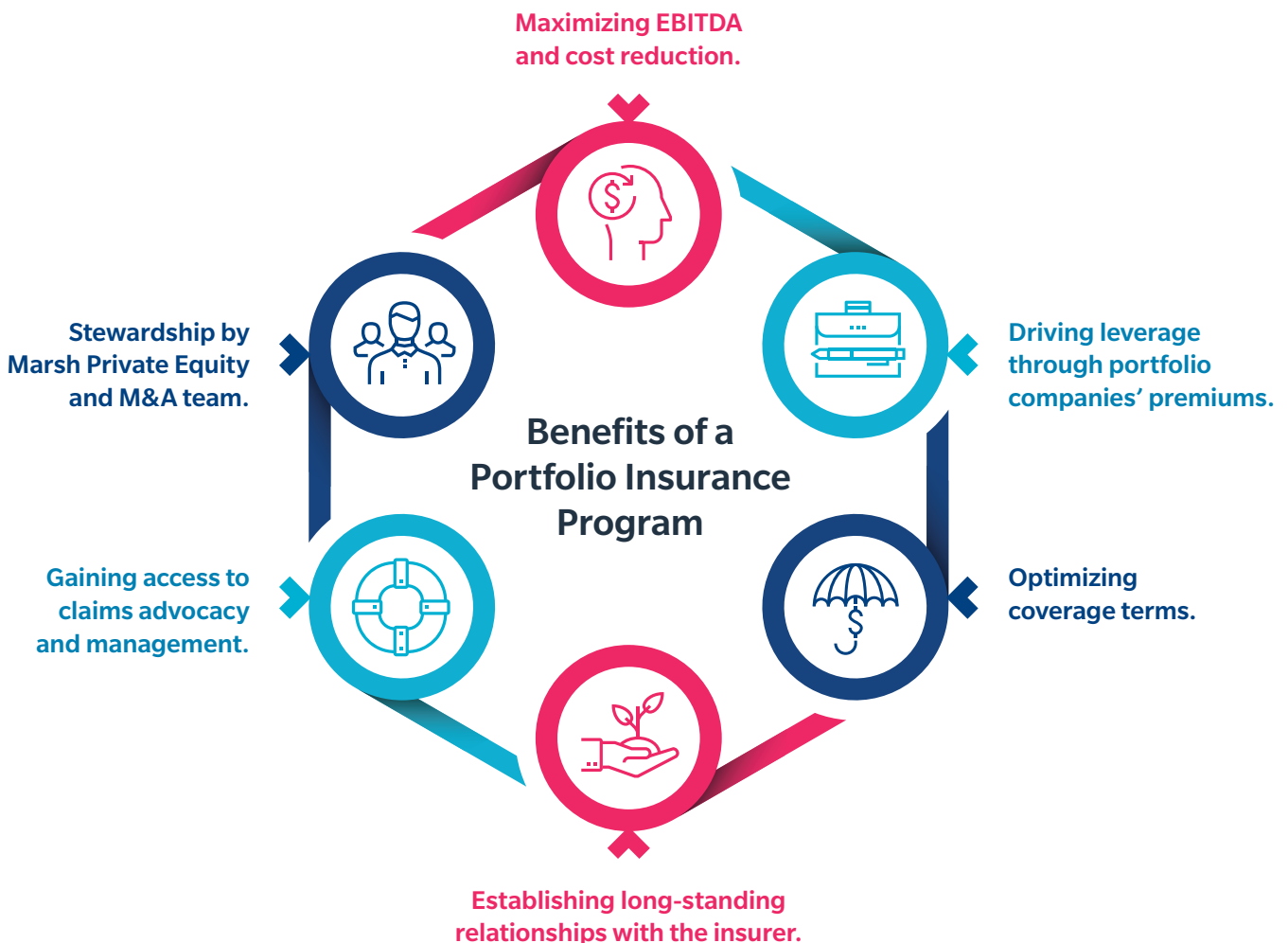
Marsh is also able to perform ad-hoc and interim insurance due diligence for asset managers and/or landlords who have transferred their obligations to insure to their tenants. This will ensure that their tenants are maintaining an acceptable level of insurance and have procured insurances that comply with contractual agreements.

Debt Financiers

Before any lender agrees to finance commercial and high-quality real estate, they will need the confidence that the risks associated with the property have been identified and satisfactorily addressed. Marsh provides risk advisory services to lenders looking to finance real estate developments. Marsh will work with the lender and their advisors (i.e. legal, financial, technical) along with other project parties such as the sponsor's insurance brokers, to identify, analyze and resolve key insurance issues in the project. By preserving the project's value and managing its risks, Marsh ultimately renders the project more bankable while fulfilling our duty of care to lenders.

Portfolio Insurance Programs

Following the acquisition or divestment, the asset will be rolled in or out of the Marsh-structured portfolio insurance program, which may bring about various benefits, such as:



Stewardship by Dedicated Marsh Portfolio Manager

The dedicated portfolio manager from the Private Equity and M&A team will be the fund's primary contact and will oversee the portfolio's insurance needs across all stages of the fund lifecycle. The portfolio manager will provide regular reporting such as monthly calls, which offer a convenient oversight on the insurance claims of the portfolio's assets. On top of that, the portfolio manager will provide an annual stewardship report that presents, a snapshot of your risk management efforts and highlights achievements for easy presentation to the board.

Transaction Risk Solutions

WARRANTY & INDEMNITY INSURANCE

During acquisitions and disposals, Marsh can arrange for Warranty and Indemnity ("W&I") insurance to reduce the potential risks associated with a transaction. W&I insurance can be used to bridge the gap between the different needs of the buyer and the seller. Furthermore, it can quicken the deal pace by facilitating negotiations during discussions on the seller's representations and warranties.

Where the fund is disposing of an asset through an auction process, Marsh can arrange for W&I Insurance for potential buyers. This involves conducting an initial SPA review and discussion, approaching markets, and preparing an explanatory note for bidders. Upon confirmation of the winning bidder, Marsh will be "flipped" to the buyer, who will work with Marsh and the selected insurer(s) to complete the underwriting process and arrange for insurance cover to be in place. This process can help funds achieve a clean exit and enhance deal value. (See case study 3).

Tax Insurance

Across Asia, tax laws are getting more complex. Hence, there is an increasing uncertainty as to whether a particular tax position may be challenged by the tax authorities. While taxpayers may prefer to adopt certain positions and interpretations to their advantage (especially when the tax laws are not clear), the additional tax exposure (including penalties and interest) may be significant. To manage this, tax insurance can be used to transfer relevant risks to insurers and obviate the need for any remedial actions, providing valuable certainty to the taxpayer. Tax insurance can also be employed to transfer tax risk relating to M&A transactions. Such policies are used by sellers to back an indemnity or are taken up by buyers when their sellers are unwilling to stand behind the potential liability on specific tax issues.

Some common issues faced in real estate deals are:

- Characterization of trading gains versus capital gains.
- Availability of treaty benefits.
- Deductibility on certain expenses (e.g. interest expense).



Case Studies



CASE STUDY 1

Insurance Due Diligence

TARGET

Warehouse Facility located in Singapore (the “Property”)

OWNER

Regional real-estate-focused private equity fund

PROJECT SIZE

Approximately S\$75 million

JURISDICTION

Singapore

RISK SOLUTION

Marsh recommended procuring insurance to plug the gaps in the existing insurance program, including:

- Reviewing the reinstatement cost of the Property and update the property damage sum insured.
- Updating the business interruption sum insured to the recommended amount.
- Updating the list of extensions in the policies.

RESULT

Following the due diligence exercise, Marsh assisted the Target in implementing the recommendations within our due diligence exercise. The resulting insurance program was compliant with contractual requirements and provided the required level of protection to the asset owner for their Property and profits.

CASE STUDY 2

Real Estate Financing

PROJECT

Five Star Hotel and Residential located in Bangkok, Thailand (the “Property”)

LENDER

International Bank

COUNTRY

Thailand

MARSH RECOMMENDATION

The review of the Property’s existing sums insured revealed the following shortfalls:

- Property damage sum insured not procured on full replacement values.
- Business Interruption sum insured calculation methodology was incorrect.
- Indemnity Period was below the market standard for hospitality clients.

Uninsured exposures: Terrorism and Sabotage, which was considered a significant risk given the emerging occurrence of terrorist activity in Bangkok at that time.

RESULT

Marsh highlighted these material deficiencies in the Project’s insurance program to the Lender, which led to a roundtable discussion with the borrower and their broker to rectify the identified lapses in cover. Marsh was also able to guide the brokers and the local insurers to correctly address Lender’s interests and mitigate uninsured exposures through insurance solutions.

CASE STUDY 3

Warranty and Indemnity (“W&I”) Insurance

TARGET

Two Office Buildings in Singapore

SELLER

Asian-Family-Owned Private Equity Fund

BUYER

Real Estate Private Equity Fund based in Singapore

PROJECT SIZE

Approximately US\$400 million

JURISDICTION

Singapore

ISSUE

The private equity seller approached Marsh at the start of the auction process, with a desire to achieve a clean exit and not stand behind the representations and warranties in the SPA.

RISK SOLUTION

Marsh conducted an initial review of the SPA and approached the market for quotes. Upon confirmation of the winning bidder, Marsh was “flipped” to work with the buyer and the selected insurer to complete the underwriting process.

RESULT

Marsh was able to put in place a Buy-side W&I insurance for a 100% limit of liability. The policy was structured with NIL retention, corresponding with the SPA, which was NIL recourse to the seller. This provided insurance coverage that was as back-to-back as possible to the SPA. Marsh was also able to negotiate for a policy with no transaction-specific exclusions. Ultimately, the seller achieved a clean exit as the buyer no longer required the seller to stand behind their warranties and unknown future liabilities.

CASE STUDY 4

Tax Indemnity Insurance

TRANSACTION

International Banks

ISSUE

The SG SPV was an investment holding company that indirectly held interests in Korean real estate through a Korean entity. The SG SPV was held by two unrelated shareholders (“Shareholder A” and “Shareholder B”). Shareholder A wished to exit the investments by transferring shares in the SG SPV to Shareholder B.

Under Korean tax law, where a taxpayer becomes a controlling shareholder that owns more than 50% of shares or ownership interest in a target company through the acquisition of shares, the controlling shareholder shall be deemed to have acquired the target company’s assets (i.e. the Korean real estate) that are subject to an acquisition tax. Hence, there was a risk that the Korean acquisition tax may apply to the transfer of shares in the SG SPV from Shareholder A to Shareholder B.

Given that the potential tax exposure was significant, any tax liability arising from the sale of the SG SPV would make the deal unattractive. Hence, the buyer required certainty that the transfer of shares in the SG SPV would not be subject to acquisition tax in Korea.

RISK SOLUTION

The Client obtained a strong favorable Tax Opinion from a leading tax consultant and approached Marsh to place a Tax Liability policy to cover the potential liability arising from the event where the Local Tax authority was successful in imposing the deemed acquisition tax.

RESULT

Marsh approached the relatively new tax insurance market and was able to structure and place a tax liability policy with a limit of up to USD 20 million. In the event of a challenge by the authorities, this limit was sufficient to cover the advance tax payments required by the Korean tax authority for the taxpayer to proceed with an appeal. The Client will be to proceed with the transaction with certainty on the tax outcome.

About Our Team

Private Equity and Real Estate (“PEMA”)

Marsh’s Private Equity and M&A Services is a dedicated team of specialists who focus on the risk and insurance issues that influence negotiations and the long-term financial success of a merger, acquisition, divestment, or project financing of your real estate asset.

Established over three decades ago, our global practice of over 160 professionals based in more than 25 countries has advised on over 10,000 transactions (including project finance deals). These transactions include real estate M&A, divestments, privatizations and structured finance transactions. We provide cross-border, on the ground and industry-focused teams to reflect the geographic reach of a transaction. In Asia, we have offices in the countries fully teamed with multi-lingual professionals from a diverse range of backgrounds including legal, banking, finance, and insurance.

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