ORIGIN
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Spotlight on Challenging Markets

Recent developments in strategic, capital and structural advisory solutions

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Innovative. Independent. Experienced. Canada's Largest M&A Advisory Boutique

COVID-19 IMPACT

Origin’s Comment

These are extraordinary times. We’re facing a global health crisis that is rapidly becoming a financial and existential crisis for many businesses. At Origin, our collective expertise, experience, and extensive investor relationships may be useful to businesses faced with current challenges, and we are here to help.

Our team is deeply engaged with its broad network of capital providers, backstopping our commitment to support Canadian businesses with thoughtful debt, equity and structural solutions. Our goal: to help businesses navigate through this challenging period, then thrive when we emerge on the other side.

In this Issue

In this issue, you’ll find:

- The most recent data for BIA filings by industry
- CCAA proceedings: what the numbers are showing
- Beyond R&W: Insurance Solutions for Distressed Deals – An interview with BFL Canada execs diving into how the industry has responded to the crisis, and what insurance solutions are available to support distressed deals

Business and Industry Filings Update – May 2020

Data for May business BIA filings continues the same trend as seen during the COVID-19 impact – namely a fairly sharp decrease in the number of such filings.

- Arts, Entertainment and Recreation, Retail, and Management have gone against this trend
- While still down YTD, Mining and Oil and Gas Extraction filings picked up in May fairly materially (doubling from 5 YTD April to 10 through May)

CCAA proceeding information is available to present and, while numbers are small and subject to more noise, June continued May's trend of material increases in number of filings, and we are already well above 100% increase above 2019 levels with another 12 proceedings in June alone.

Consumer insolvencies in May sat at roughly half their 2019 rate, similar to experience in April, showing that CERB and other programs are offsetting the spike in unemployment, and reflecting that fewer consumers see a benefit from declaring bankruptcy.

All Canadian BIA Bankruptcies and Proposals

NAICS Economic Sector	YTD May	Change From 2019 Levels
Accommodation and Food Services	193	-23%
Construction	173	-46%
Retail Trade	173	9%
Manufacturing	112	-21%
Professional, Scientific and Technical Services	85	-35%
Transportation and Warehousing	77	-29%
Other Services	67	-17%
Real Estate and Rental and Leasing	54	-18%
Wholesale Trade	53	-35%
Arts, Entertainment and Recreation	51	59%
Admin & Support, Waste Mgmt and Remediation	48	-36%
Management of Companies and Enterprises	44	13%
Information and Cultural Industries	27	-25%
Health Care and Social Assistance	24	-31%
Agriculture, Forestry, Fishing and Hunting	23	-26%
Finance and Insurance	13	-62%
Mining and Oil and Gas Extraction	10	-41%
Educational Services	10	-23%
Utilities	3	0%
Public Administration	0	0%
Total Business BIA Filings	**1,240**	**-25%**
CCAA Proceedings - YTD May	**26**	63%
CCAA Proceedings - YTD through June	**38**	138%
Consumer Insolvencies	**46,038**	-18%

Source: Office of the Superintendent of Bankruptcy Canada

JOHN ANTONECCHIA SEAN FLINN

BEYOND R&W: INSURANCE SOLUTIONS FOR DISTRESSED DEALS

Before the onset of the pandemic, Representations & Warranties (R&W) insurance had become a standard in Canadian M&A transactions above a certain deal size threshold. With the onset of the COVID-19 crisis, deal volume has dropped dramatically, while CCAA filings are on the rise. Against this backdrop, we spoke with Sean Flinn and John Antonecchia, Co-Heads of the M&A Practice at BFL Canada, about:

i) How the insurance industry has responded to the crisis from a R&W insurance perspective; and
ii) As we anticipate an increase in distressed deal activity, whether insurance offerings will be available to support and help facilitate those transactions.

BFL Canada is one of the largest employee-owned and operated commercial insurance broker and consulting services firm in Canada.

OMP: *How has the insurance industry reacted to the crisis?*

JA/SF: The insurance industry reacted well from a R&W insurance perspective, on deals that were in the interim period, signed pre-COVID and closed during COVID. On the whole, insurers generally accepted the terms agreed to at closing, despite the risks associated with COVID, and the potential for increased claims.

- **Going forward, expect to do COVID diligence through the interim period**

On deals bound in a COVID world, insurers typically include some form of COVID-19 exclusion in their policies, with the approach varying among insurers. In addition, if there is a difference between signing and closing dates, some insurers may require a COVID-19 exclusion during the interim period; on "bring down", they will expect ongoing COVID-19 diligence has been done to a level of materiality consistent with that expected on signing.

- **Pricing remains largely unchanged**

Pricing remains at pre-COVID levels: while deal volume is down, insurers' appetite for business remains strong, so pricing reflects a desire to win despite perceived higher risk. Some insurers, however, are offering a less restrictive COVID exclusion at a higher price.

With deal value currently trending smaller, in Canada, insurers are willing to do smaller deals (sub-$15 million) at smaller premiums when they are confident that appropriate diligence is being done.

BEYOND R&W: INSURANCE SOLUTIONS FOR DISTRESSED DEALS

OMP: Is there a role for R&W insurance in distressed deals?

JA/SF: We have ongoing conversations with insurers and insolvency practitioners to understand what is possible so that we are prepared to support distressed M&A. We're hearing the following:

- **R&W insurance may help in distressed deal situations**

There is likely a place for R&W insurance in distressed deal situations. For example, in the context of a sale process, there is a trend to "pre-packaged insolvency preparation": essentially, getting ready for CCAA by getting ducks in a row to get through as quickly as possible and minimize reputational damage.

Where a sale process is run concurrently with CCAA proceedings, the deal could be shopped with a R&W insurance package to support a potential bidder. This could be particularly attractive, potentially expanding the field of buyers beyond those used to doing deals on an "as is, where is" basis, on a transaction where there otherwise might not be much of an indemnity.

- **Stalking horse bids**

In a bankruptcy situation, there is also the possibility of including a fully stapled, underwritten policy as part of a stalking horse bid, with the cost built into the break fee.

- **No seller indemnity deals**

A trend that we are seeing in the US is the "no seller indemnity" deal, where all reps and warranties terminate on closing, and the only recourse is through the insurance policy. This public style transaction lends itself well to the distressed space. At the moment, we're only seeing this on approximately 20% of deals in Canada (vs 80% in the US), however, that may change as the volume of distressed deal activity rises.

OMP: *Are there any other insurance offerings that could be useful in distressed deal situations?*

JA/SF: There are also more "surgical" approaches on the insurance side that could be a good fit for distressed deals, most notably, Successor Liability Insurance ("SL" insurance).

- **When SL insurance is useful**

In situations where reps and warranties are not that substantial, R&W insurance will not be useful. There may, however, be other specific liability risks that make successor liability insurance the best solution. We have seen this surgical approach used to mitigate environmental, product liability, intellectual property, and tax issues.

Beyond R&W: Insurance Solutions for Distressed Deals

There may also be successor liability risks associated with customer contracts, or “fraudulent conveyance” risks associated with assets, where a Contingent Liability policy may ease the sale of substantially all the assets of an insolvent company.

OMP: Any final thoughts you’d like to share?

JA/SF: As we are likely to be seeing an increase in distressed deal activity, it’s helpful to know that insurers are getting comfortable with a range of distressed deal solutions: the traditional R&W offering, public style deals with no seller indemnity, and the bigger box of successor liability insurance.

About Origin Merchant Partners

Origin Merchant Partners is an independent investment bank that provides value added corporate finance, mergers and acquisitions and merchant banking services delivered by senior professionals. Our clients engage us for our dedicated, high level of service and independent advice to address their strategic and financial plans

Origin Merchant Partners
220 Bay Street, Suite 1500
P.O. Box 23
Toronto, Ontario
M5J 2W4

OMP Restructuring Team:

Jim Osler
Principal
T: 416-800-0784
jim.osler@originmerchant.com

Lindsay Adam Weiss
Principal
T: 416-775-3656
lindsay.weiss@originmerchant.com

Robert Fedrock
Advisor
T: 416-817-8054
robert.fedrock@originmerchant.com