

The Willis Index

Willis

Mergers and Acquisitions Newsletter

The quarterly newsletter of the International Mergers and Acquisitions Practice

Q4 2005

KKR completes full exit from Willis

Willis has announced and completed a secondary offering for the sale of 6.1 million shares previously held by Kohlberg Kravis Roberts (KKR) and Fisher Capital.

Willis has purchased 1.5 million of the shares in a private transaction with the remaining shares being publicly offered. KKR has now fully exited their holding in Willis Group common stock, although certain KKR executives will continue to maintain their personal investment. These transactions represent the last stages of KKR's orderly disposal program which commenced approximately five years ago with a flotation on the New York Stock Exchange (NYSE) in 2001. The flotation happened some two and a half years after the legendary buy-out firm led the take private of the company in July

1998 in a deal worth GBP951m. Today Willis' market capitalisation is in excess of GBP3,500m. Willis looks forward to supporting KKR as they continue to seek out investment opportunities with both their US and dedicated European fund, along with their developing presence in Asia through recently opened offices in Hong Kong and Tokyo.

Japanese M&A capabilities

Asian M&A is continuing to be a topic of conversation for a number of professionals in the global financial sponsor community and Japanese strategic buyers are now flexing their muscles both domestically and internationally. This has been demonstrated by recent deals such as the Kao acquisition of Molton Brown and Fuji's acquisition of Sericol Inks (both targets being private equity backed in their own right). Willis has now launched a dedicated M&A practice in Tokyo as part of our Asian M&A practice and with an increasing number of private equity firms opening offices in the country. We look forward to working with a number of our international clients as they develop their activities there.

Portfolio insurance initiatives

The theme of Active Management (as defined in a recent McKinsey report) is becoming increasingly prevalent amongst private equity firms with an increasing focus on generating operational value rather than just financial structuring in portfolio companies. Insurance is a key workstream in such initiatives with reviews across the portfolio often yielding substantial savings and, more importantly, ensuring that the portfolio investment are suitably insured in terms of both width of coverage and limits.

We have been involved in developing a number of initiatives with private equity firms and believe that our thinking is at the forefront of portfolio insurance programmes in UK and Europe. This is reflected in our recent appointment to act as portfolio insurance broker to the various investee companies of Baugur in UK. We are also seeking to enhance efficiencies still further by developing web enabled and other online technology solutions to deliver insurance policies and solutions to private equity backed businesses.

Environmental Insurance Solutions from Willis M&A Practice

Environmental liabilities can seriously affect a company's liquidity and create a drag on corporate performance, which may in turn undermine investor and customer confidence. These liabilities, whether real or perceived, tend to crystallise and become a priority issue during the course of business transactions.

Increasingly stringent environmental legislation, improved awareness of environmental issues within the property and financial sectors and escalating costs of dealing with contamination are often key causes.

The Willis Environmental Team, which forms part of the Mergers & Acquisitions Practice, is ideally placed to deliver innovative, robust and cost effective insurance solutions. We enjoy considerable market prominence due to the significant volumes of business transacted with the global Environmental Insurance Market. However, our market leverage goes beyond size alone; it is also developed from our experience, creativity, flexibility and commercial insight.

For more information visit www.willis.com/environmental.

Willis Index Publications

The specialist divisions of Willis FINEX produce regular publications on the relevant issues affecting the insurance industry and the impact they have on various business sectors. To request editions of The Willis Index including Financial Institutions, Professional Indemnity, Directors' & Officers' Liability or Environmental Liability please contact Melanie Barnes at barnesmx@willis.com.

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Historical Exposure – A case study

Willis Mergers and Acquisitions Practice recently undertook a due diligence exercise for a UK domiciled multi-national company looking to acquire a UK distribution business. The target business was an investee company of a private equity house which had held the business for a number of years.

During the early stages of the due diligence process, it became clear that there was loss activity involving employee disease claims relating to a part of the target business that had been discontinued during the early 1990's. Whilst the current insurance arrangements were given a clean bill of health, the investigation into the loss activity led to a concern that warranted further investigation. Claims had been brought, during the time that the private equity fund had been in ownership of the business, by previous employees who had been involved in past asbestos related activities.

Industrial disease claims had been brought over a number of recent years relating to period of employment as far back as 1953 with a number of unknown claim values, uncertainty of cause, and scant information on the circumstances surrounding the apportionment of liability. It was necessary to investigate a number of areas to provide the complete picture to the acquiring client.

Firstly, the Employers Liability coverage was investigated. Although a comprehensive history was obtained going back over fifty years there were two issues, namely insolvency and partial identity. Certain insolvent insurers were identified, and although the Financial Services Compensation Scheme (FSCS) was available to pick up claims from 1972 onwards, insolvency impacted a number of preceding years. This was a direct exposure to the balance sheet of the business. In addition to the insolvency issue, there were four insurance years where the identity of insurance policy in force was not known or identifiable before signing. In such circumstances, the FSCS will not meet claims brought against the company.

Secondly, the history surrounding the business practices was required. It became apparent that the business, over the course of the past thirty years, had undertaken a number of acquisitions of its own – on a variety of different platforms. In one instance, an acquisition was an asset transaction, with the past liability apparently being left with the vendor. Equally, the business practices involved a plethora of approaches to customer requirements. This resulted in employees and sole trade sub-contractors being utilised. The questions arose - Were they correctly declared to insurers by the original 'employer'? Did employees work elsewhere in the same business sector? Could contribution be obtained from other employers?

The number of employees and sub-contractors had to be investigated, together with the identity and length of service. With the assistance of legal and financial advisors, historical payroll records were recovered to provide certainty of the employee numbers and to trend the use of sub-contractors over the period in question.

Lastly, the complete loss experience with regard to employers liability was specifically investigated. Employee claims were predominantly related to asbestos exposure with symptoms varied across Pleural Plaque, Asbestosis and Mesothelioma. Willis examined the latest Judicial Study on General Damages to develop a picture of the likely settlement value attaching to potential claims likely to be brought.

In order to provide certainty to the open areas of exposure an actuarial analysis was undertaken by a third party to establish the potential future exposure from industrial disease claimants. In parallel, Willis worked with insurers of the acquiring company to look for a further level of retrospective coverage in the event that claims were brought against the target across years where the original insurers were unidentified.

At the commencement of the assignment the acquiring client was looking at uncertainty of the current industrial disease exposure, ability to recover from insurers, and greater uncertainty to future loss development. At the conclusion of the insurance due diligence process, the acquiring entity was able to sign with knowledge of the past and current exposure, an overview of the likely development of loss activity and the certainty of what protection would be available in the event that further claims arose.

Simon Dodsworth, Project Director, +44 (0)20 7975 2094.



Artist impression of the "Willis Building" currently under construction in the City of London, due for completion late 2007.

New joiners

Johan Forsgård

Originally from the Island Åland in the Baltic Sea, 26 year old Johan Forsgård holds an LL.M from Gothenburg University. Johan started his career at a small private bank as a bank lawyer in 2002. At the same bank he later changed focus and became Operational Risk Manager with, among other tasks, responsibility for the group's insurance cover. As a result of this role Willis were aware of Johan and he was recruited to be a Project Manager in our Nordic M&A Practice where he started in November 2005.

As a former islander, Johan enjoys sailing, running and golfing. Summers are often spent on Åland with family and friends. John says "It is a perfect combination to be able to relax on Åland during summer and then spend rest of the year working and enjoying Stockholm." Johan also enjoys spending time with his relatives in US, especially in Florida.

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Analysis of Industry Sector Specific Risks

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The Willis M&A Practice provides due diligence and deal facilitation consultancy for clients undertaking acquisitions across a broad range of industry sectors. In this and future editions of the M&A Index, we will review risks specific to businesses operating in the following industry sectors:

Infrastructure:

- Airports
- Roads/Tunnels/Bridges
- Water/Electricity/Gas
- Healthcare
- Leisure (Pubs/Fitness Clubs)
- Financial Services
- Defence
- Retail
- Energy

Infrastructure Risks – Airport Operators

Historically the majority of civil aviation airports have been owned and managed by government, both in the UK and worldwide. Privatisation of airport operations commenced in the 1980s, with BAA in the UK being an early example of this government divestment strategy.

International airports demand significant levels of capital expenditure to ensure that infrastructure and facilities remain up to date and appropriate for passenger and cargo throughput. This significant expenditure is unattractive to governments who will typically sell a concession to operate an airport for a time period of 30-40 years and impose minimum capital expenditure requirements upon the privatised airport operator. The level of airport privatisation across Continental Europe has increased significantly in recent years and, with the accession of 10 new countries to the European Union in 2005, the process is now accelerating eastwards. Governments of countries with emerging economies, such as India, are also now seeking to privatise key airport operations.

A privately owned airport operation concession should generate a stable, long-term investment return. Revenue will be generated from the following areas:

Aviation charges:

- Take off/Landing and Aircraft Standing fees.

Non aviation revenue:

- Rental income from terminal retail space.
- Car parking.
- Sub-lease of airport ground space for hotel/business park developments.

Airports present a unique risk profile, combining high levels of aviation liability risk (insurance limits of US\$500million to US\$1.5billion are often purchased) with significant property and business interruption exposures. Environmental risk is also a factor at the majority of established airport sites. Key factors that need to be considered in relation to insurable risks presented by a civil aviation airport are as follows –

Liability risks to:

- Aircraft operators and passengers should inadequate security screening of passengers and cargo lead to losses caused by aircraft hi-jack and/or terrorism.
- Aircraft operators should defects to runways/taxiways/aprons cause loss or damage to aircraft.
- Aircraft operators should airport vehicles working in the apron areas cause impact damage to aircraft.
- Aircraft operators should failure of air traffic control result in loss or damage to aircraft (Air traffic control responsibility may not always be retained by the airport operator, improving its risk profile)
- Passengers, employees and users of the airport site through loss or damage caused by defects to terminal and other buildings / inability to safely evacuate in the event of fire or other emergency situation
- Employees caused through inadequate health and safety training, particularly whilst working in the airside environment.

Property and Revenue Stream Protection. Ensuring that:

- Reinstatement valuations for terminal and other key buildings are adequate and up-to-date.
- Business Interruption insurance is purchased with an Insured Limit and Maximum Indemnity period which is reflective of the time needed to clear and fully reinstate buildings/business operations after a major loss.
- Third-party occupiers of airport terminal space (retail stores, catering concessions, etc.) are contractually obliged to insure property and liability risks arising from their business operations.
- Disaster Recovery/Business Continuity planning is up-to-date and fully tested.
- Terrorism risks (where appropriate) are insured.

Environmental Risk, contamination of soil and groundwater caused by:

- Solvents used in aircraft cleaning and de-icing
- Leakage from fuel stores
- Fire-fighting chemicals (usually in the vicinity of an airfield fire training area)
- Historical use of an airfield for military purposes may result in old, unexploded ordnance being buried on-site
- Asbestos insulation within terminal and other airport buildings.

In a full due diligence exercise each of these risks will be reviewed and recommendations made where current insurance and risk management arrangements can be improved upon. Substantial knowledge of the global aviation insurance market also allows the Willis M&A team to benchmark the level and scope of insurance cover purchased by an airport operator and to provide an estimate of insurance budget cost for an airport operation concession post-completion.

Once agreement has been reached to purchase an airport operation concession, the M&A team can then facilitate the arrangement of a full new insurance programme for the business, utilising the leading global broking expertise of the Willis Aviation division.

Martin Bennett, Project Director, +44 (0)20 7975 2393.

Meet the Team



Tony Burns BSc (Hons) Chem Eng International Development Director, Germany

Tony joined a former company of Willis Germany almost 20 years ago and has played a significant role for Willis working for multinational clients since that time. A qualified Chemical Engineer from the UK, Tony has lived and worked in Germany for almost 30 years. He launched his career in the insurance

industry over 30 years ago with a US insurance company as a fire protection engineer in the USA, UK and Germany. During this time Tony has worked for a number the major multinational companies around the world, prior to focussing on complex multinational property program placements. The knowledge gained over this time has given Tony in-depth and hands-on knowledge of the international M&A sector.

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Willis Mergers & Acquisitions Practice performed insurance due diligence and structured a transactional insurance product on the

£77,000,000

acquisition of

Bezier Holdings Limited

by

MID OCEAN PARTNERS

August 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence on the

acquisition of

CASA REHA
VON MENSCH ZU MENSCH

by

Advent International
GLOBAL PRIVATE EQUITY

September 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence on the

acquisition of

CMGL
CORPORATE MANAGEMENT GROUP LIMITED

by

a newco backed by

SOVEREIGN CAPITAL

September 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence on the

£465,000,000

acquisition of

Inexus Group Holdings Limited

by

challenger
Financial Services Group

September 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence on the

£177,000,000

acquisition of

178 pubs from the Spirit Group

by

TCG
a newco backed by the Alchemy Investment Plan

ALCHEMY

September 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence on the

acquisition of

Derby Cycle

by

Finattem Beteiligungsgesellschaft
Frankfurt am Main, Germany

September 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence and structured a transactional insurance product on the

acquisition of

WARNER HOWARD

by

plc Group plc

October 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence on the

£75,800,000

acquisition of

Sporting Index
World Leaders in Sports Spread Betting

by

HgCapital

October 2005
This announcement appears as a matter of record only

Gras Savoye (a Willis Partner) Mergers & Acquisitions Practice performed insurance due diligence on the

Euro 37,000,000

managed buy-out of

pronatura.com

by

ACTIVA CAPITAL

October 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence on the

Euro 835,000,000

acquisition of

SELENIA
FLUIDS & LUBRICANTS

by

KKR

November 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence on the

acquisition of

SCHENCK
MEASURING AND PROCESS TECHNOLOGIES

by

HgCapital

November 2005
This announcement appears as a matter of record only

Willis Mergers & Acquisitions Practice performed insurance due diligence on the

Euro 650,000,000

acquisition of

TDC Forlag

by

European Directories SA

December 2005
This announcement appears as a matter of record only