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SHAW

**Middle-Market**  
**M&A**  
**SurveyBook**

2016 Survey of Key M&A Deal Terms

# Introduction

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Seyfarth Shaw LLP is pleased to present the 3rd edition of its Middle-Market M&A SurveyBook (“Survey”), which analyzes key transaction terms included in over 200 middle-market (<\$1 billion) private target acquisition agreements signed in 2015.<sup>1</sup> The information presented is intended to serve as a guide to buyers, sellers and deal professionals on “what’s market” when negotiating private target acquisition agreements in what we expect will be an active 2016.

The Survey focuses on key deal terms comprising the “indemnity package” included in almost all private target acquisition agreements to address the issue of a seller’s potential post-closing liability to a buyer and defining the scope by which the purchase price paid to a seller may be potentially clawed back by a buyer.

The data analyzed in this Survey suggests that the current M&A environment is continuing to have a favorable impact on key deal terms from a seller’s perspective. For example, our Survey data shows an increase in the use of escrow periods of 12 months or less, a decrease in median escrow amounts and a higher percentage of deals employing an indemnity cap of 10% or less, in each case, as compared

to the two prior years. Buyers continue to attempt to differentiate themselves and present a more compelling bid for acquisition targets or their assets by taking on more risk in their acquisition agreements and offering more aggressive contractual terms to sellers. Buyers are also increasingly purchasing representation and warranty insurance in an effort to make their acquisition proposal even more attractive to a seller by limiting potential post-closing liability of the seller.

According to *Mergermarket*, 2015 North American middle-market M&A deal volume declined from the historic highs of 2014 due in part to the growing valuation gap between buyers and sellers.<sup>2</sup> High valuations were fueled by, among other things, large numbers of potential buyers competing for fewer quality assets, inexpensive financing, and the sometimes unrealistic application of mega merger multiples to middle-market deals. The high valuations that were attached to many middle-market M&A transactions have also contributed to a more seller-friendly M&A environment in 2015.

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To be sure, each deal has unique facts and circumstances that impact the negotiation of the acquisition agreement, including, importantly, the relative leverage of the buyer and seller. It is nonetheless helpful when negotiating an acquisition agreement to have a strong understanding of where the terms of your “indemnity package” fall in the current market spectrum. This Survey aims to arm you with this information. Our Survey provides you with data on these key terms, together with our insights, in an easily readable format and is intended to be a quick reference guide to assist buyers, sellers and deal professionals negotiating private target acquisition agreements.

If you would like more information regarding the data presented in our Middle-Market M&A SurveyBook, we welcome the opportunity to further discuss our findings with you.

<sup>1</sup>For purposes of this Survey, “purchase price” means the total cash consideration paid by the buyer in a transaction, but does not include contingent purchase price payments (e.g., earnouts). This Survey does not include any transactions that involved the payment of any consideration other than cash.

<sup>2</sup>Mergermarket, *Mid-Market M&A: The Valuation Gap*, March 2016

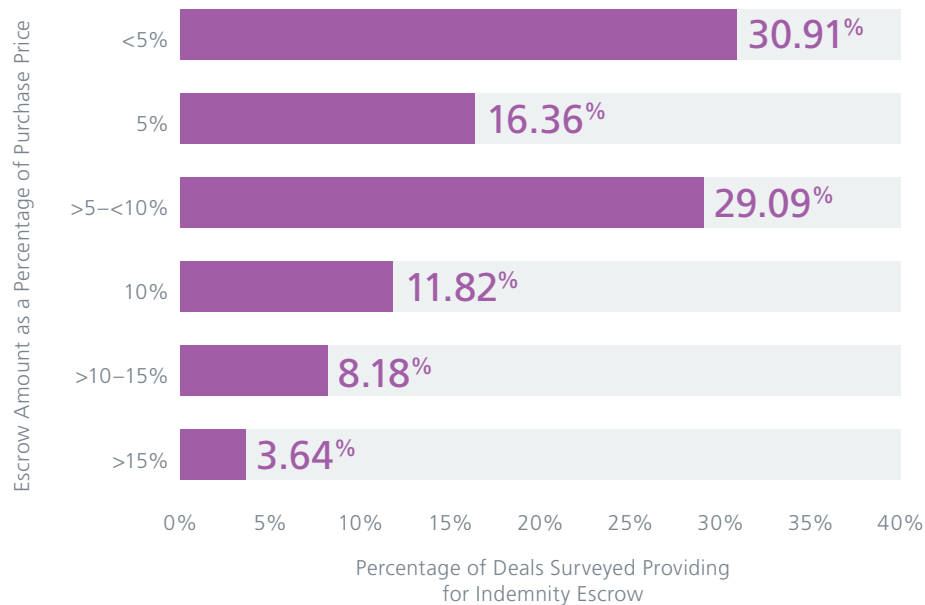
## Key Deal Terms Surveyed\*

- Indemnity Escrow Amount
- Indemnity Escrow Period
- Representation & Warranty Survival Period
- Carve Outs to General Survival Period
- Indemnity Basket Type
- Indemnity Basket Size
- Indemnity Cap

\*A glossary of these terms can be found on page 10.

# Indemnity Escrow Amount

Approximately 52% of all deals surveyed provided for an indemnity escrow.



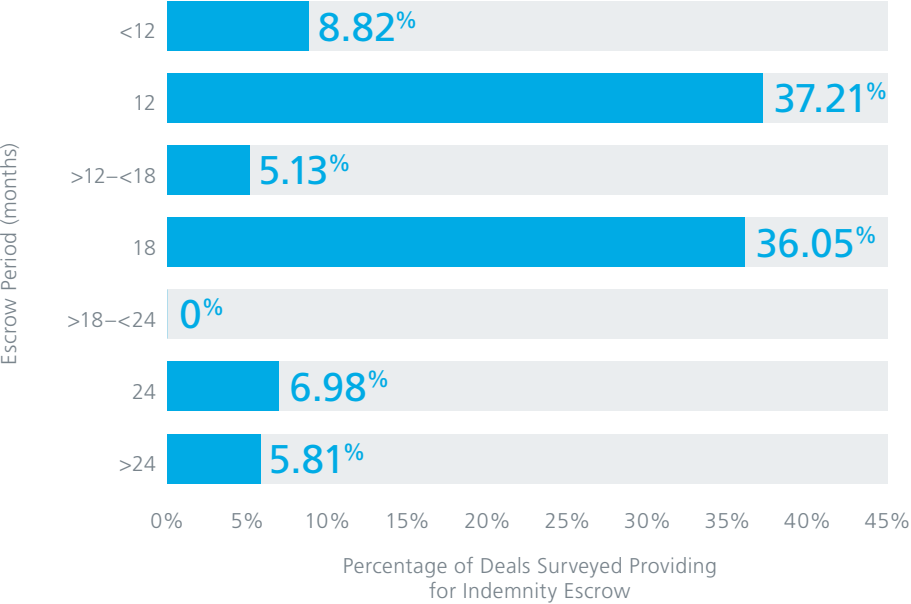
## Observations\*

Of the deals surveyed which provided for an indemnity escrow:

- The median indemnity escrow amount in 2015 was 6% (compared to 7.41% in 2014 and 8.78% in 2013).
- Approximately 76% had an indemnity escrow amount of less than 10% (compared to 59% in 2014 and 48% in 2013).
- Approximately 31% had indemnity escrow amounts of less than 5% (compared to 21% in 2014 and 15% in 2013). Our data suggests that the use of representation and warranty insurance has contributed to the increase in the number of deals with indemnity escrow amounts under 5%.

\*Data used in this Survey for prior year comparisons has been derived from the results of our prior surveys.

# Indemnity Escrow Period

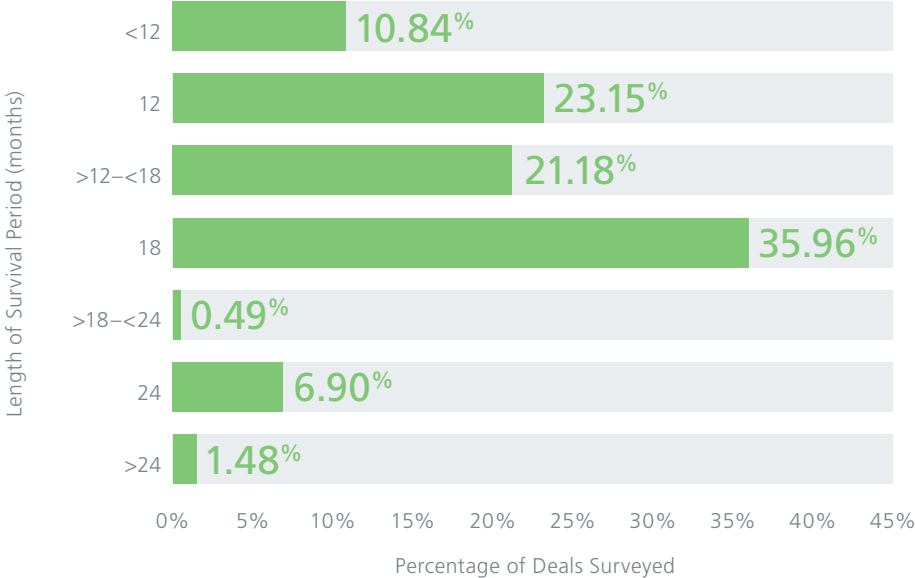


## Observations

Of the deals surveyed which provided for an indemnity escrow:

- The median indemnity escrow period increased slightly in 2015 to 16.5 months (compared to 15 months in 2014 and 2013).
- The percentage of deals with an indemnity escrow period of 12 months or less increased to over 46% in 2015 (compared to approximately 40% in 2014 and 34% in 2013).

# Representation & Warranty Survival Period\*

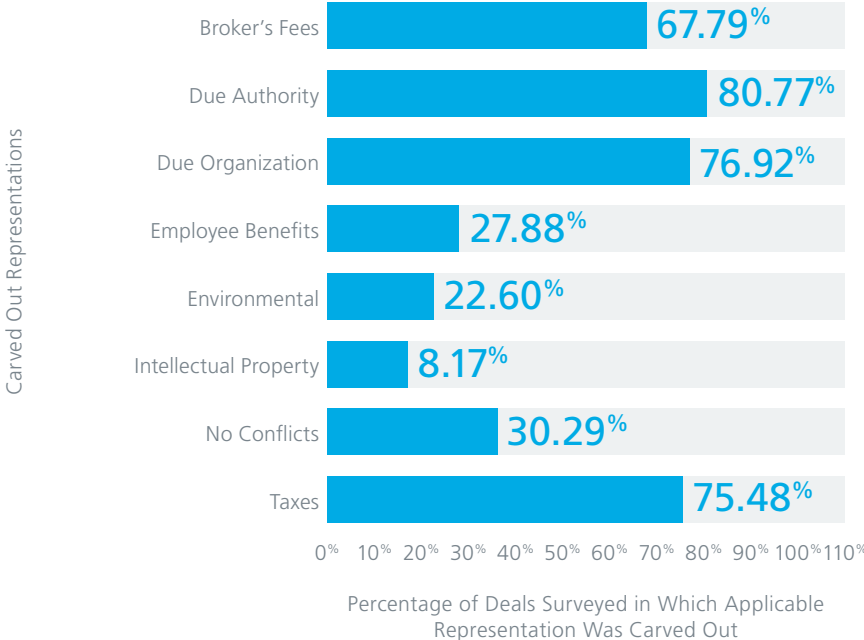


## Observations

- The median survival period for deals surveyed was 15 months, which has remained consistent since 2013.
- Approximately 80% of deals surveyed had survival periods from 12 to 18 months, representing a slight increase when compared to 78% in 2014.
- Approximately 36% of deals surveyed had a survival period of 18 months, representing an increase when compared to 32% in 2014.

\*For purposes of this Survey, the survival periods set forth in this chart is for “general” representations and warranties. This chart does not take into account longer survival periods for certain representations and warranties that are sometimes carved out of the general survival period (see page 6 for information regarding carve outs).

# Carve Outs to General Survival Period



## No Conflicts

The percentage of deals surveyed that carved out representations and warranties regarding no conflicts has steadily increased from approximately 23% in 2013 to 25% in 2014 and 30% in 2015.

## Other Carved Out Representations

### Capitalization

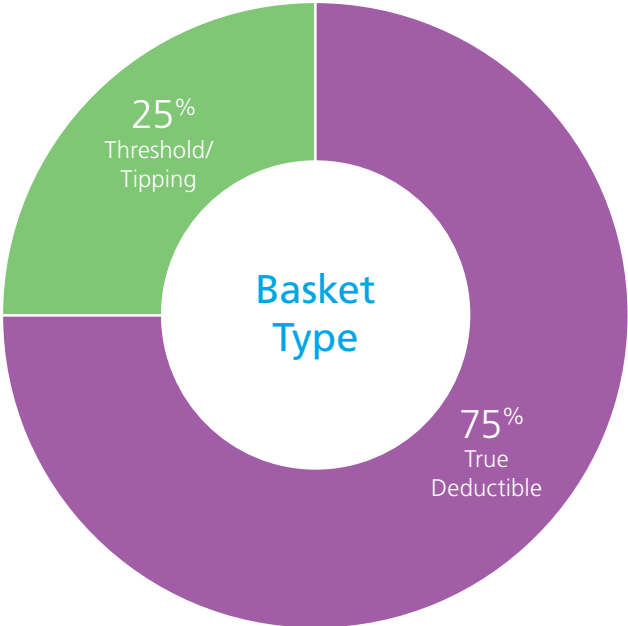
Approximately 72% of deals surveyed involving the purchase of equity interests carved out representations and warranties regarding capitalization from the general survival period.

### Title to Assets

Approximately 51% of deals surveyed involving the purchase of assets carved out representations and warranties regarding title to assets from the general survival period.

# Indemnity Basket Type

Approximately 89% of deals surveyed provided for an indemnity basket, broken down as follows:

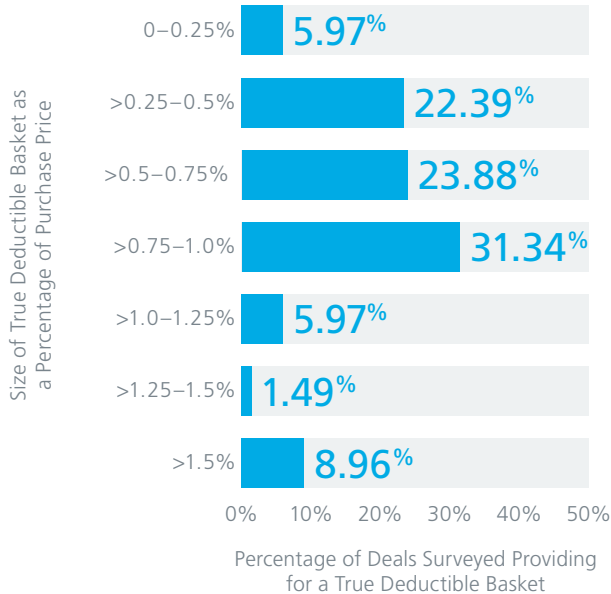


## Observations

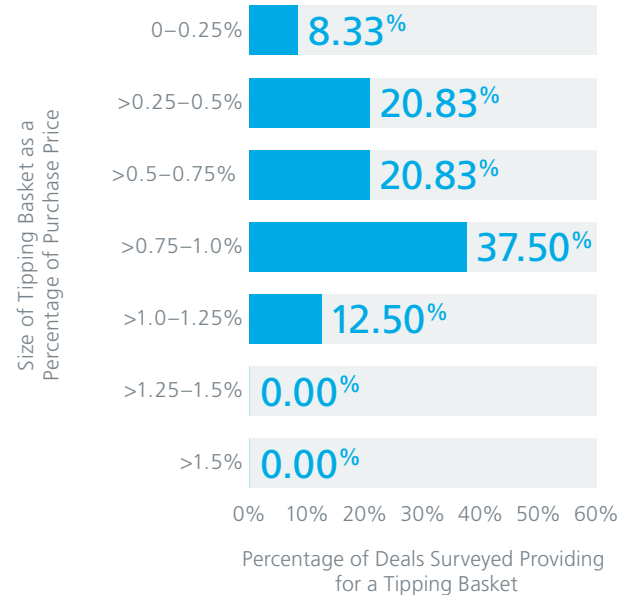
- Approximately 89% of deals surveyed provided for an indemnity basket (compared to 91% in 2014 and 97% in 2013).
- True deductible basket types fell from approximately 83% in 2014 and 82% in 2013 to approximately 75% in 2015. Accordingly, the use of threshold/tipping basket types increased in 2015 when compared to 2014 and 2013.

# Indemnity Basket Size

## True Deductible Basket Size



## Threshold/Tipping Basket Size

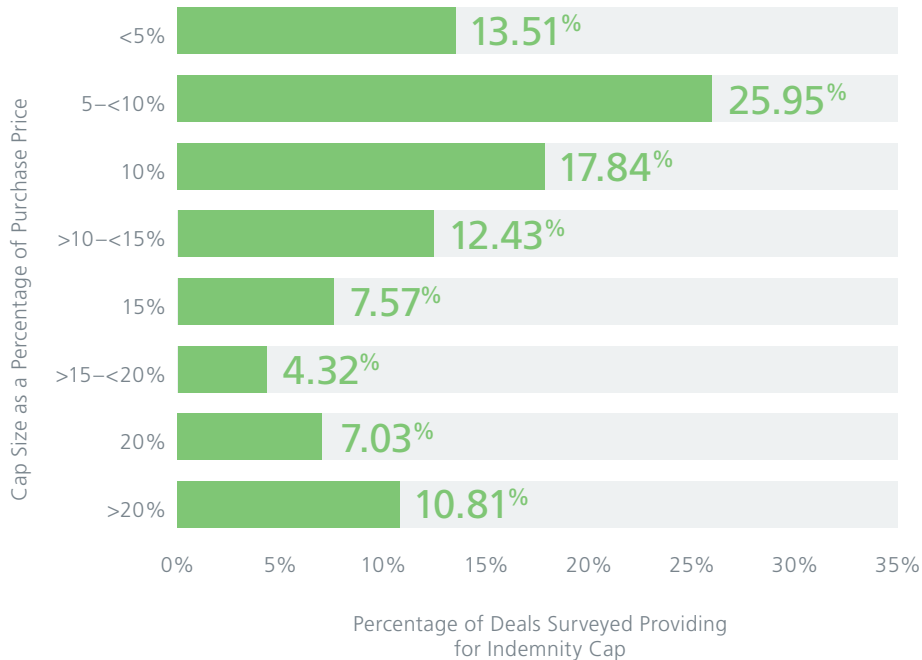


## Observations

- Median basket size remained about the same at 0.75% of the purchase price in 2015 (compared to 0.76% in 2014).
- The median basket size for deals surveyed having a true deductible was 0.84% of the purchase price in 2015 (compared to 0.80% in 2014).
- The median basket size for deals surveyed having a threshold/tipping basket was 0.72% of the purchase price in 2015 (compared to 0.73% in 2014).
- Approximately 72% of deductible baskets were greater than 0.5% of the purchase price (compared to 70% in 2014).
- The percentage of deals with a true deductible basket size of 1% or less was approximately 84% (compared to 75% in 2014).

# Indemnity Cap Size

Approximately 93% of deals surveyed had an indemnity cap.



## Observations

- Median indemnity cap remained unchanged since 2013 at 10%.
- Approximately 57% of transactions in 2015 had a cap of 10% or less (compared to 51% in 2014 and 50% in 2013).
- Approximately 14% of deals surveyed had an indemnity cap of less than 5% of the purchase price, which represents an increase from 2014 when 10% of deals surveyed had indemnity caps of less than 5% of the purchase price.

# Glossary

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## Indemnity Escrow Amount

The indemnity escrow amount is the portion of the purchase price held in escrow to serve as a fund to satisfy indemnification claims against the seller.

## Indemnity Escrow Period

The indemnity escrow period is the length of time after the transaction closing date that the indemnity escrow amount is held before being released to the seller.

## Representation & Warranty Survival Period

The survival period is the length of time after the transaction closing date during which a party may make claims for breaches of representations and warranties.

## Carve Outs to General Survival Period

Certain specified representations and warranties may be carved out of the general survival period for representations and warranties and survive for a longer period of time.

## Indemnity Basket

An indemnity basket requires a party to incur a certain amount of indemnifiable losses before it can seek indemnification from the other party. There are generally two types of baskets: **true deductibles** and **threshold/tipping baskets**. With a true deductible, the indemnifying party is only responsible for losses exceeding the basket amount. With a threshold/tipping basket, the indemnifying party is responsible for all losses from dollar one once a party's indemnifiable losses reach the basket amount. Indemnity baskets typically apply only to breaches of "general" representations and warranties.

## Indemnity Cap

The indemnity cap limits a party's maximum liability under the indemnification provisions to a stated dollar amount. Indemnity caps typically only apply to breaches of "general" representations and warranties.

# Accolades

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Recognized as a leading middle-market M&A (sub-\$500m) practice by *Legal 500* since 2012 and shortlisted for its 2015 US Practice of the Year Award in the M&A Corporate and Commercial: Mid-Market category.



*Law360* ranked us among the top 100 U.S.-based firms with the most merger and acquisition partners globally.



*U.S. News & World Report: Best Lawyers  
2016 "Best Law Firms" recognized  
Seyfarth's Corporate Law practice.*



Finance Monthly's Deal Maker  
of the Year Awards 2015  
recognized Seyfarth's work as  
M&A counsel to Wilson Sporting  
Goods during their acquisition  
of the Louisville Slugger Brand.

# For More Information

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Disclaimer: The acquisition agreement provisions that form the basis of this Survey are drafted in many different ways and do not always fit precisely into particular “data point” categories. Therefore, Seyfarth Shaw LLP has had to make various judgment calls regarding how to categorize certain provisions and has rounded certain figures for ease of presentation. As a result, the conclusions presented in this Survey may be subject to important qualifications that are not expressly articulated in this Survey. The findings presented in this Survey do not necessarily reflect the views of Seyfarth Shaw. In addition, while Seyfarth Shaw gathers its data from sources it considers reliable, it does not guarantee the accuracy or completeness of the information provided within this Survey. Seyfarth Shaw makes no representations or warranties, expressed or implied, regarding the accuracy of this material.

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