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Middle-Market
M&A
SurveyBook

2017 Survey of Key M&A Deal Terms

Introduction

Seyfarth Shaw LLP is pleased to present the 4th edition of its Middle-Market M&A SurveyBook (“Survey”) which analyzes key transaction terms included in over 150 middle-market (i.e., transactions with a purchase price of less than \$1 billion) private target acquisition agreements signed in 2016.¹ 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 2017.

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 while the current M&A environment is still trending to be more favorable to sellers as has been the case over the past two years, there are indications to suggest that certain terms are slightly less seller favorable than 2015. For example, our Survey data shows an increase in the median escrow period, an increase in the

number of deals with an indemnity escrow amount of 10% or more, an increase in the median escrow amount, and an increase in the use of tipping baskets as opposed to a true deductible.

The competition among buyers searching to acquire quality assets continues to be fierce and the purchase of representation and warranty insurance continues to be a powerful tool used by buyers in an effort to make their acquisition proposal more attractive to a seller by significantly limiting potential post-closing liability of the seller.

North American middle-market M&A deal volume and deal value declined 17.98% and 8.69%, respectively, in 2016.² It appears that a key driver for the reduction in deal activity was political uncertainty prior to the U.S. election, which is not unusual in an election year, and post-election uncertainty regarding the incoming Trump administration’s policies in the areas of taxation, interest rates and financial industry regulation, among others. It is important to note, however, that M&A activity in the last couple of years was at or near record highs and consequently 2016 was still a solid year for M&A despite the declines noted above.

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 and help answer the question of “what’s market?”. Our Survey provides you with data on these key terms, together with our insights, in an easily readable format as a quick reference guide to assist you in 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.

¹For 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.

²Source: S&P Capital IQ.

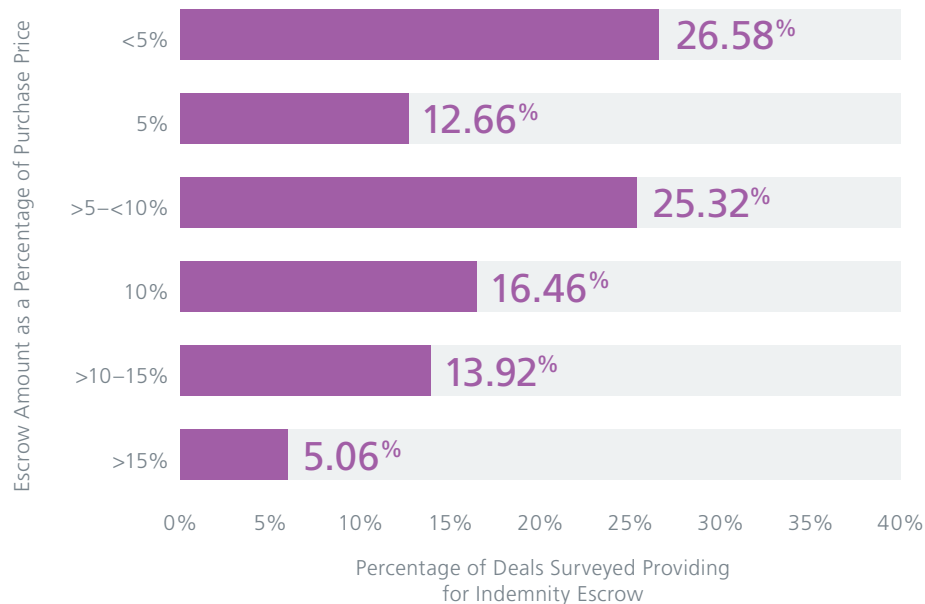
Key Deal Terms Surveyed*

- 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 55% of all deals surveyed provided for an indemnity escrow.



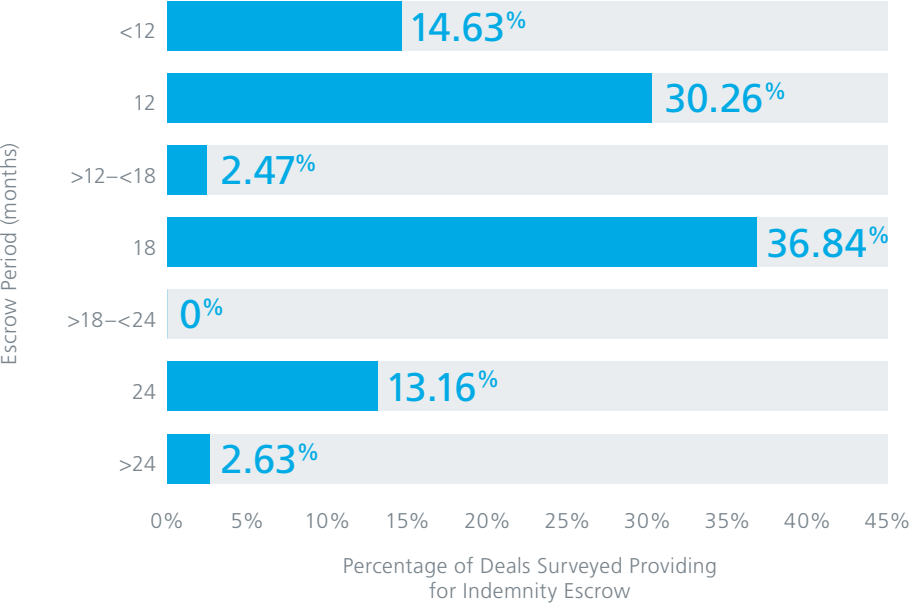
Observations*

Of the deals surveyed which provided for an indemnity escrow:

- The median indemnity escrow amount in 2016 was 8% of the purchase price (compared to 6% in 2015, 7.41% in 2014, and 8.78% in 2013).
- Approximately 65% had an indemnity escrow amount of less than 10% (compared to 76% in 2015, 59% in 2014, and 48% in 2013).
- Approximately 27% had indemnity escrow amounts of less than 5% (compared to 31% in 2015, and 21% in 2014). As recently as 2013, only 16% of deals had indemnity escrow amounts of less than 5%.

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

Indemnity Escrow Period

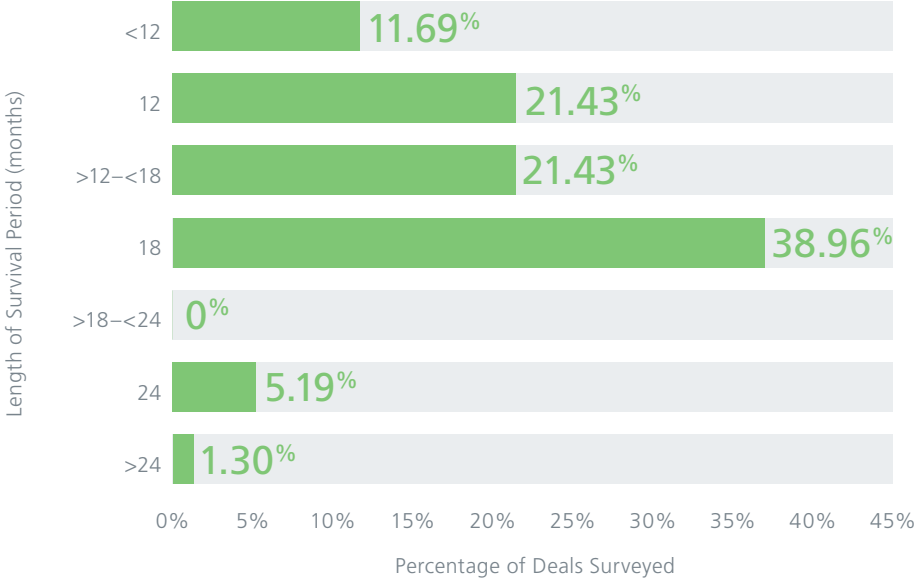


Observations

Of the deals surveyed which provided for an indemnity escrow:

- The median indemnity escrow period increased slightly in 2016 to 18 months (compared to 16.5 months in 2015 and 15 months in 2014 and 2013).
- The percentage of deals with an indemnity escrow period of 12 months or less remained relatively unchanged at approximately 45% in 2016 compared to 46% in 2015. This percentage has steadily increased since 2013 when the percentage of deals with an indemnity escrow period of 12 months or less was only 34%.
- The percentage of deals with an indemnity escrow period of 24 months or greater increased to approximately 16% in 2016 as compared to 13% in 2015 and 11% in 2014.

Representation & Warranty Survival Period*

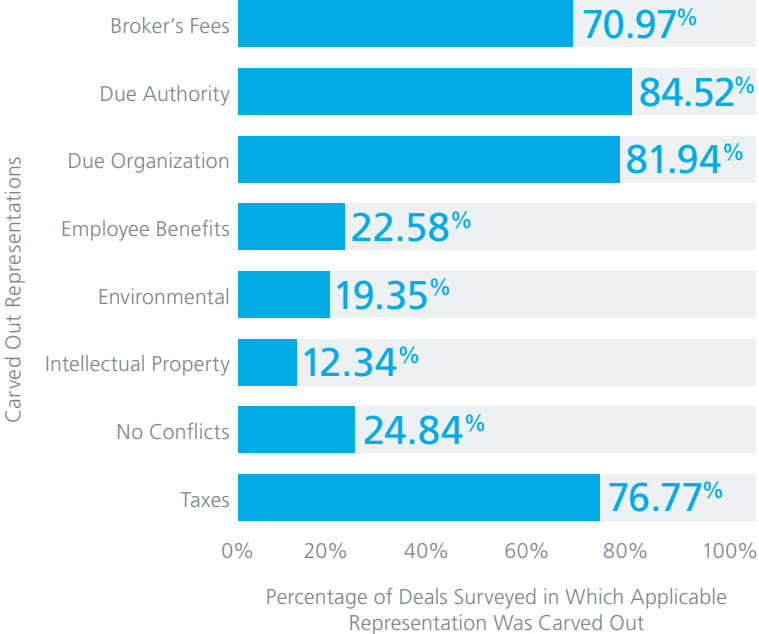


Observations

- The median survival period for deals surveyed was 15 months, which has remained consistent since 2013.
- Approximately 82% of deals surveyed had survival periods from 12 to 18 months, representing a slight increase when compared to 80% in 2015 and 78% in 2014.
- Approximately 39% of deals surveyed had a survival period of 18 months, representing a continued increasing trend when compared to 36% in 2015 and 32% in 2014.

*For purposes of this Survey, the survival periods set forth in this chart are 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



Employee Benefits and Environmental

- The percentage of deals surveyed that carved out representations and warranties regarding employee benefits was approximately 23% in 2016 compared to 28% in 2015.
- The percentage of deals surveyed that carved out representations and warranties regarding environmental matters was approximately 19% in 2016, which has been on a steady decline since 2013 when it was 30%.

Other Carved Out Representations Capitalization

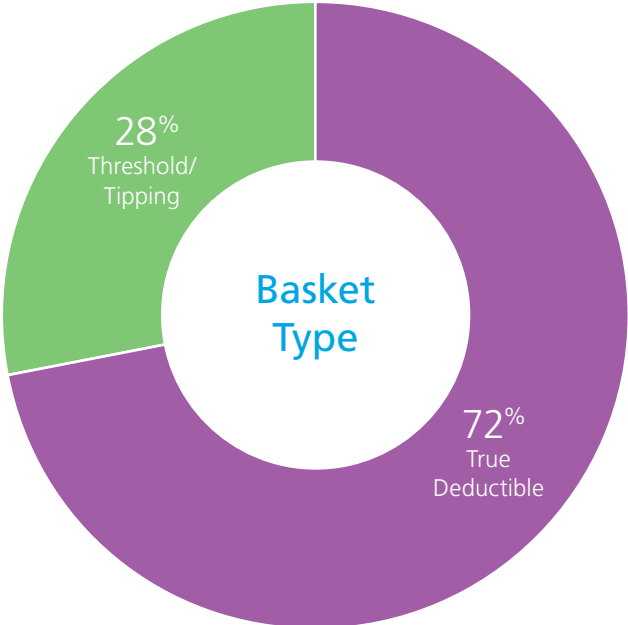
Approximately 75% of deals surveyed involving the purchase of equity interests carved out representations and warranties regarding capitalization from the general survival period (compared to 72% in 2015).

Title to Assets

Approximately 67% of deals surveyed involving the purchase of assets carved out representations and warranties regarding title to assets from the general survival period (compared to 51% in 2015).

Indemnity Basket Type

Approximately 91% of deals surveyed provided for an indemnity basket, broken down as follows:

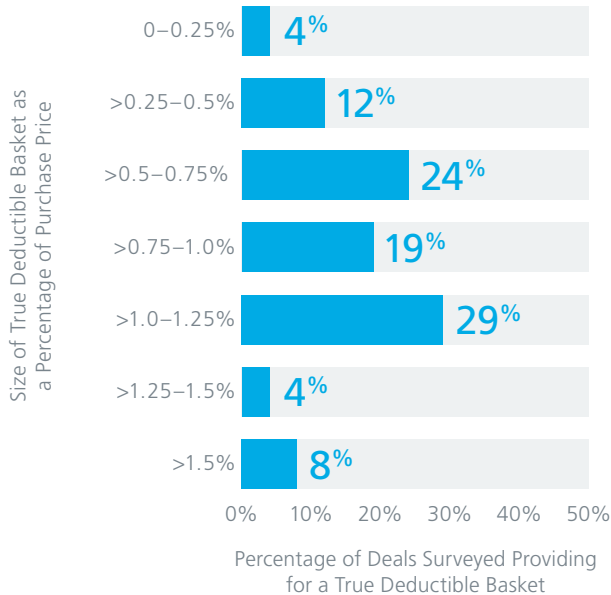


Observations

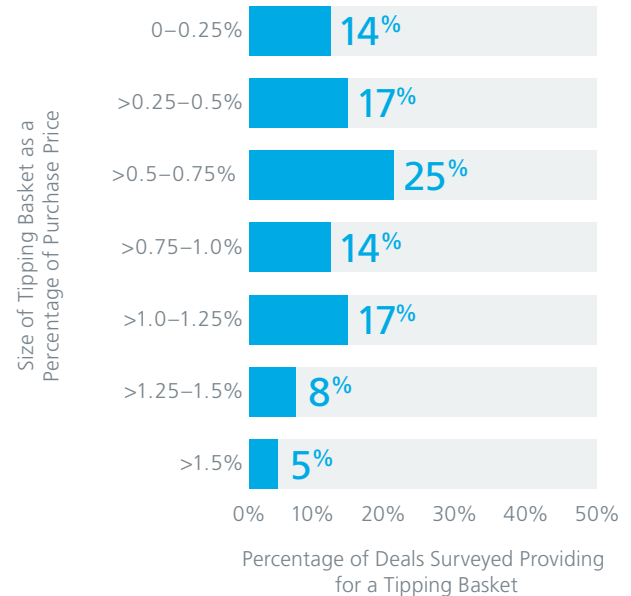
- Approximately 91% of deals surveyed provided for an indemnity basket (compared to 89% in 2015, 91% in 2014 and 97% in 2013).
- The use of true deductible basket types decreased to approximately 72% of deals with baskets in 2016 from approximately 75% of deals with baskets in 2015. Accordingly, the use of threshold/tipping baskets increased to approximately 28% in 2016 from approximately 25% in 2015.

Indemnity Basket Size

True Deductible Basket Size



Threshold/Tipping Basket Size

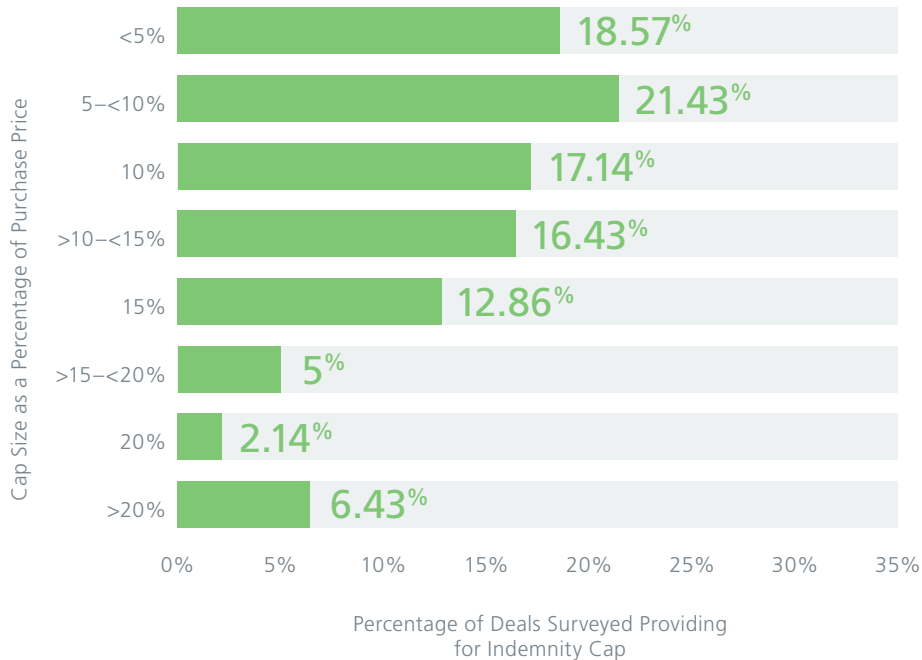


Observations

- Median basket size remained unchanged from 2015 at 0.75% of the purchase price.
- The median basket size for deals surveyed having a true deductible was 0.82% of the purchase price in 2016 (compared to 0.84% in 2015).
- The median basket size for deals surveyed having a threshold/tipping basket was 0.53% of the purchase price in 2016, a significant decrease from 0.72% in 2015.
- Approximately 84% of true deductible baskets were greater than 0.5% of the purchase price (compared to 72% in 2015), and approximately 41% of such baskets were greater than 1% of the purchase price (compared to 16% in 2015).

Indemnity Cap Size

Approximately 93% of deals surveyed had an indemnity cap.



Observations

- Median indemnity cap continues to remain unchanged since 2013 at 10%.
- Approximately 57% of transactions in 2016 had a cap of 10% or less, unchanged from 2015.
- Approximately 19% of deals surveyed had an indemnity cap of less than 5% of the purchase price, which represents an increase from 2015 when 14% of deals surveyed had indemnity caps of less than 5% of the purchase price.

Glossary

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.

Seyfarth's Leading Middle-Market M&A Practice



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



Recognized as a leading middle-market M&A (sub-\$500m) practice by *The 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.



U.S. News & World Report: Best Lawyers 2017 "Best Law Firms" recognized Seyfarth's Corporate Law and Mergers & Acquisitions Law practices.

The Seyfarth team “works with clients to help them build their businesses in an efficient and high-quality manner.”

– Client quote, *The Legal 500* (2016)

Seyfarth’s “counsel during M&A procedures is consistently accurate and timely, and the team’s knowledge and expertise proves invaluable.”

– Client quote, *The Legal 500* (2016)

“M&A knowledge is deep, and the team is extremely responsive; it is pretty much on call for clients 24/7 and brings together all the firm’s resources to meet clients’ needs.”

– Client quote, *The Legal 500* (2015)

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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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