



M&A INDEMNIFICATION SURVEY



2017 SURVEY OF KEY M&A INDEMNIFICATION DEAL TERMS

We are pleased to present the findings from our 2017 survey of key M&A indemnification deal terms.

Our Methodology

This study analyzes the key indemnification terms of 100 publicly filed acquisition agreements dated between June 1, 2016, and August 16, 2017, with values between \$100 million and \$4.6 billion. The median deal size was \$250 million.

For this survey, we collected a sampling of asset purchase, stock purchase and merger agreements publicly filed with the U.S. Securities and Exchange Commission in which the target was a privately held business (including subsidiaries of public companies) and the buyer negotiated an indemnification remedy for breaches of representations, warranties and covenants that continued after the closing date.

While we note that our review and analysis are not technically scientific and do not include private transactions for which no agreement is publically available, we believe that the results generally reflect the climate of M&A transactions during the period.



Key Data Points Surveyed

The key data points that we analyzed in our survey included the following:



Survival Periods

Carve Outs to General Survival Period

Classification of Fundamental Representations

Indemnity Baskets and Caps

Materiality Scrapes

Exclusions from Indemnifiable Damages

Net of Insurance Clauses

Sandbagging Clauses

The **Key Findings** from our survey included the following:

MEDIAN SURVIVAL PERIOD WAS **18 MONTHS**

MEDIAN BASKET SIZE WAS **0.40%** OF THE PURCHASE PRICE

MEDIAN INDEMNITY CAP SIZE WAS **10%** OF THE PURCHASE PRICE

75% OF THE DEALS SURVEYED INCLUDED A MATERIALITY SCRAPE AND **40%** OF THE DEALS SURVEYED INCLUDED A DOUBLE MATERIALITY SCRAPE

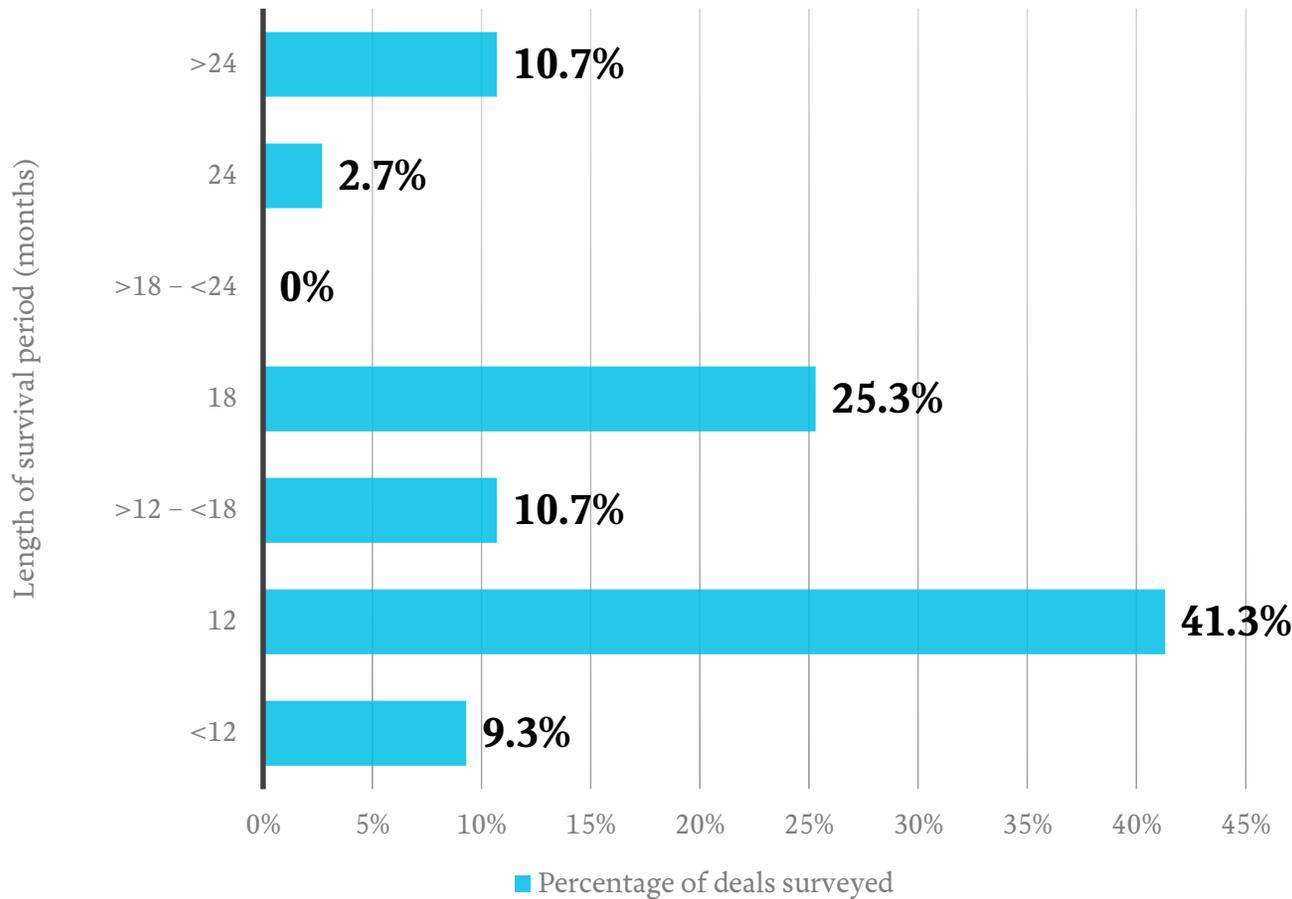
42% OF THE DEALS SURVEYED EXPRESSLY EXCLUDED CONSEQUENTIAL DAMAGES FROM INDEMNIFIABLE DAMAGES

ONLY 8% OF THE DEALS SURVEYED EXPRESSLY INCLUDED DIMINUTION IN VALUE IN THE DEFINITION OF INDEMNIFIABLE DAMAGES

75% OF THE DEALS SURVEYED WERE SILENT WITH REGARD TO SANDBAGGING



REPRESENTATION & WARRANTY GENERAL SURVIVAL PERIOD

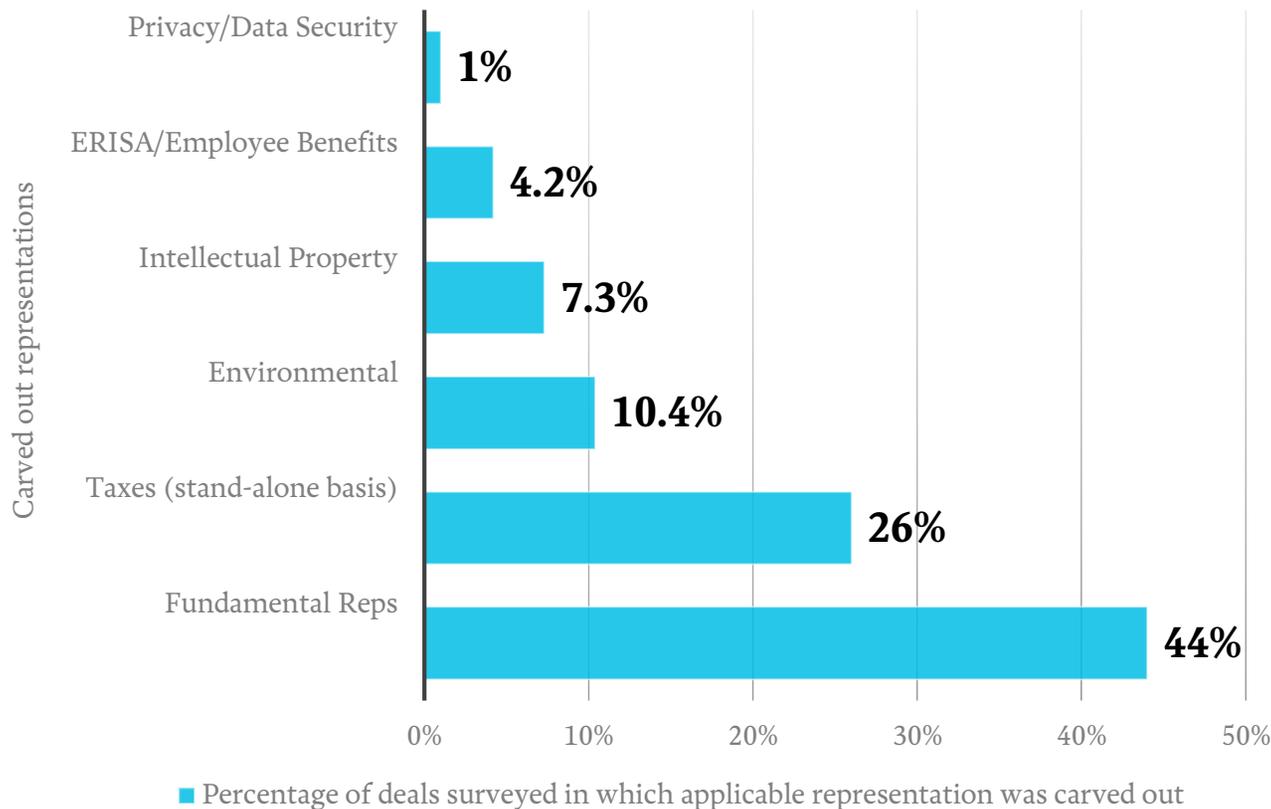


Comments

- For purposes of this survey, the survival periods set forth in this chart are for general representations and warranties. For certain representations that are sometimes carved out of the general survival period, see page 6.
- Approximately 77% of deals surveyed had survival periods of from 12 to 18 months.
- The median survival period for deals surveyed was 18 months; the shortest survival period was six (6) months; and the longest survival period was 72 months.



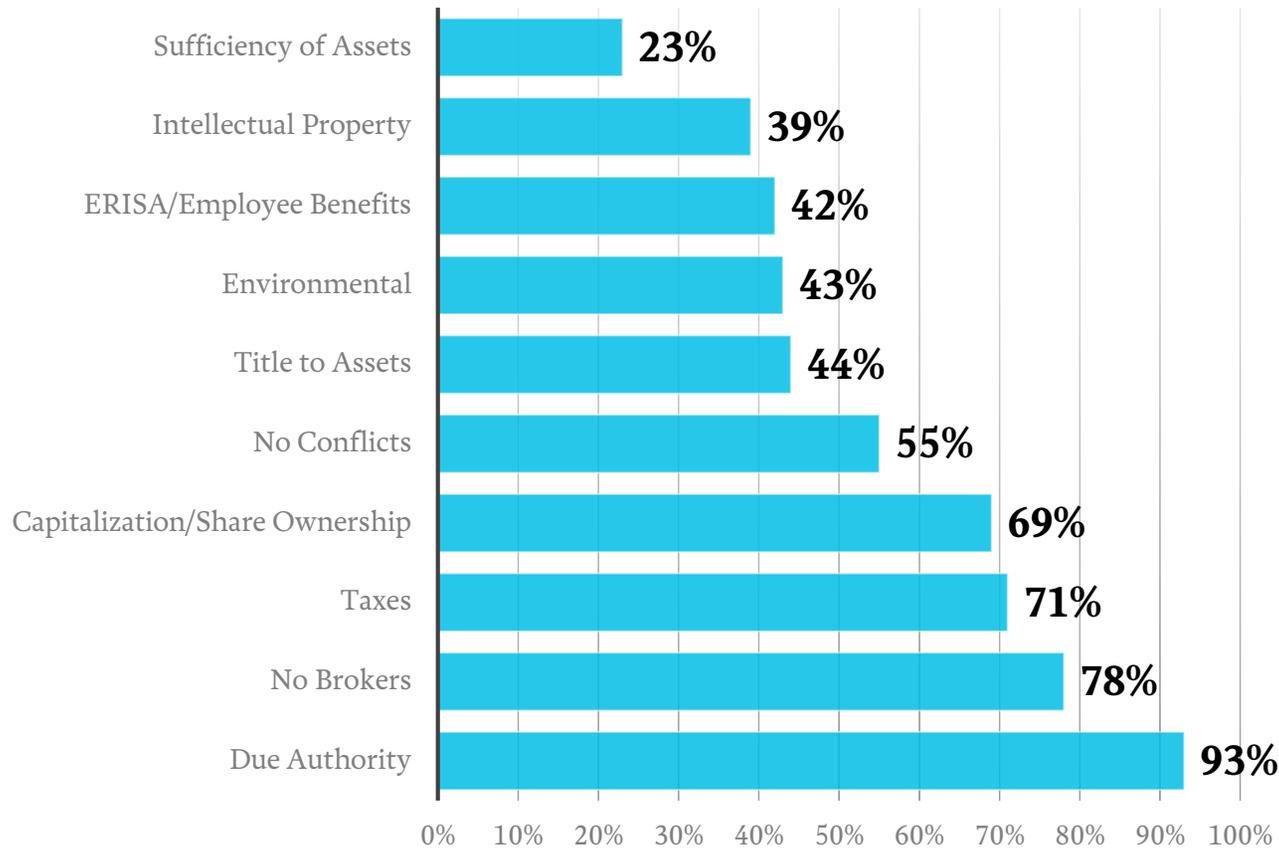
CARVE OUTS TO GENERAL SURVIVAL PERIOD



Comments

- In a majority of the deals surveyed, the “Fundamental Representations” included the seller’s representations relating to due authorization, no brokers, capitalization/share ownership and taxes, see page 7.
- In approximately 37% of the deals surveyed, no representations and warranties were carved out of the general survival period.
- The tax representation was included in the definition of a “Fundamental Representation” in 71% of the deals surveyed and, on a stand-alone basis, as a carve out to the general survival period in an additional 26% of the deals surveyed.

FUNDAMENTAL REPRESENTATIONS & WARRANTIES



■ Percentage of Deals Surveyed in which the Applicable Representation was included as a Fundamental Representation

Comments

- Fundamental Representations & Warranties of the seller consist of those key representations needed to insure that the buyer obtains the benefit of its bargain.
- Fundamental Representations & Warranties are often carved out from the general survival period, indemnification basket and indemnification cap.



COVENANT SURVIVAL PERIOD

In approximately 60% of the deals surveyed, no time limit was specified as to when the buyer would be entitled to bring a claim based on a breach of covenant by the seller.

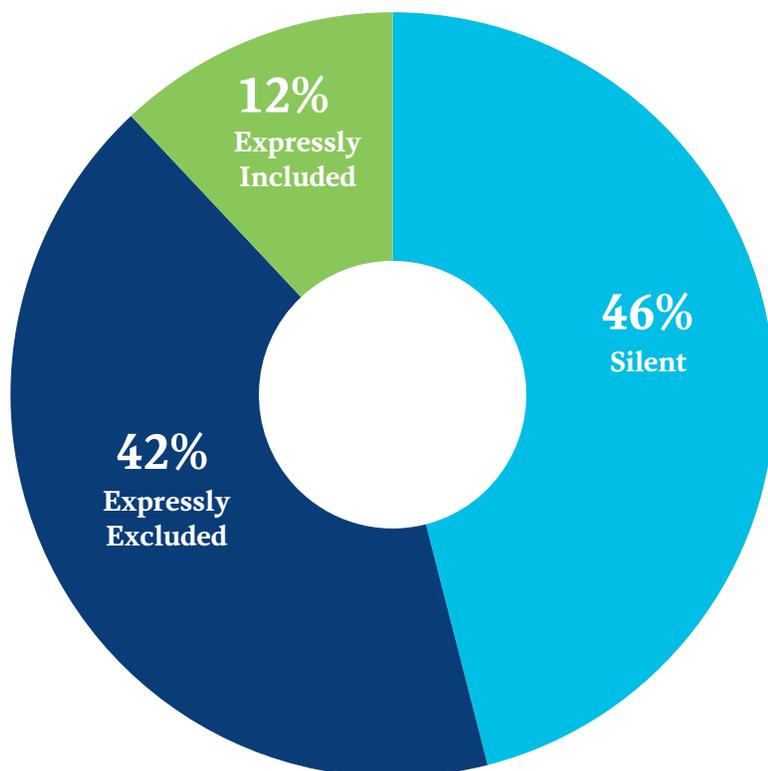
An additional 25% of the deals surveyed provided that such claims must be brought prior to the expiration of the applicable statute of limitations.

The median covenant survival time period was 36 months for those few deals in which a time period was specified by the parties.



EXCLUSIONS FROM INDEMNIFIABLE DAMAGES

Consequential Damages as an element of Damages

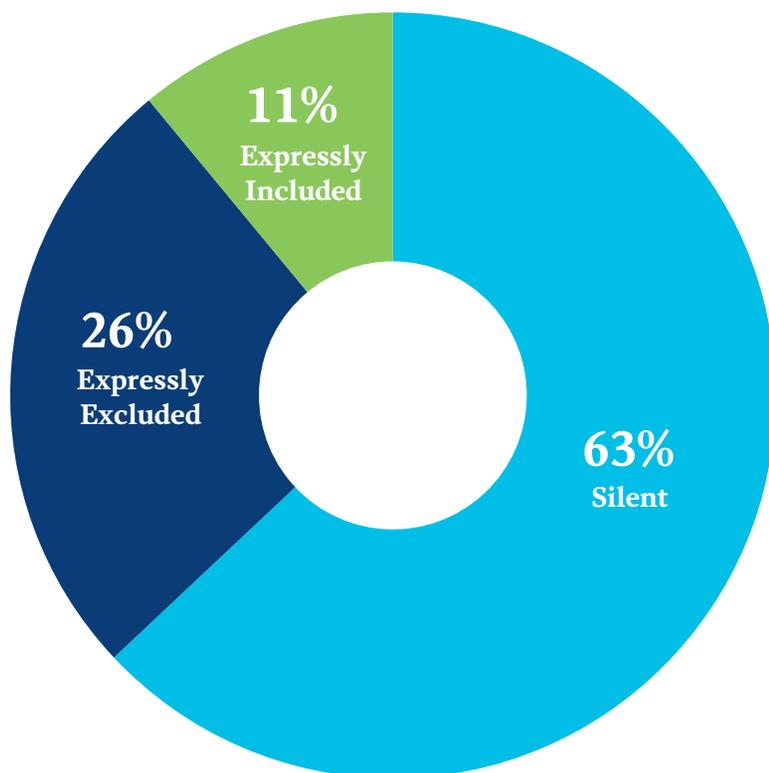


Comments

- Consequential damages compensate the buyer for actual losses resulting from a breach of the seller's representations or warranties.
- However, determining what are "consequential" damages and what are direct or general damages remains difficult to apply in practice. (See *Biotronik A.G. vs. Conor MedSystems Ireland Ltd.* (NY Ct. of Appeals, March 27, 2014).
- In approximately 30% of the deals surveyed, there was an exception to the waiver with respect to damages paid by the buyer to a third-party. As a result, these third-party damages could be recouped from the seller notwithstanding an express exclusion of consequential damages in the acquisition agreement.

EXCLUSIONS FROM INDEMNIFIABLE DAMAGES

Loss of Revenue, Income or Profits as an element of Damages

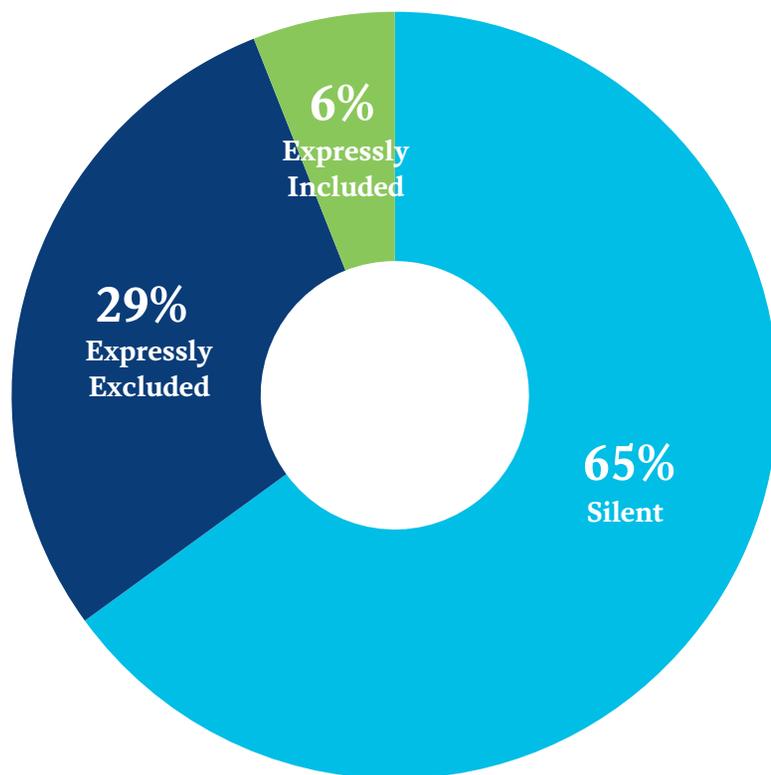


Comments

- When the buyer's ability to recover for loss of revenue, income or profits is excluded separately from indemnifiable damages (and not as an example of consequential damages), the buyer would be unable to recover even when the loss of revenue, income or profit was the direct result of the seller's breach.
- For example, if the seller made material misrepresentations relating to the existence of an income-producing contract when the contract had in fact been terminated by its customer, the loss of revenue, income or profits might reasonably be considered direct damages that would not be excluded by a consequential damage waiver, but the damages would be excluded if this separate clause relating to loss of revenue, income or profits was included.

EXCLUSIONS FROM INDEMNIFIABLE DAMAGES

Incidental Damages as an element of Damages



Comments

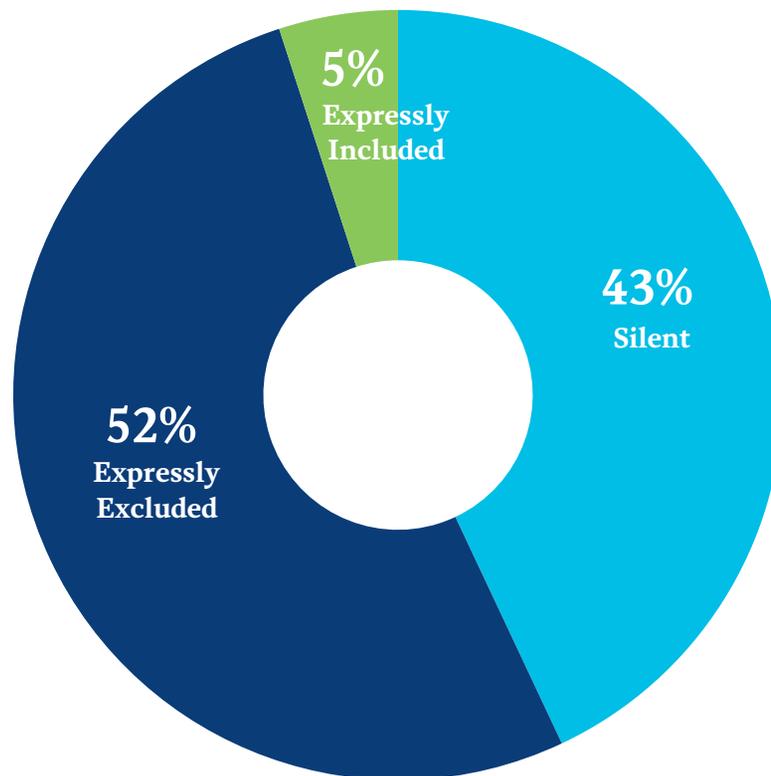
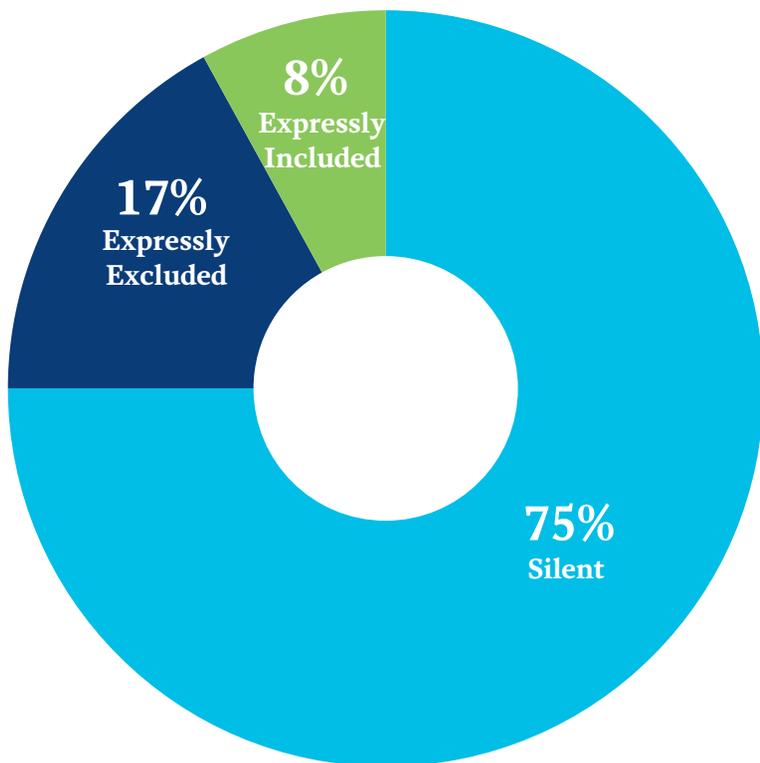
- Incidental damages include expenses incurred by the non-breaching party to avoid other losses caused by the breach.



EXCLUSIONS FROM INDEMNIFIABLE DAMAGES

Diminution in Value as an element of Damages

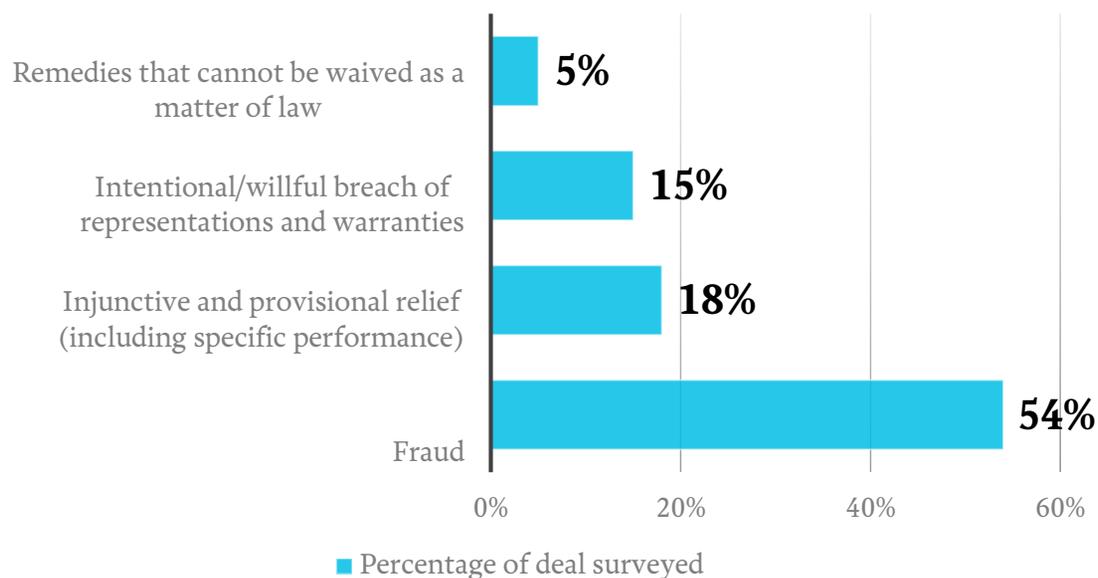
Punitive Damages as an element of Damages



INDEMNIFICATION AS EXCLUSIVE REMEDY

In 80% of the deals surveyed, the indemnification article of the acquisition agreement was the exclusive remedy for breaches of the acquisition agreement.

Common carve-outs to the exclusive remedies clause included the following:



Comments

- In those cases in which the indemnification article does not provide the exclusive remedy, the buyer would be entitled to recover all damages arising from the breach without regard to any baskets, caps or exclusions from indemnifiable damages or other seller-favorable limitation of liability provisions.

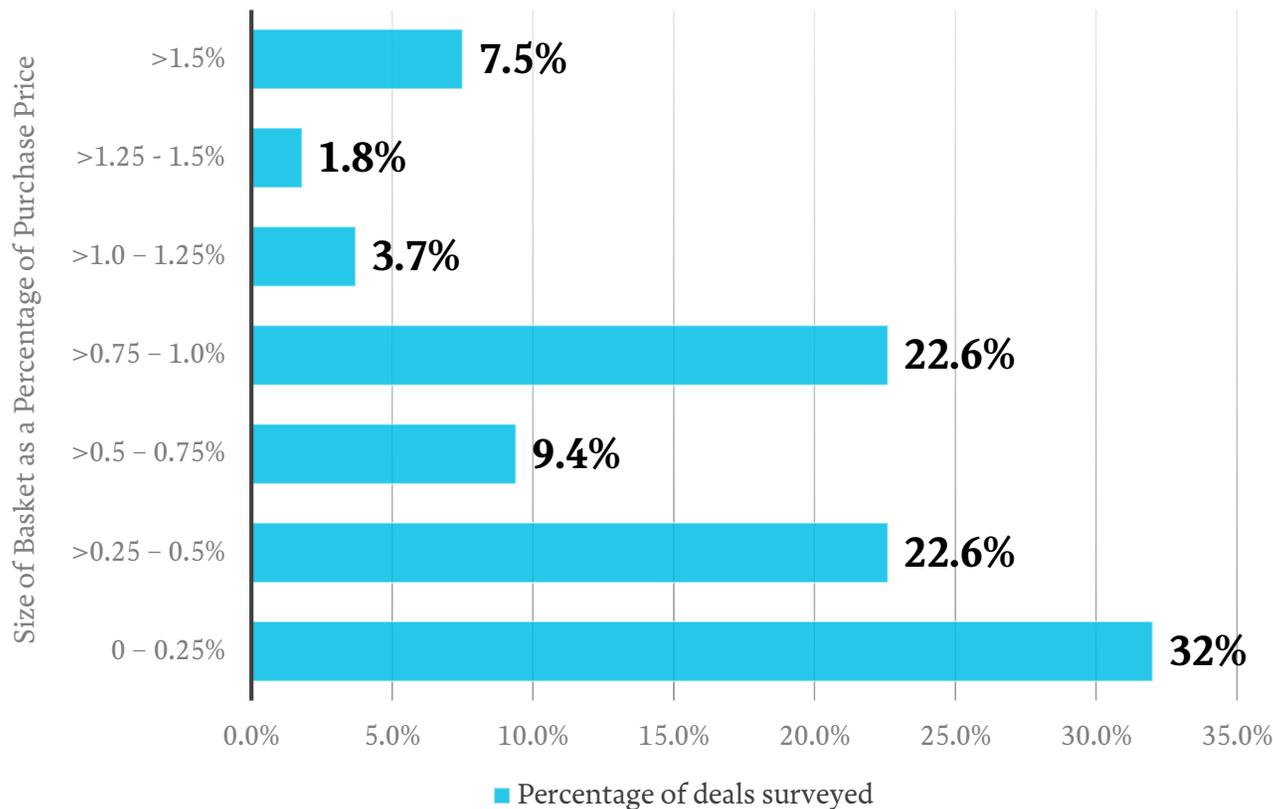
INDEMNIFICATION NET OF INSURANCE

In 62% of the deals surveyed, the damages recoverable by an indemnified party are calculated net of any insurance proceeds received by the indemnified party on account of such loss or damage.

However, only 35% of those deals that provided that the damages recoverable would be calculated net of insurance imposed an affirmative obligation on the indemnified party to use commercially reasonable efforts (or a similar undertaking) to seek a recovery under the insurance policies covering the loss.



INDEMNITY BASKET SIZE

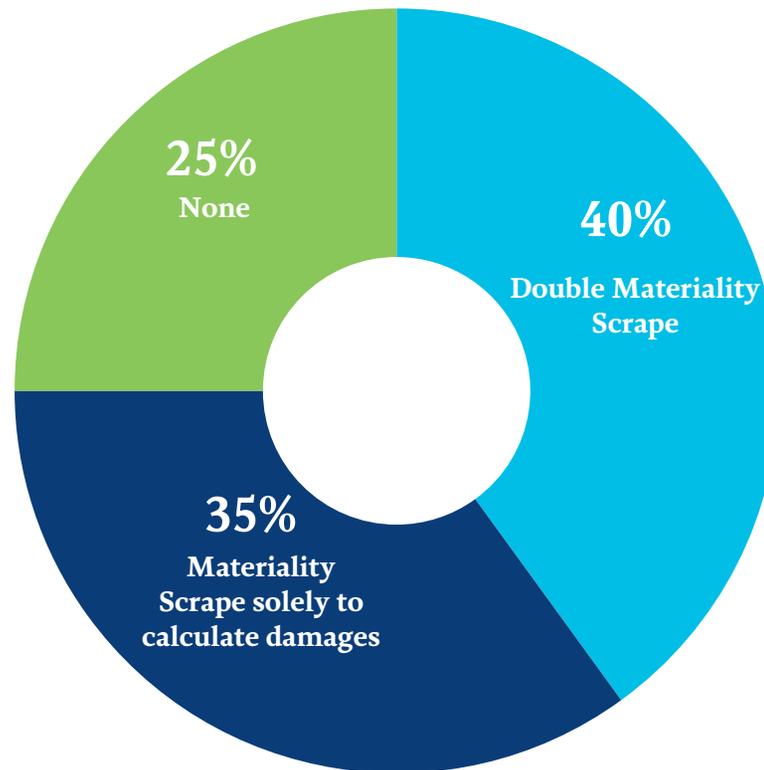


Comments

- The median basket size was 0.40% of the Purchase Price.
- In a majority of the deals surveyed, the basket size did not exceed 0.50% of the purchase price, which is substantially lower than the average basket of all types included in prior deal surveys conducted by SRS and the ABA for 2012–2015. (See 2016 SRS Acquiom M&A Deal Terms Study, analyzing private target deals between 2012 and the end of 2015; and 2014 ABA Private Target Mergers & Acquisitions Deal Points Study).

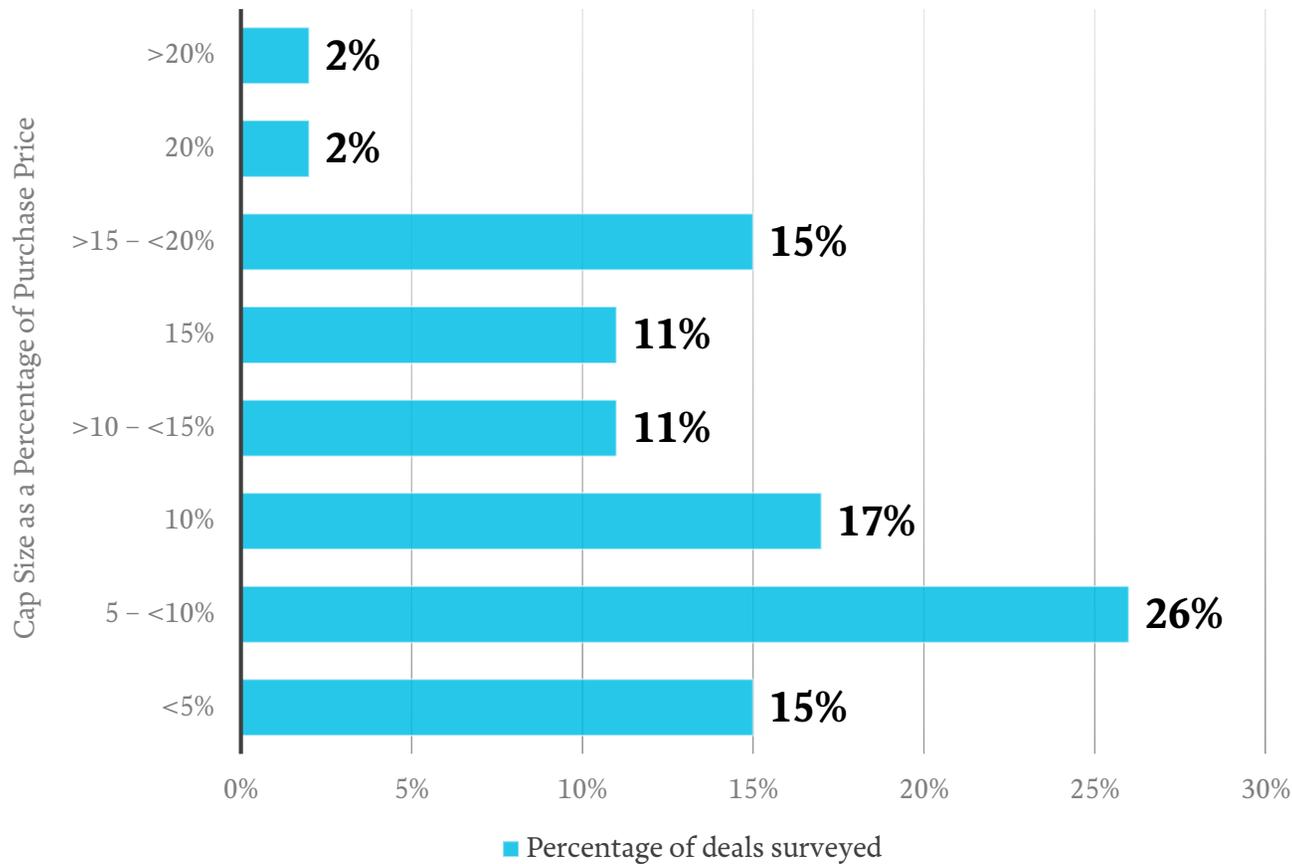
MATERIALITY SCRAPE

Approximately 75% of the deals surveyed included a materiality scrape provision. In approximately 40% of the total deals surveyed, the materiality scrape clause was used both for the purpose of calculating the amount of losses or damages **and** for determining whether a breach of a representation or warranty has occurred. This type of double materiality scrape is a buyer-friendly provision.



INDEMNITY CAP SIZE

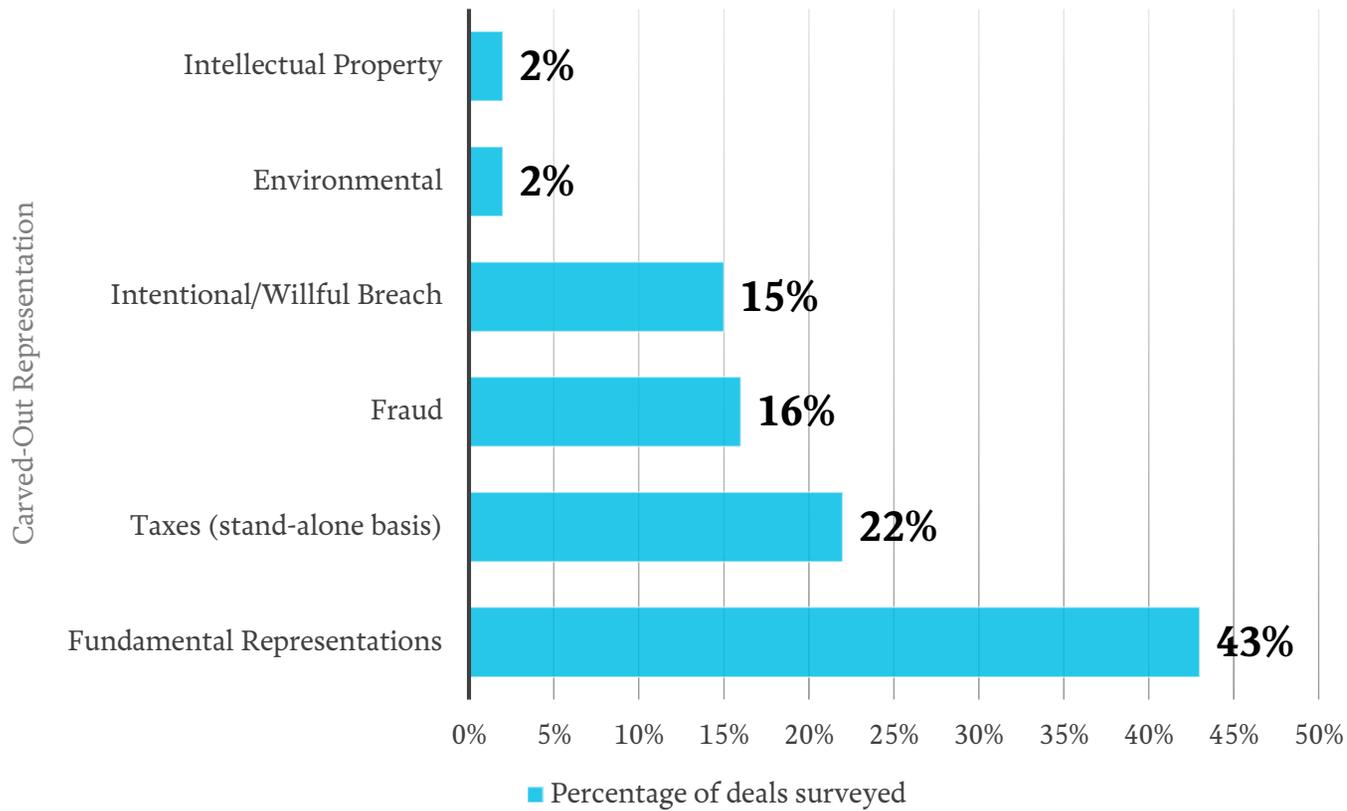
Approximately 76% of the deals surveyed had an indemnity cap.
The median cap size was 10%.



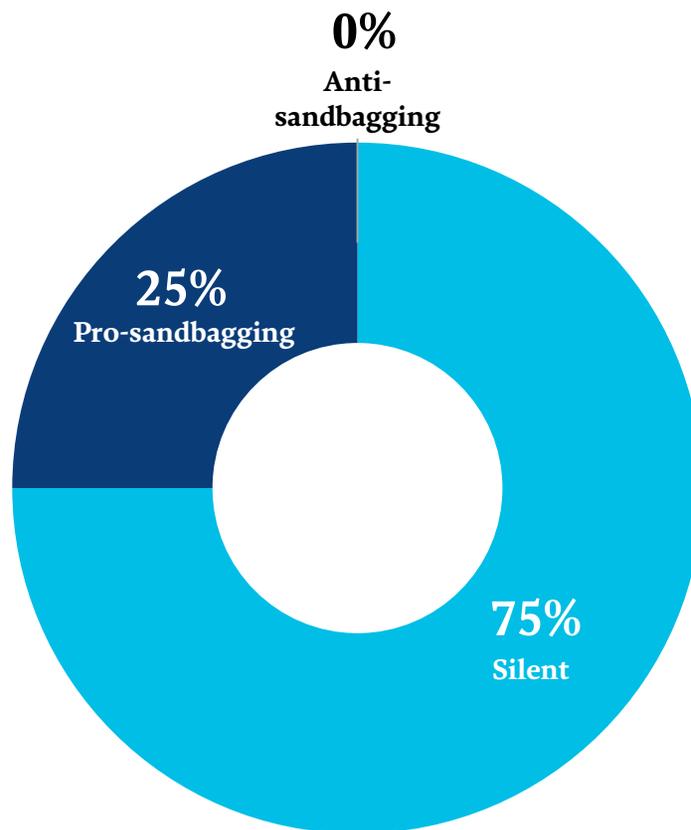
Comments

- Approximately 58% of transactions that included an indemnity cap had a cap of 10% or less.

INDEMNITY CAP CARVE-OUTS



SANDBAGGING CLAUSES



Comments

- Pro-sandbagging clauses (or knowledge savings clauses) expressly provide that the buyer's indemnification or other remedy is not affected by any knowledge of the buyer.
- Anti-sandbagging clauses limit the seller's liability for losses resulting from breaches of representations or warranties if the buyer had knowledge of the breach. None of the deals surveyed included an anti-sandbagging clause.
- In some jurisdictions (notably New York), there is a risk of a waiver if the buyer closes over a known breach of representation by the seller unless the buyer's rights are preserved in the acquisition agreement or an ancillary agreement.

WHAT OUR CLIENTS SAY...

Below are some quotes from our recent *Chambers USA* rankings.

“They **relate to the business side** of the thought process. They don’t approach it from a legal perspective, **they understand the nuances of the deal.**”

“We like them particularly because they are **thorough and sensitive** to the kinds of deals we do.”

“They are very **proactive** and have a **very good understanding of our business**. It is that understanding that makes their advice impactful.”

“Very good; they are very knowledgeable, they have **top-notch attorneys** and are **very responsive.**”

“My overall impression is excellent. I would definitely recommend them, especially because of their willingness to **control costs while still providing top-tier results.**”

“They do a really good job of trying to **handle everything we do**. We are very specialized and they do a good effort of **getting themselves up to speed.**”

“Their **client service is excellent**. They are very responsive; if we send an e-mail or call it always gets answered the same day. They are exemplary on that front.”

“They are willing to make time and provide solutions and options. Their different specialties provide a **broad array of expertise when needed.**”

“There have been many significant changes in our business market and Nixon Peabody has guided us through all of them very skillfully. **Their advice and counsel has been invaluable.**”

“The team was outstanding in **client service, value** for money, **transparency** and **working together.**”

“**They’re very practical and business-minded.** The first thing they want to know is what we are trying to accomplish from a business perspective.”



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ABOUT NIXON PEABODY

We see 21st century law as a tool to help shape our clients' futures.

Our focus is on knowing what is important to our clients now and next so we can foresee obstacles and opportunities in their space and smooth the way. We ensure they are equipped with winning legal strategies as they navigate the exciting and challenging times we live in.

Our ability to do this comes from these working principles:

- We're curious and extremely focused on understanding our clients' businesses and industries.
- We tap the collective intelligence of Nixon Peabody to deliver the best thinking and create value for our clients throughout the world.
- We lean forward into the future, together with our clients, to see and prepare for what's ahead.

Working together, we handle complex challenges in litigation, real estate, corporate law, intellectual property and finance anywhere in the world.



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