

Business Transaction Marketplace

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Benchmarking Deal Points

In the [September 2012](#) issue of *Business Transaction MarketplaceSM*, we discussed certain terminologies that often appear in Purchase and Sale (P&S) Agreements. Many of those terms deal with the *allocation of risk* between the buyer and seller - we'll call them negotiated *deal points*. As was discussed in the [May 2007](#) issue of *Business Transaction MarketplaceSM*, one of the four propositions of principled negotiation is to use "objective criteria" to test the parties' deal point positions.



In this issue of *Business Transaction MarketplaceSM*, we'll list certain benchmarks from various deal point studies that can provide objective criteria to buyers, sellers and their advisors as they negotiate certain deal points in P&S Agreements.

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Sources of Objective Criteria



The following are the three (3) Studies used to obtain deal point benchmarks referenced in this article:

1. (ABA) 2011 Private Target Mergers & Acquisitions Deal Points Study, by the American Bar Association: (a) sampling of 100 public available acquisition agreements; (b) transaction value range \$25-960 million; (c) stock deals 83%; asset deals 17%; (d) seller makeup: entrepreneurial - 47%; financial - 45%; corporate - 8%
2. (SRS) 2012 SRS M&A Deal Terms Study, by Shareholder Representative Services: (a) sampling of 342 private target acquisitions; (b) median deal size was \$75 million; (c) 85% of the deals the buyer paid cash; (d) top 3 Industries: 22% software; 15% business products and services; 13% IT Services
3. (HL) 2011 Purchase Agreement Study, by Houlihan Lokey's Merger & Acquisitions Group: (a) middle market change of control transactions; (b) transaction value range \$10 million-\$1 billion; (c) stock deals 83%; asset deals 17%; (d) 90% of the deals the buyer paid cash; (e) buyers from 2002-2010: 61% strategic; 39% financial (of which 87% platform; 13% add-on)

Deal Point Benchmarks

The Tables below show the frequency (%) in which certain deal points appeared in P&S Agreements.



Earn-Outs: An agreement in the sale of a company where the buyer agrees to pay the seller consideration in the future (typically cash or stock) based upon certain future events or performance of the business post-close. Because earn-out payments are contingent on the future performance of the acquired company, they are not included in the purchase price (see the [September 2009](#) issue of *Business Transaction MarketplaceSM* for a further discussion of earn-outs).

	Table 1 - Earn-out Metric			Table 2 - Earn-out Period			
Deal Point	Revenue	Earnings /EBITDA	Gross Margin and Other	≤12 mos.	>12 and ≤24 mos.	>24 and ≤36 mos.	>36 mos.
ABA	37%	32%	31%	27%	30%	33%	10%
SRS	60%	20%	20%	20%	33%	13%	34%

Survival Period: The length of time (in months) after the closing date during which the representations and warranties must be true and the seller is responsible for indemnifying the buyer (e.g., claims by the buyer must be made on or before that date).

Table 3 - Representations and Warranties Survival Period				
Deal Point	≤12 mos.	>12 and ≤18 mos.	>18 mos.	Silent and Other
ABA	28%	48%	18%	6%
SRS	26%	59%	15%	-
HL	Median Survival Period - 18 months			

Basket: The dollar amount set forth as the minimum loss that must be suffered by the buyer before the buyer can recover damages under the indemnification provisions.

Deductible Basket: Seller is only responsible for damages exceeding the basket amount (e.g., under a deductible basket of \$100, if a claim of \$150 is made then the seller must pay \$50).

Dollar-One Basket (aka Tipping Basket): Seller is responsible for all damages once damages reach the threshold basket amount (e.g., under a dollar-one basket of \$100, if a claim of \$150 is made then the seller must pay \$150).

Deal Point	Table 4 - Basket Type			Table 5 - Basket % of Transaction Value		
	Deductible	Dollar-One	Combination	≤.5%	>.5% and ≤1%	>1%
ABA	59%	31%	10%	41%	47%	12%
SRS	37%	58%	5%	52%	40%	8%
HL	81%	19%	-	Median % of TV - .6%		

Cap: The maximum amount of damages the buyer can recover from the seller under the indemnification provisions. Many agreements include separate caps for different types of breaches.

Table 6 - Cap % of Transaction Value				
Deal Point	<10%	≥10% and ≤15%	>15% and ≤25%	>25%
ABA	43%	31%	14%	12%
SRS	23%	62%	13%	2%
HL	Median % of TV - 10%			

Escrow/Holdbacks: A portion of the consideration that is deposited with a neutral third party (in the case of an escrow) or withheld by the buyer (in the case of a holdback) to be applied toward future indemnification claims by the buyer. After a specified period of time, any consideration remaining in the escrow or holdback account is released to the seller.

Table 7 - Escrow/Holdback % of Transaction Value					
Deal Point	≤5%	>5% and ≤7%	>7% and ≤10%	>10% and ≤15%	>15%
ABA	17%	16%	34%	24%	9%

Escrow Period: The length of time (in months) after the closing date that the escrow is held before being released to the seller.

Table 8 - Escrow/Holdback Period			
Deal Point	≤12 mos.	>12 and ≤18 mos	>18 mos.
SRS	23%	54%	23%
HL	Median Escrow/Holdback Period - 18 months		

Final Comment

Parties to a business acquisition are advised to seek the assistance of legal counsel who are trained and experienced in drafting and negotiating deal points in P&S Agreements.