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## **CMS M&A Study 2015: Sellers Strengthen their Negotiation Position in European Transactions Market**

**The risk distribution in M&A deals in Europe again tends to favour sellers. At the moment they have noticeably better chances of asserting their positions, concludes the CMS European M&A Study 2015.**

Last year, sellers succeeded more often in enforcing lower liability caps for warranty violations than in the year before. Moreover, warranty claims of buyers more frequently required exceeding certain threshold values (de minimis and basket clauses).

For the study, CMS analysed 2,414 transactions involving non-listed companies that the law firm advised on between 2007 and 2014. Uniform criteria were applied to evaluate various industries and European regions. The study includes a total of 346 transactions that were carried out in the year 2014 alone.

“This study offers a unique insight into the market, also regarding regional and industry-specific particularities in deal structures”, says Peter Huber, Managing Partner and head of the transactions team at CMS in Vienna. “Last year, we witnessed transactions that were comparable to pre-crisis levels in number and size. At the moment all signs suggest that this development will continue.”

The higher level of activity benefits sellers: in addition to lower liability caps, de minimis and basket clauses, also the increase in other provisions favouring sellers are indicative of a seller-friendly market. Two pro-seller mechanisms, warranty and indemnity (W&I) insurances as well as locked boxes to determine the purchase price based on the most recent audited financial statements available, were increasingly included in contracts in 2014. “Moreover, MAC clauses with a right of withdrawal for the buyer and non-compete clauses remain relatively rare. Limitation periods for warranty claims are also getting shorter”, explains Peter Huber.

There are still regional differences in company deal structures.

Transactions in German-speaking countries were the least likely to have a short limitation period (only 14 percent have periods of up to twelve months); earn-outs continued to be popular with 22 percent of deals containing respective provisions. Locked-box clauses increased from 46 percent in 2013 to

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53 percent in 2014, basket clauses saw a decline from 64 to 63 percent, and de minimis provisions rose from an average of 60 percent in the previous seven years to 67 percent.

“Transactions in Central and Eastern Europe saw an increase in the use of MAC clauses with a right of withdrawal for the buyer between the signing of the deal and the date it takes effect”, states Johannes Trenkwalder, a partner at CMS in Vienna responsible for M&A and head of the CMS office in Kyiv. “38 percent of the deals included such clauses”, he specifies. In German-speaking countries, merely 10 percent of the concluded transactions contained a MAC clause.

There is also a noticeable difference in contract design used in Europe and the US, especially with regard to purchase-price adjustment clauses – in the US the share of contracts containing them reached 85 percent, in Europe it was only 45 percent. “The European share could, however, increase in the course of the year as currency risks are increasingly hedged again”, predicts Alexander Rakosi, a partner in the transactions team at CMS Vienna, who also has several years of experience in advising on M&A deals at a renowned US business law firm. “The surprising decoupling of the Swiss franc from the euro in January 2015 and the further economic and political development of the euro will probably further this trend.” According to the current study, the number of deals with purchase-price-adjustment mechanisms has slightly increased from 2013 to 2014, reversing the trend of the last couple of years.

#### **Further key conclusions of the CMS European M&A Study 2015:**

- Compared to the European average, the share of contracts with a maximum liability limit of over 50 percent for sellers was particularly low in France and the Benelux countries (26 and 29 percent, respectively), while the share of such deals in the buyer-friendly UK amounted to 61 percent.
- Locked-box clauses, where the purchase price is mostly based on the most recent audited financial statements available, increased substantially in 2014, especially in Southern Europe and France (an increase of more than 20 percent could be observed in both countries).
- The use of earn-outs, where the final purchase price depends on the development of the targeted company, grew significantly last year. While only 14 percent of all analysed deals contained such a provision in 2013, earn-outs were used in 19 percent of transactions concluded in 2014. In the Benelux countries, France and Germany, the number of transactions is thus comparable to the US (25 percent). In 2014, 57 percent of the deals had an earn-out period of between twelve to 24 months, compared to 48 percent in 2013. Earn-out calculations based on earnings before interest, taxes, depreciation and amortisation (EBITDA) still prevail, but turnover-based criteria have increased (31 percent in 2014 compared to 21 percent in 2013). The share of merely profit-based earn-outs fell to six percent.
- In almost all regions, de minimis clauses – where the buyer can only make claims if they are in excess of a minimum value – are a frequently used tool in contract design. The trend observed in the previous years thus continues.
- The contract parties often agreed on basket clauses, which protect the seller against minor claims beyond de minimis thresholds, also in 2014. Basket clauses were included in 69 percent of the deals. European deals frequently also stipulate that upon exceeding a certain threshold the entire loss becomes refundable, while in the US only the amount exceeding the threshold value becomes liable to indemnification.
- While in the previous seven years, an average of 39 percent of buyers found safeguards for warranty claims (such as bank guarantees) important, this figure dropped to 29 percent in 2014.

*We are happy to send the full version of the study to journalists upon request.*

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