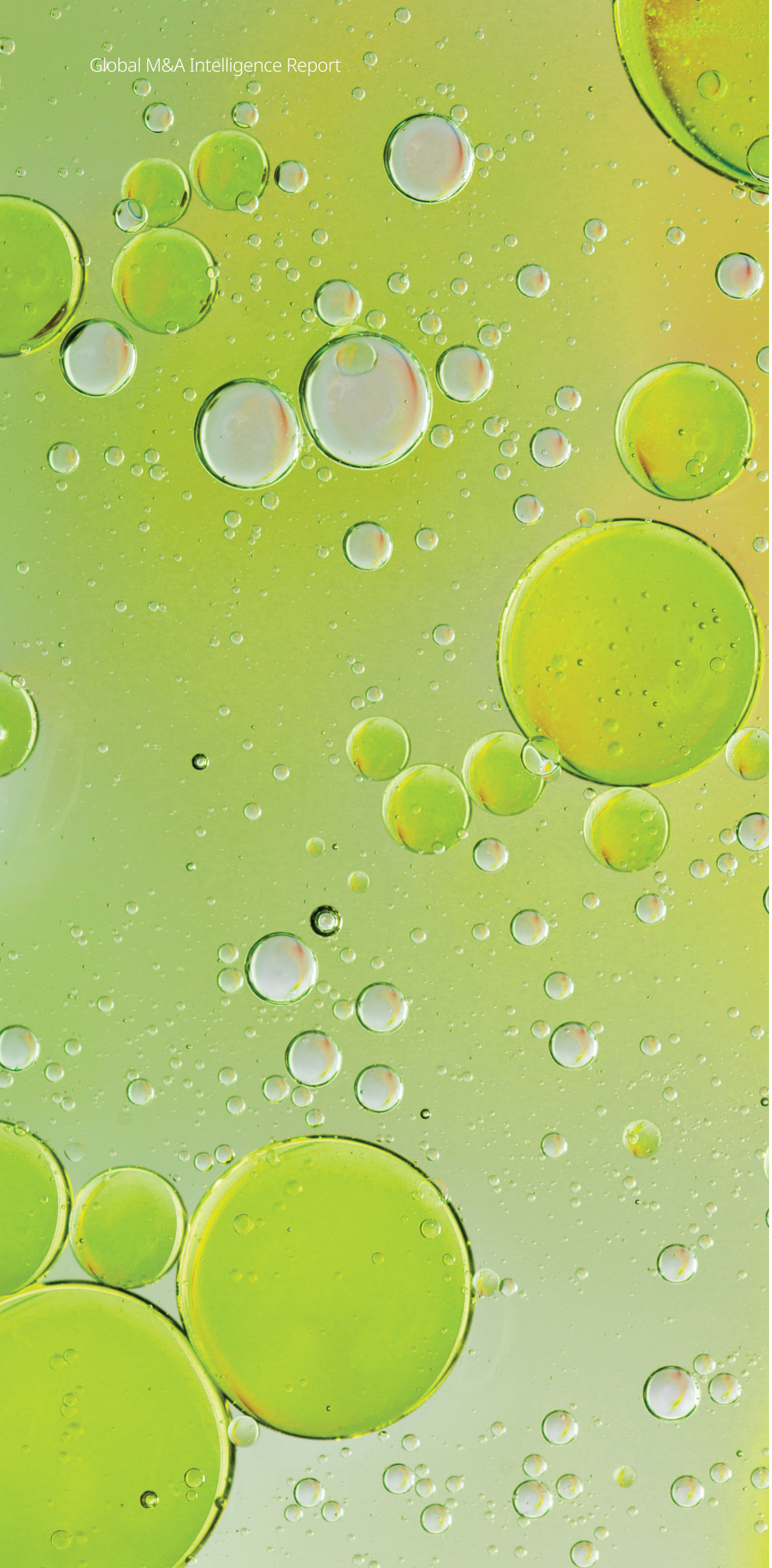
Global M&A Intelligence Report

2023

DLA PIPER

#1 Global M&A
by deal count
(for the last 13 years)
Mergermarket, 2010–2022



Special thanks

Ever since the launch of our first M&A Report in 2015 our Head of Knowledge Julia Wood has been a driving but invisible force in making the reports such a success. She is now starting a well deserved retirement and this edition is dedicated to her with all our thanks and best wishes.

This report is based on an analysis of approximately 800 private M&A deals undertaken in 2022 – including approximately 120 in the UK, 170 in Continental Europe, 200 in the Nordics, 250 in the US and 50 in Asia Pacific. It also draws on the analysis of over 2,500 further deals undertaken in 2018-2021 for our earlier M&A Intelligence reports. Our DLA Piper M&A Trends Database now includes over 5,000 deals.

#1 Global M&A representing Companies by deal count
(for the last 3 years)
(*PitchBook, 2020-2022*)

#1 Europe Private Equity by deal count - Buyouts & Exits combined
(*Mergermarket, 2017-2022*)

Contents

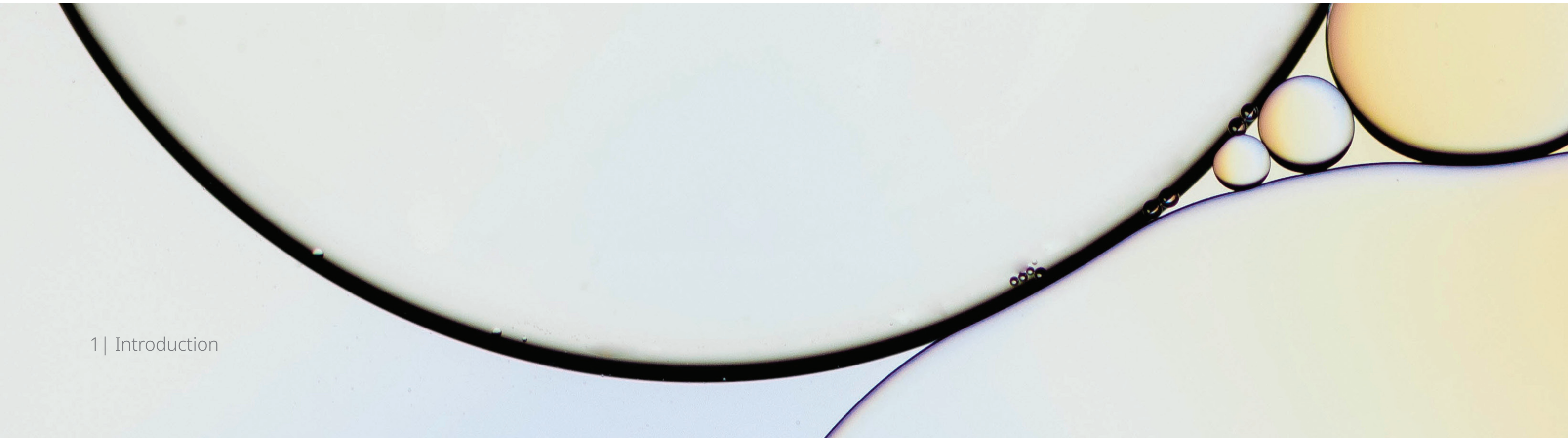
1 | Introduction

Welcome to the ninth edition of DLA Piper's Global M&A Intelligence report. Our 2022 report showed a bullish global M&A market that had bounced back strongly following the impact of the COVID-19 pandemic. Along with many market commentators, we predicted a cooling in the M&A market as central banks continued to wean markets off the high-octane fuel of cheap money on easy terms but, as ever, the market has not behaved in quite the way we might have expected. Overall deal volumes were down in 2022 but that was following a record-breaking 2021 and they remained above pre-pandemic levels; a robust performance all things considered.

In Q1 of 2022, the war in Ukraine threatened to disrupt Central and Eastern Europe (CEE) and global M&A markets by accelerating many of the key macro-economic trends that were already playing out in the market: high energy prices; rising inflation; and more expensive and harder to obtain debt financing. But, despite these challenges, the M&A market was active. Private equity players accelerated their exits to capitalise on the gains. This created opportunities for strategic international buyers to pursue investments. Large businesses focused on reorganisations, streamlining their operations and shedding non-core business segments. The bottom line: the market sustained robust activity across multiple sectors, boosting optimism for a positive 2023 in M&A.

So, what does the data show us?

2022 was very much a year of two halves in the global M&A market, with a strong start to the calendar year and a tightening M&A environment in the second half of the year. Deal terms in general did not change very much, although the use of auctions and parties involved in them did change noticeably.



Why is that?

Ordinarily, any market in which there are fewer buyers would result in more favourable terms for buyers, but that's not quite how deal terms seem to be playing out in the current market. Many seller-friendly deal features such as locked box, fully insured deals and shorter limitation periods have become so embedded in certain markets that, notwithstanding a theoretically improved bargaining position, buyers don't seem to have pushed for significantly more favourable terms. This may be a timing point and we may see deal terms move back in favour of buyers over time. But looking back over the nine editions of our report, we see an M&A market in which deal terms continue to move in favour of sellers – in slower markets the speed of that drift may slow (and it may even reverse at the margins) but the overall direction of travel is clear.

Aside from general economic conditions, geopolitics continues to influence M&A deal terms. Protectionism found its political voice in the wake of the COVID-19 pandemic, partly through more robust anti-trust analysis of transactions by regulators. But 2022 showed an explosion in Europe of laws mandating pre-closing national security / foreign direct investment filings. In the absence of significant anti-trust issues, FDI clearance is often the biggest gating item to closing.

Boards focusing on factors such as ESG means M&A deals are looked at through a different lens, something many advisors are struggling to accommodate. In the meantime, key innovations such as the growing adoption of AI will drive significant M&A activity as step changes in technology always do.

One thing the deal data consistently shows us is that while there are global trends in M&A – part of which is a convergence of deal terms – there are very distinct local market practices. And the party that properly understands the local market has an advantage over its competitors.

DLA Piper has an unrivalled track record of doing more M&A globally than any other law firm in each of the last 13 years. Our deals database now extends to well over 5,000 transactions in varied M&A environments and we can mine that data to give our clients insight into global markets that only a law firm of our size and strength in M&A can bring.

We hope you find the report insightful and useful and would be delighted to discuss any aspect of it in more detail.

Rob Salter
Partner, UK

Jon Kenworthy
Partner, UK

Tim Wright
Partner, UK

Chris Arnold
Partner, UK

Chris Giordano
Partner, US

2 | 2022 – a year of two halves?

The first half of 2022 saw a continuation of the hot market of 2021 despite external macro-economic shocks such as the war in Ukraine. In the second half, rising interest rates in response to high inflation led to a tightening in the debt financing markets. The restricted availability and high cost of debt had a particular impact on private equity M&A activity in the second half of the year. We reviewed our deal data to establish whether the contrasting deal environments in each half of the year also resulted in changes to deal terms. In general, they didn't – but the profile of parties involved in auction processes and use of pricing mechanisms was noticeably different.

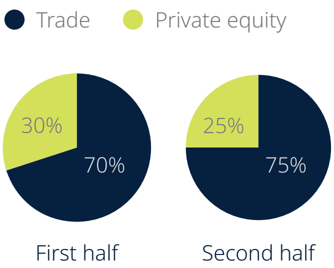
#1 Global M&A representing Investors by deal count
(*PitchBook, 2022*)

#1 Europe Private Equity by deal count - Exits
(for the last five years)
(*Mergermarket, 2018-2022*)

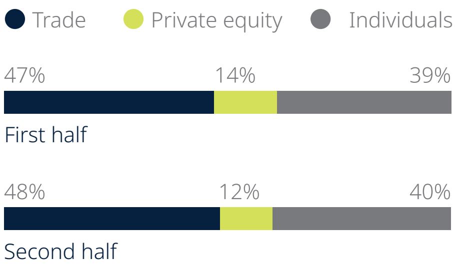
Types of buyer and seller

We didn't see much difference in buyer and seller types in deals overall between the first and second halves of the year except for a slight decrease in private equity buyers and sellers.

Buyers by type



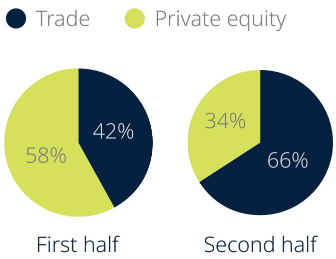
Sellers by type



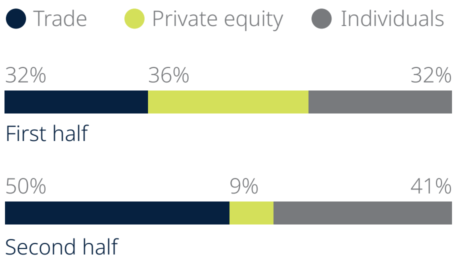
Auctions

Although we saw a similar proportion of auction processes in the first and second halves of the year, there was a noticeable difference in the nature of the buyers and sellers who participated in those processes. We saw a significant decrease in private equity buyers and sellers in auction processes in the second half of the year – in particular sellers. This is probably because of the tightening of debt markets in the second half of 2022, which both restricted the availability of secondary buyouts as an exit for private equity sellers and made acquisition financing more difficult for private equity buyers.

Buyers in auctions



Sellers in auctions



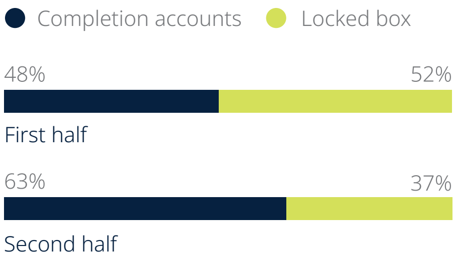
Pricing mechanisms

We saw a noticeable increase in the use of completion accounts in both auctions and non-auctions in the second half of the year – indicative of a more cautious, buyer-friendly deal environment and the reduction in private equity activity during this period, which probably lessened the competitiveness of some auction processes. This could also be, in part, down to timing. The majority of companies have 31 December financial year ends, so the audited accounts become increasingly old and stale in the second half of a calendar year. Buyers may not be prepared (particularly in a market such as this) to transact on old locked box accounts or unaudited accounts so may push for a completion accounts pricing mechanism.

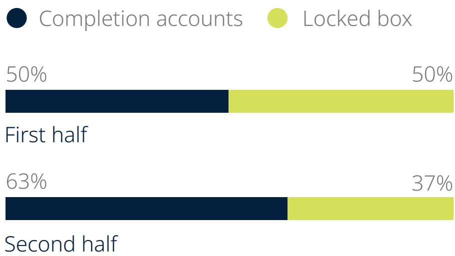
"The tapering M&A market in the second half of 2022 saw deal terms start to turn in favour of buyers, and sellers starting to focus on completion protection measures."

Shane Bilardi
Partner, Australia

Pricing mechanism - auctions



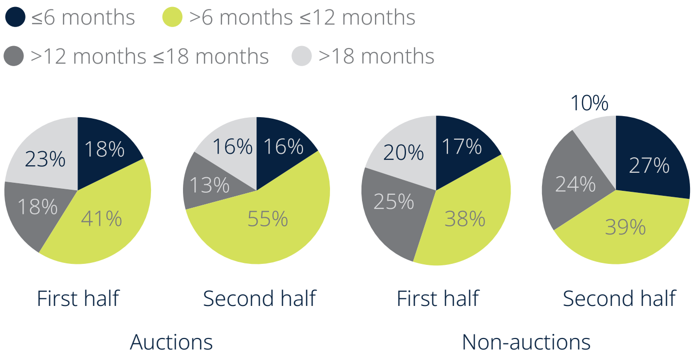
Pricing mechanism - non-auctions



Leakage claim periods

Surprisingly, given a less seller-friendly environment in the second half of the year, our data indicates that there was a shift towards shorter leakage claim periods in second half auctions, perhaps because those auctions that did go ahead were very competitive. Otherwise, leakage claim periods were broadly consistent across both halves of the year.

Leakage claim periods

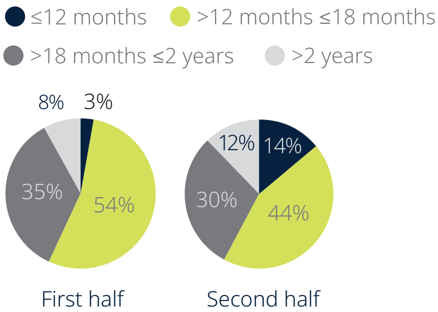


Limitations

COMMERCIAL WARRANTY PERIODS

In the second half of the year, we saw increases in both shorter commercial warranty periods (those of 12 months or less) and in longer periods (those over two years), although the most common period was between 12 and 18 months in each half of the year.

Commercial warranty periods – excluding buy-side insurance

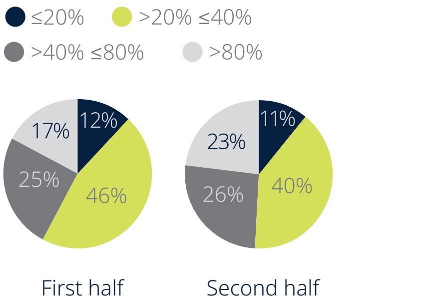


COMMERCIAL WARRANTY CAP

There was little difference in the size of commercial warranty caps achieved by sellers between the first and second halves of the year.

Our data indicates that while the deal environment may have become more challenging in the second half of the year, this didn't flow through to a significant shift in the balance of power between buyers and sellers as far as contractual limitations on liability were concerned. What our data doesn't show is where sellers had to reassess their valuation expectations and accept a lower price than they'd originally hoped for in the second half of the year.

Commercial warranty cap – excluding buy-side insured deals



3 | How ESG is changing M&A

"ESG is not a component part of how transactions are carried out – it's an additional lens by which the transactions as a whole are now viewed. With increasing regulation requiring the private sector to consider climate, nature and social issues in both their own operations and supply chains, the sphere of concern for businesses has expanded beyond traditional perimeters in recent years. Understanding ESG-related risks and opportunities is a core factor in M&A deals."

Kelly Sporn
Special Counsel and Head of Strategic Delivery - Sustainability and ESG

Not all ESG due diligence is created equal. Some approaches dive too deep into one issue and lose commerciality. Other approaches are superficial to the point of attracting accusations of greenwashing. Striking the right balance is one of the many challenges M&A professionals have in meeting stakeholders' expectations.

ESG can be a dealbreaker. It's an opportunity to add value to a transaction. And it's an important part of integration planning.

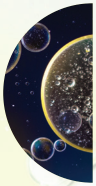
Even the most straightforward M&A transactions have never been purely about the numbers. Understanding and explaining ESG issues in a transaction is an important part of modern M&A.

Good deals need to integrate operations, realise synergies, and address stakeholders' perceptions. Though M&A practitioners might try to translate these qualitative concepts into quantitative measures, it's a challenge inherent in turning non-monetary risks and opportunities into dollar values. And it's one of the key reasons two-thirds of deals fail to deliver the forecast return.

So rather than trying to incorporate non-financial considerations into a valuation model, M&A practitioners create frameworks to weigh up risks and opportunities as part of a deal thesis. It's crucial to give a robust account of ESG issues and be proactive in managing the integrated organisation's ESG profile after completing a deal. It's a way to capture value and avoid potential dealbreaker issues.

ESG is important now – and will likely become more so

Good ESG due diligence will likely become more important because of:



1.
the risk of failing to meet material stakeholders' expectations

2.
the risk of business disruption from regulatory, environmental and social issues

3.
the risk of inheriting ESG exposure and liabilities

Meeting material stakeholders' expectations

ESG is a broad and varied set of risks. And regulation varies from country to country. The best way for an organisation to set its ESG ambitions is to look at what its material ESG stakeholders expect. Those stakeholders include customers, suppliers, investors and employees. But it can also include members of the public and activist groups, and competitors and regulators in foreign jurisdictions. Maybe the most important stakeholders in terms of driving ESG due diligence expectations are investors and directors. They know how ESG performance affects returns and how important it is to comply with the law. M&A professionals have to know which stakeholders are material in the context of the deal and understand what they expect in terms of managing ESG risks and opportunities.

The risk of business disruption

The complex regulatory environment creates a growing risk of business disruption. Companies have to be aware of the existing and evolving regulatory landscape across all their operational jurisdictions – and those of their target. Penalties for non-compliance or expensive rectification activity will reduce the expected financial benefit of the transaction.

The risk of inheriting ESG exposure

Companies face legal, financial and reputational risks if they "import" or "export" ESG risks through acquisitions, sales or divestments. Hidden ESG risks can reduce deal valuation or even lead to post-deal claims. Missed opportunities to show ESG progress can leave unrealised value for a seller. It's hard for M&A professionals to understand sources of risk and opportunity. They have limited capacity and, often, a lack of ESG experience. An independent expert can identify these risks and opportunities. They'll manage and reduce or remove a source of potential value destruction – or create value.

"ESG is no longer a 'nice to have' consideration in deals. Environmental, social and governance performance can add a premium for sellers, mitigate risks for buyers, and is a key part of transaction planning"

Sean Faehrmann

International Director, Sustainability and Organisational Change, DLA Piper Business Advisory

ESG matters in different ways for different deals

The above three factors are behind the increasing need to consider the ESG implications of a transaction. But robust due diligence might not always be warranted. It depends on the industry, size, complexity and jurisdiction(s) involved.

Some industries are more exposed to environmental risks than others. Small and medium enterprises might have fewer internal resources to dedicate to managing their ESG risk profile. So they'd benefit from external help. Complex transactions and those in relatively advanced jurisdictions from an ESG perspective (North America, Europe and some areas of Asia Pacific) will need tailored and comprehensive ESG due diligence.

The best approach to ESG due diligence depends on an organisation's position. Acquisitive businesses with a strong internal ESG position will want to know the actual performance of the target – not just what's in the sustainability report. This means assessing the target's actual ESG performance and its alignment with the buyer's own performance and ambitions. This usually starts with a materiality assessment. The buying party will then decide on how far to go with target due diligence. For sellers, organisations are increasingly considering whether their ESG profile is a source of risk exposure or a potential opportunity. Seller ESG reviews are most relevant for businesses facing a high likelihood of enhanced buyer scrutiny on ESG credentials. This might be because of the industry, scale or history, compressed timeframes and a lack of internal ESG expertise.

ESG can also drive a price premium based on existing, planned or potential ESG activities. Seller ESG due diligence is less common than target due diligence. But organisations preparing for sale are expected to be ready to give a good account of their ESG profile. We're also witnessing a small but growing number of sellers who are assessing the ESG credentials of potential buyers when deciding who to sell to. The structure and approach to ESG due diligence is evolving. And while there's a growing understanding of the importance of addressing the ESG implications of engaging in M&A, many organisations often have limited experience in approaching the task. Opinions vary greatly, with some arguing for a highly robust and detailed approach, while others prefer a more commercial, pragmatic and limited scope. It's important to identify and mitigate ESG risks. But due diligence has to be efficient, cost-effective and tailored to the specific target and transaction.

4 | Merger control and FDI

"2022 saw an explosion in laws mandating pre-closing national security/foreign direct investment filings across Europe, meaning that for transactions that do not get bogged down in material antitrust concerns, the biggest gating item to closing now is often FDI clearance."

Matt Evans
Partner, UK

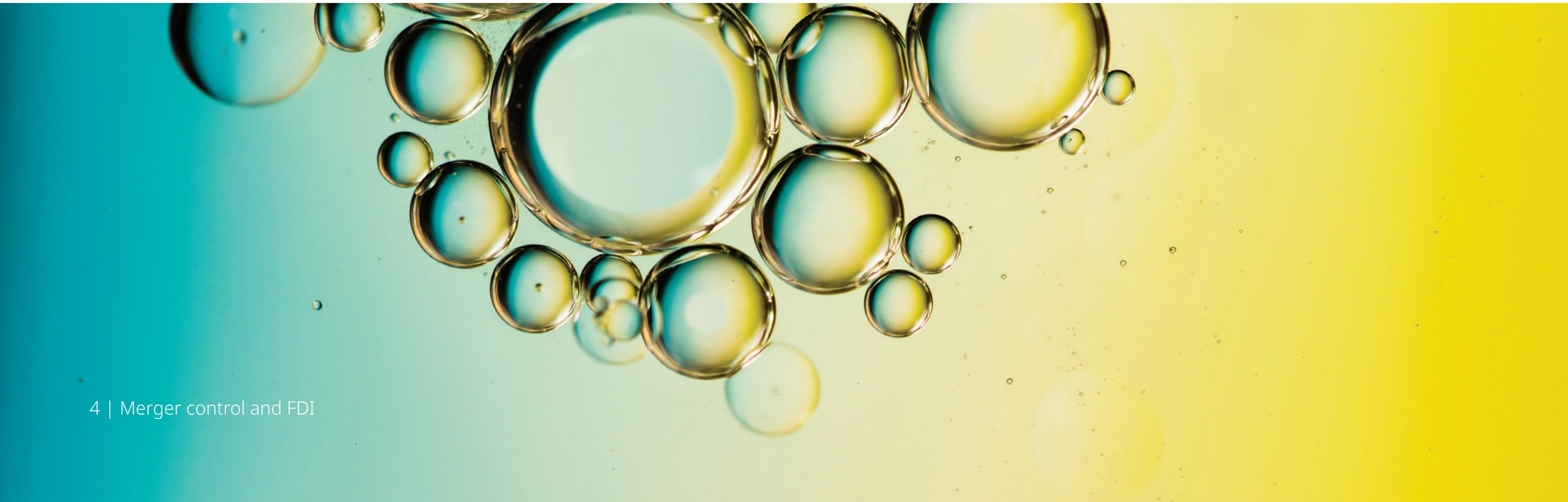
Multiple new foreign direct investment (FDI) regimes came into force in 2022 and merger control authorities stepped up enforcement. It's never been more important to think about merger control and FDI filings at the outset of M&A transactions.

Merger control

DIFFERENT APPROACHES

In 2022 global regulators continued to take different approaches to handling merger control notifications for the same transaction. High-profile examples included Cargotec/Konecranes, the first parallel Phase 2 review conducted by the UK's Competition and Markets Authority (CMA) and the European Commission since Brexit. The CMA blocked the transaction. The Commission accepted a remedy package. Other examples included Meta/Kustomer and Booking/eTraveli, both of which required an extended Commission Phase 2 review, while being cleared by the CMA at Phase 1.

Dealmakers should think about the risk of different approaches when considering deal timetables. Even if a deal is cleared quickly by one authority, we can't assume another authority will do the same. Even where the competition issues in each jurisdiction are broadly the same.



INCREASE IN EU ENFORCEMENT

EU merger control conditions are more prevalent for large deals than small deals. Merger control conditions were included in 75% of all our large deals in Continental Europe in 2022 (valued at over EUR250 million), compared to only 23% of our small deals (valued at under EUR50 million).

This is to be expected, higher value deals typically involve parties with higher levels of turnover and higher turnover triggers for merger control filings. But the risk of the Commission intervening in smaller deals has increased following an EU Court of Justice ruling that EU Member States may refer to the Commission mergers that meet neither national nor EU notification thresholds but threaten to significantly affect competition in a Member State.

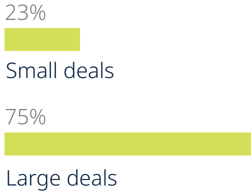
The EU General Court confirmed in 2022 that the Commission can accept referral requests from Member States (Article 22 Referrals) and review transactions even where they don't meet EU or individual Member State merger control thresholds. For example, in Illumina/GRAIL (the case prompting the EU court decision), the Commission conducted a post-completion merger control investigation of Illumina's acquisition of GRAIL and blocked the transaction. This was despite GRAIL having no turnover in the EU at all.

That point of law is currently under appeal. But, for the time being, dealmakers should be wary of Article 22 Referrals for EU deals raising substantive competition issues (no matter how small the target is). And target revenue is not a good indicator of market power – for example, where the target is an important innovator or tech startup.

"In Germany, the scope of FDI screening was significantly expanded in 2021. This led to a 90% increase in FDI cases filed with the German Ministry for Economic Affairs and Climate Action (MCA)."

Gerald Schumann
Partner, Germany

Merger approval condition – Continental Europe



INCREASED FOCUS ON GUN-JUMPING

There's been an increased focus in 2022 on implementation of mergers without having first received mandatory merger clearances – so-called "gun-jumping".

Spain's National Markets and Competition Commission imposed its highest fine for gun-jumping since 2013 (EUR1.5 million). Record gun-jumping fines were issued in Brazil (EUR11.6 million) and Portugal (EUR2.5 million). Competition authorities issued their first ever gun-jumping fines in Morocco (approx. EUR1 million) and Mozambique (less than EUR1 million).

These fines fall well short of gun-jumping fines imposed in recent years by the European Commission (eg EUR124.5 million, reduced by 5% on appeal, against telecoms company Altice) and by France (EUR80 million, coincidentally also against Altice).

China is still a prominent enforcer. It issued 32 separate fines in 2022 (including its maximum fine for the first time). It also amended its merger control laws to increase the penalties for gun-jumping to RNB5 million for non-anti-competitive deals and up to 10% of group global turnover for anti-competitive deals.

Dealmakers should be wary of gun-jumping merger control regimes. Saudi Arabia, Morocco and Russia are particularly tricky jurisdictions to navigate. They can all capture foreign-to-foreign transactions, even where no local turnover is made.

"HELL OR HIGH WATER" CLAUSES

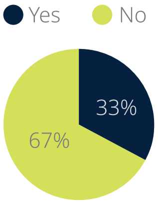
Given rising deal uncertainty, "Hell or High Water" clauses (HOHW) have become increasingly common. HOHW clauses commit the buyer to taking "all steps necessary" to obtain anti-trust or other regulatory approvals for a transaction (including disposing part of the target's business or other aspects of the buyer's business).

HOHW clauses were used in 33% of our UK merger control deals in 2022 but only in 8% of our merger control deals globally. Of these, 67% of UK HOHW clauses included absolute commitments.

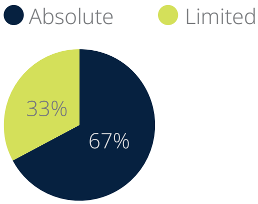
HOHW clauses were generally more attractive than break fees, which were used in 9% of our UK deals, compared to 5% globally.

HOHW clauses expose buyers to all competition risks from deals and can be unattractive where there are competition concerns (especially if there's a risk of the deal being blocked or of remedies being required). If an HOHW clause is needed, buyers should try to make sure they have as much control of the regulatory process as possible.

Merger clearance: HOHW clause UK



Merger clearance: Type of HOHW clause UK



FDI

NEW REGIMES

Multiple countries introduced or expanded their FDI screening regimes in 2022, including the UK, Romania and Russia. Belgium, Slovakia, the Netherlands, Ireland, Estonia, Slovenia, Canada and Sweden are also expected to introduce new or enhanced FDI regimes in 2023.

Many new regimes are wide in scope and will capture transactions across a variety of sectors – including intra-group transactions in some circumstances. With a lack of case law or precedents, dealmakers should be cautious of new authorities taking a conservative approach to the scope of their legislation. Dealmakers also need to look out for delays to deal timetables (because of new screening authorities not having enough capacity or infrastructure to cope with the level of notifications).

INCREASE IN FDI FILINGS

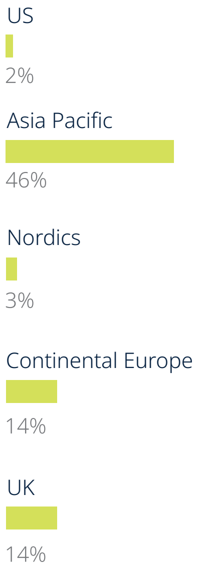
There's been a marked increase in FDI filings in the last year. The EU, the UK, Australia and New Zealand are particular hot spots.

Of all our conditional deals in Asia Pacific, 46% included an FDI condition. And FDI conditions were included in 14% of all our conditional deals in the UK and Continental Europe, compared to less than 4% of our conditional deals in the Nordics and the US.

FDI conditions are likely to increase in European transactions (where every EU Member State other than Cyprus, Croatia and Bulgaria now has an FDI regime or is due to implement one in the next year).

Buyers should pay close attention to EU cooperation on FDI filings. A filing made in one Member State can be flagged to authorities in all other Member States.

Deals with FDI conditions: By region



UK's National Security and Investment Act

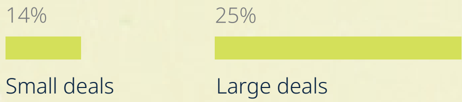
2022 was the first year of the UK's new national security regime, under the National Security and Investment Act 2021 (NSIA). The NSIA is a hybrid mandatory/voluntary notification regime. It requires mandatory notification for transactions involving changes of control over targets with UK activities in 17 sectors (including defence, AI and energy).

According to UK government data, 222 notifications were made in the first three months of the NSIA regime. Most of them related to defence, military and dual-use goods, government suppliers or AI. Less than 8% of the deals were "called-in" for an extended national security review.

Most deals notified in 2022 were cleared unconditionally. Based on publicly available information, only nine transactions were cleared subject to behavioural conditions. And only five were prohibited (three involved a buyer from China, one from Hong Kong and one from Russia).

UK FDI conditions are becoming more common. But they vary in prevalence by deal size. While 25% of our large deals (over EUR250 million) contained a UK FDI condition, only 14% of our small deals did (under EUR50 million). This is likely to be a quirk of the transactions in question. There's no deal size threshold for mandatory notifications, so, over time, we expect a similar proportion of deals to include a UK FDI condition, regardless of transaction value.

FDI condition - UK



5 | Buy-side insurance

Buy-side deal insurance continues to be an integral part of many M&A deals in the US, Europe and Asia Pacific. The product is still welcomed by buyers and sellers alike for its ability to enable a smooth transaction-reducing warranty and tax indemnity negotiations, offering sellers a clean exit, and giving buyers increased control over contractual protections. However, our data shows that 2022 is likely to go down as a year of transition for the product.

Use of buy-side insurance

GENERAL

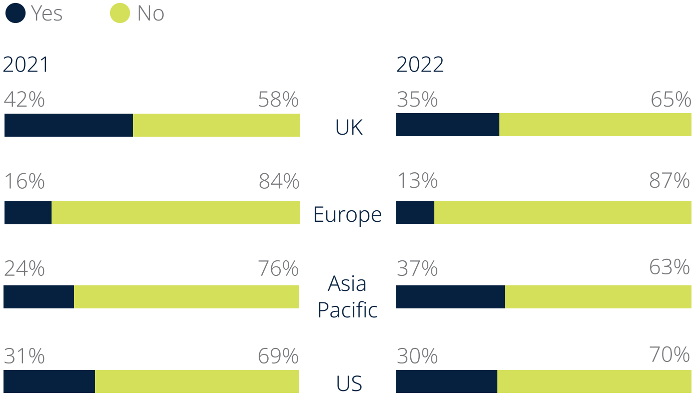
Interestingly, while insurance remains a common aspect of M&A deals, the percentage of global deals with buy-side insurance fell slightly in 2022, with the UK seeing the biggest decrease. This is perhaps symptomatic of a general move towards more buyer-friendly terms in M&A deals in 2022, which resulted in slightly more buyers reverting to more traditional contractual protections.

Asia Pacific is an outlier here seeing a 13% increase in the number of insured deals between 2021 and 2022. Throughout 2022, we saw a boom in UK insurance markets bring new capacity into the Asia Pacific market as the UK and Europe slowed down and established UK market players looked to expand into the Asia Pacific market.

"Whilst W&I insurance is now intrinsic to many M&A transactions, it is a product that continually evolves. We have seen it expand further into small and medium sized deals and geographically into emerging markets. At the same time new products are developing to deal with specific transactional or other contingent risks (particularly tax, environmental and IP) and the market will continue to innovate to provide further transactional solutions for buyers and sellers alike."

Jonathan Clarke
Partner, UK

Deals with buy-side insurance

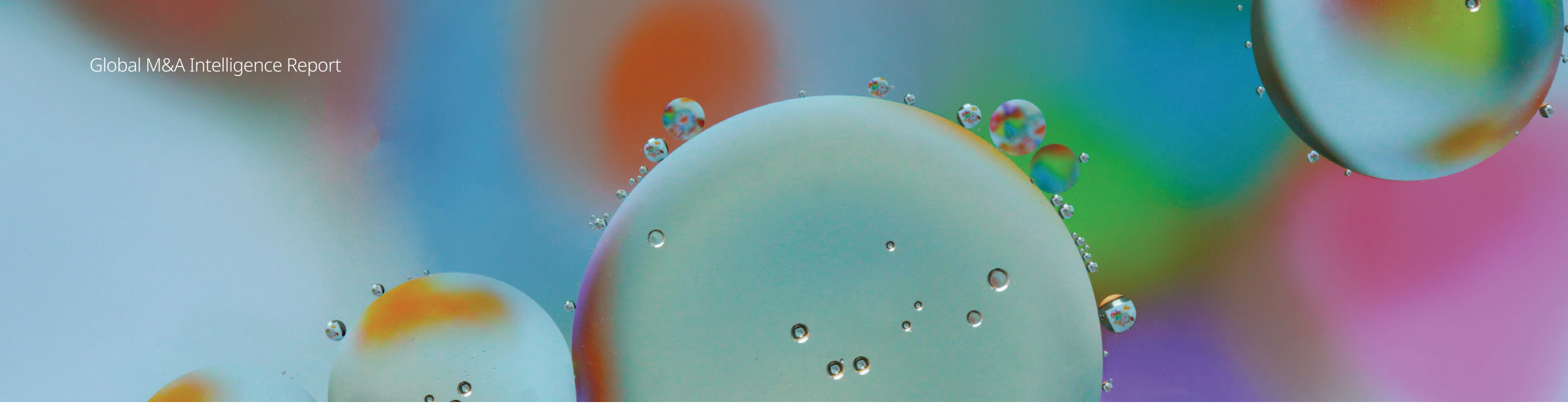


TRANSATLANTIC INFLUENCES

Since 2020 we've seen an increase in North American buyers procuring European targets and using transactional liability insurance. This trend is likely to continue and as a result insurers in the European and Asia Pacific markets are increasingly able to accommodate North American enhancements (such as scrapes of the data room, disclosure and due diligence reports and an indemnity basis of recovery) and in some cases a fully synthetic North American policy to remain competitive with North American insurance markets.

"For US buyers, who are already familiar with a US-style policy and US-style underwriting, our experience is that they want a consistent experience with the W&I product and process for transactions where the target company has little to no US presence."

Eric Wang
Partner, US



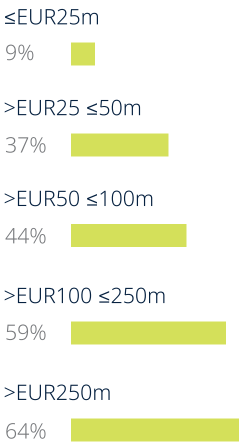
IMPACT OF DEAL SIZE AND PROCESS

Consistent with the last three years, buy-side insurance has been obtained on a larger percentage of auction deals than non-auction deals irrespective of deal size, and buy-side insurance tends to be more prevalent as deals increase in value.

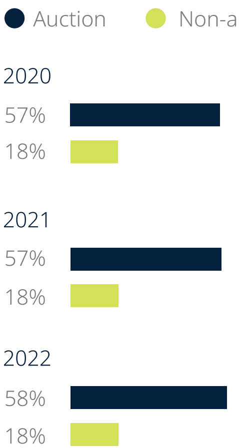
We expect that the difference between deal size and prevalence of insurance will flatten over the course of the next few years as market players are now either offering specific SME policies or are focusing their capacity on this end of the market.

The increased use of buy-side insurance on auction transactions is unsurprising. Auctions are a seller-friendly mechanism and M&A insurance is a seller-friendly transaction solution.

Deals with buy-side insurance by deal size



Deals with buy-side insurance by deal process



> "One of the clear benefits of W&I policies is the synthetic extension of the general warranty period, which we now see frequently, often for no additional premium. Many claims develop after the two year mark, so this is a real 'value add' for insureds."

Laura Marcelli
Partner, UK

Impact of buy-side insurance on deal terms

CAP SIZE

Consistent with previous years, most insured deals continue to have caps of less than 10%. The exception is in Asia Pacific where cap size tends to be larger than 10%. We've seen very large programmes of insurance with syndicated policy limits or "towers" of up to 30% of deal value being put together on auction deals in Asia Pacific through 2021 and 2022.

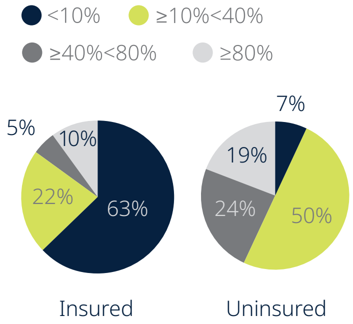
This contrasts with uninsured deals where only 7% of global deals have a cap of less than 10% – confirming that the product is used in cases where buyers have a greater tolerance for the overall risk of the business they're buying.

CLAIM PERIODS

We continue to see a great deal of regional variation in relation to warranty claim periods on insured deals. In the US, more than 88% of insured deals have warranty periods of 12 months or less. In Europe, the majority of insured deals had a warranty claim period of between 12 months and two years. And in Asia Pacific, most insured deals had a limitation period of two to three years for commercial warranties.

Deal process did not particularly drive shorter warranty periods on insured deals, except in the US where two-thirds of insured auctions had a warranty period of six months or less compared to 23% of non-auctions.

Commercial warranty cap



> "With the rise of W&I in use, we've seen a corresponding rise in the number of transactions with no survival of the commercial reps and warranties, especially in competitive auctions, which is likely the reason for the shorter-than-average survival periods in US transactions."

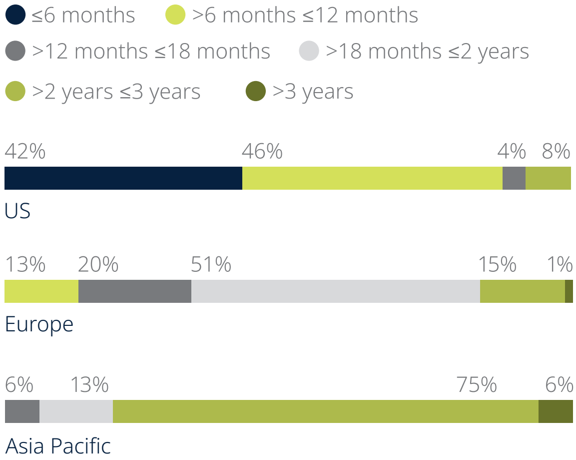
David Richardson
Partner, US

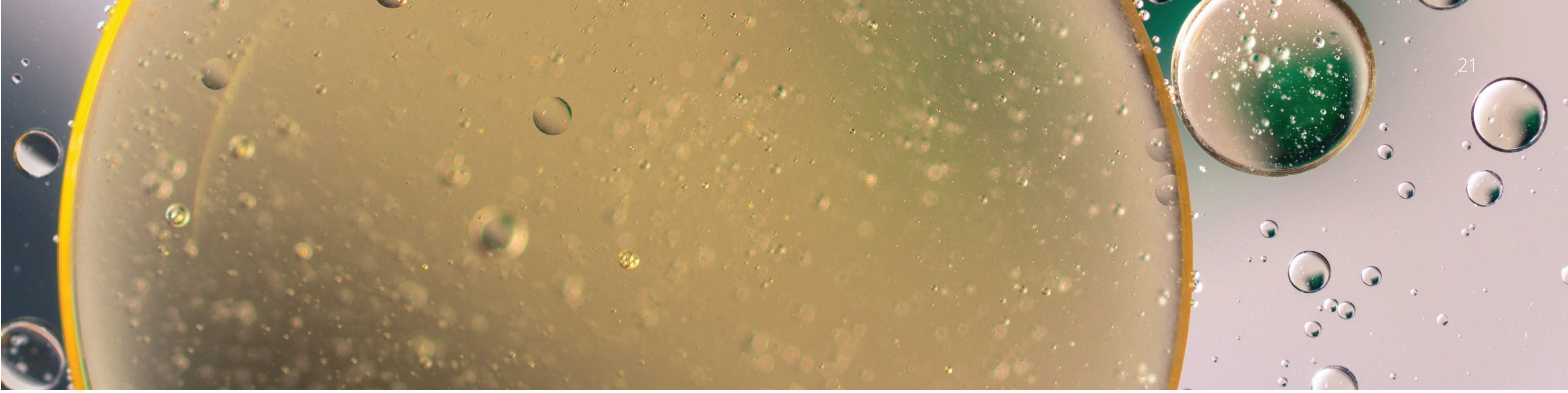
REPETITION OF COMMERCIAL WARRANTIES

As in previous years, our data indicates that warranties and representations are typically repeated at closing on deals in the US and Australia whereas in Europe and Asia repetition of warranties is less common. This difference comes from the willingness of insurers in the US and Australia to cover repeated warranties and representations at closing without requiring a thorough updated disclosure exercise. This has been standard practice in the US for decades and the increased use of buy-side insurance has not changed this practice. US policies balance coverage for interim period breaches between pre-existing and "new" interim period facts and circumstances leading to the breach.

This contrasts with the position often taken by insurers in Europe and Asia, where there's a requirement to bring down the disclosure process. This may expose the buyer to the disclosure of a matter which is not then covered by insurance.

Commercial warranty periods in buy-side insured deals





This is an important difference in approach – leaving European and Asia Pacific buyers potentially exposed for disclosures revealed in a bring down process between signing and closing. These buyers have two options. Firstly, buyers can purchase "new breach" cover for an additional premium (although this cover is not widely available and its substance is still not precisely defined in a European deal context). Secondly, the buyers can make sure the SPA provides the necessary breathing space to enable the buyers to take practical steps to ensure they're not materially prejudiced by the subject matter of any interim period disclosures.

"New breach cover provides coverage for breaches of warranty which have occurred post-signing and before closing, of which the buyer has become aware before closing, for an additional premium. New breach cover is typically only provided for rolling 30-day periods and up to a maximum of three periods and W&I insurers will determine on a case-by-case basis whether it's offered. Take up of this enhancement has been slow and typically buyers have chosen to mitigate their risk in respect of these disclosures using other mechanisms in the SPA."

Jyoti Singh
Partner, Australia

TAX

Contingent or specific risk tax policies are also increasingly seen for known tax risks. Such policies are a useful way of covering risks in transactions (eg real estate) where there's a hard nominal cap and the buyer's only options in relation to disclosed tax risks are to either negotiate an indemnity with the seller or get an insurer to specifically cover the risk.

LOCKTON
UNCOMMONLY INDEPENDENT

We're grateful to Lockton for providing commentary on market trends in 2022, their outlook for 2023 and for providing indicative pricing for buy-side insurance below.

Market trends in 2022

While the end of 2021 saw underwriting capacity constrained, the market was more stable throughout 2022 as M&A volumes steadied, insurers increased headcount and new entrants joined the market. A number of themes emerged:

- **Pricing** – the decline in M&A activity from Q2 onwards led to a "softer" market. Many transactions saw strong competition among insurers, with more competitive pricing and insured-friendly terms.
- **Enhancements** – we saw insureds making increased use of policy enhancements which, with lower premiums, came at a lower aggregate cost. US-inbound investors have made wide use of insurers' ability to offer an indemnity measure of damages, improving their coverage position against what would have been the position under the sale agreement. Insureds are also making use of data room, due diligence and knowledge scrapes to further enhance their coverage positions.
- **Cyber** – the last few years have seen a significant hardening of the cyber insurance market, with sustained increases in pricing being further exacerbated by the war in Ukraine. With concerns in the market that some targets may be under-insured, insurers are focusing on managing cyber risk, in many cases excluding cyber-related issues altogether or limiting cover to certain diligenced warranties and sub-limiting their exposure.
- **ESG** – with the growing importance of this area for buyers, sellers are increasingly being asked to give ESG-focused warranties and we've seen more transactions where buyers have undertaken specific ESG diligence. We expect this trend to continue and for this to become a particular area of focus for insurers during the underwriting process. Buyers should note that, if the transaction documents contain specific ESG warranties, insurers will require commensurate ESG due diligence to be undertaken and may exclude cover if there are gaps between the warranty suite and the diligence review.
- **Claims** – the number of notifications as a proportion of risks bound has remained fairly stable at around 20%, with the expected uptick in notifications as a result of COVID-19 not materialising. The largest claims continue to arise from accounting and finance issues.
  In particular, errors in management accounts seem to be an increasing source of notifications, which is likely to result in greater underwriting scrutiny of management accounts warranties by insurers. There's also been an increase in claims resulting from condition of assets and IP-related issues (mostly driven by third-party claims).

LOCKTON
UNCOMMONLY INDEPENDENT

Outlook for 2023

Lockton expect the market conditions of 2022 to continue in 2023. Q1 has already seen a number of new insurers and products come to market, with insurers focusing on their product offering in an attempt both to broaden the range of insurable deals and to offer more comprehensive coverage. This will lead to several developments:

- **SME transactions** – insurers are increasingly focusing on this segment of the market. Historically, smaller deals have been harder to insure due to a lack of insurer appetite and less competitive premiums. This is now changing, with several insurers offering SME-specific policies (both sell-side and buy-side). These are underpinned by either a more tech-driven or streamlined process with a higher level underwrite, leading to lower costs and a quicker timeline.
- **Known risks** – insurers have continued to add headcount to strengthen their tax and contingent risk offerings and we expect to see the nascent contingent risk market continue to grow and dealmakers become more aware of the product. The market's broader appetite to insure known risks is also increasing, with innovative products offering affirmative coverage for IP and environmental risks, whether on a standalone basis or alongside W&I cover.
- **Synthetic cover** – the market continues to innovate with regard to synthetic cover (where the insurer will provide warranties rather than a seller or a management team). The most typical use for a synthetic policy is on distressed sales – for an administrator not willing to provide warranty cover, it opens up the pool of potential buyers; for buyers, it provides protection that otherwise would not be available. However, there are wider uses for synthetic policies, particularly on public-to-private transactions; while the relevant takeover rules and market practice will require careful management of the W&I process and the release of information to insurers, synthetic coverage may see the W&I market increasing its appetite to insure P2Ps.
- **Claims experience** – given the large number of W&I policies placed in 2021 and into 2022, the number of claims will increase (although not necessarily as a proportion of policies placed). As more claims stories emerge, clients will become more aware of the response from insurers on claims and the role of a broker in claims-handling. While greater competition between insurers has generally been positive (with lower premiums and wider coverage for insureds), experienced dealmakers may look for insurers with more established, solid teams and a good track record on claims.

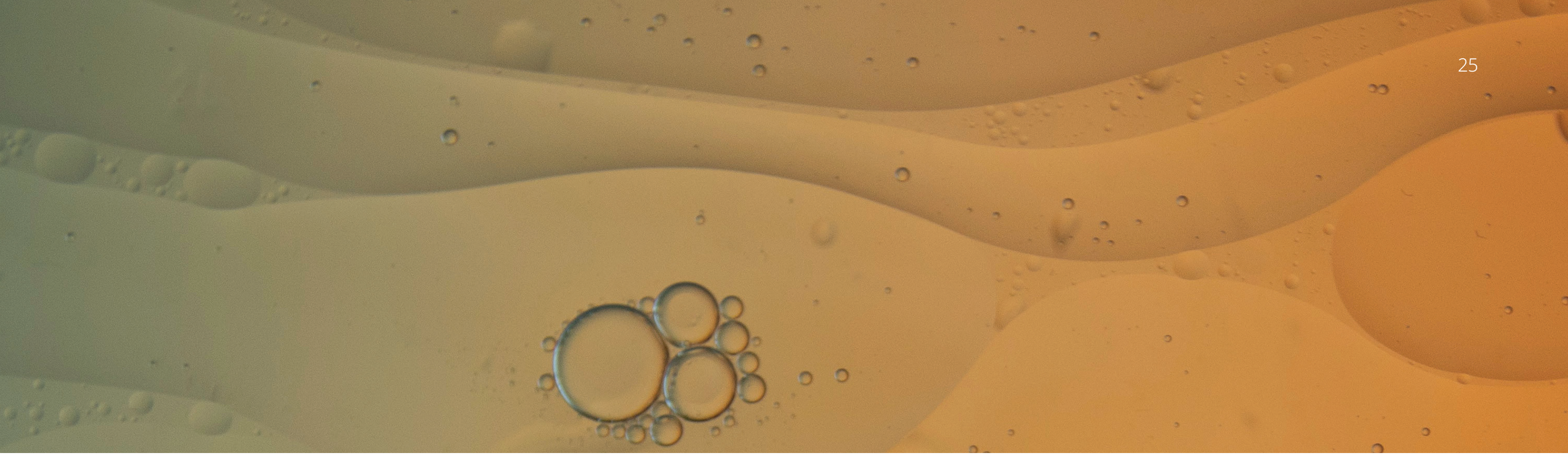
Indicative pricing for buy-side W&I

Different factors drive the pricing of buy-side W&I policies, including:

- the location of the target business and its operations
- the target's sector
- specific risk items identified in due diligence
- insurance market capacity

Lockton have provided the following indicative pricing (as at the date of this report) across a range of industries and geographies.

SECTOR	UK AVERAGE PRICING (AS A PERCENTAGE OF POLICY LIMIT)	UK AVERAGE EXCESS (AS A PERCENTAGE OF DEAL VALUE)
Operational		
Automotive	1.23%	0.25%
Business services	0.85%	0.5%
Education	0.98%	0.5%
Energy	0.9%	0.25%
Engineering	1.08%	0.5%
Financial services	1.11%	0.5%
FMCG	1.02%	0.35%
Healthcare	1.67%	0.35%
Infrastructure	1.02%	0.25%
Leisure	1.07%	0.5%
Manufacturing	1.13%	0.5%
TMT	1.1%	0.5%
Transport and logistics	1.05%	0.25%
Real estate		
Hotel	0.97%	0.35%
Industrial and logistics	0.6%	0.1%
Office	0.55%	0%
Residential/student accommodation	0.61%	0.1%
Retail	0.84%	0%



REGION	OPERATIONAL AVERAGE PRICING (AS A PERCENTAGE OF POLICY LIMIT)	REAL ESTATE AVERAGE PRICING (AS A PERCENTAGE OF POLICY LIMIT)
Asia	2.3%	1.5%
Australasia	1.3%	1.1%
Benelux	1.3%	0.8%
CEE	1.3%	0.8%
DACH	1.4%	0.7%
France	1.4%	0.8%
Latin America	3.5%	3%
MENA	1.9%	1%
Nordics	1.2%	0.8%
Southern Europe	1.4%	1.1%
US	3.2%	2.5%

6 | Deal terms in the US, UK and Europe – similarities and differences

We continue to see that the UK broadly remains a seller-friendly environment for M&A deal terms, whereas the US market is much more balanced. The European market is closer in approach to the UK. In some aspects, however, the picture was more nuanced in 2022 given the general cooling of the market, particularly in the second half of the year.

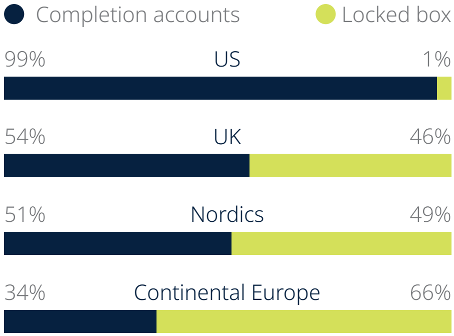
Closing pricing mechanism

Virtually all US deals have a completion accounts pricing mechanism. In Europe, locked box mechanisms prevail, with completion accounts found in just under half of majority share deals. Locked box mechanisms have become firmly established in Continental Europe, where they were seen in two-thirds of deals in 2022. In contrast, we've consistently seen over the last few years that locked box mechanisms are failing to gain any sort of traction in the US. However, the UK saw a slight shift towards completion accounts in 2022, perhaps indicative of a more uncertain deal environment.

"Both US and UK buyers have been active in Continental Europe despite the war in Ukraine. Deal terms are influenced by their domestic markets and the use of pricing mechanisms familiar in their home jurisdictions illustrates this."

Nils Krause
Partner, Germany

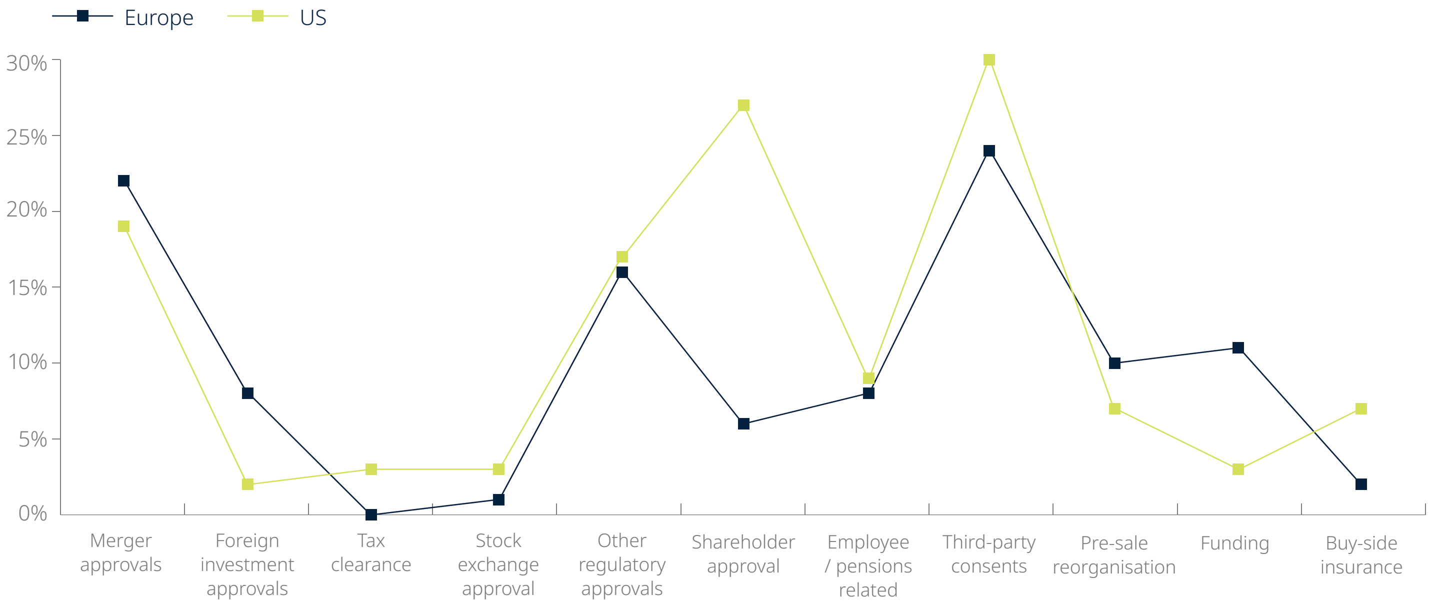
Closing pricing mechanisms



Conditions

As in 2021, the types of conditions seen in US and European deals were notably similar, although merger control and foreign direct investment approvals are more frequently seen in Europe compared to the US.

Conditions: US vs Europe



Gap protections

We consistently see that US deals have many more "outs" for a buyer than in Europe – material adverse change (MAC) conditions are more common and protections for warranty breach are standard. In Europe, use of gap protections is not significantly different between the UK, Continental Europe and the Nordics.

In North America, although MAC conditions to closing are more commonly seen than in Europe, they're also highly negotiated in every deal with a myriad of exceptions resulting in an extremely high threshold which must be met before the condition can be invoked. This means MAC conditions are rarely invoked in practice – there has only been one reported case in which a buyer successfully used a MAC condition to terminate the acquisition.

#1 Europe M&A by deal count
(for the last ten years)
(*Mergermarket, 2013-2022*)

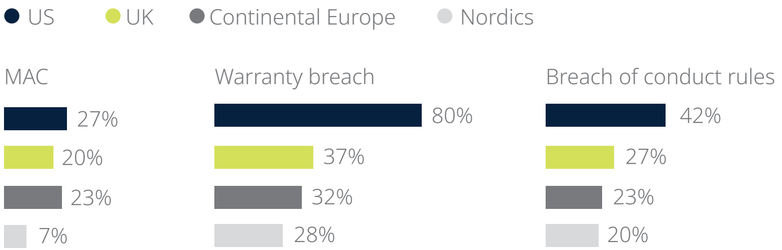
#1 UK M&A by deal count
(for the last thirteen years)
(*Mergermarket, 2010-2022*)

#4 US M&A by deal count
(*Mergermarket, 2022*)

"Contrary to European market standards, US buyers in European deals still tend to expect a number of exit rights between signing and closing a transaction, including material adverse effect and warranty bring down protections, allowing the purchaser to walk away from and refuse to close the transaction rather than being forced to close and 'only' claim monetary compensation for certain breaches."

Benjamin Parameswaran
Partner and Global Co-Chair, Corporate

Gap protections



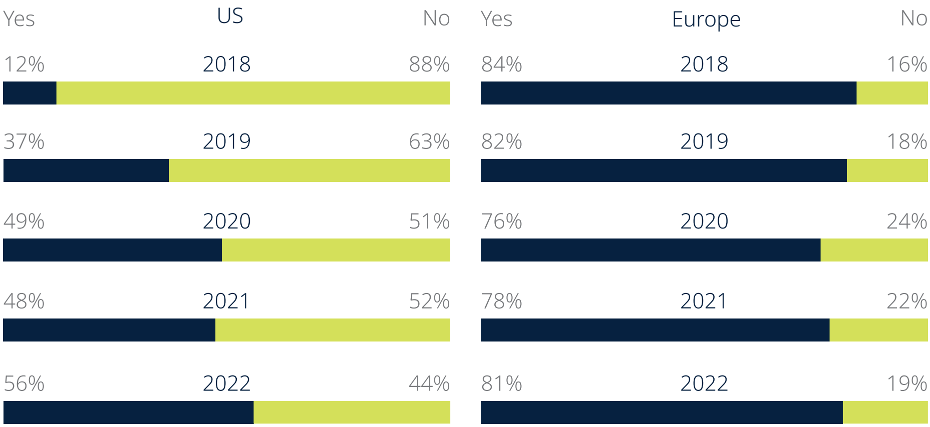
Data room disclosed

In Europe, it remains standard practice for all data room documents to be treated as generally disclosed against the warranties as a whole. Interestingly, while general disclosure of the data room has been increasingly seen in US deals over the last several years, it's still not market standard. It'll be interesting to see whether general disclosure of the data room continues to gain traction and whether the marked difference in approach between the US and Europe continues to narrow.

"In the US, general disclosure of the data room continues to be a highly negotiated provision and, with a softening of the market, we expect to see buyers continue to push back on the inclusion of this provision."

Jon Venick
Partner, US

Data room disclosed



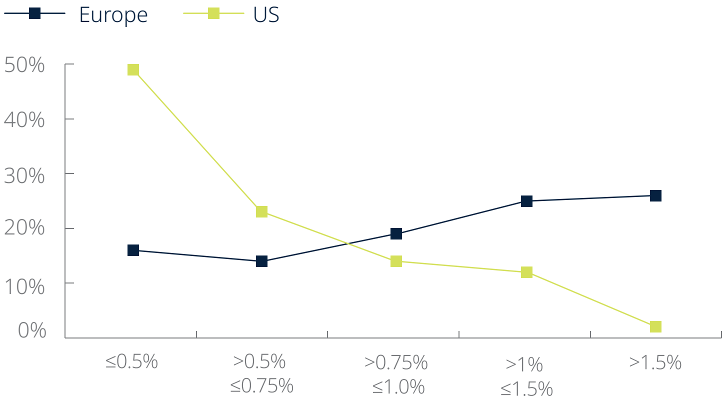
Limits on commercial warranties

There remain marked differences between US and European deals, with jurisdictional differences in Europe too.

CLAIMS THRESHOLD

In uninsured deals, claims thresholds are generally lower in the US. Nearly half of uninsured US deals had a claims threshold of 0.5% of the price or less. This is driven largely by the increased prevalence of thresholds that are set as an excess/deductible – found in nearly half of US uninsured deals this year. In contrast, thresholds set as an excess are unusual in European deals – in nearly 90% of uninsured European deals, the claims threshold was set as a trigger or tipping basket. As a result, claims thresholds tend to be higher in Europe compared to the US – around half are more than 1% of price.

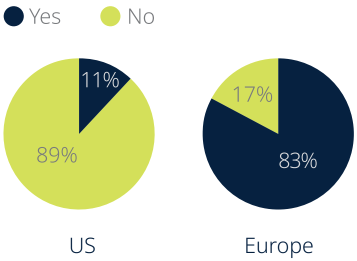
Claims threshold as % of price (excluding buy-side insured deals)



SMALL CLAIMS EXCLUSION

Small claims (or individual de minimis) exclusions are common in Europe, whereas they're only seen in a minority of US deals. There are some regional differences in Europe but generally the vast majority of deals in each of the UK, Nordics and Continental Europe include a small claims exclusion.

Small claims or de minimis



COMMERCIAL WARRANTY CAP (EXCLUDING BUY-SIDE INSURANCE DEALS)

The commercial warranty cap is typically lower in uninsured US deals compared to European deals. Just over half of uninsured US deals included a cap lower than 20% of price – compared to only 12% of European deals. Deal size and deal process did not particularly influence the level of cap in the US.

In Europe, cap size is generally driven by deal process and deal size – auctions continue to drive lower caps and caps tend to be lower as deal value increases. Caps below 20% of price are more common in Europe further up the value chain (in deals above EUR250 million) whereas the most common cap for smaller to mid-size deals is between 20% and 40% of price.

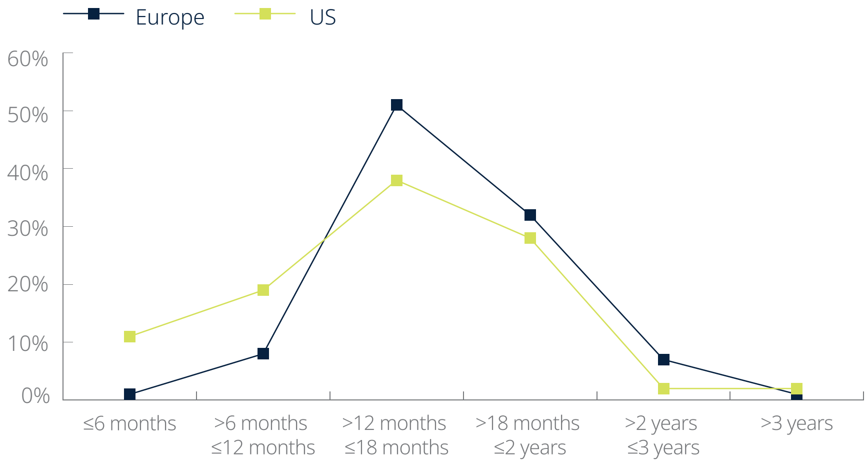
"It's important for buyers and sellers to understand what standard deal terms are in the jurisdiction where they're transacting, particularly if it's not their home jurisdiction. Buyers and sellers may be able to take advantage of more buyer or seller (as applicable) friendly deal terms in that jurisdiction than they would in their own jurisdiction. Conversely, something that's 'normal' in their home jurisdiction may be seen as very aggressive by their counterparty and could create deal issues if requested."

Maria Doralt
Partner, Austria

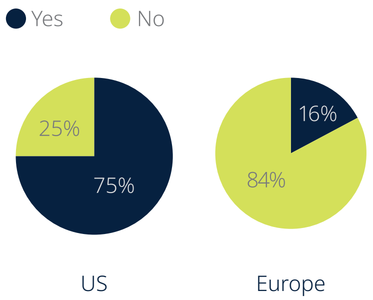
COMMERCIAL WARRANTY PERIOD (EXCLUDING BUY-SIDE INSURANCE DEALS)

US commercial warranty claim periods are generally shorter than those in Europe. The US continues to see warranty periods of 12 months or less in around 30% of its uninsured deals (in Europe, less than 10%), although in both the US and Europe the most common claim period was 12–18 months.

Commercial warranty period
(excluding buy-side insured deals)



Deals with security for claims



SECURITY FOR CLAIMS

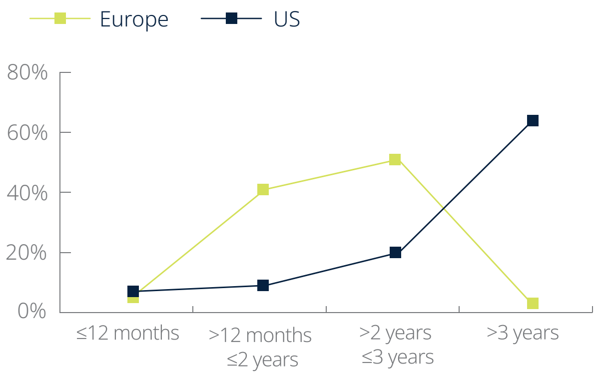
Escrow or holdback for claims remains standard practice in the US – whereas in Europe, escrows or holdbacks are seen in only a minority of deals and generally only where there's concern about the financial standing of the seller or otherwise in respect of the seller's ability to meet warranty claims.

The typical escrow period for US deals is 12 months for insured deals and 18 months for uninsured deals. In Europe, escrows tend to be more bespoke so release periods are more varied – but most commonly are between 12 months and 2 years. Escrow amounts are more standard in the US too, generally around 10% of price in uninsured deals and 1–2% of price in insured deals. Escrow amounts in European deals vary depending on the nature of the claims being secured, but tend to be 10% or below on insured deals and greater than 10% on uninsured deals.

NON-COMPETE PERIODS

US deals, in particular those involving individual or family sellers, generally include longer non-compete periods given by sellers than in Europe. In both the US and Europe, we tend to see shorter periods when trade or private equity are selling, as they're reluctant to accept restrictions on their post-closing commercial activities. In addition, non-compete periods above three years are generally unenforceable in Europe, whereas in the US, periods of up to five years are usually enforceable provided they're given as part of the deal consideration.

Non-compete periods



7 | Are deals becoming less certain?

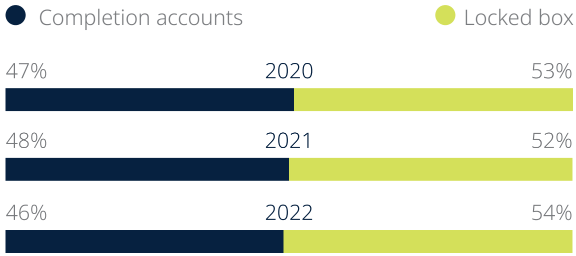
Undoubtedly 2022 was a year of increased economic uncertainty, especially during the second half of the year. Was this turbulent environment also reflected in deal terms? In this section, we look at some key deal terms to assess whether deal terms relating to pricing and execution are becoming less favourable for sellers.

There were variations within Europe – in the UK where the locked box has been established for many years, its use slightly decreased in 2022, perhaps due to the increasing prevalence of smaller deals in the second half of the year in tightening debt markets.

Pricing mechanisms

A locked box mechanism offers sellers (and buyers) price certainty and, in an auction, enables sellers to directly compare bids (as they're made on the same financial basis). Locked box continues to be the favoured pricing mechanism in Europe and was used in the majority of European deals for the third year running. In contrast, completion accounts continue to dominate in North America and Asia Pacific – we've seen very little movement towards adoption of locked box mechanisms in the US in particular.

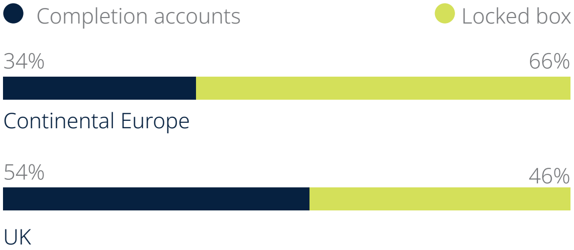
Closing pricing mechanism: European majority share deals



"In Japan, the US-style purchase price adjustment structure has been prevalent, but recently we're seeing an increase in locked box structures in auction deals."

Masahiko Ishida
Partner, Japan

Closing pricing mechanism: Majority auction share deals



Locked box continued to be used in the majority of auction deals in Europe, driven by its use in two-thirds of Continental European auctions. In contrast, a majority of UK auctions used completion accounts. We think this is likely to be caused by decreased private equity activity in auctions overall, especially in the second half of 2022 (see section 2) and some increased caution in the market generally following a hot seller's market in 2021.

Earn-outs

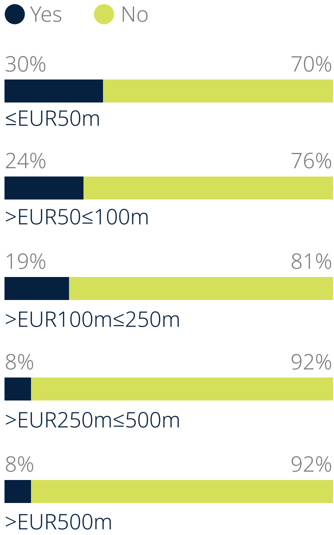
Uncertain markets can lead to valuation difficulties and greater uncertainty over post-closing performance. Earn-outs are a way to bridge pricing gaps between buyers and sellers. We saw nearly a 20% increase in earn-outs in the 2022 deals surveyed compared to 2021, driven mainly by an increased use of earn-outs in Europe and Asia Pacific – perhaps an indication of a softening market.

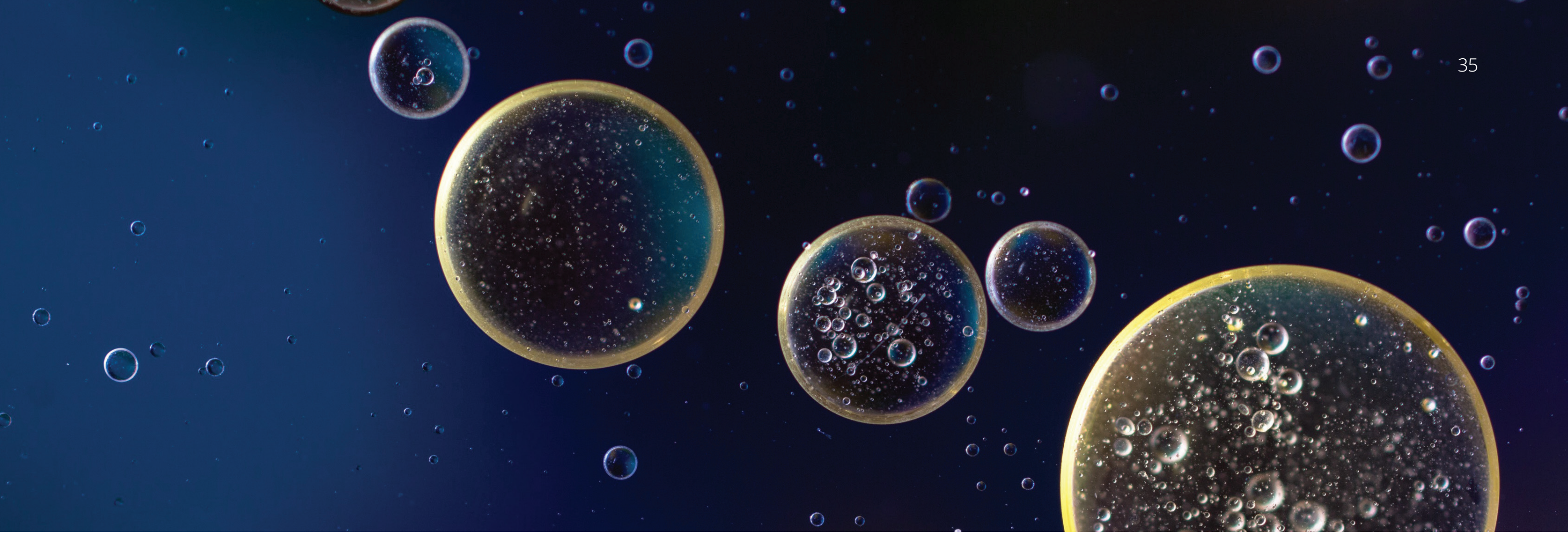
The continued strength of the technology sector in 2022 may also have been a factor – earn-outs have historically been more common in this sector and in 2022 more than a quarter of technology deals included an earn-out.

In Europe, we consistently see a greater use of earn-outs in sub-EUR25 million deals, as this deal size typically includes early stage deals, sales by founders and smaller businesses that are likely to be more dependent on key individuals. In 2022, however, we saw earn-outs become increasingly common in deals between EUR25 million and EUR100 million. For example, in Continental Europe 54% of deals between EUR25 million and EUR50 million included an earn-out.

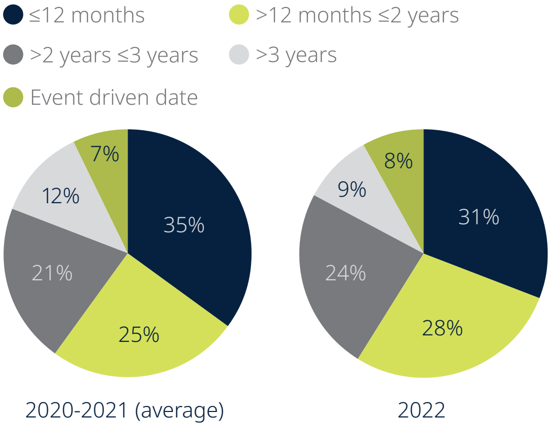
#1 Europe Telecoms, Media & Technology M&A by deal count
(for the last thirteen years)
(*Mergermarket, 2010-2022*)

% of deals with earn-outs by deal value





Earn-out periods



In deals containing an earn-out mechanism, an earn-out period of up to one year remained prevalent globally. But we saw a shift towards longer earn-out periods particularly in the UK, Continental Europe and Asia Pacific. In these regions, the majority of earn-out periods were between 12 months and three years. This means a longer period of price uncertainty for sellers and could indicate that buyers had less confidence in future business performance.

"Earn-outs and equity rollovers have continued to be a key feature of technology M&A in the Asia Pacific region. While earn-outs are seen in trade sales, private equity funds focused on software almost always require key managers to continue with a meaningful stake rolled over following a buyout."

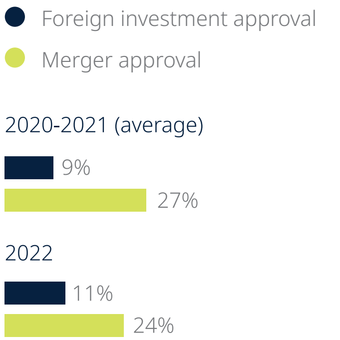
Joel Cox
Partner, Australia

Conditional deals

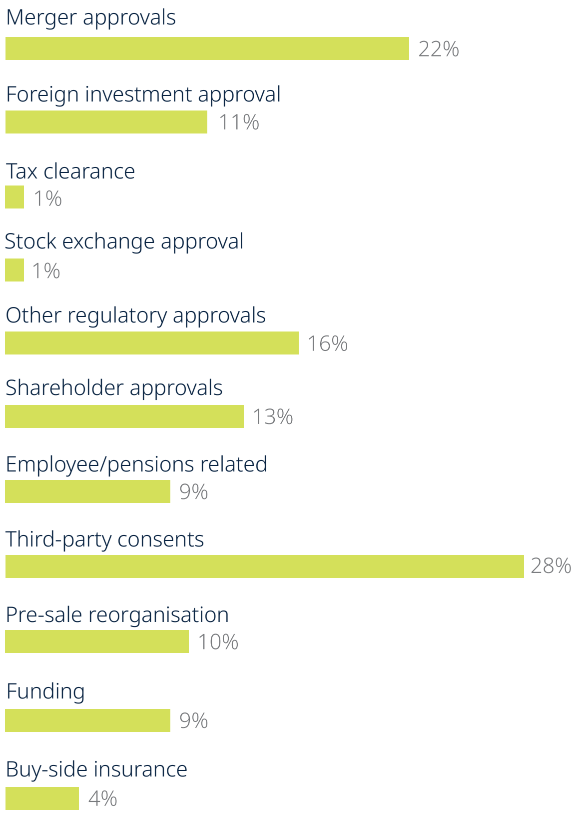
A deal with a split signing and closing is inherently more uncertain. Any condition to closing which is outside the immediate control of the parties inevitably creates greater execution risk – in particular conditions which are dependent on the approval of a third-party such as those triggered by merger control laws, foreign direct investment restrictions and other regulatory requirements or third-party consents.

A majority of deals surveyed had a split signing and closing, a slight increase from both 2020 and 2021. Merger control/anti-trust approvals, other regulatory approvals and third-party consents were the most common conditions, with some regional differences. Perhaps surprisingly given the introduction of additional foreign direct investment regulation in many European jurisdictions in the last couple of years, we saw only a slight increase in foreign investment approval conditions across all of our deals globally during 2022.

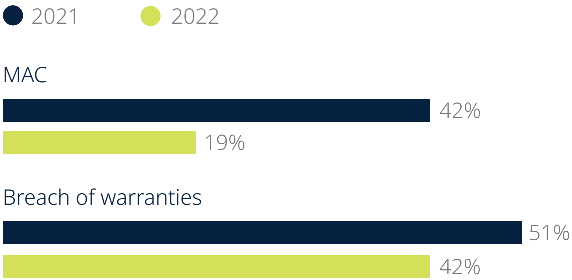
Merger and FDI conditions



Conditions: All deal types



Gap protections



Gap protection

Managing and allocating risks relating to the target's business during the gap between signing and closing is one of the most complex issues in private M&A. Typical gap protections in all regions include a buyer's right not to close if there has been:

- a breach of representations and warranties – both those given at signing and, in some cases, as repeated or "brought down" after signing (with differing standards of materiality applicable to the representations and warranties which are brought down);
- a failure to comply with interim covenants (typically in "all material respects"); and/or
- a material adverse change (MAC) – being the occurrence of an unexpected event that has a materially adverse effect on the target's business taken as a whole.

In a softening market, we might expect the use of MAC clauses and other gap protections to increase. This was not the case in 2022 and our data shows a decline in the use of MACs overall. We also saw a slight decline in the use of termination rights around breach of warranty. We saw similar trends during the COVID-19 pandemic when the use of MACs and provisions allowing termination for a material breach of warranties repeated at closing also declined.

Perhaps the biggest decision for parties was really whether or not to proceed with a deal and once that commitment was made, sellers were willing to push hard to avoid the uncertainty of "get out" clauses.

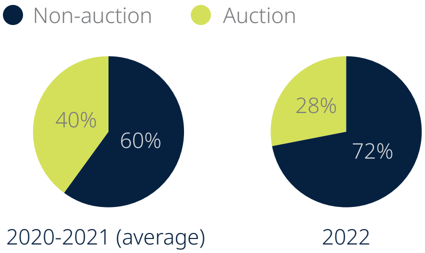
"In North America, a MAC condition to closing is fairly standard. More importantly, a MAC bring down on the representations is standard and present in virtually every public deal. Given recent global events and market volatility, we expect to see an increased use of the straight 'No MAC' closing condition."

Chris Giordano
Partner, US

8 | Are deal terms changing in auctions?

Overall, we saw a reduction in the use of auction processes in 2022 across all deal sizes. This is perhaps one of the factors we think demonstrates a slightly softer market than in 2021. Fewer competitive auction processes also had some effect on the deal terms achieved in auctions this year.

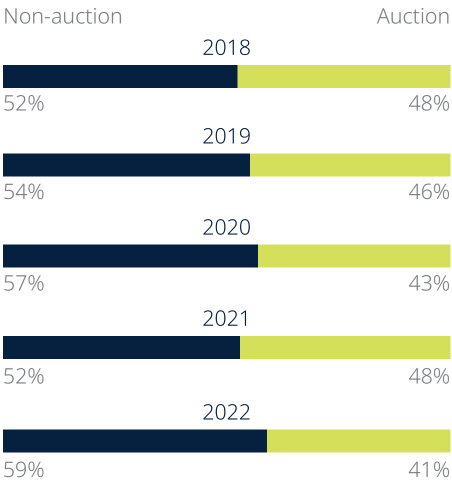
Deal process: Deals over EUR50m



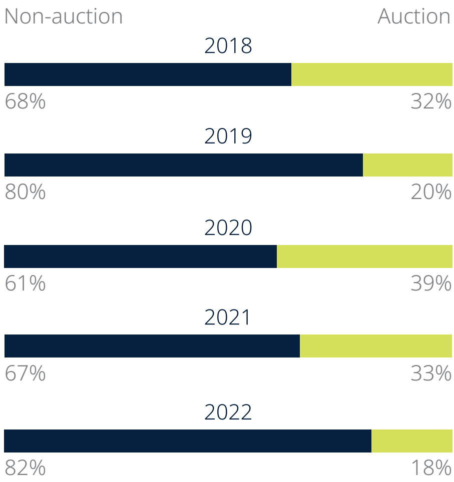
Buyers and sellers in auctions

Although private equity sellers continued to use auctions in more of their exits than trade sellers, both trade and private equity sellers opted for an auction in fewer of their exits compared to previous years.

Private equity sellers: Deals over EUR50m



Trade sellers: Deals over EUR50m

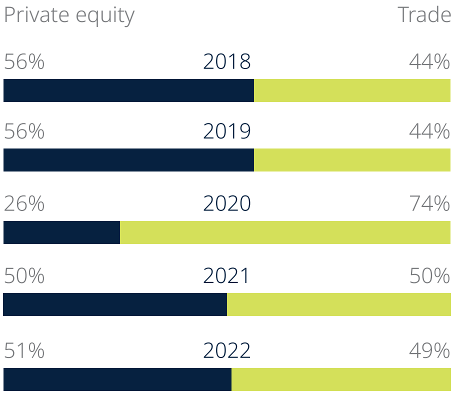


Private equity buyers narrowly won the majority of auctions, although private equity's success in auctions hasn't yet returned to the levels seen in 2018–19.

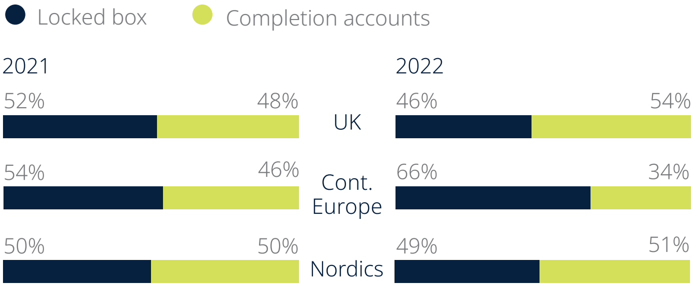
PRICING MECHANISM

Overall, locked box mechanisms continued to be used in the majority of auction deals in Europe, although their use slightly decreased compared to 2021.

Buyers in auctions



Closing price mechanism: European majority share deals



"2022 saw fewer auctions than in 2021 and, importantly, fewer really competitive processes. This affected the deal terms seen in auctions, which were more buyer friendly than they were in 2021."

Tracey Renshaw
Partner, UK

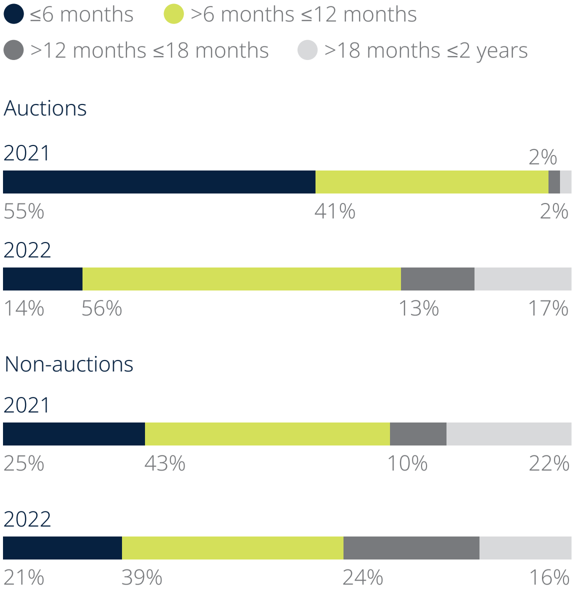
"In the Netherlands we see that trade buyers are gaining momentum in auctions and are willing to commit to locked box and the use of W&I insurance to be competitive with private equity bidders."

Daphne Bens
Partner, Netherlands

LEAKAGE CLAIM PERIODS

In 2021, it was clear that auctions generally delivered shorter leakage claim periods for sellers. In 2022, this was less obviously the case – as leakage claim periods generally increased, we saw the differences between auctions and non-auctions narrow.

Leakage claim periods: By deal process



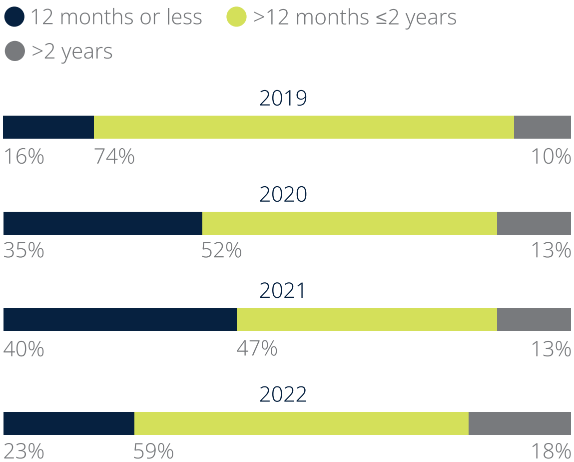
GAP PROTECTION

While our data indicates that in the US, deal process had little effect on whether buyers were able to obtain MAC and breach of warranty gap protections, outside the US and perhaps as you would expect, buyers remain less likely to obtain these gap protections in auctions.

AUCTION COMMERCIAL WARRANTY PERIODS

We saw a shift towards longer commercial warranty periods in auctions during 2022 – again perhaps indicative that there were fewer of the highly competitive auction processes we saw in 2021.

Auctions commercial warranty periods

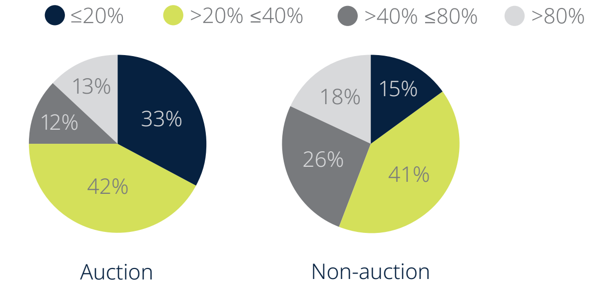


#4 Americas M&A by deal count
(*Mergermarket, 2022*)

COMMERCIAL WARRANTY CAPS (EXCLUDING BUY-SIDE INSURED DEALS)

We saw a slight shift towards higher caps in 2022 – although this was more significant in non-auction deals. In auction deals, the majority of commercial warranty caps were below 40% of price, as in 2021 – but we saw fewer deals with caps below 20% in 2022.

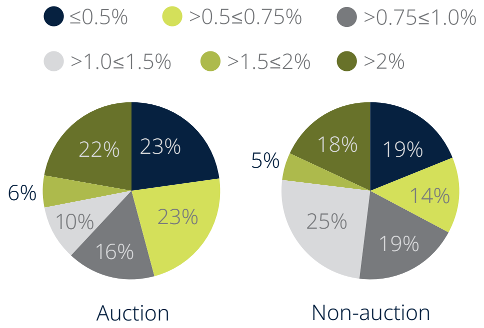
Commercial warranty cap (excluding buy-side insured deals)



CLAIMS THRESHOLD (EXCLUDING BUY-SIDE INSURED DEALS)

Auctions did not particularly drive higher claims thresholds for sellers in 2022, except for thresholds above 1.5% of price. Thresholds in non-auction uninsured deals remained broadly consistent with 2021.

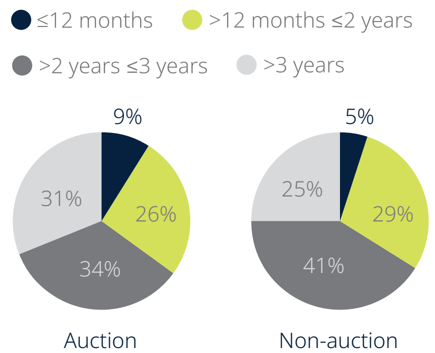
Claims threshold as % of price (excluding buy-side insured deals)



RESTRICTIVE COVENANT PERIODS

Deal process does not seem to have a significant effect on the length of non-compete and non-solicitation covenants in the context of a sale of a business. Generally, there's a trend towards slightly shorter non-competes and non-solicits on auction deals, although year-on-year changes have not been significant.

Non-compete periods: By deal process



9 | Are limitations shifting in favour of buyers?

Despite a more buyer-friendly environment in 2022, we haven't seen a dramatic change in limitations in favour of buyers. This is perhaps indicative that market practice around limitations has become ingrained in many regions – such that external events affecting M&A deal-making generally do not permeate into negotiations around limitations in the acquisition agreement once the parties have committed to doing the deal.

"Well-advised parties spend little time negotiating limitations. Market standard positions have been further entrenched with the acceptance of W&I as a conventional M&A tool."

Victoria Rhodes
Partner, UK

As has been the case for several years – including during the COVID-19 pandemic – we continue to see consistent themes in our data.

Commercial warranty claim periods

In all regions, the majority of uninsured deals had a time limit for commercial warranty claims of two years or less. We saw a reduction in warranty claim periods of 12 months and below (except in the US) – possibly driven by fewer auction processes during 2022.

Commercial warranty caps

Globally, the majority of commercial warranty caps in uninsured deals were less than 40% of price and most commonly between 20% and 40% of price (although in small deals it's not unheard of to see caps of 100% of purchase price). In the US, in uninsured deals, the majority of caps were below 20% of price, whereas in Europe the majority were between 20% and 60%. We saw fewer caps below 20% in 2022 compared to the two previous years, indicative of a slight shift towards a more buyer-friendly approach. Deal process and deal size continue to drive lower commercial warranty caps – we saw lower caps generally in auctions and lower caps as deal size increases. Caps below 20% of price were more common in mid and large sized deals, whereas caps above 40% were unusual in these deal size ranges.

Small claims exclusion

Globally, small claims exclusions (where claims below a specified amount are ignored completely or ignored in meeting any claims threshold or basket) were most commonly between 0.05% and 0.1% of price.

Claims threshold

It's standard market practice to have a claims threshold or basket when commercial warranties are given – being an amount which claims must exceed before they can be brought against the sellers. In the majority of deals in Europe and Asia Pacific, the claims threshold is set as a trigger or "first dollar basket" – in the US, in uninsured deals, thresholds remain evenly split between a trigger or "dollar-one" recovery and an excess or deductible (when set as an excess/deductible, the buyer can only recover amounts above the threshold). The majority of claims thresholds globally were below 1% of price, although in Europe we saw a slight shift to larger thresholds as the most common threshold was between 1% and 1.5% of the price. This suggests a shift in favour of sellers rather than buyers.

For further details, see our databank on 2022 deals in section 12.

10 | How deals are different in Benelux

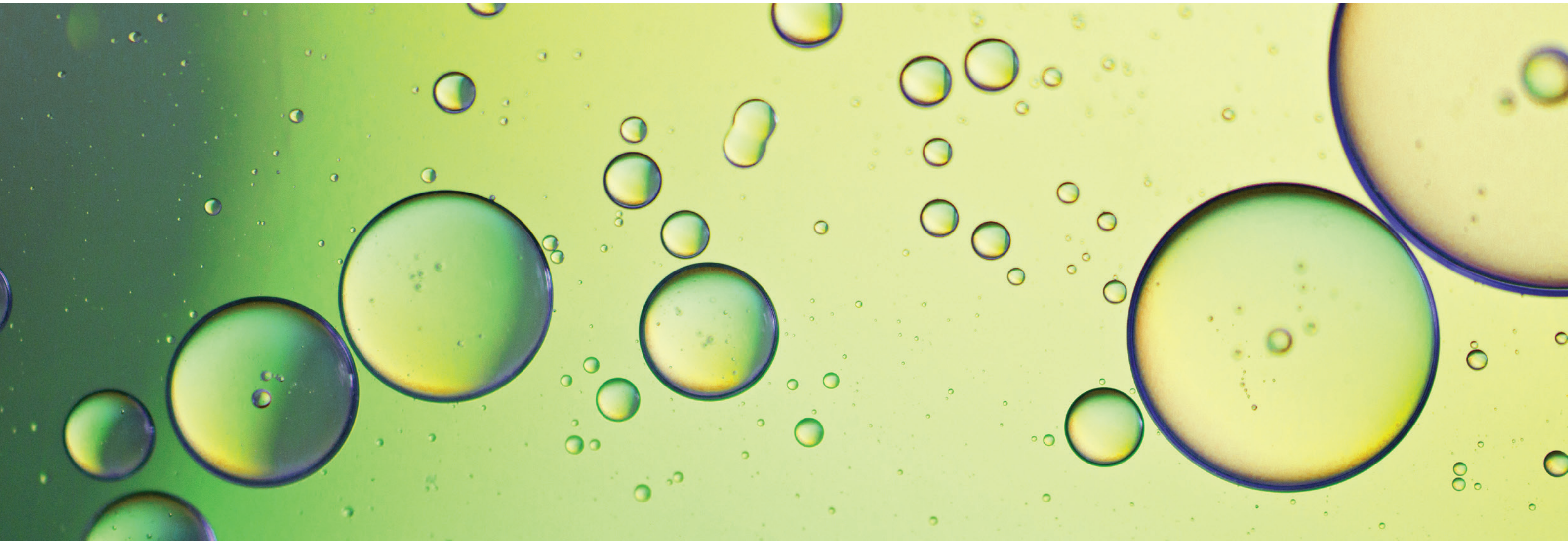
"Benelux is often viewed as one single, harmonized M&A market, but buyers and sellers alike should be aware that transaction terms and processes in the three countries differ quite substantially."

Koen Selleslags
Partner, Belgium

M&A rankings often present Benelux as one single, monolithic market. This is because Belgium, the Netherlands and Luxembourg are relatively small. But it doesn't do justice to the different approaches to M&A in these countries.

M&A markets differ substantially between the three countries because of their different economic make-up. Perhaps more surprising, transaction terms and processes are also very different.

Sellers and buyers should always consider local practice when undertaking M&A transactions. Benelux shows there are significant differences between neighbouring countries. Even though on first glance they look very similar.



M&A market

Belgium has historically been an SME country. Relatively few businesses have grown into huge multinational groups. Often, once SMEs reach a certain size, the owners look for an opportunity to sell, rather than growing the business to take it to the next level. But recently this is starting to change. More Belgian companies are doing acquisitions abroad. But there are still many SMEs (with retirement-age owners) coming on to the market.

The Netherlands business world has traditionally been very international in its outlook. We can see this in the many global powerhouses with Dutch roots. The beneficial tax system and other incentives encourage multinational groups to move their corporate headquarters to the Netherlands.

Luxembourg is quite different from Belgium and the Netherlands. Because of its size, the market for local strategic M&A transactions is much smaller. But Luxembourg has developed a highly technical fund market. Its capital market is also very well developed – many public transactions are structured through Luxembourg.

#1 Benelux M&A by deal count

(*Mergermarket, 2022*)

"Unlike most other countries, the works council plays an important role in a transaction. But if their involvement is well managed, this is a matter of timing more than anything else."

Pieter Paul Terpstra
Partner, Netherlands

Transaction terms and process

The influence of Anglo-Saxon deal terms is very clear throughout the whole Benelux region. But the Netherlands is generally quicker to adopt new trends. For example, warranty and indemnity insurance was common in the Dutch market years before it took off in Belgium. Tax indemnities are standard in Dutch deals. Most Belgian transactions only provide tax warranties.

There are also significant differences in M&A process in the three countries. A good example is employee involvement. In the Netherlands, the target's works council (which businesses with 50 employees or more must have) plays an important role in the deal process. It has a crucial advisory function on the transfer of control after the transaction and the related financing aspects. The works council procedure has to be managed carefully. And it inevitably affects the timing of the transaction process.

In Belgium, there's no formal advisory role for employees – though they do need to be informed of the transaction before it's made public and consultation requirements may also apply.

Share transfer formalities are also different. In the Netherlands, a notary public has to be involved in a share deal. They'll deal with the formal recording of the transaction in the corporate registers. And they usually act as an agent in purchase price payment. In Belgium, legal counsel usually take care of the transfer formalities.

11 | M&A in Southeast Asia: Key challenges and issues

"In Southeast Asia, understanding the unique differences across jurisdictions and specific nuances within them is a key ingredient to ensuring success. Local and on-the-ground advisors are an important component in not only navigating cultural and regulatory differences but can also challenge practices and processes that may simply not apply in this diverse region."

David Kuo
Partner, Singapore

We highlight the key challenges of doing M&A transactions in Southeast Asia and how foreign buyers can be successful in the region.

Diversity of jurisdictions

Southeast Asia is often described as a homogeneous region. But each country is very different in size, political and legal system, level of development and culture.

The size of the economies differ massively. Laos's GDP is USD15 billion. Indonesia's is USD1.4 trillion. The relative wealth also varies enormously. Cambodia, Laos and Myanmar have GDP per capita of under USD2,000. Singapore's GDP per capita is USD84,500 – higher than most developed nations.

Because of this diversity, cultural and market practices can vary greatly. A buyer needs to understand these differences to be successful in pursuing M&A opportunities in the region.

#1 South East Asia M&A by deal value
(*Mergermarket, 2022*)

Lack of targets for control acquisitions

Relative to its size, Southeast Asia has much fewer M&A transactions compared to Western countries. It's hard to find appropriate targets and willing sellers. Why is that?

- **Concentration of ownership.** In most countries in Southeast Asia, a handful of families run large conglomerates that dominate in many segments in the local economy. These families often don't want to sell their businesses, even by the second or third generation. The businesses are often viewed as an heirloom to be passed on to future generations.
- **Preference for IPOs.** Buying a successful startup businesses in Southeast Asia can be difficult. Business owners everywhere can be attached to the company they founded. But it's often even more difficult to convince business owners in Southeast Asia to sell their company. There's a strong preference for IPO over a trade sale. Taking a company public is seen as the ultimate goal of starting a business. Many of the stock exchanges in the region will list relatively small companies. And they often have standards that are relatively lax compared to stock exchanges in Western jurisdictions. So an IPO is the preferred exit (over a trade sale).

Foreign ownership restrictions

In most countries in Southeast Asia, foreign owners have to comply with a range of restrictions. The restrictions vary from country to country:

- **Vietnam**: Foreign banks can establish wholly owned subsidiaries as an LLC with a minimal equity capital and approval from the State Bank of Vietnam. They can also acquire up to 30% of a domestic bank (with no single foreign shareholder owning more than 20%, and each holder above 5% subject to fulfilling certain asset and profitability conditions).
- **Indonesia**: Foreign investments are subject to an extensive regulatory framework. An "Investment List" sets out those sectors where foreign investment is restricted, the requirement to incorporate a specific type of company that allows foreign investment (a PT PMA), and licensing requirements based on the sectors it operates in.
- **Philippines**: Foreign investments are subject to equity ownership limitations based on sectors. For example, public utilities, private land, educational institutions can only be owned up to 40% by foreigners (subject to limited exceptions). Where equity ownership interests are imposed, foreign investors need to be prepared to accept JV structures, often with only limited consent rights and no control. Some may pitch deals with nominee or trustee structures to circumvent these restrictions. But foreign investors have to be careful using mechanisms like this. They can be (and often are) invalidated.

Regulatory environment

Many businesses in Southeast Asia rely on good relationships with the government and local authorities. Foreign buyers have to be careful these relationships continue after the acquisition and can be sustained lawfully. Particularly in less developed countries, there are often issues around the US Foreign and Corrupt Practices Act and the UK Bribery Act. Proper due diligence is key in uncovering these issues (as potential illegal payments are often disguised as legitimate expenses).

Key recommendations

We've looked at the challenges of doing M&A transactions in Southeast Asia. What should a foreign buyer do to be successful in the region?

- **Use local, knowledgeable advisors.** The most fundamental key to completing a successful M&A transaction is having a good team in place. In Southeast Asia, this means making sure the relevant internal and external experts understand the region well. There are many traps in doing transactions in certain parts of Southeast Asia and people with local experience are irreplaceable to make sure the buyer avoids them. Applying a standard European or North American approach to a deal in Southeast Asia won't work. You have to understand the regulatory regime and market practices in each country.
- **Do your due diligence.** Having an established process is important in identifying the potential issues and pitfalls. Proper due diligence is vital. In many jurisdictions, this goes beyond the typical legal and financial review that's done in Western jurisdictions. In many instances, background checks and other types of risk analysis investigations may be appropriate to identify a target's practices that may be problematic.
- **Enforce your rights.** Buyers can't just rely on the legal protections in the transaction documents to protect their interests. In some jurisdictions in Southeast Asia, enforceability of claims (particularly by foreign parties) may not be transparent or easily accessible. A foreign investor has to understand the regulatory and enforcement landscape. And if there's a dispute where the local counterparty doesn't have assets in other jurisdictions that can be enforced upon, the foreign investor may have to rely on other tools. These can include public relations, getting help from relevant foreign embassies and lobbying government regulators to pressure the local counterparties.

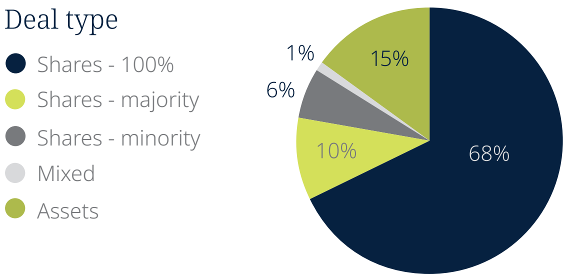
12 | DLA Piper M&A Databank on 2022 deals

12.1 Deal types and process

In all regions in 2022, share deals continue to dominate with 78% of the deals surveyed structured as an acquisition of all, or the majority of, the shares of a target company.

Asset deals account for less than 10% of European deals, but were more common in the US, accounting for 29% of US deals surveyed.

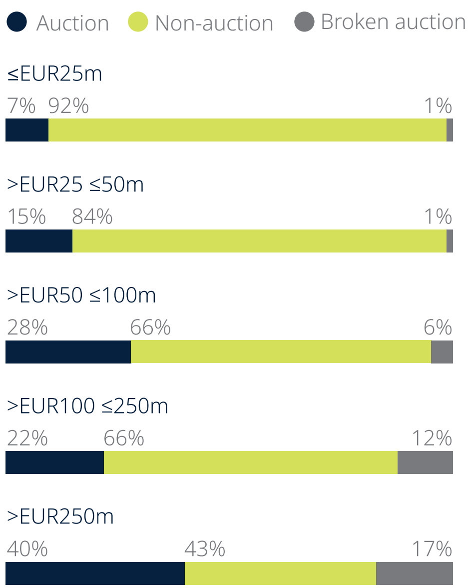
Deal type



Overall, we saw a slight reduction in auctions in 2022, perhaps indicative of a slightly softening market. Consistent with previous years, we saw the use of auctions increase with deal size.

Broken auctions were driven by successful pre-emptive bids.

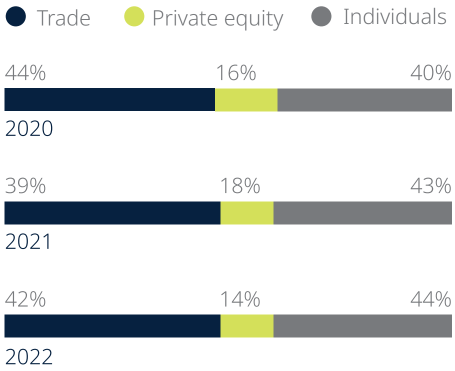
Deal process by deal value



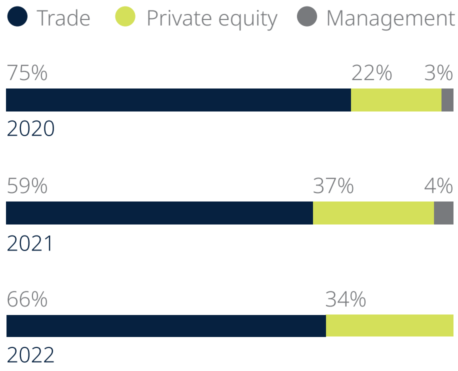
With some regional variation, overall 2022 saw a slight reduction in the number of private equity sellers with trade sellers dominating in Europe and Asia Pacific and individual sellers forming the majority of sellers in the US.

Trade buyers were seen in two-thirds of global deals surveyed, an increase compared to 2021. In the US, trade buyers increased their share of auction purchases to 40%, although private equity buyers made up nearly half of buyers in US deals overall.

Sellers by type



Buyers by type



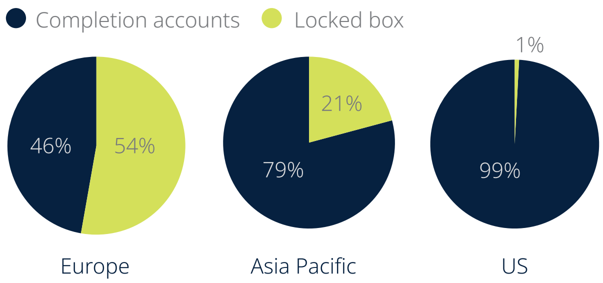
12.2 Closing pricing mechanisms: Majority share deals

Locked box continues to be the favoured pricing mechanism in Europe and was used in the majority of European deals for the third year running.

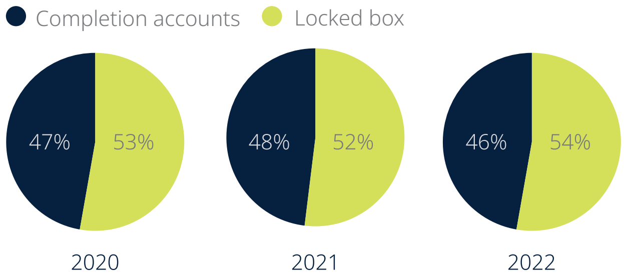
In the US and Asia Pacific, completion accounts continued to dominate, although the use of locked box mechanisms increased in Asia Pacific.

Where completion accounts were used, a combined net debt and working capital metric remained the favoured adjustment.

Closing pricing mechanism: By region



Closing pricing mechanism: Majority share deals Europe



#1 Nordics M&A by deal count
(for the last six years)
(*Mergermarket, 2017-2022*)

#1 Denmark M&A by deal count
(for the last five years)
(*Mergermarket, 2018-2022*)

#3 CEE M&A by deal count
(*Mergermarket, 2022*)

#4 Australasia M&A by deal count
(*Mergermarket, 2022*)

#1 Europe Industrials & Chemicals M&A
(*Mergermarket, 2017-2022*)

#1 Europe Consumer M&A
(*Mergermarket, 2018-2022*)

#3 Middle East & Africa M&A by deal count
(*Mergermarket, 2022*)

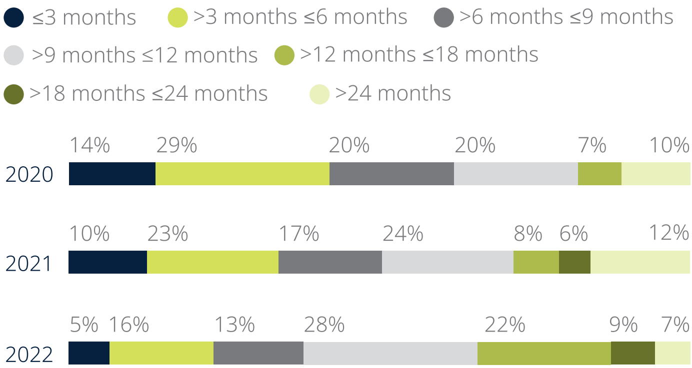
#4 DACH M&A by deal count
(for the last two years)
(*Mergermarket, 2021-2022*)

12.3 Locked box in Europe

A locked box mechanism protects buyers from the unauthorised extraction of value or "leakage" after the date to which the locked box accounts are prepared. This protection period is usually time limited.

2022 saw a shift towards longer leakage claim periods in Europe – two-thirds of European locked box deals saw a leakage claim period of more than nine months. In contrast, leakage claim periods greater than nine months were seen in only half of locked box deals in 2021 and in less than 40% of locked box deals in 2020.

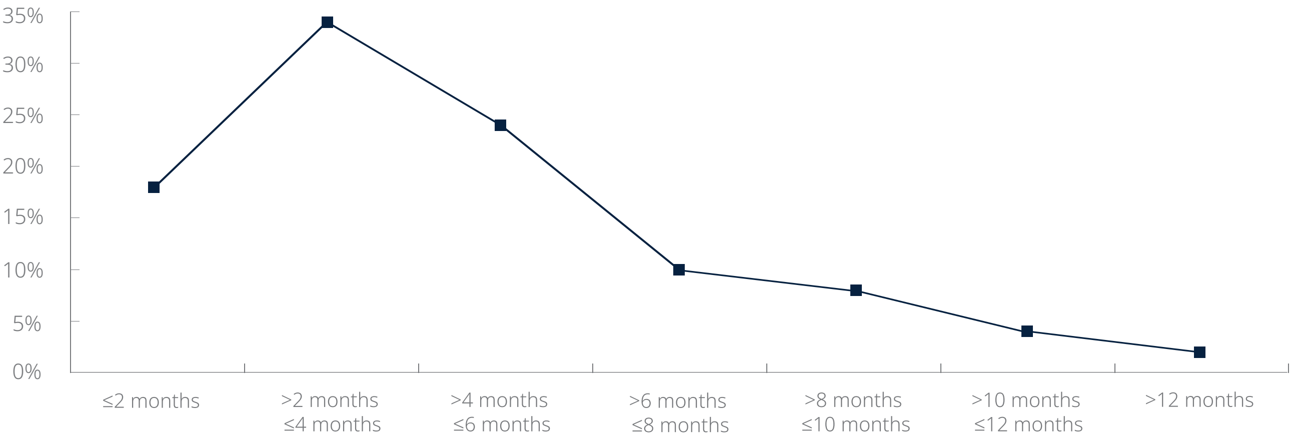
European leakage claim periods 2020-2022



The majority of locked box accounts in European deals that used a locked box pricing mechanism were audited.

For the third year running, locked box accounts were typically less than six months old.

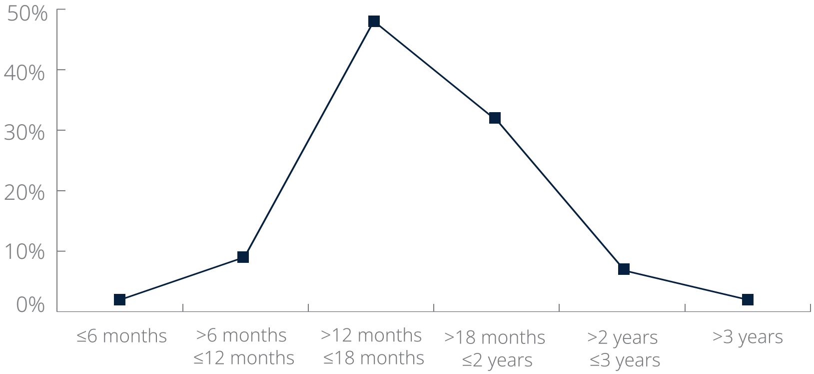
Age of locked box accounts: European majority share deals

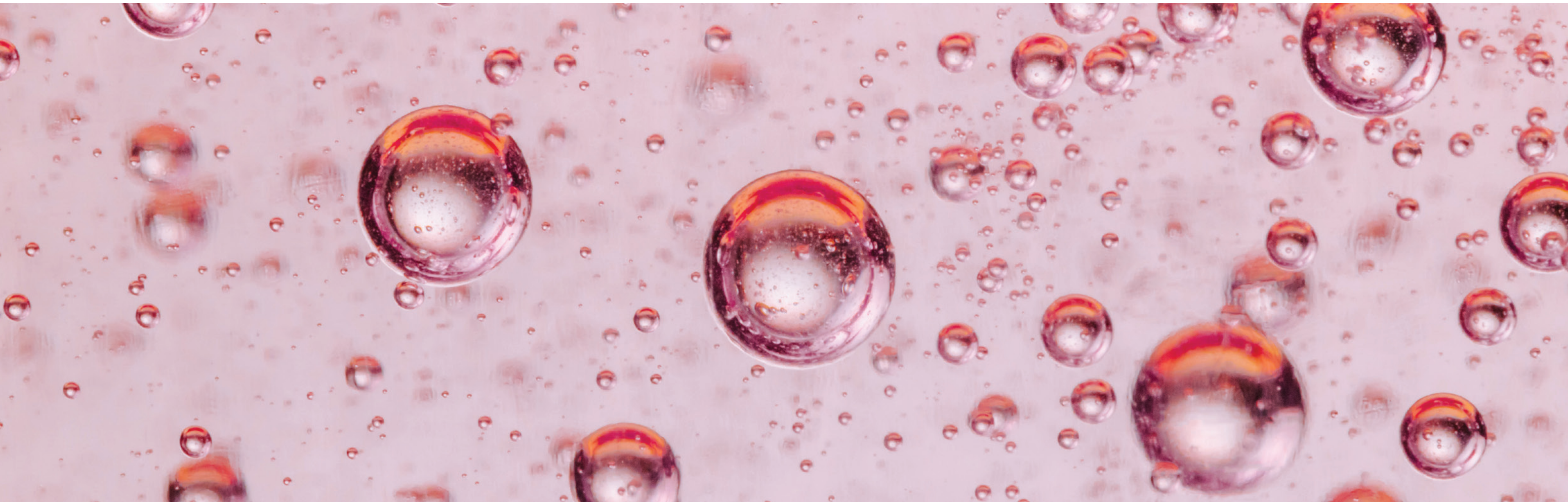


12.4 Commercial warranties: Time limits (excluding buy-side insured deals)

As in 2021, the majority of uninsured deals globally had a time limit of two years or less for commercial warranty claims.

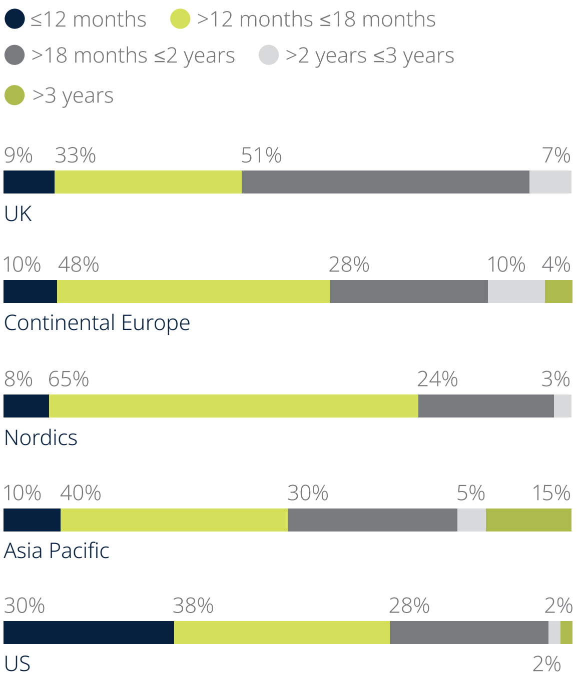
Commercial warranty period
excluding buy-side insured deals: Global





Regional variations remain with the US seeing the shortest time limits – nearly a third of deals had a warranty claim period of 12 months or less. The Nordics also saw shorter time limits – nearly three-quarters of deals had a warranty period of up to 18 months.

Commercial warranty time limits (excluding buy-side insured deals)

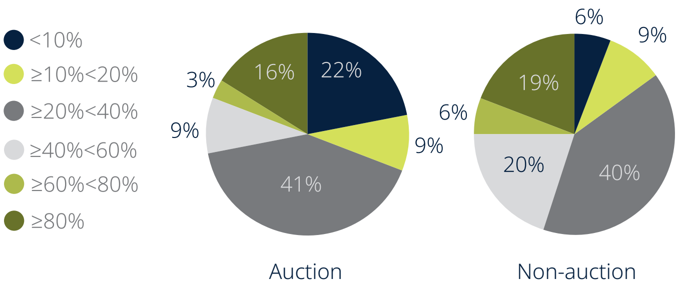


12.5 Commercial warranties: Financial cap (excluding buy-side insured deals)

Deal process continues to drive lower caps – globally 23% of uninsured auctions had a cap of less than 10%.

There are regional variations - the majority of caps in the US are below 20%, whereas in Europe the majority are between 20% and 60%.

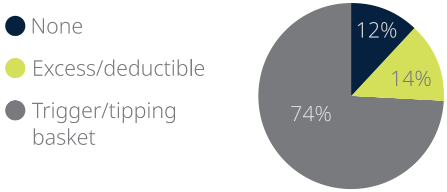
Commercial warranty cap as % of price (excluding buy-side insured deals)



12.6 Claims threshold or basket (excluding buy-side insured deals)

In uninsured deals with commercial warranties, a claims threshold was included in nearly 90% of deals and in the vast majority of those deals the threshold was set as a trigger or tipping basket.

Claims threshold
(excluding buy-side insured deals)

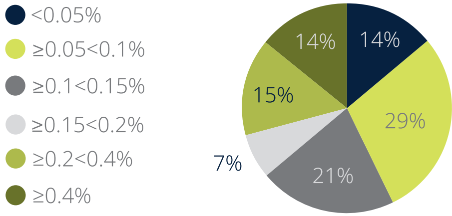


12.7 Commercial warranties: Small claims or de minimis

Although inclusion of a small claims exclusion or de minimis continues to be standard market practice in most European jurisdictions and increasingly in Asia Pacific, its use declined in 2022 in the US and was seen in only 11% of US deals surveyed.

Consistent with 2021, the most common small claims exclusion in the Nordics, UK and Asia Pacific was between 0.05% and 0.1% of price. This range was also the most common in Continental Europe in 2022. In the US, the most common exclusion was less than 0.05% of price.

Small claims exclusion as % of price

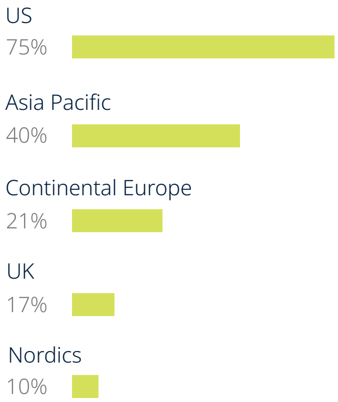


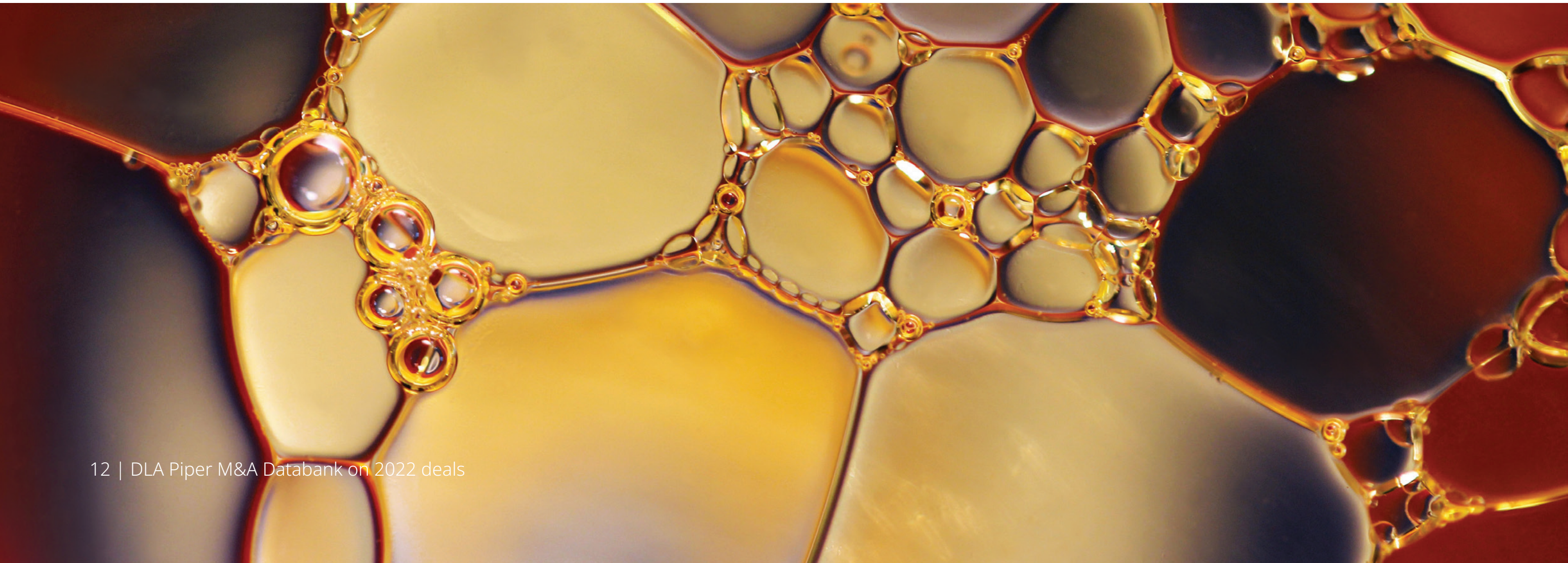
12.8 Security for claims

In the US, security for claims by way of escrow or holdback remains standard practice, seen in three-quarters of the deals surveyed. Typically US escrows on uninsured deals are 10% or less of price and secure completion accounts, warranty claims and specific indemnities for a period of up to 18 months.

In Europe, security for claims is seen in only a minority of deals and is driven by the nature and extent of the claims being secured and the financial standing, location and negotiating strength of the parties. When provided, escrows tend to be larger, longer in duration and cover more types of claim than in the US. In 2022, most escrows or holdbacks on European deals were more than 10% of price and a significant proportion were above 20% of price.

Deals with security





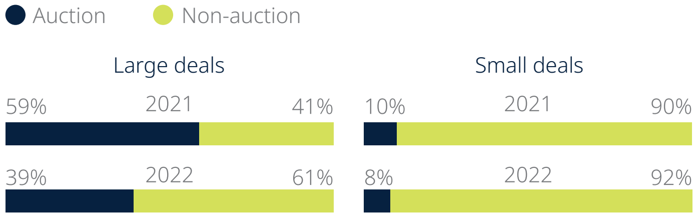
12.9 Large vs small deals

We continue to see some interesting differences between deal terms on large deals (above EUR250 million) and those on small deals (below EUR50 million).

Auction vs non-auction

Auctions are significantly more common in large deals – they remain attractive to sellers of high value assets. Having said that, fewer large deals used auction processes in 2022. As debt markets tightened in the second half of the year, this probably limited the ability of sellers to undertake competitive sale processes as the pool of available buyers, including private equity buyers, diminished.

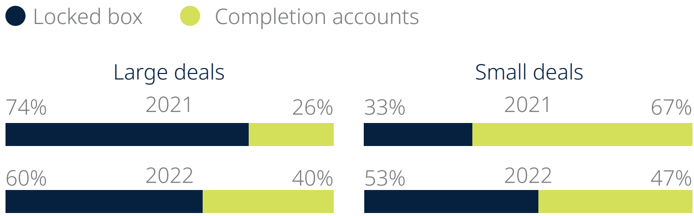
Deal process



Pricing mechanism

In Europe, locked box mechanisms continue to increase in popularity in small deals – used in over half of small deals (compared to a third of small deals in 2021). In contrast, use of locked box mechanisms declined slightly in large deals, probably driven by the fact that there were fewer auction processes.

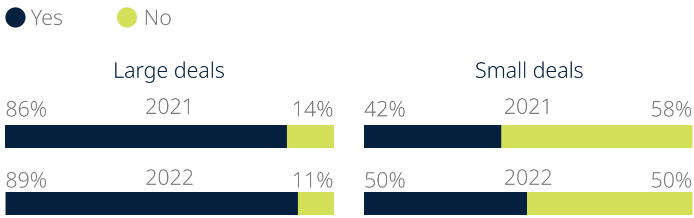
European pricing mechanism



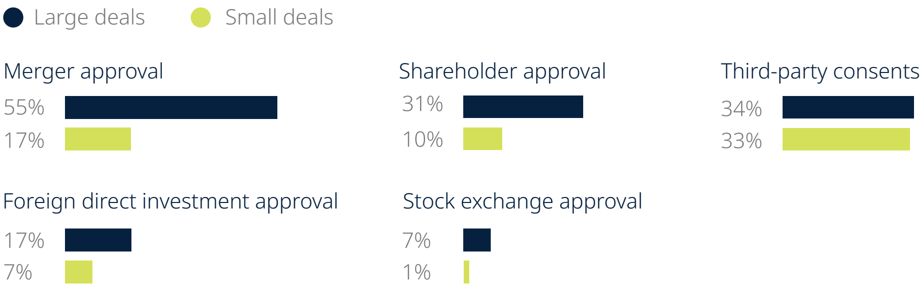
Split signing and closing

As in 2021, the vast majority of large deals had a split signing and closing, compared to around half of small deals. This is primarily due to large deals being much more likely to hit merger control turnover filing thresholds.

Split signing and closing

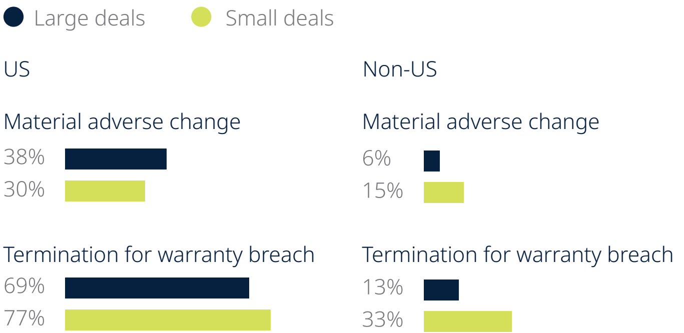


Conditions



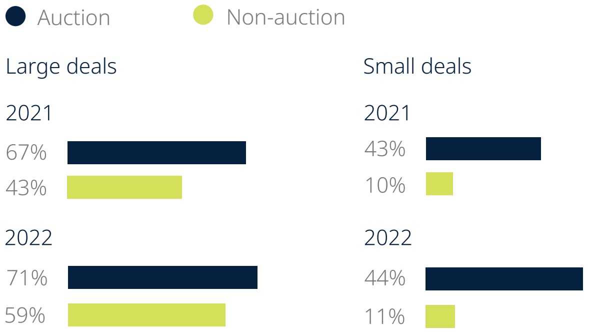
Our data continues to indicate that conditions to closing triggered by regulatory and legal requirements relating to merger clearance, foreign direct investment, shareholder approval and stock exchange requirements are more likely to be needed in large deals. Again, this is not surprising.

Gap protection



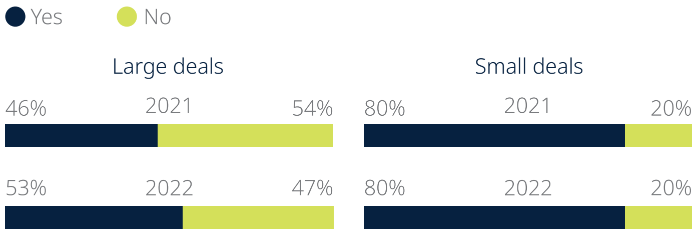
In the US, where formal MAC protections are an established feature of deals of all sizes, we continue to see that buyers in large deals were more successful in obtaining MACs than buyers in small deals. Outside the US, the reverse is true (as it was in 2021) – buyers on large deals are slightly less likely to successfully negotiate a MAC and breach of warranty protection, compared to buyers in small deals. This is a surprising difference, which is difficult to explain, but the relative prevalence of competitive auctions in large deals may have had an impact.

Buy-side insured deals by deal process



Buy-side insurance is used much more frequently on large deals – an increasing majority of both large auction and non-auction deals used buy-side insurance in 2022.

Non-compete



We continued to see significantly more non-competes given on small deals compared to large deals. Large deals tend to involve large trade or private equity sellers – trade sellers will not give non-competes if they have retained businesses with similar activities and private equity sellers will almost never give non-competes. Smaller deals are more likely to involve individual sellers, whose customer and market knowledge buyers are keen to protect post-closing.

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We guide our clients through every stage of a deal; from due diligence and structuring through to negotiation and preparation of deal documents. We also understand that proper acquisition planning and disciplined post-merger integration can significantly enhance a deal's success.

Our international corporate reorganisations practice helps our clients identify opportunities and plan for and implement legal changes that help deliver the anticipated deal benefits and synergies.

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