# Drafting the acquisition agreement – introduction to the seller’s position

This section considers the contractual protections generally required for the seller in relation to warranty claims

# Introduction to the seller’s contractual protections

The seller’s solicitors will want to ensure that their client’s exposure under the acquisition agreement is reduced to a minimum. The seller’s solicitors will generally seek to achieve this in three ways:

1. **negotiation -** seeking to amend, or even strike out, those of the warranties which are too broad in scope and/or cover matters outside the control of the seller and, where possible, avoiding indemnities altogether (or limiting their scope as far as possible);
2. **disclosure** - disclosing against those of the remaining warranties that are incorrect or inaccurate; and 1
3. **limitation** - including a series of seller protection provisions limiting the seller’s liability under the acquisition agreement.

You shall now consider each of these in turn in this element and the next two elements.

**Negotiating warranties**

In a typical acquisition agreement, the warranties and indemnities will take up more than half the document.  (The time taken to negotiate this part of the document will in part depend on whether there is warranty and indemnity insurance in place for the transaction (see later Topics for more information)).

Warranties and indemnities are statements of fact and promises (respectively) given on the day of completion (or on signing and completion if there is a split, which will be dealt with when you look at completion).

When reviewing warranties proposed by the other party’s solicitor it is important to consider the **purpose of each warranty** being proposed **and the impact** it will have on your client and the other party. Bear in mind the contractual protections are a negotiation, and the aim of both parties is to achieve agreement without being exposed to unfair or unnecessary risk.

# Striking out or amending the warranties

**Striking out the warranties**

The seller’s solicitors should seek to have some warranties **removed** altogether if the seller is being required to give a statement in relation to something over which it has **no control.** Examples of this include warranties in relation to something that will take place **after the date** on which the warranty is given or because it is within the control of another person for example the buyer or a third party.

The seller’s solicitor should analyse every warranty carefully to ensure they are **within the seller’s control** before agreeing to them.

The seller’s solicitor should also seek to remove warranties that are not relevant to the target or its business.

**Amending the warranties**

In other cases, a warranty may be acceptable in principle, but the seller’s solicitors will want to make some amendments to the way it is drafted in order to get rid of ambiguity and/or narrow its scope, often so as to make it more practical to disclose against.

# Striking out the warranties - example

As you now know the seller’s solicitors should seek to have warranties removed altogether if the seller is being required to give a statement in relation to something over which it has no control.

**Example:** The buyer’s solicitors may have included a warranty to the effect that none of **target’s customers** will terminate their business dealings with the target **as a result of the sale** or that all of the debts owing to the target will be recovered within **one month after completion**.

The warranties refer to termination of business dealings and repayment of debts after completion (i.e. after the seller has sold the target). In addition, both events are within the control of a third party (customers or debtors). The seller has no control over these things and so **should not agree** to give the warranties.

# Amending the warranties – examples

Examples of warranties that may be acceptable in principle, but the seller’s solicitors will want to make some amendments to the way it is drafted to **get rid of ambiguity and/or narrow its scope**, often to make it more practical to disclose against.

**Example:** The buyer’s solicitors may have included a warranty that the target is not involved in any litigation or disputes of any nature. Even if the target is not involved in any major litigation, it may be involved in a number of small disputes with customers as a result of routine debt collection. If the warranty is left unamended, then the seller will have to disclose details of all these small disputes to be sure of avoiding liability for breach of warranty under the acquisition agreement. To avoid the need for this, the seller’s solicitors may ask for the warranty to be amended so that it only covers litigation and disputes having a value over a minimum amount (for example, £5,000).

# Awareness qualification

Another way in which the seller may seek to amend the warranties is to qualify them by the **seller’s awareness**. The effect of this qualification is to shift the risk on to the buyer.

**Example:** The buyer’s solicitors may have included the following warranty “*no customer or supplier of the Company is subject to a relevant insolvency procedure within the meaning of the Insolvency Act 1986.”* The seller’s first reaction to this will be to strike it out because it is outside the seller’s control. If the buyer insists it wants comfort regarding the continued trading of the customers and suppliers the seller may consider giving the warranty provided it is subject to its awareness. The warranty could be amended to read *“****so far as the seller is aware*** *no customer or client of the Company is subject to a relevant insolvency procedure within the meaning of the Insolvency Act 1986”.*

Where the warranties are qualified by the seller’s awareness in this way the buyer will often insist on a provision in the acquisition agreement that the seller is deemed to have the awareness it would have had after making due and careful enquiries of specified parties. In the case of **Triumph Controls UK Limited v Primus International Holding Co** [2019] EWHC 565 (TCC) the seller was deemed to have awareness if making enquiries of certain named individuals would have yielded the relevant information.

From the seller’s perspective the problem with agreeing to make such enquiries is that, in the above example, the seller would need to check the status of all of its customers and suppliers. This would alert the parties to the forthcoming sale which would otherwise have been confidential. In addition, it will be impractical for the seller to ask each customer and supplier so the seller will want to limit such enquiries to material counterparties.

**A common compromise** is for the parties to agree a definition of the seller’s knowledge as the actual knowledge of certain named individuals, for example members of senior management.

Each warranty must be analysed carefully by the buyer’s solicitors before they agree to a qualification on an awareness basis as the awareness qualification shifts the risk of unknown issues onto the buyer. Awareness may be more appropriate when you wouldn’t expect the seller to know about certain matters.

# Limiting the indemnities

The seller’s solicitors should ensure that any **indemnities refer only to very specific types of risks.** The seller should not accept indemnities which are general in nature. Indemnities should refer only to particular identifiable (and quantifiable) types of liability.

Even if a transaction has warranty and indemnity insurance in place (see later Topics for more information), where a risk is known it will not be covered by the insurance and so a buyer may still require indemnities even where warranty and indemnity insurance is in place.

# Seller’s claim against management

It is usually the managers and/or the directors of the target who provide the information about the target required under the warranties and in the disclosure letter. If those managers and/or directors are not also shareholders of the target they may still be employed by the target following completion.

In such a situation the buyer will want to ensure that the seller cannot take action against them if the information they have provided proves to be untrue. The buyer will usually seek confirmation from the seller that it has not relied on such information and that it will not take any action against the managers/directors (except those who are also sellers) in respect of the information supplied to it.

# Summary

The seller’s solicitors will seek to limit the seller’s liability under the acquisition agreement in the following ways:

* Narrowing the scope of the warranties given by the seller and limiting the indemnities given by the seller;
* Disclosing against warranties; and
* Inserting seller protection clauses into the acquisition agreement.