Sellers' Warranties

- by Christer Nilsson
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In the warranty section of a share purchase agreement (SPA), the sellers are required to provide warranties regarding essential circumstances in the company and its operations. The warranties are generally made on the date when the seller and buyer sign the SPA.

Signing and closing

If the closing of the transaction (the point in time when the shares change owners) takes place at a later date than the signing date, it is often a hot topic to agree whether the warranties are made on the date of signing only or at signing *and* also at closing. Notably, in case there is an extended period between signing and closing, it is reasonable to require the seller to renew its warranties at closing.

It should be noted, however, that sellers never should agree to provide forward-looking warranties, i.e., not give warranties relating to events that may happen in the future. Further, sellers' warranties should be made by each seller individually and severally, and not jointly and severally.

Examples of typical and fundamental warranties are sellers' full ownership of the shares in the company and that the shares are not subject to any encumbrances, the accuracy of financial information, tax payments, material agreements, salaries and remuneration, and the company's compliance with relevant laws, regulations and policies.

Actual guarantees based on facts

Some warranties state positive facts such as that the company owns real estate, production facilities, material rights such as trademarks patents – all listed in an appendix to the agreement. Other warranties may state negative facts, e.g., the company is not involved in any legal disputes or that no ongoing customer contracts exceeding 5% of sales are terminated or has expired. An important matter when negotiating the warranty clauses is

whether the warranties should only relate to the current situation of the business or should it also refer to past circumstances.

Seller's knowledge

In some instances, the seller knows that a specific warranty is true and fact-based – for example, that none of the company's ten largest suppliers have terminated their supplier agreement. However, in other cases, the seller may not be entirely sure if the warranty can be fact-based or not, e.g., "no key supplier intends to terminate its contract with the company." The warranty, in such a case, becomes a matter of risk allocation. If the seller provides the warranty, the seller will be responsible for the cost the buyer receives if a critical supplier will terminate the agreement. If the seller does not give the warranty, any damages will be borne by the buyer.

The sellers may still need to provide warranties even if the sellers do not know for a fact if a warranty statement is entirely accurate or not. One way of dealing with this tricky situation is by using the phrasing "seller's knowledge." Then, only the circumstances that a seller knew about applies when the warranties were provided. An example of wording is "insofar as the seller knows, none of the company's ten largest suppliers intend to terminate an agreement with the company."

Note that "seller's knowledge" does not include what the management or an employee of the company know about a circumstance – provided that the seller was not informed.