



COLLYER BRISTOW

COMMERCIAL DISPUTES **KNOW-HOW GUIDES**

BREACH OF WARRANTY CLAIMS (SHARE ACQUISITION)

Warranties are contractual statements of fact that are typically given by a seller to a buyer in a share purchase agreement (“SPA”) or other contract as one of the ways in which risk is allocated between parties in the acquisition of a target company (the “Target”). The warranties give the buyer a remedy (in the form of a damages claim) if the statement turns out to be untrue/the warranties are breached.

COMMERCIAL DISPUTES KNOW-HOW GUIDES

Giving warranties encourages the seller to be upfront and disclose potential issues with the Target. Failing to make adequate disclosure could result in a breach of warranty claim. If, in fact, the facts giving rise to the breach were disclosed, this will provide the seller with protection against a claim or (at least) a defence.

Warranties given by a seller typically confirm the condition of the company being sold, and could include the following:

- Warranties that the Target is not subject to (or likely to become subject to) litigation.
- Warranties that the Target's accounts give a true and fair view of the company's financial position and comply with any relevant accounting principles.
- Warranties that assets have, at all material times, been insured.

These are just a few examples, and warranties found in an SPA are often numerous (and heavily negotiated) and for this reason, are often put in a separate schedule.

THE VALUE OF WARRANTIES

Warranties may provide a useful remedy to a buyer if they are breached but their value may be limited in various ways. Some of these are, however, dependent on the parties negotiating position.

- A breach of warranty claim may need to be brought within a certain limited time period;
- Recovery under a breach of warranty claim may be subject to a financial cap;
- If the warrantor becomes insolvent or moves to a jurisdiction where it is more difficult to enforce a claim, the warranty may be of limited value (although it is common for the warrantor to have provided security for breach of warranty, often in the form of the retention of a portion of the sale proceeds in an escrow account, the provision of a bank guarantee, a Warranty and Indemnity insurance policy or otherwise);
- The damages available for breach of warranty are usually calculated as the value of the Target if the warranty had been true (i.e. the "as warranted value") less the actual value of the shares (the "as is value"). It can be difficult to show the impact of the breach on the value of the shares in the Target and this is may be heavily disputed and a matter for expert evidence from valuers; and
- Depending on the circumstances, damages may not be a sufficient remedy for a buyer who, rather than financial compensation for the loss to share value, prefers to end the contract.

A seller may also seek to argue that the buyer has not mitigated the buyer's loss or that any loss was too remote and so the seller is not liable for it.

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MULTIPLE WARRANTORS: LIABILITY AND CONTRIBUTION

If there are multiple sellers (and, therefore, multiple warrantors) it is important, when drafting the SPA, to consider how liability is to be apportioned between warrantors and for the warrantors to agree between them as to how contribution to damages is to be ascertained, otherwise this will be in the discretion of the Court.

NOTICE OF THE BREACH OF WARRANTY CLAIM

It is common for SPAs to specify the manner in which notice must be given of a breach of warranty claim and that the seller will not be liable unless such notice is given and the notice provisions are followed including that the notice is given in the manner specified. If a breach of warranty claim involves a dispute as to whether the notice was given was adequate what is adequate will depend on the wording of the SPA.

This is part of a series of practical know-how guides for those involved in commercial disputes whether the dispute has led to litigation or not. They provide basic information on a wide range of disputes topics but are not a substitute for specific legal advice. For further guidance on the topic please contact any member of the commercial disputes team.



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