

Our Guide to Representations & Warranties

Representations & Warranties (R&W) are essential elements in any share purchase agreement (SPA) within an M&A process. Their function is to protect both parties and define the conditions in which the transaction takes place.



1 What is R&W?

Representations

These are statements about the current or past state of the company, such as the accuracy of financial statements, the existence of litigation, and regulatory compliance.

Guarantees (Warranties)

These are promises or guarantees that certain conditions will be maintained in the future, otherwise, if proven to be false, the party offering the promises will assume responsibility.

R&Ws can refer to multiple different matters, including:

- Legal capacity and powers.
- Corporate matters.
- Tax obligations.
- Employment and social security obligations.
- Contracts and insurance.
- Litigation.
- Shares or stock subject to the sale.
- Financial statements and financial position.
- Licences, authorisations and administrative permits.
- Assets.
- Commercial and intellectual property.
- Personal data protection.

2 Who should grant the Representations & Warranties?

Depending on the structure of the deal and the transaction terms, R&W may be granted by different parties:

Seller:

The seller is generally the main party responsible for providing R&W regarding the business. These statements cover financial, legal, tax, and operational aspects. Since the buyer relies on these statements to make their decision, it is crucial that they are accurate and verifiable.

Buyer:

In some transactions, particularly those involving a Special Purpose Vehicle (SPV) with no track record, the buyer may also grant certain R&W, ensuring financial transparency to complete the deal.

Key Shareholders:

In some cases, the seller's shareholders may also be required to grant R&W, especially if they hold a significant stake or are part of the management body. This provides the buyer with an additional layer of financial assurance.

3 Buyer Protection Mechanisms

R&W is only effective if backed by solid mechanisms that ensure their compliance. In small and mid-market deals, sellers often have limited resources to cover claims, therefore protective measures are essential. To mitigate this risk, common mechanisms include:

Escrow or Retentions:

A portion of the purchase price is held in escrow, enabling the buyer to claim indemnities if discrepancies arise. This guarantees the availability of funds to cover potential breaches.

Seller's Shareholder Support:

In some deals, the seller's partners or shareholders may personally back the R&W. While often resisted, this offers valuable assurance for the buyer.

R&W Insurance:

Specialised insurance policies exist to protect the buyer if R&W proves to be false or inaccurate. However, such policies may have limitations, such as the exclusion of known issues.

4 Liability Framework for R&W

The liability framework sets temporary and monetary limits:

Time Limits

Since sellers cannot be held liable indefinitely, survival periods are usually set between 12 and 24 months. For employment, tax, and administrative matters, claim periods typically match their statutory limitation periods.

Monetary Limits

Common types include:

- **Liability Cap:** Maximum liability amount, usually linked to the purchase price.
- **De Minimis:** Minimum claim threshold.
- **Basket Deductible:** Amount beyond which damages are indemnifiable.

This can apply from the first euro (tipping basket) or only the excess above the threshold.

Fraudulent acts or wilful misconduct are usually excluded from these limitations, as are basic R&W declarations, such as the capacity to enter into the agreement, ownership of shares, and company existence.

5 Conclusion

The Representations & Warranties are a fundamental pillar in M&A transactions, as they provide security and trust to both parties. While the seller generally assumes most of the responsibility for the accuracy of disclosed information, the buyer must ensure protective mechanisms are in place to mitigate risks. Careful and strategic negotiation is essential to balance both parties' interests and avoid future disputes.



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