

Tax Warranties: **What you need to know**

On a share sale, it is common for a buyer to seek protection against pre-completion tax liabilities, in part through Tax Warranties. In essence, a tax warranty is no different from any other warranty, in that it is a contractual representation of fact made by the seller to the buyer about (in the case of a tax warranty) the tax affairs of the target company. The Tax Warranties, like the share warranties, can be used as the basis of a tax claim against a seller, but given that most sellers have also signed up to a tax covenant, where a claim is more likely to be made, they are mainly used to provoke the disclosure of any tax issues that may affect the target company. This is because a Tax Warranty can be disclosed against through the disclosure process to prevent a claim being brought (whereas no disclosure will normally be possible against the Tax Covenant).

Whilst the tax due diligence process can also flush out information about the target company, as the Tax Warranties form the basis of a claim against a seller, they are an important additional tool of the buyer to ascertain more information about the target company. The information that can be obtained through disclosure against the Tax Warranties may result in a further tax indemnity being sought, a price chip, retention or possibly a buyer pulling out of a transaction if a tax disclosure is very serious and detrimental. This information also informs the Buyer as to whether, in general, the target has been diligent in undertaking its tax compliance obligations (and if this is not the case, whether personnel changes may be necessary post-completion).

There is always some debate about the length or scope of the Tax Warranties, although a full set should cover matters such as tax compliance, investigations and disputes, arrangements giving rise to tax liabilities at or after completion, tax clearances, specific corporation tax issues, corporate groups, international aspects, tax avoidance, close companies and construction industry scheme matters.

To properly negotiate the Tax Warranties, a detailed knowledge of the tax system is required as the Tax Warranties are both varied and involve complex issues that may or may not be relevant for a particular transaction and so tax specialists should always be involved.

Corporate lawyers should keep a close eye on what is disclosed against Tax Warranties and ask tax colleagues to flag anything material that may need to be factored into the commercial negotiation of the deal.