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A SELLER'S GUIDE TO POST-CLOSING TERMS

When selling a business, signing and closing the transaction may feel like the finish line—but for sellers, the post-closing period can carry significant ongoing exposure. While the pre-closing focus is often on valuation, structure, and timing, sellers must also be mindful of the buyer protections that remain in place after the deal closes.

These post-closing mechanisms—such as covenants, indemnities, purchase price adjustments, escrow arrangements, and representations and warranties insurance (RWI)—carry real implications for sellers, affecting not only their potential financial liability but also their ability to fully exit the business.

Understanding and negotiating these terms thoughtfully can help sellers preserve deal value, minimize risk, and achieve a cleaner exit.

Covenants: Limiting Post-Deal Constraints

Post-closing covenants are commitments sellers agree to uphold, often as a condition of receiving full consideration or payment. These provisions are designed to protect the value of the acquired business and can vary in scope depending on the deal.

NON-COMPETE

Non-compete covenants, while standard, should be carefully negotiated to ensure they are reasonable in terms of duration, geography, and scope.

NON-SOLICITATION

Non-solicitation covenants restrict sellers from contacting former employees or customers. Clear definitions and time frames help both parties avoid misunderstandings or unintentional breaches.

CONFIDENTIALITY

Confidentiality covenants help protect proprietary information and are generally less contentious, but sellers should ensure carve-outs for publicly known information and retained knowledge that may be useful in future ventures.

Indemnification: Defining and Capping Liability

Indemnification provisions are the most direct way sellers remain liable after closing. These clauses allocate responsibility for certain risks to the seller—most often breaches of representations and warranties or pre-closing liabilities.

> Sellers should seek caps, baskets, and survival periods to limit the scope and duration of their exposure.

A common structure involves a general cap equal to a percentage of the purchase price, with certain claims (like fraud or key liabilities) potentially carved out.

CAP

A maximum dollar amount the seller can be liable for. Often, representations and warranties are separated into different groups, and each group might have its own designated cap.

SURVIVAL PERIOD

Limits how long post-closing claims can be made.

BASKET

A threshold amount that must be met before the buyer can make a claim against the escrow amount. This protects the seller from being nickeled and dimed by the buyer for trivial amounts.

EXPERIENCE MATTERS

There are well-established market norms for caps, baskets, and survival periods. An experienced M&A attorney can help guide sellers through these terms.

Tax liabilities, environmental issues, and litigation tied to pre-closing events often fall outside standard limitations, so it's important for both parties to clearly define these carve-outs and understand their potential impact.

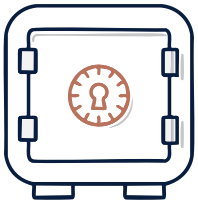
Negotiating strong indemnification terms is critical to avoiding open-ended risk that can undermine the financial benefit of the deal.

Purchase Price Adjustments: Reducing Surprises

Purchase price adjustments are mechanisms used to ensure the business is delivered in the financial condition agreed upon at signing. These provisions help align the final purchase price with the company's actual performance or position at closing, and clarity in their design is important to avoid post-closing disputes.

Working capital adjustments should be based on a well-defined methodology and benchmarked against historical norms to reduce post-closing friction.

Earnouts, which can be beneficial in bridging valuation gaps, can also cause uncertainty for sellers. Clear, objective performance metrics can help minimize surprises. Transactions with earnouts often align best with sellers who plan to retain some influence over operations post-closing.



Locked-box structures offer sellers greater price certainty. If negotiated properly, these mechanisms allow sellers to fix the price as of a specific historical date, providing greater price certainty and limiting buyer adjustment claims.

Escrow and Holdback Provisions: Managing Withheld Funds

Escrows and holdbacks are commonly used in M&A transactions to secure post-closing claims and provide the buyer with a source of recovery if needed. These mechanisms can impact the timing and distribution of deal proceeds, so sellers should seek to:

- Limit escrow amounts to a reasonable percentage of the deal value
- Clearly define the duration of the hold period
- Tailor offset rights (e.g., applying earnout shortfalls against escrow) to specific deal terms
- Consider representations and warranties insurance to reduce or eliminate the need for escrows altogether.

Representations and Warranties Insurance (RWI): A Cleaner Exit

RWI Advantages for Sellers

- Lower escrow (or no escrow at all)
- Faster access to full deal proceeds
- A significantly cleaner break from the business

RWI has become an increasingly common tool to protect buyers while simultaneously benefiting sellers. With an RWI policy in place, much of the risk associated with breaches of representations and warranties shifts to an insurer rather than the seller.

While sellers may be asked to share in the cost of the policy or cooperate with underwriting diligence, RWI policies can offer meaningful benefits in deals of sufficient size or complexity.

For sellers, post-closing protections in M&A deals play a critical role in bridging the gap between buyer and seller interests. While they help get deals done by providing buyers with important safeguards, they also introduce ongoing obligations and potential liabilities. Whether through indemnities, covenants, or purchase price mechanics, each term deserves careful consideration to avoid unwarranted exposure.

As tools like RWI become more prevalent, savvy sellers are using them to reduce friction, accelerate payouts, and walk away with greater finality. With thoughtful structuring and skilled negotiation, buyers and sellers can align on terms that protect deal value while supporting a clean and efficient transition.