

A FOUNDER'S GUIDE

You Sold Your Company. When Do You Relax?

Where your liability lives, and how to limit it.

Tony Bell

ATTORNEY, PAG LAW

THE GOAL

You didn't grind for years
to spend the next three
worried.

Founders work 80-hour weeks. Everything demands attention, everything is a decision about what to prioritize, and it goes on for years. Many build their companies with an exit in mind, one that hopefully provides a life-changing return.

So when the deal finally closes, they want to relax.

Whether they actually can is decided long before closing, in the terms they negotiated.

It's never possible to eliminate the risk.
**It is always possible to understand it
and limit it.**

The money doesn't all **arrive at closing.**

When we begin an M&A process, some clients expect their payday to come on the day they sign their closing documents. That is not always what happens.

Often you are paid in tranches. And often a portion is held back: a holdback, reserved for a period of time in case the buyer finds liabilities, or anything else that requires you to indemnify them.

The holdback is not a formality.

A piece of your money sits where the buyer can still reach it, **for exactly as long as the agreement says.**

Your liability has a **specific address.**

It comes from two places: what you represented in the transaction, and what you agreed to indemnify the buyer for.

Founders want a good understanding of everything they are indemnifying for. Not a general sense of it. An actual understanding, clause by clause.

Once you know where the exposure sits, containment is the whole game.

Once you know where the exposure sits, **containment is the whole game.**

What you are indemnifying for.

Breaches of your representations and warranties

Everything you told the buyer was true about the company: the accuracy of its financial statements, its contracts and its performance under them, its proper payment of taxes.

Breaches of your covenants

Everything you promised to do, or not do, after closing. Not to compete with the buyer. Not to disclose the terms of the deal. To assist with the transition.

Every representation you made about the company must be true

LIMIT 01

Cap the indemnity.

At most, cap your indemnification obligations at the total purchase price. You should never be able to lose more than you were paid.

Then split the cap. Fundamental breaches, the ones so important that breaching them makes the value of the deal worthless, stay at the purchase price.

The liability cap for all other representations should be much lower. The accuracy of your financial statements, your representations about your contracts, data privacy, employee matters. Real obligations, but not things that destroy the entire value of the deal. You often see them capped around 5-10% of the purchase price.

These are not things that destroy the entire value of the deal. **They should not cost you the whole deal.**

Negotiate a **basket**.

Small breaches need a floor. If the buyer's damages come in below a set amount, often around 1-2% of the purchase price, they do not get to recover at all. They only begin to recover once damages climb above that number.

That is the basket, and it exists for one reason.

So that a founder is **not losing**
sleep over little things.

LIMIT 03

Limit the survival period.

You should not carry potential liability until the end of time. Your representations should survive for a defined window and then expire.

For non-fundamental representations, that window is usually around a year, maybe eighteen months.

Once it passes, you are paid in full, any holdback is released, and the exposure is finished. You are not three, four, five years down the line still wondering whether someone is going to sue you.

Once it passes: **paid in full, holdback released, finished.**

LIMIT 04

Insure the representations.

In larger deals, there is another option: move the risk to an insurer. Representation and warranty insurance (RWI) is a policy that covers breaches of your representations. If something turns out to be wrong, the buyer's first call goes to the carrier instead of to you.

RWI policies typically have a retention, which works like a deductible, and damages up to that amount must be covered by the sellers. The retention is often around 0.5-2% of the purchase price. Coverage above that commonly runs to roughly 10-20% of the purchase price.

Your money is not the buyer's remedy anymore. **The policy is.**

LIMIT 04, CONTINUED

What it covers, and what it costs.

In many deals, sellers can negotiate for zero liability for breaches covered by the RWI policy. However, some issues, like fundamental representations and specific areas of concern in a deal, are often not covered by RWI policies.

Plus, there are other complications when RWI is brought into a deal. The underwriters run their own diligence, so expect more questions, more documents, and a few extra weeks of process the deal would not otherwise have.

And someone pays the premium, usually a few percent of the coverage purchased. That is a negotiation, and how it's split depends on the deal.

**Insurance moves the risk. It does not
make it free.**

What relaxation **actually looks like.**

It is not the absence of risk. No transaction gives you that.

It is a ceiling you can point to, a floor beneath which nothing counts, and a date after which the whole thing is closed.

That is the difference between a founder who has sold a company and a founder who is still, five years on, waiting to find out how it went.

Not the absence of risk.
**A capped, dated,
quantified version of it.**

IN SHORT

Four limits, in one page.

1

Cap the indemnity. Purchase price for fundamental breaches, **around 5-10% for the rest.**

2

Negotiate a basket. **Nothing recoverable below roughly 1-2%.**

3

Limit the survival period. **Twelve to eighteen months, then it is over.**

4

Insure the representations. **In larger deals, the RWI policies cover damages up to 10-20% of the purchase price.**

You cannot eliminate the risk. You can put a **ceiling, a floor and an end date** on it.



ABOUT THE AUTHOR

Tony Bell

ATTORNEY • PAG LAW

Tony Bell is a corporate attorney at PAG Law in Miami, where he advises founders and investors on M&A and venture transactions across the U.S. and Latin America.

You cannot eliminate the risk. You can always
understand it and limit it.

Educational overview. Not legal advice. Consult counsel for your specific situation.