



## The importance of the balance sheet in M&A transactions

*Ruling of the Supreme Court of 21 December 2021*

### Background

All M&A operations involve negotiating and formalizing extensive documentation. It is crucial to clearly identify the key aspects of this documentation both from a business and legal/contractual point of view. On the one hand, it allows to strengthen the negotiating position and to prioritise objectives. On the other hand, it allows drawing up clear and well-focused transactional documents that address the concerns of the parties involved.

The balance sheet is one of these key aspects. Not only for valuation/pricing purposes, but also for interpreting various contractual provisions, especially representations and warranties. The Supreme Court judgment we are discussing illustrates this point very well.

### Court's position

The case revolves around the interpretation of a settlement agreement involving the transfer of shares of company "A". The dispute centered on whether company A had been transferred with a debt to company B or if it was transferred debt-free. The settlement agreement contained contradictory provisions on this matter.

On the one hand, the agreement included a representation stating that "the company has not assumed debts not reflected in the balance sheet attached as Annex X". The contested debt did appear in the balance sheet included in Annex X.

On the other hand, the agreement stated that "the company has no financial obligations to third parties other than those indicated in Annex Y". Annex Y did not list the disputed debt.

Faced with this contradiction, the Supreme Court relied on the balance sheet of Company A (prepared ad hoc for the transaction) to clarify the true intention of the parties. The Court emphasised that the balance sheet "corresponds to the state of the company just before the transfer", and that "the liabilities are not hidden and the acquirer was not only in a position to know them, but could not fail to know them". On this basis, the Court concluded that Company A was transferred with the contested debt, noting that "for the debt to be considered as having ceased to exist as a result of the transaction, there would have to have been a clear waiver of its claim."

### Conclusion

When negotiating and drafting contracts in M&A operations, a thorough understanding and control of the balance sheet and financial information are essential. This judgment teaches us that in the face of a contractual contradiction, a line from the balance sheet can carry more weight than a line from the contract in clarifying the true intent of the parties.