

■ Buying and Selling a Dental Practice

■ - the legal process

Part 12: Warranties



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Warranties are an important part of the Sale and Purchase agreement or contract.

Warranties are statements of fact made by the seller, about the practice, assets, contracts, employees, accounts and other relevant matters. The buyer is entitled to rely on the warranties.

Subject to various agreed limitations, if a warranty turns out to be incorrect (a 'breach of warranty') and the buyer incurs costs or suffers a loss as a result, then the buyer may be entitled to sue the seller for the amount of financial loss.



The existence of warranties in the contractual documentation also acts as an incentive to the seller to disclose to the buyer any facts or circumstances that could otherwise lead to costs or losses for the buyer. Warranties and disclosure of facts and circumstances that are necessary to caveat those warranties (often in a "Disclosure Letter") drags such issues into the open before the contract is signed, giving the buyer the opportunity to renegotiate the price due to the risk of such losses being suffered, demand a retention of the purchase price to meet such amounts or, at the very least, require the inclusion of indemnities in the contract so that the seller has to reimburse the buyer for any such amounts.

The principle of "caveat emptor" or 'buyer beware' is the default position, the seller does not have to tell the buyer anything, it is for the buyer to make enquiry. Consequently, the buyer must undertake a rigorous due diligence process. However, how can a buyer trust the replies given by the seller? This is a question that does not need to be answered as warranties protect the buyer from misleading and untruthful replies and information.

For example, a warranty by the seller confirming "all information given by the seller or the seller's solicitor in response to enquiries of the buyer or the buyer's solicitor are true, accurate, complete and not misleading" is imperative. Such a warranty protects the buyer in the event that any replies to due diligence enquiries were untrue or misleading and the buyer suffers as a result, as the buyer can sue for breach of that warranty.

It may be that the seller is aware of facts or circumstances that might affect the buyer's decision to purchase at the agreed price or at all. Unless the buyer asks the correct question, the seller may not tell the buyer or need to tell the buyer about such facts or circumstances. Consequently, a buyer would be sensible to require the seller confirm by a warranty stating "the seller is not aware of any facts or circumstances that have not been disclosed that would reasonably affect the willingness of the buyer to purchase on the terms of this agreement".

Consequently, if the buyer knows that a large corporate is about to open a branch in the next road, doesn't tell the buyer, and following completion the buyer loses patients to the new local corporate practice when it opens, then it may be possible to sue the seller for the losses incurred due to breach of such a warranty. Of course, proving the seller knew will always be difficult for the buyer.

General Warranties

There are a number of warranties that a buyer will require no matter what type of business he is seeking to acquire, including the business of a dental practice. Here are some examples.

Whether or not the business makes a profit is often indicated mainly by the accounts. However, figures can be manipulated. It is also very rare for a dental practice's accounts to be audited. Furthermore, the last full annual period to which the latest accounts relate could have ended some time ago, and a lot can happen during such periods! Consequently, it is sensible for the buyer to require the seller to warrant that:

"the last accounts give a true, fair and reasonable view of the profit, income and expenses of the practice as at the date of the accounts"

"since the date of the accounts there has been no substantial adverse change in the income or expenses of the practice and the financial or trading position of the practice has not substantially deteriorated".

Such warranties should force the seller to disclose any facts or circumstances that he knows contradict these warranties, for example, if some unusual accounting method was used or some item was included or not included in the accounts and the reasons for it, or a deterioration in the financial results of the practice since the last accounts. If the seller doesn't, then the buyer is at least protected to an extent by the opportunity to sue the seller for breach of warranty.

The terms and conditions of all employees are protected on a sale of any business. The buyer inherits the employees on their current terms and the law robustly protects employees from unilaterally imposed changes by a new owner of the business. Consequently, a buyer will require a seller disclose the details of all employees and their employment terms. This is especially the case as often staff wages are the largest business expense, having a great affect on profit. Consequently a buyer will want the seller to warrant that:

"the employees disclosed are all of the employees of the practice, work solely in the practice and no other person works in the practice"

"the terms and conditions of employment disclosed are all of the terms and conditions of the employees".

If the seller has omitted a central member of staff (for whatever reason, including perhaps that he is planning to take that member of staff with him to a new practice) from disclosure or has omitted some central

term of the employees (for example, a contractual annual bonus) then the buyer could sue the seller for the losses arising from his breach of warranty (for example, the costs to the buyer of recruiting to replace the lost member of staff, or the costs of providing the annual bonus).

Warranties specific to dental practices

There are certain warranties that a buyer of a dental practice would be sensible to require.

For example, it may be that, during the weeks and months following completion, the buyer discovers patients who have suffered defective treatment, or due to sloppy practice, return to the practice due to treatment failing. The buyer is then faced with two options – tell the patient that their remedy is against the dentist who carried out the treatment and that they should track him down, or provide remedial treatment to the patient and put right what is wrong. The former risks losing a patient and dissipating the goodwill purchased (and is not possible in any event if the practice is a company that the buyer has purchased) and the latter costs time and money. Therefore the seller should be required to warrant that:

“at no time has any patient of the practice been provided with defective or negligent treatment and the seller knows of no facts, circumstances or treatment that may give rise to a complaint by a patient”.

Such a warranty should ideally be linked to an appropriate retention of the purchase price, so that in the event that the buyer has to carry out such remedial work, the monies are available to draw upon to compensate him without having to sue for breach of warranty. Of course, if the seller can prove that he has no track record or history of ever having any returning patients, the seller could legitimately resist a retention.

Since 1 April 2011, dental practices have had to be registered with the Care Quality Commission (CQC). A failure to be registered or non-compliance with the legal requirements can ultimately lead to the practice being closed down. Whilst the buyer can inspect the practice once or twice, it is the seller alone who knows in depth whether his practice is compliant or not. Furthermore, he may know of outstanding complaints that may lead to an investigation and the imposition of conditions on or withdrawal or suspension of registration by the CQC. The seller may be tempted to keep such things to himself, worried that disclosure may risk the sale and hoping that the complaint may just ‘go away’. Consequently, a buyer should require the seller warrant that:

“the seller and the practice are registered with the CQC, are fully compliant with the requirements of the CQC and the seller is not aware of any facts, circumstances or matter that could or may lead to a withdrawal or suspension of registration or the imposition of conditions on registration”.

In an NHS or mixed practice it is important for the buyer to know the history of the delivery of NHS services and the GDS contract he is to inherit. For example, that is because the PCT has the entitlement under the GDS contract in certain circumstances to terminate the contract if the contract-holder at any time has received more than one breach or remedial notice. This is a key question to ask during the due diligence process. However, to further protect the buyer, the seller should be required to warrant that:

“no breach or remedial notice has been served or threatened by the PCT and the seller knows of no reasons why the PCT could legitimately serve a remedial or breach notice”.

Worse-case scenario, if it turns out the PCT has served a notice in the past and following completion, served another notice for a breach that occurred before completion and serves notice of termination, the loss to the buyer may be great. That loss may be recovered from the seller in a claim for breach of the above warranty.

Agreeing limitations to the warranties

It is common for the seller giving warranties, to want to limit the effect of the warranties and the opportunity for the buyer to make warranty claims. Whilst in contract law the default position is that a contractual party can sue the other up to 6 years following the contract being made, it is common to limit the effectiveness of warranties and the right to sue for breach of warranty for a shorter period. That period may be negotiated, and is often the period following completion during which any breach is likely to be discovered. For example, 18 to 24 months would often be long enough for a patient to return complaining about defective treatment, however it depends on the treatment and the nature of the defective work.

A seller would also not want the buyer to come to him cap-in-hand every few days and weeks following completion in relation to every minor potential breach. Most buyers want a clean break as possible. Consequently, it is common to agree ‘de minimus’ levels, financial levels below which the buyer cannot claim against the seller and perhaps not until those claims reach a certain threshold in aggregate. There is significant scope to negotiate and agree different thresholds and levels in relation to the warranties in general and specifically.

In relation to the practice property, it is common for few if any warranties to be offered by the seller. A seller will often stick to a ‘sold as seen’ stance. The buyer has the opportunity and right to conduct a survey and assure himself that the property is in suitable condition. However, if the seller refuses to allow such a survey to occur, then with suspicion aroused, a buyer should require the seller warrant the condition of the property.

A seller would rather give no warranties – sticking to a ‘sold as seen’ stance. Indeed often that may be acceptable to a buyer, and reflected in and the basis on which the purchase price is agreed.

However, the majority of the time a buyer will want comprehensive warranties. These act as comfort and security to the buyer, they may flush out issues and disclosure, the buyer can then renegotiate the price or demand specific indemnities or even a retention of the purchase price to meet the potential costs of those specific issues.

A seller will want to limit and restrict the warranties and the opportunities of the buyer to sue for breach of warranty as much as possible. A buyer will want as few limitations and restrictions as possible.

However, it is a negotiation. A seller refusing to agree to warranties or unduly concerned about restrictions can raise suspicion. The buyer may ask himself - why won't the seller warrant this? What is he hiding? Often he won't be hiding anything, he just wants a clean break as possible...but one never knows!

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