

September 16, 2008

## 9th Circuit Court of Appeals M&A Decision – Indemnification Periods Shorter than Applicable Statute of Limitations May be Subject to Attack

In Western Filter Corporation v. Argan, Inc. (see 2008 U.S. App. LEXIS 18147), the 9th Circuit Court of Appeals, in reversing the district court's grant of summary judgment in favor of the sellers, reached the conclusion under California law that a provision in a stock purchase agreement limiting the survival of representations and warranties to one year after closing did **not** mean that claims for breaches of representation and warranties must be asserted, if at all, within one year after the closing. This decision is consistent with the 9th Circuit's decision in Herring v. Teradyne, Inc. (242 F. App'x 469, 9th Cir. 2007).

### Recommendation

Because of strict construction rules in other states (including New York) and potential public policy issues in some states (including Florida) with having time claim periods shorter than applicable statute of limitations, we think that – at least for sellers – the acquisition agreement should provide that the reps and warranties survive the closing but that claims under the indemnity may be made only within the specified period, making sure that the indemnity is stated to be the exclusive post-closing remedy. A clearly stated provision that restricts survival to a specified period may be just as effective absent the public policy issues. Finally, sellers may want to add the qualifying phrase “whether or not a longer period would be permitted by applicable law” to avoid any assertion of ambiguity.

### Analysis of Decision

Briefly stated, the 9th Circuit held that while California law permits parties to agree to limit indemnification claim periods to ones shorter than the otherwise applicable statute of limitations, under California law (acknowledging that California law is different than at least some other jurisdictions), such limitations are construed strictly. (New York also has a strict construction rule for limitations on contractual limitations on statutes of limitation.) This imposed a felt duty upon the 9th Circuit to search for ambiguity in the survival clause. The court found ambiguity—concluding that a reasonable reading of the clause was “the one-year limitation serves only to specify when a breach of the representations and warranties may occur, but not when the action must be filed.”

The reasonableness of this reading of the clause is questionable: representations and warranties are breached if at all when made at the signing of the acquisition agreement or re-made or “brought down” at the closing. So, unless the sellers were making additional representations after the closing, it is unclear how they could be breached during the one year survival period.



*If you have questions regarding this alert, or the services we provide, please contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.*

B. Scott Burton	404.853.8217	<a href="mailto:scott.burton@sutherland.com">scott.burton@sutherland.com</a>
Robert E. Copps	212.389.5045	<a href="mailto:robert.copps@sutherland.com">robert.copps@sutherland.com</a>
James D. Darrow	202.383.0132	<a href="mailto:james.darrow@sutherland.com">james.darrow@sutherland.com</a>
Peter H. Dean	212.389.5064	<a href="mailto:peter.dean@sutherland.com">peter.dean@sutherland.com</a>
Charles D. Ganz	404.853.8125	<a href="mailto:charles.ganz@sutherland.com">charles.ganz@sutherland.com</a>
Thomas C. Herman	404.853.8089	<a href="mailto:tom.herman@sutherland.com">tom.herman@sutherland.com</a>
Thomas B. Hyman Jr.	404.853.8098	<a href="mailto:tom.hyman@sutherland.com">tom.hyman@sutherland.com</a>
Edward W. Kallal Jr.	404.853.8104	<a href="mailto:edward.kallal@sutherland.com">edward.kallal@sutherland.com</a>
Mark D. Kaufman	404.853.8107	<a href="mailto:mark.kaufman@sutherland.com">mark.kaufman@sutherland.com</a>

© 2008 Sutherland. All Rights Reserved.

This communication is for general informational purposes only and is not intended to constitute legal advice or a recommended course of action in any given situation. This communication is not intended to be, and should not be, relied upon by the recipient in making decisions of a legal nature with respect to the issues discussed herein. The recipient is encouraged to consult independent counsel before making any decisions or taking any action concerning the matters in this communication. This communication does not create an attorney-client relationship between Sutherland and the recipient.

1

# SUTHERLAND

Douglas J. Leary  
David A. Zimmerman

202.383.0703  
404.853.8507

[doug.leary@sutherland.com](mailto:doug.leary@sutherland.com)  
[david.zimmerman@sutherland.com](mailto:david.zimmerman@sutherland.com)