

# BUYING STOCK IN TENNESSEE: AN ANNOTATED MODEL TENNESSEE STOCK PURCHASE AGREEMENT

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## PRELIMINARY NOTE

This form of annotated Tennessee stock purchase agreement (“Model Tennessee SPA”) is styled similarly to the *Model Stock Purchase Agreement with Commentary*<sup>2</sup> published by the American Bar Association (“ABA”). Like the ABA’s model agreement, this Model Tennessee SPA is annotated with explanatory footnotes. Unlike the ABA’s model agreement, however, this Model Tennessee SPA, a relatively short-form agreement, is intended to serve more as a reference tool rather than as a form agreement. Also, it is written and annotated with a focus on Tennessee law and practice.

This Model Tennessee SPA is a near-final acquiror’s form of agreement; it was originally drafted by acquiror’s counsel and has been fully negotiated. Because this is an acquiror’s form of agreement, the representations and warranties in the model generally favor the acquiror in their breadth and allocate much of the risk of a failed closing to the selling shareholders.<sup>3</sup> The Model Tennessee SPA’s provisions

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<sup>2</sup> COMMITTEE ON NEGOTIATED ACQUISITIONS, MODEL STOCK PURCHASE AGREEMENT WITH COMMENTARY (American Bar Association 1995) [hereinafter, the “ABA MODEL AGREEMENT”].

<sup>3</sup> The Tennessee Business Corporations Act uses the term “shareholders” in describing equity owners of a Tennessee corporation, while the corporation statutes of some other states, including Delaware, generally use the term “stockholders.” See TENN. CODE ANN. § 48-11-201 (2002); DEL. CODE ANN.

and related annotations nonetheless are meant to benefit all drafters – those representing acquirors, selling shareholders, and interested third parties. Empty brackets or bracketed text are inserted where deal-specific information (e.g., party names, dollar amounts that are transaction-dependent, disclosures about a party’s business or financial condition, or time frames) is required. The styles and “practice points” of the authors are reflected in this Model Tennessee SPA, and the ABA’s model agreement and other sources of general application also are cited in support of their views, as applicable.

This Model Tennessee SPA is based on a number of general premises. First, it assumes that the acquiror is a privately held Tennessee corporation with total assets in excess of \$100,000,000. The acquiror is seeking to buy all of the outstanding shares of stock of the corporation being acquired, also a privately held Tennessee corporation (the “target”). The acquiror is purchasing the stock with cash. The target is a middle-market medical device manufacturer and distributor<sup>4</sup> with domestic operations that include a production plant. Its annual net sales range from \$50,000,000 to \$500,000,000. The target employs between 100-250 full-time employees.<sup>5</sup> We have assumed that Tennessee law will apply to both the document and the subject stock purchase transaction, and the choice of law provision in Section 8.08 of the Model Tennessee SPA reflects this assumption.

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tit. 8, § 211 (2001). *But see* DEL. CODE ANN. tit. 8, §§ 141 (2002) & 144 (2001) (in which “shareholders” is used).

<sup>4</sup> The fact that the target manufactures and distributes medical devices necessitates compliance with applicable law and all relevant rules and regulations of the federal Food and Drug Administration (“FDA”), including those that may apply to business combination transactions. *See, e.g.*, 21 U.S.C. § 360(b) (2000) (requiring annual registration of owners and operators of medical device manufacturers); 21 C.F.R. § 807.26 (2003) (requiring notice of a change in ownership or corporate structure). Congress established the FDA to, among other things, “protect the public health by ensuring that . . . there is reasonable assurance of the safety and effectiveness of devices intended for human use.” *See* 21 U.S.C. § 393(b)(2) (2000).

<sup>5</sup> Because the target employs over 100 full-time employees, the target may be required to notify its employees of a lay-off under the Worker Adjustment and Retraining Notification Act, should a mass lay-off be anticipated. *See* 29 U.S.C. § 2101(a) (2000); LOU R. KLING & EILEEN T. NUGENT, *NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES AND DIVISIONS* § 5.08 (2003).

This transaction involves the offer and sale of securities.<sup>6</sup> In the Model Tennessee SPA, the acquiror offers to purchase, and the selling shareholders offer to sell, common stock of the target. As a general matter, under Section 5 of the Securities Act of 1933, as amended (the “1933 Act”),<sup>7</sup> absent an available exemption, securities cannot be offered or sold without registration.<sup>8</sup> Similar restrictions exist under the Tennessee Securities Act of 1980, as amended (the “Tennessee Act”).<sup>9</sup> Accordingly, the parties to a stock purchase agreement should always consider whether the offer and sale of the target’s securities by the target’s shareholders are exempt from registration under federal and state securities laws. Typically, a stock purchase transaction like that provided for in the Model Tennessee SPA is exempt

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<sup>6</sup> As a result of the acquisition, the acquiror (a corporation with more than \$100,000,000 in total assets) would hold an aggregate total amount of voting securities of the selling shareholders with an assumed value in excess of \$50,000,000. Because the target is a manufacturing company with annual net sales in excess of \$10,000,000, the transaction must comply with certain notice and waiting period requirements under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended. *See* 15 U.S.C. § 18a (2000). These “jurisdictional thresholds” automatically adjust for inflation beginning on September 30, 2004. *See* STEPHEN M. AXINN ET AL., ACQUISITIONS UNDER THE HART-SCOTT-RODINO ANTITRUST IMPROVEMENTS ACT § S.02[3][c] (2d ed. 1988 & Supp. 2002). There has been notable antitrust enforcement activity in recent years in connection with business combination transactions involving medical device manufacturers. *See* M. Howard Morse, *Settlement of Intellectual Property Disputes in the Pharmaceutical and Medical Device Industries: Antitrust Rules*, 10 GEO. MASON L. REV. 359, 363-364 (2002) (“Much of the FTC’s enforcement in the pharmaceutical and medical device industries has involved mergers and acquisitions requiring government reporting under the Hart-Scott-Rodino Antitrust Improvements Act of 1976.”).

<sup>7</sup> *See* 15 U.S.C. §§ 77a-77aa.

<sup>8</sup> *See id.* § 77e. Exempt securities, as a general matter, are described in Section 3 of the 1933 Act. *See id.* § 77c. Exempt transactions are described in Section 4 of the Act. *See id.* § 77d. *But see id.* §§ 77c(a)(9) to 77c(a)(12), each of which apparently provide for transactional exemptions.

<sup>9</sup> *See* TENN. CODE ANN. § 48-2-104 (2002). The Tennessee Act is found in the Tennessee Code Annotated at §§ 48-2-101 to 48-2-126. State securities laws often are referred to as “Blue Sky” laws. *See* *Hall v. Geiger-Jones Co.*, 242 U.S. 539, 550 (1917).

The name that is given to the law indicates the evil at which it is aimed, that is, to use the language of a cited case, “speculative schemes which have no more basis than so many feet of ‘blue sky’”; or, as stated by counsel in another case, “to stop the sale of stock in fly-by-night concerns, visionary oil wells, distant gold mines and other like fraudulent exploitations.”

*Id.* The first state to pass securities laws was Kansas in 1911. *See* *State v. Agey*, 88 S.E. 726, 728 (N.C. 1916); LOUIS LOSS AND JOEL SELIGMAN, SECURITIES REGULATIONS 9-10 (3d ed. 1995).

from registration under the 1933 Act as a transaction by a person other than the issuer, an underwriter, or a dealer and may be exempt from registration under the Tennessee Act under one or more transactional exemptions.<sup>10</sup> Even if a stock purchase is exempt from registration under federal and state securities laws, a purchase or sale of stock may give rise to securities fraud claims under the 1933 Act or the Securities Exchange Act of 1934, as amended (the “1934 Act”).<sup>11</sup> Under Section 10(b) of the 1934 Act, for example, it is unlawful for any person “[t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance” in contravention of Securities and Exchange

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<sup>10</sup> See 15 U.S.C. § 77d(1); TENN. CODE. ANN. § 48-2-103(b)(4) (exempting sales by affiliates of an issuer to under 15 purchasers, under certain circumstances); *id.* § 48-2-103(b)(7) (exempting “[a]ny transaction in the outstanding securities of an issuer by or on behalf of a person who is neither the issuer of such securities nor an affiliate of such issuer, at a price reasonably related to the market price” that meets certain information disclosure requirements); *id.* § 48-2-103(b)(8) (exempting “[a]ny isolated transaction in securities not involving the issuer of such securities, an underwriter of such securities, or an affiliate of the issuer of such securities.”); see generally ABA MODEL AGREEMENT, *supra* note 2, at 141 (citing to the “so-called 4(1½) exemption, which applies to a private sale between non-issuers and non-underwriters.”); Fredrich H. Thomforde, Jr., *Exemptions from SEC Registration for Small Businesses*, 47 TENN. L. REV. 1, 37-40 (1979) (describing then existing Tennessee securities law exemptions). Under the predecessor to the Tennessee Act, a Tennessee court found that the Tennessee registration requirements apply to private, as well as public, offerings of securities. See *Tucker v. McDell’s, Inc.*, 359 S.W.2d 597, 600 (Tenn. Ct. App. 1961). As a general matter, where a high-net-worth acquiror (or an acquiror that otherwise has substantial financial wherewithal) is knowledgeable about business and financial matters and has had the opportunity to perform diligence on the target, there would seem to be little need to protect the acquiror through securities registration requirements. Similarly, selling shareholders of a small, privately held enterprise (especially a close corporation) are likely to have significant knowledge about the corporation being sold and also may have sufficient knowledge of business and financial matters to evaluate the terms and provisions of an equity purchase transaction. Where these selling shareholders are paid cash for their shares, the need to protect them with securities registration requirements seems limited, at best. Accordingly, one would think that an exemption from registration should be available for a transaction between or among acquirors and selling shareholders with these characteristics. For a thoughtful discussion of the importance of basic securities law knowledge to transactional lawyers, see Bryn Vaaler, *Financing a Small Business in Mississippi: A Practitioner’s Guide to Federal and State Securities Exemptions*, 63 MISS. L.J. 129, 129-38 (1993).

<sup>11</sup> See 15 U.S.C. §§ 78a-78mm (2000). A stock purchase agreement is not, however, a “prospectus” that gives rise to securities fraud liability under Section 12(2) of the 1933 Act. See *Gustafson v. Alloyd Co.*, 513 U.S. 561, 584 (1995); see also J. Dormer Stephen III, *Gustafson: One Small Step (Backward) for Private Plaintiffs, One Giant Leap (Backward) for the Securities Bar*, 49 OKLA. L. REV. 425, 439 (1996); Note, *Gustafson v. Alloyd Co.: The Continued Shrinking of Private-Plaintiff Remedies Under the 1933 Securities Act*, 27 LOY. U. CHI. L.J. 149, 151 (1995).

Commission rules.<sup>12</sup> A like provision is found in Tennessee law.<sup>13</sup> As a general matter, however, a privately held corporation that has not filed any registration statements under the 1933 Act would not be required to file periodic reports or other reports or statements under the 1934 Act.<sup>14</sup>

Finally, the authors desire to note that they have constructed the Model Tennessee SPA with an eye to “plain English” drafting conventions. For example, the authors have avoided the use of “hereof,” “thereof,” “hereunder,” “thereunder,” “hereby,” “thereby,” “whereof,” “wheretofore,” and “whereas.” Moreover, the authors have chosen to use the shorter “under” in lieu of “pursuant to,” and have endeavored to eliminate the ambiguous and overly frequent use of the word “such”

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<sup>12</sup> 15 U.S.C. §78j(b). Most securities fraud actions are brought under Section 10(b) of, and Rule 10b-5 under, the 1934 Act. See 17 C.F.R. § 240.10b-5 (2003); see also Matthew T. Bodie, *Aligning Incentives with Equity: Employee Stock Options and Rule 10b-5*, 88 IOWA L. REV. 539, 546 (2003) (“Rule 10b-5 remains the focus for almost all securities class actions seeking relief for alleged fraud.”); Christopher M. Fairman, *Heightened Pleading*, 81 TEX. L. REV. 551, 597 n.338 (2002) (“Most securities fraud lawsuits allege 10b/10b-5 Claims.”); Nicholas L. Georgakopoulos, *Frauds, Markets, and Fraud-on-the-Market: The Tortured Transition of Justifiable Reliance from Deceit to Securities Fraud*, 49 MIAMI L. REV. 671, 672 n.3 (1995) (“The most famous securities fraud rule is Rule 10b-5 . . . .”); Margaret V. Sachs, *Exclusive Federal Jurisdiction for Implied Rule 10b-5 Actions: The Emperor Has No Clothes*, 49 OHIO ST. L.J. 559, 581 (1988) (characterizing Rule 10b-5 litigation as “the most widely used of any of the federal securities fraud actions.”). Claims in these actions include, among others, materially false or misleading disclosures, failures to disclose material information, insider trading, and “outsider trading.” See, e.g., *United States v. O’Hagan*, 521 U.S. 642 (1997) (“outsider trading”); *Basic Inc. v. Levinson*, 485 U.S. 224 (1988) (alleging materially misleading disclosures and failures to disclose material facts); *Dirks v. SEC*, 463 U.S. 646 (1983) (insider trading in the tipper/tippee context); *Chiarella v. United States*, 445 U.S. 222 (1980) (classical insider trading).

<sup>13</sup> Under Tennessee law:

It is unlawful for any person, in connection with the offer, sale or purchase of any security in this state, directly or indirectly, to: (1) [e]mploy any device, scheme, or artifice to defraud; (2) [m]ake any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading; or (3) [e]ngage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

TENN. CODE ANN. § 48-2-121.

<sup>14</sup> See generally 15 U.S.C. § 78m(a) (requiring the filing of periodic reports by an issuer that has a class of securities registered under Section 12 of the 1934 Act); *id.* at § 78o(d) (requiring the filing of periodic reports by an issuer that has filed a registration statement under the 1933 Act).

as an adjective. The authors have adopted these conventions and choices in an effort to create a clear, readable form of contract.

## STOCK PURCHASE AGREEMENT

This Stock Purchase Agreement (this “**Agreement**”) is made as of December 1, 2003, among [name of acquiring corporation], a Tennessee corporation (the “**Buyer**”), [name of target (corporation being sold)], a Tennessee corporation (the “**Company**”), the shareholders of the Company listed on the signature page of this Agreement (the “**Shareholders**”), and [name of shareholders’ agent] (“**Shareholder Agent**”).<sup>15</sup> Capitalized terms used in this Agreement are defined in the text and set forth in boldface type; an index of these defined terms is attached to the end of this Agreement.

### RECITALS<sup>16</sup>

The Buyer desires to acquire all of the capital stock of the Company owned by the Shareholders, comprising all of the outstanding capital stock of the Company (the “**Stock**”), upon the terms and subject to the conditions of this Agreement.

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<sup>15</sup> The purpose of the Shareholder Agent is to serve as the Shareholders’ representative to the Buyer and to serve as the attorney-in-fact for all of the Shareholders throughout the transaction and during post-closing matters. The specific language of the appointment of the Shareholder Agent, which is contained in Section 8.16 of this Model Tennessee SPA, defines the scope of the Shareholder Agent’s powers and duties. As a practical matter, the appointment of a Shareholder Agent can reduce the burden and complexity of communications and decision making between the parties. For a discussion of the limitations of the authority of an attorney-in-fact appointed to act on behalf of a shareholder in the context of transferring shares of stock, see *Krug v. Watson*, 45 F.3d 430 (Tale), available at 1994 WL 714315 (6th Cir., Dec. 21, 1994).

<sup>16</sup> Although typically not considered a binding part of an agreement, the recitals can be important when interpreting the intent of the parties. See *In re Pyramid Operating Authority, Inc.*, 144 B.R. 795, 814 (Bankr. W.D. Tenn. 1992) (“[R]ecitals . . . may have a material influence in construing the contract and determining the intent of the parties, and in such respect they should, so far as possible, be reconciled with the operative clauses and be given effect.”); ABA MODEL AGREEMENT, *supra* note 2, at 3. Given that the purpose of the recitals is to provide the context for the agreement, we have written these recitals in “plain English” without traditional, but superfluous, words and phrases such as “Witnesseth,” “Whereas,” and “Now, therefore.” For further discussion of plain English and other contract drafting conventions as they apply to agreement preambles and recitals, see GEORGE W. KUNEY, *THE ELEMENTS OF CONTRACT DRAFTING* 27-28, 41 (Thomson-West 2002); Angela Humphries Hamilton & Joan MacLeod Heminway, *Buying Assets In Tennessee: An Annotated Model Tennessee Asset Purchase Agreement*, 4 *TRANSACTIONS: TENN. J. BUS. L.*, 209, 211 n.10 (2003).

The Shareholders desire to sell the Stock to the Buyer upon the terms and subject to the conditions of this Agreement.

In consideration of the premises and mutual promises set forth below and for other good and valuable consideration,<sup>17</sup> the receipt and sufficiency of which are acknowledged, the parties agree as set forth below.

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<sup>17</sup> It is not necessary to include a statement of consideration in the recitals as long as the agreement itself requires consideration in order to be enforceable. *See* THOMAS M. LEVEILLE, TENNESSEE LEGAL AND BUSINESS FORMS Vol. 1, Sec. 1:83 (West 2003). For a brief discussion on the importance of consideration and the drafting of statements of consideration, see KUNEY, *supra* note 16, at 59-60.



## AGREEMENT

### ARTICLE I PURCHASE AND SALE OF STOCK

1.01. Purchase and Sale of Stock. On the Closing Date, the Shareholders shall sell to the Buyer, and the Buyer shall purchase from the Shareholders, all of the Shareholders' rights, title<sup>18</sup> and interest in and to the Stock,

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<sup>18</sup> The meaning of the term "title" as it applies to a holder's legally recognized ownership interest in equity securities of an issuer is unclear. See Michael J. Halloran, *Rendering Opinions of Law – Opinions in Registered Offerings*, in OPINION LETTERS OF COUNSEL 9, 35 (Practicing Law Institute 1984); Scott Fitzgibbon and Donald W. Glazer, *Legal Opinions on Secondary Sales of Stock*, 1988 COLUM. BUS. L. REV. 149, 150-51 (1988) ("The words 'title' and 'encumbrances,' however, are not used by corporate law or Article 8 of the Uniform Commercial Code to define the rights of a purchaser of stock. Lacking firm statutory grounding, those terms are susceptible to a variety of interpretations."). Tennessee's Uniform Commercial Code, for example, provides for the legal transfer and registration of securities, without defining legal title. See TENN. CODE ANN. §§ 47-8-301 to -307, 47-8-401 to -407(2002). However, legal title to stock generally is deemed to reside in holders of record of the certificates representing that stock (i.e., those holders whose names are set forth in the ownership and transfer records of the issuer as the owners of the shares of stock represented by that certificate). See *Peters v. Neely*, 84 Tenn. 275, 282 (1886) ("An assignment of the stock on the books of the company passes the legal title everywhere . . ."). However, indicia of ownership short of record ownership also may evidence legal title. See *Knox County v. Fourth & First Nat'l Bank*, 182 S.W.2d 980, 984 (Tenn. 1944) ("Under the Uniform Stock Transfer Act, section 4094 *et seq.*, of the Code, title vests in the holder of certificates of stock when those certificates are indorsed or accompanied by a power of attorney authorizing their transfer."); *West Nashville Planing-Mill Co. v. Nashville Sav. Bank*, 6 S.W. 340, 342 (Tenn. 1887) ("Thus an assignment of a certificate of stock is held to pass the legal title to such shares to the assignee, even without transfer upon stock book or other notice to the corporation."); *Peters*, 84 Tenn. at 282 ("[T]he assignment of the certificate with a power of attorney to assign on the books" passes legal title of stock in Tennessee). The foundational Tennessee opinion in this area articulates the debate as to the validity of stock title not evidenced on the issuing corporation's books and records.

It came before this court in *Cornick v. Richards*, 3 Lea 1, where the contest was between the holder of a certificate so assigned as collateral security and other creditors of the assignor. Two of the judges, McFarland and Cooper, were of opinion that a complete legal title to stock could only be acquired by a transfer on the books of the company; that an assignment of a certificate of stock, with a blank power of attorney to make the transfer on the books, did not give a complete legal title, but only an equity, good between the parties, and which might be made good against the corporation, and against the creditors and assignees of the assignor by notice to the corporation. The other three judges held that the assignment of the certificate, with a blank power of attorney signed by the assignor, either by way of sale or as collateral security, would pass the title to the

free and clear of all liens, claims and encumbrances of any nature whatsoever (collectively, “**Liens**”).

1.02. Purchase Price.

(a) The purchase price for the Stock (the “**Purchase Price**”) shall be equal to (i) \$[ ] (the “**Preliminary Purchase Price**”), (A) as that amount may be adjusted under Section 1.03(a), (B) plus the amount of the Company’s cash, cash equivalents and marketable securities as of the Closing Date, (C) minus all amounts paid by the Company to satisfy accrued bonuses under the Company’s executive annual incentive compensation plan and the amount of the Company’s obligations in respect of short-term and long-term indebtedness for borrowed money, letters of credit, capital leases and other indebtedness (other than accrued expenses and trade payables, to the extent not evidenced by a note) as of the Closing Date (collectively, the “**Closing Purchase Price**”), as that amount may be further adjusted under Section 1.03(b), plus (ii) any amounts payable to the Shareholders under Section 1.04.

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assignee as against the creditors of the assignor, without any transfer upon the books of the company, or notice to the corporation.

Cherry v. Frost, 75 Tenn. 1, 8 (1881). New York law, however, evidences a more well settled view.

It has also been settled, by repeated adjudications, that, as between the parties, the delivery of the certificate, with assignment and power indorsed, passes the entire title, legal and equitable, in the shares, notwithstanding that, by the terms of the charter or by-laws of the corporation, the stock is declared to be transferable only on its books; that such provisions are intended solely for the protection of the corporation, and can be waived or asserted at its pleasure, and that no effect is given to them except for the protection of the corporation; that they do not incapacitate the shareholder from parting with his interest, and that his assignment, not on the books, passes the entire legal title to the stock, subject only to such liens or claims as the corporation may have upon it, and excepting the right of voting at elections, etc.

McNeil v. Tenth Nat’l Bank, 46 N.Y. 325, 331 (1871). In any case, it is true that those not holding legal title to securities still may have and exercise beneficial ownership or other legally recognized rights or interests, as required or permitted by binding and enforceable contract provisions or applicable law, and this Model Tennessee SPA reflects this reality by accompanying the word “title” with the words “rights” and “interest.” These three terms, when used together, should adequately protect the Buyer. *But see* KUNEY, *supra* note 16, at 37 (regarding legal “doublets” and “triplets”).

(b) The Closing Purchase Price shall be allocated among the Shareholders in the manner specified on Schedule 1.02<sup>19</sup> and shall be paid on the Closing Date as follows:

(i) \$[ ] in immediately available funds (together with all earnings on those funds, the “**Escrow Fund**”)<sup>20</sup> shall be paid by delivery to a federally insured commercial bank reasonably acceptable to the Buyer and the Shareholder Agent (the “**Escrow Agent**”),<sup>21</sup> to be held or disbursed in accordance

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<sup>19</sup> Schedule 1.02 should list each Shareholder and the Shareholder’s proportional share of the Purchase Price, including the amounts scheduled to be distributed from the Escrow Fund after the holdback period has expired. The schedule generally is prepared in columnar form, with the name of each individual Shareholder in the far left column. The Shareholders’ proportional share of the Purchase Price should correlate with the capital structure of the Company immediately prior to the Closing, subject to facts and circumstances specific to the transaction, such as adjustments for preference rights, indebtedness of a particular Shareholder to the Company, or other factors which the Shareholders may work out among themselves. Depending on the number of Shareholders and whether the Shareholders all are present at the Closing, the Buyer may wish to wire proceeds from the transaction to an account designated by the Shareholder Agent, and the Shareholder Agent then would distribute the funds in the proportions and otherwise in the manner described in Schedule 1.02. Finally, Schedule 1.02 also may be used to determine each Shareholder’s share of any indemnification obligations under Section 7.01, if the Buyer’s indemnification claims should exceed the amount of the Escrow Fund. See KUNEY, *supra* note 16, at 31 (regarding the use of information schedules in contract drafting).

<sup>20</sup> Based on the size of the transaction, the Buyer and the Shareholders have agreed to transfer a portion of the Purchase Price to an Escrow Fund administered by the Escrow Agent. An acquiror may demand an escrow provision to insure its ability to obtain jurisdiction over the selling shareholders in the event the acquiror needs to enforce its indemnification rights. The size of any escrow and the time period the funds are held in escrow will vary depending upon the perceived risks of the transaction and underlying business of the target. For a detailed discussion of escrow provisions, see ABA MODEL AGREEMENT, *supra* note 2, at 206-09; JAMES C. FREUND, ANATOMY OF A MERGER: STRATEGIES AND TECHNIQUES FOR NEGOTIATING CORPORATE ACQUISITIONS 382-88 (1975) (regarding the use of escrow arrangements in acquisition transactions); Unreported Case: *Manor Healthcare Corp. v. Tolbert*, No. 8425, 12 DEL. J. CORP. L. 297 (1987) [hereinafter, “*Manor Healthcare*”].

<sup>21</sup> A nationally recognized financial institution often serves as the escrow agent; however, in some cases, the attorney or law firm of the acquiror or selling shareholders (or both), will serve as Escrow Agent. See Hamilton & Heminway, *supra* note 16, at 221 n.31. The size of the transaction, along with the projected costs and expenses associated with a particular financial institution, attorney, or law firm, may be factors relevant to the parties’ selection of an escrow agent.

with the terms of an Escrow Agreement in substantially the form of Exhibit A (the “**Escrow Agreement**”);<sup>22</sup> and

(ii) the remainder of the Closing Purchase Price shall be paid to the Shareholders in immediately available funds.<sup>23</sup>

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<sup>22</sup> The Escrow Fund, the escrowed portion of the Closing Purchase Price, represents a pool of funds readily available in the event that the Buyer makes a claim for indemnification against the Shareholders under Article VII. An escrow arrangement such as this is a common attribute of business combination transactions. See sources cited *supra* note 20; Martin H. Brinkley, *The Regulation of Contractual Change: A Guide to No Oral Modification Clauses for North Carolina Lawyers*, 81 N.C. L. REV. 2239, 2280 (2003) (referencing the use in business combination transactions of “escrow agreements under which portions of the purchase price are retained pending the occurrence of certain events.”); Ronald J. Gilson, *Value Creation by Business Lawyers: Legal Skills and Asset Pricing*, 94 YALE L.J. 239, 282 (1984) (“the seller’s promise to indemnify the buyer is frequently backed by the buyer’s or a neutral third party’s retention of a portion of the consideration as a fund to assure the seller’s performance of its indemnification obligation.”); *Manor Healthcare*, *supra* note 20, at 300; Jeanne L. Schroeder, *Three’s a Crowd: A Feminist Critique of Calabresi and Melamed’s One View of the Cathedral*, 84 CORNELL L. REV. 394, 485 (1999) (“In corporate acquisitions, it is common for buyers to ‘hold back’ or escrow part of the purchase price for a negotiated period to allow rival claimants to step forward.”). The Escrow Agreement, a negotiated contract among the Buyer, the Shareholder Agent (on behalf of the Shareholders), and the Escrow Agent, typically would include provisions relating to (among other potential items): the receipt and investment of, and allocation of investment proceeds on, the Escrow Fund; the matters as to which claims may be made against the Escrow Fund; the procedures for making claims and disbursing amounts in the Escrow Fund; the payment of fees of the Escrow Agent; liability standards and indemnification regarding the actions of the Escrow Agent; and the interpretation, amendment, and termination of the Escrow Agreement.

<sup>23</sup> A privately negotiated, secondary stock purchase transaction like the one represented in this Agreement is considered a transfer of property and, as a business transaction, is not separately ordained by corporate law or any other specific body of statutory law. Accordingly, the form of consideration paid or delivered to a selling shareholder by an acquiror of stock is not restricted by corporate law and may consist of any elements of value acceptable to the selling shareholders. Consideration used in a stock purchase may consist of (among other things) cash, securities, other property, or any combination of these elements. Conversely, state corporate law generally does restrict the consideration that may be received by corporations in primary stock issuances. See TENN. CODE ANN. § 48-16-202(b) (“The board of directors may authorize shares to be issued for consideration consisting of any tangible or intangible property or benefit to the corporation, including cash, promissory notes, services performed, contracts for services to be performed, or other benefits to be received, or other securities of the corporation.”). Consideration for mergers also typically is provided for by statute. See TENN. CODE ANN. § 48-21-102 (restricting merger consideration to “[s]hares, units, cash or other property, obligations or other securities of one (1) or more of the surviving or new corporations or limited partnerships or of any other party to the merger; or . . . [a]ny combination of the foregoing”). To the extent that the consideration in the transaction consists in whole or in part of property properly classified as securities (stock, notes, debentures, etc.),

### 1.03. Working Capital Adjustment; Post-Closing Audit.

(a) Not more than 10 business days<sup>24</sup> prior to the Closing Date,<sup>25</sup> the Shareholders and the Buyer will, in good faith,<sup>26</sup> jointly estimate what the

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consideration should be given to compliance with federal and state laws governing the registration of securities. *See* 15 U.S.C. §§ 77a-77aa; TENN. CODE ANN. §§ 48-2-101 to -201. Promissory notes, for example, may be used as consideration in a stock purchase transaction. Under those circumstances, a practitioner should assess whether the promissory notes being offered in the transaction constitute “securities” such that federal or state securities registration requirements apply. *See* 15 U.S.C. § 77b(a)(1) (defining the term “security” under the 1933 Act to include “any note,” unless the context otherwise requires); TENN. CODE ANN. § 48-2-102(16) (defining the term “security” under Tennessee law to include, unless the context otherwise requires, “any note” other than “[a] note or other evidence of indebtedness issued in a mercantile or consumer, rather than an investment, transaction”); *Reves v. Ernst & Young*, 494 U.S. 56, 64-65 (1990) (adopting the “family resemblance” test to determine when a note is a security under the 1934 Act). Moreover, to the extent that financial instruments or agreements classifiable as “investment contracts” are used as consideration in a stock purchase transaction, federal or state securities registration requirements likely would apply because investment contracts also are securities under federal and state law, unless the context otherwise requires. *See* SEC v. W. J. Howey Co., 328 U.S. 293, 298-99 (1946) (defining an “investment contract” under the Securities Act of 1933, as amended); *King v. Pope*, 91 S.W.3d 314, 322 (Tenn. 2002) (“The appropriate test for defining an ‘investment contract’ under Tennessee law is the Hawaii Market test . . .”). Earnouts, *see infra* note 32, also may be securities under the 1933 Act. *See* Lori Anne Czepiel, *Bridging the Valuation Gap: Ten Key Issues to Consider When Structuring an Earnout*, in ACQUIRING & SELLING THE PRIVATELY HELD COMPANY – A SATELLITE PROGRAM 578 (Practicing Law Institute 2003).

<sup>24</sup> The term “business days” is not defined in this Model Tennessee SPA; however, the term generally refers to weekdays on which banks in an applicable jurisdiction are open for business. *See Master Power Purchase and Sale Agreement*, 21 ENERGY L.J. 301, 309 (2000) (defining a business day to include “any day except a Saturday, Sunday, or a Federal Reserve Bank holiday”). *See also* Hamilton & Heminway, *supra* note 16, at 219 n.25.

<sup>25</sup> Generally, the Buyer and the Shareholders negotiate the date on which the Working Capital estimate takes place, but, given the Shareholders’ presumed familiarity with the Company’s business and financial affairs and the Buyer’s earlier motive and opportunity to perform due diligence on the Company, ten business days (or approximately two calendar weeks) prior to the Closing Date is within a customary range.

<sup>26</sup> Like all contracts, securities purchase transactions and acquisition agreements include an implied covenant of good faith and fair dealing. *See* Judd F. Sneirson, *Merger Agreements, Termination Fees, and the Contract-Corporate Tension*, 2002 COLUM. BUS. L. REV. 573, 627 (“Implied provisions in every contract, such as the implied covenant of good faith and fair dealing, can, like conventional contract damages, offer a middle ground in these situations and give a potential acquiror a less favorable, but

Company's Working Capital will be as of the Closing Date on a reasonable basis using the Company's then available financial information; if the Shareholders and the Buyer cannot agree on an estimate, then the Company's Working Capital shall be estimated by taking the average of the respective good faith determinations of the Shareholders and the Buyer. The amount of the Company's Working Capital as finally estimated is referred to as "**Estimated Working Capital.**" At the Closing, the Preliminary Purchase Price will be adjusted on a dollar-for-dollar basis as follows: if Estimated Working Capital exceeds the Working Capital Peg, then the Preliminary Purchase Price will be increased by the amount of the excess; if Estimated Working Capital is less than the Working Capital Peg, then the Preliminary Purchase Price will be decreased by the amount of the deficiency. The adjustment to the Preliminary Purchase Price described in this Section 1.03(a) shall be in addition to, and shall be made prior to, any adjustments to the Preliminary Purchase Price made in compliance with Section 1.02(a)(i)(B) or (C).

(b) On or before March 31, 2004, the Buyer shall prepare and deliver to the Shareholder Agent the Company's audited financial statements for the fiscal year ended December 31, 2003, a balance sheet of the Company as of the Closing Date prepared in accordance with generally accepted accounting principles ("**GAAP**") applied on a basis consistent with prior periods and, to the extent that the same are consistent with GAAP, the Company's current accounting principles and policies as reflected in the Company's books and records prior to the Closing Date (the "**Closing Balance Sheet**")<sup>27</sup> and its calculation of the Company's Working

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similar, contractual provision in place of what it bargained for and lost."); Andrew Laurance Bab, Note: *Debt Tender Offer Techniques and the Problem of Coercion*, 91 COLUM. L. REV. 846, 861-66 (1991). The implied covenant has been recognized by courts construing business and commercial transactions in Tennessee. See *Wallace v. Nat'l Bank of Commerce*, 938 S.W.2d 684, 686 (Tenn. 1996) ("In Tennessee, the common law imposes a duty of good faith in the performance of contracts."); *Johnson v. Welch*, No. M2002-00790-COA-R3-CV, 2004 Tenn. App. LEXIS 86, at \*25-26, 48-49 (Tenn. Ct. App., Feb. 9, 2004); *Covington v. Robinson*, 723 S.W.2d 643, 645 (Tenn. Ct. App. 1986) ("Every contract imposes upon each party a duty of good faith and fair dealing in its performance and enforcement."). The Tennessee Uniform Commercial Code also includes a good faith obligation. See TENN. CODE ANN. § 47-1-203 (2002). Because the existence, nature and extent of a contracting party's implied obligation of good faith is determined by decisional law, however, contracting parties often provide for an express good faith obligation in provisions where the obligation is particularly important.

<sup>27</sup> This Model Tennessee SPA contemplates that the Buyer will prepare the initial version of the Closing Balance Sheet instead of the Shareholders. If the Shareholders will no longer be active participants in the Company, the Buyer likely will be in a better position to deliver the initial version

Capital as of the Closing Date; provided, however, that the Buyer will use its reasonable commercial efforts<sup>28</sup> to provide the Shareholder Agent with a preliminary Closing Balance Sheet by February 29, 2004.<sup>29</sup> The Shareholder Agent shall have a period of 30 days after receipt of the Closing Balance Sheet and the Buyer's Working Capital calculation to review them and to notify the Buyer of any disputes regarding the Closing Balance Sheet or Working Capital calculation.<sup>30</sup> During the 30-day review period, the Shareholder Agent shall have full access to the Buyer's work papers and to the persons who prepared the Closing Balance Sheet, the Buyer's Working Capital calculation and the Company's Working Capital calculation. If the Shareholder Agent notifies the Buyer of any disputes in accordance with this Section 1.03(b), then the parties will negotiate in good faith in an effort to resolve those disputes. If the parties are unable to resolve any dispute within 30 days after the Buyer receives notice, then either party may submit that dispute for resolution to an

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of the Closing Balance Sheet; however, in many cases, the Shareholders (or previous management), along with the Company's previous auditor, will have relevant "institutional knowledge" regarding the Company, which may enable the Shareholders, working with the Company's previous auditor, to deliver the Closing Balance Sheet on a quicker and more efficient basis. In either case, the parties should ensure that the Closing Balance Sheet is prepared in accordance with the Company's historic practices. *See infra* Section 1.05.

<sup>28</sup> "Reasonable commercial efforts," "commercially reasonable efforts," "reasonable best efforts," "best efforts," and like performance standards are found throughout acquisition agreements and tend to be negotiated terms. Although there is some debate about the matter, "best efforts" may be interpreted as requiring the most significant effort on the part of the performing party. *See* ABA MODEL AGREEMENT, *supra* note 2, at 5, 154; KLING & NUGENT, *supra* note 5, at § 13.06; George W. Dent, Jr., *The Role of Lawyers in Strategic Alliances*, 53 CASE W. RES. L. REV. 953, 954 (2003) (stating "... lawyers often feel uneasy when a contract specifies that the performance required on one side is to use 'best efforts.'"); Hamilton & Heminway, *supra* note 16, at 239-40 n.64 (regarding: the "commercially reasonable efforts" and "best efforts" standards in an asset purchase agreement); Glenn D. West & Susan Y. Chao, *Corporations*, 56 SMU L. REV. 1395, 1422-23 (2003) (regarding "best efforts" and "reasonable best efforts" obligations under a merger agreement); *see generally infra* Section 4.05 of this Model Tennessee SPA (discussing the obligation of parties with respect to action to be taken under the Agreement).

<sup>29</sup> This date is negotiable. It represents a reasonable date for completion of audited financial statements and gives the Buyer a date to "press for" that is earlier than its ultimate deadline (allowing for more time to correct errors should there be mistakes in the financial statements).

<sup>30</sup> The Closing Balance Sheet may be the subject of dispute for various reasons, including the calculation of the adjustment for Working Capital and the potential tax implications of the Closing Balance Sheet on the parties. In certain cases, the Buyer may view the review process as another chance to perform due diligence on the Company (in a somewhat limited capacity).

accountant with an independent accounting firm of recognized national or regional standing mutually acceptable to the Buyer and the Shareholder Agent. If they cannot agree, the Shareholder Agent and the Buyer shall choose a Big Four accounting firm by lot (with each party having the right to strike one firm).<sup>31</sup> The resolution of any dispute by that accounting firm shall be rendered within 30 days after submission of the dispute to the accounting firm and shall be conclusive and binding upon the parties. The fees and expenses of the accounting firm shall be shared 50% by the Shareholders and 50% by the Buyer.

(c) If the Company's Working Capital, as determined in accordance with Section 1.03(b), is less than the Estimated Working Capital, then the Shareholders shall pay to the Buyer the amount of the deficiency (in the proportions set forth on Schedule 1.03(c)). If the Company's Working Capital, as determined in accordance with Section 1.03(b), exceeds the Estimated Working Capital, then the Buyer shall pay to the Shareholders the excess amount (distributed among the Shareholders in the proportions set forth on Schedule 1.03(c)). All payments under this subsection shall bear interest from the Closing Date to the date of payment at the rate of [ ]% per annum<sup>32</sup> and shall be made within 10 days (1) after conclusion of the 30-day review period described in Section 1.03(b) or, (2) if the Shareholder Agent notifies the Buyer of a dispute under Section 1.03(b), after final resolution of any disputes under Section 1.03(b).

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<sup>31</sup> The dispute resolution method utilized in this Agreement contemplates that the parties will use a Big Four national accounting firm as the final arbitrator. The use of Big Four national accounting firm may be appropriate in many cases, particularly when the parties are from different regions of the country and are concerned about territorial biases of a local or regional accounting firm. However, when selecting a dispute resolution mechanism for the Closing Balance Sheet and the Working Capital calculation, the parties should consider the size of the transaction along with the projected cost of the desired dispute resolution mechanism in making a final determination as to the dispute resolution mechanism and who will serve as the arbitrator/mediator. For a discussion of the use of alternative dispute resolution provisions in business contracts, see KUNEY, *supra* note 16, at 113-15.

<sup>32</sup> The purpose of this provision is to compensate the recipient of the proceeds from the Working Capital adjustment for the time-value of the Working Capital shortfall or surplus. When establishing an acceptable interest rate, the parties should keep in mind the usury laws of the State of Tennessee. *See generally* TENN. CODE ANN. § 47-14-117 (2002). A legally permissible interest rate will be based upon the applicable formula rate, which is defined as "an annual rate of interest four (4) percentage points above the average prime loan rate . . . , or twenty-four percent (24%) per annum, whichever is less." TENN. CODE ANN. § 47-14-102(6).



(d) “**Working Capital Peg**” means \$[ ], and the Company’s “**Working Capital**” means the working capital of the Company determined in accordance with GAAP applied on a basis consistent with prior periods and, to the extent that the same are consistent with GAAP, the Company’s current accounting principles and policies as reflected in the Company’s books and records prior to the Closing Date and otherwise in the manner specified on Schedule 1.03(d).

#### 1.04. Earn-Out Payment.<sup>33</sup>

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<sup>33</sup> An “earn-out” or “earnout” is a contingent portion of an acquisition purchase price, payable by an acquiror to a seller only upon the satisfaction of certain conditions relating to the financial performance of the acquired business for a fixed period of time after the closing of the acquisition. See FREUND, *supra* note 20, at 204. Freund explains earn-outs as follows:

[A]lthough the transfer of the seller’s business to the purchaser is completed at the closing, the payment of at least a portion of the price is made expressly contingent on the achievement by the seller’s company (operating either as a subsidiary or division of the purchaser) of certain specified levels of earnings during a period of several years *following* the closing.

*Id.*; see also Czepiel, *supra* note 23, at 573 (stating “[a]n earnout is a form of contingent payment, which may be a useful method of determining a purchase price when a buyer and seller cannot agree on the value of the business to be sold.”); Ronald J. Gilson, *Value Creation by Business Lawyers: Legal Skills and Asset Pricing*, 94 YALE L.J. 239, 262-64 (1984) (explaining the context and value of earnout pricing in business transactions); Dale Arthur Oesterle, *The Inexorable March Toward a Continuous Disclosure Requirement for Publicly Traded Corporations: “Are We There Yet?”* 20 CARDOZO L. REV. 135, 225 n.169 (1998) (“An earnout is a portion of the purchase price determined by an allocation of a period of future earnings of the business.”); Scott R. Peppet, *Contract Formation in Imperfect Markets: Should We Use Mediators in Deals?*, 38 OHIO ST. J. ON DISP. RESOL. 283, 286 (2004) (“Lawyers can bridge such gaps, however, using an ‘earnout contract’ that makes payment contingent on performance.”). The negotiation dynamic regarding earnout provisions is well explained by Professor Jeffrey L. Kwall.

Often, the seller of a business is far more optimistic about its future prospects than the buyer, and she will demand a higher price than the buyer is willing to pay. The buyer might pay the higher price if he were certain that the seller’s expectations would materialize, but this will not be known until after the business is transferred. Making a part of the purchase price contingent on future profits bridges the gap - if the profits the seller anticipates materialize, the seller receives additional consideration; if the profits fail to materialize, the buyer's cost does not increase.

Jeffrey L. Kwall, *Out with the Open-Transaction Doctrine: A New Theory for Taxing Contingent Payment Sales*, 81 N.C.L. REV. 977, 979 (2003). Earnouts are typically heavily negotiated, with the crux of the negotiations being centered around the formula to be used, the manner of computing earnings for purposes of the formula, tax implications relating to the contingent payments, how and by whom the

(a) Within 10 days after they have been prepared and approved by the Company's board of directors, but in no event later than March 31, 2005, the Buyer shall deliver to the Shareholder Agent a copy of the Company's audited financial statements for the fiscal year ended December 31, 2004 (the "**Company Financial Statements**"), together with its calculation of the Company's EBITDA and the Earn-Out Payment, as applicable, calculated in accordance with this Section 1.04. The Shareholder Agent shall have a period of 30 days after receipt of the Company Financial Statements and the Buyer's EBITDA and Earn-Out Payment calculation to review them and to notify the Buyer of any disputes regarding the Company Financial Statements or either calculation. During the 30-day review period, the Shareholder Agent shall have full access to the Buyer's work papers and to the persons who prepared the Company Financial Statements and calculated EBITDA and Earn-Out Payment, as applicable. If the Shareholder Agent shall so notify the Buyer of any disputes, then the parties will negotiate in good faith in an effort to resolve those disputes. If the parties are unable to resolve any dispute within 30 days after the Buyer receives notice, then either party may submit that dispute for resolution to an accountant with an independent accounting firm of recognized national or regional standing mutually acceptable to the Buyer and the Shareholder Agent. If they cannot agree, the Shareholder Agent and the Buyer shall choose a Big Four accounting firm by lot (with each party having the right to strike one firm). The resolution of any dispute by that accounting firm shall be rendered within 30 days after submission of the dispute to the accounting firm and shall be conclusive and binding upon the parties. The fees and expenses of the accounting firm shall be shared 50% by the Shareholders and 50% by the Buyer. The Buyer also shall cause the Company to deliver to the Shareholder Agent interim financial statements at the same time that it delivers those statements to its senior lenders. The Buyer's obligation to deliver Company Financial Statements and interim financial statements shall cease once the Earn-Out Payment (if any) has been made in full.

(b) No amount shall be payable under this Section in respect of the Earn-Out Payment unless the Company's EBITDA for its fiscal year ended December 31, 2004, exceeds \$[A]. If the Company's EBITDA for that fiscal

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business will be run during the earn-out period, and the rights of the purchaser to terminate the agreed-upon management of the business or to liquidate the business during the earn-out period (the "kick-out clause"). See FREUND, *supra* note 20, at 206-23; Czepiel, *supra* note 23, at 573-79 (raising these and other earnout issues).

year exceeds \$[A], the Company shall pay to the Shareholders an amount (the “**Earn-Out Payment**”) equal to the lesser of (i) \$[B] or (ii) the amount obtained under the following formula:<sup>34</sup>

$$\text{Earn-Out Payment} = \$[B] \times \frac{2004 \text{ EBITDA} - \$[A]}{1,000,000}$$

The Earn-Out Payment shall be made within 30 days after either conclusion of the 30-day review period described in Section 1.04(a) or, if the Shareholder Agent notifies the Buyer of a dispute under Section 1.04(a), after final resolution of all dispute under Section 1.04(a). The Earn-Out Payment shall be shared among the Shareholders in the same proportions as payments made to the Shareholders under Section 1.03(c).

(c) The Company’s “**EBITDA**”<sup>35</sup> for a particular fiscal year means its net income for that fiscal year, minus the portion of that net income (or plus any losses) attributable to businesses acquired by the Company after the Closing Date, plus (or minus), to the extent deducted (or added) in determining net income:

- (i) interest expense;
- (ii) any provision for (or any benefit from) income and franchise taxes; and

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<sup>34</sup> Earn-out provisions are notoriously complex but serve a significant purpose in that they provide an acquiror with additional security that the acquiror is not paying too much for the target. Earn-out provisions also reward sellers in that the acquiror is required to make an additional payment to the sellers if the target achieves certain financial milestones during a specified period of time following the closing. *See generally* sources cited *supra* note 33.

<sup>35</sup> EBITDA is the acronym for “earnings, before interest, taxes, depreciation and amortization.” In the context of this transaction, EBITDA is used to measure the basis of the Earn-Out Payment. Because the method of calculating EBITDA can vary considerably from business to business (and person to person), it is critical that the Buyer and the Shareholders establish some criteria for all parties to follow for calculating EBITDA in the context of this transaction to ensure that the Earn-Out Payment actually coincides with measures of the financial performance of the Company. For a discussion of how EBITDA is used to value businesses, see ROBERT B. DICKIE, FINANCIAL STATEMENT ANALYSIS AND BUSINESS VALUATION FOR THE PRACTICAL LAWYER 114-15 (American Bar Association 1998).

(iii) depreciation and amortization.

(d) If, prior to the payment in full of the Earn-Out Payment, if any, there shall occur (i) a merger or consolidation under which all of the outstanding shares of the Company are converted into or exchanged for securities or property of another Person; (ii) the acquisition by a Person or group of related Persons<sup>36</sup> in a single transaction or a series of related transactions of more than 50% of the issued and outstanding shares of the Company; or (iii) the sale of all or substantially all of the assets<sup>37</sup> of the Company in a single transaction or a series of

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<sup>36</sup> The term “group of related Persons” is not defined in this Agreement. As a general matter, a group of related persons may be deemed to include Persons (as defined in Section 2.04 of this Agreement) who are personally or professionally affiliated or associated with each other in some way. *See* ABA MODEL AGREEMENT, *supra* note 2, at 26-27 (defining “Related Person”); Glenn E. Coven, *The Affinity Provisions of the Internal Revenue Code: A Case Study in Nonsimplification*, 45 TENN. L. REV. 557, 598 (1978) (noting that, for specific federal income tax purposes, a “group of related persons” includes “the taxpayer, his spouse, and his children”). A drafter may determine to add clarity to the term by defining it expressly in the agreement or by defining the term “Person” broadly to include groups of individuals or entities that the drafter intends to target. Various statutory and regulatory definitions may be useful in constructing definitions of this kind. For example, the rules and regulations under the 1934 Act indicate that a “group,” for purposes of determining the beneficial ownership of securities under Section 13(d) of the 1934 Act, is constituted “[w]hen two or more persons agree to act together for the purpose of acquiring, holding, voting or disposing of equity securities of an issuer. . . .” 17 C.F.R. § 240.13d-5(b)(1) (2003). Rules and regulations under the 1934 Act also define the term “affiliate” to include “a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified” and the term “associate” to include

(1) any corporation or organization (other than the registrant or a majority-owned subsidiary of the registrant) of which such person is an officer or partner or is, directly or indirectly, the beneficial owner of 10 percent or more of any class of equity securities, (2) any trust or other estate in which such person has a substantial beneficial interest or as to which such person serves as trustee or in a similar fiduciary capacity, and (3) any relative or spouse of such person, or any relative of such spouse, who has the same home as such person or who is a director or officer of the registrant or any of its parents or subsidiaries.

17 C.F.R. § 240.12b-2 (2003).

<sup>37</sup> The term “substantially all” is not defined in this Agreement. The Tennessee Corporation Act makes use of this term, in a similar context, without definition. *See, e.g.*, TENN. CODE ANN. § 48-22-101(a) (“[a] corporation may. . . [s]ell, lease, exchange, or otherwise dispose of all, or substantially all, of its property in the usual and regular course of business”); TENN. CODE ANN. § 48-22-102(a) (“A corporation may sell, lease, exchange, or otherwise dispose of all, or substantially all, of its property . . . otherwise than in the usual and regular course of business . . . if the board of

related transactions, then the Buyer shall establish or cause to be established an escrow fund in the amount of \$[ ]<sup>38</sup> out of the proceeds of that transaction for the purpose of satisfying the obligations of the Buyer under this Section 1.04 in respect of the Earn-Out Payment.

(e) Until December 31, 2004, the Buyer shall cause the Company to be operated in a manner substantially consistent with past practice (it being understood that this shall not prevent the Company from making acquisitions,

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directors proposes and its shareholders approve the proposed transaction.”). Similarly, the General Corporation Law of the State of Delaware provides that:

Every corporation may at any meeting of its board of directors or governing body sell, lease or exchange all or substantially all of its property and assets, including its goodwill and its corporate franchises, upon such terms and conditions and for such consideration, which may consist in whole or in part of money or other property, including shares of stock in, and/or other securities of, any other corporation or corporations, as its board of directors or governing body deems expedient and for the best interests of the corporation . . . .

DEL. CODE ANN. tit. 8, § 271(a) (2001). Although no Tennessee court yet has construed the meaning of “substantially all” under Tennessee law, the term has been construed many times by the Delaware State courts under the corporate and contract law of Delaware and other jurisdictions. *See* *Gimbel v. Signal Cos.*, 316 A.2d 599, 606 (Del. Ch. 1974), *aff’d*, 316 A.2d 619 (Del. 1974) (finding that an asset sale transaction represents a sale of “substantially all” of the assets if “the sale is of assets quantitatively vital to the operation of the corporation and is out of the ordinary and substantially affects the existence and purpose of the corporation . . .”); *In re Nantucket Island Assocs. Ltd. P’ship Unitholders Litig.*, 810 A.2d 351, 369-70 (Del. Ch. 2002) (“Our jurisprudence eschewed a definitional approach . . . focusing on the interpretation of the words “substantially all” in favor of a contextual approach . . . .”); *Winston v. Mandor*, 710 A.2d 835, 843 (Del. Ch. 1997) (“The . . . determination of whether there is a sale of substantially all assets . . . depends upon the particular qualitative and quantitative characteristics of the transaction at issue. Thus, the transaction must be viewed in terms of its overall effect on the corporation, and there is no necessary quantifying percentage.”); *Philadelphia Nat’l Bank v. B.S.F. Co.*, 199 A.2d 557, 561-62 (Del. Ch. 1964), *rev’d on other grounds*, 204 A.2d 746 (Del. 1964) (finding a corporation’s sale of a noncontrolling stock interest in another entity to be a sale of substantially all of the corporation’s assets under a Pennsylvania law indenture, stating that “an investor should not be without remedy when his corporation, in breach of contract, abruptly disposes of what has ostensibly been its principal business.”).

<sup>38</sup> This dollar amount generally would be equal to the maximum amount of the Earn-Out Payment, as calculated in accordance with Section 1.04(b) of this Model Tennessee SPA.

growing the business or taking steps to improve profitability).<sup>39</sup> The Buyer and the Company shall not seek to avoid or reduce the amount of the Earn-Out Payment.

1.05. Calculations. All calculations in this Article I shall be made in accordance with GAAP applied on a basis consistent with prior periods and, to the extent that the same are consistent with GAAP, the Company's current accounting principles and policies as reflected in the Company's books and records prior to the Closing Date.

## ARTICLE II REPRESENTATIONS AND WARRANTIES OF THE COMPANY PARTIES

The Company and the Shareholders (collectively, the "**Company Parties**")<sup>40</sup> represent and warrant to the Buyer as follows:

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<sup>39</sup> Until the Earn-Out Payment period ends, the Buyer is required to operate the Company in essentially the same manner as it was operated before Closing. The purpose of this covenant is to ensure that the Earn-Out Payment will be based upon the Company's actual financial performance after the Closing, based on operations substantially equivalent to those conducted by the Company prior to the Closing. This covenant also reduces the risk of the Buyer manipulating the operations of the business to avoid making the Earn-Out Payment. *See* FREUND, *supra* note 20, at 203-23; *see also* ABA MODEL AGREEMENT, *supra* note 2, at 43 (advising drafters that they may want to define various standards, including "past practice," used in purchase price adjustment provisions).

<sup>40</sup> This Model Tennessee SPA does not specify the precise nature of the joint representations and warranties (or indemnification) made in this Article II. The representations may be made either (a) proportionately (making more likely the prospect that each Shareholder may be held liable only for his, her, or its proportional share of any damages arising from or in connection with a breach) or (b) jointly and severally (allowing for each Shareholder to be held individually liable for the entire amount of damages arising from or in connection with a breach).

Holding each negligent actor liable for all the damages caused by all the negligent actors substantively distinguishes joint and several liability from several liability. Under several liability, each actor is liable for only its proportionate share of the damages, usually its percentage fault. The plaintiff's right to sue each tortfeasor separately, or not at all, or all together, distinguishes joint and several liability procedurally from joint liability. Under joint liability, all the defendants must be sued together and their liability adjudicated in one action.

Daniel J. Bussel, *Liability for Concurrent Breach of Contract*, 73 WASH. U. L.Q. 97, 110-11 (1995). *See* Robert C. Riter, Jr. & David A. Pfeifle, *An Invitation for Lawyers' Participation in Civil Justice Reform*, 42 S.D. L. REV. 243, 245 (1997) (noting, with respect to tort reform, that "[j]oint and several liability represents a social policy regarding the choice between "insuring" plaintiffs through wealthy, but

2.01. Organization and Qualification. The Company is a corporation duly organized,<sup>41</sup> validly existing, and in good standing under the laws of

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minimally liable defendants, or reducing the total amount paid to plaintiffs while protecting some defendants.”). The Shareholders generally would prefer proportionate liability for breach of a representation, while the Buyer typically would desire joint and several liability for breach of a representation. The Buyer may, however, bargain the joint and several character of the representations and warranties away based upon, among other things, the nature of the indemnification provisions and the attributes and size of the closing escrow.

An acquisition agreement . . . is a negotiated document that in large part reflects the parties’ relative bargaining power and the other attendant circumstances (including time pressure). This is, in turn, a function of the basic economics of the transaction: the attractiveness of the purchase price, the prospect of competing purchasers and the availability on the market of substitutes for the business being acquired. Nowhere is this concept truer than in the case of the Seller’s representations and warranties, in terms of both their number and their scope, and the related indemnification provisions.

KLING & NUGENT, *supra* note 5, at § 11.01[2]. Under certain circumstances, a purchaser of stock may agree to accept representations and warranties from less than all of the selling shareholders (where, for example, certain shareholders own *de minimis* amounts of stock in the company being acquired). As with all substantive issues involving representations and warranties (which cannot be evaluated in isolation, but rather in conjunction with covenants, conditions, and indemnification), the following advice is extremely well taken:

[W]hen thinking about these sorts of clauses as a drafter, *you should approach the problem from the desired remedy first*. For example, if certain facts are misstated, what remedy do you wish to seek [and against whom]? Possibilities include rescission pre-closing, rescission post-closing, or consequential or liquidated damages from the other party or from a credit-worthy third party or fund. Then select the provisions that will produce a cause of action for your client that is ripe when needed, lies against the appropriate defendant, and provides the desired remedy.

KUNEY, *supra* note 16, at 75 (2002) (bracketed text added by authors).

<sup>41</sup> Use of the terms “duly organized” and “duly incorporated” is common to acquisition agreements and legal opinions in the United States. See Stephan Hutter, *Rethinking Legal Opinion Letters: The Corporate Opinion in International Transactions*, 1989 COLUM. BUS. L. REV. 427, 429-31 (describing the meaning and usage of these terms in opinion letters). As a general matter, substantiation of a representation that a corporation is *duly* organized or incorporated (as opposed to an equivalent representation that does not include the word “duly”) requires an inquiry into more than just the certified records of the Secretary of State in the jurisdiction of incorporation. (*E.g.*, internal governance records of the corporation, including consents or minutes of meetings of the incorporator(s) or initial board of directors, should be examined to ensure that all steps to effectuate

the State of Tennessee. The Company is duly qualified to do business as a foreign corporation and is in good standing in the jurisdictions listed on Schedule 2.01, which are all of the jurisdictions in which the ownership of its properties or the nature of its business makes that qualification necessary, except to the extent that the failure to be so qualified has not resulted in, and is not likely to result in, a material adverse change (a) in the business, operations, prospects,<sup>42</sup> or financial condition of the Company, or (b) in the ability of the Company Parties to consummate the transactions contemplated by this Agreement and the other Transaction Documents (a “**Material Adverse Change**”).<sup>43</sup>

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incorporation have been properly authorized and taken.) Substantiation of a mere incorporation representation may only require an inquiry with the appropriate Secretary of State’s office.

<sup>42</sup> Most sellers in an acquisition context will attempt to delete the word “prospects” when used in this context because of its undefined and somewhat amorphous forward-looking character.

It also bears noting that there are significant variations as to how forward looking the representation is. For example, some include ‘prospects’ in the list of things that there has been no material adverse change in. Others don’t talk about prospects, but still refer to events which “are reasonably likely” to have a material adverse effect on the business, etc; still others refer only to events which “have had” such an effect. From the Seller’s perspective, one of the potentially problematic aspects of the forward looking formulations is that they can, after the fact, result in triggering indemnification obligations of the Seller for events it neither knew about nor had reason to know about.

KLING & NUGENT, *supra* note 39, at § 11.04[9]. See Jonathon M. Grech, Comment: “*Opting Out*”: *Defining the Material Adverse Change Clause in a Volatile Economy*, 52 EMORY L.J. 1483, 1488-89 (2003) (regarding “prospects” generally in a material adverse change definition).

Most likely, courts will interpret forward-looking language to include the seller’s “prospects.” Conversely, without forward-looking language, the court may construe the MAC provision strictly so as not to include the future earnings potential or projections of the seller. Further, specifically disclaiming such forward-looking representations and warranties provides additional safety to the seller.

*Id.* at 1515-16.

<sup>43</sup> For information about certain drafting and litigation benefits and perils associated with material adverse change clauses, see, e.g., Kari K. Hall, *How Big is the MAC?: Material Adverse Change Clauses in Today’s Acquisition Environment*, 71 U. CIN. L. REV. 1061 (2003); Bradley D. Peters, *Material Adverse Change Clauses Following the Tyson Decision*, 3 TRANSACTIONS: TENN. J. BUS. L. 19 (2001); Grech, *supra* note 42.



2.02. Authority; Authorization; Legal Capacity. The Company has the corporate<sup>44</sup> power and authority (a) to own its properties and assets, (b) to conduct its business as presently conducted, and (c) to execute, deliver, perform and consummate the transactions contemplated by this Agreement and the other Transaction Documents. Each Shareholder has all necessary legal capacity to enter into this Agreement and the other Transaction Documents to which that Shareholder is a party.

2.03. Execution and Binding Effect. This Agreement has been, and on the Closing Date the other Transaction Documents will be, duly and validly executed and delivered by the Company Parties signing the Agreement and the other Transaction Documents. This Agreement constitutes (and, upon execution and delivery of the other Transaction Documents, each of them will constitute) the legal, valid and binding obligation of the Company Parties signing the Agreement and the other Transaction Documents, enforceable against those Company Parties in accordance with their respective terms.

2.04. No Breach, Default, Violation or Consent. The execution and delivery by the Company Parties of this Agreement and the other Transaction Documents to which any of them is a party and the performance and consummation by the Company Parties of the transactions contemplated by this Agreement and to the other Transaction Documents do not and will not:

- (a) violate the Company's charter or by-laws;
- (b) breach or result in a default (or an event which, with the giving of notice or the passage of time, or both, would constitute a default)

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<sup>44</sup> Acquirors sometimes omit or try to delete the adjective "corporate" in this type of representation. This omission or deletion generally is inappropriate. A corporation does not exist but for a statute allowing for its incorporation and the corporation's authority therefore derives from the corporation law under which it is organized. A possible exception exists for corporations operating in regulated environments where the applicable regulations circumscribe the authority of the corporation. Typically, regulatory compliance of this kind is handled through a "no violations or approvals" representation like that included as Section 2.04 of this Model Tennessee SPA. Regardless, the parties should carefully consider and negotiate the nature and extent of the authority to be covered by the representation, rather than relying without question on the inclusion or omission of the word "corporate." See generally ABA MODEL AGREEMENT, *supra* note 2, at 51-52 (requiring the usage of "corporate" in this context).

under, require any consent under, or give to others any right of termination, acceleration, suspension, revocation, cancellation or amendment of, any Company Agreement or Company Permit or any contract, agreement, instrument or document to which any Shareholder is a party or by which any Shareholder or its assets are bound;

(c) breach or otherwise violate any order, writ, judgment, injunction or decree issued by any federal or state court, administrative agency or commission or other governmental authority or instrumentality (each, a “**Governmental Entity**”) by which any Company Party or any of its respective assets is bound (each a “**Governmental Order**”);

(d) violate any law, rule, regulation, ordinance or code of any Governmental Entity (each a “**Governmental Rule**”); or

(e) require any consent, authorization, approval, exemption or other action by, or any filing, registration or qualification with, any person or entity (each a “**Person**”), it being understood that the Company Parties make no representation or warranty as to whether any filing is required under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended (the “**HSR Act**”),<sup>45</sup> or whether the Buyer’s status is such that the transfer of the Stock to the Buyer is exempt from the registration requirements of applicable federal or state securities laws.<sup>46</sup>

2.05. Ownership and Control. Schedule 2.05 correctly and completely sets forth: (a) the authorized capitalization of the Company; (b) the number of shares of each class of capital stock of the Company issued and outstanding; and (c) the names of the record and beneficial owners of each share of the Company’s capital stock and the number of shares of each class of the Company’s capital stock owned of record or beneficially by each of those Persons. The issued and outstanding shares of the Company’s capital stock have been duly authorized and validly issued and are fully paid and non-assessable. Except as disclosed on Schedule 2.05, there are no outstanding (x) options, warrants, agreements, or other rights for the acquisition of shares of the Company’s capital

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<sup>45</sup> See *supra* note 6.

<sup>46</sup> See *supra* note 10.

stock; (y) securities or other obligations of the Company which are convertible into shares of the Company's capital stock; or (z) sale agreements, shareholder agreements, pledges, proxies, voting trusts, powers of attorney, restrictions on transfer or other agreements or instruments that are binding on any of the Shareholders (exclusive of any agreement to which the Buyer is a party) and that relate to the ownership, voting or transfer of any shares of the Company's capital stock.

2.06. Subsidiaries. Except as disclosed on Schedule 2.06, the Company does not own any stock, partnership interest or other equity interest in any other Person.

2.07. Financial Statements. The Company has previously delivered to the Buyer true and complete copies of its: (a) audited balance sheets and statements of income, retained earnings and cash flows as of and for its fiscal years ended December 31, 2002, 2001, and 2000, including all applicable footnotes; and (b) unaudited interim balance sheets and statements of income, retained earnings and cash flows as of and for the nine-month period ended September 30, 2003 (the "**Current Financial Statements**" and, together with the items described in clause (a) above, the "**Financial Statements**"). The Financial Statements present fairly in all material respects the financial condition of the Company as at the end of the covered periods and the results of its operations and its cash flows for the covered periods. The Financial Statements were prepared in accordance with GAAP, applied on a consistent basis throughout the covered periods, subject, in the case of the Current Financial Statements, to year-end audit adjustments (which will not, in the aggregate, be material, except as disclosed on Schedule 2.07) and the lack of footnotes and other presentation items. To the best<sup>47</sup> of the Company Parties' knowledge,<sup>48</sup> except as and to the extent disclosed in the Current Financial

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<sup>47</sup> The adjective "best," as it is used here, may be objectionable to the Company Parties for at least two reasons, including the difficulty in ascertaining whether an aggregated group knowledge meets the standard and the uncertain meaning of the term "best." Typically, the ensuing discussion among the parties productively focuses on the person or group of people most likely nature to have the relevant knowledge and the nature and extent of the diligence required to be exercised by that person or those people. Accordingly, the issue often is resolved by defining knowledge in a manner that covers these matters to the mutual satisfaction of the parties. *See infra* note 48.

<sup>48</sup> Many parties to acquisition agreements now define the term "knowledge" in their agreements. *See* ABA MODEL AGREEMENT, *supra* note 2, at 20-21. For example, one recent stock purchase agreement includes the following definition of knowledge:

Statements or on Schedule 2.07, the Company has no liabilities of any kind, whether direct or indirect, fixed or contingent or otherwise, other than (x) executory obligations under Company Agreements that are not required to be set forth in the Current Financial Statements in accordance with GAAP and (y) liabilities incurred in the ordinary course of business since September 30, 2003 (the “**Financial Statement Date**”).<sup>49</sup>

2.08. Bank Accounts. Schedule 2.08 sets forth a correct and complete list of the names and locations of all banks, trust companies, savings and loan associations and other financial institutions at which the Company maintains accounts of any nature, the type and number of all listed accounts and the names of all persons authorized to draw on or make withdrawals from each account.

2.09. Tax Matters.<sup>50</sup> Except as otherwise disclosed on Schedule 2.09:

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“Knowledge” shall mean: (i) with respect to Sellers, the actual knowledge of the directors; and (ii) with respect to Buyer, the actual knowledge of Buyer personnel (other than attorneys) who conducted due diligence, in each case without imposing any obligation on such persons to conduct any investigation.

Stock Purchase Agreement by and among Sonic Media Corp. and the shareholders of Global Botanics Inc., dated as of Mar. 26, 2004, filed as Exhibit 2.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission by Sonic Media Corp. on April 9, 2004, at 4, *available at* [http://www.sec.gov/Archives/edgar/data/1175594/000114420404004547/v02571\\_2-1.htm](http://www.sec.gov/Archives/edgar/data/1175594/000114420404004547/v02571_2-1.htm) (last visited May 13, 2004). As indicated *supra* note 47, these definitions tend to focus on answering the questions (a) “knowledge of whom?” and (b) “based on what level of inquiry or diligence?”

<sup>49</sup> The Shareholders should check with the Company’s accountants to ensure that appropriate exceptions are taken. *See generally* ABA MODEL AGREEMENT, *supra* note 2, at 59-64 (regarding “financial statements” representations generally).

<sup>50</sup> The Shareholders should consult with the Company’s tax accountant, tax lawyer, or other tax preparation expert regarding the contents of this provision. *See generally* KLING & NUGENT, *supra* note 5, at § 11.04[13]. This tax representation is relatively simple in many respects. For example, the provision uses “taxes, interest, penalties, assessments and deficiencies” and “tax returns and reports” rather than more complex and comprehensive defined terms (typically, “Taxes” and “Tax Returns,” respectively) for the same purpose. *Id.* at 11-68 n.115; *see also* ABA MODEL AGREEMENT, *supra* note 2, at 29-30, 79-81.

(a) all tax returns and reports required to be filed by the Company have been properly prepared and filed;

(b) the Company has paid, or has made adequate reserves on its books for the payment of, all taxes, interest, penalties, assessments and deficiencies (i) shown to be due on those tax returns and reports, or (ii) claimed to be due by any Governmental Entity, or (iii) which the Company is required to withhold on behalf of any other Person;

(c) the reserves and provisions for taxes on the books of the Company are adequate for all open years and for its current fiscal period and, except in the case of reserves and provisions for taxes on interim financial statements, properly classify the Company's tax obligations as either current or deferred;

(d) the Company Parties have no knowledge of any proposed assessment of any additional taxes by any Governmental Entity or of any basis for any proposed tax assessment (whether or not reserved against);

(e) the federal income tax liabilities of the Company have been finally determined by the Internal Revenue Service (the "IRS"), or the time for audit has expired, for all fiscal periods ending on or prior to December 31, 2000;<sup>51</sup>

(f) the Company is not currently being audited for tax compliance by any Governmental Entity, and no audit for tax compliance is pending or, to the best of the Company Parties' knowledge, threatened;

(g) the Company has not made any tax elections that (i) were in effect in any past year for which the time for audit has not expired, (ii) are currently in effect, or (iii) will be in effect at any future time; and

(h) the Company has not given any waiver or extension of any period of limitation governing the time of assessment or collection of any tax.

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<sup>51</sup> This date is intended to refer to closed tax years for the Company. The general statute of limitations for tax claims is three years from the time the taxpayer files the related tax return, subject to certain exceptions, special rules and extension by agreement. *See* 26 U.S.C. § 6501 (2000).

2.10. Litigation. Except as disclosed on Schedule 2.10, there is no pending or, to the best of the Company Parties' knowledge, threatened investigation, action or proceeding against the Company by or before any Governmental Entity or arbitrator. Except as disclosed on Schedule 2.10, there is no pending or, to the best of the Company Parties' knowledge, threatened investigation, action or proceeding against any Shareholder by or before any Governmental Entity or arbitrator that, if determined adversely to that Shareholder, would materially<sup>52</sup> and adversely affect his, her, or its ability to consummate the transactions contemplated by this Agreement. Schedule 2.10 sets forth a correct and complete list of each investigation, action and proceeding described in the preceding sentences, the parties to the investigation, action or proceeding, the alleged basis for the investigation, action or proceeding, the relief sought in the investigation, action or proceeding and the current status of the investigation, action or proceeding.

2.11. Absence of Certain Changes and Events. Except as disclosed on Schedule 2.11, since the Financial Statement Date:

(a) the Company has not incurred any material obligation or liability except for normal trade obligations and accrued expenses incurred in the ordinary course of business;

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<sup>52</sup> A certain number of representations or warranties in an acquisition agreement are qualified by the adverb "materially" or the adjective "material." The concept of "materiality" limits the representation to matters of some significance. See BLACK'S LAW DICTIONARY 991 (7th ed. 1999) (defining "material" as "of such a nature that knowledge of the item would affect a person's decision-making process; significant; essential"); KUNEY, *supra* note 16, at 76 ("Materiality thresholds should be set at levels that sound appropriate alarms but filter out noise generated by immaterial claims."); *Basic v. Levinson*, 485 U.S. 224, 231 (1988) (finding that an omitted fact is "material" in the context of Rule 10b-5 claim "if there is a substantial likelihood that a reasonable shareholder would consider it important" or if there is "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available"); *Smith v. Tenn. Furniture Indus., Inc.*, 369 S.W.2d 721, 728 (Tenn. 1963) (citing Webster's definition of "material" as meaning "[o]f solid or weighty character, of consequence, important"). This same result also may be achieved by setting numerical or dollar-amount thresholds in appropriate provisions. See the text accompanying *infra* notes 53-55.

(b) no casualty, loss or damage in excess of \$[ ]<sup>53</sup> in the aggregate has occurred with respect to any of the Company's assets, whether or not the same is covered by insurance;

(c) the Company has not sold, transferred or otherwise disposed of any of its assets or any interest in any of its assets, or agreed to do any of the foregoing, except for sales of inventory in the ordinary course of business and except for dispositions of other assets which are not necessary to the business or operations of the Company (or which have been replaced) and which have a fair market value of not more than \$[ ]<sup>54</sup> in the aggregate;

(d) the Company has not written off as uncollectible any of its accounts receivable or written down the value of any of its assets, except in each case in the ordinary course of business and at a rate no greater than that in existence during the nine-month period ending on the Financial Statement Date;

(e) the Company has not waived or released any of its material rights with respect to its business or assets or permitted any of those rights to lapse;

(f) no executive officer or other individual who, in the reasonable judgment of the Company, was a key employee of the Company has left his or her employment with the Company;

(g) the Company has not granted, and is not committed to grant, any salary or wage increases to any of its employees;

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<sup>53</sup> Generally, this dollar amount is determined based on a percentage of the Company's total assets that the Buyer and the Shareholders agree represents a significant impairment of the Company's asset value – one that impacts the Buyer's valuation of the Company enough (as compared to that valuation as of the Financial Statement Date) to warrant at least an adjustment in the purchase price. *See* Hall, *supra* note 43, at 1087 (noting, with respect to material adverse change clauses, that “[c]ompanies can set threshold amounts or develop formulas for the court to apply to determine if the parties would have intended that the impact of a change be deemed material.”).

<sup>54</sup> Typically, the Buyer is not concerned about ordinary course sales of nonessential, qualitatively insignificant assets, so long as those assets also are quantitatively insignificant (*i.e.*, having a dollar value not in excess of a *de minimis* threshold amount). The omitted dollar value represents that *de minimis* threshold dollar amount. *See* Grech, *supra* note 42, at 1498 (noting, with respect to material adverse change clauses, that “[a]dverse changes that fall under the threshold value will not relieve the acquirer [sic] from its obligation to perform.”).

(h) the Company has not made, or committed to make, any capital expenditures in excess of \$[ ]<sup>55</sup> in the aggregate, exclusive of purchases of automobiles;

(i) there has been no payment, discharge or other satisfaction of any liabilities of the Company, whether direct or indirect, fixed or contingent or otherwise, other than the satisfaction, in the ordinary course of business, of liabilities reflected on the Current Financial Statements or incurred in the ordinary course of business since the Financial Statement Date;

(j) the Company has not declared or paid any dividend or other distribution in respect of any of its capital stock or agreed to declare or pay any dividend or distribution;

(k) the Company has not introduced any material change with respect to its business, including without limitation with respect to the products or services it sells, the areas in which its products or services are sold, its methods of manufacturing or distributing its products, its marketing techniques or its accounting methods; and

(l) no Material Adverse Change,<sup>56</sup> and no event that is likely to result in a Material Adverse Change, has occurred.

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<sup>55</sup> This dollar amount limits capital expenditures that may be made by the Company during the period following the Financial Statement Date to a level deemed acceptable to the Buyer. Both this dollar amount and any exceptions to the spending cap are negotiated on a case-by-case basis. See Hall, *supra* note 43, at 1087.

<sup>56</sup> Typically, Shareholders will resist a broad, catch-all representation or warranty with respect to there having been, or there being, a material adverse change.

In negotiating the MAC clause, the seller will typically prefer to have no MAC clause at all, so that the buyer accepts all the risk of possible business changes. However, if a MAC clause must be included, the seller will want to limit the outs for the buyer as much as possible in order to keep the buyer committed to the transaction and protect itself from the negative exposure a broken deal could create. In order to do this, the seller should try to limit the events that trigger the definition of materiality in the MAC clause.

Hall, *supra* note 43, at 1064.



2.12. Customers and Suppliers. Schedule 2.12 (a) sets forth a correct and complete list of the top 20 customers and top 20 suppliers of the Company during its fiscal year ended December 31, 2002, and during the nine months ending on the Financial Statement Date and (b) indicates with respect to each the name, address and dollar volume of business with the Company (including the primary categories, based on purchases or sales, of products bought or sold). The Company is not required to provide any material bonding or other financial security arrangements in connection with its transactions with any customer or supplier required to be disclosed on Schedule 2.12. Since the Financial Statement Date, no customer or supplier required to be disclosed on Schedule 2.12 has terminated its relationship with, or materially reduced its purchases from or sales to, the Company, and the Company Parties have no knowledge that any of those customers or suppliers intends to terminate its relationship with, or materially reduce its purchases from or sales to, the Company.

2.13. Constituent Documents; Governmental Rules; FDA Compliance.<sup>57</sup>

(a) The Company is in compliance with (i) its charter and by-laws and (ii) all Governmental Rules applicable to the Company, its business, or its assets, except in each case for any non-compliance disclosed in any schedule referenced in this Section 2.13 and any non-compliance that, individually or in the aggregate, has not resulted in, and is not likely to result in, a Material Adverse Change.

(b) Schedule 2.13(b) sets forth a list of the Company's 510(k) notifications and pre-market approval applications ("PMA's"). All listed 510(k) notifications, PMA's and related documentation are in substantial compliance with applicable requirements of the United States Food and Drug Administration ("FDA"). All of the Company's products, where required by applicable law, are being marketed under a valid 510(k) notification or PMA. All of the Company's

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<sup>57</sup> Specific representations relating to compliance with specialized regulations often are crafted in consultation with counsel expert in that specialized area. When regulatory counsel is unavailable, however, drafters frequently turn to applicable scholarship and practitioner literature for general information and recent transaction documents involving similarly situated regulated entities for drafting precedent. See, e.g., William M. Brown, *Grandfathering Can Seriously Damage Your Wealth: Due Diligence in Mergers and Acquisitions of Medical Device Companies*, 36 GONZ. L. REV. 315 (2000/2001) (regarding due diligence and successor liability in acquisitions of medical device manufacturers).

products in commercial distribution which are not marketed under a valid 510(k) notification or PMA also are listed on Schedule 2.13(b), together with a statement describing the reasons why those products are being marketed without notification or approval, as applicable. The Company has obtained and maintains all necessary regulatory approvals from applicable foreign regulatory agencies relating to all products distributed and sold by the Company. All products sold or marketed by the Company are listed with the FDA in accordance with 21 C.F.R. Section 807. The Company has filed with the FDA all required medical device reports for deaths, serious injuries and reportable malfunctions. Schedule 2.13(b) further identifies all internal audit reports (as required by 21 C.F.R. Section 820.20) conducted by the Company since December 31, 2001.

(c) Schedule 2.13(c) contains a correct and complete list of: (i) to the knowledge of the Company Parties, all products which have been recalled by the Company in the United States and outside the United States (whether voluntarily or otherwise) at any time since December 31, 2001; (ii) to the knowledge of the Company Parties, all proceedings in the United States and outside of the United States at any time since December 31, 2001, against the Company, the outcome of which dictated the withdrawal, detention, suspension, cessation of marketing, recall or seizure of any product or, the outcome of which dictated criminal or civil penalties or injunctive relief relating to any product; (iii) to the knowledge of the Company Parties, all proceedings at any time since December 31, 2001, the outcome of which dictated the closure or suspension of operations of any of the Company's facilities (or portions of those facilities) or, the outcome of which dictated criminal or civil penalties or injunctive relief relating to any of Company's facilities; and (iv) to the knowledge of the Company Parties, all FDA Forms 483 and all FDA warnings or FDA regulatory letters and notices of adverse findings since December 31, 2001, addressed to the Company relating to any product manufactured, sold or distributed by the Company. Except as set forth on Schedule 2.13(c), all manufacturing facilities operated by the Company are registered with the FDA in accordance with 21 C.F.R. Section 807.

(d) Schedule 2.13(d) sets forth a list of all written documents from any Person received since December 31, 2001, by the Company that relate to the Company's noncompliance with reporting, registration, labeling, good manufacturing practices, advertising and other requirements under the federal Food, Drug and Cosmetic Act, as amended. Except as so disclosed, the Company is operating in compliance with all applicable FDA rules, regulations and policies the noncompliance with which could result in a Material Adverse Change.

(e) Except as set forth on Schedule 2.13(e), to the knowledge of the Company Parties, there are no facts which are reasonably likely to cause or require: (i) the denial, withdrawal, recall or suspension of any product sold by the Company; (ii) a change in the marketing classification or labeling of any product sold by the Company; or (iii) a termination or suspension of marketing of any product sold by the Company.

2.14. Governmental Orders. Schedule 2.14 sets forth a correct and complete list of all Governmental Orders, together with the Governmental Entity who issued the same and the subject matter of those Governmental Orders. The Company is in compliance with all Governmental Orders, except for non-compliance that, individually or in the aggregate, has not resulted in, and is not likely to result in, any Material Adverse Change.

2.15. Company Permits. Schedule 2.15 sets forth a correct and complete list of all permits, licenses, franchises, certificates, authorizations, consents and approvals that have been obtained from or issued by any Governmental Entity and that are necessary for the ownership or operation of the Company or the ownership, operation, or use of its assets (collectively, the “**Company Permits**”), and indicates for each whether any consent from the issuing authority is required in connection with the consummation of the transactions contemplated by this Agreement. The Company Permits have been validly acquired, are in full force and effect, and represent all governmental permits, licenses, franchises, certificates, authorizations, consents, and approvals necessary under applicable Governmental Rules for the Company to carry on its business as now being conducted and to own, operate, or use its assets, except where the Company’s failure to obtain or maintain any Company Permit has not resulted in, and is not likely to result in, any Material Adverse Change. No violations have been recorded against any Company Permit, no citation, notice, or warning has been issued by any Governmental Entity with respect to any Company Permit, no investigation or hearing has been held by or before any Governmental Entity with respect to any Company Permit, the Company has not received any notice from any Governmental Entity that it intends to cancel, revoke, terminate, suspend, or not renew any Company Permit, and the Company Parties have no knowledge of any basis for any of the foregoing. The Company is in compliance with all Company Permits, except for noncompliance that, individually or in the aggregate, has not resulted in, and is not likely to result in, a Material Adverse Change.

2.16. Environmental Matters. Except as disclosed on Schedule 2.16.<sup>58</sup>

(a) no Hazardous Substances have been or are being generated, used, processed, treated, stored, released, transported, or disposed of by the Company, except in compliance with applicable Environmental Rules;

(b) to the best of the Company Parties' knowledge, no Person who has leased, occupied, or used any real property now or previously owned, leased, occupied, or used by the Company generated, used, processed, treated, stored, released, transported, or disposed of any Hazardous Substances on that property;

(c) to the best of the Company Parties' knowledge, no Hazardous Substances are present on or under any real property (including without limitation in any body of water located on or adjacent to any real property or any groundwater located under any real property) now or previously owned, leased, occupied, or used by the Company, or in any improvement located on that real property, in quantities or at levels which require reporting or remediation under any applicable Environmental Rule;

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<sup>58</sup> Most drafters welcome the assistance of an environmental lawyer in drafting this representation. Absent this counsel, however, transactional lawyers can look to a large and growing body of literature in determining and assessing the appropriate contents of an environmental compliance representation. *See, e.g.*, ABA MODEL AGREEMENT, *supra* note 2, at 108-13 (covering a number of important points regarding environmental representations); KLING & NUGENT, *supra* note 5, at § 11.04[11] (regarding environmental representations generally); Albert Bates, Jr. IV et al., *Asset Purchases, Successor Liability, and Insurance Coverage: Does the Tail Always Follow the Dog?*, 100 W. VA L. REV. 631 (1998); Charles P. Efflandt, *When the Tail Wags the Dog: Environmental Considerations and Strategies in Business Acquisitions, Sales and Merger Transactions*, 39 WASHBURN L.J. 28 (1999); Eva M. Fromm et al., *Environmental Law and Business in the 21st Century: Allocating Environmental Liabilities in Acquisitions*, 22 IOWA J. CORP. L. 429 (1997); Irma S. Russell, *Unreasonable Risk: Model Rule 1.6, Environmental Hazards, and Positive Law*, 55 WASH & LEE L. REV. 117, 182 n.165 (1998) (citing to various sources on the importance of environmental issues in business transactions); Ram Sundar & Bea Grossman, *The Importance of Due Diligence in Commercial Transactions: Avoiding CERCLA Liability*, 7 FORDHAM ENVTL. L.J. 351 (1996); Gray E. Taylor, *Environmental Contractual and Due Diligence Issues in Buying or Selling a Business: Some Border Crossing Thoughts*, 5 WIS. ENVTL. L.J. 173 (1998) (regarding environmental provisions in the United States and Canada); Colleen E. Healy & Mark S. Hacker, Comment: *The Importance of Identifying and Allocating Environmental Liabilities in the Sale or Purchase of Assets*, 10 VILL. ENVTL. L.J. 91 (1999).

(d) no underground storage tanks are located on any real property owned, leased, occupied, or used by the Company; and

(e) no event has occurred and no condition exists with respect to the Company or its business or assets which was caused by the act or omission of the Company or, to the best of the Company Parties' knowledge, any other Person and which has resulted in, or is likely to result in, any material liability, cost or expense under any applicable Environmental Rule to the Company or any other Person who owns or operates its business or assets, and the Company has not received any notice from any Governmental Entity or other Person of its intention to impose any of those liabilities, costs or expenses upon the Company or any Person.

(f) As used in this Section 2.16, the following terms have the following meanings:

“**Environmental Rule**” means any Governmental Rule in effect on or prior to the Closing Date that relates to Hazardous Substances, pollution, or protection of the environment, natural resources or public health or safety, including without limitation any Governmental Rule relating to the generation, use, processing, treatment, storage, release, transport, or disposal of Hazardous Substances and any common laws of nuisance, negligence, and strict liability relating to that Government Rule, together with all rules, regulations, and orders issued under that Governmental Rule, as any of them may have been amended through the Closing Date.

“**Hazardous Substance**” means any substance which constitutes, in whole or in part, a pollutant, contaminant, toxic or hazardous substance or waste under, or the generation, use, processing, treatment, storage, release, transport, or disposal of which is regulated by, any Governmental Rule.

#### 2.17. Real Property.

(a) Schedule 2.17(a) sets forth a correct and complete list of (i) all real property currently owned, leased, or used by the Company (collectively, the “**Real Property**”); (ii) all leases, subleases, and other material agreements or rights under which any Person has the right to occupy or use any real property owned by the Company; and (iii) all leases, subleases and other material agreements or rights under which the Company has the right to occupy or use any real property owned by others.

(b) Except as disclosed on Schedule 2.17(b), all buildings and other improvements located on the Real Property which are necessary or desirable to the conduct of the Company's business as currently conducted (including without limitation all water, sewer, gas, electrical, and HVAC systems servicing the Company's business) are in good operating condition.

(c) All buildings and other improvements located on the Real Property, and the use of the Real Property by the Company and all Persons claiming under the Company, comply in all material respects with all Governmental Rules relating to zoning and land use and with all easements, covenants and other restrictions applicable to the Real Property. To the best of the Company Parties' knowledge, Schedule 2.17(c) sets forth a correct and complete list of all zoning or building code variances and special permits the absence of which would cause the representation and warranty in the previous sentence to be untrue.

(d) The Real Property: (i) is adequately serviced by all utilities necessary for the conduct of the Company's business as currently conducted on the Real Property; (ii) has adequate means of ingress and egress, either directly or by means of perpetual easements or rights-of-way which run with the Real Property; (iii) has adequate parking that is sufficient to meet the needs of the Company's employees and business invitees and to comply with applicable Governmental Rules; and (iv) is not located in whole or in part within an area identified as a flood hazard area by any Governmental Entity.

#### 2.18. Personal Property.

(a) Schedule 2.18(a) sets forth a correct and complete list of all leases and other agreements (i) under which the Company leases any equipment, machinery, fixtures, tools, dies, patterns, vehicles, computer hardware or software, or furniture (collectively, the "**Equipment**") and (ii) that require payments by the Company in excess of \$[ ]<sup>59</sup> per year.

(b) Except as disclosed on Schedule 2.18(b), all Equipment owned or leased by the Company (other than Equipment that is not

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<sup>59</sup> This dollar amount reflects an understanding among the Buyer and the Shareholders as to the dollar amount of payments that make the Company's Equipment leases material. The threshold amount typically is determined after the Buyer has performed significant business diligence on the Company.

necessary or desirable to the conduct of the Company's business as currently conducted) is in good operating condition, is suitable for the purposes for which it is used, and constitutes all Equipment necessary to conduct the Company's business as currently conducted.

(c) Except as disclosed on Schedule 2.18(c), all raw material, work-in-process, and finished goods inventory of the Company (i) is in all material respects of a quantity and quality usable and saleable in the ordinary course of the business and (ii) except for items acquired or produced after the Financial Statement Date, is reflected on the Current Financial Statements at the lower of cost or market in accordance with GAAP applied on a consistent basis.

(d) Except as disclosed on Schedule 2.18(d), all accounts receivable of the Company: (i) represent amounts receivable for goods actually delivered or services actually provided (or in the case of non-trade receivables, represent amounts receivable in respect of other bona fide business transactions); (ii) are not subject to any material defenses, counterclaims or rights of setoff; (iii) have been billed and are generally due and payable within [30] days<sup>60</sup> after billing; and (iv) are fully collectible in the ordinary course of business, except, in the case of receivables arising prior to the Financial Statement Date, to the extent of the reserves set forth in the Current Financial Statements and, in the case of receivables arising after that date, to the extent of a reasonable allowance for bad debts.

(e) Schedule 2.18(e) sets forth the total amount of the Company's accounts receivable outstanding as of November 30, 2003, together with the aging of those receivables, from the date of billing, based on the following schedule: [0-30] days; [31-60] days; [61-90] days; and over [90] days.<sup>61</sup>

2.19. Intellectual Property. Schedule 2.19 sets forth a correct and complete list of (a) all patents, registered and unregistered trademarks, service marks, logos, domain names, corporate, and trade names, and registered and common law copyrights, and all applications which are owned by or licensed to the Company or are otherwise used by the Company in its business (together with all other

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<sup>60</sup> This 30-day period reflects the ordinary course billing cycle for the Company as ascertained from the Company's management.

<sup>61</sup> These time ranges derive from the ordinary course billing cycle for the Company as ascertained from the Company's management and reflected in subsection (d) of this Section 2.18.

proprietary information used by the Company in the conduct of its business, the “**Intellectual Property**”); (b) all licenses or other agreements under which any Person has the right to use any Intellectual Property owned by the Company; (c) all licenses or other agreements under which the Company has the right to use any Intellectual Property owned by others; (d) all consents that must be obtained, all filings that must be made, and all other actions that must be taken in respect of the Intellectual Property in connection with the consummation of the transactions contemplated by this Agreement, and (e) all corporate and fictitious names used by the Company in the past five years (including the corporate names of any businesses that have been acquired by the Company during that time period). The Company has the lawful right to use all of the Intellectual Property, and no use of any proprietary equipment, devices or processes developed by the Company or, to the best of the Company Parties’ knowledge, any other Intellectual Property infringes upon the lawful rights of any other Person. To the best of the Company Parties’ knowledge, no Person is using any Intellectual Property in a manner which infringes upon the lawful rights of the Company.

2.20. Title to Assets. Except as otherwise disclosed on Schedule 2.20: (a) the Company has (i) good and marketable fee simple title to all Real Property purported to be owned by it, (ii) good and marketable title to all other assets purported to be owned by it, and (iii) good leasehold title to all assets purported to be leased by it; and (b) the Shareholders have good and marketable title to the capital stock of the Company purported to be owned by them, in each case free and clear of all Liens. All scheduled Liens will be removed on or prior to the Closing Date, other than those marked as “**Permitted Liens**” on Schedule 2.20.

2.21. Pension Plans.<sup>62</sup> Schedule 2.21 sets forth a true, correct and complete list of all Pension Plans. Except as disclosed on Schedule 2.21:

(a) the IRS has issued favorable determination letters to the effect that each Pension Plan is qualified within the meaning of Section 401 of the Code and that each related trust is exempt under Section 501 of the Code, correct and complete copies of which have been delivered to the Buyer, and the

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<sup>62</sup> A practitioner with access to an employee benefits lawyer or other professional that is familiar with the Company’s plans and agreements is best advised to consult with that professional as to the appropriate scope and contents of this representation and the representation in Section 2.22 of this Tennessee Model SPA. *See generally* ABA MODEL AGREEMENT, *supra* note 2, at 82-92; KLING & NUGENT, *supra* note 5, at § 11.04[14].



Company Parties have no knowledge of any fact which may adversely affect the qualified status of any Pension Plan or related trust;

(b) each Pension Plan and each related trust has been established, maintained and administered in all material respects in compliance with ERISA, the Code, and all other applicable Governmental Rules;

(c) none of the transactions described in Section 406 of ERISA or Section 4975 of the Code, and none of the events described in Section 4043 of ERISA, have occurred with respect to any Pension Plan;

(d) neither the Company nor any ERISA Affiliate has contributed to, or is or has been under any obligation to contribute to, any Multiemployer Plan;

(e) the Company has delivered to the Buyer correct and complete copies of (i) the IRS Form 5500 most recently filed with respect to each Pension Plan; and (ii) the summary plan description for each Pension Plan;

(f) there are no actions, suits, investigations, or other proceedings pending or, to the best of the Company Parties' knowledge, threatened against any Pension Plan or related trust or any fiduciary thereof; and

(g) there are no outstanding Governmental Orders that name any Pension Plan or its fiduciaries or are directed to any Pension Plan or its fiduciaries or assets.

As used in this Section 2.21, the following terms have the following meanings:

“**Code**” means the Internal Revenue Code of 1986, and all rules, regulations and orders issued under that Code, as they may be amended.

“**ERISA**” means the Employee Retirement Income Security Act of 1974 and all rules, regulations and orders issued under that Act, as they may be amended.

“**ERISA Affiliate**” means any trade or business that, together with the Company, is treated as a single employer under Section 4001(b)(1) of ERISA or Sections 414(b), (c), (m), or (o) of the Code.

“**Multiemployer Plan**” means a “multiemployer plan,” as defined in Section 4001(a)(3) of ERISA.

“**Pension Plan**” means any “employee pension benefit plan,” as defined in Section 3(2) of ERISA, (i) that is maintained for past or present employees of the Company or any ERISA Affiliate or (ii) to which the Company or any ERISA Affiliate made, or was required to make, contributions within the preceding five years.

2.22. Welfare Plans. Schedule 2.22 sets forth a correct and complete list of all Welfare Plans. Except as disclosed on Schedule 2.22: (a) each Welfare Plan has been established, maintained, and administered in all material respects in compliance with ERISA, the Code, and all other applicable Governmental Rules, and (b) all payments that the Company is required to make in respect of any Welfare Plan on or prior to the date of this Agreement have been made. As used in this Section, “**Welfare Plan**” means any “employee welfare benefit plan” as defined in Section 3(l) of ERISA: (i) that is maintained for past or present employees of the Company or any ERISA Affiliate, or (ii) to which the Company or any ERISA Affiliate made, or was required to make, contributions within the preceding five years.

2.23. Personnel Matters.

(a) Schedule 2.23(a) sets forth a correct and complete list of: (i) all directors and executive officers of the Company; (ii) all other employees of or consultants to the Company whose annual compensation (including bonuses and commissions) during the Company’s fiscal year ended December 31, 2002, was \$[ ] or more; (iii) the current job title or relationship to the Company of each Person described in clauses (i) and (ii) above; (iv) the amount of compensation (including bonuses and commissions) paid to each Person during the Company’s fiscal year ended December 31, 2002, and what each of them is expected to receive in the Company’s current fiscal year; and (v) any employee benefits or perquisites available to any Person that are not generally available to employees of the Company.

(b) Except as disclosed on Schedule 2.23(b), the Company is not a party to any employment, consulting or similar agreement, written or oral, with any Person.

(c) Except as disclosed on Schedule 2.23(c): (i) no employees of the Company are represented by any labor union or similar organization; (ii) the Company is not party to any collective bargaining or similar agreement covering any of its employees; and (iii) to the Company Parties' knowledge, no labor union or similar organization or group of employees has made a demand for recognition, filed a petition seeking a representation proceeding or given the Company notice of any intention to hold an election of a collective bargaining representative at any time during the past three years.

(d) Except as disclosed on Schedule 2.23(d): (i) no strike, work stoppage or contract dispute involving any employees of the Company currently exists or, to the Company Parties' knowledge, is threatened; and (ii) no investigation, action or proceeding by or before any Governmental Entity which relates to allegedly unfair or discriminatory employment or labor practices or the violation of any Governmental Rule relating to employment or labor practices is pending or, to the best of the Company Parties' knowledge, threatened.

2.24. Insurance. Schedule 2.24 sets forth a correct and complete list of all insurance policies of which the Company is the owner, insured, loss payee or beneficiary (each, a "**Policy**") and indicates for each Policy any pending claims under that Policy (other than workers compensation claims, all of which are fully insured). Except as disclosed on Schedule 2.24: (a) the Company has not failed to give any notice or present any material claim under any Policy in a timely fashion or as otherwise required by the Policy; (b) the Company has paid in full all premiums under Policies that were due and payable on or prior to the date of this Agreement; (c) no Policy provides for retrospective or retroactive premium adjustments; (d) the Company has not received notice of any material increase in the premium under, cancellation or non-renewal of, or disallowance of any claim under any Policy; (e) the Company has not been refused any insurance, nor has its coverage been limited by any carrier; and (f) since December 31, 1997, the Company has maintained, or been the beneficiary of, general liability and product liability Policies reasonable, in both scope and amount, in light of the risks attendant to its business and that provide coverage comparable to coverage customarily maintained by others in similar lines of business, and these Policies have been "occurrence" Policies and not "claims made" Policies.

2.25. Indebtedness.

(a) Schedule 2.25(a) sets forth a correct and complete list of all agreements, documents, instruments, and securities that are currently in effect and that create, evidence, or secure any indebtedness of the Company (including capital leases but exclusive of trade payables, to the extent not evidenced by a note, and accrued expenses) or under which the Company has guaranteed any indebtedness or other obligations of any other Person (exclusive of endorsements of checks in the ordinary course of business).

(b) Schedule 2.25(b) sets forth a correct and complete list of all outstanding trade payables and accrued expenses more than [30] days overdue<sup>63</sup> and, with respect to any trade payables or accrued expenses which have not been paid due to a dispute with a vendor, identifies the nature of the dispute.

2.26. Other Material Company Agreements. Schedule 2.26 sets forth a correct and complete list of all leases, licenses, contracts and other agreements, written or oral, to which the Company is a party or by which the Company or any of its assets are bound (collectively, “**Company Agreements**”), other than: (a) Company Agreements listed on any of Schedule 2.17 through Schedule 2.25; (b) Company Agreements involving the payment by or to the Company, or creating any liability of the Company (whether direct or indirect, fixed or contingent), of less than \$[ ]<sup>64</sup> over the term of the Company Agreement (exclusive of Company Agreements, that require performance by the Company other than the payment of money or the delivery of goods); and (c) Company Agreements that are cancelable by the Company on [30]<sup>65</sup> days’ notice or less without any material liability to the Company.

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<sup>63</sup> The need for and nature of any disclosure of outstanding payables and accrued expenses is a matter of negotiation between the Shareholders and the Buyer. These negotiations may include a discussion as to the need for disclosure of accrued expenses that are not significantly overdue, based on ordinary course conduct in the Company’s business. This discussion may result in a period shorter (or, more typically, longer) than 30 days.

<sup>64</sup> This amount represents the dollar value of payments or liabilities that renders a Company Agreement immaterial to the Buyer. This dollar amount is negotiated among the parties, with the Buyer typically articulating a relatively low number and the Shareholders arguing for a higher value.

<sup>65</sup> Dollar-value thresholds are not the only means of delimiting the materiality or immateriality of a disclosure item. Agreements may be qualitatively, as well as quantitatively, unimportant to a target,

2.27. Status of Company Agreements. Each Company Agreement listed on any of Schedule 2.17 through Schedule 2.26 is in full force and effect and is enforceable against the Company (and, to the best of the Company Parties' knowledge, the other parties to each Company Agreement) in accordance with its terms. The Company is in compliance with each Company Agreement in all material respects. To the best of the Company Parties' knowledge, all other parties to the Company Agreements are in compliance in all material respects with the terms of the respective Company Agreement to which they are parties. Except as disclosed on Schedule 2.27, no consent of the other parties to the Company Agreements is required in connection with the consummation of the transactions contemplated by this Agreement.

2.28. Transactions with Affiliates. Except as disclosed on Schedule 2.28: (a) none of the customers, suppliers, distributors or sales representatives of the Company are Affiliates of the Company or of any of its officers, directors or shareholders; (b) none of the properties or assets of the Company are owned or used by or leased to any Affiliates of the Company or of any of its officers, directors or shareholders; (c) no Affiliate of the Company or of any of its officers, directors or shareholders is a party to any Company Agreement; and (d) no Affiliate of the Company or of any of its officers, directors or shareholders provides any legal, accounting or other services to the Company. As used in this Agreement, the term "**Affiliate**" means, with respect to any Person: (i) any director, officer, employee, shareholder, partner or principal of that Person; (ii) any other Person of which that Person is a director, officer, employee, shareholder, partner or principal; (iii) any Person who directly or indirectly controls or is controlled by, or is under common control with, that Person; and (iv) with respect to any Person described above who is a natural person, any spouse and any relative (by blood, adoption or marriage) within the third degree of consanguinity of the Person, and the term "**control**" shall mean, with respect to any Person, the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a Person, whether through ownership of voting securities, by contract or otherwise.

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and clause 2.26(c) includes a description of Company Agreements that are immaterial on this combined basis. One of the authors of this Model Tennessee SPA refers to these immaterial agreements as "disposable contracts." The determination of the appropriate qualitative and quantitative limits for immateriality are, again, the subject of negotiation among the parties. *See supra* note 63.

2.29. Brokers. Except for [name of investment banker], the Company Parties have not employed or retained, and have no liability to, any broker, agent or finder on account of this Agreement or any of the other Transaction Documents or the transactions contemplated by this Agreement or the other Transaction Documents. The Shareholders will be solely liable for all amounts payable to [name of investment banker].

2.30. Delivery of Documents; Accurate Disclosure. The Company has previously delivered to the Buyer correct and complete copies of each Company Agreement listed on Schedule 2.17 through Schedule 2.26 and of each additional agreement, document, and instrument that the Buyer (or its accountants or attorneys) has requested in writing. None of the representations and warranties of the Company set forth in this Agreement (a) is false in any material respect, (b) contains any untrue statement of a material fact or (c) omits any statement of material fact necessary to make the statements made in this Agreement not misleading.<sup>66</sup>

2.31 Disclaimer of Other Representations and Warranties; Disclosure.

(a) The Company Parties do not make, and have not made, any representations or warranties relating to the Company or its business or otherwise in connection with the transactions contemplated by this Agreement other than those expressly set forth in this Article II. Without limiting the generality of the foregoing, the Company Parties have not made, and shall not be deemed to have made, any representations or warranties in the Confidential Information Memorandum relating to the business of the Company prepared by [name of investment banker] on behalf of the Company Parties and supplied to the Buyer prior to the date of this Agreement (the “**Confidential Information Memorandum**”) or in any presentation of the business of the Company in connection with the transactions contemplated by this Agreement, and no statement contained in the Confidential Information Memorandum or made in any

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<sup>66</sup> For a discussion of the reasoning behind inclusion of this representation, see KLING & NUGENT, *supra* note 5, at § 11.04[16]. Many sellers in acquisitions will insist that this representation also be given by the acquiror, even where the acquiror’s representations and warranties are limited in scope and content. *See, e.g.*, ABA MODEL AGREEMENT, *supra* note 2, at 134-35; Hamilton & Heminway, *supra* note 16, at 237 n.57.

presentation shall be deemed a representation or warranty under this Agreement or otherwise. It is understood that any cost estimates, projections or other predictions, offering materials or presentations, including without limitation the Confidential Information Memorandum, are not, and shall not be deemed to be or to include, representations or warranties of the Company Parties. No Person has been authorized by the Company Parties or the Company to make any representation or warranty relating to the Company, its business or otherwise in connection with the transactions contemplated by this Agreement.

(b) Notwithstanding anything to the contrary contained in this Agreement or in any of the schedules referenced in this Article II, any information disclosed on one schedule shall be deemed to be disclosed on any other schedules so long as the Buyer can reasonably determine from the disclosure that the disclosed information is responsive to the representations and warranties to which the other schedule relates.<sup>67</sup>

### ARTICLE III REPRESENTATIONS AND WARRANTIES OF THE BUYER<sup>68</sup>

The Buyer represents and warrants to the Company Parties as follows:

3.01. Organization. The Buyer is a corporation duly organized, validly existing and in good standing under the laws of the State of Tennessee.

3.02. Authority and Authorization. The Buyer has the corporate power and authority (a) to own its properties and assets, (b) to conduct its business as presently conducted, and (c) to execute, deliver, perform and consummate the transactions contemplated by this Agreement and the other Transaction Documents.

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<sup>67</sup> The inclusion of this representation may be a matter of debate among the parties to an acquisition agreement. *See id.* at 225 n.37; ABA MODEL AGREEMENT, *supra* note 2, at 224-25.

<sup>68</sup> A number of representations included in Article III of this Model Tennessee SPA raise issues identical or similar to those raised by the authors in connection with the Company Parties' representations included in Article II. These matters are not separately referenced in this Article III. Additional Buyer representations and warranties may relate to Buyer's financial condition, ability to obtain financing or solvency. The representations and warranties of the Buyer set forth in this Model Tennessee SPA are somewhat "bare bones" and do not (but certainly could) include statements regarding the Buyer's financial status (e.g., its solvency or its ability to pay or finance the purchase price).

3.03. Execution and Binding Effect. This Agreement has been, and on the Closing Date the other Transaction Documents will be, duly and validly executed and delivered by the Buyer. This Agreement constitutes (and upon execution and delivery of the other Transaction Documents, each of them will constitute) the legal, valid and binding obligation of the Buyer, enforceable against the Buyer in accordance with their respective terms.

3.04. No Breach, Default, Violation or Consent. The execution and delivery by the Buyer of this Agreement and the other Transaction Documents and the consummation by the Buyer of the transactions contemplated by this Agreement and the other Transaction Documents do not and will not:

- (a) violate the Buyer's charter or by-laws;
- (b) breach or result in a default (or an event which, with the giving of notice or the passage of time, or both, would constitute a default) under, require any consent under, or give to others any rights of termination, acceleration, suspension, revocation, cancellation or amendment of, any contract, agreement, instrument or document to which the Buyer is a party or by which the Buyer or any of its properties or assets is bound;
- (c) breach or otherwise violate any order, writ, judgment, injunction or other decree issued by any Governmental Entity by which the Buyer or any of its properties or assets is bound;
- (d) violate any Governmental Rule; or
- (e) require any consent, authorization, approval, exemption or other action by, or any filing, registration, or qualification with, any Person, it being understood that the Buyer makes no representation or warranty as to whether the transfer of the Stock to the Buyer is exempt from the registration requirements of applicable federal or securities laws.

3.05. Brokers. The Buyer has not employed or retained, and has no liability to, any broker, agent or finder on account of this Agreement or any of the other Transaction Documents or the transactions contemplated by this Agreement or the other Transaction Documents.



3.06. Investment.

(a) The Buyer is acquiring the Stock for its own account for investment, without a view to, or for resale in connection with, the distribution of the Stock in violation of federal or state securities laws and with no present intention of distributing or reselling any part of the Stock. The Buyer will not distribute or otherwise dispose of the Stock in violation of the Securities Act of 1933, as amended (the “**Securities Act**”).

(b) The Buyer understands that the Stock has not been registered under the Securities Act or the securities laws of any state and must be held by the Buyer indefinitely unless subsequently registered under the Securities Act and any applicable state securities laws or unless an exemption from registration becomes or is available.<sup>69</sup>

ARTICLE IV  
TRANSACTIONS PRIOR TO CLOSING

4.01. Conduct of Business Prior to Closing. At all times prior to the Closing Date, the Company shall:

(a) operate its business only in the ordinary course and consistent with past practice;

(b) use its commercially reasonable efforts to preserve its business organization intact, to keep available to the Buyer the services of its present officers and employees and to preserve for the Buyer the goodwill of customers, suppliers and others having business relations with the Company;

(c) maintain its equipment and machinery in good repair and operating condition, ordinary wear and tear excepted;

(d) maintain in full force and effect all Company Permits and Policies;

(e) not enter into any contract or commitment, except a contract or commitment that is made in the ordinary course of business, the terms of

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<sup>69</sup> See *supra* notes 7 & 8 and accompanying text.

which are consistent with past practice and reasonable in light of then current conditions;

(f) not terminate, cause the termination of, amend, renew or extend any Company Agreement, unless, in each case, that action is in the best interest of the Company;

(g) not waive or release any of its material rights or permit any of its material rights to lapse;

(h) not sell, transfer or otherwise dispose of any of its assets or any interest in its assets or agree to do any of the foregoing, except that the Company may sell inventory in the ordinary course of business;

(i) not incur, make, assume or suffer to exist any Lien, tenancy or other matter affecting title to any of its assets, except Liens for taxes not yet due and payable;

(j) not make, change or revoke any tax election or make any agreement or settlement with any taxing authority;

(k) not merge or consolidate the Company with or into any other entity or agree to merge or consolidate the Company with or into any other entity;

(l) not incur any indebtedness other than trade payables incurred in the ordinary course of business and not guarantee any indebtedness or other obligations of any other Person;

(m) not grant or commit itself to grant any salary or wage increases to any of its employees and not pay bonuses, except in a manner consistent with past practice;

(n) not make or commit itself to make any capital expenditures in excess of \$[ ];<sup>70</sup>

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<sup>70</sup> Typically, acquirors will limit capital expenditures to be made between signing and closing to a specific dollar amount or specific projects. The dollar value of any cap on, and the nature of any permitted, capital expenditures is negotiated among the Shareholders and the Buyer. *See supra* note 55.

(o) not issue or sell any of its capital stock or other securities, not declare or pay any dividends or other distributions in respect of any of its capital stock and not agree to do any of the foregoing;

(p) comply with applicable Governmental Rules in all material respects;

(q) take no action, and use its commercially reasonable efforts to prevent the occurrence of any event or the existence of any condition, that would result in any of the Company Parties' representations and warranties in this Agreement not being true and correct; and

(r) promptly inform the Buyer of the occurrence of any event or the existence of any condition which constitutes or, with the giving of notice or the passage of time, or both, is likely to constitute, a Material Adverse Change.

4.02. Conduct of the Shareholders Prior to Closing. At all times prior to the Closing Date, the Shareholders shall:

(a) not sell, transfer or otherwise dispose of any of the Stock or any interest in the Stock and not agree to do any of the foregoing;

(b) not accept any dividend or other distribution in respect of any of the Stock;

(c) not incur, make, assume or suffer to exist any Lien or other matter affecting title<sup>71</sup> to any of the Stock;

(d) not enter into any shareholder agreements, voting trusts, restrictions on transfer or other agreements or instruments that would be binding on the Buyer as the owner of the Stock; and

(e) take no action, and use their best efforts to prevent the occurrence of any event or the existence of any condition, that would result in

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<sup>71</sup> See *supra* note 18 and accompanying text.

any of the Company Parties' representations and warranties in this Agreement not being true and correct.

4.03. Satisfaction of Certain Obligations. On or prior to the Closing Date, the Company shall have paid or otherwise satisfied: (a) all taxes owed by the Company which are due and payable on or prior to the Closing Date; (b) all amounts accrued under the Company's executive annual incentive compensation plan; and (c) all fees and expenses incurred by the Company in connection with any of the Transaction Documents or the transactions contemplated by the Transaction Documents. In addition, all agreements between the Company and any of its current or former shareholders or any Affiliates of those shareholders shall have been terminated, and the Company shall have no further liability or obligation under any of those agreements.

4.04. Access to Information. At all times prior to the Closing Date, the Company shall furnish to the Buyer and its employees, counsel, accountants and other agents and consultants: (a) full access during normal business hours to its properties, books and records, and personnel; and (b) any information as any of them reasonably may request.

4.05. Best Efforts. The parties agree to use commercially reasonable best efforts to take or cause to be taken any action and to do or cause to be done anything necessary or advisable, or reasonably requested by the other party, in order to consummate the transactions contemplated by this Agreement and the other Transaction Documents. Without limiting the generality of the foregoing, the parties agree to take all commercially reasonable actions necessary in order to obtain any consent or approval of any third party, including without limitation any Governmental Entity, that is required in connection with this Agreement or the other Transaction Documents or any of the transactions contemplated by this Agreement or by the other Transaction Documents.

ARTICLE V  
CLOSING AND CLOSING CONDITIONS

5.01. Closing.<sup>72</sup> The closing of the transactions contemplated by this Agreement (the “**Closing**”) shall take place at 10:00 a.m., local time, on January 16, 2004,<sup>73</sup> at the offices of [**Law Firm, Address, City, State, Zip**], or at another time or place, or on another date not later than [**date**], as the parties may mutually agree. The date on and time at which the Closing occurs is referred to in this Agreement as the “**Closing Date**.”

5.02. Conditions Precedent to Obligations of the Buyer. The obligations of the Buyer under this Agreement to proceed with the Closing shall be subject to the satisfaction by the Company Parties on or prior to the Closing Date of each of the following conditions precedent:

(a) Accuracy of Representations and Warranties. The representations and warranties of the Company Parties set forth in this Agreement shall be true and correct<sup>74</sup> on and as of the Closing Date with the same force and effect as though made on and as of that date.

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<sup>72</sup> Provisions like those found in Section 5.01 of this Model Tennessee SPA frequently are included in Article I or Article II of an acquisition agreement (together with other key terms of the overall transaction) and not (whether with or apart from the closing conditions) near the end of the agreement. *See* ABA MODEL AGREEMENT, *supra* note 2, at 34-35 (sharing an analogous provision in Section 2.3 of Article 2 of an exemplar stock purchase agreement); KUNEY, *supra* note 16, at 25 (citing closing provisions as “core substantive provisions” that precede the representations and warranties, among other things, in an overall agreement outline); *id.* at 164 (showing an analogous provision in Section 2.2 of Article 2 of an exemplar asset purchase agreement). The authors have determined to retain the provision here in Article V, however, since the provision relates to the closing (and, therefore, the content of the remainder of Article V).

<sup>73</sup> This date allows for, among other things, the filing of an appropriate premerger notification and the expiration of the attendant waiting period under the HSR Act. *See* 15 U.S.C. § 18a(b) (2000) (providing that the minimum statutory waiting period for a stock purchase transaction of this kind is 30 days, subject to early termination by the Federal Trade Commission and the Assistant Attorney General in charge of the Antitrust Division of the Department of Justice); AXINN ET AL., *supra* note 6, at § 1.03[2][a].

<sup>74</sup> By making this condition absolute (i.e., unqualified as to materiality), the drafters have avoided the problem of “double materiality” – a problem that arises when both a representation and the related bring-down condition to closing include materiality caveats.

If, representing the purchaser, you have acceded to a provision in the conditions

(b) Performance and Compliance. The Company Parties shall have performed or complied in all material respects<sup>75</sup> with each covenant and agreement to be performed or complied with by them under this Agreement on or prior to the Closing Date.

(c) Consents and Approvals. The Company Parties shall have obtained or made each consent, authorization, approval, exemption, filing, registration or qualification, required to be obtained or made by any of them in connection with the execution, delivery and performance of this Agreement and the other Transaction Documents and the consummation of the transactions contemplated by this Agreement and the other Transaction Documents.

(d) Litigation. There shall be no pending or threatened action by or before any Governmental Entity or arbitrator (i) seeking to restrain, prohibit or invalidate any of the transactions contemplated by this Agreement or any of the other Transaction Documents or (ii) seeking monetary relief against the Buyer

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article limiting the purchaser's termination right to misrepresentations having a material adverse effect upon the seller, while at the same time in the representations article you have permitted the seller numerous materiality caveats, then you run the risk of double materiality – *i.e.*, the aggregate total of omitted information which does *not* constitute misrepresentations can be quite large without acting as a partial trigger to the condition.

FREUND, *supra* note 20, at 245. See ABA MODEL AGREEMENT, *supra* note 2, at 158-60. Under these circumstances,

[a] Buyer might argue that the “in all material respects” language should be deleted from the bringdown. After all, the representation already is limited to material breaches of material agreements. Why, the Buyer might ask, should it not be able to refuse to close if the representation was false in *any* respect? The Seller would most likely argue that the qualification in the bringdown is there for dealing with other representations which do not themselves have materiality limitations. This use of double materiality appears quite often, especially in public company deals, and most Buyers appear to accept it.

KLING & NUGENT, *supra* note 5, at § 11.03[3].

<sup>75</sup> The use of a materiality qualifier here should be evaluated to ensure that “double materiality” issues have been avoided or are tolerable to the Buyer. See *supra* note 74 (regarding “double materiality”).

by reason of the consummation of those transactions, and there shall not be in effect any order, writ, judgment, injunction or decree issued by any Governmental Entity by which the Buyer or any of its properties or assets is bound that has that effect.

(e) Material Adverse Change. No event shall have occurred and no condition shall exist that constitutes or, with the giving of notice or the passage of time or both, is likely to constitute a Material Adverse Change.

(f) Officers Certificate. The Company shall have delivered to the Buyer a certificate of its President, dated the Closing Date and certifying that each of the conditions specified in subsections (a), (b), (c), (d)(i) and (e) above have been met.

(g) Secretary's Certificate. The Company shall have delivered to the Buyer a certificate of its Secretary, dated the Closing Date and certifying: (i) that correct and complete copies of the Company's charter and by-laws are attached to the certificate; (ii) that correct and complete copies of each resolution of the Company's board of directors approving this Agreement and the other Transaction Documents to which the Company is a party and authorizing the execution of this Agreement and those other Transaction Documents and the consummation of the transactions contemplated by this Agreement and those other Transaction Documents are attached to the certificate; and (iii) the incumbency and signatures of the officers of the Company authorized to execute and deliver, on behalf of the Company, this Agreement and the other Transaction Documents to which the Company is a party.

(h) Opinion of Counsel. The Company Parties shall have delivered to the Buyer and its lenders an opinion of their counsel dated the Closing Date and in form and substance reasonably satisfactory to the Buyer and its lenders and their respective counsel.<sup>76</sup>

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<sup>76</sup> When at all possible, the parties should negotiate the form – even the actual contents – of closing opinions in advance of the signing of the acquisition agreement in order to avoid confrontation among the lawyers about the nature and extent of those opinions at a time when other conditions to closing have been or soon will be satisfied. A form of opinion may be scripted out in the acquisition agreement or may be attached to the agreement as an exhibit. *See, e.g.*, ABA MODEL AGREEMENT, *supra* note 2, at 169-70 (showing and describing a condition that references a form of a closing opinion as an exhibit). No lawyer gives a legal opinion lightly (as they are legal liability documents for the lawyer and her firm), and yet no lawyer wants to be the one holding up her client's transaction. *See* KUNEY, *supra* note 16, at 31 (making a similar point as to information schedules). The contents of

(i) Other Transaction Documents. The Company, the Shareholders and any other required parties (other than the Buyer) shall have executed and delivered to the Buyer the Escrow Agreement and any other documents and instruments, in form and substance satisfactory to the Buyer and its counsel, that shall be necessary or desirable in order to consummate the transactions contemplated by this Agreement, each dated the Closing Date (together with this Agreement and any agreements listed in Section 5.03(h), the “**Transaction Documents**”).<sup>77</sup>

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an appropriate legal opinion in the acquisition context generally focus on transaction-related legal issues.

Opinion recipients request closing opinions because they want assurance that the transaction is what they expect it to be from a legal standpoint. They want company counsel to tell them that the company is indeed a corporation and, to the extent applicable, that the stock they are buying has been validly issued, the agreement they are entering into and note they are receiving are enforceable obligations of the company, and required filings have been made and approvals obtained. They also want to be advised that in entering into the transaction the company is not violating any laws, material contracts to which it is a party, or court orders to which it is subject and is not the subject of any pending or threatened legal proceedings that would adversely affect the transaction or the company’s business.

Donald W. Glazer, *Closing Opinions for the Non-Specialist*, in DONALD W. GLAZER, ET AL., LEGAL OPINION PRACTICE 128 (2000).

Typical opinions include due organization and existence, corporate power to conduct its business and enter into and consummate the acquisition agreement, due authorization and enforceability of the acquisition agreement, execution and performance of the acquisition agreement not violating law, charter and bylaws, injunctions and material agreements or required governmental consents or approvals.

Lou R. Kling et al., *Summary of Acquisition Agreements*, 51 U. MIAMI L. REV. 779, 803 (1997). See Leslie L. Gardner, Note: *Attorney Liability to Third Parties for Corporate Opinion Letters*, 64 B.U. L. REV. 415, 418-19 (1984) (“Although opinion letters vary from transaction to transaction, they commonly provide an opinion as to one or more of the following issues: corporate status, stock, corporate power and action, contractual remedies, and the absence of conflicts.”). For a brief, general discussion regarding the role of opinions of counsel in business contracts, see KUNEY, *supra* note 16, at 143-45.

<sup>77</sup> Other agreements may be added to this list, as needed.



(j) Stock Certificates. The Shareholders shall have delivered to the Buyer the certificates evidencing the Stock, duly endorsed for transfer in blank.

5.03. Conditions Precedent to Obligations of the Company Parties. The obligations of the Company Parties under this Agreement to proceed with the Closing shall be subject to the satisfaction by the Buyer on or prior to the Closing Date of each of the following conditions precedent:

(a) Accuracy of Representations and Warranties. The representations and warranties of the Buyer set forth in this Agreement shall be true and correct<sup>78</sup> on and as of the Closing Date with the same force and effect as though made on and as of that date.

(b) Performance and Compliance. The Buyer shall have performed or complied in all material respects<sup>79</sup> with each covenant and agreement to be performed or complied with by it under this Agreement on or prior to the Closing Date.

(c) Consents and Approvals. The Buyer shall have obtained or made each consent, authorization, approval, exemption, filing, registration or qualification required to be obtained or made by it in connection with the execution, delivery and performance of this Agreement and the other Transaction Documents and the consummation of the transactions contemplated by this Agreement and the other Transaction Documents.

(d) Litigation. There shall be no pending or threatened action by or before any Governmental Entity or arbitrator (i) seeking to restrain, prohibit or invalidate any of the transactions contemplated by this Agreement or any of the other Transaction Documents or (ii) seeking monetary relief against any Company Party by reason of the consummation of those transactions, and there shall not be in effect any Governmental Order that has that effect.

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<sup>78</sup> See *supra* note 74 (regarding “double materiality”).

<sup>79</sup> The use of a materiality qualifier here should be evaluated to ensure that “double materiality” issues have been avoided or are tolerable to the Shareholders. See *supra* note 74 (regarding “double materiality”).

(e)      Officer's Certificate. The Buyer shall have delivered to the Company and the Shareholders a certificate of its President, dated the Closing Date and certifying that each of the conditions specified in subsections (a), (b), (c) and (d)(i) above have been met.

(f)      Secretary's Certificate. The Buyer shall have delivered to the Company Parties a certificate of its Secretary, dated the Closing Date and certifying: (i) that correct and complete copies of the Buyer's charter and by-laws are attached to the certificate; (ii) that correct and complete copies of each resolution of the Buyer's board of directors approving this Agreement and the other Transaction Documents to which the Buyer is a party and authorizing the execution of this Agreement and those other Transaction Documents and the consummation of the transactions contemplated by this Agreement and those other Transaction Documents are attached to the certificate; and (iii) the incumbency and signatures of the officers of the Buyer authorized to execute and deliver, on behalf of the Buyer, this Agreement and the other Transaction Documents to which the Buyer is a party.

(g)      Opinion of Counsel. The Buyer shall have delivered to the Company Parties an opinion of the Buyer's counsel dated the Closing Date and in form and substance reasonably satisfactory to the Company Parties and their counsel.

(h)      Other Transaction Documents. The Buyer and any other required parties (other than the Company Parties) shall have executed and delivered to the Company Parties the Escrow Agreement and any other documents and instruments, in form and substance satisfactory to the Company and its counsel, that shall be necessary or desirable in order to consummate the transactions contemplated by this Agreement, each dated the Closing Date.<sup>80</sup>

(i)      Purchase Price. The Buyer shall have delivered the Escrow Fund to the Escrow Agent and the remainder of the Closing Purchase Price to the Shareholders.

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<sup>80</sup> Other agreements may be added to this list, as needed.

ARTICLE VI  
NON-COMPETITION AND NON-SOLICITATION<sup>81</sup>

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<sup>81</sup> Courts generally enforce covenants not to compete entered into in connection with the sale of a business more willingly than they enforce noncompetition covenants entered into in, *e.g.*, employment arrangements. *See Alexander & Alexander, Inc. v. Danahy*, 488 N.E.2d 22, 28 (Mass. App. Ct. 1986) (“ . . . there are considerations which dictate that noncompetition covenants arising out of the sale of a business be enforced more liberally than such covenants arising out of an employer-employee relationship.”).

Courts are less likely to enforce restrictive covenants in employment contracts because an employee usually has little, if any, bargaining power. On the other hand, because of the presumed equality of bargaining power between a buyer and a seller of a business, and because the buyer is paying for the “goodwill” associated with the seller's business, which goodwill is often related to the seller personally, courts are more likely to enforce restrictive covenants incident to the sale of a business.

John W. Bowers, et al., *Covenants Not to Compete: Their Use and Enforcement in Indiana*, 31 VAL. U. L. REV. 65, 82 (1996). *See* ABA MODEL AGREEMENT, *supra* note 2, at 285. A recent article notes the relative state of the law of noncompete provisions in Georgia, which is representative of that in other jurisdictions.

[N]oncompete provisions . . . commonly appear in agreements relating to the sale of a business. In such cases, the seller promises not to compete with the buyer of the business after the sale. Traditionally, the Georgia courts have willingly enforced broad restraints if they were ancillary to the sale of a business. With restrictions ancillary to the sale of a business, the courts will allow the restriction to be effective for a significantly longer duration than if the restriction is in an employment agreement. More importantly, the court, in effect, will modify or “blue pencil” a noncompete agreement ancillary to the sale of a business so that it is reasonable and enforceable. As will be seen below, Georgia courts will not “blue pencil” restraints in employment agreements.

Steven E. Harbour, *Restrictions on Post-Employment Competition by an Executive Under Georgia Law*, 54 MERCER L. REV. 1133, 1138 (2003). *See* John Dwight Ingram, *Covenants Not to Compete*, 36 AKRON L. REV. 49, 49 n.2 (2002) (“Covenants in such situations are more readily enforced by the courts because buyer and seller, or former partners, usually have equal bargaining power, and the ‘good will’ Compete of the business is an important and valued asset.”); Jordan Leibman & Richard Nathan, *The Enforceability of Post-Employment Noncompetition Agreements Formed After At-Will Employment Has Commenced: The “Afterthought” Agreement*, 60 S. CAL. L. REV. 1465, 1577 (1987) (“In any event, in the realm of sales of those businesses where noncompetition agreements are of some importance, it is clear that absent the enforceability of those agreements, fewer sales of businesses would be consummated.”). Under Tennessee law, reasonable (as to both time and geographical territory), fair noncompete covenants entered into in connection with the sale of a business typically are enforceable.

6.01. Non-Competition and Non-Solicitation.

(a) During the period commencing with the date of this Agreement and ending on the fifth anniversary of the Closing Date, the Shareholders shall not, and shall cause their respective Affiliates<sup>82</sup> not to, directly or indirectly, engage in, own, be employed by, consult with or otherwise render services to any Person who is engaged in any Competing Business; provided, however, that the ownership of an equity interest of not more than 2% in a publicly traded entity that is engaged in a Competing Business, without more, shall not constitute a violation of this covenant.

(b) During the period commencing with the date of this Agreement and ending on the fifth anniversary of the Closing Date, the Shareholders shall not, and shall cause their respective Affiliates not to, directly or indirectly: (i) solicit the trade of, or trade with, any customer or supplier of the Company or any of its Affiliates such that the customer or supplier of the Company or Affiliate

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Generally speaking, “a covenant which is incidental to the sale and transfer of a trade or business, and which purports to bind the seller not to engage in the same business in competition with the purchaser, is lawful and enforceable”, . . . provided such covenants are reasonable and go no further than affording a fair protection to the buyer.

Greene County Tire & Supply, Inc. v. Spurlin, 338 S.W.2d 597, 599-600 (Tenn. 1960). See Hogan v. Coyne Int’l Enters. Corp., 996 S.W.2d 195, 204 (Tenn. App. 1998) (noting that “such covenants are enforceable ‘if they are reasonable under the particular circumstances’” and describing the components and application of this reasonableness standard); Butts v. Birdwell, 503 S.W.2d 930, 937 (Tenn. App. 1973) (assessing the reasonableness, in terms of time and territory, of a noncompete agreement and concluding that it “is not unreasonable and is fairly enforceable in equity.”). For an interesting discussion of the historical background of covenants not to compete in and outside Tennessee, see Michael L. Agee, Comment: *Covenants Not to Compete in Tennessee Employment Contracts: Almost Everything You Wanted to Know But Were Afraid to Ask*, 55 TENN. L. REV. 341 (1988). For additional general information about covenants not to compete, see KUNEY, *supra* note 16, at 123.

<sup>82</sup> Depending on the circumstances, it may be appropriate to restrict the senior management of the Company from engaging in a competitive business after closing. Where the manager is also a selling shareholder, this type of noncompete provision may be seen by a court as “a hybrid, meaning that it ha[s] characteristics of a covenant incident to the sale of a business as well as an employer-employee covenant not to compete.” Suggs v. Glenn, C.A. No. 837, 1989 Tenn. App. LEXIS 37, at \*7 (Tenn. Ct. App. Jan. 20, 1989).

reduces the amount of business that it does (or, but for that solicitation, would do) with the Company or any of its Affiliates, or (ii) solicit or induce any employee, distributor, sales representative, agent or contractor of the Company or any of its Affiliates to terminate his, her or its employment or other relationship with the Company or any of its Affiliates.

(c) If any Shareholder shall be in breach of any of the provisions of subsection (a) or subsection (b) above, then the time periods set forth in those subsections shall, as they relate to the breaching party, be extended by the length of time during which the breaching party is in breach of any of those provisions.

(d) As used in this Section 6.01, the following terms have the following meanings:

(i) **“Competing Business”** means the manufacturing, marketing or selling of products or services which are competitive with any Products and that are directly or indirectly marketed or sold in the Territory;

(ii) **“Product”** means (A) any product or service that the Company or any of its Affiliates is manufacturing, marketing, selling or developing on the date of this Agreement and (B) any other product or service that the Company or any of its Affiliates has marketed, sold or developed at any time during the three-year period immediately prior to the date of this Agreement; and

(iii) **“Territory”** means [ ],<sup>83</sup> in each case in which the Company or any of its Affiliates has marketed or sold any Products at any time during the three-year period immediately prior to the date of this Agreement.

6.02 Equitable Relief. The Shareholders acknowledge and agree that the Company would be irreparably damaged if any of the provisions of Section 6.01 are not complied with in accordance with their specific terms or are otherwise breached. Accordingly, it is agreed that the Buyer and the Company shall be entitled

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<sup>83</sup> This blank should specify the geographical territory in which the Buyer seeks to restrict the Selling Shareholders and their Affiliates from competing. *See, e.g., Greene County*, 338 S.W.2d at 600-01 (one hundred mile radius for an automobile truck tire recapping and repairing company is reasonable); *Butts*, 503 S.W.2d at 937-38 (three-county route for oil products business is not unreasonable).

to an injunction or injunctions to prevent breaches of Section 6.01 and shall have the right to specifically enforce Section 6.01 and its terms and provisions against the Shareholders in addition to any other remedy to which the Buyer and the Company may be entitled under this Agreement, at law or in equity.

6.03. Severability. It is the intent of the parties that each provision of Section 6.01 be adjudicated valid and enforced to the fullest extent permissible under the laws and public policies of each jurisdiction in which adjudication of the validity or enforcement of Section 6.01 is sought. In furtherance of the foregoing, each provision of Section 6.01 shall be severable from each other provision, and any provision of Section 6.01 that is prohibited or unenforceable in any jurisdiction shall be subject to the following:

(a) if the prohibited or unenforceable provision is contrary to or conflicts with any requirement of any statute, rule or regulation in effect in the jurisdiction, then the requirement shall be incorporated into, or substituted for, the prohibited or unenforceable provision to the minimum extent necessary to make the provision valid or enforceable;

(b) the Governmental Entity or arbitrator considering the matter is authorized to (or, if that Governmental Entity or arbitrator is unwilling or fails to do so, then the parties shall) amend the unenforceable provision to the minimum extent necessary to make the provision valid or enforceable, and the parties consent to the entry of an order amending the provision to that extent for that purpose; and

(c) if any unenforceable provision cannot be or is not reformed and made valid or enforceable under subsection (a) or subsection (b) of this Section 6.03, then the prohibited or unenforceable provision shall be ineffective in that jurisdiction to the minimum extent necessary to make the remainder of Section 6.01 valid or enforceable in that jurisdiction.

Any application of the foregoing provisions to any provision of Section 6.01 shall not (x) affect the validity or enforceability of any other provision of Section 6.01 or (y) prevent the prohibited or unenforceable provision from being adjudicated valid or enforced as written in any other jurisdiction.

ARTICLE VII  
INDEMNIFICATION

7.01. Indemnification by the Shareholders. The Shareholders shall defend, indemnify and hold harmless the Buyer and the Company and their respective directors, officers, employees and agents (each a “**Shareholder Indemnitee**”) from and against any and all claims (including without limitation any investigation, action or other proceeding, whether instituted by a third party against a Shareholder Indemnitee or by a Shareholder Indemnitee for the purpose of enforcing its rights under this Agreement), damages, losses, liabilities, costs and expenses (including without limitation reasonable attorneys’ fees and court costs) that constitute, or arise out of or in connection with:

(a) any misrepresentation or breach of warranty under Article II (a “**Shareholder Warranty Breach**”);

(b) any default by the Company Parties in the performance or observance of any of their covenants or agreements under this Agreement or any other Transaction Document; or

(c) any liability (each, an “**Excluded Liability**”) set forth on Schedule 7.01(c).

7.02. Indemnification by the Buyer. The Buyer shall defend, indemnify and hold harmless the Shareholders and their respective partners, directors, officers, employees and agents (each a “**Buyer Indemnitee**”) from and against any and all claims (including without limitation any investigation, action or other proceeding, whether instituted by a third party against a Buyer Indemnitee or by a Buyer Indemnitee for the purpose of enforcing its rights under this Agreement), damages, losses, liabilities, costs and expenses (including without limitation reasonable attorneys’ fees and court costs) that constitute, or arise out of or in connection with:

(a) any misrepresentation or breach of warranty under Article III (a “**Buyer Warranty Breach**”); or

(b) any default by the Buyer in the performance or observance of any of its covenants or agreements under this Agreement or any other Transaction Document.

7.03. Representation, Settlement and Cooperation. If any investigation, action or other proceeding (each a “**Proceeding**”) is initiated against any Shareholder Indemnatee or Buyer Indemnatee (each, an “**Indemnatee**”) and the Indemnatee intends to seek indemnification from the Shareholders or the Buyer (each an “**Indemnitor**”), as applicable, under this Article VII on account of the Indemnatee’s involvement in the Proceeding, then the Indemnatee shall give prompt notice to the applicable Indemnitor; provided, however, that the failure to so notify the Indemnitor shall not relieve the Indemnitor of its obligations under this Article VII but instead shall reduce those obligations by the amount of damages or increased costs and expenses attributable to the failure to give notice. Upon receipt of notice of a Proceeding for which indemnification is available under this Article VII, the Indemnitor shall diligently defend against the Proceeding on behalf of the Indemnatee at it’s, the Indemnitor’s, own expense, using counsel reasonably acceptable to the Indemnatee; provided, however, that if the Indemnitor shall fail or refuse to conduct the defense, or if the Indemnatee has been advised by counsel that it may have defenses available to it which are different from or in addition to those available to the Indemnitor or that its interests in the Proceeding are adverse to the Indemnitor’s interests, then the Indemnatee may defend against the Proceeding at the Indemnitor’s expense. The Indemnitor or Indemnatee, as applicable, may participate in any Proceeding being defended against by the other at its own expense and shall not settle any Proceeding without the prior consent of the other, which consent shall not be unreasonably withheld. The Indemnitor and Indemnatee shall cooperate with each other in the conduct of any Proceeding.

7.04. Notice and Satisfaction of Indemnification Claims. Indemnification claims against the Shareholders shall be satisfied first by set-off against the Escrow Fund, prior to being satisfied out of any other funds of the Shareholders. No indemnification claim shall be deemed to have been asserted until the applicable Indemnitor has been given notice by the Indemnatee of the amount of the claim and the facts on which the claim is based (including evidence supporting the amount of the claim) or, in the case of claims to be satisfied out of the Escrow Fund, any other notice that is required by the Escrow Agreement. For purposes of this Article VII, notice of an indemnification claim shall be deemed to cover claims arising out of or in connection with all related Proceedings so long as, in the case of Proceedings instituted by third parties, the Indemnatee complies with Section 7.03. Indemnification claims (other than those satisfied out of the Escrow Fund) shall be paid within 30 days after the Indemnitor’s receipt of the notice described in this Section 7.04 (including the required evidence of the amount of the claim). Evidence of (a) the amount of the claims for which the Indemnatee seeks indemnificatioin, and



(b) Indemnitor's liability shall be in form and content reasonably satisfactory to the Indemnitor.

7.05. Duration of Indemnification Obligations. Claims for indemnification under this Article VII only may be asserted within the following time periods:

(a) Claims arising out of or in connection with any Shareholder Warranty Breach under Section 2.09 (Tax Matters) may be asserted until 60 days after the running of the statute of limitations applicable to the taxable period to which a particular claim relates;

(b) Claims arising out of or in connection with any Shareholder Warranty Breach under Section 2.16 (Environmental Matters) or the Excluded Liability identified under the heading "Environmental Matters" on Schedule 7.01(c) may be asserted at any time on or prior to the [**typically, second to fifth**]<sup>84</sup> anniversary of the Closing Date;

(c) Claims arising out of or in connection with any Shareholder Warranty Breach under Section 2.05 (Ownership and Control) or,

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<sup>84</sup> As a general matter, negotiations regarding the survival of representations and warranties beyond the closing of an acquisition should be governed by a realistic assessment by all parties of the time needed by the acquiror to discover a possible breach and bring a claim for that breach. *See* Hamilton & Heminway, *supra* note 16, at 250 n.78 ("At a minimum, the buyer should request that the representations and warranties survive until they can be independently verified by the buyer in the ordinary course of business."). This time period may vary, depending on the financial reporting cycle of the acquiror and the subject matter of the representation or warranty.

If the representations do survive the closing, it will often be the case that they will survive until the expiration of the applicable statute of limitations for contracts. But it is not unusual for the parties to agree on a somewhat shorter period of time that the representations will survive and form the basis for a cause of action. Most representations will generally survive for one to two years, with those relating to taxes, employee benefits, environmental issues and due authorization of the transaction surviving significantly longer.

Kling et al., *supra* note 76, at 805.

insofar as those claims relate to title to the Stock only, Section 2.20 (Title to Assets) may be asserted at any time;<sup>85</sup>

(d) Claims arising out of or in connection with any Shareholder Warranty Breach may be asserted at any time if the applicable representation or warranty was fraudulently made;

(e) All other claims for indemnification under Section 7.01(a) may be asserted at any time on or prior to the [typically, first to third]<sup>86</sup> anniversary of the Closing Date; and

(f) Other claims for indemnification may be asserted at any time.

7.06. Indemnification Threshold and Cap. Notwithstanding any other provision of this Agreement:

(a) No Indemnitor shall have any indemnification obligations under Section 7.01(a) (exclusive of a Shareholder Warranty Breach under Section 2.30), Section 7.01(c) or Section 7.02(a) (exclusive of a Buyer Warranty Breach under Section 3.04(e) that relates to the HSR Act or under Section 3.05 or Section 3.06) unless and until the claims asserted against the applicable Indemnitor exceed \$[ ] in the aggregate (the “**Threshold Amount**”).<sup>87</sup> If indemnification

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<sup>85</sup> On the theory that representations regarding the legal ownership of the securities being purchased and the title to any key assets are at the heart of the acquiror’s benefit of the bargain in an acquisition, the parties often agree that these representations survive the closing indefinitely.

<sup>86</sup> See *supra* note 84.

<sup>87</sup> This dollar amount generally is termed a “basket.” See ABA MODEL AGREEMENT, *supra* note 2, at 204; Hamilton & Heminway, *supra* note 16, at 253 n.79. The dollar value and nature of the basket often is hotly negotiated. Specifically, the dollar value of a basket varies significantly depending on a variety of factors, including: whether basket is a “true deductible” or “tipping basket” (see *infra* note 88); the indemnification cap, if any; the amount of the purchase price; and other facts and circumstances specific to the transaction. Selling shareholders typically argue for a basket to avoid the administrative difficulties associated with small indemnification claims. The acquiror may refute the selling shareholders’ argument by stating that the acquiror has agreed to qualify certain of the representations and warranties by materiality to avoid the same administrative difficulties (or “nickel and diming”) and that the inclusion of both materiality qualifications and a basket would be “double dipping.” See ABA MODEL AGREEMENT, *supra* note 2, at 204. The Threshold Amount, as defined in

claims exceed the Threshold Amount, the Indemnitor shall be liable for all indemnification claims properly asserted against it, including those comprising the Threshold Amount.<sup>88</sup>

(b) The Shareholders' indemnification obligations arising out of or in connection with a Shareholder Warranty Breach (i) under Section 2.05 (Ownership and Control) or (ii) as to title to the Stock under Section 2.20 (Title to Assets) shall be capped at \$[ ].<sup>89</sup> The Shareholders' indemnification obligations arising out of or in connection with any other Shareholder Warranty Breach or any Excluded Liability shall be capped at \$[ ].<sup>90</sup> All other indemnification obligations shall be unlimited as to dollar amount.

#### 7.07. Other Limitations on Indemnification Provisions.

(a) Any payment made by an Indemnitor to an Indemnitee under this Article VII (i) shall be net of any insurance proceeds realized

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this section, is not applicable in the event of covenant defaults (which are indemnifiable under Sections 7.01(b) and 7.02(b)). Claims relating to these defaults are indemnifiable from the first dollar of liability.

<sup>88</sup> The basket here serves as a nuisance threshold or "tipping basket." Effectively, once the Threshold Amount is exceeded, the Buyer can claim all allowable amounts under the indemnification provisions. (In other words, in the case of a "tipping basket," the acquiror is only responsible for damages arising from indemnifiable claims until the amount of the damages exceeds the basket, at which time the selling shareholders would be required to indemnify the acquiror for all damages, including the basket.) If the basket were a "true deductible," the acquiror would be responsible for all damages arising from indemnifiable claims up to the basket, even if and when the damages were to exceed the basket. *See* ABA MODEL AGREEMENT, *supra* note 2, at 204.

<sup>89</sup> The amount of this indemnification cap is often separate from and higher than the indemnification cap for other shareholder warranty breaches because the representations and warranties subject to this indemnification cap are at the heart of the value of the transaction (*i.e.*, the stock being purchased). This indemnification cap is often as high as 100% of the purchase price.

<sup>90</sup> The indemnification cap is a critical negotiating point and could be considered the most important provision in the agreement (except for purchase price). In essence, the amount of the indemnification cap allocates post-closing liability risks arising from pre-closing activities. The amount of the indemnification cap is based upon numerous factors, including the amount of the purchase price, the time period that the representations and warranties will survive, the risks inherent in the target's business, the acquiror's tolerance for risk, and many other factors specific to the particular facts and circumstances of the underlying transaction.

by and paid to the Indemnitee in respect of the indemnification claim and (ii) shall be net of an amount equal to any tax benefits realized by the Indemnitee that are attributable to losses giving rise to the indemnification claim.

(b) No Shareholder shall be liable for the breach by any other Shareholder of the covenants set forth in Section 6.01 or Section 8.03 or for any related indemnification obligation under Section 7.01.

(c) Except as otherwise provided in subsection (b) above, each Shareholder shall be jointly and severally liable for a breach of this Agreement by any of the Shareholders and for the related indemnification obligations of the Shareholders under Section 7.01, but only to the extent of the Escrow Fund. After the Escrow Fund has been exhausted, each Shareholder only shall be liable for a proportionate share of each indemnification claim equal to the percentage set forth opposite its name on Schedule 1.03.<sup>91</sup>

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<sup>91</sup> This Model Tennessee SPA provides that the Shareholders' joint and several liability extends only to the extent of valid claims up to and including the value of the Escrow Fund; Shareholders are proportionately liable for valid claims exceeding that amount. This is a middle-of-the-road approach. This Model Tennessee SPA also could provide for unrestricted or unlimited joint and several liability for the Shareholders in the event of a breach, or it merely could limit the amount for which the Shareholders may be held liable in some way (*e.g.*, by imposing an overall or specific use cap or by limiting the Shareholders' liability to amounts held in the Escrow Fund). *See supra* notes 89 & 90; Hamilton & Heminway, *supra* note 16, at 253 n.79; Kling et al., *supra* note 64, at 805 ("It is the authors' experience . . . that most agreements provide that, absent fraud, the indemnification provisions are the exclusive remedy."). Note that subsections (a) and (b) of Section 7.07 of this Model Tennessee SPA also place limits on the indemnification responsibilities and benefits of the contracting parties. Also note that, because indemnification is a matter of contract, indemnification liability also can be limited or expanded to include matters that do not constitute a breach of the acquisition agreement by, for example, providing that the selling shareholders indemnify the acquiror for specific liability events that occur after the closing of the transaction (*e.g.*, litigation awards or settlements, employee benefit plan liabilities, etc.).

As to the buyer's post-closing activities, certain matters may be singled out and treated as specific items with respect to which the buyer will be indemnified. These areas often include particular pending litigations or pending or threatened claims which the seller has agreed to retain responsibility for, taxes due for periods prior to the closing, the collectibility of accounts receivable and certain environmental matters, as well as indemnification for third party claims.

Kling et al., *supra* note 64, at 804-05. *See also* Hilton v. CET/DDT Corp., 1990 Tenn. App. LEXIS 40 (Tenn. App. 1990) (in which the court describes and adjudicates specific indemnification claims). The

7.08. Exclusive Remedy. Except: (a) as otherwise provided in Section 6.02; (b) for any equitable remedies which the parties may pursue to prevent a breach of Section 8.03; and (c) for enforcement actions of any kind or nature regarding the terms and provisions of this Article VII, the indemnification under this Article VII shall be the parties' sole and exclusive remedy, each against another, with respect to matters arising under this Agreement. The parties waive and release any other rights, remedies, causes of action or claims of any kind or nature arising under this Agreement.

#### ARTICLE VIII MISCELLANEOUS PROVISIONS<sup>92</sup>

8.01. Amendments. This Agreement may be amended only by a writing signed by each of the parties, and any amendment shall be effective only to the extent specifically set forth in that writing.

8.02. Assignment. Neither this Agreement nor any right, interest or obligation under this Agreement may be assigned, pledged or otherwise transferred by any party or parties, whether by operation of law or otherwise, without the prior written consent of the other party or parties; provided, however, that the Buyer (a) may assign its rights under this Agreement to any successor by merger or purchase of all or substantially all of the Buyer's assets (but only if the purchaser expressly assumes the obligations of the Buyer under this Agreement) and (b) may collaterally assign its rights under this Agreement to any lender.

8.03. Confidentiality.

(a) As used in this Section 8.03, the “**Confidential Information**” of a party means all information concerning or related to the business, operations, financial condition or prospects of the party or any of its Affiliates, regardless of the form in which that information appears and whether the information has been reduced to a tangible form. The Confidential information of a

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possibility of indemnification for specified non-breach liabilities has been left open in Section 7.01(c) of this Model Tennessee SPA.

<sup>92</sup> Many practitioners characterize the “Miscellaneous Provisions” of an acquisition agreement “boilerplate.” For a discussion of important considerations relating to the content and drafting of these provisions, see KUNEY, *supra* note 16, at 107-12.

party specifically includes: (i) all information regarding the officers, directors, employees, equity holders, customers, suppliers, distributors, sales representatives and licensees of the party or its Affiliates, in each case whether present or prospective; (ii) all inventions, discoveries, trade secrets, processes, techniques, methods, formulae, ideas and know-how of the party or its Affiliates; and (iii) all financial statements, audit reports, budgets and business plans or forecasts of the party or its Affiliates. The Confidential Information of a party does not include: (A) information which is or becomes generally known to the public through no act or omission of another party; and (B) information which has been or is lawfully obtained by another party from a source other than the party to whom the Confidential Information belongs (or any of its Affiliates or their respective officers, directors, employees, equity holders or agents), so long as, in the case of information obtained from a third party, the third party was or is not, directly or indirectly, subject to an obligation of confidentiality owed to the party to whom the Confidential Information belongs or any of its Affiliates at the time the Confidential Information was or is disclosed to the other party.

(b) Except as otherwise permitted by subsection (c) below, each party agrees that it will not, without the prior written consent of the other party, disclose or use for its own benefit any Confidential Information of the other parties.

(c) Notwithstanding subsection (b) above, each party shall be permitted to:

(i) disclose Confidential Information of another party to the disclosing party's officers, directors, employees, equity holders, lenders, agents and Affiliates, but only to the extent reasonably necessary in order for that disclosing party to perform his, her or its obligations and exercise his, her or its rights and remedies under this Agreement, and that disclosing party shall take all action as shall be necessary or desirable in order to ensure that each of the Persons to whom Confidential Information is disclosed maintains the confidentiality of that Confidential Information;

(ii) make additional disclosures of or use for its own benefit Confidential Information of another party, but only if and to the extent that the disclosures or use are specifically contemplated by this Agreement; and

(iii) disclose Confidential Information of another party to the extent, but only to the extent, required by Governmental Rules; provided, however, that prior to making any disclosure under this subsection, the disclosing party shall notify the party whose Confidential Information must be disclosed, and that party shall have the right to participate with the disclosing party in determining the amount and type of Confidential Information, if any, that must be disclosed in order to comply with Governmental Rules.

8.04. Counterparts; Telefacsimile Execution. This Agreement may be executed in any number of counterparts, and by each of the parties on separate counterparts, each of which, when so executed, shall be deemed an original, but all of which shall constitute but one and the same instrument. Delivery of an executed counterpart of this Agreement by telefacsimile<sup>93</sup> shall be equally as effective as delivery of a manually executed counterpart of this Agreement.<sup>94</sup> Any party delivering an executed counterpart of this Agreement by telefacsimile also shall

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<sup>93</sup> The word “telefacsimile” may be unfamiliar to some and oddly formal to others, who might use “facsimile” or “teletype” in its place. A former Tennessee law defined the term to mean “every process in which electronic signals are transmitted by telephone lines for conversion into written text.” See Jeffrey L. Reed, Comment: *The Tennessee Consumer Protection Act: An Overview*, 58 TENN. L. REV. 455, 496 n.338 (1991). Although only vestigial references to the word appear in Tennessee statutes, the authors chose this term to describe what most colloquially term “faxed signature pages” because of its broad applicability and continued popular, commercial, and scholarly use. See Jan Hemm Pritchard, *Keeping the Fax Private*, 52 J. MO. B. 279 (1996) (describing the history and usage of telefacsimile machines as they relate to privacy issues); Marc E. Szafran, Note: *A Neo-Institutional Paradigm for Contracts Formed in Cyberspace: Judgment Day for the Statute of Frauds*, 14 CARDOZO ARTS & ENT L.J. 491, 503 n.55 (1996) and accompanying text (describing telefacsimile transmission and its importance to commercial transactions).

<sup>94</sup> Most parties to a business combination find telefacsimile signatures a convenience, if not a necessity. Even transactions in which the parties all are residents of or present in the State of Tennessee, it may be difficult to assemble the various selling shareholders in one location on a specific date or dates for the purpose of executing a stock purchase agreement. Given the apparent desirability of telefacsimile signatures, it is important that the parties to acquisition agreements and their legal counsel evaluate the validity and enforceability, under applicable law, of contracts executed in whole or in part by the transmission of signatures by telefacsimile. In Tennessee, it may be important to expressly provide for the effectiveness, as between or among the parties to a business contract, of telefacsimile signatures. See generally *Love v. Coll. Level Assessment Servs.*, 928 S.W.2d 36, 38 (Tenn. 1996) (finding that a notice of appeal transmitted by telefacsimile is ineffective in perfecting an appeal due, in part, to the absence of clear, express, detailed provisions authorizing the use of facsimile transmission). However, telefacsimile transmissions have been accepted by courts for many purposes since the 1980’s. See John Robinson Thomas, Note: *Legal Responses to Commercial Transactions Employing Novel Communications Media*, 90 MICH. L. REV. 1145, 1155-60 (1992) (describing the use, interpretation, and enforcement of telefacsimile representations of contract execution).

deliver a manually executed counterpart of this Agreement, but the failure to deliver a manually executed counterpart shall not affect the validity, enforceability or binding effect of this Agreement.

8.05. Entire Agreement. This Agreement and the other Transaction Documents contain the entire agreement of the parties with respect to the transactions contemplated by this Agreement and the other Transaction Documents and supersede all prior written and oral agreements, and all contemporaneous oral agreements, relating to these transactions.

8.06. Expenses. Except as otherwise specifically provided in this Agreement or in any other Transaction Document, each party shall be responsible for the expenses it may incur in connection with the negotiation, preparation, execution, delivery, performance and enforcement of this Agreement and the other Transaction Documents; provided, however, that if the Closing occurs, then the Shareholders shall be responsible for all transaction-related expenses incurred by or on behalf of the Company on or prior to the Closing Date.

8.07. Further Assurances. The parties shall from time to time do and perform any additional acts and execute and deliver any additional documents and instruments that may be required by applicable Governmental Rules or reasonably requested by any party to establish, maintain or protect its rights and remedies under, or to effect the intents and purposes of, this Agreement and the other Transaction Documents.

8.08. Governing Law. This Agreement shall be a contract under the laws of the State of Tennessee and for all purposes shall be governed by and construed and enforced in accordance with the laws of that State.

8.09. Notices. Unless otherwise specifically provided in this Agreement, all notices, consents, requests, demands and other communications required or permitted under this Agreement:

- (a) shall be in writing;
- (b) shall be sent by messenger, certified or registered U.S. mail, a reliable express delivery service or telefacsimile (with a copy sent by one of the foregoing means), charges prepaid (as applicable), to the appropriate address(es)



or number(s) set forth below or to another address or number as to which any party may inform the others by giving five business days' prior notice:

If to the Company Parties:

With a copy to:

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

Attn: \_\_\_\_\_

Attn:

Telefacsimile No.:(\_\_\_\_) \_\_\_\_\_

Telefacsimile No.: (\_\_\_\_)

If to the Buyer:

With a copy to:

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

Attn: \_\_\_\_\_

Attn:

Telefacsimile No.: (\_\_\_\_) \_\_\_\_\_

Telefacsimile No.: (\_\_\_\_)

and

(c) shall be deemed to have been given on the date of receipt by the addressee (or, if the date of receipt is not a business day, on the first business day after the date of receipt), as evidenced by (i) a receipt executed by the addressee (or a responsible person in his or her office), the records of the Person delivering the communication or a notice to the effect that the addressee refused to claim or accept the communication, if sent by messenger, U.S. mail or express delivery service, or (ii) a receipt generated by the sender's telefacsimile machine showing that the communication was sent to the appropriate number on a specified date, if sent by telefacsimile.

8.10. Publicity.<sup>95</sup> Neither party shall make any press release or other public announcement regarding this Agreement or the other Transaction Documents or any transaction contemplated by this Agreement or the other Transaction Documents until the text of the release or announcement has been submitted to the other party and the other party has approved it.

8.11. Severability. The severability of Section 6.01 is governed by Section 6.03. Any provision of this Agreement other than Section 6.01 that is prohibited or unenforceable in any jurisdiction shall, as to that jurisdiction, be ineffective to the extent of the prohibition or unenforceability without invalidating the remaining portions of this Agreement or affecting the validity or enforceability of the provision in any other jurisdiction.

8.12. Successors and Assigns. This Agreement shall be binding upon and shall inure to the benefit of each of the parties and their respective heirs, successors and permitted assigns.

8.13. Termination.

(a) This Agreement may be terminated at any time prior to the Closing:

(i) by mutual agreement of the Buyer and the Company Parties;

(ii) by the Buyer (A) if there has been a material misrepresentation by the Company Parties under this Agreement or a material breach by the Company Parties of any of their warranties or covenants set forth in this Agreement or (B) if any of the conditions specified in Section 5.02 shall not have been fulfilled within the time required and shall not have been waived by the Buyer;

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<sup>95</sup> Frequently (and especially where public companies are parties), provisions such as these are qualified by the legal or regulatory obligations of the parties. See *Adams TV of Memphis, Inc. v. ComCorp of Tenn.*, 969 S.W.2d 917 (Tenn. Ct. App. 1997) (quoting an exemplar provision from an asset purchase agreement); See ABA MODEL AGREEMENT, *supra* note 2, at 214-15; Hamilton & Heminway, *supra* note 16, at 255 n.83 and accompanying text.

(iii) by the Company Parties (A) if there has been a misrepresentation by the Buyer under this Agreement or a material breach by the Buyer of any of its warranties or covenants set forth in this Agreement or (B) if any of the conditions specified in Section 5.03 shall not have been fulfilled within the time required and shall not have been waived by the Company Parties; or

(iv) by the Buyer or the Company Parties if the Closing shall not have occurred prior to March 31, 2004; provided, however, that the Buyer or the Company Parties may terminate this Agreement under this subsection (iv) only if the Closing shall not have occurred on or prior to March 31, 2004, for a reason other than a failure by the party or parties asserting the right to terminate to satisfy the conditions to Closing of the other party or parties set forth in Section 5.02 or 5.03.

(b) If this Agreement is terminated by either the Company Parties or the Buyer as provided in Section 8.13(a) then no party shall have any further obligations or liabilities under this Agreement except for obligations or liabilities arising from a breach of this Agreement prior to the termination or that survive the termination by their own terms.

8.14. Waivers. The due performance or observance by the parties of their respective obligations under this Agreement and the other Transaction Documents shall not be waived, and the rights and remedies of the parties under this Agreement and the other Transaction Documents shall not be affected, by any course of dealing or performance or by any delay or failure of any party in exercising any right or remedy. The due performance or observance by a party of any of its obligations under this Agreement or any other Transaction Document may be waived only by a writing signed by the party against whom enforcement of the waiver is sought, and any waiver shall be effective only to the extent specifically set forth in that writing.

8.15. Knowledge Parties. References in this Agreement to the Company Parties' knowledge or words of similar import shall mean the knowledge of [Names], assuming reasonable investigation and inquiry as to the subject matter in question is made of the Company's other officers, directors, management employees and outside counsel and accountants.<sup>96</sup>

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<sup>96</sup> For information about the importance of identifying these knowledge parties, see *supra* notes 47 & 48.

#### 8.16 Appointment of Shareholder Agent.

(a) The Shareholders irrevocably constitute and appoint the Shareholder Agent as their agent and attorney-in-fact (i) to give and receive all notices under this Agreement, (ii) to execute and deliver all documents and instruments required to be executed and delivered by the Shareholders or any of them under this Agreement and the other Transaction Documents, and (iii) to receive all payments that are required to be made to the Shareholders under this Agreement. The Shareholder Agent accepts this appointment.

(b) Nothing contained in this Agreement shall be deemed to make the Shareholder Agent personally liable to the Shareholders because of service in its capacity as agent and attorney-in-fact. In performing any of its duties under this Agreement, the Shareholder Agent shall not incur any liability to the Shareholders for losses, damages, liabilities or expenses, except for its own gross negligence, recklessness or willful misconduct. The Shareholder Agent shall have no obligation to take any action under this Agreement on behalf of the Shareholders that requires the expenditure of money unless the Shareholder Agent receives satisfactory assurances from the Shareholders that it will be reimbursed by the Shareholders for those expenditures.

(c) It is expressly understood and agreed that this power of attorney and the agency created by this Section 8.16 (i) is coupled with an interest of the Shareholders, (ii) shall be binding on and enforceable against the respective heirs, personal representatives, successors and assigns of the Shareholders, and (iii) shall not be revoked or terminated by the bankruptcy or dissolution of any Shareholder.

SIGNATURE PAGE TO STOCK PURCHASE AGREEMENT<sup>97</sup>

**BUYER:**

By \_\_\_\_\_

Name:

Title:

**COMPANY:**

By \_\_\_\_\_

Name:

Title:

**SHAREHOLDERS:**

\_\_\_\_\_  
Name:

\_\_\_\_\_  
Name:

\_\_\_\_\_  
Name:

**SHAREHOLDER AGENT:**

By \_\_\_\_\_

Name:

Title:

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<sup>97</sup> The decision of whether to label or entitle the signature page of an acquisition agreement is made based on law firm forms and personal style. Many practitioners, however, do start the parties' signature lines on a separate page (even if it means leaving a short page preceding the signature page or pages) for convenience in drafting and telefacsimile transmissions. See *supra* notes 93 & 94. For helpful guidance regarding traditional and electronic signatures and related considerations, see KUNEY, *supra* note 16, at 117-22.

**DEFINITIONS**

<u>Definition</u>	<u>Page</u> <sup>98</sup>
Affiliate	255
Agreement	217
Buyer	217
Buyer Indemnitee	273
Buyer Warranty Breach	273
Closing	263
Closing Balance Sheet	224
Closing Date	263
Closing Purchase Price	220
Code	251
Company Agreements	254
Company Financial Statements	228
Company	217
Company Parties	232
Company Permits	245
Competing Business	271
Confidential Information	279
Confidential Information Memorandum	256
Control	255
Current Financial Statements	237
Earn-Out Payment	229
EBITDA	229
Environmental Rule	247
Equipment	248
ERISA	251
ERISA Affiliate	251
Escrow Agent	221
Escrow Agreement	222
Escrow Fund	221
Estimated Working Capital	224

---

<sup>98</sup> Generally, page numbers would be keyed to pages in the Agreement. For ease of reference in this Model Tennessee SPA, however, the authors have included in this column the page references in this volume.

Excluded Liability	273
FDA	243
Financial Statement Date	238
Financial Statements	237
GAAP	224
Governmental Entity	236
Governmental Order	236
Governmental Rule	236
Hazardous Substance	247
HSR Act	236
Indemnitee	274
Indemnitor	274
Intellectual Property	250
IRS	239
Liens	220
Material Adverse Change	234
Multiemployer Plan	252
Pension Plan	252
Permitted Liens	250
Person	236
PMA's	243
Policy	253
Preliminary Purchase Price	220
Proceeding	274
Product	271
Purchase Price	220
Real Property	247
Securities Act	259
Shareholder Agent	217
Shareholder Indemnitee	273
Shareholder Warranty Breach	273
Shareholders	217
Stock	217
Territory	271
Threshold Amount	276
Transaction Documents	266
Welfare Plan	252
Working Capital	227
Working Capital Peg	227