

Corporate Finance/M&A - Austria

Supreme Court considers recovery provisions in purchase agreements

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General provisions

Share purchase agreements usually set out extensive representations regarding the transaction target. Unless otherwise stipulated, such representations could be interpreted and enforced under the rules of either warranty law or, alternatively, tort law.

In practice, share purchase agreements provide that buyers are entitled to monetary compensation for any breach of representations only and specify a mechanism for calculating the amount. Further, most contracts explicitly exclude any other legal remedies, which means that the legal concept under which compensation may be enforced is open to interpretation.

However, different legal concepts impose different standards of proof on the buyer; the buyer may even be entitled to different amounts of compensation from the vendor for any breaches. One such example involves the consideration of any advantages which might result from breaches or remedying of representations. While any advantages for the buyer arising from a breach by the vendor are generally taken into account under tort law principles, they are not considered under warranty law principles due to a difference in calculation methods. The consequences of these differences were highlighted in a recent Supreme Court judgment.⁽¹⁾

Recent Supreme Court judgment

The claimant sold two plots of land to the defendant. Shortly after the conclusion of the contract, the relevant construction authority ordered the defendant to register an easement with the local land registry for one of the plots for the benefit of the other plot, and to comply with additional construction-related requirements. As a result of these instructions, the resale value of the land decreased considerably, even though the defendant expressly disclosed to the claimant its intention subsequently to sell the purchased land. The defendant therefore did not pay the entire purchase price and the claimant tried to enforce the outstanding amount.

The court of first instance awarded part of the purchase price to the claimant under consideration of certain counterclaims made by the defendant as a consequence of the land's decrease in value. The court of appeal in principle upheld this decision, but stated that the decrease in value of one plot (due to the burden of the easement) had to be offset against the increase in value of the other plot (due to the benefits of the easement).

The Supreme Court partly overturned this decision and confirmed that a price reduction was to be determined according to the relative calculation method. This calculation method takes into account only the relationship between the price and value of the acquired item(s) by comparing the defect-free object to the defective object. According to this method, only the decrease in the value of one plot (but not the increase in value of the other plot) could be taken into account. The financial situation of the buyer and potential advantages which the buyer could realise as a result of the breach of representations were disregarded.

Implications

In its recent decision the Supreme Court confirmed that a price reduction under Austrian tort law takes into account advantages which a buyer might obtain by the

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correction of a defect only under exceptional circumstances. Such advantages are considered under Austrian tort law only under application of a concrete calculation method, as this method compares the buyer's assets before and after the damage occurred.

Although not referring to the acquisition of a corporation or business by means of either a share or asset deal, this ruling therefore again illustrates difficulties which could easily occur when Anglo-American legal M&A concepts are incorporated into contracts governed by Austrian law. Should the parties not conclusively stipulate the consequences of a contractual breach of representations, including the exact calculation method of the damage resulting from such a breach, the consequences could differ from the expected.

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Endnotes

(1) 3 Ob 109/10 s.

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