Annual Survey of Judicial Developments Pertaining to Mergers and Acquisitions

*By the Annual Survey Working Group of the M&A Jurisprudence Subcommittee, Mergers and Acquisitions Committee, ABA Section of Business Law**

The primary charge of the Annual Survey Working Group is to monitor and summarize annually significant judicial decisions related to mergers and acquisitions ("M&A") that we believe are of the greatest interest to M&A practitioners.[1]

The decisions summarized in this year's Annual Survey are

Rep and Warranty Survival Clause as Contractual Statute of Limitations

1. *GRT, Inc. v. Marathon GTF Technology, Ltd.*

Implied Covenants and Binding Provisions

2. *Emposimato v. CIFC Acquisition Corp.*
3. *Patriot Rail Corp. v. Sierra Railroad Co.*
4. *Hulbert v. Port of Everett*

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1. To be included in the Annual Survey, cases must meet two criteria:

   1. The decision must address a transaction involving a change of control, including by means of a merger, sale of equity interest, or recapitalization, or a sale of all or substantially all of a company's assets or of a subsidiary or division.
   2. The court must (i) interpret or apply the provisions of an acquisition agreement or an agreement preceding an acquisition agreement (e.g., letter of intent, confidentiality agreement, or standstill agreement); (ii) interpret or apply a state statute (e.g., general corporation, limited liability company, or partnership law) that governs one of the constituent entities; (iii) rule on a successor liability issue; or (iv) decide a breach of fiduciary duty claim (although the survey may not include all fiduciary duty cases if they appear to have received sufficient publicity in other publications during the year).

Excluded are cases dealing exclusively with federal law, securities law, tax law, or antitrust law.

Tortious Interference Against Topping Bidder

5. *Ventas, Inc. v. HCP, Inc.*

Application of a Merger Agreement to Non-Signatory Stockholders

6. *Aveta Inc. v. Cavallieri*

Meaning of "Best Efforts"

7(i). *Kevin M. Ehringer Enterprises, Inc. v. McData Services Corp.*
7(ii). *Denil v. Deboer, Inc.*

Breach of Good Faith Negotiation Covenant

8. *Romtec v. Oldcastle Precast, Inc.*

Letter of Transmittal in Short-Form Merger

9. *Roam-Tel Partners v. AT&T Mobility Wireless Operations Holdings Inc.*

Merger as Assignment

10. *Meso Scale Diagnostics, LLC v. Roche Diagnostics GmbH*

Fiduciary Termination Right Requirements

11. *Monty v. Leis*

Successor Liability

12. *Einhorn v. M.L. Ruberton Construction Co.*

Fraudulent Inducement and Disclaimers of Reliance

13(i). *OverDrive, Inc. v. Baker & Taylor, Inc.*
13(ii). *Allen v. Devon Energy Holdings, L.L.C.*

Case Summaries

1. *GRT, Inc. v. Marathon GTF Technology, Ltd.* (Survival Clause as a Contractual Statute of Limitations)

In *GRT, Inc. v. Marathon GTF Technology, Ltd.*, the Delaware Court of Chancery interpreted a survival clause in a securities purchase agreement (the "Agreement") as a contractual statute of limitations.[2] In particular, the court construed a provision in the Agreement stating that certain representations would survive one year after closing and that, after one year, all associated remedies would terminate (the "Survival Clause") as a contractual statute of limitations on any claims for breach of such representations one year after closing. As a result, the *GRT* court granted the defendant's motion to dismiss claims for breach of representations arising out of the Agreement on the basis that such claims were time-barred.

2. No. 5571-CS, 2011 WL 2682898 (Del. Ch. July 11, 2011).

Background

The plaintiff entered into a series of agreements with the defendant, including the Agreement, in connection with a joint venture in which the defendant agreed to build a testing facility in exchange for access to the plaintiff's intellectual property.[3] In the Agreement, the defendant represented that the facility would be designed to meet certain objectives (the "Design Representations").[4] The Agreement closed on July 18, 2008 (the "Closing Date").[5] Following the closing, the plaintiff was permitted to inspect the facility to determine whether the defendant had breached the Design Representations.[6] If the defendant had breached the Design Representations, then the Agreement required the defendant to make the necessary modifications to the facility.[7] The plaintiff alleged that, post-closing, it repeatedly notified the defendant that the facility was not consistent with the Design Representations.[8] However, the defendant did not make any modifications to the design or construction of the facility.[9] The plaintiff filed suit against the defendant for breach of the Design Representations on June 16, 2010, approximately two years after closing.[10]

Survival Clause

The Survival Clause provided that the Design Representations would "survive for twelve (12) months after the Closing Date, and will thereafter terminate, together with any associated right of indemnification pursuant to Section 7.2 or 7.3 or the remedies provided pursuant to Section 7.4 [the remedial obligations]."[11] The plaintiff argued that such a clause simply described the time period during which a breach could occur, subject to the applicable statute of limitations, rather than the time period during which a claim had to be filed.[12] The plaintiff also argued that it was not suing for breach of the Design Representations but rather for a breach of the remedial obligations that were triggered by the failure to cure the breach of the Design Representations.[13]

Delaware Law

The court noted that, under Delaware law, the default statute of limitations for breach of contract is three years, which begins to run when the contract is

3. *Id.* at *4.
4. *Id.*
5. *Id.*
6. *Id.*
7. *Id.*
8. *Id.* at *5.
9. *Id.*
10. *Id.*
11. *Id.* at *7.
12. *Id.* at *2.
13. *Id.*

breached.[14] Because representations and warranties generally speak to the state of facts at closing, a breach of contract claim will often accrue at closing.[15] The court noted that parties to a contract may shorten the time period in which a claim must be brought and that such a shortening of the statute of limitations does not conflict with Delaware public policy.[16] The court noted that the interpretation of the Survival Clause was a question of pure contract interpretation and that, unlike other jurisdictions where a contractual shortening of the statute of limitations has to be clear and unequivocal,[17] Delaware law does not impose a higher standard of interpretation on provisions shortening the statute of limitations.[18] The court then discussed general principles of contract construction, noting that language in a contract must be given "its ordinary and usual meaning"[19] and must be construed objectively in terms of what a reasonable person in the position of the parties would have understood.[20]

Analysis

The court analyzed the Agreement as creating a three-step scheme for recovery for breach of the Design Representations post-closing. In the event of a breach of the Design Representations, the defendant was obligated to remedy the breach.[21] If the remedial steps taken by the defendant did not cure the breach so as to make the Design Representations true in all material respects, then the plaintiff could sue the defendant for a breach of contract claim, based on the breach of the remedial obligations, and seek an order of specific performance.[22] Under the court's interpretation of the Agreement, the remedy of specific performance could not be imposed until the plaintiff demonstrated a breach of the Design Representations. Accordingly, the court rejected the plaintiff's attempt to bypass a suit for breach of the Design Representations by alleging breach of the remedial obligations.[23]

The court then focused on the claims for breach of the Design Representations and held that the Survival Clause acted as a contractual statute of limitations that

14. *Id.* at *6.

15. *Id.*

16. The court noted that this was not the case with expanding the statute of limitations, which the courts have found to be inconsistent with the public policy underlying statutes of limitation. *Id.* at *15 n.80. After recognizing that public policy considerations may impact a court's interpretation of a contractual provision modifying the statute of limitations, the court instructed that a provision shortening the statute by contract does not "violate the unambiguously negative command of" the statute as a provision lengthening it does, thereby allowing "access to the state's courts for suits the legislature has declared moribund." *Id.*

17. The court noted, as one example, *Western Filter Corp. v. Argan, Inc.*, 540 F.3d 947, 949 (9th Cir. 2008), in which the court construed California law. *GRT*, 2011 WL 2682898, at *3 & n.5.

18. *GRT*, 2011 WL 2682898, at *3.

19. *Id.* at *6 (quoting AT&T Corp. v. Lillis, 953 A.2d 241, 252 (Del. 2009) (quoting Lorillard Tobacco Co. v. Am. Legacy Found., 903 A.2d 728, 739 (Del. 2006))).

20. *Id.* (citing Rhone-Poulenc Basic Chems. Co. v. Am. Motorists Ins. Co., 616 A.2d 1192, 1196 (Del. 1992)).

21. *Id.* at *9.

22. *Id.* at *9–10.

23. *Id.* at *10.

limited the time in which the claims for such breach could be filed.[24] The court based its holding on the plain meaning of the contract and its reading of the contract as a whole, a survey of relevant case law and commentary to determine what transactional lawyers traditionally intended survival provisions to mean, and the "business context" in which the Agreement was negotiated.[25]

Plain Language and Contract as a Whole

The court found that the plain language of the Survival Clause could only be read as a contractual statute of limitations because the provision was drafted in a "liability-limiting fashion," i.e., the Design Representations and the associated remedies would "terminate" one year after closing.[26] The court explained that under Delaware rules of contract interpretation, the parties were not required to utilize clear and unequivocal language to shorten the statute of limitations (although the court suggested that the language at issue might have satisfied such a standard).[27] The court read the contract as a whole and noted that certain other representations and warranties survived closing indefinitely, while others survived until the expiration of the applicable statute of limitations.[28] Read together, these provisions suggested that the parties intended the "survival" terminology to limit the time for bringing various claims.[29]

Interpretation by Courts and Commentators

In reaching its conclusion, the court also considered what transactional lawyers have traditionally meant when using survival clauses.[30] The court noted that there are at least four ways to address the duration of representations and warranties and the suits arising from their breach.

First, contracts may provide that representations and warranties terminate at closing.[31] According to the court, in that case, the parties have no basis for a post-closing suit seeking remedy for any alleged misrepresentation—when the representations and warranties terminate, so does any remedy for their breach.[32]

24. *Id*.
25. *Id*.
26. *Id*.
27. *Id*.
28. *Id*. at *11.
29. *Id*.
30. The court stated that its interpretation of the Survival Clause was consistent with Delaware precedent, citing the Superior Court's decision in *Sterling Network Exchange, LLC v. Digital Phoenix Van Buren, LLC*, No. 07C-08-050WLW, 2008 WL 2582920 (Del. Super. Ct. Mar. 28, 2008). However, it should be noted that although the *Sterling* court described the survival clause at issue there as a contractual statute of limitations, the court ultimately construed the survival clause as creating a time period during which *notice* of claim had to be given rather than the time during which a claim had to be *filed. See GRT*, 2011 WL 2682898, at *12.
31. *GRT*, 2011 WL 2682898, at *13.
32. *Id*.

Second, contracts may be silent with respect to whether representations and warranties survive or expire at closing. In this circumstance, according to the court, the result is not entirely clear.[33] Accordingly, if the goal is to preserve remedies post-closing for breach of representations and warranties, the court advised that cautious parties should include express language stating that the representations and warranties survive.[34]

Third, contracts may contain a survival period during which the representations and warranties will survive, such as the Survival Clause.[35] The court noted that many commentators believe that the effect of such a clause is to limit the time period during which a claim for breach of representations and warranties may be filed, thus creating a contractual statute of limitations.[36] On the other hand, the court acknowledged that some commentators have suggested that "survival" terminology is less than clear, but the court noted that its analysis was based on the common understanding of the language rather than suggested improvements by commentators.[37]

Fourth, contracts may provide that the representations and warranties will survive indefinitely.[38] Although such provisions could mean that the parties would face indefinite post-closing liability, because of the public policy underlying statutes of limitations and courts' general refusal to permit parties to extend the statute of limitations by contract, the court stated that the "general rule is that in such a situation, courts will treat the indefinite survival of representations and warranties as establishing that the ordinarily applicable statute of limitations governs the time period in which actions for breach can be brought."[39]

Accordingly, the court suggested that, under Delaware law, such a provision would be treated as running with the otherwise applicable statute of limitations.[40] Based on the court's survey of relevant case law and commentary, the court concluded that practitioners generally intend a survival clause to create a contractual statute of limitations.[41]

Business Context of Contract

Finally, the court also considered the context in which the Agreement was negotiated to support its interpretation of the Survival Clause.[42] The court did not find it "plausible" that the parties would have intended the Survival Clause to give the plaintiff four years after the contract closed to bring breach of Design Representation claims (which would have been the result under the plaintiff's

33. *Id.*
34. *Id.*
35. *Id.* at *14.
36. *Id.*
37. *Id.*
38. *Id.* at *15.
39. *Id.*
40. *Id.*
41. *Id.*
42. *Id.* at *16.

interpretation).[43] The court found that if the parties had intended such a result, they would have included the Design Representations in the category of representations that would survive indefinitely.[44]

Conclusion

The court held that, in light of its construction of the Survival Clause as unambiguously establishing a one-year statute of limitations for breach of the Design Representations, the plaintiff's claims with respect to such representations were time-barred and dismissed.[45] The court held that remedial obligations under the contract also expressly terminated after one year.[46]

The court's analysis shows that use of a survival clause, with additional language terminating the remedy for breach of the representations and warranties at the end of the survival period, may be construed as a contractual statute of limitations under Delaware law.

2. *Emposimato v. CIFC Acquisition Corp.* (Breach of Implied Covenant, Anticipatory Breach, and Expectancy Damages)

In its review of opposing motions to dismiss, the New York Supreme Court in *Emposimato v. CIFC Acquisition Corp.*[47] concluded that several triable issues of fact remained with respect to whether a seller's ineffective termination of a stock purchase agreement permitted the buyer to recover expectancy damages.[48]

In 2008, Paul Emposimato and other shareholders ("Sellers") entered into a stock purchase agreement (the "Agreement") with CIFC Acquisition Corp. ("CIFC"), an acquisition entity created by Jefferies Capital Partners IV, L.P., a private equity investment firm ("Jefferies"), whereby Sellers would sell to CIFC all of their stock in Concordia International Forwarding Corp. ("Target").[49] The Agreement provided that closing would occur after (1) Sellers delivered to CIFC disclosure schedules and CIFC acknowledged that, in its sole discretion, it was satisfied with the disclosure schedules and other diligence, and (2) subsequent to such acknowledgement, CIFC had been given access to and completed "Sensitive Diligence" with respect to Target's customers and vendors and other matters.[50] Sellers delivered disclosure schedules on April 14, 2008, and, fifty-three days later, delivered a termination notice because CIFC failed to deliver the acknowledgement.[51] Sellers brought suit seeking both a declaratory judgment that they appropriately

43. *Id.*
44. *Id.*
45. *Id.* at *17.
46. *Id.*
47. No. 601728/2008, 2011 WL 833801 (N.Y. Sup. Ct. Mar. 7, 2011), *aff'd*, 932 N.Y.S.2d 33 (App. Div. 2011).
48. *Id.* at *27.
49. *Id.* at *1.
50. *Id.*
51. *Id.* at *2.

terminated the Agreement and damages for CIFC's and Jefferies' breach of the implied covenant of good faith and fair dealing.[52] CIFC counterclaimed, alleging that Sellers breached the Agreement and that Sellers' unsuccessful attempt to terminate the Agreement was an anticipatory breach entitling CIFC to expectancy damages for the failed acquisition.[53]

Sellers' Claim for Declaratory Relief

In addressing Sellers' first claim, the court issued a declaratory judgment that Sellers' attempt to terminate the Agreement was not authorized under its terms. This declaration—the opposite of the declaratory relief sought by Sellers—was based on the court's determination that the disclosure schedules delivered on April 14 were not final.[54] The court noted that the Agreement required Sellers to deliver a "final version" of the disclosure schedules "in reasonable and customary form."[55] However, when the schedules were transmitted on April 14, the cover e-mail stated that the schedules remained subject to Sellers' review and comment.[56] Additionally, several of the schedules delivered either contained the notation "Need to Discuss" or had not been fully completed as required by the Agreement.[57]

In the absence of any evidence demonstrating Sellers' intent that the April 14 disclosure schedules were to be considered final by CIFC, the court determined that the April 14 schedules were not final.[58] Accordingly, Sellers could not rely on the termination provision that permitted termination thirty days following the delivery of final schedules.[59]

Sellers' Claim for Breach

Sellers also claimed that CIFC and Jefferies breached their implied covenant of good faith and fair dealing by making unreasonable requests for information and failing to deliver the required acknowledgement. CIFC moved to dismiss this claim because Sellers did not properly terminate the Agreement and because Jefferies was not a party to the Agreement.[60]

The court denied CIFC's motion for two reasons. First, the court found that Sellers' ineffective termination of the Agreement and CIFC's and Jefferies' alleged breaches were not mutually exclusive.[61] Second, the court refused to dismiss the claim against Jefferies solely because Jefferies was not a party to the Agreement.[62]

52. *Id*. at *3.
53. *Id*.
54. *Id*. at *9.
55. *Id*. at *3.
56. *Id*.
57. *Id*. at *4–5.
58. *Id*. at *9.
59. *Id*.
60. *Id*. at *10.
61. *Id*.
62. *Id*. at *11.

The court noted Sellers' allegation that CIFC was a "mere shell corporation" with "substantially no assets of its own."[63] The court reasoned that Jefferies could be liable under "principles of corporate veil piercing or alter ego liability"[64] if Sellers met the "heavy burden" of proof for supporting such a claim;[65] however, because the determination of such liability is a highly fact-intensive inquiry, the court denied CIFC's motion to dismiss.[66]

CIFC's Counterclaims for Breach

CIFC counterclaimed that Sellers breached implied and express terms of the Agreement because Sellers were not responsive to CIFC's requests for information. The court stated that CIFC failed to provide sufficient information indicating that CIFC made requests for information and that such information was required to be provided by Sellers under the terms of the Agreement.[67]

CIFC also counterclaimed that Sellers' attempted termination of the Agreement was an actual or anticipatory breach of the Agreement, and as a result, CIFC sought expectancy damages of at least $30 million.[68] The court noted, "As a general rule, a party seeking damages for anticipatory breach or repudiation of a contract may seek either expectancy damages, which are intended to place the party in as good a position as if the contract had been performed, or restitutionary damages, which are intended to place the party in as good a position as if the contract had never been entered into."[69]

CIFC moved for partial summary judgment, and Sellers moved to dismiss CIFC's claim. Both motions were denied by the court. With respect to CIFC's motion for summary judgment, the court determined that CIFC's claim for anticipatory breach would be successful only if CIFC could show that it was "ready, willing and able to perform its obligations" under the Agreement but for Sellers' anticipatory breach.[70] In the court's view, CIFC failed to establish such facts in its moving papers because there remained a number of contingencies and unsatisfied conditions to closing under the Agreement, including that CIFC had not made a prima facie showing that it would have been financially able to close.[71]

Sellers argued for dismissal of CIFC's counterclaim on the basis that the Agreement was a preliminary agreement evidencing an agreement to negotiate in good faith and that expectancy damages would not be permitted.[72] Further, Sellers argued that even if expectancy damages were appropriate, they would be $0 be-

63. *Id.*
64. *Id.*
65. *Id.* (internal quotation omitted).
66. *Id.*
67. *Id.* at *12.
68. *See id.*
69. *Id.*
70. *Id.* at *13.
71. *Id.* at *13–14.
72. *Id.* at *14.

cause the value of the stock on the date of the alleged breach was the same as the consideration recited under the Agreement.[73] The court denied Sellers' motion and found that all of the evidence pointed to the Agreement being final and binding between the parties, despite the fact that there were open items at the time of signing.[74] Additionally, the court stated that because five months had lapsed between signing and the alleged breach, it was not certain that the value of the stock as of the date of the alleged breach was the same as the value on signing.[75]

Finally, the court stated that expectancy damages were not barred due to the Agreement's prohibition of consequential damages because expectancy damages were general damages rather than consequential damages.[76]

Conclusion

Although Sellers' request for declaratory relief was denied, the court permitted cross-claims for breach to proceed to trial.[77] The court found that expectancy damages were permitted in the event of an anticipatory breach and were not barred by a prohibition on consequential damages.[78] The court also determined that the Agreement was final and binding despite certain unresolved items between the parties.[79]

3. *Patriot Rail Corp. v. Sierra Railroad Co.* (Covenants Implied in a Letter of Intent)

In *Patriot Rail Corp. v. Sierra Railroad Co.*,[80] the court addressed, under California law, claims that a potential buyer breached covenants implied in an otherwise non-binding letter of intent and claims of intentional misrepresentation and fraud asserted against both the potential buyer and an individual employee of the potential buyer.[81]

The claims arose following negotiations over the purchase by Patriot Rail Corp. ("Patriot") of Sierra Railroad Company's ("Sierra") short-line railroad operations.[82] Patriot and Sierra signed an NDA in connection with the potential purchase.[83] During the negotiations, Sierra sought a long-term contract to replace the short-term contract that provided rail services to McClellan Business Park ("McClellan") and introduced Patriot to McClellan as a potential buyer of Sierra that could fund Sierra's expansion at the McClellan site.[84] Shortly thereafter, McClellan announced

73. *Id*.
74. *Id*. at *14–23.
75. *Id*. at *25.
76. *Id*. at *24.
77. *Id*. at *14.
78. *Id*. at *24–25.
79. *Id*. at *23.
80. No. 2:09-cv-00009-MCE-EFB, 2011 WL 318400 (E.D. Cal. Feb. 1, 2011).
81. *Id*. at *1.
82. *Id*.
83. *Id*.
84. *Id*.

that it was starting a Request for Proposal ("RFP") process for the long-term contract.[85] Patriot submitted an RFP response and won the contract, and Sierra sued Patriot, claiming, among other things, breach of the NDA.[86]

Sierra dismissed its complaint, however, after Patriot and Sierra agreed to continue their acquisition talks and entered into a letter of intent ("LOI").[87] The parties ultimately terminated their negotiations and further litigation ensued, with Pacific claiming breach of contract, breach of the implied covenant of good faith and fair dealing, fraud and unfair competition, and Sierra counterclaiming on the same bases, as well as for negligent and intentional interference with prospective economic advantage.[88] This opinion addresses Patriot's motion for summary judgment.

Claims Allowed Against the Potential Buyer

A. Implied Covenant of Intent

The court noted that the LOI contained language providing that it was nonbinding, and that accordingly, Patriot's failure to acquire Sierra by itself would not breach the LOI.[89] The court held, however, that the LOI included an implied covenant that Patriot had the intent of purchasing Sierra; the court held specifically that "implied covenants will be found if after examining the contract as a whole it is so obvious that the parties had no reason to state the covenant, the implications arise from the language of the agreement, and there is a legal necessity."[90]

As evidence that Patriot lacked the implied intent to purchase, Sierra cited Patriot's RFP proposal, in which Patriot named a contractor other than Sierra as the group it would partner with on the McClellan project.[91] Sierra argued that Patriot would have named Sierra in its RFP proposal if it had intended to purchase Sierra.[92] The court noted that whether the parties were still in negotiations was not an undisputed fact, and thus not suitable for summary judgment.[93]

B. Implied Covenant of Good Faith and Fair Dealing

The court stated that the obligations under the LOI included the implied covenant of good faith and fair dealing, which could be violated by a "conscious and deliberate act, which unfairly frustrates the agreed common purposes and disappoints the reasonable expectations of the other party," even with respect to a covenant that was merely implied, rather than expressed.[94] The court accordingly denied summary judgment with respect to that claim.[95]

85. *Id*. at *2.
86. *Id*.
87. *Id*.
88. *Id*.
89. *Id*. at *5.
90. *Id*. at *6.
91. *Id*.
92. *Id*.
93. *Id*. at *7.
94. *Id*. (internal quotation omitted).
95. *Id*.

C. Torts, Unfair Competition, and Other Claims

The court allowed claims of intentional and negligent interference with prospective economic advantage to continue, on the basis that Sierra could have won the McClellan contract.[96] Sierra also asserted claims of unfair competition under section 17200 of California's Business and Professions Code, which prohibits any unlawful, unfair or fraudulent act or practice, and which the court stated could be supported by the claims of fraud and breach of implied covenant with respect to the acquisition negotiations.[97] The court also denied Patriot's motion for summary judgment with respect to Sierra's fraud claim.[98]

Claims Allowed Against an Individual Employee

Sierra claimed that misleading statements made by an employee of Patriot induced Sierra to provide the employee with confidential information that he then passed along to Patriot, which aided Patriot in the McClellan RFP, and that the employee had instructed Sierra not to take any action that could "jeopardize the contemplated buyout transaction."[99] The court stated that "in cases involving intentional misrepresentation or fraud, an employee or agent may be individually responsible for the commissions of that tort," and that the employee could be personally liable if he was aware that Patriot lacked the intent to purchase Sierra's operations from Sierra but continued to obtain confidential information.[100]

Conclusion

This case shows that the court may find implied covenants within an otherwise non-binding letter of intent. To find implied covenants, the court will consider whether the alleged implied covenant is so obvious that the parties had no reason to state the covenant, the implications arise from the language of the agreement, and there is a legal necessity to do so.

4. *Hulbert v. Port of Everett* (Indemnification Provisions Do Not Preclude Claim for Contribution Under Environmental Statutes)

In *Hulbert v. Port of Everett*,[101] a seller of land sought a declaration that the agreement pursuant to which the land was sold barred any claims by the buyer for contribution under the Model Toxins Control Act ("MTCA"). The buyer counterclaimed for contribution. The trial court entered summary judgment for the buyer.

96. *Id.* at *9.
97. *Id.* at *10–11.
98. *Id.* at *10.
99. *Id.* at *11.
100. *Id.*
101. 245 P.3d 779 (Wash. Ct. App. 2011).

The Hulberts sold thirty acres of land to the Port of Everett in 1991 through an Agreement of Purchase and Sale (the "Agreement").[102] The Port, according to the court, was "aware that the [p]roperty likely had environmental issues."[103] A certificate (the "Certificate") attached as an exhibit to the Agreement provided that the Hulberts would indemnify the Port for three years against any environmental liability arising from the site.[104] In the Agreement, the Port acknowledged that it had inspected the physical condition of the property and accepted it, subject to the terms and conditions of the Agreement and the Certificate relating to hazardous materials investigation and cleanup.[105] The Port made no claim for indemnification during the three years following the sale.[106]

In 2006 (fifteen years after the signing of the Agreement), the Washington State Department of Ecology required the Port to perform remedial investigation and cleanup work on the property, and the Hulberts were notified that they were potentially responsible for investigation and remediation costs under the MTCA.[107] The Hulberts filed a complaint in the superior court, seeking a declaration that the Agreement barred claims by the Port for MTCA contribution and seeking to enjoin the Port's investigation and remediation pending a determination of the Hulberts' liability.[108] The trial court concluded that the Agreement did not bar MTCA liability and entered final judgment for the Port, including an award of attorney's fees, and the Hulberts appealed.[109]

On appeal, the Hulberts argued, among other things, that the Agreement conditioned the Port's acceptance of the property on the limitations in the Certificate and that its reference to fifteen environmental statutes evidenced the parties' intent to allocate all environmental liability, that the subject matter and circumstances and subsequent acts of the parties demonstrated their intent to preclude MTCA liability, and that there was no intent that the Port intended to reserve an MTCA contribution right.[110]

The Washington Court of Appeals, after noting that parties can allocate their environmental liabilities under the MTCA, held that the Agreement

> does not objectively manifest a mutual intent that the Hulberts, after the termination of the three-year period, would be released from all environmental liability, including under the MTCA or any other statute. Instead, the Certificate simply guarantees the Port that the Hulberts would be responsible for any costs or expenses related to the presence of hazardous substances on the Property for three years following the sale. . . . [I]n the absence of any language indicating that the Port agreed to release or

102. *Id.* at 781.
103. *Id.* at 782.
104. *Id.*
105. *Id.* at 785.
106. *Id.* at 782.
107. *Id.*
108. *Id.*
109. *Id.* at 783.
110. *Id.*

> waive any *other* rights it might have in the future, the Agreement did not preclude a statutory MTCA contribution action after the three years expired.[111]

The court rejected the Hulberts' argument based on the subject matter and objectives of the Agreement, refusing to consider extrinsic evidence to show an intention independent of the contract.[112]

Conclusion

In drafting acquisition agreement provisions allocating responsibility and providing indemnification for environmental conditions and claims, lawyers need to consider not only indemnification issues but also the possibility of statutory claims and related claims for contribution under environmental statutes.

5. *Ventas, Inc. v. HCP, Inc.* (Tortious Interference with Prospective Advantage Claim Against Topping Bidder)

The U.S. Court of Appeals for the Sixth Circuit, in *Ventas, Inc. v. HCP, Inc.*,[113] affirmed a district court's rulings against a purported topping bidder in connection with a $101 million jury award for tortious interference with prospective advantage.[114] The topping bidder eventually withdrew its bid, but the buyer had to increase its offer price to get approval from the target's unitholders, and the jury required the topping bidder to pay the buyer for the aggregate increased price.[115] The court stressed the need to be "circumspect" in reviewing tortious interference claims between competitors, but noted that "the public interest in full and fair competition is furthered by imposing liability . . . for fraudulently leveraging a public market to sabotage a competitor."[116] The court also reversed the district court's ruling that the buyer could not also seek punitive damages, exposing the topping bidder to additional damages.[117]

Background

The suit arose from an auction for Sunrise Senior Living Real Estate Trust ("Sunrise"), a Canadian REIT.[118] Ventas and HCP each signed a standstill agreement prohibiting bids outside the auction process for eighteen months following completion of the auction.[119] As a practical matter, each bidder had to reach an agreement with Sunrise's long-term manager, Sunrise Senior Living, Inc. ("SSL"),

111. *Id.* at 784.
112. *Id.* at 785.
113. 647 F.3d 291 (6th Cir. 2011).
114. *Id.* at 296.
115. *Id.* at 303.
116. *Id.* at 311.
117. *Id.* at 296.
118. *Id.* at 297.
119. *Id.*

before it could make a final bid for Sunrise.[120] Ventas reached an agreement with SSL, but HCP could not.[121] Sunrise eventually accepted Ventas's offer of $15 per share.[122] The price represented a "record-breaking" 50 percent premium, and unitholder approval "seemed to be a foregone conclusion."[123] The Ventas purchase agreement included a no-shop provision and required Sunrise to enforce existing standstill agreements.[124]

One month later, HCP announced, via a press release, a new offer of $18 per share.[125] HCP told Sunrise, but did not disclose publicly, that the bid in fact was subject to reaching an agreement with SSL.[126] Sunrise issued its own press releases, noting HCP's undisclosed condition of reaching an agreement with SSL.[127] Ventas also issued a press release, noting that HCP's bid was in breach of the standstill agreement and was conditional.[128]

Ventas and Sunrise brought actions in Canada with respect to HCP's standstill agreement.[129] The court there held that the standstill agreement precluded HCP from submitting its topping bid and that Sunrise must enforce the standstill agreement against HCP.[130] The Canadian court also found that Sunrise had "acted reasonably in designing and conducting the auction process so as to maximize value."[131] HCP then withdrew its bid.[132]

Ventas was unable to close the acquisition on its original terms, however, as Sunrise unitholders rejected the bid of $15 per share.[133] Ventas responded with a new offer of $16.50 per share, which the Sunrise unitholders approved.[134]

Following the closing, Ventas brought an action in Kentucky, alleging tortious interference with contract and tortious interference with a prospective advantage.[135] The district court dismissed the former claim, but allowed the latter to proceed to trial.[136] A jury found that HCP's actions amounted to tortious interference, with damages equal to the difference between the $15 and $16.50 offers, for an aggregate of $101 million.[137]

120. *Id.*
121. *Id.* at 297–98.
122. *Id.* at 298.
123. *Id.* at 299.
124. *Id.*
125. *Id.*
126. *Id.*
127. *Id.* at 300.
128. *Id.*
129. *Id.* at 301.
130. *Id.*
131. *Id.*
132. *Id.*
133. *Id.*
134. *Id.*
135. *Id.*
136. *Id.* at 302.
137. *Id.*

Opinion

A. Improper Interference

The court noted that Kentucky law generally follows the *Restatement (Second) of Torts*. Under the *Restatement*, as cited by the court, intentional interference arises when one "intentionally and improperly interferes with another's prospective contractual relation,"[138] and, to determine whether that interference is improper, "consideration is given to [among other things] . . . the actor's motive."[139] The court noted that the Kentucky Supreme Court had summarized the test for improper interference as requiring a showing of "malice or some significant wrongful conduct."[140]

The court also noted that claims between competitors require a "more exacting standard."[141] In particular, the *Restatement* provides that competition alone does not constitute improper interference, and that improper interference between competitors will not be found where, among other things, "the actor does not employ wrongful means."[142] The court thus approved the district court's instruction to the jury that in order to find "improper interference" it must find that HCP employed "significantly wrongful means," which includes "conduct such as fraudulent misrepresentation, deceit and coercion," and that to do so, the jury could consider "the parties' conduct, motive and the circumstances of the transaction."[143]

The court found that the evidence was sufficient to support a finding that HCP's "improper interference" caused injury to Ventas, despite HCP's arguments that Ventas had not separated the impact of any misrepresentations by HCP from the impact of HCP's truthful statements.[144] HCP's press release announcing its offer did not say that the offer was conditional on reaching agreement with SSL or that HCP had failed to reach an agreement with SSL during the initial auction process; in fact, HCP's press release stated that the terms of the topping bid were "identical to the transaction entered into by Ventas" and that it had a "greater certainty of completion."[145] HCP never sent Sunrise a signed, unconditional offer, despite verbal assurances by HCP's CEO that a signed agreement had been sent.[146] HCP had indicated that it was interested in "moving on to other things" and, in the midst of its topping bid for Sunrise, had made a $3.1 billion offer for a different company.[147] Sunrise's investor base also changed after HCP announced its topping bid, with new unitholders who "were largely arbitragers from the United States [who] had little incentive" to accept Ventas's original bid even after HCP withdrew the topping bid.[148]

138. *Id.* at 306 (quoting Restatement (Second) of Torts § 766B (1979)).
139. *Id.* (quoting Restatement (Second) of Torts § 767).
140. *Id.* (internal quotations omitted).
141. *Id.* at 306.
142. Restatement (Second) of Torts § 768.
143. *Ventas*, 647 F.3d at 308.
144. *Id.* at 316–18.
145. *Id.* at 315.
146. *Id.* at 300.
147. *Id.* at 298.
148. *Id.* at 317.

B. Breach of Standstill

The court affirmed the district court's decision to allow the jury to give some, though not decisive, weight to HCP's breach of the standstill agreement. The district court instructed the jury that the breach "alone is not sufficient to establish tortious interference" but "may be considered along with the other evidence in determining whether HCP engaged in improper interference."[149] The court rejected HCP's challenge to the jury instructions, noting that the breach "illuminates [HCP's] anti-competitive activities" and "is central to an understanding of Ventas' allegations of fraud and deception."[150]

C. Punitive Damages

The court reversed the district court's holding that Ventas could not seek punitive damages from HCP. Under Kentucky law, punitive damages can be available where a defendant "act[s] toward [a] plaintiff with oppression, fraud, or malice."[151] Here, Ventas was claiming fraud, which Kentucky law defined as "an intentional misrepresentation, deceit, or concealment of a material fact known to the defendant and made with the intention of causing injury to the plaintiff."[152]

In this case, the court stated, "a reasonable jury could conclude that HCP engaged in its fraudulent conduct with the intention of inflicting harm on Ventas."[153] In addition to the misrepresentations by HCP, the court noted that HCP's conduct suggested that "its purported offer . . . was not genuine," given, among other things, that the initial proffered agreement was unsigned, that the CEO then stated that he had sent a signed copy to Sunrise when he in fact had not, and that HCP seemed to be moving "on to other things" with its potential acquisition of another company.[154]

Conclusion

Ventas reiterates the strong public interest in competition. However, it also reminds us that claims of tortious interference, though subject to "heightened scrutiny"[155] when made between competitors, may be supported if a topping bidder is not motivated by a genuine desire to acquire the target and uses wrongful conduct.

A genuine, bona fide bid, even if it breaches a standstill agreement, may benefit shareholders in some ways and does not necessarily support tort claims against the topping bidder. But a bid that is accompanied by misrepresentations and breaches a standstill agreement, and is made primarily to hurt a competitor, may

149. *Id.* at 309 (quoting record).
150. *Id.* at 312.
151. *Id.* at 319 (quoting Ky. Rev. Stat. Ann. § 411.184(2)).
152. *Id.* (quoting Ky. Rev. Stat. Ann. § 411.184(1)(b)).
153. *Id.* at 321.
154. *Id.*
155. *Id.* at 309.

amount to the kind of "wrongful conduct" that supports a claim of tortious interference, and makes the awarding of substantial damages a very real possibility.

6. *Aveta Inc. v. Cavallieri* (Minority Stockholders Bound by Post-Closing Adjustment Provisions of Merger Agreement Despite Not Signing Agreement and Not Having Voted on Merger)

The Delaware Court of Chancery in *Aveta Inc. v. Cavallieri*[156] granted the plaintiff's motion for summary judgment and denied the defendant shareholders' cross-motion for summary judgment, finding that a contractual process for calculating post-closing adjustments to the plaintiff's acquisition price for Preferred Medicare Choice, Inc. ("PMC") was binding on both former PMC stockholders who signed the purchase agreement and on those who did not.

The case before the court was one of numerous, related actions, filed in Delaware and Puerto Rico, arising out of the 2006 acquisition of PMC, a Puerto Rico corporation, by plaintiff Aveta Inc. ("Aveta"), a Delaware corporation.[157] That transaction was approved by holders of PMC's Class A shares, who collectively held a controlling interest in PMC.[158] Holders of PMC's Class B shares held only a minority interest.[159] They were not allowed to vote on the merger and did not sign the agreement governing the transaction (the "Purchase Agreement").[160] Rather, the Purchase Agreement was signed only by the Class A holders.[161]

The Purchase Agreement included a procedure for calculating certain post-closing adjustments, whereby Aveta would initially determine the adjustment amount and then submit its figure for review to one of PMC's former controlling stockholders, Roberto L. Bengoa ("Bengoa"), whom the former controlling stockholders appointed as the Shareholders' Representative (the "Shareholders' Representative").[162] The Purchase Agreement also specified that any dispute over the post-closing adjustments would be settled through binding arbitration by an accounting firm.[163]

After closing, a dispute arose between Aveta and Bengoa regarding determination of the post-closing adjustments.[164] When Bengoa refused to comply with the arbitration provision of the Purchase Agreement, Aveta brought suit in Delaware to compel arbitration (the "Arbitration Action"), and the Court of Chancery entered an order requiring Bengoa to arbitrate.[165]

While Aveta's litigation against Bengoa was pending in the Court of Chancery, certain former PMC stockholders began to dispute Bengoa's authority to represent

156. 23 A.3d 157 (Del. Ch. 2010).
157. *See id.* at 162–64.
158. *Id.* at 163–64.
159. *Id.* at 164.
160. *Id.* at 163–64.
161. *Id.* at 163.
162. *Id.* at 162.
163. *Id.*
164. *Id.* at 165.
165. *Id.* at 166–67.

them. Two groups of those stockholders filed complaints in Puerto Rico challenging the procedures for determining the post-closing adjustments, claiming that a non-binding term sheet signed by Aveta and Bengoa as a framework for potentially resolving their disagreement (the "Total Proposal") novated the Purchase Agreement.[166] Aveta responded by commencing an action in the Court of Chancery against PMC's former controlling stockholders (the "Principal Shareholder Defendants") and PMC's former minority stockholders who had brought the Puerto Rico actions (the "Class B Defendants").[167] The Puerto Rico actions were stayed pending the outcome of the action in Delaware.[168]

Defendants Bound by the Actions of Their Representative

The court first held that both the former Class A and Class B PMC stockholders were bound by Bengoa's actions and that his authority was irrevocable. The court held that the Principal Shareholder Defendants were bound because they had irrevocably appointed Bengoa as their agent.[169] The provision of the Purchase Agreement naming Bengoa as Shareholders' Representative was "clear and unambiguous," and Bengoa's status as a former majority stockholder who would have received merger consideration created an interest sufficient to render his agency irrevocable.[170] The court also recognized a basis to support the irrevocability of Bengoa's agency under *Abercrombie v. Davies*,[171] which held that "parties may agree to and be bound by a provision by which they commit themselves to keep an irrevocable proxy in effect in order that the so-called 'arbitration' provisions of the Agreement may be implemented," and that such an agreement is all the more binding "where a strong element of reliance is involved."[172] The Principal Shareholder Defendants appointed Bengoa as their agent to complete the post-closing adjustments, and Aveta relied on such appointment in negotiating the merger.[173] The principles of *Abercrombie* therefore created a separate basis to find Bengoa's agency irrevocable.

The court's determination that the Class B Defendants were bound by Bengoa's actions turned on corporate law, rather than agency. Under the internal affairs doctrine, Puerto Rico law governed the merger.[174] The court recognized that section 3051 of the Puerto Rico General Corporation Law at the time of the merger paralleled section 251 of the Delaware General Corporation Law as it existed before 1996.[175] Both statutes provided that terms of a merger agreement "may de-

166. *Id.* at 165–77.
167. *Id.* at 167.
168. *Id.*
169. *Id.* at 171.
170. *Id.* at 169.
171. 123 A.2d 893 (Del. Ch. 1956), *rev'd on other grounds*, 130 A.2d 338 (Del. 1957).
172. *Aveta*, 23 A.3d at 169 (quoting *Abercrombie*, 123 A.2d at 906).
173. *Id.* at 170.
174. *Id.* at 168.
175. *Id.* at 171.

pend upon facts ascertainable outside of such agreement," if the procedure for applying such facts were clearly expressed in the agreement.[176] The court engaged in a statutory analysis of the pre-1996 Delaware statute to determine whether the post-closing adjustments were dependent on facts ascertainable outside of the agreement as contemplated by Puerto Rico law. Ultimately, the court concluded that section 3051 as it existed in 2006 would have included the post-closing adjustments as "provisions dependent on 'facts ascertainable outside of the merger agreement,'" and that the Class B Defendants were therefore bound by Bengoa's actions, regardless of Bengoa's authority under principles of agency.[177]

In addition to holding that the defendants were bound by the post-closing adjustments as negotiated by Bengoa, the court rejected the defendants' argument that they should be permitted to intervene in the potential arbitration to resolve the post-closing adjustment dispute.[178] The court concluded that allowing such participation would both run contrary to Aveta's reliance interest in the provisions it had negotiated in the Purchase Agreement and, further, "would rewrite the Purchase Agreement to craft a different set of procedures for determining how certain 'facts ascertainable outside of such agreement . . . shall affect the terms of the agreement.'"[179]

The Total Proposal Did Not Novate the Purchase Agreement

The court next addressed whether the Total Proposal had novated or amended the Purchase Agreement such that the defendants would not be bound by the post-closing adjustments. The court had previously addressed this issue in a 2009 decision holding Bengoa in contempt for refusing to arbitrate, and restated its holding here that the Total Proposal was nothing more than "an unenforceable agreement to agree" and could be read sensibly only in conjunction with the Purchase Agreement.[180] Finding that the Principal Shareholder Defendants were in privity with Bengoa, the court applied the doctrine of res judicata to prevent them from raising the same claim.[181] The court noted that res judicata might also apply to prevent the Class B Defendants from again raising the issue, but concluded that the argument was more appropriately dismissed under stare decisis, as the Class B Defendants had failed to distinguish their claims from those already adjudicated in the previous contempt decision.[182]

The Puerto Rico Actions Breached the Forum Selection Provision in the Purchase Agreement

Having determined that all defendants would be bound by Bengoa's actions, the court next held that defendants had breached the Purchase Agreement by filing

176. *Id.* (quoting P.R. Laws Ann. tit. 14, § 3051(b); citing Del. Code Ann. tit. 8, § 251(b)).
177. *Id.* at 178 (internal quotation omitted).
178. *Id.* at 181.
179. *Id.* (internal quotation omitted).
180. *Id.* at 179.
181. *Id.*
182. *Id.* at 180 (citing Kohls v. Kenetech Corp., 791 A.2d 763, 770 (Del. Ch. 2000)).

suit in Puerto Rico, in violation of its Delaware forum selection provision.[183] The Principal Shareholder Defendants were clearly required to adhere to the forum selection provision by their voluntary decision to sign the Purchase Agreement.[184] The Class B Defendants, who did not sign the Purchase Agreement, nevertheless "bound themselves by their conduct."[185] The court concluded that the Class B Defendants could not have sued in Puerto Rico under the Total Proposal without invoking the terms of the Purchase Agreement, which the Total Proposal allegedly modified.[186] Having done so, and thereby having argued for enforcement of certain provisions of the Purchase Agreement, the Class B Defendants were "estopped from picking only the provisions they like and ignoring the others."[187] Moreover, by attempting to "have it both ways," the defendants forced Aveta into "duplicative and unnecessary litigation."[188] The court therefore held the defendants jointly and severally liable for the fees and expenses Aveta incurred in the Puerto Rico action.[189] The court also awarded Aveta its fees and expenses in the current litigation in accordance with the Purchase Agreement's fee-shifting provision.[190]

Conclusion

Although construing Puerto Rico corporate law, the Court of Chancery's holding referred to section 251 of the Delaware General Corporation Law and appears to confirm that, under Delaware law as well, corporate stockholders can effectively be bound to post-closing adjustment provisions in an agreement, including provisions designating a "stockholder's representative" to resolve disputes on behalf of all stockholders. Stockholders who are not signatories to the agreement will also be bound by post-closing adjustment provisions, so long as those provisions are properly drafted to make the merger consideration dependent on "facts ascertainable outside of such agreement."

The *Aveta* decision, however, did not address efforts to bind non-signatory stockholders through other means or to other aspects of a merger agreement, such as efforts to impose direct contractual indemnification obligations on non-signatory stockholders. Although the Delaware General Corporation Law and the provisions of the Puerto Rico General Corporation Law in effect at the time of the merger at issue in *Aveta* would permit constituent corporations to make any of the terms of a merger agreement dependent upon facts ascertainable outside of the merger agreement, that does not necessarily make it possible to bind non-signatories to contractual obligations in a merger agreement through means other than contractual adjustments to contingent merger consideration.[191]

183. *Id.*
184. *Id.* at 182.
185. *Id.*
186. *Id.*
187. *Id.*
188. *Id.*
189. *Id.*
190. *Id.* at 182–83.
191. For example, another recent Court of Chancery decision—*Roam-Tel Partners v. AT&T Mobility Wireless Operations Holdings Inc.*, No. 5745-VCS, 2010 WL 5276991 (Del. Ch. Dec. 17, 2010)

The decision also confirms that non-signatory stockholders can be bound by a forum selection provision in a merger agreement, and be required to commence any litigation arising under the agreement in the selected forum.

7. *Kevin M. Ehringer Enterprises, Inc. v. McData Services Corp.*; *Denil v. DeBoer, Inc.* ("Best Efforts" in Acquisition Agreements)

Many M&A agreements contain covenants obligating the parties to use their "best efforts" to accomplish specified actions.[192] Some of these agreements define the term "best efforts" in order to provide guidance as to what is meant by "best efforts."[193] Other agreements make a considered effort not to define the term "best efforts." Decisions in 2011 by the Fifth Circuit and the Seventh Circuit illustrate what can happen when "best efforts" is not defined and a dispute arises as to whether a party satisfied the party's obligation to use such efforts.

Fifth Circuit (Texas Law). In *Kevin M. Ehringer Enterprises, Inc. v. McData Services Corp.*,[194] the technology company purchaser of two product lines sued the defendant seller for, *inter alia*, failing to comply with its covenant to use its "best efforts" (an undefined term) to continue to promote, market, and sell the products post-closing and fraudulently inducing it to enter into the purchase agreement when it never intended to use such efforts.[195]

As to the fraudulent inducement claim under Texas law, the Fifth Circuit explained that "mere failure to perform contractual obligations as promised does

(discussed below)—casts doubt on the validity of efforts to utilize a letter of transmittal to impose direct indemnification and other obligations on stockholders who are not parties to the merger agreement but who sign the letter of transmittal. The *Roam-Tel* court held that if a corporation has a legal obligation to pay merger consideration to stockholders pursuant to the terms of a merger agreement and Delaware law, then a letter of transmittal ordinarily will not be effective to impose additional contractual obligations on stockholders who sign it because no consideration exists to support such obligations. *Id.* at *6.

192. *See, e.g.*, Mergers & Acquisitions Comm. of the ABA Section of Bus. Law, Model Stock Purchase Agreement with Commentary §§ 5.7, 6.3, at 211–15, 224 (2d ed. 2010); Comm. on Negotiated Acquisitions of the ABA Section of Bus. Law, Model Asset Purchase Agreement with Commentary § 5.7, at 167–68 (2001) [hereinafter Model Asset Purchase Agreement].

193. *See*, e.g., Model Asset Purchase Agreement, *supra* note 192, § 1.1, at 15. Section 1.1 defines "best efforts" as follows:

> "Best Efforts"—the efforts that a prudent Person desirous of achieving a result would use in similar circumstances to achieve that result as expeditiously as possible, *provided, however*, that a Person required to use Best Efforts under this Agreement will not be thereby required to take actions that would result in a material adverse change in the benefits to such Person of this Agreement and the Contemplated Transactions, or to dispose of or make any change to its business, expend any material funds or incur any other material burden.

Id.

194. 646 F.3d 321 (5th Cir. 2011).

195. *Id.* at 323. The plaintiff also sued for breach of contract, alleging that the defendant failed to use its best efforts in fulfilling its contractual obligations. *Id.* The district court granted summary judgment in favor of the defendant on the plaintiff's breach of contract claim, concluding that the limitation-of-remedies clause prevented the plaintiff from recovering lost profits, which were the only damages the plaintiff sought for the breach of contract claim. *Id.* As a result, the Fifth Circuit did not rule on the plaintiff's breach of contract claim. *Id.*

not constitute fraud but is instead a breach of contract," and "[t]o be actionable as fraudulent inducement, a breach must be coupled with a showing that the promisor never intended to perform under the contract."[196] The court accepted the defendant seller's argument that the plaintiff purchaser could not prove that the defendant had no intent to perform or, more specifically, there was nothing by which to measure the breach and lack of intent to perform because "best efforts" had no precise meaning either in the agreement or under the law.[197]

The Fifth Circuit then concluded that although "'best efforts' provisions may be enforceable under Texas law if they provide some kind of objective goal or guideline against which performance is to be measured, a party cannot prove a fraudulent inducement claim based on a promisor's intent not to perform under a provision that has no objective measure."[198] The "best efforts" provision *sub judice* did not provide a goal or guideline by which the defendant could have been expected to measure its progress.[199] Because the agreement's use of the term "best efforts" was too indefinite and vague to provide a basis for enforcement as a matter of Texas law, the Fifth Circuit decided that the issue should not have been submitted to the jury.[200] The Fifth Circuit suggested that "as promptly as practicable" would be a sufficient guideline to make a "best efforts" obligation enforceable.[201]

Seventh Circuit (Wisconsin Law). In *Denil v. DeBoer, Inc.*,[202] the meaning of "best efforts" (not defined) was construed in the context of an agreement that required the parties to use their "best efforts" to enter into an agreement for the sale of a minority interest in a business.[203] The sale was to have been to two individuals who had taken over management of the business under an employment contract that provided that their employment could be terminated if they failed to purchase the stock of the controlling stockholder without paying the severance amount that would have been due if they were terminated without cause.[204]

The buy-sell contract was never signed, and the two individuals were fired as a result, and did not receive the severance payment that would have been due if they had been discharged without cause.[205] The two former employees sued for breach of contract.[206]

The Seventh Circuit noted that the term "best efforts" was not defined, and the parties offered no evidence of communications during negotiation to assist

196. *Id.* at 325.
197. *Id.* at 326.
198. *Id.* at 327 (citing Herrmann Holdings Ltd. v. Lucent Techs. Inc., 302 F.3d 552 (5th Cir. 2002); CKB & Assocs., Inc. v. Moore McCormack Petroleum, Inc., 809 S.W.2d 577 (Tex. App. 1991)). The Fifth Circuit did note that the terms "goal" or "guideline" need not be read narrowly. *Id.* at 326.
199. *Id.* at 327.
200. *Id.*
201. *Id.* at 326 (citing *Herrmann*, 302 F.2d at 559).
202. 650 F.3d 635 (7th Cir. 2011).
203. *Id.* at 637.
204. *Id.*
205. *Id.*
206. They sought reinstatement or the money due to them if terminated without cause, the opportunity to invest in deBoer, and also brought a claim for tortious interference with contract. *Id.* at 637–38.

the court in ascertaining the intent of the parties.[207] In rejecting the employees' contention that the controlling shareholder did not fulfill its promise to use "best efforts" to reach agreement on a buy-sell contract, the court noted that agreements to agree are not enforceable in Wisconsin.[208] The court considered if the best efforts undertaking is not an agreement to agree, it might have been intended as an agreement to engage in good-faith bargaining toward a contract, but if that is the meaning of the "best efforts" clause at issue, then both sides performed as required by exchanging many proposals and making counterproposals over the six-month negotiation period.[209] Here, the fact that one final disagreement over a business issue could not be bridged does not imply that either side failed to bargain in good faith.[210] Summary judgment for the defendants was affirmed by the Seventh Circuit.[211]

Conclusion

Courts struggle over the intent of parties who agree to exert "best efforts." While courts may be willing to enforce such provisions, some courts may find that such provisions, if not defined, in effect are unenforceable. Parties that wish to have greater certainty are well-advised to define or at least include some parameters for measuring "best efforts."

8. *Romtec v. Oldcastle Precast, Inc.* (Breach of Good Faith Negotiation Covenant; Expectancy Damages for Breach of Letter of Intent)

In *Romtec v. Oldcastle Precast, Inc.*,[212] the U.S. District Court for the District of Oregon denied the defendant's motion to dismiss a claim brought by the plaintiff seeking consequential damages resulting from breach of an obligation to negotiate in good faith contained in a letter of intent.[213]

In January 2008, Romtec Utilities Inc. ("Romtec"), an Oregon corporation, was engaged in discussions with Oldcastle Precast, Inc. ("OPI"), a Washington corporation wholly owned by Oldcastle Inc., regarding OPI's potential acquisition of Romtec.[214] On January 25, Romtec received a "Valuation and Outline Proposal" from OPI, which provided that any potential acquisition by OPI of Romtec would be contingent upon formal agreements, including a stock purchase agreement, as

207. *Id.* at 638.
208. *Id.*
209. *Id.* The Seventh Circuit also noted that a best efforts clause generally requires one party to make appropriate investments for another's benefit; however, that is not at all what it means in a negotiation context, such as the one in this case. *Id.*
210. *Id.*
211. *Id.*
212. No. 08-06297-HO, 2010 WL 4978980 (D. Or. Dec. 2, 2010).
213. *Id.* at *1.
214. *Id.* at *2.

well as approval of the OPI group president.[215] Romtec agreed to the terms of the proposal, including the stated conditions.[216]

In March 2008, Romtec executed a letter of intent ("LOI") and an offer letter ("Offer Letter").[217] Both were prepared by an OPI vice president on behalf of OPI, setting forth the parameters for the negotiation of the potential purchase of Romtec's shares by OPI.[218] The LOI stated, in relevant part:

> This letter confirms that [Oldcastle] and Tim Bogan (Seller) have agreed to negotiate with respect to the terms for a sale of the stock of [Romtec] on the basis of the attached offer letter dated March 24, 2008. Further, this letter of intent is non-binding and no party will have any legally enforceable obligation to proceed with such sale of the stock of [Romtec] until definitive agreements are executed and delivered. Both parties will use good faith effort to consummate the transaction based on this Letter of Intent. If an agreement is not signed, there will be no break-up fee due either party.[219]

After the execution of the LOI and the Offer Letter, the parties began negotiating the terms of the proposed stock purchase.[220] Between April 18, 2008, and June 9, 2008, counsel to Romtec and OPI negotiated, drafted, and exchanged various transaction documents, including the stock purchase agreement.[221] On May 19, 2008, OPI's president submitted to Oldcastle Inc. documentation pertaining to the proposal and acquisition rationale for the prospective purchase of Romtec's shares.[222] Oldcastle Inc., a wholly owned subsidiary of CRH plc ("CRH"), forwarded the proposal to CRH on May 29, 2008, and then, based on comments from CRH, submitted a revised proposal to CRH on June 5, 2008.[223] Shortly after receiving the revised proposal, a financial analyst with CRH indicated that there was a possible problem with the acquisition.[224]

Nevertheless, on June 9, 2008, counsel for OPI e-mailed Romtec a revised version of the stock purchase agreement, saying: "Please note that the stock purchase agreement remains subject to Oldcastle's review and internal approval processes. However, I have deleted the document number in the footer of the signature pages so you can have it signed tomorrow to hold pending the signing and closing if that is convenient for you."[225]

Two days after receiving the revised stock purchase agreement, Romtec's counsel sent signed copies of the documents to OPI's counsel.[226] On June 13, 2008, OPI's counsel wrote to Romtec indicating that he had reviewed the signed

215. *Id.*
216. *Id.*
217. *Id.*
218. *Id.*
219. *Id.*
220. *Id.*
221. *Id.*
222. *Id.*
223. *Id.*
224. *Id.* at *3.
225. *Id.*
226. *Id.*

documents sent to OPI "to hold in escrow pending signing and closing" and then on June 19, 2008, wrote again stating "once we have approval we can move very quickly . . . since all contracts etc. have been finalized."[227]

On July 1, 2008, the CEO of CRH informed OPI that CRH was not approving the proposed acquisition of Romtec's shares, and on July 2, 2008, OPI informed Romtec that CRH was not going to approve the transaction.[228]

Breach of Covenant of Good Faith

Romtec filed suit against OPI seeking declaratory relief, specific performance, and damages alleging that OPI breached an agreement to purchase all outstanding shares of Romtec. OPI moved for summary judgment, which on January 12, 2010, the court denied.[229] After an unsuccessful attempt by the parties to settle the case, Romtec filed an amended complaint on August 4, 2010.[230] OPI moved to dismiss Romtec's fourth claim in the amended complaint in which Romtec sought expectancy damages of $5.9 million, plus interest from July 2, 2008, until paid.[231]

Expectancy Damages

OPI argued that "expectancy damages are not available *as a matter of law* for the breach of a letter of intent," asserting that under Oregon law the only damages available for a breach of a letter of intent are reliance damages.[232] Romtec disagreed with the defendant's analysis of cited case law, arguing that consequential damages are available because the parties agreed in the letter of intent that they would use good faith efforts to consummate the transaction.[233] Because OPI refused to sign the contract documents that it had drafted, it breached that duty.[234] Romtec further argued that because the promise to use good faith efforts to consummate the transaction was expressly binding on both parties, all of the plaintiff's consequential damages flowing from a breach of that promise are recoverable.[235]

The court generally agreed with Romtec, concluding that where a letter of intent imposes a binding obligation to negotiate in good faith and a defendant breaches that duty, a plaintiff may recover expectancy damages when those damages are reasonably certain and there is no agreement limiting the parties' liability for those damages.[236] The question of whether the LOI actually obligated the defendant to

227. *Id.* (ellipses in original).
228. *Id.*
229. *Id.* at *1.
230. *Id.*
231. *Id.*
232. *Id.* (emphasis added) (quoting Def.'s Memo. Supp. of Mot. to Dismiss Pl.'s Fourth Claim for Relief in the Am. Compl. ¶ 3); *id.* at *3 (citing Logan v. D.W. Sivers Co., 169 P.3d 1255 (Or. 2007) (holding the plaintiff could not recover consequential damages because the damages sought did not result from the defendant's breach of any of its binding obligations under the letter of intent)).
233. *Id.* at *3.
234. *Id.*
235. *Id.*
236. *Id.* at *3–4.

use good faith efforts to consummate the transaction was not before the court and so the ruling did not address that question.

The court stated that, as a matter of law in Oregon, if a plaintiff can prove that but for the defendant's bad faith the parties would have made a final contract, then the loss of the benefit of the contract is a consequence of the defendant's bad faith and, provided it is foreseeable, the defendant may be liable for the plaintiff's consequential damages.[237] The court noted that the LOI contained certain conditions related to the consummation of the acquisition, but none of the conditions limited the parties' consequential damages resulting from a breach of the obligation to use good faith efforts to consummate the transaction.[238]

Conclusion

The court's decision confirmed that a plaintiff's damages arising from a primarily non-binding letter of intent are not limited to reliance damages as a matter of law. Where the letter of intent is found to contain a binding obligation, including an obligation to use good faith efforts to consummate the transaction, and any damages resulting from a breach of such a binding obligation are not limited by the parties, a breach of that binding obligation allows the plaintiff to recover expectancy damages, provided such damages may reasonably have been within the contemplation of both parties at the time of the formation of the agreement as the proximate and natural consequence of a breach by the defendant.

9. *Roam-Tel Partners v. AT&T Mobility Wireless Operations Holdings Inc.* (Minority Stockholder Permitted to Rescind Waiver of Appraisal Rights Despite Signing Letter of Transmittal and Being Sent Merger Consideration)

In *Roam-Tel Partners v. AT&T Mobility Wireless Operations Holdings Inc.*,[239] the Delaware Court of Chancery granted petitioner Roam-Tel Partners' motion to determine the members of an appraisal class filed in connection with a post-merger appraisal action under Delaware's appraisal statute, section 262 of the Delaware General Corporation Law.[240] In granting the motion, Vice Chancellor Strine held that even though a stockholder signs a letter of transmittal waiving its right to an appraisal and is sent a check for the merger consideration, the stockholder may nevertheless rescind that waiver and perfect its appraisal rights if it makes the appraisal demand within the statutory election period and does not actually accept the merger consideration.[241]

The appraisal action arose from a short-form merger in which AT&T Mobility Wireless Operations Holdings Inc. ("AT&T Mobility"), the controlling stock-

237. *Id.* at *4.
238. *Id.*
239. No. 5745-VCS, 2010 WL 5276991 (Del. Ch. Dec. 17, 2010).
240. *Id.* at *1.
241. *Id.* at *14.

holder of St. Cloud Cellular Telephone Co. ("St. Cloud"), cashed out St. Cloud's minority stockholders.[242] On July 22, 2010, several days after consummation of the merger, AT&T Mobility sent an appraisal rights notice (the "Notice") to St. Cloud's minority stockholders in accordance with section 262.[243] The Notice informed minority stockholders of their right to demand appraisal within twenty days of the mailing of the Notice.[244] If stockholders chose not to opt for appraisal, the Notice instructed them to complete and submit to AT&T Mobility the attached letter of transmittal (the "Letter of Transmittal"), as well as to attach their stock certificates.[245] In return, AT&T Mobility would provide those stockholders with the merger consideration.[246]

ARAP Partners ("ARAP"), which owned 5,154 St. Cloud shares before the merger, contacted AT&T Mobility after receiving the Notice and requested the contact information for other St. Cloud minority stockholders.[247] AT&T Mobility denied ARAP's request.[248] Thereafter, on July 30, 2010, ARAP submitted its signed Letter of Transmittal, along with its stock certificate, to AT&T Mobility.[249] On August 5, AT&T Mobility canceled ARAP's stock certificate and mailed ARAP a check for $307,642.26, which represented the merger consideration for ARAP's stock.[250]

In the same week, a representative of Roam-Tel Partners contacted ARAP to advise that a group of minority stockholders planned to file an appraisal action.[251] Based on that information, ARAP mailed a letter to AT&T Mobility on August 9, and informed it of ARAP's demand for appraisal.[252] Two days later, the deadline for making a timely appraisal demand, ARAP sent back the uncashed merger consideration check to AT&T Mobility by overnight mail.[253] AT&T Mobility rejected ARAP's return of the consideration and appraisal demand.[254]

Roam-Tel Partners subsequently commenced an appraisal action in the Delaware Court of Chancery under section 262, and filed a motion requesting the court to determine the members of the appraisal class, arguing that ARAP should be included in the class.[255]

242. *Id.* at *1.
243. *Id.*
244. *Id.*
245. *Id.*
246. *Id.*
247. *Id.* at *2.
248. *Id.*
249. *Id.*
250. *Id.*
251. *Id.*
252. *Id.*
253. *Id.*
254. *Id.*
255. *Id.*

The Letter of Transmittal Was Not a Valid Contract Because No Consideration Existed

The Court of Chancery first rejected AT&T Mobility's argument that AT&T Mobility and ARAP entered into an enforceable contract when ARAP signed the Letter of Transmittal and sent its stock certificate to AT&T Mobility.[256] Because AT&T Mobility effected a short-form merger and cashed out the minority stockholders, it had the legal obligation to pay each minority stockholder the merger consideration.[257] Accordingly, the two parties did not form a valid contract when ARAP signed the Letter of Transmittal because no consideration existed for ARAP's alleged promise to accept the merger consideration to the exclusion of a demand for appraisal.[258]

Surrendering Stock Certificate Did Not Forfeit Appraisal Rights

The court also rejected AT&T Mobility's argument that physical possession of the stock certificate by a stockholder is necessary on the date such stockholder makes demand for an appraisal.[259] The court examined the requirement in section 262(a) that a stockholder "hold shares of stock" in the corporation on the date it made its demand for an appraisal.[260] The court explained that the term "stockholder," in a case where the effect of a short-form merger was immediately to cancel the minority investors' shares, included "those stockholders of record who held shares immediately before the effective date of the short-form merger."[261] The court thus found that the key requirement for making an appraisal demand was not physical possession of the stock certificate, but rather that the stockholder "was a record owner of the shares for which he is making an appraisal demand on the last day anyone could have been a record owner of those shares and did not later purport to sell his statutory right to accept the merger consideration or seek appraisal."[262]

Stockholder Validly Withdrew Earlier Waiver of Appraisal Rights

Vice Chancellor Strine next rejected AT&T Mobility's argument that ARAP irrevocably waived its statutory right to an appraisal when it signed and mailed

256. *Id.* at *6.
257. *Id.*
258. The court recognized that situations might occur where a surviving corporation offers something in excess of what a minority stockholder is statutorily entitled to receive in exchange for the minority stockholder's waiver of its right to an appraisal. Under those circumstances, the court noted, an enforceable contract would arise because the waiver is supported by consideration. *See id.*
259. *Id.*
260. *Id.* at *7 (quoting Del. Code Ann. tit. 8, § 262(a)).
261. *Id.*
262. *Id.*

the Letter of Transmittal, along with its stock certificate, to AT&T Mobility in exchange for the merger consideration.[263] The court held that AT&T Mobility suffered no prejudice and that public policy supported permitting ARAP to rescind its waiver under the circumstances.[264]

The Vice Chancellor discussed the equitable doctrines of waiver and estoppel, observing that waiver is a unilateral action not requiring detrimental reliance, while estoppel involves an element of reliance.[265] "[E]quitable estoppel arises when, by its conduct, a party intentionally or unintentionally leads another, in reliance on that conduct, to change position to his detriment."[266] The court explained that a party may retract a waiver before the other party materially changes his position in reliance, but if estoppel exists, the waiving party may not revoke its waiver.[267]

The Vice Chancellor determined that AT&T Mobility suffered no prejudice as a result of ARAP's decision to change its mind.[268] The court emphasized AT&T Mobility's admission that it suffered no prejudice, ARAP's prompt return of the uncashed merger consideration check, and ARAP's demand for appraisal within the twenty-day statutory election period.[269] Vice Chancellor Strine explained that, at most, AT&T Mobility would suffer "the disappointment of seeing an appraisal class grow, having believed that it faced no risk because that stockholder had earlier indicated a desire to forgo an appraisal."[270] The court did not believe "psychic injury" to a non-human corporation amounted to the sort of reliance necessary to justify denying a stockholder the chance to change its mind within the statutory election period.[271] Nevertheless, the court recognized the potential for a claim of detrimental reliance if ARAP "cashed or further negotiated the check."[272]

The court also emphasized that the appraisal statute limits prejudice to the surviving corporation in the context of a short-form merger by affording stockholders only twenty days after the mailing of the appraisal rights notice to make an appraisal demand.[273] The court explained that ARAP's conduct was consistent with the "basic principle underlying the appraisal statute" because it made an election during the statutorily prescribed twenty-day period.[274] The court distinguished ARAP's conduct from cases in which stockholders lost their right to appraisal by accepting the merger consideration, explaining that ARAP never "took the merger consideration in the sense that [it] exercised dominion over it and then sought to reverse course."[275]

263. *Id.* at *9.
264. *Id.*
265. *Id.*
266. *Id.*
267. *Id.*
268. *Id.* at *9–10.
269. *Id.* at *10.
270. *Id.*
271. *Id.*
272. *Id.*
273. *Id.* at *11.
274. *Id.* at *12.
275. *Id.*

Conclusion

While the Court of Chancery's conclusion in *Roam-Tel Partners* that a stockholder who waives appraisal rights can withdraw the waiver in certain circumstances is significant in itself, the decision has important implications that may extend beyond the context of appraisal rights waivers. The principle that an otherwise valid waiver can be revoked in the absence of detrimental reliance by the non-waiving party may have consequences outside the statutory appraisal context.[276]

Similarly, the holding that no consideration exists sufficient to make a letter of transmittal a binding contract may apply to other circumstances in which the parties to a merger agreement attempt to impose obligations, through a letter of transmittal, on stockholders who are not signatories to the merger agreement, such as obligations to indemnify the acquirer for breaches of representations and warranties by the target corporation.

10. *Meso Scale Diagnostics, LLC v. Roche Diagnostics GmbH* (Reverse Triangular Merger May Constitute Assignment by Operation of Law)

In *Meso Scale Diagnostics, LLC v. Roche Diagnostics GmbH*,[277] the Delaware Court of Chancery denied the defendant's motion to dismiss claims that the defendant breached the non-assignment provision of an agreement. In doing so, the court held that a reverse triangular merger may constitute an assignment by operation of law, at least where the plaintiff alleges that more than a mere change of ownership has occurred.

The plaintiff Meso Scale and the defendants—Roche, IGEN, and BioVeris—were parties to a series of agreements relating to the plaintiff's license rights to technology owned by IGEN.[278] In one of these agreements—the Global Consent—the plaintiff consented to a transaction whereby BioVeris obtained IGEN's assets subject to the license rights held by the plaintiff.[279] The Global Consent provided: "Neither this Agreement nor any of the rights, interests or obligations under this Agreement shall be assigned, in whole or in part, by operation of law or otherwise by any of the parties without the prior written consent of the other parties."[280]

Roche subsequently acquired BioVeris through a reverse triangular merger without first seeking consent from Meso Scale.[281] Meso Scale claimed breach of contract, alleging that the merger constituted an assignment by operation of law

276. *See* Amirsaleh v. Bd. of Trade of the City of New York, Inc., 27 A.3d 522 (Del. 2011) (holding, based on principles articulated in *Roam-Tel Partners*, that corporation had waived deadline for submitting elections to receive cash or stock merger consideration and had not validly rescinded the waiver before the plaintiff submitted an otherwise untimely election form).

277. No. 5589-VCP, 2011 Del. Ch. LEXIS 61 (Del. Ch. Apr. 8, 2011).

278. *Id.* at *9–10.

279. *Id.* at *16.

280. *Id.* at *29.

281. *Id.* at *21.

of BioVeris's intellectual property, thereby requiring Meso Scale's consent.[282] The defendant filed a motion to dismiss, arguing that a change in control of a continuing corporation, as occurred with respect to BioVeris, is not an assignment by operation of law or otherwise.[283]

Reverse Triangular Merger as Potentially an Assignment by Operation of Law

The defendant argued that the mere acquisition of a corporation does not involve an assignment by operation of law of the rights and obligations of the corporation, as long as the corporation's form and contractual responsibilities are preserved.[284] The defendant analogized the reverse triangular merger at issue to a stock acquisition where the Delaware courts have held that where an acquirer purchases the stock of a corporation, that purchase does not, in and of itself, constitute an assignment to the acquirer of any contractual rights or obligations of the corporation whose stock is sold.[285]

The plaintiff, on the other hand, alleged that as a general matter in the corporate context, the phrase "assignment by operation of law" would commonly be understood to include a merger.[286] Moreover, the plaintiff alleged that more than a mere change in ownership of BioVeris had occurred. In particular, soon after the merger was completed, the defendant laid off all BioVeris employees, vacated the company's facilities, and notified customers that product lines were being discontinued, "leaving BioVeris as nothing more than a holding company for [Roche's] intellectual property and license rights."[287] Accordingly, the plaintiff argued that "by operation of law" was intended to cover mergers that effectively operated like an assignment, even if it might not apply to mergers merely involving a change of control.[288]

The court found that the parties offered competing, but reasonable, constructions of the term "by operation of law" and, therefore, found that term within the Global Consent to be ambiguous. The court refused to grant the defendant's motion to dismiss.[289] Although the court did not decide the case on the merits, its ruling shows that a reverse triangular merger may trigger a consent requirement in a non-assignment clause when the merger results in more than a mere change in ownership.[290]

282. *Id.* at *22–23.
283. *Id.* at *23.
284. *Id.* at *37.
285. *Id.* at *40–43.
286. *Id.* at *47.
287. *Id.* at *22.
288. *Id.* at *52.
289. *Id.* at *46 ("While Roche's construction of 'by operation of law' is reasonable, it has cited no Delaware case that holds that [a reverse triangular merger] in circumstances comparable to this case cannot constitute an assignment by operation of law. In addition, the plaintiff has alleged specific facts in support of its allegation that more than a mere change of ownership occurred with regard to BioVeris as a result of the Merger. Thus, while I find Roche's construction reasonable, it is not necessarily the only reasonable interpretation.").
290. *Id.* at *51.

Potentially Broad Construction of Rights Arising "Under" an Agreement

Also of note, the court refused to take a narrow view of what constitutes a right "under" an agreement. The text of the non-assignment clause at issue in the Global Consent stated that none of the rights, interests, or obligations "under this Agreement" shall be assigned by operation of law or otherwise.[291] The defendant argued that the plain meaning of "under" in the phrase "under this Agreement" is that the non-assignment clause applied only to the rights, interests, and obligations created or established by the Global Consent (the contract that included the non-assignment clause at issue), not those created or established by other contracts.[292] Because rights, interests, and obligations relating to BioVeris's patents and licenses arose from contracts executed earlier or contemporaneously, and not from the Global Consent, the defendant argued that those patents and licenses were not subject to the non-assignment clause.[293]

The plaintiff, on the other hand, argued that "under" means "within the grouping or designation of."[294] It contended that the non-assignment clause incorporated by reference all of the rights, interests, and obligations concerning the patent agreements and that the rights, interests, and obligations created by other contemporaneous transaction documents also would come "under" the non-assignment clause's umbrella.[295] The court refused to resolve this ambiguity at the motion to dismiss stage, finding that both constructions were reasonable and leaving open the possibility that the term "under" could be interpreted very broadly in future proceedings.[296]

Conclusion

Although only a ruling on a motion to dismiss, and thus not on the merits, the court's holding suggests that, in some circumstances, a reverse triangular merger may constitute an assignment by operation of law, at least where the plaintiff alleges that more than a mere change of ownership has occurred.

11. *Monty v. Leis* (*Omnicare* Issues and Fiduciary Termination Rights in Certain Agreements)

In *Monty v. Leis*,[297] the California Court of Appeal held that a corporation may grant option rights for more shares than are authorized by the articles of incorporation at the time the option is granted.[298] The court further held that, assum-

291. *See id*. at *29.
292. *Id*. at *31.
293. *Id*.
294. *Id*. at *32 (quoting Pl.'s Opp. to Def.'s Mot. to Dismiss 18).
295. *Id*.
296. *Id*. at *34.
297. 193 Cal. App. 4th 1367 (2011).
298. *Id*. at 1373.

ing a transfer of the majority of corporate stock constituted a "sale or transfer of substantially all of [the] corporation's assets," the purchaser of that stock could by itself approve the transaction after the transfer.[299] Finally, the court concluded that the company's board of directors (the "Board") was not required to include in a stock purchase agreement a "fiduciary out" provision allowing the corporation to avoid the agreement if the corporation received a better offer before the closing.[300]

Facts

Pacific Capital Bank ("PCB"), a California corporation, suffered significant losses in the real estate loan market, and the Office of the Comptroller of the Currency and the Federal Reserve Bank required it to improve its capital position by a certain deadline, or risk seizure by federal regulators followed by liquidation.[301] To improve its capital position, PCB first amended its articles of incorporation to increase its authorized common stock from 100 million to 500 million shares.[302] The amendment was approved by PCB's shareholders.[303] PCB then entered into an investment agreement with Ford Financial Fund, LP ("Ford"), whereby Ford agreed to provide $500 million in new capital in exchange for 225 million shares of common stock and 455,000 shares of preferred stock (the "Agreement").[304] The preferred stock was convertible to 2.275 billion shares of common stock.[305] Whereas the initial 225 million and 455,000 shares of common and preferred stock, respectively, were authorized by the newly amended articles, the 2.275 billion shares of common stock were not.[306] PCB's articles, however, authorized the Board to issue "blank check" preferred stock—that is, stock that could be issued subject to any rights and conditions the Board might deem proper.[307] Neither the Agreement nor the issuance of the preferred stock convertible into 2.275 billion shares of common stock was approved by the then-existing shareholders.[308]

Certain shareholders sought a preliminary injunction enjoining the closing of the Agreement and, alternatively, rescission in case the Agreement closed.[309] The trial court denied the injunction.[310] PCB issued the new shares of common and

299. *Id.*
300. *Id.* at 1374–75.
301. *Id.* at 1370.
302. *Id.*
303. *Id.*
304. *Id.*
305. *Id.*
306. *Id.*
307. *Id.*
308. *Id.* PCB decided not to seek shareholders' approval apparently because it was facing pressure to close the transaction quickly and obtain the funding before the mandated deadline to improve its capital position. *Id.* In fact, PCB, whose shares were traded on the NASDAQ exchange, was required by the NASDAQ rules to obtain shareholders' approval of the investment transaction. *See id.* PCB, however, obtained an exemption from NASDAQ on the ground that the potential delay in obtaining shareholders' approval would threaten the financial viability of the company. *Id.* at 1370–71.
309. *Id.* at 1371.
310. *Id.*

preferred stock pursuant to an exemption for threats to financial viability from NASDAQ rules that otherwise would have required a shareholder vote.[311] The new common shares gave Ford ownership of a majority of PCB's stock, which Ford then voted to amend PCB's articles to authorize the issuance of the 2.275 billion shares of common stock on the conversion of the new preferred shares.[312] The shareholders appealed, and the Court of Appeal affirmed.[313]

Analysis

The Legality of a Stock Acquisition Transaction Is Moot and Will Not Be Set Aside on Appeal After the Trial Court's Refusal to Issue Preliminary Injunction

The court held the appeal was moot because the transaction closed after the trial court denied the issuance of the preliminary injunction.[314] The court relied on Second Circuit and district court decisions for the proposition that the substantial changes in the structure and status of a business after the closing of a merger or acquisition render the return to the initial status quo difficult and so the legality of the transaction is moot.[315] The court emphasized that setting aside the Agreement would require, at a minimum, the return to Ford of $500 million plus interest, and the "loss of so much capital would undoubtedly cause federal regulators to seize the bank and liquidate its assets."[316]

Notwithstanding this finding, however, the court, at the shareholders' request, went further and addressed the merits of the shareholders' argument.

Grant of Option Rights for More Shares than the Corporation Was Then Authorized to Issue Was Not Improper

The court rejected the shareholders' argument that the investment agreement improperly required PCB to issue more shares than were authorized by its articles in violation of California Corporations Code section 405(a).[317] The court found that nothing in that section required an amendment of the articles at the time the option rights were granted, and that the articles could therefore be amended

311. *See id.*
312. *See id.*
313. *See id.* at 1375.
314. *Id.* at 1371–72.
315. *Id.* (citing Bank of New York Co. v. Ne. Bancorp, Inc., 9 F.3d 1065, 1066–67 (2d Cir. 1993); FTC v. Exxon Corp., 636 F.2d 1336, 1342–43 (D.C. Cir. 1980)). "'Mergers and acquisitions are often followed by a commingling of assets and other substantial changes in the structures of the enterprises involved. Once those changes occur, it is often impossible . . . to compel a return to the status quo, and the legality of the challenged merger or acquisition may become essentially a moot question.'" *Id.* at 1372 (ellipses in original) (quoting *FTC*, 636 F.2d at 1342).
316. *Id.* at 1372.
317. *Id.* Section 405(a) provides: "If at the time of granting option or conversion rights or at any later time the corporation is not authorized by its articles to issue all the shares required for the satisfaction of the rights, if and when exercised, the additional number of shares required to be issued upon the exercise of such option or conversion rights shall be authorized by an amendment to the articles." Cal. Corp. Code § 405(a) (West 1990).

to authorize additional shares at any later time, including after the closing of the Agreement.[318]

Because Ford became a majority shareholder after the closing, Ford's vote alone was sufficient to amend the articles to authorize the additional shares necessary to exercise its conversion rights.[319] Accordingly, both the grant of the option rights for more shares than PCB was authorized at the time to issue and Ford's subsequent amendment of the articles to authorize the additional shares were proper.[320]

The Investment Agreement Did Not Require Shareholders' Approval Prior to Closing

The court next rejected the shareholders' argument that the sale of up to 91 percent of PCB's stock under the Agreement must have been approved by the existing shareholders.[321] First, the court found that the Agreement did not amount to "a sale or transfer of substantially all of [PCB's] assets" subject to shareholders' approval under California Corporations Code section 1001(a).[322] The court noted that the only authority cited by the shareholders for that proposition involved a sale of tangible assets, rather than stock, and was therefore distinguishable.[323] Moreover, the court stated that even if section 1001(a) did apply, it allowed approval by the shareholders "either . . . before or after the transaction," and thus Ford would have been able to approve the transfer after the sale.[324]

The Board Did Not Violate Its Fiduciary Duty by Not Including a "Fiduciary Out" Provision in the Agreement

Finally, the court rejected the shareholders' contention that PCB's Board breached its fiduciary duty by failing to include a "fiduciary out" provision that would have allowed PCB to "back out" of the deal if a better offer were received.[325]

The court declined to follow the Delaware Supreme Court case of *Omnicare, Inc. v. NCS Healthcare, Inc.*[326] which, according to the shareholders, required a board

318. *Monty*, 193 Cal. App. 4th at 1372–73. The court apparently read the words "at any later time" to modify the clause "the additional number of shares required to be issued upon the exercise of such option or conversion rights shall be authorized by an amendment to the articles." *Id.* ("The subdivision recognizes that there may be a lapse of time between the granting of the option or conversion rights and the exercise of the rights. It clearly does not require that the articles be amended at the time of the granting of the option or conversion rights. It states, 'If at the time of granting option or conversion rights *or at any later time* . . . .' Nothing in section 405, subdivision (a) requires an amendment of the articles at the time the option or conversion rights are granted." (ellipses in original)). The court dismissed Shareholders' argument that the phrase "at any later time" contemplated a situation where the number of shares was sufficient at the time the option or conversion rights were granted but later decreased so as to be insufficient to satisfy the option or conversion rights. *Id.* at 1373 ("Certainly that is one situation where the phrase 'or at any later time' applies. But nothing in section 405 limits its application to that situation."). Although questionable, the court's interpretation of section 405(a) represents the current state of law in California.

319. *Id.* at 1373.

320. *See id.*

321. *Id.*

322. *Id.* (quoting CAL. CORP. CODE § 1001(a)).

323. *Id.* Specifically, Shareholders relied on *Solorza v. Park Water Co.*, 86 Cal. App. 2d 653 (1948).

324. *Monty*, 193 Cal. App. 4th at 1373.

325. *Id.* at 1374.

326. 818 A.2d 914 (Del. 2003).

of directors to include a "fiduciary out" clause in a merger agreement.[327] Instead, the court relied[328] on *Jewel Companies, Inc. v. Pay Less Drug Stores Northwest, Inc.*,[329] holding under California law that a board of directors "may lawfully bind itself in a merger agreement to forbear from negotiating or accepting competing offers."[330] Accordingly, the court held PCB's Board had no duty to include a "fiduciary out" termination clause in the investment agreement.[331]

Conclusion

The situation before the *Monty* court was unusual, involving the threatened takeover of a corporation subject to federal banking regulations. Accordingly, the court's holding, especially with respect to the "fiduciary out" termination provision, ultimately may be limited to the facts of the case.

12. *Einhorn v. M.L. Ruberton Construction Co.* (Buyer Liable for Seller's Obligations to Contribute to Multi-Employer Pension Plan)

Einhorn v. M.L. Ruberton Construction Co.[332] involved a successor liability claim brought under the Employee Retirement Income Security Act ("ERISA") against the purchaser of assets of a business for delinquent employee benefit fund contributions owed by the seller.

Statewide Highway Safety, Inc. ("Statewide"), a highway construction company with facilities in New Jersey, was required to make contributions to the Teamsters' Pension Trust Fund and Welfare Fund of Philadelphia and Vicinity (the "Funds") pursuant to two collective bargaining agreements with Teamsters Local Union No. 676 ("Local 676").[333] Statewide faced financial hardship and the pos-

327. *Monty*, 193 Cal. App. 4th at 1374.

328. *Id.*

329. 741 F.2d 1555 (9th Cir. 1984).

330. *Id.* at 1564. The full holding of *Jewel* was that "a corporate board of directors may lawfully bind itself in a merger agreement to forbear from negotiating or accepting competing offers *until the shareholders have had an opportunity to consider the initial proposal*." *Id.* (emphasis added). The *Jewel* court emphasized that "[w]hile the board can bind itself to exert its best efforts to consummate the merger under California law, it can only bind the corporation temporarily, and in limited areas, *pending shareholder approval*." *Id.* (citations omitted) (emphasis added). "[The shareholders] remain free to accept or reject the merger proposal presented by the board, to respond to a merger proposal or tender offer made by another firm subsequent to the board's execution of the exclusive merger agreement, or to hold out for a better offer." *Id.* Shareholders in *Monty*, however, did not vote directly on the investment agreement or the transaction, including the issuance of shares to Ford, even though they voted on the amendment of PCB's articles to increase the authorized stock as needed for the conversion of the new preferred shares (which vote was obtained by consent of Ford as holder of a majority of the shares). For this reason, the *Jewel* court's holding may not be directly applicable to the situation in *Monty*.

The *Jewel* court also declined to address the question of "whether upon the unsolicited receipt of a more favorable offer after signing a merger agreement the board still must recommend to its shareholders that they approve the initial proposal." *Id.* at 1564 n.13.

331. *Monty*, 193 Cal. App. 4th at 1374.

332. 632 F.3d 89 (3d Cir. 2011).

333. *Id.* at 91.

sible loss of public contract work in New Jersey based on allegations of fraud.[334] The Funds audited Statewide's payroll records, revealing contribution delinquencies of almost $600,000.[335] M.L. Ruberton Construction Company ("Ruberton"), a general construction company, entered into negotiations with Statewide for the purchase of Statewide's assets.[336] Local 676, fearing Ruberton (a non-union employer) would not agree to become a party to Statewide's collective bargaining agreements, obtained a temporary restraining order enjoining consummation of the sale, and negotiations among Statewide, Ruberton, and Local 676 followed.[337] Two agreements were executed, one between Local 676 and Statewide providing that the union would dismiss the injunction suit without prejudice and Statewide would cooperate with the audit and timely remit future contributions, and the second between Local 676 and Ruberton, providing that Ruberton would hire, subject to its work needs, the existing workforce of Statewide covered by the collective bargaining agreement and a newly negotiated agreement would govern all Ruberton employees.[338] Neither agreement addressed Ruberton's potential successor liability for the delinquent contributions.[339] Statewide then sold its assets to Ruberton for $1.6 million in cash.[340]

Following the sale, Ruberton leased Statewide's facility in Folsom, New Jersey (which had been purchased by a company related to Ruberton), hired more than half of Statewide's former employees, took over several of Statewide's projects, and auctioned off assets purchased from Statewide that were not used in Ruberton's expanded operations, realizing just more than $600,000.[341]

Approximately two months after the sale, Einhorn, as administrator of the funds, filed an action against Statewide and Ruberton for the delinquent contributions, claiming that Ruberton was liable as a successor in interest to Statewide.[342] The parties reached a settlement agreement, but Statewide breached the settlement agreement and Einhorn filed an action against Ruberton in the United States District Court for the District of New Jersey. Einhorn was unable to enforce a judgment it obtained against Statewide in the first action.[343]

In the district court, both parties assumed that the Seventh Circuit's decision in *Upholsterers' International Union Pension Fund v. Artistic Furniture of Pontiac*[344] provided the applicable rule of law.[345] That case held that a purchaser of assets may be liable for the seller's delinquent ERISA fund contributions to vindicate important federal statutory policy where the buyer had notice of the liability prior to

334. *Id.*
335. *Id.*
336. *Id.*
337. *Id.*
338. *Id.* at 92.
339. *Id.*
340. *Id.*
341. *Id.*
342. *Id.* at 93.
343. *Id.*
344. 920 F.2d 1323 (7th Cir. 1990).
345. *Einhorn*, 632 F.3d at 93.

the sale and there was sufficient evidence of continuity of operations between the entities.[346] The district court declined to follow *Artistic Furniture*, interpreting the Third Circuit's prior decision in *Teamsters Pension Trust Fund of Philadelphia and Vicinity v. Littlejohn*[347] to hold that "universal concepts of corporate law supplied the federal common law rule of successor liability in the present ERISA case."[348] Finding no express assumption of liability, no de facto merger, no fraudulent purpose, and that the conditions for "mere continuation of the seller" were not met, the district court granted Ruberton's motion for summary judgment.[349]

The court of appeals reviewed lines of cases in which it and other courts, following *Golden State Bottling Co. v. NLRB*,[350] had expanded successor liability in the labor field and then extended the labor law successorship doctrine to employment discrimination claims.[351] Summarizing its decisions in those cases, the court said that in the employment discrimination context it had found the imposition of successor liability appropriate where the successor was on notice, there was "sufficient continuity of operations and workforce," and the predecessor was unable to provide adequate relief, and had considered that the successor employer had ample opportunity to insulate itself from liability during the negotiations.[352] The "requirement of notice and the ability of the successor to shield itself during negotiations temper concerns that imposing successor liability might discourage corporate transactions."[353] Taking into account Congress's purpose in enacting the Multiemployer Pension Plan Amendments Act of 1980,[354] which amended ERISA to prevent the adverse consequences of individual employer's withdrawal from multiemployer pension plans, and the adverse consequences to employees of Statewide's failure to pay contributions, the court decided to follow the Seventh Circuit's opinion in *Artistic Furniture* and to apply its successor liability precedents in the labor and employment discrimination contexts to contribution claims under ERISA.[355]

The court remanded the case to the district court to apply the *Golden State* successorship doctrine to determine whether Ruberton is liable for Statewide's delinquencies. Noting that at oral argument the parties did not dispute that the notice requirement had been satisfied, the court stated that "the only issue on remand will be whether Ruberton substantially continued Statewide's operations."[356] "Under the substantial continuity test courts look to, *inter alia*, the following factors: continuity of the workforce, management, equipment and location, completion of work orders begun by the predecessor, and constancy of customers."[357]

346. *Upholsterers' Int'l Union Pension Fund*, 920 F.2d at 1327, 1329.
347. 155 F.3d 206 (3d Cir. 1998).
348. *Einhorn*, 632 F.3d at 94.
349. *Id.*
350. 414 U.S. 168 (1973).
351. *Einhorn*, 632 F.3d at 94–95.
352. *Id.* at 95.
353. *Id.* at 96.
354. Pub. L. No. 96-364, 94 Stat. 1208 (1980) (codified in scattered sections of 26 & 29 U.S.C.).
355. *Einhorn*, 632 F.3d at 96–98.
356. *Id.* at 99.
357. *Id.*

Conclusion

The court noted and cited a number of other circuit and district courts that have extended the *Golden State* rationale to delinquent pension fund contributions.[358] Its opinion, and the open-ended nature of the substantial continuity test, is a reminder to M&A practitioners that the usual corporate common law rules of successor liability may not apply in many circumstances, including labor law, employment discrimination, and ERISA, and that it can be difficult to predict when successor liability will be imposed.

13. *OverDrive, Inc. v. Baker & Taylor, Inc.*; *Allen v. Devon Energy Holdings, L.L.C.* (General Disclaimer and Release Provisions Did Not Bar Fraud Claims)

A party to an M&A agreement may attempt to bring tort-based fraud and negligent misrepresentation claims on the alleged inaccuracy of both purported pre-contractual representations and express, contractual warranties.[359] The seller can endeavor to reduce the risk of such post-closing claims by the buyer through provisions in the agreement to the effect that the agreement is the exclusive agreement between the parties, that the seller is not responsible for any statement not made within the four corners of the agreement, and that the seller's responsibility for those statements is contractually limited.[360]

Delaware Law: *ABRY Partners* and Later Cases

In *ABRY Partners V, L.P. v. F&W Acquisition LLC*,[361] a stock purchase agreement included a non-reliance clause by the buyer, indicating that the buyer was not relying upon any representations and warranties not stated in the contract. The Delaware Chancery Court wrote that such provisions are generally enforceable when they are the product of give-and-take between commercial parties who had the ability to walk away freely, noting that Delaware courts have "honored clauses in which contracted parties have disclaimed reliance on extra-contractual representations, which prohibits the promising party from reneging on its promise by premising a fraudulent inducement claim on statements of fact it had previously said were neither made to it nor had an effect on it."[362] The court wrote "that a party cannot promise, in a clear integration clause of a negotiated agreement, that it will not rely on promises and representations outside of the agreement and then shirk its own bargain in favor of a 'but we did rely on those other representations'

358. *Id.* at 98–99.

359. *See, e.g.*, Glenn D. West & W. Benton Lewis, Jr., *Contracting to Avoid Extra-Contractual Liability—Can Your Contractual Deal Ever Really Be the "Entire" Deal?*, 64 Bus. Law. 999 (2009); Byron F. Egan, Patricia O. Vella & Glenn D. West, Contractual Limitations on Seller Liability in M&A Agreements (Oct. 20, 2011), *available at* http://images.jw.com/com/publications/1669.pdf.

360. *See supra* note 359.

361. 891 A.2d 1032 (Del. Ch. 2006).

362. *Id.* at 1056.

fraudulent inducement claim."[363] Merger or integration clauses that do not clearly state that the parties disclaim reliance upon extra-contractual statements will not relieve a party of its oral and extra-contractual fraudulent representations, but a clear anti-reliance clause by which the plaintiff has contractually promised that it did not rely upon statements outside the contract's four corners in deciding to sign the contract will be enforced.[364] In *ABRY*, however, the court allowed a fraud claim to proceed where, notwithstanding a clear anti-reliance provision, the plaintiff alleged that the defendant had intentionally lied within the four corners of the agreement.[365]

In *OverDrive, Inc. v. Baker & Taylor, Inc.*,[366] the defendant allegedly breached its promises in a joint venture agreement to distribute plaintiff's audiobooks and other digital media exclusively to defendant's books and physical media customers.[367] The agreement provided that "[n]either party is relying on any representations, except those set forth herein, as inducement to execute this Agreement."[368] The plaintiff alleged that the defendant intentionally lied about specific provisions in the agreement in failing to reveal plans to use digital media information received from the plaintiff in digital media arrangements with competitors.[369]

In denying the defendant's motion to dismiss, the Delaware Chancery Court wrote that under *ABRY*, use of an anti-reliance clause "is contrary to public policy if it would operate as a shield to exculpate defendant from liability for its own intentional fraud."[370] Although the language of the anti-reliance clause in the agreement was clear and unambiguous, public policy precluded it from being effective to bar enforcement of promises that went to the very core of the agreement.[371]

Texas Law: *Allen v. Devon Energy Holdings, L.L.C.*

In *Allen v. Devon Energy Holdings, L.L.C.*,[372] plaintiff Allen alleged that defendants Chief Holdings, L.L.C. ("Chief") and Trevor Rees-Jones, Chief's manager and majority owner, fraudulently induced him to redeem his interest two years before the company was sold to an unaffiliated third party for almost twenty times the redemption sales price.[373] The defense argued that the disclaimers and release provisions in the redemption agreement barred Allen's fraud claims by negating

363. *Id.* at 1057.
364. *Id.* at 1056, 1059.
365. *Id.* at 1064–65.
366. No. 5835-CC, 2011 WL 2448209, at *1 (Del. Ch. June 17, 2011).
367. *Id.* at *1.
368. *Id.* at *6 (alteration in original).
369. *Id.*
370. *Id.*
371. *Id.*
372. No. 01-09-00643-CV, 2011 WL 3208234 (Tex. App. July 28, 2011).
373. *Id.* at *1. Allen and Rees-Jones served together as partners at a prominent Dallas law firm. *Id.* at *1–2. Allen was an oil and gas transactions lawyer, and Rees-Jones was a bankruptcy lawyer before leaving the firm to go into the oil and gas business. *Id.* Allen was one of Chief's early investors, and allegedly relied on investment advice from Rees-Jones. *Id.* at *2.

reliance or materiality as a matter of law.[374] In denying Allen's motion for summary judgment, the court of appeals held that the redemption agreement did not bar Allen's claims, and that fact issues existed as to fraud and other claims.[375]

In November 2003, Rees-Jones called Allen to make Chief's offer to redeem his Chief equity interest.[376] He followed up with a letter explaining the reasons for and terms of the redemption offer, to which he attached an independent valuation firm's opinion on Chief's market value and an appraisal of Chief's existing gas reserves and future drilling prospects.[377] The valuation report included discounts for the sale of a minority interest and for lack of marketability.[378] The letter also included Rees-Jones's pessimistic assessment of a number of facts and events that could negatively impact Chief's value in the future.[379]

The redemption proposal languished for seven months until Rees-Jones notified Allen in early June 2004 that Chief was ready to proceed with the redemption.[380] Allen asserted that events that positively affected the value of Chief's oil and gas properties were not disclosed to him and would have materially impacted his decision to redeem his interest.[381]

Chief provided Allen with a written redemption agreement for the first time in June 2004, and "insisted" that the contract be signed by the end of the month.[382] The parties did not exchange drafts, and Allen stated that he had only three days to review the agreement before signing because he was on vacation for much of the time.[383]

The redemption agreement contained an "independent investigation" paragraph, a general "mutual release," and a merger clause which, the defendants claimed, barred Allen's fraud claims negating reliance or materiality as a matter of law.[384] The "independent investigation" paragraph provided that: (1) Allen based his decision to sell on his independent due diligence, expertise, and the advice of his own engineering and economic consultants; (2) the provided appraisal and the reserve analysis were estimates and other professionals might provide different estimates; (3) events subsequent to the reports might "have a positive or negative impact on the value" of Chief; (4) Allen was given the opportunity to discuss the

374. *Id.* at *1.

375. *Id.* The court also held that the redemption agreement did not bar Allen's claims for fraud under the Texas Securities Act because section 33L thereof declares void any provision in which a buyer or seller of a security waives "compliance with a provision of this Act." *Id.* at 32. *But see* Lone Star Fund V (U.S.), L.P. v. Barclays Bank PLC, 594 F.3d 383 (5th Cir. 2010) (allowing a nuanced contractual limitation on remedies to preclude a securities fraud claim because plaintiff failed to allege a misrepresentation in light of the "repurchase or substitute" clauses in the parties' mortgage-backed securities purchase contracts).

376. *Allen*, 2011 WL 3208234, at *2.

377. *Id.*

378. *Id.*

379. *Id.*

380. *Id.* at *4.

381. *Id.*

382. *Id.*

383. *Id.*

384. *Id.*

reports and obtain any additional information from Chief's employees as well as the valuation firm and the reserve engineer; and (5) the redemption price was based on the reports regardless of whether those reports reflected the actual value and regardless of any subsequent change in value since the reports.[385] The independent investigation paragraph also included mutual releases "from any claims that might arise as a result of any determination that the value of [Chief] . . . was more or less than" the agreed redemption price at the time of the closing.[386]

In a separate paragraph entitled "mutual releases," each party released the other from all claims that "they had or have arising from, based upon, relating to, or in connection with the formation, operation, management, dissolution and liquidation of [Chief] or the redemption of" Allen's interest in Chief, except for claims for breach of the redemption agreement or breach of the note associated with the redemption agreement.[387] Another paragraph contained a merger clause stating that the redemption agreement "supersedes all prior agreements and undertakings, whether oral or written, between the parties with respect to the subject matter hereof."[388]

Allen argued that fraudulent inducement invalidates the release provisions in the redemption agreement as "[f]raud vitiates whatever it touches."[389] The court rejected that argument, but held that the release provisions in the redemption agreement were not sufficiently explicit to negate Allen's fraud in the inducement claims.[390]

The court wrote that Texas has not adopted a per se rule that a disclaimer of reliance automatically precludes a fraudulent inducement claim.[391] Instead, Texas allows a disclaimer of reliance to preclude a fraudulent inducement claim only if the parties' intent to release such claims "is clear and specific."[392] The court found the following failings with the disclaimer language in the redemption agreement:

First, the disclaimer did not clearly and unequivocally disclaim Allen's reliance on Rees-Jones's representations.[393]

Second, the broad language releasing "all claims, demands, rights, liabilities, and causes of action of any kind or nature" did not specifically release fraudulent inducement claims or disclaim reliance on Rees-Jones's and Chief's representations.[394] Although the disclaimer did release claims "of any kind or nature" which

385. *Id.* at *6.
386. *Id.*
387. *Id.*
388. *Id.*
389. *Id.* (quoting Stonecipher v. Butts, 591 S.W.2d 806, 809 (Tex. 1979)).
390. *Id.* at *9 (citing Italian Cowboy Partners, Ltd. v. Prudential Ins. Co. of Am., 341 S.W.3d 323 (Tex. 2011) (concluding that "the contract language in this case does not disclaim reliance or bar a claim based on fraudulent inducement" because it did not include an "expressed clear and unequivocal intent to disclaim reliance or waive claims for fraudulent inducement"); Schlumberger Tech. Corp. v. Swanson, 959 S.W.2d 171, 181 (Tex. 1997) (stating that "a release that clearly expresses the parties' intent to waive fraudulent inducement claims, or one that disclaims reliance on representations about specific matters in dispute, can preclude a claim of fraudulent inducement")).
391. *Id.* at *7.
392. *Id.*
393. *Id.* at *8.
394. *Id.* at *9.

necessarily includes fraudulent inducement, the "elevated requirement of precise language" requires more than a general catch-all—it must address fraud claims in clear and explicit language.[395]

Third, the merger clause stated that the contract is the "final integration of the undertakings of the parties hereto and supersedes all prior agreements and undertakings," but did not include clear and unequivocal disclaimer of reliance on prior representations.[396]

Fourth, the redemption agreement failed to state that the only representations that had been made were those set forth in the agreement.[397]

Fifth, it did not contain a broad disclaimer that no extra-contractual representations had been made and that no duty existed to make any disclosures.[398]

Sixth, it did not provide that Allen had not relied on any representations or omissions by Chief.[399]

Finally, it did not include a specific "no liability" clause stating that the party providing certain information will not be liable for any other person's use of the information.[400]

The court was careful to state it was not requiring that the words "disclaimer of reliance" be stated in order for a disclaimer to preclude a fraudulent inducement claim or that each one of these issues must be addressed in every disclaimer.[401] Rather, the court stated that "[i]t is sufficient to include (1) a clear and unequivocal disclaimer of reliance; (2) an express waiver specific to fraudulent inducement claims; or (3) an all-embracing disclaimer of any and all representations and any duty to make any disclosures."[402] It is not sufficient to say, as the defendants did, that the agreement taken as a whole adds up to a clear anti-reliance provision.[403]

The independent investigation clause stated that Allen "based his decision to sell" on his own independent due diligence investigation, his own expertise and judgment, and the advice and counsel of his own advisors and consultants.[404]

395. *Id.*
396. *Id.*
397. *Id.* at *9–10.
398. *Id.*
399. *Id.*
400. *Id.*
401. *Id.* at *10.
402. *Id.*
403. *Id.* at *9–10. The requirement in *Allen* and other Texas cases that a disclaimer of reliance be clear and unequivocal could be extended to include a requirement that the disclaimer be conspicuous. In *Staton Holdings, Inc. v. Tatum, L.L.C.*, 345 S.W.3d 729 (Tex. App. 2011), the Texas Court of Appeals held that contractual provisions that call for an extraordinary shifting of risk between the parties are enforceable only if they are conspicuous and expressed in specific terms within the four corners of the contract. *Id.* at 733 (citing Dresser Indus., Inc. v. Page Petroleum, Inc., 853 S.W.2d 505, 508 (Tex. 1993); Ethyl Corp. v. Daniel Constr. Co., 725 S.W.2d 705, 708 (Tex. 1987)). The *Staton Holdings* case is another example of a Texas court acknowledgement that Texas law respects freedom of contract, including the right of parties to limit contractually their tort and other liabilities arising in respect of contracts, but that the Texas courts regard such a shifting of liability as so extraordinary that they require it to be clear, unequivocal, and conspicuous in the contract so that there is no question that the parties knowingly bargained for that outcome.
404. *Allen*, 2011 WL 3208234, at *8.

The court found, however, that the statement of reliance on the identified factors did not clearly and unequivocally negate the possibility that Allen also relied on information he had obtained from Chief and Rees-Jones; consistent with the terms of the redemption agreement, Allen could have relied on both.[405] The court found it incongruous to state that Allen could not rely on the information he was given, and noted the absence of the words "only," "exclusively," or "solely" was of critical importance.[406]

Rees-Jones and Devon argued that the redemption agreement contained language that released Allen's claims against them and that this language shows that the parties agreed broadly to disavow the factual theories asserted by Allen.[407] Although the redemption agreement released the parties from claims that arise from a determination that the redemption price did not reflect Chief's market value at closing, it did not negate Allen's claims that Rees-Jones made misrepresentations and omissions concerning Chief's future prospects.[408] Further, the release barred any claim by Allen based on a change in value from time of the appraisal provided by Chief to the date of redemption only, and did not cover Allen's claims that Rees-Jones and Chief withheld information relating to Chief's future prospects and potential value.[409]

The court further wrote that even a clear and unequivocal disclaimer of reliance may not bar a fraudulent inducement claim unless "(1) the terms of the contract were negotiated [and not] boilerplate; (2) the complaining party was represented by counsel; (3) the parties dealt with each other at arm's length; and (4) the parties were knowledgeable in business matters."[410] The court found that Allen as an oil and gas attorney could not complain that he was not represented by counsel and was not knowledgeable.[411] The court, however, found fact issues as to the other two factors (whether the contract was negotiated and whether the parties dealt with each other at arm's length) and declined to grant the defendant's motion for summary judgment.[412] The court declined to say whether all four tests must be satisfied for an otherwise clear and unequivocal disclaimer of reliance to be enforceable.[413]

Conclusion

Allen recognizes that contractual provisions that negate the element of reliance required for a common law fraud claim can be effective to preclude a buyer's

405. *Id.*
406. *Id.*
407. *Id.* at *9.
408. *Id.*
409. *Id.*
410. *Id.* at *10. In *McLernon v. Dynegy, Inc.*, 347 S.W.3d 315, 330 (Tex. App. 2011), the Texas Court of Appeals applied the same test in sustaining an employer's motion for summary judgment in the context of a settlement agreement and release executed in connection with the termination of an executive vice president of the employer.
411. *Allen*, 2011 WL 3208234, at *10.
412. *Id.* at *10–13.
413. *Id.*

equitable fraudulent inducement claim for rescission, but also illustrates a judicial reluctance to dismiss a well-pled case at the motion to dismiss or summary judgment stage based on such a provision, sometimes finding drafting inadequacies or fact issues. As a result of *Allen* and other cases, sellers should consider the following drafting principles:

- Do not use provisions that appear to be boilerplate, and tailor the limitation of liability provision for each transaction in a way that shows that it has been specifically negotiated.
- Expressly disclaim reliance on any representations that are not embodied in the four corners of the agreement.
- Expressly state that no reliance is being placed on any statements (i) by any representative of any of the parties whose liability is limited or (ii) in the dataroom (if such is the case).
- Expressly state that fraud in the inducement claims are being released.
- Expressly state that no reliance has been placed on any prior representations.
- Include both broad inclusive words of limitation of liability and then specifically address the particular kinds of representations not being relied upon.