



Recent Developments in M&A Law

The mergers and acquisitions (M&A) market continues to run hot, with 2021 set to outpace recent years as measured by both deal volume and total deal value. Courts have been busy too, issuing a variety of rulings that will impact M&A transactions and other business arrangements. We focus on two important cases below.

Manti Holdings LLC v. Authentix Acquisition Co.

This case arose from a merger of Authentix Acquisition Co. with a third-party acquirer. Before the merger, Authentix and its stockholders entered into a stockholders agreement that provided for drag-along rights, requiring all stockholders to consent to a sale of Authentix and refrain from exercising appraisal rights if the sale was approved by holders of a majority of Authentix shares. Subject to certain conditions, appraisal rights in the M&A context allow stockholders to pursue a valuation at fair market value in lieu of accepting an M&A transaction price.

Holders of a majority of Authentix shares later approved the sale of Authentix. Although they signed the stockholders agreement, dissenting stockholders sought to perfect their alleged appraisal rights and brought suit against Authentix, seeking statutory appraisal under Section 262 of the Delaware General Corporation Law (DGCL).

The Delaware Supreme Court held that Section 262 does not prohibit sophisticated and informed stockholders, who are represented by counsel and who have bargaining power, from voluntarily agreeing to waive appraisal rights in exchange for valuable consideration. The court reasoned that: (1) the DGCL is a broad enabling act allowing freedom for private ordering; (2) Section 262 does not contain any language preventing stockholders from agreeing to an ex ante waiver of appraisal rights; and (3) public policy does not prohibit sophisticated and informed stockholders from waiving appraisal rights in exchange for valuable consideration. The court's ruling established that a Delaware corporation can enforce appraisal waivers against its own stockholders.

The decision does not, however, directly address the enforceability of other waivers, such as waivers of books and records rights. The court warned that certain rights may be viewed as so fundamental to the corporate form that they cannot be waived, such as "rights designed to police corporate misconduct or to preserve the ability of stockholders to participate in corporate governance." The decision nevertheless serves as a guidepost for, among others, private equity and venture capital investors whose investments typically include drag-along rights with appraisal waivers.

Online HealthNow, Inc. and Bertelsmann, Inc. v. CIP OCL Investments, LLC, et al.

This case arose from the acquisition of OnCourse Learning Corp. Following the acquisition, the buyers sued CIP OCL Investments LLC and a related entity (CIP), both of which were affiliated with the target company, as well as multiple executives, alleging misrepresentation or concealment of millions of dollars of tax liabilities during the sales process.

The purchase agreement included an anti-reliance provision stating that the buyers relied only on the contractual representations and warranties in entering into the purchase agreement. However, by means of a "no-survival" clause, the purchase agreement was structured so that all representations and warranties, including regarding tax matters, expired at closing. In addition, the purchase agreement included a non-recourse provision limiting recourse for claims, including against non-parties affiliated with the target company—a scope that included CIP.

Buyers alleged they became aware of false tax representations only after the closing and that CIP was aware for years of the target's failure to accrue tax liabilities associated with online transactions. After the closing, buyers asserted approximately \$18 million in purchase price adjustments. Sellers disagreed and buyers brought their claim for fraud, among others.

The Delaware Court of Chancery rejected CIP's defensive arguments that it could not be liable for fraud due to a combination of the non-reliance provision, the expiration of representations and warranties at closing, and

the non-recourse provision. The court held that Delaware public policy does not allow expungement of fraud claims through a contractual walk-away construct where a party, or in this case, even a non-party, seeks to avoid liability for fraud. Moreover, Delaware public policy does not allow persons who knowingly participate in fraud to escape liability merely by not entering into the subject contract or not themselves making representations and warranties.

The Court of Chancery relied on a prior case, *ABRY Partners V, L.P. v. F & W Acquisition LLC*. In *ABRY Partners*, the Delaware Supreme Court held that "a seller may not contractually limit its liability for making knowingly false statements within the contract itself." In *ABRY Partners*, the court balanced two key interests: (1) Delaware's longstanding tradition of respect for private ordering and carefully negotiated risk allocation; and (2) evidence of Delaware law's "strong and storied intolerance of fraud." The court balanced these two interests by explaining that contractual terms "exempting a party from tort liability for harm caused intentionally or recklessly [are] unenforceable on grounds of public policy." Ultimately, under *ABRY Partners*, in situations where "an agreement purports to limit liability for a lie made within the contract itself, and parties know of the lie, such parties cannot skirt liability through contractual limits within the very contract they procured by fraud."

Applying the legal framework from *ABRY Partners*, the Court of Chancery held that the no-survival clause in the purchase agreement did not bar a fraud claim. In reaching this conclusion, the court determined that the "weight of authority" and "Delaware's public policy" prevented the sellers and CIP from invoking a survival clause "in a contract allegedly procured by fraud to eviscerate a claim that the contract itself is an instrument of fraud."

The court also noted that the holding in *ABRY Partners* "implicitly rejected the argument that a non-recourse provision will operate to insulate a third-party from liability when that party facilitated the target's lies." The court reasoned that the non-recourse provision at issue could not therefore be invoked to avoid liability, primarily because of the allegations that CIP "[knew] of and facilitated the fraudulent misrepresentations in the [stock purchase agreement]."

John Bradley is a Partner in the firm's Corporate and Securities practice. John's practice includes representation in mergers and acquisitions on behalf of buyers and sellers; corporate governance and advising senior executives, directors, and public company boards and committees; periodic and other reporting under the Securities Exchange Act of 1934; debt and equity securities offerings, including registered public offerings under the Securities Act of 1933; venture capital financings; software licensing transactions; and drafting and negotiating a wide variety of business agreements.



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