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NON-RELIANCE AND WAIVER CLAUSES IN NDA PRECLUDE FRAUD CLAIMS BY WOULD-BE PRIVATE EQUITY BUYER

The Delaware Supreme Court affirms enforceability of non-reliance and waiver provisions in a non-disclosure agreement to bar claims by a would-be buyer of a business based on alleged fraudulently omitted or misstated information in due diligence.

In *RAA Management LLC v. Savage Sports Holdings Inc.*, Del., No. 577, 2011 (May 18, 2012), the Delaware Supreme Court held that a bidder for a business is barred by non-reliance and waiver clauses in the parties' non-disclosure agreement from suing the target for fraud based on alleged knowingly false statements in the due diligence disclosures. Accordingly, it affirmed the Superior Court's grant of the target's motion to dismiss.

The plaintiff, a private equity fund, contended that it would not have considered purchasing Savage had it known from the beginning of the bid process of certain alleged unrecorded liabilities or claims. The bidder was seeking reimbursement of $1.2 million in due diligence and negotiation costs. The target argued that the claim was barred by the following provisions of the non-disclosure agreement:

> You [RAA] understand and acknowledge that neither the Company [Savage] nor any Company Representative is making any representation or warranty, express or implied, as to the accuracy or completeness of the Evaluation Material or of any other information concerning the Company provided or prepared by or for the Company, and none of the Company nor the Company Representatives, will have any liability to you or any other person resulting from your use of the Evaluation Material or any such other information. Only those representations or warranties that are made to a purchaser in the Sale Agreement when, as and if it is executed, and subject to such limitations and restrictions as may be specified [in] such a Sale Agreement, shall have any legal effect.
>
> You [RAA] understand and agree that no contract or agreement providing for a transaction between you and the Company [Savage] shall be deemed to exist between you and the Company unless and until a definitive Sale Agreement has been executed and delivered, and you hereby waive, in advance, any claims . . . in connection with any such transaction unless and until you shall have entered into a definitive Sale Agreement.

RAA made four arguments that these non-reliance and waiver provisions should not apply:

> (1) that the non-reliance provisions only applied to unintentional inaccuracies,
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> (2) that the provisions were ambiguous,

(3) New York's "peculiar knowledge" exception applied, and

(4) the NDA is unenforceable for public policy reasons (*i.e.*, that parties may not use contracts to shield themselves from liability for their own fraud).

The Supreme Court rejected each of these arguments and stated that it would come to the same conclusion regardless of whether New York or Delaware law applied.

The Supreme Court found that the non-reliance language was unambiguous and did not distinguish between due diligence information that was inaccurate because of negligence, mistake, intent or fraud and, therefore, the plaintiff's first two arguments were without merit. In doing so, the Delaware Supreme Court held that the Delaware Court of Chancery had interpreted and enforced nearly identical provisions in prior cases, and in both cases had found such provisions unambiguous.

The Supreme Court also rejected the plaintiff's argument based upon the so-called "peculiar knowledge" exception, under which some New York courts have held, in the context of completed sale transactions, that claims of fraudulent inducement would not be barred if the facts at issue were "peculiarly within the misrepresenting party's knowledge." The Delaware Supreme Court agreed with the defendant's argument that this doctrine has largely been rejected in cases where sophisticated parties could have contracted for themselves. Further, they held that applying the peculiar knowledge exception in this circumstance would preclude sophisticated parties from ever having an enforceable agreement that a bidder would not bring claims if it walked away from negotiations.

Lastly, the Supreme Court rejected the policy argument advanced by the plaintiff bidder that "the general rule prohibits parties from using contracts to shield themselves from liability for their own fraud." Rather, The Delaware Supreme Court relied upon the Chancery Court's holdings in *Abry Partners V, L.P. v. F&W Acquisition LLC*, 891 A.2d 1032 (Del. Ch. 2006) and other cases. It quoted with approval Vice Chancellor (now Chancellor) Strine's opinion in *Abry Partners* as follows: "To fail to enforce non-reliance clauses is not to promote a public policy against lying. Rather, it is to excuse a lie made by one contracting party in writing—the lie that it was relying only on contractual representations and that no other representations had been made—to enable it to prove that another party lied orally or in a writing outside the contract's four corners. For the plaintiff in such a situation to prove its fraudulent inducement claim, it proves itself not only a liar, but a liar in the most inexcusable of commercial circumstances: in a freely negotiated written contract. Put colloquially, this is necessarily a 'Double Liar' scenario. To allow the buyer to prevail on its claim is to sanction its own fraudulent conduct."

By its decision in this case, the Delaware Supreme Court has provided strong support for the holding in *Abry Partners* that a properly drafted non-reliance clause in a definitive acquisition agreement will bar fraud claims based on statements and omissions made in the diligence process or otherwise outside of the four corners of the definitive agreement. It is, however, not clear that the same rule applies if the fraud claim is brought under the federal securities laws. In *AES Corp. v. Dow Chemical Co.*, 325 F.3d (3d Cir. 2003), the Court of Appeals for the Third Circuit held that a non-reliance clause is not effective to bar the claim as a matter of law, but is admissible as evidence on the issue of whether the buyer's reliance was reasonable, while in *Harsco Corp. v. Segui*, 91 F.3d 337 (2d Cir. 1996), the holding of the Court of Appeals for the Second Circuit was similar to that in *Abry Partners*.

A copy of the decision is available at: http://courts.state.de.us/opinions/download.aspx?ID=172770

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