CLIENT ALERT

M&A Transactions: Developments in NDAs

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A recent decision by the Delaware Supreme Court serves as an important reminder to potential buyers and sellers in M&A transactions of the important role non-disclosure agreements (NDAs) can play in fixing the limits of potential liability for sellers during the due diligence phase of a transaction. Claims of misrepresentation can arise not only after a purchase agreement is signed or a transaction consummated, but even when the negotiations break down and an agreement is never executed. Buyers can incur significant costs pursuing an acquisition; if negotiations fall apart before a definitive agreement is reached and the buyer believes the seller made misrepresentations during the process that mislead the buyer into continuing to incur such costs, the buyer may seek to recoup these expenses from the seller. However, in *RAA Management, LLC v. Savage Sports Holdings, Inc.,* the Delaware Supreme Court recently reminded potential buyers that they will have very limited, if any, recourse or remedies against a seller in connection with a potential transaction until a definitive agreement is signed.

Background

RAA Management was interested in possibly purchasing Savage Sports, so the two parties entered into a NDA prior to Savage Sports disclosing confidential information to RAA as part of the due diligence process. The NDA included a broad non-reliance provision that disclaimed "any" representation or warranty as to the accuracy of any information it provided to RAA during due diligence and disclaimed "any" liability resulting from the use of such material, except as might be set forth in a definitive agreement. The NDA also included a broad waiver of claims by which RAA waived "any" claims in connection with the transaction unless a definitive agreement was entered into.

Upon executing the NDA, RAA began its due diligence of Savage Sports. After several months of due diligence, RAA terminated negotiations when it learned of three significant liabilities of Savage Sports. RAA then sued Savage Sports, alleging that Savage Sports knowingly made material fraudulent misrepresentations and omissions during the due diligence process. RAA alleged that as a result of its reliance on Savage Sports' representations, RAA spent $1.2 million on due diligence and negotiation expenses that RAA would not have spent had Savage Sports made accurate and complete disclosures earlier on in the process. RAA demanded Savage Sports be held liable to RAA for the $1.2 million in expenses.

On May 18, 2012, the Delaware Supreme Court held that even if Savage Sports did knowingly make material fraudulent misrepresentations and omissions, the disclaimer of reliance clause in the NDA barred RAA's claim. The Court explained that not only did the plain language of the non-reliance provision bar the claim, but

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prior case law, public policy and the efficient functioning of the M&A markets are all in favor of allowing sophisticated M&A parties to allocate risk by disclaiming reliance on representations made *outside* a final agreement.

Lessons Learned

Buyers should be aware that they will likely have limited, if any, recourse against the seller for expenses or any other losses incurred by the buyer in connection with a potential transaction if a definitive agreement is not signed. A buyer could try to protect itself in one of the following ways:

- require that the standard non-reliance and waiver clauses that are ordinarily included in NDA be omitted;
- have the seller represent and warrant that its disclosures during due diligence are accurate and complete;
- have an exception to the non-reliance provisions that would hold the seller liable for fraudulent or intentionally inaccurate information; or
- delay relatively expensive aspects of the due diligence review until later in the due diligence process when a deal is more certain.

On the other side, sellers of businesses should ensure that their NDAs contain standard broad disclaimers of reliance and waivers of claims clauses and resist making any changes to these clauses. Given the statements in *RAA Management* that standard non-reliance and waiver clauses generally result in no potential liability for sellers, any deviation from standard language may be interpreted to mean the parties intended something different, thereby potentially exposing sellers.

For more information, please contact the author.

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