



Appraisal Claim Waivers and Deal Covenants

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Editor's note: Katherine Henderson, Amy Simmerman and Brad Sorrels are partners at Wilson Sonsini Goodrich & Rosati. This post is based on a WSGR publication by Ms. Henderson, Ms. Simmerman, Mr. Sorrells, Ryan Greecher, Nate Emeritz, and Toni Wormald, and is part of the Delaware law series; links to other posts in the series are available [here](#). Related research from the Program on Corporate Governance includes [Appraisal After Dell](#) by Guhan Subramanian and [Allocating Risk Through Contract: Evidence from M&A and Policy Implications](#) (discussed on the Forum [here](#)).

On May 15, 2019, Vice Chancellor Slight of the Delaware Court of Chancery issued a ruling addressing important issues related to private company deal litigation. Specifically, the decision addressed when a release of claims and covenant not to sue can bar ensuing appraisal and fiduciary claims by stockholders. The case, *In re Altor BioScience Corporation*, involved the acquisition of Altor BioScience Corporation (Altor) by an affiliate of a large stockholder of Altor by way of a merger. The plaintiffs asserted appraisal claims and breaches of fiduciary duty claims against the Altor board, including the chairman of Altor, who was also an indirect holder of 51 percent of Altor's stock and the CEO, chairman, and 85 percent stockholder of the acquiror.

The issue before the court concerned whether appraisal and fiduciary claims brought by two stockholders and former members of the Altor board, Clayland Gray and Adam Waldman, were contractually barred by letter agreements that they entered into prior to the deal in connection with the settlement of a dispute that had arisen between factions of the Altor board. The court noted at the outset that the purpose of the letter agreements was to broker a "peace in the valley," in the midst of great tension between two factions of the Altor board." The two key provisions of the letter agreements were Section 3 and Section 7, pursuant to which Gray and Waldman had agreed to release certain claims and not to sue certain individuals and entities in exchange for receiving "valuable consideration," including "substantial" stock options.

Section 3 of the letter agreements contained a broad release of claims against a class of Company Releasees that included the defendants and any successor of Altor. It stated that Gray and Waldman will not "file, charge, claim, sue, or cause or permit to be filed or charged any action or claim for damages or other relief against any of the Company Releasees for any matter arising from the creation of the earth through the Closing Date." It also stated that "[n]othing in the foregoing releases shall relieve the Company of its obligations under...this letter agreement or...for any act occurring after the date of this letter agreement."

Section 7 of the letter agreements contained a standstill and a separate covenant not to sue. Specifically, it stated that Gray and Waldman shall not "directly or indirectly commence, prosecute

or cause to be commenced or prosecuted against any Company Releasee any action or other proceeding of any nature before any court, ...except for the Company's breach of this letter agreement." Section 7 also listed specific actions that Gray and Waldman shall not take with respect to Altor for the five-year standstill period.

In their motion for summary judgment, the defendants argued that the letter agreements contractually barred plaintiffs Gray and Waldman from asserting their fiduciary and appraisal claims.

The plaintiffs argued that their claims were not barred, among other things, because: (1) the letter agreement provisions in Sections 3 and 7, when read together, were ambiguous, and as a result the defendants' overreaching interpretation of the provisions was untenable; (2) the defendants' interpretation would violate public policy because it would allow the defendants to escape liability for unknown future claims; and (3) the plaintiffs did not expressly waive in the letter agreements their statutory right to appraisal as required under Delaware law.

The Decision

The court addressed the fiduciary claims separately from the appraisal claims. With respect to the fiduciary claims, the court distinguished Section 3 from Section 7 by explaining that Section 3 was a release, which did not address future claims, while Section 7 was a covenant not to sue, which did not relinquish any claims but rather was a specific covenant offered to specific parties in exchange for "valuable consideration" ("substantial" stock options). The court held that the language of the covenant not to sue was "clear and unambiguous" in providing that Gray and Waldman would not commence, prosecute, or cause to be commenced or prosecuted against any Company Releasee, any action, or other proceeding for five years after execution of the agreement. Because nothing in Section 7 prohibited all other stockholders unaffiliated with the parties to the letter agreements from asserting claims, and other stockholders were in fact bringing similar claims, the letter agreements did not violate public policy. Thus, the court held that the fiduciary claims brought by plaintiffs Gray and Waldman (and his wife) were barred by the letter agreements.

The court specifically rejected the plaintiffs' argument that such covenants were per se unenforceable because they immunized the defendants from claims for future fiduciary misconduct. The court noted that "parties can release unknown claims and damages that arise in the future." The court distinguished the cases cited by the plaintiffs, noting that covenants not to sue have been held unenforceable only where the harm suffered was unique to the particular plaintiff such that others could or would not bring the lawsuit. Thus, in a case "where a defendant effectively locked up the only stockholder who would or practically could challenge a breach of fiduciary duty by entering into a standstill [agreement] with that stockholder, ... the Court could then, and probably would, void that standstill covenant as unenforceable as a matter of public policy." Because such considerations were not applicable in this case, the covenants were enforceable.

The covenants not to sue did not, however, bar the appraisal claims because the letter agreements did not contain an express waiver of the statutory appraisal right. The court reasoned that "there can be no waiver of a statutory right unless that waiver is clearly and affirmatively expressed in the relevant document." Here, the references to "actions" and "proceedings" were

not sufficient to constitute such a knowing waiver, particularly where nothing in the “letter or spirit” of Section 7 suggested that the parties intended to waive such rights. This contrasts from another recent case—*Manti Holdings, LLC v. Authentix Acquisition Co.*, C.A. No. 2017-0887-SG (Del. Ch. Oct. 1, 2018)—in which the Court of Chancery, at least based on the facts before it, enforced an express appraisal rights waiver in a contract.

Takeaways

- A waiver of appraisal claims must be clear and express in order to be enforceable.
- Covenants not to sue on future claims can be enforceable. However, if a particular plaintiff suffers unique harm which no other party can seek to address, a court may allow that plaintiff to proceed on public policy grounds.
- Covenants not to sue that apply to all stockholders may not be enforceable and thus may not serve to extinguish fiduciary claims.