
January 8, 2016

Delaware Court of Chancery Holds Extra-Contractual Fraud Claim Is Barred By Anti-Reliance/Integration Clauses

In *Prairie Capital III v. Double E Holding Corp.*, the Delaware Court of Chancery held that the anti-reliance and integration clauses in a stock purchase agreement barred the purchaser's claim for fraud to the extent based on extra-contractual representations or omissions during the course of negotiations.

In 2012, funds sponsored by a private equity firm (the "Sellers") negotiated the sale of a portfolio company (the "Company") to funds sponsored by another private equity firm (the "Purchaser"). The Purchaser's offer was conditioned on the completion of due diligence and verification that the Company had met certain financial goals. The parties then executed a stock purchase agreement ("SPA") that provided that the representations and warranties in the SPA "constitute[d] the sole and exclusive representations and warranties" of the Company and the Sellers and that all other representations and warranties were specifically disclaimed (the "Exclusive Representations Clause"). The SPA further contained an integration clause that stated that the agreement set forth the entire understanding of the parties with respect to the transaction and superseded any other agreements and representations (the "Integration Clause").

Subsequently, the Purchaser alleged that Company representatives had falsified records to make it appear as though the Company had met its financial goals and submitted a claim that the Company, its subsidiaries and members of management had engaged in fraud. Nevertheless, the Sellers' representative filed suit in the Delaware Court of Chancery to compel the release of funds held in escrow under the SPA. The Purchaser responded by asserting counterclaims for fraud, aiding and abetting fraud and conspiracy to engage in fraud based in part on extra-contractual statements and omissions that the Purchaser alleged were false. The Sellers moved to dismiss the counterclaims on the grounds that the Purchaser had disclaimed reliance on extra-contractual representations in the SPA. The Purchaser countered by arguing that the Exclusive Representations and Integration Clauses did not constitute a clear, enforceable anti-reliance clause barring fraud claims based on extra-contractual representations and, even if they did, the clause did not apply to its claims for fraudulent omission and concealment.

The Delaware Court of Chancery granted the Sellers' motion to dismiss in part, holding that the SPA foreclosed claims based on extra-contractual representations and omissions. In doing so, the court noted that:

- *Together, the Exclusive Representations and Integration Clauses added up to a clear anti-reliance clause, which a Delaware court will enforce.* – The Court held that "[i]f a party represents that it only relied on particular information, then that statement establishes the universe of information on which that party relied. Delaware law does not require magic words."
- *The anti-reliance clause barred fraud claims based on both extra-contractual representations and omissions.* – The Court explained that parties in an arms' length contractual setting, such as the negotiation of the SPA, do not have an affirmative duty to speak. Thus, any claim of fraud necessarily depends on some form of representation and cannot start from an omission. For arms' length

counterparties, therefore, contractual provisions that identify the representations on which a party exclusively relied define the universe of information that is in play for purposes of a fraud claim.” The Court concluded that the Exclusive Representations Clause “defined the universe of information on which [the Purchaser] relied” and “bar[red]not only fraud claims based on extra-contractual representations but also fraud claims based on extra-contractual omissions.” Notwithstanding the foregoing, however, the Court noted that if a party in an arms’ length negotiation chooses to speak, it cannot lie or speak so partially or obliquely so as to mislead. Further, once a party allows its counterparty to conduct an investigation, the party cannot conceal information because permitting the investigation operates as the functional equivalent of providing information.

Although the Court granted the Sellers’ motion to dismiss the Purchaser’s claims for fraud to the extent they were premised on extra-contractual representations or omissions, it also held that the Purchaser had sufficiently alleged that other representations in the SPA were false when made such that the Purchaser could still pursue its claims for fraud based upon those representations.

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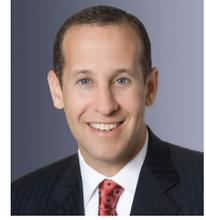
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