CONFIDENTIALITY AGREEMENTS: HOW TO DRAFT THEM AND WHAT THEY RESTRICT

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Involvement: Mr. Egan is Senior Vice Chair and Chair of Executive Council of the M&A Committee of the American Bar Association and served as Co-Chair of its Asset Acquisition Agreement Task Force, which wrote the *Model Asset Purchase Agreement with Commentary* (2001). He is Chair of the Texas Business Law Foundation; is a former Chair of the Business Law Section of the State Bar of Texas and former Chair of that section's Corporation Law Committee; and on behalf of these groups, has been instrumental in the drafting and enactment of many Texas business entity and other statutes. He is also a member of the American Law Institute.

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Appendix A – Confidentiality Agreement

CONFIDENTIALITY AGREEMENTS: HOW TO DRAFT THEM AND WHAT THEY RESTRICT

By Byron F. Egan[1]

I. Confidentiality Agreements And Their Effects Are Evolving

A confidentiality agreement (also sometimes called a non-disclosure agreement or "*NDA*") is typically the first stage for the due diligence process in a business combination or joint venture transaction (collectively, "*M&A*") as parties generally are reluctant to provide confidential information to the other side without having the protection of an NDA. The target typically proposes its form of NDA,[2] which may provide that it makes no representations regarding any information provided, and a negotiation of the NDA ensues. Some NDAs contain covenants restricting activities of the buyer after receipt of confidential information.[3]

The recent cases discussed below highlight that possible consequences of an agreement to maintain the confidentiality of information can be far reaching and are evolving. These cases also teach that, in addition to the importance of having contractual provisions sufficient to accomplish the intended objectives, director awareness of the effects of provisions in NDAs their companies enter into can have fiduciary duty implications. Thus, the lessons of these recent

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[2] An annotated seller's form of confidentiality agreement is attached as Appendix A. *See also* Article 12 of the ABA Model Asset Purchase Agreement (2001) and the Model Confidentiality Agreement accompanying the ABA Model Public Company Merger Agreement (2011).

[3] *See*, *e.g.*, *Goodrich Capital, LLC and Windsor Sheffield & Co., Inc. v. Vector Capital Corporation*, 11 Civ. 9247 (JSR) (S.D.N.Y. June 26, 2012) (confidentiality agreement prohibited use of confidential information solely to explore the contemplated business arrangement and not to minimize broker's role or avoid payment of its fees; a prospective bidder used information provided about other comparable companies to acquire one of the other companies; broker's lawsuit against that prospective bidder for breach of contract for misusing confidential information survived motion to dismiss); *In re Del Monte Foods Company Shareholders Litigation*, C.A. No. 6027-VCL, 2011 WL 532014 (Del. Ch. Feb. 14, 2011), (confidentiality agreement restricted bidders from entering into discussions or arrangements with other potential bidders; in temporarily enjoining stockholder vote on merger because target was unduly manipulated by its financial adviser, Delaware Vice Chancellor Laster faulted bidders' violation of the "no teaming" provision in the confidentiality agreement and the target's Board for allowing them to do so). *See* discussion of *Del Monte* case at then *see* Byron F. Egan, *How Recent Fiduciary Duty Cases Affect Advice to Directors and Officers of Delaware and Texas Corporations*, University of Texas School of Law 35th Annual Conference on Securities Regulation and Business Law, Austin, TX, Feb. 8, 2013, 252-55 nn.779-781, http://www.jw.com/publications/article/1830.

cases should be considered by counsel and discussed with the client before an NDA is entered into for a significant transaction.

II. No Representations

In *RAA Management, LLC v. Savage Sports Holdings, Inc.*,[4] the Delaware Supreme Court held that non-reliance disclaimer language in a confidentiality agreement was effective to bar fraud claims by a prospective buyer. The prospective buyer had been told by seller during early discussions that seller had no significant unrecorded liabilities, but due diligence showed otherwise. The confidentiality agreement provided that seller made no representations regarding any information provided and that buyer could only rely on express representations in a definitive acquisition agreement, which was never signed. The non-reliance provision in the NDA at issue in the *RAA* case provided as follows:

> 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.

After deciding not to pursue a transaction, the buyer sued seller to recover its due diligence and other deal costs. In affirming the Superior Court's dismissal of the buyer's complaint, the Delaware Supreme Court in *RAA* wrote:

> Before parties execute an agreement of sale or merger, the potential acquirer engages in due diligence and there are usually extensive precontractual negotiations between the parties. The purpose of a confidentiality agreement is to promote and to facilitate such precontractual negotiations. Non-reliance clauses in a confidentiality agreement are intended to limit or eliminate liability for misrepresentations during the due diligence process. The breadth and scope of the non-reliance clauses in a confidentiality agreement are defined by the parties to such preliminary contracts themselves. In this case, RAA and Savage did that, clearly and unambiguously, in the NDA.
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> * * *
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> The efficient operation of capital markets is dependent upon the uniform interpretation and application of the same language in contracts or other documents. The non-reliance and waiver clauses in the NDA preclude the fraud claims asserted by RAA against Savage. Under New York and Delaware law, the

[4] 45 A3d 107 (Del. 2012).

> reasonable commercial expectations of the parties, as set forth in the non-reliance disclaimer clauses in Paragraph 7 and the waiver provisions in Paragraph 8 of the NDA, must be enforced. Accordingly, the Superior Court properly granted Savage's motion to dismiss RAA's Complaint.

The *RAA* holding was consistent with other cases upholding non-reliance provisions under Delaware law. In *ABRY Partners V, L.P. v. F&W Acquisition LLC*,[5] a stock purchase agreement included a merger clause or a "buyer's promise" that it was not relying upon any representations and warranties not stated in the contract, and the Delaware Chancery Court wrote that such provisions are generally enforceable:

> When addressing contracts that were the product of give-and-take between commercial parties who had the ability to walk away freely, this court's jurisprudence has . . . honored clauses in which contracted parties have disclaimed reliance on extra-contractual representations, which prohibits the promising party from reneging on its promise by premising a fraudulent inducement claim on statements of fact it had previously said were neither made to it nor had an effect on it.
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> * * *
>
> The teaching of this court . . . is that a party cannot promise, in a clear integration clause of a negotiated agreement, that it will not rely on promises and representations outside of the agreement and then shirk its own bargain in favor of a "but we did rely on those other representations" fraudulent inducement claim. The policy basis for this line of cases is, in my view, quite strong. If there is a public policy interest in truthfulness, then that interest applies with more force, not less, to contractual representations of fact. Contractually binding, written representations of fact ought to be the most reliable of representations, and a law intolerant of fraud should abhor parties that make such representations knowing they are false.
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> * * *
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> Nonetheless, . . . we have not given effect to so-called merger or integration clauses that do not clearly state that the parties disclaim reliance upon extra-contractual statements. Instead, we have held . . . that murky integration clauses, or standard integration clauses without explicit anti-reliance representations, will not relieve a party of its oral and extra-contractual fraudulent representations. The integration clause must contain "language that . . . can be said to add up to a clear anti-reliance clause by which the plaintiff has contractually promised that it did not rely upon statements outside the contract's four corners in deciding to sign the contract." This approach achieves a sensible balance between fairness and equity — parties can protect themselves against unfounded fraud claims through explicit anti-reliance language. If parties fail to

[5] 891 A.2d 1032 (Del. Ch. 2006).

> include unambiguous anti-reliance language, they will not be able to escape responsibility for their own fraudulent representations made outside of the agreement's four corners.

In *Abry*, however, the Court allowed a fraud claim to proceed where, notwithstanding a clear anti-reliance provision, the plaintiff alleged that the defendant had intentionally lied within the four corners of the agreement.[6]

In *Pyott-Boone Electronics Inc., etc. v. IRR Trust for Donald L. Fetterolf Dated December 9, 1997*,[7] a diversity action involving the sale of a Virginia business, the disappointed buyer sued for damages for breach of the purchase agreement as well as for related tort claims and claims for breach of the Virginia Securities Act based on information that was furnished to buyer pursuant to a due diligence request months before the purchase agreement was signed. In dismissing the complaint the Court, applying Delaware law pursuant to the agreement's choice of law clause, found that plaintiff's breach of contract claim was founded on an impossibly broad interpretation of a provision to the effect that all representations and warranties in the agreement were correct and did not misstate or omit to state any material fact. The Court stated that "to reach the conclusion that the plaintiff advocates, the warranties contained in [that representation] would effectively encompass every statement any of the defendants ever made to the plaintiff regarding the sale throughout months of negotiations." In construing the provision, the Court was influenced by the purchase agreement's entire agreement provision which provided:

> This Agreement, including the Schedules and Exhibits hereto, together with the Confidentiality Agreement constitutes the entire agreement of the parties hereto respecting its subject matter and supersedes all negotiations, preliminary agreements and prior or contemporaneous discussions and understandings of the parties hereto in connection with the subject matter hereof. There are no restrictions, promises, representations, warranties, agreements or undertakings of any party hereto with respect to the transactions contemplated by this Agreement, the Confidentiality Agreement, or the Transaction Documents, other than those set forth herein or therein or in any other document required to be executed and delivered hereunder or thereunder.

The Court held that "[t]he plain language of [the entire agreement provision] states that the parties made no representations beyond those specifically included in the agreement. If the

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[6] *See* Glenn D. West & W. Benton Lewis, Jr., *Contracting to Avoid Extra-Contractual Liability—Can Your Contractual Deal Ever Really Be the "Entire" Deal?*, 63 Bus. Law. 999 (August 2009). *Cf. OverDrive, Inc. v. Baker & Taylor, Inc.*, 2011 WL 2448209 (Del.Ch. June 17, 2011), which arose out of a joint venture agreement providing that "[n]either party is relying on any representations, except those set forth herein, as inducement to execute this Agreement," and in which the plaintiff alleged that defendant intentionally lied about specific provisions in the joint venture agreement by failing to reveal plans to use confidential information received from plaintiff in arrangements with competitors; in denying defendant's motion to dismiss, Chancellor Chandler wrote that "[u]nder the teaching of *ABRY Partners V, L.P. v. F&W Acquisition LLC*, use of an anti-reliance clause in such a manner is contrary to public policy if it would operate as a shield to exculpate defendant from liability for its own intentional fraud—'there is little support for the notion that it is efficient to exculpate parties when they lie about the material facts on which a contract is premised.'"

[7] ____ F. Supp. 3d ____ (No. 1:12CV00048 Jan. 15, 2013).

plaintiff wished to rely upon the [information furnished during the due diligence process], it should have negotiated for its explicit inclusion in the [purchase agreement].” Thus, the Court gave effect to the bargain the parties made as set forth in their contract.

Texas courts have dealt with non-reliance provisions outside of the M&A arena and have imposed conditions to their enforceability not found in Delaware cases. In *Italian Cowboy Partners, Ltd. v. Prudential Ins. Co.*,[8] the Texas Supreme Court held that a merger clause does not waive the right to sue for fraud should a party later discover that the representations it relied upon before signing the contract were fraudulent, unless the clause also disclaims reliance on representations (thus negating an essential element of a claim for fraudulent inducement) and it is insufficient to merely state that promisor has not made any representations or promises except as expressly set forth in the agreement.

Italian Cowboy was influential in *Allen v. Devon Energy Holdings, L.L.C. F/K/A Chief Holdings, L.L.C. and Trevor Rees-Jones*,[9] in which Allen alleged that Chief and Trevor Rees-Jones, Chief‘s manager and majority owner, fraudulently induced him to redeem his interest two years before the company sold for almost 20 times the redemption sales price to Devon Energy Production Company, L.P. The defense focused on disclaimers and release provisions in the redemption agreement, which it contended barred Allen’s fraud claims by negating reliance or materiality as a matter of law. The Court of Appeals held that the redemption agreement did not bar Allen’s claims, and that fact issues existed as to fraud and the existence of a fiduciary relationship, in reversing the trial court’s summary judgment for the defense and for such purpose assuming the correctness of the facts alleged by Allen below.

Allen and Rees-Jones served together as partners at a prominent Dallas law firm. Allen was an oil and gas transactions lawyer, and Rees-Jones was a bankruptcy lawyer before leaving the firm to go into the oil and gas business. Allen was one of Chief’s early investors, and relied on investment advice from Rees-Jones.

In November 2003, Rees-Jones decided to redeem the minority equity interests in Chief. He sent to the minority members a letter explaining the reasons for and terms of the redemption offer, to which he attached (1) an independent valuation firm’s opinion on Chief’s market value and (2) an appraisal of Chief’s existing gas reserves and future drilling prospects. The valuation report included discounts for the sale of a minority interest and for lack of marketability. The letter also included Rees-Jones’s pessimistic assessment of a number of facts and events that could negatively impact Chief’s value in the future.

The redemption proposal languished for seven months until June 2004 when Rees-Jones notified the minority members that Chief was ready to proceed with the redemption. Three of the minority members (including Allen) accepted the redemption offer, and four others chose to retain their interests. There were positive developments in the Barnett Shale area where Chief operated and within Chief in the seven months between the November 2003 offer and the June

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8 341 S.W.3d 323 (Tex. 2011).

9 367 S.W.3d 355 (Tex. App.—Houston [1st Dist.] March 9, 2012; case settled in 2013 while writ of error pending).

2004 redemption, and Allen asserts that these events, which Allen claimed were not disclosed to him and would have materially impacted his decision to redeem his interest.

Chief provided Allen with a written redemption agreement for the first time in June 2004, and "insisted" that the contract be signed by the end of the month. The parties did not exchange drafts, and Allen stated that he had only three days to review the agreement before signing because, as he was on vacation for much of the time.

The redemption agreement contained several release clauses which are discussed below, including an "independent investigation" paragraph, a general "mutual release," and a merger clause which defendants claimed barred Allen's fraud claims negating reliance or materiality as a matter of law. The "independent investigation" paragraph provided that (1) Allen based his decision to sell on his independent due diligence, expertise, and the advice of his own engineering and economic consultants; (2) the appraisal and the reserve analysis were estimates and other professionals might provide different estimates; (3) events subsequent to the reports might "have a positive or negative impact on the value" of Chief; (4) Allen was given the opportunity to discuss the reports and obtain any additional information from Chief's employees as well as the valuation firm and the reserve engineer; and (5) the redemption price was based on the reports regardless of whether those reports reflected the actual value and regardless of any subsequent change in value since the reports. The independent investigation paragraph also included mutual releases "from any claims that might arise as a result of any determination that the value of [Chief] . . . was more or less than" the agreed redemption price at the time of the closing.

In a separate paragraph entitled "mutual releases" each party released the other from all claims that "they had or have arising from, based upon, relating to, or in connection with the formation, operation, management, dissolution and liquidation of [Chief] or the redemption of" Allen's interest in Chief, except for claims for breach of the redemption agreement or breach of the note associated with the redemption agreement. Another paragraph contained a "merger clause" stating that the redemption agreement "supersedes all prior agreements and undertakings, whether oral or written, between the parties with respect to the subject matter hereof."

Allen argued that fraudulent inducement invalidates the release provisions in the redemption agreement as "fraud vitiates whatever it touches," citing *Stonecipher v. Butts*.[10] In rejecting that argument but holding that the release provisions in the redemption agreement were not sufficiently explicit to negate Allen's fraud in the inducement claims, the Court of Appeals wrote:

> The threshold requirement for an effective disclaimer of reliance is that the contract language be "clear and unequivocal" in its expression of the parties' intent to disclaim reliance. [citations omitted] In imposing this requirement, the Texas Supreme Court has balanced three competing concerns. First, a victim of fraud should not be able to surrender its fraud claims unintentionally. [citations omitted] Second, the law favors granting parties the freedom to contract knowing that courts will enforce their contracts' terms, as well as the ability to

[10] 591 S.W.2d 806, 809 (Tex. 1979).

> contractually resolve disputes between themselves fully and finally. [citations omitted] Third, a party should not be permitted to claim fraud when he represented in the parties' contract that he did not rely on a representation . . .

The Court then said that in view of these competing concerns, Texas allows a disclaimer of reliance to preclude a fraudulent inducement claim only if the parties' intent to release such claims "is clear and specific." Among the failings the Court found with the disclaimer language in the redemption agreement were: (i) it did not say none of the parties is relying upon any statement or any representation of any agent of the parties being released hereby; (ii) the broad language releasing "all claims, demands, rights, liabilities, and causes of action of any kind or nature" did not specifically release fraudulent inducement claims or disclaim reliance on Rees-Jones and Chief"s representations (although it did release claims "of any kind or nature" (which necessarily includes fraudulent inducement), the elevated requirement of precise language requires more than a general catch-all--it must address fraud claims in clear and explicit language); (iii) the merger clause stated that the contract is the "final integration of the undertakings of the parties hereto and supersedes all prior agreements and undertakings," but did not include clear and unequivocal disclaimer of reliance on oral representations; (iv) the redemption agreement failed to state that the only representations that had been made were those set forth in the agreement; (v) it did not contain a broad disclaimer that no extra-contractual representations had been made and that no duty existed to make any disclosures; (vi) it did not provide that Allen had not relied on any representations or omissions by Chief; or (vii) it did not include a specific "no liability" clause stating that the party providing certain information will not be liable for any other person's use of the information.

The Court was careful to state it was not requiring that the words "disclaimer of reliance" must be stated in order for a disclaimer to preclude a fraudulent inducement claim or that each one of these issues must be addressed in every disclaimer. Rather, the Court stated that the redemption agreement lacked the following: "(1) an all-embracing disclaimer that Allen had not relied on any representations or omissions by Chief; (2) a specific 'no liability' clause stating that the party providing certain information will not be liable for any other person's use of the information; and (3) a specific waiver of any claim for fraudulent inducement based on misrepresentations or omissions."

Although the independent investigation clause stated that Allen "based his decision to sell" on (1) his own independent due diligence investigation, (2) his own expertise and judgment, and (3) the advice and counsel of his own advisors and consultants, the Court found that the statement of reliance on the identified factors did not clearly and unequivocally negate the possibility that Allen also relied on information he had obtained from Chief and Rees-Jones, and consistent with the terms of the redemption agreement, Allen could have relied on both. The Court found it incongruous to state that Allen could not rely on the information he was given, and noted the absence of the words "only," "exclusively," or "solely" are of critical importance in this case.

Rees-Jones and Devon argued that the redemption agreement contained language that released Allen's claims against them and that this language shows that the parties agreed broadly to disavow the factual theories he now asserts in his lawsuit. Although the redemption agreement released the parties from claims that arise from a determination that the redemption

price did not reflect Chief's market value at closing, it did not negate Allen's claims that Rees-Jones made misrepresentations and omissions concerning Chief's future prospects. Further the release disclaimed any claim by Allen based on a change in value from the 2003 appraisal to the date of redemption only, but the language did not cover Allen's claims that Rees-Jones and Chief withheld information relating to Chief's future prospects and potential value.

The Court further wrote, citing *Forest Oil Corp. v. McAllen*,[11] that even a clear and unequivocal disclaimer of reliance may not bar a fraudulent inducement claim unless (1) the terms of the contract were negotiated or boilerplate; (2) the complaining party was represented by counsel; (3) the parties dealt with each other at arm's length; and (4) the parties were knowledgeable in business matters. The Court found for defendants on two of the factors (Allen as an oil and gas attorney could not complain that he was not represented by counsel and was not knowledgeable). The Court, however, found fact issues as to the other two factors (whether the contract was negotiated and whether the parties dealt with each other at arm's length) and declined to grant Defendant's motion for summary judgment. The Court declined to say whether all four tests must be satisfied for an otherwise clear and unequivocal disclaimer of reliance to be enforceable.

In *Staton Holdings, Inc. v. Tatum, L.L.C.*,[12] a Texas Court of Appeals held, as a matter of first impression, that an express-intent requirement, under which a release of liability is enforceable only if the intent to grant such a release is expressed in specific terms within the four corners of the contract, applies to prospective releases of future breaches of warranty in service transactions. In so holding, the Court wrote:

> We begin by reviewing Texas's express-negligence jurisprudence. Under Texas law, certain kinds of contractual provisions that call for an extraordinary shifting of risk between the parties are subject to the fair-notice doctrine. *See Dresser Indus., Inc. v. Page Petroleum, Inc.*, 853 S.W.2d 505, 508 (Tex. 1993). In *Dresser Industries*, the Texas Supreme Court held that a release of liability for future negligence is enforceable only if it comports with both prongs of the fair-notice doctrine: the conspicuousness requirement and the express-negligence test. Id. at 509. Under the express-negligence test, a release of future negligence is enforceable only if the intent to grant such a release is expressed in specific terms within the four corners of the contract. *Id.* at 508; *see also Ethyl Corp. v. Daniel Constr. Co.*, 725 S.W.2d 705, 708 (Tex. 1987) (adopting the express-negligence test in the context of indemnity clauses). If a similar express-intent rule applies to breach-of-warranty claims, the release involved in this case is suspect because it does not expressly state that Staton is waiving claims for future breaches of warranty.
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> The Texas Supreme Court has extended the express-negligence test to some claims besides negligence. In 1994, the supreme court held that an indemnity agreement will not be construed to indemnify a party against statutorily imposed strict liability unless the agreement expressly states the parties' intent to

[11] 268 S.W.3d 51 (Tex. 2008).

[12] 345 S.W.3d 729 (Tex.App.—Dallas 2011).

provide for indemnification of such claims. *Houston Lighting & Power Co. v. Atchison, Topeka & Santa Fe Ry. Co.*, 890 S.W.2d 455, 458-59 (Tex. 1994). The court indicated that the same express-intent rule would apply to claims for strict products liability.

* * *

After considering the reasons supporting *HL & P's* extension of the express-intent rule to strict liability, we conclude the express-intent rule applies to breach-of-warranty claims.

* * *

The release involved in this case does not expressly release claims for future breaches of warranty, so it does not bar Staton's breach-of-warranty claims . . .

The *Staton Holdings* case is another example of a Texas court acknowledgement that Texas law respects freedom of contract, including the right of parties to contractually limit their tort and other liabilities arising in respect of contracts, but that the Texas courts regard such a shifting of liability as so extraordinary that they require it to be clear, unequivocal and conspicuous in the contract so that there is no question that the parties knowingly bargained for that outcome. In that respect *Staton Holdings* is consistent with the results in *Italian Cowboy* and *Allen*, although the application of express negligence principles is new and an extension. These three 2011 cases suggest that the following principles should be considered when attempting to contractually limit liabilities under Texas law:

- Do not appear to use boilerplate provisions, however comprehensive, and tailor the limitation of liability provision for each transaction in a way that shows that it has been specifically negotiated and is not merely a boilerplate provision.

- Expressly disclaim reliance on any representations that are not embodied in the four corners of the agreement, and perhaps even in particular enumerated sections thereof.

- Expressly state that no reliance is being placed on any statements (i) by any representative of any of the parties whose liability is limited or (ii) in the dataroom (if such is the case).

- Expressly state that fraud in the inducement claims are being released.

- Expressly state that no reliance has been placed on any prior representations.

- Include both broad inclusive words of limitation of liability and then specifically address the particular kinds of representations not being relied upon.

- Put the limitation of liability provision in italics, bold face or other conspicuous type.[13]

A non-reliance provision based on those Texas principles might read as follows:

____ Entire Agreement, Non-reliance, Exclusive Remedies and Modification

(a) This Agreement supersedes all prior agreements, whether written or oral, between the parties with respect to its subject matter (including any letter of intent and any confidentiality agreement between Buyer and Seller) and constitutes (along with the Disclosure Letter, Exhibits and other documents delivered pursuant to this Agreement) a complete and exclusive statement of the terms of the agreement between the parties with respect to its subject matter. This Agreement may not be amended, supplemented or otherwise modified except by a written agreement executed by the party to be charged with the amendment.

(b) Except for the representations and warranties contained in Article 3 [the representations and warranties section of the Agreement], none of Seller or any Shareholder has made any representation or warranty, expressed or implied, as to Seller or as to the accuracy or completeness of any information regarding Seller furnished or made available to Buyer and its representatives, and none of Seller or any Shareholder shall have or be subject to any liability to Buyer or any other Person resulting from the furnishing to Buyer, or Buyer's use of or reliance on, any such information or any information, documents or material made available to Buyer in any form in expectation of, or in connection with, the transactions contemplated by this Agreement.

(c) Following the Closing, the sole and exclusive remedy for any and all claims arising under, out of, or related to this Agreement, or the sale and purchase of the Seller, shall be the rights of indemnification set forth in Article 11 [the indemnification section of the Agreement] only, and no person will have any other entitlement, remedy or recourse, whether in contract, tort or otherwise, it being agreed that all of such other remedies, entitlements and recourse are expressly waived and released by the parties hereto to the fullest extent permitted by law.

(d) The provisions of this Section 13.7 [the entire agreement provision] and the limited remedies provided in Article 11, were specifically bargained for between Buyer and Sellers and were taken into account by

[13] *See* Comment to Section 11.11 on pp 259-262 of Byron F. Egan, *Acquisition Structure Decision Tree*, TexasBarCLE & Business Law Section of State Bar of Texas, Choice & Acquisition of Entities in Texas Course, San Antonio, TX, May 24, 2013, http://www.jw.com/publications/article/1844, regarding the express negligence doctrine.

Buyer and the Sellers in arriving at the Purchase Price. The Sellers have specifically relied upon the provisions of this Section 13.7 and the limited remedies provided in Article 11 in agreeing to the Purchase Price and in agreeing to provide the specific representations and warranties set forth herein.[14]

(e) All claims or causes of action (whether in contract or in tort, in law or in equity) that may be based upon, arise out of or relate to this Agreement, or the negotiation, execution or performance of this Agreement (including any representation or warranty, whether written or oral, made in or in connection with this Agreement or as an inducement to enter into this Agreement), may be made only against the entities that are expressly identified as parties hereto. No Person who is not a named party to this Agreement, including without limitation any director, officer, employee, incorporator, member, partner, stockholder, Affiliate, agent, attorney or representative of any named party to this Agreement ("Non-Party Affiliates"), shall have any liability (whether in contract or in tort, in law or in equity, or based upon any theory that seeks to impose liability of an entity party against its owners or affiliates) for any obligations or liabilities arising under, in connection with or related to this Agreement or for any claim based on, in respect of, or by reason of this Agreement or its negotiation or execution; and each party hereto waives and releases all such liabilities, claims and obligations against any such Non-Party Affiliates. Non-Party Affiliates are expressly intended as third party beneficiaries of this provision of this Agreement.

(f) This Agreement may not be amended, supplemented or otherwise modified except by a written agreement executed by the party to be charged with the amendment.

While the foregoing provision is lengthy and is intended to address the concerns expressed by the courts in the *Italian Cowboy*, *Allen* and *Staton Holdings* cases, circumstances and future cases will no doubt suggest revision of the foregoing in particular cases.

[14] This alternative is derived from the Model Provisions suggested in Glenn D. West and W. Benton Lewis, Jr., *Contracting to Avoid Extra-Contractual Liability—Can Your Contractual Deal Ever Really Be the "Entire" Deal?*, 64 Bus. Law. 999, 1038 (Aug. 2009), as well as the *Italian Cowboy*, *Allen* and *Staton Holdings* discussed above; *see* Byron F. Egan, Patricia O. Vella and Glenn D. West, *Contractual Limitations on Seller Liability in M&A Agreements*, University of Texas School of Law 7th Annual Mergers and Acquisitions Institute, Dallas, TX, October 20, 2011, at Appendix B, *available at* http://images.jw.com/com/publications/1669.pdf.

III. De Facto Standstill

In *Martin Marietta Materials, Inc. v. Vulcan Materials Co.*,[15] the Delaware Supreme Court upheld a pair of NDAs and temporarily enjoined Martin Marietta Materials from prosecuting a proxy contest and proceeding with a hostile bid for its industry rival Vulcan Materials Company. After years of communications regarding interest in a friendly transaction, Vulcan and Martin Marietta in the spring of 2010 executed two NDAs to enable their merger and antitrust discussions, each governed by Delaware law:

- A general non-disclosure agreement requiring each party to use the other's confidential information "solely for the purpose of evaluating a Transaction," which was defined as "a possible business combination transaction . . . between" the two companies, and prohibiting disclosure of the other party's evaluation material and of the parties' negotiations except as provided in the agreement, which had a term of two years.

- A joint defense and confidentiality agreement, intended to facilitate antitrust review signed about two weeks after the non-disclosure agreement requiring each party to use the other's confidential information "solely for the purposes of pursuing and completing the Transaction," which was defined as "a potential transaction being discussed by" the parties, and restricting disclosure of confidential materials.

Neither NDA contained an express standstill provision. When the agreements were signed, both parties were seeking to avoid being the target of an unsolicited offer by the other or by another buyer. Accordingly, the agreements protected from disclosure the companies' confidential information as well as the fact that the parties had merger discussions.

After its economic position improved relative to Vulcan, Martin Marietta decided to make a hostile bid for Vulcan and also launched a proxy contest designed to make Vulcan more receptive to its offer. The Court found that Martin Marietta used protected confidential material in making and launching its hostile bid and proxy contest.

The Court then construed the language of the NDAs to determine that Martin Marietta had breached those agreements by (1) using protected information in formulating a hostile bid, since the information was only to be used in an agreed-to business combination; (2) selectively disclosing protected information in one-sided securities filings related to its hostile bid, when such information was not disclosed in response to a third-party demand and when Martin Marietta failed to comply with the agreements' notice and consent process; and (3) disclosing protected information in non-SEC communications in an effort to "sell" its hostile bid. The Court emphasized that its decision was based entirely on contract law, and its reasoning did not rely on any fiduciary principles.

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[15] No. 254,2012, C.A. No. 7102 (Del. July 10, 2012), affirming *Martin Marietta Materials, Inc. v. Vulcan Materials Co.*, C.A. 7102-CS (Del. Ch. May 4, 2012). *See* XVII Deal Points (The Newsletter of the Mergers and Acquisitions Committee of the ABA Bus. L. Sec.) at 23-26 (Summer 2012).

The Court held that, although the NDAs did not expressly include a standstill provision, Martin Marietta's breaches entitled Vulcan to specific performance of the agreements and an injunction. The Court therefore enjoined Martin Marietta, for four months, from prosecuting a proxy contest, making an exchange or tender offer, or otherwise taking steps to acquire control of Vulcan's shares or assets.

IV. Express Standstill and "Don't Ask, Don't Waive" Provisions

Some NDAs do contain express standstill provisions that (i) prohibit the bidder from making an offer for the target without an express invitation from its Board and (ii) preclude the bidder from publicly or privately asking the Board to waive the restriction.[16] Such provisions in NDAs, which are sometimes referred to as "Don't Ask, Don't Waive" provisions, are designed to extract the highest possible offer from the bidder because the bidder only has one opportunity to make an offer for the target unless the target invites the bidder to make another offer *sua sponte*.[17] Bidders who do not execute NDAs with "Don't Ask, Don't Waive" provisions generally are not precluded from submitting multiple offers for the company, even after a winning bidder emerges from an auction.[18]

The legitimacy of "Don't Ask, Don't Waive" provisions was recognized in *In re Topps Co. Shareholders Litigation*,[19] in which Chancellor (then Vice Chancellor) Strine enjoined a stockholder vote on a merger until the target waived a standstill agreement. The target's Board had refused to waive the standstill in order to permit a strategic rival to make a tender offer on the same terms it had proposed to the Board and to communicate with Topps stockholders in connection with the vote on the proposed transaction the Board had approved with a private equity investor. In holding that the Board was misusing the standstill agreement solely in order to deny its stockholders the opportunity to accept an arguably more attractive deal and to preclude them from receiving additional information about rival's version of events, the Court wrote that standstill agreements can have legitimate purposes, including in the final round of an auction where a Board in good faith seeks to extract the last dollar from the remaining bidders, but can be subject to abuse:

> "Standstills serve legitimate purposes. When a corporation is running a sale process, it is responsible, if not mandated, for the board to ensure that confidential information is not misused by bidders and advisors whose interests are not aligned with the corporation, to establish rules of the game that promote an orderly auction, and to give the corporation leverage to extract concessions from the parties who seek to make a bid.

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16 Peter J. Walsh, Jr., Janine M. Salomone and David B. DiDonato, *"Don't Ask, Don't Waive" Standstill Provisions: Impermissible Limitation on Director Fiduciary Obligations or Legitimate, Value-Maximizing Tool?*, ABA Business Law Section, Business Law Today (January 23, 2013), http://apps.americanbar.org/buslaw/blt/content/2013/01/delawareinsider.shtml.

17 *Id.*

18 *Id.*

19 *In re Topps Company Shareholders Litigation*, 926 A.2d 58 (Del. Ch. 2007); *see also* Byron F. Egan, *How Recent Fiduciary Duty Cases Affect Advice to Directors and Officers of Delaware and Texas Corporations*, University of Texas School of Law 35th Annual Conference on Securities Regulation and Business Law, Austin, TX, Feb. 8, 2013, 198-203 nn.641-648, http://www.jw.com/publications/article/1830.

> "But standstills are also subject to abuse. Parties like Eisner often, as was done here, insist on a standstill as a deal protection. Furthermore, a standstill can be used by a target improperly to favor one bidder over another, not for reasons consistent with stockholder interest, but because managers prefer one bidder for their own motives."[20]

Later in *In re Celera Corp. Shareholder Litigation*,[21] Vice Chancellor Parsons held that although in isolation the "Don't Ask, Don't Waive" provisions arguably fostered the legitimate objectives set forth in *Topps*, when viewed with the no-solicitation provision in the merger agreement, a colorable argument existed that the collective effect created an informational vacuum, increased the risk that directors would lack adequate information, and constituted a breach of fiduciary duty. The Court commented that the "Don't Ask, Don't Waive" standstill provisions blocked certain bidders from notifying the Board of their willingness to bid, while the no-solicitation provision in the merger agreement contemporaneously blocked the Board from inquiring further into those parties' interests, and, thus, diminished the benefits of the Board's fiduciary-out in the no-solicitation provision and created the possibility that the Board would lack the information necessary to determine whether continued compliance with the merger agreement would violate its fiduciary duty to consider superior offers.

In late 2012, two Chancery Court opinions, *In re Complete Genomics, Inc. Shareholder Litigation*[22] and *In re Ancestry.com Inc. Shareholder Litigation*,[23] considered the propriety of a target company's inclusion in standstill agreements of a "Don't Ask, Don't Waive" provision which became the "emerging issue of December of 2012," in the words of Chancellor Strine. In *Complete Genomics* the Board of a company in financial straits decided to explore "all potential strategic alternatives," including initiation of a process to find a buyer. Prospective bidders were required to sign confidentiality agreements, some of which included standstill provisions that prohibited the bidders from launching a hostile takeover and prohibited the prospective bidders from *publicly* asking the Board to waive the standstill restrictions, but one also forbade the prospective bidder from making a *nonpublic* request for such a waiver.[24] In a bench ruling, Vice Chancellor Laster analogized the "Don't Ask, Don't Waive" provision (at least insofar as it prohibited *nonpublic* waiver requests) to "bidder-specific no-talk" clauses criticized by the Court of Chancery in previous cases as being violative of the Board's "duty to take care to be informed of all material information reasonably available," rendering it the "legal equivalent of willful blindness" to its fiduciary duties.[25] The Vice Chancellor commented that while "a board doesn't

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[20] 926 A.2d at 91 (Del. Ch. 2007).

[21] C.A. No. 6304-VCP (Del. Ch. Mar. 23 2012) (Transcript), *aff'd in part rev'd in part on other grounds*, 2012 WL 6707746 (Del. Dec. 27, 2012).

[22] Telephonic Oral Argument and the Court's Ruling, *In re Complete Genomics, Inc. S'holder Litig.*, C.A. No. 7888-VCL (Del. Ch. Nov. 27, 2012).

[23] The Court's Ruling on Plaintiffs' Motion for Preliminary Injunction, *In re Ancestry.com Inc. S'holder Litig.*, C.A. No. 7988-CS (Del. Ch. Dec. 17, 2012).

[24] Robert S. Reder, *Delaware Chancellor Weighs in on "Don't Ask, Don't Waive" Provision of Standstill Agreement*, Bloomberg BNA Corporate Practice Library, 28 CCW 24 (2013).

[25] The Vice Chancellor wrote:

> In my view, a Don't Ask, Don't Waive Standstill resembles a bidder-specific no-talk clause. In *Phelps Dodge Corporation v. Cyprus Amax* [1999 WL 1054255, at *2 (Del. Ch. Sept. 27,

necessarily have an obligation to negotiate," it "does have an ongoing statutory and fiduciary obligation to provide a current, candid and accurate merger recommendation," which encompasses "an ongoing fiduciary obligation to review and update its recommendation," and a "Don't Ask, Don't Waive" provision in a standstill is "impermissible" to the extent it limits a board's "ongoing statutory and fiduciary obligations to properly evaluate a competing offer, disclose material information, and make a meaningful merger recommendation to its stockholders." These are ongoing obligations no matter how pristine the process adopted by the Board in making its initial decision to approve a transaction and recommend it to stockholders.

In *Ancestry.com*, the bidders in an auction initiated by the target were required to sign confidentiality agreements containing standstill restrictions that included "Don't Ask, Don't Waive" provisions.[26] The ultimate winner in this process was a private equity firm which did not "demand an assignment" of the provision in the merger agreement, thereby leaving it within the target's discretion whether or not to allow unsuccessful bidders to make unsolicited topping bids prior to receiving stockholder approval. Chancellor Strine generally praised the process followed by the Ancestry Board, noting that the Board was "trying to create a competitive dynamic" and the process "had a lot of vibrancy and integrity to it … ." With respect to the "Don't Ask, Don't Waive" provision, the Chancellor noted that while it "is a pretty potent provision," he was aware of "no statute" or "prior ruling of the Court" that rendered such provisions "per se invalid," and wrote that a "Don't Ask, Don't Waive" provision actually may be used by a "well-motivated seller … as a gavel" for "value-maximizing purposes" by communicating to bidders that "there really is an end to the auction for those who participate," creating an incentive for bidders to "bid your fullest because if you win, you have the confidence of knowing you actually won that auction at least against the other people in the process," which may attract prospective bidders to a process that has "credibility so that those final-round bidders know the winner is the winner, at least as to them."

The Chancellor was, however, troubled by the target's failure to disclose in proxy materials sent to stockholders the potential impact of the "Don't Ask, Don't Waive" provision on the bidding process, warned that directors "better be darn careful" in running an auction process to be sure that "if you're going to use a powerful tool like that, are you using it consistently with your fiduciary duties, not just of loyalty, but of care." Chancellor Strine faulted the lack of proxy statement disclosures regarding the "Don't Ask, Don't Waive" provision as "probabilistically in violation of the duty of care" since the Board was "not informed about the potency of this clause," and it "was not used as an auction gavel." Once the winning bidder "did not demand an assignment of it," the Board did not "waive it in order to facilitate those bidders which had signed up the standstills being able to make a superior proposal." The Chancellor "enjoin[ed] the deal subject to those disclosures being promptly made."

1999)], Chancellor Chandler considered whether a target board had breached its fiduciary duties by entering into a merger agreement containing a no-talk provision. Unlike a traditional no-shop clause, which permits a target board to communicate with acquirers under limited circumstances, a no-talk clause -- and here I'm quoting from the Chancellor -- "not only prevents a party from soliciting superior offers or providing information to third parties, but also from talking to or holding discussions with third parties."

[26] Robert S. Reder, *Delaware Chancellor Weighs in on "Don't Ask, Don't Waive" Provision of Standstill Agreement*, Bloomberg BNA Corporate Practice Library, 28 CCW 24 (2013).

V. Lessons from the Cases

The cases discussed above teach that even a simple agreement to maintain the confidentiality of information can be enforced in ways that can change the course of a major transaction. Further, the emphasis placed by the Courts on the directors understanding the power of NDA provisions suggests that counsel should consider the implications thereof on the fiduciary duties of directors and help their clients understand them.

Confidentiality Agreement

PRELIMINARY NOTE

The confidentiality or non-disclosure agreement (**"Confidentiality Agreement"**) is usually the first document in the acquisition process, and is signed by the prospective buyer (**"Recipient"**) before the seller (**"Discloser"**) provides any confidential information. Confidentiality agreements are primarily a concern for the seller who is disclosing essential and very confidential information regarding its assets and business to the prospective buyer who is currently or, if the transaction is not consummated, may later become a competitor of the seller or the ultimate purchaser of its business. Consequently, this form of Confidentiality Agreement has been prepared as a Discloser's first draft and includes provisions favorable to the Discloser. The Recipient may want to modify many of its provisions to be more in the Recipient's favor.

This Confidentiality Agreement has no "sunset" provision and is silent on the topics of the duration of obligations of confidentiality and to what extent the obligations continue if the acquisition closes or does not close. Absent such a provision, the Discloser may take the position that they continue forever. The Recipient, on the other hand, may think that even the Discloser's proprietary know-how will become obsolete and assert that all obligations of confidentiality should come to an end at some early point. The parties may consider whether their interests would be served by "sunsetting" the Confidentiality Agreement as a whole or by providing different survival provisions for different categories of information or different obligations of confidentiality. If the parties decide to enter into a transaction, the definitive acquisition agreement often deals with the extent to which the Confidentiality Agreement (or portions of it) will be modified or superseded by that agreement, particularly in terms of the typical "integration" provision.

This form of Confidentiality Agreement takes the form of a "unilateral agreement" that protects Discloser's confidential information in the hands of Recipient. Discloser may want details about Recipient's capacity to finance the transaction, other transactions Recipient has done, the identity of Recipient's lenders and other confidential information. Moreover, where the consideration includes securities of buyer, the Discloser may require confidential information about the Recipient at a very early stage. Accordingly, the Recipient and the Discloser may find it appropriate to make obligations under the Confidentiality Agreement reciprocal and bilateral. An alternative, when the parties have initially signed a unilateral Confidentiality Agreement presented by the Discloser (the seller) to the Recipient (the buyer), is for the parties to enter into a mirror agreement to protect the Recipient's information in the hands of the Discloser (of course, in that case, the prospective buyer will be the **"Discloser,"** and the prospective seller will be the **"Recipient"**).

FORM OF CONFIDENTIALITY AGREEMENT

[Date]

[Name]
[Discloser]
[Address]

PRIVATE AND CONFIDENTIAL

Dear __________:

In connection with the consideration by __________ (**"Recipient"**) of a possible transaction (the **"Transaction"**) with __________ (**"Discloser"**), Recipient has requested access to certain information, properties and personnel of Discloser.

COMMENT

In its first sentence, this Confidentiality Agreement defines that Recipient's use of Confidential Information is limited to Recipient's consideration of the proposed transaction. The Confidentiality Agreement does not characterize the transaction, does not identify the parties as "buyer" and "seller," and describes the transaction only as "possible" to avoid implication that any agreement about the transaction has been made between the parties or will be created by the Confidentiality Agreement.

In consideration for and as a condition to Discloser's furnishing access to such information, properties and personnel of Discloser as Discloser, in its sole discretion, agrees to deliver or otherwise make available (**"disclose"**) to Recipient, Recipient agrees to the terms and conditions set forth in this agreement:

COMMENT

Although the Confidentiality Agreement does not expressly provide that Discloser must disclose all information requested by Recipient, consideration is often given to the inclusion here of the following language: "Discloser may, in its sole discretion, withhold information where it concludes that the disclosure of such information would violate applicable law, breach a duty, subject Discloser to risk of a material penalty, or be detrimental to its interests, in which case it shall advise Recipient as to the general nature or category of information withheld." In some circumstances, the Discloser may be prohibited from disclosing certain information by restrictions under its existing contractual relationships.

1. CONFIDENTIAL AND PROPRIETARY NATURE OF THE INFORMATION

Recipient acknowledges the confidential and proprietary nature of the Confidential Information (as defined below), agrees to hold and keep the Confidential Information as

provided in this agreement and otherwise agrees to each and every restriction and obligation in this agreement.

2. CONFIDENTIAL INFORMATION

As used in this agreement, the term **"Confidential Information"** means and includes any and all of the items described in paragraphs (a) and (b) below that has been or may hereafter be disclosed to Recipient by Discloser or by the directors, officers, employees, agents, consultants, advisors or other representatives, including legal counsel, accountants and financial advisors (**"Representatives"**) of Discloser:

(a) trade secrets concerning the business and affairs of Discloser (which includes the materials dated ________ ____, 20___, and disclosed to Recipient by __________), product specifications, data, know-how, formulae, compositions, processes, designs, sketches, photographs, graphs, drawings, samples, inventions and ideas, past, current, and planned research and development, current and planned manufacturing or distribution methods and processes, customer lists, current and anticipated customer requirements, price lists, supplier lists, market studies, business plans, computer software and programs (including object code and source code), computer software and database technologies, systems, structures and architectures (and related processes, formulae, composition, improvements, devices, know-how, inventions, discoveries, concepts, ideas, designs, methods and information), __________ and any other information, however documented, that is a trade secret within the meaning of __________ § ____-____-____ [applicable state trade secret law]); and

(b) information concerning the business and affairs of Discloser (which includes historical financial statements, financial projections and budgets, historical and projected sales, capital spending budgets and plans, the names and backgrounds of key personnel, personnel training techniques and materials and _____), however documented, or is otherwise obtained from review of Discloser's documents or property or discussions with Discloser's Representatives or by Recipient's Representatives (including current or prospective financing sources) or Representatives of Recipient's Representatives irrespective of the form of the communication, and also includes all notes, analyses, compilations, studies, summaries and other material prepared by Recipient or Recipient's Representatives containing or based, in whole or in part, upon any information included in the foregoing.

Any trade secrets of Discloser will also be entitled to all of the protections and benefits under _____ Section _____ [applicable state trade secret law] and any other applicable law. If any information that Discloser deems to be a trade secret is found by a court of competent jurisdiction not to be a trade secret for purposes of this agreement, such information will in any event still be considered Confidential Information for purposes of this agreement. In the case of trade secrets, Recipient hereby waives any requirement that Discloser submit proof of the economic value of any trade secret or post a bond or other security.

To the extent that any Confidential Information may include materials subject to the attorney-client privilege, the Discloser is not waiving and will not be deemed to have waived or diminished its attorney work-product protections, attorney-client privileges or similar protections and privileges as a result of disclosing any Confidential Information (including Confidential

Information related to pending or threatened litigation) to Recipient, regardless of whether Discloser has asserted or is or may be entitled to assert such privileges and protections. The parties (a) share a common legal and commercial interest in all such Confidential Information that is subject to such privileges and protections; (b) are or may become joint defendants in proceedings to which such Confidential Information covered by such protections and privileges relates; and (c) intend that such privileges and protections remain intact should either party become subject to any actual or threatened proceeding to which such Confidential Information covered by such protections and privileges relates. In furtherance of the foregoing, Recipient shall not claim or contend, in proceedings involving either party, that Discloser waived its attorney work-product protections, attorney-client privileges or similar protections and privileges with respect to any information, documents or other material not disclosed to Recipient due to Discloser disclosing Confidential Information (including Confidential Information related to pending or threatened litigation) to Recipient.

COMMENT

The term **"Confidential Information"** is defined broadly to include all information concerning the business and affairs of Discloser that will be disclosed to Recipient. Exceptions are carved out—not from the definition but rather as exceptions to the obligation of nonuse and nondisclosure in Sections 6 and 7 below—in order to provide for circumstances in which the information is no longer required to be treated as Confidential Information. Such circumstances include information that becomes generally available to the public (other than by a result of unauthorized disclosure) or information that is otherwise made available to Recipient without a wrongful act on the part of the party providing the information.

In the absence of a confidentiality agreement and subject to applicable state law, trade secrets, but not confidential information, can be protected from disclosure. *See* RESTATEMENT OF THE LAW OF UNFAIR COMPETITION § 41, cmt. d (1995). Many states have adopted a version of the Uniform Trade Secrets Act that defines information as a "trade secret" if it (a) derives economic value from being generally unknown to other persons who can obtain economic value from its disclosure or use and (b) is subject to efforts that are reasonable under the circumstances to maintain its secrecy or confidentiality. *See* UNIF. TRADE SECRETS ACT § 1(4), 14 U.L.A. 438 (1990) and 152 (1998 supp.). The Restatement of the Law of Unfair Competition Section 39 defines trade secrets slightly differently, but comment b to that section states that the definition is intended to be consistent with the definition in the Uniform Trade Secrets Act. The Uniform Trade Secrets Act and the Confidentiality Agreement complement one another because protection of information under such trade secret law provides Discloser with another enforceable way to prevent misappropriation of information. Many states have also adopted criminal statutes specifically addressed to the misappropriation of trade secrets. In other states, more general criminal statutes have been interpreted to reach such misappropriations. In some circumstances, a misappropriation of trade secrets may also violate federal wire and mail fraud statutes (18 U.S.C. §§ 1341, 1343), the National Stolen Property

Act (18 U.S.C. § 2314) and the Economic Espionage Act of 1996 (18 U.S.C. §§ 1831 et seq.).

The Confidentiality Agreement serves three primary purposes: (a) it expands the state law protection of trade secrets to confidential information, (b) it clarifies and delineates the obligations of Recipient, particularly with respect to its Representatives, and (c) it helps Discloser demonstrate that it used appropriate efforts to protect the information.

The Uniform Trade Secrets Act Section 1(4) requires reasonable efforts "under the circumstances" to maintain the secrecy of information constituting trade secrets, and such efforts are at least advisable for confidential information. While executing the Confidentiality Agreement demonstrates such efforts, stamping materials to be protected "CONFIDENTIAL" further demonstrates such efforts. If the parties decide to require that all documents containing confidential information be stamped, the Discloser should include a provision that its inadvertent failure to stamp a document is not a waiver of its confidentiality. The Discloser should, at a minimum, keep a list or copies of all documents disclosed to the Recipient and all persons with whom the Recipient spoke.

Both the Discloser and the Recipient may find it advantageous to have significant oral information promptly confirmed by the Discloser in writing as being confidential and acknowledged by the Recipient. In the event of a dispute over the disclosure, the evidentiary problems of proof are lessened when oral communications are reduced to writing. Because of the difficulty in consistently adhering to such requirement, the Confidentiality Agreement excludes such a requirement. Additionally, there may be oral disclosures sufficiently sensitive that neither party wants them reduced to writing.

Special issues may arise when the Recipient is a competitor or potential competitor of the Discloser. In such cases, the Recipient may not wish to review (and the Discloser may not wish the Recipient to review) certain technical information in order to preclude any future claims of misuse of proprietary information. It may prove advantageous to list or otherwise describe all such excluded materials in, or on a schedule or supplement to, the Confidentiality Agreement.

Further, when the acquisition involves a competitor, special steps need to be taken in connection with the disclosure of pricing or other competitively sensitive information. The Recipient's possession of such information could be damaging evidence if the acquisition is not completed and an antitrust claim is subsequently asserted. Alternatives to not disclosing such information are to (a) limit disclosure to the Recipient's personnel who are not in a position to use the information in a manner that would violate the antitrust laws or (b) defer disclosure until as late as possible in the process.

The risks that preacquisition disclosure of sensitive information will violate antitrust laws can be considerable. In the settlement of a divestiture case in which it found unlawful preacquisition transfers of competitively sensitive information, the Federal Trade Commission imposed lengthy bans upon the divesting company's obtaining or providing such information in any future acquisition of a competitor's stock or assets without specific safeguards. *In re* Insilco Corp., FTC File No. 961-0106, 5 Fed. Trade Reg. Rptr. (CCH) ¶ 24,319 (Aug. 27, 1997); *see* Blumenthal, *The Scope of Permissible Coordination between Merging Entities prior to Consummation*, 63 ANTITRUST L.J. 1 (1994).

The final paragraph of Section 2 addresses how to disclose sufficient information to the Recipient to facilitate a meaningful evaluation of litigation-related confidential information without waiving the attorney-client and other privileges that protect the information.

Furthermore, if the acquisition is not consummated, the Recipient should be required to return the competitively sensitive information (together with copies and derivative materials) or to certify to the Discloser that all copies of such information have been destroyed. Section 9 of the Confidentiality Agreement imposes such a requirement.

3. RESTRICTED USE OF CONFIDENTIAL INFORMATION

Recipient agrees that the Confidential Information (a) will be kept confidential by Recipient and Recipient's Representatives and (b) without limiting the foregoing, will not be disclosed by Recipient or Recipient's Representatives to any person (including current or prospective financing sources) except with the specific prior written consent of _____ (the **"Discloser Contact"**) [a designated individual or a designated position, such as chief financial officer] or except as expressly otherwise permitted by this agreement. It is understood that Recipient may disclose Confidential Information to only those of Recipient's Representatives who (a) require such material for the purpose of evaluating the Transaction and (b) are informed by Recipient of the confidential nature of the Confidential Material and the obligations of this agreement. Recipient further agrees that Recipient and Recipient's Representatives will not use any of the Confidential Information either for any reason or purpose other than to evaluate and to negotiate the Transaction. Recipient also agrees to be responsible for enforcing this agreement as to Recipient's Representatives and to take such action, legal or otherwise, to the extent necessary to cause them to comply with this agreement and thereby prevent any disclosure of the Confidential Information by any of Recipient's Representatives (including all actions that Recipient would take to protect its own trade secrets and confidential information) except as permitted by this agreement.

COMMENT

The Confidentiality Agreement defines who will be allowed to use the Confidential Information and the scope and extent of such use.

The foregoing provisions require only that Recipient inform the persons to whom the Confidential Information is disclosed of the confidential nature and the obligations under this Agreement. A Discloser may want to add clauses providing that the Confidential Information may not be disclosed except to persons approved in writing by the Discloser contact prior to any disclosure and requiring such persons to acknowledge, in writing, the obligations of the Confidentiality Agreement. Such written acknowledgment could be accomplished by having a one-sentence cover letter signed by each Representative ("I hereby agree to be bound by the attached agreement from X to Y dated Z") or (as a less burdensome alternative) by having the Recipient's Representatives sign a statement acknowledging that they are familiar with the confidentiality obligations in the Confidentiality Agreement and agree to be bound by its provisions. Another alternative is to merely provide in the Confidentiality Agreement that the Recipient retains responsibility for any unauthorized disclosures or use of the confidential information and for ensuring compliance with the Confidentiality Agreement. This approach may be more acceptable to the Discloser if the Recipient's employees have signed secrecy agreements as a condition of employment with the Recipient.

4. NONDISCLOSURE OF TRANSACTION

Except as expressly permitted by Section 3 and except as expressly permitted by a definitive agreement with respect to the Transaction, if any, entered into between the parties, neither Recipient, Discloser nor their Representatives will disclose to any person the fact that the Confidential Information has been disclosed to Recipient or Recipient's Representatives or that Recipient or Recipient's Representatives have inspected any portion of the Confidential Information or that any discussions or negotiations are taking place concerning the Transaction, provided, however, Recipient and its Representatives may make such a disclosure if, and solely to the extent that, Discloser has already done so or Recipient has received the written opinion of its outside counsel that such a disclosure must be made by Recipient in order that it not commit a violation of law, and further provided, Recipient and its Representatives shall consult with Discloser, to the extent reasonably practicable, before making any such disclosure, and any such permitted disclosure shall not affect or impair Recipient's obligations of confidentiality with respect to the Confidential Information. Without limiting the generality of the foregoing, Recipient further agrees that, without the prior written consent of Discloser, Recipient will not, directly or indirectly, enter into any agreement, arrangement or understanding, or any discussions that might lead to such an agreement, arrangement or understanding, with any person regarding a possible transaction involving Discloser[, provided, however, nothing contained herein shall be deemed to inhibit, impair or restrict the ability of Recipient or its Representatives to have discussions or negotiations with other persons relating to potential financing and/or partnering in connection with and/or investment in the Transaction so long as each of such persons agrees in writing to be bound by the terms of this agreement].

COMMENT

As the parties often want to keep secret the very fact of any negotiation discussions, the Confidentiality Agreement prevents the disclosure of such information or the fact that negotiations are taking place.

Because Recipient may need to disclose the pendency of the discussions under certain circumstances (e.g., under federal securities laws), Recipient is permitted to disclose information without violating Section 4 based upon the written opinion of its counsel that the disclosure is required by applicable law. Recipient is obligated to consult with Discloser, to the extent reasonably practicable, before making any such disclosure.

5. DISCLOSER CONTACT

All requests by Recipient or Recipient's Representatives for Confidential Information, meetings with Discloser's personnel or Representatives or inspection of Discloser's properties must be made to the Discloser Contact.

COMMENT

The Confidentiality Agreement imposes a procedural "bottleneck" whereby all communications with employees of Discloser must be approved by a designated Representative of Discloser—the Discloser Contact—in advance. This procedure provides an opportunity for any employees to be interviewed to be briefed beforehand by Discloser and its counsel so that no unauthorized disclosures of information will be made.

The Discloser and the Recipient may want to implement mechanisms to catalog, control and monitor the delivery of, and access to, Confidential Information and also to coordinate their efforts to some degree.

6. EXCEPTIONS

All of the foregoing obligations and restrictions do not apply to that part of the Confidential Information that Recipient demonstrates (a) was or becomes generally available to the public prior to, and other than as a result of, a disclosure by Recipient or Recipient's Representatives or (b) was available, or becomes available, to Recipient on a nonconfidential basis prior to its disclosure to Recipient by Discloser or a Discloser's Representative, but only if (i) the source of such information is not bound by a confidentiality agreement with Discloser or is not otherwise prohibited from transmitting the information to Recipient or Recipient's Representatives by a contractual, legal, fiduciary or other obligation and (ii) Recipient provides Discloser with written notice of such prior possession either (A) prior to the execution and delivery of this agreement or (B) if Recipient later becomes aware of (through disclosure to Recipient or otherwise through Recipient's work on the Transaction) any aspect of the Confidential Information of which Recipient had prior possession, promptly upon Recipient becoming aware of such aspect.

COMMENT

There is often an exception for materials independently developed by a Recipient, but it is not included in this Confidentiality Agreement because of the potential for disputes over what was "independently developed."

The requirement that the Recipient demonstrate prior possession shifts the burden of proof to the person claiming to be exempt from the obligations of confidentiality.

In certain instances, the Discloser will include a provision prohibiting the Recipient from competing with the Discloser for a specified period of time because of the difficulty the Discloser might otherwise have in proving that the Recipient did, in fact, use the confidential information in its business. Such a noncompetition provision is generally strongly resisted by prospective buyers who are engaged, or have an interest in engaging, in the same business as the Discloser. Moreover, there may be antitrust risks in such a restriction on competition.

7. LEGAL PROCEEDINGS

If Recipient or any of Recipient's Representatives becomes legally compelled (by oral questions, interrogatories, requests for information or documents, subpoena, civil or criminal investigative demand or similar process) to make any disclosure that is prohibited or otherwise constrained by this agreement, Recipient or such Representative, as the case may be, will provide Discloser with prompt notice of such legal proceedings so that it may seek an appropriate protective order or other appropriate relief or waive compliance with the provisions of this agreement. In the absence of a protective order or Recipient's receiving such a waiver from Discloser, Recipient or its Representative is permitted (with Discloser's cooperation but at Recipient's expense) to disclose that portion (and only that portion) of the Confidential Information that Recipient or the Representative is legally compelled to disclose; provided, however, that Recipient and Recipient's Representatives must use reasonable efforts to obtain reliable assurance that confidential treatment will be accorded by any person to whom any Confidential Information is so disclosed.

COMMENT

A Confidentiality Agreement will not protect Discloser against disclosures of information required by legal proceedings. The Discloser, however, wants to be in a position to object to the disclosure of any information or, at a minimum, that it is able to limit or control the scope of any court-ordered disclosure. The Confidentiality Agreement addresses this concern by requiring Recipient and its Representatives to notify Discloser upon their receipt of any such request for information, which enables Discloser to seek a protective order or other relief.

8. CONTACT WITH EMPLOYEES

Without the prior written consent of the Discloser Contact, neither Recipient nor any of Recipient's Representatives will (a) initiate or cause to be initiated (other than through the Discloser Contact) any communication with any employee of Discloser concerning the Confidential Information or the Transaction or (b) for a period of two years after the date of this agreement, solicit or cause to be solicited the employment of any person who is now employed by Discloser.

COMMENT

The Recipient typically wants to interview employees of the Discloser while in the process of evaluating the acquisition. The Discloser, however, may object because (1) it may prematurely communicate to the Discloser's employees the possibility of a sale of the business and (2) it raises the concern that the Recipient may solicit these employees for employment if the acquisition is not consummated.

Thus, the Confidentiality Agreement requires that Recipient not to solicit any employees of Discloser for a period after the date of the Confidentiality Agreement. The Recipient may argue that this provision should be limited to "key" employees, excluding those not encountered in connection with (or more broadly, not involved with) the proposed acquisition. The Recipient may also insist on being permitted to continue ordinary-course-of-business hiring practices, e.g., help-wanted ads in newspapers and trade publications. A possible solution is to list the "protected" employees or define them to include those persons involved in negotiating the acquisition.

9. RETURN OR DESTRUCTION OF CONFIDENTIAL INFORMATION

If Recipient determines that it does not wish to proceed with the Transaction or if Discloser notifies Recipient that it does not wish Recipient to consider the Transaction any further, then (a) Recipient (i) shall promptly deliver to Discloser Contact all documents or other materials disclosed by Discloser or any Discloser's Representative to Recipient or Recipient's Representatives constituting Confidential Information, together with all copies and summaries thereof in the possession or under the control of Recipient or Recipient's Representatives, and (ii) shall destroy materials generated by Recipient or Recipient's Representatives that include or refer to any part of the Confidential Information, without retaining a copy of any such material or (b) alternatively, if the Discloser Contact requests or gives his prior written consent to Recipient's request, Recipient will destroy all documents or other matters constituting Confidential Information in the possession or under the control of Recipient or Recipient's Representatives. Any such destruction pursuant to the foregoing must be certified by an authorized officer of Recipient in writing to Discloser (and such certification shall include a list of the destroyed materials).

COMMENT

The Recipient will often prefer to destroy materials rather than return them. This is particularly the case because the distinction between Confidential Information disclosed by Discloser and Confidential Information generated by Recipient is often hard to apply in practice. The Recipient's Representatives may well have made notes on the documents they received from the Discloser or incorporated the content of those documents into memoranda and analyses, which are not readily redactable. Accordingly, the Recipient may be unwilling to accept a provision that permits the Discloser to withhold consent to the Recipient's blanket destruction as an alternative to return. The Discloser may be willing to permit blanket destruction but only when the documents disclosed by it that are to be destroyed, rather than returned, are listed. The Recipient may find this unduly burdensome. In addition, the Recipient may want to couple the destruction alternative with a right to retain an archival set of all confidential information with its in-house or outside lawyers.

10. NO OBLIGATION TO NEGOTIATE OR ENTER A TRANSACTION

Discloser reserves the right, in its sole discretion, to reject any and all proposals made by Recipient or Recipient's Representatives with regard to a Transaction and to terminate discussions and negotiations with Recipient and Recipient's Representatives at any time. Neither Recipient nor Discloser shall have rights or obligations of any kind whatsoever with respect to the Transaction by virtue of this agreement other than for the matters specifically agreed to herein. Without limiting the preceding sentences, nothing in this agreement requires either Recipient or Discloser to enter into a Transaction or to negotiate such transaction for any specified period of time.

COMMENT

See *Crane Co. v. Coltec Industries, Inc.*, 171 F.3d 733 (2d Cir. 1999), in which two public companies entered into a confidentiality agreement that contained a provision similar to the second sentence of Section 10 above which was applied as part of the justification for holding that the plaintiff had no contractual right that was violated when the other party entered into a merger agreement with another suitor.

The parties may want to consider provisions that the confidentiality obligations terminate upon the completion of the acquisition and add a separate section to the Confidentiality Agreement stating the survival period of the confidentiality obligations if the acquisition closes or fails to close.

11. NO REPRESENTATIONS OR WARRANTIES

Discloser retains the right to determine, in its sole discretion, what information, properties and personnel it wishes to make available to Recipient, and neither Discloser nor its Representatives make any representation or warranty (express or implied) concerning the completeness or accuracy of the Confidential Information, except pursuant to representations and

warranties that may be made in a definitive agreement for the Transaction, if any, between the parties.

COMMENT

Because at the time the parties enter into the Confidentiality Agreement neither the Discloser nor the Recipient knows what information might be of particular interest to the Recipient or whether the discussions will lead to a definitive agreement, the Discloser may seek a disclaimer of any representations or warranties concerning the accuracy or completeness of the Confidential Information. This provision is common.

In *RAA Management, LLC v. Savage Sports Holdings, Inc.*,[1] the Delaware Supreme Court held that non-reliance disclaimer language in a confidentiality agreement was effective to bar fraud claims by a prospective buyer. The prospective buyer had been told by seller during early discussions that seller had no significant unrecorded liabilities, but due diligence showed otherwise. The confidentiality agreement provided that seller made no representations regarding any information provided[2] and that buyer could only rely on express representations in a definitive acquisition agreement, which was never signed. After deciding not to pursue a transaction, the buyer sued seller to recover its due diligence and other deal costs. In affirming the Superior Court's dismissal of the buyer's complaint, the Delaware Supreme Court wrote:

> Before parties execute an agreement of sale or merger, the potential acquirer engages in due diligence and there are usually extensive precontractual negotiations between the parties. The purpose of a confidentiality agreement is to promote and to facilitate such precontractual negotiations. Non-reliance clauses in a confidentiality agreement are intended to limit or eliminate liability for misrepresentations during the due diligence process. The breadth and scope of the non-reliance clauses in a confidentiality agreement are defined by the parties to such preliminary contracts themselves. In this case, RAA and Savage did that, clearly and unambiguously, in the NDA.
>
> * * *
>
> The efficient operation of capital markets is dependent upon the uniform interpretation and application of the same language in contracts or other documents. The non-reliance and waiver clauses in the NDA preclude the fraud claims asserted by RAA against Savage. Under New York and Delaware law, the

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1 45 A3d 107 (Del. 2012).

2 With respect to the effectiveness of non-reliance clauses to eliminate extra contractual liabilities, *see infra* the Comment to Section 13.7.

> reasonable commercial expectations of the parties, as set forth in the non-reliance disclaimer clauses in Paragraph 7 and the waiver provisions in Paragraph 8 of the NDA, must be enforced. Accordingly, the Superior Court properly granted Savage's motion to dismiss RAA's Complaint.

12. REMEDIES

Recipient agrees to indemnify and hold Discloser and its Shareholders[, and Discloser's Representatives,] harmless from any damages, loss, cost or liability (including legal fees and the cost of enforcing this indemnity) arising out of or resulting from any disclosure by Recipient or Recipient's Representatives of the Confidential Information other than as expressly permitted by this agreement. In addition, because an award of money damages (whether pursuant to the foregoing sentence or otherwise) would be inadequate for any breach of this agreement by Recipient or Recipient's Representatives, and any such breach would cause Discloser irreparable harm, Recipient also agrees that, in the event of any breach or threatened breach of this agreement, Discloser will also be entitled, without the requirement of posting a bond or other security, to equitable relief, including injunctive relief and specific performance. Such remedies will not be the exclusive remedies for any breach of this agreement but will be in addition to all other remedies available at law or equity to Discloser.

COMMENT

The Discloser wants the Recipient to acknowledge its right to injunctive relief in order to facilitate the Discloser's obtaining an injunction if it is the Discloser's best remedy. The Recipient may object to the legal fees provision, and perhaps an intermediate position is to provide that the prevailing party receives its legal fees reimbursed. The Discloser may also want to add the bracketed phrase to include its Representatives among the indemnitees if they are at risk for any of the kinds of matters covered by this section.

13. ATTORNEY-CLIENT PRIVILEGE

Discloser is not waiving, and will not be deemed to have waived or diminished, any of its attorney work product protections, attorney client privileges, or similar protections and privileges as a result of disclosing its Confidential Information (including Confidential Information related to pending or threatened litigation) to the Recipient, regardless of whether the Discloser has asserted, or is or may be entitled to assert, such privileges and protections. The parties (a) share a common legal and commercial interest in all of the Discloser's Confidential Information that is subject to such privileges and protections, (b) are or may become joint defendants in Proceedings to which the Discloser's Confidential Information covered by such protections and privileges relates, (c) intend that such privileges and protections remain intact should either party become subject to any actual or threatened Proceeding to which the Discloser's Confidential Information covered by such protections and privileges relates, and (d) intend that after the Closing the Recipient shall have the right to assert such protections and privileges. No Recipient shall admit, claim or contend, in Proceedings involving either party or otherwise, that any Discloser waived any of its attorney work product protections, attorney client privileges, or similar protections and

privileges with respect to any information, documents or other material not disclosed to a Recipient due to the Discloser disclosing its Confidential Information (including Confidential Information related to pending or threatened litigation) to the Recipient.

COMMENT

One of the more troublesome problems related to the disclosure of Confidential Information during the due diligence process is how to disclose certain information to the Recipient to facilitate a meaningful evaluation of litigation related Confidential Information without waiving any work product protections, attorney client privileges, and similar protections and privileges. The language constitutes an attempt to allow the seller to furnish to the buyer Confidential Information without waiving the seller's work product, attorney client privilege and similar protections by demonstrating that the buyer and seller have or should be presumed to have common legal and commercial interests, or are or may become joint defendants in litigation. *See* Section 6 (Privileged Information) of Model Confidentiality Agreement which accompanies the ABA Model Public Company Merger Agreement.

14. MISCELLANEOUS

COMMENT

The following miscellaneous provisions are similar to those under Article 13 of the Model Asset Purchase Agreement and are subject to the comments under that Article for discussion of issues and considerations in using these provisions.

(a) *Modification*. This agreement and the agreements set forth in this agreement may be modified or waived only by a separate writing signed by Discloser and Recipient expressly modifying or waiving this agreement orsuch agreements.

(b) *Waiver*. Neither the failure nor any delay by any party in exercising any right, power or privilege under this agreement will operate as a waiver of such right, power or privilege, and no single or partial exercise of any such right, power or privilege will preclude any other or further exercise of such right, power or privilege or the exercise of any other right, power or privilege.

(c) *Person*. The term **"person"** means any individual, corporation (including any nonprofit corporation), general or limited partnership, limited liability company, joint venture, estate, trust, association, organization, labor union or other entity or governmental body.

(d) *Severability*. The invalidity or unenforceability of any provision of this agreement shall not affect the validity or enforceability of any other provisions of this agreement, which shall remain in full force and effect. If any of the covenants or provisions of this agreement are determined to be unenforceable by reason of its extent, duration, scope or otherwise, then the parties contemplate that the court making such determination shall reduce such extent, duration, scope or other provision and enforce them in their reduced form for all purposes contemplated by this agreement.

(e) *Costs*. Recipient agrees that if it is held by any court of competent jurisdiction to be in violation, breach or nonperformance of any of the terms of this agreement, then it will promptly pay to Discloser all costs of such action or suit, including reasonable attorneys' fees.

(f) *Section Headings, Construction*. The headings of Sections in this agreement are provided for convenience only and will not affect its construction or interpretation. All references to **"Section"** or **"Sections"** refer to the corresponding Section or Sections of this agreement unless otherwise specified. All words used in this agreement will be construed to be of such gender or number as the circumstances require. Unless otherwise expressly provided, the word **"including"** does not limit the preceding words or terms.

(g) *Jurisdiction; Service of Process*. Any action or proceeding seeking to enforce any provision of, or based upon any right arising out of, this agreement may be brought against either of the parties in the courts of the State of ______ County of ______, or, if it has or can acquire jurisdiction, in the United States District Court for the ______, District of ______, and each of the parties consents to the jurisdiction of such courts (and of the appropriate appellate courts) in any such action or proceeding and waives any objection to venue laid therein. Process in any action or proceeding referred to in the preceding sentence may be served on any party anywhere in the world.

(h) *Governing Law*. This agreement will be governed by the laws of the State of ______ without regard to conflicts-of-laws principles.

(i) *Execution of Agreement*. This agreement may be executed in one or more counterparts, each of which will be deemed to be an original copy of this agreement, and all of which, when taken together, shall be deemed to constitute one and the same agreement. The exchange of copies of this agreement and of signature pages by facsimile transmission shall constitute effective execution and delivery of this agreement as to the parties and may be used in lieu of the original agreement for all purposes. Signatures of the parties transmitted by facsimile shall be deemed to be their original signatures for any purpose whatsoever.

[consider adding the following, if appropriate]

(j) *Construction*. The parties have participated jointly in the negotiation and drafting of this agreement. If an ambiguity or question of intent or interpretation arises, this agreement shall be construed as if drafted jointly by the parties and no presumption or burden of proof shall arise favoring or disfavoring any party by virtue of the authorship of any of the provisions of this agreement.

If you are in agreement with the foregoing, please sign and return one copy of this agreement, which thereupon will constitute our agreement with respect to its subject matter.

Very truly yours,

[Discloser's Name]

By:_______________
Name:
Its:

DULY EXECUTED and agreed to on _____ _____, 20_____.

[Recipient's Name]

By:_______________
Name:
Its: