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Court of Chancery Decision Underscores Need to Exclude "Willful Breaches" from the "Effect of Termination" Provision in a Merger Agreement—Yatra v. Ebix

Yatra Online v. Ebix (Aug. 30, 2021) serves as a reminder that, under the "effect of termination" provision in most merger agreements, a party's termination of the agreement extinguishes all liability of both parties for pre-termination breaches of the agreement. Most agreements exclude fraud from the extinguishment of liability, and some (but not all) exclude "willful breaches." In *Ebix*, the effect-of-termination provision did *not* exclude willful breaches from the extinguishment of liability upon termination of the agreement. The target terminated the agreement after the buyer allegedly had a change of heart about the deal, deliberately breached its representations and covenants in an effort to prevent satisfaction of the closing conditions, and showed no intention of ever closing. The court held that the target had no remedy, however, given the extinguishment of the buyer's liability under the effect-of-termination provision.

Key Points

- **The decision serves as a reminder that an "effect of termination" provision may eliminate all liability for pre-termination breaches.** The court explained that, under the provision at issue (as drafted without an exclusion for willful breaches), the target company had the choice *either* (a) to seek damages for the buyer's breaches and/or seek specific performance of the agreement (in both cases, while *not* terminating the agreement), *or* (b) to terminate the merger agreement (in which case neither party would have liability for any pre-termination breaches). Accordingly, before terminating a merger agreement, a party should fully understand the effect the termination would have on its post-termination rights and remedies, particularly with respect to the possibility of an inability to recover damages for the counterparty's pre-termination breaches.

- **A party generally would choose to terminate the merger agreement, rather than seeking damages or specific performance, when:** the party has concerns over its own potential liability (and prefers to terminate the agreement to eliminate that risk); it has decided that it too would prefer not to proceed with the transaction; or it is single-focused on moving on to find an alternative deal or strategy—in each case, notwithstanding having to forego the potential of obtaining damages for the counterparty's breaches.

- **Drafters should carefully consider whether the "effect of termination" provision should exclude *willful* breaches (as well as fraud) from the extinguishment of liability.** In addition, it may be useful to define the concept of "willful breach" in the agreement given the possible ambiguity

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as to whether "willful" suggests an intention to commit the act that was committed or an intention to breach the agreement. Finally, although not an issue in *Ebix*, drafters should be careful to ensure that the effect-of-termination provision is consistent with the merger agreement provisions relating to survival, fraud carveouts, termination fees, and the like.

Background. Ebix, Inc. ("Buyer") and Yatra Online, Inc. ("Target") entered into a merger agreement on July 16, 2019 (the "Merger Agreement") after extensive negotiations. The Merger Agreement provided that Buyer would acquire Target in a reverse triangular merger pursuant to which Target stockholders would receive shares of Buyer convertible preferred stock (the "Preferred Stock"), at a fixed exchange ratio, for each share of Target common stock. In addition, Target stockholders had a right, at their option, in the 25th month after closing, to require Buyer to exchange any then unconverted shares of Preferred Stock for $5.31 per share in cash (the "Put Right") (thus providing the Target shareholders with a floor under which the price for their shares could not fall). After signing, Buyer allegedly had a change of heart about proceeding with the deal when, due to the COVID-19 pandemic, its stock price dropped, ballooning the value of the Put Right compared to Buyer's market capitalization. Allegedly, Buyer then, in an effort to "sabotage" the deal, allegedly breached certain of its representations and warranties and covenants in the Merger Agreement. After Target had (reluctantly) agreed to numerous extensions of the "End Date" in the Merger Agreement, and after the final End Date passed with "no hint" that Buyer intended ever to close, Target sued Buyer for damages and exercised its right to terminate the Merger Agreement. The court, at the pleading stage, dismissed the suit, ruling that the Effect of Termination provision in the Merger Agreement barred post-termination claims for pre-termination contractual breaches. The court also dismissed Target's claims against Buyer for fraud and against Buyer's lenders for tortious interference with the Put Right.

Discussion

Buyer's alleged misconduct included the following:

- Repeatedly delaying the filing of a registration statement with the SEC to register the Preferred Stock—notwithstanding its obligation under the Merger Agreement to file promptly;
- Continually seeking to renegotiate key deal terms post-signing—including elimination of the Put Right even though it was a critical component of the merger consideration;
- After entering into an Extension Agreement with Target to again extend the End Date, failing to take any of the actions specifically agreed to therein—including not providing revised drafts clearly reflecting the proposed modified terms; not responding to Target's requests for basic due diligence information; and continuing to try to renegotiate additional terms; and
- Secretly entering into an amendment to its Credit Agreement (the "Credit Agreement Amendment"), under which any implementation of the Put Right would cause an immediate default under the Credit Agreement—notwithstanding Buyer's representations and covenants in the Merger Agreement that the contemplated transactions would not violate any of its material agreements.

The court wrote that, notwithstanding the alleged misconduct, "[Target] agreed [in the Effect of Termination provision] that termination of the Merger Agreement would terminate liability for breach of that contract," and Target terminated the Merger Agreement. The court "will not redline the parties' bargained-for limitations of liability."

The court rejected Target's alternative interpretation of the "Effect of Termination" provision. The provision read as follows:

> **Section 8.2. Effect of Termination.** In the event of **any termination of this Agreement** as provided in Section 8.1, **the obligations of the parties shall terminate and there shall be no liability on the part of any party with respect thereto**, except for [specified provisions relating to confidentiality, disclaimers, expenses, termination fees and miscellaneous provisions], each of which shall survive the termination of this Agreement and remain in full force and effect; provided, however, that…**nothing contained herein shall relieve any party from liability for damages arising out of any fraud occurring prior to such termination**, in which case the aggrieved party shall be entitled to all rights and remedies available at law or equity.

Buyer argued that Target's decision to terminate the Merger Agreement eliminated any potential liability "with respect to" *its obligations under the Merger Agreement* (*i.e.*, for Buyer's alleged breaches of the Merger Agreement). Target argued that its termination of the Merger Agreement eliminated potential liability "with respect to" *the termination of the Merger Agreement* (*i.e.*, it did not eliminate damages for Buyer's prior breaches of obligations under the Merger Agreement, but eliminated only damages caused by the act of terminating the Merger Agreement). In other words, Target argued that the provision did not extinguish all claims for breach of the Merger Agreement, but, instead, served only to make clear which contractual obligations carried forward after a termination of the Agreement and which did not. Target contended that the provision was "ambiguous," at best, with respect to the effect of termination of the Merger Agreement on a party's post-termination remedies.

Vice Chancellor Slights disagreed and held that all claims for pre-termination breaches of the Merger Agreement were extinguished. The Vice Chancellor observed that secondary sources explain that the consequence of termination of a merger agreement usually is that all of the agreement provisions, with a few specified exceptions, "will terminate and no longer be of any force and effect." He stated that, while under the common law, termination of an agreement results in the agreement becoming void, termination does not, standing alone, result in an elimination of liability for pre-termination breaches; *however*, when parties provide that "there shall be no liability on the part of either party" upon termination, they "alter the common law rule and broadly waive contractual liability and all contractual remedies."

The Vice Chancellor also found that the language and structure of the provision supported an interpretation extinguishing all liability for pre-termination breaches of obligations if the Merger Agreement was terminated. For example, the Vice Chancellor found that Target's position that the provision only extinguished liability arising from a termination of the Agreement was inconsistent with the language immediately following "with respect thereto," which refers to exceptions for certain specified *obligations* under the Merger Agreement from the effects of the contractual limitation of liability. He also found that the Target's contention that a termination leaves claims for pre-termination breaches of contract unaffected was inconsistent with the express carveout of liability for "fraud occurring prior to such termination" (which carveout, in the court's view, implied that liability for all other claims for acts "occurring prior" to termination would not survive post-termination).

The court's other holdings were as follows:

- ***There was no separate remedy available for breach of the Extension Agreement***, as the Extension Agreement was intended to modify the terms of the Merger Agreement and nothing suggested that it was not subject to the Effect of Termination provision in the Merger Agreement.

- ***The implied covenant of good faith was not applicable***, as the best efforts clause in the Merger Agreement left no "gap" for the implied covenant to fill with respect to Buyer's obligations to act to satisfy the closing conditions.

- ***Target did not establish that Buyer's alleged fraud, or the lenders' alleged tortious interference, caused Target's loss.*** Target asserted that Buyer's entering into the Credit Agreement Amendment and making fraudulent extra-contractual promises about proceeding to closing precluded Target from pursuing specific performance; however, the court stated, specific performance was not an option available to Target *in any event* because Buyer could not implement the Put Right without the SEC having declared the registration statement for the Preferred Stock effective, which it had not. Target also asserted that Buyer's lenders tortiously interfered with the Put Right by entering into the Credit Agreement Amendment. The court stated that Target could have sued for specific performance once the registration statement was approved, but Target "elected to terminate the Merger Agreement before that condition to closing occurred"; and, notwithstanding the Credit Agreement Amendment, specific performance of the Put Right would not have been available to Target in any event due to the lack of approval of the registration statement. Therefore, the lenders' actions "did not stand alone as an impediment to [Target]'s ability to pursue specific performance of the Merger Agreement."

Practice Points

- **Merger agreement parties should carefully consider drafting the "effect of termination" provision to carve out willful breaches from the extinguishment of liability, and should consider defining "willful breaches."** In its *Hexion* decision (2008), the Court of Chancery stated that, under the common law, a "knowing and intentional" breach of a merger agreement occurs when a party knowingly (in other words, consciously rather than by accident) takes an action that results in a breach, with no requirement that the breaching party knew or intended that the action would breach the agreement. Since then, many merger agreements have defined the phrase to avoid that interpretation. For example, the merger agreement at issue in the *Cigna-Anthem* litigation (2020), provided as follows: "'Willful breach' means a material breach of this Agreement that is the consequence of an act or omission by a party with the actual knowledge that the taking of such act or failure to take such action would be a material breach of this Agreement."

- **The *timing* of termination of a merger agreement generally would not change the result under a standard "effect of termination" provision.** In *Ebix*, Target argued that the provision's extinguishment of liability was inapplicable because Target had terminated the agreement *after* it filed suit against Buyer. The court found the timing of the termination irrelevant given that the provision stated that liability would be extinguished upon "*any* termination" of the agreement.

- **A party should not terminate a merger agreement without fully understanding the effect of termination on its rights and remedies.** After execution of a merger agreement, legal counsel should consider providing the client with a summary of its obligations, rights, and remedies that apply pre- and post-closing or termination.

- **Any exclusion from the extinguishment of liability under the effect-of-termination provision should be consistent with the parties' intentions and other contractual provisions relating to termination.** For example, if the target has a right to receive a reverse

termination fee upon termination of the agreement by the buyer, it should be made clear whether the fee is the target's sole remedy for termination and whether the target could or could not seek damages for any pre-termination willful breaches by the buyer.

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