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Considerations When Publicly Filing Merger Agreements: the Ninth Circuit Suggests that Shareholders may be Able to Claim Reliance on Representations and Warranties

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The recent Ninth Circuit Court of Appeals decision in *Glazer Capital Management, LP v. Magistri*, 549 F.3d 736 (9th Cir. 2008) suggests that public companies could be subject to securities fraud liability claims from investors based on the statements contained in the representations and warranties section of merger agreements – despite such representations and warranties not being intended as disclosures for securities law purposes. While merger agreements may be required to be disclosed to investors in connection with a company's public filing obligations, conventional practice has been to exclude the disclosure schedules to the merger agreement from the public filing. The disclosure schedules function to outline exceptions to the representation and warranty statements made in a merger agreement, which typically follow standard language.

The combined effect of the *Glazer* decision and an earlier report issued by the Securities and Exchange Commission ("SEC") is that public companies should consider carefully publicly disclosing material exceptions to the representations and warranties contained in publicly-filed merger agreements and consider adding appropriate disclaimers to public filings, including disclaimers as to the purpose of the representations and warranties in the merger agreement and the limits and qualifications to the statements being made.

Background and Analysis of the Court

The *Glazer* case was a class action against InVision Technologies, Inc., alleging public misstatements made by

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InVision in violation of certain securities fraud provisions of the Securities Exchange Act of 1934 ("Exchange Act"). The complaint was based on statements made by InVision in a merger agreement entered into with General Electric. In particular, the representations and warranties section of the merger agreement stated that InVision was in material compliance with all laws, and that, to its knowledge, the company was not in violation of the anti-bribery provisions of the Exchange Act.

On the day the merger was announced, InVision filed its annual report on Form 10-K with the SEC and attached a copy of the merger agreement as an exhibit. The merger agreement stated that the representations and warranties were qualified by a separate non-public disclosure schedule. However, as is customary for public company filings in the context of a merger, the disclosure schedule was never filed with the SEC nor otherwise publicly disclosed.

Months later, InVision issued a press release revealing that potential violations of the Foreign Corrupt Practices Act ("FCPA") by the company had been uncovered as part of an internal investigation. After this press release, InVision's share price fell by more than $6 per share and a class action complaint was ultimately filed against InVision, asserting that the representations in the merger agreement concerning FCPA compliance amounted to false and misleading statements to investors.

In response to the allegations, InVision argued that, because the representations were made directly to a private party in a private agreement, the statements could not support a securities fraud claim by public investors. InVision also asserted that no reasonable investor would have relied on the representations and warranties contained in the merger agreement. To support this, InVision referred to language in the merger agreement that the agreement was not intended to confer any rights or remedies on any person other than the parties to the agreement and that the representations and warranties in the agreement were qualified by information contained in a separate non-public disclosure schedule.

Although the court ultimately dismissed the plaintiffs' claim on other grounds, the court disagreed with InVision's argument that the context in which the statements were made could not support a securities fraud claim. The court stated, " ... the fact that the merger agreement was a private document and

included reference to a non-public disclosure schedule would not, as a matter of law, prevent a reasonable investor from relying on its terms." Accordingly, investors may rely on representations and warranties contained in a merger agreement as statements of fact when the merger agreement is filed with the SEC as an exhibit to a company's public filings and not otherwise adequately qualified in a public filing.

The court's statements in *Glazer* are consistent with an earlier investigation report issued by the SEC in 2005 in connection with the settlement of an SEC enforcement action against the Titan Corporation. In that report, the SEC highlighted that public disclosures regarding material contractual provisions, such as representations and warranties, must not be misleading. The SEC stated that a representation in a disclosure document filed with the SEC, whether by incorporation by reference or other inclusion, constitutes a disclosure to investors, and warned that it will consider enforcement action against companies that fail to adequately qualify such disclosures.

Take-aways from the Glazer Decision

In light of the *Glazer* decision and the SEC's report on Titan, public companies should think carefully about how material agreements in SEC filings should be disclosed. Specifically, public companies should consider including general disclaimers in both merger agreements and in the corresponding public filings made with the SEC concerning (i) the private purpose of the representations and warranties contained in the merger agreement, (ii) the fact that the representations are qualified by a confidential disclosure schedule containing non-public information, and (iii) the persons entitled to enforce the merger agreement. Companies should also review the disclosure schedules and consider the disclosure of any material information that has not otherwise been disclosed.

Until this area of the law is clarified or the *Glazer* decision is overturned, these considerations may result in increased negotiation over representations and warranties in merger agreements with a view to the public filing of the document, and also may result in increased attention paid to the public disclosure of merger agreements and the information contained in disclosure schedules.

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