December 12, 2017

Delaware Court of Chancery Specifically Enforces Oral Settlement Agreement with Activist Investor

Recently in *Sarissa Capital Domestic Fund LP* v. *Innoviva, Inc.*, the Delaware Court of Chancery specifically enforced a disputed oral settlement agreement in a proxy contest between Innoviva, Inc. and Sarissa Capital Management resulting in two dissident directors being seated on the Innoviva board. The court held that the principals of Innoviva and Sarissa had entered into a valid, binding (albeit oral) agreement that required, among other things, Sarissa to cease its proxy solicitation in exchange for two seats on the Innoviva board. Due in part to what the court referred to as Innoviva's "opportunistic maneuvers" of reneging on the agreement only after it became clear that it would win the proxy contest despite early predictions of a loss, the court used its equitable powers to award Sarissa specific performance of the settlement agreement.

Background

In February 2017, Sarissa launched a proxy contest to replace three of Innoviva's seven directors at the company's April 2017 annual meeting. After the leading U.S. proxy advisory firms all recommended that stockholders vote for the Sarissa nominees, Innoviva sought a potential settlement of the proxy contest. The Innoviva board appointed James Tyree, the vice chairman, as its "point person" in settlement discussions with Sarissa, which were being led on Sarissa's side by its founder and chief investment officer, Alexander Denner.

The parties reached an oral agreement that in exchange for Sarissa ending its proxy campaign and related litigation, Innoviva would expand its board from seven to nine members and appoint two Sarissa nominees to the board. The parties also agreed that they would issue a conciliatory press release announcing the settlement. The main point of contention between the parties was over Innoviva's demand that Sarissa enter into a standstill agreement for a period of time, which both parties labeled a "deal breaker."

Less than 24 hours before the annual meeting, the outcome of the board election remained in doubt because two large index fund stockholders had not indicated how they would vote. When one of these index fund stockholders eventually indicated that it would vote in favor of Sarissa's nominees, the board, reasoning that it was also likely to lose the vote of the other large index fund stockholder, abandoned its demand that Innoviva enter into a standstill. Tyree (again as authorized by the board and Innoviva) communicated this by telephone to Denner, who accepted, with the parties orally confirming that they "had a deal" and that it would be left to other team members to "prepare the 'paperwork . . . to get it done.'" Neither party indicated that the deal was contingent on execution of the paperwork, nor that it was subject to further board approval.

Before the definitive agreement was executed, however, Innoviva learned that the other large index fund stockholder had in fact voted for the board's slate of directors, ensuring a win for the board nominees. At the direction of the board, Tyree then contacted Denner to inform him that the board determined not to proceed with the settlement, but instead to proceed with the stockholder vote the following day. Tyree disagreed with the board's decision to abandon the settlement, and this disagreement was a factor in his decision to later resign from the board.

On the day of the annual meeting, Sarissa filed an action under Section 225 of the Delaware General Corporation Law, seeking a declaration that the parties entered into a binding settlement agreement and seeking specific performance of that agreement.

Analysis

In a post-trial opinion by Vice Chancellor Slights, the court held as follows:

- *Tyree had authority to enter into an oral settlement agreement with Sarissa on behalf of Innoviva.* The court found that Tyree had both actual and apparent authority to bind Innoviva to an oral settlement agreement with Sarissa within certain parameters.
  - Moreover, the court held that there was a proper delegation of the board's duty to fill board vacancies. Innoviva had argued that the board's delegation of authority to Tyree was invalid because its bylaws stated that "decisions regarding who should fill Board vacancies cannot be delegated to an individual director or a third person, but must be decided by the entire Board acting by majority vote." The court noted, however, that an alternative section of Innoviva's bylaws provides that newly created directorships may only be filled by a "majority vote of directors then in office." Under this latter provision, the board was permitted to decide (without a formal vote) who should fill any to-be-created directorships and to authorize Tyree to bind the board to that decision by contract.
- *The parties formed a valid, binding oral contract.* Relying on prior decisions, the court noted that a contract exists when (i) the parties have made a bargain with "sufficiently definite" terms and (ii) the parties have manifested mutual asset to be bound by that bargain. Based on the record here, the court noted that "the objective, contemporaneous evidence" reflects that Denner and Tyree reached agreement on the essential terms when Tyree communicated to Denner, and Denner accepted, the board's offer to settle without the standstill. According to the court, a "reasonable negotiator" would have concluded that there was agreement on the essential terms, and therefore, negotiations concluded. Neither party indicated that the settlement was contingent on the execution of a written

agreement, finalization of the joint press release or approval by the board. The court, therefore, held that a valid, binding agreement existed upon Denner's acceptance.

- *Specific enforcement of the settlement agreement was warranted.* Sarissa was able to demonstrate each element of an award of specific performance with clear and convincing evidence, including: (i) the existence of a valid, enforceable settlement agreement; (ii) the "essential elements" of that agreement; and (iii) the absence of an adequate legal remedy because money damages would not adequately compensate it for its loss of opportunity to secure representation on the Innoviva board. In addition, Sarissa established that it was, and continued to be, "ready, willing and able to perform" its contractual obligations, as it stopped soliciting proxies when it believed an agreement was reached, and instructed its counsel to finalize the relevant documents. Finally, the court concluded that "the 'balance of the equities' . . . favor[ed] granting specific performance" because "Innoviva's opportunistic maneuvers to escape its contractual obligations offend[ed] basic notions of equity." Indeed, the court noted that Tyree was the only person acting with "good conscience" within Innoviva as it relates to Sarissa, and he was so offended by the board's conduct that he resigned as vice chairman.

Takeaway

The court's decision in *Sarissa* demonstrates the importance of counseling clients to expressly provide that oral business deals are contingent upon the parties agreeing on definitive language in a written agreement, particularly under circumstances in which the counterparty is likely to take important irreversible actions in reliance on the oral business agreement.

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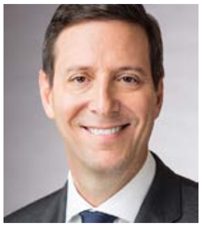

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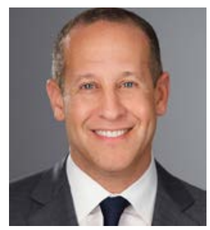

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