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Chancery Court Considers Whether Either Party to Failed Multibillion Dollar Merger Was Entitled to Payment of a Fixed Termination Fee

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Based on literal reading of merger agreement, Vice Chancellor denies termination fee to one merger partner but holds open possibility that the other was entitled to reimbursement fee, pending factual determinations

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INTRODUCTION

The Williams Companies, Inc. ("*Williams*") and Energy Transfer L.P. ("*ETE*") are "significant players in the energy pipeline business" (quoting *Williams II* below). On September 28, 2015, Williams and ETE agreed to a complicated "multi-billion-dollar merger" (quoting *Williams II* below) structured to provide "tax free" (quoting *Williams I* below) treatment for ETE *via* a merger agreement ("*Merger Agreement*"). Shortly thereafter, the transaction "foundered on the shoal of a declining energy market," making the transaction "far less attractive to ETE," who "sought a way out" (quoting *Williams III* below). Fortunately for ETE, the market decline also made it impossible for ETE's tax counsel to issue an opinion confirming the "tax-free" status of the transaction for ETE ("*Tax Opinion*") (quoting *Williams III* below). And because receipt of the Tax Opinion was a condition to ETE's obligation to consummate the transaction ("*Tax Condition*"), ETE refused to close. Then, the day following passage of the Merger Agreement's June 28, 2016, outside date for completing the transaction ("*Outside Date*"), ETE sent Williams a notice purporting to terminate the Merger Agreement ("*Termination Notice*").

In response, Williams sought specific performance of the transaction from the Delaware Court of Chancery ("*Chancery Court*"). On June 24, 2016, Vice Chancellor Sam Glasscock III refused to grant Williams' requested relief. *Williams Cos., Inc. v. Energy Transfer Equity, L.P.*, No. 12168-VCG, No. 12337-VCG, 2016 WL 3576682 (Del. Ch. June 24, 2016), *aff'd*, 159 A.3d 264 (Del. 2017) ("*Williams I*"). In so ruling, the Vice Chancellor found that ETE's tax counsel acted "independently and in good faith" in declining to issue the opinion (quoting 159 A.3d 264). For a discussion of *Williams I*, see Robert S. Reder & Nicole A. Dressler, *Delaware Court Refuses to Enjoin Buyer From Terminating Merger Agreement Due to Failure of Closing Condition*, 71 VAND. L. REV. EN BANC 49 (2018).

Ultimately, "[t]he failure of the merger was bruising to both sides," who "sought to dress their wounds with the balm of contractual damages" through litigation in Chancery Court (quoting *Williams III* below). Each party claimed the other breached the Merger Agreement in a variety of ways and sought unspecified damages. In addition, each sought payment from the other of a fixed fee payable upon termination of the Merger Agreement under specified circumstances. In separate decisions issued some thirty months apart, Vice Chancellor Glasscock considered whether ETE or Williams was entitled to the requested fee. In *Williams Cos., Inc. v. Energy Transfer Equity, L.P.*, No. 12168-VCG, No. 12337-VCG, 2017 WL 5953513 (Del. Ch. Dec. 1, 2017) ("*Williams*

II"), the Vice Chancellor ruled that Williams was not required, under the literal terms of the Merger Agreement, to pay ETE a $1.48 billion termination fee ("*Termination Fee*"). Then, in *Williams Cos., Inc. v. Energy Transfer LP*, No. 12168-VCG, No. 12337-VCG, 2020 WL 3581095 (Del. Ch. July 2, 2020) ("*Williams III*"), the Vice Chancellor denied ETE's motion for summary judgment seeking to dismiss Williams' contention that it was entitled to a $410 million reimbursement fee ("*Reimbursement Fee*"). The Vice Chancellor's analyses of the relevant provisions of the Merger Agreement should be of interest to any legal practitioner who advises clients in the M&A setting.

I. FACTUAL BACKGROUND

A. Key Merger Agreement Provisions

1. Termination Fee

Section 5.06(d)(iii) of the Merger Agreement required Williams to pay the Termination Fee if ETE terminated the Merger Agreement due to a withdrawal by the Williams board of directors ("*Williams Board*") of its initial recommendation ("*Williams Board Recommendation*") to Williams stockholders to vote in favor of the transaction ("*Williams Board Recommendation Withdrawal*"). To support its claim to the Termination Fee, ETE argued that even though the Williams Board "did not formally" make a Williams Board Recommendation Withdrawal, the Williams Board "informally decided (in light of ETE's perceived disinclination to merge) that it was more lucrative to Williams to pursue negotiation of a walk-away payment from ETE than to consummate the Merger" (quoting *Williams II* here and below in the next three subsections unless otherwise noted).

In effect, ETE argued that the Williams Board engaged in "a *de facto* 'withdrawal' " of the Williams Board Recommendation by allowing Williams to (i) "issue[ ] press releases that signaled Williams' pessimism about the Merger to the market," (ii) sue ETE's Chief Executive Officer in an effort "to damage investor confidence in [him]," (iii) "use[ ] the media to portray ETE in a negative light," and (iv) issue proxy materials "that undermined the financial projections used to initially recommend the Merger to Williams' stockholders." ETE contended that it was entitled to the Termination Fee because it delivered the Termination Notice in the wake of these events.

Williams disputed this claim, countering that (1) ETE terminated the Merger Agreement after its counsel declined to issue the Tax Opinion, and (2) not only did the Williams Board not formally issue a Williams Board Recommendation Withdrawal but, to the contrary, (i) Williams asked the Chancery Court to "specifically enforce" the Merger Agreement, (ii) the Williams Board affirmed its recommendation of the transaction "several times during the pendency of the Merger," and (iii) the "overwhelming majority of Williams' stock was voted in favor of the Merger." In short, Williams argued that "it would be passing strange for two parties to a merger agreement to structure the agreement so that a party which desired to exit the agreement could do so, over the other party's objections, and at the same time receive the windfall of a substantial termination fee."

2. Reimbursement Fee

ETE conditioned its willingness to sign the Merger Agreement on Williams exiting a "roll-up transaction" to which it was committed (quoting *Williams III*). Because this exit required Williams to pay a $410 million termination fee to the counterparty, the Merger Agreement provided that if either party terminated the Merger Agreement under specified circumstances, ETE would pay Williams the Reimbursement Fee. Specifically, Section 5.06(f) of the Merger Agreement provided that either party was entitled to terminate if (among other reasons) the transaction was not completed by the Outside Date, and if, at the time of any such termination, certain conditions to closing were not satisfied ("*Specified Conditions*"), ETE was required to pay the Reimbursement Fee to Williams. The parties did not dispute that ETE delivered the Termination Notice after the Outside Date. However, ETE claimed it was not required to pay the Reimbursement Fee because it terminated the Merger Agreement due to the failure of the Tax Condition, which was not one of the Specified Conditions.

II. THE VICE CHANCELLOR'S ANALYSIS

A. Williams Not Required To Pay Termination Fee

In asserting its entitlement to the Termination Fee, and to refute Williams' charge that it was seeking a "windfall," ETE argued that Delaware, as "a contractarian state," allows parties to retain "the benefits of their bargains, good, bad, and indifferent."

Rather than dispute this argument, Vice Chancellor Glasscock declared that the Merger Agreement, "as written, [was] fatal to ETE's contention here." Rejecting ETE's theory of "*de facto* withdrawal," the Vice Chancellor relied on the fact that "[t]here are no allegations . . . that the [Williams Board], or any subcommittee thereof, ever formally modified (or expressed the intent to so modify) the Recommendation." Therefore, the conditions necessary to trigger payment of the Termination Fee were not present.

For the Vice Chancellor, ETE's actual complaint focussed on the Williams Board's "strategy under which [Williams] took a number of actions which ETE deems inimical to consummation of the merger." While "those efforts may be contractually meaningful in terms of the 'best efforts' requirement that the Merge Agreement imposed on Williams" to consummate the transaction, Section 5.06(d)(iii) of the Merger Agreement "was careful to cabin ETE's entitlement to the Termination Fee to those situations in which [Williams] Board (or subcommittee) action modified (or proposed to modify) the required [Williams] Board Recommendation." In essence, while a court might someday determine that Williams' strategy supported ETE's breach of contract claim, based on the plain language of the Merger Agreement, ETE was not entitled to payment of the narrowly constructed Termination Fee.

B. ETE's Obligation To Pay the Reimbursement Fee

The question of Williams' entitlement to the Reimbursement Fee was not as straightforward. In fact, due to remaining questions of fact that could not be resolved on summary judgment, Vice Chancellor Glasscock did not issue a definitive ruling regarding payment of the Reimbursement Fee. On the other hand, based on his reading of the Merger Agreement, the Vice Chancellor was "able to address and clarify the contractual obligations of the parties" relating to the Reimbursement Agreement (quoting *Williams III* here and below in this subsection unless otherwise noted).

First, ETE argued that because it terminated the Merger Agreement due to non-satisfaction of the Tax Condition, rather than one of the Specified Conditions, ETE was not required to pay the Reimbursement Fee. In other words, in ETE's view, Section 5.06(f) required that non-satisfaction of one of the Specified Conditions be the reason for termination of the Merger Agreement. Vice Chancellor Glasscock found "no causal language" in "the plain text" of Section 5.06(f) requiring that "termination must result from the unsatisfied condition." To the contrary, the fact that ETE terminated the Merger

Agreement due to non-satisfaction of the Tax Condition was not a bar to payment of the Reimbursement Fee if any of the Specified Conditions were then unsatisfied.

Second, ETE made what the Vice Chancellor called the "oxymoronic" argument that, at the point the Tax Opinion became unavailable and ETE was no longer required to close, "ETE's conditional obligations to perform *any further task or requirement* related to the conclusion of the Merger" were "extinguished." This argument, according to the Vice Chancellor, ignored the Merger Agreement's "survival clause," which provided that the Reimbursement Fee provision (among others) survived termination of the Merger Agreement. To rule otherwise would render the benefits of the Reimbursement Fee "illusory," a bridge too far for the Vice Chancellor.

Third, ETE claimed that Williams, by "ma[king] itself available to consummate the Merger," despite non-satisfaction of various closing conditions, "conceded that any possible breach ETE may have committed was not material." As a result, ETE posited that Williams effectively waived all the Specified Conditions and, "as a matter of law," was not entitled to the Reimbursement Fee. Once again, Vice Chancellor Glasscock rejected ETE's approach. While "[c]ontinuing performance waives the argument that the waiving party's performance obligation was discharged, . . . the non-breaching party's continued performance does not admit or concede or conclusively establish that a breach was immaterial." Accordingly, the question of non-satisfaction of any of the Specified Conditions was "really a factual one" not determinable on a motion for summary judgment.

CONCLUSION

As a pro-contractarian state, Delaware permits, and indeed encourages, contracting parties to allocate risks as they see fit. However, as *Williams I* and *Williams II* demonstrate, once those risks have been clearly allocated, they will be strictly construed, and the parties will be bound to their negotiated agreement. According to Vice Chancellor Glasscock, "Delaware courts 'will not rewrite the contract to appease a party who later wishes to rewrite a contract he now believes to have been a bad deal. Parties have a right to enter into good and bad contracts; the law enforces both' " (quoting *Williams III*).

In *Williams I* and *Williams II*, ETE and Williams sought some recompense for the demise of their failed multibillion dollar transaction, each claiming entitlement to a fixed fee negotiated in the Merger

Agreement. For its part, "ETE, having successfully resisted Williams' attempt to force consummation of the merger," placed itself "in the unlikely position of arguing that it [wa]s also entitled to" the Termination Fee (quoting *Williams II*). Based on his reading of the Merger Agreement, the Vice Chancellor rejected ETE's theory that the Williams Board engaged in a *de facto* withdrawal of its recommendation to stockholders. Because, among other factors, the Merger Agreement required a formal withdrawal, ETE was not entitled to the Termination Fee.

While the Vice Chancellor could not, in light of unresolved factual issues, definitively rule on Williams' entitlement to the Reimbursement Fee, he did reject several theories offered by ETE in opposition to payment of the fee. In short, ETE failed to establish that recovery of the Reimbursement Fee was barred as a matter of law. Therefore, Williams' entitlement to the Reimbursement Fee depended on resolution of the remaining factual issues concerning whether the Specified Conditions were satisfied when the Merger Agreement was terminated.