
Shedding Light on the Elusive and Mysterious “Material Adverse Effect” Clause

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INTRODUCTION

In “sign then close” contracts governing mergers and acquisitions, buyers routinely demand the inclusion of a “Material Adverse Effect” (“MAE”) or “Material Adverse Change” (“MAC”) clause that permits them to avoid closing the transaction in the event a MAE occurs. In other circumstances, contracting parties include a MAE clause, sometimes in the form of a representation and warranty or covenant, allowing for indemnification or recovery of damages. Although MAE clauses are clearly commonplace in mergers and acquisitions contracts,¹ the extent to which these provisions actually permit buyers to avert closings is less clear. A lack of clarity tends to cause confusion and frustration, particularly on the part of sellers confronted with buyers invoking MAE clauses. Sellers frequently choose to renegotiate the purchase price downward due to uncertainty about their prospects in litigation or because a closing delay would seriously impact the business.² On the other side of the equation, buyers also struggle to understand when their invocation of a MAE clause to avoid a closing would be deemed justified by a court.³ This article seeks to educate parties negotiating MAE clauses or engaged in disputes over the applicability of a MAE clause under New York law. In particular, this article examines how courts interpret and apply MAE clauses, and provides some practical tips for drafters.⁴

Although New York law is the focus of this article, Delaware courts have provided the most detailed and comprehensive analyses of MAE clauses. Indeed, a decision out of the Delaware Chancery Court (*In re IBP, Inc. Shareholders Litigation*, 789 A2d 14 (Del Ch 2001)) actually serves as the primary authority on New York law on this topic. Therefore, any analysis of New York law should begin with a review of Delaware MAE cases.

DELAWARE CASE LAW (SELLER FRIENDLY)

Delaware case law is generally considered as the most authoritative and comprehensive in the area of MAE clauses. The language of a typical MAE clause is extremely broad on its face, and might cause a reader to expect that it is extraordinarily buyer friendly. In practice, however, Delaware courts have made clear that even broadly-drafted MAE clauses are difficult for buyers to rely on. The weight of the precedent described in this section illustrates that a buyer seeking to rely on such a clause to terminate a transaction bears a heavy burden of proof. As shown below, courts typically require the buyer to prove—often with expert testimony and detailed financial evidence—that the event in question was unforeseeable at the time the buyer executed the contract, and that the event will significantly impact the earnings of the target in the long-term.

In *In re IBP, Inc. Shareholders Litigation*, 789 A2d 14 (Del Ch 2001), the Delaware Chancery Court performed in-depth analysis of, and applied, New York law concerning a MAE clause. There, IBP and Tyson Foods had entered into a merger agreement containing a seemingly buyer-friendly clause permitting Tyson to terminate the transaction before closing in the event of a MAE. The parties defined "MAE" in a circular fashion, which is not uncommon, to include "any event, occurrence or development of a state of circumstances or facts which has had or reasonably could be expected to have a Material Adverse Effect . . . on the condition (financial or otherwise), business, assets, liabilities or results of operations of [IBP] and [its] Subsidiaries taken as a whole" (*id.* at 65). Tyson terminated the transaction on the eve of closing because of an alleged sharp drop in IBP's financial performance in the last quarter of 2000 and first quarter of 2001, combined with the discovery of accounting impropriety at one of IBP's subsidiaries. The Delaware Chancery Court disagreed that these circumstances constituted a MAE, holding that:

"Practical reasons lead me to conclude that a New York court would incline toward the view that a buyer ought to have to make a strong showing to invoke a Material Adverse Effect exception to its obligation to close. Merger contracts are heavily negotiated and cover a large number of specific risks explicitly. As a result, even where a Material Adverse Effect condition is as broadly written as the one in the Merger Agreement, that provision is best read as a backstop protecting the acquiror from the occurrence of *unknown events that substantially threaten the overall earnings potential of the target in a durationally-significant manner*. A short-term hiccup in earnings should not suffice; rather the Material Adverse Effect should be material when viewed from the longer-term perspective of a reasonable acquirer" (*id.* at 68 [emphasis added]).

After analyzing all of the facts and circumstances in great detail, the court concluded that Tyson had not met its burden to prove by convincing expert evidence that the long-term earnings of the business would decline materially compared with its historical performance.

Delaware courts have consistently held buyers to a high threshold of proof in other cases as well, repeatedly citing *In re IBP* as setting forth the applicable standard.⁵ To date, Delaware courts have found that a MAE occurred, justifying termination of a contract, in only one instance, and that situation was extreme.⁶ In *Cooper Tire & Rubber Co. v Apollo*

(*Mauritius Holdings Pvt. Ltd.*, No. 8980-VCG, 2014 WL 5654305 (Del Ch Oct. 31, 2014), the Delaware Chancery Court determined that a MAE had occurred, justifying termination of the contract before closing, where a labor union and joint venture partner of the seller physically took over the seller's tire manufacturing facility in China, stopped all tire production, and physically barred the seller's access to the facility and its financial records, which in turn prevented the seller from satisfying closing conditions.

A case currently pending in Delaware may result in significant case law development on MAE clauses: *Alere Inc. v. Abbott Laboratories Inc.*, Case Nos. 12691, 12872, & 12963 (Del. Ch.). There, the seller Alere sued to force a \$5.8 billion merger to close. The buyer Abbott Laboratories, in turn, invoked the MAE clause, arguing that the following events qualified as a MAE: a FCPA probe into Alere by the United States Department of Justice, Alere's delay in filing its annual report with the SEC, a market recall of one of Alere's products, the expulsion of an Alere subsidiary from the federal Medicare program, and a significant drop in Alere stock prices. The case is still in the discovery phases, but warrants future consideration, given that the facts alleged by Abbott seem potentially extreme enough to qualify as a MAE, even under a broad definition of the term, and even in the Delaware courts.

NEW YORK CASE LAW (ALSO MOSTLY SELLER FRIENDLY)

As the *IBP* court noted in 2001, and which remains true today, New York authority on the quantum of evidence needed to invoke MAE clauses is sparse, and the authority that exists is not particularly informative. What is apparent from federal district court cases out of New York is that the question of whether a MAE has taken place usually presents a factual inquiry, thus preventing summary judgment, and expert testimony and detailed financial information is virtually always necessary.⁷ Additionally, the buyer's knowledge and the foreseeability of an event are critical to determining whether the event in question amounted to a MAE.⁸ In other words, if a buyer had knowledge prior to the execution of the purchase contract of a risk that a particular event or set of circumstances might occur, such awareness severely undermines the buyer's contention that the occurrence of that event or set of circumstances amounted to a MAE, justifying termination of the contract.

It appears that only one New York state court has analyzed the applicability of a MAE termination provision in a merger or acquisition contract under New York law,⁹ and its decision is consistent with the *IBP* and Delaware cases in recognizing the heavy burden placed on a buyer seeking to escape a transaction. In *Bear Stearns Companies, Inc. v. Jardine Strategic Holdings Limited*, No. 31731/87, 26513/87, 1988 NY Misc LEXIS 892 (Sup. Ct. New York County June 17, 1988), *aff'd* 143 AD2d 1073 (1st Dept 1988), Bear Stearns and Jardine had entered into a contract providing that Jardine would make a tender offer for 20% of Bear Stearns' outstanding stock at a set price. The agreement permitted Jardine to terminate the offer prior to the actual tender if:

"any change shall have occurred or been threatened, other than as contemplated in the Transaction Agreement in the business, properties, assets, liabilities, condition (financial or otherwise), operations or results of operations of the Company or any of its subsidiaries taken as a

whole, or the Purchaser shall have become aware after [execution of the agreement], of any fact with respect to the Company that, in the reasonable judgment of the Purchaser has material adverse significance with respect to the value of the Shares to the Purchaser" (*id.* at *4).

After execution of the contract, but before the tender offer was made, the stock market crashed, causing the net profits of Bear Stearns to drop by 99.2%, compared to the same financial quarter a year earlier, and the quarterly performance was "97.8% lower than the next wors[t] quarter in Bear Stearns' public history"—causing a "precipitous drop in the price of Bear Stearns' stocks." Jardine terminated the transaction pursuant to the MAC clause, arguing that "a One Hundred Million dollar loss in the two days following the 'crash' and Bear Stearns' unprecedented net comparable losses for the quarter ending October 30, 1987, were sufficient to establish a 'material adverse change' in Bear Stearns' 'results' of operations." Bear Stearns then sued Jardine for breach of contract, seeking damages based on Jardine's termination of the transaction. The Appellate Division, First Department refused to grant Jardine's motion to dismiss, and likewise refused to grant summary judgment to Jardine. The court noted that a one-quarter downturn cannot prove that a MAC occurred, particularly because Jardine knew it was acquiring an interest in a volatile, risky business subject to fluctuating market conditions outside of its control. The court commented that "one can fairly assume that Jardine was fully apprised of the risks inherent in the business in which it sought to make a substantial investment."

Federal district courts in New York have decided cases involving MAE clauses, but the results are somewhat mixed. Some decisions are aligned with the *Bear Stearns* analysis and Delaware precedent.¹⁰ At least two cases decided by federal district courts in New York, however, seem at odds with the other cases cited above. Both were issued by the Southern District of New York, and notably, both involved MAE clauses contained in warranties or covenants, rather than in termination provisions of the contract.

In *Am. Transtech Inc. v U.S. Trust Corp.*, 933 F Supp 1193 (SDNY 1996), the court concluded that the seller had breached a warranty that it was not aware of any litigation (pending or threatened) that would constitute a MAE because it disclosed a pending proceeding on a disclosure schedule, stating the risk was \$76,000, when in actuality the risk was \$188,053. In the second case, *Coastal Power Intern., Ltd. v Transcontinental Capital Corp.*, 10 F Supp 2d 345 (SDNY 1998), the district court held that the seller had breached its covenant to take steps to prevent a MAE from occurring by failing to maintain insurance coverage for its floating power plant, which ultimately resulted in \$2 million in costs borne by the buyer after it purchased the power plant for \$70 million. The precedential value of these decisions is uncertain given that they contain little to no analysis of the MAE clause itself and of the materiality of the event to the parties' transaction. The absence of a discussion of any case law interpreting MAE clauses is unfortunate because the balance of the two decisions (addressing other arguments and claims) is heavy with comprehensive analyses. It is therefore unclear the extent to which the court and parties in those cases actually analyzed the materiality of the event claimed to amount to a MAE. Perhaps more importantly, however, each of these cases involved a buyer *that had already closed the transaction*, and that was suing the seller for *damages* based upon an alleged breach of a warranty or covenant. It may very well be that the court was more

willing to find that a MAE occurred for purposes of a buyer's claim for damages than it would have been had the buyer been asserting its right to terminate the agreement before closing.

The remaining cases in New York where courts have determined that the facts and evidence supported the finding of a MAE involve sets of facts that, in many cases, would not be difficult for a seller to distinguish (similar to the *Cooper Tire* decision out of Delaware). For example, in *Pan Am Corp. v Delta Air Lines, Inc.*, 175 BR 438 (SDNY 1994), a buyer's termination of a contract on the basis of a MAE was upheld where the seller, Pan Am, while in bankruptcy, suffered such a "rapid deterioration" of revenue and flight bookings and an increase in expenses that, all of the witnesses agreed, it could not meet its bankruptcy business plan and would not be able to repay loans intended to fund the proposed transaction and held by the prospective buyer. In another case, *LaSalle Bank Nat'l Ass'n v Citicorp. Real Estate, Inc.*, No. 01 Civ. 4389(AGS), 2002 WL 181703 (SDNY Feb. 5, 2002), a federal district court found that a complaint adequately stated a claim (seeking repurchase of a loan based upon the occurrence of a MAE) where the buyer pled that the seller had failed to disclose facts showing that the borrower would likely default, and that those facts ultimately contributed to the borrower's default. The court recognized, however, that discovery might show otherwise.

POTENTIAL DIFFERENCES IN INTERPRETATION OF MAE CLAUSES BASED ON LOCATION IN THE AGREEMENT (*i.e.*, TERMINATION CLAUSE VERSUS WARRANTY OR COVENANT)

The location of a MAE clause in a contract could be significant, and drafters should consider which placement best serves the client's interests. Most of the reported cases, including many of the examples above, involve MAE clauses appearing in a termination provision of a merger or acquisition contract—*i.e.*, the buyer may terminate the deal if a MAE occurs. In other cases, however, a MAE clause may appear in the form of a warranty that continues through closing or re-warranted through a "Bring Down Certificate" to the closing itself (*e.g.*, the seller warrants that no MAE has occurred), and/or in the form of a covenant (*e.g.*, the seller covenants that it will not permit a MAE to occur before closing, or that it will inform the buyer of a MAE).¹¹ The buyer's remedy for breach of a warranty or covenant is often post-closing indemnification rather than rescission. Although case law has yet to directly address the intersection of MAE case law and New York law governing breach of warranty claims, drafters and litigators alike should know that aspects of New York law governing enforcement of claims for breach of warranty might prove useful to a buyer.

For example, New York expressly rejects "reliance" on a warranty as an element in breach of warranty claims. Even if a buyer knew of facts showing that a warranty was false at the time of contract execution, as long as those facts did not originate from the seller (*e.g.*, during due diligence or on disclosure schedules), the buyer may still prevail on its claim for breach of warranty.¹² Therefore, the requirement that buyers seeking to invoke a MAE termination provision must prove that the event in question was unforeseeable at the time it executed the contract may not be as strictly required for a buyer seeking to prove the occurrence of a MAE for purposes of a breach of warranty claim. A court

might, for example, ease the burden of proof in breach of warranty situations by requiring the buyer to prove that the event in question was unforeseeable based solely upon the information and documents disclosed by the seller during due diligence. The presence of sandbagging or anti-sandbagging clauses in the contract might also affect a court's interpretation of a MAE clause contained within a representation and warranty.

On the other hand, sellers agreeing to inclusion of a MAE warranty provision in addition to a MAE termination provision could build in protections by negotiating a limitation on the buyer's remedy for breach of the MAE warranty. For example, the indemnification provision of the contract might limit the remedies of a buyer for breach of the MAE warranty to situations where the buyer had no knowledge (whether from the seller or other sources) of the MAE prior to closing. If the buyer had knowledge of the MAE from any source, the buyer's sole remedy would be to terminate the contract before closing.

SELLER'S PROBLEM OF REMEDIES

A seller suing for breach of contract, based upon a buyer's wrongful invocation of a MAE clause to terminate a deal before closing, faces a problem of remedies. A seller with a remedy for specific performance is the best situated, whereas a seller left with a claim for damages or indemnification could find itself in a precarious position. Under New York law, the measure of damages in this situation is the difference between the purchase price and the value of the target on the date of the buyer's breach.¹³ Accordingly, to prevail on its breach claim for damages, the seller must prove that: (a) the value of the target decreased between execution of the contract and the buyer's termination of the contract, but (b) that the decline in value is not the result of a MAE. Depending upon the facts, this could be a difficult argument to make.

PRACTICAL TIP FOR RESEARCHING "MATERIAL ADVERSE EFFECT" CASE LAW

For litigators researching this issue, it is important to note that the term "material adverse effect" appears in some other lines of cases that are irrelevant or distinguishable from those involving MAE clauses in mergers and acquisitions contracts. For instance, the meaning of "material adverse effect" in securities fraud cases involving allegations that a misrepresentation materially impacted stock prices is irrelevant in the context of a MAE clause used in a contract governing a commercial merger or acquisition.¹⁴ Courts have also distinguished MAE clauses in a merger or acquisition context from MAE clauses in the insurance context; New York case law imposes a lighter burden upon an insurer to prove that a fact undisclosed by the insured amounted to a MAE, thereby justifying rescission of coverage, because New York protects the interests of insurers in receiving complete and accurate information before issuing a policy.¹⁵ The same term (with different accompanying meanings) is also frequently used in employment discrimination cases under Title VII (material adverse effect on employment), in SEQRA cases (material adverse effect on the environment), and in cases where an attorney wishes to withdraw as counsel (material adverse effect on the client). So beware when conducting research to avoid spinning your wheels in these distinguishable buckets of case law.

TAKE-AWAYS

As a survey of the case law reveals, the typical MAE termination clause, which on its face appears to heavily favor buyers, is actually more favorable to sellers. A buyer seeking to terminate a contract based upon an alleged MAE bears the heavy burden of proving that the risk was not foreseeable at the time the buyer executed the contract, and that the event in question will significantly impact earnings of the target in the long term. But whether an event amounts to a MAE is an inherently factual question, which in and of itself gives some leverage to buyers seeking to negotiate a reduction in purchase price or more favorable transaction terms because the issue is unlikely to be resolved without a trial.

As noted in Robert L. Haig, *Commercial Litigation in New York State Courts* §§ 80.20, 80.21 (3d ed 2010), drafters (presumably buyers) often make a “strategic drafting choice” to define a MAE or MAC in broad and vague terms, and “seem to prefer more general, open-ended MAC clauses, with their potential for ambiguity and fact specific resolution, or MAC clauses that eliminate certain broad categories from coverage, such as a general drop in the stock market, as opposed to specific and clearly defined MAC clauses.”

Given that the case law that has emerged from the New York and Delaware courts tends to tip the scales in favor of sellers, buyers negotiating such clauses in New York or in contracts with New York choice of law provisions should consider whether they might actually better protect themselves through more specific drafting. Buyers must balance their interest in drafting a very broad, catch-all MAE clause against their interest in being able to successfully invoke it. For example, buyers could theoretically draft a MAE clause that supplies protection in the event of even foreseeable events, or events that have a short-term impact on earnings, as long as the language of the MAE clause is sufficiently clear. Sellers seeking greater clarity and predictability, on the other hand, should consider negotiating carve-outs for certain categories of events or a minimum amount of monetary damage or harm that could trigger the MAE clause.¹⁶ As is true with the drafting of all contract provisions, clarity and specificity can help to reduce exposure to lengthy and costly litigation.

ENDNOTES

- ¹ Nixon Peabody's 2016 MAC Survey reflected MAC clauses appearing in 92% of surveyed publicly filed deals.
- ² See 4B Robert L. Haig, Commercial Litigation in New York State Courts §§ 80.20, 80.21 (3d ed 2010), Chapter 80, Michael J. Chepiga and Paul C. Curnin, *Mergers and Acquisitions* (providing examples of parties who settled rather than litigating the MAE question). One recent case in the Southern District of New York – *Innkeepers USA Trust v. Cerberus Capital Management LP*, Case No. 1:11-ap-02557 – involved a buyer's attempt to terminate a \$1.1 billion deal based on a strict MAE clause with no carve-outs. The case was settled when the parties agreed to reduce the purchase price by \$100 million. In another recent case, Verizon successfully negotiated a \$315 million reduction in the purchase price for Yahoo (amounting to a 7.2% reduction), in part, by invoking a MAE clause based upon Yahoo suffering the largest known data breach in history.
- ³ Typically, sunk costs and general deal momentum prevent buyers from completely walking away from the transaction. Instead, buyers often threaten to invoke the MAE clause to terminate the contract, and use the clause as leverage to renegotiate more favorable transaction terms.
- ⁴ As a practical matter, even when drafters anticipate a short duration between execution of the contract and closing, they should give careful thought to the language and placement of a MAE clause. Closings are often unexpectedly delayed, particularly when conditioned upon factors outside of the parties' control, such as regulatory approvals. The longer the delay, the more variables enter the equation, and the more likely it becomes that a buyer will find a reason to invoke the MAE clause to terminate the contract or as leverage to renegotiate its terms. Therefore, even where the parties do not anticipate a lengthy delay between signing and closing, they should carefully consider how best to draft the MAE clause to maximize protection.
- ⁵ See *Hexion Specialty Chemicals, Inc. v Huntsman Corp.*, 965 A2d 715, 738 (Del Ch 2008) ("A buyer faces a heavy burden when it attempts to invoke a material adverse effect clause in order to avoid its obligation to close" and as of the date of this decision, "Delaware courts have never found a material adverse effect to have occurred," which "is not a coincidence."); *Frontier Oil v Holly Corp.*, No. 20502, 2005 WL 1039027 (Del Ch April 29, 2005) (seller represented that there were no actions pending or threatened other than those that would not have or reasonably be expected to have a MAE; buyer did not meet its burden of proving that a MAE had occurred after court unexpectedly rejected seller's legal defense in a pending proceeding; defense costs would range from \$15 million to \$20 million, and buyer did not show that this expense would materially affect long-term earnings into the future); but see *Osrsm Sylvania Inc. v Townsend Ventures, LLC*, No. 8123-VCP, 2013 WL 6199554 (Del Ch Nov. 19, 2013) (holding that a complaint adequately stated a claim for breach of a MAE warranty).
- ⁶ In another case, the Delaware Chancery Court found that a complaint, which alleged the seller had purposely manipulated financial statements and engaged in fraudulent business practices to paint a sanguine picture of the company for the buyer, when accepted as true, and when given the benefit of all reasonable inferences, adequately stated a claim for breach of a MAE warranty. (See *Osrsm Sylvania Inc. v Townsend Ventures, LLC*, No. 8123-VCP, 2013 WL 6199554 [Del Ch Nov. 19, 2013]). This decision caused a stir when it was first issued, but seems to have lost its luster. First, the case was never reported. Second, the court was applying a low standard for purposes of ruling on the seller's motion to dismiss. Third, the buyer alleged outright fraud on the part of the sellers, which gave a different backdrop than most MAE cases. And fourth, the MAE clause in question was located in a warranty provision rather than a termination provision. Below is a discussion of the different placement of MAE clauses.
- ⁷ See *Alliance Industries, Inc. v Longyear Holdings, Inc.*, 854 F Supp 2d 321 (WDNY 2012) (denying cross-motions for summary judgment on whether a MAE had occurred because although both parties had submitted expert opinions, neither party presented sufficient evidence to show the financial effect on the target's total assets and bottom line); *Solutia Inc. v FMC Corp.*, 456 F Supp 2d 429, 442 (SDNY 2006) ("[W]hether a particular non-disclosure could, in a 'party's commercially reasonable judgment, have a material adverse effect on the joint venture' is a question inherently difficult to resolve on summary judgment . . ."); *Gusmao v GMT Grp., Inc.*, No. 06 Civ. 5113(GEL), 2008 WL 2980039 (SDNY 2008) (issue of fact existed as to whether MAE occurred where buyer alleged that seller's Brazilian subsidiary was not in compliance with Brazilian law); *Pfizer v Stryker Corp.*, 348 F Supp 2d 131 (SDNY Aug. 1 2004) (issue of fact existed as to whether MAE occurred where buyer alleged that certain prosthetic joints sold by target were not in compliance with law); but see *IOP Cast Iron Holdings, LLC v. J.H. Whitney Capital Partners, LLC*, 91 F. Supp. 3d 456, 472 (SDNY 2015) (dismissing complaint for failure to state a claim where the MAE clause excluded "any adverse change in the general business or economic conditions generally affecting the industries in which [Aarrowcast] or any of its Subsidiaries operates," unless the change in business or economic conditions had a 'disproportionate effect,'" and where the complaint's allegations were plainly based on changed conditions that generally impacted the industry).

ENDNOTES

- ⁸ See *Sekisui Am. Corp. v Hart*, 15 F Supp 3d 359 (SDNY 2014) (after bench trial, holding that the failure of a particular project of the target company was not a MAE because at the time the buyer entered into the agreement, it knew that the fate of that project was uncertain); *Pfizer, Inc.*, 348 F Supp 2d 131 (denying buyer's motion for summary judgment because an issue of fact existed as to whether the buyer had knowledge at the time it entered into the agreement of the circumstances it now claims amounted to a MAE); *Shurtleff v Huber*, 186 F Supp 241 (SDNY 1960) (noting that a buyer's conduct in moving forward with a transaction despite knowing a fact, and then bringing suit claiming that the fact is a MAE, would be "quite relevant to the issue of materiality").
- ⁹ Several other cases decided by New York State courts mention MAE clauses, but did not actually analyze or determine whether a MAE had occurred. (See e.g. *Katz v NVF Co.*, 100 AD2d 470 [1st Dept 1984] [noting in a decision in a shareholder suit that the buyer and seller had agreed a MAE occurred and mutually terminated the merger where the target experienced a decline from \$2 million in net earnings to \$6 million in net loss]; *Honua Fifth Ave. LLC v 400 Fifth Realty LLC*, 122 AD3d 434 [1st Dept 2014] [finding an issue of fact as to whether buyer properly terminated the agreement to purchase real estate on the ground that an alleged air infiltration defect had a "material adverse effect" on the fair market value of certain residential units, but setting forth no analysis]; *Hanil Bank, New York Agency v A & E Intern., Ltd.*, 264 AD2d 346 [1st Dept 1999] [finding an issue of fact regarding the happening of default events, one of which could have been a MAE, but containing no analysis]). Another New York court decision addresses the applicability of a MAE clause, but involved an alleged breach of a MAE warranty by an insured; it did not involve a MAE termination provision (*AMBAC Assur. Corp. v First Franklin Financial Corp.*, 40 Misc 3d 1214[A] [Sup. Ct. 2013]). Further, as described below, MAE clauses in the insurance context are materially different than MAE termination clauses in mergers and acquisitions contracts. Another New York decision analyzes the applicability of a MAE clause permitting rescission of a contract for construction of a penthouse (*Plaza PH2001 LLC v Plaza Residential Owner LP*, 98 AD3d 89 [1st Dept 2012] [complaint stated claim based upon alleged material adverse changes to construction plans]), and is not particularly useful in the mergers and acquisitions context.
- ¹⁰ See e.g. *Sekisui Am. Corp. v Hart*, 15 F Supp 3d 359 (SDNY 2014) (after a bench trial, finding no MAE had occurred because the buyer knew before entering into the transaction that the fate of the target's breast cancer diagnostic assay project was uncertain, and therefore the ultimate failure of that project was not a MAE); *Rus, Inc. v Bay Industries, Inc.*, No. 01 Civ.6133C(GEL), 2004 WL 1240578 (SDNY May 25, 2004) (SDNY 2004) (not permitting MAE defense instruction to go to the jury where the evidence showed that the buyer terminated the contract only because of environmental issues, not because of profit swings).
- ¹¹ As noted above, the two Southern District of New York cases that are apparently at odds with other New York and Delaware cases on MAE clauses—*Am. Transtech Inc. v U.S. Trust Corp.*, 933 F Supp 1193 [SDNY 1996] and *Coastal Power Intern., Ltd. v Transcontinental Capital Corp.*, 10 F Supp 2d 345 [SDNY 1998]—both involved MAE clauses that were not located in a termination provision, but in a warranty or covenant. These cases did not directly address the intersection of MAE case law and case law on breach of warranty or breach of a covenant. But they certainly seemed to relax the burden of proof, particularly with regards to the materiality requirement.
- ¹² See *CBS Inc. v Ziff-Davis Pub. Co.*, 75 NY2d 496 (1990) (reliance is not a required element of a breach of warranty claim); *Coastal Power Intern., Ltd.*, 10 F Supp 2d 345 (SDNY 1998) (breach of warranty claim is barred only if buyer received facts indicating falsity of warranty from the seller, rather than from a third party).
- ¹³ See *Emposimato v CICF Acquisition Corp.*, 89 AD3d 418, 421 (1st Dept 2011); see also *White v Farrell*, 20 NY3d 487 (2013).
- ¹⁴ See *Alliance Industries, Inc.*, 854 F Supp 2d at 332.
- ¹⁵ See e.g. *Syncora Guarantee Inc. v EMC Mortg. Corp.*, 874 F Supp 2d 328 (SDNY 2012) (finding another MAE case "inapposite" because it did not involve an insurer, and citing N.Y. Ins. Law § 305); see also *AMBAC Assur. Corp. v First Franklin Financial Corp.*, 40 Misc 3d 1214(A) (Sup. Ct. 2013).
- ¹⁶ The 2016 NP MAC Survey reflects that on average, MAC clauses included 12.6 carve-outs per agreement. Common carve-outs included, for example, carve-outs for disproportionate effects, general economic conditions, industry wide changes, changes in laws and regulations, changes in GAAP, changes resulting from announcement of the agreement, changes resulting from actions contemplated by the agreement, failure to meet revenue or earnings projections, changes in interest rates, changes in political conditions, employee attrition, and reduction of customers or decline in business. On the other hand, none of the surveyed agreements included a quantification for "materiality."

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