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News & Types: Commercial, Competition & Trade Update

Termination and Settlement Agreement is Really Final, In Spite of Efforts to Overturn

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Most parties which conclude a release and settlement, or similar, agreement would probably expect the agreement to be final. According to a recent decision in the 7th Circuit Court of Appeals, this expectation is reasonable and parties can count on such an agreement to be enforced. (ADM Alliance Nutrition, Inc. v. SGA Pharm Lab, Inc. and Shawn Yu, 7th Circuit Court of Appeals, Nos. 16-2331 and 16-2593, December 14, 2017)

SGA Pharm Lab had been supplying ADM Alliance Nutrition (an affiliate of Archer, Daniels Midland, a large agricultural processor and food ingredient provider) with a product used to make medicated animal feed. The parties entered into a Purchase and Development Agreement on February 7, 2013 ("Purchase Agreement"). The Purchase Agreement required SGA to provide a signed and dated Certificate of Analysis detailing the potency of the product for each production lot it shipped to ADM. SGA's compensation was in part based on the potency of the product. Apparently, ADM received an offer to sell "New Animal Drug Applications" (NADA's) to a third party, which gave SGA the option to purchase the NADA's. SGA declined this option. For reasons that are unclear from the opinion (but do not bear on the key issue), SGA and ADM terminated their business relationship through a Termination and Settlement Agreement on September 12, 2014 ("Termination Agreement"). ADM was required to pay to SGA $750,000 within two days of the date ADM closed on the sale of the NADA's to the third party. This was completed.

But ADM claimed it later discovered that the Certificates of Analysis overstated the potency of the product. ADM asserted that it overpaid SGA by $1.1 million and would not have paid the $750,000 if had known of the misrepresentation. So ADM brought a breach of contract claim and fraud against SGA and a fraud claim against Yu, SGA's President. SGA and Yu filed a motion to dismiss the complaint.

The district court appears to have blind-sided ADM by treating the motion to dismiss as a motion for judgment on the pleadings. Consequently, the district court issued judgment in favor of SGA and Yu and awarded SGA and Yu $23,685 in attorneys' fees based on the provision in the Termination Agreement granting legal fees to the prevailing party. ADM appealed.

Judge Williams, who wrote the opinion, spent zero time on the merits of the fraud and breach of contract allegation. So the reader may wonder whether this is a case of crooks at SGA that got away with a fraud or ADM's regret at unintentionally giving up a claim they thought had merit.

In the end, it didn't matter. Virtually the entire opinion was devoted to whether ADM could evade the release language in the Termination Agreement. For this purpose, the court quoted from the Termination Agreement at length:

> ". . . . ADM hereby fully, completely, irrevocably and unconditionally releases, remises, acquits, and forever discharges SGA and its directors, officers, shareholders, members, managers, employees, agents, representatives, successors and permitted assigns (collectively, the "SGA Parties") of and from any and all charges, complaints, claims, promises, agreements, controversies, actions, causes of action, damages, suits, rights, expenses, losses, liabilities and obligations of any nature whatsoever (including attorneys' fees and costs actually incurred) (collectively, "Claims"), whether legal or equitable, whether known or unknown, that ADM may have against one or more of the SGA Parties . . ."

Said Judge Williams, "The language in these paragraphs is clear: it releases SGA and Yu from any and all claims arising out of the Purchase Agreement."

The court acknowledged that fraud was not specifically mentioned in the release language. But was to no avail to ADM since "the fact that a claim is not specifically listed in the release does not necessarily preclude that claim from having been within the contemplation of the parties and therefore barred." The fact that ADM did not know of the alleged fraud did not help it either, since the release referred specifically to known and unknown claims.

ADM cited Illinois cases that seemed to support its argument, specifically one in which an Illinois Appellate Court examined "the circumstances surrounding the execution of the release" in upholding a fraud claim by a party that had signed a release. But the court believed that the Illinois Supreme Court would not follow a "circumstances of the transaction" standard to permit parol evidence in construing an otherwise unambiguous release. ". . . [W]hen a contract is unambiguous on its face, the intent of the parties must be construed without consideration of parol evidence."

The court also agreed with SGA and Yu's argument that reliance is an element of a fraud claim and the Termination Agreement included specific non-reliance language: "No representations or commitment were made by the parties to induce each other to enter into this Agreement other than as expressly set forth herein."

To pile on to ADM, Judge Williams also affirmed the award of attorneys' fees. The Termination Agreement provided that if a legal action was brought to enforce or interpret the Termination Agreement, or because of an alleged breach, the prevailing party was entitled to attorneys' fees and costs. (The court did not discuss the fees and costs that were incurred in the appeal.)

It seems like a straightforward case. A party signed an all-encompassing release and later regretted it, claiming it discovered fraud after the signature. So what is to be learned?

The easy answer is to exclude fraud in the release. Fraud is often excluded in merger and acquisition agreements, especially in the provision excluding reliance on representations and warranties outside the agreement. But in the context of a release agreement, it is more difficult to exclude fraud. Parties to a hard fought dispute or litigation want finality. In addition, clever litigators can easily include a fraud count in a breach

of contract claim. So excluding fraud creates a huge loophole that risks reviving a dispute that the parties want to be done with.

Another approach is to limit the release to the transaction or dispute involved, especially if there is ongoing business or transactions that are still in progress. But even this might be hard in an actual case.

Probably the best lesson is to understand the scope of the release and to make sure that there are no potential transactions or claims that might unintentionally be released. The burden, properly, should be on the party which is granting the release.