

How Recent Del. Rulings Clarify M&A Deal Fraud Carveouts

By **Anthony Boccamazzo** (March 3, 2026, 6:18 PM EST)

After spending months or years conducting due diligence, negotiating and finalizing an M&A transaction, parties are hopeful that everything postclosing will run smoothly.

However, as is the case with all best-laid plans, after a buyer begins operating the target, the buyer and/or seller often learn of issues that they were not aware of during the transactional process. Typically, these issues, such as customer relationships that had soured or additional preclosing tax liabilities, are addressed by the agreement's representations and warranties.

As a result, parties typically have recourse for any breaches under the parties' representations and warranties insurance or the agreement's indemnity provisions, which are usually the exclusive remedy for any breaches of the parties' representations and warranties.

However, due to policy limits for representations and warranties insurance and caps in the indemnity framework of M&A agreements, a buyer and/or a seller may not be made whole, leaving parties exposed to millions of dollars of risk.

Likewise, buyers and/or sellers may learn that their contractual counterparty knew the representations were false when they made them, but, nonetheless, proceeded with the transaction anyway. In these instances, parties typically look to the fraud carveouts in the parties' agreement to address these difficult situations.

One of the primary elements of a fraud claim, as opposed to a breach of contract claim, is usually justifiable reliance by the party claiming that it was defrauded. For example, a party to an M&A transaction typically cannot claim it was defrauded when it knew, prior to closing, that the other party's representation was false.

Issues of justifiable reliance can often be complicated in the M&A space due to the terms of the parties' agreement — which often limit what representations parties can justifiably rely on — and due to the due diligence process, where the parties gain their own knowledge of the other's business.

However, recent Delaware guidance has provided further clarity regarding when a party can or cannot justifiably rely on certain representations made during the course of an M&A transaction. Specifically, the Delaware courts have addressed the (1) scope and enforceability of antireliance provisions; and (2)



Anthony Boccamazzo

whether a party can justifiably rely on a representation it knew or should have known was false due to its own due diligence.

Fraud Carveouts to Representations and Warranties Insurance and Indemnity Provisions

Typically, M&A agreements provide that representations and warranties insurance and/or the agreement's indemnity provisions are the sole or exclusive remedies for any party's breaches of the representations and/or warranties in an M&A agreement.

Representations and warranties insurance is insurance that is obtained by a party to the M&A agreement — most commonly the buyer — that shifts the risk from the buyer and/or seller to a third-party insurer with respect to breaches of the parties' representations and warranties.

According to a Dec. 17 study by the American Bar Association examining private targets being acquired by public companies, approximately 63% of agreements include a reference to representations and warranties insurance.[1] Typically, when a transaction involves such insurance, the parties' recourse for any breaches of the representations and warranties is to assert a claim under the policy, which can often be complicated and time-consuming.

Likewise, there are also specific policy limits to representations and warranties insurance, and, thus, parties may not be made whole if their claim is in excess of the policy limits.

M&A agreements also typically include indemnity provisions in addition to and/or in lieu of representations and warranties insurance. Under a typical indemnity provision, a buyer or seller must provide notice to its contractual counterparty of a claim for a breach of the representations and warranties of the agreement. If the claim is valid — which is an issue that often ends up being litigated — the breaching party is required to indemnify the nonbreaching party.

Like representations and warranties insurance, there are often caps as to the amount available to the aggrieved party under the indemnity provisions. For example, the amount available to the aggrieved party may be limited to a certain amount held in escrow. Likewise, there are often baskets — thresholds similar to an insurance deductible — and buckets, amounts dedicated to different types of claims, in indemnity provisions, which further complicate how much a party is entitled to if it has a valid indemnification claim.

According to the ABA study, approximately 89% of M&A agreements provide that the indemnity provisions are the exclusive remedy for the breach of a representation and/or warranty under the agreement.[2]

However, both representations and warranties insurance policies and indemnity provisions often include an exception for fraud, referred to as a fraud carveout. If a fraud carveout applies, parties are typically not limited to the representations and warranties insurance policy of the indemnity provisions as their sole remedy for inaccurate representations and warranties.

Importantly, parties are not limited to the policy limits under which representations and warranties insurance applies or the caps of the agreement's indemnity provisions if fraud is present and if the agreement permits the party to assert a fraud claim.

The fundamental and complicated questions then become whether a party can assert a claim for fraud

under the parties' agreement, and whether a party's misrepresentation constitutes fraud. In recent months, the Delaware courts have provided additional guidance on these thorny issues.

Johnson & Johnson — When a Party Can Justifiably Rely on Representations Made Outside the Agreement

One key issue that parties often face is whether their agreements permit them to assert a fraud claim when they relied on representations made outside their agreement. For example, during the course of the parties' discussions, one of the parties may make representations, whether orally or by email, etc., to induce the other to agree to the transaction, but those representations are not ultimately included in the final executed written agreement.

The issue then becomes whether the aggrieved party can assert a fraud claim based on that extracontractual representation, or whether they are barred by an agreement's antireliance provisions. This was one of the many issues addressed by the Delaware Supreme Court's Jan. 12 decision in *Johnson & Johnson v. Fortis Advisors LLC*.^[3]

In this case, Fortis Advisors sued Johnson & Johnson on behalf of Auris' former stockholders concerning Johnson & Johnson's \$3.4 billion acquisition of Auris, a company that created a surgical robot product known as iPlatform. Fortis sued for a breach of the parties' earnout provisions, which entitled the stockholders to additional consideration if Johnson & Johnson reached certain milestones with respect to sales of the iPlatform robot.

Likewise, in addition to its contractual earnout claims, Fortis alleged that Johnson & Johnson fraudulently induced Auris' stockholders to agree to a certain earnout milestone worth \$100 million, rather than accepting more money up front. The basis of the fraud claim was that Johnson & Johnson's CEO verbally told Auris that achieving the milestone was such a "high certainty" that Johnson & Johnson viewed it as an up-front payment.

Among many other findings, in September 2024, the Delaware Court of Chancery found that Johnson & Johnson's representation was fraudulent when that certain milestone was not reached, and that the \$100 million was never paid.

Johnson & Johnson appealed to the Delaware Supreme Court, arguing that, among other things, the agreement precluded Fortis' fraud claim because it contained an exclusive remedy provision in the indemnification provisions as well as certain antireliance provisions, which are specific terms in an agreement that preclude parties from relying on representations made outside that agreement.

Specifically, Johnson & Johnson argued that an antireliance provision included in the parties' agreement, which stated that Johnson & Johnson would not rely on any extracontractual representations made by Auris, should have also precluded Auris from relying on Johnson & Johnson's representations made outside the agreement.

However, in its January decision, the Delaware Supreme Court rejected Johnson & Johnson's arguments. The court, relying on its 2006 decision in *ABRY Partners V LP v. F&W Acquisition LLC*,^[4] found that Delaware law only enforces antireliance provisions where the party has "unambiguously contracted that it did not rely upon statements outside the contract's four corners in deciding to sign the contract."

The Delaware Supreme Court found that the antireliance provision in the parties' agreement only

prohibited Johnson & Johnson from relying on Auris' representations made outside of the contract, not the other way around. Thus, the court found that Johnson & Johnson did not have a similar protection, and that Auris could rely on Johnson & Johnson's verbal or other noncontractual representations as the basis for a fraud claim.

Consequently, the Delaware Supreme Court reaffirmed ABRY Partners and found that a one-sided antireliance clause, i.e., a clause that only precludes one party from relying on extracontractual representations, cannot be relied upon by the other party to evade a fraud claim.

Consequently, the Delaware Supreme Court has made clear that exclusive remedy provisions in an M&A agreement will not preclude extracontractual fraud claims absent clear and unambiguous language stating that the party is not relying on those representations.

Paragon Metals — When a Breach Becomes Fraud

Another primary issue facing parties contemplating a fraud claim is when they can convert a simple breach of a representation contained in an M&A agreement to a fraud claim. This question often turns on whether the breaching party knew the representation was false, and, more complicated, if the aggrieved party could justifiably rely on the representation.

Delaware is a pro-sandbagging state, which means that under Delaware law, absent express contractual language to the contrary, a party can typically assert a claim for a breach of representation or warranty in an agreement, even if the aggrieved party knew that its counterparty's representation and/or warranty was inaccurate. The rationale for sandbagging is that the parties negotiated and agreed to the representation and/or warranty, and thus, the nonbreaching party should receive the benefit of the parties' bargain.

However, as discussed, one of the key elements of a fraud claim is that a party has to show it justifiably relied on the other party's alleged fraudulent representations. Therefore, while a party can assert a breach of contract claim when it knew the representation was false, it cannot assert a fraud claim based on that same false representation.

Issues typically arise in the middle ground where a party did not necessarily know that a representation was false but could or should have known of its falsity, particularly when it conducted its own due diligence. That was the question addressed by the Delaware Superior Court in August 2025 in *Paragon Metals Holdings LLC v. Smith*.^[5]

In the Paragon case, the buyer of a machined components and metals company asserted claims for fraud against the sellers relating to the sellers' failure to disclose certain information concerning its customer relationships. Specifically, the buyer alleged that the seller failed to disclose that two of the company's top 10 customers had informed the company prior to closing that they planned to materially decrease their business.

According to the buyer, the seller's failure to disclose this information constituted fraud under various representations in the agreement, including the agreement's representations concerning the company's customer relationships and whether a material adverse effect had happened to the company.

Just after the closing, the buyer claimed that it learned that one customer would move the manufacturing of its parts in-house and the other would substantially reduce its volume of orders, both

of which the court found that the seller knew prior to closing due to forecasts that it had received from those customers.

However, after a five-day trial, on Aug. 13, 2025, the Delaware Superior Court rejected the buyer's fraud claims. The court found that the buyer did not justifiably rely on the seller's representations because the buyer knew or should have known the representations were false during the buyer's due diligence on the transaction. For example, the court found that, during due diligence, the buyer had met with and obtained its own forecasts from the two customers it now complained about.

The court further found that the buyer knew or should have learned from those forecasts and meetings that the two customers' markets would be "softening" postclosing. Likewise, the court found that the buyer's team had discussed these specific issues concerning the two customers with the seller prior to closing, demonstrating that the buyer was at least aware of certain issues with these customers.

Thus, although the court recognized the representations in the agreement were false, the court found that the buyer could not assert a fraud claim because it knew or should have known about the customers' declining business with the company.

As a result, whether a breach will turn into a fraud claim will often turn on what the party claiming the breach actually knew or should have known regarding the representation and/or warranty prior to closing.

Conclusion

While this recent Delaware guidance is helpful in understanding certain complex issues relating to fraud claims in M&A transactions, many questions and complexities remain as to the viability of parties to assert fraud claims in addition to their breach of contract claims.

Anthony Boccamazzo is counsel at Olshan Frome Wolosky LLP.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of their employer, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] American Bar Association, Private Target Mergers & Acquisitions Deal Points Study (Including Transaction from 2024 and Q1 2025), (12/17/25).

[2] *Id.*

[3] *Johnson & Johnson v. Fortis Advisors LLC*, No. 490, 2024, 2026 WL 89452 (Del. Jan. 12, 2026).

[4] *Abry P'rs V, L.P. v. F & W Acq. LLC*, 891 A.2d 1032, 1059 (Del. Ch. 2006).

[5] *Paragon Metal Holdings LLC v. Smith*, No. N21C-12-090 SKR CCLD, 2025 WL 2531610, at *1 (Del. Super. Ct. Aug. 13, 2025).