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Plain Language of Provision in Right of First Refusal Agreement Requiring 60 Days' Notice to All Stockholders Sufficient to Defeat Motion to Dismiss

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In *Gower v. Trux, Inc., et al.*, 2022 WL 534204 (Del. Ch.) (Fioravanti, V.C.), the Court of Chancery denied a challenge, at the motion to dismiss stage, to claims seeking to invalidate a sale of all of the stock of Trux, Inc. (the Company). Looking to the plain text of the governing right of first refusal agreement (the ROFR Agreement), the Court held that the plaintiff had adequately pled noncompliance with a notice provision that triggered a waterfall of priority rights of first refusal and co-sale rights.

The claims were brought by the Company's former CEO and a Company stockholder against the Company's other individual stockholders and Viking Venture Partners, LLC (Viking), which owned a 22% stake prior to purchase of all of the Company's stock. The crux of the plaintiff's claims was that he was not given the requisite 60 days' notice of the proposed sale to Viking, thus rendering the sale null and void ab initio per the ROFR Agreement's express terms.

In the event a stockholder wished to sell or transfer its stock to a third party, the ROFR Agreement prescribed a process to be followed that triggered several rights of first refusal. The initial step in the ROFR Agreement process was the delivery of a proposed transfer notice (the Proposed Transfer Notice) to all stockholders at least 60 days in advance of the contemplated closing of the stock sale transaction. Upon delivery of the Proposed Transfer Notice, the waterfall of rights of first refusal kicked in, as follows:

- Viking had 15 days following delivery of the Proposed Transfer Notice to exercise its primary priority right of first refusal.
- During that same 15-day period, a defined set of secondary stockholders could exercise their secondary right of first refusal, subject to Viking's exercise of its higher-priority right of first refusal. If a stockholder declined to exercise its secondary right of first refusal, notice of that decision was required to be delivered to a defined set of tertiary stockholders, the Company, and the selling stockholder.
- Within 30 days of delivery of the Proposed Transfer Notice, the tertiary stockholders could exercise their tertiary priority right of first refusal. If a tertiary stockholder declined to exercise its right of first refusal, a notice of that decision was required to be delivered to the Company and the selling stockholder.
- If shares remained after the exercise (or not) of all rights of first refusal, the Company had 10 days (40 days after delivery of the Proposed Transfer Notice) to exercise a right to repurchase any of the remaining offered shares. If the Company declined that right, the stockholders that had already exercised their right of first refusal had another 15 days to purchase any remaining outstanding shares on offer.

- Should offered shares still remain after the Company's repurchase right, each stockholder could exercise a co-sale right—to participate on a pro rata basis in the sale of shares to the third party—by serving a notice within 15 days of delivery of the tertiary notice (55 days after delivery of the Proposed Transfer Notice).

The ROFR Agreement provided that any proposed transfer that did not comply with the above-described procedure "shall be null and void ab initio, shall not be recorded on the books of the Company or its transfer agent and shall not be recognized by the Company."

The plaintiff alleged that he received 15 days' notice of the proposed stock sale to Viking, and not the 60 days' notice to which he was entitled under the ROFR Agreement. The defendants asserted that the plaintiff was only entitled to 15 days' notice because he intended to exercise a co-sale right, not a right of first refusal, and otherwise had sufficient time to evaluate the proposed transaction.

The Court held that the plaintiff had adequately pled that the sale transaction to Viking was the product of a breach of contract—specifically, noncompliance with the required notice procedures. Looking to the ROFR Agreement's plain language, the Court held that all stockholders were entitled to 60 days' notice of a proposed stock sale transaction regardless of whether it was known or anticipated that a stockholder lower down in the priority scheme did not intend to or could not otherwise exercise its right of first refusal. The Court likewise rejected that the defendants had "substantially complied" with the ROFR Agreement's notice provision given the lack of an attempt to provide the required notice and that an unsigned written consent waived the required timing for the Proposed Transfer Notice. Moreover, because the ROFR Agreement contemplated corporate action to not record or recognize a transaction that is void for noncompliance with notice procedures, the Court found that the Company was a proper defendant, albeit nominal, for the plaintiff's claim requesting a declaration that the sale transaction to Viking was null and void.

Rights of first refusal are a common and beneficial mechanism to exert control over who becomes a stockholder in a particular company. Co-sale rights have a corresponding function: to allow all stockholders to enjoy the benefits of a stock sale or other liquidity event proposed by a single stockholder. Delaware law empowers stockholders to enter into agreements codifying agreed-on rights of first refusal and co-sale rights. Notice requirements are basic, yet fundamental, components of rights of first refusal and/or co-sale rights, as reflected by the *Gower v. Trux* decision. They should be literally construed and complied with to ensure the integrity of a proposed transaction, especially where, as in *Gower v. Trux*, the governing agreement provides that a stock sale can be declared null and void in the event of noncompliance.