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Court of Chancery Rules That 'Commercially Reasonable Efforts' Obligation Does Not Imply a 'Duty to Warn'

Contributor

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Recent Delaware decisions in *Williams Companies v. Energy Transfer Equity, L.P.*, and *Akorn, Inc. v. Fresenius Kabi AG*, examined contract provisions requiring "commercially reasonable efforts" and "reasonable best efforts" and concluded that these provisions imposed affirmative obligations on parties to "take all reasonable steps" to satisfy the subject contractual condition and to disclose the awareness of a "problem" and work together with the contractual counterparty to try to solve the perceived issue.[1] In *Vintage Rodeo Parent, LLC v. Rent-A-Center, Inc.*, C.A. No. 2018-0927-SG, the parties agreed to use "commercially reasonable efforts" to "consummate and make effective as promptly as practicable ... the transactions contemplated by" a merger agreement. The Delaware Court of Chancery analyzed whether the affirmative obligations articulated in *Williams* and *Akorn*, among other cases, also gave rise to a "duty to warn" after a party determined to terminate a merger agreement under a contractual right to do so. The Court of Chancery held that they did not.

In *Vintage*, after an expedited trial, the Court of Chancery held that defendant Rent-A-Center, Inc. (RAC) validly terminated its merger agreement with plaintiff Vintage. Vintage and RAC had agreed to a transaction whereby Vintage would acquire all of RAC's shares for $15.00 per share, which represented a 47% premium to the unaffected price. While the merger agreement contained an "End Date" of 11:59 p.m. on December 17, 2018, if the merger was still under regulatory review at that time, either party could elect to extend the End Date twice, in three-month increments, simply by "delivering written notice" to the other party prior to the End Date.

Through no fault of RAC, the merger was still in the middle of regulatory approval as December 17, 2018, approached, and it was clear that approval would not be obtained before the End Date. In early December, RAC's board of directors concluded that, because RAC's performance had improved, it was in the best interest of RAC and its stockholders to terminate the merger with Vintage if the opportunity arose. However, the RAC board expected Vintage to deliver written notice to extend the End Date and determined that RAC should therefore continue its efforts to consummate the merger. Thereafter, RAC management proceeded in a "business as usual" fashion with Vintage, including in their joint dealings with regulators, and no one informed Vintage of the RAC board's conclusion that it might terminate the agreement if the opportunity arose. When Vintage did not deliver notice to extend the End Date on December 17, 2018, RAC sprang into action, delivering written notice terminating the merger and issuing a press release five minutes later notifying the market of the termination. Vintage quickly filed litigation in Delaware alleging breach of contract, among other claims, and asked the Court of Chancery to order RAC to close the merger.

Vintage argued that RAC had breached its obligation to use "commercially reasonable efforts" to close the merger because RAC's "business as usual" conduct after RAC's board had decided it wanted to terminate the merger deceived Vintage, and RAC was obligated to give Vintage a "heads-up" that RAC was planning to terminate the merger. The court disagreed and found that RAC did nothing untoward. The court stated that "parties are assumed to have knowledge of their own contractual rights" under Delaware law. Unlike other Delaware cases, the evidence did not show that RAC was aware of any "problem" and failed to address it. There was no evidence that RAC knew that Vintage was unaware of, or mistaken about, its contractual rights.[2] To the contrary, the court

[1] *See Williams Companies v. Energy Transfer Equity, L.P.*, 159 A.3d 264, 273 (Del. 2017); *Akorn, Inc. v. Fresenius Kabi AG*, C.A. No. 2018-0300-JTL, slip op. at 225 (Del. Ch. Oct. 1, 2018), *aff'd*, 198 A.3d 724 (Del. 2018) (TABLE).

[2] The court also expressly declined to consider whether such inaction would have resulted in a breach of the commercially reasonable efforts provision.

found the opposite: RAC assumed Vintage would exercise its right to extend the End Date. According to the evidence at trial, "[i]t appear[ed] that Vintage simply forgot the End Date in the Merger Agreement — and its implications."

The court also rejected Vintage's argument that the parties' joint efforts to close the merger, which contemplated deadlines beyond the December 17, 2018, End Date, was evidence of deception sufficient to warrant ordering RAC to close the merger. The court noted that Vintage did not allege fraud and that RAC was merely doing what it was contractually required to do: take efforts to obtain regulatory approval and close the merger. The court also found legitimate business reasons for not informing Vintage of the RAC board's decision to terminate the merger if given an opportunity. For example, the court noted that such disclosure "could have upset its merger partner and complicated their relationship going forward" if Vintage had extended the End Date and the merger had closed.

Finally, the court also found that the "commercially reasonable efforts" provision did not imbue RAC with a "duty to warn" Vintage that RAC would terminate the merger agreement if given the opportunity. First, the court noted that such an "advance notice" provision was not in the relevant section of the merger agreement, though the merger agreement did require advance notice before exercising several other termination rights. The court stated that it "should refrain from writing a provision into a contract when the parties could have done so themselves, but chose not to." Second, the court held that there was no duty to warn here because "[c]ommercially reasonable efforts do not require that sophisticated parties remind one another of their contractual rights."

Succinctly summarizing its conclusion, the court stated that "[i]f an agreement to use commercially reasonable efforts to comply with obligations in a contract means that a party cannot exercise its bargained-for right to terminate that contract, that bargained-for right would be illusory." The court found that RAC validly terminated the agreement.

The *Vintage* case serves as a reminder that Delaware courts will give great weight to the express rights and obligations negotiated by sophisticated parties who act in good faith during the post-signing process. Following on the heels of the *Williams* opinion in the Delaware Supreme Court and the *Akorn* opinions in the Delaware Supreme Court and the Delaware Court of Chancery, the *Vintage* case adds to the recent slate of case law further refining what Delaware courts expect from sophisticated parties that agree to "reasonable" efforts provisions.