Delaware Supreme Court Reverses Preliminary Injunction Requiring Go-Shop; Reaffirms "No Single Blueprint" to Satisfy *Revlon* Duties

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On Friday, December 19, 2014, the Delaware Supreme Court reversed a preliminary injunction entered by the Delaware Court of Chancery which had (a) barred, for 30 days, a stockholder vote to approve the combination of C&J Energy Services, Inc. and a division of Nabors Industries Ltd., (b) required C&J to conduct a "go-shop" during that period and (c) preemptively declared that such "go-shop" did not constitute a breach of the "no-shop" or other deal-protection provisions in the Nabors/C&J merger agreement. In reversing the injunction, the Supreme Court held that the C&J board likely satisfied its *Revlon* duties (to the extent such duties applied), notwithstanding the lack of a pre-signing market check, given that "[w]hen a board exercises its judgment in good faith, tests the transaction through a viable passive market check, and gives its stockholders a fully informed, uncoerced opportunity to vote to accept the deal, [Delaware courts] cannot conclude that the board likely violated its *Revlon* duties."

The transaction at issue is structured as a so-called "tax inversion." While C&J stockholders will own 47% of the shares (with Nabors owning 53% of the shares) of a new Bermuda company, C&J negotiated for a number of governance rights that favor C&J stockholders, including the right to designate a majority of the initial board and control of the nominating committee, supermajority voting requirements, a right for C&J stockholders to receive pro rata consideration in any future sale of the company and a standstill obligation and transfer restrictions binding on Nabors. Moreover, the merger agreement contained a "fiduciary out" for the C&J board should a superior proposal emerge.

On November 24, 2014, in a bench ruling, the Court of Chancery entered a preliminary injunction after finding that heightened *Revlon* duties applied and that the shareholder-plaintiffs had made a "plausible" showing of a likelihood of success on the merits that the C&J board had breached its fiduciary duty of care in approving the transaction. The Court of Chancery noted that, while the facts presented a close call, it appeared that the C&J board had approached the deal as an acquisition, rather than as a sale, had taken no steps to shop the company, and had failed to sufficiently inform itself that the value received would be the best attainable value for stockholders. Importantly, the Court of Chancery made no finding as to the aiding and abetting claim asserted against Nabors.

On appeal, the Supreme Court reversed the decision, holding that the lower court misapplied the standard for a preliminary injunction, which requires a plaintiff to show a *reasonable* likelihood of success on the merits of its claims, and not simply a *plausible* likelihood of success. Indeed, the Supreme Court found that there was no reasonable probability that the C&J board failed to comply with *Revlon*, reiterating longstanding Delaware law that there is "no single blueprint" to satisfy a board's *Revlon* duties. The Supreme Court again held that a board can satisfy such duties without conducting an active market check "so long as interested bidders have a fair opportunity to present a higher-value alternative, and the board has the flexibility to eschew the original transaction and accept the higher-value deal." Here, the Supreme Court relied on the facts that: (1) the merger agreement permitted a passive, post-signing market check with a "modest" 2.3% termination fee; (2) there appeared to be no improper board motives present; (3) the board appeared to be well informed of value and the deal structure, as evidenced by its negotiations for protective governance provisions; and (4) C&J stockholders will have an informed, uncoerced opportunity to vote on the deal. Accordingly, the Supreme Court found that the record did not support a conclusion that the C&J board likely breached its fiduciary duties and thus did not support the entry of the preliminary injunction.

Notably, the Supreme Court also held that it was improper for the Court of Chancery to enter a mandatory injunction declaring that the court-ordered "go-shop" would not violate the Nabors/C&J merger agreement because to do so would deprive Nabors of its contractual rights without any finding of wrongdoing by Nabors.

The decision clears the way for a merger vote and, regardless of the outcome, offers a number of key takeaways:

- This case provided the Supreme Court with a timely opportunity to provide a salient reminder that the original *Revlon* decision, and the *QVC* decision that followed it, largely involved questions of loyalty—*i.e.*, "board resistance to a competing bid after the board had agreed to a change of control, which threatened to impede the emergence of another higher-priced deal." Shareholder-plaintiffs in particular often seek to stretch the teachings of *Revlon* to require boards to become auctioneers any time they engage in a change-of-control transaction. Here, the Supreme Court rejected this notion and stated that "*Revlon* does not require a board to set aside its own view of what is best for the corporation's stockholders and run an auction whenever the board approves a change of control transaction." Thus, the decision reinforces that a passive, post-signing market check may be used to satisfy *Revlon* where the board is adequately informed, there are no material barriers against the emergence of a superior proposal and the company's stockholders are provided with a non-coercive, fully informed shareholder vote.
- The decision also reaffirms that, while the Court of Chancery's equitable powers are broad, Delaware courts generally are reluctant to "blue-pencil" merger agreements and other agreements, particularly where doing so would eliminate or substantially change the rights of innocent buyers who negotiated for such terms at arm's length. The opinion strongly suggests that the Court of Chancery would first need to conclude that the buyer aided and abetted an underlying breach of fiduciary duties by the target's board before depriving that buyer of its bargained-for deal-protection provisions.
- In its analysis, the Supreme Court did not address one of the more provocative questions arising from the case—namely, whether the transaction constituted a change-of-control that triggered *Revlon* duties. In a footnote, the Court recognized that even the seminal *QVC* decision (Del. 1993) suggested that "contractual provisions limiting the power of a majority stockholder and securing the minority's ability to share in any future control premium might take a transaction out of Revlon's reach" but declined to consider whether *Revlon* applied given the timing exigencies and the potentially novel issues that would be involved in such an analysis. Instead, the Court assumed, for the sake of analysis, that *Revlon* applied.
- In addition to tax inversions, many other structures (*e.g.*, Reverse Morris Trusts, reverse mergers and mergers of equals) often contain protective provisions that are designed to enhance the protections of public stockholders relative to a majority or significant minority stockholder. There are also other contexts in which the applicability of *Revlon* may be unclear, such as in deals involving mixed cash and stock consideration. The case serves as a reminder that many deals that may not resemble a traditional change-of-control transaction may trigger (or may be argued to have triggered) enhanced scrutiny.

See a copy of the Delaware Supreme Court's opinion in *C&J Energy Services, Inc. v. City of Miami General Employees' and Sanitation Employees' Retirement Trust.*

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