EFiled: Apr 02 2020 05:21PM EDT
Transaction ID 65554329
Case No. 2020-0249-

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

Level 4 Yoga, LLC, Plaintiff, v. CorePower Yoga, LLC, CorePower Yoga Franchising LLC, Defendants.	)	C.A. No. _____

VERIFIED COMPLAINT

Plaintiff Level 4 Yoga, LLC ("Plaintiff"), by and through its undersigned counsel, alleges for its Verified Complaint against Defendants CorePower Yoga, LLC and CorePower Yoga Franchising LLC (together, "Defendants"), as follows:

NATURE OF THE ACTION

1. Defendants, franchisors of the CorePower branded yoga studios throughout the United States, wanted to buy thirty-four CorePower Yoga-branded yoga studios owned and operated by Plaintiff in five states. Plaintiff gave Defendants a call option on the studios in a Call Option Agreement dated as of April 27, 2017 (the "Call Option"). In the spring of 2019, Defendants expressed an interest in exercising the Call Option but on different timing than the parties had agreed two years earlier. Plaintiff was willing to sell but was reluctant to put off the immediate closing provided in the Call Option. Defendants pressed for additional time and, ultimately, the parties settled on a closing date of April 1, 2020, with a valuation date

of March 31, 2019 and with no closing conditions, all as reflected in the parties' Asset Purchase Agreement as amended in January 2020 (the "Agreement").

2. Now, while people around the world deal with the devasting consequences of the COVID-19 pandemic, Defendants have seized upon the crisis to renege. The Agreement has no *force majeure* clause that would allow Defendants to back out, so Defendants have manufactured a series of excuses based on the temporary closure of their yoga studios—Plaintiff's and Defendants'—to claim a material adverse effect that justifies not closing on the purchase.

3. The law in Delaware, whose decisional law and jurisdiction the parties incorporated into the Agreement, is clear that "a corporate acquirer may be assumed to be purchasing the target as part of a long-term strategy. The important consideration therefore is whether there has been an adverse change in the target's business that is consequential to the company's long-term earnings power over a commercially reasonable period, which one would expect to be measured in years rather than months." *Hexion Specialty Chemicals, Inc. v. Huntsman Corp*., 965 A.2d 715, 738 (Del. Ch. 2008). The temporary closure of Plaintiff's studios pursuant to state and local temporary quarantine directions, all as required by the Legal Compliance provisions of the Agreement and studio franchise agreements, do not justify Defendants' refusal to perform.

4. Plaintiff therefore brings this action for a declaratory judgment that Defendants are obligated to close the transaction contemplated by the Agreement, for specific performance under the Agreement, and for such contract damages as are occasioned by Defendants' unlawful refusal.

5. Driven by the terms set in the Call Option, the timing, sequence, and conditions of closing were a significant part of negotiating the Agreement. Rather than immediately closing on the purchase of the yoga studios, Defendants sought and received agreement on a delayed and staggered closing where the parties would break the yoga studios into groups and close on each group of yoga studios on different dates. Plaintiff conditioned their agreement to the delays on the following conditions: the Agreement would contain no conditions to closing and Defendants, not Plaintiff, would assume any market and industry-wide risk associated with the delayed closing. After months of these negotiations and numerous extensions of the Call Option, the parties executed the Agreement on November 27, 2019. A true and correct copy of the Agreement as amended in January 2020 is attached to this complaint as **Exhibit A.**[1]

6. As the Agreement makes clear, the parties specifically envisioned that there may be market and industry-wide events, including events like COVID-19,

[1] Exhibits C, E, F, G, H, I and K to the Agreement have been excluded to preserve confidentiality.

that would impact the yoga business between execution and closing and the parties assigned the risk of those events to Defendants. Since the Call Option had set target dates that formed the foundation of the payment and studio transfer dates in the Agreement, Defendants agreed that they were required to move forward with each of the staggered closing dates whether or not market events occurred.

7. The Agreement expressly provides that on April 1, 2020 (the "Initial Closing Date"), Defendants were required to pay Plaintiff $6,254,452.34 (minus certain estimated assumed liabilities) for the purchase of eight yoga studios located in Colorado, with subsequent closings to occur at later dates. Further closing dates are scheduled for July 1, 2020 and October 1, 2020.

8. Until mere days before the Initial Closing Date, the Defendants did not mention anything about a material adverse effect on operations in Plaintiff's studios or in Defendants' studios, did not ask for a delay in the Initial Closing Date, and did not ask for additional time to complete the balance of the transaction in light of the pandemic. Defendants just want out of the obligation to buy Plaintiff's thirty-four yoga studios because COVID-19 and the government responses to it, including the temporary closure of businesses like yoga studios, have changed the economics of the deal.

9. This is precisely the risk that Defendants agreed to assume when they bargained for a delayed and staggered closing. Defendants, who are owned by a

large private equity firm and were represented by sophisticated counsel, could have demanded that the Agreement include a closing condition allowing them to back out of the Agreement in an unexpected market downturn or due to an unexpected event, but they did not. Defendants could have insisted that the Agreement include a *force majeure* clause, but they did not. Defendants could have set a break fee that allowed them to walk away from the deal for a fixed amount of money, but they did not.

10. On April 1, 2020, Defendants failed to proceed with the Initial Closing Date, breaching the Agreement. As a result of Defendants' breach, Plaintiff is entitled to a declaration of its rights under the Agreement, to specific performance, and to recompense for the damages it has incurred, and will continue to incur, as a result of Defendants' conduct.

PARTIES

11. Plaintiff Level 4 Yoga, LLC is a Colorado limited liability company that operates franchised yoga studios under the CorePower Yoga brand.

12. Defendant CorePower Yoga, LLC is a Colorado limited liability company that owns and operates yoga studios throughout the United States.

13. Defendant CorePower Yoga Franchising, LLC is a Colorado limited liability company and the franchising arm for CorePower Yoga, LLC in the United States.

JURISDICTION AND VENUE

14. This Court has jurisdiction over the action and the parties, per the terms of the Agreement. Ex. A, Agreement § 8.10.

15. The Agreement is governed by Delaware law. *Id.* § 8.9.

16. The Agreement expressly provides that, by executing the Agreement, each party "irrevocably submits to the exclusive jurisdiction of the state courts of the State of Delaware or the United States District Court located in the State of Delaware for the purpose of any Action between the parties arising in whole or in part under or in connection with this Agreement." *Id*. § 8.10.1(a).

FACTUAL BACKGROUND

A. The Parties Negotiate and Execute the Asset Purchase Agreement.

17. Plaintiff owns and operates CorePower Yoga-brand yoga studios throughout the United States. The studios are operated under franchise agreements that, among other things, require franchisees to comply with all local laws and regulations applicable to the studios.

18. Defendant CorePower Yoga, LLC also owns and operates yoga studios throughout the United States. Defendant CorePower Yoga Franchising, LLC is the franchising arm for CorePower Yoga, LLC in the United States. Defendants' yoga studios operate under the same general conditions and terms, including the

obligation to comply with all local laws and regulations, as are applicable to Plaintiff's studios.

19. In April 2017, Plaintiff gave Defendants a call option on the studios in a Call Option Agreement dated as of April 27, 2017 (previously defined as the "Call Option"). A true and correct copy of the Call Option Agreement is attached to this complaint as **Exhibit B**. The Call Option provided for Defendants to purchase certain yoga studios from Plaintiff and to execute an Assignment and Assumption Agreement with respect to the applicable Assumed Liabilities, Transferred Contracts, Transferred Leases, and Transferred Permits associated with those studios, all at a certain price determined as of a date triggered by the Exercise Notice, all of which terms are defined in the Call Option.

20. On April 3, 2019, a Control Event as defined under Section 1(b) of the Call Option occurred and Defendants issued an Exercise Notice, exercising their Purchase Rights (as defined in the Call Option). The parties began discussing the timing of and valuation of the Purchase Rights under the Call Option for Defendants' purchase of certain business assets and liabilities from Plaintiff, including thirty-four of its yoga studios in Colorado, Illinois, North Carolina, South Carolina, and Arizona.

21. During the negotiation of the Agreement, Plaintiff sought an immediate closing on all locations as provided in the Call Option.

22. Defendants wanted all of the economic terms in the Call Option, but they negotiated for a delayed and staggered closing in tranches of studios, further divided by state, in order to extend the time during which Defendants would absorb Plaintiff's thirty-four studios as well as extend the time when Defendants would pay for those studios.

23. The parties ultimately compromised, and as memorialized in the Agreement, Plaintiff agreed to a staggered closing with closing dates for groups of studios on April 1, July 1 and October 1, 2020, but without any closing conditions and with Defendants assuming any market and industry-wide risk between execution of the Agreement and closing.

24. On November 27, 2019, the Plaintiff and Defendants entered into the Agreement.

25. The Agreement divides the studios into three separate tranches: Tranche 1, Tranche 2, and a "Development" tranche, each of which has a different closing date under the Agreement. *See* Ex. A, Agreement at Ex. D., Closing Schedule.

26. Tranche 1 consists of eight yoga studios located in Colorado and fifteen studios located in Illinois. *Id.* The closing date for the Colorado studios in Tranche 1 was the Initial Closing Date, April 1, 2020. Valuation for the studios in Tranche 1 was set as of March 31, 2019, so no intervening events affect the valuation of the

studios in Tranche 1. On the Initial Closing Date, Defendants were required to pay Plaintiff $6,254,452.34, less certain assumed liabilities. *Id.* § 2.2.1(i). Defendants did not do so.

27. The closing date for the Illinois studios in Tranche 1 is October 1, 2020, with the studios valued as of March 31, 2019, so that no intervening events affect that valuation. On October 1, 2020, Defendants are required to pay Plaintiff an additional $13,850,773.05, minus certain assumed liabilities. *Id.*

28. Tranche 2 consists of studios located in Arizona and North Carolina, the closing date for which is July 1, 2020. For these studios, Plaintiff agreed to accept some pricing risk from intervening events, and the payment due from Defendants to Plaintiff for these studios will be determined by a formula incorporating the net income, interest expense, taxes, depreciation, and amortization of the Tranche 2 studios as of March 31, 2020. *Id.* § 2.2.2. This is the only portion of the purchase price for which Defendants successfully negotiated, and for which Plaintiff agreed to accept, pricing risk for events after March 31, 2019.

29. Finally, the Development Tranche consists of studios located in South Carolina, North Carolina, and Arizona, with a closing date of July 1, 2020, with the studios valued as of March 31, 2019 so that no intervening events affect that valuation. Defendants agreed to a purchase price for these studios of $3,212,623. *Id.* §§ 2.2.3-2.2.4.

30. At the time of closing, the Agreement generally provides that Defendants would pay the specified portions of the purchase price to Plaintiff and that Plaintiff would provide certain documentation for the transfer of ownership, such as bills of sale. *See id.* § 2.4.[2]

31. The Agreement contains no conditions that must be satisfied by Plaintiff in order for the closing date for the Colorado studios in Tranche 1 to occur on the Initial Closing Date, or for either of the subsequent two closings to occur.

32. Rather, the Agreement reflects Defendants' unconditional promise to purchase all of the thirty-four yoga studios for the specified purchase price.

B. Defendants Breach the Agreement by Wrongfully Refusing To Close.

33. After executing the Agreement and in the time leading up to the Initial Closing Date, Plaintiff worked diligently to prepare the necessary materials for closing, at considerable expense, and worked in good faith with Defendants and their counsel to be prepared for closing.

34. Beginning in late March 2020, Defendants' sponsor, TSG Consumer Partners, began to indicate that Defendants might not want to close on April 1, 2020,

[2] The exception to this structure was the Development Tranche. Unlike for Tranches 1 and 2, where the purchase price is due to be paid to Plaintiff at closing, the purchase price for the Development Tranche was effectively paid upon execution of the Agreement by way of a refund of certain franchise fees and development costs incurred by Plaintiff, plus a premium. The Development studios are subject to a cash flow arrangement set forth in Section 2.2.4 of the Agreement.

because the transaction was no longer as attractive to the sponsor as it had been before the shutdowns caused by COVID-19.

35. At the same time, however, Defendants' lawyers and key personnel continued to work with Plaintiff on the documentation for the Initial Closing Date, including notifications of the handover to Plaintiff's Colorado employees and to customers of the impending change. On March 12, 2020, Defendants even proposed accelerating the closing for the Arizona, North and South Carolina studios from July 1 to June 1, 2020 (11 studios). Through March 24, 2020, well after studios around the country began to comply with local temporary closure orders, Defendants' counsel continued preparing documents for the assumption and transfer of the assets and liabilities, including documenting the Assumed Liabilities, Transferred Contracts, Transferred Leases and Transferred Permits mandated by the Agreement.

36. On March 24, 2020, Defendants' counsel informed Plaintiff's counsel that they were suspending work on the closing process per instruction from their client. Defendants' transition teams were not advised of this decision, however, and were taken by surprise when they were advised on the afternoon of March 27, 2020, the Friday before the Initial Closing Date, that transition efforts were to stop.

37. In an email late on March 26, 2020, and a subsequent letter dated March 30, 2020, Defendants and their owners advised Plaintiff that Defendants deemed

Plaintiff to have failed to operate the studios in the ordinary course of business in violation of the following provisions of the Agreement:

- Section 3.6(a), which calls on Plaintiff, the Seller, to conduct the Business in the Ordinary Course of Business so that the Business does not experience a material loss;
- Section 3.6(e), which requires that the "Seller has not terminated or closed any facility, business or operation";
- Section 3.6(l), which requires that Seller conduct the Business in the Ordinary Course of Business so that the Business does not experience a Material Adverse Effect;
- and Section 5.1, which requires that the Seller conduct the Business "only in the Ordinary Course of Business"—detailing multiple components of the business that must be so conducted "consistent with past practice."

Other discussions confirmed Defendants' position. Defendants now wrongfully contend that their contractual performance has been "discharge[ed]" based on Plaintiff's purported "repudiate[ion of] multiple material obligations" in the Agreement. Letter from N. Leondakis to C. Kenny (Mar. 30, 2020), attached hereto as **Exhibit C**.

38. These contentions find no basis in the Agreement or in Plaintiff's operation of the businesses to be sold. Both Plaintiff and Defendants have closed their yoga studios around the country in compliance with temporary orders from state and local authorities to contain COVID-19. Since the pandemic arrived in the United States, that has become the "ordinary course of business."

39. The Agreement defines Ordinary Course of Business as "an action taken by any Person in the ordinary course of such Person's business which is consistent with the past customs and practices of such Person … which is taken in the ordinary course of the normal day-to-day operations of such Person." Ex. A, Agreement at Ex. A, Certain Defined Terms.

40. The Agreement specifically requires that at the time of closing, Plaintiff not be in violation of "any Legal Requirement . . . in connection with the conduct or operation of the Business and the ownership or use of the Acquired Assets." Ex. A, Agreement § 3.11.1.

41. Plaintiff has complied with all its obligations under the Agreement, including with the representations, warranties, and covenants that Plaintiff would continue operating the yoga studios in the Ordinary Course of Business. There has been no change in business operations that was unique to Plaintiff.

42. To the contrary, the COVID-19 pandemic and the government responses to it, which included certain governmental requirements to temporarily

close businesses, were general market conditions, the risk of which Defendants agreed to incur in the Agreement.

43. Plaintiff continued to operate its business as it had prior to execution of the Agreement, including by operating in compliance with all applicable government regulations and orders as required by Section 3.11.1. Defendants also have continued to operate their businesses as they had done prior to execution of the Agreement, including by operating in compliance with all applicable government regulations and orders.

44. Both Plaintiff and Defendants also have operated their own studios consistent with the obligations of the franchise agreements in the wake of the COVID-19 pandemic. The Plaintiffs have continued to abide by the local orders to close temporarily, which the franchise agreements require. Defendants—which also operate numerous studios throughout the United States—have taken similar, or the same, actions as have been necessitated for Plaintiff's business by the COVID-19 pandemic and government responses. This was not a change in either Plaintiff's or Defendants' operations—it is a general market issue which is, by its terms, temporary.

45. This all demonstrates that Plaintiff has operated and continues to operate its studios in the ordinary course of business consistent with Sections 3.6(a) and 5.1 of the Agreement, which requires businesses to abide by government and

public health directives regarding the COVID-19 pandemic. Indeed, were Plaintiff to seek permission from Defendants to comply with these directives as if they were outside the ordinary course of business, Defendants could hardly refuse or demand that the Plaintiff's studios remain open in the face of local directives, especially when Defendants' studios also have temporarily ceased operations to comply with similar orders in Defendants' locations.

46. Similarly, Plaintiff has not terminated or closed any of the studios in violation of Section 3.6(e). This provision plainly was not intended to cover temporary closures such as those that have been required by governmental authorities in response to the COVID-19 pandemic.

47. Nor has a material adverse effect occurred triggering Section 3.6(l). A covenant to conduct business in the ordinary course so that the business does not suffer a material adverse effect "is best read as a backstop protecting the acquiror from the occurrence of unknown events that substantially threaten the overall earnings potential of the target in a durationally-significant manner. A short-term hiccup in earnings should not suffice." *In re IBP, Inc. Shareholders Litig.*, 789 A.2d 14, 65-71 (Del. Ch. 2001) (finding no material adverse effect where contract defined material adverse effect as "any event, occurrence or development of a state of circumstances or facts which has had or reasonably could be expected to have a Material Adverse Effect" . . . "on the condition (financial or otherwise), business,

assets, liabilities or results of operations of [IBP] and [its] Subsidiaries taken as whole . . . .” and contract contained no specific exclusions for declines in the overall economy, relevant industry sector, or adverse weather or market conditions). Delaware courts have found that a buyer “faces a heavy burden when it attempts to invoke a material adverse effect clause in order to avoid its obligation to close.” *Hexion*, 965 A.2d at 738. This Court has observed the following when construing language quite similar to that in the parties’ Agreement here: “While frequently alleged, breaches of a MAE clause are rarely proven.” *Project Boat Holdings, LLC v. Bass Pro Grp., LLC*, No. CV 12606-VCS, 2019 WL 2295684, at *22 (Del. Ch. May 29, 2019), judgment entered, (Del. Ch. 2019).

48. Like any standard material adverse effect clause, the Agreement’s language is intended to allocate firm-specific or long-term risk to Plaintiff and to keep short-term or market and industry-wide risk, like the effects of a pandemic, on Defendants.

49. This provision does not contain a promise by Plaintiff that it will prevent any market, industry, or other broad circumstance from arising that could impact Plaintiff’s business, along with similarly impacting that of any number of other businesses. This was not a guarantee against a market downturn. The Agreement provides a mechanism for Defendants to make a post-closing indemnification claim if they are aggrieved; it does not allow Defendants to refuse

to close, to refuse to make payments due, or to refuse to execute the Assignment and Assumption Agreement even if Plaintiff's representations turn out not to be true.

50. Moreover, Plaintiff's operations have not been disproportionately impacted by the COVID-19 pandemic to any greater extent than other similarly situated yoga studios, as Defendants' decision to temporarily close their company-owned studios demonstrates.

51. In contrast to Defendants, Plaintiff has performed all of its obligations due under the Agreement, and there is no unfulfilled condition precedent for the closings to occur.

52. While Plaintiff insisted that the parties proceed with the Initial Closing Date, it has expressed, and continues to express, willingness to work with Defendants to accommodate such matters as are occasioned by the temporary disruptions of the pandemic provided that Defendants assure Plaintiff of their ultimate performance of the Agreement.

53. By refusing to close on April 1, 2020 or work with Plaintiff, Defendants breached the agreement.

C. Defendants' Breach of the Agreement Has Caused and Will Continue to Cause Harm to Plaintiff.

54. Defendants' refusal to fulfill its contractual obligations under the Agreement has caused, and will continue to cause, substantial damages to Plaintiff.

55. At significant cost, Plaintiff has had to revive business processes so as to prepare for Plaintiff's continued operation and management of the locations that are subject to the impending close.

56. At significant cost, Plaintiff has foregone other business opportunities, including but not limited to those opportunities intended with respect to the funds that would be transferred upon the closings.

57. Plaintiff has incurred costs to protect its interests under the Agreement.

58. All of the damages Plaintiff has incurred and will continue to incur are a result of Defendants' improper refusal to close as the Agreement requires.

FIRST CAUSE OF ACTION

Declaratory Judgment

59. Plaintiff incorporates by reference and realleges each and every allegation contained above, as though fully set forth herein.

60. Pursuant to 10 *Del. C.* § 6501, this Court has the power to grant declaratory judgments "to declare rights, status and other legal relations" that "shall have the force and effect of a final judgment or decree."

61. The Agreement is a valid and enforceable contract between Plaintiff and Defendants.

62. Plaintiff has performed all of its obligations under the Agreement regarding the sale of the studios.

63. Defendants have refused to perform in accordance with their obligations under the Agreement by failing to close on the Initial Closing Date and stating their intention not to close on any of the subsequent closing dates.

64. Therefore, Plaintiff is entitled to a declaration that the Agreement remains in full force and that Defendant is obligated to fulfill all of its obligations, including closing obligations, under the Agreement and the Assignment and Assumption Agreement for each of the studios.

SECOND CAUSE OF ACTION

Specific Performance

65. Plaintiff incorporates by reference and realleges each and every allegation contained above, as though fully set forth herein.

66. The Agreement obligated Defendants to close on the Tranche 1 Colorado studios on April 1, 2020, and obligates Defendants to close on the Tranche 2 Studios on July 1, 2020, the Development studios on July 1, 2020, and the Tranche 1 Illinois studios on October 1, 2020.

67. Defendants breached the Agreement by refusing to close on the Initial Closing Date.

68. Defendants will further breach the Agreement by failing to proceed with future closings.

69. In Section 8.11 of the Agreement, the parties expressly acknowledged and agreed "that the other parties would be damaged irreparably in the event any of the provisions of this Agreement are not performed in accordance with their specific terms or otherwise are breached or violated." Ex. A, Agreement § 8.11.

70. "Accordingly, each of the parties agree[d] that, without posting bond or other undertaking, the other parties will be entitled to an injunction or injunctions to prevent breaches or violations of the provisions of this Agreement and to enforce specifically this Agreement and the terms and provisions hereof in any Action." *Id.*

71. Plaintiff lacks an adequate remedy at law.

72. Pursuant to § 8.11, Plaintiff is entitled to a decree of specific performance requiring Defendants to proceed with the closings and to comply with their obligations under the Agreement.

73. Plaintiff seeks an order requiring such specific performance.

THIRD CAUSE OF ACTION

Breach of Contract

74. Plaintiff incorporates by reference and realleges each and every allegation contained above, as though fully set forth herein.

75. Section 2.2 of the Agreement sets forth the purchase price Defendants agreed to pay in exchange for Plaintiff's sale of thirty-four studios to Defendants over the six-month period between April 1, 2020 and October 1, 2020.

76. Plaintiff has performed all of its obligations due under the Agreement regarding the sale of the studios.

77. Defendants have refused to perform their obligations to close for certain studios and to pay Plaintiff the agreed-upon purchase price.

78. As a result of Defendants' breach of the Agreement, Plaintiff has incurred and will continue to incur significant damages. Those damages are exacerbated each day Defendants refuse to close, and will be even more significant in the event that the Court declines to award specific performance.

79. Accordingly, Plaintiff is entitled to and seeks damages in an amount to be proven at trial.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff respectfully requests that the Court enter judgment in favor of Plaintiff and against Defendants and issue an order as follows:

1) Granting all relief requested in this Complaint;

2) Declaring that the Agreement remains in full force and effect and Defendants are required to meet their obligations under the Agreement;

3) Ordering specific performance of Defendants' contractual obligations, including their closing obligations;

4) Enjoining Defendants from continuing to breach the terms of the Agreement;

5) Directing that Defendants account to Plaintiff for all damages suffered as a result of the Defendants' breach of the Agreement;

6) Awarding to Plaintiff the costs and disbursements of this action, including reasonable attorneys' fees; and

7) Granting such other and further equitable relief as this Court may deem just and proper.

/s/ Lisa A. Schmidt
Lisa A. Schmidt (#3019)
Matthew D. Perri (#6066)
Richards, Layton & Finger, P.A.
One Rodney Square
920 North King Street
Wilmington, Delaware 19801

Attorneys for Level 4 Yoga, LLC

OF COUNSEL:

Michael Dockterman
Cara Lawson
Steptoe & Johnson LLP
227 West Monroe Street, Suite 4700
Chicago, Illinois 60606

Dated: April 2, 2020