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## Obtaining Business Judgment Deference in a Controlling Stockholder Take-Private

Delaware Court of Chancery applies business judgment rule to controlling stockholder take-private and grants summary judgment in favor of defendants in the context of dual independent approvals by a special committee and minority stockholders

### Implications for our Clients

- After *In re MFW Shareholders Litigation*, controlling stockholders now potentially can obtain business judgment rule review of freeze-out merger transactions if:
  - the controller, at the outset, conditions the transaction on the approval of both a special committee and a majority of the minority stockholders;
  - the special committee is independent;
  - the special committee is empowered to freely select its own advisors and reject the controller's proposal;
  - the vote of the minority stockholders is fully-informed; and
  - there is no coercion of the minority stockholders.
- If business judgment rule review is available for these transactions, defendants are much more likely to prevail on dispositive motions, greatly reducing the damages risk and settlement value of stockholder litigation challenging freeze-outs.
- Special committees and controlling stockholders alike may continue to complete transactions under existing law on the basis of special committee or majority of minority approval alone, with a resulting burden shift.

### Summary

MacAndrews & Forbes (MacAndrews) owned 43 percent of M&F Worldwide (MFW). In June 2011, MacAndrews publicly offered to purchase the remaining MFW shares it did not already own for \$24 per share.

In its letter, MacAndrews indicated that the proposed transaction would be subject to the approval of a special committee of MFW's independent directors, and that it would not proceed with the transaction absent the special committee's approval. In addition to approval of the special committee, MacAndrews' letter made clear that any transaction would be subject to a non-waivable condition requiring approval of a majority of the MFW shares not owned by MacAndrews or its affiliates.

The MFW board created a special committee of independent directors, which hired independent legal and financial advisors. After negotiation with MacAndrews and deliberation with its advisors, the special committee approved the proposed transaction at \$25 per share, a 47 percent premium over the price at which MFW's stock closed before MacAndrews announced the proposed acquisition.

In a thoughtful decision founded in Delaware precedent, academic scholarship and studies of institutional investor and director voting behaviors, the Court of Chancery granted the defendants' motion for summary judgment, concluding that the combination of an independent special committee and a non-waivable majority of the minority vote provision should entitle defendants to the protections of the business judgment rule.

### Discussion

As we reviewed in our June 2010 M&A Commentary, [Practical Implications of CNX Gas on Controlling Shareholder Acquisitions](#), application of the business judgment rule in the circumstances found in the MacAndrews-MFW acquisition eliminates the dichotomy between controlling stockholder mergers and tender offers and provides another alternative by which to obtain business judgment rule review instead of the

significantly more exacting scrutiny implicated by entire fairness review.

The flexibility afforded by the opportunity to obtain business judgment rule review where dual independent approvals are obtained allows controllers to evaluate the particular circumstances of any proposed transaction, the relationship with the independent directors, and the expected outcome of a special committee process while also providing the controlling stockholder a significant benefit from using the special committee and majority-of-the-minority framework. Before *CNX Gas* and now *In re MFW*, controlling stockholder mergers would always be subject to entire fairness review, with a shift in the burden of persuasion as the only benefit a controller could hope to obtain. Under this new framework, however, the controller can obtain meaningful litigation benefits from ceding control of the transaction to the special committee and minority stockholders. At the same time, the decision appears to leave open the traditional burden-shifting approach under the entire fairness standard if a controller does not want to provide the protections necessary to obtain business judgment rule review.

*In re MFW* further clarifies the scope of authority required for a special committee to be effective. Specifically, the controller must agree beforehand not to proceed without the blessing of the special committee, and the special committee must have authority to negotiate (and not just evaluate) the proposal, including the ability to definitively reject the acquisition proposal. Importantly, the court does not go so far as to require that the special committee be given the full authority of the board of a non-controlled company, such as the ability to institute a rights plan or other defensive measures against the controller.

The decision is consistent with the recent and recurring theme in the Court of Chancery that an informed (and independent) stockholder decision as to a pending transaction is much preferred to judicial second guessing of the merits or value of a proposed strategic transaction, particularly where no alternative transaction is available to stockholders, whether due to the lack of competing bidders or the unwillingness of a controller to sell.

The decision also devoted substantial effort to addressing the absence of direct Delaware Supreme Court precedent on the specific facts presented, and anticipates Supreme Court review and definitive guidance on the question of whether entire fairness review may be avoided by using this dual independent approval approach. Further or contrary guidance on these matters may yet be forthcoming from that court.

**If you have any questions about this *M&A Client Alert*, please contact one of the authors listed below or the Latham attorney with whom you normally consult:**

[Mark Gerstein](#)

[Andrew Farthing](#)

[Bradley Faris](#)

[Blair Connelly](#)

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