

**DELAWARE COURT OF CHANCERY  
APPLIES THE BUSINESS JUDGMENT  
RULE TO A SQUEEZE OUT  
TRANSACTION**

In a much anticipated decision, *In re MFW Shareholders Litigation*, Chancellor Strine applied the business judgment rule to a going-private transaction with a controlling stockholder because the transaction was conditioned upfront on approval by both an independent committee and a majority-of-the-minority stockholder vote. Applying this standard, the Court granted summary judgment dismissing all claims against defendants. Download a copy of the Court's decision by clicking here.

**BACKGROUND**

Almost twenty years ago, in *Kahn v. Lynch Communications Systems, Inc.*, the Delaware Supreme Court held that a controlling stockholder squeeze out achieved through a negotiated merger agreement would be reviewed under the "entire fairness" standard regardless of whether the transaction was subject to approval of an independent committee of directors or of a majority of the minority stockholders. The use of either device, however, could shift the burden of proof to a stockholder challenging the transaction. The *Kahn v. Lynch* decision did not address whether the stringent entire fairness standard or deferential business judgment rule standard would apply if both procedural devices were used properly. Since the *Kahn v. Lynch* decision, several Court of Chancery opinions had suggested in *dicta* that use of both procedural protections might change the standard of review from entire fairness to business judgment.

**THE 6 CONDITIONS**

In *MFW*, the Court of Chancery, held that there were no material disputed facts as to whether: (i) the board committee that approved the squeeze-out merger with the controlling stockholder had been fully functioning and comprised of independent directors, and (ii) the vote of the holders of a majority of the outstanding shares held by unaffiliated

stockholders had been uncoerced and fully informed. In so holding, the Court announced that the business judgment rule will be applied in a controlling stockholder squeeze out if the following 6 conditions are met: "(i) the controller conditions the procession of the transaction on the approval of both a special committee and a majority of the minority stockholders; (ii) the special committee is independent; (iii) the special committee is empowered to freely select its own advisors and to say no definitively; (iv) the special committee meets its duty of care; (v) the vote of the minority is informed; and (vi) there is no coercion of the minority." The Court of Chancery observed, however, the ultimate authority regarding the applicable standard of review – the Delaware Supreme Court – has yet to weigh in.

**IMPLICATIONS**

*MFW* represents a significant development in the ongoing debate over the standard of review in controlling stockholder squeeze outs. The full contours of that debate, including issues regarding the necessary mandate of a special committee and whether the same standard of judicial review should apply in a squeeze out structured as a tender offer rather than a negotiated acquisition, continue to evolve as evidenced by *MFW*. Those involved in a squeeze out transaction should continue to assess carefully the mandate of any special committee appointed to address the transaction and the potential benefits and detriments of coupling committee approval with a majority-of-the-minority vote.

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Contact the following Morris Nichols attorneys for a more complete discussion of the implications of *In re MFW Shareholders Litigation*.

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