

Kahn v. M&F Worldwide Corp.: Delaware Supreme Court Sets Criteria for Applying Business Judgment Rule to Controlling Stockholder Going-Private Transactions

On March 14, 2014, in *Kahn v. M&F Worldwide Corp.*, the Delaware Supreme Court held that the deferential business judgment standard of review should apply to a going-private merger between a controlling stockholder and its corporate subsidiary where the transaction is conditioned upon approval from both an independent special committee and an informed, uncoerced vote of a majority of the minority stockholders. *Kahn* presented a question of first impression for the Delaware Supreme Court and gave the court an opportunity to articulate clear guidelines for how a controlling stockholder that takes a company private can avoid a rigorous entire fairness review.¹

I. Background and Procedural History

The dispute arose from a 2011 acquisition by MacAndrews & Forbes Holdings, Inc. (“MacAndrews”), the controlling stockholder holding 43% of M&F Worldwide Corp. (“MFW”) voting shares. In June 2011, MacAndrews offered to take MFW private. MacAndrews’ offer contained two notable conditions: (1) negotiation and approval by a special committee of independent MFW directors and (2) approval of the acquisition by a majority of the minority stockholders who were unaffiliated with MacAndrews. The offer also stated that MacAndrews was not interested in selling its stock to a third party.

Presented with MacAndrews’ proposal, the MFW board formed a special committee of independent directors who then hired its own counsel and financial advisors. The special committee was empowered to negotiate with MacAndrews the terms of the proposed merger and, if it did not view the transaction as fair or in the best interests of the company, to reject the offer. In December 2011, the going-private transaction closed after being approved by a 65.4% vote of MFW’s minority stockholders.

Plaintiffs initially sought to enjoin the transaction but withdrew their request for injunctive relief after taking expedited discovery. After the transaction closed, Plaintiffs sought relief against, among others, MacAndrews and MFW’s directors, including members of the special committee, for breach of fiduciary duty. Following extensive discovery, Defendants moved for summary judgment, which the Court of Chancery granted.

The Court of Chancery held—and the Delaware Supreme Court affirmed on appeal—that the deferential business judgment standard, rather than the more rigorous entire fairness standard, should apply “if, *but only if*:

- (i) the controll[ing stockholder] conditions the transaction on 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 acts with care;
- (v) the minority vote is informed; and
- (vi) there is no coercion of the minority.”²

¹ *Kahn v. M&F Worldwide Corp.*, No. 334, 2013, slip op. (Del. Mar. 14, 2014) [hereinafter “Slip Op.”], available at <http://courts.delaware.gov/opinions/download.aspx?ID=202790>.

² *In Re MFW Stockholders Litigation*, 67 A.3d 496 (Del. Ch. 2013), available at <http://courts.delaware.gov/opinions/download.aspx?ID=189940> (emphasis by the Court of Chancery); see also Slip. Op. at 18.

The Court of Chancery concluded that these factors were met and that Plaintiffs had failed to raise any genuine issue of material fact to the contrary. After reviewing the merger under the business judgment standard, the Court of Chancery granted Defendants' motion for summary judgment.

II. The Court's Decision

The Delaware Supreme Court adopted the fact findings of the Court of Chancery and rejected the Plaintiffs' arguments that members of the special committee were not sufficiently independent and did not exercise due care in evaluating the MacAndrews offer. The Delaware Supreme Court noted that the case presented a question of first impression: "what should be the standard of review for a merger between a controlling stockholder and its subsidiary, where the merger is conditioned *ab initio* upon the approval of **both** an independent, adequately-empowered Special Committee that fulfills its duty of care, and the uncoerced, informed vote of a majority of the minority stockholders [?]"³ The court distinguished the facts of this case from a line of cases, such as *Kahn v. Lynch Communication Systems, Inc.*⁴ and its progeny, where the controlling stockholder in each case did not forfeit its voting power by agreeing to a non-waivable majority of the minority condition. That is, *Lynch* and its progeny did not involve mergers conditioned on *both* procedural protections that were set forth by the controlling stockholder in this case.

Ultimately, the Delaware Supreme Court held that the business judgment standard of review should apply in "mergers between a controlling stockholder and its corporate subsidiary, where the merger is conditioned *ab initio* upon both the approval of an independent, adequately-empowered Special Committee that fulfills its duty of care; and the uncoerced, informed vote of a majority of the minority stockholders."⁵ In summarizing its holding, the court adopted verbatim the six-factor test articulated by the Court of Chancery and quoted above.

The Delaware Supreme Court found that the business judgment standard of review should apply in this case because the prerequisite circumstances were satisfied here. First, the court noted that MacAndrews conditioned its offer upon dual procedural protections, i.e., approval by a special committee and a majority of the minority stockholders. Next, the court concluded that Defendants "successfully established a record of independent committee effectiveness and process that warranted a grant of summary judgment . . ."⁶ Finally, the court determined that the majority of the minority vote was fully informed and not coerced.

III. Significance

Kahn v. M&F Worldwide sets forth clear guidelines for arranging transactions involving controlling stockholders that can reduce the likelihood of costly and time-consuming stockholder lawsuits that often accompany the announcements of mergers.

³ Slip Op. at 11-12 (emphasis by the Delaware Supreme Court).

⁴ *Kahn v. Lynch Comc'n. Sys., Inc.* 638 A.2d 1110 (Del. 1994).

⁵ Slip Op. at 15.

⁶ *Id.* at 21.

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Jon Mark at 212.701.3100 or jmark@cahill.com; John Schuster at 212.701.3323 or jschuster@cahill.com; or Maryana Lyakhovetsky at 212.701.3684 or mlyakhovetsky@cahill.com.

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