Delaware Supreme Court Clarifies Standard of Review for Conflicted Stockholder Transactions with In re Match Group Opinion

April 8, 2024

On April 4, 2024, the Delaware Supreme Court issued its opinion in *In re Match Group, Inc. Derivative Litigation*, clarifying that the heightened entire fairness standard of review applies to judicial review of any transaction (not only freeze-out mergers) in which a controlling stockholder stands on both sides of the transaction and receives a non-ratable benefit. To shift the standard of review from the onerous entire fairness to deferential business judgement, a corporation must employ both an independent special committee and an uncoerced, fully informed, unaffiliated stockholder vote, and thus fully follow the so-called *MFW* framework outlined by the Supreme Court in 2014 in *Kahn v. M & F Worldwide Corp.*[1] Doing so, the Court stated, is necessary for a controlling stockholder to show that it has "irrevocably and publicly disable [d] itself from using its control to dictate the outcome of the negotiations and the shareholder vote"[2] in order to restore the business judgment rule's protections pre-trial. Employing either one of the protections, however, is still a valuable tool to shift the burden of proving that a conflicted transaction was entirely fair from the defendant to the plaintiff, although the standard of review will remain entire fairness.

In 2020, IAC/InterActiveCorp, the controlling stockholder of Match Group, Inc., undertook a reverse spin-off transaction that left the new parent cash-rich and with little to no debt and the new Match Group, Inc. highly leveraged and subject to restrictive short-term governance provisions. Although the separation was conditioned from the start upon both the recommendation of a Match Group, Inc. special committee and the approval of the unaffiliated stockholders, former Match Group, Inc. unaffiliated stockholders challenged the separation. Their claims amounted to allegations of unfair price—that IAC/InterActiveCorp received significant non-ratable benefits in the separation, to the detriment of the unaffiliated stockholders—and unfair process—that the special committee was conflicted and that the proxy disclosures misled the unaffiliated stockholders by not sufficiently disclosing the ties of one of the three special committee members to the controlling stockholder.

The Court of Chancery held that defendants satisfied *MFW*'s requirements and consequently, that the protections of the business judgment rule applied. After applying the deferential business judgment standard of review, the Court of Chancery dismissed the complaint. According to the Court of Chancery, the plaintiffs

failed to plead that either a majority of the members of the special committee were not disinterested and independent or that a minority of the members somehow infected or dominated the decision-making process. Further, the Court of Chancery found that there was sufficient disclosure of the interested special committee member's ties to the controlling stockholder because the proxy incorporated Match Group, Inc.'s prior-year Form 10-K, which disclosed the ties.

The Supreme Court disagreed with the Court of Chancery's conclusion that only a majority of the special committee must be independent. In situations where a special committee is formed to secure the protections of business judgment review, the Court explained, replicating arm's length bargaining by removing the influence of the controlling stockholder requires that every director on the committee be independent. Consequently, the Court found that the Match Group, Inc. plaintiffs sufficiently pleaded that the special committee in the separation was not independent and reversed the Court of Chancery's decision to apply the business judgment rule and dismiss the complaint.

The Court additionally addressed and disagreed with defendants' argument on appeal that *MFW* and its predecessors should be limited to only freeze-out mergers involving controlling stockholders. Outside that context, defendants argued, any one of three cleansing mechanisms—approval by either a majority independent board or a special committee of independent directors or a majority of unaffiliated stockholders—is sufficient to invoke the business judgment standard of review in a conflicted transaction. The Court noted that it could not perceive any legal basis for treating review of the inherent coercion present in conflicted transactions differently in the freeze-out merger context. Examining precedent, the Court found that even outside the freeze-out merger context, where an independent committee negotiated the transaction and thus only one *MFW* mechanism was used, entire fairness was the standard of review. The use of an independent committee alone, it reiterated, may still serve to shift the burden of proving entire fairness from the defendant to the plaintiff.

Key Takeaways

- Transactions involving a controlling stockholder that stands on both side of the transaction and receives a non-ratable benefit will be reviewed under the heightened standard of entire fairness.
- To receive the protections of the business judgment rule in a conflicted transaction, a corporation must employ both an independent special committee and an uncoerced, fully informed, unaffiliated stockholder vote.
- Use of only one mechanism is still a valuable tool to shift the burden of proving entire fairness from the controlling stockholder to the plaintiff.
- Best practice is to form a special committee in a conflicted transaction even if the corporation is not seeking to shift the standard of review.

- Seek counsel early in the process if considering a potentially conflicted transaction, since the Court has said that, for *MFW* protections to apply, a controlling stockholder must condition a transaction on an independent special committee and an uncoerced, fully informed, unaffiliated stockholder vote before economic negotiations begin.

If you need help evaluating a potentially conflicted transaction and procedural safeguards, reach out to Jane Trueper or any member of the Lathrop GPM's Corporate & Business Law Team.

[1] 88 A.3d 635.

[2] *In re Match Group, Inc. Derivative Litigation*, *supra* note 1, at 37-38 (internal quotations and citations omitted).