

Delaware Chancery Court: *MFW*'s Procedural Safeguards Were Not Satisfied Where a Majority of the Special Committee Members Allegedly Had a Material Self-Interest in the Transaction

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On February 26, 2020, the Delaware Chancery Court held that the business judgment standard of review did not apply to a controlling stockholder transaction that was conditioned on *MFW*'s procedural safeguards because plaintiffs alleged that "three of the four members of the special committee had a material self-interest in the transaction."^[1] *In re AmTrust Fin. Servs. Stockholder Litig.*, 2020 WL 914563 (Del. Ch. 2020) (Bouchard, C.). The court found that *MFW*'s requirement of special committee independence "was intended to ensure not only that members of a special committee must be *independent* in the sense of not being beholden to a controlling stockholder, but also that the committee members must have no disabling personal *interest* in the transaction at issue."

The court explained that "directors are interested in a transaction if they expect to derive any personal financial benefit from the transaction as opposed to a benefit which devolves upon the corporation or all stockholders generally." Moreover, "[i]n the absence of self-dealing, for the interest of a director to be disabling, the benefit must be alleged to be *material* to that director."

In the case before it, plaintiffs alleged that the transaction "was expected to extinguish viable derivative claims exposing [three of the four members of the special committee] to significant personal liability." Plaintiffs argued that the court should follow the analysis in *In re Riverstone Shareholder Litig.*, 2016 WL 4045411 (Del. Ch. July 28, 2016), which involved a similar situation. The *Riverstone* court found that "the [d]irector [d]efendants [allegedly] obtained a special benefit for themselves" "by orchestrating a merger that extinguished a possible derivative action." The court found it significant plaintiffs had alleged that (1) the directors were aware of the derivative claim, (2) the claim was viable, and (3) the potential liability was material to each of the directors.

The *AmTrust* court found "*Riverstone* sets forth an appropriate framework" for evaluating plaintiffs' contention that a majority of the special committee members had a material self-interest in the transaction. The court noted that defendants did not dispute that (1) these special committee members were aware of a potential derivative claim, (2) the claim was viable, and (3) "the potential liability they faced was material to each of them personally," as the estimated net settlement value was between \$15 million and \$25 million. Moreover, the court found plaintiffs adequately alleged that the transaction had the practical effect of extinguishing the committee members' liability. The court

therefore “conclude[d] that [p]laintiffs have pled a reasonably conceivable set of facts showing that each of the conditions necessary to apply the *MFW* framework to subject the [t]ransaction to business judgment review have not been satisfied.”

[1] In *Kahn v. M&F Worldwide Corp.*, 88 A.3d 635 (Del. 2014) (*MFW*), the Delaware Supreme Court held that the business judgment standard of review applies to a controlling stockholder transaction if the transaction “is conditioned *ab initio* upon the approval of both an independent, adequately-empowered [s]pecial [c]ommittee that fulfills its duty of care, and the uncoerced, informed vote of a majority of the minority stockholders.” Please [click here](#) to read our discussion of the *MFW* decision.

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