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CONTROL AND ITS DISCONTENTS

JILL E. FISCH & STEVEN DAVIDOFF SOLOMON†

A series of recent Delaware decisions highlights the Delaware courts' growing skepticism toward corporate actions in controlled companies. We analyze these

† Jill E. Fisch is the Saul A. Fox Distinguished Professor of Business Law at the University of Pennsylvania Carey Law School and a Fellow of the European Corporate Governance Institute; Steven Davidoff Solomon is the Alexander F. and May T. Morrison Professor of Law at the University of California, Berkeley School of Law and a Research Member of the European Corporate Governance Institute. We thank Leo E. Strine, Jr., Travis Laster, Steve Bainbridge, David J. Berger, Itai Fiegenbaum, Frank Gevurtz, Richard Horvath, Kobi Kastiel, Bill Lafferty, Ted Mirvis, Elizabeth Pollman, and participants at the Conference on Corporate Law 2024 at the University of Athens Faculty of Law, the Drexel University Thomas R. Kline School of Law Faculty Workshop, the 2024 UCLA Corporate and Securities Litigation Workshop, and the Hebrew University, Jerusalem School of Law Herzog Conference for helpful comments. We also thank Erika Doane for outstanding research assistance.

decisions, noting their application to what we term "new" control situations and the per se application of fiduciary duties and entire fairness to controllers. We contend that this application contradicts both the theoretical and economic justifications for limiting the fiduciary duties of controllers, particularly when they undertake actions in their capacity as shareholders. We argue that, outside the context of freeze-outs and similar transactions, strict scrutiny is both economically unnecessary and impractical. We further argue that controlling shareholders acting in their capacity as shareholders should not be considered fiduciaries. Instead, we propose that Delaware defer to existing market forces and structural safeguards. To address the risk of board domination, we propose that where a controller has plausibly distorted the board process, the decision be subject to intermediate scrutiny. To further strengthen the incentives of directors to resist such domination, we propose a greater focus on the actions of dominated directors who favor the interests of a controller over those of the corporation.

INTRODUCTION

In *Tornetta v. Musk*, the Delaware Chancery Court invalidated a $55.8 billion pay package granted to Elon Musk by the Tesla board and approved by the Tesla shareholders.[1] The landmark decision rested upon a fundamental principle: "Musk controlled Tesla."[2] Musk's pay package was therefore subject to scrutiny under the "entire fairness" doctrine.[3] Having determined the appropriate standard of review, the court held that the package failed under such scrutiny, and that Tesla's attempts to implement procedural protections for the compensation decision were insufficient—the board approval and shareholder vote were defective.[4] The flaws were fatal, and the court rescinded the entire $55.8 billion pay plan.[5]

Musk, the court determined, was a controlling shareholder despite the fact that he owned only 21.9% of Tesla's voting stock.[6] In so holding, the court recognized the novelty of its ruling, stating that it had determined "to 'boldly go where no man has gone before,' or at least where no Delaware court has tread."[7] The court's conclusion was based on the finding that Musk's stock ownership, coupled with his influence on the board itself and with respect to the pay package, sufficed to constitute control.[8]

Tornetta should be understood in the context of two other equally world-changing decisions. A few months before *Tornetta*, in *In re Sears Hometown & Outlet Stores, Inc. Stockholder Litigation*,[9] the Delaware Chancery Court appeared to extend the context in which a controlling shareholder is subject to fiduciary duties to actions taken through the exercise of shareholder voting rights. Then, just a few months after *Tornetta*, in *In re Match Group, Inc. Derivative Litigation*, the Delaware Supreme Court held that the entire fairness standard of review applied to all corporate decisions in which a controlling shareholder stood "on both sides of a transaction with the controlled corporation and received a non-ratable benefit."[10] To substitute business judgment rule deference for this heightened scrutiny, a controlling shareholder must adhere to the special cleansing procedure previously recognized in the *MFW* case.[11] The *MFW* procedure, which was initially

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1 310 A.3d 430, 445, 544 (Del. Ch. 2024).

2 *Id.* at 446.

3 *Id.* at 497.

4 *Id.* at 526-44.

5 *Id.* at 547 ("Plaintiff has demonstrated that rescission is reasonable, appropriate, and practicable.").

6 *Id.* at 502.

7 *Id.* at 446 (citing *Star Trek: The Original Series* (Paramount Pictures 1968)).

8 *Id.* at 502 ("This unique suite of allegations makes it undeniable that, with respect to the Grant, Musk controlled Tesla."). In a subsequent decision, the court found that Tesla's shareholder ratification of the pay package in 2024 did not suffice to correct its deficiencies. *See* Tornetta v. Musk, C.A. No. 2018-0408-KSJM, 2024 WL 4930635, at *1 (Del. Ch. Dec. 2, 2024). The Court also awarded the plaintiffs' counsel $345 million in attorneys' fees. *Id.*

9 309 A.3d 474 (Del. Ch. 2024).

10 315 A.3d 446, 451 (Del. 2024).

11 Kahn v. M&F Worldwide Corp. (MFW), 88 A.3d 635 (Del. 2014).

applied in the freeze-out context and, at least historically, was rarely utilized, includes "approval by a well-functioning independent committee and the affirmative vote of the fully informed and uncoerced minority stockholders."[12] The *Match* court added that, for a board committee to meet the *MFW* standard, all members of the committee (rather than simply a majority) must be independent of the controlling shareholder.[13]

Together, the *Tornetta*, *Sears Hometown*, and *Match* decisions highlight Delaware courts' growing skepticism toward corporate actions in controlled companies. This skepticism has potentially wide-ranging implications. Language in the decisions suggests the possibility that, going forward, courts will apply entire fairness to a wide range of transactions and to an arguably increasingly expansive set of shareholders. At the same time, the fact-specific analysis in the decisions suggests that the *MFW* procedures, although required in more cases to avoid entire fairness review, may be less readily available to accomplish that objective. In combination, these decisions and several others reflect an evolving approach to the role and responsibilities of controlling shareholders.

We trace the development of this approach from the traditional analysis of controlling shareholder duties which was, as we explain, focused primarily on majority shareholder freeze-outs and similar transactions.[14] Our concern

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12 *Match*, 315 A.3d at 462. The *MFW* court further explained that these procedural protections must be in place "*ab initio*." *MFW*, 88 A.3d at 646; *see also* Flood v. Synutra Int'l, Inc., 195 A.3d 754, 761-63 (Del. 2018) (discussing the *ab initio* requirement).

13 *Match*, 315 A.3d at 452.

14 For purposes of this Article, "similar transactions" include freeze-outs accomplished through either a tender offer or a merger. They also include transactions in which a controlling shareholder sells a substantial asset to the corporation, purchases a substantial asset from the corporation, or engages in a merger between the corporation and another entity under its control. *See, e.g.*, *In re* Tesla Motors S'holder Litig. (SolarCity), 298 A.3d 667, 705-06 (Del. 2023) (treating Tesla's acquisition of SolarCity as a conflicted transaction and applying entire fairness standard). In such cases, as in a freeze-out, the controlling shareholder is on both sides of the transaction. In the *Tremont* line of cases, for example, the plaintiff challenged as self-dealing a stock purchase from a company controlled by the same controllers as the purchasing company. *See* Kahn v. Tremont Corp. (Tremont II), 694 A.2d 422, 428 (Del. 1997); Kahn v. Tremont Corp. (Tremont I), C.A. No. 12339, 1996 WL 145452 (Del. Ch. Mar. 21, 1996), *rev'd on other grounds*, *Tremont II*, 694 A.2d at 424 (applying entire fairness, despite approval by a special committee of independent directors). The Delaware Supreme Court in *Tremont II* held that entire fairness was applicable because, as in a freeze-out, the controlling shareholder was on both sides of the transaction. *Tremont II*, 694 A.2d at 428. We further note that, as a law professor's amicus brief in *Match* observed, controllers can structure transactions in a variety of ways to evade a limit that focuses narrowly on freeze-out transactions. *See* Amicus Curiae Brief of Academics in Support of Appellants at 10-11, *In re* Match Grp., Inc., Derivative Litig., 315 A.3d 446 (Del. 2024) (C.A. No. 2020-0505-MTZ), ID No. 70770232 (providing examples of potential transaction structures). Accordingly, when we use the term "freeze-out" in this article, we intend it to encompass transactions in which the controller is on both sides—a usage that includes technical freeze-outs and other transactions that are economically equivalent. *See id.*

is not whether this evolution is faithful to, or a natural extension of, the language of the earlier decisions but whether the current approach to control is theoretically defensible or pragmatically appropriate.

Our theoretical critique is grounded in the fundamental principle that shareholders do not, and we argue should not, owe fiduciary duties to the corporation and their fellow shareholders when they act in their traditional capacity as shareholders.[15] We situate this principle in the historical underpinnings of controlling shareholder fiduciary duty articulated over seventy-five years ago in the Delaware Supreme Court's *Ringling Bros.* decision.[16] The rationale for this principle is that individual shareholder action is not taken in a fiduciary capacity on behalf of the corporation. Actions taken by shareholders as shareholders are also limited by the existing structural mechanisms of corporate governance; the actions of the board of directors and the unaffiliated shareholders play a critical role in converting "shareholder action" into "corporate action." These governance mechanisms have been shown to work imperfectly in cases involving majority shareholder freeze-outs, warranting the additional oversight of entire fairness. But the rationale for heightened review of controlling shareholder actions beyond that context has been under-theorized.

Two components of the Delaware courts' recent jurisprudence warrant particular analysis. The first is the expanded and increasingly flexible definition of what it means to be a controlling shareholder. As the *Tornetta* court acknowledged, its treatment of Musk as a controlling shareholder was novel.[17] The parameters by which the court reached its conclusion, however, logically extend to a host of other situations involving shareholders with far less than fifty percent voting power who exercise control through soft measures, such as serving as a superstar CEO or exercising outsize influence on a particular transaction. We term these situations "new" control. Corporations are willing to confer control rights and shareholders are capable of exerting substantial influence on corporate decisions in a growing number

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15 Shareholders have the power to vote, to sue, and to sell their shares. This power encompasses individual actions rather than actions on behalf of the corporation. *See, e.g.*, Randall S. Thomas & Patrick C. Tricker, *Shareholder Voting in Proxy Contests for Corporate Control, Uncontested Director Elections and Management Proposals: A Review of the Empirical Literature*, 70 OKLA. L. REV. 9, 11 (2017) ("[T]hey can sell their shares, vote them where allowed, or sue the company and its management to enforce its officers and directors' fiduciary duties.").

16 *See* Ringling Bros.-Barnum & Bailey Combined Shows, Inc. v. Ringling, 53 A.2d 441, 447 (Del. 1947) ("Generally speaking, a shareholder may exercise wide liberality of judgment in the matter of voting, and it is not objectionable that his motives may be for personal profit, or determined by whims or caprice, so long as he violates no duty owed his fellow shareholders.").

17 Tornetta v. Musk, 310 A.3d 430, 446 (Del. Ch. 2024) ("This decision dares to 'boldly go where no man has gone before,' or at least where no Delaware court has tread." (citing *Star Trek: The Original Series* (Paramount Pictures 1968)).

of situations that do not involve ownership of a majority economic interest. As a result, cases involving new control will arise with increasingly frequency.[18]

The capaciousness of controlling shareholder status is significant because that status triggers the imposition of fiduciary duties and the potential application of entire fairness scrutiny. As a result, our second concern is that heightened scrutiny will be applied to an increasing range of decisions. Examples include the *Sears Hometown* decision's application of fiduciary principles (although not entire fairness) to a shareholder acting in his capacity as a shareholder and the *Match* court's conclusion that entire fairness analysis applies to any transaction in which a controlling shareholder receives a non-ratable benefit. Together with the broad definition of control, these decisions support significant judicial oversight of controlling shareholder transactions. We challenge this approach and its assumption that all controller transactions are inherently and equally coercive[19] as being in tension with the fundamental structure of corporate law, which places legal authority for corporate action in the corporation's officers and directors and relies on entire fairness as a way of disciplining the use of fiduciary authority. The expansive application of entire fairness works particular mischief in cases involving the capacity of a shareholder to exert influence on corporate transactions, to avail itself of statutory governance rights, or to block decisions that it opposes.[20] Given the market's seeming acceptance of the view that control mechanisms can provide value, the courts' current approach is problematic in that it increases the cost and uncertainty associated with the exercise of those mechanisms.[21] Absent a

18 *See, e.g.*, Ric Marshall & Jonathan Ponder, *Ownership and Control 2022, Global Equities Concentration on the Rise*, MSCI 3, 5 (July 11, 2022), https://www.icgn.org/sites/default/files/2022-11/Ownership%20and%20Control%202022_%20Global%20Equities%20Concentration%20on%20the%20Rise.pdf [https:// perma.cc/ZB4M-X7JS] (documenting increased ownership concentration in global equity markets, including a substantial increase in the number of controlled companies).

19 Although that characterization may be factually accurate, it fails to recognize that the degree and nature of such control varies. Moreover, we urge caution in articulating potentially broad-based fiduciary principles on the basis of actions taken by individual and potentially distinctive corporate personalities.

20 For a recent, perceptive piece also analyzing this issue, see Stephen M. Bainbridge, *A Course Correction for Controlling Shareholder Transactions* (UCLA Sch. L., L. & Econ. Rsch. Paper No. 24-07, 2024), https://ssrn.com/abstract=5022685.

21 We note that the presence of controlling shareholders in U.S. companies is more prevalent than commonly supposed. *See, e.g.*, Clifford G. Holderness, *The Myth of Diffuse Ownership in the United States*, 22 REV. FIN. STUD. 1377, 1378 (2009) (presenting statistics on the widespread existence of large blockholders at U.S. public firms). The number of controlling shareholders increases still more if we extend the definition to include shareholders who exercise control by contract as opposed to solely through economic ownership or formal voting rights. *See, e.g.*, Gladriel Shobe & Jarrod Shobe, *The Dual-Class Spectrum*, 39 YALE J. REG. 1343, 1345-46 (2022) (explaining that shareholder agreements can serve as a substitute for dual class voting structures).

clear indication that the traditional approach to control is deficient, we question the justification for change.

Our analysis suggests three implications. First, we highlight the inherent subjectivity in the concept of "new" control and the line-drawing problems that it creates. We agree that shareholders can exercise power through a variety of mechanisms, but we question whether the exercise of that power invariably does or should serve as a trigger for treating that shareholder as a fiduciary and applying entire fairness. Our analysis questions the assumption that the exercise of shareholder power, particularly in "new" control situations, is inherently coercive, illegitimate, or corrupting—an assumption upon which the current approach appears to be premised. This assumption is of particular concern because the structure of the corporate form, including the statutory authority of the board, limits the ability of a shareholder to exercise corporate power.[22] We further observe that the true impact of shareholder power depends on a variety of factors, including the extent of a shareholder's voting rights, the structural features of the corporation, the characteristics of the corporation's officers and directors, the overall composition of the shareholder base, and the disciplinary effect of the markets in which the corporation operates.

Second, the line-drawing challenges associated with "new" control as exacerbated by the evolving approach to *MFW* have rendered the potential for procedural cleansing uncertain. We explain why the courts' demanding standard for procedural fairness is in tension with the practicalities of controlled companies. The difficulty in assuring ex ante that a process will be sufficiently rigorous to meet the *MFW* standard undercuts the claim that the impact of control creep is limited. Rather, we predict that a growing number of corporate decisions will be subject not just to litigation challenges, but to merits-based scrutiny under an entire fairness standard.

Third, we consider the pragmatic challenges that stem from the courts' analysis. Doctrines like the business judgment rule are premised on the principle that courts are poorly situated to evaluate the merits of corporate decisions.[23] As a result, entire fairness scrutiny has traditionally focused on conflict transactions involving traditional corporate fiduciaries—officers and directors. Courts have been more restrained in applying entire fairness to

22 These principles are limited by the legislature's adoption of Delaware General Corporate Law (DGCL) § 122(18), which permits shareholder agreements that authorize shareholders to exercise traditional board powers. DEL. CODE ANN. tit. 8, § 122(18) (2024). We address this issue in Part III, *infra*.

23 *In re* Citigroup Inc. S'holder Derivative Litig., 964 A.2d 106, 124 (Del. Ch. 2009) ("[T]he business judgment rule prevents a judge or jury from second guessing director decisions if they were the product of a rational process and the directors availed themselves of all material and reasonably available information.").

actions involving controlling shareholders, focusing primarily on old control situations and corporate freeze-outs—transactional contexts in which there is a material, quantifiable, and disproportionate benefit to the controller and a market-based framework for analyzing the fairness of the transaction. The extension of entire fairness review to all decisions in which a controlling shareholder receives a non-ratable benefit undermines that principle. Evaluating fair process in situations in which a substantial shareholder exerts some degree of board influence and evaluating fair price outside the transactional context (such as in decisions regarding reincorporation, amendment of the charter, or the setting of CEO pay) potentially bring the courts into treacherous territory.

We therefore call for a reconsideration of the application of fiduciary principles to controlling shareholders. Specifically, we argue that when a shareholder acts in its capacity as a traditional shareholder—even a shareholder with effective voting control—it should be treated as a fiduciary only in freeze-outs and similar transactions in which the controller obtains an economic benefit directly at the expense of the minority shareholders or in instances of outright fraud.[24] We similarly challenge the application of shareholder-level fiduciary principles in cases of "new" control. While we recognize that a shareholder may use soft power[25] to usurp the role of an officer or director, we argue that liability in such cases stems from, and should be limited to, actions taken in the capacity of a traditional fiduciary.[26] Our more nuanced approach relieves the courts of the difficult task of analyzing entire fairness in situations that are highly fact-specific and subject to longstanding structural and market constraints.[27]

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24 *See supra* note 14 (discussing what transactions constitute "similar transactions").

25 As the courts have explained, soft power encompasses control mechanisms beyond voting authority. *See, e.g.*, *In re* Pattern Energy Grp. Inc. S'holders Litig., C.A. No. 2020-0357-MTZ, 2021 WL 1812674, at *38 (Del. Ch. May 6, 2021) ("It is an open question under Delaware law whether the [non-stockholder] Entity Defendants' soft power alone, anchored in historical and commercial ties and the contractual Consent Right, can support including the Entity Defendants in a control group and imposing fiduciary duties.").

26 A controlling shareholder may hold a position as a director or officer and therefore act in that capacity. A shareholder may also exercise the functions of a traditional fiduciary pursuant to a shareholder agreement. *See generally* Gabriel Rauterberg, *The Separation of Voting and Control: The Role of Contract in Corporate Governance*, 38 YALE J. REG. 1124, 1140 (2021) (exploring the allocation of control rights through shareholder agreements).

27 As our discussion below explains, although cases evaluating the duties of controlling shareholders involve both public and private companies, our analysis focuses primarily on the public company context for two reasons. First, public companies are subject to the transparency requirements and price discipline of the capital markets, including the likelihood that minority shares trade at a discount that reflects controlled company status. *See, e.g.*, Dieckman v. Regency GP LP, 155 A.3d 358, 366-67 (Del. 2017) (observing that, in the publicly traded partnership context, even when fiduciary duties are waived, investors receive some protection from public disclosures about the entity). Second, both the control relationships and contractual efforts to navigate those

A potential concern with our reliance on existing structural mechanisms is the prospect that a controlling shareholder will dominate traditional fiduciaries—a concern that, as the court recognized in *Tornetta*, may be present in a variety of "new" control contexts. Whether a shareholder possesses soft or hard control, that control, or merely the threat of its use, can corrupt the procedural safeguards of the corporate form. That corruption, we argue, is better addressed not by creating new fiduciaries, but by imposing greater accountability on traditional corporate fiduciaries. We therefore argue that, in the controlling shareholder context, such accountability should be imposed on officers and directors rather than on shareholders.

We offer three suggestions for addressing accountability in controlled companies. First, where a plaintiff sufficiently alleges both that a controlling shareholder has dominated a board decision and that the decision results in a quantifiable benefit to the controller to the detriment of the minority shareholders, but the transaction is not akin to a freeze-out, we propose that the board's decision be subject to the one-step cleansing applicable to director- and officer-conflicted transactions,[28] rather than requiring the court to choose between business judgment rule deference and the *MFW* approach.[29] Second, where the decision has not been properly cleansed, we argue for the application of the *Coster* intermediate scrutiny standard.[30] *Coster* enables the court to examine the reasonableness of the decision as a

relationships in the private company context are often bespoke and less likely to be analyzed in the context of litigation. *See generally* Jill E. Fisch, *Stealth Governance: Shareholder Agreements and Private Ordering*, 99 WASH. UNIV. L. REV. 913, 946-48 (2022) (describing opacity and information costs in private companies). As a result, the potential application of our analysis to private companies is beyond the scope of this Article.

28 *See, e.g.*, *In re* KKR Fin. Holdings S'holder Litig., 101 A.3d 980, 1001 (Del. Ch. 2014), *aff'd*, 125 A.3d 304 (Del. 2015) ("[T]he legal effect of a fully-informed stockholder vote of a transaction with a non-controlling stockholder is that the business judgment rule applies and insulates the transaction from all attacks other than on the grounds of waste, even if a majority of the board approving the transaction was not disinterested or independent.").

29 We are not the first to advocate a single-step cleansing mechanism in controlled transactions. *See, e.g.*, William T. Allen, Jack B. Jacobs & Leo E. Strine, Jr., *Function over Form: A Reassessment of Standards of Review in Delaware Corporation Law*, 26 DEL. J. CORP. L. 859, 882 (2001) ("The better policy, we think, is to afford business judgment review treatment to self-interested mergers that are approved by either an effective independent director committee or by a majority of the minority stockholder vote."). Because controlling shareholder freeze-outs present distinctive concerns, we—unlike these three Chancellors—do not advocate replacing the *MFW* procedure with single-step cleaning in those transactions.

30 Coster v. UIP Cos., 300 A.3d 656, 671 (Del. 2023). In *Coster*, the court applied the intermediate scrutiny standard from cases such as *Unocal Corp. v. Mesa Petrol. Co.*, 493 A.2d 946, 954 (Del. 1985), both to board decisions applying defensive measures in response to a takeover threat and to board actions that interfere with shareholder voting rights. *Coster*, 300 A.3d at 668. Under this intermediate standard, a board's action must be in response to a threat to an important corporate interest and must be both "reasonable in relation to the threat posed and . . . not preclusive or coercive to the stockholder franchise." *Id.* at 672-73.

substantive matter but involves a less demanding inquiry than entire fairness. Third, we argue that where a director, as a result of controlling shareholder domination, acts other than in good faith, the director does and should face potential liability for a breach of the duty of loyalty (which is not subject to exculpation). We encourage plaintiffs and courts to deepen their focus on such director liability to increase the incentives both for directors to resist controlling shareholder domination and for controlling shareholders to support directors who are sufficiently independent to withstand allegations of domination.[31]

We note in particular that, by limiting the application of entire fairness to decisions at controlled companies, our proposal reduces the potential impact of characterizing a shareholder as controlling. We thus mitigate the challenges posed by the evolution of controlling shareholder liability not by denying the existence of soft control but by tempering the consequences of both its existence and its exercise. We therefore acknowledge the line-drawing challenges associated with the evolution of soft control but do not directly address those challenges in this Article.[32]

We proceed as follows. In Part I, we document Delaware's treatment of controlling shareholders under the principles of what we term "old" control. We show that historically, the courts have found shareholders with majority or near-majority voting control to be controlling. Even in such circumstances, the courts have applied fiduciary duties and entire fairness review sparingly and primarily to transactional events where the controller receives a quantifiable and material benefit to the detriment of the minority shareholders. As a practical matter, the application of this test has largely been limited to freeze-outs. Part II delineates the expansion of these principles through the series of post-*MFW* cases culminating in *Tornetta*, *Sears Hometown*, and *Match*. Part III discusses the implications of this expanded vision of control. We trace the extension of concepts of control beyond share ownership or mathematical voting power—what we term "new" control—explaining how *Tornetta* and its progeny potentially subject a broad range of decisionmakers and corporate actions to entire fairness analysis. We identify the consequences of the *Match* decision's approach to *MFW* compliance. And we explore a variety of practical concerns raised by the application of entire fairness to an expanded range of decisions by controlled

31 We note that these incentives extend beyond those provided by market forces and participants such as institutional investors, proxy advisors, and the media. *See* Lawrence A. Hamermesh, Jack B. Jacobs & Leo E. Strine, Jr., *Optimizing the World's Leading Corporate Law: A Twenty-Year Retrospective and Look Ahead*, 77 BUS. LAW. 321, 342 (2022) (asserting that such forces will enable independent directors to resist controlling shareholder demands).

32 We do believe that the Delaware approach to what constitutes control warrants refinement, a matter we address in Part III.

companies as well as the tension between the expanded role of controlling shareholders as fiduciaries and the structural features of corporate law. We conclude in Part IV by setting out our proposals to realign the doctrine applicable to controlling shareholders based on our theory of what it means for a shareholder to exercise control in the corporate context as well as the long-recognized economic value inherent in control.

I. CONTROLLING SHAREHOLDERS IN DELAWARE CORPORATE LAW

A. *Control as an Economic Concept*

Historically, commentators and corporate participants have understood control as an economic concept for ordering the corporation and directing its endeavors. As one commentator notes, "the standard law-and-economics model posits that control of a corporation is a valuable asset independent of either economies of scale or potential monopoly rents."[33]

The theory of economic corporate control recognizes the value of control in and of itself. More specifically, control over a corporation is a definable asset that can be transferred and regulated. In their book *The Modern Corporation and Private Property*, for example, Adolf A. Berle, Jr. and Gardiner C. Means describe control as an asset that belongs to the corporation.[34] As a result, they reason that any premium from a sale of corporate control should go to the corporate treasury.[35] This approach contrasts with cases such as *Zetlin v. Hanson Holdings*,[36] which recognize the right of controlling shareholders to transfer their stock at a premium. *Zetlin* and similar cases recognize both that control is an economic asset owned by the controlling shareholder and that the right to benefit from that control belongs to the shareholder and not the corporation.[37]

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33 Jay B. Kesten, *Managerial Entrenchment and Shareholder Wealth Revisited: Theory and Evidence from a Recessionary Financial Market*, 2010 BYU L. REV. 1609, 1619.

34 ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 244 (1933).

35 *Id.* ("[T]he power going with 'control' is an asset which belongs only to the corporation; and that payment for that power, if it goes anywhere, must go into the corporate treasury.").

36 397 N.E. 2d 387, 388 (N.Y. 1979).

37 *See also* Cheff v. Mathes, 199 A.2d 548, 555 (Del. 1964) ("[I]t is elementary that a holder of a substantial number of shares would expect to receive the control premium as part of his selling price . . . ."); Levy v. Am. Beverage Corp., 38 N.Y.S.2d 517, 526 (App. Div. 1942) ("Control might have lawful advantages . . . . We see no reason why the value of control would not be a lawful property right of the controlling stockholders . . . ."). *See generally* Alfred Hill, *The Sale of Controlling Shares*, 70 HARV. L. REV. 986 (1957) (setting forth authority that control is a value accruing to the controller).

Berle and Means's assertion that the value of control belongs to the corporation has been rejected.[38] Modern courts and commentators instead regard the controlling shareholder as entitled to treat control as a private asset and defend the economic efficiency of doing so. Henry Manne, for example, argued both that it was economically efficient to enable the owner of a controlling block to receive a premium and that regulations which limit that premium or impede efficient transfers of control interfere with the most productive use of the corporation's assets.[39] This reasoning led Manne to criticize takeover defenses on the basis that they diminish the value of control by hindering its transfer and exercise.[40]

Recognizing and protecting the right of an owner to benefit from control also provides theoretical advantages to minority shareholders. Zohar Goshen and Assaf Hamdani explored this theory in a recent article, explaining that "control allows entrepreneurs to pursue business strategies that they believe will produce above-market returns by securing the ability to implement their vision in the manner they see fit."[41] The entrepreneur, they argue, "values control because it protects her against the possibility of subsequent midstream investor doubt and objections regarding either the entrepreneur's vision or her abilities."[42] The authors postulate that control itself is not an "unalloyed evil."[43] Instead, control—particularly "new" control—"creates value for controlling and minority shareholders alike."[44] In this regard, "[c]orporate law should secure minority shareholders' rights to a pro-rata share of the corporate pie, while preserving the controller's freedom to pursue

38 The primary case to take this approach was *Perlman v. Feldmann*, 219 F.2d 173, 178 (2d Cir. 1955) ("[W]hen the sale [of control] necessarily results in a sacrifice of this element of corporate good will and consequent unusual profit to the fiduciary who has caused the sacrifice, he should account for his gains."). Despite support among some academics, the rule in *Perlman* has not been followed. *See, e.g.*, Victor Brudney, *Equal Treatment of Shareholders in Corporate Distributions and Reorganizations*, 71 CALIF. L. REV. 1072, 1130 (1983) (noting that, while "puzzling," imposing liability or requiring accounting for sale of controlled shares is "far from uniformly accepted"). *See generally* William D. Andrews, *The Stockholder's Right to Equal Opportunity in the Sale of Shares*, 78 HARV. L. REV. 505 (1965) (weighing various justifications for *Perlman* and ultimately proposing an alternative rule).

39 Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110, 116-17 (1965).

40 *Id.*; *see also* Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161, 1199-1201 (1981) (explaining the importance of management passivity in response to a takeover so that economic resources can be directed to their highest valued use).

41 Zohar Goshen & Assaf Hamdani, *Corporate Control and Idiosyncratic Vision*, 125 YALE L.J. 560, 565 (2016); *see also id.* at 566 (explaining that investors "value control because it allows them to minimize agency costs").

42 *Id.* at 565 (emphasis omitted).

43 *Id.* at 560.

44 *Id.*

her idiosyncratic vision to maximize the corporate pie."[45] In essence, Goshen and Hamdani, among others, treat economic control as an asset that can also benefit minority shareholders.[46]

The theory of economic control thus recognizes that the existence of a majority stockholder does not present an inherent corporate governance problem.[47] Indeed, the finance literature has observed that the presence of a large blockholder can enhance the value of the firm by controlling managerial agency costs.[48] Ronald Gilson and Alan Schwartz have similarly argued that majority shareholders can provide efficient monitoring of management, and allowing controllers to obtain private benefits of control creates an incentive for them to engage in such monitoring.[49] Moreover, the majority shareholder's economic stake is likely to align its interests in operational decisions with those of the minority shareholders.[50] As Albert Choi observes, concentrated ownership can enhance long-term firm value even in circumstances in which a controlling shareholder is able to extract private benefits of control.[51]

Nonetheless, the presence of control creates opportunities for private expropriatory gain by the controller. An extensive literature explores the risks of tunneling or other diversion of corporate assets to the controller.[52] In other words, control can be an economic benefit, but it can also provide undue and inordinate gains to the controller at the expense of other stockholders.

Corporate law and market forces (as well as regulation) attempt to balance the benefits of control while containing its dark side. Ronald Gilson, for example, explains that shareholder control reflects a potential trade-off and

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45 *Id.* at 595-96.

46 *Id.* at 596-97; *see also* Byung Hyun Ahn, Jill E. Fisch, Panos N. Patatoukas & Steven Davidoff Solomon, *Synthetic Governance*, 2021 COLUM. BUS. L. REV. 476, 513-15 (documenting benefits to minority shareholders from dual class shares with sunset provisions).

47 Goshen & Hamdani, *supra* note 41, at 617.

48 *See, e.g.*, Ronald J. Gilson & Jeffrey N. Gordon, *Doctrines and Markets: Controlling Controlling Shareholders*, 152 U. PA. L. REV. 785, 785-86 (2003) ("The presence of a controlling shareholder reduces the managerial agency problem, but at the cost of the private benefits agency problem. Non-controlling shareholders will prefer the presence of a controlling shareholder so long as the benefits from reduction in managerial agency costs are greater than the costs of private benefits of control.").

49 Ronald J. Gilson & Alan Schwartz, *Corporate Control and Credible Commitment*, 43 INT'L REV. L. & ECON. 119, 122-23 (2015).

50 *Id.*

51 Albert H. Choi, *Concentrated Ownership and Long-Term Shareholder Value*, 8 HARV. BUS. L. REV. 53, 56-57 (2018); *see also* Jonathan R. Macey, *Delaware Law Mid-Century: Far from Perfect but Probably Not Leaving for Las Vegas* 6-7 (Yale L. & Econ. Rsch. Paper, 2024), https://ssrn.com/abstract=5043887 (arguing that market forces protect minority shareholders from expropriatory actions by controlling shareholders).

52 *See* Yong Lim & Geeyoung Min, *Competition and Corporate Governance: Teaming Up to Police Tunneling*, 36 NW. J. INT'L L. & BUS. 267, 269 (2016) (describing tunneling as "a well-known ailment in the corporate governance pathology").

that "a controlling shareholder may police the management of public corporations better than the standard panoply of market-oriented techniques employed when shareholdings are widely held."[53] One reason is that "[b]ecause she holds a large equity stake, a controlling shareholder is more likely to have the incentive either to monitor managers effectively or to manage the company itself and, because of proximity and lower information costs, may be able to catch problems earlier."[54] Gilson observes, however, that controlling shareholders can receive their own private pecuniary gains by appropriating corporate assets.[55]

Gilson notes that both law and market forces play a strong role in monitoring controlling shareholders. He observes:

> The empirical evidence supports the proposition that minority shareholders are not uniquely disadvantaged in an efficient controlling shareholder system. Good law keeps diversion of pecuniary private benefits of control low and, in a reasonably efficient stock market, the costs of these payments for focused monitoring, as well as the risk that the talent of future generations of managers will regress to the mean, will be priced."[56]

The benefits of controlling shareholders, therefore, are greatest in jurisdictions with both functionally effective law and efficient markets, which collectively serve to monitor and discipline controlling shareholders. In the next subsection, we further address the important interrelationship between legal rules and effective market discipline in regulating controlling shareholders.

B. *Controlling Shareholders and Fiduciary Duties*

The idea that control is an asset that can provide benefits yet be misused has informed notions of control in fiduciary and corporate law. More specifically, since the nineteenth century, corporate law has imposed obligations on those who exercise control over the corporation, recognizing explicitly and implicitly the value of this control and the implication of legal restrictions. In the United States, this fiduciary and related law has been the primary means of regulating controlling shareholders.[57]

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53 Ronald J. Gilson, *Controlling Shareholders and Corporate Governance: Complicating the Comparative Taxonomy*, 119 HARV. L. REV. 1641, 1651 (2006).

54 *Id.*

55 *Id.* at 1664.

56 *Id.* at 1667.

57 That being said, section 13(d) of the Securities Exchange Act, 15 U.S.C. § 78m(d), requires anyone acquiring five percent of the voting power of an issuer to disclose its ownership position and various other information. Congress adopted section 13(d) to "alert the marketplace to every large, rapid aggregation or accumulation of securities, regardless of technique employed, which might

Fiduciary duties in corporate law apply, for the most part, to actions by a corporation's officers and directors. The reason for this is that officers and directors are classic fiduciaries—they exercise control over decisions that are made with "other people's money."[58] Under the common law, transactions between the corporation and such fiduciaries were inherently void or voidable at the option of the corporation.[59] Delaware adopted section 144 of the Delaware General Corporate Law (DGCL) to modify this rule by providing procedural protections that would exempt conflict-of-interest transactions from voidability.[60] Subsequent case law interpreted this statute to nonetheless require that a transaction be entirely fair[61] but developed procedural mechanisms—specifically, independent board approval or an informed shareholder vote—that would cleanse a transaction involving a conflicted officer or director from entire fairness review and enable a court to apply the deferential business judgment rule to a lawsuit challenging such a transaction.[62]

Controlling shareholders differ from officers and directors in two ways. First, they do not have the power to act for the corporation or make decisions on its behalf. Second, they are principals, not agents, which gives them the right to act in accordance with their individual objectives rather than those of the corporation.[63] As a result, Delaware courts and courts in other states historically distinguished between shareholders and management, holding that, as a general matter, shareholders are not fiduciaries and do not owe duties to the corporation.[64] Even controlling shareholders owe fiduciary

represent a potential shift in corporate control." GAF Corp. v. Milstein, 453 F.2d 709, 717 (2d Cir. 1971), *cert. denied*, 406 U.S. 910 (1972).

58 LOUIS BRANDEIS, OTHER PEOPLE'S MONEY AND HOW THE BANKERS USE IT (1914); *see also* D. Gordon Smith, *Delaware's Corporate Fiduciary Law Canon* 7 (unpublished manuscript) (on file with authors) ("The role of fiduciary law is to regulate relationships where one party (the fiduciary) exercises discretionary authority over the resources or practical interests of another party (the beneficiary).").

59 Marciano v. Nakash, 535 A.2d 400, 403 (Del. 1987).

60 DEL. CODE ANN. tit. 8, § 144 (2024).

61 *See, e.g.*, Fliegler v. Lawrence, 361 A.2d 218 (Del. 1976) (adopting a two-tiered analysis in which section 144 was applied along with entire fairness).

62 *See, e.g.*, *In re* Wheelabrator Technologies S'holders Litig., 663 A.2d 1194, 1203 (Del. Ch. 1995) ("Approval by fully informed, disinterested shareholders pursuant to § 144(a)(2) invokes 'the business judgment rule and limits judicial review to issues of gift or waste with the burden of proof upon the party attacking the transaction.'" (quoting *Marciano*, 535 A.2d at 405 n.3)).

63 Mary Siegel, *The Erosion of the Law of Controlling Shareholders*, 24 DEL. J. CORP. L. 27, 36 (1999) ("[B]ecause shareholders can act in their own self-interest, courts should expect shareholders to assume fiduciary responsibilities only when they exercise power not as shareholders but as managers, negotiating or dictating both sides of a transaction.").

64 *See, e.g.*, Voigt v. Metcalf, C.A. No. 2018-0828-JTL, 2020 WL 614999, at *10 (Del. Ch. Feb. 10, 2020) ("A stockholder that does not control the corporation is not a fiduciary and cannot be held liable for breaching non-existent duties.") (citing Basho Techs. Holdco B, LLC v. Georgetown Basho

duties to the corporation and other shareholders only in limited circumstances.[65] Absent those circumstances, courts largely held that controlling shareholders are not subject to fiduciary duties and are legally entitled to act in their own best interests and accrue the benefits of control.[66]

The Delaware Supreme Court famously delineated this principle in the 1940s in *Ringling Bros.-Barnum & Bailey Combined Shows v. Ringling*.[67] In *Ringling Bros.*, the court upheld a trust agreement among shareholders to vote and control the corporation.[68] The court premised its decision on the wide berth given to stockholders to exercise the shareholder franchise with impunity as well as the ability to separate the vote from the other ownership attributes of stock.[69] The court stated that "[g]enerally speaking, a shareholder may exercise wide liberality of judgment in the matter of voting, and it is not objectionable that his motives may be for personal profit, or determined by whims or caprice, so long as he violates no duty owed his fellow shareholders."[70] *Ringling Bros.* thus recognized the right of

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Invs., LLC, 2018 WL 3326693, at *25 (Del. Ch. July 6, 2018), *aff'd sub nom.* Davenport v. Basho Techs. Holdco B, LLC, 221 A.3d 100 (Del. 2019)).

65 Delaware courts have not been explicit about the basis for this position. In some cases, the courts have held that while a controlling stockholder has fiduciary duties, entire fairness did not apply. In other cases, the courts have rejected the premise that a controlling shareholder is a fiduciary in the context of a decision that does not involve obtaining a benefit at the expense of the minority. In this Article we refer to the imposition of fiduciary duties, as more recent decisions have done, as triggering entire fairness review.

66 *See, e.g.*, Jeffrey N. Gordon, *Systematic Stewardship*, 47 J. CORP. L. 627, 666-67 (2022) ("[E]ven for controlling shareholders, there are no shareholder duties, except in frank self-dealing."); *see also* Adolf Berle, Jr., *"Control" In Corporate Law*, 58 COLUM. L. REV. 1212 (1958). Berle explored the current state of the law of controller liability and theorized that "[t]he control-function wherever and however held in the corporation is a responsible, not an irresponsible function. It must be used for the benefit and advantage of the corporation, and, where used to benefit holders of control (for example, electing one of them to a salaried office in the corporation or contracting with interests allied to the control-holders), it must not damage the corporation or be unfair or inequitable to it." *Id.* at 1225.

67 53 A.2d 441, 447 (Del. 1947). This issue was not novel in Delaware and had been previously addressed in Heil v. Standard Gas & Elec. Co., 151 A. 303, 304 (Del. Ch. 1930) ("[S]tockholders have the right to exercise wide liberality of judgment in the matter of voting and may admit personal profit or even whims and caprice into the motives which determine their choice, so long as no advantage is obtained at the expense of their fellow stockholders.").

68 *Ringling Bros.*, 53 A.2d at 448.

69 *Id.* at 447.

70 *Id.*; *see also* Bershad v. Curtiss-Wright Corp., 535 A.2d 840, 845 (1987) ("Stockholders in Delaware corporations have a right to control and vote their shares in their own interest. They are limited only by any fiduciary duty owed to other stockholders. It is not objectionable that their motives may be for personal profit, or determined by whim or caprice, so long as they violate no duty owed other shareholders."). In *Ringling Bros.*, the court also stated that a shareholder was free to vote "so long as he violates no duty owed his fellow shareholders." 53 A.2d at 447. The court then, without explanation, cited *Heil v. Standard Gas. & Elec. Co.*, 151 A. 303 (Del. Ch. 1930), a case that involved whether a shareholder outside the voting context had reaped a "peculiar" benefit from the transaction at issue. *Id.* at 305. Although the *Heil* court found no such benefit, the language formed

shareholders, even controlling shareholders, to vote in their self-interest—a principle still recognized by Delaware courts.[71]

In *Bershad v. Curtiss-Wright Corp.*,[72] decided forty years after *Ringling Bros.*, the Delaware Supreme Court extended to the sale context the principle that a majority shareholder is not a fiduciary when acting in its capacity as a shareholder. In *Bershad*, the court held that "a stockholder is under no duty to sell its holdings in a corporation, even if it is a majority shareholder."[73] This was true even if the sale would "profit the minority."[74] Applying that rule, the justices rejected a stockholder's claim that a controller breached its duties by engaging in a squeeze-out rather than exploring a sale of the company to a third party.[75] Thus, the controlling shareholders had no obligation to sell in such a situation and were not subject to any fiduciary duty to the other shareholders or corporation, including *Revlon* duties.[76]

Similarly, the Delaware courts have held that controlling stockholders exercising their right to block shareholder action are not subject to fiduciary review. In *Frantz Manufacturing Co. v. EAC Industries*, decided a few years before *Bershad*, the Delaware Supreme Court upheld a controlling shareholder's adoption by written consent of a bylaw that required director unanimity in order to protect its interests.[77] The court specifically held that although it would review the transaction for its equitable nature (a review that did not speak of entire fairness), the controller was justified in its "attempt to avoid its disenfranchisement as a majority shareholder."[78]

Then-Vice Chancellor Strine expounded on the scope of *Frantz* in *Hollinger International, Inc. v. Black*.[79] In *Hollinger*, a controlling shareholder had amended the company's bylaws to dissolve a special committee of the board and prevent it from approving a sale.[80] The Vice Chancellor upheld the

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the basis for imposing entire fairness review on controllers in a wide array of cases involving a "unique benefit." *See infra* Section II.A.

71 *See* Tanzer v. Int'l Gen. Indus., 379 A.2d 1121, 1124 (Del. 1977) ("[F]or more than fifty years our Courts have held, consistent with the general law on the subject, that a stockholder in a Delaware corporation has a right to vote his shares in his own interest, including the expectation of personal profit, limited, of course, by any duty he owes to other stockholders.").

72 535 A.2d 840 (1987). *Bershad* also included the language from *Ringling Bros.* that, while controlling shareholders are free to vote their shares, they "are limited only by any fiduciary duty owed to other stockholders." *Id.* at 845. Again, the fiduciary duties the court was referring to were unspecified.

73 *Id.* at 845.

74 *Id.*

75 *Id.* at 842.

76 *Id.* at 841-42 (citing Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986)).

77 501 A.2d 401, 407 (Del. 1985).

78 *Id.*

79 844 A.2d 1022 (Del. Ch. 2004).

80 *Id.* at 1029.

statutory authority of the controlling shareholder to engage in this behavior but struck down the bylaw on equitable grounds (again, without applying entire fairness). Specifically, Vice Chancellor Strine stated that "it is no small thing to strike down bylaw amendments adopted by a controlling stockholder . . . ."[81] Vice Chancellor Strine nonetheless found that action was required "because those amendments complete a course of contractual and fiduciary improprieties" and that "Inc.'s written consent was the culmination of Black's efforts on his (and Inc.'s) behalf to end-run the Strategic Process he had agreed to lead and support."[82]

These precedents show that Delaware law has historically provided a wide berth to shareholders, including controlling shareholders, to exercise their rights as shareholders without being subject to fiduciary duties and the application of entire fairness review. Concededly, cases like *Frantz* and *Hollinger* acknowledged that controlling shareholder transactions can be subject to attack on equitable grounds. Importantly, however, the rationale for such an attack was interference with the board process and not a standalone fiduciary duty owed by the controlling shareholder or the application of entire fairness to the controller's actions.

In addition, the traditional controlling shareholder cases largely relied on objective measures of control.[83] Indeed, early cases used the terminology of "majority shareholder" rather than "controlling shareholder" and focused on situations in which shareholders owned a majority or near majority of the corporation's voting stock.[84] To be fair, courts extended the concept of a majority shareholder not merely to those shareholders that held mathematical control—that is, more than fifty percent—but also to those that owned a substantial percentage of stock and exercised effective control.[85] As the Delaware Supreme Court explained in *Kahn v. Lynch Communication Systems*, "a shareholder owes a fiduciary duty only if it owns a majority interest in or exercises control over the business affairs of the corporation."[86]

Subsequent cases expanded on *Lynch* to recognize that a large shareholder could exercise control without holding an absolute majority of the

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81 *Id.* at 1081.

82 *Id.*

83 In contrast, Adolf Berle recognized the flexible nature of control. In 1958, he defined control as "the capacity to choose directors" and argued that "[a]s a corollary, it carries capacity to influence the board of directors and possibly to dominate it." Berle, *supra* note 66, at 1212.

84 *See, e.g.*, Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1343 (Del. 1987).

85 *See, e.g.*, Singer v. Magnavox Co., 380 A.2d 969, 979-80 (Del. 1977); Tanzer v. Int'l Gen. Indus., Inc., 379 A.2d 1121, 1123 (Del. 1977).

86 638 A.2d 1110, 1113 (Del. 1995) (quoting Ivanhoe Partners, 535 A.2d at 1344) (emphasis omitted).

corporation's shares,[87] but they generally applied the fiduciary duties associated with majority shareholder status only to such shareholders if they exercised actual control of corporate conduct in the specific transaction under scrutiny.[88] As Larry Hamermesh, Jack Jacobs, and Leo Strine explain, "Under Delaware law, it was historically difficult to establish that a stockholder having less than majority ownership was a controlling stockholder."[89]

C. *Fiduciary Duties and Freeze-Outs*

Cases in which a controlling shareholder obtains a pecuniary benefit directly from or at the expense of the minority shareholders constitute a longstanding exception to the principle that fiduciary duties do not apply to a controlling stockholder. The prototypical case for the imposition of such duties is when a controlling shareholder initiates a transaction to freeze out the minority shareholders. Such duties also apply in similar transactions, such as when the majority shareholder sells an asset to the corporation or purchases an asset from the corporation.[90] Analogous reasoning extends to when a controller knowingly sells to a looter or is grossly negligent in allowing such a sale.[91] As detailed below, Delaware has historically taken a nuanced approach to this exception, recognizing both the confined fiduciary duties applicable to shareholders and the value inherent in allowing majority shareholders to enjoy benefits associated with their controlling ownership.

Delaware set out the context in which controlling shareholders would be treated as fiduciaries in *Sinclair Oil Corp. v. Levien*.[92] In *Sinclair Oil*, decided in 1971, the parent corporation was accused of using its control to cause its subsidiary to pay dividends, preventing the further development of the subsidiary and providing the parent corporation, which needed liquidity, with cash.[93] The court held that although the parent corporation owed a fiduciary

87 Courts recognized that not all shareholders vote and that, as a result, a large block minority block will, as a practical matter, often be sufficient. As the court explained in *Cysive*, however, that block must be sufficient that the controller's vote is likely to be sufficient "without having to attract much, if any, support from public stockholders." *In re* Cysive, Inc. S'holders Litig., 836 A.2d 531, 552 (Del. Ch. 2003).

88 *See* Gilbert v. El Paso Co., 490 A.2d 1050, 1055 (Del. Ch. 1984) ("[A] shareholder who owns less than 50% of a corporation's outstanding stocks does not, without more, become a controlling shareholder of that corporation, with a concomitant fiduciary status.").

89 Hamermesh, Jacobs & Strine, *supra* note 31, at 345.

90 *See, e.g.*, Kahn v. Tremont Corp. (Tremont II), 694 A.2d 422, 428-29 (Del. 1997) (applying fiduciary duties to controlled company's purchase of stock owned by the controlling shareholder).

91 *See, e.g.*, Harris v. Carter, 582 A.2d 222, 233 (Del. Ch. 1990) ("[T]he owners of control are under a duty not to transfer it to outsiders if the circumstances surrounding the proposed transfer are such as to awaken suspicion and put a prudent man on his guard.").

92 280 A.2d 717 (Del. 1971).

93 *Id.* at 719.

duty to the minority shareholders when dealing with its subsidiary, its actions in the case at bar need not be analyzed under entire fairness because the dividends in question were paid ratably to all shareholders:

> A parent does indeed owe a fiduciary duty to its subsidiary when there are parent-subsidiary dealings. However, this alone will not evoke the intrinsic fairness standard. This standard will be applied only when the fiduciary duty is accompanied by self-dealing—the situation when a parent is on both sides of a transaction with its subsidiary. Self-dealing occurs when the parent, by virtue of its domination of the subsidiary, causes the subsidiary to act in such a way that the parent receives something from the subsidiary to the exclusion of, and detriment to, the minority stockholders of the subsidiary.[94]

Accordingly, the court held that the appropriate standard of review was the business judgment rule.[95] To be sure, the court recognized that a parent–subsidiary transaction could be subject to entire fairness where there was something provided to the "exclusion of, and detriment to" the minority stockholders.[96] However, the court also noted that such a benefit would have to be attributable to the "domination of the subsidiary."[97] In other words, the application of fiduciary duties and entire fairness required two elements—first, a transaction between the company and the controller to the detriment of the minority, and second, domination of the company by the controller in the transaction itself. Outside of this context, the shareholder, when acting in a shareholder capacity, was not subject to such fiduciary duties.

In *Puma v. Marriott*, decided shortly after *Sinclair Oil*, the court similarly upheld a transaction between the Marriott Corporation ("Marriott") and the Marriott Group—members of the Marriott family who collectively owned forty-six percent of Marriott's stock.[98] The transaction was negotiated and approved by a majority of independent Marriott directors and approved by the shareholders.[99] Although Marriott's process arguably met the standard of entire fairness, the court expressly declined to apply that standard, concluding instead that because the plaintiff had not shown that the Marriott family dominated the independent directors (and therefore was not a controller), the applicable standard of review was the business judgment rule.[100]

94 *Id.* at 720.
95 *Id.* at 722.
96 *Id.* at 720.
97 *Id.*
98 283 A.2d 693, 695 (Del. Ch. 1971).
99 *Id.*
100 *See id.*

Similarly, in *Nixon v. Blackwell*, a case decided more than twenty years after *Sinclair Oil*, the court concluded that fair treatment of minority shareholders did not require that they receive the same benefits as the majority.[101] In that case, minority shareholders sued the directors of a closely held corporation, asserting that a failure to pay them dividends was a denial of "liquidity" and a breach of fiduciary duty.[102] The Delaware Supreme Court held that there was no fiduciary rule that granted the minority shareholders in a close corporation the right to "equal treatment."[103] Instead, the analysis was that elaborated in *Sinclair*—entire fairness applied when there was a benefit to the controlling shareholder in a transaction to the exclusion of, and detriment to, the minority stockholders where domination existed.[104]

Thus, although historically controlling shareholders were not subject to general fiduciary duties, early cases recognized the application of such duties under confined circumstances.[105] These circumstances aligned with the law and economics literature of the time, which called for limited fiduciary duties for controlling shareholders with exceptions when a controller obtained a pecuniary benefit by taking undue advantage of a corporation or minority shareholders.[106] As a result, the early case law on controlling shareholder fiduciary duties and the application of entire fairness as a general matter arose primarily in the context of freeze-outs.[107]

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101 626 A.2d 1366, 1379 (Del. 1993) ("The Class B stock was given no voting rights because those stockholders were not intended to have a direct voice in the management and operation of the Corporation. They were simply passive investors—entitled to be treated fairly but not necessarily to be treated equally.").

102 *Id.* at 1373.

103 *Id.* at 1377.

104 *Id.* at 1375.

105 *See, e.g.*, Canal Cap. Corp. v. French, C.A. No. 11,764, 1992 WL 159008, at *2-4 (Del. Ch. July 2, 1992) (applying the business judgment rule to a services agreement with a controlling stockholder after independent board approval); Getty Oil Co. v. Skelly Oil Co., 267 A.2d 883, 887-88 (Del. 1970) (applying the business judgment rule to a disputed transaction involving a controlling stockholder where domination was not found).

106 *See* Allied Chem. & Dye Corp. v. Steel & Tube Co. of Am., 120 A. 486, 491 (Del. Ch. 1923) ("[I]f the majority stockholders so use their power to advantage themselves at the expense of the minority, their conduct in that regard will be denounced as fraudulent . . . . [But] it is not true that every personal advantage which the majority secures is to be regarded as vitiating in character. An examination of the cases to which special attention is directed by the complainants in this connection will disclose that the personal advantage accruing to the majority is in some way derived from, or intimately associated with, the corporate assets themselves."); *see also* Robert W. Hamilton, *Private Sale of Control Transactions: Where We Stand Today*, 36 CASE W. RSRV. L. REV. 248, 249-50 (1986) (explaining the "long settled law" that controlling shareholders may receive a premium for their shares without sharing it with other shareholders); Saul X. Levmore, *A Primer on the Sale of Corporate Control*, 65 TEXAS L. REV. 1061, 1061-63 (1987) (arguing that forcing controlling shareholders to share stock sale profits with non-selling minority shareholders provides non-sellers a "double advantage").

107 *See, e.g.*, Weinberger v. UOP, Inc., 457 A.2d 701, 710-11 (Del. 1983) (holding that a majority shareholder's cash out merger must satisfy standards of fair price and fair process).

We theorize that transactions in which the majority shareholder froze out the minority shareholders and became the sole owner of the corporation should be viewed as different and inherently coercive for two reasons.[108] First, unlike operational decisions, in freeze-outs, the majority shareholder's interests directly oppose those of the minority shareholders—every dollar the majority shareholder gains is a dollar lost by the minority shareholders.[109] Second, a freeze-out is an end-game situation in that after the freeze-out, the minority shareholders will no longer be investors in the company. Accordingly, any economic value from the freeze-out (such as the majority shareholder's ability to reduce managerial agency costs or other cost savings) inures exclusively to the benefit of the majority shareholder, absent statutory protections such as dissenters' rights.[110]

In line with this theoretical approach, Delaware historically applied this heightened standard of review only to transactions in which the purchaser or counterparty was, at the time of the transaction, a majority or near-majority shareholder. As the Delaware Supreme Court explained in *Citron v. Fairchild Camera & Instrument Corp.*, "[u]nder Delaware law, until the conclusion of the tender offer, [the buyer of a controlling share] owe[s] no fiduciary duty of candor to [the corporation's] stockholders."[111] The Delaware Supreme Court reiterated this point in *Corwin v. KKR Financial Holdings*, in which it rejected the argument that KKR was a controlling shareholder of KKR Financial Holdings where, despite plaintiff's allegations of control, "KKR owned less than 1% of Financial Holdings' stock, had no right to appoint any directors, and had no contractual right to veto any board action."[112]

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108 *See, e.g.*, Kahn v. Tremont Corp. (Tremont I), C.A. No. 12339, 1996 WL 145452, at *7 (Del. Ch. Mar. 21, 1996) ("[A] controlling shareholder transaction . . . of course is the context in which the greatest risk of undetectable bias may be present."). A second prominent line of cases outside Delaware identified distinctive concerns posed by a controlling shareholder in a close corporation. *See* Robert B. Thompson, *The Shareholder's Cause of Action for Oppression*, 48 BUS. LAW. 699, 713 n.83 (collecting cases). These cases developed the "doctrine of oppression" to respond to abusive actions by controlling shareholders and subjected such actions to greater judicial scrutiny. Although various states adopted the doctrine of oppression or similar standards to scrutinize this conduct, Delaware rejected the idea of special rules for oppressive actions outside a statutory close corporation. *See* *Nixon*, 626 A.2d at 1380-81 (rejecting the application of the oppression doctrine). Significantly, however, oppression was a more rigorous standard than entire fairness and could not be established through evidence of mere self-dealing by a controlling shareholder. *See, e.g.*, Fix v. Fix Material Co., 538 S.W.2d 351, 358 (Mo. Ct. App. 1976) (defining oppression as "burdensome, harsh and wrongful conduct" or "a visible departure from the standards of fair dealing, and a violation of fair play").

109 *See* John C. Coates IV, *"Fair Value" as an Avoidable Rule of Corporate Law: Minority Discounts in Conflict Transactions*, 147 U. PA. L. REV. 1251, 1314 (1999) ("[T]he net effect of a freeze-out is to transfer value from minority shareholders to fiduciaries.").

110 *See id.*

111 569 A.2d 53, 70 (Del. 1989).

112 Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304, 306 (Del. 2015).

The court's focus on freeze-outs was largely in line with the theoretical prospect of domination and the end-stage nature of the transaction.[113] As then-Vice Chancellor Strine explained, the prospect of coercion both undermines the board's potential independence and potentially compromises the significance of minority shareholder approval.[114] Even the cases applying heightened review to freeze-outs involved both the controlling shareholder's explicit domination of the company and board and actions that appeared to bypass or interfere with the corporation's authorized decisionmaking process.[115] This view was reinforced in the case of *Glassman v. Unocal Exploration Corp.*, where the court held that the structure of DGCL section 253 and the lack of board or minority rule meant that a short-form statutory merger was subject to business judgment review, not entire fairness.[116]

Beyond the freeze-out context, and again in line with our theoretical justification, Delaware courts historically limited the application of entire fairness in corporations with controlling shareholders. In 2014, Vice Chancellor Parsons explained the state of play in *In re Crimson Exploration Inc. Stockholder Litigation*.[117] He stated that Delaware courts did not apply "[e]ntire fairness . . . solely because a company has a controlling stockholder."[118] Instead, he explained that cases in which fiduciary duties apply—and hence the standard of entire fairness is employed—fall into "one of two categories: (a) transactions where the controller stands on both sides; and (b) transactions where the controller competes with the common stockholders for consideration."[119] He further observed:

> The case law has recognized only a few situations where, despite the stockholders receiving the same consideration, the controller nonetheless receives a unique benefit and the court applies entire fairness: (a) the controller eliminates something bad for it and good for the minority . . . or (b) all parties suffer a sub-optimal sale price, but the controller still benefits because it receives cash to satisfy an idiosyncratic liquidity problem . . . .[120]

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113 As we explain below, courts also have a benchmark when evaluating the fairness of freeze-outs by comparing the value minority shareholders would obtain in an arms-length third party transaction. *See infra* Section III.C.

114 *In re* Cox Commc'ns, Inc. S'holders Litig., 879 A.2d 604, 619 (Del. Ch. 2005).

115 *See, e.g.*, Weinberger v. UOP, Inc., 452 A.2d 701, 703-08 (Del. 1983) (addressing a controlling shareholder's alleged failure to disclose all material information about a transaction). Moreover, at least initially, Delaware courts seemed to limit application of this doctrine to mergers and not tender offers. *See* Solomon v. Pathe Commc'ns Corp., 672 A.2d 35, 39-40 (Del. 1996).

116 777 A.2d 242, 247-48 (Del. 2001).

117 *In re* Crimson Exploration Inc. S'holder Litig., C.A. No. 85141-VCP, 2014 WL 5449419, at *10 (Del. Ch. Oct. 24, 2014).

118 *Id.* at *12.

119 *Id.*

120 *Id.* at *20.

Thus, outside these confined areas, controlling shareholders were not deemed fiduciaries, including in transactions where they exercised their statutorily authorized power as shareholders.

II. EXTENDING CONTROLLING SHAREHOLDER FIDUCIARY DUTIES

As described in Part I, until recently, the application of fiduciary duties and entire fairness principles to controlling shareholder actions focused largely on the freeze-out context.[121] In Delaware, the extent to which other transactions were subject to entire fairness review remained an open question at best and, when such review was extended, it appeared to require the controlling shareholder to dominate the board process as well as a quantifiable benefit to the controller to the detriment of the minority. Outside these transactions, the courts generally ruled that transactions involving controlling shareholders were not subject to entire fairness review. As we delineate below, however, a series of cases in the last decade has taken a different approach both by applying fiduciary duties and entire fairness review to a broader range of corporate decisions and by expanding the concept of a controlling shareholder.

A. *Fiduciary Duties for Controlling Shareholders*

We believe a turning point occurred in *In re EZCORP Inc. Consulting Agreement Derivative Litigation*.[122] In that case, the plaintiff brought suit challenging three advisory services agreements which, he alleged, were a means for EZCORP's controlling shareholder, Phillip Ean Cohen, to extract a non-ratable benefit from EZCORP.[123] Cohen controlled EZCORP through a dual class voting structure, in which his class B shares, despite representing only 5.5% of EZCORP's outstanding equity, gave him 100% of EZCORP's voting power.[124]

The plaintiff attempted to hold Cohen liable for aiding and abetting a breach of fiduciary duty by EZCORP's directors, apparently because Cohen was not acting on behalf of EZCORP with respect to the advisory

121 In *EZCORP*, Vice Chancellor Laster disputed this proposition, citing a number of cases which applied entire fairness review outside the freeze-out context. *In re* EZCORP Inc. Consulting Agreement Derivative Litig., C.A. No. 9962-VCL, 2016 WL 301245, at *12-15 (Del Ch. Jan. 25, 2016). We acknowledge the holdings of these cases but question the extent to which they stand for the general proposition that entire fairness applies, as a per se matter, to transactions with a controlling shareholder. We therefore view *EZCORP* as taking a doctrinal step beyond the cases it cites.

122 *Id.*

123 *Id.* at *1.

124 *Id.* at *2.

agreements.[125] Vice Chancellor Laster rejected this theory but instead reasoned that, as a controlling shareholder, Cohen owed fiduciary duties to EZCORP.[126] Consequently, he held that the plaintiff had a direct claim against Cohen for breaching those duties.[127] In so doing, the Vice Chancellor relied upon federal precedent:

> An ultimate human controller who engages directly or indirectly in an interested transaction with a corporation is potentially liable for breach of duty, even if other corporate actors made the formal decision on behalf of the corporation, and even if the controller participated in the transaction through intervening entities.[128]

The Vice Chancellor took a broad view of control, looking at "who wields control in substance."[129] He then considered and rejected the proposition that controlling shareholders only owe fiduciary duties to the corporation in freeze-out transactions, concluding instead that such duties are owed in any transaction in which a controller extracts a non-ratable benefit regardless of whether domination is evident in the transaction itself.[130] Although the court acknowledged some ambiguity in how courts had applied the demand requirement in the context of such transactions, it concluded that demand could not be excused given the prospect of controlling shareholder domination.[131] The court cited facts tending to indicate the potential for such domination, noting that Cohen had attempted to influence EZCORP's nominally independent directors both by inviting them to serve on the boards of EZCORP's affiliates and by firing those directors if they displeased him.[132] Having concluded that Cohen could be liable for breaching his fiduciary duties, the court then determined that the applicable standard of review was entire fairness and that compliance with the *MFW* procedure was required for the case to be resolved through a motion to dismiss.[133]

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125 *Id.* at *8.

126 *Id.* at *9-11.

127 *Id.* at *10-11.

128 *Id.* at *9.

129 *Id.*

130 *Id.* at *12 ("The entire fairness framework clearly governs squeeze-out mergers, but Delaware courts also have applied it more broadly to transactions in which a controller extracts a non-ratable benefit.").

131 *Id.* at *29 ("[I]f the omnipresent specter [of a conflicted board] is enough to excuse demand, then excusal would follow more readily when directors must confront a dominant stockholder who will continue in control of the entity and enjoys both the hard and soft power to engage in potentially blatant, but more likely subtle acts of retribution."). The court acknowledged that "the choice between *Aronson* and other precedents is something only the Delaware Supreme Court can resolve." *Id.* at *30.

132 *Id.* at *4, *6.

133 *Id.* at *30-31.

Cohen and the other defendants in *EZCORP* sought interlocutory appeal, claiming that the decision raised a novel and material issue concerning the appropriate standard of review for controller transactions. In one of two applications, the defendants wrote:

> The Supreme Court has never had an opportunity to decide how the holdings in the *MFW* decisions would apply outside of the controlling stockholder merger context. This case presents that opportunity, and along with it the opportunity to harmonize under one unified framework what this Court has identified as "considerable tension" between lines of Court of Chancery and Supreme Court authority.[134]

Both the Chancery Court and the Supreme Court denied the two motions for interlocutory appeal. At the same time, Cohen challenged the Chancery Court's decision on the basis that, by recognizing a direct claim against Cohen that had not been asserted in the complaint, it misapplied the applicable pleading standards. The Chancery Court subsequently issued a memorandum opinion stating that "[t]here are no claims currently pending against Cohen or Madison Park."[135] The case settled before the issues could be fully resolved.[136]

Subsequently, several other Delaware decisions, relying in part on *EZCORP*, concluded both that entire fairness review was triggered by a

134 Thomas C. Roberts' Application for Certification of Interlocutory Appeal and Joinder in Phillip Ean Cohen, MS Pawn Corp. and MS Pawn L.P.'s Application for Certification of Interlocutory Appeal at 1, *In re* EZCORP Inc. Consulting Agreement Derivative Litig., C.A. No. 9962-VCL, 2016 WL 469590 (Del. Ch. Feb. 3, 2016).

135 *In re* EZCORP Inc. Consulting Agreement Derivative Litig., C.A. No. 9962-VCL, 2016 WL 727771, at *2 (Del. Ch. Feb. 23, 2016).

136 *See* Dave Simpson, *EZCorp. Investors Seek OK For $6.45M Del. Suit Settlement*, LAW360 (Mar. 5, 2018), https://www.law360.com/articles/1018598/ezcorp-investors-seek-ok-for-6-45m-del-suit-settlement [https://perma.cc/4E8Y-XLQ3] (describing a settlement proposal). The arguments in the *Match* case involved supplemental briefing on the place of *EZCORP* within Delaware jurisprudence. In *Match*, the appellants argued that "*Ezcorp* also ignored the decisions making clear that *Lynch*'s inherent coercion concept was confined to squeeze-outs." *See* Supplemental Opening Brief of the IAC Defendants at 27, *In re* Match Grp., Inc. Derivative Litig., 315 A.3d 446 (Del. 2024) (C.A. No. 2020-0505-MTZ), ID No. 70364115 [hereinafter IAC Supplemental Opening Brief]. They also argued that

> *Ezcorp* cited, but gave no weight to the decisions of then-Vice Chancellor Berger in *Canal*, Chancellor Chandler in *Tyson*, and Vice Chancellor Noble in *Dolan*, finding that each had somehow failed to appreciate that the concept of inherent coercion rendered the traditional approach to controller conflict transactions improper. *Ezcorp* gave more respectful treatment to this Court's *Aronson* decision, but ultimately determined not to follow it—finding it to have been an improvident departure from the general concept of inherent coercion, and incompatible with the *MFW* creep that *Ezcorp* created.

Id. at 27-28.

conflicted controlling shareholder transaction outside the freeze-out context and that such review could only be avoided by compliance with the *MFW* procedures.[137] For example, in *IRA Trust FBO Bobbie Ahmed v. Crane*,[138] Chancellor Bouchard, ruling two years after *EZCORP*, found that a reclassification implemented through a charter amendment required application of the entire fairness standard and that, to avoid entire fairness review, the *MFW* framework was required.[139] The majority control shareholder, NRG, had proposed "that Yield undertake a recapitalization where Class A stockholders would be issued one share of a new class of non-voting common stock for each Class A share they held. NRG intended for Yield to use the non-voting common stock as currency to acquire assets in the future."[140] According to the opinion, this action was undertaken at the behest of NRG to perpetuate NRG's voting control.[141] The court held that the transaction implicated controlling shareholder fiduciary duties and entire fairness review even though it involved a pro-rata distribution of the non-voting stock, explaining that "NRG received a uniquely valuable or 'non-ratable' benefit in connection with the Reclassification that was not shared with the Company's other stockholders, namely the ability to perpetuate its majority control over Yield."[142] The court further cited *EZCORP* for the proposition that "numerous types of transactions involving controlling stockholders outside the context of a merger or acquisition . . . have triggered entire fairness review."[143]

The court stated that it could "see no principled basis on which to conclude that the dual protections in the *MFW* framework should apply to squeeze-out mergers but not to other forms of controller transactions."[144] Because the transaction had been conditioned on and approved by a majority of the minority of shareholders and by a special committee of directors, however, the court found that the requirements of *MFW* had been met and dismissed the complaint.[145]

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137 *See* Alex Lindsey, Note, *Expanding MFW: Delaware Law Should Offer a Business Judgment Rule Safe Harbor for All Conflicted Controller Transactions*, 29 FORDHAM J. CORP. & FIN. L. 339, 343, 356-58 (describing three categories of "MFW creep"); *see also* IRA Tr. FBO Bobbie Ahmed v. Crane, C.A. No. 12742-CB, 2017 WL 6335912, at *6-7 (Del. Ch. Dec. 11, 2017) (identifying several types of conflicted controller transactions that trigger entire fairness analysis).

138 *Crane*, 2017 WL 6335912.

139 *Id.* at *7, 9, 11-12.

140 *Id.* at *1.

141 *Id.*

142 *Id.* at *7.

143 *Id.*

144 *Id.* at *11.

145 *Id.* at *4-5, 21.

In addition to relying on *EZCORP*, Chancellor Bouchard cited a decision by Vice Chancellor Slights in *In re Martha Stewart Living Omnimedia, Inc. Stockholder Litigation*.[146] In that decision, plaintiffs challenged a merger of Martha Stewart Living with a third-party corporation, asserting a breach of fiduciary duty claim against Martha Stewart herself and claiming that "she leveraged her position as controller to secure greater consideration for herself than was paid to the other stockholders."[147] The court acknowledged that prior cases had not addressed whether the *MFW* framework applied to a transaction in which, unlike a freeze-out, a controlling shareholder is a seller only.[148] While the court held that *MFW* would apply in the situation where "it is well-pled that the controller, as seller, engaged in a conflicted transaction by wrongfully diverting to herself merger consideration that otherwise would have been paid to all stockholders,"[149] it held that the allegations were not well-pled and that the *MFW* standard was met anyway.[150]

Similarly, in *Palkon v. Maffei (TripAdvisor)*, Vice Chancellor Laster concluded that entire fairness applied to TripAdvisor's decision to move its state of incorporation from Delaware to Nevada.[151] Plaintiffs alleged that the reincorporation was an effort by the controlling shareholder, Greg Maffei, and the defendant directors to secure the greater litigation protection afforded to corporate fiduciaries by Nevada law.[152] The court agreed: "The reduction in the unaffiliated stockholders' litigation rights inures to the benefit of the stockholder controller and the directors. That means the conversion confers a non-ratable benefit on the stockholder controller and the directors, triggering entire fairness."[153]

Notably, *TripAdvisor* appeared to expand the scope of unique benefit beyond quantifiable economic consideration, holding that the unique benefit was protection from litigation for the controlling shareholder and a reduction in the litigation rights of the minority shareholders.[154] The implications of

146 C.A. No. 11202-VCS, 2017 WL 3568089 (Del. Ch. Aug. 18, 2017).

147 *Id.* at *1-2.

148 *Id.* The court explicitly stated that it "disagree[d] with Stewart that the risks and incentives differ significantly as between two-sided controller transactions and one-sided controller transactions where the controller is alleged to have competed with the minority for consideration." *Id.* at *17.

149 *Id.* at *18.

150 *Id.* at *25.

151 311 A.3d 255, 261 (Del. Ch. 2024).

152 *Id.*

153 *Id.*

154 *Id.* at 283-84. The decision appears to leave open the scope of the benefit to the controller necessary to trigger entire fairness. Historically cases viewed this issue as one in which the controller receives a "benefit" and there is an "expense" to the minority. However, *TripAdvisor* opens the door to arguments that any controller benefit triggers entire fairness review whether or not there is any detriment to the minority. We believe this issue is likely to be litigated heavily in coming years.

TripAdvisor are uncertain at the time of the writing of this Article, as the case is still pending and, in a rare move, the Delaware Supreme Court granted the defendants' motion for an interlocutory appeal.[155] Assuming the Delaware Supreme Court upholds the *TripAdvisor* rule, any transaction going forward in which the controller obtained a benefit (quantifiable or otherwise) would be subject to entire fairness review unless the transaction applied *MFW* cleansing mechanisms.

Perhaps the most significant application of controlling shareholder fiduciary duties took place in *In re Sears Hometown & Outlet Stores, Inc. Stockholder Litigation*, decided a month before *TripAdvisor*.[156] *Sears Hometown* involved the controlling shareholder of Sears, Eddie Lampert.[157] When the board of Sears endorsed a plan to liquidate the business, Lampert, who believed that the plan would destroy value, voted to implement measures to block the liquidation plan, including electing new directors and enacting bylaws that would make the adoption of the liquidation plan more difficult.[158] Although plaintiffs did not allege that Lampert dominated the board or received a non-ratable benefit, the court nonetheless interpreted the cases we discuss in Part I to hold that Lampert owed a fiduciary duty to the minority shareholders in connection with the exercise of his voting power as a shareholder.[159] Moreover, the court explained that this fiduciary duty included both a duty of loyalty and a duty of care on a modified basis.[160] As the court explained:

> [W]hen exercising voting power affirmatively to change the status quo, a controlling stockholder owes a fiduciary duty of loyalty which requires that the controller not intentionally harm the corporation or its minority stockholders, plus a fiduciary duty of care that requires that the controller not harm the corporation or its minority stockholders through grossly negligent action.[161]

Accordingly, the court applied heightened scrutiny (although not entire fairness) to Lampert's exercise of his voting rights but concluded that Lampert acted reasonably and found no breach of fiduciary duty.[162]

155 *Palkon*, 311 A.3d, *interlocutory appeal accepted*, No. 125,2024, Docket Entry No. 5 (Del. Apr. 16, 2024).

156 309 A.3d 474 (Del. Ch. 2024).

157 *Id.* at 486.

158 *Id.* at 483.

159 *Id.* at 512.

160 *Id.*

161 *Id.*

162 *Id.* at 516-19.

These cases—culminating in *Sears Hometown*—broaden the scope of corporate transactions in which Delaware courts have applied fiduciary principles to scrutinize the role of a controlling shareholder.[163] Significantly, the use of fiduciary principles goes beyond the direct holdings of *Frantz* and *Hollinger* which, although applying equitable scrutiny to controller actions, did not hold that those actions were fiduciary in nature such that entire fairness applied.[164] Critically, we believe that the application of fiduciary principles is in theoretical tension with prior Delaware precedent, which recognized that a controller can act selfishly in its individual capacity, including by obtaining a premium for sale of its shares that is not paid to a minority.[165] Thus, *Sears Hometown* marks the dam breaking—the application of fiduciary duties to controlling shareholders when they exercise their individual shareholder rights.[166]

The foregoing series of decisions reflects a marked trend in the Delaware courts, though it was initially confined to the Chancery Court. Notably, several of these decisions were made at the motion to dismiss stage rather than after a trial.

The Delaware Supreme Court validated this trend in the spring of 2024 in *Match*.[167] After requesting supplemental briefing on the questions of whether entire fairness analysis applies to transactions outside the merger context and whether such transactions can only be cleansed through use of the *MFW* procedures,[168] the court confirmed that when a controller was

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163 *See also, e.g.*, Berteau v. Glazek, C.A. No. 2020-0873-PAF, 2021 WL 2711678, at *12-15 (Del. Ch. June 30, 2021) (applying entire fairness to a merger transacted by a controlling shareholder); Knight v. Miller, C.A. No. 2021-0581-SG, 2022 WL 1233370, at *10 (Del. Ch. Apr. 27, 2022) ("[E]ntire fairness applies to transactions whereby [controlling shareholders] receive a non-ratable benefit.").

164 Frantz Mfg. Co. v. EAC Indus., 501 A.2d 401, 408-09 (Del. 1985); Hollinger Int'l, Inc. v. Black, 844 A.2d 1022, 1060-78 (Del. Ch. 2004).

165 *See* Cheff v. Mathes, 199 A.2d 548, 555 (Del. 1964) ("[I]t is elementary that a holder of a substantial number of shares would expect to receive the control premium as part of his selling price."); Mendel v. Carroll, 651 A.2d 297, 305 (Del. Ch. 1994) ("The law has acknowledged, albeit in a guarded and complex way, the legitimacy of the acceptance by controlling shareholders of a control premium.").

166 *See* Hamermesh, Jacobs & Strine, *supra* note 31, at 325 (arguing that the extension of entire fairness review to transactions where a fiduciary receives an additional benefit is "a context where it does not fit"). While it is not clear from the decision itself, *Sears Hometown* implies that these fiduciary duties apply to any exercise of a controller's voting control even if there is no disagreement with the board. *See* 309 A.3d at 505. However, as one practitioner has noted to us, there is little reason to subject the controller's actions to heightened scrutiny if they are consistent with board decisions that are protected by the business judgment rule such as the implementation of governance changes or operational decisions.

167 *In re* Match Grp. Derivative Litig., 315 A.3d 446 (Del. 2024).

168 Michael D. Blanchard, Jody C. Barillare & Brian Loughnane, *Delaware Reconsiders Scope of the MFW Doctrine in Match.com Case*, MORGAN LEWIS LAWFLASH (Dec. 13, 2023), https://www.morganlewis.com/pubs/2023/12/delaware-reconsiders-scope-of-the-mfw-doctrine-in-matchcom-case [https://perma.cc/V3X2-WBXP].

involved, the application of entire fairness review was not limited to freeze-outs or similar transactions. Citing its decisions in the *Lynch* and *Tremont* line of cases, the court explained:

> Even in non-freeze out transactions . . . [t]he underlying factors which raise the specter of impropriety can never be completely eradicated and still require careful judicial scrutiny. This policy reflects the reality that in a transaction such as the one considered in this appeal, the controlling shareholder will continue to dominate the company regardless of the outcome of the transaction. The risk is thus created that those who pass upon the propriety of the transaction might perceive that disapproval may result in retaliation by the controlling shareholder.[169]

The court further explained that, in all such transactions, the defendant was required to satisfy *MFW*'s requirements "to change the standard of review to business judgment."[170] The court stated that *MFW* was applicable outside the freeze-out context because it "[could not] find any statement in *MFW* that distances our law in any transactional setting from the inherent coercion described in *Lynch*."[171]

In *Match*, the non-ratable benefit was the result of a spin-off transaction.[172] The court analyzed neither whether such benefit was at the expense of the minority nor if there was domination in the transaction itself. The court did, however, acknowledge that entire fairness review would not apply when "the controlling stockholders received the same benefit as other stockholders."[173] The court also rejected the defendants' claims that market mechanisms were sufficient in this context, citing *Lynch* and *Tremont II*.[174]

Appellants heatedly disputed this seeming extension of *Lynch* and *Tremont II* to all controller transactions, arguing in supplemental briefing that the inherent coercion view of the *Tremont* cases was contradicted by other Delaware precedents (discussed in Part I of this Article).[175] Further, they argued that this view would have been opposed by Chancellor Allen, the lower court judge, in the *Tremont* cases itself, citing an influential article coauthored by Chancellor Allen after his decision in *Tremont I* in which he argued for providing "full cleansing effect" to a controller squeeze-out

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169 *Match*, 315 A.3d at 464-65 (quoting Kahn v. Tremont Corp. (Tremont II), 694 A.2d 422, 428 (Del. 1997)).

170 *Id.* at 471.

171 *Id.* at 467.

172 *Id.* at 451.

173 *Id.* at 467.

174 *Id.* at 468 (discussing *Tremont II*, 694 A.2d at 428, and *Kahn v. Lynch Commc'n Sys.*, 638 A.2d 1110 (Del. 1994)).

175 IAC Supplemental Opening Brief, *supra* note 136, at 17-23.

conditioned on approval by a majority of the minority stockholders or approval by independent directors.[176]

Match further rejected the proposition that the independence of a majority of committee members was sufficient to meet the requirements of *MFW*. Notably, the court so held even in the absence of allegations that the controlling shareholder dominated the committee.[177] Because the court found one of the three committee members was not independent, it concluded that Match had failed to satisfy the *MFW* standard and entire fairness review was required.[178]

In sum, the current state of play is heavy judicial scrutiny of decisions by corporations with a controlling shareholder.[179] A controlling shareholder may be viewed as owing fiduciary duties to the corporation even when acting solely in its capacity as a shareholder. Decisions in which the shareholder has received a non-ratable benefit (even decisions in which that benefit does not come at the expense of the minority shareholders) will be subject to entire fairness review absent compliance with the *MFW* procedures. Further, the courts have made *MFW* compliance more difficult by imposing a demanding standard of independence for the special committee.[180] Most importantly, as we discuss in the next Section, the potential universe of corporations with a controlling shareholder has arguably expanded.

B. *Extending Who Is a Controller*

At the same time as Delaware courts have applied fiduciary duties and entire fairness review to a broader range of transactions, they have extended the concept of a controlling shareholder to encompass elements of what we term "new" control. To be sure, the increased use of dual class structures

176 *Id.* at 30 (citing Allen, Jacobs & Strine, *supra* note 29, at 1306-09, 1306 n.75). According to the appellants, the article further "explained why real-world market evidence exposed inherent coercion as an untenable concept and demonstrated that the traditional approach's deference to decisions made by independent directors and disinterested stockholders is wise policy." *Id.*

177 *Match*, 315 A.3d at 472 ("[T]he plaintiffs did not plead that [the non-independent committee member] 'dominated' or 'infected' the Committee's decision-making process.").

178 *Id.* at 473. The Chancery Court held that it was only necessary that a majority of the committee be independent and found that it was. *Id.* Both courts agreed, however, that one of the committee members was not independent because of his "longstanding business affiliations" with the controlling shareholder. *Id.*

179 *See generally* J. Travis Laster, *The Distinctive Fiduciary Duties That Stockholder Controllers Owe*, 20 N.Y.U. J.L. & BUS. 461 (2024) (reviewing the state of play).

180 We note that the courts' analysis of director independence in the context of *MFW* appears to be more demanding than that applied in the demand context, although a full analysis of this issue is beyond the scope of this Article. *See, e.g.*, United Food & Com. Workers Union v. Zuckerberg, 262 A.3d 1034, 1060-61 (Del. 2021) (considering and rejecting challenges to directors' independence at Facebook in the demand context despite controlling shareholder Mark Zuckerberg's power to elect the board).

created a new category of controlling shareholders who did not hold a majority economic interest.[181] Dual class structures have the potential to reduce the beneficial features of concentrated control because a disparity between voting and economic rights heightens the risk of controller self-dealing.[182] Nonetheless, Delaware doctrine can easily accommodate the proposition that control should be premised on a shareholder's voting power rather than economic ownership. As a result, the courts have readily characterized such shareholders as controlling without extensive analysis.[183]

The broader extension of fiduciary duties to shareholders holding significantly lower stakes came hesitantly. In the *SolarCity* litigation, plaintiffs argued that Elon Musk, who owned 22.1% of Tesla's stock at the time, should be treated as a controlling shareholder.[184] Addressing the issue in the context of a motion to dismiss, Vice Chancellor Slights concluded that the complaint had alleged sufficient facts to make it "reasonably conceivable" that Musk was a controlling shareholder.[185] Although Musk's ownership stake was "relatively low," the court explained that "there is no absolute percentage of voting power that is required in order for there to be a finding that a controlling stockholder exists."[186]

In agreeing with the proposition that a 22.1% interest could be sufficient to render Musk a controlling shareholder, the court cited a number of earlier

181 Dual class structures are designed to provide a shareholder with voting control despite a lack of majority economic interest. As such, dual class structures present distinctive risks of opportunistic behavior. At the same time, market practices suggest that investors voluntarily invest in companies with dual class structures and perceive some benefits to doing so. *See, e.g.*, Ahn, Fisch, Patatoukas & Solomon, *supra* note 46, at 514. The ability to exercise control through high-vote stock means that a controlling shareholder influences a variety of corporate decisions—from election of directors to adopting bylaws—solely in its capacity as a shareholder. Dual class structures also involve, in some cases, particularized governance issues such as equal treatment provisions and sunset extensions. *See, e.g.*, Caley Petrucci, *Equal Treatment Agreements: Theory, Evidence & Policy*, 40 YALE J. ON REGUL. 620 (2023) (discussing equal treatment provisions); David J. Berger, Jill Fisch & Steven Davidoff Solomon, *Extending Dual-Class Stock: A Proposal*, 25 THEORETICAL INQUIRIES L. 23 (2024) (discussing sunset extensions). The extent to which a high-vote shareholder's power is a bargained-for feature of a dual class structure or warrants heightened judicial scrutiny raises distinctive questions, some of which extend beyond the scope of this Article.

182 *See, e.g.*, Lucian A. Bebchuk & Kobi Kastiel, *The Perils of Small-Minority Controllers*, 107 GEO. L.J. 1453, 1465-66 (2019) (discussing how dual class structures enable shareholders to exercise control despite owning "a small minority of the company's equity").

183 *See, e.g.*, *In re* EZCORP Inc. Consulting Agreement Derivative Litig., C.A. No. 9962-VCL, 2016 WL 301245, at *9 (Del Ch. Jan. 25, 2016) ("Delaware corporate decisions consistently have looked to who wields control in substance.").

184 *In re* Tesla Motors, Inc. S'holder Litig. (SolarCity), C.A. No. 12711-VCS, 2018 WL 1560293, at *2 (Del. Ch. Mar. 28, 2018).

185 *Id.* at *1.

186 *Id.* at *14 (quoting *In re* PNB Holding Co. S'holders Litig., No. Civ. A. 28-N, 2006 WL 2403999, at *9 (Del. Ch. Aug. 18, 2006), and comparing the decision with *In re* Zhongpin Inc. S'holders Litig., C.A. No. 7393-VCN, 2014 WL 6735457, at *1, *12 (Del. Ch. Nov. 26, 2014) (finding that a 17.3% shareholder could be reasonably viewed as a "controller")).

decisions in which plaintiffs alleged that shareholders with similarly sized blocks should be treated as controlling shareholders.[187] Notably, although courts in some of these cases accepted those allegations at the motion to dismiss stage, the decisions did not ultimately resolve the issue.[188] Thus, in 2016, the court concluded in *In re PNB Holding Co. Shareholders Litigation* that, where a group of officers and directors collectively held 33.5% of the company's stock, they should not be treated as a controlling group. As the court explained, "[f]or starters, even taken together, the directors and officers of PNB did not control a majority of the company's voting power."[189] In addition, although recognizing that the law allowed a court to

> impose fiduciary obligations on stockholders who, although lacking a clear majority, have such formidable voting and managerial power that they, as a practical matter, are no differently situated than if they had majority voting control, [that] test is not an easy one to satisfy and stockholders with very potent clout have been deemed, in thoughtful decisions, to fall short of the mark.[190]

Similarly, after reviewing a range of cases involving allegations that a minority blockholder should be treated as controlling, the court in 2014 in *In re Crimson Exploration Inc. Stockholder Litigation* explained that "the scatter-plot nature of the holdings highlights the importance and fact-intensive nature of the actual control factor."[191] The court then explained that prior cases required a plaintiff to show actual domination by a large blockholder for the court to accept the categorization of controlling shareholder.[192] The court noted that "[a]bsent a significant showing [of domination] such as was made in these prior cases, the courts have been reluctant to apply the label of controlling stockholder—potentially triggering fiduciary duties—to large, but minority, blockholders."[193] And in *Skye Mineral Investors, LLC v. DXS Capital (U.S.) Ltd.*, the court, again at the motion to dismiss stage, accepted the premise that defendants could be controlling shareholders on the basis of being non-majority shareholders with blocking rights.[194] As the court explained, however, although mere blocking rights would not likely be

187 *Id.* at *14 n.220.

188 *See* Larkin v. Shah, C.A. No. 10918-VCS, 2016 WL 4485447, at *2 (Del. Ch. Aug. 25, 2016) (finding that a 23.1% minority stockholder was not a controlling stockholder).

189 *PNB Holding*, 2006 WL 2403999, at *9.

190 *Id.*

191 *In re* Crimson Expl. Inc. S'holder Litig., C.A. No. 85141-VCP, 2014 WL 5449419, at *10 (Del. Ch. Feb. 25, 2014).

192 *Id.* at *12.

193 *Id.*

194 Skye Min. Invs., LLC v. DXS Cap. (U.S.) Ltd., C.A. No. 2018-0059-JRS, 2020 WL 881544, at *1 (Del. Ch. Feb. 24, 2020).

sufficient to support an allegation of control, the plaintiffs alleged that the blocking rights both gave defendants "the unilateral power to shut [the company] down—full stop" and that the defendants actually exercised those rights.[195]

In *SolarCity*, Vice Chancellor Slights concluded that the issue of "[w]hether a large blockholder is so powerful as to have obtained the status of a 'controlling stockholder' is intensely factual [and] it is a difficult [question] to resolve on the pleadings."[196] The court noted that plaintiffs identified several factors in addition to Musk's stock ownership, including

> (1) Musk's ability to influence the stockholder vote to effect significant change at Tesla, including the removal of Board members; (2) Musk's influence over the Board as Tesla's visionary, CEO and Chairman of the Board; (3) Musk's strong connections with members of the Tesla Board and the fact that a majority of the Tesla Board was "interested," as that term is defined in our law, in the Acquisition; and (4) Tesla's and Musk's acknowledgment of Musk's control in its public filings.[197]

It concluded that these allegations were sufficient to survive a motion to dismiss. Ultimately, the court never resolved the question of whether Musk was a controlling shareholder at trial, deciding instead that the transaction was entirely fair.[198]

Like *SolarCity*, *Tornetta* involved allegations against Elon Musk in his capacity as controlling shareholder of Tesla.[199] In *Tornetta*, the plaintiff-shareholder class challenged Musk's enormous $55.8 billion pay package.[200] This package had been approved by the purportedly non-independent directors as well as by stockholders.[201] Additionally, its size was based on Musk increasing the value of Tesla by $600 billion.[202]

Chancellor McCormick began the opinion in *Tornetta* by observing that Musk's status as a controlling shareholder had been *raised*, but not decided, in the *SolarCity* litigation.[203] The Chancellor then concluded that it was now

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195 *Id.* at *27.

196 *In re* Tesla Motors, Inc. S'holder Litig. (SolarCity), C.A. No. 12711-VCS, 2018 WL 1560293, at *13 (Del. Ch. Mar. 28, 2018).

197 *Id.*

198 *In re* Tesla Motors, Inc. S'holder Litig. (SolarCity), C.A. No. 12711-VCS, 2022 WL 1237185 (Del. Ch. Apr. 27, 2022), *aff'd*, 298 A.3d 667 (Del. 2023).

199 Tornetta v. Musk, 310 A.3d 430, 445 (Del. Ch. 2024) ("[T]o invoke the entire fairness standard, the plaintiff argues that Musk's compensation plan was a conflicted-controller transaction. The plaintiff thus forces the question: Does Musk control Tesla?").

200 *Id.*

201 *Id.* at 446.

202 *Id.* at 447.

203 *Id.* at 501.

appropriate to decide the issue, remarking that "[t]his question of whether Musk controls Tesla has thus proven evasive. It is as good a time as any to run it to ground."[204]

The Chancellor explained that the analysis of control was pragmatic and required a plaintiff to show that a controlling shareholder was similarly situated to one that had majority voting control. She then explained that this inquiry required an analysis of whether a stockholder could exercise what she termed "effective control" based on factors that include: (1) "ownership of a significant equity stake (albeit less than a majority)," (2) "the right to designate directors (albeit less than a majority)," (3) "decisional rules in governing documents that enhance the power of a minority stockholder or board-level position," and (4) "the ability to exercise outsized influence in the board room, such as through high-status roles like CEO, Chairman, or founder."[205]

Chancellor McCormick also distinguished between general control and transactional control, reasoning that control could be operational in a specific transaction.[206] She stated:

> To establish transaction-specific control, a plaintiff must show that the stockholder "exercise[d] actual control over the board of directors during the course of a particular transaction[.]" This analysis often focuses on relationships "with key managers or advisors who play a critical role in presenting options, providing information, and making recommendations[.]" It can also address "the exercise of contractual rights to channel the corporation into a particular outcome by blocking or restricting other paths," and "commercial relationships," although those factors are less relevant here. Ultimately, "[i]t is impossible to identify or foresee all of the possible sources

204 *Id.* at 502.

205 *Id.* at 500.

206 *Id.* The concept of transaction-specific control, which suggests that the decision of whether a shareholder controls a corporation may vary depending on the transaction at issue, appears to have its origins in *In re Western National Corp. Shareholders Litigation*, in which the court stated that

> a significant stockholder that does not, as a general matter, exercise actual control over the investee's business and affairs or over the investee's board of directors but does, in fact, exercise actual control over the board of directors during the course of a particular transaction, can assume fiduciary duties for purposes of that transaction.

C.A. No. 15927, 2000 WL 710192, at *20 (Del. Ch. May 22, 2000); *see also* Elizabeth Pollman & Lori W. Will, *The Lost History of Transaction-Specific Control*, 50 J. CORP. L. (forthcoming 2025). Rather than recognizing the existence of transaction-specific control in that instance, however, the decision rejected the proposition that a forty-six percent shareholder had transaction-specific or general control based solely on its voting power. *Western Nat'l*, 2000 WL 710192, at *25. Similarly, the court refused to apply fiduciary principles to the defendant's exercise of that power. As the court explained, the alleged controller's "exercise of its statutory rights as a stockholder to oppose a merger . . . is of no legal consequence." *Id.* at *8.

of influence that could contribute to a finding of actual control over a particular decision."[207]

The Chancellor noted that this was a fact-specific inquiry, stating: "[b]oth general control and transaction-specific control call for a holistic evaluation of sources of influence."[208]

In conducting this holistic evaluation, the *Tornetta* opinion drew heavily on the concept of a "superstar CEO."[209] The court explained that "CEO superstardom is relevant to controller status because the belief in the CEO's *singular* importance shifts the balance of power between management, the board, and the stockholders."[210] Based on a comprehensive analysis of Musk's ties, the court found he had transactional control, stating:

> The collection of features characterizing Musk's relationship with Tesla and its directors gave him enormous influence over Tesla. In addition to his 21.9% equity stake, Musk was the paradigmatic "Superstar CEO," who held some of the most influential corporate positions (CEO, Chair, and founder), enjoyed thick ties with the directors tasked with negotiating on behalf of Tesla, and dominated the process that led to board approval of his compensation plan. At least as to this transaction, Musk controlled Tesla.[211]

Chancellor McCormick then found that Tesla had not satisfied *MFW* because (1) the compensation package was not approved by truly disinterested directors, and (2) the shareholder vote was not fully informed. As a result, the Chancellor held that she was required to apply entire fairness review to Musk's compensation package. With respect to the process, the Chancellor gave great weight to the fact that, in her words, the option grant was not the product of arms-length negotiations. Drawing from the freeze-out cases, the court stated that "[t]he lack of arm's-length negotiations can overshadow positive aspects of a process."[212] Fair process in a conflicted merger, however, is designed to replicate the negotiations that would take place between independent third parties. In contrast, no negotiation of CEO pay can fairly

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207 Tornetta v. Musk, 310 A.3d 430, 500 (Del. Ch. 2024) (citations omitted).

208 *Id.*

209 The court cited a law review article, Assaf Hamdani & Kobi Kastiel, *Superstar CEOs and Corporate Law*, 100 WASH. U. L. REV. 1353 (2023), which developed the concept of a superstar CEO to explain why such CEOs enjoy substantial influence over corporate decisions but warned that "turning the elusive notion of a superstar CEO into a legal test for control will be costly." *Id.* at 1400.

210 *Tornetta*, 310 A.3d. at 507.

211 *Id.* at 446.

212 *Id.* at 529-30.

be described as an arms-length process, especially when it involves an incumbent CEO.[213]

The court also stressed the sheer magnitude of the compensation package.[214] As the court explained:

> There is no absolute limit on the magnitude of a compensation grant that could be considered fair. But "[p]rocess can infect price." And "where the pricing terms of a transaction that is the product of an unfair process cannot be justified by reference to reliable markets or by comparison to substantial and dependable precedent transactions, the burden of persuading the court of the fairness of the terms will be exceptionally difficult."[215]

Because Chancellor McCormick held that the defendants failed to satisfy their burden of showing that the compensation package was entirely fair, she ordered that the package be rescinded entirely.[216]

Tornetta represents yet another milestone in applying controlling shareholder status, after a full trial, to someone holding far less than a near majority of voting power. The opinion's analysis further suggests that its principles could be used to impose fiduciary duties on a wide array of individuals with limited stockholdings and whose potential influence over a corporation is not based on their voting power.[217] Indeed, as we discuss in the

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213 *See generally* LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION 23-44 (2004).

214 This aspect of the court's decision somewhat resembled the Supreme Court's decision in *Rogers v. Hill*, 289 U.S. 582 (1933), in which it invalidated the compensation package of executives at the American Tobacco Co. *See id.* at 591 (reasoning that even a stockholder vote cannot "be used to justify payments of sums as salaries so large as in substance and effect to amount to spoliation or waste of corporate property").

215 Tornetta v. Musk, 310 A.3d 430, 533 (Del. Ch. 2024) (citations omitted).

216 *Id.* at 544 ("The court orders rescission of the Grant as a remedy for Defendants' fiduciary breaches."). Courts and commentators have observed, however, that for a judge to determine when an executive pay package is reasonable is a fraught endeavor, and prior judicial skepticism of pay packages based on their size has been short-lived. *See, e.g.*, Harwell Wells, *"No Man Can be Worth $1,000,000 a Year": The Fight Over Executive Compensation in 1930s America*, 44 U. RICH. L. REV. 689, 730 (2010) (describing judicial retreat from the approach taken in *Rogers v. Hill* and explaining that this retreat can be explained, in part, by "judges' growing doubts about their ability to determine what constituted reasonable compensation"); Omari Scott Simmons, *Taking the Blue Pill: The Imponderable Impact of Executive Compensation Reform*, 62 SMU L. REV. 299, 339-40 (2009) ("The epic *Disney* litigation reflects this judicial reluctance to second guess executive compensation despite significant board dysfunction.").

217 We acknowledge that the extent to which other courts will base a finding of control on similar facts is unclear. In *Sciannella v. AstraZeneca UK Ltd.*, C.A. No. 2023-0125-PAF, 2024 WL 3327765 (Del. Ch. July 8, 2024), Vice Chancellor Fioravanti concluded that AstraZeneca was not a controlling shareholder of Viela despite the fact that AstraZeneca owned 26.72% of Viela stock, possessed various blocking rights, had placed its former executives in all five top positions at Viela, had successfully obtained board representation, and had relationships with other Viela directors. *Id.* at *16-17.

next Part, the expansion of controlling shareholder status to those who exercise power over a corporation—what might be termed "soft control"—can similarly be extended even to those who own no stock at all.

Thus, we have identified a series of decisions that, over time, mark a sea change in Delaware doctrine on the fiduciary obligations of controlling shareholders, the standard applicable to controllers who engage in actions vis-à-vis the corporation, and the concept of control itself. Together, they mark an expansion with significant implications not just for what is now termed a controlling shareholder but also for companies and corporate transactions generally. We discuss these implications in the next Part.

III. THE IMPLICATIONS OF THE CURRENT APPROACH

In this Part we analyze key implications of the current Delaware approach. The full scope of this approach has yet to be judicially fleshed out, at least in terms of its implementation. Moreover, practitioners are still adjusting to the impact of these recent decisions, and we expect the practices involving the use of *MFW* procedures, for example, will continue to evolve. Nonetheless, we believe that the implications we outline below are substantial.

A. *The Line-Drawing Question*

Tornetta reflects a trend by the courts to treat those who exercise influence over corporate decisions as controlling shareholders even when they hold far less than a majority of the corporation's voting power. *Sears Homeland* intensifies the impact of this approach by extending the application of fiduciary principles (albeit at a reduced level) even when a shareholder is acting solely in its shareholder role. The resulting judicial scrutiny of a range of corporate decisions is in tension with the traditional deference of the business judgment rule.

Our reading of the history suggests that the traditional determination of whether someone was a controlling shareholder was both objective and binary. It was objective in the sense that it required a shareholder to control a majority or near majority of voting power. It was binary in the sense that a shareholder either *was* or *was not* a controlling shareholder rather than being considered a controlling shareholder for some purposes and not others.[218] As

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[218] *See, e.g.*, Siegel, *supra* note 63, at 38-39 ("Once a court determines that a minority shareholder is a controlling shareholder, the courts have not differentiated between those that control because they are minority shareholders who have dominated the transaction and those who control because they own a majority of stock. . . . The courts either have not recognized or have not found the distinctions significant between being a majority shareholder and being a dominating minority shareholder.").

detailed in Section III.C below, these doctrinal features are critically important in that they affect the ability of corporations to plan their decisions and to determine ex ante the procedural requirements that apply.

Tornetta and the cases on which it relies shift the analysis from voting control to domination, soft power, or even the capacity to influence. They also suggest that control can be context- or transaction-specific, meaning that a shareholder's status depends on the amount of influence that it can or does exert in a specific situation. We term this approach "new" control to capture the types of control that do not depend on majority or near-majority stock ownership.

Tornetta offers an example of one type of soft control: the possession of a substantial minority block, which by itself would not give a shareholder the power to dictate voting outcomes, coupled with other types of soft power. As the *Tornetta* court explained, soft power can come from the shareholder's other roles in the company such as founder, CEO, or Chairman. Other courts have been even more expansive. Vice Chancellor Laster, for example, stated in *Voigt v. Metcalf*:

> Examples [of the sources of influence that could lead to a finding of actual control] include, but are not limited to, (i) relationships with particular directors, (ii) relationships with key managers or advisors, (iii) the exercise of contractual rights to channel the corporation into a particular outcome, and (iv) the existence of commercial relationships that provide the defendant with leverage over the corporation, such as status as a key customer or supplier.[219]

In contrast, as discussed above, older cases required both that a shareholder hold a majority or near majority of the corporation's voting power and that the shareholder dominate the corporate decisionmaking process before treating that shareholder as a fiduciary.[220] Domination continues to play a role in the "new" control cases, but courts vary in the extent to which they require actual domination. In *In re Oracle Corp. Derivative Litigation*, which involved a challenge to Oracle's acquisition of NetSuite, for example, the plaintiffs alleged that Larry Ellison was a controlling shareholder of Oracle.[221] At the time, Ellison owned thirty percent of Oracle's stock, which constituted the largest block. He was Oracle's founder and former CEO and, at the time of the acquisition, a director and Chief Technology Officer.

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219 Voigt v. Metcalf, C.A. No. 2018-0828-JTL, 2020 WL 614999, at *12 (Del. Ch. Feb. 10, 2020).

220 *See, e.g.*, Kahn v. Lynch Commc'n Sys., 638 A.2d 1110, 1114 (Del. 1994) ("For a dominating relationship to exist in the absence of controlling stock ownership, a plaintiff must allege domination by a minority shareholder though actual control of corporation conduct.").

221 *In re* Oracle Corp. Derivative Litig., C.A. No. 2017-0337-SG, 2023 WL 3408772, at *1 (Del. Ch. May 12, 2023).

According to the *Oracle* court, "[a] plaintiff must show that the alleged controlling stockholder *in actuality* dominated the corporate conduct, either generally or with respect to the transaction in question, to hold the stockholder to duties as a fiduciary."[222] Because the court concluded that Ellison had not dominated the transaction, it held that entire fairness review was not warranted.[223]

Oracle's requirement of actual domination appears to be the exception, however. More recent cases have taken a different approach, relying heavily on a shareholder's potential ability to influence corporate decisions—so-called inherent coercion—rather than allegations of actual domination.[224] As Vice Chancellor Laster explained in *Voigt*, for example, one means of pleading the requisite degree of control is to show that the defendant shareholder "as a practical matter, possesses a combination of stock voting power and managerial authority that enables him to control the corporation, if he so wishes."[225]

Part of the difference in approach may be the stage of the litigation. Delaware courts may require a lesser showing at the motion to dismiss stage. As a practical matter, however, denial of the motion to dismiss has tremendous implications in terms of the ongoing cost and burden of litigation. It is unsatisfying to accept a vague standard even at this stage with the implication that the question of whether the defendant exercised sufficient control can be sorted out later. Moreover, if actual domination is a requirement for a blockholder to be treated as a controlling shareholder, the plaintiff should be required to assert sufficient facts establishing such domination, and an inference that potential influence is sufficient to infer domination is problematic.[226]

A perhaps better explanation for the courts' expansive approach to control is the expanding protection of directors and officers from liability in connection with these transactions. DGCL section 102(b)(7) allows corporations to exculpate directors, and now officers, from liability for decisions that do not involve a breach of the duty of loyalty or a lack of good

222 *Id.* at *19.

223 We note that an appeal of the *Oracle* decision is pending.

224 *But see* Sciannella v. AstraZeneca UK Ltd., C.A. No. 2023-0125-PAF, 2024 WL 3327765, at *16-18 (Del. Ch. July 8, 2024) (holding that, where plaintiff alleges that a minority blockholder is a controlling shareholder, plaintiff's allegations of domination must involve actual rather than potential control).

225 Voigt v. Metcalf, C.A. No. 2018-0828-JTL, 2020 WL 614999, at *11 (Del. Ch. Feb. 10, 2020) (citing *In re* Cysive, Inc. S'holders Litig., 836 A.2d 531, 553 (Del. Ch. 2003)).

226 *See* Puma v. Marriott, 283 A.2d 693, 695-96 (Del. Ch. 1971) (granting a motion to dismiss where the complaint failed to allege that the Marriott family, which owned forty-six percent of the stock, dominated the independent directors).

faith.[227] *Cornerstone* authorizes courts to dismiss exculpated directors at the pleading stage.[228] Even when directors or officers allegedly act pursuant to a conflict of interest, their liability can be cleansed through a single step of an independent board committee or minority shareholder approval. As a result, minority shareholders alleging misconduct increasingly seek to impose liability on purportedly controlling shareholders. Indeed, perhaps recognizing the potential expansion of control concepts implicated by their pleadings, plaintiffs in several of the foregoing cases did not allege that shareholders were liable directly for a fiduciary breach but that they aided and abetted the board's breach of fiduciary duty.[229]

Moreover, the courts' reasoning conceivably extends the breadth of "new" control further. If controller status is based on influence, it is unclear why even a nominal shareholding is necessary. To be sure, in *Corwin*, the Delaware Supreme Court held that ownership of less than one percent of a company's stock, coupled with financial and contractual influence, was insufficient to make the defendant a controlling shareholder and thereby subject the transaction at issue to entire fairness analysis.[230] As a practical matter, however, corporate participants can exercise soft power over corporate decisions through a variety of mechanisms other than share ownership.

One example, drawing upon the analysis in *Tornetta*, would involve premising control on status as a superstar CEO alone.[231] As noted above, corporate law currently treats officers, even powerful ones, differently from controlling shareholders.[232] Officers can be protected through exculpatory charter provisions pursuant to DGCL section 102(b)(7), and officer conflicts can be cleansed through just a shareholder vote. Indeed, the historical antecedents of distinctive treatment for controlling shareholders are premised on the position that the potential influence of a controlling shareholder is somehow different. But if controlling shareholder status and the associated fiduciary duties are based partly on a shareholder's position as an officer, the distinction breaks down.

227 DEL. CODE ANN. tit. 8, § 102(b)(7) (2024).

228 *In re* Cornerstone Therapeutics Inc., S'holder Litig., 115 A.3d 1173, 1187 (Del. 2015) ("[W]hen the plaintiffs have pled no facts to support an inference that any of the independent directors breached their duty of loyalty, fidelity to the purpose of Section 102(b)(7) requires dismissal of the complaint against those directors.").

229 We discuss this point further in note 328 and accompanying text.

230 Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304, 306-07 (Del. 2015).

231 *See, e.g.*, Hamdani & Kastiel, *supra* note 209, at 1367 (arguing that a superstar CEO's influence is not based on his stock ownership).

232 *See* Kahn v. M&F Worldwide Corp. (MFW), 88 A.3d 635, 648-49 (Del. 2014) (explaining traditional reluctance to defer to process protections of independent board and shareholder approval in controlling shareholder mergers).

It would also be plausible to argue that a defendant has sufficient influence over corporate actions solely on the basis of contractual rights to be treated as equivalent to a majority stockholder and therefore a controller under Delaware law.[233] Contracts can provide parties with control in several ways. Minority shareholders can agree to act collectively by voting their shares pursuant to a voting agreement.[234] Shareholders (and non-shareholders as well) can enter into contracts that afford them rights that would typically require a majority of voting power, such as the right to appoint or remove director candidates.[235] These shareholder agreements have become increasingly prevalent in large private-equity-backed or venture-capital-funded private companies but are also common in publicly traded companies.[236] Finally, shareholder agreements can authorize signatories to exercise powers typically exercised by the board, such as the power to implement operational decisions, select officers, or determine executive compensation.[237]

To the extent that contractual rights can provide signatories with equal or greater control over corporate decisions than majority shareholders, it is unclear why controlling shareholder status requires any stockholdings at all. Indeed, the plaintiffs in *Skye Mineral* asserted claims against defendants who held no shares in the company.[238] Although the court rejected the proposition that those defendants exercised actual control, it did not hold that stock ownership was required for someone to be a controller.[239] Moreover, with the passage of section 122(18) of the DGCL, there may be a significant expansion

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233 *See, e.g.*, *In re* Pattern Energy Grp. Inc. S'holders Litig., C.A. No. 2020-0357-MTZ, 2021 WL 1812674, at *1 (Del. Ch. May 6, 2021) ("Recognizing that neither the investor nor the supplier owned Company stock, I leave open the possibility that the plaintiff may establish the investor, supplier, and management stockholders formed a control group, given the investor's consent right and other pervasive sources of soft power over the Company and its sales process.")

234 *See* Hamermesh, Jacobs & Strine, *supra* note 31, at 346-48 (discussing judicial analysis of whether such arrangements should result in a group of shareholders being treated as a control group).

235 *See* Rauterberg, *supra* note 26, at 1144-46 (describing how shareholding agreements allow noncontrolling shareholders to exercise control over corporate governance.)

236 *See* Fisch, *supra* note 27, at 915-17 (describing the use of shareholder agreements by venture-backed startups as a governance tool); Rauterberg, *supra* note 26; Shobe & Shobe, *supra* note 21 ("[C]orporations commonly and increasingly grant insider shareholders disproportionate control . . . in separate contracts between the insiders and the company.").

237 *See, e.g.*, W. Palm Beach Firefighters' Pension Fund v. Moelis & Co., 311 A.3d 809, 817-23 (Del. Ch. 2024) (discussing and invalidating several such provisions); DEL. CODE ANN. tit. 8, § 122(18) (2024) (explicitly authorizing shareholder agreements that grant shareholders the power to exercise what would otherwise be within the board's statutory authority under § 141(a)).

238 Skye Min. Invs., LLC v. DXS Cap. (U.S.) Ltd., C.A. No. 2018-0059-JRS, 2020 WL 881544, at *26-28 (Del. Ch. Feb 24, 2020).

239 *See id.* at *27 ("Noronha, Michael Riady, Stephen Riady, and LCR owned *no* SMP units, appointed *none* of SMP's Board members and held *no* contractual blocking rights.").

of agreements that confer control rights upon parties that do not hold majority voting power.[240]

"New" control could also extend to other types of shareholder influence. A number of Chancery Court decisions have referenced DGCL section 203—Delaware's anti-takeover statute—and its twenty percent threshold as a possible determinant of control.[241] Activist investors, despite typically owning less than ten percent of the issuer's stock, are often successful in pressuring issuers to make decisions that are favorable to the activist.[242] The determination that an investor with even a five percent stake has the potential to affect control is the basis for the requirement that investors acquiring such a stake publicly disclose their holdings pursuant to SEC rule 13D.[243] Engine No. 1, for example, ran a successful proxy contest in which it was able to secure board representation at Exxon—representation that the activist promised to use to cut Exxon's investment in oil and gas projects.[244] This influence led Iman Anabtawi and Lynn Stout to argue that activists should be treated as controlling shareholders and subject to fiduciary duties.[245] Although

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240 DEL. CODE ANN. tit. 8, § 122(18) (2024). Significantly, the statute does not require the recipient of contractual control rights to be a current shareholder.

241 *See, e.g.,* Tornetta v. Musk, 310 A.3d 430, 503 (Del. Ch. 2024) (citing section 203 to support the conclusion that a twenty percent holding can suffice for control); see also DEL. CODE ANN. tit. 8, § 203(c)(4) (2024) ("A person who is the owner of 20% or more of the outstanding voting stock of any corporation, partnership, unincorporated association or other entity shall be presumed to have control of such entity, in the absence of proof by a preponderance of the evidence to the contrary . . . ."). Vice Chancellor Laster has also publicly argued that section 203 is an appropriate reference point for definition of control in the fiduciary context. *See* Travis Laster, *Wondering About "Control"? The General Assembly Already Defined It.*, LINKEDIN (Feb. 4, 2024), https://www.linkedin.com/pulse/wondering-control-general-assembly-already-defined-travis-laster-4czme [https://perma.cc/8278-ZSBB] ("People have been talking about 'control' for decades, and particularly since *MFW* and *Corwin* made 'control' a bigger deal. When someone asks me about 'control,' I have good news. The General Assembly already defined it. That definition appears in Section 203 of the DGCL, and it has two parts.").

242 *See, e.g.*, Pat Tucker, Garrett Muzikowski & Sean Lange, *What Settlement Data Says About the Evolution of Activism*, HARV. L. SCH. F. ON CORP. GOVERNANCE (July 15, 2024), https://corpgov.law.harvard.edu/2024/07/15/what-settlement-data-says-about-the-evolution-of-activism [https://perma.cc/995M-D4BD].

243 Similarly, the potential that the acquisition of non-majority block holdings can influence control has led corporations to adopt poison pills with increasingly low triggers. *See, e.g.*, Williams Cos. S'holders Litig., C.A. No. 2020-0707-KSJM, 2021 WL 754593, at *1 (Del. Ch. Feb. 26, 2021) (analyzing a poison pill with a five percent trigger threshold); Ofer Eldar, Tanja Kirmse & Michael D. Wittry, *The Rise of Anti-Activist Poison Pills* 2 (Eur. Corp. Governance Institute, Finance Working Paper No. 869, 2023) ("[P]oison pills in the last decade have substantially lower ownership triggers.").

244 *See* Anna Christie, *The Agency Costs of Sustainable Capitalism*, 55 U.C. DAVIS L. REV. 875, 924-25 (2021) (describing Engine No. 1's proxy campaign). According to Exxon, efforts to change the nature of its business in this way are contrary to the interests of other shareholders. Complaint at 2-4, Exxon Mobil Corp. v. Arjuna Cap., LLC (N.D. Tex. Jan. 21, 2024) (No. 4:24-cv-00069-P).

245 Iman Anabtawi & Lynn Stout, *Fiduciary Duties for Activist Shareholders*, 60 STAN. L. REV. 1255, 1260 (2008).

concededly, an activist cannot succeed in a proxy contest unless it obtains the support of other shareholders,[246] as Sarah Haan has documented, a substantial majority of activist campaigns result in settlements between the activist shareholder and the issuer.[247] In those settlements, the issuer may agree to provide the activist with board representation and to make other changes.[248] Importantly, these settlements are not subject to approval by the other shareholders, and they typically give the activist ongoing non-ratable benefits.[249]

Even non-activist shareholders could fall within the broad definition of controllers. Today, most shares of publicly traded companies are held by institutional investors, and a relatively small number of those investors dominate.[250] These institutions can exercise a considerable degree of influence over issuer policies.[251] Institutional-investor voting has been highly influential in causing issuers to adopt a variety of governance reforms and has extended to more controversial topics, including climate change and diversity, equity, and inclusion initiatives. One paper, for example, finds that the largest institutional investors had a significant impact on the number of women serving on corporate boards.[252] Significantly, issuers can often exercise this influence through behind-the-scenes engagement, which is less transparent than voting.[253] Some commentators argue that, because of the substantial

246 Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 113 COLUM. L. REV. 863, 899 (2013).

247 Sarah C. Haan, *Shareholder Proposal Settlements and the Private Ordering of Public Elections*, 126 YALE L.J. 262, 279 (2016).

248 *Id.*

249 See, for example, Jim Woolery's discussion of the activist settlement agreement in *Miller v. Bartolo*, C.A. No. 2024-0176-JTL (Del. Ch. 2024). Jim Woolery, *From Moelis to Miller: How to Settle with Activists*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Mar. 26, 2024), https://corpgov.law.harvard.edu/2024/03/26/from-moelis-to-miller-how-to-settle-with-activists [https://perma.cc/M3M8-GL7S].

250 *See, e.g.*, Jill Fisch, Assaf Hamdani & Steven Davidoff Solomon, *The New Titans of Wall Street: A Theoretical Framework for Passive Investors*, 168 U. PA. L. REV. 17, 19-20 (2019) (describing the emerging role of the "Big Three" asset managers: BlackRock, Vanguard, and State Street); Merritt B. Fox & Menesh S. Patel, *Common Ownership: Do Managers Really Compete Less?*, 39 YALE J. ON REG. 136, 139 (2022) ("Three management companies alone—Vanguard, BlackRock, and State Street (the 'Big Three')—manage funds holding in aggregate approximately 21% of the shares of a typical S&P 500 firm.").

251 The potential influence of large institutional investors has spawned an extensive "common ownership" literature. *See, e.g.*, Kenneth Khoo, *Transaction Costs in Common Ownership*, 25 U. PA. J. BUS. L. 209, 262 (2023) (discussing how engagement can facilitate anticompetitive behavior).

252 *See* Todd A. Gormley, Vishal K. Gupta, David A. Matsa, Sandra C. Mortal & Lukai Yang, *The Big Three and Board Gender Diversity: The Effectiveness of Shareholder Voice*, 149 J. FIN. ECON. 323, 343 (2023).

253 *See, e.g.*, Jill E. Fisch & Jeff Schwartz, *Corporate Democracy and the Intermediary Voting Dilemma*, 102 TEXAS L. REV. 1, 4 (2023) ("[V]oting is merely the tip of the iceberg; direct engagement with issuers is a key component of [institutional investors'] stewardship efforts.").

influence of institutional investors, their voting and engagement on these issues should subject them to fiduciary duties.[254] Relatedly, Exxon sued two of its institutional investors for filing a shareholder proposal, which, according to Exxon, sought to change Exxon's business model at the expense of shareholder value.[255] Although the complaint did not assert fiduciary duty claims, such claims would appear viable under an expansive concept of control.

The analogy to controllers extends further. In the Tesla-SolarCity merger, a number of large institutional investors were invested in both Tesla and SolarCity.[256] As a result, in voting their Tesla shares (to approve the merger), their voting preferences may have been influenced by the impact of the merger on their SolarCity investments. In litigation challenging the merger, plaintiffs argued that this conflict of interest should cause the court to disregard those votes.[257] Because non-controlling shareholders are permitted to act in accordance with their own self-interest, the argument would, in effect, have extended the legal principles applicable to controllers to these shareholders.

The use of "new" control is superficially appealing in that it offers a more nuanced and pragmatic evaluation of a shareholder's potential influence over corporate decisions. At the same time, as these examples show, it has the potential to expand the scope of the controlling shareholder concept far beyond traditional limits and, as a result, to extend entire fairness review to an increasing number of corporate decisions. One potential response to these concerns is that corporations can mitigate them by adhering to the procedural protections set out in *MFW*. In this next Section, we demonstrate why this solution is problematic.

B. *Application of* MFW *in Controlled Companies*

The courts' willingness to expand the application of entire fairness analysis appears to be based, in part, on the premise that corporations can always adhere to the *MFW* procedures and, by so doing, return the standard of review to the business judgment rule. If a corporation does so, it will be able to have the lawsuit dismissed and avoid the fact-intensive analysis of fair

254 *See, e.g.*, Marlo Oaks & Todd Russ, *A Historic Breach of Fiduciary Duty*, WALL ST. J. (May 15, 2023, 6:14 PM), https://www.wsj.com/articles/a-historic-breach-of-fiduciary-duty-shareholder-proposals-proxy-adivsory-climate-43baa5ba [https://perma.cc/4J77-JJJE] ("[I]nstitutional investors must vote for what is in the best financial interest of shareholders."). Such duties would be in addition to those owed by institutional money managers to their own investors.

255 Complaint, *supra* note 244, at 2-4.

256 *In re* Tesla Motors, Inc. S'holder Litig. (SolarCity), C.A. No. 12711-VCS, 2018 WL 1560293, at *10 & n.183 (Del. Ch. Mar. 28, 2018).

257 *Id.* The court did not have occasion to address this argument.

process and fair price. We argue in this Section, however, that the promise of transactional certainty through *MFW* compliance is overstated.[258]

MFW requires that for a corporate decision to receive business judgment review, that decision must be conditioned up front and subsequently receive approval by a disinterested independent committee that fulfills its duty of care and an uncoerced informed vote by a majority of the minority shareholders.[259] Yet compliance with *MFW* is more complex than it initially appears. Uncertainty about whether a court will determine that a corporation has complied adequately and apply the safe harbor likely explains the failure of many corporations to use *MFW*, presumably anticipating that an attempt at compliance will not meaningfully reduce their litigation risk.[260]

Consider first the requirement that the *MFW* procedures be established ab initio. The courts have repeatedly held that if the defendants engage in substantial economic negotiations prior to conditioning a transaction on *MFW* compliance, the transaction will not receive the benefit of the safe harbor.[261] For a freeze-out transaction, establishing the start of the negotiations is relatively straightforward, but determining the start of other corporate decisions is more difficult. Similarly, it is often unclear at the outset whether a particular decision will result in a controller receiving a non-ratable benefit. A third party, for example, may seek to purchase a corporation and, in the course of the negotiations, decide to provide the controller with

258 Our concerns about the likelihood that a court will find that a corporation has successfully complied with the *MFW* procedures has empirical support. One source reports that "[o]verall, during *MFW*'s 10-year history, *MFW* defenses succeeded in 10 of 26 cases for an aggregate success rate of 38.5%." Nathaniel J. Stuhlmiller & Brian T.M. Mammarella, *'MFW' Just Turned 10, but Is It Worth the Candle?*, DEL. BUS. CT. INSIDER (July 3, 2024), https://www.rlf.com/wp-content/uploads/2024/07/MFW-Just-Turned-10.pdf [https://perma.cc/HV76-F9K5].

259 Olenik v. Lodzinski, 208 A.3d 704, 715 (Del. 2019). Some commentary has described *MFW* as imposing six requirements. *See, e.g.*, Christopher B. Chuff, Joanna J. Cline & Matthew M. Greenberg, *MFW Pitfalls: Bypassing the Special Committee and Pursuing Detrimental Alternatives*, HARV. L. SCH. F. ON CORP. GOVERNANCE (June 30, 2020), https://corpgov.law.harvard.edu/2020/06/30/mfw-pitfalls-bypassing-the-special-committee-and-pursuing-detrimental-alternatives [https://perma.cc/96PP-NWQE].

260 *See, e.g.*, Meredith Kotler, Ethan Klingsberg & Marques Tracy, *Maybe Entire Fairness Review Isn't So Bad After All: Lessons from BGC Partners and Other Recent Controlling Shareholder Transactions*, FRESHFIELDS (Sept. 9, 2022), https://blog.freshfields.us/post/102hwqh/maybe-entire-fairness-review-isnt-so-bad-after-all-lessons-from-bgc-partners-a [https://perma.cc/LQ5G-7ZWA] ("While the business judgment rule undoubtedly remains appealing to many controlling stockholders, there may be reasons why some may choose not to go down the MFW path and instead embrace entire fairness review . . . ."). In addition to uncertainty about whether the safe harbor will be available, corporations may wish to retain greater flexibility in negotiating or fear the uncertainty of a majority of the minority vote. *Id.*

261 *See, e.g.*, *Olenik*, 208 A.3d at 718 (holding that *MFW* protections were not satisfied because economic discussions took place months before *procedural* protections were implemented); Flood v. Synutra Int'l, Inc., 195 A.3d 754, 756 (Del. 2018) (requiring the implementation of MFW procedures "before there has been any economic horse trading").

different consideration, an ongoing consulting agreement, or some other type of benefit. Finally, to the extent that a court applies a context-specific concept of soft control to a shareholder that holds substantially less than majority voting power, the transaction-specific factors relevant to the assessment of control may not even have occurred at the time that the corporation must decide whether to commit to an *MFW* process.

Second, *Match* provides that a transaction will not receive the protection of *MFW* unless the entire special committee is independent.[262] Director independence (like controlling shareholder status) is a complex and fact-dependent analysis.[263] Even if a corporation attempts to create an independent committee, subsequent judicial review may determine that one or more directors is not sufficiently independent. Indeed, *Tornetta* offers an example of a high level of judicial scrutiny, which, at least for some of the challenged directors, broke new ground in identifying factors that could constitute conflicts.[264] To be sure, even a director's expectation of future rewards may create a disabling conflict.[265] Yet a discerning standard of independence is likely to generate widespread litigation disputes about director independence in almost every controller case. Indeed, while the court in the *Trade Desk* case found this hurdle met, it still resulted in substantial and costly litigation.[266] Nor is this a problem that can necessarily be solved by bringing in a single director or new directors, particularly if Delaware takes an expansive view of independence. Although corporations appear to be using new directors or single director committees, there are reasons to question whether such actions truly achieve a fair process.[267] Directors who are hired for the purpose of *MFW* cleansing will likely understand that their role is to bless the transaction rather than condemn it.[268] Directors' incentives may also

262 Notably this reflects a change from prior law. *See* City Pension Fund for Firefighters & Police Officers v. Trade Desk, Inc., C.A. No. 2021-0560-PAF, 2022 WL 3009959, at *11-12 (Del. Ch. July 29, 2022) (rejecting plaintiff's challenge to the independence of the special committee where plaintiff did not "meaningfully challenge" the independence of two of the three committee members).

263 Beam v. Stewart, 845 A.2d 1040, 1050 (Del. 2004) (describing the standards for determining director independence).

264 Tornetta v. Musk, 310 A.3d 430, 509-511 (Del. Ch. 2024).

265 *See* Da Lin, *Beyond Beholden*, 44 IOWA J. CORP. L. 515, 553 (2019) ("[T]he prospect of future reward from the controlling shareholder can also impact director behavior.").

266 *Trade Desk*, 2022 WL 3009959, at *11-12.

267 *See, e.g.*, Elizabeth Pollman, *Strengthening Special Committees*, 9 U.C. DAVIS BUS. L.J. 137, 139 (2009) (arguing special committees should consist of more than one member).

268 As noted in the *Maffei* oral argument, this problem limits, as a practical matter, the independence even of temporary or single purpose directors. *See* Oral Argument at 19:30, Maffei v. Palkon, No. 125,2024 (Del. 2024), https://vimeo.com/1024769093.

be affected by their compensation and the prospect of future directorships.[269] Indeed, there are reasons to question whether any director at a controlled company can be considered truly independent.[270] And a court's finding of even one conflict on a committee will prevent the application of *MFW*.[271]

The informed shareholder vote raises similar concerns. Corporate law commentators are familiar with plaintiffs' willingness to challenge virtually any corporate disclosure as inadequate,[272] and there is no reason to believe that the disclosures in connection with the *MFW* shareholder vote will be immune from those challenges. As with director independence, however, the assessment of whether a disclosure is adequate frequently involves a close call, which is evidenced by the regular disagreement between the Chancery Court and the Delaware Supreme Court on this point. The fact-specific nature of the inquiry heightens the difficulty of ensuring that the required disclosures are sufficient to withstand a litigation challenge.

This concern is illustrated by the post-*Match* decision in *City of Sarasota Firefighters' Pension Fund v. Inovalon Holdings, Inc.*[273] In *Inovalon*, the CEO and founder Keith Dunleavy controlled the company through high-vote dual class stock.[274] Nordic Capital, a private-equity firm, proposed a buyout of Inovalon, but due to financing needs, it required a rollover of $700 million of Dunleavey's shareholdings.[275] The Inovalon board agreed to the transaction, and the shareholders of Inovalon (including the minority shareholders voting separately) approved the buyout.[276]

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269 Kathleen Wilson-Thompson, for example, who was appointed to the Tesla board of directors in 2018, was the sole member of the special committee that recommended Tesla shareholders ratify Elon Musk's pay package in 2024. Wilson-Thompson earned $50 million from exercising stock options granted to her as compensation for her director position and continues to have options valued at approximately $150 million more. Kirsten Grind, Emily Glazer, Rebecca Elliott & Coulter Jones, *The Money and Drugs That Tie Elon Musk to Some Tesla Directors*, WALL ST. J. (Feb. 3, 2024), https://www.wsj.com/tech/elon-musk-tesla-money-drugs-board-61af9ac4 [https://perma.cc/3WUY-SYB7].

270 *See, e.g.*, Giovanni Strampelli, *How to Enhance Directors' Independence at Controlled Companies*, 44 IOWA J. CORP. L. 103, 120 (2018) ("[I]ndependence requirements specified by law . . . are not able to ensure that directors will actually act in a truly independent way.").

271 *In re* Match Grp., Inc. Derivative Litig., 315 A.3d 446, 462-63 (Del. 2024) (holding the committee must be completely independent).

272 *See, e.g.*, Jill E. Fisch, Sean J. Griffith & Steven Davidoff Solomon, *Confronting the Peppercorn Settlement in Merger Litigation: An Empirical Analysis and a Proposal for Reform*, 93 TEXAS L. REV. 557, 558 n.4, 559 (2015) (describing the ubiquity of challenges to the adequacy of merger disclosures and arguing that, although the challenges frequently result in corrective disclosures, those disclosures do not provide meaningful value to shareholders).

273 319 A.3d 271, 274-75 (Del. 2024).

274 *Id.* at 275 n.9.

275 *Id.* at 281-82.

276 *Id.* at 282-83.

Plaintiffs sued, claiming that entire fairness review applied to the transaction since Dunleavy was a controlling shareholder.[277] In response, the defendants claimed compliance with *MFW* procedures. The Chancery Court agreed and dismissed the case.[278] The Delaware Supreme Court, sitting en banc, reversed.[279] The basis of the Court's ruling was Inovalon's failure to make full disclosure in connection with the shareholder vote.[280] Specifically, the Court found that, in three cases, the proxy statement failed to disclose certain potential conflicts by Inovalon's investment bankers. The Court remanded for further proceedings, which presumably will include entire fairness review.[281]

Inovalon demonstrates the effect of the current approach. Historically, a rollover of the nature described above would not be subject to entire fairness analysis. Indeed, in contrast, a Delaware Chancery Court opinion recently dismissed, under *Corwin*, a claim that a similar transaction was a breach of fiduciary duties.[282] Moreover, *Inovalon* was not a freeze-out, but rather a transaction where the buyer—in order to obtain financing from the controlling shareholder—was requiring a rollover to enable the transaction to move forward.[283] The transaction was negotiated on an arms-length basis between independent directors and approved by the majority of the minority shareholders. To be sure, there is the potential here for soft control to come into play, but the use of dual procedural mechanisms mitigated against a finding of domination which, in any event, the court did not require.[284] Nonetheless, these types of rollovers are now within the per se entire fairness ambit unless the company strictly complies with *MFW*.

C. *Entire Fairness and Transactional Uncertainty*

Ambiguity on the definition of a controlling shareholder, on the types of transactions that will be subject to entire fairness analysis, and on the ability of a corporation to rely on compliance with *MFW* create transactional

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277 *Id.* at 283.

278 *Id.* at 284.

279 *Id.* at 275.

280 Plaintiff originally alleged that the proxy was materially deficient in six ways. *Id.* at 286-87. The trial court carefully considered and rejected each allegation. *Id.* at 287-88. The Supreme Court disagreed with some, but not all, of the trial court's analysis. *Id.* at 289-304.

281 *Id.* at 304-05.

282 *In re* Anaplan, Inc. S'holders Litig., C.A. No. 2022-1073-NAC, 2024 WL 3086013 (Del. Ch. June 21, 2024).

283 Steven M. Davidoff & Matthew D. Cain, *Form Over Substance? The Value of Corporate Process and Management Buy-Outs*, 36 DEL. J. CORP. L. 849, 873 (2011).

284 Rather, the court found that the committee acted with due care. *Inovalon*, 319 A.3d at 286.

uncertainty.[285] The courts' willingness to subject decisions at controlled corporations to heightened scrutiny imposes an effective tax on operating as a controlled company. These costs are particularly great when a controlled company engages in a transaction that provides a controller with an ascertainable benefit. The rationale for the control premium is that a controller will likely be able to engage in such transactions, and transactions that benefit both the controller and the minority shareholders are socially desirable; yet going forward, such transactions will invariably face costly litigation challenges.

The law provides no ready way to evaluate the fairness of transactions that provide positive yet differential benefits to both the controller and minority shareholders.[286] In the limited context of freeze-outs and similar transactions, courts can rely on well-developed tools for evaluating the fairness of transaction price, specifically the price shareholders would have obtained through an arms-length third-party transaction. Even those tools often deteriorate into a battle of the experts. In contrast, as the *Tornetta* decision illustrates, courts and commentators have struggled for decades with the question of how to determine whether an executive compensation package is fair.[287] Corporations and courts have debated how to measure fairness in the context of a third-party buyout in which a controlling shareholder receives higher consideration for its shares than the minority shareholders.[288] *TripAdvisor* involves an unprecedented effort to measure the impact of a company's decision to reincorporate in Nevada on minority shareholders.[289] As we have observed in other work, similar problems plague other decisions, such as decisions to extend a sunset provision for a dual class voting structure.[290]

These concerns provide reasons to question the move toward greater judicial scrutiny of controlled company decisions. We note that heightened judicial oversight of controlling shareholder transactions is in tension with

285 *See* Kotler, Klingsberg & Tracy, *supra* note 260 ("[C]onditioning a transaction on compliance with *MFW* is no guarantee that the business judgment rule will end up applying . . . .").

286 Indeed, the question of whether a controlling shareholder has received a differential benefit is often itself unclear. *See, e.g.*, Petrucci, *supra* note 181, at 644-47 (discussing various cases involving challenges to differential treatment of controlling shareholders).

287 *See, e.g.*, Rogers v. Guaranty Trust Co., 288 U.S. 123, 127 (1933) (considering a challenge to executive pay as excessive).

288 *See, e.g.*, *In re* Delphi Fin. Grp. S'holder Litig., C.A. No. 7144-VCG, 2012 WL 729232 (Del. Ch. Mar. 6, 2012) (challenging differential consideration negotiated by a controlling shareholder in a third-party buyout); *see also* Petrucci, *supra* note 181, at 641-43 (critiquing the *Delphi* decision).

289 We note that this issue was raised to the Delaware Supreme court in Oral Argument at 20:30, Maffei v. Palkon, No. 125,2024 (Del. 2024), https://vimeo.com/1024769093 (observing the problems associated with using stock price movements to evaluate fair price, particularly at the time that a board is considering the possibility of reincorporation).

290 Berger, Fisch & Solomon, *supra* note 181, at 24-25.

Delaware's general deference to corporate decisions—deference premised on the fact that judges are poorly suited to evaluate the reasonableness of such decisions. An unwillingness to countenance judicial second-guessing of corporate decisions was the original basis for the business judgment rule.[291] Outside the controlling shareholder context, this deference has only increased in recent years. The implementation of exculpation provisions, for example, has resulted in an absence of judicial scrutiny for director and officer misconduct unless that misconduct involves self-dealing or rises to the level of bad faith.[292] Similarly, the Delaware Supreme Court has implemented a broad policy of allowing shareholder approval to substitute for judicial review even under the reasonableness standard of *Coster*.[293]

We also note that controlling shareholders operate within a broader corporate structure. Directors of Delaware controlled corporations, as at all corporations, make operational decisions. Those directors exercise broad discretion pursuant to DGCL section 141(a) and are subject to fiduciary duties to the corporation and its minority shareholders regardless of who elects them. The power of shareholders, even controlling shareholders, to participate in corporate decisions, is starkly limited by Delaware law. Although a controlling shareholder may ultimately have the power to replace existing directors who fail to follow its wishes, a change in board composition does not alter the fiduciary principles to which all directors are subject. Moreover, even minority shareholders can play an important role; institutional investors and proxy advisors have regularly shown their ability to influence board decisions even in controlled companies and controller transactions.[294]

Controlled companies are also subject to market discipline. To the extent that controlling shareholders destroy corporate value or engage in excessive self-dealing, the market for the shares of controlled companies will reflect those risks. The existence of a minority discount reflects the possibility that a controlling shareholder will behave opportunistically.[295] Minority shareholders appear willing to bear the cost of a controlling shareholder and,

291 *See supra* note 23.

292 *See* Stone v. Ritter, 911 A.2d 362, 364 (Del. 2006) (recognizing that, due to exculpation provision, directors did not face liability absent conduct amounting to bad faith).

293 Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304, 309 n.19 (Del. 2015).

294 *See generally* Khoo, *supra* note 251 (describing the influence of large institutional investors on firm decisions).

295 *See, e.g.*, Adam C. Pritchard, *Tender Offers by Controlling Shareholders: The Specter of Coercion and Fair Price*, 1 BERKELEY BUS. L.J. 83, 99 (2004) ("It does not take a zealous faith in the efficient capital market hypothesis to see that the risks of appropriation by the controlling shareholder will lead investors to discount the value of shares in a company that has a dominant shareholder.").

in some cases, may benefit from its presence.[296] Contrary to the implicit assumption in recent cases that controlling shareholders are likely to engage in excessive self-dealing, the market appears to reflect a trend toward greater acceptance of controlling shareholders and an increasing number of arrangements designed to facilitate that control. Examples include the expanded market acceptance of dual class structures,[297] extensive use of shareholder agreements affording control rights outside the dual class context,[298] and the consistent willingness of shareholders to approve transactions that provide differential value to controlling shareholders.[299]

Perhaps most importantly, controlling shareholder power is unlikely to persist if it fails to create value for minority shareholders. As Hamdani and Kastiel observe, the power of a superstar CEO is "limited in scope and duration" and only likely to persist as long as investors believe that the CEO is creating extraordinary value.[300] "The board is more likely to challenge such CEOs," they explain, "if [the CEOs] lose their star aura or if the expected harm from self-dealing exceeds the surplus generated by their unique contribution to company value."[301] Similarly, an activist shareholder cannot obtain board representation without the support of other shareholders, and those same shareholders, as well as other directors, constrain the ability of the activist to use that representation to influence corporate decisions.[302] Even if institutional investors had sufficient voting power at their portfolio companies to sacrifice firm-specific economic value in favor of broad-based societal objectives, their ability to do so would be constrained by the market power of their beneficiaries.[303] At the same time, as Elizabeth Pollman and Yifat Aran have demonstrated, market forces are often a viable match for structural power, and even a founder-CEO or a shareholder with majority voting control may find himself ousted if he is no longer serving the

296 When a court then limits the ability of the controller to exercise control, it is denying the controller its bargained-for right.

297 *See generally* Jill E. Fisch & Steven Davidoff Solomon, *Dual Class Stock*, *in* THE OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE (Jeffrey N. Gordon & Wolf-Georg Ringe eds., 2d ed. forthcoming 2025), https://ssrn.com/abstract=4436331.

298 *See* Rauterberg, *supra* note 26, at 1129-30; *see also* Shobe & Shobe, *supra* note 21, at 1382 (offering shareholder agreements as an example of a market check working alongside dual class voting mechanisms).

299 *See generally* Petrucci, *supra* note 181 (analyzing data on equal treatment charter provisions).

300 Hamdani & Kastiel, *supra* note 209, at 1399.

301 *Id.*

302 *See, e.g.*, Air Prods. & Chems., Inc. v. Airgas, Inc., 16 A.3d 48, 76 (Del. Ch. 2011) (providing an example of directors elected by a hostile bidder to a target board who subsequently rejected the bidder's acquisition proposal).

303 *See* Sam Glasscock III, *Ruminations on Appraisal*, DEL. LAW., Summer 2017, at 9 (suggesting that if minority stockholders face exploitation, they have the market power to stem this exploitation).

corporation effectively.[304] In earlier work, Kastiel shows that controlled companies can also be the subject of successful shareholder activism.[305] He finds that "although controlled companies are more insulated from activism than widely held companies, they are not fully immune to it."[306] He further "documents a non-negligible number of shareholder engagements with controlled firms."[307]

Our analysis identifies a series of significant implications of the recent controlling shareholder decisions that appear at odds with the fundamental market approach of Delaware law. Recent cases are also likely to force the Delaware courts into a substantial use of judicial resources, both to implement the current approach and to define its scope and limitations. In the next Part, we argue for an alternative approach based on a firmer theoretical analysis of both controlling shareholders and fiduciaries.

IV. A NEW APPROACH TO CONTROLLING SHAREHOLDER DUTIES

A. *When Is a Controlling Shareholder a Fiduciary?*

Although we believe that imposing fiduciary duties and entire fairness on controlling shareholders in the context of freeze-outs continues to be appropriate, subjecting transactions outside the traditional freeze-out context to entire fairness review is antithetical to the theoretical rationale for fiduciary duties in the first instance.[308] Fiduciary duties are ex-ante default rules imposed in order to guide conduct that cannot otherwise be bargained for.[309] They serve as rules that can be enforced by the court when market breakdowns occur but are not intended to deprive a party of a benefit that was freely bargained for.[310] Moreover, they should only be imposed if the

304 *See generally* Yifat Aran & Elizabeth Pollman, *Ousted*, 25 THEORETICAL INQUIRIES L. 231 (2024).

305 *See generally* Kobi Kastiel, *Against All Odds: Hedge Fund Activism in Controlled Companies*, 2016 COLUM. BUS. L. REV. 61.

306 *Id.* at 67.

307 *Id.* Recent work by Chun Zhou, Wei Zhang, and Dan W. Puchniak provides similar evidence that the amount of successful shareholder activism at controlled companies in China is nontrivial. *See* Chun Zhou, Wei Zhang & Dan W. Puchniak, *The Overlooked Reality of Shareholder Activism in China: Defying Western Expectations*, 15 HARV. BUS. L. REV. (forthcoming 2025), https://ssrn.com/abstract=4853552.

308 *See* D. Gordon Smith, *The Critical Resource Theory of Fiduciary Duty*, 55 VAND. L. REV. 1399, 1402 (2002) ("[F]iduciary relationships form when one party (the 'fiduciary') acts on behalf of another party (the 'beneficiary') while exercising discretion with respect to a critical resource belonging to the beneficiary.") (emphasis omitted).

309 *Cf.* Smith, *supra* note 58 at 7 ("Fiduciary law is distinct from contract law and classic tort law.").

310 *See id.* ("[T]he primary role of fiduciary law is to prevent opportunistic behavior by a corporate fiduciary, thus protecting vulnerable beneficiaries . . . .")

benefits of judicial oversight outweigh the costs, including the costs of the litigation necessary to subject transactions to judicial scrutiny.

At the same time, the value of judicial oversight must be weighed against the structural and market forces that constrain controlling shareholder opportunism outside the freeze-out context. Transactions like the reincorporation at issue in *TripAdvisor*, for example, require approval both by the board of directors and by the shareholders.[311] Accordingly, Maffei, acting on his own, could not cause the corporation to act. A similar analysis applied in *Trade Desk*, when the controlling shareholder sought to amend the charter to implement a sunset extension.[312] Thus the structure of Delaware law already provides gatekeepers to protect against abuse.[313] Similarly, a corporation is subject to the discipline of the capital markets, as well as the softer pressures imposed by creditors, employees, and the media, and evidence shows that these tools can be effective in addressing minority shareholder harm even in cases in which a controlling shareholder exercises hard control.[314]

Moreover, imposing fiduciary duties in these circumstances lacks—for the reasons we outline—a recognition of the value of control. The current trend toward heightened judicial oversight of decisions by controlled companies imposes substantial and additional costs on the ability of the controller to reap documented intangible and tangible benefits from control, which may produce additional benefits to minority shareholders and the corporation itself. We also believe that it interferes with the value of control embedded within the DGCL and cases such as *Ringling Bros.* and *Bershad*, which recognize the value of control and the ability of shareholders to exercise that control through statutory rights.[315] As a result, fiduciary duties should be

311 *See* Palkon v. Maffei (TripAdvisor), 311 A.3d 255, 262 (Del. Ch. 2024) (discussing the dual board and shareholder approval requirements).

312 City Pension Fund for Firefighters & Police Officers v. Trade Desk, Inc., C.A. No. 2021-0560-PAF, 2022 WL 3009959, at *13 (Del. Ch. July 29, 2022).

313 While one could argue that these features also apply in freeze-outs, the difference is that a freeze-out is an end-stage transaction in which existing shareholders lose their potential sway. Similarly, freeze-outs more closely reflect a zero-sum game in which the value received by the controlling shareholder comes at the direct expense of the minority. Finally, courts evaluating the fairness of the price in a freeze-out are engaged in a quantitative assessment with an established basis in law and theory and for which they can access market-based tools and comparable transactions. In contrast, the nature and even the existence of harm to minority shareholders in non-freeze-out cases requires a more qualitative and arguably speculative determination.

314 *See generally* Aran & Pollman, *supra* note 304; Yifat Aran, Brian Broughman & Elizabeth Pollman, Executive Turnover at Dual-Class Firms (Aug. 26, 2024) (unpublished manuscript) (on file with authors) (documenting the effectiveness of market pressures in removing executives at controlled companies).

315 *See generally* Deborah A. DeMott, *Organizational Incentives to Care About the Law*, 60 L. & CONTEMP. PROBS. 39 (1997) (discussing the role of fiduciary duties and the incentives embedded within these duties).

limited to those cases in which the prospect of coercion is highest and in which these countervailing factors are absent.[316]

Within this framework, we note the particular incongruity of imposing heightened duties on a controlling shareholder acting solely in its capacity as a traditional shareholder.[317] Such "traditional" actions include nominating directors, voting on director elections and shareholder proposals, and amending the bylaws. They include a controlling shareholder using its voting power to block actions that require shareholder approval such as a charter amendment or merger—even when the controlling shareholder does so in a manner that is contrary to the preferences of other shareholders.

Current doctrine is most problematic in these cases because it creates a direct conflict between a controlling shareholder's economic right to act out of self-interest and the potential that self-interested action will be contrary to the best interests of the corporation or other shareholders. The challenge is increased by the fact that normal corporate governance procedures—such as board action and minority shareholder approval—are not available as checks on the controlling shareholder's actions.

The court in *Sears Hometown* sought to balance these considerations by subjecting the shareholder's actions to intermediate scrutiny.[318] We argue against this approach based both on the principles underlying fiduciary duties and the framework of Delaware corporate law. In an action for breach of such duties, controlling shareholders are not protected from the risks of hindsight bias and excessive litigation through traditional legal protections such as the business judgment rule and exculpation. Most problematically, a duty of loyalty analysis is inapposite with respect to actions in which the controlling shareholder is pursuing an individual economic interest. Such a shareholder is, by definition, engaged in self-dealing.[319] The critical point is that when a shareholder acts in its capacity as a shareholder, it is not acting on someone

316 We note here that our proposal differs from that of Stephen Bainbridge who would place fiduciary duties on controlling shareholders but address issues with Delaware's current line of jurisprudence by, among other proposals, narrowing the definition of controller and narrowing "the class of cases under which entire fairness is the standard of review by adopting a reinvigorated *Sinclair Oil* threshold test under which entire fairness is triggered only when the controller receives a benefit at the expense of and to the exclusion of the minority." Bainbridge, *supra* note 20, at 9-10.

317 We do not include in this context a shareholder who exercises board authority pursuant to a shareholder agreement. Under those circumstances, the shareholder is acting as a traditional fiduciary and should be analyzed as such.

318 *In re* Sears Hometown & Outlet Stores, Inc. Stockholder Litigation, 309 A.3d 474, 516 (Del. Ch. 2024) ("This decision therefore applies enhanced scrutiny to evaluate the Controller Intervention.").

319 *See, e.g.*, Zipora Cohen, *Fiduciary Duties of Controlling Shareholders: A Comparative View*, 12 U. PA. J. INT'L BUS. L. 379, 394 (1991) (explaining that directors must take "into account solely the interests of the company [while controlling shareholders] act to further their own interests, as owners of the company's capital").

else's behalf as would a fiduciary, but rather exercising, as a principal, economic interests that it has obtained through market-based transactions.[320]

By rejecting the application of fiduciary duties in this context, our proposal reduces the difficulty of distinguishing between controlling and non-controlling shareholders. It is no longer necessary to answer the question of whether a mutual fund or hedge fund should be characterized as a controlling shareholder so long as that shareholder is not acting in a fiduciary capacity. Consequently, we do not propose adjustments to the definition of controller in this Article, although we recognize that the breadth of Delaware's current definition may be undesirable.[321]

The line between a shareholder acting in a traditional shareholder capacity and exercising broader control over corporate operations can, of course, be hard to discern. As noted above, shareholder agreements may give shareholders the authority to exercise traditional board powers, and we argue that, where they do so, such shareholders should be treated as fiduciaries.[322] Shareholders may, in addition, exercise more limited contractual rights, such as blocking rights, that potentially impact the interests of minority shareholders.[323] Such rights are particularly common in the private company context. We argue that the abuse of such contractual rights can be policed through the implied covenant of good faith and fair dealing, such that the additional imposition of fiduciary duties is unnecessary.[324]

We acknowledge that shareholders often act in multiple roles in which they also serve as officers or directors (i.e., as traditional fiduciaries). We do not intend our proposal to apply to shareholders when they act in their

320 We note that although the courts have expanded the treatment of controlling shareholders as fiduciaries, they have paid relatively less attention to the question of what obligations such fiduciary status would entail. As Zipora Cohen observes, the fact that someone is a fiduciary does not necessarily address the scope of their fiduciary obligations. *See id.*; *see also* Ernest Lim, *The Government Controlling Shareholder as a Fiduciary: Implications for Climate Change Management and Litigation*, 35 EUR. BUS. L. REV. 311 (2024) (exploring fiduciary obligations of the government as a controlling shareholder).

321 For a recent proposal arguing that the definition of controller should be limited, see Bainbridge, *supra* note 20.

322 See *supra* note 317 and accompanying text.

323 The classic example is *Basho Techs. Holdco B, LLC v. Georgetown Basho Invs., LLC*, 2018 WL 3326693, at *29 (Del. Ch. July 6, 2018), *aff'd sub nom. Davenport v. Basho Techs. Holdco B, LLC*, 221 A.3d 100 (Del. 2019), in which the court held that a shareholder exercised control by virtue of, inter alia, the exercise of its contractual rights to "maneuver[] the Company into a position of maximum financial distress."

324 *See, e.g.*, Dieckman v. Regency GP LP, 155 A.3d 358, 367 (Del. 2017); *see also* Franklin A. Gevurtz, *Corporate Rulers and Their Councils: Are Directors Becket or Cromwell When Dealing With Controlling Shareholders?*, 27 U. PA. J. BUS. L. (forthcoming 2025) (manuscript at 25), https://ssrn.com/abstract=4613022 (observing that the "abuse of a contractual advantage to gain more than originally bargained for" can potentially be addressed through the implied covenant of good faith and fair dealing).

capacity as such. Indeed, *Sears Hometown* recognized the fact that when a shareholder also acts as an officer or director, imposing separate fiduciary obligations on actions taken in the capacity of shareholder may not be necessary.[325] Similarly, Chancellor McCormick could have characterized Tesla's approval of Musk's compensation package as a conflicted officer transaction and invalidated the transaction on the basis that neither the board's approval nor the shareholder vote was sufficiently independent, without the need to examine whether Musk was a controlling shareholder.[326] Similarly, although it would have been more difficult, the court could have determined that the conflicted board members were not acting in good faith when they approved the package.[327] Both alternatives show that the Delaware courts already have tools to address the possibility of controlling shareholder domination without expanding the scope of controller fiduciary duties.

In a similar vein, we also note that Delaware has recognized the availability of a claim against non-fiduciaries for aiding and abetting a breach of fiduciary duty. In such cases, a defendant may be liable for aiding and abetting, even where the traditional fiduciary is subject to exculpation.[328] To the extent that a shareholder impedes the board's decisionmaking process or defrauds the directors, aiding and abetting offers a basis for imposing liability that does not require characterizing the shareholder's role as fiduciary in nature.

We also note that, without holding a formal board position, a shareholder who participates in board meetings and actively influences the other directors may constitute a de facto or shadow director and, as such, incur fiduciary obligations to the corporation.[329] Such cases are beyond the scope of our

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325 *See, e.g.*, Paula J. Dalley, *The Misguided Doctrine of Stockholder Fiduciary Duties,* 33 HOFSTRA L. REV. 175, 212 (2004) ("As directors and officers, [controlling shareholders] will be subject to the usual fiduciary duties in acting on behalf of the corporation.").

326 This potential did not crystalize in *Tornetta* as the plaintiff class voluntarily dismissed its claims against the director defendants. *See* Stipulation & [Proposed] Order Governing Decertification of Class, Dismissal with Prejudice of Direct Claims, & Schedule and Terms for Plaintiff's Motion for Leave to File Verified Amended Derivative Complaint, Tornetta v. Musk, 310 A.3d 430 (Del. Ch. 2024), No. 294. In addition, because the plaintiff sought recission rather than money damages, DGCL § 102(b)(7) would not have presented an impediment to the court providing the requested relief.

327 *See, e.g.*, *In re* Tyson Foods, Inc. Consol. S'holder Litig., 919 A.2d 563, 593 (Del. Ch. 2007) (holding that the complaint adequately alleged that members of Tyson's compensation committee acted disloyally and in bad faith in approving stock option grant).

328 *See, e.g.*, RBC Cap. Mkts., LLC v. Jervis, 129 A.3d 816, 865 (Del. 2015) (rejecting defendant's argument that imposing such liability "would create an anomalous imbalance of responsibilities where a non-fiduciary may be held liable for an unintentional violation of a fiduciary duty by a fiduciary").

329 *See, e.g.*, *In re* Ionica PLC, 241 B.R. 829, 839 (Bankr. S.D.N.Y. 1999) (explaining that, under U.K. law, "[a] 'shadow director' is 'a person in accordance with whose directions or instructions the directors of the company are accustomed to act,' other than those rendering professional advice").

analysis, although we note that in the United Kingdom, courts have recognized that the mere fact that someone serves as a shadow director will not subject them to the same fiduciary obligations as a de jure director.[330]

B. *Strengthening the Guardrails at Controlled Companies*

By acknowledging that controlling shareholders, in most instances, should not be held to fiduciary duties, we do not want to minimize the problem of domination and inherent coercion. Indeed, the central concern about transactions at controlled companies is the risk that controlling shareholder domination will taint the corporate decisionmaking process.

This taint can arise in several ways. First, a controlling shareholder can use its voting power to nominate and elect loyal directors who are inclined to favor the controlling shareholder's interests. Second, a shareholder can use its power to remove and replace directors whom it views as insufficiently responsive to its concerns. Third, a shareholder can take or threaten to take other actions, such as amending the bylaws, making a tender offer, or selling stock. To the extent that directors have other business relationships or employment positions with the controlling shareholder, the shareholder can also threaten to end those relationships. Courts have recognized that this domination can lead directors to fail to adhere to proper procedures in evaluating corporate decisions or to give undue weight to the interests of the controlling shareholder, even when those interests are adverse to the interests of other shareholders and the corporation.[331] Even in freeze-out cases in which a controlled company forms a special committee to negotiate the transaction, courts have found that directors sometimes fail to function independently. As then Vice-Chancellor Strine argued, the men and women who populate the committees are rarely individuals "whose own financial futures depend importantly on getting the best price and, history shows, [they] are sometimes timid, inept, or . . . , well, let's just say worse."[332] In sum, some boards at controlled companies may not act with the independence expected of directors.

At the end of the day, however, corporate law operates under a framework of board primacy. Directors, not shareholders, are responsible for addressing unfairness in corporate actions. The solution, then, is to buttress the board's

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330 *See, e.g.*, Ultraframe (UK) Ltd v. Fielding [2005] EWHC (Ch) 1638 [1279] ("There is no specific statutory provision that says that a shadow director owes the same duties to a company as a *de jure* or *de facto* director.").

331 *See, e.g.*, Leo E. Strine, Jr., *The Delaware Way: How We Do Corporate Law and Some of the New Challenges We (and Europe) Face*, 30 DEL. J. CORP. L. 673, 678 (2005) ("[T]here is an obvious fear that even putatively independent directors may owe or feel a more-than-wholesome allegiance to the interests of the controller, rather than to the corporation and its public stockholders.").

332 *In re* Cox Commc'ns, Inc. S'holders Litig., 879 A.2d 604, 619 (Del. Ch. 2005) (Strine, V.C.).

ability to act independently, rather than imposing fiduciary duties on shareholders that prevent them from acting out of self-interest. We note that judicial oversight of board decisions incorporates longstanding doctrines such as the obligation of directors to become informed, the virtue of relying on the collective decisionmaking process of a board, and the protection of directors against excessive litigation through the balance struck by features such as the business judgment rule, D&O insurance, and exculpatory charter provisions. Focusing on the board allows the courts to apply the longstanding presumption of regularity to most decisions at controlled companies without triggering the more onerous entire fairness scrutiny. Focusing on the board's role relieves the courts of the difficult task of determining when a shareholder exercises sufficient control to trigger entire fairness.

As with our analysis of controlling shareholder liability, we do not propose changing the legal standard applicable to controlling shareholder freeze-outs, for which we believe entire fairness remains the appropriate standard of review. We argue that the solution to concerns of domination in non-freeze-out cases is strengthening the ability of the board to act independently of controlling shareholder influence.

We offer three suggestions for doing so.[333] First, where a plaintiff sufficiently alleges both that a controlling shareholder has dominated a board decision and that the decision results in a quantifiable benefit to the controller to the detriment of the minority shareholders, we propose that the decision be subject to the one-step cleansing applicable to director and officer conflicted transactions rather than the *MFW* approach. That is, we propose that the fully informed approval of either the disinterested directors or disinterested shareholders cleanse the transaction, subjecting it to the business judgment rule rather than entire fairness scrutiny. We believe that this approval, together with market mechanisms and the board-level fiduciary duties (enhanced as we discuss further below), is sufficient to remove the taint of domination without the additional costs of the full *MFW* process.[334] We note that our proposal would require the plaintiff to allege actual rather than potential domination. As with our discussion of the duties of controlling shareholders as shareholders, and because the burden of procedural cleansing is substantially less, our proposal reduces the need to address with precision the boundaries of who constitutes a controlling shareholder. The implications of being characterized as controlling are simply less fraught.

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333 We note that in cases of shareholder action by a majority controller, courts can also engage in equitable review of such transactions as in *Frantz*.

334 We do not address in this Article the application of *MFW* to freeze-outs. An academic literature addresses this issue and the limits of *MFW*. *See, e.g.*, Itai Fiegenbaum, *The Geography of MFW-Land*, 41 DEL. J. CORP. L. 763 (2017) (arguing that requiring the application of MFW protections to all controlling stockholder transactions is misguided).

Second, where a plaintiff sufficiently alleges domination and the decision has not been properly cleansed through the aforementioned single-step process, or where the court determines that the cleansing is procedurally deficient, we propose that the court review the decision under the enhanced scrutiny standard[335] from *Unocal* and *Coster* as applied in *Sears Hometown*.[336] As in those cases, enhanced scrutiny offers a mechanism by which a court can apply a reasonableness standard that is more deferential than entire fairness review without necessarily presuming that a board's actions are valid. Notably, because this standard is more deferential than entire fairness, it reduces the stakes of failing to comply with the *MFW* procedures, potentially reducing what threatens to become highly burdensome collateral litigation over issues such as the independence of the special committee or the adequacy of the disclosure to shareholders.[337] In addition, the more deferential standard relieves the courts of the difficult task of determining whether decisions such as reincorporation or compensation are entirely fair in the absence of meaningful quantitative benchmarks for fairness.

Moreover, the courts developed the enhanced scrutiny standard in *Unocal* and *Revlon* precisely for the purpose of guarding against soft conflicts that might compromise the ability of a board to operate independently.[338] More specifically, in the cases of *Unocal* and *Revlon* the court was addressing the "omnipresent specter that a board may be acting primarily in its own interests"[339] where actual misconduct is not apparent. In such circumstances, intermediate scrutiny serves to provide a judicial check on the possibility that control can be used to for nonobvious self-dealing. Thus, our extension of that approach to other soft conflicts is historically grounded.

In applying intermediate scrutiny, we propose a similar test to that laid out in *Coster*. The plaintiff, we argue, should have the initial burden of putting forth colorable allegations that the board was dominated by a controlling shareholder in the challenged decision. If the plaintiff meets that burden, the

335 We draw from the court's discussion of enhanced scrutiny in *In re Sears Hometown & Outlet Stores, Inc. Stockholder Litigation*, 309 A.3d 474, 514-16 (Del. Ch. 2024).

336 *See supra* note 30 and accompanying text.

337 We note that Itai Fiegenbaum takes the opposite position, arguing that the entire fairness standard is necessary because, in its absence, plaintiffs' attorneys will be unwilling to bring sufficient litigation challenges to police potential self-dealing. Itai Fiegenbaum, *The Controlling Shareholder Enforcement Gap*, 56 AM. BUS. L.J. 583, 607-09 (2019).

338 *See, e.g.*, Unocal Corp. v. Mesa Petrol. Co., 493 A.2d 946, 954 (Del. 1985) (observing that enhanced scrutiny is appropriate "[b]ecause of the omnipresent specter that a board may be acting primarily in its own interests"); Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 184 (Del. 1986) ("[W]hen a board ends an intense bidding contest on an insubstantial basis, and where a significant by-product of that action is to protect the directors against a perceived threat of personal liability for consequences stemming from the adoption of previous defensive measures, the action cannot withstand the enhanced scrutiny which *Unocal* requires of director conduct.").

339 *Id.* at 180 (citing *Unocal*, 493 A.2d at 954).

board must first establish that it acted "in good faith, after a reasonable investigation, to achieve a legitimate objective."[340] Second, the board must establish that its actions constituted a reasonable means for accomplishing that objective. As in the *Coster* context, a reasonableness standard means that the court does not simply defer to the board's judgment, as it would under the business judgment rule, but instead evaluates whether that judgment falls within a range of reasonableness.[341] We observe that this level of judicial scrutiny enables a court to operate as a meaningful check on director domination as well as to "smoke out mere pretextual justifications for improperly motivated decisions."[342] It also preserves the ability of the company and board, provided the burden is not shifted, to dismiss litigation at the motion to dismiss stage. Moreover, because intermediate scrutiny only applies if plaintiffs sufficiently allege domination, our proposal provides an incentive for controlling shareholders to support directors who are sufficiently independent to withstand allegations of domination.

Third, we propose that courts and plaintiffs be more attentive to directors of controlled companies who, as a result of controlling shareholder domination, inappropriately act in furtherance of the controlling shareholder's interests rather than those of the corporation. Although under existing law, these directors act in bad faith,[343] we believe courts and plaintiffs have been insufficiently demanding of them. If directors act in bad faith, their conduct subjects them to liability for money damages, and they are not subject to exculpation. As with the *Caremark* line of cases, we reason that the risk of monetary liability is necessary to provide director incentives to act independently and, as with the *Caremark* decision, we encourage courts to remind directors of controlled companies of this exposure.[344]

340 *Sears Hometown*, 309 A.3d at 516.

341 Importantly, reasonableness is a far less demanding standard than entire fairness. We also recognize that this proposal represents a partial overruling of *Sinclair Oil* in its oversight of "European tunnelling", the diversion of assets from the company to the controller. *See* Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971). However, we believe that a reasonableness standard is more workable than entire fairness, particularly in light of today's more professional boards which are better able to monitor these issues than at the time *Sinclair Oil* was decided. In this regard, *Coster* retains a role for meaningful judicial oversight.

342 *In re* Dollar Thrifty S'holder Litig., 14 A.3d 573, 598-99 (Del. Ch. 2010).

343 Under *Stone v. Ritter*, bad faith encompasses actions "where the fiduciary intentionally acts with a purpose other than that of advancing the best interests of the corporation." 911 A.2d 362, 369 (Del. 2006).

344 Recent decisions of the Delaware courts underscore the timeliness of our proposal. *See* Firefighters' Pension System v. Found. Bldg. Materials, Inc., 318 A.3d 1105, 1119 (Del. Ch. 2024) (denying a motion to dismiss and finding a claim stated for non-exculpated breach of fiduciary duties because "it is reasonably conceivable that the [special] committee members consciously disregarded their duties and deferred to" a controlling shareholder).

CONCLUSION

We explore the evolving concept of control in corporate law and its implications for fiduciary duties in companies with controlling shareholders. We describe how both the situations in which courts have treated someone as a controlling shareholder and the situations in which controlling shareholder status triggers entire fairness review have expanded from the traditional cases involving freeze-outs by majority shareholders. We develop the implications of this expansion and show the tension in reconciling it with shareholders' economic rights.

We propose an alternative to the current approach. Rather than imposing per se fiduciary obligations upon shareholders acting in their capacity as shareholders, we argue that the law instead should subject board action at controlled companies to greater scrutiny. In particular, we suggest an intermediate standard of review for board decisions, coupled with the meaningful prospect of liability for directors who succumb to shareholder domination in approving a transaction benefiting a controller. By cabining the scope of entire fairness review, we reduce the implications of the increasingly complex task of determining whether someone is a controlling shareholder.

Ultimately, we believe that our proposed alternative is attentive to both the economic benefits and detriments of control and consistent with the principle in Delaware that control in and of itself does not create trust-like fiduciary duties. It is also consistent with the carefully calibrated governance of corporations under Delaware law and in the public capital markets which imposes strict judicial scrutiny only when there is clear evidence of market failure. Finally, our proposal provides bright-line transactional rules for corporate planners, which can be reflected in corporate governance procedures and the market prices of public companies.