

## Court of Chancery of Delaware: Applies Entire Fairness Standard to De-SPAC Merger (Securities Law Alert)

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On January 3, 2022, the Court of Chancery of Delaware largely denied motions to dismiss in a class action for breach of fiduciary duties alleging that the directors, officers, and controlling stockholder of a SPAC (special purpose acquisition company) withheld material information from the public stockholders, which allegedly impaired their right to redeem their shares before the de-SPAC merger. [In re MultiPlan S'holders Litig., 2022 WL 24060 \(Del. Ch. Ct. 2022\) \(Will, V.C.\).](#)<sup>[1]</sup> The court held that: (i) plaintiffs pleaded direct claims centering around the purported impairment of their redemption right; (ii) the entire fairness standard of review applied at the pleading stage; and (iii) plaintiffs had pleaded a non-exculpated disclosure claim against the SPAC's controlling stockholder and former directors.

### Background

The SPAC's initial public stockholders purchased IPO units consisting of one common share and a fractional warrant for \$10 per unit. The sponsor of the SPAC was ultimately controlled by a sole stockholder (the "Controlling Stockholder"), who had previously sponsored several SPACs. The sponsor's primary form of compensation was "founder" shares. If the SPAC entered into a business combination within two years, the founder shares would convert into common shares. If no transaction was completed, the SPAC would liquidate, the public stockholders would receive their investment back plus interest and the founder shares would have no value.

The SPAC entered into a merger with a healthcare data analytics firm and, in September 2020, the SPAC issued a proxy statement that solicited stockholder votes on the deal. The SPAC's certificate of incorporation established that the public stockholders could either exercise their redemption right (then equal to \$10.04) held by the SPAC trust or remain as investors in the post-combination entity. In October 2020, the SPAC's stockholders "overwhelmingly" voted to approve the business combination and the de-SPAC merger was completed. In November 2020, a short-seller published a negative report alleging that the target's largest customer was building a competing in-house product. The post-merger company's stock fell to a then-closing low of \$6.27 the following day.

### Procedural History

Plaintiffs alleged that the SPAC's fiduciaries omitted material information in the proxy. Counts I, II, and III of the complaint were direct claims for breach of fiduciary duty against certain SPAC directors, officers, and the Controlling Stockholder. Plaintiffs alleged that defendants, putting

their own financial interests ahead of the public stockholders’ interests, failed to disclose facts that impaired the public stockholders’ informed exercise of their redemption and voting rights. Defendants moved to dismiss.

**Plaintiffs Pleaded Facts Supporting a Reasonable Inference That Entire Fairness Applies**

An issue before the court was whether to apply the business judgment rule, which is Delaware’s “default standard of review” or entire fairness, which is Delaware’s “most onerous standard of review” to the de-SPAC merger. The court determined that plaintiffs pleaded facts supporting a reasonable inference that entire fairness applied on two independent bases. First, plaintiff alleged that the de-SPAC merger was a conflicted controller transaction. Second, plaintiff alleged that a majority of the SPAC board was conflicted either because the directors were self-interested or because they lacked independence from the Controlling Stockholder.

Noting that entire fairness was not triggered by the mere presence of a controlling stockholder, the court explained that plaintiffs must also adequately plead that the Controlling Stockholder engaged in a conflicted transaction. Delaware courts place conflicted controller transactions implicating entire fairness into one of two categories: “where the controller stands on both sides”<sup>[2]</sup> and “where the controller competes with the common stockholders for consideration.” As to the second category, the court explained that a controller competes with common stockholders when he “receives a unique benefit by extracting something uniquely valuable to the controller, even if the controller nominally receives the same consideration as all other stockholders to the detriment of the minority.”<sup>[3]</sup> *IRA Tr. FBO Bobbie Ahmed v. Crane*, 2017 WL 7053964 (Del. Ch. 2017, revised 2018).

**Plaintiffs Pleaded Facts Supporting a Reasonable Inference That the Controlling Stockholder Received a Unique Benefit**

Focusing on the period before the de-SPAC merger when the public stockholders held redemption rights backed by the trust, the court determined that the allegations pleaded facts supporting a reasonable inference that there was a unique benefit to the Controlling Stockholder. The court pointed out that the merger had a value to the common stockholders if shares of the post-merger entity were worth \$10.04, but that the merger was valuable to the Controlling Stockholder “well below” \$10.04 because the value of the Controlling Stockholder’s compensation would drop to zero if no merger occurred. The court determined that “[t]he potential conflict between [the Controlling Stockholder] and public stockholders resulting from their different incentives in a bad deal versus no deal is sufficient to pass the ‘reasonably conceivable’ threshold[ ]” found in Rule 12(b)(6).

**Plaintiffs Pleaded Facts Supporting a Reasonable Inference That the Stockholders’ Redemption Rights Were Impaired Through Failure to Disclose Material Information**

The court finally found that plaintiffs’ breach of fiduciary duty claims were reasonably conceivable because they alleged that the directors “failed, disloyally, to disclose information necessary for the plaintiffs to knowledgeably exercise their redemption rights.” The court emphasized that “plaintiffs’ claims are [not] viable [ ] simply because of the nature of the transaction or resulting conflicts[ ]” and that the court’s “conclusion does not address the validity of a hypothetical claim where the disclosure is adequate and the allegations rest solely on the premise that fiduciaries were necessarily interested given the SPAC’s structure.” Indeed, the court stated that “[i]f public stockholders, in possession of all material information about the target, had chosen to invest rather than redeem, one can imagine a different outcome.”

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<sup>[1]</sup> Simpson Thacher represents defendant MultiPlan Corp. f/k/a Churchill Capital Corp. III in this action.

<sup>[2]</sup> The court found that the Controlling Stockholder did not stand on both sides of the de-SPAC merger as this was an arms-length transaction between two unaffiliated parties.

<sup>[3]</sup> A controller also competes with common stockholders when the controller “receives greater monetary consideration for its shares than the minority stockholders” or “takes a different form of consideration than the minority stockholders[.]”

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