DELAWARE'S "CONTROL GROUP" JURISPRUDENCE: A SURVEY OF RECENT DECISIONS

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This article describes the development of Delaware's control group jurisprudence in recent years. Whether stockholders are members of a "control group" under Delaware law has consequences. The fiduciary duties that run with controlling stockholder status impact the viability of pleadings stage motions by potentially heightening the applicable standard of review and dictating which defenses are available to defendants. The article examines the Delaware Supreme Court decisions that have prompted stockholder plaintiffs to focus on pleading the existence of a controller or control group. That increased focus by stockholder plaintiffs has led to the Delaware courts issuing at least ten rulings addressing whether a group of stockholders constituted a "control group" since 2017. We explain that this series of recent rulings reflects only the most recent example of Delaware's commitment to a common law process that refines its corporate law iteratively and quickly. That process, and the resulting body of case law, now guides future transactional planning and also provides predictable results in future litigation.

Since 2017, the Delaware Supreme Court and the Delaware Court of Chancery have together issued at least ten rulings analyzing whether a group of stockholders constituted a "control group" for purposes of Delaware law. This Article surveys those decisions, explains how broader developments in Delaware corporate law brought the control group issue to the forefront, and addresses how the resulting opinions reflect the Delaware judiciary's ability to build a critical mass of guidance for transactional attorneys seeking insight into a particular topic.

The short story is that the Delaware Supreme Court issued decisions in *Gentile v. Rossette*[1] and *Corwin v. KKR Financial Holdings*[2] that led stockholder plaintiffs to challenge transactions with controlling stockholders as a means of avoiding the business judgment rule. Attempts to lump together multiple stockholders as a control group followed. The cases led to the Court of Chancery and the Delaware Supreme Court issuing lengthy opinions addressing these issues. Now, just five years later, a "cohesive body of law" exists to guide parties.[3] As discussed below, the best way to understand the post-*Corwin*[4] decisions is to perceive a "spectrum" of results that can be classified based on recurring factors.

The Article proceeds as follows.[5] Part I explains how *Gentile* and *Corwin* prompted stockholder plaintiffs to focus on controllers generally. Part II surveys the post-*Corwin* control group decisions. Part III discusses takeaways from the decisions. Part IV explains how together the decisions reflect the vigor of Delaware's common law.

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1. 906 A.2d 91 (Del. 2006).

2. 125 A.3d 304 (Del. 2015).

3. *See* Donald F. Parsons, Jr. & Jason S. Tyler, *Docket Dividends: Growth in Shareholder Litigation Leads to Refinements in Chancery Procedures*, 70 WASH. & LEE L. REV. 473, 474 (2013).

4. 125 A.3d 304 (Del. 2015).

5. This Article focuses on Delaware law and so it does not delve into the definition of "control group" under federal securities laws or regulations unless addressed in the Delaware opinions.

I. THE GROWING IMPORTANCE OF CONTROLLING STOCKHOLDERS

When a stockholder or group of stockholders gains control is "an age-old issue."[6] The task of "[a]rticulating standards to identify the presence of such a group has bedeviled courts for nearly a century."[7]

Two Delaware Supreme Court decisions brought the issue to the forefront. The first was the 2006 decision in *Gentile*, which granted stockholders post-merger standing to pursue dilution claims in limited circumstances.[8] A dilution claim is traditionally a derivative claim, and a merger extinguishes standing to assert it.[9] Under *Gentile*, a *claim* could be "both derivative and direct" if:

> (1) a stockholder having majority or effective control causes the corporation to issue "excessive" shares of its stock in exchange for assets of the controlling stockholder that have a lesser value; and (2) the exchange causes an increase in the percentage of the outstanding shares owned by the controlling stockholder, and a corresponding decrease in the share percentage owned by the public (minority) shareholders.[10]

A key component of this formulation is the presence of a controlling stockholder. *Gentile* precipitated a series of decisions about what constituted a control group.[11] One of those cases introduced the "legally significant connection" test, discussed below. That decision was a 2009 opinion in *Dubroff v. Wren Holdings* where Vice Chancellor Noble wrote:

> Although a controlling shareholder is often a single entity or actor, Delaware case law has recognized that a number of shareholders, each of whom individually cannot exert control over the corporation (either through majority ownership or significant voting power coupled with formidable managerial power), can collectively form a control group where those shareholders are connected in some legally significant way-e.g., by contract, common ownership, agreement, or other arrangement-to work together toward a shared goal.[12]

Because a plaintiff could preserve post-merger standing to assert a dilution claim if a controlling stockholder was involved, parties joined issue over the "legally significant connection test."

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6. *See* Ann M. Lipton, *After Corwin: Down the Controlling Shareholder Rabbit Hole*, 72 VAND. L. REV. 1977, 1997–98 (2019). There are also federal securities law and stock exchange listing requirements that address the issue, which are beyond the scope of this article.

7. *Id*.

8. 906 A.2d 91 (Del. 2006).

9. *See generally* Brookfield Asset Mgmt., Inc. v. Rosson, 261 A.3d 1251, 1262 (Del. 2021) (discussing continuous ownership requirement).

10. *Gentile*, 906 A.2d at 100.

11. *Compare* Carsanaro v. Bloodhound Techs., Inc., 65 A.3d 618, 659 (Del. Ch. 2013) (holding control group was adequately pled as part of analyzing a *Gentile* claim) and *In re* Nine Sys. Corp. S'holders Litig., 2013 WL 771897, at *6 (Del. Ch. Feb. 28, 2013) (ruling at summary judgment that the Court could not conclude as a matter of undisputed fact that there was no control group as part of *Gentile* analysis) *with* DiRienzo v. Lichtenstein, 2013 WL 5503034, at *25 (Del. Ch. Sept. 30, 2013) (holding control group was not adequately pled as part of analyzing a *Gentile* claim).

12. 2009 WL 1478697, at *3 (Del. Ch. May 22, 2009).

The second Delaware Supreme Court decision to spur control group jurisprudence was the 2015 ruling in *Corwin v. KKR Financial Holdings*.[13] There, the Delaware Supreme Court concluded "when a transaction not subject to the entire fairness standard is approved by a fully informed, uncoerced vote of the disinterested stockholders, the business judgment rule applies."[14] Subsequent decisions interpreted the "not subject to the entire fairness language" of *Corwin* to mean *Corwin* applies "absent a looming conflicted controller."[15] In practice *Corwin* "widened the gulf between [review of] transactions that involve a controlling shareholder and those that do not."[16] For plaintiffs, identifying a conflicted controlling stockholder became key to avoiding *Corwin.*

After *Corwin*, the arguments on motions to dismiss fell into a pattern:

> In the realm of Delaware post-closing shareholder litigation, over the past seven years, a rhythm has emerged in the assertion of claims and defenses as our courts have clarified and refined the application of standards for reviewing fiduciary conduct. *In hopes of securing more rigorous judicial scrutiny of fiduciary conduct, stockholders invoke the sounds of minority blockholders who act as if they are controlling stockholders*, fiduciary decisionmakers who are overcome by allegiances to the controller, and stockholders who are coerced to sell their shares while starved of accurate and complete information. *In hopes of securing more judicial deference to fiduciary decision making, defendants invoke the sounds of passive minority blockholders* and presumptively disinterested, independent (and often exculpated) fiduciaries who have faithfully served fully informed, uncoerced stockholders.[17] *Gentile* and *Corwin* thus set the rhythm that cases danced to, leading to rulings on the control group issue.

While these judicial developments were taking place, dynamic market changes created more parties who arguably were controllers or part of a control group. "Due to a confluence of factors, including an unprecedented influx of available private capital, startups are staying private longer on average and raising larger late-stage funding rounds from [a] greater diversity of investors" that includes "mutual funds, pension funds, hedge funds, corporate investors, and sovereign wealth funds."[18] These "investors are often granted individualized rights, such as designated board seats and the ability to block various corporate actions," meaning "corporate control rights are increasingly allocated in unique and idiosyncratic ways" across increasingly complex share structures involving multiple classes.[19] The same became true for public companies, where dual-class stock and other techniques enabled the consolidation of control rights.

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13. 125 A.3d 304 (Del. 2015).

14. *Id.* at 309.

15. Larkin v. Shah, 2016 WL 4485447, at *13 (Del. Ch. Aug. 25, 2016).

16. Lipton, *supra* note 6, at 1979.

17. *In re* GGP, Inc. S'holder Litig., 2021 WL 2102326 (Del. Ch. May 25, 2021) (emphasis added); *see also* Note, *Controller Confusion: Realigning Controlling Stockholders and Controlled Boards*, 133 HARV. L. REV. 1706, 1712 (2020) (stating "controlling stockholder status remains significant, both for the individual in acquiring fiduciary duties and for the board that may find its decisions subject to heightened scrutiny and difficult to cleanse").

18. Elizabeth Pollman, *Startup Governance*, 168 U. PA. L. REV. 155, 175 (2019).

19. Ann M. Lipton, *The Three Faces of Control*, 77 BUS. LAW. 801, 803 (2022); *see also* Pollman, *supra* note 18, at 175 (discussing increasing complexity of startup governance and capital structures).

Thus, the controller designation under Delaware law took "on a new legal significance at the precise moment when business realities have made the exercise of control more difficult to ascertain."[20] The confluence of these events led to a flurry of decisions.

II. *POST-CORWIN* CONTROL GROUP DECISIONS

The Court of Chancery and the Delaware Supreme Court have issued a series of decisions on controllers and control groups. This section discusses those cases as a predicate for identifying common characteristics.

A. *Van der Fluit v. Yates*[21]

This *Van der Fluit* decision provides a blueprint for post-*Corwin* control group arguments. The plaintiffs argued *Corwin* did not apply to Oracle's acquisition of Opower, Inc., because of the existence of a control group.[22] The Court of Chancery decided that there was no control group, but that *Corwin* still did not apply because of disclosure violations.[23] Despite clearing the *Corwin* hurdle, the plaintiff failed to allege non-exculpated breaches of fiduciary duty, resulting in the dismissal of the complaint.

1. Background

Opower was founded by Yates and Laskey. At the time of the merger, Yates was the company's CEO, board chairman, and owned 22.4% of its outstanding stock, largely through preferred shares. Laskey was the company's president, a member of its board, and owned 17.4% of the company's outstanding stock, again largely through preferred shares. New Enterprise Associates ("NEA") was a venture capital fund that held 21.8% of the company's outstanding stock, and had a director designee on the company's board. MHS Capital was an early seed investor that held an 8.3% ownership stake.[24] Yates, Laskey, NEA, and MHS were parties to an Investor Rights Agreement that gave "registration and informational rights to early stage investors" that held preferred stock.

For roughly two years, Oracle flirted with purchasing Opower, finally making a firm offer to purchase Opower for $9-$10 per share. Opower ran a sale process, hired an investment banker to seek other bids, and negotiated with Oracle for a higher offer. No other bidders emerged, and Opower accepted an offer from Oracle at $10.30 per share. When finalizing the deal, the company's largest investors entered into side agreements. Numerous stockholders, including Yates, Laskey, and NEA, entered into tender and support agreements that committed them to the transaction. Yates, Laskey and other members of management negotiated for the right to convert their unvested Opower options into comparable unvested Oracle options.[25]

2. Analysis

After the stockholders filed suit, the defendants moved to dismiss the complaint. The parties' briefing focused on the relevant standard of review. The plaintiffs advanced multiple arguments as to why the business judgment rule did

20. Lipton, *supra* note 6, at 1990.

21. 2017 WL 5953514 (Del. Ch. Nov. 30, 2017).

22. *Id.* at *6; *see Corwin*, 125 A.3d 304 (Del. 2015).

23. *Yates*, 2017 WL 5953514, at *1.

24. *Id.* at *1–*2.

25. *Id.* at *3.

not apply. The court addressed three primary issues: whether there was a controlling stockholder, whether informed and uncoerced stockholders approved the transaction, and whether the stockholders adequately pled non-exculpated claims for breach of fiduciary duty.[26]

The plaintiff argued that Yates, Laskey, NEA, and MHS were a control group based on their combined stock holdings, which gave them approximately 70% of the company's voting power, their connections through the Investor Rights Agreement (which pre-dated the IPO), and their entry into the tender and support agreements, which MHS did not sign. Quoting Chancery precedent, the court observed that "[s]tockholders can collectively form a control group where those shareholders are connected in some legally significant way—e.g. by contract, common ownership, agreement, or other arrangement—to work together toward a shared goal."[27] "The law does not require a formal written agreement, but there must be some indication of an actual agreement. Plaintiffs must allege more than mere concurrence of self-interest among certain stockholders to state a claim based on the existence of a control group."[28]

The court concluded NEA and MHS were not members of a control group based on the Investor Rights Agreement, which "contain[ed] no voting, decision-making, or other agreements that bear on the transaction challenged in the instant case."[29] The tender and support agreements also were not sufficient, as they only reflected a "concurrence of self-interest among certain stockholders."[30] Many stockholders signed tender and support agreements, and the plaintiffs "offer[ed] no explanation for why NEA and MHS are members of an alleged control group while the numerous other signatories to these agreements [were] not."[31] The plaintiffs noted that NEA had a director designee, but the plaintiffs failed to explain why that fact mattered.

The plaintiffs did not plead "meaningful connections" or "managerial control" between Yates and Laskey, because the complaint failed to plead any facts about their personal relationships, working relationships, a history of voting together, or instances where they together dominated the board or the operations of the company. It was not enough that they held approximately 30% of the company's voting power, were parties to the Investor Rights Agreement and tender and support agreements, rolled-over their options, and accepted jobs with Oracle post-closing. The court distinguished *Frank v. Elgamal*, because in that case, four individuals held 71.19% of the outstanding voting power, compared to Yates and Laskey's holdings of less than 30%.[32] The complaint also lacked specific allegations of managerial control, such as the presence of subordinates or family members on the board or in the management of the company suggesting "day-to-day managerial supremacy."[33]

3. Key Takeaway

Yates was one of the earliest post-*Corwin* decisions to consider control group allegations. The decision built upon the existing precedent to avoid a rule that would lump together all early, venture, and management investors. It refined

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26. Technically the deal was a tender offer structured under 8 *Del. C.* § 251(h). The Court noted that it had already decided the question of whether *Corwin* applied to such a structure involving tendering of shares in a tender offer, rather than voting shares in favor of a merger. *Id.* at *5 (citing *In re* Volcano Corp. S'holder Litig., 143 A.3d 727, 747 (Del. Ch. 2016), *aff'd*, 156 A.3d 697 (Del. 2017) (TABLE)).

27. *Id.* (quoting Frank v. Elgamal, 2012 WL 1096090, at *8 (Del. Ch. Mar. 30, 2012)).

28. *Id* (quoting *In re* Crimson Expl. Inc. S'holder Litig., 2014 WL 5449419, at *15 (Del. Ch. Oct. 24, 2014)).

29. *Id.* at *6.

30. *Id.* (quoting *In re* Crimson Expl. Inc. S'holder Litig., 2014 WL 5449419, at *15).

31. *Id.* at *6.

32. *See* 2012 WL 1096090, at *4 (Del. Ch. Mar. 30, 2012).

33. *Yates*, 2017 WL 5953514, at *7 (quoting *In re* Cysive Inc. S'holders Litig., 836 A.2d 531, 552 (Del. Ch. 2003)).

the focus on pre-existing stockholder agreements to consider whether the agreements conferred voting or decision-making authority on specific investors in the challenged transaction, rather than on issues generally. In taking these steps, the decision provided the cornerstone for future control group rulings.

B. *In re Hansen Medical, Inc. Stockholders Litigation*[34]

The author of *Yates*, then Vice Chancellor Montgomery-Reeves, addressed the control group question again only months later in *Hansen*. In fact, the court noted in a footnote it issued *Yates* after briefing on the motion to dismiss in *Hansen* had concluded.[35] Foreshadowing the back and forth between the two decisions, the Vice Chancellor *sua sponte* distinguished *Yates* in concluding that the *Hansen* plaintiffs had pled enough facts to support an inference of a control group between two investors who owned 65% of the company's equity and had a "history of coordination" that impacted the deal.[36]

1. Background

The plaintiffs in *Hansen* challenged a squeeze-out merger. Hansen had struggled to avoid defaulting on its debt.[37] The acquirer identified certain "Key Stockholders" that it wanted to negotiate with directly to ensure their support for the merger.[38] The result of that demand was for the acquirer and the Key Stockholders to enter into "agreements that allowed the Key Stockholders, but only the Key Stockholders, to negotiate directly with" the acquirer.[39] Through those negotiations, the Key Stockholders received the ability to roll over their shares into stock of the acquirer—an option not provided to other stockholders—and agreed to vote for the merger.[40]

2. Analysis

To show that two of the Key Stockholders constituted a control group, the plaintiff cited their extensive historical ties and their large stockholdings, which comprised 65% of the equity. The court noted that those stockholders "acted in concert when dealing with their Hansen holdings," including through their initial participation in a private placement, their later participation in two additional private placements, and their outsized influence over those private placements.[41] Looking beyond Hansen, the two had a twenty-one year history of "coordinating their investment strategy in at least seven different companies," and had designated themselves as a "group" in SEC filings related to a different company.[42]

The court explained how those factors resulted in the stockholders being connected in a legally significant way:

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34. 2018 WL 3025525 (Del. Ch. June 18, 2018).

35. *Id.* at *6 n.79.

36. *Id.* at *7–8.

37. *Id.* at *2–3.

38. *Id.* at *3.

39. *Id.* at *7.

40. *Id.* at *4.

41. *Id.* at *2.

42. *Id.* at *7.

> Although each of these factors alone, or perhaps even less than all these factors together, would be insufficient to allege a control group existed, all of these factors, when viewed together in light of the Controller Defendants' twenty-one year coordinated investing history, make it reasonably conceivable that the Controller Defendants functioned as a control group during the Merger.
> . . . .
> Defendants offer reasonable explanations for some of the connections, parallel investments, and actions of the purported control group. One might even argue that they offer a more compelling version of events. It may well be that Defendants' version prevails at a later stage of litigation. At the motion to dismiss stage, however, the question is not whether Plaintiffs offer the only, or even the most, reasonably conceivable version of events. Rather, the question is whether Plaintiffs have stated a reasonably conceivable claim for which relief can be granted."[43]

The court therefore denied the defendants' motion.

3. Key takeaway

The key distinction that separated *Hansen* from *Yates* was the clear coordination by the investors and their history of investing together in other companies. Based on that factor, *Hansen* and *Yates* stand at on opposite sides of the spectrum, with each providing an example of what allegations do or do not plead a control group. As we will see, that is how both litigants and the courts have used the decisions going forward.

C. *Carr v. New Enterprise Associates, Inc.*[44]

In *Carr v. New Enterprise Associates, Inc.*, the Delaware Court of Chancery partially dismissed claims for breach of fiduciary duty brought by stockholders of Advanced Cardiac Therapeutics, Inc. ("ACT").[45] The lead plaintiff was a co-founder of ACT who alleged that New Enterprise Associates, Inc. ("NEA") was ACT's controlling shareholder and had breached its fiduciary duties orchestrating a self-interested transaction. The court held that the complaint had not adequately alleged the existence of controller.

1. Background

NEA invested in ACT in 2014 by purchasing preferred stock. NEA also entered into a voting agreement with ACT. The plaintiff alleged that soon after the investment, NEA began making changes in ACT. The plaintiff also alleged that NEA engineered the issuance of additional shares of preferred stock to increase its control of the company. The changes NEA madse included appointing a new CEO, removing two directors, and filling one of the seats.[46] The key issuance of preferred stock occurred in April 2014, when NEA and other select investors acquired Series A-2 preferred shares, resulting in NEA owning more than 65% of ACT's shares on an as converted basis.[47] The plaintiff was not invited

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43. *Id.* at *7–8.

44. 2018 WL 1472336 (Del. Ch. Mar. 26, 2018).

45. *Id.* at *1.

46. *Id.* at *3.

47. *Id.*

to participate. The consent approving the transaction acknowledged that four of the six directors had a material financial interest in the deal.[48]

The Series A-2 issuance valued ACT at approximately $15 million.[49] Six months later, ACT sold a warrant to Abbott Laboratories ("Abbott") for $25 million that gave Abbott the option to purchase all of ACT's equity for up to $185 million.[50] The Warrant Transaction was conditioned on Abbott acquiring another company, Topera, where NEA and Abbott were the principal investors.[51] Meanwhile, another bidder offered to acquire ACT for up to $300 million.[52] In October 2016, ACT repurchased the warrant from Abbott for $25 million in cash.[53] On these facts, the plaintiff alleged that NEA became ACT's controlling stockholder and then breached its fiduciary duties by orchestrating the potential sale of ACT to Abbott for an undervalued price.[54]

2. Analysis

The court dismissed the claim against NEA based on its status as a controlling stockholder for purposes of the Series A-2 transaction.[55] Ultimately, the court determined that plaintiff did not adequately plead that there was a control group at the time of the Series A-2 financing given that nothing in the voting agreement between NEA and other stockholders constituted a "pact" to work together.[56] The court concluded that the voting agreement only addressed the election of two of seven directors and did not result in NEA having control of the board. Because the allegations about NEA's status as a controller failed, the court dismissed the claims against NEA.

3. Key takeaway

Carr builds on *Yates* by focusing on the nature of the agreement. Under the court's analysis, an agreement addressing a different topic (the appointment of two of seven board seats) did not bind the parties in a legally significant way for a different transaction, such as the merger.[57] Adequately pleading a control group allegation requires additional facts showing a plan by the parties to advance common goals or interests.

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48. *Id.* at *4.

49. *Id.* at *3.

50. *Id.* at *1.

51. *Id.* at *1–2, *5.

52. *Id.*

53. *Id.* at *6.

54. *Id.* at *1.

55. *Id.* at *9–10.

56. *Id.* at *10.

57. 2018 WL 1472336, at *10 (Del. Ch. Mar. 26, 2018).

D. *Sheldon v. Pinto Technology Ventures, L.P.*[58]

The Delaware Supreme Court weighed in on control group jurisprudence in *Sheldon v. Pinto Technology Ventures, L.P.* The Court of Chancery dismissed the plaintiffs' breach of fiduciary duty claims, concluding the plaintiff failed to plead the existence of a control group. The Delaware Supreme Court affirmed and, in doing so, provided the first in depth analysis from the state's high court on what constitutes a control group.

1. Background

Through various rounds of financings, including a recapitalizing transaction, three venture capital firms (the "VCs") acquired approximately 60% of the outstanding shares of IDEV Technologies, Inc. ("IDEV").[59] After electing not to participate in the recapitalization, certain founders and stockholders were diluted from over 3.7% ownership to less than 0.1%.[60] Ultimately, IDEV was acquired for $310 million, leaving the plaintiffs with approximately $22,500 in merger proceeds, compared to more than $11.6 million that they would have received before the recapitalization.[61] The plaintiffs claimed they had standing to assert a *Gentile* claim post-closing because the VCs had acted together as a control group.[62] To support their claim, they alleged that the VCs (1) collectively owned more than 60% of the company's outstanding shares, (2) could each nominate a director to the board under a stockholders agreement, (3) had a coordinated history of co-investing, and (4) acted together to force through the recapitalization.[63] The plaintiffs analogized the facts to those present in *Hansen*.[64]

2. Analysis

The Court of Chancery dismissed the complaint, concluding there was no control group. The court compared the allegations to those in *Yates* and *Hansen* and concluded that they fell "short of those in *Hansen*, and were more akin to those in *van der Fluit v. Yates*."[65] After a detailed discussion of those decisions, the court explained that the VCs "in this case were not as intertwined, collaborative, or exclusive as the members of the *Hansen* control group."[66] That was because the plaintiffs failed to allege the same connections as those in *Hansen*, instead "merely indicat[ing] that venture capital firms in the same sector crossed paths in a few investments" which was "different from the 'long history of cooperation and coordination' in *Hansen*."[67]

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58. 2019 WL 336985 (Del. Ch. Jan. 25, 2019), *aff'd*, 220 A.3d 245 (Del. 2019).

59. *Id.* at *2–4.

60. *Id.* at *2.

61. *Id.* at *4.

62. *Id.* at *7 (citing *Gentile*, 906 A.2d 91 (Del. 2006)).

63. *Id.* at *7–8.

64. *Id.*

65. *Id.* at *9.

66. *Id.*

67. *Id.*

It was also important to the court that the VCs "were not the only participants" in the various IDEV financing rounds, and there was no agreement requiring any stockholders to vote in favor of the challenged transactions.[68] The plaintiffs lacked a response to the fact that "[o]ther investors participated in those rounds and received the same securities, but [were] not alleged to be part of the control group."[69] In sum, to the vice chancellor, the "case more closely resembles *van der Fluit* than *Hansen*," and so warranted the same result.[70]

The court also noted that plaintiffs were wrong to "seek a charitable reading of their allegations based on *Hansen*'s explanation that determining 'whether a control group exists is fact intensive' and 'particularly difficult to ascertain at the motion to dismiss stage.'"[71] Instead, *van der Fluit* made "clear the Court can decide the issue at the motion to dismiss stage, and a plaintiff must still plead facts that make the conclusion reasonably conceivable."[72]

3. Supreme Court decision

On appeal, the Supreme Court analyzed the prior Chancery cases addressing control groups and adopted the legally significant connection standard articulated in numerous Chancery decisions:

> To demonstrate that a group of stockholders exercises control collectively, the [plaintiff] must establish that they are connected in some legally significant way—such as by contract, common ownership, agreement, or other arrangement—to work together toward a shared goal. To show a legally significant connection, the [plaintiff] must allege that there was more than a mere concurrence of self-interest among certain stockholders. Rather, there must be some indication of an actual agreement, although it need not be formal or written.[73]

The Supreme Court described *van der Fluit* and *Hansen* as "two cases on opposite ends of the spectrum," and compared the facts before it to those two decisions.[74] The court agreed with the Vice Chancellor that (1) the ability of the VCs to appoint directors did not, without more, establish domination or control; (2) the plaintiffs had not pled that the VCs had a "long and close relationship" when the complaint only named four companies in which two or more of the VCs had co-invested and no instances where all three VCs participated; and (3) the stockholders agreement that bound *all* of the company's stockholders was unrelated to the merger and did not dictate action in connection with the deal. Because the complaint failed to show that the VCs had more than a "mere concurrence of self-interest," the Supreme Court concluded the Court of Chancery had correctly dismissed the complaint for failure to state a claim.[75]

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68. *Id.*

69. *Id.*

70. *Id.* at *10.

71. *Id.* at *11.

72. *Id.*

73. Sheldon v. Pinto Tech. Ventures, L.P., 220 A.3d 245, 251–52 (Del. 2019).

74. *Id.* at 250.

75. *Id.*

4. Key takeaway

As the first Delaware Supreme Court decision to address the standard for determining a control group, this decision immediately became the leading authority on the legally significant connection standard. The Supreme Court's approach of analogizing the facts of a case to the earlier precedents provided a model used in future decisions applying that standard.

E. *Silverberg v. Padda*[76]

In *Silverberg v. Padda*, the Court of Chancery partially granted a motion to dismiss claims brought by common stockholders who alleged that the directors of Health Integrated Inc. ("HII" or the "Company") breached their fiduciary duties by approving a sale in which common stockholders received no consideration.[77] In its ruling, the court ruled that plaintiffs had not adequately alleged the existence of a control group to retain standing under *Gentile*.[78]

1. Background

At various times, HII received financing from private investors by issuing both preferred shares and convertible debt.[79] The plaintiffs' complaint challenged two series of financing transactions and an asset sale.[80] The first series of financing transactions occurred between 2003 and 2012, when multiple venture capital firms invested in several rounds of preferred stock and debt instruments convertible into preferred stock.[81] The second series of financing transactions occurred between 2014 and 2016, when some of the same venture capital firms, as well as others, participated in several offerings of notes and convertible debentures.[82] Then, in June 2016, HII approved a new offering of notes convertible to a new issuance of Series C preferred shares (the "June 2016 New Notes Offering").[83] The Series C preferred shares carried liquidation rights superior to all the other classes of shares,[84] and several firms exchanged their existing securities for notes convertible to Series C preferred shares.[85] All of their shares were exchanged without the investors providing the company with any new capital.[86] Additionally, the June 2016 New Notes Offering modified an existing management equity carve-out equal to five percent of the adjusted enterprise value of the Company that guaranteed distributions to management after Series C preferred stockholders but before any Series B or B-1 preferred stockholders.[87] In December 2017, an affiliate of

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76. 2019 WL 4566909 (Del. Ch. Sept. 19, 2019).

77. *Id.* at *1.

78. *Id.* at *7 (citing *Gentile*, 906 A.2d 91).

79. *Id.* at *2.

80. *Id.* at *2–3.

81. *Id.* at *2.

82. *Id.* at *2–3.

83. *Id.* at *3.

84. *Id.*

85. *Id.*

86. *Id.*

87. *Id.*

Exlservice Holdings, Inc. ("Exlservice") acquired substantially all of HII's assets.[88] The $22 million in consideration satisfied part of the preferred stock's liquidation preference. The common stockholders received nothing.[89]

2. Analysis

The court partially granted a motion to dismiss.[90] The plaintiffs relied on the repeated investments from 2004 and 2016 to show a legally significant connection among a group of funds that collectively held more than 50% of the company's outstanding voting power.[91] The plaintiffs pointed out that by participating in the same transactions, the VC funds received the same rights,[92] but the court rejected that argument, viewing the allegations as only showing a "parallel interest among the alleged group members," not a legally significant connection.[93] The court explained that because determining whether a control group exists is fact intensive and difficult to ascertain at the motion to dismiss stage, a "formal written agreement" or "blood pact" is not necessary to prove a legally significant connection on the pleadings.[94] However, plaintiffs must show that the alleged group intended to work together toward a shared goal through a contract, common ownership, an agreement, or some other arrangement rather than allege they had "parallel interests."[95]

The plaintiffs also alleged "that the venture capital fund defendants shared an unspoken *quid pro quo*, whereby each of their board representatives approved current offerings in consideration for past or future support from other venture capital funds."[96] The court also declined to credit that argument, reasoning that the plaintiffs failed to allege that the funds were connected "in a legally significant way" as to "voting, decision-making, or other agreements that bear on the transaction[s]."[97] Therefore, the court concluded that even at the plaintiff-friendly motion to dismiss stage, plaintiffs' allegations did not support a reasonable inference of a control group and the fiduciary claims are therefore derivative.[98]

3. Key takeaway

The *Silverberg* court's analysis builds on the reasoning in *Pinto* and illustrates the difficulties in pleading a control group. Under *Silverberg*, the joint amendment of a corporate document or the approval of challenged transactions is not sufficient to make stockholders a control group.

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88. *Id.*

89. *Id.*

90. *Id.* at *13.

91. *Id.* at *6.

92. *Id.*

93. *Id.*

94. *Id.*

95. *Id.*

96. *Id.* at *7.

97. *Id.*

98. *Id.*

F. *Garfield v. BlackRock Mortgage Ventures, LLC*[99]

In *Garfield v. BlackRock*, the Court of Chancery denied a defendant's motion to dismiss a stockholder's challenge to the fairness of a reorganization, ruling that the stockholder plaintiff's complaint supported a reasonably conceivable inference that two institutional investors constituted a control group.[100] The court credited the allegations that two institutional investors exercised at least transaction-specific control because they stood to receive unique benefits from the transaction, had unilateral rights under the operating agreement to veto the reorganization, and had the right to designate four of the eleven board members of the parent corporation.

1. Background

During the 2008 financial crisis, BlackRock, Inc. ("BlackRock") and Highfields Capital Management ("HC Partners") formed Private National Mortgage Acceptance Company, LLC ("PennyMac, LLC") for the purpose of acquiring loans from financial institutions seeking to reduce mortgage exposure.[101] PennyMac LLC then formed a public REIT and sold 93.5% of the REIT's shares to public investors and 6.5% of its shares to BlackRock, HC Partners, and management.[102]

In 2013, the parties completed an "Up-C" transaction to place a new publicly traded corporation, PennyMac, Inc. (collectively with PennyMac, LLC, "PennyMac") above PennyMac, LLC.[103] PennyMac, Inc. issued Class A common stock to the new public stockholders.[104] These Class A common stockholders owned 15% of the voting rights and 100% of the economic rights in PennyMac, Inc. The corporation also issued Class B common stock to existing PennyMac, LLC Unitholders (the "LLC Unitholders") that carried the remaining 85% of the voting rights of PennyMac.[105] The Up-C offering documents described BlackRock and HC Partners as "strategic investors/partners."[106] The Up-C structure was designed in part to allow the LLC Unitholders to realize tax benefits.[107]

In 2018, Kurland proposed a reorganization that would allow the LLC Unitholders to exchange their units for common stock in a tax-free exchange.[108] The proposed reorganization required a majority vote of the PennyMac stockholders voting as a single class, and so Kurland, BlackRock, and HC Partners could deliver the necessary vote.[109] The

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99. 2019 WL 7168004 (Del. Ch. Dec. 20, 2019).

100. *Id.* at *1.

101. *Id.*

102. *Id.* at *2.

103. *Id.*

104. *Id.*

105. *Id.*

106. *Id.*

107. *Id.*

108. *Id.* at *3.

109. *Id.*

Board established a special committee to evaluate the reorganization.[110] The special committee recommended the full board approve the reorganization, which it did.[111]

Before final approval, HC Partners and BlackRock sought, and the board approved, a new provision that required the consent of HC Partners and BlackRock to terminate the reorganization.[112]

After stockholders approved the reorganization and it closed, a Class A stockholder sued the BlackRock, HC Partners and PennyMac directors who did not serve on the special committee, alleging that BlackRock and HC Partners constituted a control group.[113] The plaintiff argued that the reorganization created benefits for the defendants who held units in the LLC, but not for the stockholders who held Class A common stock in PennyMac.[114] The defendants moved to dismiss, arguing that they should obtain the deference of the business judgment rule because the reorganization was cleansed under *Corwin*.[115]

2. Analysis

The court declined to dismiss the plaintiff's claim, ruling that the plaintiff alleged sufficient facts to allow the court to infer that BlackRock and HC Partners constituted a control group, rendering entire fairness the proper standard of review.[116] The court first focused on the following allegations: (i) BlackRock and HC Partners controlled 46.1% of the voting stock, (ii) they had unilateral rights to block the reorganization, and (iii) they each had the right to appoint two representatives to the Board for a total of four out of eleven.[117]

Having decided that "control" was adequately alleged, the court then applied the "legally significant connection" test to determine if BlackRock and HC Partners could be treated as a group, describing that "an array of plus factors" suggested both historical ties and transaction-specific ties.[118] There was a ten year history of co-investment in PennyMac with no gaps, along with that documents that referred to them interchangeably as "Sponsor Members" and strategic partners, plus public disclosures similarly using similar nomenclature.[119] There were also transaction-specific ties including: (i) management meeting with BlackRock and HC Partners multiple times before ever presenting Kurland's proposal to the Board; (ii) management not meeting with BlackRock and HC Partners separately; (iii) management meeting jointly with BlackRock and HC Partners to negotiate the Reorganization and granting them preferential review before the Board had considered the proposal; (iv) management's presentations depicting BlackRock and HC Partners as a collective unit; and (v) BlackRock and HC Partners' ultimate success in securing "a late-in-the-game revision in the form of an exclusive [termination right]."[120]

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110. *Id.*

111. *Id.*

112. *Id.*

113. *Id.*

114. *Id.* at *7

115. *Id.* (citing *Corwin*, 125 A.3d 304).

116. *Id.* at *12.

117. *Id.* at *8.

118. *Id.* at *9.

119. *Id.*

120. *Id.* at *9–10.

The court rejected the Defendants' argument that the interests of BlackRock and HC Partners were not aligned due to differential tax treatment, explaining that "despite the distinguishable tax differences, BlackRock and HC Partners shared an interest in gaining a maximum percentage of the combined entity by optimizing the exchange ratio."[121] The court also rejected Defendants' argument that there could be no reasonable inference of a control group because no written agreement executed by BlackRock and HC Partners provided them rights in connection with the reorganization.[122]

The court noted that a lack of formal or written agreement pertaining to the transaction is not fatal, and that the totality of the facts made it reasonably conceivable at the pleading stage that BlackRock and HC Partners were a control group.[123]

3. Key Takeaway

The *Garfield* case demonstrates that the control group test is a holistic analysis in which the existence of multiple "plus" factors can support an inference of a control group.[124] While no single historic or transaction-specific tie standing alone would have been sufficient, the factors taken together were enough. *Garfield* also makes clear that just as with a single stockholder, a control group does not need to own a majority of the company's voting power to be deemed to have control.[125]

G. *In re USG Corporation Stockholder Litigation*[126]

In this opinion, the court granted a motion to dismiss claims brought by former USG Corporation ("USG") stockholders alleging breaches of fiduciary duty in connection with USG's sale to a strategic buyer ("Knauf").[127] Again applying the "legally significant" connection test from recent precedent, the court held that plaintiffs had not adequately pled the existence of a control group.

1. Background

USG was a manufacturer and distributor of building materials.[128] Knauf beneficially owned approximately 10.6% of USG's outstanding common stock at the time that the merger agreement was executed (the "Merger Agreement"), and had done multiple transactions with USG (including a joint venture and purchasing a USG division).[129] Berkshire initially acquired a stake in USG in 2000 on the open market.[130] Berkshire later provided a backstop

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121. *Id.*

122. *Id.*

123. *Id.* at *10–11.

124. *Id.*

125. *Id.*

126. 2020 WL 5126671 (Del. Ch. Aug. 31, 2020). It should be noted that in chronological order, a decision in *Skye Mineral Investors, LLC v. DXS Capital (U.S.) Ltd.*, 2020 WL 881544, (Del. Ch. Feb. 24, 2020) comes next. We have omitted *Skye Minerals* because it involved a limited liability company rather than a corporation and dealt with unique features of that entity.

127. *USG*, 2020 WL 5126671 at *1, *3.

128. *Id.* at *3.

129. *Id.*

130. *Id.*

commitment to purchase USG shares as part of a rights offering, and through those purchases and subsequent open market purchases and transactions involving convertible notes, increased its ownership to approximately 31% of the outstanding stock.[131]

In 2017, Knauf contacted Berkshire about acquiring Berkshire's stake for $40 per share.[132] Knauf subsequently proposed to USG to acquire all of its common stock for $40.10 per share.[133] The Board discussed the offer and the possibility of a hostile takeover by Knauf, which Berkshire could support because of its interest in exiting its investment in USG.[134] The Board believed that USG's intrinsic value was $50 per share, and it rejected Knauf's proposal as "inadequate and insufficient."[135]

In 2018, Knauf proposed to acquire USG for $42 per share and indicated that Knauf and Berkshire could launch a tender offer if USG refused to negotiate in good faith.[136] Berkshire later gave Knauf an option to purchase its USG shares for $42 per share.[137] When USG rejected Knauf's proposal as inadequate, Knauf successfully carried out a withhold campaign for four of USG's director nominees.[138] After that, USG agreed to a deal at $44 per share.[139] After the deal closed, a USG stockholder challenged the transaction as a breach of duty and alleged that Knauf and Berkshire constituted a control group.

2. Analysis

The court granted the defendant's motion to dismiss.[140] The plaintiffs conceded that the alleged control group "never entered a meeting of the minds" and that Berkshire's interests were "allied with the other unaffiliated stockholders."[141] Although the complaint's allegations supported an inference that both Knauf and Berkshire sought a sale of USG, their "interests diverged regarding the most important detail of the Acquisition: the price."[142] Berkshire wanted to sell its USG shares at the highest possible price. Knauf wanted to buy USG at the lowest possible price.[143] The court described the allegations about the withhold campaign as merely suggesting concurring self-interest rather than the

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131. *Id.*

132. *Id.*

133. *Id.*

134. *Id.*

135. *Id.* at *6, *19.

136. *Id.* at *6.

137. *Id.* at *7.

138. *Id.*

139. *Id.* at *11.

140. *Id.* at *31.

141. *Id.*

142. *Id.*

143. *Id.*

existence of a control group.[144] As a result, the court ruled that plaintiffs did not adequately plead the existence of a control group.[145]

3. Key Takeaway

USG shows that sometimes plaintiffs have weak cases. The opinion focused on the relationship of the alleged control group as they sat at the negotiating table. The court's conclusion makes clear that the interests of the alleged group members must align. Being on opposite sides of that table with incentives to negotiate for a better deal at the expense of the other is a factor that weights strongly against the existence of a control group.[146]

H. *In re Tilray, Inc. Reorganization Litigation*[147]

In *In Re Tilray Inc. Reorganization Litigation*, the court denied a motion to dismiss claims brought by the minority stockholders of Tilray, Inc. ("Tilray") who alleged that Tilray's directors and the founders of Privateer, a private equity firm with a majority stake in Tilray, breached their fiduciary duties by entering into a down-stream merger to gain a tax benefit not available to the minority stockholders.[148] The court credited that the plaintiffs adequately alleged the existence of a control group.

1. Background

In 2010, three friends quit their jobs to form Privateer, a private equity firm engaged in investing in the cannabis industry.[149] The "Founders," as the court referred to them, held a 70% voting stake in Privateer, and eventually they formed Tilray as a subsidiary to conduct cannabis research, cultivation, and distribution.[150] Privateer took Tilray public at $17 per share, bringing the value of Privateer's shares in Tilray to $1.275 billion.[151] In connection with the IPO, Privateer's shares converted into Class 1 common stock, carrying ten votes per share, while Tilray offered nine million shares of Class 2 common stock, carrying one vote per share, to the public. When the IPO closed, Privateer held a 75% economic interest in Tilray and controlled over 90% of its voting power.[152]

The Founders desired to access some of their new-found wealth but could not do so without incurring significant tax liabilities. Plus, significant sales could cause Tilray's stock price to plummet. To address these issues, the Founders

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144. *Id.*

145. *Id.*

146. *Id.*

147. 2021 WL 2199123 (Del. Ch. June 1, 2021). Chronologically, *In re Pattern Energy Group Inc. Stockholders Litigation*, 2021 WL 1812674 (Del. Ch. May 6, 2021) is next. That decision has a lengthy discussion of the "soft power" that can lead to a control group, but said that because the "inquiry is highly fact intensive," it was "declin[ing] to make a definitive determination" on the issue, and instead would analyze it "after the record is developed through discovery." 2021 WL 1812674 at *46. Given that approach, we have not included an analysis of that discussion.

148. 2021 WL 2199123, at *1.

149. *Id.* at *1.

150. *Id.* at *2.

151. *Id.*

152. *Id.* at *3.

contemplated a two-step reorganization of Privateer and Tilray (the "Reorganization").[153] The first step involved spinning-off Privateer's other portfolio companies. The second step involved a downstream merger in which Tilray would cancel Privateer's Tilray stock and issue Tilray stock to Privateer's stockholders.[154] The IRS would treat the share cancellation and subsequent stock issuance as a tax-free reorganization, allowing the Founders to avoid the tax consequences of a sale or distribution of its Tilray stock while maintaining control over Tilray.[155]

After the company completed the steps of the reorganization, including closing on the downstream merger, plaintiffs, holders of Tilray Class 2 stock, challenged the Reorganization, claiming that the Founders, working as a control group with Privateer, used the Reorganization to perpetuate control over Tilray and used the Reorganization to extract non-ratable tax benefits from Tilray and its minority stockholders.[156] The plaintiffs also brought a derivative breach of fiduciary duty claim against Tilray and certain Tilray directors.[157] The defendants argued that the complaint failed to adequately allege that the Founders comprised a control group.

2. Analysis

The court denied the motion to dismiss in its entirety, concluding the plaintiffs had adequately alleged that the Founders and Privateer constituted a control group given the many ties—both historical and transactional—among them.[158] The court, discussing the recent precedent and the "spectrum" described in *Sheldon*, concluded that "the control-group allegations as to the Founders veer far toward the *Hansen* side of the spectrum and perhaps state a stronger case than the allegations in *Hansen*."[159] These allegations included that the individuals had a long-time friendship, co-founded Privateer and other companies together, worked in the same office space, retained joint advisors, and acted as voting block when approving for the Reorganization.[160] The Founders also had a shared interest of avoiding massive tax liability through the Reorganization—an interest unique to the Founders and not shared by the minority stockholders—which motivated the Founders to act in lock-step in structuring and approving the Reorganization and exerting control.[161]

3. Key Takeaway

The *Tilray* decision confirms the fact intensive nature of the analysis and the importance of historical ties. In *Tilray*, the longstanding social ties between the individuals supported an inference of shared goals and motivations. The member of the alleged group also received a unique benefit from the transaction. Taken as a whole, these facts supported the existence of a control group.

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153. *Id.*

154. *Id.*

155. *Id.*

156. *Id.* at *8.

157. *Id.*

158. *Id.* *10–11.

159. *Id.* at *11.

160. *Id.*

161. *Id.* at *11.

I. *Patel v. Duncan*[162]

In *Patel v. Duncan*, the Court of Chancery dismissed claims by a stockholder of Talos Energy, Inc. ("Talos") alleging that two private equity funds, Riverstone and Apollo, who collectively held a majority of stock in Talos, comprised a control group and caused Talos to overpay in two transactions that allegedly unfairly benefited affiliates of the two private equity funds.[163] In so ruling, the court held allegations that Riverstone and Apollo comprised a control group to be insufficient.

1. Background

In 2012, defendant Timothy Duncan formed the original Talos entity, backed by private equity funds affiliated with Riverstone and Apollo.[164] Talos eventually combined with Stone Energy Corporation ("Stone Energy"). Riverstone and Apollo entered a stockholders' agreement that permitted them to appoint a majority of the board. After the combination, Riverstone and Apollo owned a majority of the company's voting power.[165] The company's public disclosures described it as a "controlled company" under applicable New York Stock Exchange (NYSE) Rules, stating: "We are controlled by Apollo Funds and Riverstone Funds. The interests of Apollo Funds and Riverstone Funds may differ from the interests of our other stockholders."[166]

During this time period Riverstone and Apollo worked together on other transactions that failed. Those were a $7.2 billion buyout of an entity that then declared bankruptcy (causing Apollo to lose over $2 billion and Riverstone over $600 million), as well as a loan Apollo provided to an entity known as Whistler, which went bankrupt and cost Apollo over $100 million, though it received the right to distributions until it was paid back on its original loans. Talos eventually acquired Whistler, allegedly making Apollo nearly whole on its Whistler investment. The plaintiff alleged that Talos overpaid for Whistler to bail out Apollo, which Riverstone went along with based on an understanding that it would get its own "sweetheart" deal.

That opportunity presented itself in 2019 when Talos acquired a portfolio of assets from entities affiliated with Riverstone (the "Challenged Transaction").[167] The plaintiff alleged that Talos "grossly overpaid" in the Challenged Transaction to follow through on getting Riverstone a "sweetheart" deal.[168]

The plaintiff alleged that the terms of the Challenged Transaction were unfair to Talos, including by providing the sellers with a new series of stock rather than common stock.[169] The plaintiff alleged that the transaction structure did not benefit Talos but rather enabled the Challenged Transaction to close more quickly without the need for a stockholder vote.[170]

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162. 2021 WL 4482157 (Del. Ch. Sept. 30, 2021), *corrected* (Oct. 4, 2021), *aff'd* 277 A.3d 1257 (Del. May 25, 2022) (TABLE).

163. *Id.* at *1.

164. *Id.* at *2.

165. *Id.* at *3.

166. *Id.*

167. *Id.* at *5–6.

168. *Id.* at *6–7.

169. *Id.* at *5–6.

170. *Id.* at *5–7.

The plaintiffs alleged that Apollo and Riverstone breached their fiduciary duties as controlling stockholders. The defendants moved to dismiss.

2. Analysis

The court granted the motion to dismiss. In arguing that a control group existed, plaintiff pointed to four factors: (1) Apollo and Riverstone's historical relationship, including Talos's purchase of Whistler; (2) Talos's disclosure that it was a controlled company, (3) the stockholders' agreement permitting Apollo and Riverstone to appoint a majority of the Board's directors, and (4) the participation of representatives from Riverstone and Apollo in the meetings where the Board discussed the Challenged Transaction.[171]

The court determined that the alleged historical ties between Riverstone and Apollo were weaker than those found in cases like *Garfield* and *Hansen*, distinguishing those cases and explaining that while the relationship between Riverstone and Apollo within Talos was significant, the two firms crossed paths in only one other transaction.[172] Second, the court determined that the public disclosure was relevant, but only addressed an NYSE rule.[173] Third, the court viewed the stockholder's agreement as non-dispositive because the agreement allowed them to appoint a majority of directors did not bear on the Challenged Transaction or bind them beyond selecting directors.[174] Fourth, the court brushed aside the argument that the mere existence of representatives at the Board meeting discussing the Challenged Transaction was suggestive of a control group, deciding that the presence of controlling stockholders at such a meeting to be expected.[175]

Having given little credence to the alleged "plus factors," the court declined to credit the *quid pro quo* arrangement. The court concluded by stating:

> In the end, Plaintiff's most significant pleading deficiency lies in the failure of his *quid pro quo*, the only argument he makes to support a transaction-specific agreement between [Apollo and Riverstone]. Though it is true Riverstone and Apollo have coinvested in Talos and crossed paths previously, the absence of any allegation or indication that they struck an agreement to work together, as in *Silverberg*, is fatal to Plaintiff's theory.[176]

This decision was appealed to the Delaware Supreme Court, which affirmed in a one page order stating the en banc court found "it evident that the judgment of the Court of Chancery should be affirmed on the basis of and for the reasons stated in the court's Memorandum Opinion dated October 4, 2021."[177]

3. Key Takeaway

Patel confirms that despite being a fact intensive analysis at the plaintiff-friendly pleading stage, the court is willing to grant a motion to dismiss without sufficient allegations. Importantly, the plaintiff's only transaction-specific tie

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171. *Id.* at *11.

172. *Id.* at *11–13.

173. *Id.* at *12.

174. *Id.* at *13.

175. *Id.* at *14.

176. *Id.* at *16.

177. *Patel v. Duncan*, 277 A.3d 1257 (Del. May 25, 2022) (TABLE).

alleged in this case was a *quid pro quo* between the alleged controlling parties, but the complete lack of any informal or formal agreement between the alleged controllers caused such argument to fail.

The lack of transaction-specific factors alleged, combined with the weakness of the alleged non-transaction specific "plus factors" was insufficient.[178]

III. TAKEAWAYS FROM RECENT DECISIONS

The recent decisions, read together, demonstrate the court's reluctance to sustain control group allegations, perhaps even more so than in the context of a single controller.[179] The result is a clear difficulty to plead the existence of a control group. In six of the nine decisions issued since 2017 (*Yates*, *Carr*, *Sheldon*, *Silverberg*, *USG*, and *Patel*), the court ruled the plaintiff had not sufficiently pled the existence of a control group. When one considers the gravity of the "controlling stockholder" designation,[180] this reluctance is understandable.[181] It avoids eroding the business judgment rule through increasing second guessing of corporate actions that merely had the support of multiple "stockholders united only by a common view of what will optimize the value of their shares,"[182] and recognizes the difference required in between a single controller and a control group.[183] *Patel* thus punctuates the series by reiterating "[w]hile the plaintiff-friendly pleading standard and fact-intensive nature of the control group inquiry loom large at this stage, these concerns do not

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178. There was one additional decision issued by the Court addressing a control group argument. In *Lockton v. Rogers*, 2022 WL 604011 (Del. Ch. Mar. 1, 2022), the plaintiff alleged that the various members of the board themselves made up a control group. The court rejected the argument, concluding they merely had "parallel interests." *Id*. at *14. We do not elaborate further because the claim that the directors, who already owed fiduciary duties, should be held to be a control group is an outlier not addressed in other opinions that focused on whether the fiduciary duty obligations of a controlling stockholder should be imposed on a group of stockholders who otherwise did not owe fiduciary duties.

179. *See In re* Crimson Expl. Inc. S'holder Litig., 2014 WL 5449419, at *12 (Del. Ch. Oct. 24, 2014) ("Absent a significant showing 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.").

180. *See Patel*, 2021 WL 4482157, at *10 ("Plaintiff's theory that the Venture Capital Defendants formed *a control group is the central feature* in the Complaint. The *viability of this theory* informs the standard of review, the availability of breach of fiduciary duty claims against the Venture Capital Defendants, and the number of Board members that may be considered interested in the Challenged Transaction.") (emphasis added); *see also* Lipton, *supra* note 19, at 827 ("Under Delaware doctrine, a single label--controlling shareholder--carries an enormous amount of legal weight. Once the label is applied to a person or institution, that entity is immediately subject to unique legal treatment along three distinct dimensions."); Note, *Controller Confusion: Realigning Controlling Stockholders and Controlled Boards,* 133 HARV. L. REV. 1706, 1712 (2020) (stating "controlling stockholder status remains significant, both for the individual in acquiring fiduciary duties and for the board that may find its decisions subject to heightened scrutiny and difficult to cleanse").

181. There admittedly is disagreement about whether Delaware law has found a satisfying resting place. *Compare* 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, 347 (2022) (describing downsides of expanding the definition of control group and praising the Delaware Supreme Court's decision in *Sheldon*, and subsequent decisions such as *Patel*, as "cabin[ing] th[at] danger," while criticizing *Hansen* and other decisions as "troublesome") *with* Gabriel Rauterberg, *The Separation of Voting and Control: The Role of Contract in Corporate Governance*, 38 YALE J. ON REG. 1124, 1170 (2021) (noting mistake of thinking "there is a simple answer that the Delaware Supreme Court missed" in *Sheldon* while proposing "approach build[ing] on a truth [*Sheldon*] ignores concerning aggregating ownership of significant blockholders").

182. 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, 347 (2022).

183. Da Lin, *Beyond Beholden*, 44 J. CORP. L. 515, 518–19 (2019) (describing findings that are "consistent with classic narratives about power: a single person with consolidated control has greater power to reward or sanction than a group of decision-makers who share control because the single person can act unilaterally and her authority over the controlled company is plenary").

require the Court to 'pile up questionable inferences until such a conclusion is reached.'"[184] Although the Supreme Court quickly affirmed *Patel* by order rather than issuing a written opinion (as it had done in *Sheldon*), this should only emphasize the precedential value of the Chancery opinion.[185]

But difficult does not mean impossible, and by explaining which facts constitute sufficiently persuasive allegations of concerted action to plead control, the decisions also animate a key principle underlying Delaware's *MFW* jurisprudence, which is that stockholders are best protected by proactively implementing procedural protections.[186] In the three decisions denying motions to dismiss it is hard to deny that the pled connections reflected significant power to influence the company.[187] In *Hansen* that was a two-decade long history of investing together that continued with multiple investments in the company at issue, and direct negotiations with the acquirer.[188] In *Garfield*, that included coordinated involvement that led to the company describing the stockholders as "strategic partners," who had preferential input and influence on the transaction.[189] In *Tilray* it took the form of the company's founders, who had strong personal ties, working toward a shared goal of minimizing tax liabilities associated with early investments, which was not an issue for other stockholders.[190] These are all fact patterns consistent with the increasing complexity of corporate capital and stockholder structures described above. Although a common thread between the decisions, it is not an outcome dispositive one. The powers and rights of the stockholders in *Hansen*, *Garfield*, and *Tilray* were specifically those associated with venture capital or early investors, and the transactions in *Garfield* and *Tilray* were complicated reorganizations, rather than third party mergers. Yet *Yates* and *Sheldon* dealt with similar allegations and relationships, and multiple opinions analyzing a single stockholder make clear that specific powers such as a blocking right "standing alone [are] highly unlikely to support either a finding or a reasonable inference of control."[191]

All of this means—perhaps for the better—that control group status is not something investors are likely to stumble into unwittingly. The added clarity connects with another principle animating *MFW*, and specifically its *ab initio* requirement, which Delaware courts continue to encourage parties to avail themselves of to avoid litigation risk,[192] because

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184. *Patel*, 2021 WL 4482157, at *11 (citing *In re* Crimson Exploration Inc. S'holder Litig., 2014 WL 5449419, at *15 (Del. Ch. 2014)).

185. *Patel*, 277 A.3d 1257; *Sheldon*, 220 A.3d 245.

186. *In re* MFW S'holders Litig., 67 A.3d 496, 526 (Del. Ch. 2013) (stating "the court concludes that the rule of equitable common law that best protects minority investors is one that encourages controlling stockholders to accord the minority this potent combination of procedural protections"), *aff'd sub nom.* Kahn v. M & F Worldwide Corp., 88 A.3d 635 (Del. 2014).

187. As noted in note 149, *supra*, *In re Pattern Energy Group Inc. Shareholders Litigation* arguably fits with these decisions, though technically the court "decline[d] to rule on the Motions to dismiss" the control group allegation "until a later stage in these proceedings." 2021 WL 1812674, at *46.

188. 2018 WL 3025525 (Del. Ch. June 18, 2018).

189. 2019 WL 7168004 (Del. Ch. Dec. 20, 2019).

190. 2021 WL 2199123 (Del. Ch. June 1, 2021).

191. Basho Techs. Holdco B, LLC v. Georgetown Basho Invs., LLC, 2018 WL 3326693, at *26 (Del. Ch. July 6, 2018); *see also* Thermopylae Cap. P'rs, L.P. v. Simbol, Inc., 2016 WL 368170, at *13 (Del. Ch. Jan. 29, 2016) ("Under Delaware law, however, contractual rights held by a non-majority stockholder do not equate to control, even where the contractual rights allegedly are exercised by the minority stockholder to further its own goals.").

192. *See In re* Tesla Motors, Inc. S'holder Litig., 2022 WL 1237185, at *48 (Del. Ch. Apr. 27, 2022) ("Before addressing the merits, I cannot help but observe that Elon (and the rest of the Tesla Board members) likely could have avoided this expensive and time-consuming litigation had they just adopted more objectively evident procedural protections. … That Elon and the Tesla Board failed to follow this clear guidance and yet prevailed here should not minimize those incentives or dilute the implications of the onerous

stockholders need to know they are controllers in order to implement *MFW*.[193] Uncertainty about whether one is part of a control group decreases the likelihood of utilizing *MFW* because the stockholders may be unwilling to in essence concede they are part of such a group by stating they will abide by *MFW*. Why would one make such a concession if he or she did not think they were part of a control group?

One final point: the decisions discussed in this article all involved pleading-stage motions. One outstanding issue that has yet to play out post-*Corwin* is what it takes parties to succeed at trial in showing there was or was not a control group, after the court had determined on the pleadings that the existence of one was reasonably conceivable.[194] Of the decisions discussed above that denied motions to dismiss and let the claims proceed, *Hansen*, *Garfield*, and *Tilray* have all settled. A similar control issue has been litigated through trial in at least one recent decision, *In re Tesla Motors, Inc. Stockholder Litigation*, though the allegations focused on a single controlling stockholder, rather than a control group.[195] Still that case fit the fact pattern of a defendant after trial arguing that the plaintiffs had failed to prove the existence of a controller, which it turned out was one of a myriad of issues that the court did not decide.[196]

If the control group issue has in fact been adequately addressed, it may be that the facts that would sustain the allegation do not exist. That seems unlikely given the dynamic of increasingly complex and bespoke governance structures described above. If such a case is tried, like all Chancery decisions the outcome will be heavily fact-dependent, turning on a weighing of whether the *allegations* of control that sustained the claims at the pleading stage survived discovery such that they could become *findings of fact*.

IV. DELAWARE'S COMMON LAW IN ACTION

What the decisions say is as important as how they were made and what that process shows about how Delaware makes its corporate law. These decisions, issued in about four years, show the "dynamism inherent in the common law

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entire fairness standard of review. Their choices constricted the presumptive path to business judgment deference and subjected Elon's conduct to post-trial judicial second-guessing. In other words, if Chancery opinions are 'parables,' let this be a parable of unnecessary peril, despite the outcome."); *id.* at *48 n.557 (noting "defense verdicts after an entire fairness review of fiduciary conduct are not commonplace—hence the advisability of structuring transactions to avoid such scrutiny as a matter of law"); *see also* Ann Lipton, *Will He or Won't He?,* Law Professor Blogs Network (July 17, 2021), https://lawprofessors.typepad.com/business_law/2021/07/will-he-or-wont-he.html (stating "some *ex ante* doubt about controller status" may better incentivize boards to "be strict about cleansing mechanisms").

193. *See In re* Rouse Props., Inc., 2018 WL 1226015, at *1 n.6 (Del. Ch. Mar. 9, 2018) ("Of course, when the corporation in which the minority blockholder owns shares does not recognize that blockholder as a controlling stockholder, its board of directors has no incentive to implement the dual protections prescribed by *MFW* (affirmed by *M&F Worldwide* [sic]). That, in turn, leaves the board exposed to entire fairness review in the event the court in a post-closing challenge to an allegedly conflicted controller transaction disagrees with the board's assessment and determines that the blockholder is, as a matter of law and fact, a controlling stockholder.").

194. One pre-*Corwin* opinion was decided post-trial, though there is no indication that it followed a motion to dismiss. *In re* PNB Hldg. Co. S'holders Litig., 2006 WL 2403999, at *10 (Del. Ch. Aug. 18, 2006).

195. 2022 WL 1237185, at *1 (Del. Ch. Apr. 27, 2022).

196. *Id*. at *2 ("Against this factual backdrop, the plaintiffs' claims against [the alleged controller], and [the alleged controller's] defenses, call out like a carnival barker, beckoning the Court to explore a wide range of interesting and arguably unsettled legal issues, including, among others, the contours and nuances of Delaware's controlling stockholder law . . . . To be sure, in answer to the barker's call, it is tempting to venture into each tent and confront the legal enigmas that await there. Given the clarity provided by compelling trial evidence, however, there is no need to take on the challenge of discerning the appropriate standard of review by which to decide the plaintiffs' claims. Even assuming (without deciding) [the existence of a] controlling stockholder, the Tesla Board was conflicted, and the vote of the majority Tesla's minority stockholders approving the Acquisition did not trigger business judgment review, such that entire fairness is the standard of review, the persuasive evidence reveals that the Acquisition was entirely fair.").

process of adjudication" given Delaware's place at the center of American corporate law.[197] The term common law is often used generally, or as an antonym to a civil law or code jurisdiction, but as others have, we want to be clear about the specific version of common law decision-making that Delaware uses to refine its corporate law.

"In many respects, Delaware's corporate law may be the last vestige of the classical 19th century common law model in America: most important legal rules are promulgated by a nonpartisan, expert judiciary; these rules are presented as derived from long-standing and widely accepted principles; the law is enforced through civil litigation brought by private parties; and even legislative amendments generate neither debate nor controversy."[198] These traits of Delaware's corporate law "represent a rather pure, and therefore rather unfamiliar, form of the common law system."[199] In this "common law fashion," the case before the court "is decided and the law is thereby evolved incrementally" with "the overall body of case law coherently fill[ing] in a map that guides transactional and corporate governance advisors in charting a course for their clients that is relatively risk free."[200]

In practice, this creates, in the words of Vice Chancellor Parsons, a "phenomenon of multiple cases posing different facets of timely questions of corporate law."[201] This phenomenon is "the natural consequence of the Court of Chancery's role as the United States' premier business court," as the resulting "volume of cases that it hears contributes importantly to this valuable predictability, even in a dynamic economic and capital marketplace."[202] Thus, "[a]s surely as Rome was built brick-by-brick, so too has Delaware developed its corporate jurisprudence case-by-case."[203] Former Chief Justice Strine has similarly written "the continued importance of the common law of corporations is not the result of happenstance, but reflects a policy choice made by the Delaware General Assembly. That choice deliberately deploys Delaware's judiciary to guarantee the integrity of our corporate law through the articulation of common law principles of equitable behavior for corporate fiduciaries."[204] A distinguished Chancery practitioner describes "[t]he success of the Chancery system" as "depend[ing] on its exposure to, and adjudication of, a large and representative docket of cases challenging transactions with Delaware-incorporated targets. The large size of the docket affords the court the necessary opportunities to develop and refine corporate law in the transactional context."[205] And there is no shortage of academic articles noting the responsiveness of Delaware's judiciary to a large volume of "hot" corporate topics as contributing to its

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197. Leo E. Strine, Jr., *The Inescapably Empirical Foundation of the Common Law of Corporations*, 27 DEL. J. CORP. L. 499, 513 (2002).

198. Marcel Kahan & Edward Rock, *Symbiotic Federalism and the Structure of Corporate Law*, 58 VAND. L. REV. 1573, 1577 (2005); *see also* Leo E. Strine, Jr., *If Corporate Action Is Lawful, Presumably There Are Circumstances in Which It Is Equitable to Take That Action: The Implicit Corollary to the Rule of Schnell v. Chris-Craft*, 60 BUS. LAW. 877, 878 (2005) (stating "many of the important principles of American-style corporate law come in the form of judge-made common law.").

199. Kahan & Rock, *supra* note 195, at 1610.

200. 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, 683 (2005).

201. Donald F. Parsons, Jr. & Jason S. Tyler, *Docket Dividends: Growth in Shareholder Litigation Leads to Refinements in Chancery Procedures*, 70 WASH. & LEE L. REV. 473, 476 (2013); *see also id.* at 524 ("Delaware's volume of corporate and alternative business entity cases, the fact that those cases are litigated before the relatively small, but expert, Delaware Court of Chancery and Supreme Court, and the responsiveness of its courts, its legislature, and the marketplace generally accelerate the development of refined doctrine, measured balance, and valuable predictability.").

202. Parsons & Tyler, *supra* note 198, at 476.

203. *Id.* at 483–84.

204. Strine, *supra* note 199, at 879.

205. William Savitt, *The Genius of the Modern Chancery System*, 2012 COLUM. BUS. L. REV. 570, 598 (2012).

success and renown.[206] The above survey of control group decisions, decided in rapid succession after the confluence of *Gentile*, *Corwin*, and changing funding mechanisms and capital structures, presents only one further example of this dynamic playing out in Delaware.

V. CONCLUSION

The preceding survey describes the development of a robust "spectrum" of decisions that now serve as analogies to help categorize new cases. As a result of the enhanced clarity that has come from the evolution of this body of case law, 2022 saw little further development in the area. A confluence of factors likely led to this development, including (i) *Gentile*'s fall (which we would suggest was at least in part hastened by how frequently such claims were brought in the context of control group arguments), (ii) transactional planners identifying potential control groups and either restructuring transactions or implementing *MFW* style protections to assure the application of the business judgment rule, (iii) plaintiff stockholders not bringing claims that are now weak under the court's precedent, and (iv) defense counsel similarly deciding against bringing weak motions to dismiss. How much each of these factors contributed to the lack of noteworthy developments in 2022 is unclear. But what is clear is that Delaware remains committed to a common law process that refines its corporate law iteratively and quickly, ensuring that it continues to provide valuable guidance to lawyers and their clients dealing with pressing corporate law issues.

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206. *See, e.g.*, Omari Scott Simmons, *Branding the Small Wonder: Delaware's Dominance and the Market for Corporate Law*, 42 U. RICH. L. REV. 1129, 1159 (2008) ("Delaware courts are often the first responders to corporate law controversies."); Jill E. Fisch, *The Peculiar Role of the Delaware Courts in the Competition for Corporate Charters*, 68 U. CIN. L. REV. 1061, 1063 (2000) ("The large volume of business litigation in Delaware, coupled with Delaware's specialized court system, results in a well developed collection of corporate law precedents.").