Cooley

Delaware Supreme Court Reverses Chancery Court, Holds Business Judgment Review Applicable to Tripadvisor's Decision to Reincorporate in Nevada

February 7, 2025

Delaware corporations contemplating conversion to another state should take note of the Delaware Supreme Court's recent decision in *Maffei, et al. v. Palkon, et al.*, in which the court ruled that Tripadvisor's decision to reincorporate in Nevada was subject to business judgment review because no existing or threatened litigation was alleged.

On February 4, 2025, the Delaware Supreme Court reversed the decision of Vice Chancellor J. Travis Laster of the Delaware Court of Chancery that entire fairness review applied to the Tripadvisor board's decision to approve corporate conversions to Nevada for Tripadvisor and Liberty TripAdvisor Holdings (Liberty). The court held that the business judgment rule was the applicable standard of review because no member of the board, including the alleged controller, received a material non-ratable benefit from the conversions.

Key to the court's decision was its disagreement with the Chancery Court's holding that the temporal distinction between existing and future potential liability did not affect whether the alleged non-ratable benefit (i.e., reduced litigation exposure) was material. After a lengthy review of precedent, the court held that temporality weighs heavily in determining materiality, and the lack of any alleged existing or threatened litigation claims that would be impaired by the conversion weighed heavily against finding the alleged non-ratable benefit material. The court noted that the record indicated the board's decision to reincorporate was made on a "clear day."

Background

For background on this case, please see our March 2024 blog post on the Chancery Court decision.

In April 2024, the Delaware Supreme Court granted an interlocutory appeal to clarify the standard of review applicable to board decisions to reincorporate in another state. The parties briefed the appeal, and the Delaware Supreme Court heard oral arguments in October 2024.

In January 2025, the plaintiffs filed a motion to dismiss the Tripadvisor appeal as moot because Tripadvisor announced it planned to acquire Liberty, and as a result, there would be no controlling stockholder. The defendants opposed the motion to dismiss, arguing that:

1. The proposed merger has not yet occurred and remains subject to stockholder approval.
2. The plaintiffs' claims are not solely based on alleged non-ratable benefits to the controller – i.e., the plaintiffs also alleged that the directors were interested in the conversions.
3. Mootness does not mandate dismissal of an appeal that presents a principle of Delaware law that could have a significant impact on future cases.

Decision

As a threshold matter, the court held that the appeal was not moot because the proposed merger had not occurred, and so Tripadvisor still had a controlling stockholder, and the issue remained live as to the directors based on the Chancery Court's holding that the plaintiffs adequately pleaded the directors also were interested in the conversions.

As to the merits, the court held that the Chancery Court erred in finding that the conversions conferred a non-ratable benefit sufficient to trigger entire fairness review. Instead, business judgment is the appropriate standard of review. In reaching this decision, the court made four key findings:

1. A non-ratable benefit must be material.
2. Temporality is key.
3. The temporality distinction aligns with other areas of Delaware law where courts have limited plaintiffs' abilities to pursue litigation based on speculative or hypothetical liability.
4. Comity considerations reinforce the court's decision.

First, the court confirmed the Chancery Court's holding that an alleged non-ratable benefit must be material to trigger entire fairness review. The court examined the three standards of review for corporate transactions and noted that transactions where a controlling stockholder transacts with the controlled corporation and receives a non-ratable benefit – i.e., a personal financial benefit from a transaction that is not equally shared by the stockholders – could trigger entire fairness review. The court recognized that "the mere fact that a controller may be better positioned after a transaction does not necessarily mean the controller received a non-ratable benefit," nor is a non-ratable benefit conferred on directors merely because a transaction provides "protection to directors against future liability exposure." Instead, to trigger entire fairness review, the alleged non-ratable benefit must be material; in other words, it must be significant enough to have made it improbable that the director could perform their fiduciary duties.

Second, the court determined that temporality is a key factor in determining materiality when the alleged non-ratable benefit from a transaction is a reduction or elimination of a fiduciary's risk of liability. Delaware precedent illustrated the importance of temporality. For example, the court noted that entire fairness review did not apply to board decisions to adopt provisions regarding the advancement of litigation expenses when those decisions were made without regard to any particular litigation or expenses. The court also noted that Delaware case law consistently draws a distinction between limitations of directors' liability exposure for past acts and future acts. Delaware courts have repeatedly declined to apply entire fairness review where directors adopted exculpation provisions under Section 102(b)(7), which, by its terms, cannot limit directors' liability for past conduct. On the other hand, Delaware courts have found that directors will receive a material non-ratable benefit and have applied entire fairness review when directors act to extinguish potential liability for past conduct.

The court held that "taken together, these cases suggest that the hypothetical and contingent impact of Nevada law on unspecific corporate actions that may or may not occur in the future is too speculative to constitute a material, non-ratable benefit triggering entire fairness review." And because the plaintiffs did not allege "that any particular litigation claims will be impaired [by the conversion] or that any particular transaction will be consummated post-conversion," the alleged non-ratable benefit of a "reduction in liability exposure under Nevada's corporate law regime was not material."

Third, the court took issue with the Chancery Court's position that such a temporal distinction is "arbitrary" and "hard to follow." Delaware courts routinely apply temporal distinctions to require litigants to do more than speculate. The court noted that Delaware ripeness and standing jurisprudence apply temporal distinctions to avoid deciding cases involving speculative litigation and issuing advisory opinions, and this principle applies with as much force here where the plaintiffs' allegations amount to mere speculation about what potential liabilities Tripadvisor's board might face in the future. The court, in a footnote, recognized:

> Plaintiffs have not alleged that Defendants have taken any articulable, material steps in connection with any post-conversion transactions. If directors or controllers were to take such steps in furtherance of breaching their fiduciary duties prior to redomesticating, even though such transactions or conduct would not be consummated or take place until after the change of corporate domicile, then our standard of review could be different. Although we do not reach that issue today, under such a scenario the conduct of those alleged to have engaged in it could still be subject to Delaware law. … But, as we have stated above, the record here suggests the existence of a 'clear day' and the absence of any material, non-ratable benefits flowing to the controller or directors as a result of the Conversions.

Finally, the court found that declining to weigh the costs and benefits between Delaware's and Nevada's corporate governance systems is consistent with furthering the goals of comity. The court elaborated on this principle, reminding the parties that state legislatures are free to take differing approaches as to the rights and responsibilities of corporations, officers and directors, and shareholders. Likewise, market participants are free to weigh the costs and benefits of those statutory systems, as well as how different state courts handle discrete issues when deciding where to incorporate.

The court found that the Tripadvisor board "considered a number of factors in their weighing of the costs and benefits of the Conversions," including "the respective court systems, the predictability of the courts with respect to corporate matters, the judges' expertise in handling such disputes, [and] the development and body of judicial decisions," among other factors. The court cautioned that "courts are ill-equipped to quantify the costs and benefits of one state's corporate governance regime over another's," and "we should be cautious about second-guessing the judgments of the directors as to how to best evaluate and weigh the various competing considerations as such factors might apply to a specific corporation." Instead, the court found it prudent to resist intruding on the valuations that both state legislators and directors of corporations make regarding the costs and benefits of corporate governance systems.

Core insights

- For Delaware corporations, the hypothetical and contingent impact of another state's corporate law regime "on unspecified corporate actions that may or may not occur in the future is too speculative to be a material, non-ratable benefit triggering entire fairness."
- Thus, any decision to redomicile in another state should be made on a "clear day." In other words, corporate fiduciaries should make that decision when they are not facing any existing or threatened litigation. Otherwise, they run the risk of losing business judgment protection and having the transaction reviewed under entire fairness.
- And, when evaluating whether to reincorporate in another state, directors should consider not only whether the conversion will reduce liability exposure, but also:
  - The respective court systems.
  - The predictability of the courts with respect to corporate matters.
  - The judges' expertise in handling such disputes.
  - The development and body of judicial decisions.
  - The familiarity of market participants with the corporate governance regime.
  - The process by which corporate statutory amendments are proposed and adopted by the state legislatures.
  - The effectiveness of the state's secretary of state office in facilitating corporate filings.
  - The existence of a corporate bar available, willing and able to handle such disputes.
- The Delaware Supreme Court's decision means that Tripadvisor and Liberty will almost surely win on remand and will be able to move forward with their conversions to Nevada without risk of liability for damages.

Key Contacts

Koji Fukumura San Diego	kfukumura@cooley.com +1 858 550 6008
Peter Adams San Diego	padams@cooley.com +1 858 550 6059

Ryan Blair San Diego	rblair@cooley.com +1 858 550 6047
Linh Nguyen San Diego	lknguyen@cooley.com +1 858 550 6168
Julian Piroli San Diego	jpiroli@cooley.com +1 858 550 6484
Ryan Ylitalo San Francisco	rylitalo@cooley.com +1 415 693 2564

This information is a general description of the law; it is not intended to provide specific legal advice nor is it intended to create an attorney-client relationship with Cooley LLP. Before taking any action on this information you should seek professional counsel.