# Delaware Chancery Court Supports Morton's Sale Process and PE Exit Motives

In a recent decision of note concerning the 2012 sale of Morton's Restaurant Group to Landry's, Inc., Chancellor Strine of the Delaware Court of Chancery found that a private equity firm with a 28 percent stake in Morton's was not a controlling stockholder, applied the business judgment rule, and dismissed the stockholder plaintiffs' challenge to the sale at the motion to dismiss stage of litigation. The *Morton's* decision will provide comfort to PE sponsors who hold minority positions in public companies, as it acknowledges the economic reality that even with a finite investment horizon, PE sponsors are incentivized to maximize an exit price and, as a result, bestow a control premium on all stockholders.

In his ruling, Chancellor Strine emphasized the fact that Castle Harlan, the 28 percent stockholder and Morton's former PE sponsor, had not exercised undue influence over the fulsome nine-month sale process, and that all of Morton's stockholders received equal consideration in the transaction. The Chancellor explained that this equal treatment among Morton's stockholders acted as a "safe harbor"; unless there were strong indications to the contrary, he would presume that Castle Harlan's interest in obtaining the best price in the transaction was aligned with the interests of the other stockholders.

In the suit, the stockholder plaintiffs alleged that Castle Harlan had pressured the Morton's Board into the transaction in order to obtain liquidity to support the launch of a new investment fund. Chancellor Strine rejected that allegation – finding that although Castle Harlan held 28 percent of Morton's shares and two out of ten board seats, it had not improperly influenced the sale process. Rather, Castle Harlan had supported a nine-month publicized process approaching more than 100 potential bidders, which rebutted any inference that Castle Harlan had pressured the Board into a fire-sale transaction to remedy a supposed immediate liquidity need. Ultimately, Chancellor Strine concluded that, absent additional indicators of control, 28% ownership does not constitute control. This lack of control, coupled with Castle Harlan receiving the same consideration received by all other stockholders, resulted in the application of the safe harbor of the business judgment rule.

Interestingly, Chancellor Strine shows clear sympathy, perhaps even support, for the PE model generally, at least as compared to the public markets. At one point, citing several market studies and academic papers, he notes that PE firms have a significantly longer holding period than the average holding period for a public stock. And, in a footnote that could be in a fund PPM, he writes:

Because of regulatory hurdles and incentives, most ordinary American investors have no vehicle to entrust a responsible portion of their 401(k) savings to private equity, despite the fact that the industry's comparatively more patient model of investing arguably better aligns with retirement investors' goals than active traded mutual funds that chase a better than market return through actively trading in non-influential blocks of equity (in defiance of accepted corporate finance theory).

Chancellor Strine's opinion is captioned *In re Morton's Restaurant Group, Inc. Shareholders Litigation*, C.A. No. 7122-CS (Del. Ch. July 23, 2013), and is available here.

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