

The (Surprising) Chances of Prevailing in an Entire Fairness Trial

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Conventional wisdom provides that the defendants in an entire fairness trial face an uphill battle. And for good reason: The entire fairness standard—which requires a reviewing court to closely examine both the business merits of a challenged transaction and the process undertaken to review, negotiate, and approve it—is Delaware corporate law’s most onerous standard of review. Defendants typically bear the burden of proof and cannot prevail by proving that the defendants acted with subjective good faith. Instead, defendants must convince the court that the transaction was objectively fair to the corporation regardless of fiduciaries’ beliefs.

There may be another reason to suspect that prevailing in an entire fairness case is difficult. Under one account, a string of defense-friendly case law prompted stockholder-plaintiffs to become more selective and prioritize stronger cases. In approximately the mid-2010s, the Delaware courts clamped down on what one jurist called the “M&A litigation epidemic” by, among other things, declining to approve so-called “disclosure-only” settlements (*In re Trulia Stockholder Litigation*), clarifying the narrow instances in which injunctive relief is appropriate under *Revlon* (*C&J Energy Services v. City of Miami General Employees*), and enunciating clear off-ramps to entire fairness review and enhanced scrutiny (*Corwin v. KKR Financial Holdings* and *Kahn v. M&F Worldwide* or *MFW*). Despite this culling exercise, the Delaware Court of Chancery became busier than ever, leading to the addition of two new vice chancellor positions, additional magistrate positions, and the appointment of Superior Court judges to preside by designation over certain types of cases filed in the Court of Chancery. The above-referenced account holds that the Court of Chancery’s increased workload resulted from a “flight to quality” whereby stockholder-plaintiffs, by dint of defense-friendly doctrines, were forced to choose only the strongest cases, spawning more claims that survived a motion to dismiss. Alternative accounts exist, including one holding that the increase in workload was the natural result of year-over-year increases in the sheer number of Delaware corporations in existence.

Whatever its genesis, the conventional wisdom that entire fairness cases are hard for defendants to win may not be correct. Indeed, in an opinion issued nearly 10 years ago (*In re Ezcorp Consulting Agreement Derivative Litigation*) the Court of Chancery, citing various sources and empirics, posited that triggering the entire fairness standard was not outcome-determinative and that defendants prevailed under that standard of review “with some degree of frequency.” This article aims to provide a similar empirical check on that proposition, updated to present day, by analyzing post-trial entire fairness rulings handed down by the Delaware Court of Chancery and Delaware Supreme Court in roughly the last 10 years. The statistics show, consistent with the *Ezcorp* court’s observation, that defendants fare surprisingly well in entire fairness trials.

This article’s methodology reflects conservative assumptions. The dataset comprises every published, post-trial opinion issued after *MFW* (which arguably marked the culmination of judicial efforts to curtail M&A litigation) in which either the trial court assessed whether a challenged transaction was entirely fair or the trial court determined at the dispositive motion stage that entire fairness applied. A case was considered a wholesale “plaintiff victory” if the plaintiff prevailed on a single entire fairness claim even if the plaintiff lost on all others. A case was considered a “defense victory” if the court held that the transaction was entirely fair, the court awarded zero damages, or the court held that the business judgment rule applied (thereby flipping a prior ruling that entire fairness applied at the dispositive motion stage). Finally, cases were placed into one of two categories: “big ticket” cases involving either a

public company transaction or a large private company transaction strongly resembling a public company sale process (e.g., large dollar amount or an extensive auction process) or “smaller-scale” cases involving a private company and typically a smaller amount in controversy. There were nine “big ticket” cases in total, seven of which were prosecuted by traditional plaintiffs firms. Full-service firms represented stockholder-plaintiffs in all 20 “smaller-scale” cases in the dataset. A trial court decision and its appeal were considered one “case” for purposes of these statistics.

Analysis of this dataset generated three key findings.

First, defendants won 66% (six of nine) of “big ticket” post-trial entire fairness cases. And because one case (*Tornetta v. Musk*) is on appeal, this percentage could jump to 77% (seven of nine). Defendants won three cases by proving that the transaction was entirely fair, two by proving that the business judgment rule applied, and one through a court determination of zero damages. In every “big ticket” case that went to trial, plaintiff proceeded on the theory that entire fairness applied due to the presence of a conflicted controlling stockholder. Interestingly, no plaintiff has brought a “big ticket” entire fairness case not involving a conflicted controller to trial in over 10 years—perhaps a reflection of *Corwin’s* potency. While the sample size is small and thus statistical power is limited, these numbers suggest that when “big ticket” controlling stockholder cases are brought to trial, defendants are more likely to win.

Second, “smaller-scale” cases are a different story. The results effectively flipped: In this category of cases, plaintiffs won 65% (13 of 20) of the time. Taken at face value, these numbers accord with the conventional wisdom that plaintiffs have an edge in entire fairness trials. But that basic intuition may be deceptively simplistic and obscure the full picture. In the full dataset, plaintiffs won in just 55% (16 of 29) of cases, hardly a decisive advantage. And for reasons just mentioned, “big ticket” cases seemingly pose a different risk profile.

Third and finally are insights on what types of entire fairness claims are most likely to make it to trial. Courts apply entire fairness review if plaintiffs demonstrate that either a majority of directors who made the challenged decision were conflicted or violated their duty of care or the transaction involved a conflicted controlling stockholder. In the vast majority of entire fairness cases that made it to trial, plaintiffs asserted the latter: 83% (24 of 29) post-trial entire fairness cases proceeded on a controller theory (three of which asserted a board conflicts theory concurrently), whereas 17% (five of 29) proceeded on a board conflicts theory. This finding arguably reinforces findings reported in a prior article: Controlled companies have historically found it difficult to satisfy the six factors required under *MFW* to reinstate the business judgment rule to a conflicted controller transaction. As such, plaintiffs may have preferentially sought to challenge (or had proportionally more success in challenging) that transactional subtype.

Importantly, the dataset does not capture the effects of Section 144 of the Delaware General Corporation Law (DGCL), which was amended earlier this year in an effort to reduce the costs and burdens associated with excessive stockholder litigation generally and controlling stockholder litigation in particular. The amendments to Section 144 both narrow the definition of “controlling stockholder” and provide new safe harbor procedures for controlling stockholder transactions that relax several more stringent aspects of *MFW’s* paradigm. Reliance on revised Section 144 may result in both fewer controller entire fairness cases making it to trial and more defense victories in those that do. As such, the statistics reported in this article may change markedly 10 years hence. In the meantime, while care should always be taken to manage conflicts and practice good governance, defense counsel may be encouraged to know that winning an entire fairness trial may not be quite as difficult as conventional wisdom would suggest in all cases.

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