BUSINESS ASSOCIATIONS

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INTRODUCTION

The *Survey* period included decisions rich in substantive discussion of applicable law, including a finding that a chief executive officer violated his fiduciary duty to shareholders in order to preserve his position;[1] a discussion by the Court of Appeals of black-letter law applicable to dissolution of a general partnership;[2] a holding that abuse of a minority stockholder by the majority, based on gender, can be grounds for dissolution of the corporation under the business corporation law;[3] and a member of a limited liability company (LLC) was allowed, in an unusual case, to be a derivative defender of the LLC rather than a derivative plaintiff.[4]

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1. *See* In re Xerox Corp. Consol. S'holder Litig., 61 Misc. 3d 176, 188, 193, 76 N.Y.S.3d 759, 768, 771 (Sup. Ct. N.Y. Cty. 2018); *rev'd sub nom.* Deason v. Fujifilm Holdings Corp., 165 A.D.3d 501, 502, 86 N.Y.S.3d 28, 29 (1st Dep't 2018).

2. *See* Congel v. Malfitano, 31 N.Y.3d 272, 279, 101 N.E.3d 341, 343, 76 N.Y.S.3d 873, 875 (2018).

3. *See* Straka v. Arcara Zucarelli Lenda & Assocs., 62 Misc. 3d 1064, 1070, 92 N.Y.S.3d 567, 573 (Sup. Ct. Erie Cty. 2019); N.Y. BUS. CORP. LAW § 1104-a(a)(1) (McKinney 2003).

4. *See* Horowitz v. 148 S. Emerson Assocs. LLC, 888 F.3d 13, 22 (2d Cir. 2018).

I. LEGISLATIVE DEVELOPMENTS

The only legislative change between July 1, 2017 and June 30, 2019 was the adoption of a requirement for the Board of Directors of every condominium created pursuant to the real property law, and every cooperative housing corporation created pursuant to the business corporation law (BCL), to report on conflicts of interest.[5]

The principle is that, each year, the cooperative housing association or condominium shall provide to its members or shareholders, as the case may be, a report signed by each of its managers or directors "containing information on any contracts made, entered into, or otherwise voted on by the board of directors" in which a director had an interest under section 713 of the BCL or section 715 of the Not-For-Profit Corporation Law ("N-PCL").[6] Unfortunately, the legislation is confusing regarding which of these two sections governs.

The reason is a drafting error which was corrected imperfectly. When the requirement was first adopted by the Legislature, the requirement in section 519-a of the N-PCL applied to "[e]very condominium or cooperative housing corporation, incorporated pursuant to this chapter,"[7] and section 715 of the N-PCL was the standard for determining whether a transaction was reportable.[8] The Act placed a similar requirement in new section 727 of the BCL, which applied to "[e]very condominium or cooperative housing corporation, incorporated pursuant to this chapter."[9] In BCL section 727, a transaction was reportable if a director was "an interested director, pursuant to section seven hundred thirteen of this chapter."[10]

Although the legislation provided that each standard for determining whether a director was "interested" corresponded to the entity-formation statute, condominiums generally are not formed under the BCL or the N-PCL, but under the Real Property Law.[11]

5. *See* Act of Sept. 12, 2017, 2017 McKinney's Sess. Laws of N.Y., ch, 805, at 836; Act of Apr. 18, 2018, 2018 McKinney's Sess. Laws of N.Y., ch. 9, at 8 (codified at N.Y. NOT-FOR-PROFIT CORP. LAW § 519-a (McKinney Supp. 2020); N.Y. BUS. CORP. LAW § 727 (McKinney Supp. 2020)).

6. BUS. CORP. § 727(a)(2); NOT-FOR-PROFIT CORP. § 519-a(a)(2).

7. Act of Sept. 12, 2017, 2017 McKinney's Sess. Laws of N.Y., ch, 805, § 519-a(a), at 863.

8. *See id.* § 519-a(a)(1), at 863–64.

9. *Id.* § 727(a), at 864.

10. *Id.* § 727(a)(2), at 864.

11. *See* N.Y. REAL PROP. LAW § 339-d (McKinney 2015); Marc H. Schneider & Dan M. Blumenthal, *Practice Commentaries*, *in* MCKINNEY'S CONSOLIDATED LAWS OF N.Y., Book 49, § 339-d, at 4 (2015).

The Legislature then amended the introductions to the two statutory sections.[12] As amended, N-PCL section 519-a(a) begins, "[a] condominium created pursuant to the real property law or a cooperative housing corporation created pursuant to the business corporation law, shall, ..."[13] N-PCL section 519-a(a)(2) provides that the standard for reporting a related party transaction is set forth in N-PCL section 715.[14] The second section, BCL section 727(a), as amended, begins, "[a] condominium created pursuant to the real property law or a cooperative housing corporation created pursuant to this chapter, shall, ..."[15] BCL section 727(a)(2) provides that the standard for reporting a transaction is the "interested director" standard set forth in BCL section 713.[16] Thus, both N-PCL section 715 and BCL section 713 apply to the report, leaving the conscientious director with the need to satisfy both sections.

II. FIDUCIARY DUTIES

One of the most interesting cases during the Survey Period was *In re Xerox Corp. Consolidated Shareholder Litigation*,[17] involving a proposal to sell Xerox Corp., a New York corporation ("Xerox"), to Fujifilm Holdings Corp. ("Fuji").[18]

The case is remarkable for several reasons: The sale transaction itself was complex.[19] Then the court held, after an extensive discussion of facts on the record that the sale "was largely negotiated by a massively conflicted CEO in breach of his fiduciary duties" in order to keep his job as CEO, and was not properly supervised by the Xerox Board.[20] The court held further that the Xerox Board was not entitled to the protection of the business judgement rule and that the transaction failed the entire fairness test,[21] and enjoined the sale transaction.[22]

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12. *See* Act of Apr. 18, 2018, 2018 McKinney's Sess. Laws of N.Y., ch. 9, at 8 (codified at N.Y. NOT-FOR-PROFIT CORP. LAW § 519-a (McKinney Supp. 2020); N.Y. BUS. CORP. LAW § 727 (McKinney Supp. 2020)).
13. NOT-FOR-PROFIT CORP. § 519-a(a).
14. *Id.* § 519-a(a)(2).
15. BUS. CORP. § 727(a).
16. *Id.* § 727(a)(2).
17. 61 Misc. 3d 176, 76 N.Y.S.3d 759 (Sup. Ct. N.Y. Cty.), *rev'd sub nom* Deason v. Fujifilm Holdings Corp., 165 A.D.3d 501, 86 N.Y.S.3d 28 (1st Dep't 2018).
18. *See id.* at 179, 76 N.Y.S.3d at 762. Xerox is incorporated under New York law. *See* Xerox Corp., Annual Report (Form 10-K) (Dec. 31, 2017).
19. *See* 61 Misc. 3d at 179–80, 76 N.Y.S.3d at 762.
20. *Id.* at 191, 193, 76 N.Y.S.3d at 770, 771–72.
21. *See id.* at 192, 193–94, 76 N.Y.S.3d at 771, 772.
22. *Id.* at 199, 76 N.Y.S.3d at 775.

Xerox then abandoned the transaction.[23] Commenting on the decision several weeks later, Professor John Coffee, approving the decision, observed that the outside directors did not seem culpable of anything beyond, at the worst, passive negligence.[24] However, the Appellate Division, First Department, reversed the trial court, and held that the business judgment rule should have covered the transaction.[25]

A. Terms of the Sale Transaction

On January 31, 2018, the Board of Xerox approved a change of control transaction with Fuji.[26] The proposed transaction called for Xerox to issue 50.1% of its shares of stock to Fuji, giving Fuji effective control of Xerox.[27] Fuji, in turn, agreed to invest $6.1 billion in cash in Xerox.[28] Fuji was going to obtain the cash from a joint venture (the "Joint Venture"), owned 75% by Fuji and 25% by Xerox, which distributed Xerox products in Asia and the Pacific Rim.[29] The Joint Venture would borrow 671 billion yen, equivalent to approximately $6.1 billion, and would use the borrowed money to redeem from Fuji all of Fuji's interest in the Joint Venture, with the result that Xerox would be the 100% owner of the Joint Venture.[30] Fuji, having received $6.1 billion from the redemption of its share of the Joint Venture had paid to it, would pay the $6.1 billion cash to Xerox to purchase enough shares to equal 50.1% share ownership in Xerox.[31]

The terms of the transaction provided that, immediately before it closed, Xerox would pay its shareholders a special dividend of $2.5

23. *See* Xerox Corp., Current Report (Form 8-K) (May 15, 2018).

24. *See* John C. Coffee, Jr., *The Lessons of Xerox: Is New York Law Now Tougher Than Delaware's?*, CLS BLUE SKY BLOG (May 21, 2018, 4:07 AM), http://clsbluesky.law.columbia.edu/2018/05/21/the-lessons-of-xerox-is-new-york-law-now-tougher-than-delawares/.

25. *See* Deason v. Fujifilm Holdings Corp., 165 A.D.3d 501, 502, 86 N.Y.S.3d 28, 29 (1st Dep't 2018).

26. *In re Xerox Corp. Consol. S'holder Litig.,* 61 Misc. 3d at 179, 76 N.Y.S.3d at 762.

27. *Id.*

28. Xerox Corp. and FujiFilm Holdings Corp., Share Subscription Agreement (Form 8-K) (Jan. 31, 2018) [hereinafter Xerox Share Subscription Agreement] (The $6.1 billion investment by Fuji in Xerox is provided in Section 1.01 of the Share Subscription Agreement dated as of January 31, 2018 between Xerox and Fuji, filed as exhibit 2.2 to the Xerox Current Report on Form 8-K filed on EDGAR on Feb. 5, 2018).

29. *See In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 179, 76 N.Y.S.3d at 762; Xerox Share Subscription Agreement, *supra* note 28 (Xerox published the terms of the Joint Venture on Jan. 31, 2018 by filing the documents on EDGAR).

30. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 179, 76 N.Y.S.3d at 762.

31. Xerox Share Subscription Agreement, *supra* note 28.

billion.[32] This special dividend would reduce the post-sale net worth of Xerox by $2.5 billion.[33] The reduction in Xerox' net worth would mean that the portion of Xerox owned by the pre-sale Xerox shareholders (that is, 49.9%) would be reduced in value by slightly less than $1.25 billion because of the special dividend.[34] The portion of Xerox owned by Fuji (that is, 50.1%), would be reduced in value by slightly more $1.25 billion because of the special dividend.[35] The Xerox shareholders would be roughly $1.25 billion better off on account of the special dividend.[36]

What the pre-transaction Xerox shareholders would give in this transaction would be 50.1%, and control, of Xerox.[37] What they would receive in return would be a changed value of their share in the Joint Venture.[38] In place of Xerox's 25% pre-transaction portion of the Joint Venture, the pre-transaction Xerox shareholders would own, indirectly, a 49.9% portion of the Joint Venture (post-transaction, Xerox would own 100% of the Joint Venture, but 50.1% of Xerox would be owned by Fuji).[39] Because the Joint Venture would incur $6.1 billion in debt to make a payment in that amount to Fuji, the value of the portion of the Joint Venture attributable to the pre-transaction Xerox shareholders would be diminished by their share, or roughly 49.9%, of that $6.1 billion in debt.[40] Thus, their share of the Joint Venture would be worth roughly $3 billion less.[41] The pre-transaction Xerox shareholders would also receive roughly $1.25 billion in additional value from the special dividend.[42] Would increasing their share of the Joint Venture be worth what they were giving up? As the court noted, "[t]he supposed value proposition of the transaction largely turned on the value of the synergies and the valuation of Fuji Xerox, both of which are highly subjective."[43]

32. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 180, 76 N.Y.S.3d at 762.

33. *See In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 180, 76 N.Y.S.3d at 762; *FUJIFILM Holdings and Xerox Announce Agreement to Combine Fuji Xerox Joint Venture with Xerox*, XEROX (Jan. 31, 2018), https://www.news.xerox.com/news/FUJIFILM-Holdings-and-Xerox-announce-agreement-to-combine-Fuji-Xerox-Joint-Venture-with-Xerox [hereinafter Agreement Announcement].

34. *See* Agreement Announcement, *supra* note 33.

35. *See id.*

36. *See id.*

37. *See In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 179, 76 N.Y.S.3d at 762.

38. *See id.*

39. *Id.*

40. *See id.*; Agreement Announcement, *supra* note 33.

41. *See* Agreement Announcement, *supra* note 33.

42. *See id.*

43. *See In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 191, 76 N.Y.S.3d at 770.

Another important detail was that Jeff Jacobson, the existing CEO of Xerox, was to be CEO of Xerox post-closing.[44] The size of the Xerox Board post-closing would be twelve directors, seven of whom would be chosen by Fuji and five of whom would be named by Xerox from its existing Board, subject to reasonable approval by Fuji.[45] The five Xerox directors were assured of remaining on the Board of post-closing Xerox for five years.[46]

B. Procedural Background of the Case

In 2017, Carl Icahn had the largest shareholding in Xerox,[47] and, in anticipation of Xerox's 2018 annual meeting of shareholders, filed a slate of four directors challenging the four members of the Xerox Board of Directors who had been on the Board the longest.[48] Xerox's Board at that time consisted of nine directors plus Jeff Jacobson, who was its Chief Executive Officer.[49]

Xerox had an advance notice bylaw which required candidates for director, other than management's nominees, to be proposed to the corporation on or before December 11, 2017.[50] Icahn requested that Xerox extend the deadline; the Board denied his request.[51] Icahn filed his slate of four candidates on the deadline.[52]

Darwin Deason had the third largest shareholding in Xerox.[53] After the Board of Xerox disclosed the proposed sale transaction with Fuji, Deason and several other shareholder plaintiffs brought an action to enjoin Xerox, Fujifilm, and various individuals from consummating the transaction.[54] Deason brought an additional action to cause Xerox to waive its advance notice by-law provision so that, even though the advance notice deadline of December 11, 2017 had passed, Deason could still nominate a slate of directors for the 2018 annual meeting.[55] The court

44. *Id.* at 180, 76 N.Y.S.3d at 762.
45. Xerox Corp., Current Report (Form 8-K) (Jan. 31, 2018).
46. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 180, 76 N.Y.S.3d at 762.
47. *See id.* at 181, 76 N.Y.S.3d at 763.
48. *Id.*
49. *Id.*
50. *See id.* at 180–81, 76 N.Y.S.3d at 763.
51. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 181, 76 N.Y.S.3d at 763.
52. *See* Xerox Corp., Statement on Schedule 13D (Dec. 11, 2017).
53. *See In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 180, 76 N.Y.S.3d at 762.
54. *Id.* at 180–81, 76 N.Y.S.3d at 763.
55. *Id.* at 181, 76 N.Y.S.3d at 763.

collected submissions from the parties and held an evidentiary hearing on April 26 and 27, 2018.[56]

C. Court's Discussion of the Facts

The court said that the critical facts for its option were "the conduct of Xerox CEO Jeff Jacobson in the time frame preceding the Board's approval of a transaction that granted control of an iconic American company to Fuji without any cash payment by Fuji to Xerox shareholders, and the Board's acquiescence in Jacobson's conduct."[57]

Fuji and Xerox had been discussing the possibility of a business combination for several years when, in March, 2017, Jeff Jacobson went to Japan and met with Fuji's chief executive officer and chief operating officer.[58] At that meeting, the officers of Fuji expressed their understanding that Xerox would need a thirty percent premium over the current market price of its stock.[59] Fuji summarized its interest in a letter, which Jacobson brought to the Xerox Board.[60] Xerox engaged a financial advisor, Centerview Partners, and Jacobson responded to Fuji that Xerox was prepared to discuss an all cash sale with an appropriate premium to Xerox's market price.[61]

Thereafter, said the court:

> Jacobson's role in negotiating the ultimate transaction must be viewed against the background of events that commenced on and after May 15, 2017, when Jacobson participated in a dinner with Carl Icahn at which Icahn told Jacobson, in the presence of two of Jacobson's direct reports, that Icahn did not believe Jacobson was the right person to be Xerox CEO and that Icahn wanted Xerox sold. Icahn further stated that Jacobson would be fired if Jacobson was unable to produce a sale transaction.[62]

Jacobson passed on his recollection of the meeting to the Board.[63]

Roughly one week later, Jacobson and the Xerox Board were told that Fuji could not proceed with a combination with Xerox because a purchase of all Xerox shares was too expensive for Fuji.[64] Jacobson's and

56. *Id.*
57. *Id.* at 182–83, 76 N.Y.S.3d at 764.
58. *See In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 183, 76 N.Y.S.3d at 764.
59. *Id.*
60. *Id.* at 183, 76 N.Y.S.3d at 764–65.
61. *Id.* at 183, 76 N.Y.S.3d at 765.
62. *Id.* at 183–84, 76 N.Y.S.3d at 765.
63. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 184, 76 N.Y.S.3d at 765.
64. *Id.*

Xerox's financial advisor, Centerview, developed a structure whereby Fuji could make a cashless acquisition of Xerox.[65]

Jacobson presented the cash-free sale concept to Fuji in June 2017.[66] Although Jacobson had received approval from Xerox's Chairman of the Board, Robert Keegan, to explore alternatives to an all-cash sale with Fuji, the full Xerox Board was unaware that Jacobson was doing so until Jacobson informed them in July 2017.[67] "For all intents and purposes," said the court, "Jacobson's cash-free acquisition concept took off the table any type of all-cash sale transaction with Fuji even though one of Xerox's financial advisors, David Hess of Centerview, testified that Fuji had cash reserves of $8 billion."[68]

When Icahn heard of Jacobson's cashless sale proposal, Icahn informed Keegan that he was "opposed [to] a transaction that would leave the [existing] Xerox shareholders with a 49.9% minority interest in a company controlled by Fuji."[69] Icahn also suggested that Keegan form a search committee to find a replacement for Jacobson.[70] The rest of the Board (other than Jacobson) agreed.[71] In July 2017, they formed a search committee, and by September 2017 they had hired a search firm, Heidrick & Struggles, to look for candidates.[72]

After interviewing candidates in October and November 2017, the Board identified a potential replacement for Jacobson named Giovanni (John) Visentin, who had been a former executive of IBM and Hewlett-Packard.[73] On November 10, 2017, Keegan advised Jacobson that he might be replaced.[74] Jacobson testified that he had previously been unaware of any efforts to replace him, but, said the court, "this testimony is suspect given the large number of people aware of the work of the Scan Committee."[75] Keegan also told Jacobson that the Board instructed Jacobson to stop further discussions with Fuji.[76]

Nevertheless, Jacobson continued to hold discussions with Fuji regarding the combination and to meet with Fuji's CEO and with another

65. *Id.*
66. *See id.* at 184, 76 N.Y.S.3d at 765.
67. *Id.* at 184, 76 N.Y.S.3d at 765–66.
68. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. at 184, 76 N.Y.S.3d at 765.
69. *Id.* at 185, 76 N.Y.S.3d at 766.
70. *Id.*
71. *Id.*
72. *Id.*
73. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 185, 76 N.Y.S.3d at 766.
74. *Id.*
75. *Id.*
76. *Id.*

top Fuji officer.[77] During these discussions, Jacobson informed Fuji that his situation at Xerox was precarious;[78] Fuji assured him that he would stay on as CEO of Xerox after closing.[79]

A Xerox Transaction Committee consisting of Keegan and three other long-serving Xerox Directors was formed in December 2017.[80] However, according to the court, except for one teleconference between Keegan and Komori, "[a]t no time . . . did *any* Xerox director participate in *any* meeting with Fuji executives; all such meetings involved Jacobson."[81]

Fuji and Xerox planned to announce the transaction on January 31, 2018.[82] On January 24, David Hess of Centerview sent an e-mail to the CEO of Fuji, stating that Xerox needed to perform more due diligence review of the Joint Venture and that the financial projections did not show sufficient value for Xerox's shareholders.[83] Therefore, said Hess, January 31 was too soon to announce the transaction.[84] Fuji responded that "Fujifilm will walk [a]way from this deal if you won't keep the announcement schedule."[85]

Centerview issued its fairness opinion on January 30, and was paid $10 million.[86] The court noted that "Centerview will receive an additional $40 million only if the transaction is consummated."[87]

D. The Court's Analysis

The court made clear its negative view of the transaction and of Jacobson's role in it.[88] The faults with the transaction were: control was transferred to Fuji with no payment to the shareholders;[89] the transaction was largely negotiated by the CEO "in breach of his fiduciary duties" and

77. *Id.* at 186, 76 N.Y.S.3d at 767.
78. *See In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 186, 76 N.Y.S.3d at 767.
79. *See id.* at 187, 76 N.Y.S.3d at 767.
80. *Id.*
81. *Id.*
82. *See id.*
83. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 190, 76 N.Y.S.3d at 769.
84. *See id.* at 190, 76 N.Y.S.3d at 770.
85. *Id.*
86. *Id.*
87. *Id.*
88. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 191, 76 N.Y.S.3d at 770.
89. *Id.* Although the Xerox shareholders would not be paid anything directly, they would have almost doubled their proportionate interest in the Joint Venture. Although the Joint Venture would be subject to significant new indebtedness, the amount of that indebtedness would be retrieved by Xerox when Fuji paid that amount into Xerox as a subscription for Fuji's 50.1%. *See supra* Part II. A.

"to further his self-interest; [90]" of the approving Board of Directors, "more than half of whom were perpetuating themselves in office for five years"[91]; and the Board did not properly supervise the "conflicted CEO."[92] These faults took "this transaction out of the realm of cases in which courts defer to the business judgment of independent directors."[93]

The court particularly criticized Jacobson:

> [O]nce Jacobson learned that he had been targeted for replacement by Xerox's largest shareholder and eventually the Board itself, he abandoned the Board's request to obtain a value-maximizing all-cash transaction and engineered the framework for a one-sided deal that includes Jacobson retaining his position as CEO post-transaction. And, at all relevant times after his May 2017 dinner with Icahn, Jacobson was consistently acting without the knowledge of the entire Xerox Board even after the Board decided in November 2017 that he immediately cease any further communications and negotiations with Fuji about a possible transaction. Despite the Board's decision, Jacobson doubled down on his efforts and worked directly with Fuji to ensure a deal that is disproportionately favorable to Fuji, not Xerox.[94]

In this motion for an injunction, the court determined that the plaintiffs had "a probability of success in establishing that [the Board], a majority of whom would have future directorship positions on the Board of the combined entity, acted in bad faith in structuring and negotiating the proposed transaction."[95] Further, Xerox's financial advisor was of the view that the transaction undervalued Xerox and paid the Xerox shareholders an inadequate premium for giving up control.[96]

With regard to Fuji's role, the court stated that "Fuji cannot be faulted for taking advantage of the opportunity Jacobson presented Fuji which, in Komori's [Fuji's President] words, enabled Fuji to 'take control of Xerox without spending a penny.'"[97] But, said the court, "that does not mean Fuji did not aid and abet a breach of fiduciary duty."[98]

The court set forth the elements of aiding and abetting fiduciary duty as "(1) a breach by a fiduciary of obligations to another, (2) that the defendant knowingly induced or participated in the breach, and (3) that

90. *Id.*
91. *Id.*
92. *Id.*
93. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 191, 76 N.Y.S.3d at 770.
94. *Id.* at 193, 76 N.Y.S.3d at 771–72.
95. *Id.* at 194, 76 N.Y.S.3d at 772.
96. *Id.*
97. *Id.* at 191, 76 N.Y.S.3d at 770.
98. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 191, 76 N.Y.S.3d at 770.

plaintiff suffered damage as a result of the breach."[99] The court observed that "knowing participation" can be found where "the terms of the transaction are so egregious . . . as to be inherently wrongful."[100]

According to the court, Fuji knew that it was inducing Jacobson to protect his own interest over the interests of Xerox's shareholders:

> [T]hroughout negotiations, Fuji's representatives Kawamura and Komori believed that the proposed transaction disproportionately favored Fuji at the expense of Xerox shareholders . . . Fuji, knowing full well that Jacobson was under enormous pressure from Icahn and the Board and that Jacobson could soon be replaced as CEO, presented Jacobson with the opportunity to stay on as CEO of the combined entity that would emerge from a change of control transaction that deprived Xerox shareholders of an adequate control premium. The communications between Kawamura and Jacobson in particular . . . demonstrate the significant degree to which the two were aligned in combating Icahn and the Board so that Fuji could consummate a deal entirely in its favor and so that Jacobson could maintain his position as CEO.[101]

Therefore, the court stated that an aiding and abetting claim against Fuji would likely succeed on the merits.[102]

The court concluded that Jacobson had a conflict of interest commencing November 10, 2017, if not earlier, and that documentary evidence showed that Jacobson proceeded to "explain his personal circumstances to Fuji and attempt to enlist Fuji's assistance in preserving his position[.]"[103] The court further concluded that "it was a breach of fiduciary duty for Keegan to authorize Jacobson to continue to be the primary interface with Fuji after Keegan both told Jacobson he could be imminently terminated and, for that reason, he should cease communications with Fuji about any transaction."[104]

99. *Id.* at 194, 76 N.Y.S.3d at 772 (quoting Higgins v. N.Y Stock Exch., Inc., 10 Misc. 3d 257, 287, 806 N.Y.S.2d 339, 364 (Sup. Ct. N.Y. Cty. 2005) (concluding that in a merger, a financial advisor's interests in the acquiring entity supported a claim that, in providing financial advisory services to the board of directors of the acquired entity on the other side, the financial advisor's "actual knowledge" of a breach of fiduciary duty and gave substantial assistance to it)).

100. *Id.* at 195, 76 N.Y.S.3d at 772 (quoting Obeid v. La Mack, No. 14-CV-6498, 2016 U.S. Dist. LEXIS 136078 at *20 (S.D.N.Y. Sept. 30, 2016) (concluding that where individuals allegedly siphoned off assets from their own company to a competitor, the competitor could be charged with aiding and abetting because the assets were valuable and the consideration paid by the competitor was negligible)).

101. *Id.* at 195, 76 N.Y.S.3d at 773.

102. *Id.* at 194, 76 N.Y.S.3d at 772.

103. *In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 187–88, 76 N.Y.S.3d at 768.

104. *Id.* at 188, 76 N.Y.S.3d at 768.

In determining that plaintiffs were likely to succeed on the merits of the aiding and abetting claim against Fuji,[105] the court cited its factual finding that Fuji's officers Kawamura and Komori thought the change in control "disproportionately favored Fuji at the expense of Xerox shareholders."[106] The court further stated that "Fuji . . . presented Jacobson with the opportunity to stay on as CEO of the combined entity that would emerge from a change of control transaction that deprived Xerox shareholders of an adequate control premium."[107]

E. Advance Notice By-Law

Xerox's advance notice by-law required Icahn and Deason to propose directors for the 2018 annual meeting of shareholders by December 11, 2017.[108]

The court, citing Delaware precedents, stated:

> It is well-settled law that a shareholder is entitled to a waiver of a corporation's advance notice deadline for nominating directors when there is a material change in circumstances of the corporation after the nomination deadline. Certain material, post-deadline changes in business policy and direction may "foreseeably generate controversy and shareholder opposition. Under those circumstances, considerations of fairness and the fundamental importance of the shareholder franchise dictate[] that the shareholders be afforded a fair opportunity to nominate an opposing slate, thus imposing upon the board the duty to waive the advance notice requirement of the by-law."[109]

In effect, the Xerox Board had an obligation to waive the nomination deadline and to allow shareholders to nominate directors to oppose them, in the case of "[c]ertain material, post-deadline changes in business policy and direction[.]"[110]

The court granted Deason's motion for an injunction, and required Xerox to waive its advance notice by-law, for thirty days.[111] Although Xerox was planning to submit the transaction to a vote of its shareholders,

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105. *See id.* at 194, 76 N.Y.S.3d at 772.

106. *Id.* at 195, 76 N.Y.S.3d at 773.

107. *Id.*

108. *See In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 180–81, 76 N.Y.S.3d at 763.

109. *Id.* at 196, 76 N.Y.S.3d at 773 (quoting Hubbard v. Hollywood Park Realty Enters., Inc., No. 11779, 1991 Del. Ch. LEXIS 9, at *39–40 (Del. Ch. Jan. 14, 1991) (citing Icahn Partners LP v. Amylin Pharm., Inc., No. 7404-VCN, 2012 Del. Ch. LEXIS 85, *8–9 (Del. Ch. Apr. 20, 2012) (granting plaintiffs expedited discovery to determine whether a post-deadline change had occurred which would entitle the stockholders to reopen the nomination process)).

110. *Id.* at 196, 76 N.Y.S.3d at 773.

111. *See id.* at 199, 76 N.Y.S.3d at 775–76.

the court thought that a proxy fight was "a fair and logical way" to give more choices to Xerox shareholders, reasoning that a different board of directors might pursue an all-cash acquisition, or might select an acquisition partner other than Fuji, or might obtain a better deal with Fuji.[112]

F. Aftermath and Reversal

The court issued its opinion on April 27, 2018.[113] In May, 2018, Jacobson resigned and was replaced by John Visentin.[114] Xerox sent Fuji a notice of termination of the sale transaction documents.[115]

Commenting on the trial court decision several weeks later, Professor John Coffee observed that the outside directors did not seem culpable of anything beyond, at the worst, passive negligence.[116] His observation foreshadowed the finding of the First Department, upon appeal of the decision, that the board's approval was subject to the business judgment rule.[117]

On October 16, 2018, the First Department reversed the trial court's decision regarding the coverage of the business judgment rule, and dissolved the injunctions against the transaction.[118] It held that the possibility for any one member of the Xerox board to be named to the board of the successor company "was not a material benefit such that it was a disabling interest."[119] The fact that Jacobson was conflicted was not dispositive, because the Xerox board knew about the conflict, and Jacobson "neither misled nor misinformed the board."[120] The board engaged advisors and discussed the Fuji transaction "on numerous occasions" prior to presenting it to the shareholders.[121] The transaction

112. *Id.* at 195–96, 76 N.Y.S.3d at 773.

113. *See In re Xerox Corp. Consol. S'holder Litig.*, 61 Misc. 3d at 176, 76 N.Y.S.3d at 759.

114. *See* Xerox Co., Current Report (Form 8-K) (May 13, 2018).

115. *See id.*

116. John C. Coffee, Jr., *The Lessons of Xerox: Is New York Law Now Tougher Than Delaware's?*, CLS BLUE SKY BLOG (May 21, 2018, 4:07 AM), http://clsbluesky.law.columbia.edu/2018/05/21/the-lessons-of-xerox-is-new-york-law-now-tougher-than-delawares/.

117. *See* Deason v. Fujifilm Holdings Corp., 165 A.D.3d 501, 502, 86 N.Y.S.3d 28, 30 (1st Dep't), *rev'g*, 61 Misc. 3d 176, 76 N.Y.S.3d 759 (Sup. Ct. N.Y. Cty. 2018) (citing Auerbach v. Bennett, 47 N.Y.2d 619, 623–24, 393 N.E.2d 994, 996, 419 N.Y.S.2d 920, 922 (1979)).

118. *See id.* at 501, 86 N.Y.S.3d at 29.

119. *Id.* at 501–02, 86 N.Y.S.3d at 29 (first citing Giuliano v. Gawrylewski, 122 A.D.3d 477, 478, 997 N.Y.S.2d 20, 23 (1st Dep't 2014); and then citing Orman v. Cullman, 794 A.2d 5, 24 (Del. Ch. 2002)).

120. *Id.* at 502, 86 N.Y.S.3d at 29 (citing Mills Acquisition Co. v. MacMillan, Inc., 559 A.2d 1261, 1264 (Del. 1989)).

121. *Id.*

was not "unreasonable on its face."[122] Accordingly, the business judgment rule should have covered the transaction.[123]

III. PARTNERSHIPS

Congel v. Malfitano involved a partner who sent a notice of withdrawal to the other partners of a general partnership, when the withdrawal was a violation of its partnership agreement.[124]

The Poughkeepsie Galleria Company (the "Partnership") was a general partnership, originally having eight partners, which owned, operated, and managed a shopping mall.[125] The defendant, Malfitano, owned a 3.08% interest in the general partnership at the time of this case.[126] In the mid-2000s, the defendant desired to have his interest in the Partnership bought out, but buyout negotiations failed.[127]

On November 24, 2006, the defendant sent a written notice to the other partners, which said: "[I]n accordance with Section 62(1)(b) of the Partnership Law, and as a general partner of the Partnership I hereby elect to dissolve the Partnership and by this notice the Partnership is hereby dissolved."[128]

The defendant claimed that the Partnership was legally required to liquidate and to buy out his interest.[129] At the time, the Partnership was refinancing a mortgage, and the defendant recorded a notice of pendency on the Partnership's real property, so the defendant's actions with respect to the Partnership could not be ignored.[130]

Three other partners of the Partnership, constituting the Executive Committee of the Partnership, brought an action on their own behalf and on behalf of the Partnership against the defendant for breach of contract,

122. *Deason*, 165 A.D.3d at 502, 86 N.Y.S.3d at 29 (citing In re MeadWestvaco Stockholders Litig., 168 A.3d 675, 682–83 (Del. Ch. 2017)).

123. *Id.* (citing Auerbach v. Bennett, 47 N.Y.2d 619, 632, 393 N.E.2d 994, 1001–02, 419 N.Y.S.2d 920, 928 (1979)).

124. *See* 31 N.Y.3d 272, 280, 101 N.E.3d 341, 344, 76 N.Y.S.3d 873, 876 (2018).

125. *See id.* at 279, 101 N.E.3d at 343, 76 N.Y.S.3d at 875.

126. *See id.* at 279, 101 N.E.3d at 343–44, 76 N.Y.S.3d at 875–76.

127. *Id.* at 280, 101 N.E.3d at 344, 76 N.Y.S.3d at 876.

128. *Id.* Section 62(1)(b) of the partnership law provides that "Dissolution is caused: 1. Without violation of the agreement between the partners, . . . (b) By the express will of any partner when no definite term or particular undertaking is specified . . . ." N.Y. P'SHIP LAW § 62(1)(b) (McKinney 2015).

129. *See Congel*, 31 N.Y.3d at 280, 101 N.E.3d at 344, 76 N.Y.S.3d at 876.

130. *See id.* A notice of pendency, filed in accordance with Article 65, with the County Clerk of the county where the property is located, provides notice that litigation is pending where "the judgment demanded would affect the title to, or the possession, use or enjoyment of, real property[.]" N.Y. C.P.L.R. 6501 (McKinney 2010).

for a declaratory judgment that the defendant had wrongfully dissolved the Partnership, and to cancel the notice of pendency.[131] Only afterward would the mortgage lender continue discussions.[132]

The Court noted that, according to the Partnership Agreement:

> [T]he Partnership "shall continue until it is terminated as hereinafter provided." In a subsequent provision, the agreement stated that the Partnership would dissolve upon "[t]he election by the Partners to dissolve the Partnership" or "[t]he happening of any event which makes it unlawful for the business of the Partnership to be carried on or for the Partners to carry it on in Partnership."[133]

The first question addressed by the Court of Appeals was whether the unilateral notice by the defendant was a violation of the partnership agreement.[134] The trial court and the Appellate Division focused on whether the partnership agreement had a "definite term" or a "particular undertaking" within the meaning of Partnership Law section 62(1)(b).[135] The Court of Appeals held, however, that dissolution was wrongful because the partnership agreement set out the methods of dissolving the Partnership, and the defendant dissolved the Partnership otherwise.[136]

It could have been argued that, because the dissolution events in the partnership agreement had not occurred, the Partnership had not been dissolved at all.[137] Recognizing the possibility of this argument, the Court observed in a footnote:

> Plaintiffs did not take the position that defendant's action had no legal effect and failed to dissolve the Partnership. On appeal, plaintiffs concede that the Partnership dissolved by operation of law. The dispute concerns whether the dissolution violated the agreement. Consequently, we have no occasion to consider whether plaintiffs would prevail if they had argued that under the agreement a purported unilateral dissolution is no dissolution at all.[138]

Emphasizing the point that the dissolution was wrongful, the Court further stated:

> Here, the agreement stated that the Partnership "shall continue until it is terminated as hereinafter provided," and, in a subsequent provision,

131. *Id.* at 280–81, 101 N.E.3d at 344–45, 76 N.Y.S.3d at 876–77.
132. *See id.* at 281, 101 N.E.3d at 345, 76 N.Y.S.3d at 877.
133. *Id.* at 279, 101 N.E.3d at 344, 76 N.Y.S.3d at 876.
134. *Congel*, 31 N.Y.3d at 287, 101 N.E.3d at 349, 76 N.Y.S.3d at 881.
135. *Id.* (citing N.Y. P'SHIP LAW § 62(1)(b) (McKinney 2015)).
136. *See id.*
137. *See id.* at 289, 101 N.E.3d at 351, 76 N.Y.S.3d at 883.
138. *Id.* at 280, 101 N.E.3d at 344, 76 N.Y.S.3d at 876, n.1.

> stated that the Partnership would dissolve upon "[t]he election by the Partners to dissolve the Partnership" or "[t]he happening of any event which makes it unlawful for the business of the Partnership to be carried on or for the Partners to carry it on in Partnership." The partners clearly intended that the methods provided in the agreement for dissolution were the only methods whereby the partnership would dissolve *in accordance with the agreement*, and by implication that unilateral dissolution would breach the agreement. In other words, the agreement contemplated dissolution only in two instances, leaving no room for other means of dissolution that would be in accordance with its terms.[139]

Partnership Law section 69(2)(b) provides in relevant part that, after a partnership has been dissolved in violation of its partnership agreement, the non-violating partners can continue the partnership business with minimal disruption:

> The partners who have not caused the dissolution wrongfully, if they all desire to continue the business in the same name, either by themselves or jointly with others, may do so, during the agreed term for the partnership and for that purpose may possess the partnership property, provided they secure the payment by bond approved by the court, or pay to any partner who has caused the dissolution wrongfully, the value of his interest in the partnership at the dissolution, less any damages[.][140]

The remaining partners of the Poughkeepsie Galleria Company partnership asserted that they were continuing the partnership business in accordance with this provision.[141]

Recovery of damages for breach of the Partnership agreement was authorized in Partnership Law section 69(2)(a)(II), which provides:

> When dissolution is caused in contravention of the partnership agreement the rights of the partners shall be as follows: Each partner who has not caused dissolution wrongfully shall have . . . The right, as against each partner who has caused the dissolution wrongfully, to damages for breach of the agreement.[142]

To sum up, the defendant was entitled to the value of his partnership interest, and the plaintiffs were entitled to damages.[143]

The plaintiffs claimed that their damages included $2,717,314.50 in attorneys' fees and $79,705.50 in experts' fees.[144] The Court denied the

139. *Congel*, 31 N.Y.3d at 289, 101 N.E.3d at 350–51, 76 N.Y.S.3d at 882–83.
140. N.Y. P'SHIP LAW § 69(2)(b) (McKinney 2015).
141. *See Congel,* 31 N.Y.3d at 280, 101 N.E.3d at 344, 76 N.Y.S.3d at 876.
142. P'SHIP § 69(2)(a)(II).
143. *Congel*, 31 N.Y.3d at 298, 101 N.E.3d at 357, 76 N.Y.S.3d at 889.
144. *Id.* at 282, 101 N.E.3d at 345, 76 N.Y.S.3d at 877.

recovery of these fees, holding that awarding them to plaintiffs "contradict[s] New York's well-established adoption of the American Rule that 'the prevailing litigant ordinarily cannot collect . . . attorneys' fees from its unsuccessful opponents.'"[145] Further:

> Plaintiffs' approach would mean that fees could be awarded to the victorious party in any breach of contract litigation, as long as that party persuaded a court that it had to litigate the issue in order to avoid the consequences of defendant's breach. Indeed, this purported exception would be so large as to swallow the American Rule.[146]

The Court closed with consideration as to whether the value of the defendant's 3.08% interest should be subject to a minority discount.[147] The Court started with a black-letter definition:

> A minority discount is a standard tool in valuation of a financial interest, designed to reflect the fact that the price an investor is willing to pay for a minority ownership interest in a business, whether a corporation or a partnership, is less because the owner of a minority interest lacks control of the business . . . . A minority discount is not relevant in valuing an asset, such as a publicly traded share, that is already priced as a minority holding, the fair market value of which can be determined simply by examining the market price of the stock.[148]

The trial court decided against applying a minority discount, based upon cases holding against use of a minority discount when valuing a minority stockholding in a closely-held corporation.[149] The appellate division reversed, distinguishing wrongful partnership dissolution from the situation where a dissenting shareholder dissolves a corporation.[150]

IV. CORPORATIONS

Section 1104-a of the business corporation law allows the holders of twenty percent or more of the voting shares of a close corporation to petition for dissolution where the controlling persons "have been guilty of illegal, fraudulent or oppressive actions toward the complaining shareholders[.]"[151] In 1984, the Court of Appeals, in ruling upon a section

145. *Id.* at 290–91, 101 N.E.3d at 352–53, 76 N.Y.S.3d at 883–84 (quoting Hunt v. Sharp, 85 N.Y.2d 883, 885, 649 N.E.2d 1201, 1202, 626 N.Y.S.2d 57, 58 (1995)).

146. *Id.* at 292, 101 N.E.3d at 352, 76 N.Y.S.3d at 884.

147. *See id.* at 279, 294, 101 N.E.3d at 344, 354, 76 N.Y.S.3d at 876, 886.

148. *Congel,* 31 N.Y.3d at 295–96, 101 N.E.3d at 354, 76 N.Y.S.3d at 886, n.10.

149. *Id.* at 284, 101 N.E.3d at 347, 76 N.Y.S.3d at 879.

150. *See id.* at 285–86, 101 N.E.3d at 348, 76 N.Y.S.3d at 880.

151. N.Y. BUS. CORP. LAW § 1104-a(a)(1) (McKinney 2003).

1104-a petition for "oppressive" conduct in the case of *In re Kemp & Beatley, Inc.*,[152] said:

> It would be inappropriate . . . for us in this case to delineate the contours of the courts' consideration in determining whether directors have been guilty of oppressive conduct. As in other areas of the law, much will depend on the circumstances in the individual case.[153]

In 2019, *Straka v. Arcara Zucarelli Lenda & Assoc. CPAs*, one of the circumstances was disrespect based upon gender.[154] Combined with other acts of unfairness, it constituted oppression justifying relief under Business Corporation Law section 1104-a(a)(1).[155]

Diane Straka, along with David A. Arcara, Jon V. Zucarelli, and Donald J. Lenda, in 2014 formed Arcara, Zucarelli, Lenda & Straka CPAs, P.C., by combining two accounting firms.[156] Each of the named CPAs was an officer, director, and twenty five percent shareholder, and each took on specific assignments: Straka's was information technology ("IT").[157] Thomas Urbanek and Sidney Weiss came from one of the combining firms, Brody, Weiss, Zucarelli & Urbanek, CPAs, P.C. (Brody Weiss), as employees rather than owners.[158]

The court held a hearing on the petition by Diane Straka under Business Corporation Law Section 1104-1(a)(1) and reported the following facts:

> Shortly after moving into the new office in January 2015, Straka met Urbanek and introduced herself. Knowing that she was a partner of the corporation, Urbanek said, "Oh, are you the one who makes me coffee?" Soon thereafter, he told her to look at a cartoon he posted on his office door that was demeaning to women. Straka received complaints that Urbanek made unsolicited, demeaning remarks to other female employees as well. Straka and those women elected not to eat in the corporate lunch room as Urbanek's comments made them uncomfortable.
>
> Straka raised the issue of Urbanek's demeaning comments to women at the office at a partnership meeting. Zucarelli volunteered to speak with Urbanek because he had worked with him the longest. At the hearing,

152. *See generally* 64 N.Y.2d 63, 473 N.E.2d 1173, 484 N.Y.S.2d 799 (1984) (involving a situation where a majority in close corporation paid profits to itself in the form of salaries and bonuses, and denied minority any share of profits by not paying any dividends).

153. *Id.* at 73, 473 N.E.2d at 1179, 484 N.Y.S.2d at 805.

154. 62 Misc. 3d 1064, 1065, 92 N.Y.S.3d 567, 569 (Sup. Ct. Erie Cty. 2019).

155. *See id.*; BUS. CORP. § 1104-a(a)(1).

156. *See Straka*, 62 Misc. 3d at 1066, 92 N.Y.S.3d at 570.

157. *See id.*

158. *Id.*

> Zucarelli testified that he went to Urbanek's office and "just said, you know, your—whatever it is, it's like, Tom, you can't do this stuff, you got to tone it down. I don't know exactly what I told him. I didn't get any resistance, he was like, okay." Zucarelli could provide no additional details of this impromptu meeting. He made no notes before, during or after the meeting, never followed up with Urbanek, and never followed up with Arcara, even though Arcara was in charge of human resources.[159]

With regard to the firm's operations, Straka as IT manager wanted to convert the firm's tax preparation software from software named Lacerte to software suite called UltraTax.[160] However:

> At a May 2015 meeting to discuss the conversion, Zucarelli talked down to Straka in front of other staff members, indicating that she did not know how to run a tax practice. On June 4, 2015, Straka sent an email message to all shareholders and staff at the corporation outlining priorities for the software conversion, with the hope that it would be completed by the end of the year. Several days later and without consulting with Straka, Lenda approved the payment of a June 9, 2015 invoice for Lacerte tax preparation software for the following year.[161]

Another operational problem was that Straka had been told, at the time the corporation was being formed, that staff employees brought over from the former Brody Weiss firm would be available for the firm's audit practice over the summer.[162] Straka found, however, that they were unavailable because Urbanek needed them, and he needed them because he would not use a computer.[163]

Then:

> Another incident occurred later in October 2015, when Straka and Lenda sat in the office conference room before a meeting. Urbanek entered and asked where he should sit. When Straka told him he could sit anywhere, Urbanek asked, "Can I sit on your lap, Diane?" Lenda smirked, and Straka told Urbanek that he could sit on Lenda's lap.
>
> Arcara recognized Urbanek's inappropriate behavior and tried to address Straka's complaints on at least two occasions. At the second meeting, Urbanek told Arcara that he would not change his behavior. The majority shareholders ultimately relocated Urbanek's office away from the corporation staff and hired external human resource

159. *Id.* at 1067, 92 N.Y.S.3d at 571.
160. *Id.*
161. *Straka*, 62 Misc. 3d at 1067–68, 92 N.Y.S.3d at 571.
162. *See id.* at 1068, 92 N.Y.S.3d at 571.
163. *Id.*

> contractors to provide sexual harassment seminars to the corporation staff and shareholders, beginning in June 2016.
>
> That same month, Straka gave formal verbal notice that she would be leaving the corporation. On August 12, 2016, Straka resigned in a letter confirming her "resignation as a shareholder, director and officer," effective that day.[164]

Importantly, Straka did not cease to be a shareholder for purposes of the court's subsequent analysis of section 1104-a, for the court held Straka's "resignation as a shareholder was made in reliance upon future redemption of her shares, which she has never tendered."[165] Therefore, she continued to be a shareholder during the relevant periods.[166]

When the corporation had originally been formed, the shareholders had agreed to "a compensation plan called the 'earnings matrix,' a formula . . . that allocated client revenues and firm expenses."[167] As it operated in practice, the earnings matrix "resulted in Straka receiving the lowest amount of compensation despite having the second highest billing and revenue in 2016."[168] Theoretically, the corporation could have paid dividends and compensated Straka in that fashion, "but the majority opted to pay only wages based upon the earnings matrix, thereby excluding Straka from sharing in the profits."[169]

In January 2017, without Straka's knowledge, the majority shareholders added Paul Eusanio as a fifth equal shareholder, so that Straka's percentage interest was reduced from twenty five percent to twenty percent.[170]

To determine whether the actions of the majority were "oppressive" within the meaning of Business Corporation Law Section 1104-a(a)(1),[171]

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164. *Id.* at 1068, 92 N.Y.S.3d at 572.
165. *Id.*
166. *See Straka*, 62 Misc. 3d at 1070, 92 N.Y.S.3d at 573.
167. *Id.* at 1066, 92 N.Y.S.3d at 570.
168. *Id.* at 1068–69, 92 N.Y.S.3d at 572.
169. *See id.* at 1069, 92 N.Y.S.3d at 572.
170. *Id.* at 1069, 92 N.Y.S.3d at 572.
171. N.Y. BUS. CORP. LAW § 1104-a(a)(1) (McKinney 2003).

> "(a) The holders of shares representing twenty percent or more of the votes of all outstanding shares of a corporation, other than a corporation registered as an investment company under an act of congress entitled 'Investment Company Act of 1940', no shares of which are listed on a national securities exchange or regularly quoted in an over-the-counter market by one or more members of a national or an affiliated securities association, entitled to vote in an election of directors may present a petition of dissolution on one or more of the following grounds: (1) The directors or those in control of the corporation have been guilty of illegal, fraudulent or oppressive actions toward the complaining shareholders . . . ." *Id.*

the Court cited the Court of Appeals' decision in *Matter of Kemp & Beatley, Inc.* for the propositions that "[a] court considering a petition alleging oppressive conduct must investigate what the majority shareholders knew, or should have known, to be the petitioner's expectations in entering the particular enterprise" and "oppression should be deemed to arise only when the majority conduct substantially defeats expectations that, objectively viewed, were both reasonable under the circumstances and were central to the petitioner's decision to join the venture."[172]

The court then ruled on what reasonable and central expectations of Straka were substantially defeated and held:

> This court finds that Arcara, Zucarelli and Lenda, and indeed, any shareholder of any corporation, should know that a female shareholder reasonably expects to be treated with equal dignity and respect as male shareholders forming the majority. Straka has demonstrated that she was not. The shareholders' slow and inadequate response to Urbanek's demeaning behavior marginalized Straka, as did the lack of respect provided to her as the head of IT at the corporation.[173]

Other frustrated expectations were:

- Collaboration from staff members coming over from Brody Weiss was promised, but not delivered.[174]
- Compensation under the earnings matrix was unfair.[175]
- The earnings matrix was used to compensate the majority shareholders by salary, as opposed to dividends: "When the majority shareholders of a close corporation award *de facto* dividends to all shareholders except a class of minority shareholders, such a policy may constitute 'oppressive actions' and serve as a basis for an order made pursuant to section 1104-a of the Business Corporation Law dissolving the corporation."[176]
- Straka's shareholder percentage was diluted without her consent.[177]

Having found oppressive conduct, the court cited *Kemp & Beatley* for authority "to determine whether some remedy short of or other than

172. *Straka*, 62 Misc. 3d at 1070, 92 N.Y.S.3d at 573 (quoting In re Kemp & Beatley, Inc., 64 N.Y.2d 63, 73, 473 N.E.2d 1173, 1179, 484 N.Y.S.2d 799, 805 (1984)).

173. *Id.*

174. *See id.*

175. *See id.*

176. *Id.* at 1070–71, 92 N.Y.S.3d at 573 (quoting *In re Kemp & Beatley, Inc.*, 64 N.Y.2d at 67, 473 N.E.2d at 1175, 484 N.Y.S.2d at 801).

177. *Straka*, 62 Misc. 3d at 1071, 92 N.Y.S.3d at 573 (citing Twin Bay Vill. v. Kasian, 153 A.D.3d 998, 1003, 60 N.Y.S.3d 560, 565 (3d Dep't 2017)).

dissolution constitutes a feasible means of satisfying both the petitioner's expectations and the rights and interests of any other substantial group of shareholders" and for "broad latitude in fashioning alternative relief."[178] The court ruled that a buyout of Straka's shares would be the proper remedy.[179]

The important conclusion from the *Straka* case is that, in the words of the court, "disrespectful and unfairly disproportionate treatment of a female shareholder by the male majority in a closely held corporation constitutes corporate oppression pursuant to Business Corporation Law section 1104-a(a)(1)."[180]

V. LIMITED LIABILITY COMPANIES (LLCS)

A. Interpreting the LLC Law

Section 508(a) of the LLC Law provides that an LLC shall not "make a distribution to a member" if, as a result, the liabilities of the LLC would exceed its fair market value.[181] Subdivision (c) of section 508 provides a three-year statute of limitations: ". . . a member who receives a wrongful distribution from a limited liability company shall have no liability under this article or other applicable law for the amount of the distribution after the expiration of three years from the date of the distribution."[182]

Geron v. Craig (In re Direct Access Partners, LLC) joined a line of decisions holding that the three-year time limit applies to proceedings under the New York Debtor and Creditor Law and section 544 of the U.S. Bankruptcy Code.[183] In *Geron*, the trustee in bankruptcy of an LLC brought an adversary proceeding to recover payments made to defendants by the LLC.[184] The trustee asserted that the payments were fraudulent transfers under the Bankruptcy Code and fraudulent convents under New York law.[185] Accordingly, the statute of limitations, argued the trustee, was the New York six-year statute of limitations.[186]

178. *Id.* at 1071, 92 N.Y.S.3d at 574 (quoting *In re Kemp & Beatley,* 64 N.Y.2d at 73, 74, 473 N.E.2d at 1180, 484 N.Y.S.2d at 806) (citing In re Clever Innovations, Inc., 94 A.D. 3d 1174, 1177, 941 N.Y.S.2d 777, 780 (3d Dep't 2012)).

179. *Id.* at 1071, 92 N.Y.S.3d at 574.

180. *Id.* at 1065, 92 N.Y.S.3d at 569.

181. *See* N.Y. LTD. LIAB. CO. LAW § 508(a) (McKinney 2016).

182. *Id.* § 508(c).

183. *See* 602 B.R. 495, 518 (Bankr. S.D.N.Y. 2019).

184. *See id.* at 503.

185. *See id.*

186. *Id.* at 513.

However, the Court noted that section 508(c) of the LLC Law provides:

> a member who receives a wrongful distribution from a limited liability company shall have no liability under this article *or other applicable law* for the amount of the distribution after the expiration of three years from the date of the distribution. [emphasis by Court][187]

Evaluating case law, the Court concluded that the three-year statute of limitations of the LLC Law took precedence.[188]

VI. DERIVATIVE LITIGATION

Horowitz v. 148 South Emerson Assocs. LLC presented the uncommon situation where an LLC member defended an action against the LLC derivatively against a plaintiff, in contrast to an LLC member who brings an action as plaintiff on behalf of the LLC against a third party.[189]

The origin of the suit was that Drew Doscher, Michael Meagher, Michael Meyer, and Stephen Smith, who were business associates at The Seaport Group, a New York City broker-dealer, formed The Sloppy Tuna, a restaurant in Montauk, New York, in 2010 and 2011.[190] Each individual was the indirect owner of twenty-five percent of the restaurant.[191] However, Doscher had a falling out with Seaport Group and Meagher, Meyer, and Smith, in January, 2013, which resulted "in a series of bitterly contested suits[.]"[192] *Horowitz* was a dispute in Federal court over "The Sloppy Tuna" name and trademark.[193]

The defendant, 148 South Emerson Associates LLC (Associates) had been formed in March 2011 to own and operate The Sloppy Tuna.[194] At the time of the *Horowitz* opinion, the owners of Associates were Michael Meyer and Drew Doscher, each owning fifty percent.[195]

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187. *Id.* at 517, citing N.Y. LTD. LIAB. CO. LAW § 508(c) (McKinney 2016).

188. *Geron,* 602 B.R. at 517.

189. *See* 888 F.3d 13, 18 (2d Cir. 2018).

190. *See id.* at 16.

191. *See id.*

192. *See id.* (citing Doscher v. Sea Port Grp. Sec., LLC, 832 F.3d 372 (2d Cir. 2016)). In a related proceeding, the Suffolk County Supreme Court noted that "The 'Sloppy Tuna' is 'the' resort hot-spot on the east end of Long Island. It is a bar-restaurant that conducts a proverbial land office business during the summer months." Meyer v. 148 S. Emerson Assoc., LLC, No. 068379/2014, 2017 N.Y. Misc. LEXIS 2157, at 1 (Sup. Ct. Suffolk Cty. May 9, 2017). *See also* Richard Johnson, *Fish tale stretches*, N.Y. POST, Mar. 7, 2019, at 14 ("Sloppy Tuna will be raucously raging on this summer, while courtroom drama stirs . . . .").

193. *See Horowitz,* 888 F.3d at 17.

194. *Id.* at 16.

195. *See id.*

Drew Doscher was also the sole member of Montauk U.S.A., LLC (Montauk), a Georgia LLC.[196] Mark Horowitz was the alleged manager of Montauk.[197] Around May of 2011, Montauk registered trademarks for The Sloppy Tuna with the U.S. Patent and Trademark Office, but did not enter into a written contract with Associates permitting Associates to use the trademarks.[198]

In January 2013, Doscher and Meyer had a falling out.[199] In October 2013, Montauk (100% owned by Doscher) and Associates (50% owned by Doscher) supposedly signed a written License Agreement for Associates' use of The Sloppy Tuna trademarks; Horowitz signed for Montauk and Doscher signed for Associates.[200] Meyer, the other fifty percent owner of Associates, claimed that the license agreement was unenforceable.[201]

Doscher and Meyer became deadlocked as owners of Associates and, on February 19, 2015, a New York state court appointed a receiver for Associates.[202] Montauk (owned by Doscher) "terminated the License Agreement" between Montauk and Associates "purportedly because the New York state court's order wrested too much control of the restaurant from Doscher."[203] Then Montauk and Horowitz sued Associates under the federal Lanham Act[204] in the U.S. District Court for the Eastern District of New York, on the grounds that Associates no longer had any right to use The Sloppy Tuna trademarks.[205]

Defending the action against Associates was counsel for Meyer (the other fifty percent owner of Associates), who was claiming to defend derivatively on behalf of Associates.[206] The Receiver for Associates provided a declaration "in which he stated that he eagerly consented to Meyer's derivative defense of the case and that, in his judgment, Meyer's derivative representation was in Associates' best interest."[207]

196. *See id.*
197. *Id.*
198. *See Horowitz,* 888 F.3d at 16.
199. *Id*. (citing Doscher v. Sea Port Grp. Sec., LLC, 832 F.3d 372, 374 (2d Cir. 2016)).
200. *Id.* at 16–17.
201. *See id.* at 17.
202. *Id.*
203. *Horowitz*, 888 F.3d at 17.
204. *Id.* at 18.
205. *See id.*
206. *See id.*
207. *Id.*

After the U.S. District Court ruled for the defense and dismissed the action, Montauk appealed,[208] one of his arguments being that "derivative representation rights do not extend to litigation *defense*."[209] The Second Circuit, applying New York law, stated:

> Montauk also argues that even if LLC members may bring derivative lawsuits, they may not derivatively *defend* lawsuits. Montauk cites no law, or reasoning, to support this contention, and the argument is not pressed in its reply brief. The argument is meritless nonetheless. . . . [T]he core question in a derivative litigation inquiry is who is a proper entity to represent the company's interests. There is no reason for different rules for that question when the company defends against rather than brings a suit.[210]

The court cited no authority in favor of derivative litigation defense. Instead, the court's opinion states that because the plaintiff did not bring forward any authority which prohibits derivative litigation defense, it should be allowed.[211] The court also ruled that derivative litigation defense is subject to the same "demand excused" rule which pertains to a derivative complaint: the litigant must make an effort to have the entity defend the action, and when the entity elects not to defend, the litigant must provide an adequate explanation why the litigant should be allowed to defend in the entity's stead.[212] In this case, the consent of the receiver for the entity was sufficient explanation.[213]

Doscher, who owned the plaintiff in *Horowitz*, was also a fifty percent owner of the defendant Associates.[214] If a receiver had not been appointed for Associates, Doscher might have been able to prevent Associates from defending itself.[215] Meyer, as the owner of the other fifty percent of Associates, should have had some way to defend against an action which would have taken away the value of Associates.[216]

CONCLUSION

The New York courts continued resolving difficult disputes of ownership and management of business associations with existing

208. *Horowitz*, 888 F.3d at 18–19.
209. *Id.* at 20.
210. *Id.* at 21–22.
211. *See id.*
212. *See id.* at 20.
213. *See Horowitz*, 888 F.3d at 21.
214. *See id.* at 17.
215. *See id.* at 21 (citing Golden Pac. Bancorp v. FDIC, No. 95-CV-9281, 2002 U.S. Dist. LEXIS 24961, at *30–31 (S.D.N.Y. 2002)).
216. *See id.* at 19.

procedural and substantive legal tools. Although the decision of the Board of Directors in the *Xerox* case[217] was ultimately upheld on appeal,[218] the trial court's description of the facts provides an instructive example of how a Board can expose itself to criticism in approving a sale of the company. The courts also outlined doctrines of business law which they continue to apply to business disputes.

217. *In re Xerox Corp. Consol. S'holder Litig.,* 61 Misc. 3d 176, 76 N.Y.S.3d 759 (Sup. Ct. N.Y. Cty. 2018).

218. *Deason v. Fujifilm Holdings Corp.*, 165 A.D.3d 501, 86 N.Y.S.3d 28 (1st Dep't 2018).