

# Business-Judgment Rule Applied in New York to Going-Private Transaction with Procedural Protections

**November 21, 2014**

The New York Appellate Division, First Department, ruled yesterday that the business-judgment rule – not the entire-fairness standard of review – can apply to a going-private transaction with the majority shareholder where the majority shareholder did not participate in the board's vote on the merger, the remaining directors were not alleged to be self-interested, and the merger required the approval of the majority of the minority shareholders. *In re Kenneth Cole Productions, Inc. Shareholder Litigation*, Index No. 650571/12 (N.Y. App. Div. 1st Dep't Nov. 20, 2014).

The ruling aligns New York law with Delaware law and provides greater protection for interested transactions implemented with procedural protections that obviate any coercion or conflicts of interest.

The case involved Kenneth Cole's effort to take private Kenneth Cole Productions, Inc., in which Mr. Cole was the majority shareholder. A shareholder challenged the transaction and alleged that the trial court should have reviewed the claims under the more rigorous "entire fairness" standard – rather than the more deferential business-judgment rule – because of Mr. Cole's role in the company. The trial court dismissed the case, and the Appellate Division affirmed.

Based on the existence of the procedural protections noted above – Mr. Cole's lack of participation in the board's decision, the requirement of majority-of-the-minority approval, and the lack of allegations that the remaining directors were self-interested – the Appellate Division held that the business-judgment rule applied. The court rejected the argument that the remaining directors were "controlled" by Mr. Cole, because "it is not enough to charge that a director was nominated by or elected at the behest of those controlling the outcome of a corporate election." The court also rebuffed the argument that the proxy statement had been misleading.

The Appellate Division's ruling accords with the Delaware Supreme Court's March 2014 decision in *Kahn v. M&F Worldwide Corp.*, which held that the "business judgment standard is the standard of review that should govern mergers between a controlling stockholder and its corporate subsidiary, where the merger is conditioned *ab initio* upon both the approval of an independent, adequately-empowered Special Committee that fulfills its duty of care; and the uncoerced, informed vote of a majority of the minority stockholders."