



Punitive Damages: Punishment for Bad-Acting Shareholders?

By Randy G. Gullickson

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Punitive damages, intended to punish willful and malicious wrongful acts, are not a part of most business lawsuits. Minnesota law prohibits plaintiffs from seeking punitive damages in a complaint at the outset of a lawsuit. Plaintiffs must instead obtain the permission of a judge to even assert such a claim by moving for leave to amend the complaint to add a punitive damages claim at a later time in the case. Such procedural hurdles and the elevated burden of proof – clear and convincing evidence – properly make punitive damages awards the exception to the rule.

Despite the hurdles, punitive damages are sometimes sought and awarded in business disputes. Successfully obtaining the right to go to trial on a punitive damages claim can significantly affect the outcome at trial, and will almost always alter the risk profile of a case that the parties must take into account while contemplating the potential of a settlement before throwing the dice on both compensatory damages and punitive damages before a judge or jury.

Some of the more dramatic punitive damage claims and awards in recent years have been seen in shareholder disputes involving owners of closely held corporations. Interestingly, disputes within family-owned businesses often seem to be more prone to punitive damage claims, which is perhaps reflective of the failure of some in the business world to heed the biblical lesson from the story of those early family business owners, brothers Cain and Abel (who, you may recall, operated a sheep herding and farming business).

In general, punitive damages can be recovered where a defendant acts with “deliberate disregard for the rights or safety of others” Minn. Stat. Sec. 549.20, subd. 1. Relationships between owners in

closely held companies are infused with fiduciary obligations to one another, including the duty to act in an honest, fair and reasonable manner in the operation of the business. Shareholder disputes generally include claims of breach of these duties (and/or other torts) that can serve as the foundation for a punitive damage claim. When the underlying duty is an exacting one – shareholders in closely held corporations are viewed as business partners who owe one another a fiduciary duty that imposes on them the “highest standard of integrity and good faith” – it is perhaps easier to identify deliberate disregard or deviations from the standard.

In 1984, the Minnesota Court of Appeals made it clear that punitive damages can be an appropriate punishment for a shareholder who acts in an aggressive manner to violate the rights of his co-shareholder. In *Evans v. Blesi*, a 50 percent defendant shareholder (Blesi) engaged in threats, intimidating tactics and dishonesty to force his co-shareholder (Evans) to sign share transfer documents giving Blesi majority control and subsequently bullied Evans into a “voluntary” resignation from the company. This conduct, according to the appellate court, justified a \$250,000 punitive damage award against the bad acting shareholder.

Two more recent cases – from courts in Minnesota and Wisconsin – resulted in larger and more dramatic damage awards in shareholder disputes involving sibling or other family rivalries. *McGrath v. MICO, Inc., et al.* was a dispute between brothers who were co-shareholders of a successful equipment manufacturer started by their father. The Nicollet County trial court judge found that shortly after their father's death, the two defendant brothers made a calculated decision to force the plaintiff brother to either accept



an ever increasing isolation and eventual separation from the company or to sue and enforce his rights. Their efforts to force Dan out of the company (without paying him fair value for his shares) involved a litany of bad acts, which the court found to be “motivated by vengeance and retribution rather than legitimate business concerns.” The defendants did not exactly make it hard for the judge to reach these findings, as the trial court decision is filled with descriptions of profanity-laced emails and other communications in which defendants exhibited their disdain for their brother and described their ongoing efforts to demean him and force him out of the business. Following trial, in addition to significant stock buy-out, compensatory damages, and attorneys’ fee awards, the trial court judge awarded the plaintiff punitive damages of over \$2.1 million against one brother and over \$1.6 million against the other brother. A jury awarded another \$1 million in punitive damages against the company on a whistleblower claim. The trial court award was affirmed on appeal.

In another “bitter interfamilial dispute,” this one across the border in Wisconsin, a father and two sons owned successful companies in the meat snack business. In *Northern Air Services v. Link*, the father and one son sought to enforce a buy-sell agreement in order to compel the second son (Jay) to surrender his shares, while Jay

counterclaimed based on allegations that as a minority shareholder he was being squeezed out of the companies in an effort to acquire his shares at a discounted price. The complex case was tried in three phases, one involving a jury trial on (1) breach of fiduciary claims asserted by Jay against his father for stripping him of all of his company responsibilities and (2) breach of fiduciary duty claims by the companies against Jay. The jury found breaches of fiduciary duty by both Jay and his father. Based on a statutory punitive damages standard that like Minnesota’s requires malicious conduct or intentional disregard of another’s rights, and in a “pox on both houses” approach, the jury found the father liable to Jay for \$736,000 for compensatory damages and \$5 million in punitive damages, while finding Jay liable to the companies for just \$1 in com-

pensatory damages and \$5 million in punitive damages. The trial court judge reduced the punitive damage awards to amounts equal to the awards for compensatory damages, although the large punitive damage award against the father was subsequently reinstated on appeal on procedural grounds.

The lessons from these family business shareholder disputes: (1) claims for punitive damages can be a significant and powerful tool in the right shareholder case; and (2) be kind to family members, especially if they are your business partners.

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