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**Betrayed, Belittled . . . but Triumphant: Claims of
Shareholders in Closely Held Corporations**

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BETRAYED, BELITTLED...BUT TRIUMPHANT: CLAIMS OF SHAREHOLDERS IN CLOSELY HELD CORPORATIONS

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I. INTRODUCTION

With the vast majority of Minnesota corporations being small, closely held businesses and most shareholders owning less than a controlling interest in the corporations, it is important for the practitioner to be familiar with the rights and remedies that are available to minority shareholders of these corporations. This Article briefly discusses the oppression of minority shareholders and then discusses the various theories and claims minority shareholders may utilize to enforce their rights. Finally, the Article discusses the general trend of increasing minority shareholder rights and the recent Minnesota Court of Appeals decision which appears to limit some of those rights.

II. THE DILEMMA OF MINORITY SHAREHOLDERS IN CLOSELY HELD CORPORATIONS

Close corporations¹ typically are formed by friends, relatives, or other business associates who choose to combine their capital, skills, labor and experience in a new business. Shareholders in a close corporation generally plan to be employed by the corporation and to have an active roll in management. As a result, shareholders usually expect to receive a salary, bonus and additional benefits consistent with their roles as employees, officers, and directors.

While close corporations begin as friendly ventures, the balance of power in the close corporation often lends itself to oppression of those shareholders who do not control the corporation and usually own only a small percentage of shares—the minority shareholders. Minority shareholders may be subjected to a “freeze out,” (sometimes known as a “squeeze out”) by the majority shareholders.² Typical “freeze out” techniques include terminating the minority shareholder’s employment with the corporation or terminating dividends and the minority shareholder’s return on his or her investment.³

Although minority shareholders in any corporation are in a difficult position due to their lack of control, minority shareholders in closely held corporations have uniquely difficult positions because their shares are not readily marketable. In other words, when minority shareholders in a large, publicly-traded corporation become dissatisfied with corporate operations, they can “vote with their feet”—sell their shares and discontinue their involvement with the corporation. Minority shareholders in the closely held corporation, on the other hand, often cannot easily sell their shares.⁴

The lack of a market for close corporation shares owned by a minority shareholder means that a non-controlling investor may be locked into a business that is providing little return on investment, or at least is failing to fulfill the owner’s nonmonetary expectations. Left without a meaningful return on his or her investment, the minority shareholder may have little choice but to sell for less than a fair price, usually to the majority shareholders.

When the Minnesota Business Corporations Act (MBCA) was enacted by the Minnesota legislature in 1981, it contained several important provisions for minority shareholders of closely held corporations.⁵ Through subsequent judicial interpretations and legislative amendments to the MBCA, minority shareholders' rights have been significantly expanded.⁶

A recent decision of the Minnesota Court of Appeals, however, takes away many of the rights that have been provided to minority shareholders over the last fifteen years.⁷ The *Skoglund* decision leaves minority shareholders' rights on unsure footing. At this time, it is unclear whether minority shareholders have reached the pinnacle of their protection, with *Skoglund* signaling a limit to their long-awaited rights, or whether *Skoglund* is an anomaly which will be remedied by further judicial decisions or legislative amendment.

III. RIGHTS AND REMEDIES OF SHAREHOLDERS IN CLOSELY HELD CORPORATIONS

The basic causes of action available to a minority shareholder are: (1) dissolution or mandatory buy-out under Minnesota Statute section 302A.751; (2) dissenter's rights actions; (3) equitable remedies under Minnesota Statute section 302A.467; or (4) shareholder derivative suits. While minority shareholders may utilize any of the causes of action, the remedies under the dissolution or buy-out provision of section 302A.751 are used most frequently by minority shareholders.⁸

A. Dissolution or Mandatory Buy-out under Section 302A.751

Section 302A.751, subdivision 1(b), offers the strongest protection for a minority shareholder in a close corporation by providing for equitable relief including, in an extreme case, dissolution of the corporation.⁹ A mandatory buy-out of shares is a very significant remedy for minority shareholders under section 302A.751. If one of the section's six enumerated circumstances is established, the court may, upon motion of a corporation or a shareholder, order the sale by a plaintiff or a defendant of all shares held by that party to either the corporation or the moving shareholders, whichever is specified in the motion.¹⁰ Typically, a minority shareholder brings a motion for a buy-out and asks that the corporation purchase the shareholder's shares. The buy-out motion contains several components which will be discussed in the following paragraphs.

1. *Unfairly Prejudicial Conduct*

When section 302A.751 was enacted in 1981, one of the grounds for bringing a claim under the provision was when the directors or those in control of the corporation had acted fraudulently, illegally, or in a manner “persistently unfair” toward one or more shareholders.¹¹ In 1983, this language was amended to the current version, providing relief for “unfairly prejudicial conduct.”¹² Under the original language of the statute, the shareholder had to establish a continuing course of abuse to meet the “persistently unfair” standard.¹³ With the amended language, a claim may succeed upon establishing just a single instance of unfairly prejudicial conduct toward the minority shareholder.¹⁴

2. *Reasonable Expectations of All Shareholders*

When it was enacted, the buy-out provision provided that, in determining whether to order a buy-out or dissolution, the court should take into consideration the special duty that shareholders of a close corporation owe to one another and the reasonable expectations of the shareholders as they existed at the inception of the corporation and during its growth.¹⁵ The concept of the shareholder’s reasonable expectations has been applied broadly to protect minority shareholder’s rights.

For instance, in *Pedro v. Pedro*, the term “reasonable expectations” was defined to include lifetime employment.¹⁶ *Pedro* involved a family-owned business owned equally by three brothers. One of the shareholder brothers brought a claim seeking dissolution of the corporation and damages for wrongful termination after he found discrepancies in the corporation’s financial records and was subsequently fired. Although the shareholder had been employed by the business for forty-five years, his brothers warned him that he would be out of the corporation if he continued his investigation. The Minnesota Court of Appeals found that “(t)he reasonable expectations of such a shareholder are a job, salary, a significant place in management, and economic security for his family.”¹⁷ The court found that the corporation violated an implied agreement to provide lifetime employment.¹⁸

In the past, Minnesota courts interpreted the “reasonable expectations” provision as requiring courts to consider only the reasonable expectations of the *complaining* shareholders.¹⁹ The 1994 amendments changed the “reasonable expectation” language, however, to “the reasonable expectations of *all* shareholders.”²⁰ The reasonable expectations of both majority and minority shareholders should now be examined by the court when determining whether to order equitable relief, dissolution or a buy-out.

3. *Presumption for Written Shareholder Agreements*

In addition, the 1994 legislature added a sentence to the buy-out provision which created a presumption that written shareholder agreements reflect the parties’ reasonable expectations for the matters addressed in the agreement.²¹

Prior to the amendment, courts had not always given significant weight to shareholder agreements. In fact, some courts acknowledged that shareholder agreements provided evidence of the shareholder's reasonable expectations, but refused to follow the plain language of shareholder or employment agreements.²² Under the 1994 amendment, however, written shareholder agreements are presumed to reflect the parties' intentions. The amendment emphasizes the importance of considering the parties' expectations as reflected in the agreements they have signed. Indeed, the amendment has the effect of encouraging parties to accurately set forth their expectations and intentions in written agreements relating to their stock or employment with the corporation. If the agreement accurately reflects the parties' expectations and is the product of arms-length negotiations, the agreement is presumptively valid.²³ A shareholder may rebut the presumption that his or her reasonable expectations are set forth in an agreement by demonstrating that the provision regarding "expectations" is ambiguous, being read out of context or not the product of an arms-length negotiation. The complaining shareholder always will have the traditional contract defenses regarding enforceability of the expectations provision of the agreement.

4. *Behavior of Minority Shareholders*

An interesting issue presented in context of the buy-out motion is whether misconduct by a minority shareholder should affect either the shareholder's right to a buy-out or the valuation of his or her shares in the buy-out process. The Minnesota Court of Appeals examined this issue and concluded that the behavior of the minority shareholder should not be considered when determining the right to a buy-out or the value of the minority shareholder's shares in a buy-out under section 302A.751.²⁴

Pooley v. Mankato Iron & Metal, Inc. involved a family corporation which was owned equally by Terry, Gregory, and Ronald Pooley.²⁵ Terry Pooley (Pooley) had a history of misconduct relating to the corporation that included pleading guilty to assault in the scope of his employment in the early 1980s.²⁶ In 1989, Pooley assaulted Gregory Pooley, damaged a customer's truck and, was convicted of assault and criminal damage to property.²⁷ After his conviction, the corporation terminated his employment and the shareholders voted him out as an officer and director.²⁸

Pooley sued the corporation and its directors for breach of an implied employment contract and for "unfairly prejudicial" conduct under section 302A.751.²⁹ The trial court found no implied contract for lifetime employment, but concluded that the corporation's directors had "unfairly prejudiced (Pooley) by freezing him out of a business in which he reasonably expected to participate."³⁰ The trial court ordered a buy-out of his shares at fair value.³¹

The trial court found and the court of appeals affirmed that Pooley was entitled to the fair value of his shares despite his misconduct.³² The corporation had also argued that balancing the equities required a discount to the value of Pooley's shares.³³ However, the court of appeals rejected that argument and determined that because the trial court had already determined that Pooley was entitled to the fair value of his shares, the court "did not have reason to later discount that value."³⁴

Even with the fairly egregious conduct of the shareholder in *Pooley*, the court refused to use “bad” behavior as a limit on the minority shareholder’s right to obtain a buy-out. *Pooley* is a good example of the strong protections that minority shareholders have been given under the MBCA.³⁵

5. *An Enlightened Decision?*

While the typical buy-out case involves the minority shareholder selling his or her shares to the corporation, the New Jersey Supreme Court, interpreting a statute remarkably similar to Minnesota Statutes section 302A.751, recently upheld a trial court ruling ordering majority shareholders to sell their controlling interest in a closely held corporation to the minority shareholder.³⁶ In *Muellenberg v. Bikon Corp.*, the court concluded that the majority shareholders exercised their majority power in a manner which conflicted with the expectations of the minority.³⁷ The minority shareholder had been primarily responsible for the company’s day-to-day operations and the majority shareholders had provided capital and the inventive genius for the company’s products.³⁸ When conflict developed among the shareholders, the majority shareholders voted to declare substantial dividends to all shareholders and to assert themselves in the daily operations of the company, thereby usurping the minority shareholder’s role.³⁹ Claiming that the corporation was deadlocked, the majority voted to dissolve the corporation and instituted proceedings to that end.⁴⁰

The New Jersey Supreme Court concluded that it was a close question whether the actions of the majority amounted to oppression.⁴¹ After carefully analyzing the New Jersey statute, which prohibited majority shareholders from abusing their authority as directors or acting oppressively or unfairly towards one or more minority shareholders in their capacities as shareholders, directors, officers or employees, the court concluded that the majority’s actions constituted oppressive conduct which frustrated the reasonable expectations of the minority shareholder.⁴² Most importantly, the court concluded that the appropriate remedy was to order the sale of the majority’s shares to the minority since the minority had the expectation of long-term employment and had, in fact, been running the company on a daily basis.⁴³

6. *Valuation of Shares in Section 302A.751 Actions*

In a court ordered buy-out, the purchase price for the shares is the “fair value” of the shares either as of the date of commencement of the action or any other date deemed equitable by the court.⁴⁴ “Fair value” shall be the price unless the parties have established another price for the shares in the corporation’s bylaws or a shareholder agreement, which price is reasonable under all circumstances.⁴⁵ The MBCA contains specific instructions regarding the procedure for determination of fair value. Because these follow the valuation procedures for dissenters’ rights actions, those procedures will be discussed in that section.⁴⁶

B. Dissenters' Rights

The dissenters' rights statutes, Minnesota Statutes sections 302A.471-473, permit a shareholder to "dissent" from certain fundamental corporate changes and obtain payment from the corporation for the "fair value" of the shares. In contrast to section 302A.751, which allows a shareholder to obtain payment for his or her shares by showing a broad range of "unfairly prejudicial conduct,"⁴⁷ the dissenters' rights statute only allows a shareholder to obtain payment for his or her shares upon the occurrence of one of five enumerated triggering events.⁴⁸

1. Triggering Events for Dissenters' Rights

Dissenters' rights are available when a shareholder dissents from various fundamental corporate changes such as a merger or amendment to the articles that will adversely affect the shareholder's rights.⁴⁹ Several decisions have further developed the circumstances under which shareholders are entitled to dissenters' rights. For instance, the Minnesota Supreme Court determined that, at least in a close corporation, the following actions "materially and adversely" affect shareholders' rights and therefore create dissenters' rights: (1) elimination of a requirement of thirty percent shareholder approval for certain major decisions; (2) reduction in the maximum number of directors from five to three; and (3) elimination of a requirement of seventy-five percent shareholder approval for bylaw amendments.⁵⁰

In an unpublished case, the Minnesota Court of Appeals held that dissenters' rights are not triggered if the corporate action from which a shareholder dissents turns out to be invalid.⁵¹ Similarly, the court of appeals has determined that a dissenting shareholder's right to payment for shares does not vest until the triggering corporate action takes effect.⁵²

2. Dissenters' Rights as Exclusive Remedy

Minnesota courts have held that the triggering of dissenters' rights forecloses a shareholder's action based on any alleged unfairness of the corporate change that gave rise to the rights. For instance, in *Sifferle v. Micom Corp.*, the Minnesota Court of Appeals held that a dissenters' rights action is the exclusive remedy available to a shareholder unless the action dissented from is fraudulent.⁵³

3. Procedure for Asserting Dissenters' Rights

The procedure for asserting dissenters' rights is specifically explained in Minnesota Statutes section 302A.473. At the outset, a corporation planning a vote at a shareholder meeting on any action that triggers dissenters' rights must include with its meeting notice a separate notice informing shareholders of their right to dissent and a brief description of the statutory procedure.⁵⁴

A dissenting shareholder then must (1) file a notice of intent to demand fair value for the shares before the vote, and (2) not vote in favor of the proposed corporate action.⁵⁵

After approval of the proposed action by the board, and when necessary the shareholders, the corporation must send shareholders who filed a notice of intent another notice of their dissenters' rights.⁵⁶ This notice must describe the dissenters' rights statute and include a form that the shareholder may use to demand payment.⁵⁷

In response to this after-the-fact notice, a dissenter has thirty days to perfect his or her rights by demanding payment from the corporation and surrendering his or her shares.⁵⁸ When the triggering corporate action occurs without a shareholder vote, this demand is the dissenter's first, and only requirement for perfecting the statutory dissenters' rights.⁵⁹

4. Valuation of Shares in a Dissenters' Rights Action

In both a dissenters' rights action and a buy-out motion under section 302A.751, the MBCA provides for determination of the "fair value"⁶⁰ of the shares using the process contained in the dissenters' rights statute.⁶¹

a. Procedure for Determining Fair Value

After the entry of a buy-out order, the corporation has five days to provide the shareholder with its determination of "fair value" and other information required by the dissenters' rights provision.⁶² If the parties do not agree on a fair value for the shares within forty days of the entry of the buy-out order, the court determines the fair value of the shares using the provisions of the dissenters' rights statute⁶³ and may also allow interest or costs.⁶⁴

The MBCA gives the court broad discretion in determining "fair value."⁶⁵ The court may take into account "any and all factors the court finds relevant" when determining "fair value."⁶⁶ The court may also appoint an appraiser "to receive evidence on and recommend the amount of the fair value of the shares."⁶⁷ The Minnesota Court of Appeals has noted that, while a court may rely on an appraiser's recommendation, it may not actually delegate its authority to determine fair value.⁶⁸

b. Determination of Fair Value

"Fair value" is not the same as, or short-hand for, "fair market value."⁶⁹ "Fair value" carries with it the statutory purpose that shareholders be fairly compensated, which may or may not equate with the market's judgment about the stock's value.⁷⁰ This is particularly appropriate in the close corporation setting where there is no ready market for the shares and consequently no fair market value.

In addition, most courts, including Minnesota's, have noted that determination of fair value requires valuation of the corporation as a whole, which is then multiplied by the dissenter's percentage of ownership, not valuation of individual shares.⁷¹ The Delaware Supreme Court, home to many high-stakes appraisal proceedings, provided a classic statement of "fair value":

The basic concept of value under the appraisal statute is that the stockholder is entitled to be paid for that which has been taken from him . . . his proportionate interest in a going concern. By value of the stockholder's proportionate interest in the corporate enterprise is meant the true or intrinsic value of his stock which has been taken by the merger. In determining what figure represents this true or intrinsic value, the appraiser and the courts must take into consideration all factors and elements which reasonably might enter into the fixing of value. Thus, market value, asset value, dividends, earning prospects, the nature of the enterprise and any other facts which were known or which could be ascertained as of the date of merger and which throw any light on future prospects of the merged corporation are not only pertinent to an inquiry as to the value of the dissenting stockholders' interest, but must be considered by the agency fixing the value.⁷²

Put another way, the statute requires valuation of the corporation as a "going concern basis."⁷³ Further, one court has noted that determination of fair value is "more akin to an artistic composition than to a scientific process."⁷⁴

A court also has discretion to award reasonable expenses, including attorney's fees and disbursements, to any of the parties if the court finds that a party has acted "arbitrarily, vexatiously, or otherwise not in good faith."⁷⁵ This provision offers additional protection for the minority shareholder who has been wronged by an abusive majority.

c. Valuation Methods

If the court does not appoint an appraiser, determination of fair value develops into a battle of the experts. The analytical methods used by experts vary, but are generally based on common principles of business valuation.

Many courts once relied on a valuation formula known as the "Delaware Block" rule. Based only on three factors, the Delaware block method made it difficult for courts to take additional factors into account, such as the difference between a growth-oriented company and an income-based company.⁷⁶ Thus, courts in Delaware and elsewhere now tend to use a more flexible approach called the "all relevant factors" method.⁷⁷

The “all relevant factors” method considers all relevant factors when non-speculative elements of value are proven.⁷⁸ This new method is consistent with the Delaware statute which was amended in 1981 to read the appraisers should “take into account all relevant factors.”⁷⁹ The only limitation on relevant factors is found in the statute itself. The statute requires that value be determined exclusive of any element of value that arose from the merger.⁸⁰ However, the “all relevant factors” method allows courts to use any method of analysis that is accepted in the financial community.⁸¹ Thus, the “all relevant factors” method provides a more flexible approach to valuation.

d. Valuation Discounts

Courts have struggled over the propriety of applying various valuation discounts in both buy-out motions and in dissenters’ rights cases. Some courts have permitted discounts for lack of control, lack of marketability, and stock transfer restrictions. Other courts have concluded that, although perhaps appropriate in other valuation settings, discounts are not relevant in determining “fair value.”

i. Discount for Lack of Control

For most valuation purposes, minority shares may be discounted to reflect the decreased value attributed to the shares’ lack of control over corporate decision-making.⁸² A minority discount can be substantial and often ranges from fifteen to thirty-five percent of value.⁸³

The Minnesota Court of Appeals has held that a minority discount is improper under the dissenters’ rights statute.⁸⁴ After surveying a split in decisions from other jurisdictions, the court concluded that the legislature’s “evident aim” of protecting dissenting shareholders precluded use of discounts for lack of control.⁸⁵ The Minnesota Court of Appeals has also rejected application of a discount for lack of control of shares in a section 302A.751 buy-out.⁸⁶

Courts in other jurisdictions have taken conflicting views on the issue of permitting a minority discount. The majority of jurisdictions, along with Minnesota,⁸⁷ have rejected the application of a discount to the dissenting shareholder’s shares based upon the shares lack of control.⁸⁸ Several courts have held, however, that a dissenting shareholder’s shares can be discounted to reflect the lack of control in the corporation.⁸⁹ Though not addressed by the court in *MT Properties*, one can argue that the cases rejecting a discount for lack of control are better reasoned because they consider the statute’s purpose, while most courts approving use of the discount have done so without analyzing the policy underlying the statute.

ii. Marketability Discounts

A discount for lack of marketability, (or illiquidity) reflects the fact that investors will pay less for an interest that cannot be freely traded, as it would be if listed on an organized exchange.⁹⁰ Jurisdictions also are split on the applicability of a discount for lack of marketability. Several courts have denied application of marketability discounts.⁹¹ Several jurisdictions, however, have permitted marketability discounts.⁹²

iii. Key Person Discount

A key person discount is applied in some business valuations to reflect the reliance of the business' success upon one individual.⁹³ At least one Minnesota court has considered the applicability of a key person discount, but did not decide the issue because it held that the shareholder was not a key person and that there were other competent people who could operate the business.⁹⁴ However, a key person discount has been upheld in Delaware.⁹⁵

iv. Discounts for Contingent Liabilities

The Minnesota Court of Appeals in *MT Properties* also considered the question of permitting reductions in value for possible corporate liabilities not shown on the corporation's financial statements.⁹⁶ In that case, the trial court had approved the corporation's three million dollar reduction in value for "contingent liabilities" based on concerns over possible labor and environmental litigation.⁹⁷ The court of appeals held that actual loss from the contingencies was "reasonably probable" and such contingencies might have been considered in a hypothetical "willing seller-willing buyer" scenario.⁹⁸ Thus, the discount was allowed.⁹⁹

C. Equitable Remedies under Section 302A.467

In addition to the other relief provided by the MBCA, equitable relief may be granted by a court in an action brought by a shareholder if the court finds that a violation of the MBCA has occurred.¹⁰⁰ This section recognizes that situations in which equitable relief may be appropriate are not easily defined in advance, as they often present novel fact situations.¹⁰¹ As a result, this section adopts a broad rule which gives the court complete discretion in ordering whatever relief it deems just and reasonable under the circumstances.¹⁰²

Minnesota courts have placed some limitations on the equitable remedies which might be awarded under section 302A.467. For instance, the Minnesota Court of Appeals held that section 302A.467 does not authorize a court to force a buy-out of dissenting shareholders when such a buy-out could not be obtained under dissenters' provision contained in section 302A.471.¹⁰³ In addition, relief under section 302A.467 is probably limited to shareholders who held their stock when the alleged wrongs that formed the basis of the suit occurred.¹⁰⁴

D. Shareholder Derivative Suits

Although any shareholder may bring a derivative suit against a corporation, understandably, they are more often brought by minority shareholders. Procedural requirements for bringing a derivative suit are governed by Rule 23.06 of the Minnesota Rules of Civil Procedure and by Federal Rule 23.1. The state and federal rules provide similar procedural hurdles. Although the Rules of Civil Procedure contain many requirements for a derivative suit, the United States Supreme Court has held that the rules are not controlling for dismissal of a suit because they are procedural rather than substantive.¹⁰⁵

1. *Requirements for Bringing Derivative Suits*

a. *Contemporaneous Ownership Requirement*

The derivative complaint must “allege that the plaintiff was a shareholder or member at the time of the transaction of which the plaintiff complains or that the plaintiff’s share or membership thereafter devolved on the plaintiff by operation of law.”¹⁰⁶ Courts have inferred from the language of the rules that the plaintiff must also maintain ownership of the stock for the duration of the suit.¹⁰⁷ Each of these requirements originates “from the equitable nature of a derivative suit which allows a shareholder ‘to step into the corporation’s shoes and to seek in its right the restitution he could not demand in his own.’¹⁰⁸

b. *Demand Requirement*

Shareholders bringing a derivative suit must make demand upon the board of directors before commencing suit.¹⁰⁹ The demand requirement gives the corporation, through its board, the opportunity to assume the action itself to remedy harm to the corporation.¹¹⁰ Minnesota Rule of Civil Procedure 23.06 requires that the derivative suit complaint allege with particularity the efforts that were made to obtain the desired action from the board or from fellow shareholders, and the reasons for the plaintiff’s failure to obtain action or for not making the efforts.¹¹¹

As indicated by the language of Rule 23.06, many states, including Minnesota, recognize an exception which may excuse the demand requirement if asking the corporation to take up the suit would be unduly expensive or “futile.”¹¹² The futility exception, as an example, may arise when the directors upon whom demand would be made have a conflict of interest regarding the suit.¹¹³ Most states require a plaintiff to plead with specificity the reasons a demand would be futile.¹¹⁴ The pleadings must “create a reasonable doubt that the directors are disinterested and independent.”¹¹⁵

The United States Supreme Court has held that availability of the futility exception for claims based on federal law must be governed by the relevant state law.¹¹⁶ In so ruling, the Court rejected the Seventh Circuit’s determination that demand is never excused for futility when the derivative suit is based on federal law.¹¹⁷ The Court thereby required federal courts to recognize the futility exception, which is provided by most states.

c. *Representation of Shareholders’ Interest Requirement*

Rule 23.06 requires a plaintiff to establish that he or she adequately represents the interest of all shareholders.¹¹⁸ Because the plaintiff is essentially enforcing the right of the corporation, the plaintiff must represent the other shareholders’ interests, in addition to his or her own, when bringing a derivative action.¹¹⁹

d. “Security for Expenses” (Bond) Requirement

Minnesota, unlike some states, does not require plaintiffs in derivative suits to provide “security for expenses,” which is typically satisfied by a bond.¹²⁰ Nineteen states (not including Delaware) have statutes permitting defendants in derivative actions to demand that the plaintiff post security for expenses, including attorneys’ fees that the corporation may incur.¹²¹ Typically with these statutes, the court determines the amount of security.¹²² In addition, most of the statutes requiring security apply only when the plaintiff is a small shareholder, typically with less than five percent ownership of a class of stock or less than twenty-five thousand dollars in market value.¹²³

Minnesota, unlike forty-one states, also does not have a general statute permitting defendants to demand that plaintiffs furnish a bond for “costs.”¹²⁴ Most federal district courts have a similar local rule, although many apply only to nonresident plaintiffs, but again, Minnesota is not among them.¹²⁵

2. *The Use of Special Litigation Committees in Derivative Actions*

When the MBCA was enacted in 1981, there was a separate section dealing with the board of director’s authority to appoint committees.¹²⁶ Section 302A.243 provided that the board could establish a committee of two or more “disinterested” directors or other persons to determine whether pursuing a legal right or remedy was in the best interest of the corporation.¹²⁷ The statute defined “disinterested” and further stated that the good faith determinations of the committee were binding upon the corporation.¹²⁸

Thus, when a derivative action was brought against a corporation, the board of directors could appoint a special litigation committee to review the allegations of the complaint. The committee had the power to hire accounting firms or other professionals to assist in the investigation of the claims. At the conclusion of its investigation, the committee would make a recommendation to the board of directors regarding whether the corporation should proceed with the claims. If the committee recommended that the corporation not pursue the lawsuit, the board of directors generally would follow the committee’s recommendation and not take any action. The shareholders who brought the possible claims to the attention of the corporation had no other recourse unless they qualified to bring their claims under Minnesota Statutes section 302A.467 or 302A.751.¹²⁹

In *Black v. NuAire, Inc.*, the Minnesota Court of Appeals interpreted the committee statute as limiting the court’s review of a committee’s decision to dismiss a shareholder’s derivative action to whether the recommendation was made by a disinterested committee conducting its investigation in good faith.¹³⁰ With its limited scope of judicial review for committee decisions, *Black* struck a blow to derivative actions. Unless shareholders could establish that the committee was not independent or did not make its recommendation in good faith, they could not bring their derivative action after the corporation had decided not to pursue it based upon a committee recommendation.¹³¹

In 1989, the year following the court of appeals’ decision in *Black*, the Minnesota Legislature repealed section 302A.243 and amended section 302A.241 to take its place. The legislature repealed section 302A.243 with the statement that the repeal “does not imply that the legislature has accepted or rejected the substance of the repealed section but must be interpreted in the same manner as if section 302A.243 had not be (sic) enacted.”¹³²

Since 1989, the corporation's authority to appoint a special litigation committee is governed by Minnesota Statutes section 302A.241, subdivision 1, which provides that corporations may appoint special litigation committees consisting of one or more independent directors or other independent persons to consider the legal rights or remedies of the corporation and whether those rights and remedies should be pursued.¹³³ It is unclear what the legislature intended by these small changes between the repealed section and the amended section. Until recently, there had been no court decisions dealing with the new amended section regarding committees.

In 1995, the Minnesota Court of Appeals reinstated the *Black* standard of judicial review for committee decisions.¹³⁴ In *Skoglund*, the court determined that under section 302.A241, judicial review of a special litigation committee recommendation was limited to whether the committee was independent and conducted the investigation in good faith.¹³⁵ The court relied on *Black*, as if section 302A.243 had never been repealed.¹³⁶

IV. DUTIES OF OFFICERS, DIRECTORS AND SHAREHOLDERS IN A CLOSE CORPORATION

A. General Duties and Obligations

Despite the important differences between larger corporations and close corporations, the MBCA does not distinguish between the two for most purposes. As a result, close corporations and their officers and directors are bound by the same duties and obligations as larger, publicly-held corporations.¹³⁷ These generally include the duties to act in good faith and in the best interests of the corporation.¹³⁸

The MBCA provides that a directors' liability to the corporation or its shareholders for monetary damages can be limited or eliminated in the corporation's articles of incorporation.¹³⁹ There is no corresponding provision for officers.

A director's liability cannot be limited or eliminated, however, for breach of the duty of loyalty to the corporation or its shareholders, for acts or omissions not in good faith, for intentional misconduct, for knowing violation of law, for conduct which generates an improper personal benefit, for violation of the securities laws, or for illegal distributions.¹⁴⁰ Further, a director's liability cannot be eliminated or limited retroactively.¹⁴¹

B. Fiduciary Duty Owed to Other Shareholders

Minnesota law, however, treats close corporations differently for the fiduciary duty owed by shareholders. The Minnesota Supreme Court has recognized that relations within a closely held corporation are similar to that of a partnership.¹⁴² In 1983, the MBCA was amended to specifically include the duty which shareholders of closely held corporations owe to each other.¹⁴³ The amendment provides that "each shareholder of a closely-held corporation has a duty to each other shareholder to act in a fair, reasonable and honest manner. . . ."¹⁴⁴

The concept that shareholders in close corporations owe fiduciary duties to each other has been applied by numerous courts.¹⁴⁵ For instance, the Minnesota Court of Appeals has noted that Minnesota law “imposes on each [shareholder] the highest standard of integrity in their dealings with each other.”¹⁴⁶ Similarly, in *Pedro v. Pedro*, the court of appeals reiterated that shareholders in a closely held corporation owe one another a fiduciary duty, including the duty to deal “openly, honestly and fairly with other shareholders.”¹⁴⁷

The Minnesota Court of Appeals also recently held that equitable owners¹⁴⁸ of stock are owed a fiduciary duty by the officers and directors of a closely held corporation.¹⁴⁹ Thus, the important concept of fiduciary duty for shareholders of closely held corporations continues to be developed through judicial interpretation.

V. NEW LIMITATION ON MINORITY SHAREHOLDERS' RIGHTS?

In a decision that appears to be at odds with the intent of the MBCA, the Minnesota Court of Appeals recently held that a shareholder must suffer an injury that is separate and distinct from any injury to the corporation to bring a claim under section 302A.751.¹⁵⁰ In *Skoglund v. Brady*, Donald Skoglund, a shareholder of a closely held corporation, objected to certain leases authorized by the corporation's board, promissory notes and bonuses issued to board members, the issuance of additional shares of the corporation's stock and the sale of some of the newly issued stock to board members at a price lower than the stock's book value.¹⁵¹ Mr. Skoglund brought both derivative and direct claims under Minnesota Statutes section 302A.751 against the corporations and the members of the board alleging that the directors breached fiduciary duties, usurped corporate opportunities and committed corporate waste and fraud.¹⁵²

The district court dismissed Mr. Skoglund's direct claims under section 302A.751 because it determined that a shareholder must have a separate and distinct injury to bring an action under section 302A.751.¹⁵³ The court determined that Mr. Skoglund's claims were derivative claims of the corporation.¹⁵⁴ The court of appeals affirmed, citing cases which state the general principle that an individual shareholder cannot assert a cause of action that belongs to the corporation.¹⁵⁵ While this general principle—involving the direct/derivative claims distinction—applies to causes of action involving corporations that are not closely held, it is questionable whether it applies to claims for equitable relief brought under section 302A.751 involving closely held corporations.¹⁵⁶

Skoglund is significant because it may restrict the availability of section 302A.751. Under *Skoglund*, if fraud or other actions by the board harmed all shareholders equally, the claim would be derivative and the section 302A.751 buy-out motion may be unavailable to minority shareholders.

The *Skoglund* court's interpretation appears at odds with the language and intent of section 302A.751. There is no language in the statute which indicates that a shareholder must have a distinct and separate injury to bring a claim under section 302A.751. To the contrary, section 302A.751 expressly provides a claim for shareholders when the corporation's assets are being misapplied or wasted.¹⁵⁷ Claims for corporate waste almost always affect all shareholders equally, and historically were brought as derivative actions.¹⁵⁸ The enactment of section 302A.751 provided for direct claims in these cases.

Skoglund is arguably the law of Minnesota.¹⁵⁹ Perhaps future judicial interpretation or legislative amendment may realign the decision with the intent of the MBCA, the statutory language and past Minnesota decisions.

VI. CONCLUSION

In the fifteen years since its enactment, the MBCA has provided minority shareholders of Minnesota closely held corporations with valuable protections. The MBCA's amendments and judicial interpretations have further extended the rights and remedies available to these shareholders. Section 302A.751, the buy-out provision, has been one of the most refreshing and distinguishing features of the MBCA in addition to one of the most powerful provisions for protecting minority shareholders' rights by penalizing corporate malfeasance by an abusive majority.

The Minnesota Court of Appeals in *Skoglund*, however, has recently limited the strength of the buy-out provision. It remains to be seen whether *Skoglund* is the start of a trend in decisions which will restrict minority shareholders' rights or whether it is an anomaly which will be rectified by future judicial interpretation or legislative amendment.

¹ The Minnesota Business Corporations Act (MCBA) defines a closely held corporation as "a corporation which does not have more than 35 shareholders." MINN. STAT. § 302A.011, subd. 6a (1994).

² See 1 F. HODGE O'NEAL & ROBERT B. THOMPSON, O'NEAL'S OPPRESSION OF MINORITY SHAREHOLDERS § 3:02 (2d ed. 1995) (illustrating various techniques for accomplishing a "squeeze out").

³ *Id.*

⁴ See 1 F. HODGE O'NEAL & ROBERT B. THOMPSON, O'NEAL'S CLOSE CORPORATIONS § 4:03 (3d ed. 1994) (noting that unlike shareholders in public corporations, shareholders in close corporations cannot easily dispose of their corporate holdings).

⁵ Compare 1981 Minn. Laws ch. 270 (original Act) with MINN. STAT. §§ 302A.001-.917 (1994 & Supp. 1995) (current Act).

⁶ See *infra* Part III.

⁷ See *Skoglund v. Brady*, 541 N.W. 2d 17 (Minn. Ct. App. 1995), *review denied* (Minn. 1996) (holding that plaintiff could not pursue an action under Minnesota Statutes § 302A.751, subdivision 1, because he did not allege an injury to himself that was separate and distinct from any injury to the corporation).

⁸ See, e.g., *Pooley v. Mankato Iron & Metal, Inc.*, 513 N.W.2d 834 (Minn. Ct. App. 1994) (involving buy-out remedy provided by Minnesota Statutes § 302A.751).

⁹ A buy-out or dissolution under Minnesota Statutes § 302A.751, subdivision 1, is appropriate under any of the following circumstances:

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1. The directors are deadlocked in the management of the corporate affairs and shareholders are unable to break the deadlock;
 2. The directors have acted fraudulently or illegally toward one or more shareholders in their capacities as shareholders, directors, or, in the case of a closely held corporation, in their capacities as officers or employees;
 3. The directors have acted in a manner unfairly prejudicial toward one or more of the shareholders in their capacities as shareholders or directors of a corporation that is not a publicly held corporation, or as officers or employees of a closely held corporation;
 4. The shareholders are so divided in voting power that they have failed to elect directors for two consecutive regular meetings;
 5. Corporate assets are being misapplied or wasted; or
 6. The period of duration provided in the articles has expired and has not been extended.

MINN. STAT. § 302A.751, subd. 1(b) (1994)

¹⁰ MINN. STAT. § 302A.751, subd. 2.

¹¹ MINN. STAT. § 302A.751, subd. 1(b) (2) (1982).

¹² MINN. STAT. § 302A.751, subd. 1(b) (2) (1984).

¹³ See Joseph E. Olson, *A Statutory Elixir for the Oppression Malady*, 36 MERCER L. REV. 627, 638 (1985) (explaining that the deletion of the term “persistently unfair” and the substitution of the term “unfairly prejudicial” was designed to guarantee that the new statute would be interpreted in a more liberal manner).

¹⁴ MINN. STAT. ANN. § 302A.751 (1994) (Reporter’s Notes 1982-84, subd. 1); see also *Sawyer v. Curt & Co.*, Nos. C7-90-2040, C9-90-2041, 1991 WL 65320, at *1 (Minn. Ct. App. Feb. 12, 1991).

¹⁵ See MINN. STAT. § 302A.751, subd. 2a (1982).

¹⁶ 489 N.W.2d 798, 803 (Minn. Ct. App. 1992).

¹⁷ *Id.* at 802 (quoting Olson, *supra* note 13 at 629).

¹⁸ *Id.*; see also *Sawyer* 1991 WL 65320, at *2. In *Sawyer*, the Minnesota Court of Appeals affirmed a buy-out of the shares of a corporation’s president and chief executive officer who had been removed from her position by the board of directors. The court determined that the shareholder’s reasonable expectations of a position in the corporation were frustrated and that she was therefore entitled to a buy-out of her shares. *Sawyer*, 1991 WL 65320, at *2.

¹⁹ See *Pedro*, 489 N.W.2d at 802.

²⁰ MINN. STAT. § 302A.751, subd. 3a (1994) (emphasis added).

²¹ The added sentence reads: (“[f]or purposes of this section, any written agreements, including employment agreements and buy-sell agreements, between or among shareholders or between or among one or more shareholders and the corporation are presumed to reflect the parties’ reasonable expectations concerning matters dealt with in the agreements.” *Id.* § 302A.751, subd. 3a (1994).

²² See, e.g., *Pedro v. Pedro*, 463 N.W.2d 285, 288-89 (Minn. Ct. App. 1990), *reconfirmed* 489 N.W.2d 798, 802 (Minn. Ct. App. 1992).

²³ Minn. Stat. § 302A.751, subd. 3a.

²⁴ *Pooley v. Mankato Iron & Metal, Inc.*, 513 N.W.2d 834 (Minn. Ct. App. 1994).

²⁵ *Id.* at 836

²⁶ *Id.*

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.*

³⁰ *Id.*

³¹ *Id.*

³² *Id.* at 838.

³³ *Id.*

³⁴ *Id.*

³⁵ It appears, however, that the court of appeals may be shifting from the strong protection previously provided to minority shareholders. See *infra* section V.

³⁶ See *Muellenberg v. Bikon Corp.*, 669 A.2d 1382 (N.J. 1996).

³⁷ *Id.* at 1388-89.

³⁸ *Id.* at 1383-84.

³⁹ *Id.* at 1384.

⁴⁰ *Id.*

⁴¹ *Id.* at 1388.

⁴² *Id.* at 1388-89

⁴³ *Id.* at 1389

⁴⁴ See § 302A.751, subd. 2.

⁴⁵ *Id.*

⁴⁶ See *infra* section III.B.4.

⁴⁷ See § 302A.751, subd. 1(b)(3).

⁴⁸ See § 302A.471, subd. 1.

⁴⁹ Specifically, the dissenters' rights statute enumerates the following fundamental corporate changes as triggering events entitling a shareholder to relief under the statute:

- a. An amendment of the articles that materially and adversely affects the rights of the dissenting shareholder;

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- b. A disposition of substantially all of the corporation's assets not made in the usual or regular course of its business;
 - c. A plan of merger to which the corporation is a party;
 - d. A plan of exchange under which the shares of the corporation will be acquired by another corporation; and
 - e. Any other corporate action taken pursuant to a shareholder vote under which the articles, bylaws, or a resolution provides that dissenting shareholders may obtain payment for shares.

Id.

⁵⁰ *Whetstone v. Hossfeld Mfg. Co.*, 457 N.W.2d 380, 381-82 (Minn. 1990). Specifically, the *Whetstone* court concluded that these actions fell within part (4) of § 302A.471, subdivision 1(a) which “[e]xcludes or limits the right of a shareholder to vote on a matter or to cumulate votes.” *Id.* at 382.

⁵¹ *Bowman v. MWCG Export Co.*, No. C4-90-1654, 1991 WL 30342, at *2 (Minn. Ct. App. Mar. 12, 1991).

⁵² *Goins v. Lang*, No. C8-93-1381, 1994 WL 43859, at *2 (Minn. Ct. App. Feb. 15, 1994). In *Goins*, the corporation had informed its shareholders of a proposed merger. *Id.* at *1. The merger ultimately did not occur because one of the corporation's lenders, whose consent was required to consummate the merger, rejected the merger. The dissenting shareholder had alleged that his dissenters' rights had been triggered when the corporation gave him untimely notice of the shareholder merger vote. The court held that because the merger did not take place, the shareholder was not entitled to dissenters' rights. *Id.*

⁵³ *Sifferle v. Micom Corp.*, 384 N.W.2d 503, 506-07 (Minn. Ct. App. 1986); *see also* *Broin v. National Computer Sys., Inc.*, No. C9-91-235, 1991 WL 204460, at *1-2 (Minn. Ct. App. Oct. 15, 1991). Although the *Sifferle* court defined “fraudulent” broadly, it rejected an even broader reading when it refused to permit shareholders to challenge the “entire fairness” of the transaction. *Sifferle*, 384 N.W.2d at 507. The entire fairness doctrine, as developed in Delaware and elsewhere, allows a shareholder to challenge a merger that violates the obligation of fair dealing among fellow shareholders. *See* *Rabkin v. Philip A. Hunt Chem. Corp.*, 498 A.2d 1099, 1104-05 (Del. 1985); *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711-14 (Del. 1983).

⁵⁴ *See* § 302A.473, subd. 2.

⁵⁵ § 302A.473, subd. 3.

⁵⁶ § 302A.473, subd. 4(a).

⁵⁷ § 302A.473, subd. 4(a) (3) (4).

⁵⁸ § 302A.473, subd. 4(b).

⁵⁹ *See* § 302A.473 subd. 4(a).

⁶⁰ If the court orders a buy-out of the shares under section 302A.751, the purchase price of the shares will be the fair value as of the date of the commencement of the action or as of another date found equitable by the court. § 302A.751, subd. 2. In a

dissenters' rights action, the valuation date is "immediately before the effective date of the corporate action" from which the shareholder dissents. § 302A.473, subd. 1(c).

⁶¹ See § 302A.473, subd. 5-8.

⁶² See § 302A.751, subd. 2. The dissenters' rights provision, which specifies the information that must be given to the shareholder, is found in Minnesota Statutes § 302A.473 subd. 5(a).

⁶³ See § 302A.473, subd. 7.

⁶⁴ See § 302A.751, subd. 2. Interest or costs are allowed under Minnesota Statutes § 302A.473, subs. 1, 8.

⁶⁵ § 302A.473, subd. 7; see also *National Computer Sys., Inc. v. Bordonaro*, No. C9-89-1370, 1990 WL 13383 (Minn. Ct. App. 1990) (asserting that it is within the court's discretion to determine fair value by the use of: market value, book value, replacement value, or capitalization of earnings).

⁶⁶ Section 302A.473, subd. 7.

⁶⁷ *Id.*

⁶⁸ *Zenanko v. Vukelich*, No. C2-90-1264, 1991 WL 6379, at *2 (Minn. Ct. App. Jan. 29, 1991); *Schaub v. Kortgard*, 372 N.W.2d 427, 430 (Minn. Ct. App. 1985) (using fair value determination of § 302A.473, subdivision 7 to establish price for mandatory buy-out under § 302A.751, subd. 2). In *Zenanko*, the court of appeals affirmed an appraisal, following a mandatory buy-out motion, that valued a co-owner's interest in the corporation at zero dollars based on the independent appraiser's determination that liabilities exceeded assets. *Zenanko* 1991 WL 6379, at *2.

⁶⁹ See, e.g., *Viacom Int'l Inc. v. Icahn*, 946 F.2d 998, 1000-01 (2d Cir. 1991); *Tri-Continental Corp. v. Battye*, 74 A.2d 71, 72 (Del. 1950); see also *supra* notes 44-46 and accompanying text.

⁷⁰ See § 302A.473, subd. 1(c) (defining "fair value of the shares" as "the value of the shares of a corporation immediately before the effective date of a corporate action referred to in § 302A.471, subdivision 1, [provision triggering dissenters' rights]"); see also 2 O'NEIL & THOMPSON, *supra* note 2, § 7:21 (discussing various approaches for determining fair value of shares in legislative or judicial buyout provisions).

⁷¹ See *MT Properties, Inc. v. CMC Real Estate Corp.*, 481 N.W.2d 383, 387 n.3 (Minn. Ct. App. 1992 (citing *Cavalier Oil Coop. v. Harnett*, 564 A.2d 1137, 1144 (Del. 1989))); see also *Spinnaker Software Corp. v. Nicholson*, 495 N.W.2d 441, 444 (Minn. Ct. App. 1993).

⁷² *Tri-Continental Corp.*, 74 A.2d at 72.

⁷³ *Id.*; *Universal City Studios, Inc. v. Francis I. duPont & Co.*, 334 A.2d 216, 218 (Del. 1975).

⁷⁴ *In re Valuation of Common Stock of Libby, McNeill & Libby*, 406 A.2d 54, 60 (Me. 1979).

⁷⁵ § 302A.751, subd. 4; § 302A.473, subd. 8.

⁷⁶ The Delaware block method relies on three different elements of value: market value, asset value, and earnings value. *See In re General Realty & Util. Corp.*, 52 A.2d 6, 14-15 (Del. Ch. 1947). *See generally* E. Veasey & J. Finkelstein, *Appraisal Rights and Fairness of Price in Mergers and Consolidations* (BNA Corp. Prac. Series No. 38 1987) (discussing Delaware's appraisal statute and the factors used for share valuation). These factors are each assigned a weight and the resulting amounts added to determine the value per share. *Id.*

⁷⁷ In *Weinberger v. UOP, Inc.* 457 A.2d 701 (Del. 1983), the Delaware Supreme Court replaced the Delaware block method of valuation with the "all relevant factors" approach used elsewhere. *Id.* at 712-14; *see, e.g.*, *Hunter v. Mitek Indus., Inc.*, 721 F. Supp. 1102, 1106 (E.D. Mo. 1989); *TV58 Ltd. Partnership v. Weigel Broadcasting Co.*, 1993 WL 285850, at *1 (Del. Ch. July 22, 1993).

⁷⁸ *See Weinberger* 457 A.2d at 712B13; DEL. STAT. § 262 (h) (1990).

⁷⁹ DEL. STAT. § 262(h) (1990).

⁸⁰ *Id.* Thus, "[o]nly the speculative elements of value that may arise from the 'accomplishment or expectation' of the merger are excluded." *Weinberger*, 457 A.2d at 713.

The Minnesota Court of Appeals has also rejected the corporation's argument that the purchase price of the merged corporation must be presumed to establish "fair value." *Spinnaker Software Corp. v. Nicholson*, 495 N.W.2d 441, 445 (Minn. Ct. App. 1993). In *Spinnaker*, the trial court's determination of fair value, which exceeded the dissenting shareholder's estimate of fair value, was upheld. *Id.* The corporation had paid the shareholder \$0.90 per common share and \$1.575 per preferred share. The shareholder demanded \$1.75 and \$3.00, respectively. The trial court concluded fair value was \$2.16 and \$3.00. *Id.* at 443.

⁸¹ *Spinnaker*, 495 N.W.2d at 445; *Weinberger*, 457 A.2d at 713.

⁸² *See* 2 O'NEIL & THOMPSON, *supra* note 2, § 7:21 (recognizing that one of the most important valuation issues in a buy-out is whether the value of stock once determined should be discounted because the stock is a minority interest).

⁸³ *See* *MT Properties, Inc. v. CMC Real Estate Corp.*, 481 N.W.2d 383 (Minn. Ct. App. 1992) (approving a 22% discount to the value of stocks to reflect, in part, the minority status of the shares). The Minnesota Court of Appeals, however, disallowed the discount. *Id.* at 386.

⁸⁴ *See id.* at 388. After trial, the district court in *MT Properties* approved the initial "fair value" payment made by the corporation, including a 22% discount value to reflect the minority status of the dissenters' shares, lack of marketability, and possible environmental contamination of corporate property. On appeal, the court of appeals first concluded that, despite the other rationales for the discount contained in the trial court's findings, "the discount . . . was attributable solely [to reflect the shareholder's] minority status." *Id.* at 386. The Minnesota Court of Appeals, however, disallowed the discount. *Id.*

⁸⁵ *Id.* at 388.

⁸⁶ *Pooley v. Mankato Iron & Metal, Inc.*, 513 N.W.2d 834 (Minn. Ct. App. 1994).

⁸⁷ In *MT Properties*, the Minnesota Court of Appeals specifically noted that its holding was in line with a majority of jurisdictions addressing the issue. *MT Properties, Inc.*, 481 N.W.2d at 387-88 nn.2, 4.

⁸⁸ The Eighth Circuit Court of Appeals, applying *MT Properties*, has rejected the use of a minority discount. *See Foy v. Klapmeier*, 992 F.2d 774 (8th Cir. 1993); *see also Hunter v. Mitek Indus.*, 721 F. Supp. 1102, 1106-07 (E.D. Mo. 1989) (opining that under Missouri's dissenting shareholder rights statute, minority and marketability discounts were not applied to calculate the fair market value of the dissenting shareholder's stock); *Rigel Corp. v. Cutchall*, 511 N.W.2d 519, 525 (Neb. 1994) (rejecting both minority and marketability discounts); *Charland v. Country View Golf Club, Inc.*, 588 A.2d 609, 611-12 (R.I. 1991) (stating what when a corporation buys out the shares of dissenting shareholders, the fact that the share are noncontrolling is "irrelevant"); *Cavalier Oil Corp. v. Harnett*, 564 A.2d 1137, 1144 (Del. 1989) (rejecting both minority and marketability discounts); *In re McLoon Oil Co.*, 565 A.2d 997, 1004 (Me. 1989) (explaining that when valuing a shareholder's stock, the court will prorate the value for the whole corporation equally); *Richardson v. Palmer Broadcasting Co.*, 353 N.W.2d 374, 379 (Iowa 1984) (finding that any effort to adjust the value of minority shares downward is "contrary to the spirit of a 'fair value' determination."); *Columbia Management Co. v. Wyss*, 765 P.2d 207, 214 (Or. 1988) (en banc) (stating that the application of minority discount penalizes all shareholders); *Walter S. Cheesman Realty Co. v. Moore*, 770 P.2d 1308, 1312 (Colo. Ct. App. 1988) (citing cases both for and against discounting the shares of minority shareholders); *Johnston v. Hickory Creek Nursery, Inc.*, 521 N.E.2d 236, 239-40 (Ill. App. Ct. 1988) (finding that the discount did not apply when the remaining shareholders bought the minority shares resulting in a substantial increase).

⁸⁹ *See Hernando Bank v. Huff*, 609 F. Supp. 1124 (N.D. Miss. 1985), *aff'd*, 796 F.2d 803 (5th Cir. 1986); *Perlman v. Permonite Mfg. Co.*, 568 F. Supp. 222 (N.D. Ind. 1983), *aff'd*, 734 F.2d 1283 (7th Cir. 1984); *Armstrong v. Marathon Oil Co.*, 513 N.E.2d 776 (Ohio 1987); *Foglesong v. Thurston Nat'l Life Ins. Co.*, 555 P.2d 606 (Okla. 1976); *Atlantic States Constr., Inc v. Beavers*, 314 S.E.2d 245 (Ga. Ct. App. 1984); *Moore v. New Ammest, Inc.*, 630 P.2d 167 (Kan. Ct. App. 1981).

⁹⁰ *See 2 O'NEIL & THOMPSON supra* note 2, § 7:21 (recognizing the fact that there is no market for stock in a close corporation is an important consideration in valuation and the decision to discount).

⁹¹ *See Foy v. Klapmeier*, Civ. No. 3-90-292, 1993 WL 246127, at *8 (D. Minn. Feb. 8, 1993). The court held the marketability discount was not appropriate as a result of the statutory obligation of the corporation to purchase the dissenting shareholder's shares the dissenters' right statute. *Id.* at *7-8. The Eighth Circuit did not address the issue on appeal. *Foy v. Klapmeier*, 992 F.2d 774 (8th Cir. 1993); *In re McLoon Oil Co.*, 565 A.2d 997 (Me. 1989); *Charland v. Country View Golf Club, Inc.*, 588 A.2d 609 (R.I. 1991).

⁹² *See Stanton v. Republic Bank*, 581 N.E.2d 678, 681-82 (Ill. 1991); *Ford v. Courier-Journal Job Printing Co.*, 639 S.W.2d 553, 556 (Ky. CT. App. 1982); *King v. F.T.J., Inc.*, 765 S.W.2d 301, 305-06 Mmo. Ct. App. 1988).

⁹³ A key person typically “performs highly personal or unique services from which the entire business income is derived.” *Nemitz v. Nemitz*, 376 N.W.2d 243, 247 (Minn. Ct. App. 1985).

⁹⁴ *Roalstad v. Roalstad*, No. C4-91-2099, 1992 WL 115379, at *1 (Minn. Ct. App. June 2, 1992).

⁹⁵ *See Hodas v. Spectrum Technology, Inc.*, Civ. A. No. 11,265, 1992 WL 364682, at *4 (Del. Ch. Dec. 7, 1992).

⁹⁶ *See MT Properties v. CMC Real Estate Corp.*, 481 N.W.2d 383, 389-90 (Minn. Ct. App. 1992).

⁹⁷ *Id.*

⁹⁸ *Id.*

⁹⁹ *Id.*

¹⁰⁰ Minnesota Statutes § 302A.467 provides:

If a corporation of an officer or director of the corporation violates a provision of this chapter, a court in this state may, in an action brought by a shareholder of the corporation, grant any equitable relief it deems just and reasonable in the circumstances and award expenses, including attorneys’ fees and disbursements, to the shareholder.

Minn. Stat. § 302A.467 (1994).

¹⁰¹ *See* MINN. STAT. ANN. § 302A.467, (West 1994) (Reporter’s Notes - 1981).

¹⁰² *Id.* (Reporter’s Notes - 1981, General Comment).

¹⁰³ *Westgor v. Grimm*, 381 N.W.2d 877, 881 (Minn. Ct. App. 1986).

¹⁰⁴ *See PJ Acquisition Corp. v. Skoglund*, 453 N.W.2d 1, 6 (Minn. 1990) (analyzing § 302A.751).

¹⁰⁵ *See Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 96-97 (1991), *rev’g*, 908 F.2d 1338 (7th Cir. 1990); *see also RCM Sec. Fund, Inc. v. Stanton*, 928 F.2d 1318, 1329 (2d Cir. 1991).

¹⁰⁶ MINN. R. CIV. P. 23.06.

¹⁰⁷ *See Lewis v. Chiles*, 719 F.2d 1044, 1047 (9th Cir. 1983).

¹⁰⁸ *Id.* (quoting *Cohen v. Beneficial Loan Corp.*, 337 U.S. 541, 548 (1949)).

¹⁰⁹ *See Winter v. Farmers Educ. & Coop. Union*, 259 Minn. 257, 266-67, 107 N.W.2d 226, 233 (1961) (requiring that demand be made to the board of directors unless a majority of the board is involved in the action precipitating the suit).

¹¹⁰ *Id.*

¹¹¹ *See* MINN. R. CIV. P. 23.06.

¹¹² *See Winter*, 107 N.W.2d at 234.

¹¹³ *See id.*

¹¹⁴ *See* Good v. Getty Oil Co., 514 A.2d 1104, 1109 (Del. Ch. 1986).

¹¹⁵ *Id.*

¹¹⁶ Kamen v. Kemper Fin. Servs., Inc., 500 U.S. 90, 101 (1991).

¹¹⁷ *Id.* at 108-09.

¹¹⁸ *See* MINN. R. CIV. P. 23.06. A derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interest of the shareholders or members similarly situated in enforcing the right of the corporation or association. *Id.*

¹¹⁹ *Id.*

¹²⁰ *See* 2 O'NEIL & THOMPSON *supra* note 2, § 8:16 (stating that many states require a plaintiff in a derivative suit to provide security for the expenses a corporation may incur in defending such a suit).

¹²¹ *See* D. DeMott, Shareholder Derivative Actions Law and Practice, § 3:01 (1994).

¹²² *Id.*

¹²³ *Id.* § 3:02

¹²⁴ *Id.* § 3:03.

¹²⁵ *Id.*

¹²⁶ Minn. Stat. § 302A.243 (1982).

¹²⁷ *Id.*

¹²⁸ *Id.*

¹²⁹ *See* Demott, *supra* note 121, § 5:01 (giving an overview of the function of a special litigation committee).

¹³⁰ Black v. NuAire, Inc., 426 N.W.2d 203, 209-10 (Minn. Ct. App. 1988).

¹³¹ *Id.*

¹³² 1989 Minn. Laws ch. 172, § 12.

¹³³ *See* MINN. STAT. § 302A.241, subd. 1 (1993).

¹³⁴ Skoglund v. Brady, 541 N.W.2d 17 (Minn. Ct. App. 1995); *see infra* notes 150-59 and accompanying text. Although there was a petition for review filed in *Skoglund*, the Minnesota Supreme Court denied the petition for review on February 27, 1996. Accordingly, *Skoglund* represents the current status of Minnesota law on this issue.

¹³⁵ *Skoglund*, 541 N.W.2d at 21.

¹³⁶ *Id.*

¹³⁷ MINN. STAT. § 302A.305 (1994) (describing duties of the chief executive officer and the chief financial officer); § 302A.361 (describing duty of officers to act in best interest of corporation); § 302A.251 (describing director's duty to act in best interest

of corporation and additional provisions for directors); § 302A.255 (describing director conflicts of interest).

¹³⁸ § 302A.251 (directors); § 302A.361 (officers).

¹³⁹ § 302A.251, subd. 4.

¹⁴⁰ *Id.*

¹⁴¹ *Id.*

¹⁴² *See Westland Capital Corp. v. Lucht Eng'g Inc.*, 308 N.W.2d 709, 712 (Minn. 1981). “We are dealing here with the special case of a close corporation, which has been described as a partnership in corporate guise.” *Id.*; *see also Whetstone v. Hossfeld Mfg. Co.*, 457 N.W.2d 380, 382 (Minn. 1990) (finding that closely held corporations are “sui generis”); *Pedro v. Pedro*, 489 N.W.2d 798, 801 (Minn. Ct. App. 1992) (stating that shareholders in a closely held corporation, much like partners in a partnership, owe one another a fiduciary duty).

¹⁴³ § 302A.751, subd. 3a.

¹⁴⁴ § 302A.751 (Reporter’s Notes-1982 to 1984, subd. 3 (a)). The fiduciary duty to other shareholders attaches immediately upon filing the articles of incorporation. *See Warthan v. Midwest Consol. Ins. Agencies*, 450 N.W.2d 145, 148 (Minn. Co. App. 1990). Creation of the fiduciary duty does not depend on whether an entity actually becomes an active, functioning corporation. *Id.*

¹⁴⁵ The Eighth Circuit Court of Appeals and the Minnesota Federal District Court have both applied the concept that shareholders of a closely held corporation owe each other fiduciary duties. *See Brennan v. Chestnut*, 973 F.2d 644, 648 (8th Cir. 1992) (citing *Harris v. Mardan Business Sys., Inc.*, 421 N.W.2d 350 (Minn. Ct. App. 1988)); *Stock v. Heiner*, 696 F. Supp. 1253, 1261 (D. Minn. 1988). In *Brennan*, the Eighth Circuit added in dictum, however, that the fiduciary duty majority shareholders owe to minority shareholders does not apply when the minority shareholder is an employee and acquires a small percentage of stock as part of an employment compensation contract. *Brennan*, 973 F.2d at 648.

¹⁴⁶ *Evans v. Blesi*, 345 N.W.2d 775, 779 (Minn. Ct. App. 1984). The court in *Evans* found that one owner’s acts of secretive planning, verbal abuse, and coercion of the resignation of his partner constituted a violation of the fiduciary duty within a close corporation. As a result, the shareholder who had resigned was awarded damages against both his partner and the closely held corporation. *Id.* at 780-81.

¹⁴⁷ *Pedro v. Pedro*, 489 N.W.2d 798, 801 (Minn. Ct. App. 1992) (quoting *Evans*, 345 N.W.2d at 779). In *Pedro*, the court found a breach of fiduciary duty based on the defendant-shareholder’s failure to make payments admittedly due the minority shareholder, interference with his responsibilities, hiring a private investigator to follow him, fabrication of accusations of neglect, and threats to fire the minority shareholder if he continued to investigate discrepancies in the company’s financial records. *Id.* at 801-02. The court rejected the defendant’s claim that there could be no breach of fiduciary duty because there was no diminution in the value of the corporation or the value of the minority shareholder’s interest. *Id.* at 802. According to the court, majority shareholders can also breach their fiduciary duty by forcing a

minority shareholder's resignation. *Id.* But see *Kelly v. Rudd*, 1992 WL 3651, at *2-3 (Minn. Ct. App. Jan. 14, 1992) (rejecting the shareholder's contention that he had a reasonable expectation of permanent employment, noting that he had signed employment contracts that provided for his termination without cause and therefore rejected the employee-shareholder's claim that his discharge constituted a breach of fiduciary duty).

¹⁴⁸ Equitable owners include pledgees of stock, trust beneficiaries where the trust owns stock, or persons who have exercised a contractual right to purchase the shares, but who have not yet closed on the purchase. See *Miller Waste Mills, Inc. v. Mackay*, 520 N.W.2d 490 (Minn. Ct. App. 1994).

¹⁴⁹ *Wenzel v. Mathies*, 542 N.W.2d 634, 640 (Minn. Ct. App. 1996).

¹⁵⁰ *Skoglund v. Brady*, 541 N.W.2d 17, 21 (Minn. Ct. App. 1995).

¹⁵¹ *Id.* at 19.

¹⁵² *Id.*

¹⁵³ *Id.*

¹⁵⁴ *Id.*

¹⁵⁵ *Id.* at 21 (citing *Arent v. Distribution Sciences, Inc.*, 975 F.2d 1370, 1372 (8th Cir. 1992)) (applying Minnesota law); *PJ Acquisition Corp. v. Skoglund*, 453 N.W.2d 1, 6 (Minn. 1990).

¹⁵⁶ In *Skoglund*, the court of appeals primarily relied upon cases addressing the general principal of the direct/derivative claim distinction. For instance, *PJ Acquisition Corp.* involved a § 302A.751 claim brought by a shareholder that did not own its shares at the time of the alleged wrongdoing. *PJ Acquisition Corp.*, 453 N.W.2d at 5. The Minnesota Supreme Court held that the claim was derivative, that the rules for derivative actions applied, and that the shareholder could not assert claims based upon alleged wrongdoing prior to the shareholder's purchase of the shares. *Id.* at 6. In so holding, the court stated, "[w]hile MINN. STAT. § 302A.751 subd. 1 (1988) does not expand the options of shareholders to bring actions seeking personal damages, as distinguished from derivative damages, the equitable remedy expanded does not replace the traditional derivative action." *Id.*

¹⁵⁷ Section 302A.751, subd. 1(b) (5).

¹⁵⁸ See JOHN H. MATHESON AND PHILIP S. GARON, MINNESOTA CORPORATION LAW & PRACTICE § 10.1, at 10-5 (1992).

¹⁵⁹ Mr. Skoglund petitioned the Minnesota Supreme Court for review of the decision on both the direct/derivative claim issue and the special litigation committee issue. See *supra* notes 134-36 and accompanying text. The Minnesota Supreme Court denied review on February 27, 1996. *Skoglund v. Brady* 541 N.W.2d 17 (Minn. Ct. App. 1995), *review denied* (Minn. 1996). However, because the decision of the court of appeals is devoid of any reasoning that explains the court's apparent departure from the clear language of the statute, its precedential value is susceptible to attack.

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