

**HAS *ISAACS V. AMERICAN IRON & STEEL*
ALTERED THE PLEADING, POLICY AND PURPOSE
SUPPORTING SHAREHOLDER DISPUTE
CLAIMS UNDER SECTION 302A.467?**

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By: Mark K. Thompson

I. INTRODUCTION

On December 28, 2004, the Minnesota Court of Appeals issued its opinion in *Isaacs v. American Iron & Steel Co.*¹ The *Isaacs* case arises out of a not uncommon dispute about the operation and control of a closely-held² Minnesota business corporation.³ On April 4, 2005, the Minnesota Supreme Court declined to review *Isaacs*.⁴

In *Isaacs*, three issues were raised on appeal. The issues decided were: 1) whether the action was rendered moot by the fact that the majority shareholder could have achieved the same end result without violating the company's bylaws; 2) whether the company's bylaws were violated when the shareholders increased the number of directors and then elected new directors to fill those positions; and 3) whether the dismissal of the shareholder's claim requesting equitable relief was proper.⁵

As to the first issue, the court of appeals concluded that mere speculation on events that could have happened did not render the action moot.⁶ In deciding the second issue, the court found that the company's bylaws, as a corporate governance document, should be interpreted according to the rules governing the construction of contracts and statutes. Applying these rules, the court found that the plain language of the company's bylaws did not preclude the shareholders from increasing the number of directors.⁷ Finally, and most importantly for this comment, the court held that the district court properly dismissed the shareholder's equitable claim because the statute cited was directed more at providing a remedy rather than establishing grounds for a claim.⁸

As this comment will discuss in more detail, the author⁹ believes the implications and holding of *Isaacs* will be argued by practitioners in a much

¹ 690 N.W.2d 373 (Minn. Ct. App. 2004), *petition for cert. filed*.

² Defined as not more than 35 shareholders. MINN. STAT. § 302A.011 (2004).

³ *Isaacs*, 690 N.W.2d at 379-80.

⁴ *Id.*, *cert. denied* (Apr 04, 2005).

⁵ *Id.* at 373.

⁶ *Id.* at 376.

⁷ *Id.* at 378.

⁸ *Id.* at 379.

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broader manner than a casual review of the case reveals. Even more likely, *Isaacs* will be argued in support of positions probably not intended by the court.

In particular, the court in *Isaacs* has redefined how business litigators plead out cases under section 302A.467 of the Minnesota Business Corporation Act (“MBCA”). In fact, it has altered the way a section 302A.467 claim must be pled and may have redefined the underlying purpose and policy supporting such a claim.¹⁰

This comment will examine the facts, procedural posture and holding of *Isaacs* as it relates to section 302A.467 claims; describe the heightened pleading requirements now imposed by the court of appeals for such claims; and discuss how the court’s decision in *Isaacs* may have rendered any section 302A.467 claim duplicative and redundant. This comment concludes by suggesting that litigators should be aware of the court’s decision in *Isaacs* as well as familiar with the implications it is sure to have for plaintiff and defense counsel alike when faced with a section 302A.467 claim.

¹⁰ Minnesota Business Corporation Act, MINN. STAT. ch. 302A (2004) (“MBCA”). The MBCA is Minnesota’s statutory scheme governing corporations. At the time it was enacted in 1981, it was considered the most innovative business corporations act of its kind anywhere in the nation. MINN. STAT. ANN. § 302A.001 note at 81 (West 2004) (Reporter’s Notes and Report to Senate); see William Z. Pentelovitch & Cynthia F. Gilbertson, *Upholding shareholders’ interests: 20 years with the Minnesota Business Corporations Act*, 58 MINN. BENCH & B., Oct. 2001, at 19.

The MBCA was drafted with the notion that all business corporations, whether closely-held or publicly-owned, should be permitted to operate with substantial flexibility and informality. *Id.* Further, that the shareholders of all business corporations are entitled to enhanced protection in terms of disclosure and management accountability. *Id.* Based on this notion, the task force that drafted the MBCA believed that the proposed new act would add substantial flexibility and informality in matters of procedure, together with substantial disclosure of and accountability for the corporate actions resulting from those procedures. *Id.*

Since more than ninety percent of all Minnesota business corporations are closely-held, it is easy to understand that most litigation under the MBCA involves shareholders in closely-held corporations. MINN. STAT. ANN. § 302A.001 note at 190 (West 2004) (Reporter’s Notes and Report to Senate). Under section 302A.751 of the MBCA, an aggrieved shareholder may bring an action for numerous enumerated conduct unfairly prejudicing their rights. Section 302A.751 empowers the courts to grant any equitable relief it deems just and reasonable in the circumstances or dissolve the corporation and liquidate its assets and business. *Id.* The latter remedy is authorized in many disputes, including when the board is deadlocked; when those controlling the corporation have acted fraudulently, illegally, or in a manner unfairly prejudicial toward one or more shareholders; or when the corporate assets are being misapplied or wasted. Likewise, section 302A.467 of the MBCA grants to a shareholder alleging a MBCA violation a private right of action and allows the courts to grant any equitable relief it deems just and reasonable in the circumstances and award expenses, including attorneys’ fees and disbursements, to the shareholder. *Id.*

II. FACTS, PROCEDURAL POSTURE, AND HOLDING

Unfortunately, *Isaacs* involves a frequently litigated factual situation regarding ownership and management of a closely-held corporation. Fred and John Isaacs, father and son, were the only shareholders in American Iron & Steel Company, a Minnesota corporation engaged in metals-recycling.¹¹ Holding fifty-four percent of the company's stock, Fred was the majority shareholder. John held the remaining forty-six percent as the minority shareholder.¹²

American Iron & Steel had been owned and operated by the Isaacs family since the late 1800's and had always been passed down from one generation to the next.¹³ To this end, the shareholders put in place an Agreement to Purchase Stock ("Agreement") in 1985.¹⁴ The Agreement permitted John, upon Fred's death, to purchase Fred's ownership interest for "book value."¹⁵

From the mid-1980's, John had handled the day-to-day operations of American Iron & Steel, holding the positions of President, CEO, COO, and Treasurer.¹⁶ Fred and John negotiated for years over amending the Agreement to increase the originally negotiated "book value."¹⁷ Regrettably, the company fell on hard financial times in the 1990's.¹⁸

In July 2002, John and Fred attended a company shareholder meeting.¹⁹ During this meeting, Fred voted his majority shares to expand American Iron & Steel's board of directors from two members to four members.²⁰ Fred nominated his wife and daughter to fill the new directorships and voted his controlling interest to elect them.²¹ Not unexpectedly, John voted against expanding the board of directors and electing the new members.²²

Throughout the remainder of 2002, the newly expanded board of directors demoted John from CEO to President, placed him on a sixty-day leave of absence and eventually fired him.²³ Following his termination, John initiated litigation against American Iron & Steel, Fred and the new board

¹¹ *Isaacs*, 690 N.W.2d at 375.

¹² *Id.*

¹³ District Court Order and Mem. at 4, *Isaacs v. Am. Iron & Steel Co.*, 690 N.W.2d 373 (Minn. Ct. App. 2004) (No. 03-2445).

¹⁴ *Id.*

¹⁵ *Id.*; see also *Rainforest Cafe, Inc. v. State of Wis. Inv. Bd.*, 677 N.W.2d 443, 452 (Minn. Ct. App. 2004) (stating that "book value is a measure derived from a company's balance sheet, which may not fully reflect the market value of a company's assets").

¹⁶ *Isaacs*, 690 N.W.2d at 375.

¹⁷ District Court's Order and Mem. at 4-5.

¹⁸ *Id.* at 4.

¹⁹ *Isaacs*, 690 N.W.2d at 375.

²⁰ *Id.*

²¹ *Id.*

²² *Id.*

²³ *Id.*

members.²⁴ John asserted multiple claims, including separate causes of action under sections 302A.467 and 302A.751 of the MBCA.²⁵

John separately pled his claims in a 113 paragraph Amended Complaint, with the three section 302A.751 claims alleging unfairly prejudicial conduct to John as a shareholder, director and employee.²⁶ The section 302A.751 claims alleged John had been treated in an unfairly prejudicial manner as a minority shareholder because the company's bylaws were violated when the board of directors was expanded and when the new board took detrimental actions regarding issues including his employment.²⁷

In Count IV of his Amended Complaint, John asserted his section 302A.467 claim.²⁸ This claim restates and realleges all of the Amended Complaint's previously plead eighty-six paragraphs, asserts that Fred and the new board members "violated the provisions of Chapter 302A" of the MBCA, and asserts John is entitled to equitable relief and "an award of his expenses, including attorneys' fees and disbursements."²⁹

The parties subsequently brought cross-motions for summary judgment and the district court partially granted the motions relating to John's claims for equitable relief under sections 302A.467 and 302A.751.³⁰ The district court also granted summary judgment as to the portion of John's section 302A.751 claim relating to the bylaw violations, but held that issue was moot because Fred could have accomplished the same ends with lawful means.³¹ As to John's section 302A.467 claim, the district court dismissed it in full for failing to specify which section of the MBCA had been violated.³²

In dismissing John's section 302A.467 claim, the district court held it was impermissibly vague, stating:

Count Four does not specify which sections of the voluminous Minn. Stat. § 302A Fred is alleged to have violated. The Table of Contents, alone, of Section 302A takes up ten pages of the statute book; the statute itself is 422 pages long and includes nearly every aspect of a corporation in Minnesota Absent any specificity in the complaint as to what wrong Fred is alleged to have committed, that cause of action cannot be allowed to proceed.³³

²⁴ *Id.*

²⁵ *Isaacs*, 690 N.W.2d at 375.

²⁶ Amended Complaint at 11-14, *Isaacs v. Am. Iron & Steel Co.*, 690 N.W.2d 373 (Minn. Ct. App. 2004) (No. 03-2445).

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.* at 15; *see also* MINN. STAT. § 302A.467 (2004).

³⁰ *Isaacs*, 690 N.W.2d at 375-76.

³¹ *Id.* at 375. This issue alone is easily the topic of an in depth article; thus, it is beyond the scope intended for this comment.

³² *Id.* at 376.

³³ District Court's Order and Mem. at 12.

The court of appeals upheld the district court's dismissal of the section 302A.467 claim based on "several independent reasons." The court reasoned that the claim was broad, section 302A.467 is "directed more at a remedy than at providing a grounding for a claim" and it was a "duplicative request for equitable relief" when contrasted with the section 302A.751 claims.³⁴ In so holding, the court determined that since John's section 302A.751 claims were tried by a referee per a stipulation between the parties,³⁵ dismissing the "duplicative" request for relief did not affect John's substantial rights.³⁶

III. MUST SECTION 302A.467 CLAIMS NOW BE PLEAD WITH HEIGHTENED SPECIFICITY?

Since the adoption of the Minnesota Rules of Civil Procedure in 1951, a complaint only needs to contain a short and plain statement of the claim showing that the pleader is entitled to relief and a demand for judgment for the relief sought.³⁷ There is no requirement in either the MBCA or the Rules of Civil Procedure to adhere to a mechanistic or rigid formula when pleading a claim.³⁸ General statements that put a party on notice of a claim are usually sufficient to state a claim.³⁹ In fact, under the Rules of Civil Procedure, only claims for fraud and mistake need to be stated with particularity.⁴⁰

In *Isaacs*, by affirming the district court's dismissal of John's section 302A.467 claim, the court has now imposed a heightened degree of specificity for a claimant asserting such a claim.⁴¹ The court has, at a

³⁴ *Isaacs*, 690 N.W.2d at 378-79.

³⁵ The referee heard the case on ten different hearing dates from January 2003 to April 2003. Respondent's Brief, *Isaacs v. Am. Iron & Steel Co.*, 690 N.W.2d 373 (Minn. Ct. App. 2004) (No. 03-2445). Summary judgment was granted on December 17, 2003 and the appeal was filed on about February 27, 2004. See District Court's Order and Mem.

³⁶ *Isaccs*, 690 N.W.2d. at 379.

³⁷ See MINN. R. CIV. P. 8.01.

³⁸ *L.K. v. Gregg*, 425 N.W.2d 813 (Minn. 1988); *Midwest Family Mutual Ins. Co. v. Schmitt*, 651 N.W.2d 843 (Minn. Ct. App. 2002); *Wells Fargo Home Mortgage, Inc. v. Newton*, 646 N.W.2d 888, 899 (Minn. Ct. App. 2002) (in "determining whether a complaint states a claim, the test is whether the facts alleged, liberally construed, [entitle the] plaintiff to any relief, either legal or equitable" (citing *Lucas v. Med. Arts Bldg. Co.*, 291 N.W. 892, 894 (Minn. 1940))).

³⁹ A specific legal theory does not need to be stated if the pleading puts the defendant on notice of the claim and contains a request for relief. See *Wilson v. Ramacher*, 352 N.W.2d 389 (Minn. 1984); *Navarre v. Wash. County. Sch.*, 633 N.W.2d 40 (Minn. Ct. App. 2001).

⁴⁰ MINN. R. CIV. P. 9.02 (providing that, "In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person may be averred generally").

⁴¹ *Isaacs*, 690 N.W.2d at 378 (stating that "We agree with the district court that the claim was broad . . .").

minimum, muddied the waters regarding the pleading requirements for a section 302A.467 claim. Not only is the court's decision contrary to the purposes and policies supporting notice pleading, the court provides no explanation or reasoning for requiring more specificity. It also appears the court, contrary to its primary role as an error correcting court, has created new law.⁴²

When the court's holding in *Isaacs* is read in conjunction with the district court's summary judgment order and memorandum, it appears that section 302A.467 claims should now be pled more specifically, like a fraud claim. In *Isaacs*, even though John specifically incorporated by reference the Amended Complaint's previously alleged 86 paragraphs, which do explain in great detail the factual allegations giving rise to his claims, that standard pleading practice apparently is now insufficient for a section 302A.467 claim.⁴³

After *Isaacs*, a cautious plaintiff should at least specifically reference another section of the MBCA when pleading their section 302A.467 claim.⁴⁴ This would assist the court and other parties determine what other MBCA violations are alleged to have occurred. A prudent plaintiff will also want to plead a broad, all-inclusive paragraph within the section 302A.467 count.⁴⁵ Likewise, a savvy defendant should move to dismiss a section 302A.467 claim if the plaintiff fails to specify another section of the MBCA to support the claim.

Shareholder disputes usually encompass other viable and common MBCA claims that can be pled in conjunction with the claimant's section 302A.467 claim. For instance, an aggrieved minority shareholder may also have claims under section 302A.251 for violations of the standard of conduct for directors, under section 302A.435 for improper or inadequate notice of meetings, and under section 302A.461 for a failure to permit inspection of the corporate books and records. Additionally, a minority shareholder can include claims under section 302A.463 for a failure to provide financial statements, under section 302A.557 for liability of shareholders for illegal distributions, and under section 302A.559 for liability of directors for illegal distributions, among many other MBCA violations.

In most closely-held shareholder disputes, a specific MBCA statutory violation is not difficult to locate. However, a technical, procedural

⁴² See *Sefkow v. Sefkow*, 427 N.W.2d 203, 210 (Minn. 1988) (recognizing that the role of the court of appeals is to correct errors).

⁴³ See Amended Complaint at 1-14.

⁴⁴ Section 302A.467 of the MBCA provides that:

If a corporation or 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.

⁴⁵ Of course, the allegation must have a factual and legal basis. MINN. R. CIV. P.

and mechanistic hurdle should not be unnecessarily placed in a claimant's way.

IV. IS *ISAACS* CONTRARY TO THE PURPOSE AND POLICY SUPPORTING A SECTION 302A.467 CLAIM?

In *Isaacs*, the Minnesota Court of Appeals substantiates and justifies dismissing John's section 302A.467 claim by finding:

[I]t significant that John Isaacs's substantive claims under section 302A.751 that were not resolved through summary judgment were fully tried to a referee. Thus, the dismissal of a duplicative request for equitable relief under section 302A.467 does not affect substantial rights.⁴⁶

Of course, at the time the district court granted summary judgment, John had not yet had his claims heard. The court's finding appears to directly contradict the election of remedies doctrine and the legislative intent underlying the MBCA. It also seems to ignore a distinct and definable difference between a section 302A.751 and a section 302A.467 claim.

The election of remedies doctrine allows a plaintiff to pursue alternative theories of recovery but prevents double recovery.⁴⁷ In *Isaacs*, the courts chose what theory John was permitted to pursue. By reasoning after the fact that John had already received what he was entitled to under section 302A.751, the courts selected John's theory of recovery. Although John did receive his "day in court" because a referee heard his case on the merits, *Isaacs* disregards the distinct differences between claims under sections 302A.751 and 302A.467.

The two major differences between claims under sections 302A.751 and 302A.467 are ascertainable from the MBCA itself. Under section 302A.751, the most commonly pled claim by minority shareholders,⁴⁸ a shareholder may bring a claim for violations of specifically enumerated conduct.⁴⁹ Claims under section 302A.751 also provide the strongest remedy

⁴⁶ *Isaacs*, 690 N.W.2d at 379.

⁴⁷ *Cashen v. Owens*, 29 N.W.2d 440 (Minn. 1947) ("The purpose of the election-of-remedies doctrine is not to prevent recourse to a potential remedy but to prevent double redress for a single wrong.") (citation omitted).

⁴⁸ See Joseph W. Anthony & Karlyn Vegoe Boraas, *Betrayed, Belittled . . . but Triumphant: Claims of Shareholders in Closely Held Corporation*, 22 WM. MITCHELL L. REV. 1173, 1176 (1996) (discussing the rights and remedies of shareholders in closely-held corporations).

⁴⁹ MINN. STAT. § 302A.751(1)(b)(1-6) (2004) (listing circumstances as deadlock, fraudulent or illegal director actions or director acting unfairly prejudicial towards one or more shareholders, lengthy shareholder division resulting in board vacancies, waste or misapplied corporate assets, and expired duration in articles).

available under the MBCA, dissolution of the closely-held corporation.⁵⁰ The list of unlawful misconduct contained in section 302A.751 is limited to fact-specific situations, which is precisely why section 302A.467 is available to a claimant.

When reviewing the section 302A.467 Reporter's Notes, the purpose of this section becomes clear. The relevant portions of the prior Minnesota business corporations' statute were restricted to certain and particular fact situations and authorized limited relief.⁵¹ The legislature's intent in enacting section 302A.467 was to give district courts wide discretion in determining the relief to be granted and the situations in which relief should be ordered.⁵²

The legislature exercised its infinite wisdom when it enacted section 302A.467. The complexity of corporate relationships and the potential for unique forms of abuse and unfair treatment of minority shareholders is as unlimited as human behavior itself. The statutory sections the MBCA replaced did not endow the courts with a broad enough discretionary mandate to cover the multitude of factual situations not specifically described in those sections.⁵³ There was also the perceived fear that any enumerated list of specific factual situations would be argued to be exclusive.⁵⁴ Accordingly, section 302A.467 was purposefully left very broad to encompass an ever-expanding myriad of potential corporate mischief. As such, section 302A.467 was drafted as a "catch-all" section for all sorts of unimaginable and unpredictable corporate misbehavior and mistreatment of minority shareholders.

V. CONCLUSION

The Minnesota Court of Appeals has imposed a new limit on claims asserted under section 302A.467 that appears to directly contradict Minnesota's 20-plus year history of extending liberal protection to minority shareholders. As such, business litigators should review *Isaacs* to familiarize themselves with the heightened pleading requirements now imposed by the court. Although it seems the court has altered the purpose and policy behind section 302A.467 claims, leaving it unclear whether they are just a "duplicative" claim under the MBCA, *Isaacs* will play a role in determining the viability of section 302A.467 claims.

⁵⁰ *Id.*

⁵¹ MINN. STAT. ANN. § 302A.467 note at 502 (West, 2004) (Reporter's Notes); *see* Anthony, *supra* note 45, at 1192 (discussing section 302A.467 claims and the limitation placed on the availability of a buy-out (citing *Westgor v. Grimm*, 381 N.W.2d 877, 881 (Minn. Ct. App. 1986))).

⁵² MINN. STAT. ANN. § 302A.467 note at 503 (Reporter's Notes).

⁵³ *Id.*

⁵⁴ *Id.* (stating that ". . . the existence of a list could be construed under the doctrine of *ejusdem generis* as limiting the power of the court to fact situations in the same class as those listed").

Unfairly treated minority shareholders in a closely-held corporation are uniquely vulnerable and require the utmost protection under the law. The Minnesota Court of Appeals appears to have disregarded that fact in *Isaacs*. As long as *Isaacs* is the law of the land, it may be wise for plaintiffs to specifically plead section 302A.467 claims, and if they do not, defense counsel should take a shot at dismissing such claims on that basis.