PROTECTING MINORITY SHAREHOLDERS IN ALASKA CLOSE CORPORATIONS

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The lack of case law in Alaska concerning close corporations, combined with recent supreme court decisions and statutory changes, has made for a confusing state of the law with respect to close corporations. This Comment outlines the nature of close corporations and the particular issues that they face, and it discusses the recent Alaska Supreme Court decisions in the Coppock cases. The Comment then offers a suggestion for how Alaska should proceed in changing and clarifying the state of close corporation law.

I. INTRODUCTION

Alaska is one of the youngest and least populous states in the Union. It should therefore come as no surprise that Alaska case law on close corporations is exceedingly thin. In fact, a case involving the protection of minority shareholders in close corporations did not come before the Alaska Supreme Court until 1980.[1] Perhaps also because of the state's small size, Alaska's statutes do not exhaustively cover topics relevant to minority shareholders. Thus, in *Alaska Plastics v. Coppock*[2] and *Stefano v. Coppock*,[3] the supreme court had a great deal of freedom to formulate Alaska law on the subject. Unfortunately, the court's opinions in these cases, combined with recent statutory changes, leave one feeling confused about the current state of the law in Alaska. This Comment critically examines these cases and statutes

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1. *See* Alaska Plastics, Inc. v. Coppock, 621 P.2d 270 (Alaska 1980).
2. *Id.*
3. 705 P.2d 443 (Alaska 1985).

and proposes a new framework within which Alaska should consider the rights of minority shareholders in close corporations.

II. THE NATURE OF CLOSE CORPORATIONS

Close corporations differ from public corporations in a number of important respects. Although there is no formal definition of a close corporation, close corporations are typified by a small number of shareholders, the absence of a market for the company's stock, and substantial participation in the business of the corporation by shareholders.[4]

A. Special Considerations of Close Corporations

1. Relative Position of Minority Shareholders. Close corporations present unique opportunities for the holders of a majority of the stock to burden the minority. In public corporations, shareholders typically receive a return on their investment through capital gains upon the sale of their stock or through the payment of dividends. In close corporations, however, there is by definition no ready public market for the sale of shares.[5] Also, shareholders in close corporations typically receive a return on their investment primarily through salaries as opposed to dividends.[6] Consequently, a shareholder in a close corporation who is not employed by the corporation often has no way to earn a return on her investment.[7] The majority shareholders can take advantage of this situation by offering to purchase the minority's shares for an unfairly low price.[8] In the absence of legal remedies, the minority shareholder might have no choice but to accept the unfair offer.[9]

2. Restrictions on the Transfer of Shares. Unlike shareholders in public corporations, shareholders in close corporations usually know and plan to work with all the other shareholders in the corporation.[10] An investment in a close corporation can be thought of as part of a "package deal" in that an individual invests only in

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4. *E.g.*, Donahue v. Rodd Electrotype Co. of New England, 328 N.E.2d 505, 511 (Mass. 1975).

5. *See, e.g.*, *Alaska Plastics*, 621 P.2d at 273.

6. 1 F. HODGE O'NEAL & ROBERT B. THOMPSON, O'NEAL'S CLOSE CORPORATIONS § 1.08 (3d ed. 1994).

7. *See, e.g.*, *Donahue*, 328 N.E.2d at 515.

8. *See, e.g.*, *id.*

9. *See, e.g.*, *id.*

10. *See* 1 O'NEAL & THOMPSON, *supra* note 6, §§ 1.02, 1.08.

contemplation of working with certain specific people in operating the business of the close corporation.[11] Consequently, shareholders in close corporations may wish to restrict the ability of a fellow shareholder to transfer her shares to a third party. Restrictions on the transfer of shares, often placed in the charter or by-laws, are a key part of close corporation planning.[12] Although a basic principle of property law is that restrictions on the alienability of property are disfavored, several forms of restrictions on the transfer of shares are allowed.[13] For example, a "right of first refusal" gives the corporation the right to purchase shares at the same price offered by any third party.[14] Also, a "consent restraint" dictates that shares cannot be sold unless the corporation (in the form of fellow shareholders) gives its approval.[15]

3. Shareholders Agreements. A special problem of a close corporation is that it is frequently rational for the majority shareholders to "freeze out" a minority shareholder by using their voting power to deny the minority a return on her investment. Although a freeze-out may take many forms, the end result is the same regardless of the form taken: the majority rids itself of an unwanted minority shareholder. In addition to relying on the fiduciary duties owed by the majority to the minority, a minority shareholder can protect herself by entering into a shareholders agreement at the onset of the corporation.[16] These agreements can be placed in the charter or by-laws.[17]

One example of a shareholders agreement is a voting agreement, in which a shareholder agrees to vote her shares a specific way.[18] Voting agreements can cover a variety of areas, including management policy, deadlock, and dissolution.[19] A buyout agreement is another way for a minority shareholder to

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11. *See* Douglas K. Moll, *Shareholder Oppression in Close Corporations: The Unanswered Question of Perspective*, 53 VAND. L. REV. 749, 757 (2000).

12. *See* 1 O'NEAL & THOMPSON, *supra* note 6, § 1.14.

13. All states permit certain restrictions on share transfers. *Id.* Some state statutes automatically prohibit share transfers in close corporations unless there is unanimous shareholder approval. *See, e.g.*, MD. CODE ANN., CORPS. & ASS'NS § 4-501 (LexisNexis 1999).

14. 1 O'NEAL & THOMPSON, *supra* note 6, § 7.05.

15. *Id.*

16. 1 *id.* § 5.01.

17. 1 *id.* § 5.03.

18. *Id.*

19. *See* 1 *id.* § 5.02.

protect herself.[20] It grants the shareholder the right to have her shares bought at a price determined by a method previously agreed to upon the happening of a specified event, such as the shareholder's departure from the employ of the corporation.[21] Alternatively, a charter provision might grant a shareholder veto power over all key decisions,[22] or an agreement may be made to compel dividends to be paid at specified intervals.[23]

B. Sources of Relief for Minority Shareholders in Close Corporations

1. The "Equal Opportunity" Principle. Most courts hold that majority shareholders owe the minority a fiduciary duty.[24] In many states, these fiduciary duties are enhanced in the close corporation context.[25] This duty has been expressed as a duty of the "highest degree of honesty and good faith."[26] Some courts have even gone so far as to hold that shareholders in close corporations owe each other the same fiduciary duty as partners in a partnership.[27]

The Massachusetts case of *Donahue v. Rodd Electrotype Co.*[28] laid out a special rule concerning the fiduciary duty owed by a controlling shareholder in a close corporation to the minority.[29] In *Donahue*, the directors of a close corporation caused the company to purchase the shares of a director who was also the firm's largest shareholder.[30] A minority shareholder sued to rescind the purchase.[31] The court noted that while close corporations and partnerships share many similarities, the use of the corporate form

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20. 2 *id.* § 9.06.
21. *Id.*
22. 1 *id.* § 3.41.
23. 2 *id.* § 9.05.
24. *See, e.g.*, Jones v. H. F. Ahmanson & Co., 460 P.2d 464, 472–74 (Cal. 1969); Guy v. Duff & Phelps, Inc., 672 F. Supp. 1086, 1090 (N.D. Ill. 1987).
25. *See, e.g.*, Donahue v. Rodd Electrotype Co., 328 N.E.2d 505, 515–16 (Mass. 1975); Orchard v. Covelli, 590 F. Supp. 1548, 1557 (D. Pa. 1984) ("Adherence by the majority interest to a fiduciary duty of strict fairness is particularly critical in the context of the closely-held corporation.").
26. *Guy*, 672 F. Supp. at 1090 (quoting Jaffe Commercial Finance Co. v. Harris, 456 N.E.2d 224, 230 (1983)).
27. *See, e.g.*, *Donahue*, 328 N.E.2d at 515; Fought v. Morris, 543 So. 2d 167, 171 (Miss. 1989); Estate of Schroer v. Stamco Supply, Inc., 482 N.E.2d 975, 981 (Ohio Ct. App. 1984).
28. 328 N.E.2d 505 (Mass. 1975).
29. *Id.* at 505–06.
30. *Id.* at 510.
31. *Id.* at 508.

gives directors of close corporations an opportunity to disadvantage the minority by, for example, refusing to declare dividends.[32] While a partner can dissolve the partnership at any time, a minority shareholder of a close corporation has no market in which to sell her shares and can only achieve dissolution of the corporation by complying with the strict terms of a state's dissolution statute.[33] The result is that a minority shareholder is often forced to deal with the majority on the majority's terms.[34] Because of this "inherent danger" to minority interests in a close corporation, the court held that shareholders in a close corporation owe each other the same fiduciary duty as partners, a duty of "the utmost good faith and loyalty."[35] The court contrasted this with the less stringent duty that applies to corporations generally.[36] As part of this enhanced fiduciary duty, the court held that "the controlling group [in a close corporation] may not . . . utilize its control of the corporation to obtain special advantages and disproportionate benefit from its share ownership."[37] Applying this rule to the facts of the case, the court held that a controlling shareholder who causes the corporation to purchase his stock has violated his fiduciary duties unless the corporation offers to purchase the minority's shares on the same terms.[38] According to the court, there were two forms of appropriate relief for the plaintiffs in *Donahue*: (1) a remission of the money the defendant director received in exchange for the shares, and (2) an order that the corporation purchase the plaintiff's shares on the same terms as those offered the defendant.[39]

Another Massachusetts case, *Wilkes v. Springside Nursing Home*,[40] was decided a year after *Donahue* and tilted the scales

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32. *Id.* at 512–13.

33. *Id.* at 514.

34. *Id.* at 515.

35. *Id.*

36. *Id.* at 515–16 ("We contrast this strict good faith standard with the somewhat less stringent standard of fiduciary duty to which directors and stockholders of all corporations must adhere in the discharge of their corporate responsibilities.").

37. *Id.* at 518.

38. *Id.* at 518–19.

39. *Id.* at 520–21 (granting the plaintiff both forms of relief). A similar rule was adopted by the California Supreme Court in *Jones v. H. F. Ahmanson & Co.*, 460 P.2d 464 (Cal. 1969). In *Ahmanson*, the court held that majority shareholders owe a fiduciary obligation to the minority and that any use to which the majority puts the corporation must benefit all shareholders proportionately. *Ahmanson,* 460 P.2d at 471.

40. 353 N.E.2d 657 (Mass. 1976).

back in favor of the majority shareholders. The court in *Wilkes* balanced the strict "equal opportunity" principle espoused in *Donahue* with the right of a shareholder to vote her shares in her own self-interest.[41] According to *Wilkes*, in order to show a breach of the fiduciary duty owed by the majority to the minority, a complaining shareholder first has the burden to show unequal treatment by the majority.[42] Thereupon, the majority has an opportunity to show that there was a valid business purpose for the unequal treatment.[43] If the majority can satisfy that burden, the minority then has the opportunity to show that the majority could have achieved its valid business purpose through an alternative less harmful to the minority.[44] Applying this test, the *Wilkes* court concluded that a minority shareholder who had not been reelected as an officer and director of the corporation was entitled to recover the salary he would have received had he remained an officer and director.[45]

Not all jurisdictions extend special protection to the shareholders of close corporations. Delaware rejected the "equal opportunity" doctrine in *Nixon v. Blackwell*.[46] In *Nixon*, minority non-employee shareholders of a close corporation[47] who acquired their shares as a gift claimed that the directors, who were the majority shareholders, breached a fiduciary duty by implementing an employee stock ownership plan and key man life insurance programs that benefited employees of the corporation with no corresponding benefit to the plaintiffs.[48] The court found that since the defendants stood to benefit from the programs, they stood "on both sides of the transaction."[49] Consequently, the court held that the defendants had the burden to demonstrate the "entire fairness" of the transactions.[50] That burden was met by the defendants, who

41. *Id.* at 663.
42. *See id.*
43. *Id.*
44. *Id.*
45. *Id.* at 664–65.
46. 626 A.2d 1366 (Del. 1993).
47. The corporation did not, however, qualify for the special provisions of Subchapter XIV of the Delaware General Corporation Law. *Id.* at 1380.
48. *Id.* at 1370–71.
49. *Id.* at 1375.
50. *Id.* at 1375–76. The court emphasized that this "entire fairness" standard was more onerous to the defendants than the business judgment rule because it requires judicial scrutiny of the transactions. In other words, because the defendants stood on both sides of the transactions the court would not merely defer to the defendant directors' judgment. *See id.*

justified the discriminatory treatment on the basis that employees and not shareholders were being favored.[51] The court rejected the notion that stockholders must always be treated equally for all purposes, emphasizing the distinction between fairness and equality.[52] In essence, the court held that the plaintiffs did not deserve the same benefits given to other shareholders because the plaintiffs were not employees of the corporation.[53]

2. Oppression. The corporation statutes of many states allow a minority shareholder to seek dissolution of a corporation upon a showing of "oppression."[54] Courts have taken a variety of approaches in determining just what constitutes "oppression," but it can generally be defined as a departure from fair play or fair dealing.[55]

Other courts have made clear that a single fiduciary violation is insufficient for a finding of oppression, so that oppression justifying dissolution will only be found when there is a continuing course of oppressive conduct resulting in disproportionate loss to the minority or demonstrating that the majority can no longer be trusted.[56] However defined, it has been said that the "oppression" standard has made it easier for minority shareholders in close corporations to obtain relief.[57]

3. "Reasonable Expectations." In *Stefano v. Coppock*, Alaska adopted the "Reasonable Expectations" test, as laid out by the New York Court of Appeals in *In re Kemp & Beatley, Inc.*,[58] for determining whether a minority shareholder in a close corporation

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51. *See id.* at 1377–78.

52. *See id.* at 1376–77.

53. *See id.* at 1377.

54. *E.g.*, MD. CODE ANN., CORPS. & ASS'NS § 3-413(b)(2) (LexisNexis 1999); MONT. CODE ANN. § 35-1-938(2)(b) (2005). Other statutes use "unfair" or "prejudicial to shareholders" rather than "oppressive." *See, e.g.*, ALASKA STAT. § 10.06.628(b)(4) (2006); CAL. CORP. CODE § 1800(b)(4) (West 1990); MINN. STAT. ANN. § 302A.751 subdiv. 1 (b)(2) (West 2004); N.D. CENT. CODE § 10-19.1-115 (2005).

55. *See, e.g.*, Polk v. Hergert Land & Cattle Co., 5 P.3d 402, 405 (Colo. Ct. App. 2000); Churchman v. Kehr, 836 S.W.2d 473, 482 (Mo. Ct. App. 1992); Giannotti v. Hamway, 387 S.E.2d 725, 730 (Va. 1990).

56. *See, e.g.*, Kisner v. Coffey, 418 So.2d 58, 61 (Miss. 1982); Baker v. Commercial Body Builders, Inc., 507 P.2d 387, 395–97 (Or. 1973).

57. *See, e.g.*, Belcher v. Birmingham Trust Nat'l Bank, 348 F. Supp. 61, 148 (N.D. Ala. 1968); Exadaktilos v. Cinnaminson Realty Co., 400 A.2d 554, 561 (N.J. Super. Ct. Law Div. 1979).

58. 473 N.E.2d 1173 (N.Y. 1984).

has been oppressed.[59] In *Kemp & Beatley*, the Court of Appeals of New York noted:

> A shareholder who reasonably expected that ownership in the corporation would entitle him or her to a job, a share of corporate earnings, a place in corporate management, or some other form of security, would be oppressed in a very real sense when others in the corporation seek to defeat those expectations and there exists no effective means of salvaging the investment.[60]

The court thus held that a complaining shareholder's reasonable expectations should be used to determine whether a minority shareholder in a close corporation has been the victim of oppression.[61] In making this determination, the court said, courts must look at what the majority shareholders knew to be the minority's expectations in joining the close corporation.[62]

The Reasonable Expectations test has been adopted in many states, although often in slightly modified forms.[63] For example, in *Meiselman v. Meiselman*,[64] the North Carolina Supreme Court held that courts should look at the entire history of the complaining minority shareholders' involvement in determining if oppression is present.[65] In other words, a court should look at the minority's reasonable expectations not only at the inception of the relationship but also as they have evolved over time.[66]

Under the Reasonable Expectations test, it is not the case that the minority's disappointment is always tantamount to oppression. Rather, oppression will be found only when expectations that were central to the minority's decision to invest in the close corporation are violated.[67]

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59. Stefano v. Coppock, 705 P.2d 443, 446 n.3 (Alaska 1985).

60. *Kemp & Beatley*, 473 N.E.2d at 1179.

61. *Id.*

62. *Id.*

63. Besides New York and Alaska, other states that have adopted the Reasonable Expectations test include North Carolina, New Jersey, Arkansas, Montana, North Dakota, South Dakota, and West Virginia. 2 O'Neal & Thompson, *supra* note 6, § 9.28.

64. 307 S.E.2d 551 (N.C. 1983).

65. *Id.* at 563.

66. *See id. But see* Graham v. Mimms, 444 N.E.2d 549, 556 (Ill. App. Ct. 1982) (holding that the intensity and content of the duty of loyalty depends on the parties' reasonable expectations at the *beginning* of the fiduciary relationship).

67. *In re* Wiedy's Furniture Clearance Ctr., 487 N.Y.S.2d 901, 903 (N.Y. App. Div. 1985).

Some states have explicitly adopted the Reasonable Expectations test in their corporate statutes.[68] Conversely, the highest court in at least one state has declined to adopt the Reasonable Expectations test because it was deemed to conflict with the state's dissolution statute, which focused on the actions of the majority shareholders, not on the minority's expectations.[69]

Corporate statutes generally provide that a shareholder's remedy for oppression is dissolution.[70] However, the corporate statutes of several states explicitly allow a court to provide relief less severe than dissolution.[71] Moreover, many courts have held that it is within a court's equitable powers to order a buyout of the complaining shareholder's shares by the corporation as a remedy less extreme than dissolution.[72]

III. FACTUAL BACKGROUND OF THE *COPPOCK* CASES

In 1961, Robert Crow and two other men, Ralph Stefano and C. Harold Gillam, formed a close corporation called Alaska Plastics to produce foam insulation at a building in Fairbanks.[73] The three incorporators each held 300 shares of stock and were the sole officers and directors of the corporation.[74] In 1970, Crow and his wife, Patricia Muir, divorced.[75] Under the property settlement, Muir received one-half of Crow's interest in Alaska Plastics (a one-sixth interest in the corporation).[76] The three original

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68. *See, e.g.*, MINN. STAT. ANN. § 302A.751 subdiv. 3 (a) (West 2004); N.D. CENT. CODE § 10-19.1-115(4) (2005).

69. *See* Kiriakides v. Atlas Food Sys. & Servs., Inc., 541 S.E.2d 257, 265–66 (S.C. 2001) (citing S.C. CODE ANN. § 33-14-300 (1990)).

70. *See, e.g.*, MD. CODE ANN., CORPS. & ASS'NS § 3-413(b)(2) (LexisNexis 1999); MONT. CODE ANN. § 35-1-938(2)(b) (2001).

71. *See, e.g.*, ARIZ. REV. STAT. ANN. § 10-1816 (2004); ME. REV. STAT. ANN. tit. 13A, § 1123 (1981) (repealed effective July 1, 2003); S.C. CODE ANN. § 33-14-310(d) (2006). Minnesota's corporate statute allows a buyout to be ordered even when the requirements for dissolution have not been proven. MINN. STAT. ANN. § 302A.751 subdiv. 1, 2 (West 2004).

72. *See, e.g.*, McCauley v. Tom McCauley & Son, Inc., 724 P.2d 232, 236 (N.M. Ct. App. 1986); *In re* Wiedy's Furniture, 487 N.Y.S.2d at 904 (N.Y. App. Div. 1985); Balvik v. Sylvester, 411 N.W.2d 383, 388–89 (N.D. 1987); Masinter v. Webco Co., 262 S.E.2d 433, 439 (W. Va. 1980).

73. Alaska Plastics, Inc. v. Coppock, 621 P.2d 270, 272 (Alaska 1980).

74. *Id.*

75. *Id.*

76. *Id.*

incorporators, however, continued to be the sole officers and directors of the company.[77]

Muir was not notified of the annual shareholders meetings in 1971, 1972, or 1974, and she received notice of the 1973 annual meeting only three hours before it was held.[78] In addition, in 1971 and 1972, when the directors held the shareholders meeting in Seattle, the two directors other than Crow brought their wives to the meetings at the company's expense.[79]

In 1971, the directors voted themselves an annual director's fee of $3000, which was paid through 1974.[80] The directors also authorized a $30,000 salary for Gillam as the general manager of the company.[81] At no time did the directors authorize the payment of dividends, and Muir did not otherwise receive money from the company.[82]

In 1974, the board purchased Broadwater Industries, a company producing a product similar to that produced by Alaska Plastics, for $50,000.[83] Muir was never consulted about the transactions, but she did not dissent from a shareholder vote held at the 1975 shareholders meeting that ratified all directors' and officers' acts from the previous year.[84] The three incorporators of Alaska Plastics also became the sole officers and directors of a corporation that was renamed Valley Plastics and made a wholly-owned subsidiary of Alaska Plastics.[85]

At the 1975 shareholders meeting, Muir offered to sell her interest in Alaska Plastics for $40,000.[86] The board refused and instead offered $20,000, which Muir rejected.[87] Shortly thereafter, the Fairbanks plant burned to the ground, essentially leaving Alaska Plastics as nothing more than a holding company for Valley Plastics.[88]

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77. *Id.*

78. *Id.*

79. *Id.* In his testimony, Stefano also admitted that bringing the wives to the shareholders meeting had no business purpose. *Id.*

80. *Id.*

81. *Id.*

82. *Id.*

83. *Id.*

84. *Id.*

85. *Id.*

86. *Id.*

87. *Id.* The board had previously offered Muir $15,000 for her shares in 1974. *Id.*

88. *Id.* at 273.

Muir sued the directors, bringing a variety of individual and derivative claims.[89] The trial court found that it was oppressive to Muir for her to continue to possess one-sixth of the shares of Alaska Plastics.[90] Subsequently, the judge ordered that Alaska Plastics buy Muir's shares at their "fair and equitable value" of $32,000.[91] The directors appealed.[92]

A. The First Alaska Supreme Court Case

In *Alaska Plastics*, the court noted the unique susceptibility of minority shareholders in close corporations to being "squeez[ed]-out" by the majority due to the absence of a ready market for the minority's shares.[93] According to the court, such a dissatisfied minority shareholder's best remedy is usually for the corporation to buy her shares at their "fair value."[94] The court focused on two circumstances in which a corporation could be ordered to buy a minority's shares.

The first was upon a petition by the minority for the dissolution of the corporation.[95] Under Alaska Statute section 10.05.540[96] (which has since been repealed), a court could order dissolution of the company upon a showing by a shareholder that "the acts of the directors or those in control of the corporation are illegal, oppressive or fraudulent" or that "corporate assets are being misapplied or wasted."[97] The court noted that dissolution is an extreme remedy, in part because it allows minority shareholders to "exercise retaliatory oppression against the majority."[98] Citing *Baker v. Commercial Body Buildings, Inc.*,[99] the court held that, despite the fact that the only remedy provided by the statute was dissolution, it was within a court's equitable powers to order a forced buyout of the minority's shares as a less drastic alternative to dissolution.[100] Accordingly, the court held that Muir's request for liquidation "could justify the trial court's order as an equitable

89. *Id.* at 273, 278.
90. *Id.* at 273.
91. *Id.*
92. *Id.*
93. *Id.* at 273–74.
94. *Id.* at 274.
95. *Id.*
96. ALASKA STAT. § 10.05.540 (repealed 1988).
97. *Alaska Plastics*, 621 P.2d at 274 (citing ALASKA STAT. § 10.05.540(4)).
98. *Id.*
99. 507 P.2d 387, 395–97 (Or. 1973).
100. *Alaska Plastics*, 621 P.2d at 274–75.

remedy" if, on remand, Muir could show that the acts of the directors were "illegal, oppressive or fraudulent."[101]

The second way in which the court stressed that a corporation could in theory be forced to purchase a minority's shares was as "an equitable remedy upon a finding of a breach of a fiduciary duty" owed by directors to shareholders.[102] The court adopted the rule in *Donahue* that shareholders in close corporations owe each other essentially the same fiduciary duty as partners in a partnership.[103] This fiduciary duty requires that if a controlling shareholder takes advantage of a special benefit, the corporation must offer the benefit to all shareholders equally.[104] The court also adopted the similar holding of *Ahmanson* that majority shareholders cannot use their position to obtain benefits not shared with the minority.[105]

The court reasoned that since none of the Alaska Plastics directors sold their shares back to the corporation, an order that the corporation purchase Muir's stock could not be justified under *Donahue* or *Ahmanson*.[106] However, the court did note that the directors' fees, the salary paid Gillam, and the personal expenses of the directors' wives paid for by the corporation could be construed as constructive dividends.[107] The court remanded the case for a determination of whether those payments were in fact constructive dividends and thus violated the rule of *Donahue* and *Ahmanson* because they were not made available to Muir.[108] The court held that the remedy for a payment of constructive dividends not shared with all shareholders is not a forced buyout of the disadvantaged shareholders' shares, but rather the remedy is for the excluded payments to be made available to all shareholders.[109]

On remand, the trial court found that Muir had demonstrated that the acts of the directors were oppressive.[110] The lower court thus ordered the corporation to purchase Muir's shares for $32,000,

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101. *Id.* at 275 (citing ALASKA STAT. § 10.05.540(4)).

102. *Id.* at 274.

103. *Id.* at 276; *see* Donahue v. Rodd Electrotype Co. of New England, 328 N.E.2d 505, 515 (Mass. 1975).

104. *Donahue*, 328 N.E.2d at 518.

105. *Alaska Plastics*, 621 P.2d at 276 (citing Jones v. H.F. Ahmanson & Co., 460 P.2d 464, 471 (Cal. 1969)).

106. *See id.* at 277.

107. *Id.*

108. *See id.* at 278.

109. *Id.* at 277.

110. *See* Stefano v. Coppock, 705 P.2d 443, 445 (Alaska 1985) (evidenced by the judgment in favor of Muir).

which the court found to be the fair value of Muir's shares.[111] The directors again appealed the case to the supreme court, arguing that the court's *Alaska Plastics* opinion precluded the lower court from ordering the buyout of Muir's shares.[112]

B. The Second Alaska Supreme Court Case

In *Stefano v. Coppock*, the supreme court affirmed the judgment of the trial court.[113] The court held, as it did in *Alaska Plastics*, that courts retain the authority to use their equitable powers to fashion remedies less drastic than dissolution.[114] The court rejected the directors' contention that a buyout of Muir's shares was actually a more drastic remedy than dissolution, reasoning that even if a buyout was more costly than dissolution, it was the most appropriate remedy for the harm done to Muir.[115]

The *Stefano* court affirmed, without any elaboration or analysis, the lower court's finding of oppression.[116] In a footnote, however, the court adopted New York's Reasonable Expectations approach for determining if minority shareholders in a close corporation have been oppressed.[117]

IV. ANALYSIS OF THE COURT'S OPINIONS IN *ALASKA PLASTICS* AND *STEFANO*

In *Alaska Plastics*, the court noted that the salary paid Gillam, the directors' fees, and the payment of the personal expenses of the directors' wives might constitute constructive dividends.[118] The court held that constructive dividends did not justify a forced buyout of Muir's shares.[119] The court also noted that a forced buyout of the complaining shareholder's shares is an available remedy for oppression.[120] Implicitly, then, the court held that the payment of constructive dividends was not by itself sufficient to warrant a finding of oppression.

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111. *Id.*
112. *Id.*
113. *Id.* at 445–46.
114. *Id.* at 446.
115. *Id.*
116. *Id.*
117. *Id* n.3. ("The question has been resolved by considering oppressive actions to refer to conduct that substantially defeats the 'reasonable expectations' held by minority shareholders." (quoting *In re* Kemp & Beatley, Inc., 443 N.E.2d 1173, 1179 (N.Y. 1984) (citations omitted))).
118. *See* Alaska Plastics, Inc. v. Coppock, 621 P.2d 270, 277 (Alaska 1980).
119. *See id.*
120. *Id*. at 275.

In adopting the Reasonable Expectations test while simultaneously upholding the lower court's finding of oppression, the *Stefano* court at least implicitly held that the evidence supported a finding that Muir's reasonable expectations were violated.[121] But if, as the court implied in *Alaska Plastics*, the payment of constructive dividends is not oppression, then the oppression must have consisted solely of the failure to allow Muir to participate in the management of the business (exemplified by the failure to notify Muir of shareholder meetings).[122] However, there is no reason to suppose that Muir expected to actively participate in the management of the business, nor would it have been reasonable for her to do so.

In reaching its conclusions, the *Stefano* court ignored the way in which Muir acquired her shares: through a divorce settlement.[123] Muir was not a typical investor in a close corporation—there was no indication that she expected or even desired a job with the company. It seems probable that Muir had no specific interest in Alaska Plastics, but rather that she merely received one-half of all her husband's property in the divorce settlement.

The two ways, short of liquidation, for an investor to receive a return on her investment in a close corporation are through employment with the company and through dividends.[124] Unless a minority shareholder is able to secure her rights through a shareholders agreement or a supermajority voting provision in the charter at the inception of a close corporation, she is always in danger of being frozen out: the majority can use its voting power to deny her a job and refuse to declare dividends.[125] Because Alaska Plastics was already up and running when Muir acquired her one-sixth share, it is doubtful that she had any opportunity to secure rights to a return on her "investment" in the corporation. Thus it was arguably unreasonable for her to expect a significant return.

To the extent that Alaska Plastics was awarding constructive dividends to some shareholders but not Muir, Muir certainly suffered an injury, the remedy for which, the *Alaska Plastics* court held, was for the dividends to be shared with her.[126] But these constructive dividends do not constitute oppression under the Reasonable Expectations approach unless Muir had reason to

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121. *See Stefano,* 705 P.2d at 446.
122. *See Alaska Plastics*, 621 P.2d.at 272.
123. *See id.* at 277.
124. *See* 1 O'NEAL & THOMPSON, *supra* note 6, § 1.09.
125. *See id*. § 1.13.
126. *See Alaska Plastics*, 621 P.2d at 277.

expect dividends, constructive or otherwise, to be paid.[127] Thus, it seems highly doubtful that Muir had any of her reasonable expectations violated. At the very least, therefore, the *Stefano* court should have explained why a finding of oppression was justified under the Reasonable Expectations approach (perhaps by finding that Muir was deemed to step into her ex-husband's shoes). Instead, the court provided no analysis at all.[128]

The *Stefano* court's upholding of a buyout of Muir's shares can be criticized as not being explicitly allowed by statute, but many courts in various jurisdictions have upheld a forced buyout as a remedy less extreme than dissolution.[129] More troubling is the court's unsupported assumption that a buyout is a less severe remedy than liquidation.[130] The court in *Alaska Plastics* noted that a primary reason a forced buyout is considered less extreme than dissolution is that dissolution allows a minority shareholder to exercise retaliatory oppression over the majority.[131] It seems, then, that the court allowed for the possibility of a buyout remedy solely because it can provide the minority shareholder with a satisfactory remedy in a manner that is less drastic to the majority. The court seems to have ignored its own reasoning, however, in merely brushing aside the majority's argument in *Stefano* that a buyout remedy is *not* a less drastic remedy than dissolution (perhaps because it would be cheaper for the majority to repurchase the corporation's assets at auction than to buy them from Muir).[132] The court conceded that a buyout may be more costly to the majority but noted that a buyout was an effective remedy for Muir.[133] By focusing on the appropriateness of a remedy from the *minority's* perspective, the court seems to have forgotten that the very purpose of the buyout remedy is its potential to provide a remedy less drastic from the *majority's* point of view.[134]

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127. *See Stefano v. Coppock*, 705 P.2d 443, 446 (Alaska 1985). Besides, as already noted, the *Alaska Plastics* court implied that it did not consider the constructive dividends to be oppressive, and the court in *Stefano* said nothing to contradict this. *See Alaska Plastics*, 621 P.2d at 277.

128. *See Stefano*, 705 P.2d at 446.

129. *See* Sauer v. Moffitt, 363 N.W.2d 269, 275 (Iowa Ct. App. 1984); 21 West, Inc. v. Meadowgreen Trails, Inc., 913 S.W.2d 858, 867 (Mo. Ct. App. 1995); Maddox v. Norman, 669 P.2d 230, 235 (Mont. 1983).

130. *See Stefano*, 705 P.2d at 446.

131. *See Alaska Plastics*, 621 P.2d at 274.

132. *See Stefano*, 705 P.2d at 446.

133. *Id*.

134. *See Alaska Plastics*, 621 P.2d at 274.

V. THE ALASKA STATUTORY APPROACH

The Alaskan involuntary dissolution statute that was in place at the time of the *Coppock* cases has been repealed and replaced with a statute that exactly parallels the California statute.[135] The current statute provides that a shareholder holding at least one-third of the total number of outstanding shares not owned by persons guilty of fraud, mismanagement, abuse of authority, or persistent unfairness to shareholders can bring suit for involuntary dissolution.[136] The available grounds for dissolution include: (1) that the majority has engaged in the gross misconduct outlined immediately above;[137] (2) that there is deadlock;[138] and, (3) in the case of corporations with fewer than thirty-five shareholders, that dissolution is reasonably necessary for the protection of the rights or interests of the complaining shareholders.[139]

Because Muir owned less than one-third of Alaska Plastics' shares, if she were to bring suit under today's statute, she could only sue if the majority had been guilty of fraud, mismanagement, abuse of authority, or persistent unfairness.[140] Otherwise, she would not own the requisite one-third of the shares held by persons not guilty of such misconduct.[141]

The current Alaska statute on involuntary dissolution is a bit confusing. In order to have standing to sue, a shareholder apparently must show what she would hope to prove at trial: that the majority has engaged in gross misconduct.[142] By contrast, the statute in place at the time of the *Coppock* cases allowed for a shareholder to bring an action to liquidate upon a showing that the majority had engaged in "illegal, oppressive or fraudulent" conduct[143] or that corporate assets were being "misapplied or wasted."[144]

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135. *See* ALASKA STAT. § 10.05.540 (1988) (repealed 1989). *Compare* ALASKA STAT. § 10.06.628 (2006) *with* CAL. CORP. CODE § 1800 (1990).

136. *See* ALASKA STAT. § 10.06.628(a)(2), (b)(4) (2006). The other circumstances enabling a suit for dissolution mentioned in the statute do not apply to Muir.

137. ALASKA STAT. § 10.06.628(b)(4).

138. ALASKA STAT. § 10.06.628(b)(2)–(3).

139. ALASKA STAT. § 10.06.628(b)(5).

140. *See* ALASKA STAT. § 10.06.628(b)(4).

141. ALASKA STAT. § 10.06.628(a)(2), (b)(4).

142. ALASKA STAT. § 10.06.628(a)(2), (b)(4).

143. ALASKA STAT. § 10.05.540(2) (1988) (repealed 1989).

144. ALASKA STAT. § 10.05.540(4) (repealed 1989).

The *Stefano* court adopted the Reasonable Expectations approach as a method of determining the existence of oppression.[145] Now that oppression is no longer explicitly an available statutory ground for dissolution in Alaska, the issue of the continued relevance of the Reasonable Expectations doctrine is unclear. Consequently, it is unclear whether Muir would be entitled to a buyout of her shares under today's statute. Scholars have assumed, however, that the Reasonable Expectations test is still good law in Alaska.[146] Also, the published version of the Alaska Code lists the *Coppock* cases as the sole annotations to section 10.06.628.[147]

One thing is clear: the statutes relating to close corporations are open-ended enough to enable the supreme court to decide for itself the precise circumstances in which a minority shareholder will be entitled to relief. Moreover, given the principle that courts are free to fashion equitable remedies less severe than dissolution, even when such remedies are not made explicitly available by statute, the supreme court is free to determine precisely what form of relief is appropriate in a given situation.[148]

VI. WHAT TEST SHOULD ALASKA ADOPT?

A. The Flaw in the Delaware Approach.

One need look no further than the *Nixon v. Blackwell* facts to find an example of a situation in which the Delaware approach to fiduciary duties owed minority shareholders is flawed.[149] Crucial to the court's rejection of the "equal access" principle was the fact that minority shareholders have an opportunity when obtaining their stock to bargain for protective provisions.[150] In addition to insisting on provisions in the charter or by-laws, the court noted that minority shareholders could enter into shareholders agreements providing for, *inter alia*, buyout provisions and voting agreements.[151] The court summarized its view as follows:

> The tools of good corporate practice are designed to give a purchasing minority stockholder the opportunity to bargain for

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145. *See* Stefano v. Coppock, 705 P.2d 443, 446 (Alaska 1985).

146. *See, e.g.*, Douglas K. Moll, *Shareholder Oppression & Reasonable Expectations: Of Change, Gifts, and Inheritances in Close Corporation Disputes*, 86 MINN. L. REV. 717, 730 n.47 (2002).

147. ALASKA STAT. § 10.06.628 Notes to Decisions (2006).

148. *See Stefano*, 705 P.2d at 446.

149. *See* Nixon v. Blackwell, 626 A.2d 1366 (Del. 1993).

150. *Id.* at 1379–80.

151. *Id.* at 1380.

> protection before parting with consideration. It would do violence to normal corporate practice and our corporation law to fashion an ad hoc ruling which would result in a court-imposed stockholder buy-out for which the parties had not contracted.[152]

The court's reasoning is persuasive until one takes account of the minority shareholder who does not have the opportunity to bargain for protections. This was the very situation in *Nixon*, and yet the court noted this fact only in passing, making no mention of the fact that its reasoning was inapplicable to the case at hand.[153]

The reasoning in *Nixon* is likewise inapplicable to the facts of the *Coppock* cases because it is unlikely that Patricia Muir had an opportunity to bargain for protections.[154] Therefore, Alaska needs a test that, unlike Delaware's approach in *Nixon*, takes into account that not all shareholders in close corporations make a conscious decision to invest their capital after having had an opportunity to weigh the risks. Nevertheless, the motivation behind the *Nixon* test is sound: when a frozen-out or oppressed shareholder is personally at fault for her own problems due to a failure to bargain for protection at the outset of the relationship with the other shareholders, a court should be less willing to grant her the remedy she requests at the expense of the corporation.[155]

B. The Limitations of the Reasonable Expectations Test.

The *Coppock* cases do an apt job of demonstrating the deficiencies in the Reasonable Expectations approach to determining the availability of relief to a minority shareholder in a close corporation. Given that she obtained her shares from her husband in a divorce settlement, Patricia Muir, in all likelihood, had no expectations, reasonable or otherwise, of receiving significant value from her shares in Alaska Plastics.[156] And yet it seems clear that she was treated unfairly by the company.[157] The company directors seem to have resented her status as a shareholder and to have done all they could to ignore her.[158] That Muir was not informed of shareholder meetings may not have

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152. *Id.*

153. *Id.* at 1379–80. "A stockholder who bargains for stock in a closely-held corporation and who pays for those shares (*unlike the plaintiffs in this case who acquired their stock through gift*) can make a business judgment whether to buy into such a minority position, and if so on what terms." *Id.* (emphasis added).

154. *See* Alaska Plastics, Inc. v. Coppock, 621 P.2d 270, 272 (Alaska 1980).

155. *See Nixon*, 626 A.2d at 1380–81.

156. *See Alaska Plastics*, 621 P.2d at 272.

157. *See id.*

158. *See id.*

caused direct material injury to her, but it indicates the attitude of the directors to Muir: they had no interest in altering their way of doing things to accommodate the new shareholder.[159] Using company assets to pay for the expenses of directors' wives may have been a sensible practice when all the shareholders of the corporation were directors with wives.[160] But once Muir came on board, this practice clearly became an inappropriate use of corporate assets as the majority directors were receiving benefits (for which there was no business purpose) to the exclusion of Muir.[161]

A possible solution to this problem is to modify the Reasonable Expectations test to provide that a transferee steps into the shoes of the transferor. In other words, if an action taken against a transferee shareholder would have violated the transferor's reasonable expectations, then the transferee's reasonable expectations will be deemed to have been violated. However, this solution is not entirely satisfactory; the circumstances of a transferor and transferee will invariably differ, so a transferor's expectations often will not be a suitable proxy for a transferee's.

Another problem with the Reasonable Expectations approach is that the extent to which wrongdoing by majority directors is required for a finding of oppression and a subsequent order of dissolution is unclear. An investor's reasonable expectations may be betrayed by the majority without any accompanying wrongdoing. For example, the directors of a company may, in a manner entirely consistent with the business judgment rule, alter the company's business plan and decide to invest corporate proceeds in the acquisition of a new plant or equipment rather than in the payment of dividends. Such actions may violate a minority shareholder's reasonable expectations of short-term dividends, and yet it seems harsh for a court to order dissolution of the corporation in such a situation.[162] Even a buyout of the minority's interests in this situation may be unfair because such a buyout may cause the corporation severe short-term liquidity problems. A

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159. *See id.*

160. *See id.*

161. *Id.*

162. Courts have indeed held that oppression can be present even when the majority directors have complied with the business judgment rule. *See, e.g.*, Exadaktilos v. Cinnaminson Realty Co., 400 A.2d 554 (N.J. Super. Ct. Law Div. 1979) (noting that the business judgment rule has failed to curb corporate abusive freeze-outs in close corporations); *In re* Topper, 433 N.Y.S.2d 359, 363 (N.Y. Sup. Ct. 1980).

court applying the Reasonable Expectations test could resolve the issue by holding that it is *per se* unreasonable for a minority shareholder to expect the corporation to forego favorable investments merely to avoid disappointing a minority shareholder. It seems a better approach, however, would be to explicitly require majority wrongdoing in order for dissolution of a close corporation to be justified. After all, the term "oppression" seems to imply the presence of wrongdoing.

Finally, the various formulations of the Reasonable Expectations test indicate that the determination of whether a violation has occurred depends on the subjective expectations of the particular minority shareholder in question (as limited by the "reasonable" standard). This requires that the majority determine the expectations of each minority shareholder before deciding whether a particular action is proper. It will often be costly, or even impossible, for the majority to obtain this information.

Thus, the Reasonable Expectations test is workable only if it is applied objectively and does not depend on the subjective expectations of the minority shareholders. Even under this approach, however, the issue of whether a hypothetical reasonable shareholder's expectations have been violated is inherently vague and would need to be fleshed out by case law, something that is in short supply in Alaska. In order to adequately protect the rights of minority shareholders without imposing paralyzing levels of uncertainty on the majority, Alaska needs an approach that is objective but that nevertheless imposes burdens on the party most likely to be at fault.

C. A Proposal for Alaska

Given the limitations of the Reasonable Expectations approach, the issue, then, is what the appropriate remedy is for Muir. There are three basic levels of relief for minority shareholders in close corporations. In increasing order of severity, they are: (1) the "equal opportunity" remedy laid down in *Donahue*[163] and *Wilkes*;[164] (2) a judicially ordered buyout; and (3) dissolution.[165]

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163. *See* Donahue v. Rodd Electrotype Co., 328 N.E.2d 505, 519 (Mass. 1975).

164. *See* Wilkes v. Springside Nursing Home, 353 N.E.2d 657, 663–66 (Mass. 1976).

165. *See, e.g.*, McCauley v. Tom McCauley & Son, Inc., 724 P.2d 232, 236 (N.M. Ct. App. 1986); *In re* Wiedy's Furniture Clearance Center Co., 487 N.Y.S.2d 901, 904 (N.Y. App. Div. 1985); Balvik v. Sylvester, 411 N.W.2d 383, 388–89 (N.D. 1987); Masinter v. Webco Co., 262 S.E.2d 433, 439 (W. Va. 1980).

1. "Equal Opportunity" Remedy. In most instances, an order requiring a corporation to share benefits disproportionately conferred on the majority with the minority will suffice to remedy a minority shareholder's injury.[166] Alaska should use a modified version of the test laid out in *Wilkes*[167] to determine when an "equal opportunity" violation has occurred. Recall that under the *Wilkes* test, a shareholder must show unequal treatment by the majority,[168] whereupon the majority has an opportunity to show that there was a valid business purpose for the unequal treatment.[169] The minority then has the opportunity to show that there was a less restrictive alternative (*i.e.*, that the majority could have achieved its purpose through an alternative less harmful to the minority).[170]

Alaska should borrow the general rule from *Wilkes* that once a minority shareholder shows that a disproportionate benefit has been conferred on the majority, the minority is entitled to relief if there was no valid business purpose for the unequal treatment or if there was a less restrictive alternative. This rule protects the interests of a minority shareholder without unduly burdening the corporation as a whole.[171]

Alaska should modify the *Wilkes* test so that the burden of proof is allocated to the party that is most likely to be the party at fault in creating the conflict. The default allocation of burdens should be the same as that laid out in *Wilkes*: the majority has the burden to show that there was a valid business purpose for the unequal treatment, whereupon the minority has the burden to show that there was a less restrictive alternative.

However, if the minority shareholder has failed to protect her rights through a shareholders agreement, then the minority should generally be viewed as the party responsible for the conflict. Consequently, the *minority* should have the burden to show that there was no legitimate business purpose for the unequal treatment.[172] Under this approach, the minority still has the opportunity to obtain relief, but the majority is given the benefit of the doubt due to the minority's fault in creating the conflict.

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166. *See, e.g.*, Kiriakides v. Atlas Food Sys. & Servs., Inc., 541 S.E.2d 257, 265–66 (S.C. 2001) (citing S.C. CODE ANN. § 33-14-300 (1990)).

167. *See Wilkes*, 353 N.E.2d at 663 (Mass. 1976); *see also supra* Section I.B.1.

168. *Wilkes*, 353 N.E.2d at 663.

169. *Id.*

170. *Id.*

171. *Id.* at 663.

172. If unsuccessful, the minority would then still have the opportunity to demonstrate a less restrictive alternative.

On the other hand, if the minority receives its shares after the formation of the corporation because of the majority's failure to place restrictions on the transfer of shares, then it is the majority, not the minority, who can blame only itself for the controversy arising from a disproportionate benefit given to majority shareholders. In keeping with a fault-based approach, the burden should be placed on the corporation to demonstrate not only a legitimate business purpose, but also the absence of a less restrictive alternative.[173] In theory, such an approach could have damaging effects on the economy because sound business decisions would sometimes be disallowed merely because the corporation could not prove that it could not have achieved a legitimate objective in some other way. However, in the long run, this approach would provide a further incentive for entrepreneurs to plan ahead at the formation of a close corporation to avoid potential conflicts that could result from outsiders obtaining part ownership in the corporation.

2. Buyout and Dissolution. In determining whether a buyout or dissolution should be ordered, a starting point is to realize the irrationality of insisting that the requirements for an order of dissolution first be satisfied before a buyout order is justified as a remedy less severe than dissolution. If a buyout is indeed a less severe remedy than dissolution, then it seems reasonable that a lesser standard of wrongdoing should have to be shown by a complaining shareholder to obtain a buyout remedy than that required to justify dissolution. Alaska should therefore make clear, through its supreme court or by statute, that the requirements for a buyout are less stringent than those needed for dissolution.

A judicially ordered buyout of a minority shareholder's shares is a much more severe remedy from the perspective of the corporation than an order to share benefits proportionately with the minority. The necessity of freeing up funds to purchase the minority's shares can deprive the corporation of the opportunity to pursue other investments and could force the selling off of currently held assets. The hardships likely to be faced by close corporations ordered to purchase an owner's shares are particularly severe in light of the fact that many close corporations are struggling businesses trying to get off the ground. Society certainly has an economic interest in seeing start-up businesses succeed and, just as importantly, in encouraging people to invest in start-up companies in the first place. Therefore, the buyout

173. *See Wilkes*, 353 N.E.2d at 663.

remedy should be available only when a pattern of conduct by the majority over time makes clear that a minority shareholder cannot hope to earn a fair return on her investment because conduct depriving her of benefits is likely to continue.

A court should be reluctant to grant a buyout remedy to a minority shareholder whose problems are in part of her own making for failure to secure a shareholders agreement to prevent unfair treatment by the majority. Nevertheless, there will be times when a minority shareholder will invest her money in a start-up close corporation and be ignorant of the ability or even the need to protect herself against freeze-out. If it becomes clear that such a shareholder is being persistently taken advantage of by the majority, a court should be willing to grant the buyout remedy in spite of the minority's blunder.

Analogously, a court should be more willing to grant the buyout remedy when a corporation has brought the attendant problems on itself by failing to restrict the transferability of its shares and thereby allowing the shares to fall into the hands of an outsider with whom the majority has little inclination to work. It would be going too far to say that, in such a situation, a complaining minority shareholder can automatically obtain a buyout anytime the majority confers upon one of its members a benefit not shared with the minority. Nevertheless, when a close corporation's problems are of its own making, a court should be less sympathetic to any difficulty the corporation may experience in summoning sufficient funds to buy back the minority's shares.

Dissolution is, as the court in *Alaska Plastics* noted, a remedy which is extremely harsh to the majority because it closes the business's doors.[174] Consequently, courts should grant the remedy only in extreme circumstances. Dissolution of the corporation should be ordered only when it is clear that, for some reason, the buyout remedy is insufficient to cure the minority's injuries. This situation might exist when, for example, a corporation simply does not have enough funds to purchase the minority's shares at anything approaching a fair price.

Again, the failure of the minority to protect its interests with a shareholders agreement should weigh against granting the minority relief (in this case, dissolution) at the expense of the majority.

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174. *See* Alaska Plastics, Inc. v. Coppock, 621 P.2d 270, 274 (Alaska 1980). An exception would exist in the case where the minority feels that, as the only bidders at an auction of corporate assets, it can start the business up again at a lower cost than would be the case in a buyout of the minority's shares. Presumably, however, this lower cost would come at the expense of the minority. This should make a court even less inclined to grant the dissolution remedy.

Likewise, the failure of the majority to protect itself by placing restrictions on the transfer of shares should weigh against the withholding of relief for the minority.

VII. APPLICATION OF THE ABOVE PRINCIPLES TO THE *COPPOCK* CASES

In obtaining her shares as part of a divorce settlement, it is doubtful that Patricia Muir had any opportunity to obtain protective provisions to guarantee any return on her interest in Alaska Plastics.[175]

However, the majority directors probably could have prevented Muir from obtaining her shares in the first place by placing a consent restraint on its shares. Alaska allows transfer restrictions,[176] which can be placed in the charter.[177] Most courts hold that general restrictions on the transfer of shares apply only to voluntary transfers.[178] Alaska's statute makes no distinction between voluntary and involuntary transfers of shares.[179] However, restrictions on transfers by operation of law may be valid if the restriction explicitly provides as such.[180]

Consequently, under the modified *Wilkes* test described above, once Muir demonstrated unequal treatment, the majority directors would have the burden to show both a legitimate business purpose for the treatment and that this purpose could not have been achieved through means less harmful to Muir.

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175. *See id.* at 272–73.

176. ALASKA STAT. § 10.06.424(a) (2006).

177. The restrictions, however, must be "reasonable." ALASKA STAT. § 10.06.210(2).

178. *See, e.g.*, *In re* Marriage of Devick, 735 N.E.2d 153, 162 (Ill. App. Ct. 2000); *see also* Mestayer v. Williams, 569 So. 2d 1102, 1106 (La. Ct. App. 1990) (holding that stock is part of the community property between husband and wife and thus that transfer restrictions on the shares were inapplicable to the wife's co-ownership of the shares). Unlike Louisiana, Alaska is not a community property state. *See* Clauson v. Clauson, 831 P.2d 1257, 1262 (Alaska 1992). Thus, the reasoning in *Mestayer* is inapplicable to the *Coppock* cases.

179. *See* ALASKA STAT. § 10.06.424(a) (2002).

180. *See, e.g.*, Bryan-Barber Realty, Inc. v. Fryar, 461 S.E.2d 29, 31–32 (N.C. Ct. App. 1995). In *Bryan-Barber*, as in the *Coppock* cases, a wife received her shares in a close corporation through a divorce settlement. *Id.* at 30. The court held: "[A] restriction on the transfer of stock does not apply to interspousal transfers of stock which is marital property *absent an express provision prohibiting such transfers*." *Id.* at 32 (emphasis added).

Muir would easily be able to demonstrate the existence of unequal treatment.[181] The majority conferred several benefits on itself that were not shared with Muir: the directors' fees, the salary paid Gillam, and the paying of the directors' wives' expenses out of company assets.[182]

For the first two of these unequal benefits, the directors would probably be able to demonstrate a legitimate business purpose: to encourage productive work on behalf of the corporation. It is doubtful that this incentive could be provided in any way other than financial compensation of the directors. Thus, unless Muir could show that the salary or fees were excessive, she likely would be unable to show that she was entitled to a *Donahue* remedy for the fees and salary.[183]

The payment relating to the directors' wives, however, is a different story.[184] It is doubtful that the directors of Alaska Plastics would be able to show any legitimate business purpose for the payments.[185] Even if they could, they would still have to demonstrate that this purpose could not have been achieved in a way less damaging to Muir. Theoretically, the directors could argue that the companionship of a director's wife on a business trip increases productivity, but this seems to be a stretch. More likely, the corporation would be required to, at the very least, share the benefits with Muir. Muir would have no use for a company policy allowing her to bring her spouse with her to shareholder meetings, but the payments, as hinted at in the *Alaska Plastics* opinion,[186] could be construed as constructive dividends, the value of which would have to be shared with Muir. After recompensing Muir, Alaska Plastics could cease the payment of constructive dividends or share an equivalent dollar amount with Muir.

A trickier question is whether the harmful conduct by the majority was so persistent that it should entitle Muir to a buyout of her shares. Although Muir was treated unfairly by the majority for a period of several years,[187] a sympathetic court might give the company a chance to cease paying constructive dividends to some shareholders but not others. However, the failure of Alaska

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181. *See* Alaska Plastics v. Coppock, Inc., 621 P.2d 270, 272–73 (Alaska 1980).

182. *Id.*

183. *See* Donahue v. Rodd Electrotype Co., 328 N.E.2d 505, 519 (Mass. 1975).

184. *See Alaska Plastics*, 621 P.2d at 272.

185. In fact, as noted above, in his testimony, Stefano conceded that there was no business purpose for bringing the wives to the shareholders meeting. *Id.*

186. *See id.* at 277.

187. *See id.* at 272–73.

Plastics to prevent the shares from falling into Muir's hands should weigh against any such leniency.

The failure to notify Muir of shareholders meetings is a less serious problem, given that there is no indication that Muir had any interest in the governance of the corporation.[188] Nevertheless, as a shareholder, Muir had the right to participate in meetings and vote on important matters, even if she was guaranteed to be out-voted every time. Therefore, the failure to notify Muir of meetings should weigh in favor of a buyout of Muir's shares.

In reality, a buyout of Muir's shares might be beneficial to both the majority and the minority. Although the majority directors might face some short-run difficulties in summoning the funds to purchase Muir's shares, in the long run they would probably be relieved to no longer have Muir as a shareholder. With Muir out of the way, the corporation could continue to pay constructive dividends without worrying about offending a non-director minority shareholder.

On the facts in the *Coppock* cases, there does not seem to be any justification for dissolution of the corporation.[189] Muir's injuries could be redressed just as well by a buyout of her shares at their fair value as by a liquidation of the company's assets.

VIII. CONCLUSION

Alaska could adopt any number of tests that would achieve substantially similar results to the test outlined above. Whatever test Alaska decides to adopt, it should ideally make its position on the protection of minority rights clear by statute. Disputes involving close corporations might not arise in Alaska very often, so it is understandable that the Alaska legislature has not seen fit to address these issues. Thus, it is up to the Alaska Supreme Court to step forward and establish clear principles regarding the protection of minority shareholders in close corporations.

Whatever test Alaska adopts regarding the protection of minority shareholders in close corporations, there are some general principles that should be followed. In determining the appropriate remedy for a complaining minority shareholder, a court should first allocate fault between the parties. The more at fault the majority is relative to the minority, the more willing a court should be to give the minority a remedy that is damaging to the majority. Fault can take a moral form, such as a violation of fiduciary duty, or a

188. *See id.*

189. *See, e.g., id.*; Stefano v. Coppock, 705 P.2d 443, 444–45 (Alaska 1985).

practical form, such as the failure of the minority shareholder to secure her rights through a shareholders agreement.

Also, Alaska must not be so generous to minority shareholders that it risks ruining profitable corporations or removing the incentive for entrepreneurs to start their own businesses. The larger economic interests of society must be considered.

With its small population and correspondingly small number of close corporations that could potentially be harmed by unwise rules of law, the supreme court is in a position to experiment; it should not be afraid to adopt a test substantially different than the ones present in other states. By keeping the above principles in mind, Alaska can fashion a policy whereby investors—both majority and minority—in close corporations know they will be treated fairly as long as they act prudently and in good faith.