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STATE OF MINNESOTA  
IN THE COURT OF APPEALS

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Arizant Inc., Arizant Healthcare Inc.,  
and Augustine Medical, Inc.,

Appellants,

vs.

Scott D. Augustine, M.D.,

Respondent.

---

APPELLANTS' BRIEF

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## LEGAL ISSUES

### **I. Did the trial court err in finding that Augustine's knowingly fraudulent conduct was unrelated to the "good faith" requirement of Minn. Stat. § 302A.521?**

The trial court held that Augustine's admissions of knowingly fraudulent conduct did not address the issue of good faith.

Bunge Corp. v. Recker, 519 F.2d 449 (8th Cir. 1975); Globus v. Law Research Serv., Inc., 418 F.2d 1276 (2d Cir. 1969); Raychem Corp. v. Fed. Ins. Co., 853 F. Supp. 1170 (N.D. Cal. 1994).

Minn. Stat. § 302A.521, subd. 2(a); Minn. Stat. § 302A.011, subd. 13.

### **II. Did the trial court err in refusing to apply collateral estoppel to prevent Augustine from relitigating the facts and issues already adjudicated by the Minnesota Federal District Court?**

The trial court held that Augustine was not collaterally estopped from claiming he had not committed intentional fraud and asserting that he acted in good faith.

Hauschildt v. Beckingham, 686 N.W.2d 829 (Minn. 2004); P.C.B., Jr. v. Cha, No. Civ. 03-6368MJDJGL, 2005 WL 1421465, at \*5 (D. Minn. June 17, 2005).

### **III. Did the trial court err in excluding key evidence of the dishonest/fraudulent conduct underlying Augustine's claim for indemnification?**

The trial court excluded evidence of Augustine's dishonest and fraudulent conduct as irrelevant.

Boland v. Morrill, 132 N.W.2d 711 (Minn. 1965); Foust v. McFarland, 698 N.W.2d 24 (Minn. Ct. App. 2005); Ulmer v. Associated Dry Goods Corp., 823 F.2d 1278 (8th Cir. 1987).

Minn. R. Evid. 401 and Committee Comment.

### **IV. Did the trial court err in refusing to allow Arizant to cross-examine and impeach Augustine about the underlying intentional misconduct?**

The trial court refused to allow Arizant to cross-examine and impeach on numerous occasions.

Murray v. Walter, 269 N.W.2d 47 (Minn. 1978); Bartosch v. Lewison, 413 N.W.2d 530 (Minn. Ct. App. 1987); Riewe v. Arensen, 381 N.W.2d 448 (Minn. Ct. App. 1986); Weyers v. Lear Operations Corp., 359 F.3d 1049 (8th Cir. 2004).

Minn. R. Evid. 607; Minn. R. Evid. 611(b).

**V. Did the trial court err in failing to instruct the jury regarding the legal definition of “good faith?”**

Arizant’s proposed jury instructions were rejected by the trial court.

Peterson v. BASF Corp., 711 N.W.2d 470 (Minn. 2006); Miller v. Byrne, 916 P.2d 566 (Colo. Ct. App. 1995); Cooper v. TWA Airlines, LLC, 274 F. Supp. 2d 231 (E.D.N.Y. 2003).

Minn. R. Civ. P. 49.01(a).

**VI. Did the trial court err by failing to determine, as a matter of law, that it was “fairly inferable” from the Separation Agreement that the independent appraisal issued by Harris Nesbitt effective March 31, 2004 was binding and conclusive?**

The trial court held that the jury was to construe the Separation Agreement and decide whether the parties “expressly stipulated” that the appraisal was to be conclusive.

Sanitary Farm Dairies, Inc. v. Gammel, 195 F.2d 106 (8th Cir. 1952); PVI, Inc. v. Ratiopharm, 253 F.3d 320 (8th Cir. 2001); Nelson v. Charles Betcher Lumber Co., 93 N.W. 661 (Minn. 1903).

**VII. Did the trial court err in still submitting Augustine’s Appraisal Challenge claim to the jury when, at the close of evidence, Augustine had offered no evidence of ambiguity as to the Separation Agreement?**

The trial court submitted the issue to the jury.

Rognrud v. Zubert, 165 N.W.2d 244 (Minn. 1969); In re Ocwen Fin. Servs., Inc., 649 N.W.2d 854 (Minn. Ct. App. 2002).

**VIII. Did the trial court err in failing to give appropriate jury instructions and include necessary questions on the Special Verdict Form relating to Augustine’s Appraisal Challenge claim?**

The trial court rejected Arizant’s proposed jury instructions and proposed special verdict questions.

Minn. R. Civ. P. 49.01(a).

**IX. Did the trial court err in awarding attorney fees in the amount of \$135,768.25 to Augustine?**

The trial court awarded attorney fees in the amount of \$135,768.25 to Augustine pursuant to Minn. Stat. § 302A.467.

Kallok v. Medtronic, Inc., 573 N.W.2d 356, 363 (Minn. 1998); Powell v. Anderson, No. C5-99-1755, 2003 WL 22705878, at \*1 (Minn. Ct. App. Nov. 18, 2003); Foy v. Klapmeier, 922 F.2d 774 (8th Cir. 1993).

Minn. Stat. § 302A.467; Minn. Stat. § 302A.521.

## STATEMENT OF CASE AND FACTS

### **I. STATEMENT OF THE CASE**

**A. Trial Court:** Hennepin County District Court

**B. Trial Judge:** Judge Harry S. Crump

**C. Nature of Case and Disposition**

At trial, Plaintiff/Appellee Scott D. Augustine, M.D. (“Augustine”) sought recovery on two separate and unrelated claims against his former employer, Defendants/Appellants Arizant Inc., Arizant Healthcare Inc., and Augustine Medical, Inc.<sup>1</sup> Augustine’s initial claim sought corporate indemnification under Minn. Stat. § 302A.521, Subd. 2(a) for a criminal fine he paid after being adjudicated guilty of knowing and willful actions constituting Medicare fraud. Augustine’s second claim sought to challenge a contractually-required independent appraisal in order to receive larger “Phantom Stock” bonuses under his December 31, 2002 Separation and Release Agreement (“Separation Agreement”) with Arizant. Each claim involves a separate and unrelated set of facts, and each claim was handled separately, both during summary judgment and at trial.

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<sup>1</sup> Appellants Arizant Healthcare Inc., and Augustine Medical, Inc. are subsidiaries of defendant Arizant Inc. For purposes of this brief, the three Appellants will be collectively referred to as “Arizant.”

## 1. Indemnification for intentional fraud

Augustine, the former Chief Executive Officer of Augustine Medical, Inc., claimed that he was entitled to statutory indemnification for a \$2 million criminal fine he paid as a result of his Medicare fraud conviction. Augustine's Stipulation of Facts in connection with his guilty plea, along with subsequent sworn testimony in open court, resulted in the Federal District Court's express adjudication that Augustine knowingly and willfully aided others in withholding from healthcare providers a material fact for use in determining rights to benefits and payments under Medicare (the "TriSpan Fraud").

Appellant Arizant asserted below during summary judgment, in post-trial motions, and reasserts here that because of Augustine's admissions and the Federal District Court's adjudication that he willfully and knowingly engaged in inherently dishonest conduct, he is precluded, as a matter of law, from meeting the standards of Minnesota's indemnification statute, Minn. Stat. § 302A.521. Arizant argued that while the mere fact of Augustine's conviction, standing by itself, does not preclude indemnification under the statute, a prior final adjudication of knowing and willful fraudulent conduct conclusively establishes lack of good faith under Minnesota law. "Good faith" is statutorily defined as "honesty in fact." Honesty, in turn, is defined as "not fraudulent." Thus, fraudulent conduct by definition involves a lack of honesty and cannot, by law, meet the definition of "good faith."

Nevertheless, the trial court held that Augustine was entitled to have a jury examine whether Augustine's conduct relative to his TriSpan Fraud met the good faith requirements of § 302A.521. The trial court then compounded its error by barring Arizant from introducing the very evidence of Augustine's underlying intentional misconduct,

which occurred in August 2000, holding that this evidence was irrelevant. Even after Augustine testified selectively about his lack of knowledge and/or involvement in the August 2000 misconduct, Arizant was barred from impeaching Augustine as to that testimony.

At the close of trial, the trial court failed to properly instruct the jury regarding the standard for “good faith” under Minn. Stat. § 302A.521. Without all of the relevant evidence and with inadequate instruction as to the applicable law, the jury found that Augustine was entitled to full indemnification for his \$2 million fine. The trial court upheld this finding despite Arizant’s motion for judgment as a matter of law or, alternatively, for a new trial.

## **2. Appraisal Challenge**

In a separate claim, Augustine sought approximately \$3.5 million in additional annual cash bonus payments under a “Phantom Stock Payment” provision in his Separation Agreement. Under the Separation Agreement, Augustine’s Phantom Stock Payments were calculated based upon an annual appraisal of Arizant’s shares conducted by an independent third-party appraiser. Augustine claimed that Harris Nesbitt, the Chicago-based independent appraisal firm hired to complete the March 31, 2004 appraisal of Arizant, undervalued Arizant by not sufficiently considering Arizant’s sale to a third party which occurred months after the valuation date.

On summary judgment and in post-trial briefing, Arizant cited controlling Minnesota law that when an intention to be bound by an appraiser’s valuation is “fairly inferable” from the plain language of a contract, courts and juries are prohibited from second-guessing an appraiser’s valuation absent a finding of fraud, corruption, or

malfeasance on the part of the appraiser. Arizant argued that it was “fairly inferable” from the unambiguous language of the Separation Agreement that the parties intended for the appraiser’s valuations to be binding. The trial court denied summary judgment and applied an improperly high legal standard:

Genuine issues of material fact exist as to whether the Separation and Release Agreement signed between Plaintiff Augustine and Defendants Augustine and Arizant regarding Plaintiff Augustine’s “Phantom Stock” valuation **expressly stipulated** that the appraisal was to be conclusive.

(emphasis added).

At trial, neither party offered evidence to establish any ambiguity in the Separation Agreement’s appraisal clause. In fact, the trial court sustained Augustine’s objections and precluded Arizant from offering any evidence on the interpretation of the Separation Agreement’s appraisal clause. Rather than construing the appraisal clause and applying controlling law to its unambiguous language, the trial court sent the claim to the jury. The trial court then failed to adequately instruct the jury as to the appropriate legal standard and refused to include necessary predicate questions on the Special Verdict Form. Without adequate instruction, the jury essentially split the difference between the independent appraiser’s valuation and the per-share price paid by a buyer of the company months after the appraiser’s valuation was performed. Based on the jury’s own independent determination of Arizant’s per-share “fair market value,” Augustine received \$1,237,851.75 in damages on this issue. The trial court upheld this finding in post-trial proceedings.

### 3. Attorney fees

Following trial, Augustine sought his attorney fees related to his indemnification claim, relying exclusively on Minn. Stat. § 302A.467, which allows, on a limited basis, a

discretionary award of attorney fees in actions “brought by a shareholder” against the directors of a corporation. Augustine argued that because he happened to be a former shareholder of Arizant, this statute entitled him to attorney fees, even though none of his claims related to his status as a former shareholder. In fact, Augustine’s suit was based solely on his position as a former officer of Arizant and was actually brought against the company and its shareholders. Nevertheless, the trial court awarded Augustine \$135,768.25 in attorney fees under § 302A.467.

## II. STATEMENT OF FACTS

### A. Augustine’s Indemnification Claim

#### 1. Arizant’s policy to disclose TriSpan coverage decisions to healthcare providers

Since the late 1990s, Augustine, then the Chief Executive Officer of Arizant, was involved in efforts to promote and obtain Medicare coverage for Arizant’s Warm-Up® Therapy Product (“Warm-Up”), which included initiatives to obtain favorable coverage decisions from regional fiscal intermediaries. (A638, A652-53). A “fiscal intermediary” is an entity tasked by the federal government to make coverage decisions as to whether healthcare providers purchasing Warm-Up would be reimbursed by Medicare. (A667-68). TriSpan Health Services (“TriSpan”) was one of those governmental fiscal intermediaries. (A667).

In November 1999, Augustine and Arizant became aware of a letter from TriSpan stating that “Medicare will not allow coverage of Warm-Up at this time.” (A439, A617, A668-69). Despite internally believing that this 1999 TriSpan letter was incorrect, Arizant adopted the policy of: (1) immediately contacting TriSpan for clarification and (2) disclosing the 1999 TriSpan letter to affected healthcare providers who may purchase

or use Warm-Up. (A439, A443, A617, A670-71, A710-12). As of December 1999, if Arizant learned that a healthcare provider was in TriSpan's territory, Arizant would fully disclose the existence of the TriSpan Warm-Up coverage exclusion, even though Arizant continued to disagree with the decision. Arizant's policy in this regard was consistent with the advice of Arizant's internal attorney, Randy Benham, at that time. (A443, A711-15).

**2. In June 2000, Augustine tells providers like Southern Medical that TriSpan now covering Warm-Up**

Augustine and his team met with TriSpan on January 14, 2000 in an attempt to change TriSpan's position denying Warm-Up coverage. (A445-46, A672, A715-16). Augustine was the lead presenter. (A445-46, A672).

By May 2000, Augustine's team believed its efforts had been successful and that TriSpan had changed its mind and would now cover Warm-Up. (A673, A716). Based on oral statements by TriSpan to Augustine's team that Warm-Up would now be covered, Augustine directed his team to launch an aggressive campaign to inform all healthcare providers in TriSpan's region that TriSpan was now covering Warm-Up. (A673). This campaign was in full swing by June 2000. (A673). One of those providers was Southern Medical Distributors ("Southern Medical"). (A673).

Southern Medical was seen by Augustine and Arizant as a significant potential purchaser of Warm-Up, having placed an initial order for over \$30,000 of product.<sup>2</sup> (A448, A673-74). On June 22, 2000, Augustine and his team met with Southern Medical as part of the campaign involving providers in TriSpan's region. (A448, A673-74).

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<sup>2</sup> Unbeknownst to Augustine, Southern Medical was in reality a governmental sting operation, posing as a distributor of healthcare products. (A740-67).

**3. New TriSpan letter on June 27, 2000 was a “total about face”**

On June 27, 2000, five days after the June 22 meeting with Southern Medical, Augustine received a letter from TriSpan dated June 19, 2000 that now characterized Warm-Up as “investigational.” (A447, A450-51, A675). Contrary to Augustine’s expectations, the letter did not say TriSpan would cover Warm-Up. (A447, A675-76). On June 28, 2000, the member of Augustine’s team who had been talking to TriSpan told Augustine that the June 2000 TriSpan letter was a “total about face from every verbal communication” with TriSpan and that investigational “general[ly] mean[s] that they won’t cover it until additional studies are completed.” (A449, A610, A676).

Initially, Augustine’s team had questions about whether TriSpan would use the new “investigational” finding to deny claims for Warm-Up. (A608-09, A611). Because of this uncertainty, Randy Benham, Arizant’s internal counsel, initially advised Arizant not to disclose the letter to providers until it knew if TriSpan was in fact using the “investigational” finding to deny claims. (A717-18). On July 10, 2000, Benham was told by a customer that TriSpan was now denying claims for reimbursement based on Warm-Up’s investigational status. (A452, A718). As a result, after July 10, 2000, Benham advised Augustine and Arizant that the new June 2000 TriSpan letter should be disclosed to all providers in TriSpan’s territory. (A719-21).

Similarly, by July 18, 2000, Arizant’s management confirmed that Arizant would again follow the 1999 policy of clarification and disclosure. (A473, A608-09, A613-15, A621-22). John Thomas, CEO of Arizant at the time, testified that as of July 18, 2000, it was not Arizant’s policy to hide the TriSpan letter or to deny it existed. (A621-22). Thomas testified that “...we were going to find out what [the letter] meant and we were

going to do the right thing.” (A611-12). As of July 18, 2000, “if anybody asked us about [the TriSpan letter] we’d tell them straight out just exactly that we had gotten a letter and what it was.” (A608-09, A621-22).

**4. Contrary to Arizant’s Policy, in August 2000 Augustine helps Hensley hide the new TriSpan letter from Southern Medical**

In August 2000, without Arizant’s knowledge, Augustine and his team intentionally withheld the June 2000 TriSpan letter from Southern Medical. Acting mainly in concert with his subordinate, Tim Hensley, Augustine ignored the established Arizant policy and intentionally helped hide the 2000 TriSpan letter from Southern Medical.

Arizant’s first meeting with Southern Medical after the June 27, 2000 negative TriSpan letter was on August 16, 2000, in Atlanta, Georgia. (A683-88). During that August 16, 2000 meeting, Hensley failed to disclose the June 2000 TriSpan letter. (A92, A114, A119, A127-29). In his deposition, Augustine testified that it was possible he knew that Hensley and others met with Southern Medical on August 16, 2000 in Atlanta. (A193). He testified he very well could have talked to Hensley about what to do with Southern Medical before he went to meet with them in August 2000, and that it was possible that he talked to Hensley about follow-up with Southern Medical. (A207-08).

On August 21, 2000, Hensley had a follow-up phone call with Southern Medical about the August 16, 2000 Atlanta meeting. (A33-53, A683-88). When specifically questioned about any letter from TriSpan, Hensley flatly denied that Arizant had received any correspondence from TriSpan. (A33, A41, A616).

MR. EDWARDS: Well, okay, but basically right now, Tim, you don't have anything from Tri-Span saying, yeah, go ahead, we approve it or anything like that . . .?

MR. HENSLEY: We don't have anything in writing.

MR. EDWARDS: Okay. All right. But y'all made a presentation, they were impressed, but you haven't gotten anything in writing?

MR. HENSLEY: True.

MR. EDWARDS: Okay. Good or bad; huh?

MR. HENSLEY: No.

(A41). In his deposition testimony, Augustine testified that Hensley may have talked to him after the August 21, 2000 meeting about denying that Arizant had received anything in writing, good or bad, from TriSpan. (A208).

On June 29, 2004, Hensley and Augustine pleaded guilty to Medicare Fraud related to failure to disclose the TriSpan letter to Southern Medical. (A84-91). During Hensley and Augustine's Change of Plea hearing on June 29, 2004, Hensley first took the stand and testified that the intentional withholding of the TriSpan letter from Southern Medical took place during the August 16, 2000 Atlanta meeting. (A92, A114-29).

Q. Sir, on or about August 16th of 2000, did you attend a meeting in Atlanta, Georgia with representatives of Southern Medical?

A. Yes, sir, I did.

Q. And at that meeting, did you not disclose the June 27th Dr. May letter to Southern Medical Distributors?

A. That is correct. I did not disclose the letter.

Q. And, sir, by entering into this stipulation of facts, do you agree that you withheld from Southern Medical Distributors a material fact for use in determining rights to benefits and payments under the Medicare program?

A. Yes, sir.

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(A128). Augustine, who was present for this sworn testimony by Hensley, then took the stand and testified he had knowingly aided and abetted Hensley's misconduct (A92, A129-45):

Q. Shortly after receipt of that [June 27, 2000 TriSpan] letter, is it the case that you intentionally and knowingly aided and abetted others in deciding not to disclose that letter in general to providers?

A. Yes.

Q. And by entering into this stipulation of facts, you admit that the facts set forth in this stipulation establish that you knowingly and intentionally aided and abetted the offense of 42 U.S.C., Section 1320a-7b(a)(2), by causing to be withheld from Southern Medical Distributors a material fact for use in determining rights to benefits and payments under the Medicare program?

A. Yes, I did.

(A143).

On June 29, 2004, Augustine also entered into a Stipulation of Facts, which became adjudicated findings of fact by the Federal District Court. (A84-91). Those findings of fact include:

3. On or about June 27, 2000, Defendant Scott D. Augustine received a letter from TriSpan Health Services, a fiscal intermediary of the Medicare program which had earlier approved coverage for WarmUp. TriSpan had now determined that WarmUp was investigational. Defendant believed that this determination was material.

4. Shortly thereafter, the Defendant knowingly and intentionally aided and abetted others in deciding not to disclose the June 27<sup>th</sup> letter to Southern Medical Distributors.

5. By entering into this Stipulation of Facts, the Defendant admits that the facts set forth herein establish that he knowingly and intentionally aided and

abetted the offense 42 U.S.C. Section 1320a-7b(a)(2) as set forth in an Information filed and is in fact guilty of that offense.

(A90-91).

At sentencing on September 8, 2004, Federal District Court Judge Montgomery noted that Augustine had “demonstrated recognition and affirmative acceptance of personal responsibility for his conduct.” (A160). In fact, the government recommended that Augustine’s sentence be reduced because he had accepted personal responsibility for his criminal conduct. (A84-90, A692).

On September 15, 2004, Judge Montgomery entered judgment against Augustine. (A165-68, A694-95). In the Judgment, the court “adjudicated that [Augustine] is guilty of withholding a material fact for use in determining rights and payments under a federal healthcare program.” (A165, A694-95). As a further result of Augustine’s admissions and criminal conviction, the United States Department of Health and Human Services has excluded him from dealing with Medicare for five years. (A696-97).

## **B. Augustine’s Appraisal Challenge Claim**

### **1. Augustine’s 2002 Separation Agreement**

In 2002, Augustine entered into an agreement related to his separation from Arizant. The 2002 Separation Agreement included a “Phantom Stock Payment” bonus provision. (A245-56). Under the Phantom Stock Payment provision, Arizant agreed to pay ten annual cash bonus payments to Augustine for fiscal years 1998 through 2007. (A245-56). Section 5 of the 2002 Separation Agreement states in its pertinent parts:

5. Phantom Stock Payment. For each of the ten (10) full fiscal years through and including the fiscal year ending March 31, 200[7], Dr. Augustine will be eligible to receive an annual cash bonus (the “Phantom Stock Payment”) based on increases in the Fair Market Value (as defined

below) of the Company's common stock, \$.01 par value (the "Common Stock") from \$25.30 per share (the initial "Common Stock Trigger Price"). The amount of any Phantom Stock Payment paid to Dr. Augustine for any fiscal year will be equal to the excess, if any, of the Fair Market Value of one share of Common Stock as of the end of such fiscal year over the applicable Common Stock Trigger Price (as adjusted pursuant to Section [5](c) below) multiplied by a number equal to the number of Phantom Shares (as determined below) then held by Dr. Augustine.

\* \* \*

(b) Determination of Fair Market Value. For purposes of this Agreement, the fair market value of Common Stock (the "Fair Market Value") will be determined as follows:

(i) Unless the Common Stock is registered under the Securities Exchange Act of 1934 and the Common Stock is either listed on a stock exchange or transactions in the Common Stock are reported on the Nasdaq System, within 60 days after the end of each fiscal year the Company will complete an appraisal of the value of the Common Stock, which appraisal will be conducted by an appraiser selected by the Board. The Fair Market Value of the Common Stock will be an amount determined by such appraisal . . . .

(A245-56).

Under the Separation Agreement, each of the ten annual cash bonus payments was to be calculated based on the change in the Fair Market Value of one share of Arizant stock between March 31 of the prior year and March 31 of the current year, multiplied by the 25,000 "Phantom Shares" provided to Augustine. (A245-56). Because Arizant was not publicly traded and, therefore, lacked a public share quote for its stock, the Fair Market Value for one share of Arizant stock "**will be an amount determined by an independent, third-party appraiser selected by [Arizant's] board.**" (A245-56). The 2002 Separation Agreement provides no mechanism for either party to challenge or question the Fair Market Value determined by that appraiser. (A245-56).

At trial, no evidence was offered by Augustine to suggest that the Separation Agreement means anything other than what its clear terms state. In fact, on Augustine's objection on parol evidence grounds, Marie Humbert, Arizant's Chief Financial Officer and then later Vice President of Finance, was precluded from giving testimony on the meaning of § 5(b). (A549). During Arizant's cross-examination of Augustine, Augustine's counsel again prevailed on a parol evidence objection regarding the valuation clause. (A698-99). Various other exhibits relating to negotiations and drafting of § 5(b) of the Separation Agreement were also rejected as inappropriate parol evidence. (A434-35, A436-38, A474-86, A543-48, A700-01, A708, A709).

## **2. 1998 to 2003 Phantom Stock Payments**

In accordance with the 2002 Separation Agreement, Arizant's Board of Directors hired reputable independent appraisal firms to determine the "Fair Market Value" of the company's stock as of March 31 for each year beginning in 1998. Piper Jaffray, a Minneapolis-based investment bank, conducted the appraisals from 1998 to 2002. (A703). Harris Nesbitt, a Chicago-based investment bank, conducted the appraisal for 2003. (A605, A705-06). Augustine's trial expert, Phil Williams, agreed that each appraisal applied an appropriate marketability/liquidity discount reflecting the company's privately held status, and an appropriate minority discount reflecting the fact that one share would not include the "control premium" associated with ownership of the entire company. (A602-04, A606-07). The Fair Market Value appraisals, together with the percent increase from the prior year and the payments to Augustine are as follows:

<b>Fiscal Year Ended March 31</b>	<b>FMV Appraisal</b>	<b>Percent Increase over Prior Year</b>	<b>Payment Made to Augustine</b>
1998	\$28.50	23.91%	\$80,000
1999	\$30.00	5.26%	\$37,500
2000	\$30.00	0.00%	\$0
2001	\$30.00	0.00%	\$0
2002	\$26.00	-13.33%	\$0
2003	\$31.00	19.23%	\$25,000

(A550-55). Augustine never objected to those appraisals by Piper Jaffray and Harris Nesbitt. (A702, A704, A706).

### **3. Attempted sale of Arizant**

In the fall of 2003, Arizant entered an auction process administered by JP Morgan to find a buyer for Arizant. (A623-24). By March 2004, after two rounds of bids, no would-be bidder was willing to purchase Arizant while Arizant remained a defendant and exposed to the risks associated with the Department of Justice prosecution of Arizant, Augustine, and the other individuals (“DOJ Matter”). (A724). As of March 31, 2004, there was no clear path for a successful resolution of the DOJ Matter and, thus, no reasonable likelihood that any bidder would purchase Arizant. (A565-66, A625-33). This situation brought the auction process to a halt as of March 31, 2004. (A725).

### **4. Harris Nesbitt’s March 31, 2004 Appraisal**

In 2004, Arizant’s Board again selected Harris Nesbitt to conduct the March 31, 2004 appraisal of one share of Arizant stock. (A726-27). Harris Nesbitt conducted the 2004 appraisal following the same methodologies it had employed in 2003 and Piper Jaffray had employed from 1995 to 2002. (A722-23). Harris Nesbitt requested and received all information pertinent to valuation of Arizant common stock, including detailed information regarding recent efforts to sell the company, which it reviewed and

considered in the course of its appraisal. (A729-35). At trial, Williams acknowledged that he had no opinion that Harris Nesbitt failed to gather or consider the appropriate information during its 2004 appraisal. (A605-06).

No one at Arizant directed Harris Nesbitt to apply any discounts in the 2004 appraisal. Rather, Harris Nesbitt alone determined the appropriate discounts for lack of marketability and minority ownership to be applied as of March 31, 2004, consistent with its past, customary practice. (A557-64). Nesbitt considered the attempted sale of Arizant and was given no instruction on how to factor the attempted sale into the discounts. (A728, A736-37).

On May 20, 2004, Harris Nesbitt issued its appraisal of the Fair Market Value of one share of Arizant Common Stock as of March 31, 2004. (A487-542). In its opinion, Harris Nesbitt set the Fair Market Value at \$37.00 to \$41.00 per share with a mid-point of \$39.00 per share. (A487-542). This value was used as the basis for calculating Augustine's 2004 Phantom Stock Payment in accordance with the 2002 Separation Agreement  $[(\$39.00 - \$31.00) \times 25,000 = \$200,000]$ . (A707).

At trial, no evidence was introduced that showed there was any fraud in connection with the Harris Nesbitt March 31, 2004 appraisal. (A633-37). Marie Humbert testified that Arizant did not push for a low appraisal by Harris Nesbitt. (A555-56). After his thorough review and critique of Harris Nesbitt's appraisal, Augustine's expert, Williams, offered no opinion that the Harris Nesbitt appraisal was a product of improper instruction or fraud.

## ARGUMENT

### I. SUMMARY OF ARGUMENT

With respect to Augustine's claim for indemnification, the trial court erred in failing to rule during summary judgment, at the close of evidence, and during post-trial motions that, as a matter of law, Augustine's prior adjudication of knowing and willful fraudulent conduct precluded him from receiving indemnification under Minn. Stat. § 302A.521.

The "good faith" standard of Minn. Stat. § 302A.521 is defined by statute as "honesty in fact." Conduct involving fraud or other knowingly dishonest or untruthful conduct fails, as a matter of law, to meet that standard. And where knowing and intentional dishonest conduct is previously and conclusively adjudicated against a corporate wrongdoer, as was the case with Augustine, collateral estoppel precludes that individual from later arguing that his conduct was not dishonest and was actually in "good faith."

Allowing the indemnification claim to proceed to a jury trial was reversible error. The trial court then compounded its error by excluding critical evidence of Augustine's underlying misconduct and by failing to properly instruct the jury regarding Augustine's indemnification claim.

With respect to Augustine's appraisal challenge claim, the trial court failed to apply controlling law and dismiss Augustine's claim as a matter of law on summary judgment, at the close of evidence, and during post-trial motions. Under Minnesota law and under the Separation Agreement, Augustine had no legal ability to request a judicial review of the independent appraiser's determination of Arizant's Fair Market Value on

March 31, 2001. The trial court furthered its error by failing to instruct the jury on the controlling law regarding independent appraisals and failed to include necessary questions on the Special Verdict Form.

## **II. STANDARD OF REVIEW**

### **A. Review of Summary Judgment Rulings**

The trial court erred in failing to grant summary judgment in favor of Arizant on both of Augustine's claims. On an appeal from summary judgment, an appellate court asks two questions: (1) whether there are any genuine issues of material fact and (2) whether the lower court erred in its application of the law. State by Cooper v. French, 460 N.W.2d 2, 4 (Minn. 1990). Furthermore, review of a summary judgment decision relates to a legal conclusion, and is thus reviewed *de novo* by the appellate court. Lefto v. Hoggsbreath Enters., Inc., 581 N.W.2d 855, 856 (Minn. 1998) (internal citation omitted).

### **B. Review of Failure to Rule as a Matter of Law**

The trial court erred at the close of evidence in failing to hold that intentional fraudulent conduct can not constitute good faith conduct and that the factual findings from Augustine's criminal conviction have collateral estoppel effect. The trial court also erred at the close of evidence in failing to apply the clear and unambiguous language of the Separation Agreement and in failing to apply controlling law to preclude Augustine from submitting his appraisal challenge claim to the jury.

An appellate court reviews the denial of a motion for judgment as a matter of law *de novo*. Pouliot v. Fitzsimmons, 582 N.W.2d 221, 244 (Minn. 1998). Similarly, the application of law to stipulated facts is a question of law, which an appellate court reviews *de novo*. Morton Bldgs., Inc. v. Commissioner of Revenue, 488 N.W.2d 254, 257

(Minn. 1992). Specifically, the availability of collateral estoppel is a mixed question of law and fact subject to *de novo* review. Falgren v. State, Bd. of Teaching, 545 N.W.2d 901, 905 (Minn. 1996). A reviewing court is not bound by and need not give deference to a district court's decision on a purely legal issue. Frost-Benco Elec. Ass'n v. Minnesota Pub. Utils. Comm'n, 358 N.W.2d 639, 642 (Minn. 1984).

### C. Review of Error in Excluding Evidence

The trial court erred in excluding critical evidence of Augustine's underlying intentional fraudulent conduct on relevancy grounds and then precluding Arizant from cross-examining and impeaching Augustine when he himself raised these same issues. The evidence was relevant, and in any case, Augustine opened the door to cross-examination and impeachment. The trial court thus abused its discretion.

The question of whether to admit or exclude evidence is within the district court's discretion, and a district court will be reversed if there is an abuse of discretion. Kroning v. State Farm Auto. Ins. Co., 567 N.W.2d 42, 45-46 (Minn. 1997). Exclusion of relevant evidence is often reversible error. See, e.g., Myers v. Winslow R. Chamberlain Co., 443 N.W.2d 211, 216 (Minn. Ct. App. 1989); Donaldson v. Pillsbury Co., 554 F.2d 825, 833-34 (8th Cir. 1977); MDU Res. Group v. W.R. Grace and Co., 14 F.3d 1274, 1280 (8th Cir. 1994); Behlke v. Conwed Corp., 474 N.W.2d 351, 356-57 (Minn. Ct. App. 1991). Exclusion of evidence for impeachment and cross-examination purposes is also often grounds for reversal. See, e.g., Riewe v. Arensen, 381 N.W.2d 448, 455-56 (Minn. Ct. App. 1986); Weyers v. Lear Operations Corp., 359 F.3d 1049, 1054-56 (8th Cir. 2004); Westcott v. Crinklaw, 68 F.3d 1073, 1077-78 (8th Cir. 1995); Newton v. Ryder Transp. Servs., Inc., 206 F.3d 772, 775-76 (8th Cir. 2000).

#### **D. Review of Failure to Adequately Instruct the Jury**

The trial court erred in refusing to instruct the jury on the applicable meaning of “good faith” and the controlling law related to Augustine’s appraisal challenge claim. Arizant was entitled to these instructions as an explanation of the law, and the trial court’s refusal was fundamental error and prejudicial.

Error in a jury instruction may be fundamental if the instruction or lack thereof destroys the substantial correctness of the entire jury charge, results in a miscarriage of justice, or leads to substantial prejudice of a party. Lindstrom v. Yellow Taxi Co., 214 N.W.2d 672, 676 (Minn. 1974). Where instructions do not fairly and correctly state the applicable law, an appellate court will grant a new trial. Alevizos v. Metropolitan Airports Comm’n, 452 N.W.2d 492, 501 (Minn. Ct. App. 1990).

### **III. INDEMNIFICATION FOR INTENTIONAL FRAUD**

#### **A. Trial court erred in permitting Augustine to litigate the issue of “good faith”**

##### **1. Intentional fraud can never be good faith**

Under Minnesota law, Augustine is permitted to receive corporate indemnification from Arizant only if he can affirmatively establish that his questioned conduct met all five criteria set forth in Minn. Stat. § 302A.521, Subd. 2(a), including that he “(2) acted in good faith.” “Good faith means honesty in fact in the conduct of the act or transaction concerned.” Minn. Stat. § 302A.011, Subd. 13.

Under the indemnification statute, the mere fact of a judgment, order, settlement, conviction or a plea of *nolo contendere* does not, itself, establish that an individual failed to meet the standard. Minn. Stat. § 302A.521, Subd. 2(b). Thus, the legal inquiry focuses not on the fact of a conviction, but on the honest or dishonest nature of the conduct giving

rise to the conviction. Here, Arizant asked the trial court and now asks this Court to hold, as a matter of law, that an individual who admits to and who is adjudicated to have engaged in intentional dishonest conduct, such as intentionally and knowingly withholding material facts from health providers, cannot meet the good faith requirement of the indemnification statute.

Minnesota courts have not directly faced how good faith under the indemnification statute relates to a prior adjudication of intentional fraud. However, the common usage of “good faith” means “freedom from intention to defraud.” Black’s Law Dictionary 477 (6th Ed. 1983). Moreover, the Minnesota statute itself defines “good faith” as “honesty in fact.” “Honest,” in turn, is defined as “not fraudulent.”<sup>3</sup> Therefore, intentional fraud, by definition, can never be “honesty in fact,” and a corporate officer adjudicated to have committed intentionally fraudulent acts may not, as a matter of law, receive indemnification for that conduct under Minn. Stat. § 302A.521, Subd. 2(a).

Courts in states that have faced the issue routinely recognize that fraudulent acts by a corporate officer, by definition, constitute bad faith. See, e.g., Bunge Corp. v. Recker, 519 F.2d 449, 452 (8th Cir. 1975) (“[m]any other courts have held that bad faith is synonymous with ‘fraud’ . . . [b]ad faith generally implies or involves actual or constructive fraud or a design to mislead or deceive another”); see also Globus v. Law Research Serv., Inc., 418 F.2d 1276, 1288 (2d Cir. 1969) (noting that corporations are

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<sup>3</sup> Webster’s II New Riverside Dictionary, Revised Edition 331 (Houghton Mifflin Co. 1996). Minnesota courts routinely consult dictionaries in defining statutory terms. See In re Wren, 685 N.W.2d 721, 724 (Minn. Ct. App. 2004) (citing Fiveland v. Bollig & Sons, Inc., 436 N.W.2d 478, 480 (Minn. Ct. App. 1989) (using dictionary to interpret statutory term “defective”)); Brandt v. Hallwood Mgmt. Co., 560 N.W.2d 396, 399-400 (Minn. Ct. App. 1997) (using Webster’s Dictionary to define “construction”).

barred from indemnifying a director for securities fraud because such action is against public policy); Raychem Corp. v. Fed. Ins. Co., 853 F. Supp. 1170, 1177 (N.D. Cal. 1994) (noting that it is only appropriate to permit indemnification for fraud when the claimant settles without admitting wrongdoing); Frick v. McClelland, 384 Pa. 597, 122 A.2d 43, 45 (1956); Commonwealth v. Smith, 242 Ky. 365, 46 S.W.2d 474, 478 (1923); Pabst Brewing Co. v. Nelson, 108 Okl. 286, 236 P. 873, 875 (1925); Polikoff v. Fin. Serv. Co., 205 N.C. 631, 172 S.E. 356, 358 (1934); Bansbach v. Zinn, 801 N.E.2d 395, 769 N.Y.S.2d 175 (N.Y. Ct. App. 2003); Pilipiak v. Keyes, 286 A.D.2d 231, 231-32, 729 N.Y.S.2d 99 (2001) (finding under a nearly identical statute that if a judgment or conviction includes a finding of deliberate dishonesty or bad faith, indemnification is precluded as a matter of law).

In addition, courts in other jurisdictions nearly uniformly hold that fraud is synonymous with bad faith. See Nordstrom, Inc. v. Chubb & Son, Inc., 54 F.3d 1424, 1434 (9th Cir. 1995) (citing case that stated that a controlling person who approves actions constituting fraud activity cannot invoke a good faith defense, in action by corporation seeking payment under directors' and officers' liability policy); United States v. Smith, 13 F.3d 1421, 1425 (10th Cir. 1994) (stating generally that bad faith and fraud are synonymous); United States v. Schwab, 88 F. Supp. 2d 1275, 1283 (D. Wyo. 2000) (in discussing a general definition, stating "bad faith" and "fraud" are synonymous, and also a synonym of dishonesty and citing Black's Law Dictionary); Acord v. Chrysler Corp., 399 S.E.2d 860, 862 (W. Va. 1990) (stating the right of rejection of satisfaction of a contract is absolute, and the "reasons cannot be investigated, if in good faith, that is, not fraudulent"); Kelley v. Jacobs, No. 21953-1-II, 1999 WL 305232, at \*5 (Wash. Ct. App.

May 14, 1999) (stating that fraud by non-disclosure or concealment in contract negotiations is bad faith); In re Foxmeyer Corp., 296 B.R. 327, 336 (Bankr. D. Del. 2003) (quoting language that “good faith” means the same thing as without actual fraudulent intent in bankruptcy, fraudulent transfer claim); In re Dewberry, 266 B.R. 916, 918 (Bankr. S.D. Ga. 2001) (stating that a debtor cannot show good faith when debtor’s omission of a creditor from his or her schedules occurred because of fraud or intentional design).<sup>4</sup>

## 2. The trial court erred by failing to apply collateral estoppel

At trial, Augustine labored to relitigate whether he did anything wrong or whether he really thought the TriSpan letter he intentionally withheld from Southern Medical was even “material.” His prior Stipulation of Facts and the federal District Court’s express findings and adjudication of his conduct should have prevented him from doing so.

Collateral estoppel will preclude litigation of an issue if (1) the issue is identical to one in a prior adjudication; (2) there was a final judgment on the merits; (3) the estopped party was a party or was in privity with a party to the prior adjudication; and (4) the

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<sup>4</sup> Courts in other states have similarly found that the statutory criteria of acting in good faith cannot be met by a party whose misconduct was knowing and/or willful. See Equitex, Inc. v. Ungar, 60 P.3d 746, 751 (Colo. Ct. App. 2002) (holding that the defendant’s intentional conduct demonstrated a lack of good faith that, as a matter of law, precluded indemnification); Biondi v. Beekman Hill House Apt. Corp., 709 N.Y.S.2d 861, 731 N.E.2d 577, 581 (2000) (“[b]ecause the underlying . . . judgment establishes that [defendant’s] acts were committed in bad faith, [defendant] is not entitled to indemnification and cannot relitigate the good faith versus bad faith issue here. . . .”); In re Landmark Land Co., 76 F.3d 553, 565 (4th Cir. 1996) (“[a]n agent who has intentionally participated in illegal activity or wrongful conduct against third persons cannot be said to have acted in good faith, even if the conduct benefits the corporation”); McLean v. Alexander, 449 F. Supp. 1251, 1266-67 (D. Del. 1978) *rev’d on other grounds*, 599 F.2d 1190 (3d Cir. 1979) (indemnity under section 145 is subject to the general public policy against indemnifying a party for his intentional wrongdoing).

estopped party was given a full and fair opportunity to be heard on the adjudicated issue. Hauschildt v. Beckingham, 686 N.W.2d 829, 838 (Minn. 2004). In determining whether the doctrine applies, the focus is on whether its application would work an injustice on the party against whom it is urged. Id. (citing Johnson v. Consol. Freightways, 420 N.W.2d 608, 613-14 (Minn. 1988)).

In the underlying criminal case, a final judgment on the merits was entered against Augustine. Augustine admitted he had a full and fair opportunity to be heard on the adjudicated issues in the underlying case. See P.C.B., Jr. v. Cha, No. Civ. 03-6368MJDJGL, 2005 WL 1421465, at \*5 (D. Minn. June 17, 2005) (holding that the plaintiff had a full and fair opportunity to challenge the basis for a disorderly conduct charge because he admitted to the conduct that justified a charge of disorderly conduct and the imposition of criminal penalties). Nor is there a question whether the conduct at issue in this claim for indemnification is identical to the conduct at issue in the prior adjudication.

Fundamental to the doctrine of collateral estoppel “is that a right, question or fact distinctly put in issue and directly determined by a court of competent jurisdiction cannot be disputed in a subsequent suit . . . .” Hauschildt, 686 N.W.2d at 837 (internal citations omitted). As the Minnesota Supreme Court notes, to permit a retrial of facts already determined in a criminal proceeding is an imposition on the courts and only tends to embarrass or bring into disrepute the judicial process. Travelers Ins. Co. v. Thompson, 163 N.W.2d 289, 294 (Minn. 1968). Findings of fact established by a court following a party’s stipulation of facts and plea agreement have collateral estoppel effect and cannot be relitigated. See Cha, 2005 WL 1421465 at \*5 (stating that a criminal conviction can

bar the plaintiff from relitigating elements of a civil claim that were decided in an earlier criminal proceeding, even if the criminal proceedings did not end in conviction) (citing Williams v. Schario, 93 F.3d 527, 528 (8th Cir. 1996) (guilty plea forecloses a later civil claim that arrest was without probable cause)).<sup>5</sup>

In the underlying criminal case, Augustine admitted to three essential facts: (1) Augustine received a letter from TriSpan, a fiscal intermediary of the Medicare Program, indicating TriSpan, which had earlier approved coverage for the Warm-Up product, had now determined that Warm-Up was “investigational”; (2) Augustine knew this determination was material to healthcare providers such as Southern Medical in deciding whether to purchase Warm-Up; (3) Augustine thereafter knowingly and willfully aided and abetted Arizant employees under his charge in withholding from Southern Medical the fact that he had received the letter from TriSpan. These findings resulted in the Federal District Court adjudicating Augustine guilty of withholding a material fact for use in determining rights to benefits and payments under a federal healthcare program. These core facts, establishing intentional fraud on the part of Augustine, were the sole bases for the criminal fine for which he sought indemnification at trial. These core facts are, as a matter of law, the opposite of “good faith,” and Augustine should not have been permitted to relitigate them.

In failing to apply collateral estoppel, the trial court permitted Augustine to contradict, explain away, and relitigate these very facts in an attempt to prove he acted in good faith. For example, Augustine was permitted to testify that “we were convinced we

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<sup>5</sup> See also, Nevins v. Christopher Street, Inc., 363 N.W.2d 891, 894 (Minn. Ct. App. 1985) (considering facts established through a defendant’s guilty plea to have collateral estoppel effect).

had done nothing wrong....” (A639). Despite the prior adjudication that he knew the June 2000 TriSpan letter was material to healthcare providers, Augustine was permitted to testify:

Q: At the time you did those things, did you think that you were breaking the rules?

A: No, I didn't. The letter really didn't change anything. . . . So I didn't see it had any affect on the rules. I didn't think we were breaking any rules.

(A658).

A: Well, the letter was simply wrong. And so we decided we weren't going to send out that letter because we didn't think that it would provide useful information to the providers.

(A656).

This is the precise reason for application of collateral estoppel. Augustine should not have been permitted to contradict previously adjudicated facts. This is particularly critical because, in addition to his admissions, Augustine affirmatively and personally accepted responsibility for his actions. His attempts to relitigate the issue undermined this personal acceptance. See, e.g., Kahn v. Inspector General of the U.S. Dep't of Health and Human Serv., 848 F. Supp. 432, 436 (S.D.N.Y. 1994); Anderson v. Thompson, 311 F. Supp. 2d 1121, 1128 (D. Kan. 2004).

**B. Trial court erred by excluding evidence of the dishonest/fraudulent conduct underlying Augustine's claim for indemnification**

Because the trial court decided that Augustine's indemnification claim should proceed to the jury on the question of whether his conduct in connection with the TriSpan Fraud constituted "good faith" conduct, the events and circumstances surrounding the August 16, 2000 and August 21, 2000 Southern Medical interactions became the key to the whole indemnification claim. By August 2000, Arizant had a clear policy to disclose

the June 2000 TriSpan letter to medical providers like Southern Medical. The August 16, 2000 Atlanta meeting and the August 21, 2000 follow-up phone call were the first communications with Southern Medical following Augustine's receipt of the TriSpan letter. Nevertheless, Augustine's subordinates failed to disclose the TriSpan letter to Southern Medical during those August 2000 communications and, in fact, went as far as to deny receiving any letter from TriSpan "good or bad." This was the exact misconduct that led to Augustine's \$2 million fine, and Augustine had the burden to prove that his involvement in this August 2000 misconduct was undertaken in good faith.

**1. At Trial, Augustine Denied Involvement in the Key August 2000 Southern Medical Communications**

There was no dispute that Augustine admitted, and the Federal District Court found in the underlying criminal matter, that he knowingly and willfully aided and abetted others in withholding the TriSpan letter from Southern Medical. Hensley testified in the underlying criminal matter that the meeting with Southern Medical during which he failed to disclose/intentionally withheld the existence of the TriSpan letter was on August 16, 2000. Having just sat through this sworn testimony by Hensley, Augustine then took the stand in the underlying criminal matter and testified that he aided and abetted this August 16, 2000 misconduct by Hensley.

Nevertheless, at trial in this matter, Augustine claimed he did nothing wrong and tried to distance himself from any knowledge of or responsibility for the August 2000 communications with Southern Medical. Augustine repeatedly and explicitly testified that he did nothing wrong: "... we were convinced we had done nothing wrong. . . ." (A639). Augustine then testified that he knew nothing about Hensley's August 2000

communications with Southern Medical. He testified that he had no idea who led the August 16, 2000 Atlanta meeting with Southern Medical. (A681-82). He testified that he did not know that the August 21, 2000 follow-up teleconference with Southern Medical even took place. (A686). Augustine testified that he didn't tell Hensley anything prior to the August 16 Atlanta meeting and that Hensley told him nothing about the August 16 meeting or the August 21 follow-up after they occurred. (A683-85).

Augustine even testified that he, in fact, personally told Southern Medical about the TriSpan decision not to cover Warm-Up. (A656). Augustine, however, carefully left out the date on which he allegedly told Southern Medical about the negative TriSpan coverage decision. This left the clear impression with the jury that Augustine himself had told Southern Medical about the TriSpan letter in August 2000. In that regard, during closing argument, Augustine's attorney stated:

And then Dr. Augustine told you something that is undisputed. Dr. Augustine told you that he actually himself spoke with Southern Medical, that company that bought Warm-Up, and he specifically told them that Tri-Span had sent a letter saying that Warm-Up was investigational. He specifically told them. That's what he said. And you did not hear one person or see one shred of evidence that disagreed. And the reason is because that is absolutely true. That is what happened. . . . Dr. Augustine did not know that the company was required to give the [TriSpan] letter to Southern Medical, and after all, [the letter] was wrong . . . .

(A738-39).

**2. Arizant was precluded from impeaching Augustine as to these key facts**

In response to Augustine's testimony denying involvement with the failure to disclose the TriSpan letter to Southern Medical in August 2000, Arizant attempted to cross-examine Augustine on these issues using Augustine's prior sworn deposition testimony. Arizant also attempted to impeach Augustine with a transcript of the August

21, 2000 follow-up teleconference that clearly showed Augustine was deeply involved with Hensley in his communications with Southern Medical. Arizant also attempted to impeach Augustine with Augustine's sworn testimony from his June 29, 2004 Change of Pleas hearing. Finally, Arizant attempted to impeach Augustine with the transcript of a January 2001 teleconference with Southern Medical to show the date and context in which Augustine allegedly "disclosed" the TriSpan letter to one employee of Southern Medical. All of this evidence and attempted impeachment was excluded on relevancy grounds. (A659-60).

In his deposition, Augustine testified that it was possible he knew that Hensley and others met with Southern Medical on August 16, 2000 in Atlanta. (A193, A648-50). Augustine admitted that he "talked to Tim about all kinds of subjects" and was "sure Southern Medical was one of them. . ." (A207, A648-50). He testified that he very well could have talked to Hensley about what to do with Southern Medical before he went to meet with them in August 2000 in Atlanta, and that it was possible that he talked to Hensley about the August 21, 2000 follow-up with Southern Medical. (A207-08, A648-50). Augustine further testified that it was possible that he had told Hensley prior to the August 21, 2000 follow-up telephone call with Southern Medical about an offer Hensley should make to Southern Medical. (A208, A648-50). Augustine also testified that Hensley might have talked to Augustine after the August 21, 2000 telephone call about denying that Arizant had received anything in writing, good or bad, from TriSpan. (A208). Yet Arizant was not permitted to impeach Augustine with any of this prior sworn testimony. (A665-66, A679-80, A684-85).

As to the August 21, 2000 follow-up telephone conference itself, Arizant would have shown that Augustine was clearly involved with Hensley regarding what to tell Southern Medical during that telephone call. During the call, Hensley and Southern Medical discussed Augustine by name over and over, referencing him eighteen times. (A33-53). Augustine was, in fact, the only Arizant employee ever referenced by Hensley or Southern Medical during the call. (A33-53). Moreover, during the call, Hensley discussed with Southern Medical directions he had received from Augustine as to what to tell Southern Medical. (A42-46). During the call, Hensley and Southern Medical began discussing Augustine's idea of a "bounty" to be paid for introductions to fiscal intermediaries. (A42-46). Hensley and the employee from Southern Medical then agreed to thereafter keep their communications secret from others at Southern Medical and Arizant. They agreed that only Augustine could be informed of the communications. (A42-44). Yet at trial, Arizant was not allowed to question Augustine about any of these details related to the August 21, 2000 telephone call even after Augustine directly opened the door. (A659-60).

Similarly, Arizant attempted but was precluded from using Augustine's own sworn testimony at the June 29, 2004 hearing in the underlying criminal case to show that the crime occurred in August of 2000 and that Augustine was well aware of it. Augustine testified at trial that he was unaware of Hensley's communications with Southern Medical in August 2000 and that he knew nothing about anything Hensley did wrong during those August 2000 communications. (A682-85). Following his testimony in that regard, Arizant sought to impeach Augustine with the sworn testimony from the June 29, 2004 Change of Plea appearances when after Hensley testify that "on or about August

16<sup>th</sup> 2000” he attended a meeting in Atlanta and at that meeting withheld the fact of the TriSpan letter from Southern Medical. Augustine then immediately testified that he knowingly and willfully aided and abetted such misconduct. (A92, A114-29, A129-45). The trial court precluded Arizant from impeaching or even referencing that under-oath testimony on the basis of “hearsay” and foundation. (A685-86).

Finally, Arizant would have impeached Augustine’s misleading testimony that he had personally disclosed the TriSpan letter to Southern Medical in a timely manner. Augustine’s only discussion with Southern Medical about the negative TriSpan decision occurred in January 2001, five months after the fraud occurred in August 2000. (A54, A56-57, A61-62). By that time, Augustine was engaged in secret bribe discussions with one employee of Southern Medical who affirmatively stated he would not disclose such information to Southern Medical. (A54-55, A57, A66-67). The trial court precluded Arizant from cross examining Augustine relative to the timing and context of his secret January 2001 communications with the Southern Medical employee on the grounds that such evidence was not relevant. (A659-60).

**3. The trial court’s exclusion of such evidence/impeachment on the basis of relevancy was reversible error**

It was clear, reversible error for the trial court to exclude the most critical evidence related to Augustine’s indemnification claim on, of all grounds, relevancy. Where a matter being tried involves a “case within a case,” such as indemnification, insurance coverage, malicious prosecution, or malpractice, exclusion of the evidence involving the underlying case on relevancy grounds is plain error. See Ulmer v. Associated Dry Goods Corp., 823 F.2d 1278 (8<sup>th</sup> Cir. 1987). This is particularly so when it was Augustine’s

burden to establish his conduct was in good faith and in attempting to do so, opened the door time and time again regarding what he knows, when he knew it, and what exactly his involvement was in the August 2000 misconduct with Southern Medical.

Minnesota Rule of Evidence 401 adopts a liberal, as opposed to restrictive, approach to relevance. If the evidence offered has *any* tendency to make the existence of a fact of consequence more or less probable than it would be without the evidence it is relevant. Minn. R. Evid. 401 (Committee Comment). A slight probative tendency is sufficient. *Id.* Furthermore, “the fact to be established need not be an ultimate fact or a vital fact. It need only be a fact that is of some consequence to the disposition of the litigation.” Minn. R. Evid. 401 (Committee Comment); see also *Foust v. McFarland*, 698 N.W.2d 24, 33-34 (Minn. Ct. App. 2005) (quoting similar language); *Boland v. Morrill*, 132 N.W.2d 711, 719 (Minn. 1965) (“If the offered evidence permits an inference to be drawn that will justify a desired finding of fact, it is relevant”).

In *Ulmer*, the plaintiff brought a malicious prosecution claim against Associated Dry Goods. The district court prevented Ulmer from presenting “virtually any evidence” of the circumstances surrounding his arrest and prosecution in the underlying case upon which the malicious prosecution claim was based. *Ulmer v. Associated Dry Goods Corp.*, 823 F.2d 1278, 1283 (8th Cir. 1987). On appeal, the district court was reversed on the ground that it committed clear error in excluding the evidence of the underlying case because the evidence, which was necessary in determining two essential elements of the malicious prosecution claim, was both relevant and probative. *Id.* at 1293. The district court was found in further error by refusing to allow Ulmer to examine a witness on the facts of the underlying prosecution. *Id.*

Here, like in Ulmer, the jury was precluded from understanding that in August 2000, without Arizant's knowledge and contrary to its policy, Augustine and his team intentionally withheld the June 2000 TriSpan letter from Southern Medical. Despite a full proffer to the court as to this evidence and its relevance to Augustine's bad faith conduct (A641-48), the trial court excluded it as irrelevant to the issue of good faith. (A659-60, A661-62, A685-86).

The trial court went even further by precluding Arizant from cross-examining Augustine when he opened the door with selective, misleading exculpatory testimony as to the August 2000 misconduct. By doing so, the trial court allowed him to tell a tale to the jury while barring Arizant from impeaching Augustine with directly contrary prior statements he, himself, made.

A witness may be cross-examined on the subject matter of the direct examination and matters affecting the credibility of the witness. Minn. R. Evid. 611(b). Thus, a witness may "open the door" to cross-examination or impeachment on a subject that might otherwise be off limits on cross. See generally, Bartosch v. Lewison, 413 N.W.2d 530, 533 (Minn. Ct. App. 1987) (stating that trial witness's testimony on direct "opened the door" for cross-examination); State v. Valtierra, 718 N.W.2d 425, 436 n.5 (Minn. 2006) (making similar statement); Stiles v. State, 664 N.W.2d 315,323 (Minn. 2003) (making similar statement). Indeed, "a wide range of inquiry should be allowed on cross-examination." Murray v. Walter, 269 N.W.2d 47, 49 (Minn. 1978) (internal citation omitted). Furthermore, it is a universal rule of evidence that "the credibility of a witness may be attacked by any party...." Minn. R. Evid. 607.

It was improper for the trial court to allow Augustine to provide selective testimony about the August 2000 misconduct, but yet preclude Arizant from cross examining and impeaching Augustine as to that testimony. This was reversible error. See, e.g., Riewe v. Arensen, 381 N.W.2d 448, 455-56 (Minn. Ct. App. 1986); Weyers v. Lear Operations Corp., 359 F.3d 1049, 1054-56 (8th Cir. 2004); Westcott v. Crinklaw, 68 F.3d 1073, 1077-78 (8th Cir. 1995); Newton v. Ryder Transp. Servs., Inc., 206 F.3d 772, 775-76 (8th Cir. 2000).

**C. At the very least, the trial court erred by failing to adequately instruct the jury as to “good faith”**

While Augustine’s claim should have never been submitted to a jury, the trial court should have, at the very least, instructed the jury as to the applicable meaning of “good faith.” Instead, the trial court rejected Arizant’s proposed jury instructions regarding good faith and adopted an instruction that failed to in any way define good faith as it relates to intentional fraud.

Jury instructions are viewed as a whole to determine whether they fairly and adequately explain the law. Peterson v. BASF Corp., 711 N.W.2d 470, 484 (Minn. 2006). Proper instructions give the jury “such explanations and instructions concerning the matter thus submitted as may be necessary to enable the jury to make its findings upon each issue.” Minn. R. Civ. P. 49.01(a).

Before trial, Arizant proposed the following jury instruction regarding good faith:

One requirement Augustine must prove is that he acted in good faith when he did the things that resulted in his criminal conviction. Acting in “good faith” means that a person acts honestly in fact. If a person does not act with honesty, then the person does not act in good faith.

Willfully or knowingly participating in an act of fraud is dishonest, and, therefore, cannot be acting in “good faith.”<sup>6</sup>

The trial court rejected Arizant’s proposed instruction. The trial court gave no instruction on the legal definition of “good faith and instead, gave only the following:

Indemnification Damages

Arizant must indemnify Scott Augustine for his fine, and his attorneys’ fees, and costs incurred in connection with the criminal proceeding if Dr. Augustine [proves that he]:

- (1) has not been indemnified by someone else for the same fine or attorneys’ fees;
- (2) acted in good faith;
- (3) received no improper personal benefit;
- (4) had no reasonable cause to believe his conduct was unlawful; and
- (5) reasonably believed that the conduct was in the best interest of the Company.

A conviction does not, of itself, establish that Dr. Augustine does not meet these criteria.

Appellate courts reverse a trial court’s failure to properly define good faith or bad faith in jury instructions. In an analogous case, Miller v. Byrne, the trial court failed to define appropriately the phrase “bad faith” in a jury instruction for a claim for bad faith breach of insurance contract. 916 P.2d 566, 572-73 (Colo. Ct. App. 1995). In reversing, the court held that the instructions failed to set forth the appropriate standard with which to measure the defendant’s conduct and that absent such an instruction, the jury may have supplied its own definition and measured the defendant’s actions “by an unknown yardstick.” Id. A new trial was granted solely due to this error.

In this case, “good faith” is specifically defined by Minn. Stat. § 302A.011, Subd. 13 as “honesty in fact.” The definition contained therein should have been the only

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<sup>6</sup> Citing as authority, CIVJIG 20.55 (modified); Minn. Stat. § 302A.011, subd. 13; Cooper v. TWA Airlines, LLC, 274 F. Supp. 2d 231, 249 (E.D.N.Y. 2003).

“yardstick” by which the jury measured Augustine’s actions. Failing to instruct the jury as to the meaning of good faith under this statute was reversible error. See also Davis v. Nat’l Pioneer Ins. Co., 515 P.2d 580, 582 (Okla. Ct. App. 1973); Maryland Cas. Co. v. Spitcaufsky, 178 S.W.2d 368, 372 (Mo. 1944).

#### **IV. APPRAISAL CHALLENGE**

Augustine’s entire Appraisal Challenge claim was premised on a request that the jury disregard Harris Nesbitt’s March 31, 2004 appraisal of Arizant’s stock price and, itself, come up with a new, higher value. Minnesota law, however, expressly precludes such a request and the trial court erred by ignoring that law and submitting Augustine’s claim to the jury for carte blanche reappraisal.

Under Minnesota law, the issue of the meaning and application of Section 5(b)’s “valuation by appraisal” provision was for the trial court. The 2002 Separation Agreement requires only that Arizant’s board of directors hire an appraiser to conduct the appraisal within sixty days of the end of Arizant’s fiscal year.” Section 5(b) goes on to provide that “[t]he Fair Market Value of the Common Stock will be an amount determined by such appraisal.” There is nothing ambiguous about that provision, and the trial court should have ruled, as a matter of law, that the Fair Market Value of one share of common stock as of March 31, 2004 was the amount determined by the 2004 Harris Nesbitt appraisal.

##### **A. Minnesota Law as to “Valuation by Appraisal” Provisions**

###### **1. Appraisal can’t be second guessed unless evidence of fraud**

Under Minnesota law, an independent appraiser’s determination of value cannot later be judicially attacked where it is “fairly inferable” that the parties intended to be

bound by the determination of the appraiser. See Sanitary Farm Dairies, Inc. v. Gammel, 195 F.2d 106, 113-14 (8th Cir. 1952); Nelson v. Charles Betcher Lumber Co., 93 N.W. 661, 662 (Minn. 1903); see also, PVI, Inc. v. Ratiopharm, 253 F.3d 320, 325-26 (8th Cir. 2001) (holding that where an appraiser was to determine which of the submitted valuations reflected the fair market value of the stock, the plaintiff could not challenge the method or result generated by the independent appraiser). When an intention to be bound is “fairly inferable” from the agreement, the valuation can *only* be attacked if it was a product of fraud, corruption or malfeasance and, thus, was “morally tainted.” Sanitary Farm Dairies, 195 F.2d at 113-14. In fact, an appraisal such as the one performed by Harris Nesbitt in 2004 under the Separation Agreement legally

cannot be judicially examined as a mere question of adequacy or inadequacy of amount but only as an issue of moral infirmity . . . and is conclusive on [the parties], except as it is vulnerable from moral taint, including a mistake so fundamental or penetrative as to require its rejection, not as a question of inadequate factual result but as a matter of irresponsible legal product.

Id.

## 2. The plain and unambiguous language of § 5(b)

The plain and unambiguous language of § 5(b) states that the “Fair Market Value of the Common Stock will be an amount determined by” an appraiser selected by Arizant’s Board. The clear language that the Fair Market Value “will be” an amount “determined” by the appraiser, more than establishes that it is “fairly inferable” that the parties agreed the appraisal to be the final determination of such value.

While Minnesota’s law only requires that it be “fairly inferable” from the contract that the parties agree to be bound by the appraisal, the trial court applied a much more stringent standard in order to justify submitting the claim to the jury. In denying

summary judgment, the trial court ruled that questions of fact existed whether the parties “expressly stipulated that the appraisal was to be conclusive.” That is simply not the standard under the law.

Moreover, at trial, no evidence of any ambiguity was presented by Augustine who had the burden of proof. In fact, Augustine affirmatively excluded parol evidence as to § 5(b). When parol evidence is excluded from trial, it is indicative of an unambiguous contract. See In re Ocwen Fin. Servs., Inc., 649 N.W.2d 854, 857-58 (Minn. Ct. App. 2002) (stating, “[w]hile courts may look at parol evidence to determine the parties’ bargain if required by some contractual ambiguity, where there is no ambiguity in the written terms of the contract, construction by a district court or an appellate court is inappropriate; the contract is interpreted according to its terms”); Alpha Real Estate Co. v. Delta Dental Plan, 664 N.W.2d 303, 312 (Minn. 2003); Triple B & G, Inc. v. City of Fairmont, 494 N.W.2d 49, 53 (Minn. Ct. App. 1992); Norwest Bank Minn. v. Midwestern Mach. Co., 481 N.W.2d 875, 881 (Minn. Ct. App. 1992).

### **3. No evidence of fraud**

Furthermore, Augustine presented no evidence of fraud in connection with the Harris Nesbitt appraisal. Marie Humbert from Arizant testified that there was no push by Arizant for a low appraisal by Harris Nesbitt. (A555-56). No evidence of fraud was elicited from any other witnesses (A633-37), including Phil Williams, an expert witness hired to evaluate the Harris Nesbitt appraisal, who essentially concurred with the methods and process employed by Harris Nesbitt in its appraisal.

**B. Trial court should have decided the issue**

Even if the trial court properly refused to decide the issue of interpretation of the “valuation by appraisal” provision on summary judgment, the trial court should have decided the issue at the close of all the evidence, when no evidence of any ambiguity or fraud was introduced at trial. At that point, the issue was for the trial court to decide as a matter of law, not the jury. See Rognrud v. Zubert, 165 N.W.2d 244, 247 (Minn. 1969) (affirming lower court, which had dismissed the jury at the close of evidence because the evidence had not raised any jury questions).

**C. Even if proper to submit to the jury, the trial court failed to adequately instruct the jury**

Even if it could be seen as proper to give the issue of contract construction to the jury, the trial court failed to properly instruct the jury on the law. The trial court should have first required the jury to make a decision as to what was “fairly inferable” from the “valuation by appraisal” language. If the jury decided that it was fairly inferable from the language that the appraisal was meant to be final and binding, then the court should have required the jury to consider the issue of fraud/malfeasance. If the jury did not find fraud/malfeasance, the trial court should have summarily ruled in favor of Arizant. Conversely, if the jury did not find the language to be final and binding, or if the jury found fraud in connection with the appraisal, then the trial court should have given a true “fair market value” jury instruction with appropriate Minnesota law. None of this occurred.

Arizant offered Proposed Jury Instruction Nos. 25-35 relating to Augustine’s Appraisal Challenge claim. In particular, Arizant offered proposed Jury Instruction Nos. 31 and 32, and provided questions on the proposed Special Verdict Form that expressly

instructed the jury on the applicable standard and required the jury to determine whether it was “fairly inferable” that the parties intended to be bound by the appraisal and whether the appraisal was or was not a product of fraud.

Rather than properly instructing the jury as to Minnesota law regarding contractual appraisal clauses, the trial court provided the jury with no instruction whatsoever regarding the law on “valuation by appraisal” provisions in Minnesota and submitted a Special Verdict Form that sought to have the jury determine the “fair market value” (small caps) for themselves. In refusing to instruct the jury as to the proper standards of law, the trial court violated Rule 49’s clear requirement that the court “give to the jury such explanations and instructions concerning the matter thus submitted as may be necessary to enable the jury to make its findings upon each issue.” Minn. R. Civ. P. 49.01(a). As Sanitary Farms holds, where parties provide that the method for ascertaining the value of something is appraisal by a third party, the result of an appraisal is “just as conclusive upon them as would be an arbitration award” and “cannot be judicially examined as a mere question of adequacy or inadequacy of amount.” Sanitary Farms, 195 F.2d at 113-14. Yet that is exactly what the trial court required the jury to do.

Instead, the trial court provided only a template breach of contract instruction and then submitted to the jury a special verdict form that asked them to determine, for themselves, whether they thought the amount of the appraisal was adequate and if not, what amount they believed would be adequate. Because Sanitary Farms expressly precludes such an examination, the trial court’s failure to instruct the jury on the law was reversible error.

**V. TRIAL COURT ERRED IN AWARDING ATTORNEY FEES TO AUGUSTINE UNDER MINN. STAT. § 302A.467**

The trial court awarded attorney fees to Augustine in the amount of \$135,768.25 pursuant to Minn. Stat. § 302A.467. Minn. Stat. § 302A.467 does not apply to an action brought by an officer of a corporation against the corporation for a claim for statutory indemnification. Because Minn. Stat. § 302A.467 does not provide discretionary authority for the award of attorney fees in cases such as this one, the trial court erred in its award of fees to Augustine.

Minn. Stat. § 302A.467 provides:

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.

The statute does not apply to actions brought by a claimant suing in his or her capacity as a director or officer. Rather, the statute is intended to aid shareholders, and more specifically, shareholders in a closely-held corporation. In fact, part of the legislative intent of the Minnesota Business Corporation Act, of which Minn. Stat. § 302A.467 is part, was to specifically expand the court's equitable powers to grant relief to an aggrieved shareholder in a closely-held corporation. Foy v. Klapmeier, 922 F.2d 774, 779 (8th Cir. 1993) (citing Sawyer v. Curt & Co., Nos. C7-90-2040, C9-90-2041, 1991 WL 65320 at \*2 (Minn. Ct. App. Feb. 12, 1991), *order for publication vacated by* 1991 WL 160333 (Minn. Aug. 2, 1991)).

In addition, while shareholders of closely-held corporations frequently serve as officers and directors of the corporation, it is only the status as shareholder, and claims uniquely related thereto, that have prompted Minnesota courts to grant equitable relief

and attorney fees under Minn. Stat. § 302A.467. See Foy, 992 F.2d at 776 (minority shareholder, who was also a vice president and later director, awarded attorney fees under Minn. Stat. § 302A.467 in *shareholder derivative suit*); Powell v. Anderson, No. C5-99-1755, 2003 WL 22705878, at \*1 (Minn. Ct. App. Nov. 18, 2003) (remanded for consideration of award of attorney fees and other equitable relief under Minn. Stat. § 302A.467 to minority shareholder and director of closely-held corporation for claim that defendants acted fraudulently and in a manner unfairly prejudicial to claimant “in her capacity as shareholder”).

Augustine’s claim for attorney fees relates solely to his claim under Minn. Stat. § 302A.521, which provides for indemnification of a director, officer, or employee. Augustine is thus suing solely in his capacity as a director, officer, or employee, and not as a shareholder. His status as a shareholder of Arizant has nothing to do and could have nothing to do with his claim for indemnification. Minn. Stat. § 302A.467 is thus inapplicable to Augustine’s claim.

Furthermore, Minnesota courts have long held that attorney fees are not recoverable in litigation unless there is a specific contract permitting or a statute authorizing such recovery. Kallok v. Medtronic, Inc., 573 N.W.2d 356, 363 (Minn. 1998); Barr/Nelson, Inc. v. Tonto’s, Inc., 336 N.W.2d 46, 53 (Minn. 1983); Cherne Indus., Inc. v. Grounds & Assocs., Inc., 278 N.W.2d 81, 96 (Minn. 1979). No contractual provision provides for attorney fees in this case. Specifically, the indemnity provision of the 2002 Separation Agreement makes no allowance for such a claim. Neither Minn. Stat. § 302A.467 nor any other statute authorizes an award of attorney fees in this case. Therefore, the trial court erred in awarding attorney fees to Augustine.

## CONCLUSION

For the foregoing reasons, Arizant respectfully requests that this Court reverse the trial court's denial of Arizant's motions for summary judgment and motion for judgment as a matter of law and remand with instructions that the trial court dismiss Augustine's claims as a matter of law. In the alternative, Arizant requests that this Court reverse and remand the matter for new trial based upon the trial court's (1) error in excluding relevant evidence at trial; (2) error in disallowing Arizant from conducting cross examination of Augustine on matters to which he opened the door; and (3) failure to properly instruct the jury. In addition, Arizant respectfully requests that this Court reverse the trial court's order granting Augustine attorney fees as contrary to law. Arizant also respectfully requests reversal of the trial court's award of costs and disbursements predicated on its erroneous rulings, as well as costs and disbursements on appeal.

Dated: September 13, 2006.

Respectfully Submitted,

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