NO. A10-2031

State of Minnesota
In Court of Appeals

Paul W. Larson and
Jesse J. Schneider,

Respondents,

vs.

Lakeview Lofts, LLC and
Todd Frostad,

Appellants.

RESPONDENTS' BRIEF

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STATEMENT OF ISSUES

1. Whether Appellants owed Respondents a fiduciary duty and duty of good faith?

   The Trial Court found that the Lakeview Lofts project is a condominium and therefore governed by the Minnesota Common Interest Ownership Act, Minnesota Chapter 515B. The Act specifically provides that during the period of declarant control the declarant and its representatives and officers shall be subject to "all fiduciary obligations and obligations of good faith applicable to any persons serving a corporation in that capacity." Minn. Stat. § 515B.3-120(2005). The Trial Court found Appellants were the "declarant" and "representatives and officers" at the time they entered into the agreement with Blackstone, and as such owed a fiduciary duty and duty of good faith to Appellants.

2. Whether Appellants breached their fiduciary duties and duties of good faith by entering into the agreement with Blackstone?

   The Trial Court found Appellants breached their fiduciary duties and duties of good faith to Respondents by entering into the agreement with Blackstone. The agreement violated RESPA and raised multiple other "red flags." Appellants ignored the multiple red flags posed by the agreement and put their own interests ahead of Respondents by entering into the agreement.

3. Whether the evidence supports the Trial Court's damage award?

   After hearing evidence presented by appraisal experts for both Appellants and Respondents, the Trial Court properly awarded damages to Respondents in accordance with the evidence and applicable law.

STATEMENT OF THE CASE

Appellant, Lakeview Lofts, LLC is a Minnesota limited liability company owned by Appellant Todd Frostad. Lakeview Lofts, LLC was created for the sole purpose of developing, marketing, and selling the Lakeview Lofts condominium project located in Spring Park, Minnesota. The Lakeview Lofts project is comprised of 39 residential condominium units and one commercial unit. Respondents are individuals who purchased residential condominiums from Appellants.

This litigation arises from Appellants' wrongful "dumping" of the last approximate 44% of the Lakeview Lofts residential units through a scheme that involved a "kickback" of nearly one million dollars to the purported purchaser/"agent" of those units. In late 2005 and early 2006, Appellants began experiencing problems with the Lakeview Lofts project—sales began to slow, 17 of the 38 residential units were unsold, Appellants' interest rate on their construction loan increased, they were delinquent on property taxes, and faced competition from another geographically close condominium project. In short, Appellants were feeling pressure to get the Lakeview lofts project closed.

In early 2006, Blackstone Sales, LLC approached Appellants and offered to purchase all of the then 17 remaining unsold residential condominium units in exchange for a "management fee" to be paid by Appellants to Blackstone. Blackstone and Appellants entered into a "verbal agreement" that provided for Appellants to pay Blackstone a "management fee" equal to between 10-11% of the purchase price for the remaining 17 units, which equated to a payment of $914,761.91. In addition to payment of nearly $1 million dollars, the parties agreed that Blackstone would not receive any payment unless all 17 units were purchased (at their full multiple listing service price) and further agreed that payment would not be made for the first seven sales.

From June 30, 2006 through September 15, 2006, Blackstone or Blackstone's nominal "purchasers" purchased all of the 17 remaining residential condominium units in the Lakeview project. Of these purchases, two individuals purchased 11 units, three units were purchased by Blackstone Sales, LLC and the remaining three units were purchased by other individual purchasers acting through or procured by Blackstone Sales, LLC. The Blackstone purchasers obtained nearly 100% financing for the 14 units they purchased. The three units purchased by Blackstone Sales, LLC were cash purchases that were subsequently mortgaged. All of the 17 units closed within a period of approximately two and one-half months, and 11 of the 17 units closed within the period of August 29, 2006 - September 15, 2006.

Although the "management fee" to be paid to Blackstone purportedly required the sale of all 17 units, the existence of the management fee was not contained on, or referenced in, either the purchase agreements or the closing documents of the first seven closings. The "management fee" was also not disclosed to the appraisers nor was there any documentation that the "management fee" was discussed with or approved by any of the lenders for the first seven sales. As a result of the Blackstone sales, Appellants were able to pay off their mortgage on the property and Lakeview Lofts, LLC received payment of $2,221,232.20 in cash at closing and made a profit of between $700,000-$800,000 on the project.

Following the Blackstone purchases, only one of the Blackstone purchasers occupied a condominium unit, and none of the Blackstone purchasers made any mortgage payments, property tax payments, or paid any condominium association dues. None of the units purchased by Blackstone or Blackstone's nominal "purchasers" were resold and all of the 17 units were foreclosed upon by the respective mortgage holders. As a result of Appellants' actions, Respondents' property suffered a significant diminution in value.

STATEMENT OF FACTS

A. Respondent Paul Larson.

Respondent Paul Larson is a Minnesota resident who is a licensed real estate agent with 29 years experience (Add. 1, ¶¶ 2.1-2.2)[1]. Respondent Larson specializes in selling and marketing real estate in Minnesota, primarily in the west metro area of the Twin Cities (Add. 1, ¶ 2.2). Larson purchased his condominium unit pre-construction from Lakeview Lofts, LLC in 2005 for a purchase price of $375,140.84 (Add. 1, ¶ 2.3). Larson closed on his condominium on December 27, 2005. As a result of purchasing the unit prior to construction, Larson received a reduction in the purchase price he paid for his condominium (*Id*). After purchasing the property, Larson immediately put improvements into his unit at a cost of more than $25,000 (Add. 1, ¶ 2.5). Larson sold his condominium in October 2009 for the amount of $270,000 (Add. 1, ¶ 2.7).

B. Respondent Jesse Schneider.

Respondent Jesse Schneider is a Minnesota resident who is a firefighter for the City of St. Paul (Add. 2, ¶ 3.1, Trans. 200). Schneider purchased his condominium unit from Lakeview Lofts, LLC in January 2006 at purchase price of $354,358.47 (Add. 2, ¶ 3.2). The estimated market value of Schneider's condominium unit for tax purposes for assessment year

[1] References to "Add." are to the Trial Court's Amended Findings of Fact, Conclusions of Law and Order dated September 17, 2010.

2009 was $182,000 and for assessment year 2010 was $166,000 (Add. 2, ¶ 3.3). Schneider testified at trial that the current assessed value (2010) represents the current value of his property (*Id.*). Respondents' expert, Calvin Haasken, testified that the current assessed value is also indicative of the current market value (*Id.*, Trans. 484).

C. Lakeview Lofts, LLC and Todd Frostad.

Appellant Lakeview Lofts, LLC is a Minnesota limited liability company that was created for the sole purposed of developing, marketing and selling the Lakeview Lofts condominium project located in Spring Park, Minnesota (Add. 1, ¶¶ 1.1-1.2). The Lakeview Lofts project is comprised of 39 residential units and one commercial unit (Add. 1, ¶ 1.3). Lakeview Lofts, LLC began selling the condominium units in late 2004 and construction on the project began in November 2004 (Add. 1, ¶ 1.4). Appellant, Todd Frostad, is a Minnesota resident who is the sole owner and principal of Lakeview Lofts, LLC (Add. 1, ¶¶ 1.5-1.6).

Appellants financed the Lakeview Lofts project through KleinBank, which held the mortgage on the property (Add. 4, ¶ 6.1). The financing KleinBank provided for the project contained a fluctuating "prime plus" interest rate (Add. 4, ¶ 6.2). As part of the financing agreement, Appellants were required to provide and adhere to a "closeout schedule" that estimated how long it would take to sell all of the condominium units (Add. 4, ¶ 6.3).

By late 2005, early 2006, the market for new condominium units had softened (Add. 4, ¶ 6.4). In early 2006, the sales of the Lakeview Lofts condominium units began to slow and by March-April 2006, Appellants were falling behind on the projections provided to KleinBank for closing out the project (Add. 4, ¶¶ 6.5-6.6). In addition to falling behind on projections for closing out the project, Appellants, in this March-April 2006 time period, were facing an increased interest rate on their loan with KleinBank, were delinquent on real estate taxes due and owing on the Lakeview project, and were facing competition from a geographically close condominium project (Add. 5, ¶¶ 6.7-6.8, Trans. 19). As of May 2006, nearly half of the residential units (17) remained unsold (Add. 5, ¶ 6.9).

D. Blackstone Sales, LLC.

In early 2006, Blackstone approached Appellants regarding the purchase of the 17 remaining unsold condominium units in the Lakeview project (Add. 5, ¶ 7.1)[2]. Blackstone purportedly represented to Frostad that it had the ability to secure purchasers for all of the 17 remaining unsold residential condominium units by either finding buyers with mortgage financing of their own and/or purchasing some of the units itself (Add. 5, ¶ 7.3). According to Frostad, Blackstone and/or the "purchasers" it was obtaining, were going to purchase the units at full price and attempt to resell them (Add. 5, ¶ 7.6). Blackstone represented that it had relationships with lenders that could help it secure buyers and Blackstone was going to either sell the condominium units on extended contract for deed terms or "rent to own" arrangements (Trans. 32).

In March or April 2006, Appellants and Blackstone entered into a verbal agreement whereby Blackstone would purchase or find purchasers for the 17 units in exchange for a "management fee" of 10-11% to be paid by Appellants to Blackstone (Add. 5, ¶ 7.4). Prior to their involvement with Blackstone, Appellants had never paid a real estate commission approaching 10-11% for any of their prior sales (Add. 6, ¶ 8.7). The total amount of this

[2] In 2009, Blackstone principal, Mike Prieskorn was indicted by federal authorities for mortgage fraud and has subsequently pleaded guilty (Add. 12, ¶ 10.10).

"management fee" equated to a payment of $914,761.91 (Add. 6, ¶ 8.6). Appellants and Blackstone purportedly never reduced the "management agreement" to writing (Add. 5, ¶ 7.5).

According to Frostad, the "management fee" was conditioned on Blackstone selling all of the 17 remaining units; in other words, Appellants would not pay a "management fee" on any of the units unless all of the units were sold (Add. 6, ¶ 8.4). It is undisputed that at the time of the Blackstone purchases, Blackstone, or the buyers they procured, could not, because of rental restrictions in the Lakeview Lofts condominium declaration, lease any of the subject 17 units to third party tenants (Add. 5, ¶ 7.7).

From June 30, 2006 to September 15, 2006, Blackstone or Blackstone "purchasers" purchased all of the 17 remaining residential condominium units in the Lakeview project (Add. 8, ¶ 9.1). Of these units, six were purchased by an individual named Ryan Simifranca, five were purchased by an individual named Casey Burns, three were purchased by Blackstone Sales, LLC, and the remaining three were purchased by other individual purchasers acting through or procured by Blackstone Sales, LLC (Add. 8, ¶ 9.1). Although the "management fee" to be paid to Blackstone required the sale of all 17 units, the "management fee' was not contained in, or referenced in, either the purchase agreements or the closing documents of the first seven of the Blackstone closings. The "management fee" was also not disclosed to any of the appraisers, nor is there any documentation that the "management fee" was discussed with or approved by the lenders for the first seven Blackstone sales (Add. 7, ¶ 8.9). Moreover, none of the 17 purchase agreements entered into with Blackstone or their buyers contained any reference to the "management fee" (Trans. 37).

Respondents' expert witness, Calvin Haasken, testified that the failure to disclose the "management fee" on the first seven units in the Blackstone transaction is significant because the appraisers hired to conduct appraisals would not be aware of the "management fee' and therefore could not use it in determining the appraisal price (Add. 7 ¶ 8.93). This is significant because the comparable sales taken into consideration by the appraisers would necessarily involve units in the same building (*Id.*). Haasken testified that the first four properties in a building that sell create a base-line property value for the rest of the properties, and that by not disclosing the "management fee' on the first seven Blackstone units, it allowed higher financing to be obtained for the remainder of the units (*Id.*). The effect of the failure to list the "management fee" on the first seven closings was to artificially inflate the comparable sales and resulted in Blackstone being able to obtain nearly 100% financing on the purchased units (Add. 7, ¶ 8.93). Appellant Frostad was certainly aware of the significance of closing the first units with Blackstone so they could be used as "comparables" for the subsequent units, as demonstrated by email communications dated August 3 and 4, 2006 between Frostad and a loan officer, wherein the following communication occurred between Frostad and the loan officer:

> "Unit 201 is waiting for another closing to use as a comp and the appraiser (Jeremy) told me he was in contact with you about that and that comp is supposed to close tomorrow through another loan officer." Frostad replied to this email with the following: "That is disappointing. The comp that Jeremy is looking for has also slid out and 'may' close Monday" (Add. 7-8, ¶ 8.94).

Although at trial Appellant Frostad denied that the comparable sale issue was a motivating reason for entering into the "back-end loaded" "management fee" agreement, his following deposition testimony—provided to refresh his recollection at trial—shows he was aware of the issue:

Q: "And you felt that the management fee repayment would have a different effect on market value of the other units on a discount?"

R: "Yes."

Q: "How?"

R: "Because the sale price has registered on title and in the County and everybody else would be consistent with the market price of the units in the building."

Q: "So, the price, the purported sale price then could be used as a comparable sale?"

R: "Right."

(Trans. 39)[3].

Blackstone and/or Blackstone "purchasers" paid the full multiple listing service ("MLS") price for each of the 17 condominium units (Add. 8, ¶ 9.3); despite the fact that all of the Blackstone transactions occurred during a period of time where the condominium market was softening (Add. 8, ¶ 9.6). All of the 17 units closed within a period of approximately two and one-half months of the first purchase agreement; 11 of the 17 units closed within the period of August 29, 2006 through September 15, 2006 (Add. 9, ¶ 9.7).

[3] Frostad apparently decided on the "management fee" instead of an agreement to discount the units "so as to hold up the sale prices of the project for future sellers" (Trans. p. 37). Coincidentally, the decision to "opt" for the "management fee" instead of the discount also resulted in more money for Frostad (Trans. 80).

During the trial, Respondents presented expert witness testimony from Calvin Haasken.[4] Mr. Haasken testified that the manner of these transactions (e.g. multiple units purchased by single individuals, close temporal proximity of closings, and sale prices of nearly 100% of MLS list prices in a softening condominium market) were so unusual so as to raise multiple red flags and pointed to potentially fraudulent financing transactions (Add. 9, ¶ 9.8). According to Haasken, the close temporal proximity of the closing dates for the units is significant because in processing the loan applications, the loan processors would not have the information necessary to take into consideration the multiple unit purchases made by individuals such as Simifranca and Burns (who collectively purchased 11 units) so they could properly evaluate the financial ability of these purchasers to make the mortgage payments on the loans (Add. 9, ¶ 9.7).

E. Post-Blackstone Transactions.

As a result of the Blackstone sales, Appellants were able to pay off the mortgage on the property and they received payment of $2,221,232.20 in cash at closing (Add. 9, ¶ 10.1). At trial, Frostad testified that Appellants made a net profit of between $700,000 and $800,000 (Add. 9, ¶ 10.2). None of the Blackstone purchasers made any mortgage payments, property tax payments or paid any condominium association dues (Add. 9, ¶ 10.3). All of the 17 units went into foreclosure (Add 9, ¶ 10.5, Trans. 102). Following the foreclosures, the Lakeview properties suffered substantial damage. Some of the unoccupied units were inhabited by

[4] Contrary to Appellants' assertion that Mr. Haasken is simply "an appraiser," Mr. Haasken is a real estate agent, the owner/broker of Chestnut Realty, Inc., a level four general real estate property appraiser, President and owner of Goldstar Mortgage (a real estate mortgage origination company), a land developer and an individual who has been a Court-appointed Commissioner, realtor, appraiser and expert witness (Trans. 163-165).

squatters, the property was vandalized, common area furnishings were stolen and there were frequent loud, boisterous incidents. The property was blighted and the reputation of the building was very poor (Add. 10, ¶ 10.6). As a result of the foreclosures, the market value of Respondents' condominiums was adversely affected (Add. 10, ¶ 10.7).

F. Trial Court Findings.

Based on the evidence at trial, Judge Peterson found that Appellants owed Respondents a fiduciary duty and that Appellants breached their fiduciary duty and obligations of good faith to Respondents by entering into the agreement with Blackstone for the sale of the 17 units (Add. 12-16, ¶ 1.0-3.7)[5].

G. Damages.

The Court heard testimony from two expert witnesses concerning the damages issue. Appellants produced Mary Bujold and Respondents presented Calvin Haasken. Bujold testified that the average market price for condominium sales, excluding Lakeview Lofts and condominiums sold for less than $100,000 or more than $1,000,000, in the seven county metro area fell 26% from 2006 to 2010 (Add. 10-11, ¶ 10.8). Bujold also testified that the average market price for condominium sales, excluding Lakeview Lofts and outliers in the Lake Minnetonka area, fell 40% as measured from 2006 to 2010. Bujold further provided the Court with evidence showing the average price of a condominium sale for the seven county

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[5] Appellants contend that the Court made a factual finding of fraud (See Appellants' Brief, page 9). Although Respondents believe that based upon the evidence and trial testimony, there could have been a finding of fraud, the trial Court did not make such a specific finding. The paragraph cited by Appellants merely notes the testimony from Respondents' expert witness.

metro area, excluding Lakeview Lofts and outliers in 2004 through 2009, experienced a decline in average market value of only 1% (Add. 10-11, ¶ 10.8).

Mr. Haasken testified that while the overall residential market values dropped from 2006 through 2010, the Lakeview Lofts project was harmed more than others (Add. 10, ¶ 10.7). According to Haasken, the effect of multiple foreclosures in a single building, such as experienced at Lakeview Lofts, can have devastating market effects (*Id.*). Because the properties that went into foreclosure were subsequently purchased at "fire sale" values, the adverse effects include: (1) the lower priced "fire sale" units will not require as large re-sale prices as other units to motivate an economically viable sale for the then owner, resulting in driving down the value of all the units in the project; (2) the appraised values will remain low; and (3) given the likely inability of the units to reach market value through resale, the "fire sale" values will have an adverse market effect on value into the foreseeable future (*Id.*). Haasken opined that the diminution in value attributable to Appellants' actions resulting in the foreclosures was 25% of the value of the property (Trans. 359-486)[6].

Respondents themselves also provided testimony concerning the damages they believe they suffered as a result of Appellants' breach of fiduciary duty. Respondent Larson opined that the diminution of value to his property was 50% (Trans. 412). In support of this opinion, Respondent conducted a market analysis and analyzed comparable sales (Trans. 409-412).

[6] Appellants assert that Haasken did not provide testimony as to the prior value of Larson's or Schneider's property. This is incorrect. The purchase prices were provided to the Court as specific Exhibits and Mr. Haasken specifically conducted the mathematical analysis using the purchase price analysis (Trans. 483).

Respondent Schneider testified that his damages were as detailed by Cal Haasken (Trans. 422).

After listening to all of the evidence and reviewing the evidence presented at trial, the Court calculated Larson's damages at $101,389.43 (Add. 18, ¶ 7.3) and Schneider's damages at $96,225.26. In addition to these damages, the Respondents were awarded $41,997.10 in attorney's fees and expenses under Minn. Stat. § 515B.3-111(b) (Add. 19, ¶ 3.0).

LEGAL ARGUMENT

I. STANDARD OF REVIEW.

The scope and meaning of the fiduciary duty under Minn. Stat. §515B.3-120 is a question of statutory interpretation. Statutory construction is a question of law the Court reviews *de novo* in writ *Kleven*, 736 N.W.2d 707, 709 (Minn. App. 2007). An appellate court reviews *de novo* the district court's construction and application of the statute, but reviews the record in the light most favorable to the district court's findings, and will reverse the findings only when the left with the definite and firm conviction that a mistake has been made, *Brand v. Brand*, 721 N.W.2d 924, 927 (Minn. App. 2006). If a statute, construed according to the ordinary rules of grammar, is unambiguous, courts may not engage in further statutory construction and must apply its plain meaning, *State by Beaulieu v. RSJ, Inc.*, 552 N.W.2d 695, 701 (Minn. 1996).

Appellants have challenged the District Court's award of damages in this matter, but the District Court has broad discretion in determining appropriate damages, *Friend v. Gopher Co. Inc.*, 771 N.W.2d 33, 40 (Minn. App. 2009). The burden of proving damages is measured by a "fair preponderance of the evidence" standard, *Canada by Lande v. McCarthy*, 567 N.W.2d 496, 507 (Minn. 1997).

II. APPELLANTS OWED RESPONDENTS A FIDUCIARY DUTY.

The Lakeview Lofts project is a condominium project and is therefore governed by the Minnesota Common Interest Ownership Act, Minnesota Statute Chapter 515B. Pursuant to Minn. Stat. § 515B.3-120, during any period of "Declarant control" pursuant to 515B.3-103(c), "Declarant and any of its representatives who are acting as officers or directors of the association shall...(2) be subject to all fiduciary obligations and obligations of good faith applicable to any persons serving a corporation in that capacity." Minn. Stat. Sec. 515B.3-120 (2005).

A. Declarant Control Period.

Minn. Stat. §515B.3-103(c) provides: "The declaration may provide for a period of Declarant control of the association, during which a Declarant, or persons designated by the Declarant, may appoint and remove the officers and directors of the association. The period of Declarant control begins on the date of creation of the common interest community and terminates upon the earliest of the following events: (i) five years after the date of the first conveyance of a unit to a unit owner other than a declarant in the case of a flexible common interest community or three years in the case of any other common interest community, (ii) the declarant's voluntary surrender of control by giving written notice to the unit owners pursuant to section 515B.1-115, or (iii) the conveyance of 75 percent of the units to unit owners other than a declarant." Minn. Stat. Sec. 515B.3-103(c) (2005).

The Trial Court found that the period of "Declarant control" in this case ran from October 3, 2005 (the date Frostad filed the Articles of Incorporation for Lakeview Lofts Homeowners' Association) through July 7, 2006 (the date Frostad notified the condominium owners by letter of his surrender of control of the Lakeview Lofts Homeowners' Association) (App. 13 ¶ 1.4). It is undisputed that the Appellants entered into this agreement with Blackstone during the period of "Declarant control" and, during that entire time, Appellant Lakeview Lofts was the "Declarant" and Appellant Frostad was its representative acting as an officer of the association (Add. 14 ¶ 3.2).

B. Fiduciary Obligations – Good Faith.

In challenging the Trial Court's finding that Appellants' violated the fiduciary duty owed to Respondents, the Appellants are asking this Court to adopt an interpretation of Minn. Stat. §515B.3-120 that is contrary to the plain language of the statute, and are also asking this Court to adopt a factual scenario that is contrary to the Trial Court's findings. Specifically, the Appellants request the Court determine, as a matter of fact and law, that Appellants did not owe a fiduciary duty to Respondents.

1. The Statutory and Common Law Obligation.

Minnesota Statute §515B.3-120 imposes a fiduciary obligation and obligation of good faith on the declarant during the period of declarant control. Minn. Stat. §151B.3-120(2) (2005). The obligation is the same as that applicable to any persons serving a corporation (*Id.*)

The Minnesota Business Corporation Act, Minn. Stat. §302A, describes the fiduciary standard of conduct for a director and officer in a corporation as follows:

> "A director shall discharge the duties of the position of director in good faith, in a manner the director reasonably believes to be in the best interests of the corporation, and with the care an ordinarily prudent person in a like position would exercise under similar circumstances." Minn. Stat. § 302A.251.

> "An officer shall discharge the duties of an office in good faith, in a manner the officer reasonably believes to be in the best interests of the corporation, and with the care an ordinarily prudent person in a like position would exercise under similar circumstances." Minn. Stat. §302A.361.

In addition to this statutory fiduciary duty, officers, directors and shareholders in a corporation owe a common-law fiduciary duty to one another. *Berreman v. West Publ'g Co.,* 615 N.W.2d 362, 370 (Minn.App.2000), *review denied* (Minn. Sept. 26, 2000). See also, *Miller v. Miller,* 301 Minn. 207, 219, 222 N.W.2d 71, 78 (1974) (recognizing the common law principle that officers of a corporation occupy a fiduciary relationship with the corporation); *Wenzel v. Mathies,* 542 N.W.2d 634, 641 (Minn.App.1996) (same), *review denied* (Minn. Mar. 28, 1996); *In re Villa Maria, Inc.*, 312 N.W.2d 921, 922-23 (Minn.1981). The legislature did not abrogate the common law fiduciary duty when it enacted the Minnesota Business Corporation Act (MBCA), Minn. Stat. §§302A.01-917. The common law fiduciary duty continues to be available to an aggrieved party in addition to the statutory duties provided at Minn. Stat. §302A.751, Subd. 3(a), which all shareholders in a closely held corporation owe one another to act in an honest, fair and reasonable manner. See, *Berremann v. West. Pub. Ltd.*, 615 N.W.2d 362, 369 (Minn. App. 1992). The existence of a fiduciary relationship is generally a question of fact. *Carlson v. SALA Architects, Inc.*, 732 N.W.2d 324, 331 (Minn.App.2007), *review denied* (Minn. Aug. 21, 2007).

In a closely-held corporation, the shareholders, as well as the directors and officers of the corporation, have a fiduciary relationship that imposes the highest standard of integrity and good faith. *Pedro v. Pedro*, 489 N.W.2d 798, 801 (Minn.App.1992) ("The relationship among shareholders in closely held corporations is analogous to that of partners."), *review denied* (Minn. Oct. 20, 1992); *Evans v. Blesi*, 345 N.W.2d 775, 779 (Minn.App.1984), *review denied* (Minn. June 12, 1984). "Owing a fiduciary duty includes dealing 'openly, honestly and fairly with other shareholders.' " (*Id*).

As a matter of law, Appellants owed a fiduciary duty to Respondents to act in good faith, with reasonable care, and in the best interests of all condominium owners. Minn. Stat. §302A.251 (director standard of conduct); Minn. Stat. §302A.361 (officer standard of conduct); *Bolander v. Bolander*, 703 N.W.2d 529, 548 (Minn. Ct. App. 2005) (noting fiduciary duty owed by officers and directors of Minnesota corporation); *Pedro v. Pedro*, 489 N.W.2d 798, 801 (Minn. Ct. App. 1992) (discussing the fiduciary duty shareholders in a Minnesota closely held corporation owe each other). By law, Appellants must place the interests of the other owners of units in the project above their own interests, and must deal honestly, openly, and fairly with all condominium unit owners. <u>See</u> *Miller v. Miller*, 222 N.W.2d 71, 81 (Minn. 1974) (discussing duty of loyalty).

Here, the Trial Court found that Appellants owed a fiduciary duty and obligation of good faith to Respondents (Add. 12-13 ¶ 1.0, including all subparagraphs). The Trial Court's finding of a fiduciary duty and duty of good faith is supported by the record and Appellants have failed to present any evidence or argument to the contrary. The "real issue" presented by Appellants is not, as described by Appellants, whether a fiduciary duty exists, but rather whether Appellants breached the fiduciary duty that they owed to Respondents.

2. Appellants' Violation of Fiduciary Duty.

Pursuant to Minn. Stat. §515B.3-120, "The officers and directors appointed by the declarant shall have a duty to fulfill, and to cause the association to fulfill, their respective obligations under the declaration, bylaws, articles of incorporation, and this chapter and to enforce the provisions of the declaration, bylaws, articles of incorporation, and this chapter against all unit owners, including the declarant and its affiliates, in a uniform and fair manner." Minn. Stat. §515B.3-103 (2005). This "duty" is in addition to the general duty to act "in the best interests of the corporation, and with the care an ordinarily prudent person in a like position would exercise under similar circumstances and the duty which all shareholders in a closely held corporation owe one another to act in an honest, fair, and reasonable manner." Minn.Stat. §§302A.251, 302A.751, Subd. 3a (1994).

The scope of the common-law fiduciary duty among shareholders in a closely held corporation is defined as a requirement to deal "openly, honestly, and fairly" with each other. *Berreman v. West Publ'g Co.*, 615 N.W.2d 362, 371 (Minn.App.2000), *review denied* (Minn. Sept. 26, 2000). This duty encompasses both substantive and procedural obligations. *Gunderson v. Alliance of Computer Prof'ls, Inc.,* 628 N.W.2d 173, 185 (Minn.App.2001), *review granted* (Minn. July 24, 2001) *and appeal dismissed* (Minn. Aug. 17, 2001). Included within these duties is "the duty to disclose material information about the corporation."

Berreman, 615 N.W.2d at 371. Whether information is "material" depends on its probable effect on the shareholder's decision-making rights with respect to that shareholder's investment. See, *Id.* at 371-72 (approving of "probability-magnitude approach" for materiality). This balancing necessarily depends on the specific facts of each case (*Id.* at 371). Whether a fiduciary duty has been breached therefore is ordinarily a question of fact (*Id.* at 367).

At the time Appellants and Blackstone entered into their agreement in March/April of 2006, Appellants had not discussed or even disclosed the "Blackstone agreement" to the Respondents or the Lakeview Board (Add. 6 ¶ 7.10). Appellants did not inquire into or otherwise research the financial ability of Blackstone or the Blackstone "purchasers" to buy the various units (Add. 6, ¶ 7.8). And Appellants never inquired into the relationship between the "purchasers" and Blackstone, LLC (Add. 6, ¶ 7.9). These failures are incomprehensible given the structure of the transaction and other factors present during the relevant time period.

At the time of the agreement, Appellants were in a difficult financial position; the condominium units were not selling, interest on the note with KleinBank had increased, real estate taxes on the project were delinquent, and Appellants were facing competition from another geographically close condominium project (Add. 5, ¶ 6.7-6.8). Blackstone entered out of nowhere and offered to buy all of the remaining units—a solution which resolved all of Appellants' problems on the project. The proposal made by Blackstone apparently involved paying full list price for the units, mortgaging the properties to nearly 100% of the list price, and receiving a "management fee" of nearly one million dollars while somehow managing to "flip" the units in a down market for a profit, despite the fact that Blackstone and its "purchasers" were prohibited from leasing or otherwise utilizing the units in a manner to generate income to offset ongoing expenses (Add. 5, ¶ 7.7). Oddly, Appellants contend they simply entered into a verbal agreement, with an unknown entity, by which Appellants agreed to pay in excess of $900,000 over the course of approximately two and one-half months. Not only did Appellants agree to pay Blackstone in excess of $900,000, but Blackstone and Appellants apparently verbally agreed that the "management fee" would be paid only on the final closings; an agreement that violates the Real Estate Settlement Procedures Act ("RESPA") (Add. 15, ¶ 3.4). Despite this purported agreement, there is no writing that contains or references the arrangement and the "management fee" is not contained in or referenced in either the purchase agreements or the closing documents of the first seven closings; it was also not disclosed to the appraisers, nor is there any documentation that the "management fee" was discussed with or approved by lenders for the first seven sales. Based on these and other uncontroverted facts, coupled with the expert testimony provided by Cal Haasken, the Trial Court properly found that Appellants' actions in selling all of the 17 remaining units in this manner was material, raised multiple "red flags" and violated the fiduciary duty Appellants owed to Respondents (Add. 13-16, ¶¶ 3.1-3.7).

Not surprisingly, Appellants ignore the facts of this case and urge the Court to simply adopt a blanket rule that there can never be a breach of fiduciary duty or duty of good faith where the actions at issue involve a party selling property that they own. Of course, Appellants do not cite any authority for this proposition and Respondents' counsel could not locate any case authority supporting this theory. To the contrary, the relevant case law recognizes that determining the existence of a duty and whether a breach occurred is a fact question; the case law further recognizes a wide variety of actions that may breach a fiduciary duty. See, *Evans v. Blesi*, 345 N.W.2d 775, 780 (Minn. App. 1984) (finding a breach of fiduciary duty where the majority shareholder engaged in abrasive and intimidating behavior to accomplish a stock transfer and the resignation of the minority shareholder; in particular, the court found that the majority shareholder shouted at the minority shareholder and threatened to dissolve the corporation and take all the business); *Pedro v. Pedro*, 489 N.W.2d 798 (Minn._App. 1992) (recognizing job, salary and place in management as reasonable expectations in breach of fiduciary duty claim.); *McCallum v. Rosen's Diversified, Inc.*, 153 F.3d 701, 703 (8th Cir. 1998) (recognizing the liberal construction of the term "unfairly prejudicial"). Additionally, the relevant statutes do not contain any such limitations and cannot be fairly read to include any such limiting language. See, Minn. Stat. §645.16 (If the words of a statute are unambiguous, Courts must apply their plain meaning); see also, *State by Beaulieu v. RSJ, Inc.*, 552 N.W.2d 695, 701 (Minn. 1996) (If a statute, construed according to the ordinary rules of grammar, is unambiguous, Courts may not engage in further statutory construction and must apply its plain meaning.).

Here, the Trial Court's findings of fact and conclusions of law provide detailed factual findings and legal analysis supporting the conclusion that Appellants breached their fiduciary duties and obligations of good faith to Respondents, and they should not be reversed (Add. 12-16 ¶¶ 1.1-3.7).

III. APPELLANTS DO NOT HAVE JUSTIFIABLE RELIANCE.

As part of their "defense on appeal," Appellants assert that they are not liable because the respective mortgage lenders approved the financing for the Blackstone purchases (App.'s

Brief, pp. 17-18). But, Appellants' argument neglects to account for the fact that the "management fee" was not contained in, or referenced in, any of the purchase agreements or any of the closing documents for the first seven closings. The "management fee" was also not disclosed to the appraisers nor did Appellants present any evidence that the "management fee" was discussed with or approved by the lenders for the first seven sales (Add. 7 ¶ 8.9). Therefore, Appellants could not have reasonably relied on the mortgage lenders, because Appellants obviously knew the mortgage lenders did not know about the "management fee" until the last sales, by which time all the "up-front" work had been completed and processed—more importantly, there was no reliable evidence presented that the mortgage companies either knew, or approved, of Appellants' "management fee" agreement.[7] Appellants' argument must be rejected.

IV. THE DAMAGES AWARDED ARE PROPER.

A. General Statement of Damages.

A party who breaches a fiduciary duty to another is liable for the damages flowing from the breach, although damages are often not readily calculable. *Commercial Associates, Inc. v. Work Connection, Inc.*, 712 N.W.2d 772 (Minn. App. 2006). Damages can be both compensable and punitive. Damages can include a loss in a shareholder's stock, profits made by a director, or value of property at time of the breach, plus interest. *Pedro v. Pedro*, 489 N.W.2d 798, 802 (Minn. App. 1992). Where there is an injury to property, the law seeks to compensate the owner for the injury sustained. *Kopischke v.*

[7] The only individual Frostad claims he relied on before entering into the agreement with Blackstone was Darik Steinbach. It is worth noting that Mr. Steinbach refuted Frostad's assertion and refused to testify at trial for Appellants (Trans. 273).

Chicago St P M & O Ry., 40 N.W.2d 834 (Minn. 1950). Generally, the proper measure for injury to property is the diminution in value resulting from the injury (*Id.*); see also, CIV JIG 29.10; *O'Connor v. Schwartz*, 229 N.W.2d 511, 513 (Minn. 1975). The primary object of an award of damages in a civil action is just compensation, indemnity, or reparation for the loss or injury sustained. *Clark Oil Co v. Phillips Petroleum Co.*, 148 F.2d 580 (8th Cir 1945). Generally, the claimant is permitted to elect the measure of damages. See, *Hart v. North Side Firestone Dealer*, 235 Minn. 96, 98, 49 N.W.2d 587, 588 (1951);

An owner of real property may testify as to the value of his property even though the owner lays no particular foundation for his opinion. *Housing and Redevelopment Authority for the City of Minneapolis v. Zweigbaum*, 100 N.W.2d 719, 721 (Minn. 1960). Evidence that an owner is familiar with the market value of similar property is sufficient foundation to support a finding of value in the amount of the owner's opinion. *Zweigbaum*, 100 N.W.2d at 721 (Minn. 1960).

B. Statutory Damages.

Minnesota Statute Chapter 515B provides the following with respect to damages:

515B.3-111 TORT AND CONTRACT LIABILITY.

(a) Neither the association nor any unit owner except the declarant is liable for that declarant's torts in connection with any part of the common interest community. An action alleging a tort or contract violation by the association shall not be brought against a unit owner solely by reason of ownership. If the tort or contract violation occurred during any period of declarant control and the association or a unit owner gives the declarant reasonable notice of and an opportunity to defend against the action, the declarant who then controlled the association is liable to the association or to any unit owner for (i) all losses not covered by insurance suffered by the association or that unit owner, and (ii) all costs that the association would not have incurred but for the tort or contract violation.

(b) Whenever the declarant is liable to the association or a unit owner under this section, the declarant is also liable for all expenses of litigation, including reasonable attorney's fees, incurred by the association or unit owner. Any statute of limitation affecting a right of action under this section is tolled until the period of declarant control terminates. A unit owner is not precluded from maintaining an action contemplated by this section because of being a unit owner or an officer or director of the association.

515B.4-116 RIGHTS OF ACTION; ATTORNEY'S FEES.

(a) In addition to any other rights to recover damages, attorney's fees, costs or expenses, whether authorized by this chapter or otherwise, if a declarant or any other person violates any provision of this chapter, or any provision of the declaration, bylaws, or rules and regulations any person or class of persons adversely affected by the failure to comply has a claim for appropriate relief. The association shall have standing to pursue claims on behalf of the unit owners of two or more units.

(b) The court may award reasonable attorney's fees and costs of litigation to the prevailing party. Punitive damages may be awarded for a willful failure to comply.

(c) The remedies provided for under this chapter are not exclusive and do not abrogate any remedies under other statutes or the common law, notwithstanding whether those remedies are referred to in this chapter.

C. Respondent Schneider.

Respondent Schneider purchased his condominium unit from Lakeview Lofts, LLC in January of 2006 at a purchase price of $354,358.47. Respondent currently occupies his unit. At trial, Schneider presented evidence that the present market value of his property is only $166,000 (Add. 2, 18 ¶s 3.3, 7.4, Trans. 212). Plaintiff Schneider testified that the damages he sustained as a result of Appellants' actions were a decrease in the value of his condominium by 25-28% from the original purchase price (Trans. 422). Respondents' expert, Cal Haasken, testified that Schneider's property suffered a diminution in value—attributable to Appellants' actions—of 25% of the prior value, which, contrary to Appellants' assertions, Mr. Haasken did quantify as the purchase price (Trans. 359, 483). Haasken offered extensive testimony concerning the damages in this matter and concluded that the tax assessed value was indicative of the present fair market value and that he physically reviewed the subject property and inspected comparables (see generally, Trans. 354-408, 484).

Based on the evidence presented, the Court correctly found Schneider's damages to be $96,225.26, calculated as $354,558.47 (purchase price) less 26% (the average market deprecation in the seven county metro area between 2006 and 2010) less the current market value of $166,000 (Add. 18 ¶ 7.4); See, *Barnett v. St. Anthony Falls Water-Power Co.,* 22 N.W. 535, 536 (Minn. 1885) (Evidence was given on the part of the plaintiff as to the value of property, assuming it to be uninjured, and as to the value with the existing injury, but such values were estimated as of the time of the trial, which was three years after the injury occurred. The evidence being evidently offered only as proof of damages, and no objection having been interposed, held sufficient to sustain the verdict.); see also, *LaValle v. Aqualand Pool Co., Inc.*, 257 N.W.2d 324 (Minn. 1977) (property owner allowed to testify on value property would have had if constructed according to contract); *Jackson v. Buesgens*, 186 N.W.2d 184 (Minn. 1971) (owner allowed to testify as to property value on issue of damages; foundation objection went to weight, not admissibility); *Dosedel v. City of Ham Lake*, 414 N.W.2d 751 (Minn. Appl. 1987) (court accepted owner's opinion in special assessment case that property had not increased in value after paving of road).

D. Plaintiff Larson.

Respondent Larson purchased his condominium pre-construction from Lakeview Lofts, LLC in 2005 at a purchase prince $375,140.84. As a result of purchasing the unit prior to construction, Larson testified he received a significant reduction in the purchase price;

Appellants did not dispute this assertion (Add. 2, ¶ 2.3). Further, there was no evidence offered that Larson's pre-construction price was affected at all by the general housing market decline.

Larson sold his unit in October of 2009 for the amount of $270,000.00 (Add. 18, ¶ 7.3). At trial, Larson offered evidence of a market analysis he conducted to determine his damages and concurred with Mr. Haasken's testimony/analysis of the differentiation in market values between Lakeview Lofts as opposed to the general Minnetonka area (Trans. 408-414). Larson testified to a loss of several hundred thousand dollars (Trans. 90, 100, 413).

Appellants' expert, Mary Bujold, submitted an exhibit which provided an analysis of the average price of condominiums in the seven county metro area—excluding Lakeview Lofts and outliers—for the years 2004 and 2009. During this period of time, the evidence presented by Ms. Bujold established that the condominium market had a decline in market value of 1% (Add. 11, ¶ 10.8). Based on the evidence submitted by Appellants, the Trial Court determined that Larson's condominium should have had a value of $371,389.43 (representing a 1% market decline from Larson's purchase price) and from this amount the Trial Court subtracted $270,000 (the amount Larson sold his unit for in 2009) and arrived at damages of $101,389.43 (Add. 18 ¶ 7.3).

E. The Damages Awarded Were Proper.

In an effort to obtain a reversal of the Trial Court, Appellants request that the Court adopt the "damage test" they created for this appeal and then—not surprisingly since they made up the rules—seek to show how Respondents did not meet the test. Among the requirements that Appellants seek to impose is a requirement that Respondents offer evidence as to the value of the condominium units at the time of the foreclosure and a requirement that the Trial Court use the same damage calculation for both Respondents.

It is unclear why Appellants believe that the value of condominium units at the time of the foreclosure is required—it is worth noting that neither parties' expert used this "baseline" in preparing their damage analysis at trial—as the measure of damages involves: (1) amount paid for the property; (2) amount of decline in market value attributed to Appellant' breach of their duties; and (3) amount of decline in market value attributed to other factors. The additional issue raised by Appellants concerning the variation in damage analysis between Larson and Schneider is a red herring. The variations in the measure of damages used for Larson and Schneider were appropriate given that Larson sold his property and Schneider did not. The properties required a different analysis and the Trial Court's findings are supported by the record. The Trial Court's findings are supported by the evidence presented and must not be reversed.

F. Attorneys' Fees.

Minnesota Statute §§515B.3-111 and 515B.4-116 provides for the recovery of attorneys' fees to wit:

> Minn. Stat. §515B.3-111TORT AND CONTRACT LIABILITY.
>
> (b) Whenever the declarant is liable to the association or a unit owner under this section, the declarant is also liable for all expenses of litigation, <u>including reasonable attorney's fees</u>, incurred by the association or unit owner. Any statute of limitation affecting a right of action under this section is tolled until the period of declarant control terminates. A unit owner is not precluded from maintaining an action contemplated by this section because of being a unit owner or an officer or director of the association.
>
> Minn. Stat. §515B.3 (emphasis added).

515B.4-116 RIGHTS OF ACTION; ATTORNEY'S FEES.

> (b) The court may award reasonable attorney's fees and costs of litigation to the prevailing party. Punitive damages may be awarded for a willful failure to comply.

Minn. Stat. §515B.4-116 (emphasis added).

The Court found that an award of attorneys' fees was proper in this litigation and awarded the fees in accordance with the invoices submitted. It does not appear that Appellants are challenging this part of the damage award.

CONCLUSION

The law recognizes that determining the existence of a fiduciary duty, and whether a breach of that duty has occurred, are questions of fact. Appellants were in a position of control over the Lakeview Lofts condominium project and owed Respondents both statutory and common-law fiduciary duties and duties of good faith. Appellants put their interests above those of Respondents and entered into an agreement with Blackstone that can, at best, be characterized as suspicious. On its face, the deal with Blackstone had no chance of ever succeeding and a reasonable person in Appellants' position should have recognized the transaction as such. From its inception, the structure of the deal raised multiple red flags; instead of disclosing the Blackstone agreement to the individuals who would be left to deal with its after effects, Appellants turned a blind eye to the situation and cashed out. The damages resulting from Appellants' actions are very real and resulted in the value of Respondents' units being diminished and a loss of investment. Based on the evidence produced at trial and the evaluation of witness testimony, the Trial Court properly found that Appellants owed Respondents a fiduciary duty and their actions in selling the 17 condominium units to Blackstone breached that duty. The Trial Court properly awarded damages in accordance with the evidence produced at trial and relevant law. Based on the foregoing, Respondents respectfully request the Trial Court's findings of fact and conclusions of law be upheld, and the resulting judgments affirmed.

Respectfully submitted,

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