

NO. A04-2338

State of Minnesota
In Supreme Court

John S. Drewitz,

Appellant,

v.

Motorwerks, Inc., a Minnesota Corporation,
R. Jack Walser, Paul M. Walser and Andrew D. Walser,

Respondents.

APPELLANT'S BRIEF

Date of Filing of Court of Appeals' Decision: December 13, 2005

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STATEMENT OF LEGAL ISSUES

- I. **Is the Court of Appeals wrong to conclude that Motorwerks has not acted in an unfairly prejudicial manner or breached its fiduciary duty to Drewitz?**

Court of Appeals Holding: The Court of Appeals ruled against Drewitz' claim Motorwerks acted in an unfairly prejudicial manner and breached its fiduciary duty.

Most Apposite Case – *Pedro v. Pedro*, 489 N.W.2d 798, 802 (Minn. App. 1998).

- II. **Did Drewitz' shareholder status end when his employment terminated?**

Court of Appeals Holding: Drewitz' shareholder status extends until closing of his shares according to the shareholder agreement.

Most Apposite Case – *Stephenson v. Drever*, 16 Cal.4th 1167 (California 1997).

- III. **Is Drewitz' claim for shareholder status and distributions barred by res judicata because it was or could have been brought as part of the first action?**

Court of Appeals Holding: The Court of Appeals held Motorwerks breached the shareholder agreement, and held shareholder status and the right to shareholder distributions continue until a proper tender according to the shareholder agreement.

Most Apposite Case - *Hauschildt v. Beckingham*, 686 N.W.2d 829, 840 (Minn. 2004).

- IV. **Is Drewitz claim for shareholder status and distributions barred by res judicata because he was required to amend his first complaint to state such a claim but failed to do so?**

Court of Appeals Holding: The Court of Appeals held that Drewitz was not required to amend his complaint to prevent claim preclusion.

Most Apposite Case - *Fabio v. Bellomo*, 504 N.W.2d 758, 761 (Minn. 1993)(citing Minn.R.Civ.P. 15.01).

STATEMENT OF THE CASE

Appellant, as a former employee and 30% shareholder of Respondent BMW dealership Motorwerks, Inc., brought an action in May 2004 against Respondents in Hennepin County District Court for a buy-out at the fair value of his shares under Minn. Stat. 302A.751, breach of fiduciary duty, and failure to make shareholder distributions. The District Court, Hon. Marilyn Rosenbaum, dismissed the complaint on res judicata grounds, based on Appellant's 1999 lawsuit against Respondents for similar relief based on termination of his employment as general manager.

Appellant appealed to the Minnesota Court of Appeals, which reversed on December 13, 2005, holding Appellant was not divested of his shareholder rights upon termination of his employment, and that Respondents breached the shareholder agreement by failing to make a valid tender to redeem the shares.

The Court of Appeals denied the claim for a fair value buy-out of his shares based on unfair prejudice and denied the claim for breach of fiduciary duty.

Appellant petitioned the Minnesota Supreme Court for review of the unfair prejudice and breach of fiduciary duty claims.

Respondent cross-petitioned for review of the Court of Appeals' holding that Appellant had continuing shareholder status and distribution rights, and that those claims were not barred by res judicata. Respondent

also petitioned for review of the holding it breached the shareholder agreement.

The Supreme Court granted Appellant's petition for review on the issues of unfair prejudice and breach of fiduciary.

The Supreme Court partially granted Respondents' cross-petition for the issues of shareholder status, distribution rights, and res judicata of those issues. The remaining issues of Respondents were specifically denied or not granted.

STATEMENT OF FACTS

John Drewitz purchased a 30% shareholder interest of Respondent Motorwerks, Inc. ("Motorwerks"), a BMW automobile franchise, while he was the general manager of the dealership. The individual Respondents own the remaining 70%.

Respondents involuntarily terminated Drewitz' employment on December 24, 1998 by delivering a letter to his home on Christmas Eve. Drewitz commenced an action against Respondents which sought relief for wrongful termination under his employment contract and a fair value buyout of his shares under Minn. Stat. § 302A.751.¹ The Ramsey County District Court ruled on December 29, 1999 the parties' shareholder relationship was governed by a Shareholder Sale/Purchase/Redemption/Voting/Control Agreement ("Shareholder Agreement") (A1) which

¹ Ramsey County District Court Case No C0-99-508.

also petitioned for review of the holding it breached the shareholder agreement.

The Supreme Court granted Appellant's petition for review on the issues of unfair prejudice and breach of fiduciary.

The Supreme Court partially granted Respondents' cross-petition for the issues of shareholder status, distribution rights, and res judicata of those issues. The remaining issues of Respondents were specifically denied or not granted.

STATEMENT OF FACTS

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¹ Ramsey County District Court Case No. C0-99-508.

allowed Respondents to repurchase Drewitz' shares at book value rather than fair value.

Drewitz' appeal was affirmed by the Court of Appeals on May 1, 2001. *Drewitz v. Walser, et al.* 2001 WL 436223 (Minn. App. 2001) ("*Drewitz I*"). The Minnesota Supreme Court denied Drewitz' Petition for Review on June 27, 2001.

The Court of Appeals in *Drewitz I* affirmed the trial court's 1999 ruling which strictly construed the Shareholder Agreement to conclude the buy-back provision of the Shareholder Agreement was technically triggered when the employment contract expired, because the Shareholder Agreement provided for a right of redemption of Drewitz' shares upon termination of his employment "for any reason." (*Drewitz I*). The Shareholder Agreement provided for a "book value" buy-back within 90 days of termination of employment at the expiration of the employment contract (*Id*). Drewitz' employment contract ended on March 31, 1999. The closing and purchase of Drewitz' shares were to have occurred 90 days later.

After the appellate court ruling in 2001, Respondents refused to unconditionally tender the purchase price plus interest as required by the Shareholder Agreement. Drewitz eventually sued in 2004 for the mandatory purchase of his shares at fair value and for shareholder distributions. The trial court dismissed the action, and Drewitz appealed.

The Court of Appeals reversed. (*Drewitz v Motorwerks*, 706 N.W.2d 773 (Minn. App. 2005).

The Court of Appeals described Respondents' failed tenders by offering wrong amounts, repudiating contractual interest, and demanding additional conditions to the tender which were not part of the Shareholder Agreement. *Drewitz*, supra, 786. The Court of Appeals unanimously held Respondents breached the Shareholder Agreement, a holding not under review by this Court's Order of February 14, 2006.

The Court of Appeals held Drewitz remained a shareholder until Respondents made a proper tender with interest for his shares. As a shareholder, the Court of Appeals held Drewitz was entitled to shareholder distributions until his shares were repurchased. *Drewitz*, supra 787. The Court of Appeals held Drewitz' shareholder status did not end, and shareholder distribution rights continued until such time as Respondents repaid Drewitz' \$355,862 investment in the corporation with interest.

The Court of Appeals held Drewitz was not unfairly prejudiced as a shareholder, and that Respondents did not breach their fiduciary duties to Drewitz. The Court of Appeals also ruled the unfair prejudice and fiduciary duty claims were barred by res judicata, because unfair prejudice and fiduciary duty claims were part of Drewitz' 1999 suit based on his employment termination.

Drewitz' 2004 suit for unfair prejudice and breach of fiduciary duty was based on Respondents' failure to pay him after the first appeal.

This Court granted Drewitz' Petition for Review of his claims for unfair prejudice and breach of fiduciary duty. Supreme Court Order, February 14, 2006.

This Court also granted Respondents' Cross-Petition for Review of whether Drewitz' shareholder status ended when his employment terminated, and whether res judicata barred Drewitz' claim for shareholder status and distributions, on the ground the claims were part of the first action or could have been part of the first action had Drewitz sought to amend his complaint.

The Petitions for Review were only partially granted on February 14, 2006 for the limited issues described above. This Court rejected Respondents' issues claiming Drewitz waived tender of payment and rejected Respondents' petition for review that fact issues require a remand of the holding Respondents breached the contract to tender.

The facts statement of the Court of Appeals is incorporated by reference.

STANDARDS OF REVIEW

The Court of Appeals concluded that Motorwerks has not acted in an unfairly prejudicial manner and has not breached its fiduciary duty to a minority shareholder. This is a question of law and is reviewed by this

court *de novo*. *Art Goebel, Inc. v. North Suburban Agencies, Inc.*, 567 N.W.2d 511, 515 (Minn.1997).

The Court of Appeals denial of Drewitz' motion for buy-out on the basis of *res judicata* is also reviewed by this court *de novo*. *Care Inst. v. County of Ramsey*, 512 N.W.2d 443, 446 (Minn. 2000).

The Court of Appeals decision is based upon interpretation of the Shareholder Agreement. "[T]he construction and effect of an unambiguous contract are questions of law that we review *de novo*." *Wolfson v. City of St. Paul*, 535 N.W.2d, 384, 386 (Minn. App. 1995) (citing *Empire State Bank v. Devereaux*, 402 N.W.2d, 584, 587 (Minn.App. 1987)), *review denied* (Minn. September 28, 1995).

INTRODUCTION

This Court granted both Appellant and Respondents' Petitions for Review of four issues.

1. Was the Court of Appeals wrong to conclude that Motorwerks has not acted in an unfairly prejudicial manner or breached its fiduciary duty to Drewitz?
2. Did Drewitz' shareholder status end when his employment terminated?
3. Is Drewitz' claim for shareholder status and distributions barred by *res judicata* because it was or could have been brought as part of his first action?

4. Is Drewitz' claim for shareholder status and distributions barred by res judicata because he was required to amend his first complaint to state such a claim but failed to do so?

ARGUMENT

1. The Court of Appeals was wrong to conclude that Motorwerks has not acted in an unfairly prejudicial manner or breached its fiduciary duty to Drewitz.

This issue contains two interrelated issues:

- a. Whether the Court of Appeals was wrong to conclude that Motorwerks has not acted in an unfairly prejudicial manner to a minority shareholder in his capacity as a shareholder; and
- b. Whether the Court of Appeals was wrong to conclude that Motorwerks has not breached its fiduciary duty to Drewitz.

Unfairly Prejudicial Conduct

There is a clear showing of unfairly prejudicial conduct to a minority shareholder by Respondents. Even the dissent found that “Respondents have undoubtedly breached the agreement . . .”² The Court of Appeals held that Drewitz was still a shareholder because Motorwerks never performed its contract to pay the shareholder agreement price with statutory interest. If it were found that the shareholder relationship had terminated (which it had not), Respondents would argue that terminating shareholder status avoids its duty not to act unfairly prejudicial to its former

² *Drewitz v. Motorwerks*, 706 N.W 2d 773, at 789 (Minn. App. 2005).

business partner. Both legislative intent and court interpretations of the statute consistently have protected minority shareholder rights based on initial reasonable expectations and as expectations develop over the course of the relationship.³

Whether Motorwerks acted in an unfairly prejudicial manner or breached its fiduciary duty to Drewitz may become entangled in whether Drewitz' status as a shareholder ended when his employment terminated. In addition to the breaches of fiduciary duty and the breaches consisting of unfairly prejudicial conduct, if Drewitz remained a shareholder, which he did, the failure to include Drewitz in distributions is an additional breach of Motorwerks fiduciary duty to its minority shareholder and could only have occurred after Respondents failed to tender payment.

The Court of Appeals found no cases on point in Minnesota and therefore examined two lines of authority from other states. In the first line, which the Court of Appeals rejects, courts reasoned that the requirement that an employee transfer his or her shares to the corporation indicates the parties contemplated that the employee would be a shareholder only while employed by the corporation, implying an intent to terminate shareholder status even if it is omitted from the contract.

³ In *Berreman v. West Publishing Co.*, 615 N.W.2d 362 (Minn. App. 2000) Berreman submitted the affidavit of a law school professor who stated he drafted the 1983 amendments to Minn. Stat. 302A.751. He stated the amendments were not intended as a ceiling to limit fiduciary duties, but solely as a floor to insure that shareholders in "closely held corporation" would be automatically entitled to the doctrines referred to in Minn. Stat. § 302A.751, Subd. 3a.

Under the second line of authority, which the Court of Appeals held persuasive and followed, an employee's shareholder status terminates at employment only if the buy-sell agreement expressly provides that title to an employee's stock passes automatically upon termination. In following this reasoning, the Court relied on *Stephenson v. Drever*, 16 Cal.4th 1167 (California 1997). The narrow issue in *Stephenson* was whether the agreement implies an intention by the parties to deny the minority shareholder rights during the period before the shareholder is paid. The holdings in that case were delineated by the Minnesota Court of Appeals as follows:

1. The claimed implication of intent was inconsistent with the express provision of the buy-sell agreement which "gave the corporation the right and obligation to repurchase the employee's shares." *Drewitz*, supra, 784.
2. The process specified in the agreement for valuation of shares contemplated a delay in repurchase of the shares and therefore "tend[ed] to negate any inference that the parties intended that the repurchase of the shares be consummated – and a fortiori that [the former employee's] status as a shareholder be terminated – immediately upon termination. *Id.*
3. An implied intent would have the effect of stripping the right to dividends even though the former employee remained a legal

owner of shares. The court in *Stephenson* declined to “interpret the contract to produce this result without a compelling reason to draw the inference proposed.” *Id.*

4. The termination of shareholder status before the tender of the purchase price would have the effect of relieving the corporation of its fiduciary duties to a terminated minority shareholder employee. This would allow the corporation to control corporate activities in a manner detrimental to the minority. “[T]he implied contractual provision was inconsistent with the strong public interest of ensuring that corporations faithfully comply with their fiduciary obligation to minority shareholders.” *Id.*

In the *Stephenson* court's analysis, the court ruled that a buy-sell agreement is an executory agreement to buy and sell personal property, and title does not pass to the buyer until delivery is made unless there is something in the contract specifying a different intention. *Stephenson*, 1173. The court also held the shareholders were entitled to the dividends paid on the shares. *Id.* 1174. “[P]laintiff remains a shareholder of record of the corporation with all the rights appurtenant to that status.” *Id.*

The *Stephenson* court also rejected the defendant's argument that public policy considerations should infer termination of shareholder status with the shareholder's termination of employment, saying, “First, defendants cite no authority for the proposition that ‘public policy

considerations' can trump the rule of substantive law that a shareholder under an executory contract to sell his stock is entitled to the benefits of ownership until delivery is made or tendered to the buyer . . .”

Stephenson, supra, 1182.

The argument that allowing a terminated employee shareholder rights would “encourage employee-shareholder to initiate frivolous litigation in order to delay the repurchase of their shares” was also addressed in

Stephenson.

It could equally well be argued that to hold as the Court of Appeal did would encourage corporations and their majority shareholders to delay consummating the repurchase of the shares of a former employee after terminating his employment, thereby extending the period during which the latter remains, as we have said, a shareholder without a shareholder’s rights, voiceless in the conduct of the business and defenseless against neglect or overreaching by management. *Id.* 1183.

The *Stephenson* court stated,

A shareholder without a shareholder’s rights is at best an anomaly, and at worst a shadowy figure in corporate limbo who would be voiceless in the conduct of the business of which he is part owner and largely defenseless against neglect or overreaching by management. *Id.* 1177-1178

The California court in *Stephenson* articulated reasons not to add terms to a contract by “implication” when the parties did not include the important term explicitly. Furthermore, considering Minnesota’s case history of protecting minority shareholder rights, the Minnesota rule to be adopted in this case may be stronger than the rule in California. Minn.

Stat. § 302A.751 and Minn. Stat. § 302A.467 give the court broad equitable powers to accomplish a just result consistent with the obligation to avoid unfair prejudice toward a minority shareholder. Even if shareholder status did automatically end when employment was terminated without repaying the investment, it still does not follow that the court's equitable power to prevent unfair prejudice to a minority shareholder would cease to exist. Equitable power carries inherent flexibility to prevent injustice and is not bound by raw technicalities. Certainly a shareholder relationship must initially exist to come under Minn. Stat. § 302A, but the quasi-partnership duties of a closely-held corporation imply a continuing duty to avoid unfair prejudice in redeeming a partner's investment. "Although the statute does not define the phrase 'in a manner unfairly prejudicial toward . . . shareholders' we have interpreted the phrase to mean conduct that frustrates the reasonable expectations of all shareholders in their capacity as shareholders . . ." *Berreman, supra*. Respondents would urge the Court to rule they could continue to use Drewitz' one-third of a million dollar investment and keep all the corporate profits. And Drewitz' only remedy would be contractual, as though Drewitz held a low-interest promissory note. Such conduct by Respondents in breach of the Shareholder Agreement are unfairly prejudicial to Drewitz' reasonable expectation to a return on his investment until it is repaid.

The Court of Appeals unanimously recognized an undeniable breach of the contractual obligation of unconditional tender. (*Drewitz*, supra, 787, 789.) A continuing failure and refusal to honor a contract (undoubtedly frustrating the reasonable expectations of the minority shareholder) demonstrates a clear showing of unfair prejudice to the minority shareholder in this case. When the majority breaches its own contract, it would be unfairly prejudicial to add a term to the contract by “implication” purely to defeat a minority shareholder’s rights. In *Drewitz I*, the Shareholder Agreement was strictly construed. A similar standard of construction should be applied in this case. The majority shareholders urge a loose interpretation only when it favors their desired outcome, but the standard should not change.

The threat of horrors argument advanced by the corporate majority and any other business owners is easily thwarted – merely honor the contract. And if majority controllers desire shareholder status to automatically end, then at least say so explicitly in a written shareholder agreement. To ask the court to re-write the shareholder agreement after the fact is inconsistent with fundamental contract law.

Breach of Fiduciary Duty

“Fiduciary duty is the highest standard of duty implied by law.”

Black’s Law Dictionary, 625 (6th ed. 1990) cited in *D.A.B v. Brown*, 570

N.W.2d 168 (Minn. App. 1997). A fiduciary duty to a departing shareholder continues until the minority shareholder is actually paid for the shares.

The facts of the case which show unfair prejudice also demonstrate a breach of fiduciary duty. The Court of Appeals erroneously concluded there was no unfair prejudice and no breach of fiduciary duty to Drewitz. This ruling is challenged on appeal to the Supreme Court for the following reasons:

The majority shareholders continue to have fiduciary duties to a minority shareholder until the shareholder has been paid for his shares and (not "or") he ceases to be a shareholder. Fiduciary duties imply fairness to a business partner, and a business partner who holds money belonging to his partner must especially be fair when performing financial agreements between the partners to redeem a partner's investment. This principle is illustrated in other contexts of fiduciary relationships where fiduciary duties continue not only to the end of the relationship but its aftermath to honor commitments which arise from the relationship. For example, a trustee who resigns from trust duties would nevertheless have a continuing fiduciary duty to account to the trust and the beneficiary until full payment is made. No court would hold a beneficiary should be forced to sue for duty to account for money which is owed, without also ruling the trustee is in breach of its fiduciary duty. It is not a simple debtor/creditor relationship when a party owes a fiduciary relationship to another, and the fiduciary

relationship must continue as long as funds are held with fiduciary obligations attached to the handling of the money. Fairness to account includes the duty to faithfully discharge the trust duties.

Likewise, a lawyer has a fiduciary duty to account to a client for funds in the lawyer's trust account. The lawyer has a continuing fiduciary obligation to properly handle and account for entrusted funds, even if the lawyer is terminated and the attorney-client relationship ends.

If the fiduciary duty as well as shareholder status continues, the remedy for a breach of fiduciary duty should parallel the remedy for unfair prejudice. The fiduciary duty to pay according to the contract and to deal fairly with a partner is similar to the duty to honor *Drewitz*' reasonable expectation to rely on a final appellate court ruling in 2001 that he would be paid book value plus interest. The statutory remedy for unfair prejudice is a buy-out at fair value. See Minn. Stat. § 302A.751, Subd. 2. The non-statutory remedy for fiduciary duty should be co-extensive with unfair prejudice under Minn. Stat. § 302A.751, when the remedy is simply for payment of a fair value of a closely-held shareholder's investment.⁴

Respondents held hostage over a third of a million dollars belonging to

⁴ "The *Pedro* court held that where a shareholder is entitled to be bought out because he has been treated in an unfairly prejudicial manner, and where a shareholders' agreement sets forth the price at which he is to be bought out, he can be awarded damages for breach of fiduciary duty for the difference between the fair value of his shares and the purchase price specified in the shareholders' agreement." *Bench and Bar*, Upholding Shareholders' Interests – 20 Years with the Minnesota Business Corporations Act, Oct. 2001, William Pentelovitch and Cynthia F. Gilbertson citing to *Pedro v. Pedro*, 489 N.W.2d 798, 802 (Minn. App. 1998).

Drewitz. And they paid him nothing while distributing all investment returns to themselves. Having breached the obligations of the contract, Motorwerks should not enjoy the favorable benefits of the contract to purchase Drewitz' shares for less than fair value.⁵ This would force Drewitz to perform his commitment to Respondents even though Respondents breached their commitment.

Respondents state on page 26 of their brief to the Court of Appeals, "If he wants to enforce the parties' negotiated shareholder agreement, he can sue for what he claims is the proper book value with accrued interest." Fiduciary duty must prevent parties from cavalierly refusing to honor a negotiated agreement and forcing a minority shareholder to suffer the expense, delay and treachery of a lawsuit. Even with the agreed book value, Respondents would still force a lawsuit for no reason, presuming Respondents have little to lose while they burden an estranged less wealthy partner. Respondents' position is outrageous and proves the point of this case by its patent oppression of the minority shareholder.

Respondents mistakenly state, "Notably, however, all negotiations with respect to the applicable period for interest assume that it began to accrue on March 31, 1999 . . . Ultimately, however, the parties' accountants could not reach a final settlement. . ." (Respondents' Court of Appeals

⁵ "[W]here performances are to be exchanged under an exchange of promises, each party...will not be called upon to perform his remaining duties...if there has already been an uncured material failure of performance by the other party." *Restatement (Second) of Contracts* § 237 cmt B (1981).

Brief page 9). Respondents are incorrect in both statements. In fact, the accountants *did* reach an agreement on the book value. See Appellant's Exhibits A30 and A36⁶. Settlement became such a "moving target" that no agreement lasted long enough to become a tender. It is doubtful Respondents ever would have voluntarily honored its obligation to purchase Drewitz' shares, especially when Respondents invite a suit over an agreed amount. All of this transpired in 2002, after the end of the first case.

While the terms "unfair prejudice" and "breach of fiduciary duty" are not defined terms in Minn. Stat. § 302A, both are described in precedential decisions of Minnesota Courts. A controlling shareholder of a closely held corporation owes a fiduciary duty to deal openly, honestly, and fairly with minority shareholders. *Pedro v. Pedro*, 489 N.W.2d 798 (Minn. App. 1992) *review denied* (Minn. Oct. 20, 1992); *Evans v. Blesi*, 345 N.W.2d 775 (Minn. App. 1984), *review denied* (Minn. June 12, 1984). The highest standards of good faith and integrity apply in fiduciaries' dealings with one another. *Pedro*, *supra*. The phrase, "unfairly prejudicial" is to be interpreted liberally. *Pedro v. Pedro*, 463 N.W.2d 285 (Minn. App. 1990)

⁶ Letter from CFO of Walser Automotive Group, Inc, stating "Enclosed please find a copy of the stock proceeds calculation with the elements of which [sic] we agreed upon . . . After consideration I have come to realize that interest is not appropriate for the period prior to July 2001 . . . I used an interest rate of 6% which is based on the methodology we discussed. The rate is lower than the 7% we talked about . . ." and letter to the CFO from Drewitz' accountant, "Your concept of no interest because of legal actions and the Supreme Court ruling was new to me. . . I thought the settlement you, Lee and I discussed in our meeting in your store was fair and reasonable."

review denied (Minn. Jan. 24, 1991) and Reporter's Notes to Minn. Stat. § 302A.751.

At common law, shareholders owe one another a fiduciary duty. See *Fewell v. Tappan*, 27 N.W.2d 648, 654 (Minn. 1947). "The court describes [fiduciary] duty as one of 'utmost good faith and loyalty' . . ." *Donahue v. Rodd Electrotpe Co.*, 328 N.E.2d 515 (Mass. 1975) discussed in *Berremán*, *supra*. "Only South Carolina which has a statute that references both oppressive and unfairly prejudicial conduct, has explicitly defined unfairly prejudicial [conduct] . . ."

1. A visible departure from the standards of fair dealing and a violation of fair play on which every shareholder who entrusts his money to a company is entitled to rely; or
2. A breach of fiduciary duty of good faith and fair dealing; or
3. Whether the reasonable expectations of the minority shareholders have been frustrated by the actions of the majority; or
4. A lack of probity and fair dealing in the affairs of a company to the prejudice of some of its members; or
5. A deprivation by majority shareholders of participation in management by minority shareholders."

Dealing openly, honestly and fairly, with the highest standards of good faith and integrity does not describe the actions of Respondents who were entrusted with Drewitz' investment.

This unfairly prejudicial conduct by Respondents since the May 2001 decision by the appellate courts meets the standard triggering a buy-out at fair value of the shareholder's interest. For a minority shareholder to receive fair value is not a windfall – by definition the value must be "fair." A fair value buy-out only means that an advantage given by the contract is lost if a majority "undoubtedly breaches the agreement." The Court of Appeals cites to *Craigmile v. Sorenson*, 248 Minn. 286, 292, 80 N.W.2d 45, 49 (Minn. 1956) which states "It is a principle of fundamental justice that if a promisor is himself the cause of the failure of performance . . . of an obligation due him . . . he cannot take advantage of the failure." Respondents should not be allowed to take advantage of the right to a book value buy-out when it is undisputed they failed to tender payment according to the terms of their own agreement.⁷

In a key point regarding fiduciary duty, the Court of Appeals, at page 785, stated that if the parties intended shareholder status to terminate at the termination of employment, irrespective of tender, that would unfairly strip a minority shareholder of all shareholder rights while he remains legal owner of the shares. The Court of Appeals also rejected a foreign authority which holds the implied termination of shareholder status upon termination from employment served a valid business purpose because it

⁷ Respondents' Petition for Review of the Court of Appeal's disposition of this issue claiming a fact question was implicitly rejected by this Court's order of February 14, 2006

allows the corporation to be controlled by employees and avoids the possibility of interference with management by a former employee bearing a grudge against a former employer. *Gallagher v. Lambert*, 74 N.Y.2d 562, 549 N.Y.945, 549 N.E.2d 136 (1989). Yet all shareholders in a closely-held corporation owe a fiduciary duty to one another, that of the "utmost good faith and loyalty." *Rodd*, supra.

MOTORWERKS' ISSUES

The Supreme Court allowed the following issues to be raised by Motorwerks.

- 1. Did Drewitz' shareholder status end when his employment terminated?**
- 2. Is Drewitz' claim for shareholder status and distributions barred by res judicata because**
 - a. It was part of the first action; or**
 - b. It could have been brought as part of his first action?**

Shareholder Status

The Court of Appeals, relying on the language in the negotiated agreement between the parties, held nothing in the contract would have terminated Drewitz' shareholder status. "Drewitz remained a shareholder until Motorwerks tendered full payment for his shares unconditionally." *Drewitz*, supra, 785.

In addition, the Court of Appeals noted that neither Appellant nor Respondents claimed the contract between the parties was ambiguous. *Drewitz, supra*, 783. "In order to consider the intent of the parties or the circumstances surrounding the agreement the district court must first determine that the instrument is ambiguous." *Marso v. Mankato Clinic, Ltd.*, 153 N.W.2d 281 (Minn. 1967). "Here, having found no ambiguity, the district court properly restricted its consideration to the language of the instrument..." *Collins Truck Lines, Inc. v. Metropolitan Waste Control Comm.*, 274 N.W.2d 123 (Minn. 1979).

In fact, the agreements between the parties were negotiated with both parties represented by counsel. Respondents had a central role in negotiating and drafting the Agreement. There is nothing "implicit" in the Agreement that would reflect a reasonable expectation at the time of the inception of this Agreement that shareholder status would terminate along with the shareholder's employment. It is, however, explicit in the Agreement that shareholder status would end within ninety (90) days because of the express provision that the closing would occur within that time frame. The only expressed consequence of employment termination was that Drewitz could not purchase more shares. *Drewitz, supra*, 785. Respondents should not now be allowed to turn to the judicial system requesting a modification of the negotiated agreement. No statewide impact would occur if the agreement is upheld as written other than the

familiar reminder to be explicit when drafting contractual agreements.⁸ The statewide impact would reinforce the already well established concept that parties should negotiate the terms of a contract to reflect each party's expectations and requirements. If Respondents find it "implicit" that termination of employment is also a termination of shareholder status, it remains the understanding of Appellant that it did not. The Court of Appeals decision stated in its decision, "A holding to the contrary would make the provisions for the transfer of shares at closing unnecessary." (p. 785). *Drewitz, supra*, 785.

The discharged employee remains a shareholder until the corporation repurchases the shares according to the terms of the buy-sell agreement. This is consistent with the fact that the shareholder still has an investment in the business. Suppose the Respondents couldn't pay because they had depleted the company's finances. In that case, the shareholder would remain a shareholder in the company. There is no logical reason a different rule would lie if Respondents simply won't pay.

The rule urged by Respondents would allow a corporation to keep a shareholder's investment and use it for profit-making purposes without sharing profits with the minority shareholder investor. "Those in control of closely held corporations have a substantive obligation, for instance . . .

⁸ "[T]he cardinal purpose of constructing a contract is to give effect to the intention of the parties as expressed in the language they used in drafting the whole contract." *Art Goebel, Inc. v. North Suburban Agencies, Inc.*, 567 N.W.2d 511 (Minn. 1997).

not to use corporate assets preferentially.” *Crosby v. Beam*, 47 Ohio St. 3d 105, 548 N.E.2d 217, 221 (Ohio, 1989), quoted in *Gunderson v. Alliance* 628 N.W.2d 173 (Minn. App. 2001).

Res Judicata

Res judicata applies as an absolute bar to a subsequent claim when the earlier claim involved the same set of factual circumstances.

Hauschildt v. Beckingham, 686 N.W.2d 829, 840 (Minn. 2004).

Drewitz’ claim is not barred, therefore, because the claims are based on the fact that Respondents have undoubtedly breached the agreement governing termination of Appellant’s status as a shareholder by failing to pay him after the Appellant Court’s decision. Drewitz claimed in the first action he was entitled to relief under Minn. Stat. § 302A.751 for termination of his employment which frustrated Drewitz’ reasonable expectations as an employee shareholder. Drewitz did not claim he had a right to indefinite shareholder status, and in fact sought the opposite status when he sued for a buy-out under Minn. Stat. § 302A.751. The action was brought to secure a fair value buy-out arising out of the *shareholder employee termination issues*. Drewitz did not and could not have claimed lack of distributions were a justification for a Minn. Stat. § 302A.751 action, because the claim for distributions had not accrued when the action was commenced.

Drewitz had no ability to include these issues in the first action because the facts giving rise to this action had not yet occurred and the conduct of the Respondents following the 2001 appellate ruling could not have reasonably been anticipated. If, as Respondents claim, this action should be barred because the same type of claims are involved, albeit on different factual grounds, the Court of Appeals decision in *Drewitz I* would also be a license for Respondents to run roughshod over Appellant's rights, force him into litigation to attempt to recover the funds held by Respondents, and allow Respondents to continue to claim they have done nothing wrong.

The Court of Appeals erred in its holding that Drewitz' unfair prejudice claim based on failure to tender is essentially an extension of the same series of transactions that formed the basis for the original unfair treatment claim. Drewitz is not expanding on his wrongful termination of the shareholder employment claim, the sole issue in the previous litigation leading to a claim for fair value buy-out. Drewitz did not and could not have claimed in his previous action unfair prejudice and breach of fiduciary duty for Respondents' failure to honor the terms of the contract after the 2001 decision of the appellate court.

The Court of Appeals erred in finding that Drewitz' failure to return to court to enforce a book-value buy-out after the conclusion of the first appeal contravenes his claims of continuing oppression in this litigation.

There was no case left to return to court. The trial court decision denied Drewitz' claim for Minn. Stat. § 302A.751 relief. The judgment gave a final ruling. "Returning" to court by starting a new suit to enforce what had already been resolved would mean no fiduciary duty existed.

There was no reason to believe, even if it had been possible, that the lower court would have allowed a permissive right to amend the original pleadings. "The district court properly considered the stage of the proceedings in deciding to deny appellant's motion." *Fabio v. Bellomo*, 504 N.W.2d 758, 761 (Minn. 1993)(citing Minn.R.Civ.P. 15.01) and cited to in *Mosen Agamawi v. United Defense, L.P.*, unpublished, Minn. App. February 28, 2006, (A37). "Appellant's motion came months after the close of discovery and three days after the deadline for all motions to be heard. Had the motion to amend been granted, the trial court would have had to amend its scheduling order to allow for further discovery, and the eventuality of extensive motion practice. In all likelihood, the trial date would have to be substantially delayed." *Id.* The Court of Appeals holding that res judicata cannot be used to bar an action which did not exist when the prior suit was started should be affirmed. To hold otherwise would place an unreasonable burden on a litigant and the court. Res judicata is not a basis to bar just claims in this case.

CONCLUSION

We request the Court to reverse the Court of Appeals denial of Drewitz' claims for unfair prejudice and breach of fiduciary duty. Motorwerks had a fiduciary duty to its minority shareholder whose third of a million dollars it continued to utilize in a profit-making enterprise. There was never a reasonable expectation on Drewitz' part that he would only get his investment back if he brought a second lawsuit to enforce a book-value buy-out.

We request the balance of the issues on review to be affirmed, holding shareholder status continues according to the terms of the shareholder contract. The claims for shareholder status and distributions should not be barred by res judicata, as neither was part of the first action nor could have been raised in the prior case.

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The appendix to this brief is not available for online viewing as specified in the *Minnesota Rules of Public Access to the Records of the Judicial Branch*, Rule 8, Subd. 2(e)(2) (with amendments effective July 1, 2007).