

No A08-1157

STATE OF MINNESOTA

IN COURT OF APPEALS

D. RANDALL BLOHM,

Appellant,

v.

BRUCE D. KELLY and BNK, Inc. a Minnesota
Corporation, individually and collectively,

Respondents.

APPELLANT'S REPLY BRIEF

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INTRODUCTION

The most striking aspect of Respondents' Brief is its minimal discussion of the evidence. The Argument portion of the brief contains just three citations to depositions. Respondents urge this Court to defer to the Special Litigation Committee (SLC) and to the trial court with almost no analysis of the facts.

Appellant's Brief, by contrast, extensively argued the evidence of record. Appellant marshaled scores of citations to show that his claims are supported by genuine issues of material fact (See App Br , pp. 5-14, 20-22, 24, 30, 43-44) Respondents offer no rebuttal.

Respondents essentially seek to sustain a summary judgment without reference to summary judgment standards. They argue for deference to the trial court and to the SLC in the face of manifest factual issues.

As will be shown below, the trial court clearly erred in its dismissal of the direct claims in this case. Those claims were properly pled, are not moot, and are supported by genuine issues of material fact.

The trial court also clearly erred in applying the "business judgment rule" to dismiss derivative claims. The SLC made a pure legal judgment, not a "business judgment," involving a corporation that has no business, only two shareholders and no assets.

Under these circumstances, the SLC should not have been allowed to stand in the shoes of the trial court. Plaintiff's claims present plain issues of fact, and they should not have been dismissed. Thus, summary judgment should be reversed.

REPLY TO RESPONDENT'S STATEMENT OF FACTS

Respondent's Brief contains a misstatement of fact which unfairly puts the Plaintiff in a bad light. As Appellant's Brief noted, Plaintiff drafted the closing documents when BNK, Inc. sold its assets to Jim Davis's new company, Ninety Blue. (App Br., p 7) Plaintiff acted as a scrivener, and took no part in negotiating the terms of sale. He disclosed his representation of Davis to Bruce Kelly and his interest in BNK to Davis (Id ; Blohm Depo , pp 32-38, 45)

Respondent's Brief makes the following statement with regard to the asset sale:

BNK was incorporated by Blohm in 1991 (RA 28-29) He represented the interests of BNK on and off for 15 years (RA 29) However, at the closing of BNK's asset sale, Blohm represented the interests of BNK and Ninety Blue. (RA. 35-36; RA 59.) Blohm charged Kelly \$3,400 for his fee for the closing. (RA 71)

(Resp. Br., pp. 1-2 (emphasis added))

The last statement is untrue. Blohm testified that he charged no fee for the closing to Kelly or to BNK (Blohm Depo , p 45 (RA-36)) Blohm explained that the \$3,400 was payment for litigation (the "Royal Zeno" matter) that he had helped handle for BNK. (Blohm Depo., pp. 27-28, 40, 56) He produced an invoice billing BNK \$3,300 in 2003 (two years earlier) for that matter (Kelly Depo , pp. 94-95 (RA-72))

Kelly testified that the \$3,400 check was for payment of Blohm's fees, but said he didn't know what the fees were for. (Kelly Depo., pp. 43-45 (RA-71, 72)) He did not testify that the fees were "for the closing " (See id.)

ARGUMENT

I. SUMMARY JUDGMENT SHOULD BE REVERSED AS TO ALL OF PLAINTIFF'S DIRECT CLAIMS.

Appellant's Brief argued that some (at least) of his claims are direct, and not derivative. His claim for denial of access to business records demonstrably is direct. So, too, is his claim for breach of fiduciary duty by Bruce Kelly. (App. Br., pp. 18-27)

Respondents apparently concede that these claims are direct, and thus not even arguably subject to jurisdiction by the SLC. (The SLC itself acknowledged this point. (See RA-6, n. 1, RA-18, n. 6) However, Respondents contend that the claims are moot, improperly pled, and not supported by evidence. These points will be rebutted below.

A. All of Plaintiff's Direct Claims are Properly Pled

Respondents raise various contentions that the claims are improperly pled, or otherwise technically incorrect. All these contentions should be rejected. In assessing them, the court should be mindful of Minn. Stat. §302A.751 (2004).

Plaintiff expressly pled this statute, which supports all his claims for relief. (See Complaint, ¶¶ 23, 24 and Prayer for Relief ¶ 4 (A-4 to A-5); App. Br., pp. 23-26) The statute provides:

A court may grant any equitable relief it deems just and reasonable in the circumstances or it may dissolve a corporation and liquidate its assets and

business:

* * *

(b) In an action by a shareholder when it is established that:

* * *

(3) the directors or those in control of the corporation have acted in a manner unfairly prejudicial toward one or more shareholders in their capacity as shareholders or directors of a corporation that is not a publicly held corporation, or as officers or employees of a closely held corporation.

(emphasis added)

This broad and flexible grant of authority refutes the various technical objections raised by Respondent. All the direct claims argued in Appellant's Brief are viable, as shown below.

1. Denial of Access to Corporate Records

The first claim advanced in Plaintiff's Complaint is for denial of his right of access to corporate records. (Complaint, ¶¶ 11-14, 17 (A-3 to A-4)) Plaintiff sought an order that Defendants "produce for the examination of Plaintiff all of BNK's business records," and also sought attorneys' fees (Prayer for Relief, ¶¶ 1, 4 (A-5))

Respondent's Brief argues that the proper remedy was a writ of mandamus, and that Plaintiff failed to request such relief (Resp. Br., p. 9) This contention has no merit.

Mandamus is a proper form of relief for refusal to produce corporate records, but it is not the exclusive remedy. See, e.g., Skutt v. Minneapolis Basketball Corporation, 261 Minn. 577, 110 N.W.2d 495 (1961) (plaintiff brought a claim for damages for denial

of access to records, and was granted leave to examine the records by means of an ordinary motion and order).

Minn. Stat §302A.751 (2004) authorizes equitable relief in any form. (Plaintiff's prayer for an order that Defendants produce the records was the functional equivalent of a petition for writ of mandamus, in any event.) And Defendants never argued below that mandamus was the sole appropriate remedy.

Respondents' Brief also contends that the claim is "not grounded in statute," because the records sought supposedly are not specified in Minn. Stat §§ 302A.461 or 302A.463. (Resp. Br., p. 9) Respondents, however, ignore the clause of §302A.461 which expressly was pled in the Complaint and also quoted in Appellant's Brief:

A shareholder . . . of a corporation that is not a publicly held corporation has a right, upon written demand, to examine and copy, in person or by legal representative, other corporate records at any reasonable time only if the shareholder . . . demonstrates a proper purpose for the examination.

(emphasis added) (See Complaint, ¶ 17; App. Br., p. 20) The reference to "other corporate records" extends to all the records in issue here

In sum, Plaintiff's claim for access to records was properly pled and firmly grounded in the statutes. It also was grounded in the Shareholders' Agreement, discussed below

2. Breach of Fiduciary Duty

Plaintiff expressly pled breach of fiduciary duty by Bruce Kelly. (Complaint, ¶¶ 19-21) Such claims are actionable at common law and also under Minn. Stat. §302A.751, which Plaintiff pled. (Id., ¶¶ 23, 24) (App. Br., pp. 23-27)

Respondent's Brief argues that Plaintiff's claims involve breach of the Shareholders' Agreement, and should have been pled as breach of contract. (Resp. Br., pp. 11-13) This contention has no merit.

Shareholders in closely-held corporations owe each other fiduciary duties. (See App. Br., pp. 22-23) Respondent does not contest this point. A bad-faith breach of a shareholders' agreement, therefore, is a breach of fiduciary duty, and can be redressed under either theory.

Respondent's Brief also argues that the Shareholders' Agreement calls for mandatory arbitration of disputes. (Resp. Br., pp. 1 n. 2, 10) This objection was not raised in the district court. It was waived when Defendants willingly joined in submitting the parties' dispute to that court.

Respondent's Brief apparently concedes that Plaintiff has stated claims for breach of fiduciary duties under Minn. Stat. §302A.751. (Resp. Br., pp. 12-13) That statute authorizes equitable remedies for "conduct that frustrates the reasonable expectations of shareholders in a closely held corporation." *Berremann v. West Publishing Co.*, 615 N.W.2d 362, 374 (Minn. App. 2000). Respondents fall back on the argument that Plaintiff has shown "no evidence . . . that he was denied his reasonable expectations." (*Id.*, p. 13)

The ultimate issue, thus, is not whether Plaintiff's claims for breach of fiduciary duty were properly pled. The issue is whether those claims are supported by evidence sufficient to meet the standards of Minn. R. Civ. P. 56. Such proof is amply established

in the record, as was shown in Appellant's Brief. (See pp. 8-9, infra)

3. Accounting

Appellant's Brief argued that "[a] proper equitable remedy would be to require Defendants to give an accounting and to sustain the burden of proof" (App. Br., p. 25) Respondents object: "This requested remedy is new on appeal, was not presented at the trial court, is not supported by any statute or precedent, and as such is not reasonably part of this Court's review." (Resp. Br., p. 10)

All of these objections are unfounded. Plaintiff pled Minn. Stat. §302A.751, which authorizes "any equitable relief" to vindicate "the reasonable expectations of shareholders." *Berremans*, 615 N.W.2d at 374. Accounting is a well-established equitable remedy.

The whole gravamen of Plaintiff's Complaint is to obtain a fair accounting for proceeds of the asset sale. The letter from Blohm to Kelly attached to the Complaint as Exhibit B states: "Bruce, I simply want an honest count." (A-7)

Had this matter gone to trial, the Complaint clearly would have supported the requested relief -- that Kelly bear the burden of proving an accounting of the asset sale. As Appellant has shown, the burden of proof should be placed on Kelly, the controlling shareholder, under general principles of law. See, e.g., *Westgor v. Grimm*, 318 N.W.2d 56, 59 (Minn. 1982) (App. Br., p. 40). The egregious delay in producing records, and Kelly's professed loss of memory, plainly make accounting the proper equitable remedy here. (See App. Br., p. 24)

B. The Record Shows Genuine Issues of Material Fact

Respondents contend that Plaintiff's direct claims are supported by "no evidence" and "no genuine issues as to any material fact." (See Resp. Br., pp. 4-5, 13) Yet they make hardly any attempt to rebut the detailed assessment of evidence which was marshaled in the Appellant's Brief. Among the key facts which Appellants emphasized were the following:

- Blohm requested records repeatedly for more than a year before he brought this litigation (Blohm Depo., pp. 43-44, 47; Ex A and B to Complaint, admitted by Answer, ¶ 12) (App Br , 20-21)
- One of Kelly's accountant's testified that Blohm complained to him repeatedly that he "was never getting any information from Bruce." (Don Lindstedt Depo , p 96) (App Br , p 21)
- After the litigation was filed, Kelly and his attorney failed to produce many records despite repeated discovery requests and a judicial order. (Sever Aff., Ex H, attached Exs A to C) (App Br , p. 21)
- Kelly admitted in testimony that he had not even looked for some of the records, and didn't know whether he had looked for others. (Kelly Depo., pp. 87-92) (App Br., p. 21)
- After documents finally were produced in the summer of 2007, Kelly was deposed and repeatedly claimed that he couldn't remember pertinent facts. (See Kelly Depo , pp 10, 11, 12, 13, 16, 17, 18, 21, 26, 27, 37, 40, 42, 44, 46,

47, 49, 50, 52, 55, 57, 59, 61, 64, 66, 68, 72, 87, 88, 89, 90, 91, 92, 94, 95, 99, 100, 101, 105, 106, 107, 110, 111, 112, 114, 115, 116, 117, 118, 120, 121)
(App. Br., p. 24)

- Among other matters, Kelly stated that he couldn't recall how much money he received for the asset sale or how he calculated Blohm's share. He testified that he has no documents supporting the calculation. (Kelly Depo., pp. 98-99, 120) (App. Br., p. 8)
- Kelly admits that a BNK balance sheet dated shortly after the asset sale lists "Total Assets" of \$20,131.59. Beside this entry is a note in the handwriting of BNK's accountant stating: "Distributed to Bruce -- \$100 stock" and "\$20,031.59 Dist." Kelly denies receiving such a payment (nearly 10 times what Blohm received), but admits that the same amount appears on a BNK tax return. (Kelly Depo., pp. 118-120) (App. Br., pp. 7-8)
- Around the time of the asset sale, Kelly issued some \$58,308 in BNK checks to settle various accounts. Some checks were issued to Kelly personally. One check (for \$24,627) paid off the outstanding balance on Kelly's personal credit card. Kelly could not say what part of this balance was for BNK expenses, for Lake Country Classics expenses, or for personal expenses. (Ex. Q to SLC Report; Blohm Depo., pp. 57, 74-75; Kelly Depo., pp. 103-07, 111-112, 115) (App. Br., pp. 7, 44)

This evidence manifestly establishes genuine issues of material fact as to all of

Blohm's direct claims: (1) failure to produce corporate records, (2) common law breach of fiduciary duty, (3) statutory breach of fiduciary duty (violation of "reasonable expectations") and (4) an accounting. Blohm's "reasonable expectations," under the facts of record, clearly involved receiving his fair share of the asset sale with appropriate documentation.

Respondent's Brief offers only minimal rebuttal. It presents the following contentions, each of which is rebutted by evidence of record:

(1) "Blohm received regular reports from BNK's accountant" (Resp. Br., pp. 5-6)

Blohm was sent financial statements by the accountant on "a fairly regular basis." (Blohm Depo., p. 48) However, he was not given access to the underlying records essential to verify the value of BNK's assets and their disposition by Kelly -- e.g., some tax returns, the closing inventory, some bank statements and check registers, books of account, auto leases, bills of sale for equipment purchases, credit card statements and underlying invoices (Id., pp. 49-51, 54-55, 59, 65, 76, 83)

(2) "BNK's accountant, Debra Lindstedt, testified that Blohm would receive any

documents he requested" (Resp. Br., p. 6) Respondent ambiguously paraphrases this testimony (Ms. Lindstedt merely speculates as to what Kelly would have done) (See Debra Lindstedt Depo., p. 113; RA-18) In any event, Ms. Lindstedt's testimony is rebutted not only by Blohm, but also by her husband and fellow BNK accountant, Don Lindstedt. Don, not Debra, did

BNK's accounting during the period in issue (2004-05) He states that Blohm complained to him repeatedly that he was "never getting any information from Bruce." (Don Lindstedt Depo., pp. 26, 95-96)

- (3) "Blohm ... drafted the closing documents ... [and] certainly could have reviewed and kept the documents of interest to him to see if he had been fairly paid for his ownership interest." (Resp. Br., p. 6) Blohm merely acted as a scrivener for Kelly and Davis when he drafted the closing documents. He did not help negotiate the terms of sale. (Blohm Depo., pp. 32-36, 45) There is no evidence that his role in the closing gave him access to the documents at issue.
- (4) Blohm offers "nothing more than his surmises" in suggesting that he has not seen all the pertinent documents (Resp. Br., p. 6) To the contrary, Blohm specified many documents that had not been produced by the Defendants -- i.e., tax returns, accounts payable, the closing inventory, bank statements, check registers, books of account, auto leases, equipment purchases, credit card statements and underlying invoices. (Id., pp. 49-51, 54-55, 59, 65, 83) This is not a "surmise" -- such documents clearly existed, and the burden was on Defendants to find and produce them.
- (5) Production of documents was delayed because Kelly's first attorney suffered a heart attack on January 24, 2007, and was replaced by his present counsel in March 2007 (Resp. Br., p. 2) No facts concerning the illness of Kelly's first attorney, Allen Demmer, are of record Appellant does not question the truth

of Respondent's assertions on this point. However, by Respondent's own account, the heart attack took place more than a year after this litigation was filed, long after most of the demands for production of documents, and four months after an order for production had been issued by the court in a telephone conference (See Ex. H to Affidavit of Stacey Sever) (App. Br., pp. 10-11)

In sum, Respondent's Brief does not rebut Appellant's detailed analysis of the record. It merely confirms that there are genuine issues of material fact. This Court, accordingly, should reverse the trial court's entry of summary judgment as to all of Plaintiff's direct claims

C. Plaintiff's Claims are Not Moot

Respondent's Brief argues that the Plaintiff's direct claims are moot. It contends:

[T]he trial court declared that the issue of producing records was, at the time of the hearing, moot. This is based on the undeniable fact that that there is no reasonable dispute at this time as to whether the records requested had been provided. This argument is simple -- Plaintiff sought documents, Defendants produced all that they had, therefore the court had no further remedy to grant

* * *

Blohm's claims related to the supposed failure of Kelly and BNK to provide business records is moot because BNK and Kelly produced all the records Blohm sought.

* * *

Blohm has, after all discovery was completed and on the eve of trial, developed no evidence that establishes that he was denied his reasonable expectation from the proceeds of the asset sale. In other words, even if it is

accepted that Kelly breached the Shareholder Agreement in the ways Blohm alleges, without damages there is no need for relief, and therefore no action under § 302A.751. Dismissal was therefore warranted

(Resp. Br., pp. 7-8, 11, 13 (emphasis added)) These contentions have no merit.

In the first place, genuine issues of material fact exist as to whether Defendants have "produced all that they had ... all of the records Blohm sought." Blohm testified that he has not received crucial documents (e.g., the closing inventory, credit card statements and underlying invoices, auto leases, some bank statements and check registers). (Blohm Depo , pp 49-51, 54-55, 59, 65, 76, 83) Kelly stated that he did not even look to see if he had some of the records at issue. (Kelly Depo., pp. 87-92) A court clearly could find that Defendants have not proved that they produced all of the records Blohm sought.

Secondly, a genuine issue of fact exists as to whether Blohm should receive attorneys' fees for his protracted quest to review the records. He had an absolute right to see them. The record shows that he was "stonewalled," that his requests were "ignored," and that production was delayed for more than two years. (See Blohm Depo., pp. 44, 49; Exs. A and B to Complaint, admitted by Answer, ¶ 12; Ex. H to Aff of Stacey Sever)

Attorneys' fees are authorized by statute for this sort of unlawful conduct by "a corporation or an officer or director." See Minn. Stat. §302A 467. (App. Br , p. 22) Attorneys' fees also can be awarded to redress a breach of fiduciary duty. See Minn. Stat. §302A 751; *Pedro v. Pedro*, 463 N.W.2d 285, 290 (Minn. App 1991) (fees available if party breaching a fiduciary duty acted "arbitrarily, vexatiously, or not in good faith").

(App. Br., p. 24)

In the present case, a court clearly could find that Kelly acted "arbitrarily, vexatiously, or not in good faith" in refusing to produce the corporate records. A court further could find that he was not in good faith in handling the asset sale, based on his two years' delay in producing boxes of documents, the absence of crucial records, his many assertions of failure of memory, and the consequent problems of proof.

Respondent argues that the district court had discretion to deny attorneys' fees. (Resp. Br., pp 7-8) But the district court heard no witnesses, had no basis to evaluate credibility, and made no findings as to good faith. It simply granted summary judgment on grounds that "Blohm's allegations regarding access to documents are moot." (Order and Memorandum, p 9 (A-30))

This Court's standard of review as to summary judgment is not "abuse of discretion." Rather, it is "whether there are any genuine issues of material fact and whether the district court erred in its application of the law." *State by Cooper v. French*, 460 N.W.2d 2, 4 (Minn. 1990). The evidence is viewed in the light most favorable to the party against whom summary judgment was granted. *Isles Wellness, Inc. v. Progressive N. Ins. Co.*, 703 N.W.2d 513, 516 (Minn. 2005).

Applying that standard, this court should reverse the summary judgment dismissing Plaintiff's direct claims. Those claims are not moot. The record amply demonstrates genuine issues of material fact.

This Court should remand the case for trial on Plaintiff's direct claims. The

pivotal issue is whether Kelly acted "arbitrarily, vexatiously, or not in good faith" in denying access to the records. The remedies available should include, inter alia, attorneys' fees, an accounting, and damages if Kelly is unable satisfactorily to account for his disposition of the assets and division of the proceeds.

II. SUMMARY JUDGMENT SHOULD BE REVERSED AS TO ANY DERIVATIVE CLAIMS.

A. The Distinction of Direct and Derivative Claims

Appellant's Brief contended that all the claims in this matter should be treated as direct claims. Respondent's Brief offers minimal rebuttal.

The claims in issue are for improper disbursement of assets, commingling, and excessive compensation. These claims ordinarily would be derivative, but should be deemed direct in the circumstances here. This will be demonstrated below.

1. The Direct/Derivative Distinction Should not be Applied in the Circumstances Here.

Appellant's Brief argued that the direct/derivative analysis should not be applied in the case of an out-of-business corporation with two shareholders and no creditors.

Specifically:

- The analysis turns upon "whether the injury to the individual plaintiff is separate and distinct from the injury to other persons in a similar situation as the plaintiff" *Northwest Racquet Swim and Health Clubs, Inc., v. DeLoitte &*

Touche, 535 N.W.2d 612 (Minn. 1995). Here, there are no "other persons in a similar situation as the plaintiff" (App Br., pp 17-18)

- The rationale for the analysis is: (1) to limit recovery to "the real party in interest;" (2) "to avoid multiple and conflicting suits;" and (3) to "protect[] corporate creditors." *Wessin v. Archives Corporation*, 592 N.W.2d 460 (Minn. 1999). None of those considerations are present here. (App Br., pp 27-29)
- Scholarly and out-of-state judicial authority holds that "the derivative-direct distinction makes little sense when the only interested parties are two individuals" (App Br., pp 28-29)

Respondent's Brief offers no substantive rebuttal. It merely asserts, "This is not the law in Minnesota," citing general language from *Wessin* ("Where the injury is to the corporation, and only indirectly harms the shareholder, the claim must be pursued as a derivative claim"), 592 N.W.2d at 464 (Resp. Br., pp 16-17)

Wessin clearly is distinguishable from the situation here. In *Wessin*, (1) the corporation was not out of business, (2) it evidently had creditors, (3) there were more than two shareholders, and (4) the Court took note that there was no shareholders' agreement. See id. at 462. The facts of the present case are different on all these points. They militate against applying the direct/derivative distinction here.

The question presented appears to be one of first impression in Minnesota. This Court should hold that the direct/derivative analysis does not apply to an out-of-business corporation with no creditors and only two shareholders who have a comprehensive

shareholders' agreement. It should remand all the Plaintiff's claims for trial as direct claims.

2. Claims Which Otherwise Might be Derivative Should be Resolved as Part of an Accounting on Plaintiff's Direct Claims.

As shown above, an accounting is an appropriate remedy for the Plaintiff's direct claims. All the matters at issue in any derivative claims can be resolved through an accounting. Appellant's Brief argued this point (App. Br., p. 27), and Respondent offers no rebuttal.

As Appellant argued, the egregious delay in production of corporate records, and the apparent loss or withholding of some records, makes proof very difficult on all of his claims, both derivative and direct (App. Br., pp. 24-25). The appropriate remedy is to recognize that Kelly bears the burden of proof to render an accounting for BNK.

B. The Special Litigation Committee and the Business Judgment Rule

If this Court accepts the foregoing analysis, the SLC proceedings are of no consequence. All Plaintiff's claims should simply be remanded for trial as direct claims, which are beyond the jurisdiction of an SLC.

If this Court rejects the foregoing arguments and treats some of the claims as derivative, then it must review the SLC proceedings. Appellant's assessment of those proceedings is un rebutted, as shown below.

1. Untimeliness of the SLC Referral

Appellant's Brief argued that the district court erred in allowing referral to an SLC on the eve of trial in this case. The timing clearly was unfair and prejudicial to the Plaintiff (App. Br., pp. 29-33)

Respondents contend that "the timing is irrelevant." They argue that "Blohm lacks standing" to bring claims which actually belong to the corporation. Respondent asserts that the issue involves justiciability, which can be raised at any time. (Resp. Br., pp. 13-14)

This contention has no merit. Shareholders, by definition, have standing to pursue derivative actions. The issue is when, and under what circumstances, the board of directors has power to assume control of a derivative action.

Janssen v. Best & Flanagan, 662 N.W.2d 876 (Minn. 2003), emphatically set limits to that power. In *Janssen*, as here, the district court allowed a belated reference to an SLC. The Supreme Court reversed and ordered that the matter should proceed to trial as a derivative action:

We strike a balance between allowing corporations to control their own destiny and permitting meritorious suits by shareholders and members by limiting a board of directors to one opportunity to exercise its business judgment ... If the courts allow corporate boards to continually improve their investigation to bolster their business decision, the rights of shareholders and members will be effectively nullified

Id. at 889-90 (emphasis added)

A similar holding is warranted here. The supposed "investigation" by BNK's Board on the eve of trial was manifestly unfair. The trial court erred by not allowing the

derivative action to proceed to trial

Respondent contends that "courts exercise discretion every day in the management of their dockets." (Resp. Br., p. 14) But the trial court here was not managing its docket -- it was not merely postponing a trial. Rather, it was allowing an SLC to step into its own shoes as trier of fact, in a manner that clearly was unfair.

This Court should follow *Janssen* in holding that the referral was improper. As in *Janssen*, this Court should reinstate the derivative claims and order that they proceed to trial.

2. Incongruity of Applying the "Business Judgment Rule" Under the Circumstances Here

If this Court concludes that the reference to the SLC was timely, it must consider whether the trial court properly deferred to the judgment of the SLC under the "business judgment rule." Appellant's Brief argued the incongruity of applying that rule here.

Respondent's Brief offered no substantial rebuttal.

The "business judgment rule" requires that courts defer to corporate boards of directors in making business decisions. However, courts owe no deference to a purely legal analysis by an SLC that weighs no business factors. See *Janssen*, 662 N.W.2d at 888-89.

Appellant's Brief argued that the SLC in the present case rendered a purely legal analysis, like the one rejected in *Janssen*. Thus, it argued that the trial court erred in deferring to the SLC. (App. Br., pp. 38-40)

Respondent's Brief argues that "a decision to pursue litigation is a business judgment ... whether 'to spend money in pursuit of a [] claim ... would be a prudent use of [] funds.'" (Resp. Br., pp. 18-19 (emphasis is original)) (quoting *Janssen*). This is a legitimate contention as to a corporation which has a business and funds. BNK, however, has neither -- no business and no funds to spend.

The question presented here is one of first impression in Minnesota. Should the "business judgment rule" be applied to an out-of-business corporation with no assets and only two shareholders? Manifestly, it should not.

An ancient maxim of the law is *cessante ratione legis, cessat et ipsa lex* ("when the reason for the law ceases, the law itself ceases"). That maxim should control here. The reasons underlying the business judgment rule simply don't apply. Defendants should not be allowed to take tactical advantage of an incongruous application of the rule.

3. Erroneous Fact-Finding by the SLC

If this Court holds the business judgment rule applicable, it nevertheless should reject the findings of the SLC. Appellant's Brief argued that the SLC improperly imposed the burden of proof on Blohm, not on Kelly (App. Br., pp. 40-43). Respondent's Brief offers minimal rebuttal (Resp. Br., pp. 19-20).

In assessing this issue, the Court should take note of *In re UnitedHealth Group Incorporated Shareholder Derivative Litigation*, 754 N.W.2d 544 (Minn. 2008) (decided since the filing of Appellant's Brief). *In re UnitedHealth* applied the business judgment rule with special stress on the SLC's "investigative procedures and methodologies:"

[W]e hold that, under the Minnesota business judgment rule, a court should defer to an SLC's decision to settle a shareholder derivative action if (1) the members of the SLC possessed a disinterested independence and (2) the SLC's investigative procedures and methodologies were adequate, appropriate, and pursued in good faith.

Id. at 559 (emphasis added).

In the present case, the SLC's methodologies were not adequate. The SLC repeatedly imposed burdens of proof on Blohm where the law requires that they should be imposed upon Kelly. (See App. Br., pp. 40-43) This Court, accordingly, should hold that the SLC report merits no deference.

C. Genuine Issues of Material Fact

Appellant's Brief argued that he had shown the district court genuine issues of material fact with regard to all of his derivative claims. (App Br., pp. 43-44) Neither the Defendant's summary judgment memoranda nor the district court's order rebutted this analysis. They simply deferred to the SLC. (Id.)

Respondent's Brief again offers no rebuttal. If this Court holds the SLC report unworthy of deference, therefore, it should reverse the order for summary judgment.

The ultimate problem here is that the SLC was allowed to step into the shoes of the trial court in an utterly inappropriate context. The SLC then essentially granted summary judgment without applying proper summary judgment standards -- no briefing, no "genuine issues" analysis, and improper burdens of proof.

In essence, the SLC acted as an arbitrator, making a purely legal judgment but applying its own standards. This procedure was unauthorized and clearly prejudicial under the circumstances here. Thus, summary judgment should be reversed.

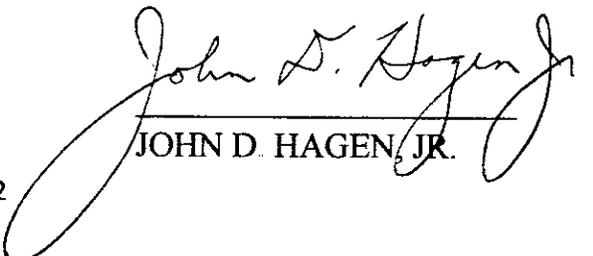
CONCLUSION

Plaintiff's direct claims for denial of access to records and for breach of fiduciary duty are not moot, and are properly pled. The record clearly establishes genuine issues of material fact on these claims. Thus, summary judgment should be reversed, and these claims should be set for trial, with attorney's fees and an accounting as potential remedies.

Plaintiff's other claims (e.g., for excessive compensation, commingling, and wrongful disbursement of assets) also should be treated as direct. If they are treated as derivative, this court should hold that the SLC report is not entitled to deference. Referral to the SLC was untimely, the "business judgment rule" should not apply, and the SLC used improper burdens of proof.

Genuine issues of material fact demonstrably exist with regard to all the Plaintiff's claims. Respondent's Brief makes almost no effort to discuss the pertinent evidence. This Court, accordingly, should reverse the summary judgment and remand the case for trial.

Respectfully submitted,



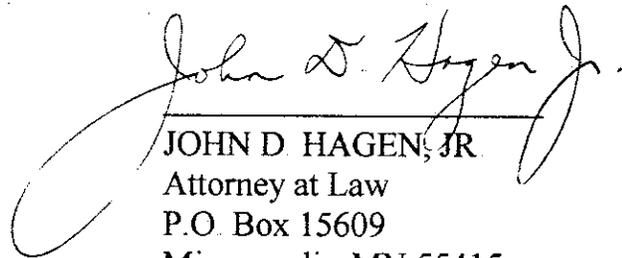
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CERTIFICATE AS TO WORD COUNT

Pursuant to Minn. R. App. P. 132.01, Subd. 3, I hereby certify that this Reply Brief was prepared using Microsoft Word 2007, in Times New Roman 13-point font, which complies with the typeface requirements of the rule. The number of words in the brief, as computed by the word processing software, is 5,461 (exclusive of the Table of Contents and the Table of Authorities), which is within the maximum permitted by the rule.



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