CHAPTER SEVEN

SHAREHOLDERS

Section 7.01 Generally

ORS 60.001(29) defines "share" to mean:

> the units into which the proprietary interest in a corporation are divided.

A "shareholder" is defined by ORS 60.001(30) to mean:

> the person in whose name shares are registered in the records of a corporation or the beneficial owner of shares to the extent of the rights granted by a nominee certificate on file with a corporation.

Although the current Act usually only uses the terms "share" and "shareholder," the terms "share" and "stock" and the terms "shareholder" and "stockholder" are synonymous. Each of these terms are used interchangeably throughout this book.

A. Shareholders are distinct from corporation.

A corporation is an artificial person, created by statute, which "is an entity separate, independent and apart from the associates who compose its stockholders." *Sneed v. Santiam River Timber Co.*, 122 Or 652, 655, 260 P 237, 238 (1927).

> A corporation is by legislative enactment, an entity. It is such, separate and distinct from the persons who own its stock. This statutory entity, so long as it exists, is the owner of all of the property which the corporation possesses. An individual shareholder has no property interest in its physical corporate assets. The persons who are shareholders have only rights of participation in the management of the corporate affairs. (citations omitted) *State of California v. Tax Commissioner of State*, 55 Wash 2d 155, 157, 346 P2d 1006, 1008 (1959).

"[A] corporation is a legal entity separate from its shareholders, directors, and officers." *Lee v. Mitchell*, 152 Or App 159, 176, 953 P2d 414, 425 (1998).

> One of the hallmarks of Anglo-American corporate law is the status of the corporation as a distinct entity, an artificial person separate from its shareholders, having the capacity to own property and to sue and be sued. As our supreme court stated over half a century ago, "[t]he corporation is an independent legal entity, separate and distinct from its stockholders." From this basic principle it follows that a corporation's "capital stock belongs to the corporation considered as a legal person; the shares are the property of the individual shareholders." Shareholders have a claim for their aliquot share of corporate assets only "*after* the debts and

> liabilities of the corporation have been satisfied and the assets have been distributed in liquidation." Because of separate identity, shareholders simply are unable to sell corporate assets; they can sell only their shares. (emphasis in original; citations omitted) *SFN Shareholders Grantor Trust v. Indiana Department of State Revenue*, 603 NE2d 194, 197-8 (Ind Tax 1992).

Since a corporation "is an entity separate and distinct from the individual owning all of the stock," even a sole shareholder is not deemed the owner of corporate property. *Patterson v. Ford*, 167 Wash 121, 125, 8 P2d 1006, 1008 (1932).

B. Directors – not shareholders – manage the corporation.

Directors, not shareholders, manage the corporation. Officers and other agents act on the corporation's behalf. Shareholders have little power with respect to the actual management of their corporation. The shareholders' role generally is limited to electing directors and to voting on extraordinary corporate events put before the shareholders by the board of directors. *Kelly v. Galloway*, 156 Or 301, 66 P2d 272, 68 P2d 474 (1937); *Baillie v. Columbia Gold Mining Co.*, 86 Or 1, 16, 166 P 965, 969, 167 P 1167 (1917); *Fidelity & Casualty Company of New York v. Central Bank of Houston*, 672 SW2d 641 (Tex App 1984); *Lycette v. Green River Gorge, Inc.*, 21 Wash 2d 859, 862, 153 P2d 873, 875 (1944).

> The power of management of the corporate affairs and the power to contract so as to bind the corporation is vested primarily in the board of directors and not in the stockholders; the principal rights of the latter, in ordinary business or trading corporations, are to attend and vote at corporate meetings, to pass and amend by-laws, to elect directors, to participate in dividends and profits, and to receive their proportionate shares of the corporate property or its proceeds upon dissolution and winding up of the corporation after payment of its debts. *Trethewey v. Green River Gorge, Inc.*, 17 Wash 2d 697, 136 P2d 999, 1010 (1943).

C. Shareholders are not agents of corporation.

Although a corporation may appoint an individual shareholder as its agent, no shareholder is inherently the agent of a corporation. Shareholders have no inherent right to act on behalf of the corporation, either individually or collectively. *Feenaughty v. Beall*, 91 Or 654, 178 P 600 (1919); *Powell v. Oregonian Ry. Co.*, 38 F 187 (D Or 1889); *Opportunity Christian Church v. Washington Water Power Co.*, 136 Wash 116, 238 P 641 (1925). The U.S. Supreme Court held:

> In *Smith v. Hurd*, 12 Met 371, 385, the relations of stockholders to the rights and property of a banking corporation are stated with his usual clearness and precision by Chief Justice Shaw, speaking for the Supreme Court of Massachusetts, and the same doctrine applies to the relations of stockholders in all business corporations. Said the Chief Justice: "The individual members of a corporation, whether they should all join, or each act severally, have no right or power to intermeddle with the property or concerns of the bank, or call any officer, agent or servant to account, or discharge them from any liability. Should all the stockholders join in a power of attorney to any one, he could not take possession of any real or personal estate, any security, or chose in action; could not collect a debt, or discharge a claim, or release damage arising from any default; simply because they are not the legal owners of the

property, and damage done to such property is not an injury to them. Their rights and their powers are limited and well defined." *Humphreys v. McKissock*, 140 US 304, 312-3 (1891).

***D. Shareholders' role may be expanded under ORS 60.265*.**

Under the current Act, shareholders may, by written agreement, restrict the discretion or powers of the board of directors or may reallocate the division of voting powers between the shareholders and the directors. ORS 60.265(1). *See* Section 4.07 of this book.

Some of the issues discussed in this Chapter do not necessarily apply to corporations in which the shareholders have entered into an agreement to restrict the power of the board of directors and otherwise complied with the requirements of ORS 60.265. A discussion of ORS 60.265 is contained in Section 4.07 of this book.

Section 7.02 Subscriptions & Other Contracts to Purchase Shares

A "subscription" is an offer to acquire shares directly from the corporation. "[T]he initial purchase of shares of a corporation is accomplished through a "subscription" for shares, either before or after incorporation." *Yeoman v. Public Safety Center, Inc.,* 241 Or App 255, 261, 250 P3d 411 (2011). As discussed below, a subscription before incorporation may also operate as a contract among the subscribers.

Subscriptions are contracts and are governed by general principles of contract law. *Finley v. Curley*, 54 Wash App 514, 774 P2d 538 (1989); *Jackson v. Southern Pan and Shoring Co.*, 258 Ga 401, 369 SE2d 239 (1988). Absent a statute or provision in the articles of incorporation to the contrary, a subscription may be either written or oral and need not be in any particular form. *Molina v. Largosa*, 465 P2d 293 (Haw 1970); *White County Guaranty Savings and Loan Association v. Searcy Federal Savings & Loan Association*, 241 Ark 878, 410 SW2d 760 (1967); *Gibson v. Oswalt*, 269 Mich 300, 257 NW 825 (1934).

ORS 60.144 does not specify the form of a subscription nor does it require the subscription to be in writing. A limited number of cases have applied the statute of frauds provision of Article VIII of the Uniform Commercial Code (Article 8-319) to stock subscriptions and these cases have required that a subscription agreement be in writing. Kummert, *Stock Subscription Law for Practitioners*, 63 WASH L REV 21, 27 (1988). Oregon apparently does not. *Yeoman v. Public Safety Center, Inc.*, 241 Or App 255, n 6, 250 P3d 411 (2011).

A board of directors may authorize the issuance of shares for cash or for consideration other than cash. Such consideration may include notes, other securities, and past and future services. ORS 60.147(2). It may include future services. *Yeoman v. Public Safety Center, Inc.,* 241 Or App 255, 250 P3d 411

(2011).

The good faith determination of the board is conclusive as to the adequacy of the consideration paid for the shares. ORS 60.147(2). *See* Section 5.13 of this book.

"The validity of a subscription agreement for capital stock of a corporation is controlled by the laws of the state or county [sic] where the corporation is organized." *May v. Roberts,* 133 Or 643, 650, 286 P 546 (1930).

A. Definitions.

The term "subscription" describes an offer to acquire shares directly from a corporation. The term "subscription" does not include offers to purchase shares from anyone other than the corporation nor does it include an offer to acquire shares held by a corporation as a trustee for a third party.

Some courts have reserved the term "subscription" for use in connection with corporations yet-to-be-formed and use the term "contracts to purchase stock" in connection with corporations already in existence. *Sprague v. Straub*, 252 Or 507, 451 P2d 49 (1969); *Commercial State Bank v. Eilers*, 124 Or 379, 264 P 452 (1928). The prevailing view is an offer to purchase original issue shares constitutes a "subscription," regardless of whether or not the corporation has as yet been formed. FLETCHER CYC CORP § 1363 (Perm Ed).

Under the current Act, the term "subscription" applies to offers both before and after incorporation (although ORS 60.144 makes some distinctions between pre-incorporation and post-incorporation subscriptions). ORS 60.001(36) says: "'Subscriber' means a person who subscribes for shares in a corporation whether before or after incorporation." But under the current Act, the term "subscription" is still limited to offers to acquire shares from a corporation, not offers made to the third party owners of shares.

Persons may become shareholders of a corporation either: (i) by acquiring shares directly from the corporation; or (ii) by acquiring shares from third parties who previously purchased the shares from the corporation (or the last person in the line of such purchasers).

The term "original issue" is commonly used to refer to shares acquired directly from a corporation. The term "secondary transaction" is one commonly used to refer to the transfer or resale of shares by a transferor other than an issuing corporation.

"Treasury shares" are shares which have been re-acquired by the corporation and held in a state of suspended animation – that is, they do not confer on the corporation the right to vote the shares, receive dividends or any of the other rights normally associated with shares - until resold by the corporation. *Kisrchenbaun v. Commissioner of Internal Revenue*, 155 F2d 23 (2nd Cir 1946). Some older cases do

not apply the term "subscription" to offers to purchase treasury shares from a corporation.

The concept of "treasury shares" has been abandoned by the Revised Model Business Corporation Act and the current Oregon Business Corporation Act. Shares re-acquired by an Oregon corporation now simply disappear into the category of authorized, but unissued, shares.

***B. Subscriptions are contracts*.**

Case law generally refers to a subscription as an "agreement" or "contract," but those terms do not adequately describe the relationship created. Before a corporation is organized, a subscription may more properly be characterized as both a *contract* among the prospective shareholders and an irrevocable *offer* from the subscriber to the corporation.

> It is, first, a contract between the subscribers themselves to become stockholders, without further act on their part, immediately on the formation of the corporation and is binding from the date of the subscription; and, second, it is in the nature of a continuing offer to the proposed corporation, which, upon acceptance by it after its formation, becomes, as to each subscriber, a contract between him and the corporation. *Balfour v. Baker City Gas Co.*, 27 Or 300, 306, 41 P 164, 165 (1895).

A subscription agreement entered into after incorporation is a contract between the subscriber and the corporation. ORS 60.144(5). Such subscription contracts are subject to ORS 60.147.

A corporation does not become a party to the subscription contract until its board of directors accepts the subscription. This usually occurs at the organizational meeting. The board may properly reject any subscription offer.

The board may authorize the issuance of shares for cash or for other consideration, such as notes, other securities and past and future services. ORS 60.147(2)*;Yeoman v. Public Safety Center, Inc.,* 241 Or App 255, 250 P3d 411 (2011). The good faith determination of the board is conclusive as to the adequacy of the consideration, ORS 60.147(3). *See* Section 5.13 of this book.

Under the current Act, a written subscription entered into before incorporation is irrevocable for a 6-month period after execution, unless the subscription itself provides for a different term, or unless ***all*** subscribers agree to its revocation. ORS 60.144(1). If after 6-months the corporation has not accepted the subscription, it becomes revocable by the subscriber. *Marcus v. Shapiro, Abramson & Schwimmer, PA.,* 620 So2d 1284 (Fla App 1993).

Under common law, the majority rule permitted subscribers to revoke their subscription offers anytime before acceptance, barring an agreement to the contrary. *Collins v. Morgan Grain Co.*, 16 F2d 671 (9th Cir 1926). This is no longer true in Oregon.

Section 7.02

A contract entered into by an existing shareholder to sell his/her own shares to a third party is governed by the general rules of contract construction. *Finley v. Curley*, 54 Wash App 514, 774 P2d 538 (1989); *Lindgren v. Dowis*, 236 Ga 278, 223 SE2d 682 (1976).

***C. Subscriber's rights & liabilities once subscription accepted*.**

A subscriber becomes liable for the subscription price as soon as the board accepts the subscription and calls for payment.

A subscriber acquires the status of shareholder upon the corporation's acceptance of the subscription, even though stock certificates have not been issued. *Babbitt v. Pacco Investors Corp.*, 246 Or 261, 425 P2d 489 (1967); *M/V La Conte, Inc. v. Leisure*, 55 Wash App 396, 777 P2d 1061 (1989); *Child v. Idaho Hewer Mines*, 155 Wash 280, 284 P 80 (1930). "An original subscriber has the rights and obligations of a stockholder, whether or not he has paid for the shares, unless the subscription is lawfully revoked." *Peifer v. DME Liquidating, Inc.*, 91 Or App 47, 753 P2d 1389 (1988), *appeal after remand*, 101 Or App 106, 789 P2d 266 (1990)(interpreting Washington law). More recently, the Oregon Court of Appeals has said that a subscriber becomes a shareholder "once the corporation accepts payment in exchange for consideration for the authorized shares." *Yeoman v. Public Safety Center, Inc.,* 241 Or App 255, 262, 250 P3d 411 (2011), although that case arose in the context of a subscription promising shares for future services and the court held that even though certificates were never issued, the subscriber became a shareholder once the services were performed.

Unless a subscription provides otherwise, a subscriber whose subscription is accepted by the corporation becomes a shareholder of the corporation even if the subscriber fails to pay the consideration described in the subscription. *Babbitt v. Pacco Investors Corp.*, 246 Or 261, 425 P2d 489 (1967). *See also* Section 3.10 of this book.

If a subscriber pays for the stock but, despite demand, the corporation refuses to deliver a share certificate, the subscriber may elect one of three remedies:

> (1) He may, is some jurisdictions, maintain a suit in equity for specific performance, and compel delivery of the stock; (2) he may treat the executory agreement as subsisting and recover the damages occasioned by the breach; or (3) he may rescind the contract and maintain an action in *assumpsit* for the recovery of the sum paid as money had and received. *Watkins v. Record Photographing Abstract Co.*, 76 Or 421, 426, 149 P 478, 480 (1915).

More recently, the Oregon Court of Appeals has said that the subscriber could "obtain injunctive relief such that the corporation's records reflect that share ownership." *Yeoman v. Public Safety Center, Inc.,* 241 Or App 255, 267, 250 P3d 411 (2011).

Under the current Act, a corporation "may authorize the issue of some or all of the shares . . . without certificates." ORS 60.164(1). The owner of such shares must be sent a written statement containing specified information. ORS 60.164(2).

***D. Qualifications to acquire shares*.**

Early case law and some early statute occasionally either established shareholder qualifications or prohibited certain persons from owning stock.

Connecticut once barred aliens from holding stock in its corporations. *State v. The Travelers Insurance Co.*, 70 Conn 590, 40 A 465 (1898). Washington law once prohibited a corporation from owning stock in other corporation. *Day v. Hecla Mining Co.*, 126 Wash 50, 217 P 1 (1923). At one time, Washington law prohibited a corporation – a majority of whose shares were owned by aliens – from owning real property in Washington. *Hastings v. Anacortes Packing Co.*, 29 Wash 224, 69 P 776 (1902).

Today there are few, if any, qualification requirements related to who may acquire shares. Even a minor may be a shareholder. *Wuller v. Chuse Grocery Co.*, 241 Ill 398, 89 NE 796 (1909). However, a minor's contract to purchase shares is likely a voidable contract due to the minor's lack of capacity. *The Indianapolis Chair Manufacturing Co. v. Wilcox*, 59 Ind 429 (1877).

There is still one common limitation. A corporate shareholder may not vote its shares in a second corporation if the second corporation owns a majority of the shares of the first corporation. ORS 60.227(2). Two corporation cannot own 100% of each other – there must be a human being involved in ownership at some level.

***E. Miscellaneous*.**

State and federal securities laws generally apply to the sale of stock. *See* ORS 59.005 *et seq*.

A more detailed discussion of shareholder liability for an unpaid subscription is contained in Section 10.10 of this book.

Section 7.03 Limited Liability

Probably the most important attribute of corporate ownership is the limited liability afforded to the owners of the corporation.

> A purchaser from a corporation of its own shares is not liable to the corporation or its creditors with respect to the shares except to pay the consideration for which the shares were authorized to be issued or specified in the subscription agreement. ORS 60.151(1).

Article XI, Section 3 of the Oregon Constitution also limits the liability of shareholders to the amount of their subscription price, except for shareholders of state banks.

> The stockholders of all corporations and joint stock companies shall be liable for the

> indebtedness of said corporation to the amount of their stock subscribed and unpaid and no more, excepting that the stockholders of corporations or joint stock companies conducting the business of banking . . . .

Circumstances under which the shareholders may be liable for unpaid subscriptions, or otherwise liable to third parties, are discussed in Chapter Ten of this book.

Section 7.04 Meetings

There are four ways for the shareholders to take action: annual meetings (ORS 60.201); special meetings (ORS 60.204); court ordered meetings (ORS 60.207); and actions without a meeting (ORS 60.211). In theory, shareholders usually do not meet often enough for there to be "regular meetings," like those held by directors.

***A. Annual meeting*.**

Shareholders meet annually to elect directors. ORS 60.307. The annual shareholder meeting takes place at the time set out in or fixed in the bylaws. ORS 60.201(1).

There are numerous cases where shareholders have sued to require the directors to hold the annual meeting on the date set in the bylaws (and language in those cases stating that the board cannot change the date of the annual shareholder meeting). *See Lerman v. Diagnostic Data, Inc.,* 421 2d 906 (Del Ch 1980); *ER Holdings, Inc. v. Norton Co.,* 735 F Supp 1094 (D Mass 1990)*; Prickett v. American Steel Corp.,* 251 A2d 576 (Del Ch 1969).

But once the shareholder meeting has occurred, the corporation has little exposure for liability for failure to strictly follow the time, place and date provisions of the bylaws. For instance, the failure to hold its annual shareholder meeting at the prescribed time and place does not invalidate any corporate action. ORS 60.201(3). There is a strong presumption in favor of the validity of shareholder meetings. A shareholder who participates in a meeting cannot later complain as to irregularities in the notice, place or date of the meeting. *Camp v. Shannon,* 162 Tex 515, 348 SW2d 517 (1961).

The current Act provides that annual meetings are to be held at the place stated in, or fixed in accordance with, the bylaws. ORS 60.201(2). Some corporations comply with the "place" requirement by including in the bylaws a provision that the annual meetings may be held at any place determined by the board of directors. If the bylaws fail to fix a meeting site, and fail to provide for a mechanism for fixing such a site, the annual meeting must be held at the corporation's principal office. ORS 60.201(2).

***B. Special meetings*.**

A special meeting of shareholders is a meeting other than the annual shareholders' meeting.

A special shareholder meeting may only be called by those persons authorized by statute to call such meetings. *Comolli v. Comolli Granite Co.*, 233 Ga 461, 211 SE2d 750 (1975).

The current Act provides that a special meeting may be called by the board of directors or by any person or persons authorized to call meetings in the articles of incorporation or bylaws. ORS 60.204(1)(a). Most commonly, the bylaws authorize one or more officers, and sometimes the board chair, to call special shareholder meetings. Permitting an officer to call a special shareholder meeting greatly decreases the time and administrative problems involved in calling a meeting. Otherwise, a two-step process would be necessary: a meeting of the board of directors would need be called and the board would, in turn, need to call a meeting of the shareholders.

> **NOTE:** Until January 1, 2003, the Act provided that a special meeting must be called by a corporation upon demand by shareholders holding at least 10% of the votes entitled to be cast at the special meeting so demanded. Since that date, ORS 60.204(1)(b) has provided that the articles of incorporation could lower this percentage, or increase it up to 25% of all votes entitled to be cast. A shareholder now can withdraw the demand up until the point when the corporation has received sufficient demands to require a meeting.
>
> A corporation wishing to avail itself of this new provision can do so be amending its articles of incorporation.

Although shareholders may demand a meeting, they do not directly call the meeting. The corporation calls the meeting after proper demand is delivered to its secretary.

> Upon receipt of writings evidencing a demand by holders of 10 percent of the votes, the corporation (through an appropriate officer) must call the special meeting at a reasonable time and place. The shareholders' demand may suggest a time and place but the final decision on such matters is the corporation's. Official Comment to Revised Model Business Act § 7.02.

The corporation sets the time and place of the meeting – ***not*** the shareholders who are demanding the meeting.

The current Act provides that special shareholder meetings are held at the place stated in, or fixed in accordance with, the bylaws. ORS 60.204(3). Some corporations comply with this requirement by including in the bylaws a provision that such meetings may be held at any place determined by the board of directors. If the

bylaws fail to fix a meeting site, and fail to provide for a mechanism for fixing such a site, special meetings must be held at the corporation's principal office. ORS 60.204(3).

If not otherwise fixed under ORS 60.207 or 60.221, the record date for determining the shareholders entitled to demand a meeting is the date the first shareholder signs the demand.

***C. Court-ordered meetings*.**

If a corporation delays too long in calling the annual shareholder meeting, or if a corporation ignores a demand for a meeting by a sufficient percentage of the shareholders, its shareholders may seek to have the court call a shareholder meeting. ORS 60.207. If the court orders a meeting, it may set the time and place for the meeting and it may establish special rules regarding record date, notice, quorum and other matters. ORS 60.207(2).

***D. Action without meeting*.**

Generally, shareholders may take an action without a meeting, but only if all shareholders entitled to vote on the action consent to it in writing. ORS 60.211(1)(a); *Hansen v. Singmaster Insurance Agency, Inc.*, 80 Or App 329, 722 P2d 1254, *opinion adhered to*, 82 Or App 219, 728 P2d 69 (1986), *rehearing denied*, 302 Or 594, 732 P2d 915 (1987).

Effective January 1, 2002, ORS 60.211 was amended to permit existing and new corporations to include in their articles a provision for shareholder action without a meeting ***by less than unanimous shareholder consent***. To take such a non-unanimous action, written consent is required from shareholders having not less than the minimum number of votes that would be necessary to take such action at a meeting in which all shareholders entitled to vote on the action were present and voting, that is, one more than a majority of the issued and outstanding shares of the class or classes entitled to vote on that issue.

> **NOTE:** Non-unanimous shareholder consent is an opt-in provision. Corporations whose articles of incorporation do not specifically provide for non-unanimous consent will be governed by the old rule. For such corporations, unanimous shareholder consent is still required.

Under prior law, the effective date of such an action was the date on which the last shareholder signed the consent, unless the consent specified an different effective date. ORS 60.211(1)(d). This is still the rule if unanimous consent is required. But if the corporation permits non-unanimous shareholder consent, the effective date is when the consent first contains sufficient signatures representing the minimum number of votes that would be necessary to take such action at a meeting. ORS 60.211(1)(e). In either case, the effective date may be specified in the

consent as an earlier or later effective date.

Under certain circumstances, nonvoting shareholders must be given notice of the proposed action before the voting shareholders begin signing the consent. ORS 60.211(4).

If shareholders take action by non-unanimous consent, the corporation must give written notice to the shareholders who did not consent promptly after the action is taken. The notice must be accompanied by the same material that would have been required to be sent to those shareholders along with the notice of the meeting. ORS 60.211(5).

Unless otherwise determined by ORS 60.207 (related to court ordered meetings) or ORS 60.221 (usual rule for fixing the record date in the bylaws or by board resolution), the record date is the date the first shareholder signs the consent resolution. ORS 60.211(2).

Compliance with the rules related to "electronic signatures" set out in ORS 60.001(13) & 84.004 could make a series of email communications into a consent resolution under ORS 60.341.

***E. Bylaws should contain rules for meetings*.**

A corporation can and should enact bylaws to control issues of internal corporate management – issues such as shareholder meetings. ORS 60.061(2); *Jacobson v. Moskowitz*, 27 NY2d 67, 313 NYS2d 684, 261 NE2d 613 (1970); *Burt v. Irvine Co.*, 224 Cal App 2d 50, 36 Cal Rptr 270 (1964). These provisions may not be inconsistent with the articles of incorporation or with the general statutes.

> It is a general rule that a corporation may enact any bylaw for its internal management so long as such bylaws are not contrary to its charter, a controlling statute, its articles of incorporation, or violative of any general law or public policy. Subject to the above qualifications, a corporation may adopt bylaws regulating the calling and conduct of corporate meetings and election of its officers. *Booker v. First Federal Savings and Loan Association*, 215 Ga 277, 280, 110 SE2d 360, 361 (1959).

See also Sabre Farms, Inc. v. Jordan, 78 Or App 323, 717 P2d 156 (1986); *State ex rel Brewster v. Ostrander*, 212 Or 177, 318 P2d 284 (1957).

***F. Notice*.**

A corporation is required to notify shareholders of the date, time and place of each annual and special shareholder meeting. ORS 60.214. Notice of such meetings must be given to shareholders not more than 60 days, and not less than 10 days, before the meeting is to occur. *Id.*

> **NOTE:** Under prior law, notice could not be given more than 50 days before the meeting. As a consequence, some corporations (particularly those formed before 1987) may still have bylaw provisions prohibiting notice more than 50 days before the meeting. Since the bylaws may set a maximum time of less

than the statutory 60 days, the more restrictive 50 day provision will apply.

Notice for a special meeting – but ***not*** notices for an annual meeting – must include the purpose of the meeting. *Compare:* ORS 60.214(2) and (3).

Only business within the purpose or purposes described in the meeting notice may be conducted at a special shareholder meeting. ORS 60.204(4).

All notices of shareholder meetings must be in writing. ORS 60.034(3).

Notice by electronic transmission – other than voice mail – is deemed to be written notice by ORS 60.034(2)(a). This would include email.

> "Electronic transmission" means a form or process of communication that does not directly involve physically transferring paper or another tangible medium and that enables a recipient to retain, retrieve and reproduce information by means of an automated process that is used in conventional commercial practice, except as provided in ORS 60.034 (4)(c).

ORS 60.034 contains permissible methods by which notice may be delivered and contains the methods for determining the effective date of any such notice.

The articles of incorporation and/or the bylaws may prescribe notice requirements not inconsistent with ORS 60.034(8).

***G. Telephone meetings*.**

Under prior law, the corporation could authorize participation in shareholder meetings by telephone. This authorization has been broadened to include newer forms of communications. ORS 60.222(1)(a) now provides:

> Shareholders and proxy holders that are not physically present for a shareholders' meeting may participate in the meeting, be deemed present in person and vote if the board of directors authorizes participation by remote communication. Participation by remote communication is subject to guidelines and procedures that the board adopts.

Remote communications means:

> any method by which a person that is not physically present at the location at which a meeting occurs may nevertheless hear or otherwise communicate at substantially the same time with other persons at the meeting and have access to materials necessary to participate or vote in the meeting to the extent of the person's authorization to participate or vote. ORS 60.001(28).

Under this provision, speaker telephones and conference calls are permitted. Passing a telephone back and forth among shareholders in the same room probably is not permitted.

"The notice of each annual or special meeting of shareholders at which the board authorizes participation in the manner described in subsection (1) of this section shall state that the board authorizes participation by remote communication and shall describe how a shareholder may notify the corporation of the shareholder's desire to participate in the meeting by remote communication. ORS 60.222(2),

Compliance with the rules related to "electronic signatures" – set out in ORS

60.001(11) & 84.004 – could make a series of email communications into a consent resolution under ORS 60.341.

***H. Record date*.**

The "record date" is the date on which a corporation determines the identity of its shareholders and of their shareholdings for purposes of notice and voting at a shareholder meeting. ORS 60.221.

The bylaws should fix a record date – a date which can be no more than 70 days before the meeting. ORS 60.221. If the bylaws do not fix a record date, the board may fix a future date as the record date. *Id.*

For actions taken without a meeting, the record date will usually be the date the first shareholder signs the consent. ORS 60.211(2).

***I. Shareholder list*.**

A corporation or its agent is required to “maintain a record of the corporation's shareholders, in a form that permits preparation of a list of the names and addresses of all shareholders in alphabetical order by class of shares showing the number and class of shares each shareholder holds.” ORS 60.771(3). For the period beginning two days after notice of the shareholder meeting is given, and continuing through the meeting, the shareholder list must be available for inspection by any shareholder entitled to vote at the meeting. ORS 60.224(2).

Generally, a corporation can only look to the shareholder list to determine who is entitled to vote at the meeting. *State ex rel Breger v. Rusche*, 219 Ind 559, 39 NE2d 433 (1942).

There are exceptions. For instance, a corporation may establish a recognition procedure which permits the beneficial owner of shares to cast the share's vote. ORS 60.234. Shareholders may vote by proxy. ORS 60.231; Section 7.05 of this book. If it acts in good faith, a corporation may permit a person other than the record holder to vote shares under those circumstances described in ORS 60.237(2).

A corporation with shares registered under the Oregon or federal securities laws may reject of vote of a person who “has failed to comply with the disclosure requirements identified in 15 U.S.C. 78m(d) or 78p(a) with respect to the registered corporation.” ORS 60.237(3).

***J. Voting*.**

For purposes of shareholder voting, each share is usually entitled to one vote. ORS 60.227(1). A shareholder owning 5 shares has 5 votes; a shareholder owning 1 share has 1 vote.

There are exceptions. If a corporation owns a majority interest in a subsidiary, shares owned by the subsidiary are usually not entitled to vote. ORS 60.227(2). Voting rights of "control shares" may be restricted in a control share acquisition.

ORS 60.807(1).

Although a corporation may have shareholders which are themselves corporations, upstream somewhere there must be a natural person or a fiduciary for a natural person. Two corporations may not own 100% of each other. ORS 60.227(2).

K. Quorum.

A quorum is the number of shareholders who must be present in order for an action of shareholders to be binding. BLACK'S LAW DICTIONARY; *Griffith v. Sprowl*, 45 Ind App 504, 91 NE 25 (1910). An action taken at a shareholder meeting lacking a quorum is invalid. *Place v. P.M. Place Stores Co.,* 950 SW2d 862 (Mo App 1996).

The quorum is a majority of the votes entitled to be cast on that matter, unless the articles of incorporation or bylaws provide otherwise. ORS 60.241(1); *ITC Cellular, Inc. v. Morris,* 909 SW2d 182 (Tex App 1995); *Gregory v. J. T. Gregory & Son, Inc.*, 176 Ga App 788, 338 SE2d 7 (1985); *Benintendi v. Kenton Hotel, Inc.*, 294 NY 112, 60 NE2d 829, 831-2 (1945). The articles or bylaws may require a quorum of more or less than a majority, but not less than one-third of the votes entitled to be cast. ORS 60.247(1).

Voters may be present at the meeting either in person or by proxy. ORS 60.231(1). Under the conditions described above, voters may participate in the meeting by telephone or other means of “remote communication.”

A quorum is measured at the start of the meeting. Once it is achieved, a quorum is deemed present throughout rest of the meeting, and any adjournments thereof, even though some shareholders leave the meeting before a particular vote. ORS 60.241(2); *ITC Cellular, Inc. v. Morris,* 909 SW2d 182 (Tex App 1995).

If voting is required by voting group – a majority of each voting group, participating as a voting group – is required for a quorum to be deemed present. ORS 60.241(1).

L. Conduct of meeting.

Effective January 1, 2003, Oregon adopted ORS 60.209 which provides rules for conducting shareholder meetings.

The new statute provides that a corporation must have a “chairperson” who shall preside at each shareholder meeting. If the bylaws do not provide for a chairperson, the board must appoint one to conduct the shareholder meeting.

Unless the articles or the bylaws provide otherwise, the chairperson “shall determine the order of business and shall have the authority to establish rules for the conduct of the meeting.” ORS 60.209(2).

The statute requires that any rules adopted must be fair to the shareholders.

ORS 60.209(3).

ORS 60.209(4) provides:

> The chairperson of the meeting shall announce at the meeting when the polls close for each matter voted upon. If no announcement is made, the polls shall be considered to have closed upon the final adjournment of the meeting. After the polls close, no ballots, proxies or votes, or any revocations or changes thereto, may be accepted.

Note: Corporations should adopt bylaw provisions which establish procedures for conducting shareholder meetings. In 2000, the Corporate Governance Committee of the American Bar Association published a Handbook for the Conduct of Shareholders' Meetings which contain model rules for that purpose. A corporation may want to incorporate some of these rules into its bylaws, or incorporate the Handbook by reference.

In this author's experience, it is uncommon for bylaws to contain much detail about the procedures for conducting shareholder meetings and for adopting resolutions. Some corporations seem to follow a procedure akin to Robert's Rules of Order, but such procedures are usually not found in the bylaws nor in corporate resolutions. Under ORS 60.60.209, the chairperson is authorized to impose such procedures on his/her own authority, provided such procedures are fair.

While the custom of making and "seconding" a motion is sometimes used at shareholder meeting, this author believes this procedure is not fair since shareholders usually own more than 1 share and each share is independently entitled to vote. If such a procedure is required, a single shareholder owning 51% of the total shares might be deprived of an up-or-down vote (a vote that the 51% shareholder is sure to win) for lack of a "second" to the motion. This is unfair.

M. Inspector of elections.

Effective January 1, 2003, Oregon adopted ORS 60.223 which requires all Oregon corporations with publicly traded shares to appoint one or more "inspectors" for voting at shareholder meetings. Non-public corporations are permitted to appoint election inspectors, but are not required to do so.

ORS 60.223(2) provides the inspectors shall:

> (a) Ascertain the number of shares outstanding and the voting power of each share;
> (b) Determine the shares represented at a meeting;
> (c) Determine the validity of proxies and ballots;
> (d) Count all votes; and
> (e) Determine the result.

The corporation can appoint one of its existing officers or employees as an inspector. ORS 60.223(3).

***N. Minutes*.**

ORS 60.771(1) requires that minutes of shareholder meetings be kept. *See* Section 4.04 of this book. Nevertheless, at least in close corporations and in family-owned corporations, the failure to keep minutes will not invalidate the actions taken. One court noted that "As to closely held corporations, in particular, action taken informally can be valid even though corporate formalities are not followed." *White v. Thatcher Financial Group, Inc.,* 940 P 2d 1034, 1037 (Colo App 1996).

> Although it would have been more orderly and businesslike, if the directors of the corporation had evidenced the understandings between the different stockholders by formal resolutions, rather than to proceed in the informal manner which they chose, nevertheless in such an instance as this, wherein all the stock of the corporation is owned by a few, and all or most of the stockholders are actively engaged in the enterprise of the corporation, it is often the practice to transact ordinary business without formal resolutions. (citations omitted) *Roles v. Roles Shingle Co.*, 147 Or 365, 371, 31 P2d 180, 182 (1934).

See also McMunn v. ML&H Lumber, Inc., 247 Or 319, 429 P2d 798 (1967); *Alpha Phi of Sigma Kappa v. Kincaid*, 180 Or 568, 178 P2d 156 (1947); *Block v. Olympic Health Spa, Inc.*, 24 Wash App 938, 604 P2d 1317 (1979); *Galler v. Galler*, 32 Ill2d 16, 203 NE2d 577 (1964); *In re B-F Building Corporation*, 284 F2d 679 (6th Cir 1960). *See also* Section 5.06 of this book.

Section 7.05 Proxies

A shareholder's right to vote is one of the most important rights incident to stock ownership. *Washington State Labor Council v. Federated American Insurance Co.*, 78 Wash 2d 263, 474 P2d 98 (1970).

At common law, shareholders could only vote *in person*, not by proxy. *Westland Development Co. v. Saavedra*, 80 NM 615, 459 P2d 141 (1969); *Klein v. United Theaters Co.*, 80 Ohio App 173, 75 NE2d 67, 70 (1947); *Harvey v. Linville Imp. Co.*, 118 NC 693, 24 SE 489 (1896).

Today, statutes provide that shareholders may vote by proxy.

A "proxy" is a:

> Written authorization given by one person to another so that the second person can act for the first, such as that given by a shareholder to someone else to represent him and vote his shares at a shareholders' meeting. Depending on the context, proxy may also refer to the grant of authority itself (the appointment), or the document granting the authority (the appointment form). BLACK'S LAW DICTIONARY (6th Ed 1990).

The Delaware courts have described a proxy as follows:

> A "proxy" or "proxy card" is merely written evidence of an agency relationship in which a principal (the shareholder of record entitled to vote) authorizes an agent (the

person designated on the proxy card) to vote the principal's shares with respect to the matters and in the manner specified in the proxy. *Parshalle v. Roy*, 567 A2d 19, 27 (Del Ch 1989).

The right to vote by proxy is not a general right, but rather a right granted and governed by statute. 14 *Op Or Atty Gen* 162 (1929); *Westland Development Co. v. Saavedra*, 80 NM 615, 459 P2d 141 (1969); *Skora v. Great Sweet Grass Oils Limited*, 30 Misc 2d 572, 205 NYS2d 98 (1960). In Oregon, the right of shareholders to vote by proxy is granted and governed by ORS 60.231.

NOTE: Proxy solicitations for most public companies are subject to detailed rules promulgated under the Securities Exchange Act of 1934, the Public Utility Holding Company Act of 1935, and/or the Investment Company Act of 1940. The rules promulgated by the federal Securities & Exchange Commission under these statutes do not apply to Oregon corporations which do not otherwise fall within the scope of these federal Acts. *Carter v. Portland General Electric Co.*, 227 Or 401, 362 P2d 766 (1961).

The right to vote by proxy may not be taken away from a shareholder by the articles, by the bylaws or by board resolution. But a corporation may adopt rules regulating the exercise of the right to vote by proxy – so long as such rules "are not unreasonable, arbitrary, or capricious." *Dixie Electric Power Association v. Hosey*, 208 So2d 751, 753 (Miss 1968); 14 *Op Or Atty Gen* 162 (1929).

Subject to such reasonable rules, a proxy may be given to any person. *People's Home Sav. Bank v. Superior Court of City & County of San Francisco*, 104 Cal 649, 38 P 452 (1894); 14 *Op Or Atty Gen* 162 (1929). A proxy given to a corporation's board of directors – as a group – should be voted as a majority of the board so determines. *Keough v. Kittleman*, 74 Wash 2d 814, 447 P2d 77 (1968). Proxies may be accompanied by secret instructions to the proxy-holder. *Id.*; *State ex rel Lally v. Cadigan*, 103 Wash 254, 174 P 965 (1918).

Only the owner of record has authority to appoint a proxy to vote the shares. A person who sells shares after the record date is still entitled to vote and can give another – including the buyer – a proxy to vote the shares. *Swaim v. Martin,* 302 Ky 381, 194 SW2d 855 (1946); *Dougherty v. Cross,* 65 Cal App 2d 687, 151 P2d 654 (1944).

Oregon law requires a proxy to be in writing and the proxy must be signed by the shareholder or its authorized representative – but otherwise, the statute does not set out any particular requirements as to the proxy's contents. ORS 60.231(2). Delaware courts have held that a proxy "must appoint someone to vote the shares and it must include some indication of authenticity, such as a signature." (citations omitted) *Lobato v. Health Concepts IV, Inc.*, 606 A2d 1343, 1347 (Del Ch 1991).

A proxy may be communicated electronically (including by facsimile), but

must be accompanied by authenticating information. ORS 60.231(2) & (3).

A proxy is presumed effective for eleven months, unless a shorter or longer period is expressly set out in the proxy. ORS 60.231(4); *Williams v. Williams*, 427 NE2d 727 (Ind App 1981), *rehearing granted in part*, 432 NE2d 417 (1982).

A proxy is generally revocable by the shareholder at any time, even if the proxy states on its face that it is irrevocable. *McKelvie v. Hackney*, 58 Wash 2d 23, 360 P2d 746 (1961); *State ex rel Everett Trust & Savings Bank v. Pacific Waxed Paper Co.*, 22 Wash 2d 844, 157 P2d 707 (1945); *State ex rel Breger v. Rusche*, 219 Ind 559, 39 NE2d 433 (1942); *Bridgers v. First Nat. Bank of Tarboro*, 152 NC 293, 67 SE 770 (1910). A shareholder's personal appearance at a shareholder meeting revokes the proxy – even an irrevocable proxy – at least where the shareholder indicates by his actions that the proxy is revoked. *Burleson v. Hayutin,* 130 Colo 58, 273 P1d 124 (1954); *Thomsen v. Yankee Mariner Corp.,* 106 Cal App 2d 454, 235 P2d 234 (1951).

There is an exception to this rule. A proxy "coupled with an interest" is irrevocable, unless the proxy itself provides otherwise. A non-exhaustive list illustrating interests which constitute appointments "coupled with an interest" is set forth in ORS 60.231(5):

(a) A pledgee;

(b) A person who purchased or agreed to purchase the shares;

(c) A creditor of the corporation that extended the corporation credit under terms requiring the authorization;

(d) An employee of the corporation whose employment contract requires the authorization; or

(e) A party to a voting agreement created under ORS 60.257.

See also Zoller v. Smith, 710 SW2d 155 (Tex App 1986); *State ex rel Everett Trust & Savings Bank v. Pacific Waxed Paper Co.*, 22 Wash 2d 844, 157 P2d 707 (1945).

Once the "interest" with which the proxy is coupled is extinguished, the proxy becomes a revocable proxy. ORS 60.231(7); *In re Fun Zones of Staten Island, Inc.,* 257 AD2d 575, 683 NYS2d 584 (1999).

A corporation may recognize the authority of a proxy, except for any express limitations appearing within the written proxy itself. ORS 60.231(9).

Section 7.06 Dividends & Other Distributions

A distribution is a transfer of corporate property to the shareholders. Distributions include dividends.

The Act defines "distribution" to means:

> a direct or indirect transfer of money or other property, except of a corporation's own shares, or incurrence of indebtedness by a corporation to or for the benefit of the corporation's shareholders in respect of any of the corporation's shares. A distribution may be in the form of a declaration or payment of a dividend, a purchase, redemption or other acquisition of shares, a distribution of indebtedness, or otherwise. ORS 60.001(7).

Corporate "profits" and "dividends" are not synonymous. *Brown v. Luce,* 231 Mo App 259, 96 SW 2d 1098 (1936); *Boothe v. Summit Coal Mining Co.*, 55 Wash 167, 104 P 207 (1909)(Rudkin concurring). "It is fundamental that corporate earnings, though amounting to corporate assets, are not the equivalent of dividends until declared such by the directors of the corporation." *In re Clark's Trust*, 29 Misc 2d 253, 217 NYS2d 396, 399 (1961).

Dividends are usually distributed pro rata among the shares of the class receiving the dividend. *Cobb v. Galloway*, 167 Or 604, 119 P2d 285 (1941). Both distributions and dividends may involve transfers of cash or of other property. *Anderson v. Burgess,* 110 Or 265, 223 P 244 (1924); *Grants Pass Hardware Co. v. Calvert*, 71 Or 103, 142 P 569 (1914). Distributions of cash are far more common than distributions of property.

Directors, not shareholders, decide when to issue dividends or other distributions. ORS 60.181(1). "In most states, the power to declare dividends is vested solely in the directors." *United States v. Byrum*, 408 US 125, 141 n 19 (1972). Courts generally will not interfere with the discretion of the board in the exercise of its business judgment in the declaration and payment of a dividend. *Gabelli & Co. v. Liggett Group Inc.,* 479 A2d 276 (Del 1984). Under very limited circumstances, a bylaw may confer authority to declare a dividend on an officer. *Blair v. Bishop's Restaurants, Inc.,* 202 Okla 648, 217 P2d 161 (1950).

A corporation has broad power to distribute its assets. *Spokane Concrete Products, Inc. v. U. S. Bank of Washington*, 126 Wash 2d 269, 892 P2d 98 (1995). There may be exceptions to this rule, such as when the corporation is insolvent. *In re Enron Corp.*, 323 BR 857 (Bankr SDNY 2005). *See* Sections 4.02 and 4.07 of this book.

Dividends and other distributions are discussed in much greater detail in Section 4.02 of this book. The power of the directors to make distributions and director liability for improper distributions are discussed Section 5.08 and 9.07 of this book.

Section 7.07 Preemptive Rights

A. Generally.

A preemptive right is the right of all shareholders to maintain their proportionate ownership in a corporation. It is the right:

> granted on uniform terms and conditions prescribed by the board of directors to provide a fair and reasonable opportunity to exercise the right to acquire proportional amounts of the corporation's unissued shares upon the decision of the board of directors to issue them. ORS 60.174(3)(a).

Preemptive rights exist to protect minority shareholders.

> Preemptive rights exist for the purpose of protecting the shareholder's interest in his control or proportionate voting rights and in his proportionate. *Fuller v. Krogh,* 15 Wis2d 412, 113 NW2d 25, 32 (1962)

Preemptive rights may be created by including a statement in the articles of incorporation to the effect that "the corporation elects to have preemptive rights," or words of similar import. ORS 60.174(3).

NOTE: Shareholders of corporations formed prior to June 15, 1987 have preemptive rights, unless the articles specifically provide otherwise (originally or by amendment). Shareholders of corporations formed on or after June 15, 1987 do not have preemptive rights, unless the articles specifically provide otherwise. ORS 60.174. The articles can, and should, state specifically whether or not preemptive rights exist in order to minimize later confusion (and legal fees) on this issue.

While preemptive rights are extremely rare in any corporation with a large number of shareholders, such rights are more common in closely held corporations. Preemptive rights give minority shareholders a chance to maintain their ratio of ownership.

EXAMPLE: A, B, and C each contribute $10,000 to ABC, Inc. and each receives 100 shares of ABC, Inc. common stock. Each is elected to be a director. At some later date, animosity develops. A and B wish to decrease C's relative ownership interest. Without preemptive rights, A and B could prevail in a vote to issue an additional 3000 shares of stock to themselves. (A and B would still be bound by their fiduciary duty to the corporation regarding fair consideration for the new shares.) C's proportional ownership interest in ABC, Inc. could be reduced to insignificance.

With preemptive rights, C would have the opportunity to purchase additional shares sufficient to maintain C's percentage ownership. The purchase would need to be on the same terms as the proposed sale to A and B. Thus, if C has access to sufficient funds and desires to do so, C could purchase 1000 shares of ABC, Inc. stock and could maintain C's one-third

ownership interest in ABC, Inc.

Some courts have held that even though a corporation does not grant its shareholders preemptive rights, the directors have a duty not to discriminate among shareholders and particularly, not to use their positions for their own personal advantage. *Schwartz v. Marien*, 37 NY2d 487, 335 NE2d 334 (1975); *Sheppard v. Wilcox*, 210 Cal App 2d 53, 26 Cal Rptr 412 (1963).

If the corporation modifies preemptive rights, this may trigger the right to dissent. ORS 60.554(1)(d)(A); *Waters v. Double L, Inc.,* 114 Idaho 256, 755 P2d 1294 (Idaho App 1987).

B. How long open?

With preemptive rights, there is no time specified during which the offer to purchase a proportionate number of shares must remain open to the shareholders. The board is merely required "to provide a fair and reasonable opportunity" for the shareholders to come forward and purchase their proportionate number of shares. ORS 60.174(3)(a); *Jones v. Morrison*, 31 Minn 140, 16 NW 854 (1883); *Bennett v. Baum*, 90 Neb 320, 133 NW 439, 442 (1911)(five days is unreasonable); *Van Slyke v. Norris*, 159 Minn 63, 198 NW 409, 412 (1924)(60 days is reasonable).

***C. Securities laws are applicable*.**

The cost and trouble of preemptive rights increases dramatically if a corporation has a significant number of shareholders.

Preemptive rights involve the offer and sale of stock for new value. As such, compliance with the securities laws is required. A corporation will likely need to comply with the federal securities laws and with the securities laws of each and every state in which it makes an offer (*i.e.,* every state in which one of its shareholders resides and in the state of its own business office).

Oregon has an exemption from registration for proportionate offerings made to existing shareholders under some circumstances. ORS 59.035(3). Many states have no such exemption. Regardless, a corporation must comply with the disclosure requirements of the various securities laws, even if exempt from registration. The costs associated with disclosure can be high.

Public companies rarely, if ever, grant preemptive rights to their shareholders.

***D. Exceptions to preemptive rights*.**

ORS 60.174(3)(c) provides that no preemptive rights exist with respect to:

(A) Shares issued as compensation to directors, officers, agents or employees of the corporation, its subsidiaries or affiliates;

(B) Shares issued to satisfy conversion or option rights created to provide compensation to directors, officers, agents or employees of the corporation, its subsidiaries or affiliates;

(C) Shares authorized in articles of incorporation that are issued within six

months from the effective date of incorporation; or

(D) Shares sold other than for money.

Given the nature and number of exceptions to preemptive rights under current law, preemptive rights today have questionable merit. Preemptive rights offer little protection when those in control of the corporation are legally astute.

For instance, a corporation is often indebted to some of its shareholders. Preemptive rights do not apply to shares issued in good faith for other than money. ORS 60.174(3)(c)(D); *Robinson v. Malheur Publishing Co.*, 272 F Supp 57 (D Or 1967).

Similarly, majority shareholders are often corporate directors, officers and employees. Preemptive rights do not apply to shares awarded as compensation to directors, officers and employees – so long as the award is approved by a majority of the shares then outstanding. ORS 60.174(3)(c)(A).

Likewise, majority shareholders may be able to amend the articles of incorporation to eliminate preemptive rights. *McCallum v. Gray*, 273 Or 617, 542 P2d 1025 (1975).

> Then turning to the view that preemptive rights are designed to guarantee the stockholder his original fraction of voting control, we are unable to perceive any difference in the constitutional implications. We know of no authority holding, that voting rights are more sacred or less mutable than money rights. It has heretofore simply been taken for granted that voting rights, so far as the constitution is concerned, are as amendable as any other.
>
> * * *
>
> Any interpretation other than the one we feel bound to adopt would seriously impair the existing rights of the holders of a majority of the stock. They purchased their holdings under the assurance of the Delaware General Corporation Law, as well as of the terms of the particular contract of the State of Delaware with defendant, that the defendant corporation, in which they were about to buy an interest, would have the right from time to time to make amendments to its charter, at the direction and with the approval of the holders of a majority (or other specified percentage) of the stock, and would thus be in a position to adjust itself to the exigencies of changing business conditions. Similarly, the minority stockholders purchased their holdings with full notice of this same mutability. The majority, therefore, cannot now be frozen by the minority to a charter which the majority regards as out of date. *Gottlieb v. Heyden Chemical Corp.*, 33 Del Ch 82, 90 A2d 660, 667 (1952).

But this may trigger the right to dissent. ORS 60.554(1)(d)(A); *Waters v. Double L, Inc.,* 114 Idaho 256, 755 P2d 1294 (Idaho App 1987).

While the protection offered by preemptive rights may once have been worthwhile, today shareholder agreements and other contracts usually offer better protection.

***E. Court protection*.**

If minority shareholders have preemptive rights and those rights are not honored, the minority may seek court protection. If either the corporation or the

majority has acted improperly, a court may require the corporation to issue minority shareholders a proportionate number of shares at the same price paid by the majority. *Browning v. C & C Plywood Corp.*, 248 Or 574, 434 P2d 339 (1968); *Cressy v. Shannon Continental Corporation*, 177 Ind App 224, 378 NE2d 941 (1978).

***F. Additional sources*.**

A discussion of preemptive rights under the current Act is contained in Art, *Corporate Shares and Distributions in a System Beyond Par Value: Financial Provisions of Oregon's New Corporation Act*, 24 WILL L REV 203, 243-5 (1988).

A discussion of the duty majority shareholders owe to minority shareholders is contained in Sections 7.10 and 7.11 of this book.

Section 7.08 Voting Trusts

***A. Defined*.**

A voting trust is a device through which some or all of the shareholders transfer the voting rights of their shares to a trustee or trustees, thus pooling the votes of those shares with the votes of the other shares participating in the trust. In a voting trust, a shareholder retains all other ownership rights in the stock (*e.g.*, the right to dividends and other distributions).

> A voting trust as commonly understood is a device whereby two or more persons owning stock with voting powers, divorce the voting rights thereof from the ownership, retaining to all intents and purposes the latter in themselves and transferring the former to trustees in whom the voting rights of all the depositors in the trust are pooled. *Peyton v. William C. Peyton Corp.*, 194 A 106, 111 (Del Ch 1937), *reversed on other grounds*, 7 A2d 737 (Del Supr 1939).

All trusts which hold stock are not voting trusts. A voting trust can be distinguished from other trusts which own and vote stock by the following criteria:

> (1) the voting rights of the stock are separated from the other attributes of ownership; (2) the voting rights granted are intended to be irrevocable for a definite period of time; and (3) the principal purpose of the grant of voting rights is to acquire voting control of the corporation. (citations omitted). *Jackson v. Jackson*, 178 Conn 42, 420 A2d 893, 895 (1979).

See also Bamford v. Bamford, Inc., 279 Neb 259, 777 NW2d 573, 578-79 (2010); *Oceanic Exploration Co. v. Grynberg*, 428 A2d 1 (Del 1981).

***B. Old rule – disfavored*.**

Initially, courts were hostile to voting trusts – particularly voting trusts in which less than all shareholders participated. *Kaufman v. Lombard*, 100 Or 378, 197 P 314 (1921); *Leadbetter v. Hawley*, 59 Or 422, 117 P 289, 117 P 505 (1911); *Keady v. United Rys. Co.*, 57 Or 325, 108 P 197 (1910); *Oceanic Exploration Co. v. Grynberg*, 428 A2d 1, 7 (Del 1981); *Bridges v. First Nat. Bank of Tarboro*, 152 NC 293, 67 SE

770 (1910); *Bostwick v. Chapman*, 60 Conn 553, 24 A 32 (1890).

Beginning in 1908 with a voting trust statute adopted by New York, followed by the pattern of condoning voting trusts by various versions of the Model Business Corporation Act, and followed by the eventual adoption of such provisions by nearly all states, judicial hostility to voting trusts has virtually disappeared. Official Comment to RMBCA § 7.30; FLETCHER CYC CORP § 2080.1 (Perm Ed). *See also Jones v. Wallace*, 291 Or 11, 628 P2d 388 (1981); *Oceanic Exploration Co. v. Grynberg*, 428 A2d 1, 7-8 (Del 1981).

***C. Current law – permitted*.**

The modern view is that voting trusts are valid, even in the absence of a statute, provided no improper motive or object is demonstrated. H.W. BALLANTINE, BALLANTINE ON CORPORATIONS 146 (1946).

ORS 60.254 specifically recognizes voting trusts and sets out the procedure which must be followed in establishing and operating such trusts. The statute requires that a copy of the trust agreement and the names and addresses of all trust participants be delivered to the corporation. This simple disclosure requirement eliminates the possibility that the voting trust may be used to create "secret, uncontrolled combinations of stockholders to acquire control of the corporation to the possible detriment of non-participating shareholders." *Lehrman v. Cohen*, 222 A2d 800, 807 (Del 1966). *See also State ex rel Elish v. Wilson,* 189 W Va 739, 434 SE2d 411, 419 (1993).

A voting trust is valid for no more than 10 years. ORS 60.254(2). A voting trust may be extended for additional periods of not more than 10 years each if some or all of the parties to the agreement assent in writing and the voting trustee delivers copies of the extension agreement and a list of beneficial owners to the corporation. ORS 60.254(3). The extension agreement only binds those parties who sign it. *Id*. The Official Comments to the Revised Model Act indicates that a voting trust for more than 10 years is valid, but only for its first 10 years. Official Comment to RMBCA § 7.30. There is case law to the contrary. *Hanley v. Most*, 9 Wash 2d 429, 115 P2d 933 (1941).

ORS 60.257 specifically recognizes shareholder voting agreements other than voting trusts. This section was included in order to clarify this issue under Oregon law. TASK FORCE REPORT § 66. A contracts which grants shareholders the right to purchase each other's stock under specified circumstances are a common type of such agreement. *See for example Card v. Stirnweis*, 232 Or 123, 374 P2d 472 (1962).

> **NOTE:** Bylaws are not shareholder agreements in the sense that unlike most contracts, bylaws can usually be amended by majority vote. *Jones v.*

Wallace, 291 Or 11, 628 P2d 388 (1981).

The trustee of a voting trust owes a fiduciary duty to its shareholder/beneficiaries. *Wool Growers Service Corp. v. Ragan*, 18 Wash 2d 655, 140 P2d 512, 527, *rehearing denied*, 18 Wash 2d 655, 141 P2d 875 (1943).

Under certain circumstances, shareholders of some corporations may enter into voting agreements which contain provisions otherwise inconsistent with the Oregon Business Corporation Act. ORS 60.265. A discussion of ORS 60.265 is contained in Section 4.07 of this book.

Section 7.09 Shareholder's Duty to the Corporation

As a general rule, an individual shareholder stands in no particular fiduciary relationship to the corporation and may deal with the corporation in an arms'-length manner. *Hagshenas v. Gaylord*, 199 Ill App 3d 60, 557 NE2d 316 (1990); *Robbins v. Huntley Cattle Co.*, 3 Wash 2d 203, 100 P2d 386 (1940).

Ordinarily, a shareholder may compete with the corporation. *Wagner v. Foote*, 128 Wash 2d 408, 908 P2d 884 (1996); *Penley v. Penley*, 101 NC App 225, 398 SE2d 671 (1990); *Witmer v. Arkansas Dailies, Inc.*, 202 Ark 470, 151 SW2d 971 (1941). A shareholder may lend money to the corporation and otherwise be a creditor. *Bellaire Securities Corporation v. Brown*, 124 Fla 47, 168 So 625 (1936). A shareholder may enforce his/her rights as a creditor and may sue or levy against corporate property. *H. K. McCann Co. v. Week*, 139 Wash 183, 246 P 292, *affirmed*, 141 Wash 702, 251 P 858 (1927). A shareholder generally has owes no fiduciary duty when buying or selling stock from another shareholder. *Hardy v. South Bend Sash & Door Co.*, Inc., 603 NE2d 895 (Ind App 1992).

A shareholder may vote his/her shares even though personally interested in the vote outcome since, in a meeting of shareholders, "each shareholder represents himself and his personal interests solely, and he in no sense acts as a trustee or representative of others." *Ostlind v. Ostlind Valve, Inc.*, 178 Or 161, 184, 165 P2d 779, 788 (1945).

Likewise, a shareholder owes no duty to other shareholders when selling shares to an outside party, other than a duty not deceive other shareholders about the terms of the sale. *Dunnett v. Arn*, 71 F2d 912 (10th Cir 1934).

> There being no fiduciary relationship existing between the stockholders of the bank so far as the sale of individual stock was concerned, there was no duty upon the part of Smith to apprise minority stockholders of Transamerica's offer. The fact that Smith et al. received more for their stock than the minority is no evidence of fraud, since it is generally recognized that the stock of majority stockholders is of more value than that of the minority. (citations omitted) *Tyron v. Smith*, 191 Or 172, 180, 229 P2d 251, 254 (1951).

While as a general rule, shareholders owe no fiduciary duty to the corporation

or the other shareholders, the general rule may not apply to shareholders who are controlling/majority shareholders or are officers or directors, each of whom can owe a fiduciary duty to the corporation and its shareholders. *See for example Naito v. Naito*, 178 Or App 1, 35 P3d 1068 (2001); *Locati v. Johnson,* 160 Or App 63, 980 P2d 173 (1999); *Wulf v. Mackey,* 135 Or App 655, 899 P2d 755 (1995); *Noakes v. Schoenborn,* 116 Or App 464, 472, 841 P2d 682 (1992); *Merger Mines Corp. v. Grismer*, 137 F2d 335 (9th Cir 1943). The fiduciary duty of directors and officers is discussed in Sections 5.14 and 6.11 of this book. The fiduciary duty of majority or controlling shareholders is discussed in Section 7.10 of this book.

Under some circumstances, all shareholders of a close corporation may owe a fiduciary duty to the corporation, as well as to each other. The duty of shareholders in close corporations is discussed in Section 7.11 of this book.

Section 7.10 Duty of Controlling Shareholders

As a general rule, an individual shareholder stands in no particular fiduciary relationship to the corporation and may vote the shareholder's personal self-interest and may deal with the corporation in an arms'-length manner. *Ostlind v. Ostlind Valve, Inc.*, 178 Or 161, 184, 165 P2d 779, 788 (1945); *Robbins v. Huntley Cattle Co.*, 3 Wash 2d 203, 100 P2d 386 (1940) "[W]hen a person becomes a stockholder in a corporation, he assents to majority rule and impliedly agrees to abide thereby." *Benton v. United States*, 114 F Supp 37, 45 (MD Ga 1953).

On the other hand, majority/controlling shareholders may owe a fiduciary duty to their fellow shareholders, at least under certain circumstances. *Naito v. Naito*, 178 Or App 1, 35 P3d 1068 (2001); *Locati v. Johnson,* 160 Or App 63, 980 P2d 173 (1999); *Wulf v. Mackey,* 135 Or App 655, 899 P2d 755 (1995); *Noakes v. Schoenborn,* 116 Or App 464, 472, 841 P2d 682 (1992);*Crosby v. Beam,* 47 Ohio St.3d 105, 108 (1989).

The United States Supreme Court said:

> A director is a fiduciary. So is a dominant or controlling stockholder or group of shareholders. Their powers are powers in trust. Their dealings with the corporation are subject to rigorous scrutiny and where any of their contracts or engagements with the corporation is challenged the burden is on the director or stockholder not to prove the good faith of the transaction but also to show the inherent fairness from the viewpoint of the corporation and those interested therein. (citations omitted) *Pepper v. Litton*, 308 US 295, 307 (1939).

In close corporations, the dominant view is that controlling shareholders owe a fiduciary duty to minority shareholders.

> Most state courts have held that a controlling shareholder owes fiduciary duties to minority shareholders, particularly in the close corporation setting. *See, e.g., Jones v. H.F. Ahmanson & Co.,* 460 P.2d 464, 470 (Cal. 1969); *Rexford Rand Corp. v. Ancel*, 58 F.3d 1215, 1220-21 (7th Cir. 1995) (applying Illinois law); *Wilkes v.*

Springside Nursing Home, Inc., 353 N.E.2d 657, 663-65 (Mass. 1976); *Gay v. Gay's Super Markets, Inc.,* 343 A.2d 577, 582 (Me. 1975); *Evans v. Blesi,* 345 N.W.2d 775, 780 (Minn. Ct. App. 1984); *Frank Lerner & Assocs., Inc. v. Vassy,* 599 N.E.2d 734, 738 (Ohio Ct. App. 1991); *Zidell v. Zidell*, 560 P.2d 1086, 1089 (Or. 1977); *Ferber v. Am. Lamp Corp*., 469 A.2d 1046, 1050 (Pa. 1983); *Nelson v. Martin,* 958 S.W.2d 643, 649 (Tenn. 1997); *J Bar H, Inc. v. Johnson,* 822 P.2d 849, 859 (Wyo. 1991). *But see, e.g., Redmon v. Griffith,* 202 S.W.3d 225, 237 (Tex. App. 2006)

Yokeno v. Sekiguchi, Civil Case No. 09-00020 (D Guam August 19, 2011).

Unfortunately, the analysis in this area is confused by the fact that majority/controlling shareholders quite frequently also serve as directors and officers. The law is clear officers and directors owe a fiduciary duty to the corporation and to the shareholders collectively. “The distinction between controlling shareholders and directors may not be of great significance in this context.” *Naito v. Naito*, 178 Or App 1, 21, 35 P3d 1068 (2001). *See* Sections 5.14 and 6.11 of this book.

There are cases, however, which hold that a person's status as a controlling shareholder alone creates a fiduciary duty. *Jones v. H.F Ahmanson & Co.*, 81 Cal Rptr 592, 460 P2d 464 (1969) is a "pure" shareholder fiduciary duty case, that is, a case in which "all actions of the defendant shareholders were taken by them in their capacity as shareholders of the operating company, not as directors.” Murdock, *"The Evolution of Effective Remedies for Minority Shareholders and Its Impact Upon Valuation of Minority Shares*," 65 NOTRE DAME L REV 425, 433-4 (1990). In *Jones*, the California Supreme Court held:

> [M]ajority shareholders, either singly or acting in concert to accomplish a joint purpose, have a fiduciary responsibility to the minority and to the corporation to use their ability to control the corporation in a fair, just, and equitable manner. Majority shareholders may not use their power to control corporate activities to benefit themselves alone or in a manner detrimental to the minority. *Jones v. H.F Ahmanson & Co.*, 81 Cal Rptr 592, 460 P2d 464 (1969).

See also Retzer v. Retzer, 578 So2d 580 (Miss 1990); *Alaska Plastics, Inc. v. Coppock*, 621 P2d 270 (Alaska 1980).

NOTE: Older cases generally speak in terms of the duty owed by "majority shareholders." The modern trend is to speak of the duty owed by "controlling shareholders." There is a now widespread recognition that one or more persons can control the corporation without necessarily owning 51% of the stock.

It is clear that someone who owns more than 50% of the shares is controlling shareholder, but the term can also include a small group of shareholders acting in concert. The American Law Institute’s Principles of Corporate Governance provide:

> A 'controlling shareholder' means a person * * * who, either alone or pursuant to an arrangement or understanding with one or more other persons:
>
> (1) owns and has the power to vote more than 50 percent of the outstanding voting equity securities * * * of the corporation; or

> (2) otherwise exercises a controlling influence over the management or policies of the corporation or the transaction in question by virtue of the person's position as a shareholder.

American Law Institute, Principles of Corporate Governance § 1.10(a) (1994).

The Oregon Court of Appeals has said:

> in order to be a controlling shareholder who owes fiduciary duties a shareholder must either be (1) an individual who owns a majority of the shares or who, for other reasons, has domination or control of the corporation or (2) a member of a small group of shareholders who collectively own a majority of shares or otherwise have that domination or control. *Locati v. Johnson,* 160 Or App 63, 69, 980 P2d 173 (1999).

Locati suggests that a common shareholder interest or motive is not determinative on whether a group of shareholders voting on the same side of a question constitute "controlling" shareholders. If fact that seems to be the rationale supporting the reversal of a jury verdict in favor of the minority shareholder after remand. *Locati v. Johnson*, 204 Or App 683, 131 P3d 779 (2006).

See also Stringer v. Car Data Systems, Inc., 108 Or App 523, 816 P2d 677, on reconsideration 110 Or App 14, 821 P2d 418 (1991), *affirmed on other grounds,* 314 Or 576, 841 P2d 1183 (1992).

***A. Oregon cases*.**

There are many Oregon cases which state that majority and control shareholders owe a fiduciary duty to the corporation and to all shareholders.

> [A controlling shareholder] assumes the obligation to manage the affairs of the controlled corporation for the benefit of all of the shareholders and not for its own aggrandizement. *Baillie v. Columbia Gold Mining Co.*, 86 Or 1, 32, 166 P 965, 974, 167 P 1167 (1917).

> "We have recognized that those in control of corporate affairs have fiduciary duties of good faith and fair dealing toward the minority shareholders." (citations omitted) *Zidell v. Zidell*, Inc., 277 Or 413, 418, 560 P2d 1086, 1089 (1977).

See also *Locati v. Johnson,* 160 Or App 63, 980 P2d 173 (1999); *Wulf v. Mackey,* 135 Or App 655, 899 P2d 755 (1995); *Noakes v. Schoenborn,* 116 Or App 464, 472, 841 P2d 682 (1992).

***B. Other states*.**

Courts in other state also have held that majority shareholders owe a fiduciary duty to the corporation and other shareholders – at least under some circumstances.

For instance under Delaware law, a majority shareholder owes a fiduciary duty to the minority shareholders "in dealing with the latter's property" in a merger transaction. *Singer v. Magnavox Co.*, 380 A2d 969 (Del 1977).

Under California law, the majority shareholder "must exercise good faith and fairness" in situations "where the control of the corporation is material." *DeBaun v. First Western Bank & Trust Co.*, 46 Cal App 3d 686, 696, 120 Cal Rptr 354 (1975).

Under Washington law, the "principle that a majority of stockholders must, at all times, exercise good faith toward the minority stockholders is well recognized." *Hay v. Big Bend Land Co.*, 32 Wash 2d 887, 897, 204 P2d 488, 494 (1949).

Under Connecticut law, "a dominant or majority shareholder bears the same fiduciary duty to the corporation and its minority shareholders as does a director." *Governors Grove Condominium Association, Inc. v. Hill Development Corporation*, 36 Conn Sup 144, 414 A2d 1177, 1183-4 (1980).

See also Estate of Schroer v. Stamco Supply, Inc., 19 Ohio App 3d 34, 482 NE2d 975 (1984); *Wilkes v. Springside Nursing Home, Inc.*, 353 NE2d 657 (Mass 1976); *Seagrave Corp. v. Mount*, 212 F2d 389 (6th Cir 1954).

***C. Exceptions*.**

Majority/controlling shareholders do not owe a fiduciary duty to the minority shareholders under all circumstances.

For instance, a controlling shareholder may vote his/her shares even though personally interested in the vote outcome since, in a meeting of shareholders, "each shareholder represents himself and his own interests solely, and he in no sense acts as a trustee or representative of others." *Ostlind v. Ostlind Valve, Inc.*, 178 Or 161, 184, 165 P2d 779, 788 (1945). *See also D'Arcangelo v. D'Arcangelo*, 137 NJ Eq 63, 43 A2d 169 (1945).

Ordinarily, a majority shareholder may sell his/her own stock to a third party – even at a premium – without breaching any duty to the minority shareholders, except for the duty to act in good faith and in a non-fraudulent manner.

> There being no fiduciary relationship existing between the stockholders of the bank so far as the sale of individual stock was concerned, there was no duty upon the part of Smith to apprise minority stockholders of Transamerica's offer. The fact that Smith et al. received more for their stock than the minority is no evidence of fraud, since it is generally recognized that the stock of majority stockholders is of more value than that of the minority. (citations omitted) *Tyron v. Smith*, 191 Or 172, 180, 229 P2d 251, 254 (1951).

Another court held:

> the power to control the corporation through majority stock ownership is not a corporate asset which must be shared with all stockholders; in a sale of stock, the role as owner takes precedence over the role as fiduciary. Thus, as a general rule a director, officer, and majority shareholder may freely negotiate a sale at a premium price of his or her stock and the benefits incident to majority ownership. *Delano v. Kitch*, 667 F2d 990, 998 (10th Cir 1981).

See also Wagner v. Foote, 128 Wash 2d 408, 908 P2d 884 (1996); *Draper v. Hay*, 555 So2d 1306 (Fla App 1990); *Yerke v. Batman*, 376 NE2d 1211 (Ind App 1978).

Section 7.11 Duty of Shareholders in Close Corporation

A. Close corporation defined.

In a leading case on the duties of shareholders in close corporations, the Massachusetts Supreme Judicial Court described a close corporation to be:

> We deem a close corporation to be typified by: (1) a small number of stockholders; (2) no ready market for the corporate stock; and (3) substantial majority stockholder participation in the management, direction and operations of the corporation. *Donahue v. Rodd Electrotype Co.*, 367 Mass 578, 586, 328 NE2d 505 (1975).

The American Law Institute's Principles of Corporate Governance defines a close corporation as follows:

> "Closely held corporation" means a corporation the equity securities of which are owned by a small number of persons, and for which securities no active trading market exists. § 1.06 ALI Principles of Corporate Governance.

A close corporation involves shares held in only "a few hands, or in a few families" with rare "buying or selling" of its shares. *Galler v. Galler*, 32 Ill 2d 15, 203 NE2d 577, 583 (1964).

The terms "close corporation" and "closely held corporation" have the same meaning and are used interchangeably.

NOTE: Some states have enacted special statutory provisions related to close corporations, provisions which generally require a corporation to take some affirmative step in order to be deemed a “close corporation” – for example, including in its articles a statement that it is a close corporation. In such states, failure to comply with these requirements may mean the corporation is not a close corporation despite it having only a few shareholders. *See for example Hunt v. Data Management Resources, Inc.,* 26 Kan App 2d 405, 985 P2d 730, 732-3 (1999); *Nixon v. Blackwell,* 626 A2d 1366, 1380 (Del 1993).

Oregon has not adopt a “close corporation” statute and, therefore, there are no statutory hoops for a corporation to jump through in order to attain such status.

B. Close corporations are like partnerships.

Many cases and commentators have noted the similarity between close corporations and partnerships.

> Close corporations have been analogized and, for some purposes, judicially treated as partnerships. The basis for the comparison is that the characteristics associated with close corporations are generally found in partnerships. Corporate status is elected by the shareholders in order to "clothe" their partnership `with the benefits peculiar to a corporation, limited liability, perpetuity and the like.'" When a close corporation is formed, the shareholders often consider themselves partners, but treat the enterprise as a corporation when dealing with others. Flowing from this analogy to partnerships, courts have imposed a fiduciary duty upon shareholders in close corporations similar to the duty of general partners owe to each other. (footnotes

> omitted) Blaiklock, *Fiduciary Duties Owed by Frozen-Out Minority Shareholders in Close Corporations*, 30 IND L REV 763, 766-7 (1997).

Another commentator has said of shareholders in close corporations:

> The shareholder is often induced to leave a secure job, mortgage his home, and invest his life and fortune in the venture. His shares often constitute the major asset in his estate. The shareholder purchases not stock, but a future. He is not investing in a legal entity, but embarking with his friends on a cooperative adventure. The reasonable expectations of such a shareholder are a job, a salary, a significant place in management, and economic security for his family. He does not want mere pieces of paper- the stock certificates. Olson, *"A Statutory Elixir for the Oppression Malady,"* 36 MERCER L REV 627, 629 (1995).

The shareholders of close corporations often elect to have their business taxed as if it were a partnership, rather than a corporation.

> The United States Internal Revenue Code gives substantial recognition to the fact that close corporations are often merely incorporated partnerships. The so called Subchapter S enables "small business corporations," defined by statute, to make an election which generally exempts the corporation from taxation and causes inclusion of the corporation's undistributed, as well as distributed, taxable income in the gross income of the stockholders for the year. This is essentially the manner in which partnership earnings are taxed. (citations omitted) *Donahue v. Rodd Electrotype Co.*, 367 Mass 578, 328 NE2d 505, 512 n 12 (1975).

Courts have noted that shareholders of close corporations often have a substantial personal investment in their corporations and often depend on the corporation for most of their income. When the majority acts improperly, there is no active market for their stock. *Rexford Rand Corp. v. Ancel*, 58 F3d 1215, 1219 (7th Cir 1995).

> At this point, the true plight of the minority shareholder in a close corporation becomes manifest. He cannot easily reclaim his capital. In a large public corporation, the oppressed or dissident minority could sell his stock in order to extradite some of his invested capital. By definition, this market is not available for shares in the close corporation.
>
> * * * *
>
> Thus, in a close corporation, the minority stockholders may be trapped in a disadvantageous situation. No outsider would knowingly assume the position of the disadvantaged minority. The outsider would have the same difficulties. To cut losses, the minority shareholder may be compelled to deal with the majority. This is the capstone of the majority plan. Majority "freeze-out" schemes which withhold dividends are designed to compel the minority to relinquish stock at inadequate prices. *Donahue v. Rodd Electrotype Co.*, 367 Mass 578, 328 NE2d 505, 514-5 (1975)).

As a consequence, many courts have analogized close corporations to partnerships. *Card v. Stirnweis*, 232 Or 123, 374 P2d 472 (1962). "The relationship among shareholders in closely held corporations is analogous to that of partners." *Pedro v. Pedro*, 489 NW2d 798, 801 (Minn App 1992).

> When a corporation is organized, the principles of the law of partnership may in very many respects be held to govern the stockholders in their conduct in respect to each other and in respect to the corporation. *Willamette Freighting Co. v. Stannus*, 4 Or

261, 269 (1872).

Before treating a close corporation as a partnership, some courts look to whether the owners view themselves as "partners." *See for example Hartung v. Architects Hartung/Odle/Burke, Inc.*, 157 Ind App 546, 301 NE2d 240 (1973).

But the partnership analogy is not perfect. For instance unlike a general partner in a partnership, a minority shareholder in a close corporation may not unilaterally dissolve the corporation. *Baker v. Commercial Body Builders, Inc.*, 264 Or 614, 630, 507 P2d 387, 394 (1973). However, ORS 60.661 permits a minority shareholder to seek judicial dissolution of a corporation for oppressive conduct. *See* Section 8.04 of this book.

C. In close corporation, all shareholders may owe fiduciary duty.

Because close corporations are like partnerships, the trend has been for courts to hold that shareholders in close corporations owe a fiduciary duty to the corporation and to each other.

> As fully discussed elsewhere in this treaties, shareholders in a close corporation stand in a fiduciary relationship to each other. Thus, for example, shareholders in a closely held corporation cannot compete for business or clients which in equity and fairness belong to the corporation. The relationship between shareholders in a close corporation vis-a-vis each other closely approximates the relationship between partners. (footnotes omitted) FLETCHER CYC CORP § 70.10 (Perm Ed).

Some courts have held that the fiduciary duty among shareholders in close corporations is even stronger than is the duty of directors and shareholders in public corporations.

> In the case of a close corporation, which resembles a partnership, duties of loyalty extend to shareholders, who owe one another substantially the same duty of utmost good faith and loyalty in the operation of the enterprise that partners owe to one another, a duty that is even stricter than that required of directors and shareholders in corporations generally. *Demoulas v. Demoulas Super Markets, Inc.*, 424 Mass 501, 677 NE2d 159, 179 (1997).

In *Donahue v. Rodd Electrotype Co.*, 367 Mass 578, 328 NE2d 505 (1975) – the leading case on the fiduciary duty of shareholders in close corporations – the court extended the "more rigorous duty of partners" to shareholders in a close corporation. *Id*. at 516. The fiduciary duty standard set out in *Donahue* has gained "widespread acceptance." 2 O'Neal's Oppression of Minority Shareholders § 7.04, pg 39.

D. Majority shareholders in close corporation owe fiduciary duty.

Majority shareholders, in both public and close corporations, owe a fiduciary duty to the corporation and its minority shareholders. It has long been held that the majority "assumes the obligation to manage the affairs of the controlled corporation for the benefit of all of the shareholders and not for its own aggrandizement." *Baillie v. Columbia Gold Mining Co.*, 86 Or 1, 32, 166 P 965, 974, 167 P 1167 (1917). *See*

also Zidell v. Zidell, Inc., 277 Or 413, 560 P2d 1086 (1977); *Hay v. Big Bend Land Co.*, 32 Wash 2d 887, 897, 204 P2d 488, 494 (1949).

Given the higher duty that has been recognized among shareholders of close corporations, it should come as no surprise that in a close corporation, a majority shareholder owes a fiduciary duty to the close corporation and its shareholders. This is true in Oregon. "The majority shareholders of a close corporation owe the minority fiduciary duties of loyalty, good faith, fair dealing and full disclosure." *Chiles v. Robertson*, 94 Or App 604, 619, 767 P2d 903 (1989). *See also Cooke v. Fresh Express Foods Corp.,* 169 Or App 101, 7 P3d 717 (2000); *Noakes v. Schoenborn*, 116 Or App 464, 841 P2d 682 (1992); *Grato v. Grato*, 272 NJ Super 140, 639 A2d 390 (1994); *Pedro v. Pedro*, 489 NW2d 798 (Minn App 1992).

***E. Business judgment rule*.**

In the context of close corporations, the business judgment rule may not apply. Although some oppression cases will cite to the business judgement rule in an oppression case, it does not appear to be determinative. In *Cooke v. Fresh Express Foods Corp.,* 169 Or App 101, 7 P3d 717, 722 (2000) (which found oppression), the court said:

> Courts give significant deference to the majority's judgment in the business decisions that it makes, at least if the decisions appear to be genuine business decisions. As we have noted, attempts to define what oppressive conduct is, instead of what it is not, have proved elusive, and cases of this sort depend heavily on their specific facts. *See Weiner Investment Co. v. Weiner,* 105 Or.App. 339, 342-43, 804 P.2d 1211 (1991). The court must evaluate the majority's actions, keeping in mind that, even if some actions may be individually justifiable, the actions in total may show a pattern of oppression that requires the court to provide a remedy to the minority.

In *Davis v. Brockamp & Jaeger, Inc.*, 216 Or App 518, 174 P3d 607, 614 (2007)(which did not find oppression), the court said the "court must defer to the business decisions made by the majority shareholders of a close corporation, as long as they are genuine."

At least in the context of shareholder oppression cases, the business judgment rule does not insulate the corporation or the controlling shareholder from oppression claims related to the firing of a founding shareholder. The alleged oppressive acts must be looked at in context and while the business judgment of management may be a factor, it does not appear to be determinative.

One court said that whether the minority shareholder was discharged "for cause or in [the majority's] good business judgment is irrelevant" because the minority shareholder's reasonable expectations had been damaged. *Topper v. Park Sheraton Pharmacy, Inc.*, 107 Misc 2d 25, 28, 433 NYS2d 359 (1980); *see also O'Donnel v. Marine Repair Servs*, 530 F Supp 1199, 1205-08 (SDNY 1982) (rejecting the defendants' asserted business justification for terminating the minority

shareholder as a pretext).

In an article on the enactment of ORS 60.952, Professor Art wrote:

> The controlling shareholders [of close corporations] inherently agree to forego, to some extent, the managerial discretion typical in non-close corporations. The business judgment rule, or other deference given to decisions of those in control, is not warranted in this situation.
>
> Removing an employee-shareholder in a close corporation from a position of influence and employment, in this view, is not accurately viewed as a managerial decision within the ordinary discretion of those in control. Instead, it is a breach of the basic bargain among the business' owners, depriving the minority shareholder of all present return on investment. Moreover, because the terminated employee-shareholder has no realistic opportunity to sell the shares at a fair value to anyone else, the owner is deprived of the investment principal. No recourse is available except for the judicial action for oppression.
>
> Under this perspective, importantly, oppression can be found even though the conduct that frustrates the minority's expectations does not entail a breach of fiduciary duty by the controlling shareholder. Conduct can be oppressive even though it does not include typical "squeeze-out" techniques, such as absence of dividends or payment of excessive salaries to the controlling shareholders. An assertion by those in control that the challenged conduct enhances corporate profitability can be rejected on the grounds that economic benefits to the business owners, rather than profitability of the business entity, was the basis of the bargain among the owners. An assertion that conduct such as terminating employment is legal, in the sense that directors are empowered by the statutes and articles of incorporation or other documents to take such action, is similarly flawed under this perspective. If those in control exercise their power in a manner that breaches the reasonable expectations of the minority, they must in some other manner fulfill the expectations. Robert C. Art, *Shareholder Rights and Remedies in Close Corporations: Oppression, Fiduciary Duties, and Reasonable Expectations,* 28 J Corp L 371, 389-90 (2003).

See also Douglas K. Moll, *Shareholder Oppression in Texas Close Corporations: Majority Rule (Still) Isn't What It Used To Be,* 9 Hous Bus & Tax L J 33, 52 (2008) ("the fact that courts applying the oppression doctrine are subjecting the majority's actions to 'reasonable expectations' or 'burdensome, harsh and wrongful conduct' standards suggests that courts are requiring majority shareholders to do more than merely articulate a rational business purpose for their decisions.").

So in effect, courts more intensely scrutinize majority shareholder decisions in close corporations, giving less weight to the normal business judgment rule deference. As one court put it:

> When it is also considered that in close corporations dividend withholding may be used by controlling shareholders to force out minority shareholders, the traditional judicial restraint in interfering with corporate dividend policy cannot be justified. *Fox v. 7L Bar Ranch Co.*, 645 P2d 929, 935 (Mont 1982).

A discussion of the business judgement rule in the context of a close corporation appears in Peeples, *The Use and Misuse of the Business Judgment Rule in the Close Corporation*, 60 NOTRE DAME L REV 456 (1985).

F. Pecuniary interest.

In order to constitute a breach of fiduciary duty, a controlling shareholder must act with the purpose of advancing his/her pecuniary interest. *Locati v. Johnson,* 160 Or App 63, 72, 980 P2d 173 (1999); *Locati v. Johnson*, 204 Or App 683, 131 P3d 779 (2006). *See also Miller v. CC Meisel Co, Inc.,* 183 Or App 148, 167, 51 P3d 650 (2002).

But all such acts are not permitted.

> Nevertheless, majority shareholders "have certain rights to what has been termed `selfish ownership' in the corporation which should be balanced against the concept of their fiduciary obligation to the minority" permitting them "room to maneuver" and "a large measure of discretion" in, among other things, hiring and firing corporate employees. Therefore, where there is an allegation of a breach of fiduciary duty, the court must allow the controlling group to demonstrate a "legitimate business purpose for its action." The minority stockholder is then allowed to "demonstrate that the same legitimate objective could have been achieved through an alternative course less harmful to the minority's interest." (citations & footnote omitted). *Pointer v. Castellani,* 455 Mass. 537, 918 N.E.2d 805, 816 (2009).

NOTE: This author believes that breach of fiduciary duty takes more than simply causing the corporation to act in some manner that advances the pecuniary interest of the controlling shareholder – it is a good thing for all shareholders if the corporation does well – a rising tide raises all boats. Rather, a breach of fiduciary duty usually only occurs when the controlling shareholder causes the corporation to act in a manner which disproportionately favors the controlling shareholder's pecuniary interest.

G. Attorney liability.

Persons who assist shareholders in breaching their fiduciary duty to the other shareholders may also be liable for the breach. *Granewich, II v. Harding*, 329 Or 47, 945 P2d 1067 (1999). For public policy reasons, this rule generally does not apply to attorneys acting within the scope of an attorney-client relationship. *Reynolds v. Schrock,* 341 Or 338, 142 P3d 1062 (2006).

H. Preponderance of evidence standard applies.

In Oregon, a breach of fiduciary duty need be proved by a preponderance of the evidence, not by clear and convincing evidence. *Sealacota Trust v. Harrison,* 1998 US Dist LEXIS 21699 (D Or 1998).

Section 7.12 Duty of Non-controlling Shareholders

***A. General rule - no fiduciary duty*.**

Ordinarily, a minority shareholder owes no fiduciary duty to the corporation or to the other shareholders. *Priddy v. Edelman*, 883 F2d 438 (6th Cir 1989); *Gilbert v. El Paso Co.*, 490 A2d 1050 (Del Ch 1984).

B. Exception - 50% shareholder.

In a close corporation with two equal shareholders, neither shareholder is a "majority" shareholder. Yet, most courts have imposed a fiduciary duty on both 50% shareholders. *See Hollis v. Hill,* 232 F3d 460 (5th Cir 2000)(terminating employment and benefits of 50% shareholder); *Hagshenas v. Gaylord*, 199 Ill App 3d 60, 557 NE2d 316 (1990)(50% shareholder breached fiduciary duty by opening a competing business); *Bar H, Inc. v. Johnson*, 822 P2d 849 (Wyo 1991)(50% shareholder owes fiduciary duty, at least until squeezed-out by other shareholder); *McLaughlin v. Beeghly*, 84 Ohio App 3d 502, 617 NE2d 703 (1992); *Zimmerman v. Bogoff*, 402 Mass 650, 524 NE2d 849 (1988).

Oregon recognizes the fiduciary duty of 50% shareholders to each other. *Locati v. Johnson,* 160 Or App 63, 980 P2d 173 (1999); *Lee v. Mitchell*, 152 Or App 159, 175, 953 P2d 414 (1998).

> Whether we consider the corporation as organized to carry out the purposes of a continuing joint venture, or simply regard the parties as equal owners of a close corporation, their relationship was such that each was entitled to the other's performance of fiduciary duties of loyalty, good faith, and full disclosure. (footnote omitted) *Delaney v. Georgia-Pacific Corp.*, 278 Or 305, 311, 564 P2d 277, 281 (1977), *supplemented*, 279 Or 653, 569 P2d 604 (1977), *appeal after remand*, 42 Or App 439, 601 P2d 475 (1979).

The fiduciary duty owed by one 50% shareholder to the other 50% shareholder terminates once either shareholders ceases to be a shareholder. *Gangnes v. Lang*, 104 Or App 135, 799 P2d 670 (1990).

It is an open question in Oregon whether this fiduciary duty terminates when one of the shareholders ceases to be involved with corporate operations, likely when the shareholder ceases to be an employee either voluntarily or involuntarily. Some courts hold this duty continues.

> Allowing a party who has suffered harm within a close corporation to seek retribution by disregarding its own duties has no basis in our laws and would undermine fundamental and long-standing fiduciary principles that are essential to corporate governance. We see no reason to take such a drastic step. "If shareholders take it upon themselves to retaliate any time they believe they have been frozen out, disputes in close corporations will only increase. Rather, if unable to resolve matters amicably, aggrieved parties should take their claims to court and seek judicial resolution. (citations omitted) *Selmark Assocs., Inc. v. Ehrlich,* 467 Mass 525, 5 NE3d 923, 944 (2014).

See also *Rexford Rand Corp. v. Ancel*, 58 F3d 1215, 1219 (7th Cir 1995).

Other courts have held that a minority shareholder of a close corporation can compete with the corporation – at least after the minority shareholder is no longer actively involved with the corporation or where the minority shareholder was oppressed. *Starsurgical Inc. v. Aperta, LLC.*, 40 F Supp3d 1069 (ED Wis 2014); *J Bar H, Inc. v. Johnson,* 822 P2d 849 (Wyo.1991). The equitable defense of unclean

hands may apply and allow such competition. *Id; Worthington v. Anderson,* 386 F3d 1314 (10th Cir 2004).

***C. Exception - minority shareholder with veto power*.**

Although courts frequently recite that shareholders in close corporations owe a fiduciary duty to each other, in the overwhelming majority of such cases, the issue before the court is whether a majority shareholder acted improperly. Usually, the minority shareholder's conduct is not at issue since an objecting minority shareholder, by definition, is the loser on a vote requiring affirmation of a bare majority. "In the literature of close corporations, the minority shareholder invariably appears in the role of victim of majority oppression." Hetherington, *The Minority's Duty of Loyalty in Close Corporations*, 1972 DUKE L J 921, 933 (1972).

But this is not always true. A minority shareholder may be in a control position when by statute, contract or a provision in the articles or bylaws, either the consent of the minority shareholder or a supermajority vote is required for approval of an action. "The purpose of unanimity and greater-than-majority voting requirements is to protect the minority against the majority." Hetherington, *The Minority's Duty of Loyalty in Close Corporations*, 1972 DUKE L J 921, 935 (1972). In such cases, a majority shareholder with control should be held to the same standards as is the majority.

> Efforts to obtain a disproportionate share of the value of a corporate enterprise should be accorded the same treatment whether the attempts are made by the majority or the minority. Conduct by any shareholder which is intended to be detrimental to the welfare of the enterprise or to subordinate its business interests to competing business interests of the shareholder is a breach of a duty of loyalty which all shareholders owe to the common venture. As far as minority interests are concerned, this proposition merely amounts to saying that were the minority's conduct makes a difference, it ought to be equally accountable for its behavior and motives as the majority. Hetherington, *The Minority's Duty of Loyalty in Close Corporations*, 1972 DUKE L J 921, 945 (1972).

The Delaware courts have stated:

> Generally, a shareholder who owns less than 50% of a corporation's outstanding stock does not, without more, become a controlling shareholder of that corporation, with a concomitant fiduciary status. For controlling stock ownership to exist in the absence of a numerical majority there must be domination by a minority shareholder through actual exercise of direction over corporate conduct. *Gilbert v. El Paso Co.*, 490 A.2d 1050, 1155 (Del Ch 1984)(citations omitted).

Although Oregon has never addressed this issue directly, the trend nationally has been to hold that a minority shareholder with a veto power has a fiduciary duty to the corporation with respect to the exercise of that veto power.

NOTE: Most, but not all, cases holding close corporation minority shareholders with veto power owe a fiduciary duty to the majority come out of Massachusetts, Illinois and the Seventh Circuit.

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The leading case is *Smith v. Atlantic Properties, Inc.*, 12 Mass App 201, 422 NE 2d 798 (1981), which involved four shareholders each owning 25% of the corporation's stock. The articles and the bylaws provided that all corporate actions must be approved by an 80% vote of the shareholders, a provision which "had the effect of giving any one of the four original shareholders a **veto** in corporate decisions." *Id.* at 799.

The business was profitable and three of the shareholders wanted to declare dividends, fearing that failure to due so would result in imposition of a federal tax penalty for an unreasonable accumulation of corporate profits. For several years, one shareholder vetoed dividends and the IRS repeatedly imposed a penalty. The majority sued the 25% shareholder, asserting that he had breached his fiduciary duty to the majority. The court agreed.

> The 80% provision may have substantially the effect of reversing the usual roles of the majority and the minority shareholders. The minority, under that provision, becomes an ad hoc controlling interest. *Smith v. Atlantic Properties, Inc.*, 12 Mass App 201, 422 NE 2d 798, 802 (1981).

Under *Smith*, a "minority shareholder whose conduct is controlling on a particular issue" is bound by the same fiduciary standard as is the majority. *Id*. at 803, n 9.

In *Rexford Rand Corp. v. Ancel*, 58 F3d 1215, 1219 (7th Cir 1995), a minority shareholder was fired as an employee of the corporation. Two years later, the minority shareholder discovered that the corporation had inadvertently neglected to file its annual report and had been involuntarily dissolved. He then reserved the corporate name for his own benefit, making the name unavailable to the corporation when it sought re-instatement. The corporation sued, claiming the minority shareholder had violated his fiduciary duty. In finding for the corporation, the court said:

> In addition, minority shareholders owe a duty of loyalty to a close corporation in certain circumstance. Minority shareholders have an obligation as *de facto* partners in the joint venture not to do damage to the corporate interests. If a minority shareholders [sic] harms the corporation through "unscrupulous and improper `sharp dealings'" with the majority, he has breached his duty of loyalty. 10.
>
> Footnote 10. In addition, a minority shareholder owes a fiduciary duty to the corporation when his interests are controlling on a particular issue. (citations omitted) *Rexford Rand Corp. v. Ancel*, 58 F3d 1215, 1219 (7th Cir 1995).

See also Selmark Assocs., Inc. v. Ehrlich, 467 Mass 525, 5 NE3d 923, 944 (2014); *A. W. Chesterton Co., Inc. v. Chesterton*, 907 F Supp 19 (D Mass 1995), *affirmed*, 128 F3d 1 (1997); *Matteson v. Ziebarth*, 40 Wash 2d 286, 242 P2d 1025 (1952); *Helms v. Duckworth*, 249 F2d 482 (DC Cir 1957).

Other courts have held that a minority shareholder of a close corporation can compete with the corporation – at least after the minority shareholder is no longer actively involved with the corporation or where the minority shareholder was oppressed. *Starsurgical Inc. v. Aperta, LLC.*, 40 F Supp3d 1069 (ED Wis 2014); *J Bar H, Inc. v. Johnson,* 822 P2d 849 (Wyo.1991). The equitable defense of unclean hands may apply and allow such competition. *Id; Worthington v. Anderson,* 386 F3d 1314 (10th Cir 2004).

Section 7.13 Power of Court to Protect Minority Shareholders

Courts have the equitable power to set aside acts of majority shareholders when necessary to protect minority shareholders. *Browning v. C & C Plywood Corp.*, 248 Or 574, 434 P2d 339 (1968); *Stanely v. Luse*, 36 Or 25, 58 P 75 (1899); *Henry George & Sons, Inc. v. Cooper-George, Inc.*, 95 Wash 2d 944, 948, 632 P2d 512, 514 (1981); *Nelkin v. H.J.R. Realty Corp.*, 25 NY2d 543, 307 NYS2d 454, 255 NE2d 713 (1969). "While [Maryland corporation statute] only mentions dissolution as a remedy for oppressive conduct, we join other courts today 'which have interpreted their similar statutory counterparts to allow alternative equitable remedies not specifically stated in the statute.'" *Edenbaum v. Schwarcz-Osztreicherne,* 165 Md App 233, 885 A2d 365, 380 (2005).

Yet historically, courts have been reluctant to substitute the court's judgment – in effect, the minority shareholders' judgment – for the business judgment of the majority.

> In the absence of a fraudulent or coercive design or purpose on the part of the management neither the judgment of the court nor that of a minority stockholder can properly be substituted for the judgment of the majority of the directors and stockholders of a corporation. *Horner v. Pleasant Creek Mining Corporation*, 165 Or 683, 699, 107 P2d 989, 995, 109 P2d 1044 (1941).

Another court has put it more bluntly:

> No principle of law is more firmly fixed in our jurisprudence than the one which declares that the courts will not interfere in matters involving merely the judgment of the majority in exercising control over corporate affairs. *Regenstein v. J. Regenstein Co.*, 213 Ga 157, 159 97 SE2d 693, 695 (1957).

More recently, the Washington Supreme Court has said:.

> At common law, many courts refused to intervene in shareholder disputes since the State licensed the corporation, and as such the State and not the courts had the authority to dissolve the corporation. In a few jurisdictions, courts of equity began to carve out areas in which they would use the powers of the chancellors to liquidate the assets and business of the corporation. A few courts asserted the power to liquidate on a showing of irreparable injury to the shareholders and the corporation due to gross or fraudulent mismanagement. *Henry George & Sons, Inc. v. Cooper-George, Inc.*, 95 Wash 2d 944, 948, 632 P2d 512, 514 (1981).

Usually, either bad faith or fraud is required to be present in order for a

court to intervene.

***A. Statutory authority to dissolve corporation*.**

ORS 60.661(2) has long permitted a shareholder to seek judicial dissolution of a corporation when the majority's conduct is "illegal, oppressive or fraudulent" or when there is a voting deadlock. Specifically, shareholder may seek court intervention if:

> (a) The directors are deadlocked in the management of the corporate affairs, the shareholders are unable to break the deadlock and irreparable injury to the corporation is threatened or being suffered, or the business and affairs of the corporation can no longer be conducted to the advantage of the shareholders generally, because of the deadlock;
>
> (b) The directors or those in control of the corporation have acted, are acting or will act in a manner that is illegal, oppressive or fraudulent;
>
> (c) The shareholders are deadlocked in voting power and have failed, for a period that includes at least two consecutive annual meeting dates, to elect successors to directors whose terms have expired; or
>
> (d) The corporate assets are being misapplied or wasted.

Although the only remedy mentioned in this statue is dissolution, courts have usually fashioned other remedies for oppressive conduct – relying on their traditional equitable power to protect minority owners. *Browning v. C & C Plywood Corp*, 248 Or 574, 434 P2d 339 (1968); *Baker v. Commercial Body Builders, Inc.*, 264 Or 614, 507 P2d 387 (1973); *Delaney v. Georgia-Pacific Corp.*, 278 Or 305, 564 P2d 277, *supplemented*, 279 Or 653, 569 P2d 604 (1977), *appeal after remand*, 42 Or App 439, 601 P2d 475 (1979).

"While [Maryland corporation statute] only mentions dissolution as a remedy for oppressive conduct, we join other courts today 'which have interpreted their similar statutory counterparts to allow alternative equitable remedies not specifically stated in the statute.'" *Edenbaum v. Schwarcz-Osztreicherne,* 165 Md App 233, 885 A2d 365, 380 (2005).

Even though not mentioned as a remedy under ORS 60.661, a common remedy in oppression cases is an order for the controlling shareholders to purchase the shares of the oppressed minority.

> Under ORS 60.661, the trial court had the authority to choose a remedy for defendants' actions; we agree with it that requiring defendants to purchase plaintiff's shares is the preferable option. A purchase will disentangle the parties' affairs while keeping the corporation a going concern; dissolution would not benefit anyone, and plaintiff did not seek it at trial. *Cooke v. Fresh Express Foods Corp.*, 169 Or App 101, 114, 7 P3d 717 (2000).

See also Tifft v. Stevens, 162 Or App 62, 78, 987 P2d 1 (1999).

> In considering appropriate relief, judicial practice avoided penalizing controlling shareholders' ownership interests in a manner that significantly departed from what

> was required to relieve minority shareholders from the oppressive conduct, and also avoided increasing any value or benefit from a minority shareholders' interest beyond what minority shareholders could reasonably expect or the fair value of the shares. (emphasis added) *Hickey v. Hickey,* 269 Or App 258, 274-75, 344 P3d 512 (2015).

ORS 60.661 applies to all corporations – close corporations, publicly-held corporations, and everything in-between. That said, all of the cases in Oregon on judicial dissolution – and maybe all cases elsewhere as well – involve close corporations.

In 2001, ORS 60.952 took effect. The new statute applies only to close corporations. It mirrors ORS 60.661(2) in the triggering events (oppression, voting deadlock, corporate waste), but sets out a long, but non-exclusive, list of possible remedies that a court might apply – remedies previously applied by the courts. The new statute also gives the corporation the right to buy-out the complaining shareholder but gives the court the ability to set the price.

It is likely the case law interpreting the older ORS 60.661 will apply to the new statute as well.

A more in-depth discussion of these statutes and the case law interpreting them is contained in Section 8.04 of this book.

***B. Courts reluctant to intervene*.**

ORS 60.661 confers authority on the circuit courts to dissolve a corporation in certain proceedings initiated by a shareholder. This power is discretionary. Historically, courts have been disinclined to intervene and dissolve a corporation, even in cases involving deadlock or oppressive conduct.

For instance, after a lengthy discussion of the evolution of this power, the Oregon Supreme Court stated:

> The shareholder deadlock provisions of the Illinois Business Corporation Act, of the Model Business Corporation Act, and of the Oregon Business Corporation Law are clearly couched in language of permission. It is incredible that the many able lawyers who worked from time to time on these three identical acts would have used such phraseology to express a mandate. The statute contemplates that the court of equity shall take jurisdiction once a requisite showing of fact is made and contemplates further that having taken jurisdiction it will bring its discretion to bear in granting or refusing to grant equitable relief. The very fact that the legislature has made the remedy of liquidation a matter of discretion for the courts is a mandate to us to use discretion, and we would not be carrying out the legislative will by simply decreeing liquidations as a matter of course once the jurisdictional facts and nothing more are proven. The common law rule was thought to be an insufficient safeguard of the rights of the half-owner of a corporation who happened to be out of power. As we read the statute its intent is to obligate the courts to thread their way from case to case without the assistance of sweeping generalizations. *Jackson V. Nicolai-Neppach Co.*, 219 Or 560, 574-5, 348 P2d 9, 16 (1959).

See also McMunn v. ML&H Lumber, Inc., 247 Or 319, 429 P2d 798 (1967); *Henry George & Sons, Inc. v. Cooper-George, Inc.*, 95 Wash 2d 944, 632 P2d

512, 514 (1981). The *Jackson* case is discussed in a casenote in 39 OR L REV 382 (1960).

In *Baker v. Commercial Body Builders, Inc.*, 264 Or 614, 507 P2d 387 (1973), the court noted that the power granted by the judicial dissolution statute was a discretionary power and pointed out that this statutory power did not limit the court's more general equitable power to protect the minority by fashioning remedies other than dissolution.

This author has been unable to find any Oregon appellate decision where judicial dissolution has been ordered.

> **NOTE:** Despite language in many earlier cases that indicates that courts are reluctant to intervene in internal corporate disputes, there has been an increasing tendency for the Oregon Court of Appeals to intervene and fashion some remedy to protect minority shareholders. *See Hayes v. Olmsted & Associates, Inc.*, 173 Or App 259, 265, 21 P3d 178 (2001); *Cooke v. Fresh Express Foods Corp.*, 169 Or App 101, 108, 7 P3d 717 (2000); *Tifft v. Stevens,* 162 Or App 62, 78, 987 P2d 1 (1999). That remedy chosen is often the forced buy-out of the minority's shares. *Hickey v. Hickey,* 269 Or App 258, 344 P3d 512 (2015).

***C. Courts retain equitable powers*.**

In addition to the rights granted by ORS 60.661 and 60.952, courts retain the equitable power to dissolve or regulate the affairs of a corporation. *Baker v. Commercial Body Builders, Inc.*, 264 Or 614, 507 P2d 387 (1973). Oregon courts are more inclined to exercise their equitable powers to fashion remedies other than dissolution. *See for example Delaney v. Georgia-Pacific Corp.*, 278 Or 305, 564 P2d 277, *supplemented*, 279 Or 653, 569 P2d 604 (1977), *appeal after remand*, 42 Or App 439, 601 P2d 475 (1979); *Baker v. Commercial Body Builders, Inc.*, 264 Or 614, 507 P2d 387 (1973); *Browning v. C & C Plywood Corp*, 248 Or 574, 434 P2d 339 (1968).

***D. Miscellaneous*.**

Oregon courts have the power to appoint a receiver to wind up a corporation's business and affairs. ORS 60.667.

The topic of judicial dissolution is also discussed in Section 12.06 of this book.

A more detailed discussion of the rights and remedies available to minority shareholders in close corporations is contained in O'NEAL & THOMPSON, O'NEAL'S CLOSE CORP (3rd Ed); O'NEAL & THOMPSON, O'NEAL'S OPPRESSION OF MINORITY SHAREHOLDERS (2nd Ed).