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REASONABLE EXPECTATIONS V. IMPLIED-IN-FACT CONTRACTS: IS THE SHAREHOLDER OPPRESSION DOCTRINE NEEDED?

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Abstract: Courts and commentators have compared oppression law's reasonable expectations inquiry to an implied-in-fact contract analysis. This Article reveals that oppression law and contract law are actually more dissimilar in operation than they might appear. Although contract law has the tools to protect the close corporation shareholder, this Article illustrates how well-entrenched doctrinal hurdles will likely prevent it from doing so. The Article then argues that because oppressive majority conduct nevertheless breaches an actual bargain struck between the shareholders, and because the oppressive majority's actions often result in a theft of the minority's investment, contract law should take action to enforce the "deal" and to protect the minority shareholder. Thus, the Article concludes that when the oppression doctrine safeguards reasonable expectations, oppression law is effectively stepping in for contract law and is accomplishing what contract law itself should be doing. By coming to this conclusion, this Article answers a fundamental question—is the shareholder oppression doctrine needed in light of the established principles of contract law? By picking up where contract law leaves off, the shareholder oppression doctrine serves a critical protective function that justifies its independent existence.

INTRODUCTION

The law of shareholder oppression protects the close corporation minority investor from the improper exercise of majority control.[1]

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[1] The terms "majority shareholder" and "minority shareholder" (or "majority" and "minority") are used in this Article "to distinguish those shareholders who possess the actual power to control the operations of the firm from those who do not." J.A.C. Hethering-

The law of contracts applies more generally, as it seeks to enforce agreements between parties regardless of a close corporation context. When a close corporation dispute is at issue, however, it is often difficult to tell where contract law leaves off and where oppression law begins. Consider the following decision:

In *Wilkes v. Springside Nursing Home, Inc.*, Stanley Wilkes, Leon Riche, Edward Quinn, and Hubert Pipkin founded a close corporation engaged in the operation of a nursing home.[2] Each of the four founders invested $1,000 initially and obtained a 25% ownership stake in the company. They all drew an equivalent salary and participated actively in the management of the business.[3] Years later, Quinn, Riche, and Lawrence Connor[4] unjustifiably removed Wilkes as an officer and director of the corporation.[5] In addition, even though the other shareholders continued to receive their pay, Wilkes' salary was terminated.[6]

As a result of these actions, Wilkes sued the corporation and the individual shareholders.[7] In finding for Wilkes, the court stated the following:

> At the time of incorporation it was understood by all of the parties that each would be a director of [the corporation] and [that] each would participate actively in the management and decision making involved in operating the corporation. It was, further, the understanding and intention of all the parties that, corporate resources permitting, each would receive money from the corporation in equal amounts as long as each assumed an active and ongoing responsibility

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ton & Michael P. Dooley, *Illiquidity and Exploitation: A Proposed Statutory Solution to the Remaining Close Corporation Problem*, 63 VA. L. REV. 1, 5 n.7 (1977). Such power is most often determined by the size of the shareholdings. *See id.*

[2] *See* 353 N.E.2d 657, 659–60 (Mass. 1976).

[3] *See id.*

[4] By this time, Pipkin had sold his shares in the corporation to Connor. *See id.* at 659 n.4.

[5] *See id.* at 661. The *Wilkes* court noted that "the majority stockholders ... have not shown a legitimate business purpose for severing Wilkes from the payroll of the corporation or for refusing to reelect him as a salaried officer and director." *Id.* at 663; *see id.* at 661 ("The severance of Wilkes from the payroll resulted not from misconduct or neglect of duties, but because of the personal desire of Quinn, Riche and Connor to prevent him from continuing to receive money from the corporation.").

[6] *See id.* at 661.

[7] *See Wilkes*, 353 N.E.2d at 658–59.

> for carrying a portion of the burdens necessary to operate the business.[8]

In addition, the court cited Wilkes' testimony that "all four men were guaranteed directorships," and it noted that "Riche's understanding of the parties' intentions was that . . . they all would be directors."[9] Finally, the court observed that Quinn's, Riche's, and Connor's actions were "in disregard of a long-standing policy of the stockholders that each would be a director of the corporation and that employment with the corporation would go hand in hand with stock ownership."[10]

By referencing the parties' mutual "understandings," "intentions," "guarantees," and "policies," the *Wilkes* opinion has the flavor of a breach of contract decision. After all, Wilkes' victory was premised, at least in part, on Quinn's, Riche's, and Connor's "disregard" of the policies and understandings that were shared between the investors. Such disregard, of course, seems closely related to a breach of an implied agreement between the parties. Moreover, the court awarded Wilkes damages for the amount of salary that he would have received if he had remained an officer and director of the company.[11] Such a remedy reflects a standard award of expectation damages that is prevalent in breach of contract actions.[12]

The *Wilkes* court grounded its decision, however, in oppression law rather than in contract law. Wilkes asserted that "he should recover damages because the defendants, as majority stockholders in [the corporation], breached their fiduciary duty to him as a minority stockholder by their action[s],"[13] and the court similarly concluded that "a judgment shall be entered declaring that Quinn, Riche and Connor breached their fiduciary duty to Wilkes as a minority stock-

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[8] *Id.* at 659–60 (footnote omitted).

[9] *Id.* at 660 n.7.

[10] *Id.* at 664.

[11] *See id.* at 664–65 ("Wilkes shall be allowed to recover . . . the salary he would have received had he remained an officer and director of [the corporation].").

[12] By awarding Wilkes the salary that he would have received as a continuing officer and director of the corporation, the court is attempting to place Wilkes in the position that he would have been in if Quinn, Riche, and Connor had not disregarded the policies and understandings of the shareholders. This is the purpose, of course, of an expectation damages award. *See infra* notes 239–245 and accompanying text.

[13] *Wilkes*, 353 N.E.2d at 659; *see infra* notes 47–49 and accompanying text (observing that some courts define oppression as a breach of an enhanced fiduciary duty).

holder in [the corporation]."[14] Thus, although the *Wilkes* court sounded contractual themes in its discussion, the decision is based on the separate corporate law doctrine of shareholder oppression. By using contractual themes as part of its shareholder oppression analysis, however, the *Wilkes* court clearly draws a connection between the oppression and contract doctrines.

This connection between oppression law and contract law is also revealed in the language of other oppression precedents. For example, a number of courts describe oppression as the "frustration of the reasonable expectations of the shareholders."[15] When courts attempt to define a "reasonable expectation" in the shareholder oppression context, the language used is nearly identical to the conventional description of an implied-in-fact contract. Indeed, in the shareholder oppression setting, a reasonable expectation has been defined as an expectation (1) that is "known to or assumed by the other shareholders and [is] concurred in by them"[16]; (2) that is "embodied in understandings, express or implied, among the participants"[17]; and (3) that is often derived "from the parties' actions and course of conduct."[18] Similarly, in a contractual setting, an implied-in-fact contract is generally described as a "true contract" that is "grounded in the parties' agreement and tacit understanding" and whose "existence and terms are inferred from the conduct of the parties."[19]

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[14] *Wilkes*, 353 N.E.2d at 664. It should be noted that Wilkes actually brought two claims—a shareholder oppression claim as well as a claim for "breach of the alleged partnership agreement." *Id.* at 659 ("Wilkes alleged that he, Quinn, Riche and . . . Pipkin . . . entered into a partnership agreement . . . which . . . was breached . . . when Wilkes's salary was terminated and he was voted out as an officer and director of the corporation."). The court granted relief to Wilkes on the shareholder oppression claim, but it upheld the lower court's dismissal of Wilkes's breach of partnership agreement claim. *See id.*

[15] 2 F. HODGE O'NEAL & ROBERT B. THOMPSON, O'NEAL'S CLOSE CORPORATIONS § 9.29, at 132 (3d ed. 1996) [hereinafter CLOSE CORPORATIONS]; *see infra* notes 54–57 and accompanying text.

[16] Meiselman v. Meiselman, 307 S.E.2d 551, 563 (N.C. 1983); *see infra* note 60 and accompanying text.

[17] *Meiselman*, 307 S.E.2d at 563; *see infra* note 61 and accompanying text.

[18] Douglas K. Moll, *Shareholder Oppression in Close Corporations: The Unanswered Question of Perspective*, 53 VAND. L. REV. 749, 811 (2000); *see infra* note 68 and accompanying text.

[19] Kennedy v. Forest, 930 P.2d 1026, 1029 (Idaho 1997); *see, e.g.*, Reali, Giampetro & Scott v. Soc'y Nat'l Bank, 729 N.E.2d 1259, 1263 (Ohio Ct. App. 1999) (stating that, in an implied contract, "the meeting of the minds must be established by demonstrating that the circumstances surrounding the parties' transaction make it reasonably certain that the contract exists as a matter of tacit understanding") (internal quotation omitted); Staley v. Taylor, 994 P.2d 1220, 1224 (Or. Ct. App. 2000) ("In an implied-in-fact contract, the parties' agreement is inferred, in whole or in part, from their conduct.").

As these descriptions reveal, both a reasonable expectation and an implied-in-fact contract are based on shared "understandings" between the participants—i.e., understandings that the participants have "concurred in" or reached "agreement" upon. In addition, both reasonable expectations and implied-in-fact contracts are derived from the "conduct" or "actions" of the participants themselves.

Presumably as a result of these similarities, some commentators have explicitly linked the reasonable expectations analysis of oppression law to the implied agreement analysis of contract law. Reasonable expectations have been described "as an implied multilateral contract among the shareholders,"[20] and the reasonable expectations inquiry has been referred to as an "implied contract analysis."[21] Similarly, just as contract law seeks to enforce the bargain of the parties, so too does oppression law "help insure that innocent shareholders will realize their bargained-for benefit."[22]

What has not been emphasized, however, is the implication of this comparison. After all, to the extent that the reasonable expectations analysis of oppression law is rooted in contractual concepts, one could fairly ask whether an independent oppression doctrine is needed at all. Instead of concluding that a close corporation shareholder is entitled to *corporate law* relief because of a frustrated reasonable expectation, a court seemingly could reach the same conclusion on the *contract law* ground that majority action has breached an im-

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[20] Ralph A. Peeples, *The Use and Misuse of the Business Judgment Rule in the Close Corporation*, 60 NOTRE DAME L. REV. 456, 501 (1985); *see infra* note 21 and accompanying text.

[21] Lawrence E. Mitchell, *The Death of Fiduciary Duty in Close Corporations*, 138 U. PA. L. REV. 1675, 1724 n.214 (1990); *see* Terry A. O'Neill, *Self-Interest and Concern for Others in the Owner-Managed Firm: A Suggested Approach to Dissolution and Fiduciary Obligation in Close Corporations*, 22 SETON HALL L. REV. 646, 694 (1992) (describing the reasonable expectations approach as a "contractarian" approach); Peeples, *supra* note 20, at 503 (comparing a reasonable expectations analysis to an "implied contract"); *id.* at 504 n.371 ("The analogy to an implied contract is a favorite one of the courts in this [oppression] area."); *see also* Steven C. Bahls, *Resolving Shareholder Dissension: Selection of the Appropriate Equitable Remedy*, 15 J. CORP. L. 285, 326 n.247 (1990) ("Courts should analyze a claimed change in expectation in the same way they analyze a claimed codification of a contract, looking for both assent by the parties and consideration or detrimental reliance."); *id.* at 326 n.248 (noting that "an analogy to the law modifying contracts is appropriate").

[22] Bahls, *supra* note 21, at 321; *see infra* note 305. Moreover, just as the purpose of the oppression doctrine is to protect the reasonable expectations of shareholders that invest in close corporations, *see infra* Part II(C), the purpose of contract law is to "attempt the realization of reasonable expectations that have been induced by the making of a promise." 1 ARTHUR LINTON CORBIN, CORBIN ON CONTRACTS § 1, at 2 (2d ed. 1963); *see id.* (noting that the attempt to realize reasonable expectations "is believed to be the main underlying purpose" of contract law); Bahls, *supra* note 21, at 322 (stating that "[c]ontract law protects the reasonable expectations of parties to contracts").

plied-in-fact contract between the shareholders.[23] Put differently, there is no need for the shareholder oppression doctrine if an investor's reasonable expectations can be enforced as a right stemming from contract law, rather than as a right stemming from the investor's status as a close corporation shareholder.

To the extent that a reasonable expectation and an implied-in-fact contract are similar, therefore, why were the well-accepted principles of contract law[24] not used directly to remedy the plight of the close corporation shareholder? Why did contract law defer to corporate law to establish protections for minority shareholders in close corporation settings? Given that contract law strives to enforce bargains struck between parties, should contract law have deferred in this manner?

By analyzing facets of the liability and damages components of both oppression law and contract law, this Article squarely address these significant questions.[25] Moreover, by examining how the shareholder oppression doctrine operates in practice to protect reasonable expectations, this Article cuts through the rhetoric of oppression precedents and demonstrates what is actually transpiring in the liabil-

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[23] Similarly, if a reasonable expectation were roughly equivalent to an implied-in-fact contract, the evidence used to establish a reasonable expectation would presumably suffice to establish an implied-in-fact contract. Instead of trying to prove a reasonable expectation of management, for example, the oppressed shareholder could offer the same evidence as proof of an implied-in-fact contract for management. *But see infra* Part III(B)(1) (discussing problems of indefiniteness when attempting to establish an implied contract).

[24] In general, contract law has been accepted by all jurisdictions for a considerable period of time. In contrast, the shareholder oppression doctrine has only recently developed, *see, e.g.*, Donahue v. Rodd Electrotype Co., 328 N.E.2d 505, 513–15 (Mass. 1975), and a mere handful of state supreme courts has adopted the doctrine. *See infra* note 56 and accompanying text. Compared to contract law, therefore, oppression law is far less developed, and unanswered questions abound. *See* Moll, *supra* note 18, at 754 (observing that courts and commentators have not adequately considered whether shareholder oppression should be viewed from a majority or minority perspective even though the choice of perspective can make an outcome-determinative difference). In attempting to protect close corporation shareholders, therefore, it seems easier and more efficient to find such protection in established contract law rather than in newly-developed oppression law.

[25] Some commentators have implied, with no discussion, that indefiniteness and remedy problems may prevent contract law from fully protecting the reasonable expectations of close corporation shareholders. *Cf.* Bahls, *supra* note 21, at 326 & n.248 (suggesting that changes in reasonable expectations might "not [be] sufficiently definite," and citing to the "definiteness requirement found in contract law"); Robert W. Hillman, *The Dissatisfied Participant in the Solvent Business Venture: A Consideration of the Relative Permanence of Partnerships and Close Corporations*, 67 MINN. L. REV. 1, 84 (1982) (noting that if oppressive majority conduct frustrates a minority's expectations and breaches an agreement between the parties, "it may be appropriate to grant relief under the [reasonable] expectations-based analysis *if the remedies for a breach of the agreement are inadequate*") (emphasis added).

ity inquiries of many oppression courts. In so doing, this Article also raises issues regarding whether the protective rationale of the oppression doctrine can apply to other contexts and relationships.

Ultimately, this Article reveals that oppression law and contract law are more dissimilar in operation than they might appear. Although contract law has the tools to protect the close corporation shareholder, well-entrenched doctrinal hurdles (e.g., indefiniteness, expectation damages) will likely prevent it from doing so. Nevertheless, because oppressive majority conduct breaches an actual bargain struck between the shareholders, and because the oppressive majority's actions often result in a theft of the minority's investment, contract law should take action to enforce the "deal" and to protect the minority shareholder. Thus, when the oppression doctrine safeguards reasonable expectations, oppression law is effectively stepping in for contract law and is accomplishing what contract law itself should be doing.

It is important to note that this Article focuses on whether contract law could protect the oppressed shareholder through implied contracts. In the rare case where the shareholders have entered into express contracts for protection, such explicit agreements should govern. Whether the oppression doctrine is obviated by a shareholder's *ability* to enter into express contracts, however, is a separate question that is beyond the scope of this Article.

Part I of this Article discusses the nature of the close corporation and describes the development of the corporate law doctrine of shareholder oppression. Part II examines the operation of the shareholder oppression doctrine by analyzing oppression courts' usage of pattern and conduct evidence, economic understandings, and buyout remedies to establish and protect reasonable expectations. Building on this analysis, Part III explores whether contract law could use similar tools to establish and protect reasonable expectations as implied-in-fact contracts. As mentioned, because of various doctrinal hurdles associated with existing contract law, this Part argues that contract law is presently unlikely to take the broader perspective that is necessary to mimic the protections of the oppression doctrine. Part IV contends that the shareholder oppression doctrine is justified—even though protected reasonable expectations may not rise to the level of an enforceable contract—because oppressive majority conduct breaches an actual investment bargain and creates opportunities for theft. Finally, Part V considers the possibilities of extending the shareholder oppression framework to other contexts and relationships where the protection of contract law is similarly lacking.

I. THE DOCTRINE OF SHAREHOLDER OPPRESSION

A. *The Nature of the Close Corporation*

A close corporation is a business organization typified by a small number of stockholders, the absence of a market for the corporation's stock, and substantial shareholder participation in the management of the corporation.[26] In the traditional public corporation, the shareholder is normally a detached investor who neither contributes labor to the corporation nor takes part in management responsibilities.[27] In contrast, within a close corporation, "a more intimate and intense relationship exists between capital and labor."[28] Close corporation shareholders "usually expect employment and a meaningful role in management, as well as a return on the money paid for [their] shares."[29] Moreover, close corporation investors are often linked by family or other personal relationships that result in a familiarity between the participants.[30]

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[26] *See, e.g.*, Donahue v. Rodd Electrotype Co., 328 N.E.2d 505, 511 (Mass. 1975); Daniel S. Kleinberger, *Why Not Good Faith? The Foibles of Fairness in the Law of Close Corporations*, 16 WM. MITCHELL L. REV. 1143, 1148 (1990) ("Close corporations have a limited number of shareholders, and most, if not all, of the shareholders are active in the corporation's day-to-day business.").

There is some variation in the definition of a close corporation. *See* WILLIAM L. CARY & MELVIN ARON EISENBERG, CASES AND MATERIALS ON CORPORATIONS 389 (7th ed. 1995) (unabridged) ("Exactly what constitutes a close corporation is often a matter of theoretical dispute. Some authorities emphasize the number of shareholders, some the lack of a market for the corporation's stock, and some the existence of formal restrictions on the transferability of the corporation's shares."); 1 CLOSE CORPORATIONS, *supra* note 15, § 1.02, at 4-7 (noting the following possible definitions of a "close corporation": a corporation with relatively few shareholders; a corporation whose shares are not generally traded in the securities markets; a corporation in which the participants consider themselves partners *inter se;* a corporation in which management and ownership are substantially identical; and any corporation which elects to place itself in a close corporation grouping). Nevertheless, the typical close corporation possesses most, if not all, of the attributes described in these various definitions.

[27] *See* 1 CLOSE CORPORATIONS, *supra* note 15, § 1.08, at 31-32.

[28] Robert B. Thompson, *The Shareholder's Cause of Action for Oppression*, 48 BUS. LAW. 699, 702 (1993).

[29] *Id.* (footnotes omitted); *see, e.g.*, Pedro v. Pedro, 463 N.W.2d 285, 289 (Minn. Ct. App. 1990) ("[T]he primary expectations of minority shareholders include an active voice in management of the corporation and input as an employee."); 2 CLOSE CORPORATIONS, *supra* note 15, § 7.02, at 4 ("Ownership and management frequently coalesce in closely held corporations, where not uncommonly all the principal shareholders devote full time to corporate affairs. Even where one or two shareholders may be inactive, the business is normally conducted by the others without aid from nonshareholder managers.").

[30] *See, e.g.*, Robert B. Thompson, *Corporate Dissolution and Shareholders' Reasonable Expectations*, 66 WASH. U. L.Q. 193, 196 (1988).

Conventional corporate law norms of majority rule and centralized control can lead to serious problems for the close corporation minority shareholder.[31] Traditionally, most corporate power is centralized in the hands of a board of directors.[32] In a close corporation, the board is ordinarily controlled "by the shareholder or shareholders holding a majority of the voting power."[33] Through this control of the board, the majority shareholder has the ability to take actions that are harmful to the minority shareholder's interests. Such actions are often referred to as "freeze-out" or "squeeze-out" techniques[34] that "oppress"[35] the close corporation minority shareholder. Common freeze-out techniques include the termination of a minority shareholder's employment, the refusal to declare dividends, the removal of a minority shareholder from a position of management, and the siphoning of corporate earnings through high compensation to the majority shareholder.[36] Quite often, these tactics are used in combination. For example, the close corporation investor typically looks to salary rather than dividends for a share of the business returns because the

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[31] *See* 1 F. HODGE O'NEAL & ROBERT B. THOMPSON, O'NEAL'S OPPRESSION OF MINORITY SHAREHOLDERS § 1:02, at 3–4 (2d ed. 1985) [hereinafter OPPRESSION] (characterizing majority rule and centralized management as the "traditional pattern of corporate management," and noting the dangers that this management pattern presents to close corporation minority shareholders); Thompson, *supra* note 28, at 702–03 ("In a closed setting, the corporate norms of centralized control and majority rule easily can become instruments of oppression.").

[32] *See* REVISED MODEL BUS. CORP. ACT § 8.01(b) (1993) [hereinafter RMBCA] ("All corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, its board of directors . . . ."); Kleinberger, *supra* note 26, at 1152 ("In traditional theory, ultimate authority resides with the board of directors . . . .").

[33] Kleinberger, *supra* note 26, at 1151–52; *see, e.g.*, 1 OPPRESSION, *supra* note 31, § 1:02, at 3 ("Indeed, in most closely held corporations, majority shareholders elect themselves and their relatives to all or most of the positions on the board.").

[34] *See* 1 OPPRESSION, *supra* note 31, § 1:01, at 3 n.2 ("The term 'freeze-out' is often used as a synonym for 'squeeze-out.'"). It has been noted that the term "squeeze-out" means "the use by some of the owners or participants in a business enterprise of strategic position, inside information, or powers of control, or the utilization of some legal device or technique, to eliminate from the enterprise one or more of its owners or participants." *Id.* at 1. Similarly, a "partial squeeze-out" is defined as "action which reduces the participation or powers of a group of participants in the enterprise, diminishes their claim on earnings or assets, or otherwise deprives them of business income or advantages to which they are entitled." *Id.* at 1–2. *See generally* 1 *id.* §§ 3:01–3:20, 4:01–4:08, 5:01–5:39 (discussing various squeeze-out techniques); 2 *id.* §§ 6:01–6:10 (same).

[35] *See infra* text accompanying notes 52–54 (describing judicial definitions of "oppression").

[36] *See* 1 OPPRESSION, *supra* note 31, §§ 3:04, 3:06, 3:07, at 13–20, 37–58; *see also Donahue*, 328 N.E.2d at 513 (noting some of the possible freeze-out techniques).

"[e]arnings of a close corporation often are distributed in major part in salaries, bonuses and retirement benefits."[37] When actual dividends are not paid, therefore, a minority shareholder who is discharged from employment and removed from the board of directors is effectively denied any return on his or her investment as well as any input into the management of the business.[38] Once the minority shareholder is faced with this "indefinite future with no return on the capital he or she contributed to the enterprise,"[39] the majority often proposes to purchase the shares of the minority shareholder at an unfairly low price.[40]

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[37] 1 CLOSE CORPORATIONS, *supra* note 15, § 1.08, at 32; *see* Kleinberger, *supra* note 26, at 1148 ("Payout is frequently in the form of salary rather than dividends.").

Reasonable salaries paid to employees of a close corporation can be deducted by the close corporation when calculating its taxable income "and will thereby reduce the amount of income tax that the company pays." Thompson, *supra* note 30, at 197 n.12 (citing I.R.C. § 162). The corporation, however, cannot deduct dividends paid to close corporation shareholders. As a consequence, corporate income paid as dividends is subject to double taxation—once as business income at the corporate level, and once as personal income at the shareholder level. *See id.* Because of the tax system's discouragement of dividends in favor of salaries, "most close corporations provide a return to participants in the form of salary or other employee-related benefits." Thompson, *supra* note 28, at 714 n.90; *see also* 1 OPPRESSION, *supra* note 31, § 1:03, at 4–5 ("[A] close corporation, in order to avoid so-called 'double taxation,' usually pays out most of its earnings in the form of salaries rather than as dividends.").

[38] *See, e.g.*, Balvik v. Sylvester, 411 N.W.2d 383, 388 (N.D. 1987) ("Balvik was ultimately fired as an employee of the corporation, thus destroying the primary mode of return on his investment. Any slim hope of gaining a return on his investment and remaining involved in the operations of the business was dashed when Sylvester removed Balvik as a director and officer of the corporation."); 1 CLOSE CORPORATIONS, *supra* note 15, § 1.15, at 89 ("An investor taking a minority investment position in a close corporation, expecting to receive a return on the investment in the form of a regular salary, would face the risk that, after a falling out among the participants, the directors would terminate the minority shareholder's employment and deprive that investor of any return on the investment in the corporation.").

[39] Thompson, *supra* note 28, at 703; *see* 1 CLOSE CORPORATIONS, *supra* note 15, § 1.16, at 96 ("If, for example, the minority shareholder is fired from the employment that was providing the return on the investment in the close corporation, the minority may face an indefinite period with no return on the investment."); Charles W. Murdock, *The Evolution of Effective Remedies for Minority Shareholders and its Impact Upon Valuation of Minority Shares*, 65 NOTRE DAME L. REV. 425, 447 (1990) ("[T]he primary vulnerability of a minority shareholder is the specter of being 'locked-in,' that is, having a perpetual investment in an entity without any expectation of ever receiving a return on that investment.").

[40] *See, e.g.*, *Donahue*, 328 N.E.2d at 515 ("Majority 'freeze-out' schemes which withhold dividends are designed to compel the minority to relinquish stock at inadequate prices. When the minority stockholder agrees to sell out at less than fair value, the majority has won.") (citations omitted); 2 CLOSE CORPORATIONS, *supra* note 15, § 8.13, at 68 (noting that "[a] squeeze-out usually does not offer fair payment to the 'squeezees' for the interests, rights or powers which they lose"); Thompson, *supra* note 28, at 703–04 (noting that

In a public corporation, the minority shareholder can escape these abuses of power by simply selling his or her shares on the market. By definition, however, there is no ready market for the stock of a close corporation.[41] Thus, when a close corporation shareholder is treated unfairly through termination or otherwise, the investor "cannot escape the unfairness simply by selling out at a fair price."[42]

B. *The Cause of Action for Oppression*

Over the years, state legislatures and courts have developed two significant avenues of relief for the "oppressed" close corporation shareholder. First, many state legislatures have amended their corporate dissolution statutes to include "oppression" by the controlling shareholder as a ground for involuntary dissolution of the corporation.[43] Moreover, when oppressive conduct has occurred, actual dissolution is not the only remedy at the court's disposal. Both state statutes and judicial precedents have authorized alternative remedies that are less drastic than dissolution.[44] As the alternative forms of relief

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in a classic freeze-out, "the majority first denies the minority shareholder any return and then proposes to buy the shares at a very low price").

[41] *See Donahue*, 328 N.E.2d at 514 ("In a large public corporation, the oppressed or dissident minority stockholder could sell his stock in order to extricate some of his invested capital. By definition, this market is not available for shares in the close corporation."); Brenner v. Berkowitz, 634 A.2d 1019, 1027 (N.J. 1993) ("[U]nlike shareholders in larger corporations, minority shareholders in a close corporation cannot readily sell their shares when they become dissatisfied with the management of the corporation."); 2 CLOSE CORPORATIONS, *supra* note 15, § 9.02, at 4 ("[A] shareholder in a close corporation does not have the exit option available to a shareholder in a publicly held corporation, who can sell his shares in a securities market if he is dissatisfied with the way the corporation is being operated."); Thompson, *supra* note 28, at 703 ("[T]he economic reality of no public market deprives investors in close corporations of the same liquidity and ability to adapt available to investors in public corporations."); *see also* FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 230–31 (1991) (noting that "the lack of an active market in shares" prohibits close corporation shareholders from creating "homemade dividends" by selling stock).

[42] Kleinberger, *supra* note 26, at 1149.

[43] *See* Thompson, *supra* note 28, at 708. *See generally* Murdock, *supra* note 39, at 452–61 (describing the development of oppression as a ground for dissolution).

[44] *See, e.g.*, MINN. STAT. ANN. § 302A.751 subd. 1 (West Supp. 2000) (authorizing any equitable relief and specifically authorizing a buyout of the shareholder's interest); N.J. STAT. ANN. § 14A:12-7 (West Supp. 1999) (providing a nonexclusive list of possible relief that includes the order of a buyout and the appointment of a provisional director or custodian); *Brenner*, 634 A.2d at 1033 ("Importantly, courts are not limited to the statutory remedies [for oppression], but have a wide array of equitable remedies available to them."); *Balvik*, 411 N.W.2d at 388–89 (listing alternative forms of relief for oppressive conduct such as appointing a receiver, granting a buyout, and ordering the declaration of a dividend); Masinter v. Webco Co., 262 S.E.2d 433, 441 & n.12 (W. Va. 1980) (listing ten

have broadened over the years, orders of actual dissolution have become less frequent.[45] Thus, "oppression" has evolved from a statutory ground for involuntary dissolution to a statutory ground for a wide variety of relief.[46]

Second, particularly in states without an oppression-triggered dissolution statute, some courts have imposed an enhanced fiduciary duty between close corporation shareholders and have allowed an oppressed shareholder to bring a direct cause of action for breach of this duty.[47] In the seminal decision of *Donahue v. Rodd Electrotype Co.*, the Massachusetts Supreme Judicial Court adopted such a standard:

> [W]e hold that stockholders in the close corporation owe one another substantially the same fiduciary duty in the operation of the enterprise that partners owe to one another. In our previous decisions, we have defined the standard of duty owed by partners to one another as the "utmost good faith and loyalty." Stockholders in close corporations must discharge their management and stockholder responsibilities in conformity with this strict good faith standard. They may not act out of avarice, expediency or self-interest in derogation of their duty of loyalty to the other stockholders and to the corporation.[48]

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possible forms of relief for oppressive conduct such as ordering the reduction of excessive salaries and issuing an injunction against further oppressive acts). *But see* Giannotti v. Hamway, 387 S.E.2d 725, 733 (Va. 1990) (stating that the dissolution remedy for oppression is "exclusive" and concluding that the trial court is not permitted "to fashion other . . . equitable remedies").

[45] *See* Thompson, *supra* note 28, at 708; *cf.* Harry J. Haynsworth, *The Effectiveness of Involuntary Dissolution as a Remedy for Close Corporation Dissension*, 35 CLEV. ST. L. REV. 25, 50 (1986) (finding that courts ordered remedies other than dissolution in the majority of 37 involuntary dissolution cases studied). *See generally* Murdock, *supra* note 39, at 461–64 (discussing the development of alternative remedies).

[46] *See* 2 CLOSE CORPORATIONS, *supra* note 15, § 9.29, at 132 ("The inclusion of 'oppression' and similar grounds as a basis for involuntary dissolution or alternative remedies has opened up a much broader avenue of relief for minority shareholders caught up in a close corporation wracked with dissension."); Thompson, *supra* note 28, at 708–09 ("[I]t makes more sense to view oppression not as a ground for dissolution, but as a remedy for shareholder dissension.").

[47] *See* Thompson, *supra* note 28, at 726; *see also id.* at 739 ("It should not be surprising that the direct cause of action is developed particularly in states without an oppression statute, and [it] provides a vehicle for relief for minority shareholders in a close corporation where the statutory norms reflect no consideration for the special needs of such enterprises."). *See generally* Murdock, *supra* note 39, at 433–40 (discussing the development of the shareholder fiduciary duty).

[48] *Donahue*, 328 N.E.2d at 515 (citations omitted) (footnotes omitted). The *Donahue* duty of "utmost good faith and loyalty," however, was later scaled back by the same court.

Following the lead of the *Donahue* court, several courts outside of Massachusetts have also imposed an enhanced fiduciary duty running from shareholder to shareholder in a close corporation.[49]

The development of the statutory cause of action and the enhanced fiduciary duty reflect "the same underlying concerns for the position of minority shareholders, particularly in close corporations after harmony no longer reigns."[50] Because of the similarities between the two remedial schemes, it has been suggested that "it makes sense to think of them as two manifestations of a minority shareholder's cause of action for oppression."[51] In the close corporation context, therefore, it is sensible to view the parallel development of the statutory cause of action and the enhanced fiduciary duty action as two sides of the same coin—i.e., the shareholder's cause of action for oppression.

C. *Analyzing Oppression Through "Reasonable Expectations"*

The development of a shareholder's cause of action for oppression requires courts to determine when "oppressive" conduct has occurred. In wrestling with this issue, the courts have developed three principal approaches to defining oppression. First, some courts define oppression as "burdensome, harsh and wrongful conduct . . . a visible departure from the standards of fair dealing and a violation of fair play on which every shareholder who entrusts his money to a corpora-

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Due to concerns that the "untempered application of the strict good faith standard enunciated in *Donahue* . . . will result in the imposition of limitations on legitimate action by the controlling group in a close corporation which will unduly hamper its effectiveness in managing the corporation in the best interests of all concerned," the Supreme Judicial Court of Massachusetts suggested a balancing test in *Wilkes v. Springside Nursing Home, Inc.*, 353 N.E.2d 657, 663 (Mass. 1976). If the controlling group can demonstrate a "legitimate business purpose" for its actions, no breach of fiduciary duty will be found unless the minority shareholder can demonstrate "that the same legitimate objective could have been achieved through an alternative course of action less harmful to the minority's interest." *Id.*

[49] *See, e.g.*, Guy v. Duff & Phelps, Inc., 672 F. Supp. 1086, 1090 (N.D. Ill. 1987); Orchard v. Covelli, 590 F. Supp. 1548, 1556–59 (W.D. Pa. 1984); W&W Equip. Co. v. Mink, 568 N.E.2d 564, 574 (Ind. Ct. App. 1991); Evans v. Blesi, 345 N.W.2d 775, 779 (Minn. Ct. App. 1984); Fought v. Morris, 543 So. 2d 167, 170–71 (Miss. 1989); Crosby v. Beam, 548 N.E.2d 217, 220 (Ohio 1989); Estate of Schroer v. Stamco Supply Inc., 482 N.E.2d 975, 981 (Ohio Ct. App. 1984).

[50] Thompson, *supra* note 28, at 739.

[51] *Id.* at 700. *See generally id.* at 738–45 (describing the "combined cause of action for oppression").

tion is entitled to rely."[52] Second, some courts link oppression to breach of an enhanced fiduciary duty owed from one close corporation shareholder to another.[53] Third, a number of courts tie oppression to the "frustration of the reasonable expectations of the shareholders."[54] Of these three approaches, the "reasonable expectations" standard garners the most approval, and courts have increasingly used it to determine whether oppressive conduct has taken place.[55] The highest courts in several states have adopted the reasonable expectations approach,[56] and commentators have generally been in favor of the reasonable expectations standard.[57]

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[52] Thompson, *supra* note 28, at 711–12 (alteration in original) (quoting Fix v. Fix Material Co., 538 S.W.2d 351, 358 (Mo. Ct. App. 1976)); *see, e.g.*, Skierka v. Skierka Bros., Inc., 629 P.2d 214, 221 (Mont. 1981); *see also* Haynsworth, *supra* note 45, at 36–39 (describing judicial definitions of oppression).

[53] *See, e.g.*, *supra* notes 47–49 and accompanying text.

[54] 2 Close Corporations, *supra* note 15, § 9.29, at 132; *see In re* Kemp & Beatley, Inc., 473 N.E.2d 1173, 1179 (N.Y. 1984) (equating oppression with conduct that "defeats the 'reasonable expectations' held by minority shareholders in committing their capital to the particular enterprise").

[55] *See, e.g.*, 2 Close Corporations, *supra* note 15, § 9.30, at 141 ("One of the most significant trends in the law of close corporations in recent years is the increasing willingness of courts to look to the reasonable expectations of shareholders to determine whether 'oppression' or similar grounds exist as a justification for involuntary dissolution or another remedy."); *see infra* notes 56–57 and accompanying text.

[56] *See, e.g.*, Stefano v. Coppock, 705 P.2d 443, 446 n.3 (Alaska 1985); Fox v. 7L Bar Ranch, 645 P.2d 929, 933–34 (Mont. 1982); *Brenner*, 634 A.2d at 1029; *In re Kemp*, 473 N.E.2d at 1179; *Meiselman*, 307 S.E.2d at 563–64; *Balvik*, 411 N.W.2d at 388; *Masinter*, 262 S.E.2d at 442. *But see* Kiriakides v. Atlas Food Sys. & Serv., Inc., 541 S.E.2d 257, 265–66 (S.C. 2001) ("We find [that] adoption of the 'reasonable expectations' standard is inconsistent with [the South Carolina oppression-triggered dissolution statute], which places an emphasis not upon the minority's expectations but, rather, on the actions of the majority."). A number of intermediate appellate courts in other states have adopted the reasonable expectations standard as well. *See, e.g.*, Maschmeier v. Southside Press, Ltd., 435 N.W.2d 377, 380 (Iowa Ct. App. 1988); McCauley v. Tom McCauley & Son, Inc., 724 P.2d 232, 237 (N.M. Ct. App. 1986); Davis v. Sheerin, 754 S.W.2d 375, 382 (Tex. App. 1988). In states without an oppression-triggered dissolution statute, the reasonable expectations standard has also been used to determine whether a breach of the enhanced fiduciary duty has occurred. *See, e.g.*, *Wilkes*, 353 N.E.2d at 662–63; Merola v. Exergen Corp., 648 N.E.2d 1301, 1305 (Mass. App. Ct. 1995). Finally, Minnesota and North Dakota have explicitly incorporated the reasonable expectations standard into their dissolution statutes. *See* Minn. Stat. Ann. § 302A.751(3)(a) (West 1992); N.D. Cent. Code § 10–19.1–115 (1985).

[57] *See* 2 Oppression, *supra* note 31, § 7:20, at 149 ("The reasonable expectations of the shareholders, as they exist at the inception of the enterprise, and as they develop thereafter through a course of dealing concurred in by all of them, is perhaps the most reliable guide to a just solution of a dispute among shareholders . . . ."); Haynsworth, *supra* note 45, at 31 ("The third definition of oppression, initially derived from English case law, and long advocated by Dean F. Hodge O'Neal as well as other leading close corporation experts, is conduct which frustrates the reasonable expectations of the investors."); Thompson, *supra* note 30, at 211 ("Recognition of the intimate, illiquid relationship within a close

The New York decision of *In re Kemp & Beatley, Inc.* has been particularly influential in giving some context to the reasonable expectations framework. In *Kemp*, the Court of Appeals stated that "oppressive actions . . . refer to conduct that substantially defeats the 'reasonable expectations' held by minority shareholders in committing their capital to the particular enterprise."[58] As the court continued:

> A court considering a petition alleging oppressive conduct must investigate what the majority shareholders knew, or should have known, to be the petitioner's expectations in entering the particular enterprise. Majority conduct should not be deemed oppressive simply because the petitioner's subjective hopes and desires in joining the venture are not fulfilled. Disappointment alone should not necessarily be equated with oppression.
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> Rather, oppression should be deemed to arise only when the majority conduct substantially defeats expectations that, objectively viewed, were both reasonable under the circumstances and were central to the petitioner's decision to join the venture.
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> A shareholder who reasonably expected that ownership in the corporation would entitle him or her to a job, a share of corporate earnings, a place in corporate management, or some other form of security, would be oppressed in a very real sense when others in the corporation seek to defeat those expectations and there exists no effective means of salvaging the investment.[59]

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corporation therefore provides the necessary foundation for judging whether relief should be granted and, if so, what relief is appropriate; the shareholders' reasonable expectations has become the standard which best facilitates that approach.").

[58] *In re Kemp*, 473 N.E.2d at 1179.

[59] *Id.*; *see also Meiselman*, 307 S.E.2d at 563 ("In order for plaintiff's expectations to be reasonable, they must be known to or assumed by the other shareholders and concurred in by them. Privately held expectations which are not made known to the other participants are not 'reasonable.' Only expectations embodied in understandings, express or implied, among the participants should be recognized by the court.").

The *Kemp* court's focus on the shareholder's expectations at the time he decided to join the venture has been criticized as unduly narrow. *See, e.g.*, 2 Close Corporations, *supra* note 15, § 9.30, at 143 (stating that the *Kemp* court's focus "on the petitioner's expectations at the time he decided to join the enterprise is too narrow and may reflect the par-

II. Protecting the Reasonable Expectation via Shareholder Oppression

In order to compare oppression law's protection of reasonable expectations with contract law's protection of reasonable expectations, a deeper understanding of the operation of the oppression doctrine is needed. This Article contends that the shareholder oppression doctrine establishes and protects reasonable expectations in the following manner: (1) by requiring evidence suggesting that the shareholders' course of conduct in the particular dispute fits a common pattern of behavior in close corporations; (2) by understanding the economic rationale that leads a typical close corporation shareholder to commit capital to a venture; and (3) by providing a buyout remedy that effectively removes the oppressed shareholder from the company. The first two factors, of course, are primarily relevant to a liability inquiry (i.e., determining whether a reasonable expectation has been established), while the third factor is primarily relevant to a damages inquiry (i.e., determining how a frustrated reasonable expectation should be remedied). Each of these factors will be discussed in turn. Before doing so, however, an additional observation should be made. One must understand that courts conducting a reasonable expectations inquiry do not explicitly reference (at least typically) the abovementioned pattern and economic factors in their liability inquiries. Instead, most published oppression decisions merely recite that reasonable expectations "must be known to or assumed by the other shareholders and concurred in by them,"[60] or that reasonable expectations are "embodied in understandings, express or implied, among the participants."[61] These decisions generally provide little or no dis-

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ticular facts of that case," and expressing a preference for a broader standard that looks "to the shareholders' reasonable expectations as they existed at the inception of the enterprise, and as they developed thereafter through a course of dealing").

[60] Meiselman v. Meiselman, 307 S.E.2d 551, 563 (N.C. 1983); *see also In re Kemp*, 473 N.E.2d at 1179 ("A court considering a petition alleging oppressive conduct must investigate what the majority shareholders knew, or should have known, to be the petitioner's expectations in entering the particular enterprise."); *id.* at 1179 (noting that unfulfilled "*subjective* hopes and desires in joining the venture" are insufficient to establish an oppression claim) (emphasis added); *Meiselman*, 307 S.E.2d at 563 ("Privately held expectations which are not made known to the other participants are not 'reasonable.'"); Bahls, *supra* note 21, at 322 n.229 ("[C]ourts have been careful to protect only those expectations of the minority known by and acquiesced to by the majority.").

[61] *Meiselman*, 307 S.E.2d at 563; *see also* Gimpel v. Bolstein, 477 N.Y.S.2d 1014, 1019 (Sup. Ct. 1984) ("[T]he 'reasonable expectations' test is indeed an examination into the spoken and unspoken understanding upon which the founders relied when entering into the venture."); Robblee v. Robblee, 841 P.2d 1289, 1293 (Wash. Ct. App. 1992) ("'Reason-

cussion of how these "understandings" are formed or how "knowledge" and "concurrence" are to be proven. Thus, the above-mentioned contention—that a court's liability inquiry into whether a reasonable expectation has been established involves pattern and economic factors—should be understood as an attempt to explain what is actually transpiring (or, at least, what appears to be transpiring) in the liability inquiries of oppression courts.

A. *The Pattern Determination*

Courts and commentators have observed that reasonable expectations are based on understandings shared by all of the stockholders at the outset of a venture.[62] When an aggrieved shareholder asserts that majority conduct has frustrated his or her reasonable expectation of employment or management, therefore, it has been suggested that a court should first satisfy itself that all of the investors shared a basic understanding of employment or management at the inception of the venture.[63] More precisely, "the aggrieved shareholder must offer *evidence* indicating that the stockholders shared a basic understanding at the venture's inception of an entitlement to certain specific benefits (e.g., employment, management participation) due to their commitments of capital to the business."[64] Thus, for a court to find oppression liability, the aggrieved shareholder should be required to offer evidence establishing the existence of a mutual understanding (i.e., a reasonable expectation) that was ultimately frustrated by the majority's actions.[65]

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able expectations' are those spoken and unspoken understandings on which the founders of a venture rely when commencing the venture."); Hillman, *supra* note 25, at 78 ("[O]nly expectations embodied in understandings, express or implied, among the participants should be recognized."); Thompson, *supra* note 30, at 224 (observing that a reasonable expectations standard is based "on the parties' understandings").

[62] *See supra* note 61 and accompanying text.

[63] *See, e.g.*, Moll, *supra* note 18, at 810.

[64] *Id.* at 810 (emphasis added). For example, a minority shareholder complaining that his or her termination from employment improperly frustrated his or her reasonable expectation of working for the company should offer evidence establishing that the majority and minority shareholders, at the inception of the business, mutually understood that a commitment of capital to the venture entitled an investor to company employment.

[65] *See* Exadaktilos v. Cinnaminson Realty Co., 400 A.2d 554, 561 (N.J. Super. Ct. Law Div. 1979) (noting that "[t]he expectations of the parties in the instant suit with regard to their participation in corporate affairs are not established by any agreement; they must be gleaned from the evidence presented"); *see also* Thompson, *supra* note 30, at 217 ("Courts permit expectations to be established outside of formal written agreements, but the minority shareholder retains the burden of proving the existence of the expectations.").

In practice, however, any evidentiary "requirement" is loosely applied. Although explicit evidence of mutual understandings between the shareholders will occasionally be present—particularly where written documents exist that spell out those understandings[66]—such explicit evidence is usually absent. Indeed, close corporations typically operate on a more informal basis.[67] As a consequence, generic information reflecting the parties' actions and course of conduct is often the only specific evidence of a reasonable expectation before the court.[68] When that evidence matches a pattern of behavior that occurs in the typical close corporation, courts appear to be satisfied that a reasonable expectation has been established.[69] Thus, from an evidentiary standpoint, the courts' reasonable expectation analyses seem to require two types of pattern-related evidence: (1) general evidence of a behavioral pattern that appears in typical close corporations; and (2) specific evidence that the shareholders' actual course of conduct in the company at issue fits within the pattern. These two evidentiary components of the "pattern determination" will be discussed below.

1. The Behavioral Pattern in Close Corporations

To ascertain the reasonable expectations of close corporation shareholders, one could gather empirical evidence by asking a large number of stockholders about the entitlements they expected to receive as a result of their investments in close corporations.[70] Short of

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[66] *See, e.g.*, *In re* Topper, 433 N.Y.S.2d 359, 366 (Sup. Ct. 1980) ("The Court may determine the understanding of the parties as to the role the complaining shareholder is expected to play from agreements and evidence submitted."); Hillman, *supra* note 25, at 78 ("The clearest type of expectation is one which is set forth in a shareholder's agreement signed by all of the parties."); *cf.* MINN. STAT. ANN. § 302A.751(3a) (West Supp. 2000) ("[A]ny written agreements, including employment agreements and buy-sell agreements, between or among shareholders or between or among one or more shareholders and the corporation are presumed to reflect the parties' reasonable expectations concerning matters dealt with in the agreements.").

[67] *See infra* note 215.

[68] *See, e.g.*, *In re Topper*, 433 N.Y.S.2d at 365 ("The parties' full understanding may not even be in writing but may have to be construed from their actions."); Thompson, *supra* note 30, at 217 ("Expectations . . . must be gleaned from the parties' actions as well as their written documents."); *infra* note 74 and accompanying text; *cf. Meiselman*, 307 S.E.2d at 563 ("The reasonable expectations of the shareholders, as they exist at the inception of the enterprise, *and as they develop thereafter through a course of dealing concurred in by all of them*, is perhaps the most reliable guide to a just solution of a dispute among shareholders, at least a dispute among shareholders in the typical close corporation.") (emphasis added).

[69] *See infra* Parts II(A)(1), II(A)(2).

[70] It should be noted that Professors O'Neal and Thompson state in the preface to their leading oppression treatise that "this work was prepared by a combination of field

this empirical approach, however, one could simply observe what many close corporation shareholders do in fact receive once they commit capital to a venture. Such observations would constitute at least circumstantial evidence of the reasonable expectations possessed by many close corporation shareholders.

In oppression disputes, this latter approach is mimicked to a great degree. A noticeable pattern of behavior is observed in many (if not most) close corporations—i.e., shareholders invest in the company (generally as founders at the inception of the venture); they quit their prior jobs and immediately begin working for the company and serving in a management role; and they remain in employment and management positions unless dissension arises between the majority and minority investors.[71] Such a pattern implies that typical close corporation shareholders invest with the expectation that their investments entitle them to employment and management participation with the company.[72] Significantly, oppression courts appear to recognize this pattern[73] and to accept the pattern's implication. After all,

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work and library investigation." 1 OPPRESSION, *supra* note 31, at vi (Supp. 1999). Thus, the information contained in this source is based, at least in part, on empirical evidence. The treatise goes on to state that close corporation investors "usually expect to be actively involved in the management and operation of the enterprise." 2 OPPRESSION, *supra* note 31, § 7:15, at 89.

[71] *See, e.g.*, Wilkes v. Springside Nursing Home, 353 N.E.2d 657, 658–61 (Mass. 1976); Pedro v. Pedro, 489 N.W.2d 798, 799–800 (Minn. Ct. App. 1992); *In re Topper*, 433 N.Y.S.2d at 361–62; Balvik v. Sylvester, 411 N.W.2d 383, 384–85, 388 (N.D. 1987); *see also* 2 CLOSE CORPORATIONS, *supra* note 15, § 7.02, at 4 ("Ownership and management frequently coalesce in closely held corporations, where not uncommonly all the principal shareholders devote full time to corporate affairs. Even where one or two shareholders may be inactive, the business is normally conducted by the others without aid from nonshareholder managers.").

[72] *See, e.g.*, *infra* notes 74–76 and accompanying text. It is important to note that typical close corporation shareholders do possess "general" reasonable expectations that stem solely from their status as stockholders rather than from any pattern of behavior. These "general" expectations are fully protected by the shareholder oppression doctrine. *See infra* note 137 and accompanying text.

[73] The highest court of West Virginia discussed the following two "factual patterns" of close corporation conduct that often result in oppression:

> The first is where the minority shareholder has made a parity of capital investment with the other shareholders with the expectation of full-time remunerative employment with the corporation, and this expectation has been realized. Characteristically, the minority shareholder has worked for the corporation over a period of time, only to find that through no fault of his own and not as a result of any legitimate business purpose, his services and all remuneration are terminated.
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> The second pattern is where the minority holder has originally been involved in the formation of the corporation, or induced to invest in it, with the

many courts use this course of conduct—investment, followed by company employment and management—to aid their conclusion that reasonable expectations of employment and management existed.[74] Moreover, judicial acceptance of the pattern's implication is revealed by the general assertions of numerous courts that close corporation shareholders possess reasonable expectations of employment and management participation.[75] The Minnesota decision of *Pedro v. Pedro*,

> expectation of some return on his investment. Further, he has received some return, either by salary or dividend, but finds that this return has been severed for no legitimate business purpose and not as a result of any dereliction on his part.

Masinter v. Webco Co., 262 S.E.2d 433, 441 (W. Va. 1980) (citations omitted); *see, e.g.*, Donahue v. Rodd Electrotype Co., 328 N.E.2d 505, 511 (Mass. 1975) ("We deem a close corporation to [be] typified by . . . (3) *substantial majority stockholder participation in the management, direction and operations of the corporation.*") (emphasis added); *id.* at 512 ("In essence, though, the enterprise remains one in which ownership is limited to the original parties . . . [and] in which ownership and management are in the same hands . . . ."); Kiriakides v. Atlas Food Sys. & Serv., Inc., 527 S.E.2d 371, 387 (S.C. Ct. App. 2000) (noting the "ubiquitous pattern of other cases in which a minority shareholder's employment is terminated from a company, salary and benefits cease, and the shareholder is deprived of participation in management"); *cf.* CARY & EISENBERG, *supra* note 26, at 539–40 ("One way in which a court determines that reasonable expectations have been defeated by majority shareholders is by asking itself what similarly situated shareholders would have probably expected."); O'Neill, *supra* note 21, at 659 ("[I]n drawing inferences about [shareholders'] expectations, the law will inevitably be guided by a particular vision of what motivates the reasonable shareholder.").

[74] *See, e.g.*, Gunzberg v. Art-Lloyd Metal Prods. Corp., 492 N.Y.S.2d 83, 85 (App. Div. 1985) ("As a result of their long history of taking an active part in the running of the corporation, petitioners demonstrated that they had a reasonable expectation that they would continue to be employed by the company, and have input into its management."); *Balvik*, 411 N.W.2d at 388 ("Balvik quit his former job to join Sylvester in the new business enterprise, making a relatively substantial investment in the process. It is apparent from the record that Balvik's involvement with [the business] constituted his primary, if not sole, source of livelihood and that he quite reasonably expected to be actively involved in the operations of the business."); *cf.* Muellenberg v. Bikon Corp., 669 A.2d 1382, 1388 (N.J. 1996) ("In this case, it is reasonable to conclude that Burg's fair expectations were that should he give up his prior employment with a competitor company and enter this small corporation, he would enjoy an important position in the management affairs of the corporation.").

[75] *See, e.g.*, *Wilkes*, 353 N.E.2d at 662–63 ("[B]y terminating a minority stockholder's employment or by severing him from a position as an officer or director, the majority effectively frustrate the minority stockholder's purposes in entering on the corporate venture and also deny him an equal return on his investment."); Ingle v. Glamore Motor Sales, Inc., 535 N.E.2d 1311, 1319 (N.Y. 1989) (Hancock, J., dissenting) ("A person who . . . buys a minority interest in a close corporation does so not only in the hope of enjoying an increase in value of his stake in the business but for the assurance of employment in the business in a managerial position."); *In re Topper*, 433 N.Y.S.2d at 365 ("Unlike their counterparts in large corporations, minority shareholders in small corporations often expect to participate in management and operations."); *Balvik*, 411 N.W.2d at 386 ("[I]t is generally

for example, stated rather absolutely that "the primary expectations of minority shareholders include an active voice in management of the corporation and input as an employee."[76] In short, the recurring pattern of behavior in close corporations is often treated as general evidence that contributes to whether a reasonable expectation will be found.

2. Specific Evidence of Fitting Within the Pattern

Even if a broader pattern in close corporations is recognized, specific evidence from the particular dispute before the court (i.e., specific evidence establishing a reasonable expectation) seems to be necessary as well.[77] As mentioned, however, the amount of evidence needed to satisfy this "requirement" is slight at best. For example, proof (via testimony or otherwise) that the minority shareholder was a company founder who served as an employee and a manager after his or her initial investment satisfies many courts that the shareholder's situation fits within the general pattern. Correspondingly, this proof satisfies many courts that reasonable expectations of employment and management have been established.[78] This "specific evidence," of

understood that, in addition to supplying capital and labor to a contemplated enterprise and expecting a fair return, parties comprising the ownership of a close corporation expect to be actively involved in its management and operation."); *see also* 1 OPPRESSION, *supra* note 31, § 1:03, at 4 ("Quite commonly when a participant invests in a close corporation he expects to work in the business on a full-time basis."); Thompson, *supra* note 28, at 702 (noting that close corporation shareholders "usually expect employment and a meaningful role in management, as well as a return on the money paid for [their] shares").

[76] 463 N.W.2d 285, 289 (Minn. Ct. App. 1990).

[77] This "specific evidence" requirement is sensible. Otherwise, in concluding that a reasonable expectation has been established, courts would be relying on the broader pattern and would be ignoring the fact-specific evidence that arises from the particular dispute before the court. *See supra* notes 63–65 and accompanying text (describing the need to offer evidence).

[78] *See, e.g.*, *Wilkes*, 353 N.E.2d at 664 (listing factors relevant to an oppression finding and including the following: "Wilkes was one of the four originators of the nursing home venture"; "Wilkes, like the others, had invested his capital and time for more than fifteen years with the expectation that he would continue to participate in corporate decisions"; and "[the majority's] action was in disregard of a long-standing policy of the stockholders that each would be a director of the corporation and that employment with the corporation would go hand in hand with stock ownership"); *supra* note 68 and accompanying text; *infra* note 79.

Even if a shareholder's actions fall within the general pattern (i.e., investment followed by employment and management), there may be other evidence contradicting the notion that reasonable expectations of employment and management have been established. For example, the language of an express shareholder's agreement may negate any inference of a mutual understanding that the investor was entitled to employment. *See, e.g.*,

course, is minimal, as it often reflects the undisputed facts of the case.[79]

In some oppression lawsuits, however, this proof cannot be adduced, and an aggrieved shareholder is unable to demonstrate that his or her dispute matches the broader pattern of close corporation behavior. In *Merola v. Exergen Corp.*, for example, the plaintiff minority shareholder was terminated from his employment with the company.[80] Merola sued, asserting that his termination constituted a

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In re Apple, 637 N.Y.S.2d 534, 535 (App. Div. 1996) (noting that a buyout agreement explicitly bound each shareholder to sell "after ceasing for any reason, either voluntarily or involuntarily, to be in the employ of the corporation," and stating that the terminated shareholder-employee "cannot be heard to argue that he had a reasonable expectation that he would be employed and would be a shareholder for life"); *Ingle*, 528 N.Y.S.2d at 603 ("The plaintiff was aware throughout his employment of the possibility that he could be discharged at the will of the defendants since he repeatedly signed agreements which provided for his discharge 'for any reason' and for the repurchase of his interest in the corporation at that time."). When an aggrieved stockholder challenges his or her denial of employment in these shareholder agreement situations, a court should not find that a basic understanding of employment has been established. Instead, despite the fact that the shareholder's actions fall within the general pattern, a court should conclude that the alleged frustrated expectation of employment is unreasonable and unenforceable. *See also* Douglas K. Moll, *Shareholder Oppression v. Employment at Will in the Close Corporation: The Investment Model Solution*, 1999 U. ILL. L. REV. 517, 559–61 (noting that not all close corporation shareholders reasonably expect that their investments entitle them to employment); *cf.* Woodard v. Southwest States, Inc., 384 S.W.2d 674, 674 (Tex. 1964) ("Where there exists a valid express contract covering the subject matter, there can be no implied contract.").

[79] *See, e.g.*, *In re Topper*, 433 N.Y.S.2d at 361–62. As the *Topper* court stated:

> The petitions and supporting affidavits in this case show conclusively, and respondents do not deny, that petitioner Topper associated himself with [the close corporations] in the expectation of being an active participant in the operation of both corporations. To that end, petitioner terminated an employer-employee relationship in the drug business of twenty-five (25) years duration ... and uprooted himself and transported his family from ... Florida to New York.... Petitioner put his life savings into the venture.... The controlling shareholders do not deny that petitioner's expectations, not expressed in any written agreement, formed a necessary component of the corporation's formation.

Id. (footnote omitted); *see also In re* Williamson, 687 N.Y.S.2d 53, 54 (App. Div. 1999) ("We agree ... that petitioner's allegations that he was involuntarily ousted from any involvement or ownership in respondent corporation, of which he was a founding one-third shareholder, by the other two one-third shareholders, not only stated a cause of action for involuntary dissolution based on oppressive action, but also warranted the granting of the application [for relief], given papers on respondent's motion to dismiss that effectively constituted an answer but which failed to raise any genuine issues of fact on the question of oppression."); *id.* ("We note that ... petitioner's employment was an incident of his stock ownership, cloaking him with a reasonable expectation of continued employment.").

[80] *See* 668 N.E.2d 351, 352–53 (Mass. 1996).

breach of fiduciary duty.[81] In rejecting Merola's claim, the court observed that Merola was not a founder of the company, and it noted that he had been working for the company as a part-time employee before ever investing in the business.[82] Moreover, the court commented that "[t]here was no general policy regarding stock ownership and employment, and there was no evidence that any other stockholders had expectations of continuing employment because they purchased stock."[83] Merola, simply put, was unable to adduce even the minimal amount of evidence that is required for a protected reasonable expectation. In other words, Merola was unable to prove that his particular dispute fit within the broader pattern of behavior in close corporations.[84] Without any other evidence to establish a reasonable expectation of employment, the court refused to credit Merola's claim.[85]

In summary, the liability inquiries of many oppression courts seem to turn in large part on general evidence of a behavioral pattern in close corporations as well as on specific evidence that the shareholders' actual course of conduct fits within the pattern. This "pattern determination," however, is only one facet of a court's inquiry into whether a reasonable expectation exists. The economics behind close corporation investments also plays a significant role.

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[81] *See id.* at 352.

[82] *See id.* at 354. Recall that the typical pattern of close corporation behavior involves shareholders who do not begin serving as employees and managers until *after* investing their capital in the company. *See supra* text accompanying note 71; *see also* 1 OPPRESSION, *supra* note 31, § 3:06, at 42 (Supp. 1998) (noting that the shareholder oppression doctrine is unlikely to be applied "when the employment relationship dominates the shareholder relationship, for example where the individual was an employee before becoming a shareholder . . . .").

[83] *Merola*, 668 N.E.2d at 354.

[84] *See supra* note 82 and accompanying text.

[85] *See Merola*, 668 N.E.2d. at 354–55. In terms of "other evidence" to establish a reasonable expectation, a stockholder may have entered into an express agreement that guarantees his or her employment or management for a particular period of time. *See, e.g.*, McQuade v. Stoneham, 189 N.E. 234, 235 (N.Y. 1934). In such situations, a reasonable expectation of employment or management would seem to exist even if the shareholder cannot demonstrate that his or her dispute matches the broader pattern of close corporation behavior. Alternatively, regardless of whether there is sufficient pattern-related evidence, some reasonable expectations (aside from employment and management) can be established merely by the investor's status as a "stockholder." *See infra* note 137 and accompanying text.

B. *The Economic Rationale for Close Corporation Investments*

Courts may be willing to find reasonable expectations based on a broader pattern and thin specific evidence because they understand the economics behind an investor's commitment of capital to a close corporation. In other words, courts seem to appreciate that a rational minority stockholder would not invest in a close corporation without reaching a shared understanding of continued employment and management participation with the majority stockholder. As a consequence, a court may be more willing to credit an alleged reasonable expectation of employment or management participation based merely on the aggrieved shareholder's status as an employee-manager since the company's founding.

1. The Employment Interest

For many close corporation investors, the desire for employment is the principal enticement motivating their decision to commit capital to a venture.[86] Compared to similar employment in other contexts, a close corporation job is frequently associated with a higher salary,[87]

[86] *See, e.g.*, *In re Kemp*, 473 N.E.2d at 1178 ("As a matter of fact, providing employment for himself may have been the principal reason why he participated in organizing the corporation.") (internal quotation omitted); 1 CLOSE CORPORATIONS, *supra* note 15, § 1.08, at 31-32 ("Providing for employment may have been the principal reason why the shareholder participated in organizing the corporation."); *see also Wilkes*,, 353 N.E.2d at 662 ("A guaranty of employment with the corporation may have been one of the basic reason(s) why a minority owner has invested capital in the firm.") (internal quotation omitted); *In re* Wiedy's Furniture Clearance Ctr. Co., 487 N.Y.S.2d 901, 903 (App. Div. 1985) ("Although the exact amount of the capital contribution is disputed, petitioner utilized his own funds in getting this new venture underway, not simply as an investment, but to provide employment and a future for himself."); Alyse J. Ferraro, *Ingle v. Glamore Motor Sales, Inc.: The Battle Between Ownership and Employment in the Close Corporation*, 8 HOFSTRA LAB. & EMP. L.J. 193, 215 (1990) ("As the majority emphasizes, Ingle was compensated for the sale of his shares, but to believe that the dollar amount received met his expectations would be to dismiss his purpose in acquiring those shares. Ingle had reasonably expected his employment to continue until he chose to retire or to acquire his own Ford dealership . . . ."); Murdock, *supra* note 39, at 468 ("That people often invest in a closely-held corporation to provide a job is almost self-evident . . . ."); *id.* ("[T]o deny a minority shareholder employment *when a job was part of his rationale in investing* is oppressive, as is the failure to pay dividends to nonemployee shareholders when employed shareholders are receiving *de facto* dividends through salaries.") (emphasis added) (footnote omitted); *id.* at 472 ("[W]hat is at stake in the 'oppression' cases is often a job—a very attractive job."); Robert A. Ragazzo, *Toward a Delaware Common Law of Closely Held Corporations*, 77 WASH. U. L.Q. 1099, 1110 (1999) (noting that a close corporation shareholder "often invests for the purpose of having a job").

[87] This assertion, of course, assumes a comparison between similar jobs in businesses at similar stages of development. *See* 1 OPPRESSION, *supra* note 31, § 3:07, at 57 n.5 (noting

a prestigious management position,[88] and intangible benefits stemming from working for oneself.[89] Relatedly, many close corporations are small start-up businesses that face a high risk of failure.[90] Because

that "the special prerogatives enjoyed by a majority in a close corporation not infrequently block the sale of a close corporation because the majority has difficulty obtaining such lucrative employment elsewhere" (citing J.C. Hetherington, *Special Characteristics, Problems, and Needs of the Close Corporation*, 1969 ILL. L.F. 1, 20 n.72)); SHANNON P. PRATT ET AL., VALUING A BUSINESS: THE ANALYSIS AND APPRAISAL OF CLOSELY HELD COMPANIES 121 (3d ed. 1996) ("It is not uncommon to find an owner/manager of a successful closely held company earning a greater amount in annual compensation than the amount an equivalent nonowner employee would earn as compensation."); Ragazzo, *supra* note 86, at 1109 ("The shareholder may invest for the purpose of having a job that produces higher compensation than could be garnered through employment by third parties."); *see also* Bonavita v. Corbo, 692 A.2d 119, 124 (N.J. Super. Ct. Ch. Div. 1996) ("[W]hile there is no claim that the [close corporation] salaries are excessive, neither was there a showing that if the 'inside' employment were terminated those family members could earn as much elsewhere."); Nelson v. Martin, 958 S.W.2d 643, 644 (Tenn. 1997) (noting that the annual compensation of a shareholder-employee of a commercial printing business "was in excess of $250,000").

[88] *See* 1 OPPRESSION, *supra* note 31, § 3:07, at 54 (referring to the "prestige, privileges, and patronage that come from controlling a corporation and occupying its principal offices"); *id.* § 3:06, at 38 ("[L]osing the prestige of a directorship may be of considerable consequence to the shareholder."); *see also Wilkes*, 353 N.E.2d at 659–60 & n.9 (observing that all of the close corporation participants were directors of the company and that the offices of president, treasurer, and clerk were held by each of the participants over the years); *Balvik*, 411 N.W.2d at 384 (noting that both participants in a close corporation were directors of the company and observing that one shareholder-employee served as the president while the other served as the vice-president).

[89] *See Ingle*, 535 N.E.2d at 1319 (Hancock, J., dissenting) (noting "the challenge, the independence, the prestige, the feeling of achievement, and the other intangible benefits of being part of the management of a successfully run small company"); Bahls, *supra* note 21, at 290–91 (noting that close corporation ownership includes "the social status and challenge of operating one's own company and the satisfaction of providing employment to one's children"); *id.* at 319 n.212 (mentioning the "loss of satisfaction and other qualitative perks associated with operating a business"); O'Neill, *supra* note 21, at 668, 671 (describing the "psychological payoffs" that an "owner-manager" anticipates as a result of investing in a venture, including "the pleasure of being one's own boss, the feeling of satisfaction in creating a viable enterprise and even the excitement of taking a substantial risk"); Ragazzo, *supra* note 86, at 1110 ("Additionally, the employee may simply derive satisfaction from working in a business that he himself takes a substantial part in managing.").

[90] *See, e.g.*, MICHAEL E. GERBER, THE E-MYTH REVISITED: WHY MOST SMALL BUSINESSES DON'T WORK AND WHAT TO DO ABOUT IT 2 (1995). As Gerber observes:

> Businesses start and fail in the United States at an increasingly staggering rate. Every year, over a million people in this country start a business of some sort. Statistics tell us that by the end of the first year at least 40 percent of them will be out of business. Within five years, more than 80 percent of them . . . will have failed . . . . [M]ore than 80 percent of the small businesses that survive the first five years fail in the second five.

Id.; *see also* 1 OPPRESSION, *supra* note 31, § 1:04, at 8 (describing close corporations as "small business enterprises"); U.S. SMALL BUS. ADMIN., THE ANNUAL REPORT ON SMALL

of the uncertainty surrounding whether the business will have any earnings at all, let alone earnings growth or consistency,[91] the close corporation shareholder's initial decision to invest is often based primarily on the definitive benefits of close corporation employment, rather than on the speculative possibilities of earnings growth.[92] The observations of one commentator capture both of these ideas:

> In a closely held corporation, a shareholder-employee has interests in his job and stock that are often economically intertwined. Holding stock in a closely held corporation, viewed purely as an investment decision, seems almost irrational from an economic perspective. Small businesses are exceedingly risky enterprises with high failure rates. To compensate fairly for this level of risk, the expected return would also have to be disproportionately large. Moreover, many investors in small businesses invest a significant portion of their life savings in the business. This practice defeats their ability to diversify their investment portfolios and exposes them to company- and industry-specific risk. As a result, investors in closely held corporations would seem well advised to trust their capital to diversified mutual funds rather than a small corporation.
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BUSINESS AND COMPETITION 29 (1997) ("Fewer than half of all new firms are in operation after five years."); U.S. SMALL BUS. ADMIN., OFFICE OF ADVOCACY, SMALL BUSINESS ANSWER CARD, *available at* http://www.sbaonline.sba.gov/advo/stats/ec_anscd.html (last modified Apr. 20, 1999) ("Business turnover is the domain of small business."); O'Neill, *supra* note 21, at 668 n.84 ("The risk of failure of the small business enterprise is notoriously high."); Ragazzo, *supra* note 86, at 19 ("Small businesses are exceedingly risky enterprises with high failure rates.").

[91] *See, e.g.*, GERBER, *supra* note 90, at 2 (noting that "hundreds of thousands of people every year . . . pour their energy and capital—and life—into starting a small business and fail," and stating that "many others . . . struggle along for years simply trying to survive").

[92] *See, e.g.*, *Donahue*, 328 N.E.2d at 514 ("Typically, the minority shareholder in a close corporation has a substantial percentage of his personal assets invested in the corporation. The stockholder may have anticipated that his salary from his position with the company would be his livelihood.") (citation omitted); *Muellenberg*, 669 A.2d at 1385 (noting that participation in the business is the "principal source of employment and income" for many close corporation shareholders); *In re Kemp*, 473 N.E.2d at 1178 (noting that a shareholder's "participation in [a close] corporation is often his principal or sole source of income"); 1 OPPRESSION, *supra* note 31, § 1:03, at 4 ("[A close corporation shareholder] may put practically everything he owns into the business and expect to support himself from the salary he receives as a key employee of the company. Whenever a shareholder is deprived of employment by the corporation . . . he may be in effect deprived of his principal means of livelihood."); *supra* notes 87–89 and accompanying text.

> If investors in closely held corporations are economically rational, it can only be because such investments have compensating benefits not available to investors in publicly held corporations. In many cases, a shareholder in a closely held corporation expects to receive such compensating benefits [e.g., a higher salary, job security, and job satisfaction] through employment . . . . Thus, a shareholder in a closely held corporation often has a significant investment interest in his job. He often invests for the purpose of having a job, and the salary and other benefits he receives are conceived to be part of the return on his investment.[93]

A close corporation investor, therefore, considers employment with the company to be the critical component of his or her overall investment return. As a consequence, it is likely that a rational shareholder would only purchase a minority stake in a close corporation if continued employment was part of the bargain struck with the majority shareholder.[94]

2. The Management Interest

Along with the related employment interest, investors are also motivated to commit capital to a close corporation because of their desire for management participation as a director or officer of the company.[95] Aside from the prestige and other intangibles associated with holding a director or officer position,[96] a management role also presents an opportunity to effectively monitor the shareholder's investment.[97]

Within a close corporation, such a monitoring ability is vitally important. After all, close corporation shareholders often invest a substantial portion of their life savings in the company[98] and, as a con-

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[93] Ragazzo, *supra* note 86, at 1109–10 (footnotes omitted).

[94] *See infra* Part IV(A) (discussing the investment bargain struck between close corporation shareholders).

[95] *See supra* note 29 and accompanying text.

[96] *See supra* notes 88–89 and accompanying text.

[97] *Cf. Ingle*, 535 N.E.2d at 1321 (Hancock, J., dissenting) ("The same features of the minority owner-participant's status which make him particularly vulnerable to action by the majority obviously work to compel him to stay on the job. *He needs to do so to protect his investment* and to share in any increase in its value.") (emphasis added); 1 OPPRESSION, *supra* note 31, § 3:06, at 38 ("[R]emoval of a minority shareholder from the board reduces his access to information on what is going on in the corporation and thereby his ability to protect himself against squeeze plays.").

[98] *See supra* note 92.

sequence, they need some way of protecting their investment. Unfortunately, a mere shareholder has no say in routine corporate decisionmaking.[99] Moreover, although shareholders have the statutory right to inspect a company's books and records with a proper purpose,[100] that right is easily hindered by a majority shareholder intent on obstructing such an inspection.[101] As a consequence, mere shareholders often lack both a voice in the company's decisionmaking process as well as access to information about the company's affairs. Because management has the ability to make corporate decisions and has access to corporate information,[102] however, a management role provides a direct opportunity for a shareholder to effectively participate in and monitor the company's activities.[103] Ideally, such an opportunity allows the shareholder to try and steer the business away from investment-threatening decisions.

Because of the importance of a monitoring ability in a close corporation, shareholders in such ventures expect that their investments entitle them to an active management role in the company.[104] Indeed, it is likely that an economically rational shareholder would forego investing in a close corporation unless the majority stockholder shared a basic understanding of management participation in the company.[105]

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[99] *See, e.g.*, Ragazzo, *supra* note 86, at 1115 (noting that the "shareholder has little or no say in the day-to-day management of the corporation."); Robert B. Thompson & D. Gordon Smith, Fiduciary Duty and "Sacred Space" in Corporate Takeovers 5 (October 15, 2000) (unpublished manuscript, on file with author) (noting that in the corporate governance structure, "the role for shareholders is limited" as "[t]hey vote, sell or sue, each in carefully measured doses"); *id.* at 5 n.16 (observing that shareholders vote only on electing directors, amending the articles, approving mergers, approving extraordinary sales of assets, and approving dissolution).

[100] *See, e.g.*, DEL. CODE ANN. tit. 8, § 220(b) (1998).

[101] *See, e.g.*, Sec. First Corp. v. U.S. Die Casting & Dev. Co., 687 A.2d 563, 566 (Del. 1997) (involving a lawsuit filed by a plaintiff shareholder after its written demand to inspect books and records was rejected); Compaq Computer Corp. v. Horton, 631 A.2d 1, 3 (Del. 1993) (same).

[102] *See, e.g.*, DEL. CODE ANN. tit. 8, § 141(a) (1998) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors . . . ."); *id.* § 220(d) ("Any director . . . shall have the right to examine the corporation's stock ledger, a list of its stockholders and its other books and records for a purpose reasonably related to his position as a director.").

[103] *See Wilkes*, 353 N.E.2d at 662 ("Other noneconomic interests of the minority stockholder are likewise injuriously affected by barring him from corporate office. Such action *severely restricts his participation in the management of the enterprise*, and he is relegated to enjoying those benefits incident to his status as a stockholder.") (emphasis added); *supra* note 89.

[104] *See supra* note 29 and accompanying text.

[105] *See infra* notes 302–303 and accompanying text.

In short, the courts' apparent understanding and acceptance of the economic rationale underlying close corporation investments is an important component of a shareholder oppression liability inquiry. Put differently, the courts' understanding and acceptance of the economics behind a close corporation investment decision seem to contribute to judicial determinations that reasonable expectations have been established.

C. *The Buyout Remedy*

Once reasonable expectations have been established, the shareholder oppression doctrine protects them through an expansive range of remedies. It has previously been noted that legislatures and courts have authorized remedies for oppressive conduct that are less drastic than dissolution.[106] The Minnesota legislature, for example, drafted a statute that authorizes "any equitable relief" for oppressed minority shareholders.[107] In addition, judicial opinions often list various forms of relief for oppressive conduct, including the appointment of a receiver, the declaration of a dividend, the reduction of excessive salaries, and the issuance of an injunction against further oppressive actions.[108] The most common alternative remedy, however, is a "fair value" buyout of the oppressed investor's stockholdings.[109] In opera-

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[106] *See supra* note 44 and accompanying text.

[107] MINN. STAT. ANN. § 302A.751 subd. 1 (West Supp. 2000).

[108] *See supra* note 44 and accompanying text.

[109] *See* 1 CLOSE CORPORATIONS, *supra* note 15, § 1.16, at 97 (noting that buyouts "are the most common remedy for dissension within a close corporation"); Murdock, *supra* note 39, at 470 ("The most common form of alternative remedy is the buy-out of the minority shareholder."); Thompson, *supra* note 30, at 231 ("The increased use of buyouts as a remedy for deadlock or dissension is the most dramatic recent change in legislative and judicial thinking on close corporations problems."); *see also* RMBCA § 14.34(a) (1993) ("In a proceeding under 14.30(2) to dissolve a corporation . . . the corporation may elect or, if it fails to elect, one or more shareholders may elect to purchase all shares owned by the petitioning shareholder *at the fair value* of the shares.") (emphasis added); Thompson, *supra* note 28, at 718 (noting that "[s]everal of the largest commercial states permit a corporation or its majority shareholders to avoid involuntary dissolution by purchasing the shares of the petitioning shareholders at their 'fair value'").

Support for the buyout remedy exists in half the states, although the relevant statutes and judicial decisions differ in their operation. *See* Thompson, *supra* note 28, at 718. In some states, the corporation or the shareholders are permitted by statute to purchase the shares of a minority shareholder seeking involuntary dissolution. *See, e.g.*, ALASKA STAT. § 10.06.630 (Michie 1989); CAL. CORP. CODE § 2000 (West 1990); MICH. COMP. LAWS ANN. § 450.1189 (West 1990); MINN. STAT. ANN. § 302A.751 (subd. 2) (West Supp. 2000); N.J. STAT. ANN. § 14A:12-7(8) (West 1992); N.Y. BUS. CORP. LAW §§ 1104-a, 1118 (McKinney Supp. 1992); N.D. CENT. CODE § 10-19.1-115 (1985); RMBCA § 14.34(a) (1993). In other states, statutes authorize a court to order a buyout as one of several possi-

tion, the buyout awards the aggrieved shareholder his or her proportionate share of the corporation's value.[110] This corporate "appraisal" is commonly conducted by calculating the company's investment value—a measurement which is typically based upon the earnings of the close corporation at issue over a specified period of time.[111]

The breadth of remedies for shareholder oppression provides the courts with great flexibility to choose a remedial scheme that most appropriately responds to the aggrieved shareholder's harm.[112] For a number of reasons, the buyout remedy itself is particularly significant. First, the buyout remedy functions as a "market" for the aggrieved minority shareholder by allowing the shareholder to recover the capital that he or she invested in the company.[113] Given that a close corporation, by definition, lacks a market for its shares,[114] the buyout remedy offers a court-authorized exit right for close corporation shareholders that allows them to recover the earnings-based value of their investments.

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ble remedies in dissolution proceedings or in other litigation between shareholders. *See, e.g.*, ARIZ. REV. STAT. ANN. § 10-216 (West 1990); ME. REV. STAT. ANN. tit. 13A, § 1123 (West 1992); S.C. CODE ANN. § 33-14-310(d)(4) (Law. Co-op. 1994); MODEL STAT. CLOSE CORP. SUPP. §§ 41, 42 (1993). Courts have also ordered buyouts as part of their general equitable authority. *See, e.g.*, Orchard v. Covelli, 590 F. Supp. 1548, 1560 (W.D. Pa. 1984); Davis v. Sheerin, 754 S.W.2d 375, 380, 383 (Tex. App. 1988); Thompson, *supra* note 28, at 720-21 ("Courts increasingly have ordered buyouts of a shareholder's interest by the corporation or the other shareholders even in the absence of specific statutory authorization."). Finally, it should be noted that, in certain situations, the minority shareholder may be able to buy out the holdings of the majority shareholder. *See, e.g.*, Muellenberg v. Bikon Corp., 669 A.2d 1382, 1389 (N.J. 1996).

[110] A 30% shareholder, for example, owns 30% of the company and has a corresponding claim to 30% of the company's value.

[111] *See* Thompson, *supra* note 30, at 233 ("The most common method for determining fair value is to calculate investment value, usually based on the company's earnings."); *id.* ("[T]he most commonly utilized formula [for calculating investment value] treats company earnings as determinant of investment value."); *see also* Hendley v. Lee, 676 F. Supp. 1317, 1329 (D.S.C. 1987) (valuing a close corporation based upon the company's earnings); *In re* Fleischer, 486 N.Y.S.2d 272, 274-75 (App. Div. 1985) (same); Blake v. Blake Agency, Inc., 486 N.Y.S.2d 341, 348 (App. Div. 1985) ("Investment value is usually a function of the earning power of the corporation.").

[112] *See* Thompson, *supra* note 28, at 722 (observing that "most courts and legislatures have given an expansive interpretation to remedies"); *cf. Pedro*, 463 N.W.2d at 288 ("The courts should be left with as much flexibility as possible to provide an adequate remedy for the case before them.") (internal quotation omitted).

[113] *See* Moll, *supra* note 18, at 793 ("By ordering a buyout of the minority's interest at 'fair value,' the courts are effectively replicating a market for close corporation minority interests and are allowing oppressed shareholders to 'cash out' of the business.") (footnote omitted).

[114] *See supra* note 41 and accompanying text.

Second, and similarly, the buyout remedy creates an equitable "parting" between the majority shareholder and the aggrieved minority shareholder. The majority shareholder continues to operate the close corporation and to participate in the company's successes and failures, while the minority shareholder recovers the value of the shareholder's invested capital and removes himself or herself from the company's affairs.[115] In a shareholder oppression context, this equitable parting may be necessary for an effective resolution of the dispute. Alternative remedies, in other words, are often inadequate in a shareholder oppression context. For example, assume that a minority shareholder's reasonable expectation of employment is frustrated when he or she is terminated without justification[116] by the majority shareholder. A specific performance order of reinstatement is a remedial option[117] but, in an oppression context, forcing the shareholders to continue working together is often undesirable. After all, in most oppression disputes, the dissension between the majority and minority shareholders "will hamper, if not eliminate, their ability to continue working together" such that "it would be counterproductive for the oppression doctrine to require a resumption of the shareholder's involvement."[118] To put it bluntly, "[i]t no doubt is futile to expect a closely held corporation to operate smoothly when a shareholder has been frozen out, litigation has ensued, and the court has compelled the shareholder's return."[119]

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[115] *See, e.g.*, 2 OPPRESSION, *supra* note 31, § 10:09, at 60 ("The buy-out feature in these statutes is desirable because it permits shareholders who want to preserve the enterprise as a going concern to buy out dissenters, and at the same time it provides an oppressed shareholder a fair price for his holdings."); Ragazzo, *supra* note 86, at 1119 ("[The buyout] is less harsh than dissolution and often gives both parties what they want most. The majority gets to run the business as it sees fit, unfettered by the continued participation of the minority, while, at the same time, the minority receives the fair value of its investment."); Sandra L. Schlafge, Comment, *Pedro v. Pedro: Consequences for Closely Held Corporations and the At-Will Doctrine in Minnesota,* 76 MINN. L. REV. 1071, 1080 n.46 (1992) ("[T]he buyout is the preferred remedy for shareholder disputes because it allows a return of the shareholder's capital while not crippling the business."); *id.* at 1093 ("[T]he statute provides for a buyout, which the Minnesota Legislature described as the preferred remedy because it returns the shareholder's capital while leaving the business entity intact.").

[116] If the majority's allegedly oppressive action (e.g., terminating the minority's employment) is justifiable in light of the minority's misconduct or incompetence, a finding of shareholder oppression is unwarranted. *See* Moll, *supra* note 18, at 800–01, 813.

[117] *See* Ragazzo, *supra* note 86, at 1117 (noting that "the remedy for an illegal discharge of a minority shareholder might be reinstatement . . . .").

[118] Moll, *supra* note 78, at 540.

[119] Deborah A. Schmedemann, *Fired Employees and/or Frozen-Out Shareholders (An Essay)*, 22 WM. MITCHELL L. REV. 1435, 1466 (1996); *see also* RMBCA § 14.34 cmt. (1993) ("[A] resort to litigation may result in an irreparable breach of personal relationships among the

An award of compensatory damages may likewise prove inadequate in an oppression context. Returning to our example of the terminated shareholder, assume that the discharged stockholder retains his or her management position (e.g., a director) as well as his or her general stockholder right to receive a proportionate share of the corporation's income.[120] Stated differently, assume that the shareholder's reasonable expectation of employment was the only expectation that was frustrated by the majority's actions. From a damages standpoint, a court could award conventional wrongful termination damages such as back pay[121] and, in appropriate cases, front pay.[122] Such an award would appear to make the aggrieved shareholder

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shareholders of a closely-held firm, making it impossible for them to continue in business to their mutual advantage."); III E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS § 12.7, at 184 (2d ed. 1998) (noting that the refusal to grant specific performance in a personal services context is partially based "on the undesirability of compelling the continuance of personal relations after disputes have arisen and confidence and loyalty have been shaken"); 1 OPPRESSION, *supra* note 31, § 3:06, at 51 n.22 ("[S]pecific performance may be denied on the ground that goodwill and a cooperative spirit among the executives is essential to successful operation of the enterprise."); Murdock, *supra* note 39, at 428 ("[I]f the problem is triggered by animosity among the shareholders, there may be an endless parade back to court to seek additional relief, should the animosity not be resolved. Therefore, in many instances, the only permanent resolution to the problem would be to eliminate the complaining minority interest by a repurchase of shares.") (footnote omitted); Ragazzo, *supra* note 86, at 1118 ("[B]y the time such shareholder disputes get to court, the relationship between the parties has usually deteriorated to such an extent that it is impractical to expect the parties to continue in business together.").

[120] *See infra* note 137 and accompanying text.

[121] *See* 2 MARK A. ROTHSTEIN ET AL., EMPLOYMENT LAW § 9.24, at 583 (1994) ("[A] major element of damages in any discharge action is the compensation (wages, salary, commissions, or other payments, plus fringe benefits) the employee lost by reason of the discharge."); *id.* ("As a general matter, the employee should recover back pay damages, less any mitigation amounts, from the date of the discharge until the date of trial, unless his or her employment would have ended earlier for a lawful reason."); *see also Wilkes*, 353 N.E.2d at 665 (awarding a discharged shareholder "the salary he would have received had he remained an officer and director of [the company]").

[122] As commentators have noted:

> In addition to compensation lost in the past, plaintiffs often seek future damages, or front pay, for some period of time beyond the date of the trial. The duty to mitigate means that, if the court permits awards of front pay, they can go only to those plaintiffs who have not been able to find other comparable employment after their discharge; in many future damages cases, however, the employee has another job that pays less than the former employment and argues that the defendant should have to compensate him or her for the lifetime earnings differential.

2 ROTHSTEIN ET AL., *supra* note 121, § 9.24, at 583.

whole in light of the unjustified termination of employment.[123] Given the track record of oppressive majority behavior, however, the damage award is arguably inadequate, as it leaves the other aspects of the shareholder's investment bargain (e.g., management role, dividends) subject to the majority's control. In other words, it seems problematic to grant a remedy that keeps the investment of the aggrieved shareholder locked into the company and, relatedly, forces the aggrieved shareholder to trust that a previously oppressive majority shareholder will not oppress again.[124] This is particularly true given that a termination of employment is rarely the only oppressive action taken by a majority shareholder. In fact, a termination of employment is usually only one component of a broader freeze-out scheme that ultimately involves removal from management as well as cessation of dividends.[125] Even if the damages award was coupled with an injunction forbidding subsequent oppressive actions (e.g., an injunction requiring the corporation to pay reasonable dividends in the future),[126] the supervision required by the injunction would cause a court to be continually involved in the "acrimonious relationship" between the parties—a situation that courts typically attempt to avoid.[127]

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[123] Back pay and front pay awards may not make the terminated shareholder completely "whole." Such awards do not compensate the shareholder for any loss of prestige caused by removal from a management position (except to the extent that the prestige of the position was represented by a higher salary). Furthermore, such awards do not compensate the shareholder for any loss of intangible "be your own boss" value. *See supra* notes 88–89 and accompanying text.

[124] *See, e.g.*, Ragazzo, *supra* note 86, at 1118 ("[A]fter substantial illegal conduct has been proved, it is unfair to a minority shareholder to require him to continue to trust the majority to treat him and his investment in a fair manner."); *see also* Baker v. Commercial Body Builders, Inc., 507 P.2d 387, 394 (Or. 1973) (noting the possibility that "those in control of the corporation are so incorrigible that they can no longer be trusted to manage it fairly in the interests of the stockholders").

[125] *See, e.g.*, *Wilkes*, 353 N.E.2d at 661, 663 n.13 (involving a minority shareholder who was terminated from employment and removed from management in a company where no dividends were paid); Burack v. I. Burack, Inc., 524 N.Y.S.2d 457, 459–60 (App. Div. 1988) (same); *In re Topper*, 433 N.Y.S.2d at 362 (same).

[126] *See, e.g.*, Patton v. Nicholas, 279 S.W.2d 848, 857 (Tex. 1955) ("The respondents are further entitled to have the injunction provide for reasonable dividends to be thereafter declared annually from future profits of the corporation . . . ."); Ragazzo, *supra* note 86, at 1117.

[127] Ragazzo, *supra* note 86, at 1118 (observing that one difficulty with "purely compensatory forms of relief" for oppression is that "they involve the court in continued supervision of an acrimonious relationship"); *see* JOHN D. CALAMARI & JOSEPH M. PERILLO, THE LAW OF CONTRACTS § 16–5, at 668 (4th ed. 1998) ("Courts have been reluctant to enforce even non-personal services contracts on grounds of difficulty of supervision."); III FARNSWORTH, *supra* note 119, § 12.4, at 164 ("Courts have also been reluctant to order performance if difficulties of supervision or enforcement are foreseen . . . ."); *cf.* CALAMARI & PER-

Third, the buyout remedy does not require the bargain between the shareholders to be articulated with precision. Although a frustrated expectation of employment or management can trigger oppression liability and a subsequent buyout remedy, the buyout does not award damages for the value of the lost job or the lost management position.[128] Instead, the conventional buyout remedy provides the aggrieved shareholder only with the value of his or her financial investment—i.e., the value of the shareholder's proportionate interest in the company.[129] Thus, the oppression doctrine operates with an asymmetry between its liability and damages inquiries. The loss of a job or a management position often serves as a trigger of oppression liability, but the conventional buyout remedy fails to directly compensate for this liability trigger.

This asymmetry, however, does provide some benefit. Because the buyout remedy does not compensate for a frustrated employment or management expectation, there is no need for those expectations to be stated with precision. For example, if damages stemming from a termination of employment were awarded as part of a buyout remedy, a court would need to know more than the mere liability fact that a general understanding of employment was shared between the investors.[130] Indeed, to calculate a proper front pay award, a court, at a minimum, would need to know the term of employment (i.e., the duration) that the discharged shareholder was supposed to complete.[131]

ILLO, *supra*, § 16–10, at 672 ("In many cases, courts have refused to grant specific performance on grounds that supervision of performance would involve an undue investment of judicial time and effort."); III FARNSWORTH, *supra* note 119, § 12.7, at 182–83 ("A court will not grant specific performance or an injunction if this would impose on it burdens of enforcement or supervision that are disproportionate to the advantages to be gained .... The burdens may be particularly heavy if judging the quality of the performance poses difficult problems or if supervision will be required over an extended period of time.").

[128] *See* Moll, *supra* note 78, at 571–72; *see also* Bahls, *supra* note 21, at 298–99 (observing that "[a]warding the fair market value of a shareholder's interest does not compensate for the loss of an expectation of a voice in management" because "[p]roblems inherent in quantifying the value of this expectation to intangible amenities often preclude the court from awarding any value for loss of the expectation").

[129] *See supra* note 110 and accompanying text.

[130] *See supra* notes 63–65 and accompanying text (noting that a mutual understanding between the shareholders can suffice to establish a reasonable expectation).

[131] For example, assume that a shareholder has a three-year employment agreement with a close corporation. Under the agreement, the shareholder is to be paid a salary of $80,000 per year. After one year, the shareholder is terminated without cause in violation of the agreement. Despite the best efforts of the shareholder, comparable employment can only be obtained at a $60,000 salary. The termination, therefore, robbed the shareholder of the ability to earn an additional $20,000 for the remaining two years of his or her agreement. A properly discounted award of $40,000 (i.e., the $20,000 salary differential for

Because the buyout remedy does not provide damages for a frustrated employment expectation, however, such additional detail is unnecessary. Simply put, the oppression doctrine can tolerate more indefiniteness in the employment and management "terms" of the overall investment bargain because, although such terms serve an important function as broad liability triggers, they have no part in the conventional "fair value" buyout. Thus, as long as a court is satisfied that a general understanding of employment or management was shared between the investors, no further detail on these understandings is typically needed. Majority conduct that unjustifiably frustrates such general understandings (e.g., an unjustified removal from management) will trigger oppression liability and will typically allow for application of the buyout remedy.

D. *Summary*

In summary, oppression courts seem to use evidence of pattern and conduct in conjunction with an understanding of close corporation investment economics to help them determine whether a reasonable expectation has been established. Once established, however, reasonable expectations are protected under the shareholder oppression doctrine by a wide range of remedies, including a "fair value" buyout that, in operation, is sensitive to the realities of an oppression setting. Armed with this understanding of the liability and damages facets of the shareholder oppression doctrine, our attention turns to contract law and its potential for handling oppression disputes.

III. Protecting the Reasonable Expectation via Contract Law

With an understanding of how the courts use the oppression doctrine to protect reasonable expectations, it is appropriate to ask whether contract law can provide similar protection under the guise

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the two remaining years of the agreement) would represent an accurate front pay award. Without knowledge of the three-year duration of the employment agreement, however, calculating an accurate front pay award would be impossible. As a consequence, the shareholder would presumably be unable to recover front pay damages.

Even if a court decided to reinstate the discharged employee rather than to award damages, it is likely that the court would still require significant detail about the original terms of employment. *Cf.* III Farnsworth, *supra* note 119, § 12.4, at 164 ("[T]he practical exigencies of drafting decrees to guide future conduct under the threat of the severe sanctions available for contempt have moved courts to require that contract terms be expressed with greater certainty if specific relief is to be ordered than if damages are to be awarded.").

of safeguarding implied-in-fact contracts.[152] This Article contends that contract law will likely be unable to protect the reasonable expectations of close corporation shareholders because, in practice, courts tend to apply contract law in a narrow manner. Put differently, because of indefiniteness, employment at will, and statute of frauds problems, courts are likely to conclude that the oppression doctrine's reliance on pattern, conduct, and economic evidence is insufficient to establish an implied-in-fact contract. Moreover, conventional remedies in a contract dispute are probably inadequate in a shareholder oppression context.[153] Nevertheless, if an expansive view of contract law was taken, contract law could be used to protect the minority shareholder's reasonable expectations. In that instance, the need for an independent oppression doctrine would be minimized, if not eliminated.

A. *The "Contract" Between Close Corporation Shareholders*

If contract law can be used in lieu of the oppression doctrine to protect the minority's reasonable expectations of employment, management, and a share of the corporate earnings,[154] such reasonable

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[152] Because there is a paucity of cases and commentary that discuss both a shareholder oppression claim and a breach of contract claim for the same wrongful majority conduct, there are no clear answers regarding whether contract law could handle disputes that are presently handled by the shareholder oppression doctrine. Due to this minimal amount of precedent, this Article's discussion of potential problems that could derail the efforts of contract law to handle oppressive conduct should be understood as "best guesses"—i.e., best guesses of how courts would actually respond to a breach of contract claim that is premised on allegedly oppressive activity.

[153] For many years, contract law had little ability to protect the reasonable expectations of close corporation shareholders because of a separate *corporate* law problem. Indeed, shareholder agreements for continuous employment or management participation were previously unenforceable under corporate law, as they were considered to be improperly infringing on the management powers of the board of directors. *See, e.g.*, McQuade v. Stoneham, 189 N.E. 234, 236 (N.Y. 1934) ("[I]t must be ... true that the stockholders may not, by agreement among themselves, control the directors in the exercise of the judgment vested in them by virtue of their office ...."); *id.* ("Directors may not by agreements entered into as stockholders abrogate their independent judgment."); *id.* (noting that the stockholders' "power to unite" is "limited to the election of directors and is not extended to contracts whereby limitations are placed on the power of directors to manage the business of the corporation"). Modern state statutes, however, have largely eliminated this corporate law restriction. *See* Edward B. Rock & Michael L. Wachter, *Waiting for the Omelet to Set: Match-Specific Assets and Minority Oppression in Close Corporations*, 24 J. CORP. L. 913, 914 (1999).

[154] *See* Moll, *supra* note 18, at 794 ("In a close corporation ... the shareholder typically commits his capital with the expectation that his investment entitles him to employment and to a management role, as well as to a proportionate share of the company's earn-

expectations must be described in the language of contracts. To accomplish this task, it is necessary to conceptualize the contract or contracts that are arguably formed when a typical investor commits capital to a close corporation.[135] One plausible conception views the core

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ings."); *supra* note 29 and accompanying text; *see also* Michaud v. Morris, 603 So. 2d 886, 888 (Ala. 1992) ("Certain basic expectations of investors are enforceable in the courts, and among those is a right to share proportionally in corporate gains."); Bahls, *supra* note 21, at 330 ("Shareholders in close corporations expect proportional distribution of the earnings of the corporation while it is operating.").

[135] When investors commit capital to a close corporation, it could be argued that the investors have entered into a "contract" whose terms are established by the company's charter, the company's bylaws, and the state's corporations statutes. These sources primarily define the "contractual" relationship between the directors, officers, and shareholders on the one hand, and the corporation itself on the other hand. The "contract" discussed in this Article, however, is different, as it involves the bargain between the majority shareholder and the individual minority shareholders. In close corporations, in other words, the charter, bylaws, and corporate statutes do not represent the entirety of the bargain between the participants. *See, e.g., In re* Topper, 433 N.Y.S.2d 359, 365 (Sup. Ct. 1980) ("This Court . . . recognizes that in a close corporation the bargain of the participants is often not reflected in the corporation's charter, by-laws nor even in separate signed agreements."); F. Hodge O'Neal, *Close Corporations: Existing Legislation and Recommended Reform*, 33 BUS. LAW. 873, 886 (1978) ("In a close corporation, the corporation's charter and bylaws almost never reflect the full business bargain of the participants."); *id.* at 887 ("[Acts] which, in law, are a valid exercise of powers conferred by the articles may nevertheless be entirely outside what can fairly be regarded as having been in the contemplation of the parties when they became members of the company.") (internal quotation omitted); *id.* ("[E]ven when there has been nothing done in excess of power it is necessary to consider whether the situation which has arisen is not quite outside what the parties contemplated . . . and whether what has been done is not contrary to the assumptions which were the foundation of their agreement."); D. Prentice, *Protection of Minority Shareholders*, 1972 CURRENT LEGAL PROBS. 124, 134 (1972) (finding unsatisfactory the argument "that the minority shareholder has no one to fault but himself in that his exclusion from participation in the management of the company is merely a consequence of the contract between himself and the company established by the articles of association, a contract which putatively he has freely entered into," and noting that "[i]n establishing the nature of the relationship between the members of a private company, it is necessary for the courts to go beyond the provisions in the articles of association and in addition to take into consideration the expectations of the parties when the company was originally formed") (footnote omitted); *see also* EASTERBROOK & FISCHEL, *supra* note 41, at 12 ("[W]e often speak of the corporation as a 'nexus of contracts' or a set of implicit and explicit contracts. This reference, too, is shorthand for the complex arrangements of many sorts that those who associate voluntarily in the corporation will work out among themselves. This form of reference is a reminder that the corporation is a voluntary adventure, and that we must always examine the terms on which real people have agreed to participate."); Krishnan S. Chittur, *Resolving Close Corporation Conflicts: A Fresh Approach*, 10 HARV. J.L. & PUB. POL'Y 129, 159 (1990) (stating that "[t]he public corporation can be viewed as a standard form multiparty contract, some of the terms of which are specified by statute," and noting that "[t]he close corporation does not involve the same 'standard form' contract, or the consequential grant of power"); Prentice, *supra*, at 146 ("Where [expectations] have been interfered with or are in some

contract as an exchange of investment capital for a stock certificate that represents the right to be a shareholder in the company.[136] Just as in a public corporation, of course, the status of "shareholder" entitles an investor to such benefits as a proportionate share of the corporate earnings (e.g., a proportionate share of the dividends, if declared), a right to any stock appreciation, a right to inspect company books and records (with a proper purpose), a right to vote on shareholder issues, and a right to be recognized as a shareholder.[137] Unlike the public corporation, however, shareholder status in a close corporation typically conveys additional rights as well—i.e., rights to employment and management participation in the company.[138] In this "money-for-stock" conception, therefore, the minority shareholder parts with consideration (i.e., money)[139] and receives in return a stock certificate that conveys, *inter alia*, a right to employment, a right to an active

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way unfulfilled, then this should prima facie constitute oppression whether or not there was any legal impropriety.").

[136] *See generally* DEL. CODE ANN. tit. 8, § 158 (1998) ("The shares of a corporation shall be represented by certificates .... [E]very holder of stock represented by certificates and upon request every holder of uncertificated shares shall be entitled to have a certificate signed by, or in the name of the corporation ...."). The stock certificate, of course, also conveys the rights that are provided to all shareholders under the corporate law of the state (for example, the right to a proportionate share of the company's earnings). *See infra* note 137 and accompanying text.

[137] *See, e.g., Michaud*, 603 So. 2d at 888 ("Certain basic expectations of investors are enforceable in the courts, and among those is a right to share proportionally in corporate gains."); Exadaktilos v. Cinnaminson Realty Co., 400 A.2d 554, 560 (N.J. Super. Ct. Law Div. 1979) ("Profit is expected through the payment of dividends or sale of stock at an appreciated value."); Davis v. Sheerin, 754 S.W.2d 375, 382 (Tex. App. 1988) ("[W]e find that conspiring to deprive one of his ownership of stock in a corporation, especially when the corporate records clearly indicate such ownership, is ... oppressive. Appellant's conduct not only would substantially defeat any reasonable expectations appellee may have had ... but would totally extinguish any such expectations."); O'Neill, *supra* note 21, at 663 ("The shareholder of a publicly traded corporation may realize a return on her investment in either of two ways: directly, by a distribution of dividends, or indirectly, by an increase in the market value of her shares."); Schlafge, *supra* note 115, at 1077 n.29 ("Both [public corporation and close corporation] investors expect appreciation in the value of their investment."); *supra* notes 99–100 and accompanying text (discussing voting rights and inspection rights). *See generally* Moll, *supra* note 78, at 553–56 (discussing general reasonable expectations).

[138] *See, e.g., Exadaktilos*, 400 A.2d at 561 ("Unlike their counterparts in large corporations, [close corporation minority shareholders] may expect to participate in management or to influence operations, directly or indirectly, formally or informally. Furthermore, there generally is an expectation on the part of some participants that their interest is to be recognized in the form of a salary derived from employment with the corporation.") (citation omitted); *supra* notes 75–76 and accompanying text.

[139] *See infra* note 203 (noting that a shareholder's contribution of capital can be treated as "consideration").

management role, and a right to a proportionate share of the company's earnings (e.g., dividends, stock appreciation). Employment, management, and a proportionate stake in the company's profits, therefore, would be viewed as terms of this money-for-stock contract.

A single money-for-stock contract with a number of accompanying terms, however, is not the only way to conceptualize the close corporation investment contract.[140] A court may find that the close corporation bargain is comprised of a number of smaller contracts—e.g., a money-for-employment contract, a money-for-management contract, a money-for-dividends contract, etc. Such a characterization is not necessarily a stretch given that a single consideration (the minority's investment capital) can support multiple promises (e.g., the majority's promise of employment, the majority's promise of management).[141]

As will be discussed, the choice between a single money-for-stock contract and multiple money-for-benefit contracts may be important. In fact, the way in which the court conceptualizes the close corporation investment contract may significantly affect the ability of contract law to handle a typical shareholder oppression dispute.

B. *The Failure of the Pattern Determination*

1. Indefiniteness

a. *The Significance of Indefiniteness*

The indefiniteness of a communication can affect a contract analysis at two levels. First, as a threshold matter, an indefinite communication is some evidence that the parties lacked the intent to contract in the first place.[142] Before concluding that a contract has re-

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[140] *See* Morey W. McDaniel, *Bondholders and Corporate Governance*, 41 BUS. LAW. 413, 416 (1986) (noting that the average stockholder can be described as a holder of an "investment contract").

[141] *See, e.g.*, Pugh v. See's Candies, Inc., 171 Cal. Rptr. 917, 925 (Ct. App. 1981) ("A single and undivided consideration may be bargained for and given as the agreed equivalent of one promise or of two promises or of many promises.") (internal quotation omitted); CALAMARI & PERILLO, *supra* note 127, § 4.15, at 218 ("The rule is that one consideration will support many promises.").

[142] *See* CALAMARI & PERILLO, *supra* note 127, § 2.9, at 50 ("The more terms that are omitted the more likely it is that the parties do not intend to contract."); *see also* Soar v. National Football League Player's Ass'n, 550 F.2d 1287, 1290 (1st Cir. 1977) ("While an enforceable contract might be found in some circumstances if one or more of such questions were left unanswered, the accumulation in the instant case of so many unanswered questions is convincing evidence that there never was a consensus ad item between the parties."); Owen v. Owen, 427 A.2d 933, 937 (D.C. 1981) ("One of the essential elements

sulted, courts typically search for proof that both parties assented to be bound.[143] Under traditional contract law, such a search involves an inquiry into offer and acceptance.[144] A determination that words or conduct amount to an offer, however, is not a determination that is lightly made. Indeed, "[c]ourts have reason for caution, since to hold the maker of a proposal to a contract exposes the maker to liability based on the recipient's expectation interest, even in the absence of any reliance."[145] Thus, it is generally stated that the indefiniteness of the suggested bargain is a factor weighing against the conclusion that an offer—a manifestation of intent to be bound—has been established.[146] As the Southern District of New York stated:

> It is true that there is much room for interpretation once the parties are inside the framework of a contract, but it seems that there is less in the field of offer and acceptance. Greater precision of expression may be required, and less help from the court given, when the parties are merely at the threshold of a contract.[147]

Second, even if there is an intent to contract, the indefiniteness of the contract terms themselves may render the agreement unenforceable.[148] Although older authorities typically required contract terms to be stated with a high degree of specificity,[149] the modern view

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for formation of a contract is a manifestation of agreement or mutual assent by the parties to the terms thereof; in other words, to establish a contract the minds of the parties must be in agreement as to its terms. The failure to agree on or even discuss an essential term of a contract may indicate that the mutual assent required to make or modify a contract is lacking.") (internal quotation omitted) (citations omitted).

[143] *See* 1 FARNSWORTH, *supra* note 119, § 3.1, at 184.

[144] *See* 1 *id.* § 3.10, at 234 (defining an offer as "a manifestation of assent that empowers another to enter into a contract by manifesting assent in return").

[145] 1 *Id.* § 3.10, at 237.

[146] *See* CALAMARI & PERILLO, *supra* note 127, § 2.6, at 46 (noting that an "important factor[]" to be considered "[i]n determining whether a communication is an offer or not" is whether there are "detailed terms or ... only relatively few terms covered"); 1 FARNSWORTH, *supra* note 119, § 3.10, at 237 (listing "the completeness of the suggested bargain" as a factor relevant to determining whether a particular proposal amounts to an offer).

[147] United States v. Braunstein, 75 F. Supp. 137, 139 (S.D.N.Y. 1947).

[148] *See* CALAMARI & PERILLO, *supra* note 127, § 2.9, at 50 ("[E]ven if the parties intend to contract, if the content of their agreement is unduly uncertain no contract is formed ... because an agreement must be sufficiently definite before a court can determine if either party breached it.") (footnote omitted).

[149] *See, e.g.* id. § 2.9, at 53 ("[U]nder the traditional rule where the parties have purported to agree upon a material term and left it indefinite, the agreement is too vague and indefinite."); *cf.* 1 SAMUEL WILLISTON & WALTER H.E. JAEGER, A TREATISE ON THE LAW OF

permits a degree of imprecision so long as the contract terms "provide a basis for determining the existence of a breach and for giving an appropriate remedy."[150]

Although these two facets of indefiniteness are technically distinct, they are closely related in practice. The absence of essential terms affects a court's assessment of whether the parties intended to contract at all, as well as a court's ability to enforce any purported bargain. Nevertheless, depending on how the close corporation investment contract is conceptualized, the distinction between "no intent to contract" and "indefinite terms" may still have some practical significance.

b. *The Definiteness of the Close Corporation Bargain*

It has previously been suggested that courts, as part of their reasonable expectations analyses, typically rely on evidence drawn from the parties' actions and course of conduct. As mentioned, this evidentiary inquiry generally requires nothing more than proof that the aggrieved shareholder invested in the company (often as a founder) and immediately thereafter began serving as an employee and manager of the corporation. Many courts have been willing to find that such circumstantial evidence suffices to create an enforceable reasonable expectation.[151] As a matter of contract law, however, such a minimal amount of proof is problematic. Although the circumstantial evidence in close corporation disputes typically establishes very general understandings of employment and management participation, there is rarely any further evidence allowing a court to flesh out the details of these generic understandings. For example, although a shared understanding of employment and management participation may be established through evidence that the shareholders founded the close corporation, committed capital to the business, quit their prior jobs, and immediately began serving as employees and managers,[152] there is usually no evidence of the details of the arrangement

CONTRACTS § 37, at 107 (3d ed. 1957) ("[A]n agreement, in order to be binding, must be sufficiently definite to enable a court to give it an exact meaning.").

[150] *See, e.g.*, RESTATEMENT (SECOND) OF CONTRACTS § 33(2) (1981); *see also* Pyeatte v. Pyeatte, 661 P.2d 196, 200 (Ariz. 1982) ("Although the terms and requirements of an enforceable contract need not be stated in minute detail, it is fundamental that, in order to be binding, an agreement must be definite and certain so that the liability of the parties may be exactly fixed.").

[151] *See supra* notes 77–79 and accompanying text.

[152] *See supra* notes 77–79 and accompanying text; *infra* Part IV(A).

(e.g., salary, benefits, duration of employment, specific management position, termination provisions).[153] Many contracts, of course, contain vague and indefinite terms, and traditional contract doctrine has mechanisms for dealing with such imprecision.[154] The critical difference in the close corporation context, however, is that detailed terms are often completely absent.[155] Depending upon how a court conceptualizes the close corporation investment contract, this degree of indefiniteness may be problematic.[156]

For example, if the investment contract is viewed as multiple money-for-benefits contracts such as money-for-employment and money-for-management, the total absence of detailed employment and management terms would likely cause difficulties for courts attempting to find the necessary intent to contract. Simply put, it is hard to imagine a viable money-for-management contract when no position, duration, compensation, and responsibility terms are present.[157] Taken as a whole, the cumulative absence of terms about the management "agreement" may lead a court to conclude that the parties did not assent to be bound to *any* management arrangement.

An alternative money-for-stock conceptualization, however, could potentially overcome this hurdle, as an actual exchange of capital for stock certificates is generally understood in all investment situations to reflect a mutual intent to be bound—i.e., the investor binds herself to the restrictions on stock ownership that are contained in the company's articles and bylaws, and the company binds itself to provide, at a minimum, the benefits of stock ownership that the state's corporate laws require (e.g., the right to vote in the same manner as similar stockholders).[158] Even if the money-for-stock contract does convey an

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[153] *See, e.g., In re Topper*, 433 N.Y.S.2d at 361 ("These shareholder agreements provide no method for transfer or purchase of shares (except in case of death), *nor do they specify the terms of employment for Topper and shareholder Goldstein who were intended to play active management roles.*") (emphasis added); *infra* note 215 and accompanying text (observing that close corporations typically operate informally with little or no explicit terms).

[154] *See, e.g., infra* Part III(B)(1)(c) (discussing trade usage, course of performance, and course of dealing evidence).

[155] *See supra* note 153 and accompanying text.

[156] *See, e.g.,* JOHN EDWARD MURRAY, JR., MURRAY ON CONTRACTS § 38, at 83 (3d ed. 1990) ("At some point . . . the terms of the agreement may be so unclear, or the agreement may be silent on such important terms or so many terms, that courts will not be able to determine whether any breach occurred because they cannot be certain of what may have been breached.").

[157] *See supra* note 156; *cf. Pyeatte*, 661 P.2d at 200 (noting that "compensation, penalty provisions, and other material requirements of the agreement" are frequently terms that are "necessary for the required definiteness").

[158] *See, e.g.,* DEL. CODE ANN. tit. 8, § 212(a) (1998) (granting the right to vote).

intent to be bound, however, the complete absence of detailed terms would spur more indefiniteness problems, as the lack of detail would make it quite difficult for a court to make breach and remedy determinations.[159] Without any specificity regarding the duration of a management term, for example, a court would have no basis for determining whether, after five years of service, the removal of a minority shareholder from a director position constitutes a breach of contract. Similarly, without detail as to salary, it would be difficult to calculate back pay and front pay awards that are based on the salary differential between the close corporation job and the post-discharge employment.[160] In short, under either conceptualization of the investment contract, such pervasive indefiniteness makes it highly questionable whether traditional contract principles could protect a minority investor in the typical shareholder oppression dispute.[161]

The Delaware decision of *Litle v. Waters* is a rare precedent that nicely exemplifies the differing judicial treatment of breach of contract claims and shareholder oppression claims when indefiniteness is at issue.[162] In *Litle,* Thomas Litle and James Waters were shareholders in two close corporations—Direct Order Sales Corporation (DOSCO) and Direct Marketing Guaranty Trust Corporation (DMGT).[163] Waters owned two-thirds of the stock of both companies and Litle owned the remaining one-third of the shares of both firms.[164] Litle allegedly consented to DMGT electing Subchapter S corporate status[165] "in reliance

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[159] *See, e.g.*, Neely v. Banker's Trust Co. of Tex., 757 F.2d 621, 627 (5th Cir. 1985) (noting the "practical difficulties of enforcing obscure, imprecise, or otherwise incomplete promises").

[160] *Cf. Pyeatte*, 661 P.2d at 200 (observing that "compensation" is frequently a term that is "necessary for the required definiteness"); 2 ROTHSTEIN ET AL., *supra* note 121, § 9.24, at 583 ("[A] major element of damages in any discharge action is the compensation (wages, salary, commissions, or other payments, plus fringe benefits) the employee lost by reason of the discharge.").

[161] *Cf.* Bahls, *supra* note 21, at 326 ("Assent to alleged changes in expectations is not adequate if the terms and specifics of the changed expectations are not sufficiently definite for the court to fashion an appropriate order to protect the changed expectation.").

[162] Civ. A. No. 12155, 1992 WL 25758 (Del. Ch. Feb. 11, 1992).

[163] *See id.* at *1.

[164] *See id.*

[165] Companies meeting certain criteria can elect Subchapter S corporation status under the Internal Revenue Code. *See, e.g.*, CARY & EISENBERG, *supra* note 26, at 119–20 (describing the S-corporation criteria). Such an election means that "the federal government [will] not tax the income of the entity on the entity level, rather, it [will] pass through the income to its shareholders in a fashion similar to that of a partnership, notwithstanding whether or not the entity made cash distributions to its shareholders." *Litle*, 1992 WL 25758, at *1.

on Waters' alleged promise that the company always would make available sufficient funds to the shareholders to cover any taxes incurred as a result of the company's S-corp[] election."[166] No written document, however, reflected this purported promise.[167]

Waters ultimately fired Litle from his positions as president and CEO of DMGT and of DOSCO. DMGT and DOSCO were subsequently merged, and the new combined entity prospered.[168] According to Litle, the new company failed to distribute dividends even though the earnings of the business had resulted in a $560,000 tax liability to Litle.[169] As the court noted, "Litle has had to pay, or borrow in order to pay, the taxes out of his own pocket rather [than] from cash distributions from the corporation."[170]

Litle asserted that the company's continual failure to provide dividend distributions from the corporation constituted a breach of contract as well as an oppressive abuse of discretion.[171] In assessing the breach of contract claim, the court repeated Litle's allegation that an agreement to make funds available had been entered into between Litle and Waters. The court, however, concluded that the alleged agreement was "too vague and indefinite to be enforceable as a contract."[172] As the *Litle* court noted:

> Even if I assume that the parties intended to make a contract, material provisions of an agreement can be so indefinite that the agreement will not be enforced. The material terms are uncertain where they fail to provide a reasonable basis for determining the existence of a breach and for giving the appropriate remedy. *Although vagueness and indefiniteness are matters of degree, no reasonable person could find that the alleged agreement at issue contains a sufficient delineation of the material terms: the agreement has no provisions as to how much will be paid, how it will be paid, when it will be paid and to whom it will be paid.* Therefore, I dismiss the allegation as failing to state a claim for breach of a contract right . . . .[173]

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[166] *Litle*, 1992 WL 25758, at *1.
[167] *See id.*
[168] *See id.* at *1–2.
[169] *See id.* at *2.
[170] *Id.*
[171] *See Litle*, 1992 WL 25758, at *6–7.
[172] *Id.* at *6.
[173] *Id.* (emphasis added) (citations and internal quotations omitted).

With respect to the oppression claim, however, the *Litle* court did not view indefiniteness as an obstacle. Although Litle's allegation was nearly identical to his breach of contract claim—i.e., he asserted that the refusal to declare dividends constituted oppressive conduct[174]—the court found that Litle's contentions stated a cognizable oppression claim that survived a motion to dismiss. As the court observed:

> As far as whether plaintiff makes an adequate argument that defendants violated his reasonable expectations, it is only reasonable to believe that when Waters and Litle entered into these ventures that neither expected that the other would use their power so as to make the stock a liability when the company was making money in order to effectuate a squeeze out. Plaintiff makes an adequate argument that defendants violated this reasonable expectation. For example, he alleges that the company was rich with cash and that the only reason that the company did not make dividends was to aid Waters to buy Litle out for less than fair value . . . . [T]his failure to pay dividends can be especially devastating in a Subchapter S corporation setting, as this case is, since the corporation passes its income through to its shareholders even though the corporation has not made any distributions to the shareholders.[175]

Although the indefiniteness of the Litle-Waters "agreement" proved fatal to the breach of contract claim, such indefiniteness was not an obstacle to recognizing an oppression claim. *Litle,* therefore, supports the proposition that traditional contract law requires more

[174] Litle alleged that "[t]he Director Defendants' refusal to declare dividends so that Litle would suffer an oppressive tax burden constitutes a gross and oppressive abuse of discretion." *Id.* (internal quotation omitted). He also contended that "defendants' continual failure to provide distributions from the corporation so that he can pay his substantial tax liability while the corporation provides such distributions via loan repayments to the other stockholder and while the corporation is rich with cash sufficiently alleges oppressive abuse of discretion." *Id.* at *7.

[175] *Litle,* 1992 WL 25758, at *9. This passage is also significant because it illustrates the *Litle* court's understanding of the economics behind this particular close corporation investment. By highlighting the S-corporation setting and the tax implications of such an entity, the *Litle* court seems to appreciate that a rational minority stockholder would not have invested in such a venture without reaching a shared understanding of reasonable dividend payments with the majority stockholder. *Cf. supra* Part II(B) (discussing the economic rationale for close corporation investments). Because of this economic understanding, the *Litle* court may have been more willing to credit Litle's alleged reasonable expectation of dividend payments.

evidence to establish an implied-in-fact contract than the oppression doctrine requires to establish a reasonable expectation.[176] Put differently, whereas pattern and conduct evidence helps to establish reasonable expectations, such evidence is likely too thin and too indefinite to help establish similar implied-in-fact contracts.[177]

c. *Combatting Indefiniteness Through Trade Usage and Course of Performance*

As mentioned, modern contract law does have mechanisms for dealing with indefinite agreements. Trade usage and course of performance evidence, for example, can be used to interpret existing terms of a contract and to add supplemental terms to a contract.[178]

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[176] *See* Orchard v. Covelli, 590 F. Supp. 1548, 1556, 1558 (W.D. Pa. 1984) (rejecting a shareholder-employee's wrongful discharge claim on several grounds, including the ground that there was "no evidence of the existence of a contract for employment, oral or written," but granting oppression-based relief by concluding that the termination was part of a breach of fiduciary duty); *cf.* Jaffe Commercial Fin. Co. v. Harris, 456 N.E.2d 224, 229, 231–32 (Ill. App. Ct. 1983) (rejecting, on indefiniteness and other grounds, a minority's assertion that his exclusion from the company violated "an actual agreement" between the shareholders, but rejecting the same claim on completely different grounds when the exclusion from the company was recharacterized as an "oppressive freeze-out").

[177] For this reason, a claim of promissory estoppel would likely fail as well. *See, e.g.*, I FARNSWORTH, *supra* note 119, § 2.19, at 159 ("Although some courts have held that the promise [in a promissory estoppel claim] need not contain all the elements of an offer, it must be 'clear and definite' to use a phrase favored by courts.") (footnote omitted). In addition, courts have observed that "promissory estoppel only operates as a substitution for consideration." *Litle*, 1992 WL 25758, at *6 (citation omitted). Although attempts to protect the close corporation investment bargain as an implied-in-fact contract will probably encounter indefiniteness, employment at will, and statute of frauds problems, the issue of adequate consideration is unlikely to pose any difficulties. *See supra* notes 140–141 and accompanying text; *infra* note 203.

[178] *See, e.g.*, CALAMARI & PERILLO, *supra* note 127, § 2.9, at 53 (noting that "missing term[s] may be supplied by external sources, including standard terms, usages by which the parties are bound, a course of dealing between the parties prior to the agreement, and a course of performance after it. The term becomes part of the contract by implying that the parties contracted on the basis of these sources."); *id.* § 3.17, at 161–64 (explaining that trade usage and course of performance evidence can be used to interpret meaning as well as to add terms); MURRAY, *supra* note 156, § 89, at 430 ("[T]rade usage may be used by courts to interpret the expression of the parties, or it may be seen as supplying terms in the agreement of the parties."); *see also* U.C.C. § 1–205(3) (2000) ("A course of dealing between parties and any usage of trade in the vocation or trade in which they are engaged or of which they are or should be aware give particular meaning to and supplement or qualify terms of an agreement.").

It is worth noting that common-law decisions often describe trade usage, course of dealing, and course of performance collectively as "custom." *See* CALAMARI & PERILLO, *supra* note 127, § 3.17, at 161 ("The UCC has drawn a careful distinction among 'course of

Thus, it is worth asking whether trade usage and course of performance[179] evidence can be used to remedy indefinite terms in an alleged close corporation "investment contract."[180]

i. Trade Usage

Given that shareholder oppression courts tend to look to a pattern of close corporation behavior as part of their oppression determination, one might think that the concept of trade usage is analogous. After all, a "pattern" and a "trade usage" seem comparable, at least superficially, due to their focus on repeated actions between similar parties in similar situations.[181] Contract law, however, tends to

dealing,' 'course of performance' and 'trade usage,' whereas the common law decisions often inartistically meshed the three together under the classification of custom.").

[179] As the above citations indicate, course of dealing evidence can also be used to interpret existing terms and to add supplemental terms. *See supra* note 178 and accompanying text. After all, "[a] course of dealing is a sequence of previous conduct between the parties to a particular transaction which is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct." U.C.C. § 1–205(1) (2000). As the definition indicates, a course of dealing relates to conduct that occurred *prior to* the purported agreement between the parties. *See* CALAMARI & PERILLO, *supra* note 127, § 3.17, at 161. Before investing in a close corporation, the majority and minority shareholders usually have not been associated as investors in another close corporation venture. Most often, therefore, there is no course of dealing evidence available to a court. Course of performance evidence relating to conduct occurring *after* the purported investment agreement, however, is available in most (if not all) oppression disputes. *See* U.C.C. § 1–205 cmt. 2 (2000) ("Course of dealing . . . is restricted, literally, to a sequence of conduct between the parties previous to the agreement. However, the provisions . . . on course of performance make it clear that a sequence of conduct after or under the agreement may have equivalent meaning."). Such evidence may be crucial to a court wanting to fill in missing terms in order to overcome an indefiniteness problem. As a consequence, whereas course of performance evidence is independently discussed in this Article, *see supra* Part III(A)(1)(c)(ii), course of dealing evidence is not. Many of the issues related to a course of performance, however, are also applicable to a course of dealing.

[180] It is important to note that trade usage and course of performance evidence typically combat indefiniteness at the terms stage—not at the "intent to contract" formation stage. Thus, when thinking about the function that trade usage and course of performance evidence can serve, it is easier to view the investment contract as a money-for-stock arrangement where the terms, rather than the intent to contract, pose the primary indefiniteness problems. *See supra* notes 136–139, 158–160 and accompanying text. As mentioned, however, indefiniteness at the formation stage and the terms stage are closely related. *See supra* note 150 and accompanying text. To the extent that courts conclude that there was no intent to contract because of the complete absence of detailed terms, trade usage and course of performance evidence are relevant to the indefiniteness inquiry at the formation stage. In fact, by adding detail to the terms of the alleged bargain, trade usage and course of performance evidence help to counteract the lack of express detail that might otherwise prompt a "no intent to contract" finding.

[181] *Cf.* U.C.C. § 1–205 cmt. 9 (2000) (describing a "usage" as a "dominant pattern").

define trade usage in a more restrictive manner. The Uniform Commercial Code, for example, defines "usage of trade" as "any practice or method of dealing having such regularity of observance in a place, vocation or trade as to justify an expectation that it will be observed with respect to the transaction in question."[182] This more detailed definition does not seem to coincide with the pattern and conduct evidence used to analyze a shareholder oppression claim. Although post-investment employment and management participation is a regular "practice or method of dealing" in close corporations, such a practice or method is generally observed in other close corporation ventures, not in a specific "place, vocation or trade."[183] More precisely, this practice or method is observed in a particular *setting*—i.e., close corporations—that cuts across geographic regions and particular occupations. Similarly, a practice observed in a "trade" generally refers to conduct occurring in a particular industry.[184] Without some stretching, of course, close corporation investing does not fit easily into an industry classification. Nevertheless, if contract law was applied more expansively, perhaps trade usage notions could be used to incorporate pattern and conduct evidence in shareholder oppression situations.

Yet even if post-investment employment and management participation in a close corporation—i.e., pattern and conduct evidence—was considered by contracts courts as evidence of trade usage, it is unclear how this would solve the indefiniteness problem that potentially results from the cumulative absence of detailed terms. At best, the trade usage would establish that close corporation investors usually receive employment and management participation as a result

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[182] U.C.C. § 1-205(2) (2000).

[183] If close corporation investing can be viewed as a "vocation," perhaps post-investment employment and management could be characterized as a usage of trade. Such a construction seems unlikely, however, given that a "vocation" is defined as "[t]he activity on which one spends [the] major portion of his time and out of which he makes his living." BLACK'S LAW DICTIONARY 1573 (6th ed. 1990). Although close corporation shareholders may spend a good deal of time with the initial investment decision and with subsequent monitoring of the investment, most shareholders make their living off of the salary received as a close corporation employee, rather than off of the financial return on the investment itself. *See supra* notes 91-92 and accompanying text.

[184] *See* MURRAY, *supra* note 156, § 89, at 428 ("In a given trade, profession, or calling, parties may adhere to certain practices to such an extent that the practices may appear to be the 'standard' within that industry or vocation."); *cf.* U.C.C. § 1-205 cmt. 5 (2000) ("Under the requirement [of 1-205(2) on trade usage] full recognition is thus available for new usages and for usages currently observed by the *great majority of decent dealers*, even though dissidents ready to cut corners do not agree.") (emphasis added).

of their investments. Trade usage could not provide any further detail, however, as it is highly unlikely that there are common salaries, durations, etc. among close corporation employment and management positions that would constitute evidence of trade usage. As a consequence, both breach and remedy determinations would be difficult to make.[185] Even if the pattern and conduct evidence used by oppression courts could be characterized as trade usage, therefore, it is unlikely that such a characterization would overcome the indefiniteness problems suggested by *Litle* and other decisions.[186]

ii. Course of Performance

A course of performance "involves conduct after the agreement has been made."[187] Like the pattern and conduct evidence of the shareholder oppression doctrine, course of performance evidence can establish general understandings between the shareholders (e.g., employment, management). Where a minority shareholder has worked for the company and served in a management role since investing, for example, such conduct could be characterized as course of performance evidence indicating that employment and management are terms of the investment bargain.

Moreover, and in contrast to trade usage, a course of performance between the shareholders can potentially fill in the details of a generic employment or management bargain. For example, assume that a minority shareholder receives a $50,000 salary along with health benefits as an employee of a close corporation. After three years of employment, the shareholder is unjustifiably terminated. In theory, the $50,000 compensation plus benefits over the prior three years may serve as course of performance evidence that provides the salary and benefit details of the employment arrangement. In addition, a court may consider the lengths of employment of other shareholders in the close corporation as course of performance evidence

[185] *See supra* notes 159–160 and accompanying text.

[186] In other words, even if close corporation pattern and conduct evidence was characterized as trade usage, it would only establish basic agreements, such as agreements for employment and management. Without further trade usage evidence to fill in the details of these agreements, the indefiniteness hurdle would probably not be overcome.

[187] Calamari & Perillo, *supra* note 127, § 3.17, at 161; *see also* U.C.C. § 2-208(1) (2000) ("Where the contract for sale involves repeated occasions for performance by either party with knowledge of the nature of the performance and opportunity for objection to it by the other, any course of performance accepted or acquiesced in without objection shall be relevant to determine the meaning of the agreement.").

that aids the inquiry into the employment term of the discharged shareholder.[188] As mentioned, these additional details are critically important to the calculation of termination-related damages.[189] As more details are filled in, of course, the likelihood diminishes that a court will refuse to enforce a purported contract on indefiniteness grounds.[190]

Courts may encounter difficulty, however, when attempting to combat indefiniteness through course of performance evidence. First, oppressive majority conduct may occur relatively soon after the minority's commitment of capital to the venture. Because of this short time frame, a court may conclude that the shareholders' actions have not persisted long enough to constitute an established course of performance.[191] Second, in some circumstances, there may be no established course of performance at all. For example, assume that a minority shareholder alleges that the majority's failure to declare dividends constitutes a breach of an implied-in-fact contract for reasonable dividends (a money-for-benefit conception).[192] If the close corporation has never declared a dividend in the past,[193] there is no

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[188] If other shareholders in the close corporation have been working for five years, in other words, perhaps a court will conclude that five years should be considered the employment term of the discharged stockholder (such that damages can be assessed on the notion that the shareholder was terminated two years early).

[189] *See supra* note 159–160 and accompanying text.

[190] *Cf.* CALAMARI & PERILLO, *supra* note 127, § 2.9, at 52 ("Indefiniteness ... can be cured by the subsequent conduct of the parties.").

[191] *Cf.* U.C.C. § 2-208(1) (2000) (stating that course of performance is based on "*repeated* occasions for performance") (emphasis added). This argument may also be applicable to a reasonable expectations inquiry under the shareholder oppression doctrine. For example, if a minority shareholder is removed from management after only one month of service, there may be insufficient specific evidence of "fitting within the pattern" to establish a reasonable expectation. Courts applying the shareholder oppression doctrine, however, may compensate for this paucity of specific evidence by relying on their understanding of the economics behind close corporation investing. *See supra* Part II(B) (discussing the economic rationale for close corporation investments); *cf. In re Topper*, 433 N.Y.S.2d at 361–62, 365–66 (finding that a minority shareholder's reasonable expectations were frustrated even though the minority was terminated from employment and removed as an officer within one year of investing). It is unclear whether courts applying contract law would rely on economics in a similar manner. *See infra* Part III(C).

[192] Alternatively, the minority shareholder's allegation of a failure to pay dividends could be conceptualized as an allegation that the majority shareholder has breached a term of the money-for-stock contract. *See supra* notes 136–139 and accompanying text.

[193] *See, e.g., Orchard*, 590 F. Supp. at 1552; W&W Equip. Co., Inc. v. Mink, 568 N.E.2d 564, 569 (Ind. Ct. App. 1991); Wilkes v. Springside Nursing Home, Inc., 353 N.E.2d 657, 662 n.13 (Mass. 1976); Struckhoff v. Echo Ridge Farm, Inc., 833 S.W.2d 463, 465 (Mo. Ct. App. 1992); *In re* O'Neill, 626 N.Y.S.2d 813, 814 (App. Div. 1995); *In re Topper*, 433 N.Y.S.2d at 362; Zidell v. Zidell, Inc., 560 P.2d 1086, 1088 (Or. 1977).

course of performance evidence for a court to rely on. Third and finally, the use of pure course of performance evidence may still be inadequate for a court wishing to calculate termination-related damages. Because shareholders of a particular close corporation may have very different jobs and levels of competence, a court may decide that the employment term for a discharged shareholder cannot be gleaned from the lengths of employment of other shareholders in the venture.[194] Thus, although courts applying contract law in a shareholder oppression context could use course of performance evidence to help alleviate indefiniteness questions, it is by no means certain that such evidence will protect oppressed minority shareholders in all situations.[195]

2. The Employment at Will Doctrine

Aside from indefiniteness issues, the employment at will doctrine also presents difficulties for courts attempting to use pattern and conduct evidence to establish an implied-in-fact contract for employment. In general, the at will rule "allows an employer to terminate an employee with or without just cause in the absence of an agreement limiting the employee's discharge to just cause or specifying the term of employment."[196] The conventional justification for the doctrine is

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[194] Similarly, if all employees of a close corporation are also founders of the business, their lengths of employment may be equivalent. In such circumstances, of course, there is no longer term of employment for a court to use.

[195] It is important to recall that the shareholder oppression doctrine does not face the same indefiniteness concerns that are confronted by traditional contract law. From a damages standpoint, it has previously been noted that the "fair value" buyout is not dependent on major terms such as employment and management. *See supra* notes 128–131 and accompanying text. Thus, the terms themselves can be much less definite. From a liability standpoint, the pattern and conduct evidence, as well as the economic rationale for close corporation investments, suggests that close corporation shareholders generally expect permanent and continuous employment and management participation. *See supra* Parts II(B)(1)-(2); *supra* notes 71–76 and accompanying text. Thus, almost any termination of employment or removal from management will trigger oppression liability. No further "definiteness" is required. *But see* Moll, *supra* note 18, at 800–01 (observing that terminations of employment or removals from management based upon shareholder misconduct or incompetence should not trigger oppression liability).

[196] Schlafge, *supra* note 115, at 1081; *see also* Burk v. K-Mart Corp., 770 P.2d 24, 26 (Okla. 1989) ("The classic statement of the at-will rule was that an employer may discharge an employee for good cause, for no cause or even for cause morally wrong, without being thereby guilty of legal wrong."); 1 ROTHSTEIN ET AL., *supra* note 121, § 1.4, at 13 ("The doctrine of employment at will prescribed that an employee without a contract for a fixed term could be hired or fired for any reason or no reason at all."); Frank J. Cavico, *Employment at Will and Public Policy*, 25 AKRON L. REV. 497, 498 (1992) (noting that in an at will employment arrangement, "the employer may discharge an employee or an employee may

that employers need unimpeded discretion to manage their businesses and to remain competitive.[197]

In many jurisdictions, there is a strong presumption in favor of an employment at will relationship.[198] Nevertheless, the at will doctrine can be circumvented by an express or implied agreement that employment will continue for some fixed period of time or that employment will not terminate without cause.[199] Before such an agreement is recognized, however, the employee must typically establish specific and definite language by the employer that conveys a promise of continued employment[200] rather than a "mere expression of optimistic hope for a long relationship."[201] Given that reasonable expecta-

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leave at any time, for any reason, without being liable thereby for any legal wrong"); Jay M. Feinman, *The Development of the Employment at Will Rule*, 20 AM. J. LEGAL HIST. 118, 118 (1976) ("In almost every jurisdiction in the United States an employer can discharge an employee without notice and without cause unless the duration of the employment relation is specified in an employment contract."); Cornelius J. Peck, *Penetrating Doctrinal Camouflage: Understanding the Development of the Law of Wrongful Discharge*, 66 WASH. L. REV. 719, 720 (1991) ("Pursuant to the [at-will] doctrine, an employer can discharge an employee for any cause, no cause, or bad cause without liability.").

Of course, if an individual is employed under a contract for a definite term, the employee "may not be fired before the expiration of the term except for cause (or material breach), unless the contract provides otherwise." 2 ROTHSTEIN ET AL., *supra* note 121, § 9.2, at 237.

[197] *See, e.g.*, Wagenseller v. Scottsdale Mem'l Hosp., 710 P.2d 1025, 1041 (Ariz. 1985) ("[W]e are concerned not to place undue restrictions on the employer's discretion in managing his workforce . . . ."); Hunt v. IBM Mid. Am. Employees Fed. Credit Union, 384 N.W.2d 853, 858–59 (Minn. 1986) ("Imposing a good faith duty to terminate would unduly restrict an employer's discretion in managing the workforce.") (internal quotation omitted); Michael D. Moberly, *Negligent Investigation: Arizona's Fourth Exception to the Employment-at-Will Rule?*, 27 ARIZ. ST. L.J. 993, 994 (1995) (noting that the employment at will doctrine is based upon the assumption that employers need "complete freedom of contract to conduct business and [to] promote industrial growth").

[198] *See, e.g.*, Priebe v. O'Malley, 623 N.E.2d 573, 576 (Ohio Ct. App. 1993).

[199] *See, e.g.*, *Pugh*, 171 Cal. Rptr. at 924; 1 ROTHSTEIN ET AL., *supra* note 121, § 2.27, at 135.

[200] *See* 2 ROTHSTEIN ET AL., *supra* note 121, § 9.4, 250–54 (discussing oral contracts and the need for the employer's language to be sufficiently clear and definite); *cf. Orchard*, 590 F. Supp. at 1556 ("One asserting an oral contract must show that the contract was clear and precise.").

[201] 2 ROTHSTEIN ET AL., *supra* note 121, § 9.4, at 251; *see, e.g.*, Kunz v. UFCW Local 876, 5 F.3d 1006, 1008, 1011 (6th Cir. 1993) (concluding that a union representative's assurance that a new union employee would have a job "for as long as [she] wanted it" was insufficient to overcome the at will rule); Ruud v. Great Plains Supply, Inc., 526 N.W.2d 369, 370, 372 (Minn. 1995) (concluding that statements such as "good employees are taken care of," even in the context of discussions about becoming a store manager, were not sufficiently definite to establish a contract of continued employment); Taylor v. Nat'l Life Ins. Co., 652 A.2d 466, 469, 473 (Vt. 1993) (concluding that statements such as a company was a "stable employer" and that if an employee "did [his] job . . . [he] could expect . . . to

tions of employment under the oppression doctrine are often established by the *conduct* of the shareholders, rather than by any express *language* of the majority,[202] this exception to the at will doctrine may be useless to the frozen-out minority shareholder.[203] Contrary to the shareholder oppression doctrine, in other words, the fact that a shareholder has worked at a company for some time does not prevent the majority investor, under the at will rule, from terminating the shareholder's employment.

Despite the heavy presumption in favor of the at will rule, there may be ways to overcome it in the context of shareholder oppression. First, some courts have found terms of an employment contract, especially terms that deal with job security, by relying on the conduct and dealings of the parties.[204] In these cases, however, and unlike the typical close corporation dispute, there is usually other evidence of an employment contract aside from the conduct of the parties themselves.[205] Second, because the capital provided by the close corporation shareholder can be viewed as consideration for a promise (e.g., a promise of continued employment),[206] courts may conclude that the

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stay there" merely expressed hope for a long-term relationship rather than creating an enforceable promise of lifetime employment).

[202] *See supra* notes 68–69 and accompanying text; *infra* note 215.

[203] In cases involving oral promises, the employee must also give independent consideration for the employer's promise of continued employment. *See* 2 ROTHSTEIN ET AL., *supra* note 121, § 9.4, at 533. In the close corporation context, of course, this independent consideration requirement is easily met as the minority investor contributes capital to the company. *See, e.g.*, Ingle v. Glamore Motor Sales, Inc., 535 N.E.2d 1311, 1321 (N.Y. 1989) (Hancock, J., dissenting) (observing that, for typical close corporation minority shareholders, "there is consideration which would support an implied understanding that, at least, the majority owner will not discharge him arbitrarily or in bad faith and without some legitimate business reason"); Gigax v. Repka, 615 N.E.2d 644, 650 (Ohio Ct. App. 1992) (Grady, J., concurring) ("I would hold that the $70,000 in equity contributions made to the corporation by Gigax constitute consideration for his employment in addition to the services he provided, taking the relationship outside the 'at-will' definition . . . ."); *see also Pugh*, 171 Cal. Rptr. at 925 ("[I]t is more probable that the parties intended a continuing relationship, with limitations upon the employer's dismissal authority, when the employee has provided some benefit to the employer, or suffers some detriment, beyond the usual rendition of service.").

[204] *See, e.g.*, *Pugh*, 171 Cal. Rptr. at 925–26. *See generally* 2 ROTHSTEIN ET AL., *supra* note 121, § 9.5, at 254–56 (describing contracts implied from conduct).

[205] *See, e.g.*, *Pugh*, 171 Cal. Rptr. at 927 (noting that the jury could have determined that an implied promise of employment existed based on "the duration of appellant's employment, the commendations and promotions he received, the apparent lack of any direct criticism of his work, the assurances he was given, and the employer's acknowledged policies").

[206] *See supra* note 203 and accompanying text (discussing consideration).

at will doctrine is inapplicable.[207] The provision of consideration, however, would not overcome any problems of indefiniteness associated with the alleged promise. Finally, although the employment at will doctrine refuses to recognize a protected *employment* interest in the job,[208] it could be argued that the recognition of an *investment* interest in the job falls outside of the legitimate coverage of the at will rule.[209] Because close corporation employment often serves as the vehicle for distributing the business returns,[210] and because the position itself has value that often motivates an investment decision,[211] a court could decide that close corporation shareholders do have an investment interest in their jobs that makes the at will doctrine inapplicable.[212] Whether such an argument will be accepted by courts applying contract law, however, is unclear, particularly in light of the reaffirmations of the at will rule that have occurred in several states.[213] As a consequence, under contract law, the at will doctrine will likely

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[207] *See, e.g.*, Toussaint v. Blue Cross & Blue Shield of Mich., 292 N.W.2d 880, 908–09 (Mich. 1980) (Ryan, J., dissenting) ("It is well settled that in the absence of distinguishing features or provisions, *or special consideration*, such contracts are generally regarded as indefinite hirings terminable at the will of either party.") (emphasis added) (citation omitted); Cornelius J. Peck, *Unjust Discharges from Employment: A Necessary Change in the Law*, 40 OHIO ST. L.J. 1, 1 (1979) (predicting that "American courts will abandon the principle that, *absent some consideration other than the services to be performed*, a contract of employment for an indefinite term is to be considered a contract terminable at will by either party ....") (emphasis added).

[208] *See* 1 ROTHSTEIN ET AL., *supra* note 121, § 1.4, at 9 (noting that the at will doctrine "provided that employees categorized as 'at will' had no legal interest in continuing job security").

[209] *See* Moll, *supra* note 78, at 536–39 (asserting that the at will doctrine covers termination-related harms suffered in an employee capacity but not termination-related harms suffered in a shareholder/investor capacity).

[210] *See supra* notes 37–38 and accompanying text.

[211] *See supra* notes 86–92 and accompanying text.

[212] *Cf.* Ragazzo, *supra* note 86, at 1110 (noting that "a shareholder in a closely held corporation often has a significant investment interest in his job").

[213] *See, e.g.*, Arizona Employment Protection Act of 1996, ARIZ. REV. STAT. ANN. §§ 12–541, 23–1501, 41–1461 (West Supp. 1996) (codifying the common-law employment at will rule, narrowing the public policy exception to employment at will, and limiting the nature and scope of claims and remedies available to discharged employees); Montgomery Cty. Hosp. Dist. v. Brown, 965 S.W.2d 501, 502 (Tex. 1998) (reaffirming the employment at will doctrine and concluding that oral assurances of job security fail to overcome the at will rule); *see also* Jenny Clevenger, Note, *Arizona's Employment Protection Act: Drawing a Line in the Sand Between the Court and the Legislature*, 29 ARIZ. ST. L.J. 605, 614 (1997) ("The effect of the [1996 Arizona Employment Protection Act], however, is to drastically curtail and, in some instances, to abrogate entirely, the right of employees to bring actions for wrongful termination.").

continue to present a significant obstacle when employment discharges are challenged.[214]

3. The Statute of Frauds

Because the expectations of close corporation shareholders are rarely committed to writing,[215] an implied-in-fact contract for employment, management, or dividends may be unenforceable due to the statute of frauds. The relevant portion of most state statutes of frauds provides that an agreement is void if its terms will not be performed within one year from the time the agreement is entered into, unless the agreement is in writing and is signed by the party to be charged.[216] As commentators have noted, "[t]he general effect of the

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[214] *See, e.g.*, *Orchard*, 590 F. Supp. at 1556, 1558 (rejecting a shareholder-employee's wrongful discharge claim by (1) noting that there was "no evidence of the existence of a contract for employment, oral or written," (2) stating that the "position as stockholder and officer of the corporation gave . . . no position of tenured employment," and (3) citing the at will doctrine); Harris v. Mardan Bus. Sys., Inc., 421 N.W.2d 350, 354 (Minn. Ct. App. 1988) (agreeing that a shareholder was employed at will and rejecting implied agreement and promissory estoppel claims); Landorf v. Glottstein, 500 N.Y.S.2d 494, 499 (Sup. Ct. 1986) (noting that a discharged shareholder was subject to termination without cause pursuant to the at will doctrine); *Priebe*, 623 N.E.2d at 576 (Ohio Ct. App. 1993) (rejecting a shareholder's claim that he had an implied employment contract with the corporation that overcame the at will doctrine).

[215] *See, e.g.*, 1 OPPRESSION, *supra* note 31, § 2:17, at 46 ("The litigated cases show that important arrangements among participants in small business enterprises are often oral and sometimes nothing more than vague understandings, never even definitely stated orally."); Chittur, *supra* note 135, at 160 (noting that the expectations of a close corporation shareholder "may not be articulated with lawyerly precision"); O'Neal, *supra* note 135, at 883–84 ("A person taking a minority position in a close corporation often leaves himself vulnerable to squeeze-out or oppression by failing to insist upon a shareholders' agreement or appropriate charter or bylaw provisions . . . ."); *id.* at 886 ("The participants typically enter into 'agreements' among themselves, which sometimes are reduced to writing in the form of a formal preincorporation agreement or a shareholders' agreement, but which often are oral, perhaps just vague and half-articulated understandings."); *see also* *Exadaktilos*, 400 A.2d at 561 (noting that "[t]he expectations of the parties in the instant suit with regard to their participation in corporate affairs are not established by any agreement"); Chittur, *supra* note 135, at 131 (observing that "people generally avoid complex and expensive planning in small businesses"); *id.* at 139 (stating that "inadequately planned close corporations will always remain part of the picture," and noting that "[t]he most careful plan may fail to visualize some conflicts, even if it does not generate novel ones of its own").

[216] *See, e.g.*, VA. CODE ANN. § 11–2(8) (Michie 2000) ("No action shall be brought . . . [u]pon any agreement that is not to be performed within a year . . . [u]nless the . . . contract . . . or some other memorandum or note thereof, be in writing and signed by the party to be charged thereby, or his agent."); 2 ROTHSTEIN ET AL., *supra* note 121, § 9.5, at 534 ("Statutes of frauds provide that agreements, promises, or undertakings are void if the terms of the agreement are not to be performed within one year from the time of making,

statute of frauds is to render void oral contracts for longer than one year."[217] In the close corporation context, of course, implied agreements are generally established by pattern, conduct, and economic evidence—not by written or even oral language. The statute of frauds, therefore, may pose an obstacle to protecting minority shareholders under contract law.

Many courts, however, construe the statute of frauds narrowly "by holding that the statute applies only to those contracts that, at the time of making, could not possibly or conceivably be completed within a year."[218] Under this logic, one could argue that an implied-in-fact contract for continuous employment and management between close corporation shareholders is capable of performance within one year. For example, during the relevant one-year period, it is possible for a shareholder to die or to quit his or her company employment.[219] Similarly, the close corporation may cease operations during the relevant one-year period.[220]

Significantly, however, not all courts have adopted such a narrow construction of the statute of frauds. Some courts have distinguished between performance of a contract within one year, and termination of a contract within one year. Whereas performance within a year satisfies the statute of frauds, termination within a year does not.[221] The Virginia decision of *Graham v. Central Fidelity Bank* nicely exemplifies this distinction.[222] In *Graham*, the plaintiff asserted that she had an oral contract for employment that was terminable only for cause.[223]

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unless the agreement is in writing and signed by the party to be sued."). Under this language, an agreement is *valid* if (1) its terms can be performed within one year from the time the agreement is entered into; *or* (2) the agreement is in writing and is signed by the party to be sued.

[217] 2 ROTHSTEIN ET AL., *supra* note 121, § 9.5, at 534.

[218] *Id.*

[219] *See, e.g.*, II FARNSWORTH, *supra* note 119, § 6.4, at 129–30 (noting that "a growing number of courts [are] coming to regard a contract as not within the statute if one, or sometimes both, parties can terminate it within a year of its making"); 2 ROTHSTEIN ET AL., *supra* note 121, § 9.5, at 534; *see also* Taylor v. Canteen Corp., 69 F.3d 773, 785 (7th Cir. 1995) (stating that "where . . . promise of employment is cast in terms of lasting as long as the employee wants the job, the promise is capable of performance within one year"); Foley v. Interactive Data Corp., 765 P.2d 373, 382 (Cal. 1988) ("Because the employee can quit or the employer can discharge for cause, even an agreement that strictly defines appropriate grounds for discharge can be completely performed within one year—or within one day for that matter.").

[220] *See, e.g.*, 2 ROTHSTEIN ET AL., *supra* note 121, § 9.5, at 534.

[221] *See* 2 *id.*

[222] *See* 428 S.E.2d 916 (Va. 1993).

[223] *See id.* at 917–18.

According to the plaintiff, such a contract satisfied the statute of frauds because of the possibility that the plaintiff's poor performance would result in termination for cause within the first year of the contract.[224] The Virginia Supreme Court disagreed, as it observed that a discharge for cause was not a *performance* of the contract that would satisfy the statute of frauds; rather, a discharge for cause was a *termination* of the contract due to the plaintiff's breach.[225] The court concluded that the possibility of termination within a year did not satisfy Virginia's statute of frauds and, as a consequence, the contract for employment was unenforceable.[226] Depending on the jurisdiction, therefore, it may be fruitless to argue that the statute of frauds is satisfied because of the possibility of a shareholder dying or quitting within a year, or because of the potential failure of the business within a year. Courts may characterize these contingencies as "terminating" the contract rather than as completing the "performance" of the contract.

4. Summary

In combination, the indefiniteness of the close corporation bargain, the doctrine of at will employment, and the application of the statute of frauds will likely prevent a contracts court from using pattern and conduct evidence to establish protective implied-in-fact contracts for the minority shareholder. In theory, however, indefiniteness could be combated through an expansive view of trade usage and course of performance, the at will doctrine could be overcome through conduct evidence or scope arguments, and the statute of

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[224] *See id.* at 918 ("Graham argues, however, that certain contract provisions, viz., the maximum allowed amounts of total outages within any 90-day period and the probationary periods of 90 days after certain excess total outages, indicate that she could have performed her contract within one year."); *supra* note 219 and accompanying text (citing language from *Foley*).

[225] *See Graham*, 428 S.E.2d at 918 ("[A] discharge for cause is not a *performance* of the contract within the meaning of the statute of frauds, but a *termination* of the contract by reason of its breach.").

[226] *See id.* ("Because the possibility of a termination of such a contract for cause within its first year of performance does not remove it from the requirements of the statute of frauds, we conclude that the oral assurances alleged by Graham cannot be considered in deciding whether she had an employment contract that could be terminated only for cause.") (citation omitted). *But see* Floors Unlimited v. Fieldcrest Cannon, 55 F.3d 181, 186 (5th Cir. 1995) ("Texas courts would conclude that a contract for an indefinite duration, terminable only for cause, falls outside the statute of frauds."); II FARNSWORTH, *supra* note 119, § 6.4, at 128 (describing the distinction between contract performance and contract excuse/termination as "fine and often tenuous"); *supra* note 219.

frauds could be satisfied through a characterization of contingencies as contract "performance." Contract law, in other words, possesses the tools to combat the indefiniteness, employment at will, and statute of frauds hurdles. For those tools to be effective in protecting minority shareholders, however, they must be used in an expansive manner that, for the most part, goes beyond conventional applications.

C. *The Uncertain Role of Economic Understandings*

As mentioned, courts applying the shareholder oppression doctrine seem to consider the economic rationale for investing in close corporations as part of their reasonable expectations analysis.[227] It is unclear, however, whether courts applying contract law would follow a similar approach as part of their implied-in-fact contract determination. Judicial opinions often observe, for example, that "courts do not make contracts for parties."[228] Similarly, in some instances, courts rejecting a particular interpretation or refusing to imply a term explain that doing otherwise would constitute an impermissible "rewriting" of the contract.[229] The worry created by these statements, of course, is that courts will overuse them and will effectively avoid a deeper contractual analysis. In addressing shareholder oppression issues, for example, there is some concern that contracts courts may be hesitant to consider the economics behind close corporation investments when the shareholders have not clearly and specifically expressed their obligations among themselves. Using such economic considerations may

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[227] *See supra* Part II(B).

[228] *In re* Jack-Rich, Inc., 176 B.R. 476, 480 (C.D. Ill. 1994); *see also Pyeatte*, 661 P.2d at 201 ("The court's function . . . cannot be that of contract maker. Nor can the court create a contract simply to accomplish a purportedly good purpose."); *Jaffe Commercial*, 456 N.E.2d at 229 (noting the trial court's observation that the parties "cannot expect the Court to find for you a contract that you didn't take the time yourselves to memorialize"); 5 MARGARET N. KNIFFIN, CORBIN ON CONTRACTS § 24.19, at 184–85 (rev. ed. 1998) (citing cases).

[229] 5 KNIFFIN, *supra* note 228, § 24.19, at 184–85 (citing cases); *see Neely*, 757 F.2d at 628 ("Courts refuse to enforce agreements that contain indefinite promises or terms they deem essential precisely because judicial clarification of the uncertainty entails great danger of creating intentions and expectations that the parties themselves never entertained."); Daniels v. Thomas, Dean & Hoskins, Inc., 804 P.2d 359, 364 (Mont. 1990) (noting that "[e]quity can enforce provisions of contracts but it cannot supply them") (internal quotation omitted); *cf.* Metro. Life Ins. Co. v. RJR Nabisco, Inc., 716 F. Supp. 1504, 1519 (S.D.N.Y. 1989) ("These plaintiffs do not invoke an implied covenant of good faith to protect a legitimate, mutually contemplated benefit of the indentures; rather, they seek to have this Court create an additional benefit for which they did not bargain.").

be viewed as an impermissible "rewriting" of the contract between the parties.

Despite these concerns, at least some courts applying a contract analysis do rely on an economic understanding of the particular deal at issue as part of their contract interpretation or enforcement inquiries. For example, in *Stoumbos v. Kilimnik*, Kilimnik sold a business to AAM on May 1, 1982 and retained a security interest in AAM's "inventory and equipment" to secure the payment of the price.[230] The Ninth Circuit attempted to determine whether the collateral description of "inventory and equipment" in the security agreement—i.e., in the contract[231]—was meant to encompass inventory and equipment acquired by AAM *after* the May 1, 1982 sale of the business. In concluding that the contractual terms "inventory and equipment" were meant to include after-acquired inventory but not after-acquired equipment, the court explicitly looked to the economic rationale underlying the contract for security. As the court noted:

> There is substantial support for the proposition that, where a financing statement or security agreement provides for a security interest in "all inventory" (or uses similar broad language), the document incorporates after-acquired inventory. *The rationale is that inventory is constantly turning over, and no creditor could reasonably agree to be secured by an asset that would vanish in a short time in the normal course of business . . . . In addition, the rationale of the "automatic" security interest cases does not apply to after-acquired equipment. Those cases discuss cyclically depleted and replenished assets such as inventory or accounts receivable. Unlike inventory, equipment is not normally subject to frequent turnover* . . . . Kilimnik would not have had a clear reason to want after-acquired equipment covered by the purchase agreement . . . . Even if limited to the equipment on hand at the time of the sale, his interest would have been secure.[232]

Stoumbos is significant because the parties did not expressly manifest an intention to cover after-acquired inventory or equipment in their contract. Nevertheless, due to the court's understanding of the economics of the deal, the court effectively concluded that the parties

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[230] *See* 988 F.2d 949, 953 (9th Cir. 1993).

[231] *See, e.g.*, Whirlpool Corp. v. Dailey Constr., Inc., 429 S.E.2d 748, 751 (N.C. Ct. App. 1993) (noting that a security agreement "is essentially a contract between the creditor and the debtor").

[232] *Stoumbos*, 988 F.2d at 954–56 (emphasis added).

must have intended such a result (at least with respect to inventory).[233] Although there was no explicit evidence that the parties actually discussed the after-acquired inventory issue or reached a "meeting of the minds" on it, the court, by considering the parties' economic motivations for entering into the contract, proceeded as if explicit evidence of a mutual understanding (i.e., an after-acquired inventory understanding) existed.[234] This approach, of course, is quite similar to the reasonable expectations analysis of oppression law. Although explicit evidence of a mutual employment and management understanding is generally absent, oppression courts often find such an understanding (i.e., a reasonable expectation) based, at least in part, on the economic importance of a job and a management position to the rational close corporation investor.[235] Just as the *Stoumbos* court used its economic understanding to conclude that an after-acquired inventory term was part of the contract between the parties,[236] so too does an oppression court typically use its economic un-

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[233] *See id.*; *see also In re* Page, 16 U.C.C. Rep. Serv. 501, 504 (M.D. Fla. 1974) ("Needless to say, any reasonable secured party would be fully aware that this type of business presupposes a constant change in the inventory. Therefore, it is obviously unreasonable to assume that anyone would have received or acquired or intended to acquire a security interest in an inventory with the rigid limitation that it should be limited to the same items which made up the inventory on the date the document was executed.").

[234] Similarly, based on its economic understanding of the parties' contract, the *Stoumbos* court concluded that after-acquired equipment was not intended to be covered. *See Stoumbos*, 988 F.2d at 954–56. The court understood that the need for security was Kilimnik's economic motivation for taking a security interest in AAM's inventory and equipment. *See id.* More importantly, however, the court understood that Kilimnik's need for security would be satisfied without an after-acquired equipment clause because of equipment's static nature (as opposed to inventory's "turnover" nature). *See id.* In short, the *Stoumbos* court used its economic understanding of the deal to ascertain the terms that the parties, as rational actors, must have agreed to. *See id.*

[235] *See supra* Part II(B); *supra* notes 66–68 and accompanying text.

[236] It should be noted that other courts have also used their economic understanding of the deal to assist in contract interpretation. In *Whirlpool Corp. v. Dailey Construction, Inc.*, 429 S.E.2d 748 (N.C. Ct. App. 1993), for example, the North Carolina Court of Appeals attempted to determine whether Whirlpool, the secured creditor, had authorized the sale of its collateral—kitchen appliances. *See id.* at 750. By relying on its economic understanding of the arrangement, the *Whirlpool* court concluded that Whirlpool had given such authorization:

> Both Braehill and First Union claim that Whirlpool expressly consented to the transfer of the appliances by the specific language used in the security agreement .... A fair reading ... leaves no doubt that both Whirlpool and Dailey Construction knew that the appliances were to be incorporated into the ... [a]partment project and then resold as part of the project. It is clear that Whirlpool, if not expressly, then at least impliedly consented to the resale. Such a result is mandated not only by the terms of the security agree-

derstanding to conclude that employment and management "terms" are part of the investment contract in a close corporation.[237]

> ment, *but also by logic because unless the appliances were resold as part of the apartment project, Dailey Construction did not stand to profit from the project and would have been unable to repay Whirlpool* . . . .

Id. at 751 (emphasis added). Similarly, in *Cooley v. Big Horn Harvestore Sys., Inc.*, 813 P.2d 736 (Colo. 1991), the Supreme Court of Colorado relied on its economic understanding of the purchase contract at issue in concluding that consequential damages were still available despite the presence of an exclusive remedy provision in the contract:

> [T]he decision of contracting parties to limit potential remedies to the single remedy to repair or replace defective parts is based on a number of assumptions which, if unfounded, fundamentally change the parties' intended allocation of risk. These include the assumptions that the seller will diligently and in good faith attempt to repair, that the seller will be able to effect repairs within a reasonable time period, and that any consequential loss sustained during the period of repair will be minimal. *Under the rationale of these cases, a loss that is itself caused by the failure of the remedy of suit for breach of a warranty to repair or replace defective parts could not be within the contemplation of the parties, and therefore should not be prohibited when such bargained-for remedy fails of its essential purpose.* A buyer reasonably expecting to avoid significant consequential loss through the effective use of such remedy should not be required to absorb such loss when the remedy fails of its essential purpose . . . . *To the extent the parties here agreed to limit the availability of consequential damages as a remedy, they did so on the assumption that the limited warranty to repair or replace would suffice to protect the plaintiffs from substantial consequential damage losses. The total inadequacy of that warranty was neither foreseen nor bargained for.*

Id. at 746–48 (emphasis added) (citations omitted).

[237] *See supra* Part II(B). The "economic understanding" discussion in the text reflects many of the themes that underlie the contract doctrine of frustration of purpose. Such a claim typically requires proof of the following three elements:

> First, the purpose that is frustrated must have been a principal purpose of that party in making the contract . . . . The object must be so completely the basis of the contract that, as both parties understand, without it the transaction would make little sense. Second, the frustration must be substantial. It is not enough that the transaction has become less profitable for the affected party or even that he will sustain a loss. The frustration must be so severe that it is not fairly to be regarded as within the risks that he assumed under the contract. Third, the non-occurrence of the frustrating event must have been a basic assumption on which the contract was made.

Restatement (Second) of Contracts § 265 cmt. a (1981). Once again, given the economic importance of a job and a management position to the rational close corporation investor, *see supra* Part II(B), a termination of employment or a removal from management may satisfy the frustration of purpose requirements. A finding of frustration of purpose, however, "has been limited to instances where a virtually cataclysmic, wholly unforeseeable event renders the contract valueless to one party." United States v. General Douglas MacArthur Senior Vill., Inc., 508 F.2d 377, 381 (2d Cir. 1974); *see also* VJK Prods., Inc., v. Friedman/Meyer Prods., Inc., 565 F. Supp. 916, 921 (S.D.N.Y. 1983) ("[T]he frustration of purpose defense is not available where . . . the event which allegedly frustrated the purpose of the contract . . . was clearly foreseeable.") (citation omitted). Like the economic

By giving weight to the economic rationale underlying a reasonable actor's decision to enter into a particular contract, some contract law decisions have moved beyond maxims and have effectively functioned similarly to oppression law. In protecting reasonable expectations, however, the shareholder oppression doctrine relies only partially on the economic rationale underlying a shareholder's decision to invest in a close corporation. As mentioned, the oppression doctrine also uses pattern and conduct evidence, as well as the buyout remedy, to accomplish its protective goal.[238] Of course, contract law faces indefiniteness, employment at will, and statute of frauds hurdles in handling the pattern and conduct aspect of the oppression analysis. Moreover, as will be explained, there are difficulties in using traditional contract remedies to replicate a buyout. Thus, although there is some precedent suggesting that conventional contract law may have the ability to handle the "economics" component of the oppression analysis, contract law's effectiveness in protecting reasonable expectations is still suspect.

D. *The Remedies for Breach of Contract*

1. Overview

In general, when a contract has been breached, the available legal remedies seek to "restore [the aggrieved party] to the position it would have been in had the contract been performed."[239] Modern courts and commentators capture this standard by articulating three legally protected interests of a contracting party—a restitution inter-

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understanding discussion, therefore, it is unclear whether a frustration of purpose argument would prevail. After all, a court may determine that reasonable close corporation investors who serve as company employees and managers should foresee, at a minimum, that the majority may decide to terminate employees and/or remove managers in various situations (e.g., economic recession, company downsizing, shareholder misconduct).

[238] *See supra* Part II (describing how the oppression doctrine establishes and protects reasonable expectations).

[239] Interceramic, Inc. v. S. Orient R.R. Co., 999 S.W.2d 920, 927 (Tex. Ct. App. 1999); *see also* III FARNSWORTH, *supra* note 119, § 12.1, at 147 (noting that ordinarily "courts encourage promisees to rely on promises" by "attempting to put that party in as good a position as it would have been in had the contract been performed, that is, had there been no breach"); U.C.C. § 1-106(1) (2000) ("The remedies provided by this Act shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed . . . ."). It is worth noting that the expectation interest is often described as giving the plaintiff the "benefit of the bargain." III FARNSWORTH, *supra* note 119, § 12.1, at 147.

est, a reliance interest, and an expectation interest.[240] In defining these three interests, commentators have stated that the restitution interest "represents the benefits conferred upon the other party,"[241] the reliance interest "represents the detriment [the contracting party] incurred by changing position,"[242] and the expectation interest "represents the prospect of gain from the contract."[243] This more nuanced articulation of contract damages does not conflict with the general standard of placing the aggrieved party in the economic position that would have resulted from performance. Rather, the more nuanced articulation "merely represents a different breakdown of the same economic harm suffered."[244] As commentators have explained:

> Our legal system starts with the premise that the expectation interest of contracting parties deserves protection. In order to protect it to the fullest, that is, in order to put the aggrieved party in the same economic position he would have attained upon full performance of the contract, the restitution and reliance interests need to be protected as well.[245]

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[240] *See, e.g.*, III FARNSWORTH, *supra* note 119, § 12.1, at 147–48, 151–53; *see also* L.L. Fuller & William R. Perdue, Jr., *The Reliance Interest in Contract Damages (Parts I and II)*, 46 YALE L.J. 52, 53–57 (1936–37) (describing the restitution interest, the reliance interest, and the expectation interest).

[241] CALAMARI & PERILLO, *supra* note 127, § 14.4, at 545; *see* Castle v. United States, 48 Fed. Cl. 187, 200 (2000) (defining the restitution interest as "the value of the benefit conferred on the breaching party"); *see also* CALAMARI & PERILLO, *supra* note 127, § 15.2, at 600 ("'Restitution' has a very flexible meaning. It encompasses recovery in quasi contract in which form of action the plaintiff recovers a money judgment. It is also used to encompass equitable remedies for specific relief such as decrees which cancel deeds, or impose constructive trusts or equitable liens, as well as some recoveries in equity for sums of money . . . . The common thread which draws these actions together is that 'one person is accountable to another on the ground that otherwise he would unjustly benefit or the other would unjustly suffer loss.'") (citations omitted) (footnotes omitted); *id.* § 15.1, at 599 ("[T]he aim of restitution is to place both of the parties in the position they had prior to entering into the transaction."); III FARNSWORTH, *supra* note 119, § 12.1, at 152 ("The party in breach is required to disgorge what that party has received in money or services by, for example, returning the benefit to the injured party that conferred it."); *id.* ("The focus [of restitution] is on the party in breach rather than on the injured party, and the attempt is to put the party in breach back in the position in which that party would have been had the contract not been made."); *id.* § 12.19, at 321 (observing that courts "sometimes refer to the injured party's [restitution] remedy . . . as based on 'rescission' (i.e., avoidance) of the contract").

[242] CALAMARI & PERILLO, *supra* note 127, § 14.4, at 545.

[243] *Id.*

[244] *Id.*

[245] *Id.*; *see id.* § 15.7, at 609 ("It should carefully be noted, however, that in an award for damages, the plaintiff's restitutionary interest is usually protected. The plaintiff is entitled

Thus, legal remedies for breach of contract center around the expectation interest—i.e., putting the aggrieved party in the same economic position as if full performance had occurred. At times, however, damages for the expectation interest are unavailable due to a lack of credible evidence or for policy reasons.[246] When these situations arise, the injured party can often recover based on one or both of the other interests.[247]

Aside from legal remedies, the courts are also empowered to grant equitable relief for breach of contract in certain circumstances. The principal equitable remedy to enforce a contract "is an order requiring specific performance of the contract . . . ."[248] A specific performance order often "take[s] the form of a decree ordering a party affirmatively to carry out contractual duties or enjoining the party

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to losses sustained (benefits conferred on the other and reliance expenditures) as well as gains prevented."); *see* III FARNSWORTH, *supra* note 119, § 12.1; at 152 (noting that reliance damages are "a lesser included component" of expectation damages); *id.* § 12.16, at 277 (suggesting that the "cost of reliance" may be "an appreciable part of the expectation interest"). Professors Calamari and Perillo provide the following example:

> P contracts to purchase Blackacre from V for $100,000, subject to obtaining a mortgage loan, paying V $10,000 as a down payment on contracting. An appraisal commissioned by P's bank shows that Blackacre has a market value of $120,000. Upon learning of the appraisal, V repudiates. Prior to repudiation, P expended $500 for a survey of Blackacre and $500 for banking fees for his loan application, and, as was foreseen by V, $1,000 for an option to purchase adjoining land which he intended to use to provide additional parking for the structure on Blackacre. P's expectancy of profit is $20,000. His restitution interest is the $10,000 down payment. His reliance interest is $2,000. His recovery will be $31,000, his expectancy and restitution interests and that part of his reliance interest (the option money) that would not have to be expended toward earning his expectancy.

CALAMARI & PERILLO, *supra* note 127, § 14.4, at 545; *see also* Avila v. Gonzalez, 974 S.W.2d 237, 247 (Tex. Ct. App. 1998) ("Damages for breach of contract protect three interests: a restitution interest, a reliance interest, and an expectation interest. In order to put the aggrieved party in the same position he or she would occupy if the other party had fully performed, each of these interests must be protected.") (citation omitted).

[246] *See, e.g.*, ATACS Corp. v. Trans World Communications, Inc., 155 F.3d 659, 669 (3d Cir. 1998) (noting that in some breach of contract cases, "recovery based on traditional notions of expectation damages is clouded because of the uncertainty in measuring the loss in value to the aggrieved contracting party"); III FARNSWORTH, *supra* note 119, § 12.1, at 152 ("Situations in which damages have been measured by the reliance interest have characteristically been those in which damages measured by the full expectation are for some reason regarded as inappropriate . . . .").

[247] *See, e.g.*, *ATACS*, 155 F.3d at 669 (noting that "where a court cannot measure lost profits with certainty," reliance and restitution damages are available).

[248] III FARNSWORTH, *supra* note 119, § 12.2, at 154.

from acting where the contract requires forbearance."[249] Instead of ordering specific performance, of course, a court may also use an injunction to "direct a party to refrain from doing a specified act."[250] These equitable remedies are typically available, however, only when monetary damages are inadequate.[251]

2. Approximating the Buyout

As previously discussed, the buyout remedy has a number of advantages in the oppression context. It provides a "market" for the oppressed investor's holdings; it creates an equitable parting between the shareholders; and it eliminates the necessity to articulate the shareholders' bargain with precision.[252] Given these advantages, it is important to ask whether contract law could provide similar relief to the oppressed close corporation shareholder.

Initially, it is helpful to deconstruct the buyout remedy into its primary elements. In a freeze-out situation where the minority is terminated from employment, removed from management, and excluded from dividends, a buyout award is generally comprised of a return of the shareholder's original investment as well as a return of the appreciation or depreciation on the original investment.[253] Such

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[249] CALAMARI & PERILLO, *supra* note 127, § 16.1, at 612; *see also* III FARNSWORTH, *supra* note 119, § 12.5, at 165 ("The most direct form of equitable relief for breach of contract is specific performance. By ordering the promisor to render the promised performance, the court attempts to produce, as nearly as is practicable, the same effect as if the contract had been performed.").

[250] III FARNSWORTH, *supra* note 119, § 12.5, at 166. Of course, "[i]f the performance due under the contract consists simply of forbearance, the effect of an injunction is to order specific performance." III *Id.*

[251] *See, e.g.*, III *id.* § 12.5, at 170 ("[I]t came to be recognized that equitable relief would not be granted if the legal remedy of damages was adequate to protect the injured party. This historical limitation has persisted in spite of the merger of law and equity."); III *id.* § 12.5, at 167 ("A court will not, however, grant an injunction unless the remedy in damages would be inadequate."). *But see* III *id.* § 12.6, at 171 ("The tendency is, however, to liberalize the granting of specific performance and injunction by enlarging the classes of cases in which damages are regarded as an inadequate remedy .... The concept of adequacy has thus tended to become relative, and the comparison more often leads to granting equitable relief than was historically the case.").

[252] *See supra* Part II(C) (describing the advantages of the buyout remedy).

[253] *Cf.* 2 OPPRESSION, *supra* note 31, § 10:09, at 60 ("The buy-out feature in these statutes is desirable because it permits shareholders who want to preserve the enterprise as a going concern to buy out dissenters, and at the same time it provides an oppressed shareholder a fair price for his holdings."); Schlafge, *supra* note 115, at 1080 n.46 ("[T]he buyout is the preferred remedy for shareholder disputes because it allows a return of the shareholder's capital while not crippling the business."); *infra* note 254 and accompanying text.

returns stem directly from the fact that the buyout awards the aggrieved shareholder an amount equal to his or her proportional share of the corporation's fair value.[254] A corresponding result of the buyout award, of course, is that the aggrieved investor relinquishes his or her stock (and thereby his or her shareholder status) in the company.[255]

Explained in contract terminology, the buyout remedy seems to function as a hybrid of restitution and expectation awards. The return of the shareholder's original investment, for example, reflects a restitution award to the extent that the "benefit conferred" upon the majority shareholder—i.e., the initial investment capital—is repaid to the oppressed minority shareholder.[256] Compensation for the investment's appreciation or depreciation, however, suggests an expectation award. After all, a money-for-stock conceptualization of the invest-

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[254] *See, e.g., supra* notes 109–110 and accompanying text (observing that the buyout awards the "fair value" of an investor's holdings). For example, assume that a minority shareholder invests $10,000 at the company's inception and receives a 33% ownership stake in return. Ten years later, the minority shareholder is unlawfully frozen-out of the company. Based on an earnings-based valuation of the company, a court concludes that the "fair value" of the business is $300,000. Because the minority investor is a 33% shareholder, the court orders the majority to purchase the minority's holdings for $100,000. In effect, this $100,000 award reflects a return of the minority's $10,000 investment coupled with $90,000 of appreciation on that investment.

[255] In other words, because the minority's stockholdings are purchased in a buyout, the minority investor is no longer a shareholder in the corporation. *See also infra* note 256 (explaining that a buyout award will require the aggrieved shareholder to relinquish his or her stock certificate(s) to the corporation).

[256] *See* III FARNSWORTH, *supra* note 119, § 12.20, at 325 (observing that, in a restitution analysis, the "benefit conferred on the party in breach [can] consist simply of the payment of money"); *id.* at 326 ("The policy favoring restitution is reinforced by the practical convenience to the court of allowing recovery of the very sum of money paid . . . .").

Of course, in a restitution action, the aggrieved party also returns what he or she has received in the transaction. *See, e.g.*, RESTATEMENT (SECOND) OF TORTS § 552C cmt. f ("In the traditional restitution action, the plaintiff returns what he has received in the transaction, and recovers what he has parted with, so that he is in effect restored to the pecuniary position in which he stood before the transaction."); MURRAY, *supra* note 156, § 126, at 726 ("Since the purpose of restitution is to restore the parties to status quo, if the party seeking restitution has received a benefit, he must return it or offer to return it, conditional on any restitution to himself."). This proposition supports the notion that an oppressed minority shareholder will be required to relinquish his or her stock certificate(s) to the corporation as a condition of the buyout award. *Cf.* Bernstein v. Nemeyer, 570 A.2d 164, 169 (Conn. 1990) ("[I]t is a condition of rescission and restitution that the plaintiff offer, as nearly as possible, to place the other party in the same situation that existed prior to the execution of the contract."); Sneed v. State, 683 P.2d 525, 528 (Okla. 1983) (observing that a "willingness . . . to restore the opposite party to the status quo is a condition precedent" to restitution). In effect, therefore, the pre-contract position will be restored—i.e., the corporation (or the majority shareholder) will return the minority's investment, and the minority investor will relinquish his or her "shareholder" status in the corporation.

ment contract between close corporation shareholders involves an exchange of investment capital for a stock certificate with accompanying terms such as the rights to employment, management, and appreciation/dividends.[257] When the majority's oppressive actions breach these contractual terms, an expectation-oriented remedy would attempt to provide the aggrieved shareholder with the economic value of the breached terms (e.g., the value of a lost job, a lost management position, diverted dividends, and/or captured appreciation).[258] Although the conventional buyout remedy does not award damages for a lost job, a lost management position, or any diverted dividends,[259] it does compensate for any appreciation (or depreciation) on the oppressed shareholder's investment.[260] Compensation for the investment's appreciation or depreciation, therefore, does resemble a partial award of expectation damages to the extent that it attempts to put the minority shareholder in an economic position similar to if the appreciation "term" of the investment contract had not been breached.

In short, the buyout remedy functions as a combination of restitution and expectation awards to the extent that it returns the minority's investment capital to him or her as well as the appreciation or depreciation on that investment. Because the buyout remedy can be deconstructed into these restitution and expectation components, it

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[257] *See supra* notes 136–139 and accompanying text.

[258] Indeed, expectation damages seek to put the aggrieved party in the same economic position as if the contract had been performed—i.e., as if the majority shareholder had *not* breached the contractual terms by committing oppressive acts.

[259] *See* Bahls, *supra* note 21, at 298–99 (observing that "[a]warding the fair market value of a shareholder's interest does not compensate for the loss of an expectation of a voice in management" because "[p]roblems inherent in quantifying the value of this expectation to intangible amenities often preclude the court from awarding any value for loss of the expectation"); Moll, *supra* note 78, at 568–80 (explaining that a conventional earnings-based buyout fails to compensate the oppressed shareholder for the employment and management aspects of his or her investment); Murdock, *supra* note 39, at 472 (calculating the losses of a shareholder-employee who earned $250,000 per year in salary before termination and $100,000 per year in salary after termination, and implying that a standard buyout is not entirely satisfactory because it does not compensate for this loss); *see also* McCauley v. Tom McCauley & Son, Inc., 724 P.2d 232, 240–42 (N.M. Ct. App. 1982) (noting that the controlling shareholder received a dividend that was "ten (10) times greater than the amount declared but not paid to [a minority shareholder]," but affirming the trial court's "fair value" determination that did not include compensation to the minority investor for the disproportionate dividend); *cf. In re* Kemp & Beatley, Inc., 473 N.E.2d 1173, 1175–76, 1180–81 (N.Y. 1984) (affirming an award of dissolution in favor of two minority shareholders who were excluded from the company's de facto dividends, but failing to award back compensation to the two minority shareholders for the de facto dividends that they never received).

[260] *See supra* notes 253–254 and accompanying text.

seems theoretically possible for contract law to award a buyout-equivalent remedy. Once again, however, limitations that are well-ingrained in contract law may prevent such a result.

3. The Limitations of Contractual Remedies in an Oppression Context

a. *The Inadequacy of Restitution Damages*

If an oppressed close corporation shareholder pursues restitution damages,[261] a court applying contract law would have difficulty providing a buyout-equivalent remedy. Indeed, a restitutionary recovery is unlikely to include compensation for the expectation component of appreciation or depreciation;[262] instead, a court would likely award damages to the oppressed shareholder equivalent to the amount of the shareholder's original investment in the company.[263] After all, if a founding minority shareholder invested $30,000 at the inception of the venture, that $30,000 investment is arguably the "benefit conferred" upon the majority shareholder, as the majority effectively controls how that money is used. Prior to entering into the close corporation, in other words, the minority shareholder had $30,000 in available funds; thus, returning that $30,000 (adjusted for interest) would restore this initial economic position. Simply put, to the extent that "[t]he basic aim of restitution is to place the plaintiff in the same economic position as the plaintiff enjoyed prior to contracting,"[264]

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[261] As a general rule, a plaintiff in a breach of contract action may not recover both restitution and expectation damages; instead, an election of remedies is typically required. *See* CALAMARI & PERILLO, *supra* note 127, § 15.7, at 657 ("As a general rule a plaintiff may not have both restitution and damages for breach of contract."); III FARNSWORTH, *supra* note 119, § 12.19, at 320 (observing that restitution "is generally regarded as inconsistent with relief based on the contract itself").

[262] In a restitution action, the common law usually offers no protection to the plaintiff's expectation interest. *See* CALAMARI & PERILLO, *supra* note 127, § 15.7, at 609; *supra* note 261. As commentators have observed, "[i]f defective machinery were delivered and the buyer elected to return the machinery, the buyer was entitled to restitution of payments made and often certain reliance expenditures, but received no compensation for any additional cost of replacing the machinery." CALAMARI & PERILLO, *supra* note 127, § 15.7, at 609.

[263] *Cf.* III FARNSWORTH, *supra* note 119, § 12.19, at 319 (stating that restitution is "[s]ometimes . . . accomplished by requiring the party in breach to return the very benefit received and sometimes *by requiring that party instead to pay a sum of money that represents the value of that benefit*") (emphasis added).

[264] CALAMARI & PERILLO, *supra* note 127, § 15.4, at 603; *see also* III FARNSWORTH, *supra* note 119, § 12.20, at 324 ("Restitution as a remedy for breach of contract is limited to

compensation for appreciation or depreciation on the investment does not seem necessary. A mere $30,000 award (plus some market rate of interest) would probably accomplish this aim.[265]

Moreover, under mainstream contract doctrine, restitution is only available in the event of a total breach of contract.[266] If the close corporation investment contract is conceptualized as money-for-stock with accompanying employment, management, and other terms, this common-law restriction may prevent contract remedies from approximating the restitutionary aspect of the buyout remedy. For example, assume that a close corporation stockholder was unjustifiably terminated from employment but retained a management position and continued to receive a proportionate share of dividends. As a consequence, assume that the shareholder's reasonable expectation of employment was the only expectation that was frustrated by the majority's actions. In this partial freeze-out situation, a court applying contract law would have difficulty awarding restitution damages. While some of the terms of the contract have been breached (i.e., employment), other terms have been followed (i.e., management,

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benefits that are regarded as having somehow flowed from the injured party, a party that can be said to have 'lost' something that the party in breach is being asked to 'restore.'").

[265] Although it is likely a stretch, one could argue that a return of appreciation or depreciation on the original investment should be part of a restitution recovery. Given that a restitution award will require the oppressed investor to relinquish his or her rights as a shareholder, *see supra* notes 255–256 and accompanying text, such an award is probably the stockholder's last chance to recover an increase in the value of his or her investment. Courts recognizing this fact may lean towards providing a broader restitution award—i.e., one that includes appreciation or depreciation.

In addition, restitution damages are based on the "reasonable value" of the benefit conferred. CALAMARI & PERILLO, *supra* note 127, § 15.4, at 603. "Reasonable value," of course, is not a far cry from "fair value," so perhaps a contracts court would award the appreciated value of the investment as restitution damages. Of course, the "benefit conferred" to the majority shareholder is simply the dollar value of the initial investment. That initial investment has not appreciated; rather, it is the corresponding value of the minority's stock that has appreciated. In other words, assuming a $10,000 initial minority investment, the majority has been enriched only by that $10,000 (plus, presumably, interest)—not by the appreciation in the stock of the minority. Nevertheless, depending on the situation, this argument may be worth making.

[266] *See* III FARNSWORTH, *supra* note 119, § 12.19, at 320 ("Restitution as a remedy for breach is therefore limited to cases in which the injured party has a claim for damages for total breach, so that that party's remaining duties are discharged. If the claim is only one for damages for partial breach, the injured party's remaining duties are not discharged, and restitution is not available as an alternative."); *see also* Hibiscus Assocs. Ltd. v. Bd. of Trs. of Policemen and Firemen Ret. Sys., 50 F.3d 908, 916 (11th Cir. 1995) (noting that, under Florida law, the breached term must be an "essential part of the bargain . . . such that its breach destroys the entire contract"); Harris v. Metro. Mall, 334 N.W.2d 519, 524 (Wis. 1983) (observing that the breach "must be a 'total breach'" for a restitution remedy).

dividends). The "total breach" required for a restitution award would presumably require a complete freeze-out where every critical term of the contract is breached—i.e., where the minority shareholder is terminated from employment, removed from management, and excluded from dividends. Thus, in a partial freeze-out situation, contract law may not be able to replicate the restitutionary component of the buyout remedy.

The invocation of this common-law rule, however, may depend upon how the court defines the investment contract between the close corporation shareholders. As mentioned, rather than one money-for-stock contract with a number of accompanying terms, a court may conceptualize the close corporation investment bargain as a number of smaller contracts—e.g., a money-for-employment contract, or a money-for-management contract.[267] Such a conception makes it possible to award restitution damages in a partial freeze-out situation. If the majority's oppressive conduct consisted solely of the unjustified termination of the minority's employment, the termination may be characterized as a total breach of the money-for-employment contract, rather than as a partial breach of the money-for-stock contract. Thus, depending upon how a court views the close corporation investment contract, the "total breach" limitation on restitution damages may not preclude contract law from awarding restitutionary compensation in an oppression context.[268] As explained, however, such a restitutionary award is unlikely to reflect a buyout-equivalent remedy given that appreciation on the investment will probably not be included.[269]

b. *The Problems with an Expectation Recovery*

If an oppressed shareholder seeks an expectation recovery under contract law, receiving a buyout-equivalent remedy will still be problematic. For example, assume that a founding minority shareholder

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[267] *See supra* notes 140–141 and accompanying text.

[268] Of course, it is unclear whether courts applying contract law will adopt this multiple contract conception. At the very least, however, one can fairly assert that this "total breach" restriction raises some doubt about whether contract law can protect the restitutionary interest of an oppressed close corporation shareholder.

[269] *See supra* notes 262–265 and accompanying text. Where the invested capital has continuously depreciated from the time the capital was committed, of course, a restitution award of the initial investment would provide a larger recovery than the buyout's grant of the depreciated fair value of the investment. *Cf.* III FARNSWORTH, *supra* note 119, § 12.20, at 326–28 (observing that restitution damages will exceed expectation damages in situations where the contract is unprofitable).

invests $40,000 at the inception of a venture. Three years later, the majority shareholder commences a conventional freeze-out by unjustifiably terminating the minority shareholder from employment and management and by excluding the minority from dividends. Based on the money-for-stock contract and its accompanying employment, management, and dividend terms,[270] an expectation award designed to put the minority shareholder in the same economic position as if the contract had been performed would require the court to remedy these employment, management, and dividend injuries. In operation, the terminations of employment and management would presumably be remedied by orders of reinstatement or by damages equivalent to the lost employment and management positions.[271] Similarly, the dividends that were wrongfully diverted from the minority shareholder would probably be remedied through a damages award equivalent to the amount of the lost dividends, or by an injunction specifying that the amount of the diverted dividends shall be paid to the minority.[272] By addressing the losses of employment, management, and dividends, the court remedies the breached terms and puts the oppressed shareholder in the same economic position as if the terms of the contract had been performed.

Conspicuously absent from this expectation damages scheme, however, is a return of the oppressed shareholder's investment capital (i.e., the restitutionary interest) along with any appreciation or depreciation on that investment. The rationale for this absence is implicit in the goal of expectation damages, which is to put the oppressed shareholder in the same economic position as if the contract had been fully performed. After all, if the contract had been fully performed, the typical minority investor would own stock in a close corporation (representing the value of his or her financial investment) and would receive employment, management responsibilities, and proportional dividend payments (if any) from the company. While the typical freeze-out scenario does breach the employment, management, and dividend terms of the close corporation investment con-

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[270] *See supra* notes 136–139 and accompanying text.

[271] *See supra* notes 120–123 and accompanying text (discussing compensation for wrongful termination).

[272] *See, e.g.*, Patton v. Nicholas, 279 S.W.2d 848, 857 (Tex. 1955) (issuing an injunction that required a corporation and a controlling shareholder to pay a reasonable dividend "at the earliest practical date" and that ordered "reasonable dividends to be thereafter declared annually from future profits of the corporation"); *id.* (noting that "the amount of such dividend . . . shall take into consideration . . . the fact that respondents have been wrongfully deprived of their dividends since the beginning").

tract, the freeze-out does not generally affect the investor's stockholdings in the company. Indeed, a freeze-out generally leaves the investor owning stock in the close corporation (just as he or she did before the oppressive conduct), but the investor is stripped of his or her accompanying employment, management, and dividend rights.[273] Thus, an expectation award need only rectify the employment, management, and dividend harms to put the minority in the same economic position as if the contract had been fully performed.[274] Put differently, in the typical freeze-out scenario, the shareholder's invested capital is not harmed—i.e., the investor retains his or her share ownership and can still theoretically recover his or her investment (with appreciation or depreciation) through a sale of his or her holdings. Because the minority's stock ownership is retained and, in theory, is not harmed by the majority's conduct, an expectation award in a typical oppression context is not likely to include compensation for the initial investment or for any accompanying appreciation.[275] Correspondingly,

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[273] *See, e.g.*, *In re Topper*, 433 N.Y.S.2d at 362 (involving a close corporation that paid no dividends and a minority shareholder who was discharged from employment and removed as an officer); *id.* (noting that "the controlling shareholders continue to maintain [that the minority investor] has suffered no harm because his one-third (1/3) interest remains intact").

[274] In fact, an expectation award that remedied the loss of employment, management, and dividends and that returned the original investment (with appreciation) would put the oppressed shareholder in a *better* position than if full performance had occurred. The aggrieved shareholder's employment, management, and dividend rights would be remedied *and* he or she would receive the cash value of his or her otherwise illiquid stockholdings. *See supra* notes 41–42 and accompanying text (discussing the lack of a market for close corporation stock).

[275] It is possible to argue that the typical freeze-out does harm the minority's stock ownership in the company. Although a close corporation has no established market for its stock, investors can occasionally sell their holdings to private parties. *See, e.g.*, *Wilkes*, 353 N.E.2d at 660 (noting that a founding investor sold his shares in the corporation to an outside party). Prior to a freeze-out, therefore, there is a possibility of the minority selling its shares to a third party. Such a sale, however, might be subject to a minority discount on the theory that outside investors will pay less for a minority stake in a close corporation because of their inability to control management. *See infra* text accompanying note 276 (defining minority discount). To some extent, therefore, the minority discount represents the chance that the majority may act oppressively towards the minority because of the minority's lack of control.

When oppressive conduct has already occurred, however, the chance of oppression has become a certainty. As a consequence, the pre-oppression possibility of selling the minority's holdings to a third party is likely eliminated. After all, a minority stake in a close corporation is surely unattractive to outside buyers when a track record of oppressive majority conduct exists in the company. In effect, therefore, oppression can result in the minority's stockholdings becoming relatively worthless to outsiders. The only prospective purchaser is the majority itself, and it is unlikely that a fair price will be offered. *See, e.g.*, *Wilkes*, 353 N.E.2d at 664 n.14 (noting that the controlling shareholders offered to pur-

in a typical oppression context, the minority investor will maintain, at the very least, his or her shareholder status in the company. In addition, if the minority investor is reinstated to his or her employment or management positions (rather than awarded damages), the minority maintains his or her employee or manager status as well.

Even if a contracts court did provide compensation for the initial investment and any appreciation—an unlikely scenario given the above-mentioned discussion—the expectation award will still be problematic in light of the minority and marketability discounts that such a contract award is likely to include. A minority discount signifies that "investors will pay less for [a minority stake] in a close corporation because of the inability to elect a sufficient number of directors to control management."[276] A marketability discount, in contrast, is based on the notion that "shares in a closely held corporation cannot be sold as readily as shares in a corporation with securities traded over an exchange or in an established market and therefore investors tend to pay less, and sometimes significantly less, for such shares."[277] Taken together, these discounts reflect the notion that, if the majority's oppressive conduct had not breached the implied-in-fact investment contract among the shareholders, the minority investor would hold a non-controlling and relatively illiquid position in the close corporation. If a court awarded expectation damages to replicate this "no breach" economic position, the award would presumably have to reflect these lack of control and illiquidity factors. Otherwise, the compensation awarded to the minority investor for his or her hold-

chase the minority's shares for a price that one of the controlling shareholders "admittedly would not have accepted for his own shares"); Ragazzo, *supra* note 86, at 1117 (stating that an oppressive majority shareholder "often administers the coup de grace by offering to purchase the minority's stock at a fraction of its true worth"). Thus, even though a freeze-out will generally leave the minority with its stockholdings, the minority's ownership stake is still arguably harmed. The freeze-out actions virtually eliminate the possibility of a third-party sale which, in turn, effectively cripples the value of the stock. As a consequence, to put the minority in the same economic position as if the contract had been fully performed (i.e., as if a freeze-out had not occurred), an expectation recovery in a typical freeze-out situation could arguably include some amount for the diminished value of the investment.

[276] Bahls, *supra* note 21, at 301.

[277] Advanced Communication Design, Inc. v. Follett, 615 N.W.2d 285, 291 (Minn. 2000); *see id.* ("A marketability discount adjusts for a lack of liquidity in one's interest in an entity and should be distinguished from a minority discount, which adjusts for lack of control of the corporation.") (internal quotation omitted); *cf.* Bahls, *supra* note 21, at 302 (noting that a marketability discount is often imposed because, "due to the difficulty and expense associated with selling the stock at a later date, investors are not willing to pay as much for close corporation stock").

ings would arguably have a higher value than if the majority's conduct had not run afoul of the investment contract.[278]

When a buyout is awarded in a shareholder oppression context, however, oppression courts have generally avoided a minority discount.[279] The conventional rationale for such a decision is often explained as follows:

> Sale of the minority shareholders' stock to the corporation or majority shareholders is unlike a sale to third parties. When a shareholder sells his or her shares to third parties, the value of the shares sold by shareholders to third parties is indeed diminished because the third party has no right to control management. A sale to majority shareholders of a corporation, however, simply serves to consolidate the interests of those already in control. To require application of a minority discount in this case would result in a windfall for majority shareholders which is inequitable particularly when it is the majority shareholder who initially acted oppressively.[280]

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[278] For example, assume that a minority investor contributes $40,000 to a close corporation. If a court was to determine the value of the shareholder's financial investment in the company, it would presumably be based on what a willing buyer would pay the minority for its stake in the business. *See, e.g.*, ROBERT W. HAMILTON, BUSINESS ORGANIZATIONS: UNINCORPORATED BUSINESSES AND CLOSELY HELD CORPORATIONS § 14.6, at 405–06 (observing that "fair value" has no inherent meaning and that, at best, it is merely a synonym "for the basic definition of value, namely the price on which a willing buyer and willing seller agree"). Because such a stake is non-controlling and is relatively difficult to transfer, a willing buyer is unlikely to offer the full $40,000 to the minority. Instead, some discounted offer would probably be made. The court's determination of value, therefore, would be less than $40,000; moreover, that lower amount would represent the value of the minority's financial investment in the company if no oppressive conduct had occurred. Thus, a full award of $40,000 would *overcompensate* the minority given that the value of its holdings would be less than $40,000 if the investment contract had been performed (i.e., if the majority had not acted oppressively).

[279] *See* Thompson, *supra* note 30, at 234 ("[C]ourts generally have not discounted stock because it contains a minority interest . . . .").

[280] Bahls, *supra* note 21, at 302; *see also* Blake v. Blake Agency, Inc., 486 N.Y.S.2d 341, 349 (App. Div. 1985) ("[The dissolution statute] was enacted for the protection of minority shareholders, and the corporation should therefore not receive a windfall in the form of a discount because it elected to purchase the minority interest . . . . [A] minority interest in closely held corporate stock should not be discounted solely because it is a minority interest."); Thompson, *supra* note 30, at 234 ("[S]uch a [minority] discount would be inappropriate since the [buyout] purchase is by controlling shareholders or the corporation; to apply such a discount would be to further oppress minority shareholders aggrieved by the controlling shareholders' misconduct.") (citing Brown v. Allied Corrugated Box Co., 154 Cal. Rptr. 170, 175–76 (Ct. App. 1979)).

Oppression courts are more willing, however, to apply a marketability discount in a buyout proceeding.[281] For example, some courts have cited the absence of a market for a close corporation's shares as a justification for applying a marketability discount to the valuation of both minority *and* majority shares.[282] Nevertheless, many oppression courts choose not to apply a marketability discount. In fact, "some courts reject marketability discounts for reasons similar to those given for refusing minority discounts."[283] As one commentator observed:

> It seems particularly inappropriate to apply such a [marketability] discount when a shareholder is selling to a person or family that owns all or most of the other shares of the corporation. While the lack of a market affects the ability to sell minority shares in a company, the market for all of a company's assets or shares or for a controlling interest operates differently and may not be adversely influenced by the fact that the company's shares are not traded on a securities market.[284]

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[281] *See* Thompson, *supra* note 30, at 234 (noting that courts generally forego a minority discount in a buyout context, but observing that courts "have not demonstrated the same reluctance in applying a discount for lack of marketability").

[282] *See, e.g.*, *Blake*, 486 N.Y.S.2d at 349 ("A discount for lack of marketability is properly factored into the equation because the shares of a closely held corporation cannot be readily sold on a public market. Such a discount bears no relation to the fact that the petitioner's shares in the corporation represent a minority interest."); *In re* Fleischer, 486 N.Y.S.2d 272, 275 (App. Div. 1985) ("In determining the 'fair value' of the shares of a closely held corporation, discounts for the lack of marketability of such shares are appropriate and do not provide a windfall to the majority shareholders merely because the shares to be purchased by the majority . . . constitute a minority interest in the corporation").

[283] 2 Oppression, *supra* note 31, § 7:21, at 115; *see, e.g.*, Charland v. Country View Golf Club, Inc., 588 A.2d 609, 612–13 (R.I. 1991); *cf.* Hendley v. Lee, 676 F. Supp. 1317, 1330 (D.S.C. 1987) ("Discounts properly apply to the total value of the company in a 'willing buyer/willing seller' context, but do not apply at all when neither party is willing and the transaction is between insiders.").

[284] Thompson, *supra* note 30, at 235. Similarly, as Professor Bahls observes:

> If, however, a minority block of shares is sold to a shareholder who will be a controlling shareholder after the sale, the full discount for lack of marketability may be inappropriate. To the extent that the purchase allows the shareholder to consolidate control, there may be a ready market for the subsequent resale of the majority shareholder's stock. While a minority interest in a close corporation is difficult to sell, a majority interest might be sold much easier. Likewise, consolidating control may enable the majority shareholder to realize a control premium.

Bahls, *supra* note 21, at 303.

In a shareholder oppression analysis, therefore, there is a good chance that discounts for minority status and stock illiquidity will not be applied to a buyout award. Perhaps this absence of discounts is due simply to the differences between an oppression context and a willing buyer/willing seller context.[285] Perhaps, in some sense, the absence of discounts is an effort to punish the majority shareholder for causing the oppressive situation.[286] Alternatively, because the buyout remedy is essentially offered in lieu of the dissolution of the company,[287] perhaps the lack of discounts is an appropriate effort to mirror the straight pro rata distribution that would occur in a corporate dissolution proceeding.[288] Finally, given that the conventional buyout provides no compensation to an oppressed minority for many of the terms of the investment contract (e.g., no lost job or lost management compensation),[289] perhaps the absence of discounts is "overcompensation" that is tolerated in a freeze-out context. In other words, to offset the freeze-out harms that are undercompensated or not compensated at all, courts may be willing to overcompensate in other damage areas (e.g., by avoiding minority and illiquidity discounts when awarding the "fair value" of a stock).[290] Ultimately, all of these rationales are persuasive to some degree. More importantly, they highlight the inappropriateness of contract law's likely use of discounts in a shareholder oppression situation.

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[285] *See supra* notes 280, 284 and accompanying text.

[286] *See supra* note 280 and accompanying text.

[287] *See supra* notes 43–46 and accompanying text (describing the statutory cause of action for oppression).

[288] *See, e.g., Charland*, 588 A.2d at 613 ("In dissolution cases, strong reasons support the use of pro rata value without a discount .... A minority shareholder seeking dissolution claims that majority shareholders have engaged in some unfair, possibly tortious, action. If the minority shareholder succeeds in having the company dissolved, all shareholders will receive their pro rata share of the assets, with no account given to the minority [or illiquidity] status of their shares. Minority shareholders should not receive less than this value if, instead of fighting the dissolution action, the majority decides to seek appraisal of minority shares in order to buy out the minority and reduce corporate discord.").

[289] *See supra* notes 128–129, 259 and accompanying text.

[290] Relatedly, the buyout's undiscounted return of the invested capital (plus appreciation or depreciation) may simply serve as a proxy for the lost job and lost management compensation that a true expectation recovery would award in a freeze-out context.

Even if a conventional buyout did provide "lost job" or "lost management" compensation to an oppressed minority, it may be difficult to calculate such damages with reasonable certainty. For example, the loss of prestige and independence that potentially results from a termination of employment and a removal from management may be difficult to quantify. *See supra* notes 88–89, 123 and accompanying text. As a consequence, the absence of discounts may again serve as overcompensation that is tolerated by courts given the other legitimate minority harms that are too uncertain to be remedied.

In short, several critical points are apparent from this discussion. First, because a typical freeze-out does not directly affect the minority's stockholdings in a corporation, an expectation award is probably unable to provide a return of the invested capital (or any appreciation on that investment). Such a result, of course, cripples the ability of an expectation award to serve as a buyout-equivalent remedy. Second, and relatedly, an expectation-oriented award is likely subject to the above-mentioned shortcomings of reinstatement, damages, and injunctive orders in a close corporation setting.[291] In contrast to the buyout, the problems of deteriorating personal relationships, distrust of the majority, and judicial reluctance to supervise can all be present, given that an expectation recovery is apt to keep the investor in the company in some capacity.[292] Finally, even in the unlikely event that an expectation recovery did provide compensation for the value of a minority's financial investment (and, therefore, did "cash out" the minority from the company), a contracts court would probably apply minority and marketability discounts to the awarded sum.

Despite these deficiencies, an expectation recovery in a freeze-out scenario may provide greater damages than a buyout under certain circumstances. For example, where an investment has appreciated minimally (or not at all), a buyout awarding an aggrieved shareholder the "fair value" of his or her invested capital may provide a smaller recovery than an expectation award that provides compensatory damages for a lost job, a lost management position, and/or any diverted dividends.[293] In such a situation, contract remedies could theoretically provide a superior recovery to a frozen-out minority shareholder.[294] Such a result, however, presumes that the compensatory damages for the lost job, lost management position, and/or diverted dividends can be measured with some degree of certainty—a dubious proposition given the indefinite nature of the typical close corporation investment bargain. Moreover, because the other *liability* hurdles of contract law (e.g., employment at will, statute of frauds)

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[291] *See supra* notes 115–127 and accompanying text.

[292] *See supra* notes 274–276 and accompanying text.

[293] Moreover, and as mentioned, it is possible (although unlikely) for an expectation award to include a "cash-out" amount for the value of the aggrieved shareholder's financial investment. *See supra* notes 276–278 and accompanying text. That amount—even with minority and marketability discounts—would add to the compensatory damages of an expectation award and would remove the minority from the company.

[294] Of course, if the value of the investment's appreciation is substantial relative to the quantifiable value of the employment, management, and dividend harms, the buyout would provide greater compensation than an expectation recovery under contract law.

will likely pose difficulties for oppressed close corporation shareholders attempting to establish implied-in-fact contracts, these remedy considerations may have little practical significance.

IV. Justifying the Shareholder Oppression Doctrine

Although both oppression precedents and contract precedents base their decisions on breached "agreements" and "understandings" between the parties, it is clear that different meanings are ascribed to these terms. For example, whereas an enforceable "understanding" under oppression law requires little more than the fact that the shareholders at issue were founders who served as employees and managers since the company's inception, an enforceable "understanding" under contract law requires much more definiteness regarding the details of the arrangement.[295] Simply put, although contractually-rooted concepts are the focal point of oppression's reasonable expectations analysis, there are significant differences in how oppression law and contract law apply those concepts.

This analysis, of course, raises a critical question: what justifies the existence of the shareholder oppression doctrine? After all, if this Article's discussion is taken to its logical extreme, reasonable (and enforceable) expectations under oppression law could simply be characterized as failed contracts. The above-mentioned question, therefore, can be reformulated as follows: why should failed contracts be protected in the oppression context? In my opinion, at least two arguments help to answer this inquiry.

A. *The Existence of a Bargain*

In most oppression disputes, the evidence reveals that close corporation shareholders strike an actual bargain between themselves when the minority decides to commit capital to the venture. To use employment as an example, assume a typical close corporation scenario where (1) all of the shareholders invest a substantial part of their savings in the business, quit their prior employment, and immediately begin working for the company in an employment and management role; and (2) the corporation pays no dividends—instead, all of the profits are distributed as salary to the shareholders.[296] Even

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[295] *See supra* Part III(B)(1)(b) (discussing the definiteness of the close corporation bargain); *supra* notes 77–78 and accompanying text.

[296] *See supra* notes 37, 71 and accompanying text.

without an explicit agreement, it is a fair inference from this scenario that the shareholders bargained, perhaps implicitly, for an understanding that their investments entitled them to continued employment with the company. Because the shareholders left their prior employment positions, the minority *and* the majority shareholders likely understood that the close corporation jobs would become their primary (if not sole) sources of livelihood.[297] Similarly, because of the absence of dividends, they all likely understood that a job with the corporation and its accompanying salary would be the only vehicles for distributing the profits of the business and for earning a return on their investments.[298] Evidence stemming from the parties' own actions, therefore, suggests that an implicit bargain was struck between the majority and minority investors—i.e., the minority agrees to contribute capital and, in return, the majority agrees to limit its discretion to terminate the minority's employment.[299]

Aside from evidence of the parties' conduct, the economics behind close corporation investments also supports the proposition that an actual bargain has been struck between the investors. Once again, employment provides a helpful example. As mentioned, employment is typically the principal enticement motivating a stockholder's decision to invest in a closely-held venture.[300] Given the significance of

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[297] *See supra* note 92 and accompanying text; *see also* Harris v. Mardan Bus. Sys., Inc., 421 N.W.2d 350, 352 (Minn. Ct. App. 1988) (involving a close corporation majority shareholder who left prior employment with a large public company to form the close corporation); Moll, *supra* note 18, at 817 ("[T]he typical majority shareholder has often left prior employment herself to join the speculative start-up business.").

[298] *See* Nagy v. Riblet Prods. Corp., 79 F.3d 572, 577 (7th Cir. 1996) ("Many closely held firms endeavor to show no profits (to minimize their taxes) and to distribute the real economic returns of the business to the investors as salary. When firms are organized in this way, *firing an employee is little different from canceling his shares.*") (emphasis added); Landorf v. Glottstein, 500 N.Y.S.2d 494, 499 (Sup. Ct. 1986) ("In a close corporation, since dividends are often provided by means of salaries to shareholders, loss of salary may be the functional equivalent of the denial of participation in dividends."); Balvik v. Sylvester, 411 N.W.2d 383, 388 (N.D. 1987) ("Balvik was ultimately fired as an employee of the corporation, thus destroying the primary mode of return on his investment."); *see also* 1 CLOSE CORPORATIONS, *supra* note 15, § 1.15, at 89 ("An investor taking a minority investment position in a close corporation, expecting to receive a return on the investment in the form of a regular salary, would face the risk that, after a falling out among the participants, the directors would terminate the minority shareholder's employment and deprive that investor of any return on the investment in the corporation."); *supra* note 37 and accompanying text.

[299] *See supra* notes 74, 116 and accompanying text; *cf.* Hillman, *supra* note 25, at 78 ("That assumptions are not made explicit does not require that they be disregarded when they are accepted or assumed by the other participants.").

[300] *See supra* notes 86, 92 and accompanying text.

employment, rational close corporation shareholders would likely be unwilling to commit their capital unless a bargain was struck for the protection of their employment.[301] Stated more broadly, because close corporation shareholders consider their investments to be comprised of employment, management, and a proportionate share of the corporate profits,[302] a minority shareholder would likely avoid investing in a close corporation unless a bargain was struck with the majority shareholder for the protection of these investment components.[303] The economics behind the decision to invest in a close corporation, therefore, suggest that an actual (albeit implicit) bargain must have been struck between the majority and minority investors in order to induce the minority to commit his or her capital to the close corporation.[304]

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[301] In theory, there are situations where investors might purchase a minority stake in a close corporation even if they had not bargained for continuous employment. For example, there may be some close corporations that are likely to experience significant stock appreciation in a relatively short time period (e.g., Internet companies). For these companies, the potential upside from the stock appreciation may dwarf the employment benefits that an investor receives. As a consequence, an investor may be willing to risk his or her termination of employment in order to become a shareholder in the company. In addition, an investor might purchase a minority stake, even without an employment bargain, due to the investor's failure to appreciate his or her potential freeze-out risks. *See, e.g.*, William Carney, *The Theory of the Firm: Investor Coordination Costs, Control Premiums and Capital Structure*, 65 WASH. U.L.Q. 1, 59–60 (1987) ("Investors in closely held enterprises are likely to be subject to conditions of bounded rationality, under which they either fail to perceive the complete set of problems that may occur later, or underestimate the probability of their occurrence."); Thompson, *supra* note 28, at 705 ("Investors often fail to anticipate the failure of their enterprise, or demonstrate an overly optimistic trust in those with whom they are undertaking the venture."); Thompson, *supra* note 30, at 224 ("Parties entering into a business relationship are not always willing to fully explore the ramifications of possible disputes if things were to go wrong."). Finally, even without a bargain for continuous employment, some minority investors may wind up in a close corporation because they received their stock through a gift or an inheritance. *See, e.g.*, Gimpel v. Bolstein, 477 N.Y.S.2d 1014, 1017 (Sup. Ct. 1984) (involving a shareholder whose stock was received "by gift and bequest from his father").

[302] *See* Moll, *supra* note 18, at 794 ("In a close corporation, however, the shareholder typically commits his or her capital with the expectation that his or her investment entitles him or her to employment and to a management role, as well as to a proportionate share of the company's earnings. Thus, a close corporation shareholder usually understands that his or her investment return will be comprised of employment benefits, management participation, and financial sums reflecting a share of the company's earnings.") (footnote omitted).

[303] *Cf.* Bahls, *supra* note 21, at 325 (noting that "participation and rights in a closely held corporation are normally negotiated").

[304] Stated differently, to convince a rational minority investor to commit a substantial part of his or her savings to a close corporation, it is likely that the majority shareholder and the minority shareholder reached mutual understandings that restricted the majority's ability to harm the minority's investment—i.e., the minority's employment, management

Based on evidence of the parties' conduct and an understanding of the economics behind close corporation investments, therefore, a bargain exists between close corporation shareholders—i.e., a bargain that protects the investment components (employment, management, proportionate share of company earnings) of close corporation stockholders.[305] Under contract law, of course, the existence of a bargain itself is of great importance. Indeed, as long as an actual bargain exists, even a "failed contract" can be deserving of some protection under contract doctrines. For example, although indefiniteness or the statute of frauds can prohibit enforcement of an actual bargain under its terms,[306] such a "failed contract" can be protected in an "off-the-contract" manner to the extent that compensation is often provided for the unjust enrichment of the breaching party—i.e., for the benefits that the injured party has conferred upon the breaching party (restitution).[307] Such an award signifies that the existence of the

position, and share of profits. *Cf.* Edwin J. Bradley, *An Analysis of the Model Close Corporation Act and a Proposed Legislative Strategy*, 10 J. CORP. L. 817, 840 (1985) ("The majority shareholders understand that the minority shareholders have not entered the venture knowingly taking the investment risk that they may have to suffer the deprivation of any meaningful governance input or share in economic return because they have submitted to the exercise of an undiluted and untempered majority power short of fraud, misappropriations or breach of fiduciary duty.").

[305] *See In re* Topper, 433 N.Y.S.2d 359, 365 (Sup. Ct. 1980) ("These reasonable expectations constitute the bargain of the parties in light of which subsequent conduct must be appraised."); Sandra K. Miller, *A Note on the Definition of Oppressive Conduct by Majority Shareholders: How Can the Reasonable Expectations Standard be Reasonably Applied in Pennsylvania?*, 12 J.L. & COM. 51, 54 (1992) (describing the reasonable expectations approach as a "departure from the bargain struck by the majority and minority shareholders"); *supra* note 22 and accompanying text; *cf.* Bahls, *supra* note 21, at 325 ("Because participation and rights in a closely held corporation are normally negotiated, expectations are reasonable when they provide a basis for the bargain."); Murdock, *supra* note 39, at 465 (noting that when applying the reasonable expectations standard, "the crux is not identifying a traditional wrong but rather identifying the basis of the bargain—what were the explicit or implicit conditions pursuant to which the parties associated themselves together in the corporate form"); Peeples, *supra* note 20, at 504 ("If a shareholder's reasonable expectations have been frustrated, the shareholder has lost the benefit of the original bargain.").

[306] *See supra* Parts III(B)(1)(a) (discussing indefiniteness), III(B)(3) (discussing statute of frauds). It is important to remember that in the shareholder oppression context, indefiniteness and statute of frauds concerns are much less significant. With respect to indefiniteness, it has previously been noted that the "fair value" buyout is not dependent on major terms such as employment and management. Because the compensation awarded through a buyout is unrelated to the terms that trigger oppression liability, the terms themselves can be much less definite. *See supra* notes 128–131, 195 and accompanying text. Furthermore, the investment bargain of close corporation shareholders may very well satisfy the statute of frauds. *See supra* notes 218–220 and accompanying text.

[307] *See* II FARNSWORTH, *supra* note 119, § 3.30, at 413 ("Part performance of an agreement that is unenforceable for indefiniteness may . . . result in a claim in restitution."); *id.*

bargain itself—regardless of whether that bargain could be literally enforced—is a compelling factor that weighs towards the granting of some type of remedy. To a large degree, oppression law follows the same logic. Because both evidence and economics indicate that an actual bargain exists between close corporation investors, the shareholder oppression doctrine operates to provide some degree of protection to this particular bargain.

In short, the societal justification for contract law—i.e., the notion that protecting private bargains is valuable—provides an equal justification for the shareholder oppression doctrine. Just as contract law seeks to safeguard bargains—even if the bargains fail to constitute enforceable contracts[308]—oppression law seeks to provide the close corporation investment bargain with some level of protection.[309]

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§ 6.11, at 187 ("Even though the statute of frauds may prevent an injured party from enforcing the contract when the other party unjustifiably refuses to perform, courts generally allow the injured party restitution of any benefit that the injured party has conferred on the other by part performance or otherwise.").

Allowing an oppressed minority shareholder to sue "off-the-contract" for unjust enrichment would not fully protect the shareholder's interests. As the above citations indicate, the remedy for unjust enrichment is restitutionary in nature. *See also* CALAMARI & PERILLO, *supra* note 127, § 15.2, at 648–49 (noting that restitution encompasses recoveries for unjust enrichment). As a consequence, all of the problems associated with awarding restitution damages are present in the unjust enrichment context. *See supra* Part III(D)(3)(a) (noting the problems with restitution damages); *infra* notes 311–316 and accompanying text.

[308] It is true, of course, that contract law does not provide a level of protection for *all* bargains. In some situations, for example, public policy may prohibit contract law from awarding any relief for a broken bargain, even though the evidence reveals that an actual bargain did exist between the parties. *See, e.g.*, II FARNSWORTH, *supra* note 119, § 5.9, at 87–88 ("Courts generally do not grant restitution under agreements that are unenforceable on grounds of public policy .... In general, a court will simply leave the parties as it finds them, even though this may result in a benefit to one of them."). In the shareholder oppression context, however, this concern is much less acute. There is no public policy reason for refusing to enforce the investment bargain; indeed, to the extent that shareholder oppression involves the "theft" of one's investment, public policy would presumably be in favor of enforcing such a bargain. *See infra* Part IV(B). Moreover, given that "a potential source of much-needed risk capital for small business enterprises is threatened by the prevalence of squeeze-outs," 1 OPPRESSION, *supra* note 31, § 1:04, at 8, public policy would likely support efforts to combat squeeze-outs through judicial protection of the close corporation investment bargain.

[309] *Cf.* Merola v. Exergen Corp., 648 N.E.2d 1301, 1305 (Mass. App. Ct. 1995) ("[A] stockholder's expectations may arise from an express or implied understanding that falls short of an enforceable contract. The rightful expectations of the parties, not contract law, are controlling.").

B. *The Need to Combat Theft*

The existence of a close corporation investment bargain is important but, standing alone, it is insufficient to justify the remedial aspect of the shareholder oppression doctrine. Although the bargain itself justifies *some* level of protection, there is still a question as to why the oppression doctrine provides *enhanced* protection through its buyout remedy. After all, in contrast to the restitutionary award that contract law often provides when a bargain, for some reason, is unenforceable,[310] the buyout remedy awards *more* than mere restitutionary damages for a breach of the close corporation investment bargain.[311]

The critical point to understand is that a mere award of restitutionary damages to an oppressed close corporation shareholder would effectively permit the majority to steal the investment value of the minority. A simple example helps to flesh out this point. Assume that a 60% majority shareholder and a 40% minority shareholder operate a close corporation. At the time of founding the business, the majority committed $60,000 to the venture, while the minority contributed a $40,000 sum. Over the next few years, the business prospers. Unfortunately, tensions between the shareholders develop and the majority, without justification, ultimately terminates the minority from employment, removes him or her from management, and excludes him or her from dividends. At the time of the oppressive conduct, assume that the company's value had risen from $100,000 (the initial contributed capital) to $1,000,000.

With a $1,000,000 company value, of course, the 60% majority shareholder effectively owns a stake in the business worth $600,000. Similarly, the 40% minority investor owns a share of the company worth $400,000. By freezing-out the minority shareholder and by counting on a restitutionary remedy, however, the majority can increase the size and the value of its stake in the company. After all, if a restitutionary award were granted to the oppressed minority, the minority would presumably forfeit its ownership stake in return for the $40,000 that it originally invested in the company.[312] Such a result, of course, leaves the oppressive majority owning 100% of a company worth $960,000.[313] In other words, by acting illegally (i.e., oppres-

[310] *See supra* notes 306–307 and accompanying text.

[311] *See supra* Part III(D)(2).

[312] *See supra* note 256 and accompanying text.

[313] That is, the company worth $1,000,000 paid out $40,000 to the oppressed minority shareholder. As a consequence, the company's value has decreased to $960,000.

sively), the majority has increased the value of its stake in the company from $600,000 to $960,000. Correspondingly, as a result of the majority's misconduct, the value of the minority's stake in the business has decreased from $400,000 to $40,000. If such a limited award is allowed to stand, the majority, by acting oppressively, is effectively permitted to break a bargain and to confiscate $360,000 of the minority's investment value.[314] In contrast, the buyout remedy of the oppression doctrine would award the minority its proportionate share of the company's "fair value."[315] With a company value of $1,000,000, such an award would approximate $400,000.[316] Through the buyout remedy, therefore, the majority is unable to profit from its oppressive actions.

In short, although the investment bargain struck between close corporation shareholders may not rise to the level of an enforceable contract, it is an actual, existing bargain that is deserving of protection. Because a mere restitutionary award would sanction the majority's theft of the minority's investment (effectively rewarding the majority for its "bargain-breaching" oppressive conduct), however, a broad measure of relief is needed.[317] The shareholder oppression doctrine—along with its accompanying buyout remedy—justifies itself by accomplishing this purpose. It is possible, of course, to envision contract law functioning in the same manner. Indeed, in the shareholder oppression context, contract law could presumably overcome indefiniteness and other problems to recognize an investment bargain established by conduct and economic evidence. In addition, contract law could potentially recognize that a broader remedy is needed in the oppression context given that a sole award of restitution dam-

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[314] The minority owned a 40% stake of a $1,000,000 company, yielding an ownership stake worth $400,000. With a restitutionary award, however, the minority gives up its ownership stake and receives damages only in the amount of $40,000. Thus, the majority—at the minority's expense—has captured $360,000 of the minority's investment value. *See, e.g.*, Bradley, *supra* note 304, at 840 ("Never should the minority participant be understood as assenting to the effective confiscation of his or her investment . . . ."); Moll, *supra* note 18, at 817 n.267 ("[T]he majority shareholder should be viewed as simply appropriating a portion of the minority's investment to further the majority's own interests.").

[315] *See supra* note 109 and accompanying text.

[316] That is, 40% of a $1,000,000 company is worth $400,000.

[317] *See* O'Neal, *supra* note 135, at 887 ("Not to provide a remedy in circumstances of this kind is to permit the majority shareholders to exploit the minority shareholder's investment solely for their own benefit."); Prentice, *supra* note 135, at 134 (same); *cf.* 2 Oppression, *supra* note 31, § 10:07, at 36 ("Flexibility of remedy tailored to all the facts and circumstances of the case, including the shareholder's conflicting interests and motivations, is the key.").

ages leads to an unjust result. It is hard to believe, however, that contract law, as presently applied, would allow such a liberal approach to its fundamental premises. As a consequence, it is fair to assert that oppression law is doing what contract law should be doing *if* contract law took a broader perspective when identifying and enforcing bargains.

V. EXTENDING THE OPPRESSION FRAMEWORK

Because the shareholder oppression doctrine steps in for contract law to protect the close corporation investment bargain, it is worth asking whether bargains in other contexts exist—bargains that contract law does not typically safeguard—that warrant protection on the same grounds that underlie the oppression doctrine. Stated differently, are there other relationships or contexts where an actual bargain is revealed by pattern, conduct, and economic evidence, and where contract law's failure to protect this bargain results in some level of theft or unjust enrichment?

Perhaps one such relationship is the employer-employee relationship in the at will employment context.[318] The employment at will doctrine can be criticized on the ground that it creates opportunities for the employer to unjustly enrich itself by capturing the investments of "human capital" that employees make in a particular business.[319]

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[318] For general background on the employment at will doctrine, see *supra* Part III(B)(2).

[319] *See, e.g.*, Ingle v. Glamore Motor Sales, Inc., 535 N.E.2d 1311, 1317 (N.Y. 1989) (Hancock, J., dissenting) ("[P]laintiff alleges . . . that he would never have made the sacrifices and investments of time, effort and money in the business had he known that the buy-back provision would be interpreted to make him subject to summary firing at the whim of the co-owner."); Melvin A. Eisenberg, *The Conception that the Corporation is a Nexus of Contracts, and the Dual Nature of the Firm*, 24 J. CORP. L. 819, 827 (1998) (characterizing the "firm-specific skills" of an employee as "benefit[s] that will be lost if he resigns"). The idea, to some extent, is that the employer benefits from (i.e., is enriched by) the employee's efforts to learn the skills necessary for that particular employer's work. Nevertheless, because of the at will doctrine, the employer can terminate a long-term employee without compensating him or her for the loss of employment options that often results from such skill-building. *See* Peter Linzer, *The Decline of Assent: At-Will Employment as a Case Study of the Breakdown of Private Law Theory*, 20 GA. L. REV. 323, 407 (1986) ("The fact remains that nonunion private sector employees often make a critical commitment of their skills and their mobility. If they can be discharged at will, much of their investment of these 'transaction-specific assets' will be lost, especially as they age and industries migrate and change technologically.") (footnote omitted); *id.* at 408–09 ("The longer the employee has worked for a company, the more specific his job skills have become, the less mobile he is, and the more his investment in the firm becomes his only means of livelihood and self-respect."); Schmedemann, *supra* note 119, at 1438 ("Losing one's job is

Even if a notion of "theft" could be extended from financial capital to human capital, however, it is not necessarily clear that pattern, conduct, and economic evidence would establish an actual bargain between the employer and the employee for continued employment (i.e., not at will employment). For example, even if courts followed the shareholder oppression model by considering the economics behind a pure employee's decision (i.e., a nonshareholder employee's decision) to accept a job, such considerations may ultimately support the employment at will arrangement due to the bargaining power distinctions between the "shareholder employee" in the oppression context and the "pure employee" in the employment context. While it may be true that rational close corporation shareholders would not invest unless they received employment and struck a bargain for its protection,[320] such a proposition is tenable only because the close corporation investor, *ex ante*, has the bargaining leverage to demand such terms. After all, a prospective shareholder-employee of a close corporation has viable alternative options if the majority shareholder refuses to enter into a protective bargain. For example, the prospective shareholder-employee can invest his or her capital in other close corporations willing to provide more favorable terms, or the shareholder-employee can avoid close corporations all together by simply entrusting his or her capital to the stock or bond markets.[321] In addi-

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difficult because, with time, employees become bound to employers .... Employees develop job skills of little use to other employers."); J. Peter Shapiro & James F. Tune, Note, *Implied Contract Rights to Job Security*, 26 STAN. L. REV. 335, 339 (1974) ("[A]s the length of service in any particular employment increases, other options for employees in the job market may diminish."); *id.* at 339 n.35 ("To a certain extent, of course, job experience is an asset to an employee in procuring employment. However, the employee who has been at a particular job for many years may no longer possess skills that are readily transferable ...."); *id.* at 364 ("[T]he District of Columbia Court of Appeals has accepted the idea that a worker's suitability for employment elsewhere may be destroyed in part by continuation in the service of a company for a number of years.") (citing Maloney v. E.I. Du Pont de Nemours & Co., 352 F.2d 936 (D.C. Cir. 1965)); *cf.* Ian R. MacNeil, *Contracts: Adjustment of Long-Term Economic Relations Under Classical, Neoclassical, and Relational Contract Law*, 72 NW. U. L. REV. 854, 862 (1978) ("[C]onsider an employee of a small business who has been treated very decently by his employer for thirty years. He quite naturally comes to expect decent treatment throughout the relation including through retirement. Moreover, he relies on that expectation; and *if that expectation is not realized, the employer may very well have derived benefits from the reliance by the employee that, in terms of the relation as it existed, are unjustified.*") (emphasis added).

[320] Once again, this proposition is based on the importance of employment in a close corporation setting. *See supra* Part II(B)(1) (discussing the employment interest).

[321] *See* O'Neill, *supra* note 21, at 663 ("At the outset, the shareholder faces an extremely diverse array of other ... investment opportunities encompassing not only stock in other ... corporations, but also interests in mutual funds and debt securities of corpora-

tion, given that the pool of potential investors for a particular close corporation (with its own particular line of business) is, presumably, relatively small, the majority shareholder has an incentive to make concessions to secure the potential investor's much-needed capital, as another prospective investor for that particular venture may not come along for quite some time (if ever). Simply put, because the bargaining leverage at the outset favors the prospective shareholder-employee, nothing compels the shareholder-employee to invest on unfavorable terms. Thus, to induce the minority to commit his or her capital to a close corporation, it is fair to assert that an actual protective bargain must have been struck between the majority and minority investors.[322]

When "pure employees" are at issue, however, the bargaining power is often not in their favor. For example, if a lower-level prospective worker attempted to bargain with an employer for job protection, it is likely that most employers would refuse to offer such protection based on their desire to retain managerial flexibility.[323] Indeed, the pool of prospective employees is, relatively speaking, larger than the pool of prospective close corporation investors. Employers, therefore, have less of an incentive to bargain with a particular employee, as in many cases there will be a large number of alternative candidates who are also looking for employment. Moreover, to the extent that many employers share this viewpoint—i.e., refusing to offer employment protection to their non-managerial employees—pure employees in this category are likely to discover that they, unlike potential investors in a close corporation, lack reasonable alternative options. If most employers, in other words, offer similar non-protective employment terms (i.e., offer at will employment arrangements), the need to earn a living at some occupation may lead a pure employee to accept a job *without* striking a bargain for its protection. Put simply, the pure employee, if he or she desires to work, may have little or no choice at *any* employer other than accepting an at will employment arrangement.[324]

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tions, financial institutions and governmental authorities."); Ragazzo, *supra* note 86, at 1109 (noting that close corporation investors "would seem well advised to trust their capital to diversified mutual funds rather than a small corporation").

[322] *See supra* Part IV(A).

[323] *See, e.g.*, Schmedemann, *supra* note 119, at 1439 ("[A]n employer providing job security . . . reduces its flexibility somewhat."); *supra* note 197 and accompanying text.

[324] Of course, one can directly challenge the disparity of bargaining power between the employer and the employee. Perhaps one could argue that the disparity itself warrants an alteration of the at will employment arrangement or, relatedly, one could assert that the employer should not be permitted to use its bargaining power. A further discussion of

Thus, unlike the shareholder oppression context where the economic evidence suggests that a protective employment bargain has been struck, the economic evidence in the pure employment context raises the possibility that a bargain for *unprotected* employment has been struck.[325] In short, although the shareholder oppression framework could arguably be transported to the at will employment relationship, an application of the framework may lead to the same results as the present employment at will doctrine.

In contrast to the employer-employee relationship, an application of the shareholder oppression framework may produce a different legal outcome in conflicts between bondholders and stockholders. Bondholders, like stockholders, provide companies with capital in exchange for a rate of return that is generated by cash flows from the assets of the business.[326] When some corporate transactions are entered into, the effect is to transfer a portion of the bondholders' value to the shareholders, even if the bondholders object. Such events result in the shareholders profiting at the expense of the bondholders.[327] To some extent, therefore, the bondholder-shareholder conflict

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these issues is beyond the scope of this Article. Even in the absence of bargaining power disparities, however, some employees may still prefer an at will employment arrangement to the extent that the arrangement provides employees with the freedom to quit and move on at any time. *See, e.g.*, Murphy v. Am. Home Prods. Corp., 448 N.E.2d 86, 89 (N.Y. 1983) ("[W]here an employment is for an indefinite term it is presumed to be a hiring at will which may be freely terminated by either party at any time for any reason or even for no reason."). Employees with skills that are greatly in demand, for example, may have the ability to take advantage of a number of superior employment opportunities. As a consequence, they may prefer an at will employment arrangement that allows a relatively quick and hassle-free departure from their existing employer.

[325] Stated differently, the economic evidence underlying the pure employment context suggests that an at will relationship was the actual bargain of the parties. *See supra* note 324.

[326] *See* McDaniel, *supra* note 140, at 416. In other words, the bondholder is making a capital investment and it expects to get its money back plus a return on its investment. *See id.* at 417.

[327] As one commentator observed:

> A company may make an extraordinary distribution to all of its stockholders, or it may make such a distribution to only some of them, as in a major share repurchase or self-tender. If it is a cash distribution, the company may raise the cash by selling off assets. If it is a noncash distribution, the company simply declares a dividend in kind. Whether the distribution is to all of the stockholders or only some of them and whether it is in cash or in kind, the effect on bondholders is the same: the ratio of debt to equity increases and fewer assets remain to satisfy bondholder claims. Since the bonds are riskier, their price declines.

McDaniel, *supra* note 140, at 419; *see also* Metro. Life Ins. Co. v. RJR Nabisco, Inc., 716 F. Supp. 1504, 1506 (S.D.N.Y. 1989) ("Plaintiffs now allege, in short, that RJR Nabisco's ac-

can also be characterized as a relationship involving "theft" by one party at the expense of the other party. Just like the shareholder oppression context, a notion of unjust enrichment is present.[328]

Unfortunately, bondholders can be unsuccessful in their attempts to use contract law to challenge the theft of their investment value.[329] A different outcome might result, however, if the oppression framework was applied. For example, because default risk is a significant, if not primary, concern of bondholders,[330] one could argue that the economic evidence suggests that a rational bondholder would not commit significant sums of capital to a company[331] unless a bargain was struck—i.e., a bargain limiting the company's ability to engage in

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tions have drastically impaired the value of bonds previously issued to plaintiffs by, in effect, misappropriating the value of those bonds to help finance the LBO and to distribute an enormous windfall to the company's shareholders. As a result, plaintiffs argue, they have unfairly suffered a multimillion dollar loss in the value of their bonds."); McDaniel, *supra* note 140, at 418 ("Managers may make dividend, financing, and investment decisions that transfer wealth from bondholders to stockholders. Such decisions create gains for stockholders and capital losses for bondholders.").

[328] *See, e.g.*, Van Gemert v. Boeing Co., 520 F.2d 1373, 1385 (2d Cir. 1975) ("[T]he corporate stockholders benefited by not having their stock watered down by the number of shares necessary to convert [the bondholders'] debentures. But an award against Boeing will in effect tend to reduce pro tanto the equity of shareholders in the corporation and thus to a large extent those who were benefited, *one might almost say unjustly enriched*, will be the ones who pay [the bondholders'] loss.") (emphasis added); McDaniel, *supra* note 140, at 445 ("The court in *Boeing* also noted that stockholders were unjustly enriched at the expense of nonconverting bondholders, and a judgment against the corporation would retrieve the benefit. In economic terms, a wealth transfer from bondholders to stockholders would be reversed and given back to the bondholders.") (footnote omitted).

[329] *See, e.g.*, *Metro. Life*, 716 F. Supp. at 1508 ("There being no express covenant between the parties that would restrict the incurrence of new debt, and no perceived direction to that end from covenants that are express, this Court will not imply a covenant to prevent the recent LBO and thereby create an indenture term that, while bargained for in other contexts, was not bargained for here and was not even within the mutual contemplation of the parties."); *see also* McDaniel, *supra* note 140, at 413 n.1 ("A bondholder's rights are largely a matter of contract."). *But see Van Gemert*, 520 F.2d at 1383–85 (concluding that the issuing corporation breached a duty of reasonable notice that was owed to debenture holders—a duty that arose out of the contract between the issuer and the debenture holders).

[330] *See, e.g.*, *Metro. Life*, 716 F. Supp. at 1518 ("[T]he typical investor in a long-term debt security is primarily interested in every reasonable assurance that the principal and interest will be paid when due.") (internal quotation omitted); *cf.* McDaniel, *supra* note 140, at 418 ("Institutional investors employ bond analysts or purchase bond research to assess the risk of default. The price an institution is willing to pay for bonds reflects its assessment of the default risk based on circumstances known or anticipated at the time .... Losses in bond value reflect a greater risk of default, a smaller payoff to bondholders if default occurs, or both.").

[331] *See, e.g.*, *Metro. Life*, 716 F. Supp. at 1507 (noting that plaintiff bondholders invested "roughly $350 million in RJR Nabisco").

transactions that are likely to favor stockholders at the expense of bondholders. A court accepting this suggestion may decide that an implied term in the bondholders' investment contract has been breached when a company's board decides to enter into a bond-holder-risky transaction. Such a judicial outcome, of course, is by no means certain. Given that bonds are traded on an established market, perhaps the price of the bonds already reflects the anticipated default risk of the issuer.[332] A court may decide, therefore, that no further bondholder protection is warranted.[333] Nevertheless, the possibility of

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[332] *See, e.g., id.* at 1520 ("This Court has no reason to believe that the market, in evaluating bonds such as those at issue here, did not discount for the possibility that any company, even one the size of RJR Nabisco, might engage in an LBO heavily financed by debt."); McDaniel, *supra* note 140, at 418 ("A small investor need not make his own assessment of the default risk because in an efficient bond market the anticipated default risk is impounded in the price. Therefore, all bondholders are compensated ex ante for any anticipated risk of default ex post.").

[333] In addition, and similar to the employment relationship, the large number of potential bondholders for creditworthy firms may lead a specific company to reject any particular bondholder's demand that affects the company's ability to enter into particular transactions. *See, e.g., Metro. Life*, 716 F. Supp. at 1513 ("While it would be possible to broaden the change in ownership covenant to cover any acquisition-oriented transaction, [prospective bondholders] might well encounter significant resistance in implementation with larger public companies .... [I]t would seem that management of larger public companies would be particularly opposed to such a covenant since its effect would be to increase the cost of an acquisition (due to an assumed debt repayment), a factor that could well lower the price of any tender offer (thereby impacting shareholders)."); *id.* ("[I]t would be very difficult for [MetLife] to demand takeover protection in public bonds. Such a requirement would effectively take [MetLife] out of the public industrial market."); *id.* at 1521 ("[I]t is undisputed that investors like plaintiffs recognized that companies like RJR Nabisco strenuously opposed additional restrictive covenants that might limit the incurrence of new debt or the company's ability to engage in a merger."). To the extent that many companies share this view, it may be untenable for a court to conclude that bondholders would not have committed their capital unless a bargain was struck for a protective term.

Furthermore, courts are often reluctant to imply terms when there are explicit terms that are relevant to the issue in dispute. *See, e.g., id.* at 1517 (noting that an implied covenant in a contract "will only aid and further the explicit terms of the agreement and will never impose an obligation which would be inconsistent with other terms of the contractual relationship") (internal quotation omitted); *cf.* Woodard v. Southwest States, Inc., 384 S.W.2d 674, 674 (Tex. 1964) ("Where there exists a valid express contract covering the subject matter, there can be no implied contract."); *supra* note 78 (noting that express agreements can trump any alleged reasonable expectation). Although written agreements are rare in the close corporation context, *see supra* note 215 and accompanying text, a written indenture agreement is present whenever bonds are issued. *See, e.g., Metropolitan Life*, 716 F. Supp. at 1509 ("The bonds implicated by this suit are governed by long, detailed indentures, which in turn are governed by New York contract law."); CARY & EISENBERG, *supra* note 26, at 110 ("An indenture is a contract entered into between the borrowing corporation and a trustee. The trustee administers the payments of interest and principal, and monitors and enforces compliance with other obligations on behalf of the bondhold-

such a bondholder-friendly outcome illustrates that components of the shareholder oppression framework may have significance outside of the close corporation setting. In other contexts, therefore, the oppression framework may also alter the results that are presently generated by conventional legal doctrines.

CONCLUSION

Although both courts and commentators compare oppression's reasonable expectations inquiry to an implied-in-fact contract analysis, such a comparison is too readily made. The similarity between the two frameworks is, at best, present in spirit rather than in letter. While it is true that contractual themes are echoed by oppression law's inquiry into shareholders' "understandings" and "bargains," it is equally true that contract law and oppression law differ in the level of protection they offer to shareholders. Although contract law has the tools to safeguard the close corporation investor, this Article has argued that the liability restrictions and damages limitations associated with the application of modern contract law will likely leave the minority shareholder vulnerable to oppressive majority conduct. In contrast, by focusing on what is actually transpiring in oppression decisions, this Article has shown that the oppression doctrine's use of pattern and conduct evidence, economic understandings, and buyout remedies results in vastly superior shareholder protection.

At bottom, the plight of the close corporation minority shareholder is real. Oppressive conduct breaches an actual bargain between the shareholders—a bargain that typically induces the minority's initial commitment of capital to the venture—and it provides an opportunity for an unchecked majority to steal the investment of the minority. Despite this broken "deal" and the potential for theft, however, contract law is unlikely to take the broader perspective that is necessary to adequately protect the minority investor. As a consequence, there is a need for the shareholder oppression doctrine and for the protection that it offers. Moreover, as this Article has noted, there may be bargains outside of the shareholder oppression context that are worthy of similar protection.

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ers as a group. The indenture defines the assorted obligations of the borrower, the rights and remedies of the holders of the bonds, and the role of the trustee.").

To the extent that the indenture contains explicit terms that can reasonably be construed to cover the situation, implying a protective term will be difficult. *Cf. Metro. Life*, 716 F. Supp. at 1508 ("RJR Nabisco defends the LBO by pointing to express provisions in the bond indentures that, *inter alia*, permit mergers and the assumption of additional debt.").

In short, the fundamental question of whether the shareholder oppression doctrine is needed in light of the established principles of contract law can now be answered. By picking up where contract law leaves off, the shareholder oppression doctrine serves a critical protective function that justifies its independent existence.