

TABLE OF CONTENTS

| | Page No. |
|--|----------|
| I. HISTORY AND PURPOSE OF DISSENTERS' RIGHTS STATUTES | 1 |
| II. MINNESOTA'S DISSENTERS' RIGHTS STATUTES | 1 |
| A. Chapter 302A..... | 1 |
| 1. Triggering Chapter 302A Dissenters' Rights..... | 2 |
| 2. Procedure for Exercising Dissenters' Rights | 3 |
| 3. Section 302A.751 - Fair Value Determinations | 4 |
| 4. Changes to the Model Business Corporation Act Appraisal Rights | 5 |
| B. Chapter 300 Consolidations | 6 |
| C. Chapter 49 Dissenters' Rights | 7 |
| D. Federal Bank Dissenters' Rights | 8 |
| III. PRELIMINARY LITIGATION ISSUES | 8 |
| A. Jurisdiction and Venue..... | 8 |
| B. Parties | 9 |
| C. Rules of Procedure..... | 9 |
| D. Neutral Appraiser or Battle of Experts?..... | 10 |
| E. Jury Trial?..... | 11 |
| F. Is a Dissenters' Rights Action a Shareholder's Exclusive Remedy? | 11 |
| G. Is a Waiver of Dissenters' Rights Valid? | 12 |
| H. Valuation Date | 12 |
| I. How Are Unexercised Options to Be Treated in the Valuation?..... | 13 |
| J. Interest on the Award..... | 14 |
| IV. THE DISSENTERS' RIGHTS TRIAL | 14 |
| A. Issues to Be Determined by the Court or Appraisers..... | 14 |
| 1. Has the dissenter met the procedural requirements of the statute? | 14 |

| | | |
|----|---|----|
| 2. | What is the “fair value”, “fair cash value” or “value” of the dissenter’s shares? | 14 |
| B. | Valuation Decisions | 16 |
| 1. | <i>Nardini v. Nardini</i> and Revenue Ruling 59-60..... | 16 |
| 2. | <i>MT Properties v. CMC</i> | 17 |
| 3. | <i>Foy v. Klapmeier</i> | 17 |
| 4. | <i>Spinnaker Software Corp. v. Nicholson</i> | 18 |
| 5. | <i>Pooley v. Mankato Iron & Metal, Inc.</i> | 18 |
| 6. | <i>American Sharecom, Inc. v. LDB International Corporation</i> | 18 |
| 7. | <i>Jundt Associates, Inc. v. Knappenberger</i> | 19 |
| 8. | <i>Advanced Communication Design, Inc. v. Follett</i> | 19 |
| 9. | <i>Doerr v. Arundel</i> | 20 |
| C. | The 302A Dissenters’ Rights Trial | 20 |
| 1. | The corporation’s case..... | 21 |
| a. | Company representatives | 21 |
| b. | Industry expert..... | 21 |
| c. | The company’s appraiser | 21 |
| 2. | The dissenters’ case | 21 |
| D. | Admissibility of Post-Valuation Date Evidence | 22 |
| 1. | Post-valuation year-end financial statements..... | 22 |
| 2. | Post-valuation changes in the company or industry | 22 |
| 3. | Post-valuation comparable transactions..... | 23 |
| V. | SUMMARY OF VALUATION TECHNIQUES | 23 |
| A. | Income Approaches..... | 23 |
| 1. | Conducting a discounted cash flow analysis..... | 23 |
| a. | Preliminary decisions..... | 23 |
| b. | Determining cash flow | 23 |
| c. | Discounting future cash flow | 24 |

| | Page No. |
|--|----------|
| 2. Advantages of discounted cash flow method | 24 |
| B. Asset Approaches..... | 24 |
| C. Market Approaches..... | 25 |
| 1. Prior Sales | 25 |
| 2. Comparable Sales..... | 25 |
| 3. Market Capitalization Techniques | 25 |
| VI. DISCOUNTS FROM ENTERPRISE VALUE..... | 26 |
| A. Background | 26 |
| B. Minority Discount..... | 27 |
| C. Illiquidity or Lack of Marketability Discount | 27 |
| D. “Key Person”/Noncompete Discount..... | 29 |
| 1. Rationale for key person discount | 29 |
| 2. Argument against key person discount | 29 |
| VII. ATTORNEY’S AND EXPERT’S FEES | 30 |
| A. Chapter 302A..... | 30 |
| B. Chapter 49 | 31 |
| C. Chapter 300 | 32 |
| CONCLUSION..... | 32 |
| APPENDIX | 33 |
| Treatises and Articles on Dissenters’ Rights or Valuation Generally..... | 33 |
| Practitioners’ Guide to Dissenters’ Rights in Five Easy Pieces..... | 34 |

DISSENTERS' RIGHTS IN MINNESOTA

Prepared by

Thomas S. Fraser

James E. Dorsey

Emily E. Duke

Fredrikson & Byron, P.A.

Minneapolis, Minnesota

November 2002

DISSENTERS' RIGHTS IN MINNESOTA **STATUTORY DEVELOPMENTS AND VALUATION ISSUES**

I. HISTORY AND PURPOSE OF DISSENTERS' RIGHTS STATUTES

At common law, merger and other fundamental corporate transactions required unanimous shareholder consent. This created a tyranny of the minority because a single shareholder owning one share could block a major transaction such as an acquisition or a merger that was in the best interests of the corporation.

In response to this problem, state legislatures began passing statutes that would enable corporations to engage in major transactions based on simple majority vote. In Voeller v. Neilston Warehouse Co., 311 U.S. 531, 536 n.6 (1941), the United State Supreme Court characterized the balancing act that state legislatures eventually achieved:

To meet the situation, legislatures authorized the making of changes by majority vote. This, however, opened the door to victimization of the minority. To solve the dilemma, statutes permitting a dissenting minority to recover the appraised value of its shares, were widely adopted.

The legislatures eliminated a shareholder's right to veto fundamental corporate changes. In its place, the legislatures gave dissenting shareholders the right to receive a cash payment for the "fair value" of their stock.

II. MINNESOTA'S DISSENTERS' RIGHTS STATUTES (See Appendix A)

A. Chapter 302A

Most dissenters' rights proceedings will be governed by Chapter 302A of the Minnesota Statutes. There are, however, also separate dissenters' rights statutes in Chapter 49 for Banks and Chapter 300 for certain Corporate Consolidations.

The Minnesota Chapter 302A corporate dissenters' rights statutes are based on Sections 80 and 81 of the Model Business Corporation Act. As such, Minn. Stat. §§ 302A.471-.473 are fairly similar to dissenters' rights statutes in other states. The statutes put most of the procedural burdens on the corporation on the theory that the corporation gained from the elimination of the minority

shareholders' veto power. A copy of Minn. Stat. §§ 302A.471-.473 (West Desk Book 2002-2003) and accompanying Reporter's Notes is set forth in Appendix A.

1. Triggering Chapter 302A Dissenters' Rights

Minn. Stat. § 302A.471, subd. 1 lists the following corporate actions that trigger dissenters' rights:

- a. certain material amendments of the articles of incorporation affecting rights or preferences of the shareholder;
- b. a sale, lease, transfer, or other disposition of substantially all of the corporate assets other than in the usual course of business;
- c. a merger;
- d. an exchange of shares with an acquiring corporation; or
- e. any other corporate action by shareholder vote where dissenters are entitled to payment for their shares.

See also Minn. Stat. § 302A.621, subd. 6 (specifying circumstances under which dissenters' rights are triggered in a merger of subsidiary); § 302A.601, subd. 4 (dissenters' rights for shareholders of corporation involved in a merger or exchange with a domestic limited liability company Chapter 322B); and § 302A.651 (foreign corporation surviving merger must agree to be served in Minnesota in a dissenters' rights case and must agree to pay dissenters promptly).

The only published Minnesota case that discusses what actions trigger dissenters' rights held that the statutory list of triggering actions includes amendments to articles and bylaws that eliminated a shareholder's right to veto the election or appointment of directors or officers in a closely-held corporation. Whetstone v. Hossfeld Mfg. Co., 457 N.W.2d 380 (Minn. 1990). The court noted that minority investors in closely held corporations frequently insist on such protections at the time the corporation is formed. Id. at 382.

In an unpublished opinion, Bowman v. MWCG Export Co., 1991 WL 30342 (Minn. Ct. App.), the Court of Appeals held that an invalid corporate action does not trigger dissenters' rights. Interestingly, the corporate action was deemed invalid because notice of dissenters' rights had not been given.

Occasionally the corporation and one or more shareholders may disagree as to whether a corporate action triggers dissenters' rights. In that event, the shareholders may bring an action

requesting the court to order the corporation to offer dissenters' rights. This was done in both Whetstone, *supra*, and Foy v. Klapmeier, 1993 WL 246127 (D. Minn.), *modified*, 992 F.2d 774 (8th Cir. 1993). The corporation may have to pay the successful shareholder's attorneys fees and costs under Minn. Stat. § 302A.467 (court may award expenses, including attorneys' fees and disbursements to shareholder who proves that corporation has violated Chapter 302A).

2. Procedure for Exercising Dissenters' Rights

Minn. Stat. § 302A.473 specifies the following procedures for asserting dissenters' rights.

- a. Corporation's first notice to all shareholders. The notice of the shareholder meeting must inform each shareholder of the right to dissent from the proposed corporate action. A copy of the dissenters' rights statutes and a summary of the procedure under those sections must also be included. Minn. Stat. § 302A.473, subd. 2.
- b. Dissenters must notify corporation of intent to dissent. In order to preserve their dissenters' rights, shareholders must file with the corporation in advance of the vote "a written notice of intent to demand the fair value of the shares" and must not vote their shares in favor of the proposed action. Minn. Stat. § 302A.473, subd. 3.
- c. Corporation's second notice. After the vote, the dissenter is entitled to another notice from the corporation describing the procedures for depositing the shares with the corporation and receiving payment for those shares. Minn. Stat. § 302A.473, subd. 4.
- d. Dissenter demands payment and deposits share certificates with corporation. Within 30 days after receiving the notice, the dissenter must demand payment and deposit certificated shares with the corporation. Minn. Stat. § 302A.473, subd. 4(b).
- e. Corporation pays its estimate of fair value. The corporation must remit "the amount the corporation estimates to be the fair value of the shares, plus interest" accompanied by certain financial information, the basis for the corporation's estimate of fair value, and a description of the procedures for demanding supplemental payment. Minn. Stat. § 302A.473, subd. 5.
- f. Dissenter demands supplemental payment. The dissenter then has 30 days to notify the corporation of his or her estimate of the fair value of the shares and demand the difference. Minn. Stat. § 302A.473, subd. 6.

g. Corporation pays or files petition. Upon receipt of the dissenter's demand, the corporation has 60 days either to pay the amount demanded (or settle the matter for a lesser amount) or file a petition in court to obtain a judicial determination of the fair value of the shares. If the corporation does not act within the 60 day period, it is liable for the demanded amount. Minn. Stat. § 302A.473, subd. 7.

In determining whether parties have complied with these procedures, Minnesota courts have required only substantial compliance. See, e.g., Olson v. Tufford, 392 N.W.2d 281, 283-85 (Minn. Ct. App. 1986) (overly long and complicated description of procedures substantially complied with statutory requirement; sending tax return instead of balance sheet and income statement did not substantially comply; dissenter's 16-day late demand for supplemental payment substantially complied with time requirement). In some other jurisdictions, the requirements are more strictly enforced. See, e.g., Raab v. Villager Industries, Inc., 355 A.2d 888 (Del. 1976) (shareholder lost dissenters' rights for failing to have wife, as joint tenant owner of shares, sign demand for payment); McGowan v. Grand Island Transit Corp., 80 A.D.2d 731, 437 N.Y.S.2d 158 (1981) (shareholder lost dissenters' rights because demand for payment was 8 days late). But see Hunter v. Vercelloti, 649 N.E.2d. 557 (Ill. Ct. App. 1995) (dissenter did not tender her shares until after court proceedings began, but was allowed to tender them late and receive corporation's estimated value therefor, while court determined "fair value").

3. Section 302A.751 - Fair Value Determinations

Aside from section 302A.471's list of triggering transactions, an "appraisal" action may also occur under section 302A.751, subd. 2, which authorizes a buy-out of one shareholder by another shareholder or the corporation. Under this provision, the court must determine the "fair value" of the selling shareholder's shares using the valuation procedures set forth in the dissenters' rights statute. Zenanko v. Vukelich, 1991 WL 6379 (Minn. Ct. App.) (shares had fair value of zero).

However, the valuation date set forth in 302A.751 is different from that stated in 302A.473. The valuation date under 302A.751 is "the date of the commencement of the action or as of another date found equitable by the Court." Minn. Stat. § 392A.751, subd. 2. This timing difference can have a significant impact on the value of the shares appraised. See, e.g., Diebold v. Diebold, 1997 WL 309366 (Minn. Ct. App. 1997) (unpublished opinion). In deciding whether to authorize a buy-out, a court is directed under section 302A.751, subd. 3a to consider any buy-sell agreements that may exist among the shareholders as presumptively reflecting "the parties' reasonable expectations concerning matters dealt with in the agreements." The question arises, however, whether a price formula in a buy-sell agreement is therefore binding on the court once it determines that a buy-out is appropriate. Compare Pedro v. Pedro, 463 N.W.2d 285 (Minn. Ct. App. 1990) (before subd. 3a was amended in 1994 to include language concerning buy-sell agreements, court grants minority shareholder recovery in excess of that provided in buy-sell agreement) with Perry v. Perry, 1995 WL 550902 (Minn. Ct. App.)

(although minority shareholder alleged fraud and unfairness, court holds that he is limited to price set forth in buy-sell agreement).

4. Changes to the Model Business Corporation Act Appraisal Rights

In 1999, the Committee on Corporation Laws of the Section of Business Law made significant changes to the Model Business Corporation Act (“MBCA”) Chapter 13 dissenter’s rights provisions including, changing the title of Chapter 13 to “Appraisal Rights.” The most significant changes are summarized below:

- a) The new definition of “fair value” directs courts to use appraisal methods consistent with evolving economic concepts, stating that courts are to use “customary and current valuation concepts and techniques generally employed for similar businesses in the context of the transaction requiring the appraisal.” The previous definition was regarding appraisal methodology. 3 MBCA § 13.01 (3rd Ed. 1998/99 Supp.).
- b) The new definition of “fair value” specifies that discounts for lack of marketability or minority status are not to be taken in the valuation process. Id.
- c) Elimination of appraisal rights where there is public market for the shares and the shareholders are likely to receive fair value when they sell their shares in the market after announcement of an appraisal-triggering transaction (called the Market Exception To Appraisal Rights in the MBCA comments). The theory behind this change is that where an efficient market exists, the market price will adequately approximate the “fair value” of the shares. Therefore, no appraisal is necessary. See 3 MBCA § 13.01 Official Comment 1; § 13.02(b) and Official Comment 2 (3rd Ed. 1998/99 Supp.).
- d) Safe harbor from proposed market exception to appraisal rights in specified conflict transactions involving controlling shareholders or senior executives or directors. Because controlling shareholders, senior executives, or directors have the ability to affect the market price of a company’s stock, a transaction giving rise to appraisal rights will not be subject to the proposed market exception rule unless certain procedural standards are met. Id. and § 13.02(b) and Official Comment 3 (3rd Ed. 1998/99 Supp.).
- e) Corporations may eliminate or limit appraisal rights for holders of preferred shares. They may do so via their Articles of Incorporation. There is a one-year waiting period with respect to already-outstanding shares at the time an already-existing corporation chooses to so amend its Articles. 3 MBCA § 13.02(c) and Official Comment 4 (3rd Ed. 1998/99 Supp.).

f) The section dealing with exclusivity of the appraisal remedy is clarified to reflect that appraisal is not the exclusive remedy when the corporate action “was procured as a result of fraud or material misrepresentation” or when it was not properly effected under the corporate laws, articles, bylaws, or board resolution authorizing the corporate action. 3 MBCA § 13.02(d) and Official Comment 5 (3rd Ed. 1998/99 Supp.).

g) Once a shareholder decides to exercise the appraisal rights and deposits her or his shares with the company, the shareholder ceases to be a shareholder and loses all rights as such unless she or he withdraws from the appraisal process by a specified deadline. 3 MBCA § 13.23(b) and Official Comment (3rd Ed. 1998/99 Supp.).

h) The proposed changes specifically state that there is no right to a jury trial. 3 MBCA § 13.30(d) and Official Comment (3rd Ed. 1998/99 Supp.).

B. Chapter 300 Consolidations

The dissenter’s rights provisions of Chapter 300 apply only to consolidation of a few general business corporations formed prior 1933. Although Chapter 300 is the principal body of law applicable to state chartered banks, trust companies, and insurance companies, the consolidation provisions of Chapter 300 giving rise to dissenter’s rights, *i.e.* Minn. Stat. § 300.14, specifically does not apply to these types of corporations. A corporate shareholder who objects to a proposed consolidation must vote against the consolidation and object to it in writing at or before the time the consolidation vote is taken. Minn. Stat. § 300.16, subd. 1. If the shareholder has no voting rights s/he must demand in writing that the consolidated corporation pay the “*fair cash value*” of her or his stock. *Id.* Once the written demand is made, the shareholder ceases to be a shareholder and has no rights with respect to the stock, except the right to receive payment for it. Minn. Stat. § 300.16, subd. 3. If the parties cannot agree to the fair cash value, either can petition the District Court to appoint three appraisers who determine the value as of the day before the consolidation vote was taken. Either party then has ten days to object to the appraisers’ determination and obtain a bench trial. The cost of the appraisers is shared 50-50 between the corporation and objecting shareholder unless the corporation offered less than the amount determined by the appraisers. In that situation, the court may shift the costs and attorneys’ fees entirely onto the corporation. It is important to note that if either party intends to appeal the resulting court judgment, they have only *ten days after the entry of the judgment to appeal*. Minn. Stat. § 300.16, subd. 2.

C. Chapter 49 Dissenters' Rights

Under Chapter 49, shareholders in the state-chartered banks have somewhat different dissenters' rights. When two or more state-chartered banks merge or consolidate, the dissenters' rights are governed by Minn. Stat. § 49.41. When a state-chartered bank becomes a national banking association through merger, consolidation, or conversion, the dissenters' rights are governed by Minn. Stat. § 49.43.

1. State Bank-State Bank, Minn. Stat. § 49.41: Within 20 days after the shareholder meeting at which the merger/consolidation is voted upon takes place, any shareholder who voted against the corporate action may object thereto and demand payment for their stock. Then, within 60 days after the merger/consolidation becomes effective, the shareholder may apply to the District Court for the appointment of three appraisers who will determine the “*value*” of the stock. The appraisers then make and certify a written estimate of the value of the stock “*at the time of the appraisal.*” The statute does not, however, define the “time of the appraisal.” Once the bank pays the appraised amount, the dissenters cease to be shareholders. The cost of the appraisers is split 50-50 between the bank and the dissenters.

2. State Bank Becomes National Banking Association, Minn. Stat. § 49.43: Shareholders in state-chartered banks which become national banking associations, either through conversion, merger or consolidation, who vote against the corporate action, may either following the state remedy provided in Minn. Stat. § 49.43 or “any rights given by applicable law of the United States.” Under the state-law scheme, the shareholders may object to the corporate action within 20 days after the vote, and demand payment for their shares. The demand is made for the par value or book value of the stock—whichever is greater. If the bank does not pay the demanded amount, the shareholder may, within 60 days, apply to the District Court for the appointment of three appraisers. The appraisers determine the “*value*” of the shareholder's stock “*at the time of the appraisal.*” The statute does not, however, define the “time of the appraisal.” After the bank makes payment, the dissenter ceases to be a shareholder. The bank and dissenters split the cost of the appraisers 50-50.

D. Federal Bank Dissenters' Rights

When national banks merge or consolidate, or when national and state banks merge or consolidate into a national bank, dissenters' rights arise. See 12 U.S.C. §§ 215 and 215a. Both the dissenters and the surviving entity select an appraiser. The two appraisers then select a third. The resulting three-person panel then determines the "value" of the dissenter's shares by majority-vote. If the dissenter disagrees with the panel's appraisal, or if either party fails to appoint an appraiser to participate in the appraisal committee, the dissenters may request that the Office of the Comptroller of Currency ("OCC") re-appraise or appraise the value of the shares. 12 U.S.C. §§ 215(c) (consolidation) and 215a(c) (merger). The OCC appraisal is "final and binding." 12 U.S.C. §§ 215(d) and 215a(d).

The statutes do not explicitly provide for court review of OCC valuations, but courts have unanimously concluded that review is available in U.S. District Courts under the Administrative Procedure Act. Although the OCC appraisal is appealable, the chances of overturning an undesirable appraisal are slim, as the standard of review is "arbitrary and capricious."

The OCC has broad discretion in determining "value," as the term is not defined in the statute. The OCC has settled into a basic formula that it applies to each case. This formula is essentially a weighted average of three valuation methods, minus a discount for lack of marketability of the stock in appropriate cases. The three methods evaluated are: market value, investment value, and book value. Unless there is a market maker for the stock or the stock is publicly traded, the OCC will not consider the market method. Therefore, in most cases submitted to the OCC the market value factor receives 0% weight in the final value calculation. For the investment value, the OCC picks a peer group of banks with readily available earnings data develops an earnings multiple therefrom, and applies the multiple to the bank stock in question. This method receives a 75% weight (where there is no public market for the stock) in the final calculation. For the book value method, the OCC analyzes the market price to book value ratio for the peer group banks and applies a ratio to the book value for the bank stock in question. This method receives a 25% weight (where there is no public market for the stock) in the final value calculation. Finally, the OCC applies a 15% lack of marketability discount where there is no market maker or public market for the stock. Thus, the OCC's most current valuation formula for non-publicly traded bank stock is:

$$\begin{aligned} & \text{Investment Value} \times 75\% \\ & + \text{Adjusted Book Value} \times 25\% \\ & - 15\% \text{ Marketability Discount} \end{aligned}$$

III. PRELIMINARY LITIGATION ISSUES

A. Jurisdiction and Venue

The 302A petition must be filed in the county in which the “registered office” of the corporation is located. Minn. Stat. § 302A.473, subd. 7. If the surviving corporation is a foreign corporation, the petition is filed in the county of the last registered office of the nonsurviving entity. *Id.* However, in a case in which the petitioner failed to file in the proper county, Judge Danielson ruled that this was a venue issue, not a jurisdictional defect. See Whetstone v. Hossfeld Manufacturing Co., No. 88-16380 (4th Jud. Dist. Mar. 13, 1991). Under Chapter 49, the application to the district court must be filed in the county of the “principal place of business” of the surviving corporation. Minn. Stat. §§ 49.41 and 49.43. Under Chapter 300, the petition is filed with the district court in the county where the “principal office” of the consolidated company is located. Minn. Stat. § 300.16, subd. 2.

One interesting question that arises early on in Chapter 302A cases is whether the petition can be filed in or removed to federal court, assuming diversity jurisdiction is otherwise present. This issue arises because the statute specifies the county in which the petition must be filed and states that “[t]he jurisdiction of the court is plenary and exclusive.” Minn. Stat. § 302A.473, subd. 7. No Minnesota case has specifically addressed this issue. Indeed, Chapter 302A dissenters’ cases in Minnesota and other states with similar statutes have been filed in (or removed to) and decided in federal court without any apparent jurisdictional challenge. E.g., Foy v. Klapmeier, 992 F.2d 774 (8th Cir. 1993); Multitex Corporation of America v. Dickinson, 683 F.2d 1325 (11th Cir. 1982); Hunter v. Mitek Indus., Inc., 721 F. Supp. 1102 (E.D. Mo. 1989); Perlman v. Permonite Manufacturing Co., 568 F. Supp. 222 (N.D. Ind. 1983).

B. Parties

Under Chapter 302A, the corporation must name in the petition all shareholders who have properly exercised their dissenters’ rights. What if the corporation and the shareholder disagree over whether the shareholder has jumped through all of the hoops necessary to exercise dissenters’ rights? Caution dictates that the corporation include that shareholder in the petition and then ask the court to determine that the shareholder is not entitled to be a dissenter. Otherwise, if a court later determines that the corporation should have included that shareholder in the petition, the court could find that the statute requires the corporation to pay the omitted shareholder the amount demanded by the shareholder even if it exceeds the fair value as determined by the court.

Conversely, under Chapter 49, it is the dissenters who must initiate the District Court proceeding and ask the judge to appoint the three appraisers. Chapter 300, on the other hand, allows either the corporation or the dissenting shareholders to initiate the District Court proceedings and ask the Court to appoint the appraisal panel.

C. Rules of Procedure

The legislature amended Minn. Stat. § 302A.473, subd. 7 in 1993 to provide that a corporation must serve a summons and a copy of its petition on all dissenters as set forth in the rules of civil

procedure and that nonresident dissenters may be served by registered or certified mail, or by publication. The amendment also provides that, except as otherwise set forth in the statute, the rules of civil procedure apply to dissenters' rights proceedings. This resolved confusion that existed under the old statute regarding procedures for commencing the action and service of process.

The other statutes do not mention service or the rules of procedure. However, the Bank statutes appear to leave the procedure for the appraisal itself to the sound discretion of the trial court. See Minn. Stat. §§ 49.41 and 49.43.

D. Neutral Appraiser or Battle of Experts?

The Chapter 302A dissenters' rights statute provides the court with the option of appointing appraisers, with powers specified by the court, "to receive evidence on and recommend the amount of the fair value of the shares." In this respect, the statute provides a procedure similar to that in the eminent domain statute where court-appointed commissioners conduct hearings and determine the fair market value of the property in condemnation. Unlike the eminent domain statute, the corporate statute expressly makes the court-appointed appraisers an optional procedure. As set forth in the Reporter's notes to Minn. Stat. § 302A.473, subd. 7, "[b]ecause of the highly technical nature of valuation proceedings, the court may, for all intents and purposes, permit [the court-appointed appraisers] to find the fair value of the shares." Most of the cases litigated so far in Minnesota have not used this procedure. Instead, the parties have presented their evidence directly to the court rather than to court-appointed appraisers.

However, in Schaub v. Kortgard, 372 N.W.2d 427 (Minn. Ct. App. 1985), also a section 302A.751 buy-out proceeding, the trial court appointed an independent appraiser and adopted the appraiser's determination of fair value, which depended in part on the appraiser's treatment of a shareholder's loan as equity. On appeal, the Court of Appeals held that the trial court may not adopt the appraiser's valuation, which is only a recommendation, without making appropriate findings. The court did hold that it could be within a trial court's equitable discretion to treat a loan as a capital contribution. See also Zenanko v. Vukelich, 1991 WL 6379 (Minn. Ct. App.) (statute does not actually authorize a delegation of the court's equitable powers to the appraiser).

In Foy v. Klapmeier, 1993 WL 246127 (D. Minn. 1992), modified, 992 F.2d 774 (8th Cir. 1993), Judge Alsop appointed an independent appraiser and the parties also presented their own experts.

Under Chapters 49 and 300, the statute envisions an entirely different proceeding. There, the statutes explicitly delegate the valuation to the court-appointed appraisers. Nevertheless, if the Court allows the parties to present expert testimony to the appraisal panel (a procedure which could be quite expensive to the parties since they will ultimately pay the appraisal panel too), the proceeding before the appraisers could become a battle of the parties' experts seeking to persuade the neutrals.

E. Jury Trial?

Unlike the eminent domain statute, the Chapter 302A statute does not expressly accord the parties a right to a jury trial. Although “fair value” cases have been tried with and without juries in Minnesota, the Minnesota Court of Appeals has ruled that a jury trial is not available as a matter of right because a dissenters’ rights case is a special statutory proceeding akin to a case in equity. American Sharecom, Inc. v. LDB International Corporation, 1995 WL 32150 (Minn. Ct. App.) pet. for review denied (August 3, 1995). The parties and the court may agree to employ a jury either as a binding or advisory fact-finder. Cf. Pedro v. Pedro, 463 N.W.2d 285 (Minn. Ct. App. 1990), pet. for review denied (January 24, 1991) (where parties had not agreed to the use of a jury in a section 302A.751 case, trial court could use jury’s decision as advisory only).

Chapter 49 and 300 appraisals, being determined by court-appointed appraisers, clearly do not anticipate a right to a jury trial. Moreover, Chapter 49 does not even envision a right of appeal to the District Court of the appraisers’ decision. Conversely, Chapter 300 gives both parties a right to appeal the appraisers’ valuation within 10 days after it is filed in court. Minn. Stat. § 300.16, subd. 2. “If an objection is filed, it must be tried summarily by the court and judgment rendered on it.” Id. Thus, it appears that court review of the Chapter 300 appraisers’ valuation does not accord either party a right to a jury trial.

F. Is a Dissenters’ Rights Action a Shareholder’s Exclusive Remedy?

Only Chapter 302A explicitly addresses this issue. Minn. Stat. § 302A.471, subd. 4, provides that shareholders who exercise their dissenters’ rights “do not have a right at law or in equity to have a corporate action...set aside or rescinded except when the corporate action is fraudulent with regard to the complaining shareholder or the corporation.” Thus, the triggering of dissenter’s rights forecloses other shareholder claims on the essential fairness of the triggering transaction. Sifferle v. Micom Corp., 384 N.W.2d 503 (Minn. Ct. App. 1986). In Sifferle, the court held that, unless the subject transaction was fraudulent, a dissenter’s sole remedy is under the dissenters’ rights statutes. Id. at 506-07. The court ruled that squeezing out minority shareholders in a public corporation in order to take the company “private” was permitted because the statute specifically states that no business purpose is required for such a merger. Minn. Stat. § 302A.601, subd. 1. Thus, a squeeze-out merger is not a breach of the majority shareholder’s fiduciary duty so as to trigger the “fraud” exception to the statutory bar against attack of the underlying corporate transaction. Minn. Stat. § 302A.471, subd. 4 (transaction triggering dissenters’ rights may not be set aside or rescinded unless fraudulent). See also Broin v. National Computer Systems, Inc., 1991 WL 204460 (Minn. Ct. App.) (dissenters’ rights is sole remedy unless merger accomplished by deception, illegality, or a breach of fiduciary duty); Popp Telcom v. American Sharecom, Inc., 210 F.3d 928, 935-36 (8th Cir. 2000) (shareholder may sustain fraud action separate from valuation proceeding where fraud alleged went to underlying validity of squeeze-out merger).

One trial court has ruled that a dissenter who has been served with a petition under Minn. Stat. § 302A.473, subd. 7 may not bring a counterclaim attacking the terms of the underlying triggering transaction. American Sharecom, Inc. v. LDB International Corporation, No. 92-17922 (4th Jud. Dist. Minn. Feb. 24, 1993) (counterclaim alleging unfair dealing among corporate insiders dismissed without prejudice so that respondents could bring a separate action at law).

G. Is a Waiver of Dissenters' Rights Valid?

No American case discusses whether a corporation's articles of incorporation may exclude dissenters' rights. In all likelihood, any such provisions would be invalid. As one commentator wrote on this issue 60 years ago, it "would be an idle gesture to confer a right which can be rendered nugatory by the same group against whose actions it was designed to protect the minority." Levy, *Rights of Dissenting Shareholders to Appraisal and Payment*, 15 Cornell L. Q. 420, 430 (1930). In addition, several English cases hold that any attempt to limit dissenters' rights in a corporation's charter documents is ineffective and unenforceable. See Bisgood v. Henderson's Transvaal Estates, Ltd., [1908] 1 Ch. 743; Payne v. The Cork Co., [1900] 1 Ch. 308.

H. Valuation Date

A key issue is the date of valuation. The Chapter 302A statute is explicit -- the inquiry is what was the fair value "immediately before the effective date of the corporate action" that triggers dissenters' rights. Minn. Stat. § 302A.473, subd. 1(c). According to the Reporter's Notes, this is consistent with the statutory scheme to preserve the dissenters' shareholder rights until the effective date of the corporate action. Because the term "date" does not necessarily refer to a day but may refer to a time or hour (according to the dictionary definition), the valuation date is either a moment before the effective time of the merger or the day before, a distinction without a difference in most cases. Note that this valuation date automatically requires the corporation to update its appraisal because its earlier estimates of fair value required to be sent to the shareholder in advance may be different from its valuation "immediately before the effective date."

The Chapter 300 statute clears up this ambiguity, stating that the valuation date is "the day before the consolidation vote was taken." Minn. Stat. § 300.16, subd. 1. Conversely, the banking statutes are quite vague as to the valuation date, stating only that the court-appointed appraisers shall "estimate the value of the stock at the time of the appraisal." Minn. Stat. §§ 49.41 and 49.43. Thus, it is unclear if they mean the date the court-appointed appraisers write their report, a date chosen by the appraisers, or a date consistent with either a Chapter 302A valuation or a Chapter 300 valuation.

A more interesting issue is whether the corporate action itself, including any valuation inherent therein, is admissible on the valuation issue. This has ramifications that are not immediately apparent. If the fact of the squeeze-out merger is admissible, then it is difficult to argue that a marketability discount

is applicable. The squeeze-out merger creates the market for the stock -- it is a forced purchase. See discussion of discounts in Part VI below.

I. How Are Unexercised Options to Be Treated in the Valuation?

In a dissenters' rights case, the court essentially performs an exercise in long division. The court determines the value of the whole corporation (the numerator in the division problem) and then divides that "enterprise value" by the number of shares outstanding at the time of the act that gave rise to the dissenters' rights (the denominator). This gives the court a per share value of the corporation. If the majority shareholders own unexercised, in-the-money (the exercise price is less than the market price) options, a question arises as to whether those options should be counted.

None of the dissenters' rights statutes refer to options. The Chapter 49 Bank dissenter statutes and the Chapter 300 statute require a valuation of the dissenter's or shareholder's "stock." They offer no guidelines on how to calculate the value of those specific shares. Chapter 302A calls for valuation of the shares of a corporation "immediately before the effective date of the corporate action . . ." that gave rise to the dissenters' rights. The definitions section of Chapter 302A defines *share* as "one of the units, however designated, into which the shareholders' proprietary interests in a corporation are divided." Minn. Stat. § 302A.011, subd. 28. Chapter 302A also gives no guidance as to how the fair value should actually be calculated.

While the Minnesota statutes are silent on the issue, many appraisers -- particularly accountants mindful of the GAAP requirement to include such options when calculating earnings per share on a fully diluted basis -- will argue that unexercised, in-the-money options should be counted in calculating fair value of a dissenter's shares. Only one Minnesota case has addressed this issue, and there the court ruled that unexercised options of insiders need not be included in determining the value of a dissenter's shares when evidence of the value of the options was wholly speculative. American Sharecom, Inc. v. LDB International Corporation, 1995 WL 321540 (Minn. Ct. App.) pet. for review denied (August 3, 1995). In that case, the insiders tried to treat the options as if they had been exercised but they failed to include in their valuation of the company either the exercise price for the shares or the company's tax benefit from deducting the spread, which is considered compensation and therefore deductible for tax purposes. Indeed, both the trial court and the Court of Appeals determined that the insiders could not have afforded to exercise the options.

The only case outside of Minnesota to have addressed this issue is Lichtman v. Recognition Equipment, Inc., 295 A.2d 771 (Del. Ch. 1972). In that case, a dissenting shareholder sued to recover the value of his unexercised stock options that were being lost in the merger to which he had dissented. The court ruled that such options would not be counted. The court reasoned that "[t]he right to appraisal is purely statutory" and that such a right is "limited to stockholders of the merged corporation." Id. at 772. The court then concluded that "[t]he sole issue raised by a petition for appraisal is value of the defendant's stock." Id. (emphasis added); see also Gamble v. Penn Valley Crude Oil Corp., 34

Del. Ch. 359, 364, 104 A.2d 257, 260 (1954) (until options are exercised, status of option holder is not comparable to that of shareholder).

J. Interest on the Award

To compensate for the delay between loss of his or her stock and the ultimate judicial resolution of “fair value,” a Chapter 302A dissenter is entitled to interest on any award beginning five days after the effective date of the corporate transaction that triggered the dissenters’ rights. Minn. Stat. § 302A.473, subds. 1(d) and 7. See American Sharecom, Inc. v. LDB International Corporation, 1995 WL 321540 (Minn. Ct. App.) pet. for review denied (August 3, 1995). The interest rate is the pre- and post-judgment interest rate set annually under Minn. Stat. § 549.09 (5% in 2000 and 6% in 2001). The other dissenters’ rights statutes do not mention interest.

IV. THE DISSENTERS’ RIGHTS TRIAL

A. Issues to Be Determined by the Court or Appraisers

1. Has the dissenter met the procedural requirements of the statute?

In a 302A proceeding, the court must determine “whether the shareholder or shareholders in question have fully complied with the requirements of this section.” Minn. Stat. § 302A.473, subd. 7. The other dissenters’ rights statutes, which do not have the complex procedural requirements of Chapter 302A, do not even mention the issue. In most cases, this is not an issue. If it is, the question can be presented to the court through a motion for summary judgment or litigated at the trial if a fact issue is present. Corporations should not expect to have much success in disqualifying those shareholders who made clear their intention to dissent even if they did not follow the statute precisely. Judicial leniency on procedural issues is likely, as exhibited by the Court of Appeals’ holding that a dissenter’s late notice “substantially complied” with the “directory time provisions” of the statute where the corporation’s mailing was deficient and the corporation suffered no prejudice. Olson v. Tufford, 392 N.W.2d 281, 284-85 (Minn. Ct. App. 1986) (Chapter 302A case).

2. What is the “fair value”, “fair cash value” or “value” of the dissenter’s shares?

CHAPTER 302A

“Fair value” is defined by Chapter 302A as follows: “the value of the shares of the corporation immediately before the effective date of the corporate action . . .” that gave rise to the dissenters’ rights. Minn. Stat. § 302A.473, subd. 1.

This less-than-helpful definition has left much room for differences of opinion among appraisers and courts. Appraisers generally start their analysis with the familiar “willing buyer-willing seller”

definition of fair market value, but it is not controlling. In other states, the dissenters' statutes sometimes use the term "fair market value" or "cash value," though most refer to "fair value." Some cases have strained to distinguish the two concepts; however, at least one law review article finds such efforts pointless. Note, *Valuation of Dissenters' Stock Under Appraisal Statute*, 79 Harv. L. Rev. 1453, 1456 n. 18 (1966) (the various terms are synonymous). Those cases that do pay attention to this distinction suggest that "fair value" is a broader term that refers to the "intrinsic value" of shares and is not pegged to a "market" price. This concept, it is said, is intended to address those corporations, notably family-owned and other closely held corporations, that have no market for their shares. The only other guidance on the "fair value" issue provided by the statute is that the determination is to be made by "taking into account any and all factors the court finds relevant, computed by any method or combination of methods that the court, in its discretion, sees fit to use, whether or not used by the corporation or by a dissenter." Minn. Stat. § 302A.473, subd. 7. The Reporter's Notes to subdivision 7 state:

The court has complete control of the proceedings and may use any valuation method or combination of methods it sees fit, as long as the court finds the result to be the fair value of the shares as of the effective date of the action. No method is recommended because the different methods of measuring value (market, book, replacement, capitalization of earnings, etc.) are neither right nor wrong, but merely appropriate in different situations.

See Spinnaker Software Corp. v. Nicholson, 495 N.W.2d 441, 444 & n.1 (Minn. Ct. App. 1993) (quoting statute and Reporter's Notes). Thus, the results of nearly any recognized appraisal method may be received in evidence. While there are only a few broad categories of valuation techniques, the variations within each of the major categories can be substantial, and application of these techniques often leaves much to the individual judgment of the appraiser. Accordingly, the trial usually ends up as the classic battle of the valuation experts, with the court retaining broad discretion to choose any appraisal method or combination of methods, whether or not used by any of the parties.

In the only dissenters' rights cases where valuation issues have been decided by Minnesota appellate courts, the trial court's broad discretion was confirmed. In MT Properties v. CMC Real Estate Corp., 481 N.W.2d 383, 387 n.8 (Minn. Ct. App. 1992), the Court of Appeals, quoting an Iowa case, stated that "'fair value' [is] not susceptible of determination by precise mathematical computation and no one formula or figure is binding or conclusive." Similarly, in Spinnaker Software Corp. v. Nicholson, No. CT 90-004311 (4th Jud. Dist. Minn. June 6, 1992), aff'd, 495 N.W.2d 441 (Minn. Ct. App. 1993), the Court of Appeals highlighted the broad discretion of the trial court by citing the statute and Reporter's Notes. Furthermore, the Spinnaker court rejected the notion that the purchase price of a corporation is presumed to be its fair value for purposes of determining the fair value of a dissenting shareholder's shares. 495 N.W.2d at 444-45.

These cases also confirm that the purpose of a dissenters' rights proceeding is to value the corporation as a whole rather than the individual shares of a shareholder. MT Properties, 481 N.W.2d at 387 & n.3 (court required to value corporation as a whole rather than individual shares). This value is often referred to as the "enterprise" value. Foy v. Klapmeier, 1993 WL 246127 (D. Minn.), modified, 992 F.2d 774 (8th Cir. 1993).

CHAPTER 49 (BANKS) AND CHAPTER 300

The bank dissenters' rights statutes do not define "value" and no case-law interpreting the term exists. See Minn. Stat. §§ 49.41 and 49.43. Indeed, it is not even clear if the appraisers are or should be given any guidance from the court as to how to calculate "value" of the dissenter's "stock."

Likewise, Chapter 300 also lacks a definition of "fair cash value." Minn. Stat. § 300.16 gives the court no guidance as to how it should calculate the fair cash value of the stock, and no case law. That helps us to understand the term. The only case, dating back to 1932, discussing the dissenters' remedy is Patterson v. Shattuck Arizona Copper Co., 244 N.W. 281 (Minn. 1932). There, the court simply sought to treat dissenters "fairly", and fashioned relief that it thought was fair; the court did not explain any principles of valuation to support its findings, and its reasoning is so old that the case is of little or no use today.

B. Valuation Decisions

1. Nardini v. Nardini and Revenue Ruling 59-60.

In Minnesota, trial courts grappling with dissenters' cases have borrowed concepts established in divorce cases to assist them in reaching their decisions. The most commonly cited case is Nardini v. Nardini, 414 N.W.2d 184 (Minn. 1987), in which the Minnesota Supreme Court stated:

There is, of course, no universal formula for determining the value of a closely held business. No matter how experienced and objective the appraiser, the valuation of a business is an art, influenced by various subtle and subjective factors. . . . In any case a sound valuation requires not only a consideration of all relevant facts but also the application of common sense, sound and informed judgement, and reasonableness in the process of "weighing those facts and determining their aggregate significance." 414 N.W.2d at 189-90 (quoting Rev. Rul. 59-60).

In Nardini, the court suggested that Rev. Rul. 59-60, a guide to the valuation of closely-held corporations in the estate and gift tax area, provides a helpful guide in resolving valuation disputes. While a cynical reading of this Revenue Ruling might be that it merely advises consideration of all relevant factors, its listing of certain factors and the accompanying discussion of them do provide a

helpful checklist for the organization and presentation of appraisal testimony. As described in Nardini, the factors cited in Rev. Rul. 59-60 are as follows:

1. The nature of the business and the history of the enterprise from its inception.
 2. The economic outlook in general and the condition and outlook of the specific industry in particular.
 3. The book value of the stock and the financial condition of the business.
 4. The earning capacity of the company.
 5. The dividend-paying capacity.
 6. Whether or not the enterprise has goodwill or other intangible value.
 7. Sales of the stock and the size of the block of the stock to be valued.
 8. The market price of stocks of corporations engaged in the same or a similar line of business having their stocks traded in a free and open market.
2. MT Properties v. CMC.

In the late 19th century, several railroads formed a short-line railroad known as Minnesota Transfer. In 1987, four of Minnesota Transfer's five shareholders voted to merge that company with a related company. The fifth shareholder, CMC Real Estate Corporation ("CMC"), dissented from the merger--which benefited the other shareholders but not itself--and sought the "fair value" of its shares under Minnesota's 302A dissenters' rights statutes. When the trial court granted a minority discount, CMC appealed. In a case of first impression, MT Properties v. CMC Real Estate Corp., 481 N.W.2d 383 (Minn. Ct. App. 1992), the Minnesota Court of Appeals held that minority discounts should not be applied in a dissenters' rights proceeding. After reviewing how courts in other jurisdictions had ruled on the same issue, the court found that, if the Minnesota legislature had meant for such a discount to be used, it would have explicitly provided for such a discount in the statute. The court also determined that the legislative intent behind the statute was to protect dissenting shareholders. Therefore, the court prohibited the use of minority discounts in such cases.

3. Foy v. Klapmeier.

A bitter fight between a former employee/shareholder and the former employer involved a dissenters' rights claim as well as a host of other claims between the parties. The trial court disallowed a lack-of-marketability discount on the grounds that the statutory 302A dissenters' rights remedy created a market by requiring a purchase of shares. Foy v. Klapmeier, 1993 WL 246127, slip. op. at 19, ¶ 4 (D. Minn. Jan. 8, 1992). The trial court, however, did grant a minority discount. Id. slip. op. at 18, ¶ 3. On appeal, the Eighth Circuit struck down the minority discount on the basis of the intervening ruling by the Minnesota Court of Appeals in MT Properties, supra. Foy v. Klapmeier, 992 F.2d 774 (8th Cir. 1993).

4. Spinnaker Software Corp. v. Nicholson.

When two software corporations merged, a director and shareholder of the smaller publicly traded corporation exercised his dissenter's rights. The trial court found that he was entitled to more than twice what he had been paid for his common shares and nearly twice what he had been paid for his preferred shares even though the merger price had been based on arm's length negotiation. Accordingly, the trial court awarded attorneys fees to the shareholder as well. The company appealed. In Spinnaker Software Corp. v. Nicholson, 495 N.W.2d 441 (Minn. Ct. App. 1993), the court held that the trial court was entitled to overlook the allegedly arm's length price where the per share price of the merger was less than the actual market price ever was. The court also ruled that the dissenter did not need to show bad faith on the part of the company in order to collect attorneys' fees. *Id.* at 445-46. The court also held that the discrepancy between what the company had paid the shareholder and what the trial court found the shareholder was due was sufficient to show that the company had "failed to comply substantially with" Section 302A.473. It therefore upheld the award of attorneys fees.

5. Pooley v. Mankato Iron & Metal, Inc..

When two shareholders voted to remove the third shareholder as an officer and director of their corporation, the third shareholder brought suit under Minn. Stat. § 302A.751 for conduct "unfairly prejudicial" to a minority shareholder. Notwithstanding two physical assaults by the minority shareholder during the course of his employment (one on a customer and one on another shareholder), the trial court found that the minority shareholder was entitled to a buy-out using "fair value" as determined under the dissenters' rights statute. Moreover, the trial court disallowed a minority discount even though experts for both parties had applied a minority discount. In Pooley v. Mankato Iron & Metal, Inc., 1994 WL 88912, 513 N.W.2d 834 (Minn. Ct. App. 1994), the court of appeals affirmed the trial court and held that, under Minn. Stat. § 302A.751, subd. 2, a court does not abuse its discretion by not applying a minority discount.

6. American Sharecom, Inc. v. LDB International Corporation.

Minority shareholders dissented to a squeeze-out merger orchestrated by two insiders who owned only about 40% of the company but who also owned options that, if exercised, would have given them over 80% of the company. The dissenters claimed that because the insiders could never have afforded to exercise the options unless the company was sold to a third party (the taxes accruing upon exercise would have been millions of dollars), the options needed not be considered in determining the fair value of the dissenters' shares. The trial court agreed, and, in an unreported decision, the Minnesota Court of Appeals affirmed. See American Sharecom, Inc. v. LDB International Corporation, 1995 WL 321540 (Minn. Ct. App.) pet. for review denied (August 3, 1995). The Court of Appeals also held that (1) there is no right to a jury trial in dissenters' rights actions; (2) attorneys' fees may be assessed if the corporation fails to "comply substantially" with the statute; (3) there is no statutory requirement that an award of attorneys' fees be proportionate, only fair; and (4) attorneys'

fees generated while pursuing counterclaims that were eventually dismissed, were still recoverable. The Court of Appeals also noted that post-valuation date evidence is generally not admissible on the issue of value.

7. Jundt Associates, Inc. v. Knappenberger.

When the 20% minority shareholder-employee of a financial services S-Corporation, whose 80% majority shareholder was a key employee, disagreed over the role of the majority shareholder's son in the business, the minority shareholder's employment was terminated and he was required to sell his shares back to the Company. The district court refused to apply a minority discount, following the directive of MT Properties, *supra*. The court did, however apply a marketability discount of 20%. The court, relying on empirical academic studies, noted that a 30% discount was the starting-point for application of a marketability discount. In this case, because the stock not held by the minority shareholder was controlled by one person, the majority shareholder could sell (and there was a slim chance that he actually would sell) the Company, thus justifying only a 20% discount. Finally, the court refused to apply a key person discount because the key person issues in the case really affected the value of the company, not the shares. Therefore, it was more appropriate to factor the impact of a key person into the valuation of the company rather than taking a discount off at the end. Furthermore, the court noted that it would have to guess at a proper discount percentage. See, Jundt Associates, Inc. v. Knappenberger, Hennepin County Court File No. 95-1498, Findings of Fact, Conclusions of Law and Order dated May 20, 1997 (unpublished opinion).

8. Advanced Communication Design, Inc. v. Follett

When he founded Advanced Communication Design, Inc. ("ACD") in 1986, Scibora was the sole shareholder, sole director, and president. In 1990, he added two vice presidents (Follett and Stein) and let them each buy 1,500 shares of non-voting stock so that each had a one-third equity in the Company. After Stein left and sold his stock back to ACD, Scibora's wife joined as the COO and received 1,500 shares of restricted non-voting stock as compensation. Within the year, Follett was demoted to manager of special projects and had his salary reduced from \$75,000 to \$55,000. A month later he resigned, and Scibora offered to buy his 1,500 shares back for \$24,646. Both sides sued. On Follett's claim for breach of fiduciary duty, the court refused to apply a marketability discount, ordered ACD to buy his stock for \$475,381, and awarded Follett his attorneys' fees, costs and disbursements. Upon finding Follett liable to ACD for breach of an employee's duty of loyalty and interference of contract, the jury awarded damages to ACD of \$800.

Subsequently, the Minnesota Supreme Court overturned the lower court's bright-line refusal to apply a marketability discount to the minority shareholder's shares. It adopted the A.L.I. standard for court-ordered buy-outs and held that "absent extraordinary circumstances, fair value in a court-ordered buy-out pursuant to Section 302A.751 means a pro rata share of the value of the corporation as a going concern without a discount for lack of marketability." Advanced Communication Design, Inc. v. Follett,

615 N.W.2d 285, 292 (Minn. 2000). See also 2A.L.I. Principles of Corporate Governance: Analysis and Recommendations § 722 (1994). However, the court did not extend this standard to the dissenters' rights valuation context. The court found that extraordinary circumstances did exist in this case because an unfair transfer of wealth to the minority shareholder would occur. 615 N.W.2d at 293.

In evaluating whether "extraordinary circumstances" exist, the court suggested the following relevant factors as a non-exhaustive list for the court's consideration:

whether the buying or selling shareholder has acted in a manner that is unfairly oppressive to the other or has reduced the value of the corporation, whether the oppressed shareholder has additional remedies such as those available pursuant to Minn. Stat. § 302A.467 (1998), or whether any condition of the buy-out, including price, would be unfair to the remaining shareholders because it would be unduly burdensome on the corporation.

615 N.W.2d at 292-93. The court stressed that the overarching policy of the buy-out statute was to ensure a price that is fair and equitable to all parties. Id.

9. Doerr v. Arundel.

Judge William Howard of the Hennepin County District Court handled the valuation phase of a bifurcated case arising from circumstances where two business partners squeezed out a third partner essentially by dissolving the business and then selling all of its assets to a company that just the two of them owned. While plaintiff's expert appraiser presented an opinion of value; the defendants' expert offered no opinion other than a rebuttal of plaintiff's expert. Judge Howard criticized defendant's tactic and essentially adopted plaintiff's appraisal. With respect to discounts, Judge Howard refused to apply: (1) a minority discount under the ruling in MT Properties; (2) a marketability discount under the ruling in Foy and his conclusion that majority shareholders have control over whether a company is marketed for sale or not; and (3) a key person discount on the grounds that the company had a diversity of clients and customers, the ability to replace lines, deep management, and interchangeability of employees. See Doerr v. Arundel, Henn. Co. Dist. Ct. File No. EM 97-013502, Findings of Fact, Conclusions of Law, and Order dated Oct. 1, 1999 (unpublished opinion). Judge Howard also adopted the discounted cash flow analysis for that case, made adjustments for officer compensation, taxes, and sales growth, and discussed the appropriate discount rate.

C. The 302A Dissenters' Rights Trial

Chapter 49 Bank dissenters' cases and Chapter 300 consolidation dissenters' cases do not proceed to trial before the Court. Rather, the Court appoints three persons (Bank statute §§ 49.41 and 49.43) or appraisers (§ 300.16) to perform an appraisal. Thus, it is unclear exactly what generally

occurs in such valuation proceedings. It is likely that such proceedings are less formal than a 302A valuation trial. Issues that must be addressed early on will include the parties' ability to conduct discovery and present evidence to the appraiser. Furthermore, the parties may seek input to the court regarding appropriate persons or professionals to be appointed to the appraisal panel.

1. The corporation's case.

At trial, the corporation as the petitioner has the burden of proof and must present its case first. Atlantic States Construction v. Beavers, 169 Ga. App. 584, 314 S.E.2d 245, 249 (1984). This anomaly does not exist in those states, such as Delaware, where the dissenter is required to initiate the court proceeding.

a. Company representatives. Typically the corporation presents one or more corporate representatives to describe the company, its history, its business, corporate and industry outlooks, and other information called for by Rev. Rul. 59-60. This witness can also lay foundation for the information relied on by the corporation's expert witnesses -- the appraisers. The key financial data is found in the company's financial statements, but it is usually unnecessary to call the company's outside auditors merely to lay foundation for their financial statements -- both sides generally rely on these statements and there should be no dispute on this issue. The accountants may be able to provide an additional perspective on the company if needed.

b. Industry expert. The company may call an industry expert to testify about the prospects, risks, competitive factors, and other information concerning the industry.

c. The company's appraiser. The expert appraiser is the key in almost every case. As in valuation of real property, appraisers generally employ several valuation approaches and then exercise their judgment to correlate the different results into a single figure or a range of values. Cross-examination often focuses on the assumptions inherent in each valuation technique and the appropriateness of each technique to the particular company under evaluation.

2. The dissenters' case.

The dissenters' case often consists of appraisers only, although the dissenters themselves generally take the stand to explain the basis for their dissent and to state their own opinion of fair value and the reasons therefor. See, e.g., Lehman v. Hansord Pontiac Co., 246 Minn. 1, 74 N.W. 2d 305 (1955) (owner of personal or real property is presumptively acquainted with its value and may testify as to its value). But see, e.g., Carlson Equipment Co. v. International Harvester Co., 710 F.2d 481 (8th Cir. 1983) (observing that Minnesota courts have not decided whether corporate shareholders are presumptively familiar with value of business or whether specific foundation must be laid for their valuation testimony).

The legislature amended the statute in 1987 to clarify that even if the court determines the fair value of the shares to be less than that paid by the corporation, the dissenter is not obligated to refund the difference. Minn. Stat. § 302A.473, subd. 7. Thus, aside from their attorneys' fees and costs, dissenters have no risk of being in a worse position after litigation, unless the dissent is found to be arbitrary, vexatious, or not in good faith. Minn. Stat. § 302A.473, subd. 8(a) and (b).

D. Admissibility of Post-Valuation Date Evidence

A recurring issue in any valuation case is whether any valuation evidence arising after the valuation date is admissible. The issue may arise in three different contexts.

1. Post-valuation year-end financial statements.

The appraiser often relies on year-end financial statements, and rare will be the valuation date that corresponds with the end of the corporation's fiscal year. Thus, appraisers often find it convenient to rely on the financial statement with the fiscal year-end closest to the valuation date, which means that in half the cases, the valuation date will be before the closest fiscal year-end statement. This is risky because some courts will not allow opinions or evidence based on anything beyond the valuation date.

2. Post-valuation changes in the company or industry.

Post-valuation date evidence may be offered when the subsequent history of the corporation is dramatically different from the conditions prevailing on the valuation date. The temptation is irresistible for either party to offer subsequent evidence if it is helpful. The knee-jerk reaction is to exclude such evidence as irrelevant. One court allowed a party to offer such evidence for the limited purpose of testing the appraiser's underlying assumptions. The fact that future conditions assumed by the appraiser at the time did not come to pass may be evidence of the unreasonableness of the assumptions. See Austin v. City Stores Co., 89 Pa. D. & C. 57, 64-65 (1953). In another case, actual data from intervening years after the valuation date has been used to set an appropriate price-earnings ratio. In Re Valuation of Common Stock of McLoon Oil Co., 565 A.2d 997, 1003 n.6 (Me. 1989). A third reason for a court to examine data such as dramatically increased or decreased post-valuation revenues is to determine whether the cause of those changes was known or reasonably foreseeable as of the valuation date.

Post-valuation date evidence may also be admissible to show that transactions planned at the time of the merger actually came to fruition and to validate (or invalidate) the value of the assets involved. See CEDE & Co. v. Technicolor, Inc., 758 A.2d 485, 498 (Del. 2000)(the actual dollar amount of post-merger asset sales, which were forecasted pre-merger, were admissible to help place a minimum value on those assets as of the merger date). Conversely, if there are no transactions contemplated at the time of the merger, evidence of potential tax liability and expenses associated with sales of certain assets should not be considered. Paskill Corp. v. Alcoma Corp., 747 A.2d 549, 554

(Del. 2000)(court that calculated net asset value only, and that deducted speculative tax liabilities and expenses in determining net asset value, impermissibly appraised corporation on the sole basis of a theoretical liquidation net asset value).

3. Post-valuation comparable transactions.

As discussed below, appraisers will often examine comparable transactions in the course of determining their estimate of the value of the corporation. Occasionally, transactions involving similarly-sized companies in the same industry will occur between the valuation date and the trial. Generally, evidence of such transactions will not be considered unless the offering party can show that no material changes occurred in the industry between the valuation date and the trial. Even then, some courts will apply a bright-line rule and exclude such evidence. In American Sharecom, Inc. v. LDB International Corporation, 1995 WL 321540 (Minn. Ct. App.) pet. for review denied (August 3, 1995), the court reasoned that “the time at which the fair value of shares is determined is immediately before the effective date of the corporate action.” This valuation date indicates that the evidence used in determining value must be known or ascertainable on the merger date.”

V. SUMMARY OF VALUATION TECHNIQUES

Numerous valuation methodologies exist. All, however, fall into three general categories: income, asset, and market (similar to the income, replacement cost, and market approaches in valuation of real property).

A. Income Approaches

A common income approach is “discounted cash flow.” The discounted cash flow approach views the company as a money-producing entity and makes a determination as to what an investor would pay for that particular company’s cash flow.

1. Conducting a discounted cash flow analysis.

a. Preliminary decisions. Before starting a discounted cash flow calculation, an appraiser needs to make two preliminary determinations: the assumptions used in the projections (will revenues or expenses increase or decrease, will competitive or regulatory factors help or hinder profitability, etc.) and the discount rate (the return a reasonable investor would demand for the sort of risk implicit in investing in the subject company). Frequently, opposing appraisers will differ over these two components of the discounted cash flow method.

b. Determining cash flow. The first step in this technique is to project the cash flow. Projections are developed for the next five years of business operations. Assumptions as to

revenues, gross profit margin, and operating costs dramatically affect the hypothetical cash flow resulting from these projections.

c. Discounting future cash flow. Each year's projected cash flow is discounted back to present value using an appropriate discount rate to reflect the riskiness of the investment. The present values of each of the five years of cash flow are then added together. To this sum is added the "terminal" or "residual" value assigned to the entity itself, reflecting the value of the company's cash flow beyond the projected five years. This residual value is generally a function (*i.e.*, multiple) of the fifth year's cash flow, making the projected cash flow for that last year more important than any other year. The sum of the discounted cash flow for five years and the residual or terminal value is the value assigned to the company by the discounted cash flow approach.

2. Advantages of discounted cash flow method.

The advantage of the discounted cash flow approach is that it focuses on the specific company and the return to the investor from investment in that company. The disadvantage is that it is dependent on projections, for which the assumptions are crucial. It is also a method internal to the company -- meaning that it does not take into account the market's evaluation of that company or similar companies in that industry. Thus, if the market is excited about this particular industry or line of companies, the discounted cash flow approach will not necessarily reflect those market forces.

B. Asset Approaches

The most common asset approach is book value, which is merely the reported difference between assets and liabilities as they appear on the company's books. Book value has been referred to as a floor for valuing a company. See *Nardini v. Nardini*, 414 N.W.2d 184, 190 (Minn. 1987) (book value is at least a "starting point" for company in question). One problem with the asset method is that it may fail to capture the value of the business as a going concern and instead value it as a collection of assets. Another problem with book value or other asset methods is that accounting standards do not allow inclusion of certain assets -- for example, the customer base developed by a company.

A third problem with book value or other asset methods is that accounting standards often require that assets be recorded at their historical cost, not their actual market value or even replacement cost. The best example is real estate, which would often be recorded at original cost but may have a market value far different, usually greater. For instance, land owned by DuPont that was purchased in the 1700's is now listed on its balance sheet at the price paid. The historical cost of assets frequently bears little relationship to current market value. If any asset approach is used, at least some assets should be adjusted to market value.

Finally, even an "adjusted asset" approach is blind to the earnings of the company and, for example, will value a profitable company the same as an unprofitable company if the asset values are the

same. For all of these reasons, the asset approach is generally given little weight in business appraisals - it is often used more as a floor or “reasonableness check” for other methods.

C. Market Approaches

The final methodology in this triumvirate is the market approach, where the marketplace is used to place a value on a particular company. Within this broad category, at least three techniques may be employed.

1. Prior Sales.

First, historical sales of either the entire company or blocks of stock may be available. Caution must be used in evaluating past sales of stock because they may reflect minority discounts, marketability discounts, or non-arm’s length transfers.

In this respect, if a company’s shares are publicly traded, one should not assume that the price on the stock exchange will control. As discussed below in Part IV, the stock market price has a built-in minority discount, which is prohibited in dissenters’ rights cases. Evidence that the stock market price is not reliable is also admissible. See Spinnaker Software Corp. v. Nicholson, No. CT 90-004311, slip. op. at 3 (4th Jud. Dist. Minn. June 6, 1992), aff’d, 495 N.W.2d 441 (Minn. Ct. App. 1993).

2. Comparable Sales.

Comparable transactions may be available. Actual sales of similar companies may be evaluated to arrive at a hypothetical sale value of the subject company. The advantage of this approach is that, depending on comparability of the companies and the closeness in time of the transactions, it may be the closest proxy to an actual sale of the subject company between a willing buyer and willing seller in the marketplace. Moreover, this approach reflects the market response to known industry and environmental data, such as regulatory actions.

The disadvantages are obvious -- the companies individually may not be comparable or the transactions not recent. This disadvantage is often overcome by looking at a grouping of companies, no one of which is exactly comparable, but all of which are in the neighborhood. This can establish a value, or at least a range, for the subject company.

3. Market Capitalization Techniques.

The third way to use the market to obtain a value for the subject company is to apply certain market ratios or multiples derived from other companies. Although the various ratios or multiples that can be employed are limited only by the creativity of the appraiser, certain ratios are common. The most frequently used is the price-earnings ratio, which is reported daily in newspapers such as the Wall

Street Journal. This approach takes the trailing 12 months (up to the most recently reported quarterly results) of earnings per share for that company and compares it to the stock price that day as reflected by the market. The price-earnings ratios in an industry or in comparable companies can be used to determine a price for a company whose earnings are known.

Other market capitalization ratios include cash flow multiples, book value multiples, and even revenue-multiples in some industries.

The disadvantage of market ratios is that they depend on the comparability of companies and overlook other individual characteristics of each company. The advantage of this method is that it reflects the market's evaluation of the company or industry and is therefore external to the company and by definition reflective of the willing buyers and sellers in the marketplace. For a good example of a court's examining and upholding this method, see Universal City Studios Inc. v. Francis I. Dupont & Co., 334 A.2d 216 (Del. 1975).

VI. DISCOUNTS FROM ENTERPRISE VALUE

A. Background

Not apparent at the outset are certain valuation issues that can have a dramatic effect on the determination of fair value. Appraisers state that, in determining fair *market* value, various discounts are appropriate. Because a dissenters' rights proceeding determines "fair value," "fair cash value" or "value," discounts otherwise applied in the "market" may not be appropriate. Minority discounts, [lack of] marketability discounts, and "key person" discounts are often bandied about in appraisals. Depending upon the appraiser and the circumstances of the subject company, each discount, if applicable, may be 25% or more.

Appraisers violently disagree on the applicability of discounts, and the law in Minnesota is still somewhat unsettled. Disagreement on discounts can easily account for the bulk of the "spread" between the corporation's and the dissenter's views of "fair value." In virtually all other respects, the trial court's valuation is a discretionary decision. But discounts are generally viewed as a matter of law. Thus, because they are a significant item in the valuation and easily separated as a legal ruling from the trial court's other discretionary determinations, discounts are the focus of much of the appellate case law.

As one might expect, the courts outside Minnesota are split -- some allow no discounts, some allow some discounts, and some allow all discounts. In Minnesota, as discussed below, the appellate case law is evolving but the trend is to prohibit discounts in the "fair value" context. With regard to Chapter 49 and Chapter 300, there is no case law regarding the application of discounts, so the issue can only be argued by **analogy**.

B. Minority Discount

The client and appraiser, or both, may ask whether a “minority discount” is applicable. By definition, except in very limited circumstances, any dissenter will be a minority shareholder -- otherwise, the dissenter would be able to block the proposed corporate action. The theory behind a minority discount is that in the marketplace, a minority interest will command less than a pro rata share of the hypothetical value of the entire corporation (“the enterprise value”). This results from the minority shareholder’s inability to control the destiny or even day-to-day operation of the corporation. The minority discount in corporate valuation has been recognized in Minnesota case law in other contexts, most frequently in family law cases.

In MT Properties, Inc. v. CMC Real Estate Corp., 481 N.W.2d 383 (Minn. Ct. App. 1992), a case of first impression, the Court of Appeals rejected the use of a minority discount in a dissenter’s rights proceeding. In reaching its decision, the MT Properties court reviewed how courts in other jurisdictions had ruled on the minority discount issue. Courts that disallowed minority discounts generally did so because allowing minority discounts to reduce a dissenter’s “fair value” was contrary to the purposes behind dissenters’ rights statutes. Id. at 387. The effect of such a discount on the value of a dissenter’s shares is illustrated on the chart in the Appendix entitled “The Effects of Discounts.”

On the other hand, the MT Properties court noted, the courts that permitted minority discounts did so in order to prevent a minority shareholder from reaping a windfall by being paid as if he or she had a majority interest. Id. at 388. In this regard, the use of a minority discount more closely mirrors the activity of a stock market. The interplay of discounts and market mechanisms is illustrated on the chart in the Appendix entitled “Valuation Levels.”

The MT Properties court resolved these competing arguments and held that minority discounts are prohibited in 302A dissenters’ rights proceedings. The court based its holding on the grounds that Minnesota’s dissenters’ rights statutes do not expressly provide for such a discount and that the clear legislative intent was to protect minority shareholders. Id.; see also Pooley v. Mankato Iron & Metal, Inc., 513 N.W.2d 834 (Minn. Ct. App. 1994) (minority discount not applied in valuation of minority stock in buy-out ordered under Minn. Stat. § 302A.751). The court went on to say that, where a squeeze-out “calculated to damage a minority interest” has occurred, “[n]o doubt, policy arguments for dissenting shareholders are enlarged in those circumstances.” Id. at 388 n.5.

C. Illiquidity or Lack of Marketability Discount

The other issue frequently debated by appraisers, lawyers, and judges is whether a “marketability discount” is appropriate in dissenters’ cases. Often confused with a minority discount, a marketability discount reflects the shareholder’s inability readily to convert his or her holdings into cash - - i.e., the lack of a market for the shares has an impact on the value of those shares. MT Properties

specifically left open whether a “lack of marketability” or “illiquidity” discount is appropriate. 481 N.W.2d. at 387 n.1.

While a marketability discount may be applicable in a “fair market value” determination, it is probably not appropriate in a dissenter’s rights proceeding. In Foy v. Klapmeier, 1993 WL 246127 (D. Minn.), then-Chief Judge Alsop ruled out a “lack of marketability discount” in a 302A “fair value” proceeding. He stated that:

a lack of marketability discount reflects the fact that there is generally not a ready market for the shares of a closely-held corporation. No lack of marketability discount is appropriate in this case as a result of the statutory obligation of [the corporation] to purchase Foy’s shares under Minn. Stat. §§ 302A.471-473.

Slip op. at 19, ¶ 4.

Stated another way, the statute creates a market for the stock -- and, hence, makes the stock liquid -- because it requires the corporation to purchase the shares. Thus, it is paradoxical for the corporation obligated to buy the shares to assert that no market for those shares exists.

Although it did not address this issue in its opinion, the Eighth Circuit affirmed Judge Alsop’s decision in all respects except for his allowance of a minority discount. Because of the intervening decision of MT Properties, the Eighth Circuit eliminated the minority discount allowed by Judge Alsop. Foy v. Klapmeier, 992 F.2d 774, 780-81 (8th Cir. 1993). Thus, the Eighth Circuit ordered payment of the \$300,000 “enterprise value” without a discount for either lack of marketability or minority interest.

Five weeks earlier, the Minnesota Court of Appeals had made the same ruling. Just as the Eighth Circuit had done, the Minnesota Court of Appeals affirmed, without discussing the discount issue, a trial court decision rejecting a lack of marketability discount. In Spinnaker Software Corp. v. Nicholson, 495 N.W.2d 441 (Minn. Ct. App. 1993), Judge Myron Greenberg’s decision was affirmed. In his decision, Judge Greenberg distinguished between fair value and market value. After discussing the traditional fair market value definition of a willing buyer-willing seller, he said:

Fair value is understood as a shareholder’s pro-rata interest in the total value of the company. Thus, fair value is best understood as fair market value without discounts or reductions related to such factors as the size of the block of stock or the availability of a ready market for the stock.

Spinnaker Software Corp. v. Nicholson, No. CT 90-004311, slip. op. at 3 (4th Jud. Dist. Minn. June 6, 1992) (emphasis added).

Recently, the Minnesota Supreme Court ruled that a marketability discount should not be applied in a court-ordered buy-out of an oppressed minority shareholder's shares unless extraordinary circumstances justify the use of such a discount. Advanced Communication Design, Inc. v. Follett, 615 N.W.2d 285, 292 (Minn. 2000). There, the court found that extraordinary circumstances existed because not using a marketability discount would result in an "unfair" transfer of wealth to the minority shareholder. Id. at 293.

In expressly prohibiting the use of a minority marketability discount in dissenters' rights cases, the Delaware Supreme Court declared that such a discount subverts the purpose of the dissenter's rights statute in squeeze-out cases. Cavalier Oil Co. v. Harnett, 564 A.2d 1137, 1144-45 (Del. 1989). The appraisal process is to "assume that the [squeezed out] shareholder was willing to maintain his investment position, however slight, had the merger not occurred." Id. at 1145. The Delaware court concluded that the use of discounts "fail[s] to accord to a minority shareholder the full proportionate value of his shares . . . and unfairly enriches the majority shareholders who may reap a windfall from the appraisal process by cashing out a dissenting shareholder, a clearly undesirable result." Id.

D. "Key Person"/Noncompete Discount

Other discounts, such as a "key person" discount, are less common. With the loss of the minority discount in MT Properties, corporations and majority shareholders may advance this discount more often in the future until the courts determine whether it is available in a dissenters' rights case.

1. Rationale for key person discount. The central argument for a key person discount is that a company may be so dependent on one or more key people that its vitality would be threatened if those people were no longer with the company. Accordingly, it should be valued less than a similar company that is not dependent on key people. This argument is related to, and sometimes interchanged with, the argument for a "noncompete" discount. Appraisers will testify that in the real world of business acquisitions, the buyer and seller negotiate a purchase price for the seller's stock or assets and then negotiate how much of the price will be allocated to any noncompetes. This process leaves less for the shareholders. Accordingly, a corporation may argue that a dissenter is not entitled to any part of a hypothetical purchase price that would be allocated to noncompetes. The dissenters may argue that allocation of purchase price to noncompetes is merely a tax-savings device (which the IRS has just remedied - see 26 U.S.C. § 197 (1993)). Such discounts have been used by Minnesota courts in divorce matters. See Nelson v. Nelson, 411 N.W.2d 868 (Minn. Ct. App. 1987). But no Minnesota court has opined on the availability of such a discount in a dissenters' rights case.

2. Argument against key person discount. A refutation of the key person discount is found in Brown v. Allied Corrugated Box Co., 91 Cal. App. 3d 479, 154 Cal. Rptr. 170 (1979). In Brown, the plaintiffs in a dissolution/buy-out case owned 49% of the stock, and the remaining 51% of the stock was owned by the company's key salesman who controlled at least 40% of the company's

sales by virtue of personal relationships with customers. In denying the key person discount, the appellate court reasoned:

By focusing on [the majority shareholder's] ability to leave the corporation and possibly take his customers with him, the majority commissioners ignored the fact that in developing a clientele through his use and control of the corporation's assets, [the majority shareholder] was deemed to be acting for the benefit of all the shareholders, not just himself. Plaintiffs were entitled to their proportionate share of the entire corporation, including whatever goodwill [the majority shareholder] had established. Any implied threat by [the majority shareholder] to leave the corporation and destroy its goodwill should consequently not have been considered.

91 Cal. App. 3d at 488, 154 Cal. Rptr. at 177.

Judge Solum, in Jundt Associates, Inc. v. Knappenberger, Hennepin County Court File No. 95-1498, Findings of Fact, Conclusions of Law and Order dated May 20, 1997 (unpublished opinion) also refused to apply a key person discount. In Jundt, the majority stockholder (Mr. Jundt) was also the financial services company's founder and principal (if not the only) rainmaker. Judge Solum refused to apply a key person discount to the minority shareholder's shares because the key person status of Jundt really affected the overall value of the company, not any particular shares. Moreover, in order to put a percentage value to such a discount would require the court to merely guess at a percent.

Judge Howard of the Hennepin County District Court recently refused to apply a key person discount on the grounds that the company had a diversity of clients and customers, the ability to replace lines, deep management, and interchangeability of employees. See Doerr v. Arundel, Henn. Co. Dist. Ct. File No. EM 97-013502, Findings of Fact, Conclusions of Law and Order dated Oct. 1, 1999 (unpublished opinion).

VII. ATTORNEY'S AND EXPERT'S FEES

Unfortunately, the attorneys' fees and experts' fees for each side in a dissenters' rights case can easily reach into six figures. Thus, the ultimate allocation of fees and expenses is an important consideration.

A. Chapter 302A

Minn. Stat. § 302A.473, subd. 8 prescribes the allocation of fees to be made in three separate subdivisions as follows:

(a) The court shall determine the costs and expenses of a proceeding under subdivision 7, including the reasonable expenses and compensation of any appraisers

appointed by the court, and shall assess those costs and expenses against the corporation, except that the court may assess part or all of those costs against a dissenter whose action in demanding payment under subdivision 6 is found to be arbitrary, vexatious, or not in good faith.

(b) If the court finds that the corporation has failed to comply substantially with this section, the court may assess all fees and expenses of any experts or attorneys as the court deems equitable. These fees and expenses may also be assessed against a person who has acted arbitrarily, vexatiously, or not in good faith in bringing the proceeding, and may be awarded to a party injured by those actions.

(c) The court may award, in its discretion, fees and expenses to an attorney for the dissenters out of the amount awarded to the dissenters, if any.

(Emphasis added.)

A corporation fails to comply substantially either through a procedural omission or “the offering of an estimated fair value which substantially underestimates the actual fair value of the shares.” Spinnaker Software Corp. v. Nicholson, 495 N.W.2d 441, 446 & n.3 (Minn. Ct. App. 1993), citing the Reporter’s Notes to the statute. See also MT Properties v. CMC Real Estate Corp., 481 N.W.2d 383 (Minn. Ct. App. 1992) (award of fees against dissenter reversed when court also reversed trial court’s application of minority discount on dissenter’s shares). In Hernando v. Huff, 609 F. Supp. 1124 (D. Miss. 1985), the corporation offered \$80.50 per share but the court found fair value to be \$100.00 per share. In awarding expert fees, this court held that the 24% increase “materially exceeds” the corporation’s offer.

In American Sharecom, Inc. v. LDB International Corporation, 1995 WL 321540 (Minn. Ct. App.), pet. for review denied (August 3, 1995), the court affirmed the trial court’s award of costs and attorneys’ fees totaling approximately \$334,000 even though some of those fees were incurred in the course of pursuing certain counterclaims alleged by the dissenters that were dismissed by the trial court as being beyond the scope of an appraisal proceeding. The Court of Appeals reasoned that the facts underlying those claims eventually were used by the trial court in determining certain issues in the appraisal proceeding. The court concluded that “the counterclaims were intrinsically connected to the appraisal proceeding and were fairly included in the award of attorneys’ fees.” The Court of Appeals also awarded \$2,000 to the dissenters for their appellate work.

B. Chapter 49

Minn. Stat. §§ 49.41 and 49.43 have the same scheme for division of costs and fees. The statutes provide simply that the dissenters and the bank split the “charges and expenses of the appraisers” 50-50.

C. Chapter 300

Minn. Stat. § 300.16, subd. 3 provides that “if the amount determined in the [appraisal] proceeding is in excess of the amount the consolidated corporation has offered to pay as the fair cash value of the stock, the court must assess against the consolidated corporation the costs of the proceeding, including a reasonable attorney’s fee, to the stockholder and a reasonable fee to the appraisers, as it considers equitable; otherwise, the costs and fees to the appraisers must be assessed one-half against the corporation and one-half against the stockholder.” Thus, the parties split the costs and appraisal fees 50-50 unless the corporation low-balls its offer of “fair cash value.” Then, the court has discretion to impose all of the appraisal costs and fees, including the dissenters’ attorney’s fees, against the corporation if the circumstances merit such cost-shifting.

CONCLUSION

Minnesota case law has not yet fully fleshed out the statutes’ skeletal outlines of dissenters’ rights proceedings. This is especially true in the Chapter 49 Bank and Chapter 300 dissenters’ rights statutes. Trial courts and litigants are thus left with many unanswered legal questions as they grapple with appraisals and procedural issues in a dissenters’ rights case.

APPENDIX

Bibliography

Treatises and Articles on Dissenters' Rights or Valuation Generally

Norman J. Baer & Douglas L. Elsass, *Paying for a Shareholder's "Dissenting Opinion": Dissenters' Rights Actions Under the Minnesota Business Corporation Act*, The Hennepin Lawyer (May-June 1992).

Richard M. Buxbaum, *The Dissenter's Appraisal Remedy*, 23 UCLA Law Rev. (1976).

Mary Louise Fellows & William H. Painter, *Valuing Closed Corporations for Federal Wealth Transfer Taxes: A Statutory Solution to the Disappearing Wealth Syndrome*, 30 Stan. L. Rev. 895 (1978).

Harry J. Haynsworth IV, *Valuation of Business Interests*, 33 Mercer L. Rev. (1982).

Hideki Kanda & Saul Levmore, *The Appraisal Remedy and The Goals of Corporate Law*, 32 UCLA L. Rev. 429 (1985).

Bayless Manning, *The Shareholder's Appraisal Remedy: An Essay for Frank Coker*, 72 Yale L.J. 223 (1962)

Joel Seligman, *Reappraising the Appraisal Remedy*, 52 Go. Wash. L. Rev. 829 (1984).

Edward E. Shea, *Modern Business Valuation Methods*, 34 The Practical Lawyer 67 (Oct. 1988).

Ferdinand S. Tinio, Annot., *Valuation of Stock of Dissenting Shareholders in Case of Consolidation or Merger of Corporation, Sale of Its Assets, or the Like*, 48 ALR 3d 430 (1973).

Note, *Valuation of Dissenters' Stock Under Appraisal Statute*, 79 Harv. L. Rev. 1453 (1966).

Note, *Second Generation State Takeover Legislation: Maryland Takes a New Tack*, 83 Mich. L. Rev. (1984).

Note, *Dissolution and Minority Shareholder Protection in the Closed Corporation*, 1966 Wis. L. Rev. 1232.

Practitioners' Guide to Dissenters' Rights in Five Easy Pieces

1. **Select an appraiser who will stand up in court.** He or she will be presenting reams of potentially very boring information and numbers to the court. In turn, your appraiser will be vigorously cross-examined by your opponents with the help of their appraiser. You need a good, strong, articulate and independent witness.
2. **Work with your appraiser.** Advise your appraiser about the law on discounts before you receive the appraisal report. Advise your appraiser about the exact valuation date and be careful about post-valuation date evidence.
3. **Observe carefully the rules and deadlines** for dissenting and responding to a dissenter. Within prescribed time limits, the corporation must provide accurate and complete notices to shareholders and the dissenter must file up to three different notices or demands.
4. **Do not "low ball" the dissenter or file a frivolous dissent.** While this is not a major league baseball arbitration (in which the arbitrator must choose one party's number and may not split the difference), staking out an extreme position has its risks. The attorneys' and experts' fees that can be assessed under Chapters 302A and 300 are substantial.
5. **Do not assume the case will settle.** As in other divorces, emotions run high and settlements are difficult to achieve. The corporation does not want to pay a dissenter more than it paid the non-dissenters. The dissenter did not want to part with his or her stock in the first place, thinks the corporation is more valuable than it now says, and wants what is due.

\2244432\3