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NOTES

Corporation Law—*Meiselman v. Meiselman*: “Reasonable Expectations” Determine Minority Shareholders’ Rights

In a close corporation,¹ a freeze-out occurs when majority shareholders bar minority shareholders from sharing in the income or participating in the management of the corporation.² With little reason to continue as shareholders in this situation, the minority may seek to withdraw their investments. North Carolina General Statutes section 55-125(a)(4) authorizes courts to dissolve a corporation when reasonably necessary to protect the “rights or interests of the complaining shareholder.”³ In addition, section 125.1 authorizes the courts to grant other relief as alternatives to dissolution.⁴ Although the legislature authorized the dissolution remedy in 1955, the North Carolina Supreme Court only recently has fully considered it for the first time.

In *Meiselman v. Meiselman*⁵ the supreme court held that the “reasonable expectations” of minority shareholders determine their rights or interests.⁶ These reasonable expectations may arise when the minority becomes a shareholder, and may develop thereafter.⁷ Although the court attempted to ensure the liberal relief afforded by section 55-125(a)(4),⁸ the court’s reasonable expectations test falls short of relieving all minority shareholders who suffer from a “freeze-out.”⁹ Consequently, the test should be expanded to more fully encompass minority shareholders.¹⁰

In 1971 Ira Meiselman acquired approximately seventy percent of the stock in several interrelated family corporations, and his brother Michael ac-

1. A close corporation is typically owned and managed by a small number of shareholders. The shares of the close corporation generally are not traded on the securities market. See BLACK’S LAW DICTIONARY 308 (5th ed. 1979). See also *infra* notes 36-41 and accompanying text.

2. See *infra* notes 51-56 and accompanying text.

3. N.C. GEN. STAT. § 55-125(a)(4) (1982). Other provisions of § 55-125 provide for involuntary dissolution of a corporation in an action by a shareholder upon deadlock or pursuant to an existing shareholders’ agreement. The statute also provides for dissolution in an action by creditors or the attorney general. N.C. GEN. STAT. § 55-125 (1982).

4. N.C. GEN. STAT. 55-125.1 (1982). “Such relief may be granted as an alternative to a decree of dissolution, or . . . whenever the circumstances . . . are such that relief, but not dissolution, would be appropriate.” *Id.* § 55-125.1(b). Relief may include, but is not limited to: (1) modifying the corporate charter or bylaws; (2) modifying corporate resolutions or acts; (3) directing or prohibiting any act of the corporation, shareholders, directors or officers; and (4) “providing for the purchase of their fair value of shares of any shareholder, either by the corporation or by other shareholders.” *Id.* § 55-125.1(a).

5. 309 N.C. 279, 307 S.E.2d 551 (1983).

6. *Id.* at 298, 307 S.E.2d at 563.

7. *Id.*

8. *Id.* at 294, 307 S.E.2d at 560.

9. See *infra* notes 148-79 and accompanying text.

10. See *infra* notes 188-96 and accompanying text.

quired the remaining thirty percent.¹¹ The brothers worked for the family corporations,¹² but their business relationship was not harmonious.¹³ At trial, Michael contended that Ira had excluded Michael from participating in the corporations and had restricted his access to corporate offices and information. He further claimed that Ira had acquired and sold corporate assets without his consent, and had discouraged him from board participation.¹⁴ Ira contended that Michael's limited participation had been voluntary.¹⁵

In 1973 Ira formed Republic Management Corporation (Republic), assuming sole ownership.¹⁶ Republic and Eastern Federal Corporation (Eastern Federal, the parent corporation of the family businesses) then entered into a contract requiring Republic to perform management services for Eastern Federal in exchange for five and one-half percent of Eastern Federal's sales.¹⁷ In August 1979 Michael brought a suit challenging the propriety of this contract, based, in part, on Ira's sole ownership of Republic.¹⁸ In response to the suit, Ira fired Michael from the family corporations.¹⁹ In addition to losing his salary, Michael lost his car, hospital, and life insurance, his use of corporate credit cards, and his participation in a profit-sharing trust.²⁰

In response, Michael filed suit against Ira and the family corporations seeking involuntary dissolution²¹ of the corporations under section 55-125(a)(4),²² or alternatively a buyout of his share of the corporations by defendants under section 55-125.1.²³ Michael pursued his claim on the grounds

11. *Meiselman*, 309 N.C. at 282, 307 S.E.2d at 553. Michael and Ira acquired ownership of the corporations from their parents through a series of gifts and bequests ending in 1971. *Id.*

12. *Id.* at 282, 307 S.E.2d at 554.

13. *Id.* at 284-87, 307 S.E.2d at 555-56. Perhaps most indicative of the tenor of the relationship between the two brothers is Ira's comment that "[y]es, it is my position in this case that my brother, Michael, suffers . . . from crippling mental disorders and that was a reason that my father put me in control of the family corporations." *Id.* at 286-87, 307 S.E.2d at 556.

14. *Id.* at 285-86, 307 S.E.2d at 555.

15. *Id.* at 284, 307 S.E.2d at 555. Furthermore, Ira contended that Michael never had been denied participation in the management of the family corporations. *Id.*

16. *Id.* at 283-84, 307 S.E.2d at 554-55.

17. *Id.* at 284, 307 S.E.2d at 554.

18. *Id.* at 283, 307 S.E.2d at 554. The opinion does not describe the nature of this suit, but Michael apparently alleged that Ira had usurped a corporate opportunity. Michael also alleged this claim in his suit under analysis here. *See infra* note 23.

19. *Meiselman*, 309 N.C. at 283, 307 S.E.2d at 554. Ira also terminated the contract between Eastern Federal and Republic. He characterized Michael's release as incidental to the termination of the contract. *Id.*

20. *Id.*

21. A corporation may be dissolved voluntarily when shareholders agree to terminate the corporate existence. When such agreement is lacking, state intervention is required to dissolve the corporation involuntarily. *Compare* N.C. GEN. STAT. § 55-117 (1982) (voluntary dissolution by written consent of the shareholders) and *id.* § 55-118 (voluntary dissolution by action of directors and shareholders) with *id.* § 55-122 (involuntary dissolution in action by attorney general) and *id.* § 55-125 (power of courts to liquidate and decree involuntary dissolution).

22. *See supra* note 3 and accompanying text.

23. The purchase of the complaining shareholder's shares by the corporation or other shareholders enables him to liquidate his investment in the corporation. *See supra* note 4. The book value of the family corporations was \$11,168,778 on December 31, 1978. *Meiselman*, 309 N.C. at 282, 307 S.E.2d at 553.

Michael also sought to recover the profits accumulated by Republic under the contract between Eastern Federal and Republic. He pursued this derivative claim on the ground that Ira had

that an irreconcilable conflict, causing intense hostility and bitterness, existed between Michael and Ira; and that Ira had exercised his control of the corporation to exclude Michael from participation in the corporations and to fire Michael.²⁴

The trial court denied relief, but the court of appeals reversed.²⁵ The court of appeals interpreted section 55-125(a)(4) as authorizing liquidation when the complaining shareholder establishes that "basic 'fairness' compels dissolution."²⁶ The court also determined that relief under section 55-125 "does not require a complaining shareholder to show bad faith, mismanagement or wrongful conduct, but only real harm."²⁷ The court concluded that "the evidence shows that Michael's immense book value wealth is being rendered worthless to him as current income, and that, despite Michael's stock in the corporate enterprises, he is denied the benefits of that ownership."²⁸ This denial entitled Michael to relief under section 55-125.1,²⁹ and, accordingly, the court remanded for determination of an appropriate remedy other than dissolution.³⁰

In an opinion written by Justice Frye, the North Carolina Supreme Court affirmed the court of appeals' decision, but on different grounds. The court rejected the "basic fairness" and "real harm" tests of the court of appeals, holding that the "rights or interests of the complaining shareholder" under section 55-125(a)(4) are to be determined from complaining shareholder's "reasonable expectations" . . . in the corporation."³¹ The court then announced the following test:

[U]nder N.C.G.S. § 55-125(a)(4) a trial court is (1) to define the "rights or interests" the complaining shareholder has in the corpora-

breached his fiduciary duty to the family corporations. That is, he usurped the corporations' opportunity to participate in the profits generated under the contract by his sole ownership of Republic. *Id.* at 306, 307 S.E.2d at 567. "[T]he 'corporate opportunity doctrine provides that a corporate fiduciary may not appropriate to himself an opportunity that rightfully belongs to his corporation.'" *Id.* at 307, 307 S.E.2d at 568 (citing Note, *Corporate Opportunity and Corporate Competition: A Double-Barreled Theory of Fiduciary Liability*, 10 HOFSTRA L. REV. 1193, 1202-04 (1982) (citing *Guth v. Loft, Inc.*, 23 Del. Ch. 255, 271-73, 5 A.2d 503, 510-11 (1939)).

24. *Meiselman v. Meiselman*, 58 N.C. App. 758, 761-62, 295 S.E.2d 249, 252 (1982), *modified*, 309 N.C. 279, 307 S.E.2d 551 (1983).

25. *Id.* at 776, 295 S.E.2d at 260.

26. *Id.* at 766, 295 S.E.2d at 254-55. The court noted that other jurisdictions usually granted relief to minority shareholders either to relieve oppression of minority shareholders by the majority or to achieve fairness. *Id.* at 763, 295 S.E.2d at 253. The court interpreted the language of N.C. GEN. STAT. § 55-125(a)(4) (1982) as precluding an oppression-based analysis. *See also infra* notes 69-71 and accompanying text (discussion of oppression-based analysis). Accordingly, the court adopted a fairness test. This test appears to have been adopted from *Stumpf v. C.E. Stumpf & Sons, Inc.*, 47 Cal. App. 3d 230, 120 Cal. Rptr. 671 (1975). *Meiselman*, 58 N.C. App. at 763 n.8, 295 S.E.2d at 253 n.8. *See also infra* notes 74-80 and accompanying text (discussion of *Stumpf*).

27. *Meiselman*, 58 N.C. App. at 766, 295 S.E.2d at 255.

28. *Id.* at 769, 295 S.E.2d at 256. Michael's annual return from dividends was less than 2% of his investment in the corporations. *Id.* at 769 n.11, 295 S.E.2d at 256 n.11. *See also Meiselman*, 309 N.C. 302 n.5, 307 S.E.2d at 565 n.5.

29. At trial Michael dropped his claim for involuntary dissolution and sought only a buyout of his interest in the corporations. *Id.* at 761 n.5, 295 S.E.2d at 252 n.5.

30. *Id.* at 776, 295 S.E.2d at 260.

31. *Meiselman*, 309 N.C. at 298, 307 S.E.2d at 563.

tion; and (2) to determine whether some form of relief is "reasonably necessary" for the protection of those "rights or interests." For plaintiff to obtain relief under the expectations analysis, he must prove that (1) he had one or more substantial reasonable expectations known or assumed by the other participants [and concurred in by them³²]; (2) the expectation has been frustrated; (3) the frustration was without fault of plaintiff and was in large part beyond his control; and (4) under all the circumstances of the case plaintiff is entitled to some form of equitable relief."³³

The court also determined that section 55-125(a)(4), regarding dissolution, and section 55-125.1, regarding alternatives to dissolution, must be read together. Consequently, the court established that "when an action is brought under N.C.G.S. § 55-125(a)(4), the trial court is to examine . . . whether . . . liquidation is reasonably necessary," whether "'alternative' relief [under section 55-125.1(b)] is more appropriate than dissolution," or whether "'alternative' relief, but not dissolution is appropriate."³⁴ In light of the newly formulated analysis of sections 55-125(a)(4) and 55-125.1, the supreme court remanded the case for an application of the reasonable expectations test.³⁵

32. In summarizing the expectations-based analysis, the court apparently neglected to include this qualification established earlier in the opinion: "The key is 'reasonable.' In order for plaintiff's expectations to be reasonable, they must be known to or assumed by the other shareholders and concurred in by them." *Id.* This omission is noted because the qualification would appear to enhance the evidentiary burden on the complaining shareholder.

33. *Id.* at 301, 307 S.E.2d at 564.

34. *Id.* at 300-01, 307 S.E.2d at 564. Although "liquidation" and "dissolution" are not identical terms of art, the opinion treats them as synonyms for the termination of a corporation's existence. *Id.* at 301 n.4, 307 S.E.2d at 564 n.4.

Justice Martin filed a concurring opinion, joined by Chief Justice Branch and Justice Copeland. *Id.* at 314, 318, 307 S.E.2d at 571, 573 (Martin, J., concurring). Justice Martin urged that the majority test failed to consider "the actions of all the participants." *Id.* The fault or conduct of the minority shareholder should be considered, as well as whether he has "pursued all the other available statutory means for the protection of his rights." *Id.* at 315, 307 S.E. 2d at 572. Conversely, Justice Martin would also have the court consider whether the majority shareholders' acts constituted "oppression." *Id.* at 316, 307 S.E.2d at 573. See also *infra* notes 180-82 and accompanying text.

Justice Martin's reference to other statutory means of protection is apparently a reference to such statutes as N.C. GEN. STAT. § 55-25 (1982) (minority shareholders' rights to attempt to gain representation on the board of directors) and *id.* § 55-50 (minority shareholders' rights to compel dividends).

Query whether Justice Martin's concern regarding minority shareholder conduct might be covered by the majority test. See *supra* note 33 and accompanying text at subpart (3). Concerning majority shareholder conduct, the majority opinion implicitly rejected an oppression-based analysis, *Meiselman*, 309 N.C. at 297-99, 307 S.E.2d at 560 and 562-63, and explicitly rejected a focus on the majority's actions. *Id.* at 305-06, 307 S.E.2d at 566-67.

35. *Meiselman*, 309 N.C. at 314, 307 S.E.2d at 571. The supreme court also remanded for reconsideration of Michael's claim that Ira had usurped a corporate opportunity with the management contract between Republic and Eastern Federal. See *supra* note 23. The court affirmed the court of appeals' reversal of the trial court, which had found no usurpation. The case was remanded, however, for an application of the newly announced usurpation of corporate opportunity analysis.

The court of appeals recognized that "directors, officers, and majority shareholders owe a fiduciary duty and obligation of good faith to minority shareholders as well as to the corporation." *Meiselman*, 58 N.C. App. at 774, 295 S.E. 2d at 259. When such persons receive an advantage to the exclusion of some shareholders, the fiduciary duty is breached. *Id.* In light of these standards the court concluded that: "Ira, as a controlling shareholder and director of Eastern, cannot, over

As the supreme court noted, the family corporations in *Meiselman* were close corporations.³⁶ While defining "close corporation" is no simple task, many commentators limit their use of the term to corporations whose shares are not generally traded on the securities market.³⁷ Another aspect of close corporations is the typically small number of shareholders.³⁸ These shareholders generally manage the corporation as well.³⁹ The intimacy of the close corporations gives rise to a highly personal business relationship among the manager-owners.⁴⁰ Accordingly, their relationship has been characterized as similar to partners.⁴¹ This relationship contrasts with the publicly held corporation, in which ownership is disseminated among numerous shareholders, and directors and officers, who may not be shareholders, manage the corporation.

The problems that arise in close corporations often differ substantially from those of publicly held corporations. For example, two individuals who wish to start a business may regard themselves essentially as partners, presuming that they will share in the management of the business.⁴² They may incor-

Michael's objection, enter into a contract that generates a profit for a corporation which he owns alone." *Id.*

The supreme court announced the following test:

[W]hen an officer or director is charged with having usurped a corporate opportunity, he or she must establish under N.C.G.S. § 55-30(b)(3) [and *Highland Cotton Mills v. Ragan Knitting Co.*, 194 N.C. 80, 138 S.E.2d 428 (1927)] that the "corporate transaction" in which he or she has engaged is "just and reasonable" to the corporation because it was not an opportunity or "corporate transaction" which the corporation itself would have wanted. A determination of what is "just and reasonable" and, thus, whether a corporate opportunity has indeed been usurped, is, of course, one which "no hard and fast rule can be formulated."

Meiselman, 309 N.C. 310, 307 S.E.2d at 569 (citation omitted). The court elaborated by requiring an examination by the trial court of "whether the disputed opportunity is functionally related to the corporation's business [and] whether the corporation has an interest or expectancy in the opportunity." *Id.* at 311, 307 S.E.2d at 570.

36. *Meiselman*, 309 N.C. at 288, 307 S.E.2d at 557.

37. See, e.g., Davidian, *Corporate Dissolution in New York: Liberalizing the Rights of Minority Shareholders*, 56 ST. JOHN'S L. REV. 24, n.2 (1981); Hillman, *The Dissatisfied Participant in the Solvent Business Venture: A Consideration of the Relative Permanence of Partnerships and Close Corporations*, 67 MINN. L. REV. 1, 64 n.213 (1982).

This definition is implicitly accepted in North Carolina. See N.C. GEN. STAT. § 55-73(b) (1982). The statute was drafted to authorize the use of shareholder agreements in the close corporation text. Such agreements shall not be invalid "[e]xcept in cases where the shares of a corporation are at the time or subsequently become generally traded in the markets maintained by securities dealers or brokers." *Id.*

38. *Israels, The Sacred Cow of Corporate Existence: Problems of Deadlock and Dissolution*, 19 U. CHI. L. REV. 778 (1952). See also Davidian, *supra* note 37, at 24 n.2.

39. *Israels, supra* note 38, at 788.

40. *Hillman, supra* note 37, at 62.

41. See, e.g., *Helms v. Duckworth*, 249 F.2d 482, 486 (D.C. Cir. 1957) ("In an intimate business venture such as this, stockholders of a close corporation occupy a position similar to that of joint adventurers and partners."). See also *Donahue v. Rodd Electrotypes Co.*, 367 Mass. 578, 592-93, 328 N.E.2d 505, 515 (1975); *68th St. Apartments, Inc. v. Lauricella*, 142 N.J. Super. 546, 549, 362 A.2d 78, 85 (1976), *aff'd*, 150 N.J. Super. 47, 374 A.2d 1222 (1977).

42. The presumption of partnership-like decisionmaking is deemed commonplace by many commentators. See, e.g., Davidian, *supra* note 37, at 26; *Israels, supra* note 38, at 778-79; O'Neal, *Close Corporations: Existing Legislation and Recommended Reform*, 33 BUS. LAW 873, 884, 885 (1978). General partnership law typically provides that "[a]ll partners have equal rights in the

porate to acquire the limited liability,⁴³ preferred tax treatment,⁴⁴ and perpetual existence⁴⁵ that accompany the corporate form. Because of a disparity between the individuals' contributions of capital or time to the corporation, one may become a majority shareholder, the other a minority shareholder. Later a disagreement over corporate policy may arise between the individuals. If the individuals cannot reconcile their differences, the disagreement will be resolved in favor of the majority shareholder. His ownership of a majority of the voting shares and his control of the board of directors enable him to control corporate decisionmaking.⁴⁶ The minority shareholder will find that the personal relationship and presumptions of mutual decisionmaking give way to the majority rule doctrine.⁴⁷ In contrast, the publicly held corporation, characterized by dicotomous ownership and management, is controlled by an independent board.⁴⁸ Rarely could a shareholder control corporate policy or exclude other shareholders from the decisionmaking process. Should the minority shareholder in the close corporation become dissatisfied with his position, he may wish to end the business relationship by selling his shares. Unlike the shareholders of a publicly held corporation whose shares are regularly traded, however, the minority shareholder generally will find his shares unmarketable.⁴⁹

The vulnerability of the minority shareholder in the close corporation is

management and conduct of the partnership business." UNIF. PARTNERSHIP ACT § 18(e), 6 U.L.A. 213-14 (1969).

43. Tort and contractual liability arising out of corporate operations is limited to the corporate entity. That is, shareholders are not liable. H. HENN, *LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES* § 146, at 344-49 (3d ed. 1983). In a partnership, such liability extends beyond the business entity to the partners. *Id.* § 24, at 73-75.

44. Corporate income is taxed according to corporate rates, which are more favorable than comparable individual rates. *Id.* § 76, at 133. Partnership income is taxed as if received by the partners at individual rates. *Id.* § 27, at 81.

45. A partnership is generally deemed dissolved when, among other things, a partner dies or withdraws. *Id.* § 26, at 77. In contrast, the corporate entity is assumed to exist in perpetuity. *Id.* § 75, at 132.

46. General corporation law prescribes a representative form of government or corporate democracy. Holders of a majority of voting shares may elect and control a majority of the board of directors. Subsequently, corporate policy is determined by a majority vote of the board or in some instances a majority vote of the shareholders. See F. O'NEAL, "SQUEEZE-OUTS" OF MINORITY SHAREHOLDERS § 3.02 (1975); Latty, *The Close Corporation and the New North Carolina Business Corporation Act*, 34 N.C.L. REV. 432, 433 (1956).

47. "In the absence of some special control arrangement, set up by contract or special charter or bylaw provision, a corporation is subject to the principle of majority rule: holders of a majority of the voting shares govern." F. O'NEAL, *supra* note 46, § 3.03.

Indeed, one commentator has noted that the "structure of representative government 'prescribed by general corporation law' is about as appropriate for the two-man get-together in a close corporation as Robert's Rules of Order." Latty, *The Close Corporation*, in *NORTH CAROLINA CORPORATION MANUAL* 190, 191 (1960).

48. In a close corporation "the independent judgment of directors is, in fact, a fiction." Israels, *supra* note 38, at 778.

49. Potential buyers are not anxious to step into the shoes of the minority shareholder. See F. O'NEAL, *supra* note 46, § 1.03; Davidian, *supra* note 37, at 27; Comment, *Deadlock and Dissolution in the Close Corporation: Has the Sacred Cow Been Butchered?* 58 NEB. L. REV. 791, 796 (1979).

particularly illustrated by the freeze-out.⁵⁰ Freeze-outs have been described as "various techniques by which persons in control of an enterprise deprive minority owners of their interest in the business or of a fair return on their investment."⁵¹ Most often the majority will effect a freeze-out by restricting the payment of corporate dividends.⁵² If the minority is employed by the corporation, the majority ordinarily will fire him.⁵³ Ultimately the majority will "try to deprive him of every economic benefit he derives from the corporation."⁵⁴ Faced with no return on his investment, no bargaining power, and little hope of reconciliation with the majority, the minority shareholder likely will hope to withdraw from the corporation with his investment.⁵⁵ Because his shares are unmarketable, the minority may consider judicially imposed dissolution or buyout as his only available recourse.⁵⁶

Traditionally, courts have been reluctant to dissolve corporations at the request of the minority shareholders.⁵⁷ At about the turn of the century,

50. The terms "freeze-out" and "squeeze-out" are synonyms. F. O'NEAL, *supra* note 46, § 1.02 n.2. "Freeze-out" has been adopted in this note.

51. *Id.* § 3.02. The underlying causes for freeze-outs may include greed, desire for power, personality clashes, and disagreements over corporate policy. *Id.* § 2.02. The majority shareholder, however, may have a proper motive. "Minority shareholders may be so uncooperative and act so unreasonably and improperly that majority interests are justified in moving to eliminate them." *Id.* § 1.02.

In *Meiselman* Michael alleged the classic freeze-out case. Compare *infra* notes 51-56 and accompanying text (freeze-out techniques) with *supra* notes 13-14, 19-20 and accompanying text (Michael's situation).

52. F. O'NEAL, *supra* note 46, § 3.04.

53. *Id.* See also Davidian, *supra* note 37, at 27.

54. F. O'NEAL, *supra* note 46, § 3.06. "[The minority] may even find himself without life, accident, hospitalization or health insurance . . ." *Id.* "Sometimes majority shareholders drain off corporate profits by having other enterprises they own perform services for the corporation under management or service contracts . . ." *Id.* § 3.13.

Like the exercise of majority control in corporate decisionmaking, see *supra* note 47 and accompanying text, the freeze-out disappoints the presumption commonly held by the minority that he will receive employment and pecuniary benefit from the corporation. See O'Neal, *supra* note 42, at 884.

55. The alternative is in effect to abandon his investment. See Hetherington, *Special Characteristics, Problems, and Needs of the Close Corporation*, 1969 U. ILL. L.F. 1, 29.

56. Typically, state law affords the minority shareholder some statutory protection from the freeze-out. See, e.g., N.C. GEN. STAT. § 55-25 (1982) (minority shareholders' right to attempt to gain representation on the board of directors); *id.* § 55-50 (minority shareholders' right to compel dividends); *id.* § 55-67 (right to cumulative voting); *id.* § 55-38 (right to examine corporate books and records). These rights, however, may be frustrated if the majority forces the minority to litigate each time he attempts to exercise them. See F. O'NEAL, *supra* note 46, § 1.03. Dissolution or buyout allows the minority to liquidate his investment and end his business relationship.

The minority shareholder may prefer a buyout to dissolution because the liquidation value of the corporation typically is small when compared with the going concern value of the corporation. Ordinarily the judicially imposed buyout is formulated on the basis of the fair market value of the minority shares. See, e.g., N.C. GEN. STAT. § 55-125.1(a)(4) (1982).

One should distinguish the dissatisfied minority shareholder in *Meiselman* from the 50% owner who may seek relief because of "deadlock" of the corporation. Deadlock generally occurs when control of the corporation is split evenly, and the inability to reach a majority decision prevents the corporation from operating effectively. See, e.g., N.C. GEN. STAT. § 55-125(a)(1)-(2) (1982). See also Comment, *supra* note 49, at 794-95.

57. The general common-law rule was that absent statutory authority, a court of equity had no power to dissolve a solvent corporation in response to a minority shareholder's suit. See, e.g., *Steenrod v. L.M. Gross Co.*, 334 Ill. 362, 166 N.E. 82 (1929); *Strong v. McCogg*, 55 Wis. 624, 13 N.W. 895 (1882). See also J. Tingle, *The Stockholder's Remedy of Corporate Dissolution* 25-32

courts began to recognize various equitable grounds for dissolution,⁵⁸ but the circumstances under which relief was granted were unpredictable.⁵⁹ As the unique problems of close corporations became more widely recognized in the 1950s, several states, including North Carolina,⁶⁰ passed statutes authorizing dissolution as a remedy for minority shareholders.⁶¹ Today, virtually every state recognizes such statutory relief.⁶²

Despite statutory authorization of dissolution, courts still consider the remedy to be drastic.⁶³ Reluctance to dissolve continues because the value of

(1959). The traditional reluctance to dissolve can be attributed in part to the majority rule doctrine and the business judgment rule. The majority rule doctrine provides that the holders of a majority of voting shares govern the corporation. See *supra* notes 46-47 and accompanying text. "The business judgment rule recognizes a broad discretion in the directors to determine business policy and to conduct corporate affairs." F. O'NEAL, *supra* note 46, § 3.03. Courts are hesitant to substitute their judgment for elected managers who presumably have expertise in business matters. The application of these principles have produced a hands-off approach to judicial review of internal corporate affairs. *Id.*

Participants in the close corporation often think of themselves as partners. F. O'NEAL, *supra* note 46, § 2.10. See also *supra* note 42 and accompanying text. Particularly in the area of dissolution, many commentators have suggested that close corporations should be treated like partnerships. See F. O'NEAL, *supra* note 46, § 7.15; Davidian, *supra* note 37, at 66-67; Comment, *supra* note 49, at 825. Cf. Hillman, *supra* note 37, at 61-68. Partnership law generally allows free dissolution between the participants. See, e.g., UNIF. PARTNERSHIP ACT § 31, 6 U.L.A. 376 (1969).

58. See, e.g., *Ross v. American Banana Co.*, 150 Ala. 268, 43 So. 817 (1907) (complete failure of corporate purpose). See generally *Graham v. McAdoo*, 135 Ky. 677, 123 S.W. 260 (1909) (corporate ruin inevitable due to mismanagement); *Miner v. Belle Isle Ice Co.*, 93 Mich. 97, 53 N.W. 218 (1892) (failure of corporate purpose due to fraudulent mismanagement and misappropriation of funds); *Ponca Mill Co. v. Mikesell*, 55 Neb. 98, 75 N.W. 46 (1898) (gross mismanagement and misappropriation of corporate property); Comment, *supra* note 49, at 798-805 (development of equitable grounds for dissolution).

59. See Davidian, *supra* note 37, at 43; Comment, *supra* note 49, at 805.

60. North Carolina was recognized as a pioneer in close corporation legislation. 1 F. O'NEAL, *CLOSE CORPORATION LAW AND PRACTICE* § 1.14a (2d ed. 1971) [hereinafter cited as 1 F. O'NEAL]. The North Carolina Business Corporation Act of 1955 contained several statutes drafted with the close corporation in mind, including N.C. GEN. STAT. § 55-125 (1982) (involuntary dissolution). See Latty, *supra* note 47, at 191; see also *id.* at 193-204 (specific statutes intended to meet the special requirements of close corporations).

The North Carolina legislature rejected the idea of a special close corporation act separate from the general corporation act. See Latty, *supra* note 47, at 191. Such close corporation legislation is commonly referred to as an integrated close corporation act. Delaware, Maryland, Pennsylvania, and Kansas have enacted integrated acts. O'Neal, *supra* note 42, at 875. The draftsman of the North Carolina Business Corporation Act of 1955 believed that one act adequately covers all corporate activity. Consequently, the close corporation statutes are scattered throughout the general corporation act. See Latty, *supra* note 47, at 191. For a discussion of the pros and cons of integrated versus unintegrated statutes, see Karjala, *A Second Look at Special Close Corporation Legislation*, 58 TEX. L. REV. 1207 (1980).

61. See, e.g., ILL. ANN. STAT. ch. 32, § 157.86 (Smith-Hurd 1959); N.Y. STOCK CORP. LAW § 9 (1948). See generally 1 F. O'NEAL, *supra* note 60, at § 1.14a (pioneer close corporation legislation). It has been suggested that such legislation came primarily at the urging of various commentators rather than from litigation in the area of close corporation dissolution. See Hetherington, *supra* note 55, at 1-3.

62. See, 2 F. O'NEAL, *CLOSE CORPORATION LAW AND PRACTICE* § 9.28 (2d ed. 1971) [hereinafter cited as 2 F. O'NEAL]; Comment, *supra* note 49, at 807; see also *infra* note 69.

63. See, e.g., *Stumpf v. C. E. Stumpf & Sons, Inc.*, 47 Cal. App. 3d 230, 235, 120 Cal. Rptr. 671, 674 (1975) ("The minority must persuade the court that fairness requires drastic relief [of dissolution]."); *Hockenberger v. Curry*, 191 Neb. 404, 406, 215 N.W.2d 627, 628 (1974) ("The remedy of liquidation is so drastic that it must be invoked with extreme caution.") (quoting *Polikoff v. Dole & Clark Bldg. Corp.*, 37 Ill. App. 2d 29, 184 N.E.2d 792 (1962)).

a business as a going concern typically exceeds its liquidation value.⁶⁴ Consequently, several states have authorized alternatives to dissolution.⁶⁵ Alternatives may include broad discretionary powers of the court to cancel, alter, or enjoin acts of the corporation, shareholders, directors, or officers.⁶⁶ Frequently, they also include a provision authorizing a judicially supervised buyout of the minority shares by the corporation or other shareholders.⁶⁷ Such alternatives provide relief to the minority while preserving the corporation.

Generally, the grounds for alternative relief parallel those established in the state's involuntary dissolution statute.⁶⁸ Various statutory grounds for dissolution have been recognized, but most states follow the position of the Model Business Corporation Act.⁶⁹ These states focus on "illegal, oppressive

64. See, e.g., *Masinter v. Webco Co.*, 262 S.E.2d 433, 438-49 (W. Va. 1980). See also Folk, *Revisiting the North Carolina Corporation Law: the Robinson Treatise Reviewed and the Statute Reconsidered*, 43 N.C.L. REV. 768, 785 (1965); Hillman, *supra* note 37, at 47 ("Because of the possibility that some significant portion of going concern value or goodwill may not be realized if the assets are liquidated, courts frequently view corporate dissolution as a 'drastic,' 'harsh,' or 'last resort' remedy."); Comment, *supra* note 49, at 797.

65. See *supra* notes 62-64; *infra* notes 66-67 and accompanying text.

66. See, e.g., ARIZ. REV. STAT. ANN. § 10-216 (1977); CALIF. CORP. CODE § 1803 (West 1977); MICH. COMP. LAWS ANN. § 450-1825 (1974); N.C. GEN. STAT. § 55-125.1 (1982); S.C. CODE ANN. § 33-21-155 (Supp. 1982). The North Carolina statute was adopted from the South Carolina statute, which was modeled on § 210 of the English Companies Act of 1948, 11 & 12 Geo. 6, c 38. R. ROBINSON, NORTH CAROLINA CORPORATION LAW AND PRACTICE § 29-12 n.3 (3d ed. 1983).

See also Proposed Statutory Close Corporation Supplement to the Model Business Corp. Act, § 16, Report of the Committee on Corporate Laws, Section of Corporation, Banking and Business Law, American Bar Association, printed in 36 BUS. LAW. 269 (1981) (recommended dissolution alternatives).

67. See, e.g., ARIZ. REV. STAT. ANN. § 10-216 (1977); CAL. CORP. CODE § 2000 (West 1977); CONN. GEN. STAT. ANN. § 33-384 (West Supp. 1981); ILL. REV. STAT., Ch. 32, § 1214 (Supp. 1978); MD. CORPS. & ASS'NS CODE ANN. § 4-603 (1975); MICH. COMP. LAWS ANN. § 450.1825 (1974); MINN. STAT. ANN. § 302A.751 (West Supp. 1984); N.J. STAT. ANN. § 14A:12-7 (West Supp. 1981); N.Y. BUS. CORP. LAW § 1118 (Consol. 1979); N.C. GEN. STAT. § 55-125.1 (1975); S.C. CODE ANN. § 33-21-155 (Supp. 1982); W. VA. CODE § 31-1-134 (1982).

68. Alternative relief statutes typically provide for remedies other than dissolution when the minority has filed for relief under the state's dissolution statute. See, e.g., N.Y. BUS. CORP. LAW § 1118 (Consol. 1979); N.C. GEN. STAT. § 55-125.1 (1982). See also R. ROBINSON, *supra* note 66, at § 29-14 (As a formal matter the minority shareholder must bring an action under the dissolution statute but asking for relief under the alternative relief statute.).

69. "The . . . courts shall have a full power to liquidate the assets and business of a corporation:

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

(2) That the acts of the directors or those in control of the corporation are illegal, oppressive or fraudulent" MODEL BUSINESS CORP. ACT § 97(a)(2) (1980).

See, e.g., ALA. CODE § 10-2A-195(a)(1)(b) (1980); ALASKA STAT. § 10.05.540(2) (1968); ARK. STAT. ANN. § 64-908(a)(2) (1980); COLO. REV. STAT. § 7-8-113(2)(a) (Supp. 1983); IDAHO CODE § 30-1-97(a)(2) (1980); ILL. ANN. STAT. ch. 32, § 157.86(a)(3) (Smith-Hurd Supp. 1983); IOWA CODE ANN. § 496A.94(1)(c) (West Supp. 1981); MD. CORPS. & ASS'NS CODE ANN. § 3-413(b)(2) (1975); MICH. COMP. LAWS ANN. § 21.450.1825(1) (1974); MISS. CODE ANN. § 79-3-193(a)(2) (1973); MO. ANN. STAT. § 351.485(1)(b) (Vernon 1966); MONT. CODE ANN. § 35-1-921(1)(a)(ii) (1983); NEB. REV. STAT. § 21-2096(1)(b) (1977); N.J. STAT. ANN. § 14A:12-7(1)(C) (West Supp. 1983); N.M. STAT. ANN. § 53-16-16(A)(1)(b) (1978); N.Y. BUS. CORP. LAW § 1104-a(a)(1) (McKinney Supp. 1981); N.D. CENT. CODE § 10-21-16(1)(b) (1976); PA. STAT. ANN. tit. 15, § 210(A)(2) (Purdon 1967); R.I. GEN. LAWS. § 7-1.1-90(a)(2) (1970); S.C. CODE ANN. § 33-21-150(a)(4) (Law. Co-op. Supp. 1982); S.D. COMP. LAWS ANN. § 47-7-34(2) (1967); UTAH CODE ANN. § 16010-92(a)(2) (1973); VT. STAT. ANN. tit. 11, § 2067(a)(1)(B) (1973); WASH. REV. CODE

or fraudulent"⁷⁰ actions of the majority shareholders. Courts typically have interpreted such "majority oppression" statutes as requiring wrongful conduct on the part of the majority.⁷¹

North Carolina's involuntary dissolution statute differs from the majority oppression statutes because it provides for dissolution when "reasonably necessary for the protection of the rights or interests of the complaining shareholders."⁷² This language shifts the court's focus from the actions of the majority to the impact on the minority. That is, majority oppression statutes consider oppression by the majority; the North Carolina statute considers the rights and interests of the minority. Because the "rights or interests" language appears in only a few other jurisdictions,⁷³ it has received little judicial interpretation, and the effect of this shift of focus is thus unsettled. The few cases involving such statutes, however, suggest that they may afford the minority shareholder broader relief.

For example, in *Stumpf v. C. E. Stumpf & Sons, Inc.*⁷⁴ the California Court of Appeals held that a minority shareholder was entitled to dissolution after he had suffered a freeze-out.⁷⁵ Initially, the court noted that the actions of the majority did not support relief under the majority oppression provision of California's dissolution statute.⁷⁶ Then the court announced that dissolu-

ANN. § 23A.28.170(1)(b) (1969); W. VA. CODE § 31-1-41(a)(2) (1982); WYO. STAT. ANN. § 17-1-614(a)(i)(B) (1977).

70. See *supra* note 69.

71. See, e.g., *Baker v. Commercial Body Builders, Inc.*, 264 Or. 614, 628, 507 P.2d 387, 393 (1973) (oppression is "burdensome, harsh and wrongful conduct . . ."). Hillman, *supra* note 37, at 45 ("Baker represents a traditional approach under which severe misconduct is required for a finding of oppression.").

See also *Notzke v. Art Gallery, Inc.*, 84 Ill. App. 3d 294, 405 N.E.2d 839 (1980) (conspiratorial action on the part of two defendant shareholders against a third shareholder deemed oppressive); *Fix v. Fix Material Co., Inc.*, 538 S.W.2d 351 (Mo. App. 1976) (combination of long-term management controls to controlling shareholders, heavy corporate losses, and salary increases to the majority not deemed oppressive, but coming narrowly close, and continuation of such conduct might lead to dissolution in a subsequent suit); *Baylor v. Beverly Book Co., Inc.*, 216 Va. 22, 216 S.E.2d 18 (1975) (waste of corporate funds to the benefit of the majority deemed oppressive); *White v. Perkins*, 213 Va. 129, 189 S.E.2d 315 (1972) (exclusion of other shareholders from corporate participation, and personal use of corporate property by the majority, deemed oppressive); Comment, *Oppression as a Statutory Ground for Corporate Dissolution*, 1965 DUKE L.J. 128, 131 (courts have held that majority actions such as plundering the corporation, siphoning off profits through excessive salaries to themselves as officers, and running the corporation for the sole benefit of the majority constitute oppression or misconduct justifying dissolution).

72. N.C. GEN. STAT. § 55-125(a)(4) (1982).

73. See, e.g., CAL CORP. CODE § 1800(b)(5) (West 1977); N.Y. BUS. CORP. LAW § 1104-a(b)(2) (Consol. Supp. 1983). The California and New York dissolution statutes also contain "majority oppression" provisions. CAL. CORP. CODE § 1800(b)(4) (West 1977); N.Y. BUS. CORP. LAW § 1104-a(a)(1) (Consol. Supp. 1983).

74. 47 Cal. App. 3d 230, 120 Cal. Rptr. 671 (1975).

75. In *Stumpf* a father and two sons owned the corporation in equal shares. As a result of a management dispute and hostility between the brothers, one brother ceased to be employed by the corporation. It is not clear from the opinion whether he resigned or was fired. Thereafter, the father and remaining brother, as majority shareholders, removed the minority brother as an officer of the corporation. In addition, the minority brother received no salary, dividends, or other revenue from the corporation. *Id.* at 232, 235, 120 Cal. Rptr. at 672, 675. Compare *supra* notes 50-55 and accompanying text (freeze-out techniques).

76. The court's remarks were directed at the predecessor to § 1800(b)(4) of the California

tion under the "minority interests" provision⁷⁷ would be granted "when required to assure fairness to minority shareholders."⁷⁸ The origin of this fairness test is unclear.⁷⁹ Indeed, the court failed to provide any standards in determining fairness. It inferred, however, that the minority interests provision supports minority relief beyond that afforded by the standards of oppression or wrongful conduct by the majority.⁸⁰

The New York courts have also interpreted a dissolution provision grounded on the rights or interests of minority shareholders. In *In re Topper*⁸¹ the supreme court granted relief⁸² to a minority shareholder suffering from a freeze-out.⁸³ Focusing primarily on the interpretation of New York's majority oppression provision,⁸⁴ the court found that the actions of the majority "severely damaged [the minority shareholder's] *reasonable expectations*⁸⁵ and constitute[d] a freeze-out of [his] interest; consequently, they [were] deemed

Corporations Code, which is substantially the same as the current version. CAL. CORP. CODE § 4651(e) (West 1977) (repealed 1977).

(b) The grounds for involuntary dissolution are that: (4) Those in control of the corporation have been guilty of or have knowingly contended persistent and pervasive fraud, mismanagement or abuse of authority or persistent unfairness toward any shareholders or its property is being misapplied or wasted by its directors or officers.

CAL. CORP. CODE § 1800(b)(4) (West 1977).

The court of appeals affirmed the trial court's finding that the majority had not committed any "abuse of authority" or displayed "persistent unfairness" toward the minority. *Stumpf*, 47 Cal. App. at 233, 120 Cal. Rptr. at 673.

77. The action was brought under the predecessor to § 1800(b)(5) of the California Corporations Code, CAL. CORP. CODE § 4651(f) (West 1977) (repealed 1977), which is substantially the same as the current version, CAL. CORP. CODE § 1800(b)(5) (West 1977). The current version states: "(b) The grounds for involuntary dissolution are that: (5) . . . liquidation is reasonably necessary for the protection of the rights or interests of the complaining shareholder or shareholders." *Id.*

78. *Stumpf*, 47 Cal. App. at 234, 120 Cal. Rptr. at 674.

79. The court does not indicate the source of the test. The adoption of a fairness test for the minority interests provision is curious. "Persistent unfairness" by the majority toward the minority is an alternative ground for dissolution under the majority oppression provision. Indeed, the court of appeals found that the majority had not displayed "persistent unfairness." See *supra* note 76 and accompanying text; see also *infra* text accompanying note 80. Professor Hillman has suggested that the court's superficial treatment of the fairness test indicates the court was not aware of the uniqueness of the minority interests provision with which it was dealing. See Hillman, *supra* note 37, at 58 n.192.

80. *Stumpf*, 47 Cal. App. 3d at 234, 120 Cal. Rptr. at 673.

81. 107 Misc. 2d 25, 433 N.Y.S.2d 359 (1980).

82. While the court did not order dissolution, the alternative relief of a buyout was granted. The court directed the majority to purchase the shares of the minority at a fair market value determined by the court. *Topper*, 107 Misc. 2d at 28-29, 433 N.Y.S.2d at 362.

83. In *Topper* plaintiff owned a minority interest in two close corporations. Less than a year after the formation of the corporations, the majority fired the minority shareholder, terminated his salary, removed him as an officer, and changed the locks on the corporate offices. *Id.* at 27, 433 N.Y.S.2d at 362.

84. "(a) [A shareholder] may present a petition of dissolution on one or more of the following grounds:

(1) The directors or those in control of the corporation have been guilty of illegal, fraudulent or oppressive action toward the complaining shareholders." N.Y. BUS. CORP. LAW § 1104-a(a)(1) (Consol. Supp. 1983).

85. Because the minority shareholder had terminated his previous employment, invested his life savings in the corporations, and executed personal guaranties on behalf of the corporations, the court found that the minority shareholder had a reasonable expectation that he would be an active participant in the corporations. *Topper*, 107 Misc. 2d at 27, 433 N.Y.S. 2d at 361-62. Partic-

'oppressive' within the statutory provision."⁸⁶ The New York involuntary dissolution statute also provides for a consideration of the rights or interests of the minority.⁸⁷ Accordingly, the court extended the reasonable expectations test to that provision: "These rights and interests derive from the expectations of the parties and special circumstances that underlie the formation of close corporations."⁸⁸

In *Topper* the court fully embraced the reasonable expectations test that has been urged persistently by F. Hodge O'Neal,⁸⁹ a recognized authority in the close corporation field. Generally stated, the test provides that "a court should give relief, dissolution or some other remedy to a minority shareholder whenever corporate managers or controlling shareholders act in a way that disappoints the minority shareholder's reasonable expectations."⁹⁰ The basis of the test lies in the special characteristics of the close corporation. Because of substantial investment in the corporation or personal relationships among the participants, O'Neal suggests that the participants have certain reasonable expectations at the inception of the enterprise.⁹¹ These expectations typically include participation in management and employment by the corporation.⁹² While the expectations often are not reduced to writing,⁹³ the participants typically have oral agreements or "half-articulated understandings."⁹⁴ In the absence of a written agreement, courts typically allow the majority shareholder to dominate corporate decisionmaking.⁹⁵ Consequently, the minority shareholder is vulnerable to a freeze-out.⁹⁶ O'Neal concludes that it is unjust to allow a freeze-out when the participants actually have had an understanding

ipation was deemed to include participation in management and operations, and remuneration for employment with the corporation. *Id.* at 33, 433 N.Y.S. at 365.

86. *Id.* at 28, 433 N.Y.S. at 362 (emphasis added).

87. "(b) The court, in determining whether to proceed with involuntary dissolution . . . shall take into account:

(2) Whether liquidation of the corporation is reasonably necessary for the protection of the rights and interests of any substantial number of shareholders or of the petitioners." N.Y. BUS. CORP. LAW § 1104-a(b)(2) (Consol. Supp. 1983).

88. *Topper*, 107 Misc. 2d at 35, 433 N.Y.S.2d at 366.

89. *Id.* at 32-34, 433 N.Y.S. at 364-65. See F. O'NEAL, *supra* note 46, § 7.15; 1 F. O'NEAL, *supra* note 60, § 1.14c; O'Neal, *supra* note 42, at 881-88.

A reasonable expectations test also has been supported by other commentators. See, e.g., Afterman, *Statutory Protection for Oppressed Minority Shareholders: A Model for Reform*, 55 VA. L. REV. 1043, 1063 (1969); Hillman, *supra* note 37, at 75-76.

Topper's and Professor O'Neal's reasonable expectations tests have been followed in *O'Connell v. Marine Repair Servs., Inc.*, 530 F. Supp. 1199 (S.D.N.Y. 1982) (interpreting New York law); and *In re Taines*, 111 Misc. 2d 559, 444 N.Y. S.2d 540 (1981).

90. O'Neal, *supra* note 42, at 886.

91. *Id.* at 884-85.

92. *Id.*

93. "[M]ost state corporation statutes validate special charter and bylaw provisions and shareholder's agreements designed to protect minority shareholders." *Id.* at 881. The minority may lack the foresight, however, "or his bargaining position may be so weak that he is unable to negotiate for protection. Further, he may have been given or may have inherited his minority interest." *Id.* at 883.

94. *Id.* at 886.

95. *Id.* at 884.

96. *Id.* at 883.

of shareholder participation.⁹⁷ Thus, these understandings and accompanying expectations should be protected; the doctrine of majority rule should not be strictly applied in close corporations.⁹⁸ O'Neal suggests that reasonable expectations should be protected to the extent that "they exist at the inception of the enterprise, and as they develop thereafter through a course of dealing concurred in by all of [the shareholders]."⁹⁹

O'Neal notes that a reasonable expectations test might be used to provide relief in jurisdictions that have "majority oppression" statutes,¹⁰⁰ but he urges application of the test in all jurisdictions.¹⁰¹ Whether a reasonable expectations test is used to define minority relief under a majority oppression statute¹⁰² or minority interests statute,¹⁰³ the relief afforded by such a test appears to go beyond the traditional notions of minority shareholder protection.¹⁰⁴ The test abandons a focus on the oppressive acts of the majority and considers the impact upon the minority,¹⁰⁵ supporting relief even when the majority had not acted wrongfully.¹⁰⁶

The foregoing statutory provisions and judicial interpretations illustrate the variety of approaches taken in determining the extent of minority shareholder relief. Majority oppression statutes represent the majority approach. Such statutes traditionally have been interpreted as requiring wrongful conduct by the majority. Alternatively, other jurisdictions have found it more appropriate to focus on the minority. That is, how has the minority been affected by the acts of the majority? The most notable exception to the oppression as wrongful conduct approach are statutory provisions that protect the rights or interests of minority shareholders.

California has interpreted its minority interests provision as sanctioning relief when required to ensure fairness to minority shareholders. New York has interpreted such a provision as protecting the reasonable expectations of minority shareholders. In addition, the reasonable expectations test has been applied under majority oppression statutes, thus modifying the traditional in-

97. *Id.* at 887.

98. *Id.* at 886.

99. *Id.* See also Afterman, *supra* note 89, at 1064 (a court should examine the whole history of the shareholder's relationship as expectations alter and new expectations develop over the course of the shareholders' cooperative efforts in operating the corporation).

100. O'Neal, *supra* note 42, at 886.

101. *Id.*

102. The reasonable expectations test has been applied outside New York to afford minority relief under majority oppression statutes. See, e.g., *Fox v. 7L Bar Ranch Co.*, __ Mont. __, 645 P.2d 929 (1982); *Exadaktilos v. Cinnaminson Realty Co.*, 167 N.J. Super. 141, 400 A.2d 554 (1979), *aff'd*, 174 N.J. Super. 559, 414 A.2d 994 (1980); *Masinter v. Webco Co.*, 262 S.E.2d 433 (W. Va. 1980).

103. Before *Meiselman*, New York was apparently the only jurisdiction to apply the reasonable expectations test to a minority interest statute.

104. See *supra* notes 69-71 and accompanying text.

105. See Hillman, *supra* note 37, at 49. This shift in focus parallels a similar shift in the minority interest statutes. See *supra* notes 72-73 and accompanying text.

106. *Id.* See also O'Neal, *supra* note 42, at 886 (minority reasonable expectations should be protected "even though the acts of the [majority] fall within the literal scope of [their] powers or rights").

terpretation of such statutes. These tests—minority interests, fairness, or reasonable expectations—support relief when the acts of the majority have not risen to the level of wrongful conduct, but nevertheless harm minority shareholders. Consequently, dissolution or alternative remedies are more readily available under these statutes. The test for minority relief adopted in a jurisdiction, therefore, essentially determines the difficulty of attaining relief. The selection of a test implicitly balances minority interests against the interest of the majority and the corporation in avoiding the hazards that might accompany minority relief.¹⁰⁷

It has been suggested that relief to minority shareholders carries the potential for minority abuse. For example, the minority might bring or threaten to bring a dissolution suit even when the majority has acted innocently.¹⁰⁸ The minority might seek an enhanced position in the corporation, a change of corporate policy, or a buyout of his interest.¹⁰⁹ Or the minority might intentionally create discord to achieve dissolution, not because of an injurious majority but because the minority simply wants to withdraw his investment.¹¹⁰ As dissolution and alternative remedies become more easily attainable, the bargaining leverage of the minority is increased.¹¹¹ Consequently, the innocent majority may accede to the demands of the minority for fear of dissolution, or simply to avoid litigation.¹¹²

Absent minority shareholder abuse, minority relief also threatens to damage corporate viability. As minority relief becomes more easily obtainable the majority "may be forced to make their business judgments more with an eye toward avoiding [litigation] than toward serving the best needs of the corporation."¹¹³ It has also been suggested that the enhanced availability of the remedies of dissolution and buyout may diminish the financial resources available to close corporations. Lenders might be deterred from extending credit; a buyout may diminish corporate funds available for repayment, or dissolution may produce liquidation values insufficient to cover corporate debts.¹¹⁴ Investors might be deterred from contributing capital; they may be called upon to contribute to a buyout and may be unable to recoup their investment from liquidation values.¹¹⁵

The North Carolina statutes provide for minority relief "when reasonably necessary to protect the rights or interests" of the minority shareholders. The relief afforded by this minority interests provision had never been fully addressed before *Meiselman*. While a few cases have considered the provision,

107. See Davidian, *supra* note 37, at 48; Hillman, *supra* note 37, at 87-88. See also Palikoff v. Dole & Clark Bldg. Corp., 37 Ill. App. 2d 29, 184 N.E.2d 792 (1962).

108. See Davidian, *supra* note 37, at 60.

109. See Hillman, *supra* note 37, at 73.

110. See Davidian, *supra* note 37, at 45-46.

111. See Hillman, *supra* note 37, at 72-73.

112. See Davidian, *supra* note 37, at 60.

113. Note, *Corporate Dissolution for Illegal, Oppressive or Fraudulent acts: The Maryland Solution*, 28 MD. L. REV. 360, 372 (1968).

114. See Hillman, *supra* note 37, at 75.

115. *Id.*

none have provided significant interpretation.¹¹⁶ Prior to *Meiselman*, the most significant judicial development in North Carolina close corporation law was *Blount v. Taft*.¹¹⁷ In *Blount* the supreme court did not interpret the minority interests provision; however, the court did consider the minority shareholder's position in the close corporation.

In *Blount* the supreme court denied specific enforcement of a close corporation shareholders' agreement.¹¹⁸ A minority shareholder argued that the agreement could not be terminated without unanimous shareholder approval.¹¹⁹ The court held that the agreement had been legitimately terminated by a majority vote of the directors.¹²⁰ In reaching its decision, the court recognized that the problems of a close corporation "are different from those of a publicly held corporation."¹²¹ In particular, "majority rule" enables the majority shareholder to dominate corporate policy to the exclusion of the minority.¹²² To enable minority shareholders to protect themselves, noted the court, the legislature adopted North Carolina General Statutes section 55-73¹²³ to sanction shareholders' agreements.¹²⁴ By means of a shareholders' agreement, shareholders can adopt decisionmaking procedures that avoid the consequences of majority rule.¹²⁵ Because such agreements deviate from the norms of majority rule, the court deemed it reasonable "to require the degree of deviation intended be explicitly set out."¹²⁶ The court concluded: "[M]inority

116. See *Dowd v. Charlotte Pipe & Foundry Co.*, 263 N.C. 101, 139 S.E.2d 10 (1964); *Royall v. Carr Lumber Co.*, 248 N.C. 735, 105 S.E.2d 65 (1958); *W & H Graphics, Inc. v. Hambry*, 48 N.C. App. 82, 268 S.E.2d 567 (1980).

117. 295 N.C. 472, 246 S.E.2d 763 (1978).

118. *Id.* at 484-85, 246 S.E.2d at 771. In *Blount* the shareholders unanimously approved a corporate bylaw provision that limited nepotism within the corporation. The bylaws also contained a provision authorizing repeal of the bylaws by a majority vote of the directors. Subsequently, a majority did repeal the antinepotism provision. While the antinepotism provision was deemed a valid shareholders' agreement, the court found the repeal valid. *Id.*

119. *Blount*, 295 N.C. at 480, 246 S.E.2d at 769.

120. *Id.* at 485, 246 S.E.2d at 771.

121. *Id.* at 482, 246 S.E.2d at 770.

122. In [close corporations], if the internal "government" of the corporations were conducted strictly by the vote of the majority of the outstanding shares, the largest shareholder(s) could dominate the policies of the corporations over the objections of other shareholders. "In a nutshell, Family A with 51% ownership of a close corporation can live in luxury off a profitable business while Family B starves with 49%."

Id. (citations omitted).

123. N.C. GEN. STAT. § 55-73 (1981). Section 55-73(b) reads in part:

Except in cases where the shares of a corporation are at the time or subsequently become generally traded in the markets maintained by securities dealers or brokers, no written agreement to which all shareholders have actually assented, whether embodied in the charter or bylaws or in any side agreement in writing and signed by all the parties thereto, and which relates to any phase of the affairs of the corporation, whether to the management of its business or division of its profits or otherwise, shall be invalid as between the parties thereto, on the ground that it is an attempt by the parties thereto to treat the corporation as if it were a partnership or to arrange their relationships in a manner that would be appropriate only between partners.

124. *Blount*, 295 N.C. at 483, 246 S.E.2d at 770. "With respect to close corporations, the heart of the North Carolina [Business Corporation] Act is G.S. 55-73." *Id.* (citing Latty, *Close Corporations and the New North Carolina Business Corporation Act*, 34 N.C.L. REV. 432, 438-40 (1956)).

125. *Blount*, 295 N.C. at 481, 246 S.E.2d at 769.

126. *Id.* at 487, 246 S.E.2d at 773.

shareholders who would have protection greater than that afforded by Chapter 55 of the General Statutes and the judicial doctrines prohibiting breach of a fiduciary relationship must secure it themselves in the form of 'a well drawn' shareholders' agreement."¹²⁷ The *Blount* decision unquestionably provides a strong incentive for minority shareholders to protect themselves with written shareholders' agreements. *Blount*, however, does not appear to preclude minority relief in the absence of such an agreement. Indeed, the court's remarks suggest that minority relief might be afforded by other provisions of chapter 55¹²⁸ or judicial sponsorship.¹²⁹ In *Meiselman* the supreme court was faced with determining the full extent of minority shareholder protection in North Carolina.

Specifically, *Meiselman* considered the relief or protection afforded under section 55-125(a)(4),¹³⁰ which authorizes dissolution to protect the rights and interests of minority shareholders, and section 55-125.1,¹³¹ which authorizes alternative remedies. In considering the appropriate extent of minority relief in the close corporation, the court's analysis substantially paralleled the views of F. Hodge O'Neal.¹³² The court recognized that ideally a minority shareholder has provided for his own protection through a written shareholders' agreement executed at the inception of the corporation,¹³³ but noted that frequently such an agreement is not negotiated because of the minority's lack of foresight or bargaining power.¹³⁴ Despite the absence of an agreement, the minority has reasonable expectations that may include participation in corporate management and employment.¹³⁵ The majority shareholder is in a position to disappoint those reasonable expectations; "because of his greater voting power, [he] is in a position to terminate the minority shareholder's employment and exclude him from participation."¹³⁶ The absence of a market for shares of a close corporation only exacerbates the minority shareholder's problem.¹³⁷

Having examined the minority's vulnerability to a freeze-out,¹³⁸ the court recognized the need to protect the "minority shareholder whose 'reasonable expectations' have been disappointed."¹³⁹ Accordingly, the court held that a

127. *Id.* at 488, 246 S.E.2d at 773.

128. The North Carolina Business Corporation Act.

129. *See Blount*, 295 N.C. at 487, 246 S.E.2d at 773 (principle of equity or public policy); *id.* (judicial doctrine prohibiting breach of fiduciary relationship).

130. N.C. GEN. STAT. § 55-125(a)(4) (1982).

131. *Id.* § 55-125.1 (1982).

132. *Compare infra* notes 134-37 and accompanying text; *supra* notes 89-99 and accompanying text.

133. *Meiselman*, 309 N.C. at 290, 307 S.E.2d at 558. While the court did not consider *Blount*, *Meiselman* implicitly rejects any interpretation of *Blount* that suggests minority shareholders will be protected only to the extent of a written shareholders' agreement. *See supra* note 127-29 and accompanying text.

134. *Meiselman*, 309 N.C. at 291, 307 S.E.2d at 558.

135. *Id.* at 289-90, 307 S.E.2d at 558.

136. *Id.* at 290, 307 S.E.2d at 558.

137. *Id.* at 291, 307 S.E.2d at 559.

138. *See supra* notes 50-56 and accompanying text.

139. *Meiselman*, 309 N.C. at 293, 307 S.E.2d at 559.

"complaining shareholder's 'rights or interests' in a close corporation include the 'reasonable expectations' the complaining shareholder has in the corporation."¹⁴⁰

The reasonable expectations test appears consistent with the language of section 55-125(a)(4). As noted, under majority oppression statutes, courts traditionally have focused on the wrongful acts of the majority.¹⁴¹ In contrast, the minority interests language of statutes similar to section 55-125(a)(4) has been interpreted as shifting the focus to the impact on the minority.¹⁴² The reasonable expectations test has received a similar interpretation.¹⁴³ Assuming that the *Meiselman* court intended an interpretation of section 55-125(a)(4) that fulfilled the intent of the legislature, the reasonable expectations test appears to be a good choice.¹⁴⁴

The reasonable expectations test also appears consistent with the court's desire to protect the frozen-out minority.¹⁴⁵ The shift in focus of the test, from majority to minority, abandons the traditional position that minority relief requires a showing of majority wrongdoing.¹⁴⁶ Indeed, the court explicitly rejected wrongful majority action as a standard for relief.¹⁴⁷ Whereas a freeze-out might not come within the standard of wrongdoing, the reasonable expectations test holds the promise of relief to the minority who faces a freeze-out in spite of his expectations to the contrary.

The reasonable expectations test thus provides more broadly based relief to the minority than the majority wrongdoing standard. The court, however, established four prerequisites for relief under the test.¹⁴⁸ These requirements

140. *Id.* at 298, 307 S.E.2d at 563.

141. *See supra* notes 69-71 and accompanying text.

142. *See supra* notes 72-88 and accompanying text.

143. *See supra* notes 102-06 and accompanying text.

144. The *Meiselman* court might have noted that the original draft of N.C. GEN. STAT. § 55-125 (1982) also included the provision that dissolution might be granted if "[t]he acts of directors or those in control of the corporation are illegal, oppressive or fraudulent, or their acts are otherwise unfair to the minority shareholders or to any class of shareholders." Sapp, *Dissolution, Liquidation and Minority Shareholders Rights*, in NORTH CAROLINA CORPORATION MANUAL 240, 244 (1960). Such a majority oppression statute traditionally has been interpreted as requiring wrongful conduct by the majority. *See supra* notes 69-71 and accompanying text. The reasonable expectations test focuses instead on the minority and rejects the majority oppression approach. *See supra* notes 102-06 and accompanying text. Because the legislature rejected the majority oppression provision, the reasonable expectations test appears consistent with legislative intent.

145. *See supra* notes 138-40 and accompanying text.

146. *See supra* notes 69-71 and accompanying text.

147. The *Meiselman* court rejected the trial court's focus on possible wrongdoing by Ira. The trial court was instructed, on remand, to focus instead on Michael's rights or interests. *Meiselman*, 309 N.C. at 305-06, 307 S.E.2d at 566-67. Additionally, the court rejected "[t]he trial court's use of the standards of 'oppression,' 'overreaching,' 'gross abuse,' 'unfair advantage,' and the like with respect to Ira's actions." *Id.* at 306, 307 S.E.2d at 567.

148. *See supra* note 33 and accompanying text. The court's four part test is similar to that formulated by Professor Hillman.

To be entitled to relief under an expectations-based analysis, the dissatisfied shareholder should show: (1) that he or she became a participant because of a substantial expectation or set of expectations known or assumed by the other participants; (2) that the prospect that the expectation will be achieved is unlikely; and (3) that the failure to achieve the expectation was in large part beyond the control of the participant.

Hillman, *supra* note 37, at 77.

potentially preclude relief to some minority shareholders who actually have suffered a freeze-out.

The first prerequisite requires the minority shareholder to establish the existence of his reasonable expectations.¹⁴⁹

These "reasonable expectations" are to be ascertained by examining the entire history of the participants' relationship. That history will include the "reasonable expectations" created at the inception of the participants' relationship; those "reasonable expectations" as altered over time; and the "reasonable expectations" which develop as the participants engage in a course of dealing in conducting the affairs of the corporation. The interests or views of the other participants must be considered in determining "reasonable expectations." The key is "reasonable." In order for plaintiff's expectations to be reasonable, they must be known to or assumed by the other shareholders and concurred in by them. Privately held expectations which are not made known to the other participants are not "reasonable." Only expectations embodied in the understandings, express or implied, among the participants should be recognized by the court.¹⁵⁰

From this language, it appears that the minority must establish something akin to a shareholders' agreement,¹⁵¹ not written, but nevertheless an "understanding, express or implied." This requirement might be achieved easily by some minority shareholders;¹⁵² for others it may prove to be a significant obstacle. In particular, the requirement may affect minority shareholders who did not attain an understanding, who reached an understanding but cannot prove its existence, or who reached a written agreement that does not include the full understandings of the shareholders.¹⁵³

In *Meiselman* the court noted that minority shareholders often lack the bargaining power or foresight to negotiate a formal agreement at the inception of the relationship.¹⁵⁴ It is difficult to imagine how the minority's position is enhanced after entering into the corporation. The reasonable expectations test was intended to deal with the problem of the minority who failed to provide for his own protection with a formal agreement.¹⁵⁵ Yet, some minority shareholders may be unable to meet the standards of the test. A minority may have

149. See *supra* note 33 and accompanying text.

150. *Meiselman*, 309 N.C. at 298, 307 S.E.2d at 563. These guidelines substantially represent the views of Professors O'Neal and Hillman. See O'Neal, *supra* note 42, at 886; Hillman, *supra* note 37, at 77, 85-86. See also *supra* note 148.

151. See *supra* notes 123-26 and accompanying text.

152. See, e.g., *Topper*, 107 Misc. 2d at 27, 433 N.Y.S.2d at 361. ("The petitions and supporting affidavits in this case show conclusively, and respondents do not deny, that petitioner . . . associated himself with [the corporations] in the expectation of being an active participant in the operation of both corporations.")

153. The requirement may also affect the minority shareholder who cannot prove that his expectations are substantial. Under the court's guidelines for establishing reasonable expectations, "only substantial expectations should be considered." *Meiselman*, 309 N.C. at 299, 307 S.E.2d at 563. It would appear, however, that employment and management participation are expectations that meet this standard.

154. See *supra* note 134 and accompanying text.

155. See *supra* notes 138-40 and accompanying text.

or develop expectations of participation, yet, given its disadvantaged position, be unable to attain an understanding "concurred in" by the other shareholders—either expressly or by implication.¹⁵⁶

The shareholders actually may have reached an understanding regarding the participation of the minority that he may not be able to prove. If an express understanding had been reached, the majority may deny its existence. Absent an express agreement, the court suggested that implied understandings may be established by a "course of dealing" or the "history of the participants' relationship."¹⁵⁷ Such evidentiary sources do not aid the minority if the history of the relationship has been hostile. A hostile relationship does not support the conclusion that the shareholders have "concurred in" an understanding, a prerequisite to minority relief. For example, in *Meiselman* the brothers apparently never had maintained "cooperative efforts in operating the business."¹⁵⁸ Consequently, it is arguable that Ira never "concurred in" the participation of Michael in the family corporations.

The problem of proving an existing understanding appears particularly acute for the passive investor. Such an investor ordinarily commits capital to the corporation with an understanding that he will enjoy a return on his investment, yet refrain from management participation.¹⁵⁹ Initially, the corporation may be unable to generate enough profits to pay dividends. Once the corporation has earned sufficient profits, the majority may withhold dividends as a freeze-out technique. Assuming the majority denies the existence of an express agreement, the history of the relationship would not support the implication that the passive investor reasonably expected a return.

The shareholders may enter into a written agreement that does not embody all their expectations or understandings.¹⁶⁰ For example, the agreement may not include assurances of participation in management and employment. Subsequently, the minority shareholder who is suffering a freeze-out may claim a frustration of his expectations, alleging that the shareholders informally agreed to his participation and employment. While the reasonable expectations test was intended to deal with this problem,¹⁶¹ the test does not guarantee relief. In light of the existence of a written agreement that covers other aspects of substantive corporate policy, a court might conclude that the expectations were never a subject of understanding among the shareholders.¹⁶²

156. "Determining the existence of mutual acceptance of expectations becomes more difficult as the number of participants increases. What may be a manageable task when only two or three participants are involved may be exceedingly difficult as the number increases." Hillman, *supra* note 37, at 85.

157. See *supra* note 150 and accompanying text.

158. *Meiselman*, 309 N.C. at 299, 307 S.E.2d at 563.

159. See Hillman, *supra* note 37, at 79 n.248.

160. See, e.g., *Topper*, 107 Misc. 2d at 27, 33, 433 N.Y.S.2d at 361, 365.

161. See *supra* notes 138-140 and accompanying text.

162. See Hillman, *supra* note 37, at 84; see also *id.* at 78 n.246, (parol evidence rule may exclude evidence not contained in an existing written agreement).

The *Meiselman* reasonable expectations test, however, does not compel this result. Quoting

These examples illustrate cases in which minority shareholders may never meet the court's initial requirement that the minority shareholder establish his reasonable expectations. For practitioners who represent close corporation interests, the message of *Blount* and *Meiselman* appears to be to assume the worst in the close corporation relationship. That is, embody the expectations in a written shareholders' agreement. Thereafter, document any understandings reached.¹⁶³

Assuming the minority shareholder has established his expectations, he must show that they have been frustrated.¹⁶⁴ If the minority has been excluded systematically from the corporation over a substantial period of time, this requirement might be met easily. If the freeze-out has existed for a short period of time, however, a minority shareholder might be denied relief unless he can show that his expectations are unlikely to be achieved in the future.¹⁶⁵ In addition, a minority shareholder who has not suffered total exclusion might be granted more limited relief on the grounds that his expectations have been substantially fulfilled.

To satisfy the third part of the test, the minority shareholder must also show that the frustration of his expectations was not his fault and was beyond his control.¹⁶⁶ The court did not elaborate on this requirement,¹⁶⁷ but a recent New Jersey case illustrates how this requirement might deny relief. In *Exadaktilos v. Cinnaminson Realty Co., Inc.*¹⁶⁸ the court applied a test similar to a reasonable expectations test¹⁶⁹ and determined that the minority shareholder had expected to participate in the management of the corporation.¹⁷⁰ Dissolution was not granted, however, because of his unsatisfactory managerial per-

O'Neal, the court recognized that: "In a close corporation, the corporation's charter and bylaws almost never reflect the full business bargain of the participants." *Meiselman*, 309 N.C. at 299, 307 S.E.2d at 563 (quoting O'Neal, *supra* note 42, at 886). O'Neal continued, in the original text: "Even when the participants formalize their bargain in a written shareholders' agreement, their participation in the business is often grounded on assumptions that are not mentioned in the agreement." *Id.*

163. See Valenti, *Business Associations*, 33 SYRACUSE L. REV. 11, 14 (1982).

164. See *supra* note 33 and accompanying text.

165. See *Gidwitz v. Lanzit Corrugated Box Co.*, 20 Ill. 2d 208, 220, 170 N.E.2d 131, 138 (1960). See also Hillman, *supra* note 37, at 79.

166. See *supra* note 33 and accompanying text.

167. In his concurring opinion, Justice Martin stated that: "If it is determined that plaintiffs' rights or interests require protection because of plaintiffs' own conduct, it would appear improper to grant equitable relief." *Meiselman*, 309 N.C. at 315, 307 S.E.2d at 572 (Martin, J., concurring).

168. 167 N.J. Super. 141, 400 A.2d 554 (1979), *aff'd*, 174 N.J. Super. 559, 414 A.2d 994 (1980).

In *Exadaktilos* the minority shareholder received his ownership in the corporation by a gift of stock from his father-in-law. Subsequently, he was employed by the corporation. He was later fired because he failed to "learn the business." The minority brought an action for dissolution under New Jersey's majority oppression statute. N.J. STAT. ANN. § 14A:12-7(1)(c) (1983). *Cf. Topper*, 107 Misc. 2d at 29, 433 N.Y.S.2d at 362 ("[w]hether the controlling shareholder discharged petitioner for cause or in their good business judgment is irrelevant . . ."). See also Hillman, *supra* note 37, at 54 ("*Exadaktilos* represents a significant limitation on the reasonable expectations analysis, and as such it is not likely to produce results different from those of the traditional approach to oppression").

169. While the court did not explicitly recognize a reasonable expectations test, the court did apply an expectations-based analysis. See *Exadaktilos*, 167 N.J. Super. at 154-55, 400 A.2d at 561.

170. *Id.* at 155-56; 400 A.2d at 561-62.

formance.¹⁷¹ The court deemed satisfactory performance a "condition precedent" to the fulfillment of his management expectations.¹⁷² It appears then that a frozen-out minority might be denied relief if his actions have contributed to his predicament.

Finally, the minority shareholder must show that under all the circumstances of the case he is entitled to some form of equitable relief.¹⁷³ While the court considered that focusing on the acts of the majority would be inappropriate,¹⁷⁴ consideration of all the circumstances places importance on the effect of minority relief on the majority shareholders. Such circumstances appear to include the "benefit and injury"¹⁷⁵ to the other shareholders and the "rights or interests"¹⁷⁶ of other shareholders. The court failed to define such circumstances further. Whether circumstances regarding the effect on the majority might be used to deny relief to minority shareholders is unclear; however, these circumstances might mitigate relief. For example, dissolution might not be granted to the minority on the basis that the loss of the going concern value¹⁷⁷ is "unduly burdensome"¹⁷⁸ on the other shareholders. Alternatively, the court might force the majority to buy out the minority interest. Valuation of the buyout might be diminished or the terms of payment extended to relieve any perceived burden on the majority.¹⁷⁹

Nevertheless, this final requirement of the reasonable expectations test does benefit minority shareholders. Under all the circumstances, the minority needs only to show that *some* form of relief is necessary.¹⁸⁰ That is, he does not have to show dissolution is warranted before alternative relief is available.¹⁸¹ Absent the requirement that the minority must establish the necessity of "drastic"¹⁸² dissolution relief, his chances of attaining some relief may be enhanced.

171. *Id.* at 155, 400 A.2d at 561.

172. *Exadaktilos*, at 156, 400 A.2d at 562.

173. *See supra* note 33 and accompanying text.

174. *See supra* note 147 and accompanying text.

175. *Meiselman*, 309 N.C. at 296-97, 307 S.E.2d at 562 ("The statutes [N.C. GEN. STAT. §§ 55-125(a)(4); 55-125.1 (1982)] require a standard in which all of the circumstances surrounding the parties are considered . . . [T]he trial court, in deciding whether to grant relief, 'must exercise its equitable discretion, and consider actual benefit and injury to [all of] the shareholders resulting from dissolution' or other possible relief.") (citation omitted).

176. *See id.* ("The question is essentially one for resolution through the familiar balancing process and flexible remedial resources of courts of equity." To hold otherwise would allow a plaintiff to demand at will dissolution of a corporation or a forced buyout of his shares or other relief at the expense of the corporation and without regard to the rights or interests of other shareholders.") (citation omitted).

177. *See supra* note 64 and accompanying text.

178. *Meiselman*, 309 N.C. at 316, 307 S.E.2d at 573 (Martin, J., concurring)).

179. *Id.*

180. *Id.* at 301, 307 S.E.2d at 564.

181. *Id.* Because N.C. GEN. STAT. § 55-125.1 (1982) (alternatives to dissolution) provides for alternative remedies in an action filed under N.C. GEN. STAT. § 55-125 (1982) (dissolution), § 55-125.1 might be interpreted to require a showing that dissolution was warranted before alternative relief was available. The court rejected this construction. *See also* R. ROBINSON, *supra* note 66, § 29-14 (interpreting the availability of alternative relief consistently with the court).

182. *See supra* note 63 and accompanying text.

This analysis of the court's four-part reasonable expectations test reveals a standard of minority relief that goes beyond that traditionally afforded by majority oppression statutes, or any position that suggests minority interests must be protected with a written agreement. Consequently, minority shareholders may be protected to an extent not available in some other jurisdictions.¹⁸³ The analysis also indicates, however, that relief to minority shareholders may be denied or mitigated by problems of proof, the minority shareholder's conduct, or other circumstances. Some minority shareholders may never establish successfully their reasonable expectations under the standards articulated by the *Meiselman* court. That is, they may never establish the existence of an understanding, concurred in by the other shareholders.¹⁸⁴ Moreover, a minority shareholder who contributes capital to a corporation and cannot establish that management participation or pecuniary benefit, for example, were subjects of an understanding, would not appear eligible for relief under sections 55-125(a)(4) and 55-125.1.¹⁸⁵

Even when no understanding can be established, it is unreasonable to deny the frozen-out minority shareholder the means to withdraw his investment, while the majority enjoys the profitability of the business through salaries. The mere commitment of capital would seem to generate a reasonable expectation of one's participation in profits or the right to withdraw one's investment if a return is withheld. Some may argue that the frozen-out minority, unable to establish his alleged expectations, should exercise his statutory right to compel dividends.¹⁸⁶ The majority, however, may effectively frustrate this right by forcing the minority to litigate annually.¹⁸⁷ Faced with an "incorrigible" majority, dissolution and alternative remedies, such as the buyout, should be available to such a minority shareholder.¹⁸⁸ The *Meiselman* reasonable expectations test should be expanded to protect the minority who has been frozen-out yet who cannot establish his expectations of participation or pecuniary benefit as subjects of an understanding. An appropriate complement to the reasonable expectations defined and protected under *Meiselman* is the reasonable expectation that the majority will fulfill its fiduciary duty to the minority.

The doctrine of majority rule enables majority shareholders to control

183. To define more clearly statutory relief available to the minority shareholder, the North Carolina legislature might consider the incorporation of a reasonable-expectations standard into N.C. GEN. STAT. § 55-125(a)(4) (1982). See Davidian, *supra* note 37, at 62 (suggesting the legislative adoption of the reasonable expectations test in New York).

184. See *supra* note 150 and accompanying text.

185. The *Meiselman* court does hint that some factors, absent an understanding, might play a role in the reasonable expectations test. See *Meiselman*, 309 N.C. at 302, 307 S.E.2d at 565 (suggesting that Michael's "rights or interests" might be determined in part from his ownership of stock).

186. N.C. GEN. STAT. § 55-50 (1982).

187. See *supra* note 56.

188. See Comment, *supra* note 71, at 139-40 ("The courts may look for a 'pattern of conduct by the dominant shareholders and a disposition on their part to continue the pattern' that is violative of the rights and interests of the minority. When the future holds 'no hopes of abatement,' or where the majority is 'incorrigible,' dissolution may be in order.") (quoting *Gidwitz v. Lanzit Corrugated Box Co.*, 20 Ill. 208, 220, 170 N.E.2d 131, 138 (1960)).

corporate affairs. Majority shareholders should not be permitted, however, to exercise that power arbitrarily or without regard to minority interests.¹⁸⁹ That the majority owes a fiduciary duty to the minority is now widely recognized.¹⁹⁰ The applicability of such a fiduciary standard in the context of a freeze-out has been recognized by Professor O'Neal:

Any of the schemes to [freeze]-out minority shareholders raise basic questions as to the nature and extent of the duties owed by controlling shareholders, directors, and officers . . . to minority shareholders [The] view that the controlling shareholders and corporate managers do not owe duties to minority shareholders is outmoded, at least as applied to [freeze]-outs and other attempts to deprive minority shareholders of their proportionate rights without a just equivalent. Where several owners carry on an enterprise together, their relationship should be considered a fiduciary one.¹⁹¹

The North Carolina Supreme Court has applied a fiduciary standard to majority shareholders of a close corporation in *Gaines v. Long Manufacturing Co.*¹⁹² In *Gaines* a minority shareholder sought an injunction to prevent the proposed issuance of additional stock, which would have diluted his interest in the corporation.¹⁹³ The court recognized that the majority owes a fiduciary duty to the minority.¹⁹⁴ Such a relationship imposes on the majority

the duty to exercise good faith, care, and diligence to make the property of the corporation produce the largest possible amount, to protect the interests of the holders of the minority of the stock, and to secure and pay over to them their just proportion of the income and of the proceeds of the corporate property.¹⁹⁵

Actions of the majority "causing a deprivation or sacrifice of [the minority's] pecuniary interests or holdings" constitute a breach of fiduciary duty.¹⁹⁶

Like the reasonable expectations test, this fiduciary duty operates to protect minority interests by limiting the exercise of majority control. To effectuate the *Meiselman* court's goal of protecting the frozen-out minority who has

189. See F. O'NEAL, *supra* note 46, § 7.13.

190. See, e.g., *Southern Pac. Co. v. Bogert*, 250 U.S. 483, 487-88 (1919) ("The majority has the right to control; but when it does so, it occupies a fiduciary relationship toward the minority, as much as the corporation itself or its officers and directors."); *Mims v. Valley Nat'l Bank*, 14 Ariz. App. 190, 481 P.2d 876 (1971); *Jones v. H. F. Ahmanson & Co.*, 1 Cal. 3d 93, 460 P.2d 464, 81 Cal. Rptr. 592, (1969); *Bennett v. Brevil Petroleum Corp.*, 34 Del. Ch. 6, 99 A.2d 236 (Ch. Ct. 1953); *Zidell v. Zidell, Inc.*, 277 Or. 413, 560 P.2d 1086 (1977); *Seaboard Indus. v. Monaco*, 442 Pa. 256, 276 A.2d 305 (1971). See generally F. O'NEAL, *supra* note 46, § 7.13; Note, *Strict Fiduciary Duty in Close Corporations: A Concept in Search of Adoption*, 18 CAL. W.L. REV. 1 (1982).

191. F. O'NEAL, *supra* note 46, § 7.13 (footnote omitted).

192. 234 N.C. 340, 67 S.E.2d 350 (1951). A fiduciary standard also was applied in the companion case of *Gaines v. Long Mfg. Co.*, 234 N.C. 331, 68 S.E.2d 355 (1951). There the minority alleged that the majority "are willfully and deliberately failing to pay dividends, and are operating [the] business for their own gain and advantage for the purpose of rendering the stock of the plaintiff valueless and with the deliberate intent of 'freezing-out' plaintiff from his ownership in [the] corporation." *Id.* at 339, 67 S.E.2d at 361.

193. *Gaines*, 234 N.C. at 344, 67 S.E.2d at 353.

194. *Id.* at 345, 67 S.E.2d at 354.

195. *Id.* at 344, 67 S.E.2d at 353.

196. *Id.* at 345, 67 S.E.2d at 354 (quoting *White v. Kincaid*, 149 N.C. 415, 63 S.E. 109 (1908)).

failed to protect himself, it would be appropriate, therefore, to complement the reasonable expectations test with the fiduciary duty. That is, the minority's reasonable expectations should include a fiduciary duty owed the minority by the majority. Under *Gaines* this standard includes a duty to provide a return to the minority from profits. Consequently, a freeze-out would constitute a breach, to the extent pecuniary benefit is denied. Furthermore, relief under sections 55-125(a)(4) and 55-125.1 would be available to the frozen-out minority who is unable to establish an understanding.

As noted, enhanced minority shareholder relief carries with it the potential for minority shareholder abuse of the dissolution suit¹⁹⁷ and damage to corporate viability.¹⁹⁸ Ideally, the statutory scheme of minority relief and its judicial interpretation will strike a balance between minority relief and the potential hazards that accompany relief. Possibly the most unpalatable hazard is the minority shareholder who might use the dissolution suit against an innocent majority to manipulate corporate decisionmaking.¹⁹⁹ A statute that allows the majority to terminate a dissolution action upon its agreement to buy out the minority interest²⁰⁰ has been recognized as a deterrent to such abuse.²⁰¹ Faced with a certain buy-out, the minority may forego litigation based on manipulation of the corporation rather than legitimate expectations of participation.²⁰² Such a statute also enables the majority to terminate dissolution litigation that might damage the corporation.²⁰³ While North Carolina has a statutory buy-out remedy, it is granted at the court's discretion.²⁰⁴ A majority initiated buy-out statute should accompany this provision.

The reasonable expectations test in *Meiselman* certainly expands the body of North Carolina law regarding minority shareholder relief under sections 55-125(a)(4) and 55-125.1. Unfortunately, this test fails to protect some minor-

197. See *supra* notes 108-12 and accompanying text.

198. See *supra* notes 113-15 and accompanying text.

199. See *supra* notes 108-12 and accompanying text.

200. See, e.g., CAL. CORP. CODE § 2000 (West 1977):

"(a) . . . in any suit for involuntary dissolution . . . the corporation or . . . the holders of 50 percent or more of the voting power of the corporation . . . may avoid the dissolution of the corporation . . . by purchasing for cash the shares owned by the plaintiffs or by shareholder so initiating the proceeding . . . at their fair value. The fair value shall be determined on the basis of the liquidation value but taking into account the possibility, if any, of the sale of the entire business as a going concern in a liquidation."

Id.

Several states have adopted similar statutes. See, e.g., CONN. GEN. STAT. ANN. § 33-384 (West Supp. 1981); MD. CORPS. & ASSN'S CODE ANN. § 4-603 (1975); MINN. STAT. ANN. § 302A.751 (West Supp. 1981); N.J. STAT. ANN. § 14A:12-7 (West Supp. 1981); N.Y. BUS. CORP. LAW § 1118(a)-(b) (Consol. 1979); W. VA. CODE § 31-1-134 (1982).

Unlike the California statute some states provide for an alternative to lump sum cash payment by the majority. See, e.g., N.Y. BUS. CORP. LAW § 1118(a) (Consol. 1979) (providing for a buyout of shares "at their fair value and upon such terms and conditions as may be approved by the court" (emphasis added)).

201. See *Stumpf v. C. E. Stumpf & Sons, Inc.*, 47 Cal. App. 3d 230, 236, 120 Cal. Rptr. 671, 674 (1975). See also Davidian, *supra* note 37, at 48.

202. See Davidian, *supra* note 37, at 47.

203. *Id.*

204. N.C. GEN. STAT. § 55-125.1(a)(4) (1982).

ity shareholders who may in fact be suffering from a freeze-out by the majority shareholders. Consequently, the reasonable expectations test should be complemented with the standard that the majority owes a fiduciary duty to the minority. Additionally, the legislature should balance enhanced minority relief with a statutory provision permitting the majority shareholders to terminate litigation initiated under section 55-125(a)(4) when they agree to buy out the minority interest.

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