

**IN THE SUPREME COURT
STATE OF NORTH DAKOTA**

Reed H. Danuser,

Plaintiff/Appellee,

vs.

IDA Marketing Corporation; IDA of
Moorhead Corporation; James
Leach; Steve Leach; David P.
Gruenhagen; and Val Tareski,

Defendants,

IDA Marketing Corporation;
IDA of Moorhead Corporation;
and James Leach,

Appellants.

SUPREME COURT NO. 20120443

Cass County No. 09-2011-CV-00563

ON APPEAL FROM THE "JUDGMENT ENTERED ON OCTOBER 19, 2012,
AND AMENDED ON FEBRUARY 13, 2013," AND THE MEMORANDUM
OPINION GRANTING, IN PART, PLAINTIFF'S MOTION FOR
SUMMARY JUDGMENT DATED OCTOBER 6, 2011"

STATE OF NORTH DAKOTA
COUNTY OF CASS

REPLY BRIEF OF DEFENDANT/APPELLANT JAMES LEACH

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LAW AND ARGUMENT

I. The Trial Court Erred in Finding Leach Breached a Fiduciary Duty to Danuser.

A. Leach Properly Preserved the Issues of Director and Shareholder Liability for Appeal.

¶1 Issues raised in the lower court through oral argument or brief are properly preserved for appeal. See Eastburn v. B.E., 545 N.W.2d 767, 773 (N.D. 1996). In this case, Appellant James Leach necessarily preserved the issue of the extent a director owes his fiduciary duty at the lower court by arguing the standard in his Answer to Appellee Reed Danuser’s Complaint and Post-Trial Brief. (Appellant App. 68-69, Appellee App. 109.) Specifically, Leach argued the duty of directors is established within Weidner v. Engelhart, 176 N.W.2d 509 (N.D. 1970), which explains “directors of a corporation are bound to use due care and to be diligent with respect to the management and administration of the affairs of the corporation” (Appellant App. 68-69, Appellee App. 109) (emphasis added).

¶2 Leach’s Answer and Post-Trial Brief did not concede liability to Danuser individually and they essentially addressed the general rule with regard to director liability. That is, a director’s fiduciary obligation requires that he act in good faith, in a manner he reasonably believes to be in the best interests of the corporation, and with the care an ordinarily prudent person would exercise. N.D.C.C. § 10-19.1-50(1). A director’s duty, therefore, extends to the corporation itself and shareholders collectively, rather than shareholders individually. Prod. Credit Ass’n of Fargo v. Ista, 451 N.W.2d 118, 121 (N.D. 1990). Leach’s repeated argument regarding a director’s duty and potential liability to the corporation as an entity preserved the issue for appeal.

Accordingly, this Court has authority to address the issue.

¶3 The issue of the extent a shareholder owes another shareholder a fiduciary duty, and its inapplicability to the present case, is also properly before this Court due to Leach's numerous statements to Danuser and the lower court that Leach did not hold shares in IDA Marketing or IDA Moorhead at the time Danuser was terminated. (Appellant App. 51, 54, 66; Docket #261 at 15, 52-53.) Despite Leach's arguments, the lower court made a factual finding after the submissions of the parties' post-trial briefs that Leach "always held a substantial and controlling majority of the original stock" and, therefore, applied the fiduciary duty standard owed among shareholders. (Appellant App. 122, 128.) However, the lower court's factual finding was in error in light of the evidence, and this Court may now review the record to assess its misapplication. See Brandt v. Somerville, 2005 ND 35, ¶ 12, 692 N.W.2d 144.

¶4 In fact, the record frequently references that Leach owned 2,421,118 shares of IDA Moorhead prior to 1994, but sold them in exchange only for a security interest. (Appellant App. 14, 31, 51, 121-22.) Leach then regained his stock on November 29, 2010. (Id. at 125.) Yet, the date he reclaimed his stock was after the companies decided to terminate Danuser and, accordingly, was after the alleged breach of fiduciary duty took place. (Id. at 20.)

¶5 In light of the evidence, the lower court erred in applying a fiduciary duty standard applicable only to co-shareholders. By analyzing Leach's fiduciary duty to Danuser in terms of his "high fiduciary obligations" and duty "of utmost loyalty and good faith," the court erroneously applied the law. (Id. at 128.) This Court, therefore, not only has authority to review the trial court's factual findings regarding an alleged fiduciary

duty to Danuser, it should reverse its order as an erroneous view of the facts and the law.
Brandt, 2005 ND 35, ¶ 12, 692 N.W.2d 144.

B. The Court’s Statutory Authority to Order Equitable Relief to an Individual Shareholder Does Not Alter a Director’s Fiduciary Duty to Shareholders Collectively.

¶6 As noted, a director’s fiduciary duty extends to the corporation “to act in all things of trust wholly for the benefit of the corporation.” Ista, 451 N.W.2d at 121. This general rule with respect to a director’s duty recognizes that a director must act in the best interests of the corporation as a whole and its shareholders collectively. N.D.C.C. § 10-19.1-50(1). The fact that N.D.C.C. § 10-19.1-115 offers equitable remedies to an individual shareholder does not, however, impose additional, direct fiduciary obligations upon directors to those shareholders.

¶7 Although this Court has previously held “Chapter 10-19.1, N.D.C.C., imposes a duty upon officers, directors, and those in control of a corporation to act in good faith, and affords remedies to minority shareholders if those in control act fraudulently, illegally, or in a manner unfairly prejudicial toward any shareholder,” the duties and remedies within the Business Corporations Act are distinct. Lonesome Dove Petroleum, Inc. v. Nelson, 2000 ND 104, ¶ 30, 611 N.W.2d 154. The Act effectively sets forth the duty owed by directors, and it separately affords equitable remedies to shareholders for certain actions of a director. Id.; see Brandt, 2005 ND 35, ¶¶ 8-9, 692 N.W.2d 144. Therefore, the proper standard to assess a director’s fiduciary duty is not N.D.C.C. § 10-19.1-115, and is rather N.D.C.C. § 10-19.1-50, which imposes a duty on directors to the corporation as an entity and does not extend the duty to individual shareholders, such as Danuser, who have alleged a personal harm only.

C. No Special Relationship Existed Between Leach and Danuser to Impose a Direct Fiduciary Duty.

¶8 While a director’s fiduciary duty generally extends only to the shareholders collectively, a director may have a duty to an individual shareholder if he has a particularized right, contract, or special relationship with the director. See Redmon v. Griffith, 202 S.W.3d 225, 234 (Tex. Ct. App. 2006). In the context of corporate relations, courts have explained a special relationship consists of a relationship of trust and confidence, whereby a director acquires influence and betrays confidence extended by a shareholder. Cotten v. Weatherford Bancshares, Inc., 187 S.W.3d 687, 698 (Tex. Ct. App. 2006). There must also be a long business and personal relationship prior to any alleged breach of fiduciary duty in order for a special relationship to exist. Id.

¶9 Danuser attempts to argue the mere fact that Leach was a director and entered into the Shareholder Control Agreement created a special relationship, and a resulting fiduciary duty, between Leach and Danuser. However, a relationship confined solely to corporate dealings is insufficient to produce a special relationship. See id. Moreover, no evidence shows Danuser customarily received advice or judgment from Leach to entrust him with making decisions. To the contrary, the trial court determined “Leach played no role in the day to day operations of the company after the initial stock sale was negotiated.” (Appellant App. 121.) Without the existence of a special relationship, there is no basis for Leach to have a fiduciary obligation directly to Danuser.

D. Joint and Several Liability is Improper Due to the Trial Court’s Analysis of the Issue and the Lack of Authority to Order Such Liability.

¶10 Joint and several liability of a director personally liable for a breach of fiduciary

duty is neither expressly addressed nor allowed within the Business Corporations Act. However, the trial court imposed joint and several liability on Leach for all resulting damages to Danuser based on Resolution Trust Corp. v. Block, 924 S.W.2d 354 (Tenn. 1996). The court provided no other statute or case law to justify its decision and, instead, improperly relied on Block despite the fact that “unanimous recognition” of joint and several liability only extends to a director’s personal liability to the corporation as a whole. See id. at 355-56.

¶11 Danuser now argues N.D.C.C. § 10-19.1-85.1 provides a separate basis for the trial court’s order of joint and several liability because the court may grant equitable relief. However, § 10-19.1-85.1 was not cited by the trial court, nor was the court’s decision with regard to joint and several liability provided within its equitable remedies to Danuser. (Appellant App. 129-35.) Although a trial court’s incorrect basis for reaching a result may not necessarily require reversal if there is a justification under a correct law or reasoning, there is no such alternative basis to impose joint and several liability in this case. See Huber v. Farmers Union Serv. Ass’n of N.D., 2010 ND 151, ¶ 17, 787 N.W.2d 268.

¶12 Danuser relies on Pedro v. Pedro, 489 N.W.2d 798 (Minn. Ct. App. 1992), to support his conclusion that the equitable remedies of § 10-19.1-85.1 allow joint and several liability, yet the case is inapposite. In Pedro, the Minnesota Court of Appeals ordered joint and several liability on a director only because the director already presented the argument to the court and failed to raise the issue of personal liability in a previous appeal. Id. at 803. Consequently, the court could not re-address the issue. Id.

¶13 Even though the court further noted a trial court has authority to grant equitable

relief it deems just, the Pedro court did not provide any further analysis on the issue and only explained there was no contrary authority. Id. In this case, however, authority to the contrary exists in the lower court's decision, namely that courts order joint and several liability once a director has been found personally liable to the corporation itself, not individual shareholders. See Block, 924 S.W.2d at 355-56. Therefore, without a valid basis to impose joint and several liability, this Court should reverse the trial court's order regarding joint and several liability.

II. The Trial Court Erred in Assessing Danuser's Damages.

A. The Buy-Sell Agreement Signed by Danuser is Valid and Enforceable.

¶14 The Buy-Sell Agreement in this case presents the appropriate method of valuing Danuser's shares, and the trial court erred in failing to recognize its provisions. Although it is true that Leach did not sign the Buy-Sell Agreement, the agreement is nonetheless valid because it was "signed by all persons who, on the date the agreement first became effective, [were] then the shareholders of the corporation." N.D.C.C. § 10-19.1-83; (Appellant App. 39-43.) Thus, the agreement is valid, enforceable, and binding against the persons who signed the agreement, including Danuser. N.D.C.C. § 10-19.1-83.

¶15 Danuser's argument that the Buy-Sell Agreement valuation is not triggered with a breach of fiduciary duty claim is further unavailing. The agreement clearly states that the provisions shall be utilized for each departing shareholder, such as for his/her "termination." (Appellant App. 39.) Danuser's termination is precisely the occurrence in this case, thus triggering the Buy-Sell Agreement.

¶16 In addition to conforming to the technical requirements of the Business Corporations Act, the agreement also is presumed to reflect the parties' reasonable

expectations about the matters it set forth. N.D.C.C. § 10-19.1-115(4). Accordingly, the trial court was required to order any valuation of shares under the terms of the agreement. Id. § 10-19.1-115(3)(a). The trial court failed to do so, however, and this Court should reverse its damage assessment.

B. If the Trial Court Erred in its Damage Calculation, Remanding the Case is the Proper Remedy.

¶17 Danuser further questions the valuation process established within the Buy-Sell Agreement, noting it is not a workable formula and it includes incorrect numbers. If this Court should determine the formula or calculation is insufficient, affirming the trial court's damage assessment is not the proper remedy. Rather, this Court should remand the case to require application of the correct figures and formula. See *Woodworth v. Chillemi*, 1999 ND 43, ¶ 14, 590 N.W.2d 446. Moreover, remand would be necessary for the trial court's deviation from the Buy-Sell Agreement's presumptive validity, as it did not make any factual findings with regard to the agreement's unreasonableness. N.D.C.C. § 10-19.1-115(3)(a). Therefore, even if the trial court has broad authority to issue equitable relief, this Court should remand the case to allow the lower court to correct its calculation or provide an explanation regarding the unreasonableness of the agreement's terms.

CONCLUSION

¶18 Appellant James Leach respectfully requests this Court reverse the trial court's memorandum opinion and order for judgment dated October 11, 2012 and its resulting judgment and order entry of judgment dismissing all claims against Appellant Leach.

Dated this 5th day of June, 2013.

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CERTIFICATE OF COMPLIANCE

The undersigned, as attorney for Defendant/Appellant James Leach in the above matter and as author of the above brief certified that the brief is in compliance with Rule 32 of the North Dakota Rules of Appellate Procedure, that the above brief was prepared with proportional type face and that the total number of words in the brief, excluding words in the Table of Contents, Table of Authorities, Affidavit of Service, and Certificate of Compliance total 1,997.

Dated this 5th day of June, 2013.

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To the best of Affiant's knowledge, the address above given was the actual email addresses of the parties intended to be so served. The above document was duly mailed in accordance with the provisions of the Rules of Civil Procedure.

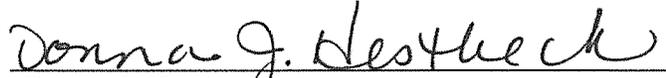
Donna J. Hestbeck

Subscribed and sworn to before me this 5th day of June, 2013.

(SEAL)

Notary Public, Cass County, North Dakota

To the best of Affiant's knowledge, the address above given was the actual email addresses of the parties intended to be so served. The above document was duly mailed in accordance with the provisions of the Rules of Civil Procedure.



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(SEAL)



Notary Public, Cass County, North Dakota

