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A Business Law Update

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Shareholder Oppression Claims in Closely Held Michigan Corporations: A Powerful Remedy Against Abuses of Power

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Most institutions in our society make decisions upon the consent of the majority, from legislatures passing important bills to families deciding on what movie to watch on movie night. Majority rule is also the way most closely held corporations conduct business, with shareholders voting on critical issues that will impact the operations or direction of the company and the company taking the action the majority shareholders decided upon, thus giving the majority control. Unless there is a unanimous decision in which all shareholders agree about a matter, some shareholders will find themselves in the minority.

While they may not have control over the business, minority shareholders in closely held Michigan corporations still have rights. One such right is the ability to challenge the acts of the company's directors and those in control of the company if they are abusing their power, taking illegal or fraudulent actions, or running the business in ways that are unfair to or oppressive to the company or shareholder(s).

When controlling shareholders or directors engage in such conduct, Section 489 of the Michigan Business Corporation Act (the "Act") provides remedies for shareholder oppression designed to protect the non-controlling shareholders as well as the business from the malfeasance of those in control. It is important to note that, while Section 489 of the Act is often described as the minority shareholder statute, the statue is not only available to minority shareholders, but to any shareholder of the company, including those who may be considered a "majority shareholder" based on their ownership percentage of the company. In *Young v. Vandermeer*, the Michigan Court of Appeals found that even though the plaintiff was the majority shareholder, she could bring a claim for shareholder oppression because she only needed to show that the defendant was in control.

Willfully Unfair and Oppressive Conduct

Disappointment in a vote's outcome or disagreement with how the directors and/or the controlling shareholders run the business alone does not constitute oppression, nor does questionable business decisions or incompetence if such actions were made in good faith. Instead, the rights and remedies established in Section 489 of the Act, are only available if a shareholder can "establish that the acts of the directors or those in control of the corporation are illegal, fraudulent, or willfully unfair and oppressive to the corporation or to the shareholder."

Section 489 of the Act goes on to define "willfully unfair and oppressive conduct" as:

> "a continuing course of conduct or a significant action or series of actions that substantially interferes with the interests of the shareholder as a shareholder. Willfully unfair and oppressive conduct may include the termination of employment or limitations on employment benefits to the extent that the actions interfere with distributions or other shareholder interests disproportionately as to the affected shareholder. The term does not include conduct or actions that are permitted by an agreement, the articles of organization, the bylaws, or a consistently applied written corporate policy or procedure."

Courts have also found that acts such as denying a shareholder's reasonable request to inspect the company's books and records, arbitrarily refusing to declare dividends, withholding information, preventing a minority shareholder from exercising shareholder rights (i.e., participating in shareholder meetings, examining financial records, voting to elect directors, etc.), unfair redemption plans, and self-dealing, could each potentially support a claim of shareholder oppression in Michigan.

In addition to providing evidence of willfully unfair and oppressive conduct, the shareholder must also be able to show intent on the behalf of the controlling shareholders or directors. In 2019, in *Franks v. Franks,* the Michigan Court of Appeals described at length how courts should analyze shareholder oppression claims, emphasizing that the review should be of the controlling shareholders' and/or directors conduct rather than the effect of that conduct on the minority. The Court of Appeals found that "the Legislature requires proof of an intent to act in a manner that was unfair and oppressive to the shareholder" to establish oppression and "[T]herefore, with regard to acts that are willfully unfair and oppressive, the complaining shareholder must prove that the directors or persons in control of the corporation engaged in a continuing course of conduct or took a significant action or series of actions that substantially interfered with the interests of the shareholder as a shareholder, and that they did so with the intent to substantially interfere with the interests of the shareholder as a shareholder." As such, "a defendant can avoid liability by showing that he or she did not have the requisite intent when he or she took the acts that interfered with

the shareholder's interests" and that the actions were taken for a legitimate business reason.

The Business Judgment Rule Is Not a Shield Against Oppression Claims

Under Michigan law, poor business decisions and bad acts are considered two different things. While the latter may support an oppression claim, the former does not necessarily expose decision-makers to liability because of Michigan's "business judgment rule." This rule, like corresponding rules in other states, protects corporate officers and directors from having the court and others second-guess their decisions if such decisions lead to bad or even calamitous outcomes, but the rule only applies to bad decisions or acts made in good faith, not those made in bad faith.

As the court in *Franks* held, "the business judgment rule does not prohibit a court from evaluating defendants' business decisions—including their dividend policy—in light of the totality of the evidence to determine whether the evidence showed that defendants formulated their policy in bad faith and as part of a plan to commit acts amounting to shareholder oppression under MCL 450.1489(1)" and "accordingly, a shareholder necessarily overcomes the business judgment rule by presenting evidence to establish the elements of a claim under the shareholder oppression statute because that statute identifies wrongful conduct and provides a remedy for it."

Remedies for Oppressed Shareholders

In Michigan, if a court finds that the directors and/or shareholders in control of a closely held corporation have engaged in oppressive conduct towards a non-controlling shareholder, the Act provides several possible remedies to protect the rights and interests of such shareholder and the business itself, including:

- dissolving and liquidating the corporation's assets and business;
- canceling or altering a provision in the corporation's articles, amendments, or bylaws;
- canceling, altering, or enjoining a resolution or other act of the corporation;
- directing or prohibiting an act by the corporation or its shareholders, officers, directors or other persons party to the action;
- ordering the purchase of a shareholder's shares at fair value, either by the corporation or by the officers, directors, or other shareholders responsible for the wrongful acts; or
- awarding damages to the shareholder or the corporation.

While non-controlling shareholders may not wield power in a closely held corporation, Michigan law does empower them with remedies if those in control abuse their authority.

If you have questions or concerns about shareholder oppression in Michigan, please contact the author, Mary Cebula, or another attorney in Bodman's Business Practice Group. Bodman cannot respond to your questions or receive information from you without first clearing potential conflicts with other clients. Thank you for your patience and understanding.

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