

STATE OF MINNESOTA

FILED

DISTRICT COURT

COUNTY OF HENNEPIN

2010 MAY -4 AM 2:42

FOURTH JUDICIAL DISTRICT

Ethylon B "E.B." Brown, Benjamin A. Myers, Robert "Bob" Scott, Shannon Hartfiel, Robert Wilson, William J. Brown, Dokor Dejevongsa, et al.

BY HENN CO. DISTRICT COURT DEPUTY CLERK ADMINISTRATOR

Plaintiffs,

ORDER GRANTING PARTIAL SUMMARY JUDGMENT

27 CV 09-2277

v.

Jordan Area Community Council, as nominal defendant and defendant employer, Michael "Kip" Browne, P.J. Hubbard, Robert Hodson, Anne McCandless, et al.

Defendants.

The above-entitled matter came before Judge Charles A. Porter, Jr. on February 18, 2010, for a hearing on Plaintiffs' Motion for Partial Summary Judgment and on Defendants' Motion for Summary Judgment and Sanctions.

Jill Clark, Esq., appeared for the Plaintiffs. David Schooler, Esq., appeared on behalf of Defendants Brown, Hodson, Hubbard, McCandless, Sorenson, JACC, and Minneapolis Neighborhood Revitalization Project. James Moore, Esq., appeared on behalf of the City of Minneapolis.

Based upon the evidence adduced, the argument of counsel, and all of the files, records, and proceedings herein,

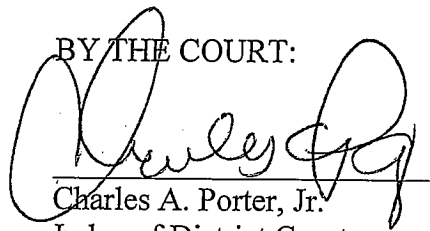
IT IS ORDERED:

1. Defendants' Motion is hereby **GRANTED** as follows: Plaintiffs' claims against Defendants Browne, Hubbard, McCandless, Hodson, and JACC (the first, second, fifth and sixth counts in the complaint, labeled consecutively as I, II, V and II) are hereby **DISMISSED WITH PREJUDICE**.
2. All other relief requested and not herein granted is **DENIED**.

3. The attached memorandum is incorporated herein.

Dated: 5-3-10

BY THE COURT:



Charles A. Porter, Jr.
Judge of District Court

MEMORANDUM

FACTS

Plaintiffs are a group of Jordan Area Community Council¹ members and one former JACC employee who bring six claims against a group of their neighbors, city councilpersons, a Minneapolis Police Department Inspector, and JACC itself. Plaintiffs' claims arise from a dispute over control and operation of JACC. Plaintiffs complaint alleges intentional interference with contract, aiding and abetting tortuous conduct, civil rights violation, breach of fiduciary duty, and breach of contract. They also seek equitable judicial intervention in JACC's operation under the Minnesota Nonprofit Corporation Act. Plaintiffs now move for summary judgment on some of their claims; Defendants Browne, Hubbard, McCandless, Hodson, and JACC move for summary judgment on all of Plaintiffs' claims against them and for sanctions.

This Court has previously addressed this matter by considering motions for a Temporary Restraining Order and a Temporary Injunction, the latter by receiving nine days of testimony and issuing findings thereupon for purposes of deciding the motions. (Order, Mar. 11, 2009; Order, July 10, 2009.) The details of this case are substantially recited in those orders, which are summarized again here for convenience. Plaintiffs Brown, Myers, Scott and Hartfiel claim to be wrongfully-oustered JACC board officers, removed and otherwise harmed by *ultra vires* actions of Defendants Browne, Hubbard, Hodson and McCandless. These Defendants are alleged to have breached their duties to the corporation by conspiring to violate its bylaws, committing waste, and otherwise not acting in the organization's best interest. Plaintiff Moore also claims that JACC violated

¹ The Jordan Area Community Council ("JACC") is a neighborhood non-profit corporation whose voting membership is comprised of individuals who live or work in the Jordan Neighborhood of Minneapolis and who have registered as members.

its employment contract with him. The remaining Plaintiffs are individuals who join in the complaint in their capacity as JACC voting members.

The claims arise from a disputed election in late 2008, which carried into 2009, to fill vacant JACC board positions. The JACC bylaws provide that the board will consist of at least five and no more than fifteen members. The membership attending JACC's annual meeting in October, 2008 did not fill vacancies on the board created by expiring terms; eight active board members remained in office. JACC membership voted to fill six board positions on January 12, 2009.

On January 14, 2008, the board of fourteen members met to elect officers. This Court denied the Plaintiffs' motions to overturn the officer slate chosen at the January 14 board meeting. Plaintiffs have since disclaimed interest in an injunctive remedy that would reinstate their standing as directors or officers. In October, 2009, JACC held its next annual meeting and elected five new board members to fill vacancies on the board, and at the time of the meeting the board had nine vacancies. The board now consists of 11 members and one *ex officio* member.

LEGAL ANALYSIS

The parties agree that the undisputed facts support judgment as a matter of law on the Nonprofit Corporation Act claim, the breach of fiduciary duty claims, and the breach of contract claim. Plaintiffs assert that disputed material facts prevent summary judgment on the remaining claims. The Court will consider the propriety of judgment as a matter of law on all of Plaintiffs' claims against Defendants JACC, Browne, Hubbard, Hodson, and McCandless, but will first briefly address Defendants' motion for sanctions.

Defendants have moved for Rule 11 sanctions as part of their summary judgment motion. Rule 11 plainly requires that a motion for sanctions be made “separately from other motions or requests.” Because Defendants’ request is not separate from their motion for summary judgment, the motion for Rule 11 sanctions must be denied.

Summary Judgment Standard

Summary judgment is appropriate when “the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits . . . show that there is no genuine issue as to any material fact and that either party is entitled to a judgment as a matter of law.” Minn. R. Civ. P. 56.03. Where material facts are in dispute, the Court must view evidence in the light most favorable to the nonmoving party, and the moving party bears the burden of proving that summary judgment is warranted. *Vacura v. Haar’s Equipment, Inc.*, 364 N.W.2d 387, 391 (Minn. 1985). On cross motions for summary judgment where there are no disputed facts, the only question is whether either party is entitled to judgment as a matter of law. Minn. R. Civ. P. 56.03. A defendant is entitled to summary judgment “when the record reflects a complete lack of proof of an essential element of the plaintiff’s claim.” *Dunham v. Roer*, 708 N.W.2d 552, 569 (Minn. App. 2006) (quoting *Lubbers v. Anderson*, 539 N.W.2d 398, 401 (Minn. 1995)).

Plaintiffs’ Fiduciary Duty Claim is Derivative in Nature and Fails as a Matter of Law

Though not directly argued by Defendants, whether some of Plaintiffs’ claims are direct or derivative is at issue. Plaintiffs’ Complaint asserts that their claims are direct claims, but acknowledge that they may actually be derivative and allege that they have satisfied the requirements of making a derivative claim. Defendants denied the allegation in their answers. Both parties’ arguments implicitly acknowledge the derivative nature of

at least some of Plaintiffs' claims. In fact, the Plaintiffs appear to have abandoned any pretense that their fiduciary duty claims are direct claims, stating that "[t]he fiduciary duty was owed by the defendant officers/board members to the JACC corporation." (Pls.' Mem, of Law Supp. Their Mot. For Partial Summ. J. 18 n.10.) Plaintiffs expressly seek attorney fees "for bringing this action on behalf of JACC." (*Id.* at 32.) The Court therefore considers whether Plaintiffs assert direct or derivative claims, and the legal significance of the distinction.

Plaintiffs claim that Defendants Browne, Hubbard, McCandless and Hodson breached their fiduciary duty "to the organization and its members." They specify that actions of these Defendants constituted breach by causing some of the Plaintiffs to be "unable to exercise their own duty to prevent director misconduct and/or violations of applicable and positive law." They further allege that JACC itself suffered from the breach. In paragraph 15 of their complaint, Plaintiffs argue that their claims are direct claims, but that "in the event any of these are deemed derivative claims," they argue that it would have been futile to make a demand on the JACC board at the time of filing the complaint because "the takeover team claiming management [was not] disinterested and/or independent."

Members may assert a cause of action belonging to a corporation if the corporation fails to pursue it. *Blohm v. Kelly*, 765 N.W.2d 147, 153 (Minn. App. 2009). If the alleged injury is a direct harm to the corporation and an indirect harm to a member, the claim is derivative in nature. *Id.* Plaintiffs have not provided evidence to establish that Browne, Hubbard, McCandless or Hodson owed a fiduciary duty besides that owed to JACC as directors. The harm alleged by plaintiffs is harm primarily to the corporation.

To the extent that a harm has been established by the evidence, it is primarily to JACC. Any claim arising from an alleged breach of fiduciary duty therefore belongs to JACC. The Court considers these claims to be derivative in nature.

In order to assert a derivative claim, a shareholder must allege either that a demand upon the corporation to pursue the claim has been refused, or that making such a demand would have been futile. *Stocke v. Berryman*, 632 N.W.2d 242, 247 (Minn. App. 2001); Minn. R. Civ. P. 23.09. A demand is generally required, though the requirement may be excused if “wrongdoers constitute a majority of the board.” *In re UnitedHealth Group Inc. Shareholder Derivative Litigation*, 754 N.W.2d 544, 550–51 (Minn. 2008) (citing *Winter v. Farmers Educ. & Coop. Union of Am.*, 259 Minn. 257, 266–67, 107 N.W.2d 226, 233 (1961)). In other words, the standard of futility is not governed by Plaintiffs’ pessimism about prevailing on the board to pursue their claims, but by the facts concerning the board’s ability to address the claims in an independent manner. *See Id.* If fatalism alone were sufficient to overcome the general demand requirement, the demand requirement would be effectively a nullity.

The decision by a corporation whether to pursue a derivative cause of action is subject to the business judgment rule. *Janssen v. Best & Flanagan*, 662 N.W.2d 876, 883 (Minn. 2003). Courts employ the business judgment rule to permit a corporation to weigh whether it is in the interests of the corporation to pursue a derivative claim. *Id. Even in cases where some or all of a board is compromised or interested in the outcome*, corporations are capable of investigating claims and making a business judgment about whether to pursue them by appointing a Special Litigation Committee comprised of disinterested board members or individuals. *In re UnitedHealth*, 754 N.W.2d at, 550–51.

Special Litigation Committees provide corporations an opportunity to avoid vexatious litigation. *Id.* at 550; *Janssen*, 662 N.W.2d at 883. Non-profit corporations possess the same power to create Special Litigation committees as for-profit corporations. *Janssen*, 662 N.W.2d at 888.

The Court concludes that the record lacks evidentiary support for Plaintiffs' allegation that failure to demand JACC pursue claims for breach of fiduciary duty was justified by futility. The record suggests that the decision not to make a demand was motivated primarily by expediency, and not by the facts concerning board members' independence. The Court notes that the Complaint identifies four board members as Defendants and five board members as Plaintiffs.² By Plaintiffs' own admission, Plaintiffs held more seats on the board than Defendants when this suit was commenced. Plaintiffs' focus on the lack of independence of the Defendant board *officers* is misplaced; what is significant whether the majority of the *board* is controlled by wrongdoers, which the plaintiffs neither allege nor establish—even after nine days of testimony and an opportunity to amend their complaint.

Plaintiffs' failure to make the generally required demand on JACC, or to provide sufficient evidence that the JACC board was incapable of independently addressing a demand (such as by appointing an independent Special Litigation Committee) defeats Plaintiffs' derivative fiduciary duty claims. Plaintiffs' election to make no demand deprived JACC of its opportunity to make a business decision about pursuing the claims, and unnecessarily places before the Court derivative claims that have not been vetted by the real party in interest. *See In re UnitedHealth*, 754 N.W.2d at 551 (discussing the

² One Plaintiff board member apparently resigned shortly after the January 14 board meeting.

purpose behind the business judgment rule); *Janssen*, 662 N.W.2d at 882–83 (same).

Summary judgment on the fiduciary duty claims is therefore appropriate on this basis.

The Court recognizes that the parties' summary judgment arguments focused not on the propriety of Plaintiffs' derivative claims, but on the fiduciary duty claims' merits. Plaintiffs identify no material fact dispute that prevents a judgment on this issue.³ The Court therefore also concludes that were it to reach the substance of the fiduciary duty claim it would accord Plaintiffs no remedy. The undisputed evidence establishes that both Plaintiffs and Defendants used determined effort to take the organization in the direction they viewed as in its best interest, while facing opposition that felt equally strongly about controlling JACC. The substantial and voluminous evidence in this case undoubtedly establishes a dispute over how JACC should be run and who should run it, but such evidence primarily concerns differences in business judgment and decisions made to get the organization back on track in a situation where it was already in continuing violation of its own bylaws.

All corporate directors have a duty to comply with corporate bylaws. *Brennan v. Minneapolis Soc. for the Blind, Inc.*, 282 N.W.2d 515, 523 (Minn. 1979). The record reflects that at least one Plaintiff had a hand in obstructing the work of the JACC board and in violating the JACC bylaws, precipitating many of the actions that Plaintiffs now complain of. The Court hesitates to apply the doctrine of unclean hands to the entire class of Plaintiffs when only some of them were demonstrably involved in culpable behavior. But the evidence does make it appear that Plaintiffs do not "fairly and adequately represent the interest of the shareholders or members similarly situated." *See* Minn. R.

³ The Court agrees with both Plaintiffs and Defendants that the material facts related to this issue are undisputed, and only the significance of the facts is subject to dispute.

Civ. P. 23.09. The derivative claims appear to be driven primarily by a minority of directors upset at having been ousted as officers in a battle for control over the organization.

Finally, during the pendency of this matter, JACC held a new round of regularly scheduled board and officer elections, which provided the membership an opportunity to weigh in on the dispute over control of the organization. A majority of the board seats were up for election. In the Court's view this governance dispute is better left to the processes provided by JACC's bylaws, which provided natural remedies to Plaintiffs.

To summarize: Plaintiffs' derivative claims are precluded because they did not make demand of JACC to pursue them and cannot establish that demand would have been futile. Plaintiffs derivative claims are barred because Plaintiffs appear not to represent the interests of the JACC membership, generally, but a subset of members sympathetic with a minority of directors. Were the court to decide the fiduciary duty claim on its merits, no remedy would be warranted by equity.

Intentional Interference with Contract

The second count in Plaintiffs' complaint, intentional interference with contract, appears to be a reformulation of the fiduciary duty claim. As the Court understands this claim, it characterizes the JACC bylaws as a contract, which the Defendants breached and thereby prevented Plaintiffs from acting in accordance with the bylaws. The court acknowledges that corporate bylaws are to be construed in the same manner as a contract. However, Plaintiffs also offer no argument or authority to support the theory that the JACC bylaws *are* a contract. This claim fails as a matter of law. To the extent this is a distinct and valid claim, it also fails for the reasons outlined in the above discussion

concerning derivative claims. Despite being framed as a direct claim, the Plaintiffs allege harm direct to JACC and indirect to Plaintiffs.

Judicial Intervention

Both parties move for summary judgment on Plaintiffs' claim for judicial intervention under section 317A.751 of Minnesota's Nonprofit Corporation Act. The section permits a court to grant whatever equitable relief is just and reasonable under the circumstances. Minn. Stat. § 317A.751, subd. 1. As discussed above, the regularly scheduled board and officer elections obviated any need for judicial intervention in the operation of the corporation. In light of all the facts, the Court concludes that no intervention is warranted.

Breach of Contract by Moore Against JACC

Finally, Plaintiff Jerry Moore claims that JACC breached its employment contract with him when it failed "to provide the facts supporting the allegation of misconduct" that led to his dismissal. This claim fails because JACC did not breach its contract with Moore.

The Court accepts as true that Moore had a written contract with JACC that provided for immediate cancellation for "misfeasance, malfeasance or moral turpitude" and that "[u]pon cancellation, JACC must disclose to Executive the act or omission upon which the cancellation of this Agreement is based." The contract had no specificity requirement for the disclosure.

JACC canceled Moore's contract on January 14, 2009 and disclosed the reason in a letter to Moore, stating: "your employment is hereby terminated because of your misconduct following the JACC election meeting on January 12, 2009." The misconduct

referred to in the letter was Moore's involvement a physical altercation involving a JACC member and a JACC director. The cancellation and the notification met the contract's requirements.

CONCLUSION

Defendants' Motion for Sanctions is **DENIED** for failing to comply with Rule 11. Plaintiffs' Claims against Defendants Browne, Hubbard, McCandless, Hodson and JACC (the first, second, fifth and sixth counts in the complaint, labeled I, II, V and II) fail as a matter of law and are **DISMISSED**.

C.A.P.