Lack of Marketability and Minority Discounts in Valuing Close Corporation Stock: Elusiveness and Judicial Synchrony in Pursuit of Equitable Consensus

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LACK OF MARKETABILITY AND MINORITY DISCOUNTS IN VALUING CLOSE CORPORATION STOCK: ELUSIVENESS AND JUDICIAL SYNCHRONY IN PURSUIT OF EQUITABLE CONSENSUS

STEPHEN J. LEACOCK*

ABSTRACT

This Article discusses the often subtle tasks faced by the courts in construing close corporations law, which is state law. The judiciary in individual states has skillfully managed the invention, continuing development and ongoing evolution of lack of marketability and minority discounts as it strives to honor its constitutional mandate to resolve controversies between minority and majority shareholders in close corporations relating to valuing close corporations' stock. These controversies arise in the context of share transactions in such corporations. Close corporations are traditionally not listed on stock exchanges, and the legislatures in some states have, in some instances, helped to facilitate the judiciary's ongoing inventive ingenuity in its continuing efforts to resolve these disputes in a context where there is usually no marketplace for the stockholders in close corporations to readily leave by selling their shares and moving on. This Article analyzes the approaches of the judiciary in individual states as the jurisdictions in the states

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collectively pursue—almost in synchrony—the elusive judicial goal of a fair and equitable resolution of close corporation valuation problems that arise in a plethora of factual share transaction settings, which demand individually tailored solutions.
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INTRODUCTION

No one aspires to be in a setting where she “can never leave.” Furthermore, whether she is leaving from, staying in, or initially becoming a stockholder in a close corporation, each shareholder probably imagines that a fair and equitable valuation of her shares is readily attainable. However, “[t]here is no single or universal method to determine [the] fair value” of shares

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1 See Maughan v. Correia, 148 Cal. Rptr. 3d. 593, 603 (Cal. Ct. App. 2012) (“[T]he trial court possibly was confusing a ‘minority discount’ with what is known as a ‘marketability discount.’”). The close corporation in the Maughan v. Correia controversy was “a family run corporation .... [Its] sole business is the operation of a hotel in San Diego.” Id. at 594.

2 See, e.g., EAGLES, Hotel California, on HOTEL CALIFORNIA (Asylum Records 1976), http://www.azlyrics.com/lyrics/eagles/hotelcalifornia.html [https://perma.cc/G999-EW5U]; Ritchie v. Rupe, 443 S.W.3d 856, 887 (Tex. 2014) (arguing that courts will certainly not permit a close corporation’s directors or controlling shareholders “to artificially deflate the shares’ value, perhaps to allow the company or its shareholders to purchase a minority shareholder’s shares for less than their true market value, or to hinder a minority shareholder’s sale of shares to third parties”) (citation omitted).

3 See, e.g., Ritchie, 443 S.W.3d at 880 (“[T]he [Texas] Business Organizations Code permits corporations to declare themselves to be ‘close corporations.’”) (emphasis added). See O’Neal & Thompson, 1 CLOSE CORPS. & LLC’S § 1:2 (rev. 3d ed. 2014); see also PRINCIPLES OF CORP. GOVERNANCE § 1.06 (1994) (“Closely held corporation means a corporation the equity securities ... of which are owned by a small number of persons, and for which securities no active trading market exists.”) (internal quotation marks omitted); Wasserman v. Rosengarden, 406 N.E.2d 131, 134 (Ill. App. Ct. 1980) (“A close corporation by definition is one in which the stock is held in a few hands, and the common stock is not frequently bought or sold.”) (citation omitted). But see Tex. Ear Nose & Throat Consultants, PLLC v. Jones, 470 S.W.3d 67, 86 (Tex. App. 2015); Sneed v. Webre, 465 S.W.3d 169, 177 (Tex. 2015) (closely held corporation separately defined). Nevertheless, in this Article, the terms “closely held corporations” and “close corporations” are treated as synonyms.


5 Lawson, 734 A.2d at 744.

6 See id. at 744 (“[F]air value’ is a flexible standard dependent on the circumstances and context of a transaction.”) (citation omitted). See generally
in a close corporation. Additionally, in some instances, fair market value may be the appropriate valuation method to use. Unfortunately, the absence of a valuation consensus can be troublesome when a shareholder wishes to escape the fiscal confinement imposed by close corporations.

Moreover, exit from a close corporation may be made more irksome if, prior to a minority stockholder’s departure, a court decreases the value of her stock after listening to the advice of valuation experts, after applying a lack of control or lack of marketability discount, or both. However, irksomeness is not


8 Maughan v. Correia, 148 Cal. Rptr. 3d. 593, 603 (Cal. App. 2012) (“[W]hat is at issue is the fair market value of a minority interest in an S corporation.”).

9 See, e.g., McMinn v. MBF Operating Acquisition Corp., 164 P.3d 41, 42 (N.M. 2007) (“[T]he state’s legislature has conferred on] shareholders who dissent from mergers the right to obtain payment for the fair value of their shares.”) (citation omitted). See also, e.g., Shriner v. Sheehan, 773 N.E.2d 833, 850 (Ind. Ct. App. 2002) (“We remand with instructions for the trial court to determine the value of the [minority stockholder]’s shares of stock based on the [stock]’s fair market value.”).


11 Also referred to as “minority” discounts. See Maughan, 148 Cal. Rptr. 3d. at 603; see also In re Estate of Hjersted, 175 P.3d 810, 817 (Kan. 2008) (“[A] minority discount allows an appraiser to adjust for a ‘lack of control’ over the entity on the theory that the minority interests are not worth the same as the majority interests due to the lack of voting power.”).

12 See Maughan, 148 Cal. Rptr. 3d. at 603 (“[A lack of marketability discount] adjusts for a lack of liquidity in [a shareholder’s] interest in an entity, on the theory that there is a limited supply of potential buyers in a closely-held
necessarily synonymous with legally actionable conduct.\(^\text{13}\) For example, in appropriate cases, a lack of marketability\(^\text{14}\) discount may be legally justified in order to achieve a fair valuation of a minority block of stock.\(^\text{15}\) Such a discount “adjusts for a lack of liquidity in [a shareholder’s] interest in an entity, on the theory that there is a limited supply of potential buyers in a closely-held corporation.”\(^\text{16}\)

In other instances, a lack of control discount\(^\text{17}\)—also referred to as a minority discount\(^\text{18}\)—may be applied by the courts as a more valid tool to attain fairness and equity.\(^\text{19}\) A lack of control discount “adjust[s] for lack of control over the business entity on the theory that non-controlling shares of stock are not worth their proportionate share of the firm’s value because they lack voting power to control corporate actions.”\(^\text{20}\) Unquestionably, a lack of marketability discount\(^\text{21}\) differs substantively\(^\text{22}\) from a lack of control discount.\(^\text{23}\) These legal realities create a potentially thorny situation\(^\text{24}\) when courts are called upon to determine whether or
not it is equitable to apply either or both of these discounts in valuing a minority shareholder’s stock in any specific close corporation valuation controversy.

“[O]f course, not all conflicts are the same.” Differences may arise as a result of the purpose of the close corporation valuation which can be, inter alia, for tax assessment, the exercise of a legally valid stock option, or dissolution of the pertinent close corporation. In other instances, internal close corporation conflicts may motivate majority shareholders to forcibly redeem minority shareholders’ stock by use of a buyout or force-out mechanism. Too often, in the heat of valuation battles, disagreements

the trial court, but nevertheless affirming the trial court’s exercise of its discretion in reaching its overall decision).

25 Jantzen v. Gordon, No. 82 C 7992, 1985 WL 2358, at *1 (N.D. Ill. Aug. 21, 1985) (“[T]here is no doubt that stock is a security in the generally accepted sense of the word.”).

26 See generally Horn v. McQueen, 353 F. Supp. 2d 785 (W.D. Ky. 2004).

27 See id. at 808 (“[T]here are three generally accepted methods or approaches [for valuing stock in close corporations]: the income approach, the market approach, and the asset approach.”) (citations omitted); see also Leacock, Valuing Stock, supra note 10, at 185; Lavene v. Lavene, 392 A.2d 621, 626 (N.J. Super. Court, Ch. Div. 1978) (“Three principal methods ... can be used for developing a value for ownership in a closely held corporation.”).


29 See, e.g., Estate of Adell v. Comm’r, T.C.M. (CCH) 2014-155, at *11 (T.C. 2014) (“The Court is asked to determine the fair market value of [the deceased’s] 100% interest in [the close corporation’s stock] on his date of death and whether the estate is liable for the ... estate tax valuation understatement penalty with respect to the [close corporation’s] stock.”) (emphasis added); see also Lavene, 392 A.2d at 624 (discussing estate and gift tax assessment); Estate of Snyder v. United States, 285 F.2d 857, 861 (4th Cir. 1961) (discussing gift tax assessment); Brooks v. Willcuts, 78 F.2d 270, 273 (8th Cir. 1935) (“[T]he Treasury Department ... was seeking a way to fix the value of stocks which were not listed on the stock exchanges.”) (emphasis added).


32 See McMinn v. MBF Operation Acquisition Corp., 164 P.3d 41, 49 (N.M. 2007) (“Today ... financial and legal practices have shifted and mergers are often used solely to eliminate minority shareholders.”) (emphasis added). See also Estes v. Idea Eng’g & Fabricating, Inc., 649 N.W.2d 84 (Mich. Ct. App. 2002).

erupt\textsuperscript{34} and lawsuits follow.\textsuperscript{35} Unavoidably, therefore, judicial selection of the most equitable\textsuperscript{36} valuation method\textsuperscript{37} to apply to the specific valuation controversy can be elusive.\textsuperscript{38}

Certainly, valuation controversies tend to arise where shareholders become adversarial because of conscious or subconscious convictions that unfairness is afoot.\textsuperscript{39} Furthermore, the court will permit a minority stockholder to present a claim that majority stockholders’ use of a corporate “freeze-out” mechanism, depriving her of an equitable and accurate determination of the inherent value of her stock in the close corporation, is unconscionable.\textsuperscript{40} Moreover, state law\textsuperscript{41} determines the valuation method to be applied in close corporation controversies, and state corporate laws may differ with respect to the relevant factors that should be taken into account in conducting the pertinent valuation.\textsuperscript{42} This makes effective judicial resolution of these differences crucial to

\textsuperscript{34} See Maughan, 148 Cal. Rptr. 3d. at 594.

\textsuperscript{35} See id.


\textsuperscript{37} Id.

\textsuperscript{38} See Shriner, 773 N.E.2d at 848 (“[W]e conclude that the trial court \textit{did not abuse its discretion} in crafting this remedy.”) (emphasis added).


\textsuperscript{40} See McMinn v. MBF Operation Acquisition Corp., 164 P.3d 41, 54 (N.M. 2007).

\textsuperscript{41} See Voeller v. Neilston Warehouse Co., 311 U.S. 531, 535 (1941) (“[T]he conditions under which corporations shall organize and operate are matters within the \textit{exclusive province of the state}, so long as those conditions do not clash with the national Constitution.”) (emphasis added).

\textsuperscript{42} See, e.g., Shriner, 773 N.E.2d at 847–48 (Ind. Ct. App. 2002) (“The unclean hands doctrine is an equitable tenet, which demands one who seeks equitable relief to be free of wrongdoing in the matter before the court .... [However, t]he doctrine of unclean hands is not favored by the courts and must be applied with reluctance and scrutiny.”) (citations omitted).
the task of reassuring litigants that the pursuit of fairness will never be compromised.  

Part I of this Article identifies the contextual setting in which close corporation stock valuation controversies arise. Part II concentrates on courts’ determinations of fair market value and assessments of the applicability of lack of marketability and minority discounts in specified settings. Part III focuses on the judiciary’s analysis of the applicability of minority and lack of marketability discounts. Part IV elaborates upon how, in fundamental change settings, corporate law has departed from requiring shareholder unanimity to full-blown majority power. It also identifies and follows the emergence of statutory appraisal rights designed to prevent victimization of minority stockholders by majority shareholders in close corporation control struggles. Part V analyzes the distinguishing characteristics between fair value and fair market value, and Part VI completes the picture by exploring court applications of fair market value conceptions to estate duty controversies.

I. THE CONTEXTUAL SETTING

Close corporations exist at common law and may also be created by statutory mandate in jurisdictions that so provide. Such corporations are routinely managed by a cohesive group of shareholders who abhor “having the harmony and balance of their business organization disturbed or ... shattered by the unwelcome intrusion of strangers.” In this regard, the courts can certainly

43 Id. at 848 (“For the unclean hands doctrine to apply, the party who is charged with having unclean hands must be guilty of intentional misconduct .... The alleged wrongdoing must also have an immediate and necessary relation to the matter being litigated.”) (citations omitted).
44 See Ritchie v. Rupe, 443 S.W.3d 856, 880 (Tex. 2014).
45 See, e.g., U.S. Bank N.A. v. Cold Spring Granite Co. 802 N.W.2d 363, 381 (Minn. Sup. Ct. 2011) (“At least two other jurisdictions—Illinois and Nevada—have concluded that the enactment of statutory closely held corporation statutes does not abrogate the common-law definition of a closely held corporation.”).
46 See Ritchie, 443 S.W.3d at 880.
47 See O’Neal & Thompson, supra note 3, § 1:12; see also Stephen J. Leacock, Share Transfer Restrictions in Close Corporations as Mechanisms for Intelligible Corporate Outcomes, 3 Faulkner L. Rev. 109, 110 n.2 (2011) [hereinafter Leacock, Share Transfer Restrictions] (“Share transfer restrictions
be perceived as strangers.\textsuperscript{48} Actually, close corporations ordinarily have a small number of stockholders who often participate in, or conduct the management of, the corporation.\textsuperscript{49} Additionally, individual states may empower close corporations to dispense with certain safeguards applicable to corporations generally.\textsuperscript{50} Indeed, in specific circumstances,\textsuperscript{51} a close corporation may dispense altogether with having a board of directors.\textsuperscript{52}

Inevitably, shareholders who own only nonvoting shares in a close corporation have no legally tenable ability to control decisions made by the corporation.\textsuperscript{53} This is the case because legally valid corporate decisions\textsuperscript{54} require a majority vote in favor of the decision\textsuperscript{55} by the members of the board of directors attending a valid board meeting at which a quorum is present.\textsuperscript{56} Additionally, in the orthodox context, where the close corporation has a board in [close corporation] bylaws are very effective in terminating conflicts between [shareholders in such corporations].”\textsuperscript{57}

\textsuperscript{48} See Schreier & Joy, supra note 10, at 857. See also Leacock, Valuing Stock, supra note 10, at 163.

\textsuperscript{49} See, e.g., Maughan v. Correia, 210 Cal. Rptr. 3d 507, 603 (Cal. Ct. App. 2012). See O’Neal & Thompson, supra note 3, at § 1:34 (“State corporations statutes centralize corporate powers in directors, but state law typically provides contractual freedom that participants in closely held firms can use to change these rules.”) (emphasis added); see also William S. Monnin-Browder, Note, Are Discounts Appropriate?: Valuing Shares in Close Corporations for the Purpose of Remedi ing Breach of Fiduciary Duty under Massachusetts Law, 40 Suffolk U.L. Rev. 723, 725 (2007) (“Close corporations ... represent the vast majority of corporate entities in the United States.”) (citation omitted).

\textsuperscript{50} See, e.g., TEX. BUS. ORGS. CODE ANN. § 21.552(2) (West 2011) (permitting shareholders in close corporations to bring derivative actions without first making a demand upon the board of directors to take appropriate action). See also Ritchie, 443 S.W.3d at 881.

\textsuperscript{51} See, e.g., Zion v. Kurtz, 405 N.E.2d 681, 684 (N.Y. 1980) (“[A shareholders’ agreement between 100% of the shareholders of a close corporation can take] all management functions away from the [corporation’s board of] directors.”) (citations omitted).

\textsuperscript{52} Id.

\textsuperscript{53} See, e.g., Advanced Commc’n Design, Inc. v. Follett, 615 N.W.2d 285, 294 (Minn. 2000) (“[W]here a shareholder has only nonvoting shares in a closely held corporation ... any significant ability to control corporate decision-making is lacking.”).

\textsuperscript{54} See, e.g., MODEL BUS. CORP. ACT § 8.01(a)–(c) (2010).

\textsuperscript{55} See, e.g., id. § 8.24(c).

\textsuperscript{56} See, e.g., id. § 8.24(a)–(d).
of directors, the board is ordinarily elected by a plurality of the votes of shares validly cast at a shareholders’ general meeting where a quorum is present. This paradigm structure empowers majority shareholders to elect the majority of the board of directors and enables the board to exercise management power without the directors fearing a sword of Damocles hanging over their heads. Such a figurative sword can consist of minority shareholder veto power.

Actually, veto powers are not illegal for minority stockholders to have and to exercise in the internal affairs of a close corporation. However, the existence and possession of a veto power would require an express provision in the close corporation’s articles of incorporation. Alternatively, a veto power will also be recognized by the courts as being legally valid and binding if a legally valid shareholders’ agreement has expressly created such a power. Moreover, courts have the judicial power to order that the articles of incorporation, or equivalent incorporation, be amended to add or include an omitted veto power where the omission of such a power is legally untenable. The courts can also rule that the party who breached the pertinent shareholder agreement—by which a legally valid veto power was created—is “estopped to rely upon the absence of those amendments from the corporate charter” to take any inappropriate corporate action.

57 See, e.g., id. §§ 7.28(a); 7.25(a)–(b).
58 See, e.g., Woodman v. Kera, LLC, 760 N.W.2d 641, 662 n.5 (Mich. Ct. App. 2008) (“The ‘Sword of Damocles’ was a sword suspended over the head of Damocles in a Greek myth.”) (citation omitted), aff’d and remanded, 785 N.W.2d 1 (Mich. 2010).
59 See, e.g., Whetstone v. Hossfeld Mfg. Co., 457 N.W.2d 380, 382 (Minn. 1990) (“[T]he trend has long been to uphold [minority shareholders’ veto powers in close corporations’ articles of incorporation].”). But see U.S. Bank N.A. v. Cold Spring Granite Co., 802 N.W.2d 363, 375–76 n.6 (Minn. 2011).
61 See, e.g., Whetstone, 457 N.W.2d at 381–82. But see U.S. Bank N.A., 802 N.W.2d at 383.
62 See, e.g., Zion, 405 N.E.2d at 684–85.
63 Id. at 685 (“[T]he certificate of incorporation may be ordered reformed, by requiring [the party who has breached the 100% shareholder agreement] to file the appropriate amendments.”).
64 Id.
65 Id. (citations omitted).
66 Id.
Actually, in close corporations, express provisions agreed to by all the shareholders for the purpose of resolving value-determination controversies work as effectively as valid share transfer restrictions to accomplish clearly conceived goals. Contract law principles provide the basis for resolution of disputes that arise in such contexts. So, when a minority shareholder relinquishes her shares, whether voluntarily or involuntarily, the neutral and impartial judicial review of such express provisions ensures that the contractual fair value of the relinquished shares is properly determined.

Also, on the one hand, the judiciary’s equitable scrutiny is unquestionably crucial in determining minority stockholders’ rights in appraisal valuation disputes when minority shareholders are leaving a close corporation. When minority stockholders are forcibly ejected from close corporations by majority shareholders or by the corporation itself, judicial scrutiny properly recognizes the rights of minority shareholders to a fair and just determination of the value of shares that they relinquish. In this respect, the judiciary’s vigilance levels the playing field and obviates the need for additional state or other institutional supervisory monitoring of the final valuation of close corporation shares. This judicial watchfulness acknowledges that, because there is no active market for purchases and sales of shares in a closely held corporation, in a sense, minority stockholders in close corporations are uniquely vulnerable.

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67 See, e.g., Kortum v. Johnson, 755 N.W.2d 432, 447 (N.D. 2008) (“Contracts are construed to give effect to the parties’ mutual intention at the time of contracting.”) (citations omitted).
68 See generally Leacock, Share Transfer Restrictions, supra note 47, at 112–13.
69 See Kortum, 755 N.W.2d at 447.
70 See, e.g., U.S. Bank N.A. v. Cold Spring Granite Co. 802 N.W.2d 363, 382–83 (Minn. 2011) (“[P]rovided the value is fair and equitable to all parties.”) (emphasis added) (citations omitted).
71 Id. at 381–82.
72 Id. at 382–83.
73 No amendments to the Securities Exchange Act of 1934 (at 15 U.S.C.A. § 78j (2015)) to extend the provisions therein to close corporations are recommended by the Author.
74 See O’NEAL & THOMPSON, supra note 3, at § 7:28 (“The lack of a market for ownership interests in a closely held business deprives participants of an objective source to measure value.”) (emphasis added).
75 Ritchie v. Rupe, 443 S.W.3d 856, 879 (Tex. 2014) (“[M]inority shareholders in closely held corporations have ‘no statutory right to exit the venture
On the other hand, when a party is about to become a minority shareholder in a close corporation, the same vulnerabilities will apply to that party even after she has actually become that minority stockholder. Upon entry into the close corporation as a minority stockholder, one becomes subject to that same “difficulty in—and sometimes even the impossibility of—selling one’s shares [which] is a characteristic intrinsic to ownership of a closely held corporation, the shares of which are not publicly traded.”

Unquestionably, therefore, those vulnerabilities should play a critical role when valuing a minority block of stock at the entry point.

The existence of these vulnerabilities supports the view that, prior to such a purchase, it is both fair and just to discount the value of the minority stockholding that the party is about to purchase. The legal justification for an appropriate discount is rational in order to account for the objectively recognizable vulnerabilities that an acquirer of a minority block of shares would find to be substantively unattractive. Irrefutably, the lack of a ready market for the sale and purchase of stock in close corporations significantly prevents a minority shareholder from being able to sell his shares and withdraw from the company at will.

Therefore, when determining the purchase price of a minority block of stock that a purchaser is about to buy, these imminent

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and receive a return of capital’ like partners in a partnership do, and ‘usually have no ability to sell their shares’ like shareholders in a publicly held corporation do.”) (citation omitted).

76 Id. at 878–79.
77 Id. at 871.
79 Id. at 604.

[W]e acknow[le]dge the fact that the controlling group in a close corporation must have some room to maneuver in establishing the business policy of the corporation. It must have a large measure of discretion, for example, in declaring or withholding dividends, deciding whether to merge or consolidate, establishing the salaries of corporate officers, dismissing directors with or without cause, and hiring and firing corporate employees.

See Monnin-Browder, supra note 49, at 724.
81 See O’Neal & Thompson, supra note 3.
disadvantages legally justify the existence and application of lack of control and lack of marketability discounts in calculating the value of the pertinent minority block of stock about to be bought and sold.

In support of fairness, it is acknowledged that in appraisal circumstances where minority shareholders are forced to accept cash for their shares, such minority stockholders strive to maximize the value of their forcibly divested stock. However, the other shareholders in close corporations are also trying to ensure the continuing integrity of the value of the shares that they own in that particular close corporation. In the context of close corporation controversies, both groups of shareholders are legally entitled to attain their respective goals of fairness in the valuation processes.

II. Fair Market Value Determination and the Application of Lack of Control and Lack of Marketability Discounts

In Maughan v. Correia, the validity of an alleged stock option agreement to acquire a minority block of stock in a close corporation came before the California Court of Appeal for resolution. The trial court had determined that application of a minority discount was required in order to properly ascertain the fair market value of the stock to which the asserted stock option agreement applied.

“Fair market value is the price at which property would change hands between a willing buyer and a willing seller,

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82 See, e.g., Maughan, 148 Cal. Rptr. 3d. at 602.
83 Id. at 602–03.
84 Id.
85 See, e.g., U.S. Bank N.A. v. Cold Spring Granite Co., 802 N.W.2d 363, 383 (Minn. 2011) (“[P]rovided the value is fair and equitable to all parties.”) (emphasis added) (citations omitted).
86 See Swope v. Siegel Robert, Inc., 243 F.3d 486, 492 (8th Cir. 2001) (“[T]he fair value of a dissenter's minority share should remain equal to the value of the majority shares.”) (citations omitted).
87 Id.
88 148 Cal. Rptr. 3d. at 602.
89 Id. at 603 (“[W]hat is at issue is the fair market value of a minority interest in an S [close] corporation.”)
90 Id. at 602.
neither under any compulsion to buy or sell and both having knowledge of relevant facts.\footnote{See, e.g., Estate of Adell v. Comm’r, 108 T.C.M. (CCH) 107, at *12 (2014) (emphasis added) (citation omitted).}

With respect to lack of control and lack of marketability discounts, these two discounts differ each from the other.\footnote{See Advanced Commc’n Design, Inc. v. Follett, 615 N.W.2d 285, 291 (Minn. 2000) (“A marketability discount ‘adjusts for a lack of liquidity in one’s interest in an entity’ and should be distinguished from a minority discount, which adjusts for lack of control of the corporation.”) (citation omitted).} A lack of control discount is a synonym for a minority discount.\footnote{Id.} In contrast, a lack of marketability discount is a synonym for a lack of liquidity discount.\footnote{See In re Estate of Hjersted, 175 P.3d 810, 817 (Kan. 2008) (“A marketability discount allows an appraiser to adjust for a ‘lack of liquidity’ in the interest itself on the theory that there is a limited supply of purchasers of that interest.”).} A lack of marketability discount compensates the acquiring party for the absence of future liquidity relating to the reduced power of the acquiring party to readily dispose of stock by sale at a future time.\footnote{Wasserman v. Rosengarden, 406 N.E.2d 131, 134 (Ill. App. Ct. 1980).} The absence of opportunities to readily dispose of shares in close corporations exists because close corporations are not usually listed on stock exchanges,\footnote{See, e.g., Sneed v. Webre, 465 S.W.3d 169, 177 (Tex. 2015).} and in fact, a state’s statute may expressly mandate non-listing of closely held corporations as statutorily defined.\footnote{See, e.g., Leacock, Share Transfer Restrictions, supra note 47, at 126; see also Leacock, Valuing Stock, supra note 10, at 170.} Of course, share transfer restrictions in a close corporation’s articles provide a rather small internal marketability opportunity “by providing an identifiable market for its shares.”\footnote{See, e.g., Ritchie v. Rupe, 443 S.W.3d 856, 867 (Tex. 2014).} However, this is a limited opportunity and is definitely not enough to justify assertions of the existence of a ready market for a close corporation’s shares.\footnote{See, e.g., Maughan v. Correia, 148 Cal. Rptr. 3d 593, 603 (Cal. Ct. App. 2012).}

Despite the differences between lack of control discounts and lack of marketability discounts, they are nevertheless confused with one another.\footnote{See, e.g., Maughan v. Correia, 148 Cal. Rptr. 3d 593, 603 (Cal. Ct. App. 2012).} This should not happen because in close
corporations, identifiable rights stem from the possession and exercise of the power to control. In such corporations, minority shareholders lack voting power and control. This is the justification for minority discounts. In recognition of these realities, “closely held corporate stock cannot be valued reasonably by the application of any inflexible formula.”

In each close corporation valuation controversy, the failure of the parties to make specific arguments plays an important role. It is up to the disputing parties to differentiate one discount from the other; otherwise, the court may combine lack of both marketability and minority discounts together and characterize the combined discount as a minority discount. The courts will then permit presentations by the adversarial parties’ valuation experts to identify and confirm the appropriate diminution in ostensible value justified by applying a lack of control discount in the exercise of the court’s discretion.

Actually, the California Court of Appeal concluded that once the trial court has exercised its discretion to determine whether

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101 See Warren v. Campbell Farming Corp., 271 P.3d 36, 45 (Mont. 2011) (“[T]he controlling group in a close corporation have certain rights to what has been termed ‘selfish ownership’ in the corporation.”) (emphasis added).

102 See Charles E. Hodges II & Karen S. Kurtz, Using Closed-End Funds to Calculate the Lack-of-Control Discount for Closely Held Businesses, 115 J. TAX’N 262, 267 (2011) (“Lack of control is generally defined as the inability to direct or influence the management of the business, to compel liquidation of the business, and to realize a pro rata share of the business’s net asset value.”).

103 See In re Estate of Hjersted, 175 P.3d 810, 812 (Kan. 2008) (“A minority discount allows an appraiser to adjust for a ‘lack of control’ over an entity on the theory that the minority interests are not worth the same as the majority interests due to the lack of voting power.”).


105 See, e.g., Maughan v. Correia, 148 Cal. Rptr. 3d 593, 602 (Cal. Ct. App. 2012) (“[H]ere, the parties do not dispute that a minority discount should be applied, and ... the underlying facts regarding damages are not otherwise in dispute.”).

106 Id.


108 See, e.g., Maughan, 148 Cal. Rptr. 3d at 605 (“[T]he court’s choice to apply a minority discount at all may involve an exercise of its discretion.”) (citation omitted).
or not to apply a discount to reflect a minority stockholder’s status, the trial court’s discretion comes to an end. The California Court of Appeal “[did] not view how the trial court applied the discount to be a discretionary function. The discount, if it is applied, must be applied in a manner consistent with the law.” So, once the trial court has exercised its discretion, if the trial court’s conclusion is that the application of a discount is appropriate, then the proper application of the pertinent discount is a question of law.

The California Court of Appeal reasoned that the value of the entire corporation must first be determined before the appropriate minority discount should be applied. It also meant that, in the controversy in issue, “the discount [was] ... to be applied only to the value of [the minority stockholder]’s proportional share of [the close corporation].” The trial court’s deduction of the contract price of the share option contract “from the value of [the minority stockholder]’s undiscounted minority interest, and then applying] the minority discount” was an error of law under California close corporation law. For example, because determination of the fair market value of all the shares in the close corporation was at issue, experts may have used closed-end fund data as a “benchmark” principle to compute the corporation’s overall value and resolve the pertinent dispute. However, once this overall value is determined, it is then apportioned to the relevant shares in order to arrive at the pro rata value of each share. After the pro rata value is determined, the lack of control discount would then be applied where legally justified, as it was in the context of the Maughan v. Correia controversy.

Inevitably, the facts and circumstances of each fair market value determination will be different. For example, in Maughan

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109 Id.
110 Id.
111 See, e.g., id.
112 Id. at 603.
113 Id. (emphasis added).
114 Id. at 604 (emphasis added).
115 Id.
117 Maughan, 148 Cal. Rptr. 3d at 603–04.
118 Id.
119 See Hodges & Kurtz, supra note 102, at 263. (“[T]he valuation of an interest in an entity starts with valuing 100% of the entity and then applying
The dispute consisted of an action brought by one family member against another to enforce an alleged stock option agreement to purchase a minority block of shares in a close corporation run by the family. The California Court of Appeal affirmed the application of a minority discount by the court below, but it modified the amount awarded to the victorious plaintiff by the trial court in order to harmonize the amount awarded with applicable state corporate law. The court held that the appellant majority shareholder was correct in his argument that it was legally appropriate to apply a minority discount in calculating the value of the minority block of shares in the controversy. The court concluded that the appellant’s argument was legally valid because a minority discount must be deducted “from the pro rata share of the value of the entire business, to reflect the absence of the power of control.”

The California Court of Appeal therefore applied the minority discount as an integral part of determining the value of the minority interest that the stockholder would have acquired, had the majority stockholder fully complied with the contested option agreement. As the court explained, a two-stage evaluation was required. First, “the value of the entire corporation is determined, and then apportioned among the various interests.” The value computed on completion of this first-stage determination represented the “pro rata ... fair market value of [all] the shares” in the corporation as a whole. The second stage required deduction of the minority discount, determined by the

discounts ... to the particular interest. There is no one correct method for valuing every business interest, and “[a]ll of the facts and circumstances of each individual case must be analyzed by the appraiser ....”) (citation omitted).

120 148 Cal. Rptr. 3d at 593.
121 Id.
122 Id.
123 Id. at 602–03.
124 Id. at 603.
125 Id. (quoting Leacock, Valuing Stock, supra note 10, at 198–99 n.174) (emphasis in original).
126 Id. at 605–06.
127 Id. at 603.
128 Id.
129 Id. (citation omitted).
130 Id. at 603–04.
court, from the first-stage pro rata value of the minority shareholder’s stock.\textsuperscript{131}

The value remaining after this deduction represented the court-determined appraisal of the minority stockholder’s shares in the close corporation.\textsuperscript{132} The court therefore ordered a downward revision of the damages awarded to the complaining party for breach of the option contract by which she would have become a minority shareholder.\textsuperscript{133} This was correct because the value of the shares, had she become a shareholder after buying them, would have been the pro rata value of those shares as appropriately discounted to reflect her minority shareholding status.\textsuperscript{134}

Application of a minority discount was therefore justified in \textit{Maughan v. Correia} because the California Court of Appeal strove to ascertain the fair market value for a minority block of shares in a close corporation in the context of an \textit{incoming} minority shareholder.\textsuperscript{135} The dispute in the case related to valuation of the minority block of shares on \textit{entry}, rather than on departure from the close corporation.\textsuperscript{136} Arguably, the controversy in \textit{Maughan v. Correia} was antithetical to an appraisal proceeding.\textsuperscript{137} An appraisal valuation applies in the circumstances of a minority stockholder’s \textit{exit} from the close corporation in which the minority shareholder previously owned the stock.\textsuperscript{138}

\section*{III. Judicial Analysis of the Applicability of Lack of Control Discounts and Lack of Marketability Discounts}

In close corporation disputes, courts will not permit a majority stockholder’s or a corporation’s devaluation of a minority stockholder’s shares by using lack of control discounts and lack of marketability discounts and then proceeding to acquire the minority shareholder’s stock at that devalued price.\textsuperscript{139} Court condonation

\begin{footnotes}
\item[131] Id. at 604.
\item[132] Id. at 603–04.
\item[133] Id. at 605–06.
\item[134] Id.
\item[135] Id. at 604.
\item[136] Id. at 603.
\item[137] See id.; see also Leacock, Valuing Stock, supra note 10, at 185–86.
\item[138] See, e.g., Leacock, Valuing Stock, supra note 10, at 185–86.
\end{footnotes}
of such conduct would be inequitable and would, therefore, be unconscionable.\textsuperscript{140} Whenever the judiciary reaches the conclusion that use of such discounts would be unfair and inequitable, the court will nullify their application without hesitation.\textsuperscript{141}

The Rhode Island Supreme Court’s decision in \textit{Charland v. Country View Golf Club, Inc.} epitomizes the invocation of the judiciary’s discretionary equitable jurisdiction in such a context.\textsuperscript{142} In \textit{Charland}, a minority shareholder in a close corporation petitioned the court for dissolution of the corporation because of the minority shareholder’s apprehension that unlawfulness was underway in the corporation.\textsuperscript{143} In order to save its own life, the corporation petitioned the court to permit it to exercise an express statutory right to purchase the petitioning stockholder’s shares instead of dissolving the corporation, as the petitioner sought to do.\textsuperscript{144} The achievement of success on its petition would enable the corporation to survive rather than be subjected to a court-ordered death sentence.\textsuperscript{145} After all, the decision as to whether or not a corporation should fight to continue its life falls within “what a board [of directors] is supposed to do—make business judgments in the best interests of the company and its stockholders.”\textsuperscript{146}

When the minority shareholder and the corporation failed to agree on a fair value determination, the Superior Court, Providence County, Rhode Island, acting as the trial court, invoked its statutory authority and appointed an appraiser to “recommend a decision on the question of fair value.”\textsuperscript{147} Unfortunately, the trial court was not entirely satisfied with the first court-appointed appraiser’s conclusions and appointed a second appraiser to determine

\textsuperscript{140} Id.
\textsuperscript{141} Id.
\textsuperscript{142} See id.
\textsuperscript{143} Id. at 609 (“Specifically [the minority shareholder] alleged that one of the officers of the corporation was engaging in illegal activities.”).
\textsuperscript{144} Id. at 610 (“First, a corporation, rather than be forced to dissolve by a shareholder dissolution petition, can elect to buy out the shareholder’s stock. Second, the corporation must pay fair value for such shares. Third, if the fair value cannot be agreed upon, the court shall determine the value of such shares as of the close of business on the day on which the petition for dissolution was filed.”).
\textsuperscript{145} Id.
\textsuperscript{146} See Strine, \textit{supra} note 28, at 681.
\textsuperscript{147} See \textit{Charland}, 588 A.2d at 610.
the fair value of the minority stockholder’s shares by a court-specified date.148

The close corporation’s major asset consisted of a golf course and therefore created “inherent difficulties”149 for the second appraiser’s efforts to determine the fair value of the minority shareholder’s stock.150 Nevertheless, on principle, the second appraiser “concluded that a ‘minority discount’ would be appropriate in determining the fair value of [the minority stockholder]’s shares.”151 The second appraiser therefore completed and submitted to the trial court two separate and distinct “fair value” valuations of the minority stockholder’s shares in the close corporation.152 The trial court could then choose either of the two valuations submitted by the second appraiser.153

In his two valuations, the second appraiser used a minority discount as part of his first valuation, but omitted such a discount from his second valuation.154 The second valuation therefore attributed a higher value to the minority stockholder’s shares in the close corporation than the first valuation specified.155 However, the second appraiser suggested to the court that, in any event, it was appropriate in this controversy to use some version of discounting as a suitable equalizer in valuing the golf course property.156 He explained that although his second valuation figure was higher than his first, the retention of a form of discounting in the final figures of his second valuation was nevertheless appropriate because comparative golf course properties were unavailable for use in his valuation procedures.157 This unavailability of relevant golf course properties necessitated the use of residential property values as a substitute for these court-ordered valuation procedures.158 He therefore retained a version of discounting in his second valuation figures in order to reflect

148 Id. at 610 n.3.
149 Id. at 610.
150 Id.
151 Id. (citation omitted).
152 Id.
153 Id.
154 Id.
155 Id.
156 Id. at 610–11.
157 Id.
158 Id.
this reduction differential in the increase of the value of the golf course property when compared to increases in residential property values.\footnote{159}

In its decision, the trial court disagreed with the use of a minority discount as the second appraiser had done in his first valuation.\footnote{160} The trial court reasoned that exclusion of a minority discount was fair and equitable in the valuation controversy because no open market ramifications were relevant to the valuation at issue.\footnote{161} The court ruled that fair market value was not legally relevant to the pertinent valuation at all.\footnote{162} Instead, the court concluded that determination of fair value was mandated by the relevant state statute.\footnote{163} As a result, the trial court declined to use the first valuation in its decision.\footnote{164} Rather, it decided that the second appraiser’s second valuation,\footnote{165} in which he excluded any orthodox minority discount, was legally correct.\footnote{166} This second higher valuation was therefore adopted by the trial court as its valuation decision.\footnote{167}

Although this second higher valuation did, in fact, exclude the use of an orthodox minority discount, it nevertheless retained a form of discounting of the value of the minority shareholder’s stock.\footnote{168} This form purported to discount the value of the minority stockholder’s shares in the golf course based upon a supposed differential in the rate of increase in the value of the golf course’s property when compared with neighboring residential properties.\footnote{169} This perceived lower rate of increase in the value of the golf course’s property, when compared to residential property values, motivated the second appraiser’s reduction in value of the minority stockholder’s shares.\footnote{170} The second appraiser concluded

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\begin{itemize}
  \item \footnote{Id. at 611.}
  \item \footnote{Id. at 610.}
  \item \footnote{Id. at 611–12.}
  \item \footnote{See, e.g., Zelouf Int’l Corp. v. Zelouf, 999 N.Y.S.2d 731, 736 (N.Y. Sup. Ct. 2014) (citing Charland, 588 A.2d at 609, with approval).}
  \item \footnote{Charland, 588 A.2d at 612.}
  \item \footnote{Id. at 612–13.}
  \item \footnote{I.e., the higher of the second appraiser’s two valuations. \textit{See supra} text accompanying note 155.}
  \item \footnote{Charland, 588 A.2d at 610.}
  \item \footnote{Id.}
  \item \footnote{Id. at 610–11.}
  \item \footnote{Id.}
  \item \footnote{Id.}
\end{itemize}
that this discounted value of the minority shareholder’s stock was in accordance with the applicable statutory mandate.\textsuperscript{171} The minority shareholder appealed the trial court’s valuation ruling.\textsuperscript{172}

Justice Kelleher of the Rhode Island Supreme Court held that neither minority status nor lack of marketability factors should have been considered in determining the fair value of the minority shareholder’s stock.\textsuperscript{173} The Rhode Island Supreme Court therefore remanded the case to the Superior Court for the fair value of the minority shareholder’s shares to be determined anew “in conformity with the rules set forth”\textsuperscript{174} in the Rhode Island Supreme Court’s opinion.\textsuperscript{175} These rules may be articulated as follows.\textsuperscript{176}

The Rhode Island Supreme Court enunciated that “a lack of marketability discount is inapposite when a corporation elects to buy out a shareholder who has filed for dissolution of [the] corporation” in which she owns her shares.\textsuperscript{177} The court reasoned that this conclusion is correct because, had the shareholder’s corporate dissolution petition been granted, \textit{all} of the shares would have shared \textit{equally} in the value remaining after all valid higher priority obligations were satisfied.\textsuperscript{178} After all, “[e]very corporation has a fiduciary duty to its shareholders.”\textsuperscript{179} Moreover, the goal of the exercise of the court’s discretion to grant the corporation’s petition for a buyout of the minority shareholder’s stock, in these circumstances, would be to save the corporation’s life rather than to punish the minority stockholder.\textsuperscript{180} The Rhode Island Supreme Court concluded that correctly interpreting the applicable statutory provisions precluded diminution of the value of the minority shareholder’s stock by the application of any discounting.\textsuperscript{181}

\textsuperscript{171} \textit{Id.} at 613.
\textsuperscript{172} \textit{Id.} at 611.
\textsuperscript{173} \textit{Id.} at 612–13.
\textsuperscript{174} \textit{Id.} at 613.
\textsuperscript{175} \textit{Id.}
\textsuperscript{176} \textit{Id.}
\textsuperscript{177} \textit{Id.}
\textsuperscript{178} \textit{Id.} (“[T]he discounting of [the minority shareholder]’s shares ... resulted in the [minority shareholder] receiving less than fair value.”).
\textsuperscript{179} \textit{See} McMinn v. MBF Operation Acquisition Corp., 164 P.3d 41, 56 (N.M. 2007) (emphasis in original).
\textsuperscript{180} \textit{Charland,} 588 A.2d at 613.
\textsuperscript{181} \textit{Id.}
Such a diminution in the value of the minority shareholder’s stock would permit the corporation to first devalue the minority stockholder’s shares, and second, to forcibly acquire such shares at the devalued price in violation of any conceivably fair conception of equitable standards. The goal of the statutory mandate granting the concession of buying out the shares of a stockholder who has petitioned for a close corporation’s dissolution was to permit the close corporation to remain in existence and continue its life as a going concern. It was not, by any stretch of the imagination, a statutory device created by the legislature to punish minority shareholders who petition for dissolution of close corporations in which such stockholders own shares.

The Rhode Island Supreme Court therefore remanded the case to the lower court with instructions to eliminate the discounting that the second appraiser had retained as an adjustment reflecting the differential in the rate of increase in value of the golf course property when compared to increases in neighboring residential properties. The Rhode Island Supreme Court reasoned that the retention of either a lack of marketability or a minority discount in the value of the minority stockholder’s shares in the circumstances of the case was inconsistent with the state’s statutory fair value mandate.

IV. HISTORICAL EVOLUTION OF LAW APPLICABLE TO DISSenting SHAREHOLDERS’ RIGHTS AND THE APPLICABILITY OF LACK OF CONTROL AND LACK OF MARKETABILITY DISCOUNTS

Historically, at common law, unanimous shareholder consent was required for a corporation to make fundamental

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182 Id.
183 Id. at 609–10 (citing R.I. GEN. LAWS ANN. § 7-1.1-90 (West 1985) (repealed 2005)).
184 Id. at 613.
185 Id. (“[T]he trial court ... did apply a discount that resulted in less than fair value being awarded to [the dissenting minority shareholder].”) (emphasis added).
186 Id. (“[N]o minority discount or lack of marketability discount should be applied in [the appraisal valuation] proceedings .... [T]he discounting of [the minority stockholder]'s shares by using residential real estate values resulted in [the minority stockholder] receiving less than fair value.”).
187 Id.
188 See Voeller v. Neilston Warehouse Co., 311 U.S. 531, 535 n.6 (1941) (“At common law, unanimous shareholder consent was a prerequisite to fundamental
This requirement of unanimity allocated to minority shareholders an identifiable “nuisance value,” consisting of the substantive equivalent of a veto power over major changes proposed by majority stockholders. In response to this undermining of the fundamental concepts of democracy in the corporate context, a number of legislatures in common law jurisdictions responded with statutory enactments.

Such legislatures statutorily restored democratic norms by expressly empowering corporations to make fundamental changes when authorized to do so by a valid majority vote of the board of directors. These legislatures reached a “decision to change the requirements for shareholder approval of major corporate transactions by allowing majority rather than unanimous shareholder approval.” Inevitably, the effect of the enactment of such legislation was the elimination, for all practical purposes, of significant minority shareholder influence over the scope and direction of the corporation’s activities. Unfortunately, over time, this led to victimization of the minority by the majority.

Furthermore, “[d]issenters’ rights were not recognized at common law.” Therefore, in response to this victimization of minority shareholders by majority stockholders, a number of states enacted statutory provisions entitling dissenting minority stockholders to be bought out by the majority shareholders upon payment of the appraised value of the minority shareholders’ changes in the corporation. This made it possible for an arbitrary minority to establish a nuisance value for its shares by refusal to cooperate.” (emphasis added).

Id. See also Blitch v. Peoples Bank, 540 S.E.2d 667, 669 (Ga. Ct. App. 2000).

Voeller, 311 U.S. at 535 n.6.

Id. See also Brown v. Arp & Hammond Hardware Co., 141 P.3d 673, 680 (Wyo. 2006).

See Voeller, 311 U.S. at 535 n.6.

Id. See also Blitch, 540 S.E.2d at 669.


See Voeller, 311 U.S. at 535 n.6; see also Brown, 141 P.3d at 680; Blitch, 540 S.E.2d at 669.

Voeller, 311 U.S. at 535 n.6.

Brown, 141 P.3d at 680.

See, e.g., Fisher v. Tails, 767 S.E.2d 710, 712 (Va. 2015) (“Appraisal rights give ‘corporate shareholders who oppose [certain] extraordinary corporate action[s]’ the right ‘to have their shares judicially appraised and to demand
“[L]egislature[s] created [these] appraisal rights to protect minority shareholders from being [unfairly] deprived of their ownership interests by majority shareholders.”

So, with minority shareholder protection as their essential goal, legislatures created a shift in the correlation of power between majority and minority stockholders in close corporations.

This shift in the correlation of power enacted by state legislatures meant that these legislatures had now granted minority shareholders the applicable statutory appraisal rights as a “substitute for the control power or value the minority [stockholders] relinquished.” Essentially, it consisted of the surrender by minority stockholders of their “veto” power over the making of any fundamental changes in the operations of close corporations in exchange for the statutory appraisal rights conferred by state legislatures. It therefore meant that unanimous stockholder consent, prior to fundamental changes in the operations of close corporations, no longer existed in corporate law. It had now been statutorily replaced by majority shareholder decision-making prior to such fundamental changes.

Thankfully, the judiciary is ready, willing, and able to protect minority stockholders’ interests in close corporation controversies in these contexts. The judiciary is vigilant and equipped to adapt and apply new equitable concepts to detect the fundamental changes that can trigger the application of statutory appraisal rights. For example, where equitably justified, the “step transaction doctrine” can be applied by the judiciary to

that the corporation buy back their shares at the appraised value.”

199 See Swope, 243 F.3d at 491 (describing “fair value’ appraisal statute[s]”) (citations omitted). See generally Wertheimer, supra note 6.

200 Swope, 243 F.3d at 491 (citations omitted).

201 Id. at 491–92.

202 Id. at 491 (citations omitted).

203 Id. at 491–92.

204 Id. at 491.

205 Id.


207 See, e.g., id. at 713 (“The step transaction doctrine ‘treats the “steps” in a series of formally separate but related transactions involving the transfer of property as a single transaction, if all the steps are substantially linked.’”) (citations omitted).

208 Id. (internal quotation marks omitted).
protect minority shareholders from nullification maneuvers conceived by majority stockholders in an attempt to circumvent the trigger and activation of appraisal rights. Unquestionably, appraisal rights statutes were not intended by legislatures to bestow upon majority stockholders a statutory license to plunder the value of minority shareholders' stock.

Actually, the appraisal rights statutes do not expressly prohibit the use of lack of control or lack of marketability discounts when valuing the shares of minority stockholders in the appraisal context. Nor do these statutes expressly mandate the application of such discounts. Of course, it is irrefutable that under corporate law, the burden to successfully prove that such discounts apply in a specific dissenting shareholder's stock valuation falls on the party asserting that such discounts must be applied by the courts. In any event, in the majority of states that have enacted dissenting shareholders' rights legislation, the judiciary has ruled that the use of such discounts in valuing the dissenting shareholders' stock is inappropriate.

Courts reason that applying such discounts might tend to inject a measure of speculation into the appraisal process. Moreover, such discounts might unfairly subvert the right of minority shareholders to be paid the fair and equitable value of the stock

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209 See, e.g., id. at 712–14.
210 Id. at 712.
212 See, e.g., Cavalier Oil Corp. v. Harnett, 564 A.2d 1137, 1144 (Del. 1989). But see Swope v. Siegel-Robert, 74 F. Supp. 2d 876, 920 (E.D. Mo. 1999) (“Where there is no objective market data available, the appraisal process is not intended to reconstruct a pro forma sale but to assume that the shareholder was willing to maintain his investment position ... had the [fundamental change] not occurred.”), aff'd in part, rev'd in part, Swope v. Siegel-Robert, Inc., 243 F.3d 486, 496–97 (8th Cir. 2001).
213 Brown, 141 P.3d at 677; see also Swope, 243 F.3d at 491.
to which they are fully entitled.\textsuperscript{216} Furthermore, the discounts might be applied in a way that could encourage the majority to squeeze out minority shareholders in a punitive manner.\textsuperscript{217} The application of such discounts could potentially penalize minority shareholders by facilitating exploitation by majority stockholders using the very statutes enacted by legislatures specifically for the protection of minority stockholders.\textsuperscript{218}

The controversy in \textit{Swope v. Siegel-Robert}\textsuperscript{219} is helpful in demonstrating the judiciary at its finest.\textsuperscript{220} The valuation controversy in \textit{Swope} related to the buyout by majority stockholders of shares owned by minority shareholders after the minority shareholders dissented from a merger of another corporation with the close corporation in which the minority shareholders owned stock.\textsuperscript{221} The Eighth Circuit therefore needed to determine whether a lack of marketability, a lack of control discount, or both applied to the pertinent valuation of the minority stockholders’ shares.\textsuperscript{222} The court concluded that the use of either or both of these discounts would be legally inappropriate.\textsuperscript{223} The court therefore disallowed both discounts, affirming in part, reversing in part, and remanding the case to the court below for implementation of the Eighth Circuit’s rulings.\textsuperscript{224}

First, with regard to the application of a lack of marketability discount, the court affirmed the lower court’s disallowance of a discount.\textsuperscript{225} The appellate court reasoned as follows: in cases where a minority shareholder was unwilling to support a merger, and the majority shareholders forcibly purchased the minority stockholder’s shares under the statutory scheme, it would be inappropriate to apply a lack of marketability discount.\textsuperscript{226} This conclusion was fair and equitable because the statutory scheme

\textsuperscript{216} \textit{Id.}
\textsuperscript{218} \textit{Id.}
\textsuperscript{219} 243 F.3d 486 (8th Cir. 2001).
\textsuperscript{220} \textit{Id.}
\textsuperscript{221} \textit{Id.} at 486.
\textsuperscript{222} \textit{Id.} at 491.
\textsuperscript{223} \textit{Id.}
\textsuperscript{224} \textit{Id.} at 499.
\textsuperscript{225} \textit{Id.} at 494.
\textsuperscript{226} \textit{Id.} at 493.
was created for the protection of minority shareholders, not to penalize them for the lack of opportunities to sell their shares.\textsuperscript{227}

Then, turning to the use of a minority discount, the court shifted focus to issues of control over corporate decision-making and away from opportunities to sell the pertinent shares.\textsuperscript{228} This shift was correct because minority discounts do not implicate marketability factors at all.\textsuperscript{229} This shift away from liquidity issues was necessary because focusing on the fairness of applying minority discounts made the power to control corporate decisions the most relevant factor for the court to analyze.\textsuperscript{230} Control over corporate decision-making is the quintessence to be construed by courts in determining whether or not minority discounts are relevant to value determinations in appraisal contexts.\textsuperscript{231}

The Eighth Circuit therefore reasoned that control over corporate decision-making was legally irrelevant to the application or non-application of lack of control or minority discounts.\textsuperscript{232} In the appraisal valuation context, “the application of a minority discount is not appropriate in an appraisal action, where the minority sellers are \textit{unwilling} to dispose of their stock.”\textsuperscript{233} This unwillingness of the minority stockholders to sell their shares was the preeminent factor in the judiciary’s determination, rather than the legally irrelevant question of how much power minority stockholders exercised over corporate decision-making.\textsuperscript{234} The court therefore ruled that “the district court erred by discounting the value of the Company’s stock to account for [the minority shareholders’] minority status.”\textsuperscript{235}

As a result of this conclusion, the Eight Circuit reversed the court below on this issue and disallowed the application of a minority discount.\textsuperscript{236} This conclusion was convincingly rational because in such contexts, the issue of control is legally irrelevant.

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\textsuperscript{227} \textit{Id.} at 493–94.
\textsuperscript{228} \textit{Id.} at 495.
\textsuperscript{229} \textit{Id.} at 491.
\textsuperscript{230} \textit{Id.} at 495.
\textsuperscript{231} \textit{Id.} at 491–92.
\textsuperscript{232} \textit{Id.} at 495.
\textsuperscript{233} \textit{Id.} (emphasis added).
\textsuperscript{234} \textit{Id.}
\textsuperscript{235} \textit{Id.}
\textsuperscript{236} \textit{Id.} at 497.
\end{flushleft}
to the determination of the value of minority shareholders’ stock.\footnote{237} It is unquestionably correct to so decide because the percentage of the close corporation’s shares owned by minority stockholders is not in question at all.\footnote{238} Rather, in contexts such as these, minority shareholders are entitled to the full value of their shares, without reference to the percentage of the total shares of the corporation their stock represents.\footnote{239} This makes sense because the essential determination is to be made on the same substantive basis as if the minority stockholders were \textit{retaining} the pertinent shares, rather than relinquishing them.\footnote{240}

However, this articulation may not always be as straightforward as it appears on the surface. On further examination, the decision in \textit{Atlantic States Construction v. Beavers} may have a potentially viable point.\footnote{241} In the case, “[t]he appeal ... was filed in the [Georgia] Supreme Court but transferred to [the appeals] court.”\footnote{242} The case arose out of a dispute from the sole minority shareholder dissenting in response to a merger between two construction companies on one side, with Atlantic States on the other.\footnote{243} In actuality, the minority shareholder owned a 10 percent interest in each of the two construction companies purporting to merge with Atlantic States.\footnote{244} The Court of Appeals of Georgia explained that “[t]he general purpose behind the statutory scheme for appraisal of dissenting shareholders’ stock is to provide an orderly and fair method to evaluate the ownership interests of shareholders who are forced from the corporation by their dissent from certain corporate action.”\footnote{245} The legislature had clearly articulated a statutory goal requiring the judiciary to draw an appropriate distinction between the corporate state of affairs \textit{before} the decision to merge when compared to the situation of the corporation \textit{after} the decision to merge.\footnote{246}

\footnote{237} \textit{Id.} at 495.  
\footnote{238} \textit{Id.}  
\footnote{239} \textit{Id.} (“[M]inority shareholders are entitled to receive the full value of their shares as if they were able to retain the stock.”) (quoting Hansen v. 75 Ranch Co., 957 P.2d 32, 41 (Mont. 1998)).  
\footnote{240} \textit{Id.}  
\footnote{242} \textit{Id.} at 247.  
\footnote{243} \textit{Id.}  
\footnote{244} \textit{Id.}  
\footnote{245} \textit{Id.} at 249 (citations omitted).  
\footnote{246} \textit{Id.}
The statutory objective was to compensate dissenting shareholders for the value of their shares as such value stood on the day immediately preceding the corporate decision to merge.\textsuperscript{247} However, “[n]o mandatory formula or methodology is [statutorily] enumerated.”\textsuperscript{248} Of course, the statutory selection of the day prior to the corporate decision to merge would tend to eliminate contamination or diminution of the value of the minority stockholders’ shares by any factors pertinent to the actual corporate decision to merge itself.\textsuperscript{249} This is arguably fair and equitable because the dissenting shareholders should be entitled to exit the corporation with the pre-merger value of their shares intact. Substantively, this means that the valuation of a dissenting shareholder’s interest should be such that it “reflects the shareholder’s actual interest in the company prior to the corporate change.”\textsuperscript{250}

Therefore, in \textit{Atlantic States},\textsuperscript{251} the Georgia Court of Appeals did not rule that minority and lack of marketability discounts are inherently legally untenable and thus to be per se disregarded as components of valuing close corporation shares generally in such appraisal disputes.\textsuperscript{252} On the contrary, the Georgia Court of Appeals enunciated that “the trial court must consider any factor bearing on the stock’s intrinsic worth.”\textsuperscript{253} Of course, in all fairness, the court emphasized that “the trier of fact must apply any ‘minority interest’ factor with caution.”\textsuperscript{254}

The court acknowledged that the application of minority discounts was not expressly precluded by statutory mandate, but reemphasized the uniqueness of the facts of each stockholder dispute relating to the valuation of close corporation shares in

\begin{itemize}
\item \textsuperscript{247} \textit{Id.} (“[D]issenting shareholders are to be compensated for ‘the fair value [of their shares] as of the close of business on the day prior to the shareholders' authorization date [the date of the shareholders' vote authorizing the proposed corporate action ...], excluding any appreciation or depreciation directly or indirectly induced by such corporate action or its proposal.’”) (citations omitted).
\item \textsuperscript{248} \textit{Id.}
\item \textsuperscript{249} \textit{GA. CODE ANN. § 14-2-1301} (1981).
\item \textsuperscript{250} \textit{See, e.g., Swope v. Siegel-Robert, Inc., 243 F.3d 486, 492} (8th Cir. 2001).
\item \textsuperscript{251} \textit{Atl. States Constr.}, 314 S.E.2d at 245.
\item \textsuperscript{252} \textit{Id.} at 251 (“We do not agree with the trial court’s conclusion that consideration of the minority nature of the dissenting shareholder's interest is against public policy.’”).
\item \textsuperscript{253} \textit{Id.}
\item \textsuperscript{254} \textit{Id.}
\end{itemize}
appraisal controversies. The court explained that “[i]f in a given case the minority nature of the interest diminishes the worth of the stock itself, there is nothing we can find in the statutory appraisal scheme that would prevent the trial court from considering the ‘minority interest’ factor and devaluing the stock accordingly.”

The Georgia Court of Appeals therefore reversed and remanded the case because of the specific facts at issue. It did so because arguments for or against the application of a minority discount needed further exploration on remand. Based upon the factual record developed by the trial court in its proceedings, the argument by the purchasing corporation that the refusal to apply a minority discount would allocate to the minority shareholder “more than the ‘value’ of the stock in hand” was rejected by the court. The court ruled that such arguments were not validly supported by the evidence presented in the case in light of the factual record. Lack of evidentiary support in the record of the court below rendered the lower court’s decision clearly erroneous, and reversal was ordered.

Additionally, in Atlantic States, the Georgia Court of Appeals rejected the minority stockholder’s assertion that the deduction of a minority discount would in effect grant the majority shareholders a “control premium.” The court was not persuaded by the minority stockholder’s argument that court authorization of the deduction of a minority discount would cause the minority stockholder to leave the corporation with less than his fair share of the close corporation’s value. As a result, the Georgia Court of Appeals reversed the trial court’s overall decision, remanded the case, and ordered a redetermination of the

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255 Id.
256 Id.
257 Id. at 253.
258 Id.
259 Id. at 251 (citation omitted).
260 Id.
261 Id. at 252 (“[T]he methodology employed by the trial court is wholly unreliable.”).
262 Id.
263 Id. at 245.
264 Id. at 251.
265 Id.
fair value of the minority stockholder’s shares. The court explained that the procedures of the statutory mandate obligated the corporation to first make an offer to the dissenting shareholder. If, at that time, the minority shareholder rejected the corporation’s initial offer, the corporation would be required to initiate the appraisal evaluation.

The court observed that it did not detect anything in the statutory appraisal scheme that precluded, per se, the use of a minority discount in conducting the statutorily required determination of the value of the minority stockholders’ shares. This point of view would clearly make a minority discount potentially applicable when the court below made its redetermination of the value of the minority stockholders’ shares on remand. Of course, the Georgia Court of Appeals’s point of view would equally make a minority discount potentially inapplicable if the trial court so decided after its evaluation based upon a full and complete factual record.

Notwithstanding the Georgia Court of Appeals’s decision in Atlantic States, arguably, when deciding dissenting shareholder buyout controversies, the majority of courts decline to apply minority discounts or lack of marketability discounts when valuing minority stockholders’ shares in appraisal settings. This emanates from a judicial perception that when a corporation elects to buy out the shares of the dissenters, lack of control and lack of marketability discounts are not perceived as being legally relevant to the determination of the value of such shares at all.

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266 Id. at 253.
267 Id. at 249.
268 Id.
269 Id.
270 Id. at 245.
271 See Swope v. Siegel-Robert, Inc., 243 F.3d 486, 495 (8th Cir. 2001) (“Most courts addressing the issue have refused to apply minority discounts.”).
272 Id. at 494 (“[M]ost courts have refused to apply a marketability discount in fair value cases.”).
273 Id.
Substantively, this is because in the setting of an appraisal prior to a forced sale of minority shareholders’ stock to majority stockholders, the shares are not being acquired by third-party outsiders in relation to the corporation, but rather by those inside the corporation. Each discount in the value of the minority shareholders’ forcibly divested stock which the court permits would have a concomitant unfair and inequitable enhancement of the value of the purchased stock in the hands of the purchasing insider shareholders. As ownership of the stock was transferred from the minority shareholder to the purchasing majority stockholder, the unfair and inequitable enhancement of the value of the purchased stock would be simultaneously transferred along with the personal property title and ownership. The forced divestiture of the minority shareholders’ stock, which the court authorized subsequent to the appraisal of the value of such shares, is not made on the same substantively equitable footing as a sale of such stock to third parties external to the corporation.

Actually, in the more recent case of Blitch v. Peoples Bank, the Georgia Court of Appeals expressed a position relating to appraisal controversies that is in harmony with the position that a majority of states support. In Blitch, the Georgia Court of Appeals observed that the revision of the Georgia Business Corporation Code embraced and followed the value judgments that the Model Business Corporations Act adopted. The Court went on to opine that this revision by the Georgia Legislature reinforced the viewpoint that in appraisal valuations, it is legally inappropriate to deduct discounts from the value of minority stockholders’ shares because of their minority status. This is

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275 Robblee, 841 P.2d at 1294 (“with a dissenting shareholder ... the sale of stock is [essentially] to the corporation”).
276 Id.
277 See, e.g., id. at 1295 (“Courts in other states have noted the unfairness of discounting minority shares where the sale is to other shareholders.”) (citation omitted). But see 395 Lampe, 2014 WL 221814 (holding that a legal right to sell the minority interest at issue on the open market existed).
278 Robblee, 841 P.2d at 1294.
280 Id. at 670.
281 Id. at 669.
283 MODEL BUS. CORP. ACT, § 13.02 (2005).
284 Blitch, 540 S.E.2d at 669.
so because, as the official comment to the Model Business Corporations Act explains, 285 “most transactions that trigger appraisal rights affect the corporation as a whole and because such discounts give the majority the opportunity to take advantage of minority shareholders who have been forced against their will to accept the appraisal-triggering transaction.” 286

This point of view is also supported by an analysis of the facts, reasoning, and resolution by the Washington Court of Appeals in Roblee v. Roblee. 287 In Roblee, two brothers owned interests in their family’s companies, with one brother owning a 51 percent controlling shareholding, and the other a minority shareholding. 288 Disputes developed between the two of them, which were followed by the majority shareholding brother terminating the employment of the minority shareholding brother in corporate activities. 289 This termination of employment led to further disputes between the two of them, followed by an agreement by both to submit their disputes to mediation. 290 The culmination of this mediation was a letter of intent relating to the division of corporate assets and the overall resolution of the pertinent disputes. 291

Thereupon, the close corporation, its associated businesses, and the majority shareholding brother filed suit seeking division of the assets in accordance with the letter of intent. 292 The trial court applied a minority discount in valuing the minority stockholder’s shares, and the minority shareholder appealed the trial court’s decision. 293

285 See id. at 670.
288 Roblee, 841 P.2d at 1290, distinguished by 395 Lampe, LLC, 2014 WL 221814 (discussing the legal right to sell the minority interest at issue on the open market existed).
289 Id.
290 Id.
291 Id.
292 Id. at 1291.
293 Id.
The Washington Court of Appeals acknowledged that by buying his brother’s minority shares, the majority stockholding brother would certainly “be ridding himself of a minority shareholder who had become, and would continue to be, extremely difficult.” The court also concluded that the valuation controversy was therefore substantively akin to a buyout by the majority stockholding brother of his brother’s minority shares. Additionally, the Washington Court of Appeals also agreed with the trial court’s reasoning that the controversy relating to the valuation of the minority shareholder’s stock should be resolved analogously to that of a dissenting shareholder buyout by the corporation holding such shares. The Court ultimately concluded that no viable legal justification in corporate law existed to support the application of a minority discount in valuing the minority stockholder’s shares. The Washington Court of Appeals therefore reversed the trial court’s application of a minority discount in valuing the shares of the minority stockholder and remanded the case to the trial court with directions to eliminate the minority discount that the trial court had applied as part of its valuation procedures.

Further support for these conclusions emanates from the Delaware Supreme Court’s interpretation of Delaware’s appraisal statute in the seminal case of Cavalier Oil Corp. In Cavalier Oil Corp., the Delaware Supreme Court very carefully evaluated the determination of the “fair value” of a dissenter’s shares by the courts below. In doing so, the Delaware Supreme Court rejected the corporation’s assertion that the dissenting shareholder’s sale of his stock to the corporation was subject to a minority discount in order to properly reflect the value of his

294 Id. at 1295.
295 Id.
296 Id. at 1294 (“Here the sale was to the functional equivalent of the corporation, that is, to Dave, the majority shareholder who controlled the corporation. No third party was involved.”) (emphasis added).
297 Id. (“The [trial] court’s analogy in its ... opinion to a dissenting shareholder finds support in the facts.”).
298 Id. at 1295.
299 Id.
300 Cavalier Oil Corp. v. Harnett, 564 A.2d 1137, 1139 (Del. 1989).
301 Id. at 1138–39.
minority stockholding status.\textsuperscript{302} The Delaware Supreme Court explained that, by any stretch of the imagination, the appraisal process is not at all predicated upon a sale between a willing seller and a willing buyer.\textsuperscript{303}

On the contrary, the predicate was that of a shareholder who was unwilling to sell his shares and, had the merger not occurred, actually preferred to retain his stock and maintain his investment position in the corporation.\textsuperscript{304} The application of a minority discount would therefore deprive the selling minority shareholder of a component of the full proportionate value of his shares in the corporation.\textsuperscript{305} The unavoidable legal effect of subjecting the minority shareholder’s stock to such a discount would be the imposition of a penalty for lack of control which would unfairly enrich the majority shareholders at the minority stockholder’s expense.\textsuperscript{306} Such a concomitant conferral of a windfall upon majority stockholders in such contexts would inescapably amount to legislative facilitation of exploitation of the statutory appraisal process.\textsuperscript{307} This “clearly undesirable result”\textsuperscript{308} was definitely not perceived by the Delaware Supreme Court as the legislature’s statutory intention.\textsuperscript{309}

Additionally, the Wyoming Supreme Court expressed a similar view in Brown v. Arp & Hammond Hardware Co.\textsuperscript{310} In Brown, the Wyoming Supreme Court concluded that it is inappropriate to apply discounts in the context of sales by minority stockholders to the majority shareholders or to the corporation in which the shares are held.\textsuperscript{311} The Wyoming Supreme Court explained the fundamental difference between the sale of shares by a minority stockholder to a third party outside the corporation and the sale of stock by a minority stockholder to a majority shareholder or to the corporation as follows.\textsuperscript{312}

\textsuperscript{302} Id. at 1145.
\textsuperscript{303} Id.
\textsuperscript{304} Id.
\textsuperscript{305} Id.
\textsuperscript{306} Id.
\textsuperscript{307} Id.
\textsuperscript{308} Id.
\textsuperscript{309} Id.
\textsuperscript{310} 141 P.3d 673 (Wyo. 2006) (citing Hansen v. 75 Ranch Co., 957 P.2d 32, 41 (Mont. 1998)).
\textsuperscript{311} Id. at 687.
\textsuperscript{312} Id.
Whereas the sale of shares by a minority stockholder to a third party outside the corporation transfers no control rights, the sale of stock by a minority stockholder to a majority shareholder in the same corporation “simply consolidates or increases the interests of those already in control.” The transfer to insiders adds additional power to the already entrenched power possessed by reason of the majority stockholding. The application of a minority discount in such a setting “would result in a windfall to the transferee.”

Thus, the conferral of such a financial windfall upon the majority stockholder would mean that concomitant financial injury to the minority stockholder would simultaneously accompany the additional control power transferred to such majority stockholders. The financial windfall derived from applying such a discount would result in adding the diminution in value of the minority shareholder’s stock to the enhancement in control power that the controlling shareholder would acquire over the corporation. This would be patently inequitable and unfair to minority stockholders.

Arguably, the earlier decision by the United States District Court for the Northern District of Mississippi in *Hernando Bank v. Huff* does not undermine these analyses. In *Huff*, the dissenting shareholders vigorously argued that the involuntary nature of a buyout controversy should be the paramount factor in the District Court’s decision-making. This argument sought to convince the District Court that applying a minority discount would punish the minority shareholders for lacking the prerequisite control that a more extensive shareholder would have had over

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313 *Id.* (“When selling to a third party, the value of the shares is either the same as or less than it was in the hand of the transferor because the third party gains no right to control or manage the corporation.”).

314 *Id.* (emphasis added).

315 *Id.*

316 *Id.*

317 *Id.*

318 *Id.*

319 *Id.*


321 *Id.*
the corporation’s operations. The District Court nevertheless concluded that “in the present case a minority discount is proper in determining the fair value of the stock of the dissenters.”

The District Court derived guidance from the earlier Mississippi Supreme Court decision in Cal-Maine Foods, Inc. v. Duvic, and concluded that such a “determination under Mississippi law is a purely factual issue to be resolved by the trier of fact.” The dissenting minority shareholders’ emphatic insistence that the involuntary nature of the transfer of ownership of their stock to the majority stockholders in a court-ordered buyout subsequent to appraisal procedures was preeminent was to no avail. The District Court simply disagreed with the minority stockholders’ argument that their “shares should be valued as a pro rata share of the corporation, and that a ‘minority discount’ due to the lack of corporate control in such shares is improper.”

Rather, the District Court concluded that these arguments reached the level of merely “superficial appeal.” The District Court reasoned that such arguments were predicated on a disregard for the fundamental difference between majority and minority control capability within the corporation and “the [C]ourt [therefore remained] unconvinced that a minority share of stock should be valued as though it were a controlling share of a corporation.” The District Court was certainly aware of the fact that the shares of the minority stockholders were being involuntarily bought out by the majority shareholders in the context of a statutory dissenting minority shareholders’ proceeding. This therefore makes the District Court’s refusal to ascribe transcendent legal force to the involuntary nature of a court-ordered transfer of the property rights of minority stockholders in this context intellectually unconvincing. In effect, the District Court did not provide a viable explanation for its decision beyond the

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322 Id.
323 Id.
324 264 So. 2d 383, 384 (Miss. 1972).
325 Hernando Bank, 609 F. Supp. at 1126.
326 Id.
327 Id.
328 Id.
329 Id.
330 Id.
principle of the degree of deference accorded by appeals courts to trial courts’ determinations of questions of fact.331

V. JUDICIAL DISTINCTIONS BETWEEN FAIR MARKET VALUE AND FAIR VALUE

In close corporation valuation disputes, the judiciary may use “fair market value”332 or “fair value.”333 When a statute expressly or implicitly mandates the use of fair value, even if the judiciary is not an agency of the legislature,334 as a coequal branch of government,335 the judiciary will treat the legislative mandate as the supreme law of the land in the particular state.336 Courts use the legally appropriate valuation method to determine the fair and equitable amount to be paid to exiting minority stockholders as the legally valid price for shares sold to majority stockholders or to the corporation.337

However, whereas “[f]air market value is the price at which property would change hands between a willing buyer and a willing seller, neither under any compulsion to buy or sell and both having knowledge of relevant facts[,]”338 “fair value” is an

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331 Id. On appeal, the Fifth Circuit affirmed the District Court’s decision without reference to the minority discount issue. See Hernando Bank v. Huff, 795 F.2d 803 (5th Cir. 1986).
333 See, e.g., McMinn v. MBF Operating Acquisition Corp., 164 P.3d 41, 42 (N.M. 2007) (“[T]he state’s legislature has conferred on] shareholders who dissent from mergers the right to obtain payment for the fair value of their shares.”) (citation omitted).
334 See Times Pub. Co. v. Ake, 645 So. 2d 1003, 1004 (Fla. Dist. Ct. App. 1994) (“[T]he judiciary, as a coequal branch of government, is not an ‘agency’ subject to the supervision or control by another coequal branch of government.”) (emphasis added) (citations omitted).
335 Id.
336 McMinn, 164 P.3d at 42.
amorphous term. Nevertheless, in determining fair value in the context of appraisal rights disputes, “most ... jurisdictions regard minority and liquidity discounts as prohibited as a matter of law.” In such disputes, “[t]here is no simple mathematical formula and each case presents its particular problem.” Moreover, “fair value” is not a synonym for “fair market value.”

Fair market value envisages a valuation emerging almost invisibly from a robustly free market of buyers and sellers freely competing with each other. Determining fair value in close corporation valuation controversies is not such a setting. As a result, the determination of fair value has taxed the courts’ ingenuity to identify and articulate it in each sui generis setting.

Of course, a state statute may expressly enact how fair value is to be determined. In such an instance, the statutory mandate of the state’s legislature is the supreme law of the land in that particular state, and the judiciary must respect and enforce it. The Minnesota statutory mandate is a case in point, where the pertinent corporate statute has empowered a close corporation’s board of directors to make the value determination when cashing out minority shares as statutorily specified. The Minnesota statute states that the board of directors’ determination

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342 Id. at 492 (“[F]air value’ in minority stock appraisal cases is not equivalent to ‘fair market value.”).
343 Id.
344 See Estate of Adell v. Comm’r, T.C.M. (CCH) 2014-155, at *12 (T.C. 2014) (“Fair market value is the price at which property would change hands between a willing buyer and a willing seller, neither under any compulsion to buy or sell and both having knowledge of relevant facts.”) (citation omitted). See also Leacock, Valuing Stock, supra note 10, at 165–66 n.16.
345 Leacock, Valuing Stock, supra note 10, at 166 n.17.
346 Id. at 167.
348 Id.
349 Id.
350 See MINN. STAT. ANN. § 302A.423 (West 2011).
is conclusive absent a finding of fraud.\textsuperscript{351} Thus, in the absence of a Minnesota court’s finding of fraud, any deviation by a Minnesota court from the state’s statutory mandate that the board of directors’ determination of value is conclusive can create a problem.\textsuperscript{352}

In \textit{U.S. Bank N.A. v. Cold Spring Granite Co.},\textsuperscript{353} the reference by the Minnesota Supreme Court to the lower court’s value determination as “problematic”\textsuperscript{354} was essentially a judicially polite ruling by the Minnesota Supreme Court that the deviation by the lower court from the statutorily conclusive value determination by the board of directors might be an error.\textsuperscript{355} However, the deviation from the board’s conclusion as to the appropriate value of the minority shareholders’ shares was not significant enough to justify judicial intervention by the Supreme Court to overturn the lower court’s decision.\textsuperscript{356} The Supreme Court determined that “any error [by the lower court] would not affect the result [in the case].”\textsuperscript{357} Therefore, the Supreme Court ruled that there was no judicial need to further address the issue of any legal error made by the lower court.\textsuperscript{358}

In interpreting the Minnesota statutory mandate\textsuperscript{359} relating to the legal effect of a board of directors’ determination, the Minnesota Supreme Court did not incorrectly ascribe to it the substantive standard of presumptive validity.\textsuperscript{360} On the contrary, the court correctly interpreted the statutory mandate as the highest legal standard, namely the standard of \textit{conclusiveness} absent a finding of fraud by the reviewing court.\textsuperscript{361} This made sense because the legislature had chosen to go beyond the standard of presumptive validity and had chosen conclusiveness as the applicable

\textsuperscript{351} \textit{Id.}
\textsuperscript{352} \textit{U.S. Bank N.A.}, 802 N.W.2d at 379 n.11 (“Because the Board’s determination of fair value is conclusive absent fraud, and the district court concluded that fraud was not present here, the district court’s finding that fair value was different from the figure determined by the Board is \textit{problematic}.”) (emphasis added).
\textsuperscript{353} \textit{Id.}
\textsuperscript{354} \textit{Id.}
\textsuperscript{355} \textit{Id.}
\textsuperscript{356} \textit{Id.} at 369.
\textsuperscript{357} \textit{Id.} at 379 n.11 (“Nevertheless, any error would not affect the result here.”).
\textsuperscript{358} \textit{Id.} (“[W]e need not address [the issue of error] further.”).
\textsuperscript{359} \textit{Id.} at 375.
\textsuperscript{360} \textit{Id.} at 375–76.
\textsuperscript{361} \textit{Id.} at 375.
standard, in the absence of a court’s finding of fraud in the directors’ decision.\textsuperscript{362}

Conceivably, in mandating the application of this highest standard of validity\textsuperscript{363} for the board of directors’ valuation decisions in close corporations, the legislature may have been doing the same as “focusing on the quality of the deliberative process [which maximizes] the directors’ ability to bring their best collective judgment to bear on the difficult decisions they must make.”\textsuperscript{364} Arguably, such a substantive approach is viable not only in the context of mergers and acquisitions,\textsuperscript{365} but also in other contexts where the board makes decisions, such as in share valuation determinations.

However, potentially mischievous issues pertaining to the valuation of stock in close corporations can arise in other controversies, as well.\textsuperscript{366} For example, some of these may revolve around a challenge to the proper exercise of statutory appraisal rights by dissenting minority shareholders who oppose a merger between the corporation in which the dissenters’ shares are owned and some other entity.\textsuperscript{367} In the context of such a controversy, the court strives to determine an appropriate “value between parties who are either unable or unwilling to voluntarily agree.”\textsuperscript{368}

\textit{Swope v. Siegel-Robert, Inc.}\textsuperscript{369} is helpful in this regard. In \textit{Swope}, the Eighth Circuit explained that the concept of fair market value is derived from a hypothetical context of willing buyers and willing sellers in an open market where the buyers and sellers are neither constrained to buy nor to sell.\textsuperscript{370} Undoubtedly, the free exercise of volition by both buyers and sellers is the transcendent factor in such a context.\textsuperscript{371} However, dissenting shareholders do not act within the confines of such a context at all.\textsuperscript{372} Rather, dissenting shareholders seeking to sell their shares

\textsuperscript{362} See id. at 379.
\textsuperscript{363} Id.
\textsuperscript{364} Strine, supra note 28, at 706.
\textsuperscript{365} Id. (“[I]n the M&A context.”).
\textsuperscript{366} See, e.g., Leacock, \textit{Valuing Stock}, supra note 10.
\textsuperscript{367} See \textit{Swope v. Siegel-Robert, Inc.}, 243 F.3d 486, 491 (8th Cir. 2001).
\textsuperscript{368} Id.
\textsuperscript{369} Id. at 493.
\textsuperscript{370} Id.
\textsuperscript{371} Id.
\textsuperscript{372} Id.
and gain their freedom by escaping from the corporation in which they own such stock are neither free nor willing participants in the sale of the shares in controversy.

In this context, dissenting shareholders may be perceived as securities-based hostages appealing to the courts to exercise principles of equity and fairness to set them free.

Furthermore, in *Swope*, the Eighth Circuit interpreted fair value to be “the proportionate share of the value of 100 percent of the equity, by entitling a dissenting shareholder to a ‘proportionate interest in the corporation, without any discount for minority status ....’” This is the case because in an appraisal controversy, the entire corporate enterprise is to be valued in order to determine a minority shareholder’s pro rata share of the total value. The court therefore concluded that “because ‘fair market value’ is irrelevant to the determination of fair value, market forces, such as the availability of buyers for the stock, do not affect the ultimate assessment of fair value in an appraisal proceeding.”

*Brown v. Arp & Hammond Hardware Co.* is another helpful example. In *Brown*, the Wyoming Supreme Court ruled that the application of a minority discount in the appraisal valuation of the minority stockholders was not legally permitted. The Wyoming Supreme Court explained that in the context of minority shareholders’ statutory appraisal rights, “our legislature’s use of the term ‘fair value’ was not a slip of the pen—the legislature did not intend to say ‘fair market value’ instead.” The legislature did not intend the substantive concept of fair market value to be the applicable standard. This is so because fair market value is a function of free bargaining between willing participants.

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373 Id. at 492 (“Dissenting shareholders, by nature, do not replicate the willing and ready buyers of the open market. Rather, they are unwilling sellers with no bargaining power.”) (citations omitted).

374 Id.
375 Id.
376 Id.
377 Id. at 493.
378 141 P.3d 673, 686 (Wyo. 2006).
379 Id.
380 Id. (emphasis added) (citation omitted).
381 Id.
382 Id.
the identification of fair value is a viewpoint arguably shared by
the American Law Institute.\textsuperscript{383} Fair value is different from fair
market value.\textsuperscript{384} In order

to find fair value, the ... court must determine the best price a
single buyer could reasonably be expected to pay for the cor-
poration as an entirety and prorate this value equally among
all shares of its common stock. Under this method, all shares
of the corporation have the same fair value.\textsuperscript{385}

In other words, since determination of the neutral value of the
entire corporation is the judiciary’s goal, the Minnesota Supreme
Court’s proposal in \textit{Advanced Communication Design, Inc. v. Follett} rings true.\textsuperscript{386} In \textit{Advanced Communication Design},\textsuperscript{387} the
Minnesota Supreme Court concluded that in determining fair
value, the court is free to rely upon “proof of value by any tech-
nique that is generally accepted in the relevant financial com-
community and should consider all relevant factors, but the value
must be fair and equitable to all parties.”\textsuperscript{388} This approach
properly refrains from elevating either the majority or the mi-
nority stockholders’ self-interest in the valuation proceedings
above the self-interest of the other.

Arguably, in the context of dissenting shareholders’ disputes
in close corporations, ascertaining the optimal valuation should
probably be viewed from the more subjective perspective\textsuperscript{389} of
the withdrawing shareholders rather than from the objective
perspective of fair market value. After all, such dissenting
shareholders are relinquishing their shares \textit{to the corporation},\textsuperscript{390}
rather than to a conceptually objective third party in an ‘arm’s

\textsuperscript{384} See Brown, 141 P.3d at 686 (“[C]ourts have held that fair value cannot
be equated with ‘fair market value.’”) (citations omitted).
\textsuperscript{385} Id. (citations omitted).
\textsuperscript{386} 615 N.W.2d 285 (Minn. 2000).
\textsuperscript{387} Id.
\textsuperscript{388} See id. at 290 (emphasis added) (citations omitted).
App. 2006) (applying corporate law “fair value” valuation standards to a
limited partnership controversy) (i.e., “[T]he \textit{intrinsic} value of the shareholder’s
economic interest in the corporate enterprise.”) (emphasis added).
\textsuperscript{390} See, \textit{e.g.}, Charland v. Country View Golf Club, 588 A.2d 609, 609–10
length context.” In contrast, fair market value would be “the price at which property would change hands between a willing buyer and a willing seller, neither under any compulsion to buy nor sell and both having knowledge of relevant facts.” It is arguably inappropriate to perceive dissenting shareholders as “willing” sellers. In all fairness, dissenting shareholders in this context are arguably coerced sellers.

VI. ESTATE TAX SETTING AND FAIR MARKET VALUE DETERMINATIONS

When a shareholder in a close corporation dies, ownership of her stock is transferred by operation of law to her estate, which becomes the new owner of the stock. This transfer of ownership of the shares subjects the fair market value of the transferred stock to estate duty imposition under tax law. As a result, a date of death valuation is required in order to properly ascertain the stock’s fair market value. Of course, the Internal Revenue Service will probably seek the most accurate assessment required by law in order to ensure that the correct assessment under estate tax law is imposed.


392 See, e.g., Swope v. Siegel-Robert, Inc., 243 F.3d 486, 491 (8th Cir. 2001) (“Determining fair value [is] ‘purposely if not wisely establish[ing] a flexible general standard for fixing value between parties who are either unable or unwilling to voluntarily agree’ ....”) (emphasis added) (citation omitted).

393 Id. at 492–93 (citations omitted).


395 See, e.g., Estate of Adell, T.C.M. (CCH) 2014-155, at *37–38 (“The Court is asked to determine the fair market value of [the deceased’s] 100% interest in [the close corporation’s stock] on his date of death and whether the estate is liable for the ... estate tax valuation understatement penalty with respect to the [close corporation’s] stock.”) (emphasis added).

396 See id. at *45.

397 See, e.g., id. at *38 (“The estate now argues that the fair market value of the [pertinent] stock it held on the valuation date was $4.3 million.
On the other hand, the deceased taxpayer’s estate will most likely seek the lowest legally permissible value under tax law in order to ensure imposition by the Internal Revenue Service of the lowest legally tenable estate tax assessment. Where on his death the deceased taxpayer owned a minority interest in a close corporation, the deceased taxpayer’s estate would arguably welcome court application of both lack of marketability and lack of control discounts in calculating the date of death value of the deceased taxpayer’s shares. The application of such discounts would have the legal effect of lowering the death-date value of the deceased shareholder’s stock in the close corporation, thereby reducing the estate tax liability of the deceased shareholder’s estate.

However, under estate tax law, fair market value is the legally applicable test for determining the value of the deceased minority shareholder’s estate that becomes subject to estate tax imposition. “Fair market value is the price at which property would change hands between a willing buyer and a willing seller, neither under any compulsion to buy or sell and both having knowledge of relevant facts.” This test differs from court valuations in the context of appraisal proceedings using the fair value test applicable to majority shareholder buyouts of minority stockholders’ shares. Use of fair market value in estate duty controversies precludes legal recognition and accommodation by the courts of claims of coercion relating to the sale of a stockholder’s minority interest in a close corporation. After all, the

[Internal Revenue Service] now asserts that the fair market value of the stock was $26,341,030.

398 Id. at *37–38.
400 See, e.g., Estate of Jelke III, T.C.M. (CCH) 2005-131, at 1068 (“We hold that 15 percent is an appropriate discount for lack of marketability .... [This is] coupled with the 10-percent discount for lack of control.”).
401 Id.
402 See Estate of Adell, T.C.M. (CCH) 2014-155, at *41.
403 Id. (emphasis added).
404 See Advanced Commc’n Design v. Follett, 615 N.W.2d 285, 290 (Minn. 2000).
405 Estate of Adell, T.C.M. (CCH) 2014-155 at *12 (“The hypothetical willing buyer and seller are presumed to be dedicated to achieving the maximum economic advantage.”) (citations omitted).
death of a minority shareholding taxpayer is the triggering factor for valuation in estate duty controversies and such deaths are involuntary.

In contrast, the ejection of minority stockholders from close corporations is a calculated intentional action by the majority shareholders. It is the voluntary and intentional nature of such actions by the majority shareholders that trigger statutory appraisal proceedings. The phenomenon of death is not a voluntary coercive separation of a minority stockholder from his ownership of stock in a close corporation at all. Corporate buyouts of minority shareholders fit such a definition, not death.

The fair market value test applicable in estate tax controversies to valuations of minority stockholders’ shareholdings in close corporations in order to determine how much estate tax the deceased minority shareholder’s estate owes to the Internal Revenue Department does not preclude application of either lack of marketability or lack of control discounts. Therefore, although in *Estate of Jelke III v. Commissioner of Internal Revenue* the United States Tax Court committed reversible error by allowing “15 percent [as] an appropriate discount for lack of marketability ... coupled with the 10-percent discount for lack of control ...”, the United States Court of Appeals for the Eleventh Circuit’s reversal and remand did not nullify either of these two discounts.

The United States Tax Court in *Estate of Jelke III v. Commissioner* was correct in observing that “the determination of the fair market value of property is a factual determination, and

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406 See Brown v. United States, 329 F.3d 664, 678–79 (9th Cir. 2003).
408 See Anderson v. CONRAIL, 297 F.3d 242, 245–46 (3d Cir. 2002).
409 See, e.g., Estate of Richmond v. Comm’r, T.C.M. (CCH) 2014-26, at *45 (T.C. 2014) (“We ... find that a marketability discount ... is reasonable in this case.”).
410 See, e.g., *Estate of Richmond*, T.C.M. (CCH) 2014-26, at *42 (“We conclude that a discount for lack of control ... is reasonable in this case.”).
412 Id. at 1068.
the trier of fact must weigh all relevant evidence of value and draw appropriate inferences.”

Although the courts do look to valuation experts for guidance, the value determination is a finding of fact, so the court is free to accept, reject, or modify the valuation conclusions of either the adversarial parties or their respective experts.

In *Estate of Jelke III v. C.I.R.*, the United States Court of Appeals for the Eleventh Circuit vacated and remanded the decision of the United States Tax Court in *Estate of Jelke III v. Commissioner of Internal Revenue* based upon the following explanation. The Eleventh Circuit explained that “[a] determination of fair market value is a mixed question of fact and law .... The mathematical computation of fair market value is an issue of fact, but determination of the appropriate valuation method is an issue of law that [the Court of Appeals] review[s] de novo.”

Therefore, based upon the United States Court of Appeals for the Eleventh Circuit’s *de novo* review of the United States Tax Court’s decision, the Court of Appeals reversed the Tax Court’s decision and remanded the case for determination anew of the fair market value of the deceased taxpayer’s estate at the time of death. Of course, on remand, lack of marketability and minority discounts could be applied if, in the exercise of its sound discretion the United States Tax Court decided to apply neither, either, or both of these discounts.

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414 T.C.M. (CCH) 2005-131, 1058 (citations omitted).
415 Estate of Adell v. Comm’r, T.C.M. (CCH) 2014-155, at *40 (T.C. 2014) (“As the finder of fact, the Court considers the underlying facts agreed upon by the parties and presented at trial and looks to the experts’ reports for guidance on deciding the valuation issue.”).
416 See, e.g., Estate of Richmond v. Comm’r, T.C.M. (CCH) 2014-26, at *21 (T.C. 2014) (“[The courts] are not bound by the opinion of any expert witness and may accept or reject such testimony in the exercise of our sound judgment.”) (citations omitted).
417 507 F.3d 1317, declined to extend, Estate of Richmond, T.C.M. (CCH) 2014-26, at *51 n.4.
419 *Estate of Jelke III*, 507 F.3d at 1321.
420 Id. (citation omitted).
421 Id. at 1333.
422 Id.
CONCLUSION

In some valuation controversies regarding the appropriate value of minority stockholders’ shares in close corporations, it is entirely fair and equitable for courts to condone use of lack of control and lack of marketability discounts. In others, it is not fair and equitable to do so at all. It is also important to appreciate that these two discounts are not synonymous with each other. Additionally, judicial consensus with respect to the role that such discounts play in fundamental conceptions of fairness in these contexts continues to evolve.

Of course, “[w]hen ... fundamentals are disregarded, key players fail to play their roles with fidelity ....”423 That being the case, based upon the controlling dynamics governing each individual controversy, individual states424 may proceed differently in calculating the value that a minority shareholder is entitled to be awarded by the courts in a valuation dispute. No one would probably contest the view that “[human] life is too complex to bring the attainment of [an ideal system] within the compass of human powers.”425

Each jurisdiction is entitled to have its own valuation approach and to weigh the factors that merit consideration based upon the subtleties of corporate law applicable to close corporations created in each state. Nevertheless, all states arguably adhere to the fundamental principle that once a court has determined that either a lack of control or a lack of marketability discount—or both—should be applied, each application “must be applied in a manner consistent with the law.”426

Fortunately, as long as decision makers “appear to have made sensible, good faith judgments for legitimate, well-documented reasons, those judgments are likely to withstand judicial scrutiny.”427 In all instances, however, when share valuation disputes arise in close corporations, each shareholder’s astute awareness of the pertinent state’s valuation principles obviates ructions.

423 See Strine, supra note 28, at 681.
424 See Voeller v. Neilston Warehouse Co., 311 U.S. 531, 535 (1941) (“The conditions under which corporations shall organize and operate are matters within the exclusive province of the state, so long as those conditions do not clash with the national Constitution.”) (emphasis added).
427 See Strine, supra note 28, at 706.