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In Connecticut, Fair is Fair: Construing Fair Value and Other Considerations in Minority Shareholder Buyouts

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There is perhaps nothing more disruptive to a closely held corporation or limited liability company than a disaffected minority shareholder. Irrespective of the merits of any complaints that an individual owner or shareholder may have, such an individual who believes that he or she has been locked out of decisions or oppressed can grind the workings of a company to a halt. However, in situations where issues of shareholder oppression advance to litigation, the law provides for resolutions allowing the parties to part ways short of full litigation. In exploring these remedies it is essential to consider that the protections afforded minority shareholders by the state of Connecticut are uniquely broad and substantial.

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Grounds for Judicial Dissolution of Company by Minority Shareholder

In the face of lockout or oppression, a minority shareholder can petition the Connecticut Superior Court for a dissolution of the company if it can be shown that:

In a proceeding by a shareholder if it is established that:

(A) (i) The directors are deadlocked in the management of the corporate affairs, (ii) the shareholders are unable to break the deadlock, and (iii) irreparable injury to the corporation is threatened or being suffered or the business and affairs of the corporation can no longer be conducted to the advantage of the shareholders generally, because of the deadlock;

(B) the directors or those in control of the corporation have acted, are acting or will act in a manner that is illegal, oppressive or fraudulent;

(C) the shareholders are deadlocked in voting power and have failed, for a period that includes at least two consecutive annual meeting dates, to elect successors to directors whose terms have expired; or (D) the corporate assets are being misapplied or wasted.

Connecticut General Statutes §33-896(a)(1).

Company May Elect to Buy Shares of Minority Shareholder to End Litigation

Left to its usual course, a lengthy legal fight might ensue, draining the resources of both the company as well as the shareholder. With an eye to avoiding such costly litigation, the law provides that the corporation or any of its shareholders may elect to purchase all shares owed to the petitioning shareholder for fair value. Connecticut General Statutes §33-900(a). By making such an election, the corporation then has sixty days in which to reach an agreement as to the fair value of the petitioning member's shares. Connecticut General Statutes §33-900(c).

Great care and consideration should be taken in deciding whether to elect to buy a shareholder's interest and the terms of settlement once the election is made. In the event that parties are unable to come to an agreement

as to fair value of the shares, the Court is then tasked with making the determination. This is a process that, under the laws of Connecticut, favors the shareholder.

Purchase of Shareholder's Shares Must be at Fair Value Rather than Fair Market Value

By its terms, the statute provides that in the even that an agreement is not reached, the Court will determine "fair value" as opposed to "fair market value." Judges interpreting the statute have confirmed that the court's inquiry into the value of a petitioning member's shares is to be made consistent with this distinction. *See DeVivo v. DeVivo*¸ 30 Conn. L. Rptr. 52 (Hartford J.D., J. Satter 2001). This means that in determining the fair value of a petitioning shareholder's shares, the Court must consider the pro rata value of the shares with no discount for marketability - or the lack of market based on the inherent illiquidity of shares in a closely held corporation. *Id* at 8 By refusing to consider a marketability discount, the determination of fair value by the Court is necessarily higher than it would be otherwise.

Not only does failure to come to a settlement during the sixty-day period run the risk of an undiscounted valuation by the Court, but it might entitle the petitioning shareholder to his or her reasonable fees for both attorneys and experts. Should the Court determine that the petitioner had probably grounds for relief under Connecticut General Statutes §33-896(a)(1), it may award both.

Ultimately, when faced with a lawsuit for dissolution, a corporation should thoroughly analyze the cost of buying a petitioner's shares as well as the merits of the reasons for the requested dissolution. By being prepared to come to a negotiated resolution, a corporation can avoid a potentially large settlement imposed by the Court as well as interest and fees for both attorneys and experts.

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