

# Minority Shareholder Oppression Remedies Do Not Apply in LLC Dispute New Jersey Law

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Wednesday, January 22, 2014

New Jersey's Appellate Division recently issued a notable decision in a case involving a dispute over ownership rights in a **Limited Liability Company (LLC)**. *Tutunikov v. Markov*, Docket No. A-1827-10T3 (N.J. Super. Ct. App. Div., August 1, 2013) (unpublished). In *Tutunikov*, the plaintiffs were two minority shareholders in a predecessor entity to two LLCs, Markov Processes International, LLC- NJ and Markov Processes International, LLC- DE (collectively, MPI). The plaintiffs had voluntarily left their positions with the predecessor corporation, which was then dissolved. Thereafter, the two LLCs were formed to carry on similar business activities. Although the plaintiffs did not actively work for those entities, there were written resolutions setting forth the percentages of their minority ownership interests. There was no executed operating agreement and the ownership percentages in the draft document differed from the resolutions. Years later, after the two LLCs were merged into a single entity and a third party agreed to invest in the company, the plaintiffs were offered a buyout at a price that they considered inadequate. The two minority members alleged oppression and sued, raising complaints about excessive salaries taken by the majority members and the majority's assertion of ownership over an additional 4.5 percent interest in the prior

corporation that the plaintiffs believed were to be "treasury" shares.

After a bench trial, the trial judge agreed that the plaintiffs had proven oppression and ordered an equitable buyout at fair value. Because the Limited Liability Company Act had no provisions regarding member oppression, the court applied the oppressed minority shareholder provisions of the New Jersey Business Corporations Act (N.J.S.A. 14A:12-7). The trial court also awarded attorneys' fees and costs, as those remedies were available under the **Business Corporation Act (BCA)**. The Appellate Division unanimously reversed, finding that the plaintiffs had no oppression claim. The appeals court found that the plaintiffs had each voluntarily removed themselves from the prior corporation in which they had been shareholders, and that the prior corporation was then dissolved. The plaintiffs then became members of an LLC, and the LLC Act (unlike the BCA) did not allow a statutory claim for oppression. The Appellate Division found the absence of an equivalent provision in the LLC Act to be no accident but, instead, a deliberate legislative decision. The court noted that, when the LLC Act was repealed in 2012 in favor of the **Revised Uniform Limited Liability Act**, the new statute included an "oppression" provision but specified dissolution as the only remedy.

Moreover, the court found that the plaintiffs had known about the alleged excessive salaries and the defendants' claims of ownership of the treasury shares long before MPI had been formed. And, even though the defendants' arrogation of the treasury shares was inconsistent with a number of documents, the appeals court held that it could not be the basis for a shareholder oppression claim once the prior corporation had been dissolved and the new LLC formed. "We do not believe that . . . the alleged act of majority shareholder oppression—the misappropriation of treasury shares—translates into a continuing cause of action after a new entity, not subject to the BCA, was formed." Slip op. at 28. In addition, the plaintiffs' reasonable expectations were essential to evaluating whether defendants' conduct was oppressive, and here the plaintiffs' "reasonable expectations" could not have been frustrated because they would not have derived any benefit (either in increased distributions or percentage ownership) from the additional treasury stock. Accordingly, the appeals court held that there was no basis for a statutory oppression claim, and consequently no basis for the trial court's award of attorney fees.

The Appellate Division then addressed the trial court's determination of the fair value of the plaintiffs' interest in the LLC. The Appellate Division approved the trial court's use of the independent third party's purchase of 9.09 percent of MPI for \$500,000 on October 31, 2005, as a measure of the value of MPI. Both sides' appraisal experts agreed that the purchase price incorporated a marketability discount of 35 percent because MPI was not a publicly traded company. The appeals court agreed that a marketability discount was appropriate in valuing MPI as an entity, rather than in valuing the plaintiffs' particular interests, quoting *Balsimides v. Protameen Chems*, 160 N.J. 352, 373-74 (1999): "Discounting at the corporate level may be entirely appropriate if it is generally accepted in the financial community in valuing businesses." The Appellate Division then approved the trial court's decision to add back the amount of the discount before calculating the value of the plaintiff's interests, but noted that the trial court had incorrectly applied the discount factor and should have divided the \$5,000,000 price by 0.65. Reversing the discount seems inconsistent with *Balsimides'* pronouncement that "discounting at the

corporate level" may be appropriate. The end result in *Tukunikov* was to confer on the plaintiffs more than their pro rata share of the real value of MPI, which was \$5,000,000.

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