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INVOLUNTARY DISSOLUTION: THEORY AND OPERATION IN PUBLICLY TRADED CORPORATIONS

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ABSTRACT

Involuntary dissolution is recognized as the primary mechanism to monitor opportunism and remedy the aggrieved minority shareholders of corporations. Contrary to general understanding, involuntary dissolution is not idiosyncratic to close corporations. However, its application to publicly traded corporations requires an approach different than the one for close corporations. This note discusses and recommends the approach necessary to justify and effectively enforce involuntary dissolution statutes' application in the context of publicly traded corporations. It expresses the opinion that the contractual view of corporate law would provide the theoretical basis necessary to construe the statute for publicly traded corporations and exemplifies its approach through the shareholder oppression law of the U.S. corporate law.

INTRODUCTION

Greater contractual freedom in corporate law, brings greater judicial activism.[1] This is a consequence of the fact that the parties in long-term relational contracts do not adopt complete contracts which address all

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1. John C. Coffee, Jr., *The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role*, 89 COLUM. L. REV. 1618, 1620 (1989).

potential contingencies and conflicts.[2] Legislatures do not ignore the fundamental manner in which the participants make corporate bargains[3] and empower the courts through "involuntary dissolution" (i.e., "judicial dissolution") statutes to monitor opportunism that arises due to this incomplete contracting.

The involuntary dissolution statutes are recognized as the primary mechanism to monitor opportunism and to remedy the aggrieved minority shareholders of close corporations.[4] While the conduct permitting the application of an involuntary dissolution statute is more easily found in the context of a close corporation, there is no reason to limit the conception to such context.[5] As a matter of fact, the legislatures' equipment of imprecise language in involuntary dissolution statutes reveals the deliberate intention to avoid restrictive construction.[6] Hence, it is no surprise that the involuntary dissolution is seen among the remedies for minority shareholders of publicly traded corporations as well as close corporations.[7] Involuntary dissolution law is applied to publicly traded corporations by courts in many jurisdictions such as Canada, United Kingdom, New Zealand, Hong Kong, Bermuda and the U.S. states of Maine and Maryland.[8]

The inherent differences between the close and publicly traded corporations, and their shareholders, require the deployment of different approaches to justify and effectively enforce the involuntary dissolution statute in the context of publicly traded corporations. This note discusses the rationale of the involuntary dissolution law and recommends the approach necessary to enforce this rationale in the context of publicly traded corporations through the most common ground for involuntary dissolution, "shareholder oppression", from the lens of U.S. corporate law. It aims to loosen the judicial reluctance when courts deal with com-

2. Manuel A. Utset, *A Theory of Self-Control Problems and Incomplete Contracting: The Case of Shareholder Contracts,* Utah L. Rev. 1329, 1332 (2003).

3. Mohamed F. Khimji & Jon Viner, *Oppression-Reducing Canadian Corporate Law to a Muddy Default*, 47 Ottawa L. Rev. 123, 150 (2015).

4. Linda L. Shapiro, *Involuntary Dissolution of Close Corporations for Mistreatment of Minority Shareholders*, 60 Wash. U. L. Q. 1119, 1122 (1982).

5. Redmon v. Griffith, 202 S.W.3d 225 (2006).

6. Re Saul D. Harrison and Sons plc, [1995] B.C.L.C. 1, 14, (Hoffmann LJ.) (Eng.).

7. IOSCO Final Report on Protection of Minority Shareholders in Listed Issuers, 31 (June 2009), *available at* https://www.iosco.org/library/pubdocs/pdf/IOSCOPD295.pdf.

8. Murat Can Pehlivanoglu, Controlling the Non- Pecuniary Private Benefits of Influencing Shareholders in Publicly Traded Corporations Through Judicial Dissolution 217 (2018) (unpublished S.J.D. dissertation, Golden Gate University School of Law) (on file with author).

plaints for the involuntary dissolution (or its alternative remedies) of publicly traded corporations.[9]

I. SHAREHOLDER OPPRESSION

The grounds for involuntary dissolution, and the persons who may file an involuntary dissolution complaint, vary among jurisdictions. In the U.S., involuntary dissolution statutes generally grant dissolution when there is deadlock among directors or shareholders, when directors or those in control have been guilty of illegal or fraudulent or oppressive actions towards shareholders, or when the property of the corporation is being wasted.[10] Among these, "oppression" appears as the most common ground[11] implemented by state legislatures for involuntary dissolution.[12] While some state statutes do not include "oppression" among its dissolution grounds in precise language, courts nevertheless apply its principles through the interpretation of similar articulated or theoretical grounds.[13]

It is important to underline that the allegation of "oppression" does not appear as a claim for relief, but rather, a legal standard to be fulfilled before a court may order liquidation (or alternative remedies) of a corporation.[14] State legislatures generally made no attempt to define oppression[15] and the definitions have been embraced by case law.[16] The courts, faced with the problem of deciding which acts are oppressive and on what basis to determine the existence of oppressive acts, have developed three definitions (i.e., standards) to define "oppression"[17]: (1) A burdensome, harsh and wrongful conduct, a visible departure of fair dealing, and violation of fair play on which every shareholder who entrusts his money to corporation is entitled to rely;[18] (2) a conduct closely related to the violation of the fiduciary duty of good faith and fair dealing owed by

9. Shapiro, *supra* note 4, at 1147 ("Judicial reluctance is most formidable, however, when courts interpret and apply involuntary dissolution statutes.").

10. *See* N.Y. Bus. Corp. L. §§ 1104, 1104-a (1979); Cal. Corp. Code § 1800 (1975).

11. Carol L. Kline, *Protecting Minority Shareholders in Close Corporations: Modeling Czech Investor Protections on German and the United States Law*, 23 B.C. Int'l & Comp. L. Rev. 229, 243 (2000).

12. White v. Perkins, 213 Va. 129, 189 S.E.2d 315 (1972).

13. For example, see O'Very v. Spectratek Technologies, Inc., No. CV 03-00540, 2004 WL 5642004 (C.D. Cal. July 26, 2004).

14. Reget v. Paige, 242 Wis.2d 278 (2001).

15. Kiriakides v. Atlas Food Systems & Services, Inc., 343 S.C. 587 (2001) (citing the official comment to S.C. Code Ann. § 33-18-400 (1990)).

16. John J. Chapman, *Corporate Oppression: Structuring Judicial Discretion,* 18 Advoc. Q. 170, 189 (1996).

17. Scott v. Trans- System, Inc., 148 Wash.2d 701 (2003).

18. Gimpel v. Bolstein, 477 N.Y.S.2d 1014 (1984).

the majority to the minority shareholders;[19] (3) a violation of the reasonable expectations of the minority.[20] Accordingly, the conduct which satisfies the adopted definition for "oppression" is deemed "oppressive". Among these definitions, the "reasonable expectations" standard appears as the most widely accepted one.[21]

The theoretical approach illuminating shareholder oppression law is built on the contractual view of corporations.[22] Likewise, the oppression action is empowered to be attentive to context and rejects the hyper-textualist construction of the corporate relationship.[23] It is not developed as a ground to resolve mechanical corporate disputes like a deadlock in corporation's governance. Therefore, the discussion of the involuntary dissolution's application to publicly traded corporations through the oppression ground would be instructive regarding judicial dissolution's eligibility in the publicly traded corporation context and the liberal construction of the applicable theoretical approach.[24]

II. RATIONALE IN THE CLOSE CORPORATION CONTEXT

The rationale for applying the involuntary dissolution statute to close corporations can be better understood by analyzing the motive and nature of the oppressive conduct. Oppression is usually directed at a shareholder personally[25] with the purpose to "freeze-out" or "squeeze-out" that minority shareholder.[26] The terms "squeeze-out" or "freeze-out" means the use of strategic position to eliminate one or more of its owners or participants from the corporation.[27] While a minority shareholder need not to be deprived of his shares to be squeezed out, "he can be oppressed by actions which reduces his claim on the corporation's assets or deprives

19. O'Brein v. Pearson, 449 Mass. 377 (2007).

20. Pehlivanoglu, *supra* note 8, at 150.

21. Douglas K. Moll, *Shareholder Oppression & Reasonable Expectations: Of Change, Gifts, and Inheritances in Close Corporation Disputes*, 86 MINN. L. REV. 717, 728-31 (2002).

22. Benjamin Means, *A Contractual Approach to Shareholder Oppression Law*, 79 FORDHAM L. REV. 1161, 1202 (2010).

23. Shannon Kathleen O'Byrne & Cindy A. Schipani, *Feminism(s), Progressive Corporate Law and the Corporate Oppression Remedy: Seeking Fairness and Justice*, 19 GEO. J. GENDER & L. 61, 100 (2017).

24. *See* Part V. Theoretical Approach.

25. Brenner v. Berkowitz, 134 N.J. 488 (1993).

26. Douglas K. Moll, *Shareholder Oppression in Texas Close Corporations: Majority Rule Isn't What It Used to Be*, 9 HOUS. BUS. & TAX L.J. 13, 33 (2001).

27. "It may be defined as the use of corporate control vested in the statutory majority of shareholders or the board of directors to eliminate minority shareholders from the enterprise or to reduce to relative insignificance their voting power or claims on corporate assets. . . . Furthermore, it implies a purpose to force upon the minority shareholder a change which is not incident to any other business goal of the corporation." Gabhart v. Gabhart, 267 Ind. 370 (1977).

him of the return on his investment to which he is entitled."[28] Common freeze-out techniques include the termination of a minority shareholder's employment,[29] the refusal to declare dividends (or declaration of inadequate dividends), the siphoning off of corporate earnings through high compensation to the majority shareholders or related-party transactions violating arms-length principle,[30] mergers[31], and misapplication or waste of corporate funds.[32] When these are the case, the minority shareholders, having no ready market for the stock of a close corporation, can be "locked-in" to the corporation, yet "frozen-out" from any business returns.[33]

Accordingly, it is said that the primary purpose of the shareholder oppression law is to protect the shareholders' investment,[34] because the oppressive conduct leaves the shareholder without any adequate means of recovering his investment.[35] This argument is supported by the fact that involuntary dissolution statutes generally provide less drastic remedies than dissolution and the most common alternative remedy is the buyout of the oppressed investor's holdings.[36] The logical implication of this view is that oppression liability arises when the value of a shareholder's investment is harmed.[37] Herein, the function of the standards (i.e., definitions) that define oppression is seen as a key to identify whether the investment is harmed.[38]

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28. F. Hodge O'Neal & Ronald R. Janke, *Utilizing Rule 10b-5 for Remedying Squeeze-Outs or Oppression of Minority Shareholders*, 16 B.C. INDUS. & COM. L. REV. 327 (1975).

29. Gunzberg v. Art-Lloyd Metal Products Corp., 112 A.D.2d 423 (1985) ("As a result of their long history of taking an active part in the running of the corporation, petitioners demonstrated that they had a reasonable expectation that they would continue to be employed by the company and have input into its management. In *Matter of Kemp & Beatley, Inc. (Gardstein)*, the Court of Appeals acknowledged that such expectations, if not realized, amount to oppression because the major part of the earnings of a close corporation are distributed in the form of salaries, bonuses and retirement benefits.").

30. Garry D. Justis, *Avoiding a Minority Shareholder Oppression Claim in a Close Corporation in Missouri: The Impact of the New Close Corporation Statutes*, 56 MO. L. REV. 274 (2011).

31. Yanow v. Teal Industries, Inc., 178 Conn. 262 (1979).

32. Muellenberg v. Bikon Corp., 143 N.J. 168 (1996).

33. Moll, *Shareholder Oppression in Texas*, *supra* note 26, at 14.

34. For a discussion of the wider policy considerations behind the enactment the involuntary dissolution statute, see generally, Pehlivanoglu, *supra* note 8.

35. Ballard v. Roberson, 399 S.C. 588 (2012) ("The concern and focus in shareholder oppression cases is that the minority 'faces a trapped investment and an indefinite exclusion from participation in business returns.'").

36. Douglas Moll, *Shareholder Oppression v. Employment at Will In the Close Corporation: The Investment Model Solution*, 1999 U. III. L. REV. 517, 546 (1999).

37. *Id.* at 551.

38. *Id*. at 552.

III. RATIONALE IN THE PUBLICLY TRADED CORPORATION CONTEXT

While it is acknowledged that the publicly traded corporation can be the subject of oppressive acts,[39] justifying the application of the involuntary dissolution statute to publicly traded corporations through a rationale such as the "harmed investment value" may be, at first glance, problematic. After all, there is, in most instances, a ready market for the shares and investors purchase the shares of a publicly traded corporation with the purpose of receiving dividends or selling the shares at an appreciated value.[40] Furthermore, when a corporation sells a share to investors (and whenever investors buy its stock on the market), the investors knowingly consent implicitly to the arrangements, including the ones which may be deemed "oppressive", that the corporation has disclosed. Because in theory, if the investors wanted to have more favorable terms in their contract (e.g., articles of incorporation) with the corporation, they would have withheld their investment.[41] Even more strikingly, a shareholder who buys the share knowing the presence of oppressive conduct in the corporation, is already compensated by buying the share at a lower price that reflects that fact,[42] as an efficient market reflects the oppression to the price even when an individual shareholder is not aware of the fact.[43]

While these assertions have a plausible basis, realities are intact. Firstly, oppressive conduct harming the shareholder's investment is in effect in the context of publicly traded corporations both through the common freeze-out techniques stated above and unconventional techniques such as extraction non-pecuniary private benefits.[44] The purpose of the conduct causing the oppression of the minority in publicly traded corporations appears as the desire to extract disproportionate gains from the

39. Fox v. 7L Bar Ranch Co., 198 Mont. 201 (1982).

40. Exadaktilos v. Cinnaminson Realty Co., Inc., 167 N.J. Super. 141 (1979).

41. Victor Brudney, *Corporate Governance, Agency Costs, and the Rhetoric of Contract*, 85 COLUM. L. REV. 1403, 1412 (1989).

42. "If shareholders buy into corporations knowing that they are run by managers and controlling shareholders who can temper profit-maximization, then shareholders will have bought in at lower stock prices that reflect that fact and can claim no tax or injury when the tempering occurs." Einer Elhauge*, Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733, 787 (2005).

43. Christopher A. Riley, *Contracting Out of Company Law: Section 459 of the Companies Act 1985 and the Role of the Courts*, 55 MOD. L. REV. 784 (1992).

44. Extraction of non-pecuniary private benefits equally happens in close corporations. However, while the non- pecuniary private benefit in the close corporation is generally extracted through a managerial position (in this case, the common freeze-out technique of employment termination applies), this is not the case with the publicly traded corporation as the management and the shareholders of this institution are generally disconnected.

corporation: This desire directly harms the value of the minority's investment even though the minority is neither the target nor the subject of the conduct.[45] Secondly, investors in publicly traded corporations have little ability to negotiate the arrangements, and their understanding about the looseness of corporate participants' obligations is problematic.[46] Moreover, without an adequate disclosure, shareholders cannot be deemed "consented" to the frustration of their expectations.[47] Even when there is adequate disclosure, shareholders would not meaningfully consent those arrangements, because consent to such oppressive actions would be underinformed due to transaction costs.[48] Thirdly, a publicly traded corporation might change its long-standing policy at some point during an investor's participation in the corporation[49] and an investor who bought the share at a price that did not reflect the oppression might find himself in a position that was not foreseeable in advance:[50] His exit by selling the

45. *See generally* Pehlivanoglu, *supra* note 8.

46. Brudney, *supra* note 41, at 1420.

47. "In much the same way, variations of core fiduciary or structural rules might be both unfairly surprising and inefficient even if impounded into the price. What will be impounded into the price is the average likelihood that managers will exploit such a provision in a manner that will significantly decrease shareholder wealth. This average may be quite small, but many investors may well have preferred not to invest in a corporation whose stock was subject to significant losses as a result of substantial nonbusiness risks." Melvin Aron Eisenberg, *The Structure of Corporation Law,* 89 COLUM L. REV. 1461, 1521 (1989).

48. "The quality of the consent to such variations would be even weaker in publicly held corporations, where true bargaining is almost impossible, and knowledge of the variation, let alone its meaning and implications, would typically be lacking. In publicly held corporations, the problem of systematically underinformed consent would apply not only to core fiduciary rules, but to core structural rules, because just as core fiduciary rules govern traditional conflicts of interest, so core structural rules govern positional conflicts. . . . Persons who proposed to buy stock in a publicly held corporation therefore would either have to expend resources to determine whether the corporation was subject to all the core rules that constrain unfair self-dealing, shirking, and positional conflicts by top managers, or assume that all corporations had adopted variations of those core rules. Either course of action would render capital markets less efficient, because investors would either put less of their money into corporate securities or demand a higher return from such securities, than would otherwise be the case." *Id.* at 1522.

49. Re Mediavision Ltd., [1992] 2 H.K.C. 629 (H.K.) ("[t]hat management may change, that management could indeed change its own mind").

50. "On the other hand, if shareholders buy their shares expecting pure profit-maximization, then they will have bought at prices that reflect that expectation and thus will suffer a loss if profits are sacrificed. Nor can they avoid the economic loss that results when a corporation embarks on a course of sacrificing profits by just selling their shares because the now-expected decline in future earnings will be capitalized into the market price at which they can sell their shares." Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest,* 80 N.Y.U. L. Rev. 733, 787 (2005).

share at the market at a price now reflecting the oppression fact[51] would cause an unfair loss for him.[52]

Accordingly, in the context of publicly traded corporations, any unjustified action which frustrates the investor's expectation of receiving sufficient dividends or selling the shares at an appreciated value would be oppressive since it would frustrate the basic reasonable expectations of the shareholders.[53] In this case, shareholders faced with oppression would lack an effective escape as the market will provide a lower break-up price for the minority shareholders.[54] Therefore, the "harmed investment value" rationale, which is built on the lack of escape mechanism reality in close corporations,[55] is partly in effect in the publicly traded corporation context as well. Then, the rationale of applying the involuntary dissolution remedies to publicly traded corporations can be traced to the willingness to remedy the shareholders when the price of the share in the marketplace is depressed.[56]

In the context of publicly traded corporations, the involuntary dissolution legislations would be explicable as part of a program to make public investment in securities markets more attractive.[57] Since a share of a corporation is more than a capitalized dividend stream,[58] there should be

51. After all, the market price of shares traded on well-developed markets reflects all publicly available information including any misrepresentations. *See* Basic Inc. v. Levinson, 485 U.S. 224 (1988).

52. Yu-Hsin Lin, Controlling Controlling-Minority Shareholders: Corporate Governance and Leveraged Corporate Control, 2017 COLUM. BUS. L. REV. 453, 493 (2017).

53. *See generally* Pehlivanoglu, *supra* note 8. The shareholders of a publicly traded corporation may well have other purposes which might be classified among reasonable expectations protected through involuntary dissolution. For more discussion, see, Pehlivanoglu, *supra* note 8, at 229.

54. "It is curious, and unusual, for shareholders in a public company to ask a court to order the company buy shares they can sell on the public market. The shares in question are listed on the Winnipeg stock exchange. Particularly if the only complaint is a lack of confidence, the quick, cheap, and simple solution is to sell them. I believe the Court can ask what is really going on here. The shareholders obviously consider the public market to be grossly under-valued. They seem to believe that the learned Chief Justice has uncovered a valuable right of which the market has been unaware: the right to force purchase at break-up value. At no point in his Reasons did the learned Chief Justice say that the shareholders could force a purchase at break-up value. But he did say that there was oppression, and he did say that the shareholders had a reasonable expectation in the maintenance of a high break-up value." Westfair Foods Ltd. v. Watt (1991), 115 A.R. 34 (Can. Alberta Q.B.).

55. Douglas K. Moll, *Shareholder Oppression in Close Corporations: The Unanswered Question of Perspective*, 53 VAND. L. REV. 749, 759 (2000).

56. Allen B. Afterman, *Statutory Protection for Oppressed Minority Shareholders: A Model for Reform*, 55 VA. L. REV. 1043, 1067 (1969).

57. Deborah Demott, *Oppressed but Not Betrayed: A Comparative Assessment of Canadian Remedies for Minority Shareholders and Other Corporate Constituents*, 56 L. & CONTEMP. PROBLS. 222 (1993).

58. *See* Gambotto v. WCP Ltd. (1995) 182 CLR 432 (Austl.).

safeguards against its expropriation by the state or private citizens. Not surprisingly, expropriation of private rights in corporate law is only granted through unambiguous statutory expression of legislative intention, such as mergers with appraisal as exclusive remedy[59] or private contracting. In this regard, involuntary dissolution statutes function as a law providing a safeguard against the expropriation of private rights through opportunism.

IV. THEORETICAL APPROACH

The effective enforcement of the involuntary dissolution statute in the publicly traded corporation context would be better ensured if the "nexus of contracts" theory of corporate law, the most academically influential attempt to articulate the doctrinal basis for corporate law in the U.S.,[60] is considered. According to the "nexus of contracts" theory of corporate law, corporations are not mere entities but a nexus of contracts[61] in which corporate constituents contract with the corporation.[62] This contractual view of corporations produces the notion of "corporate contract", which is an umbrella contract that includes all parties' bargains and asserts that the "corporate contract" should be characterized by a process of construction rather than a passive discovery.[63] Therein, corporate law's primary function is conceived of as the facilitation of the parties' bargains.[64] It is argued that "corporate law, both statutory and judicial, acts as a set of standard terms that lowers the cost of contracting"[65] and that corporate law will fulfill its function if the contract created by the corporation statute matches the results of costless bargaining.[66] The terms of the contract is articulated by the default and mandatory rules of corporate law.

59. For a discussion of appraisal as exclusive remedy, see, Mitchell Partners L.P. v. Irex Corp., 656 F.3d 201 (2011).

60. Ross Grantham, *The Rights of Company Shareholders*, 67 CAMBRIDGE L.J. 578 (1998).

61. FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 12 (1991).

62. Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance* 8-9 (UCLA, School of Law Research Paper No. 02-06, 2002) ("Yet some deference should be shown the corporation's status as a legal person. Corporate constituents contract not with each other, but with the corporation. . . . The various constituencies thus must be (and are) linked to the nexus and not to each other.").

63. Christopher A. Riley, *Contracting Out of Company Law: Section 459 of the Companies Act 1985 and the Role of the Courts*, 55 MOD. L. REV. 785 (1992).

64. Grantham, *supra* note 60, at 579.

65. EASTERBROOK & FISCHEL, *supra* note 61, at 236-37.

66. Brian R. Cheffins, *An Economic Analysis of the Oppression Remedy: Working towards a More Coherent Picture of Corporate Law*, 40 U. TORONTO L.J. 775, 787 (1990).

Capital market law (i.e., securities law) is the principal component of corporate law[67] and it regulates the institution of publicly traded corporation to a wide extent. Contractual theory is applicable to this area of law as well and the issues that it is regulating constitutes the remaining terms of the corporate contract.[68] After all, "an offer of securities to the public is an offer to enter into a contract whereby members of the public will acquire securities from their issuer. . . . The terms of that contract are based on the marketing material (prospectus) which is produced by the issuer of those securities before their issue and on a continuing basis thereafter".[69] Due to the mandatory nature of securities law, the terms of this contract are automatically added to the contract.[70] In this sense, securities law provides standard contract terms and decrease the transaction costs;[71] and in theory, the terms it mandatorily imposes on parties are, in fact, ones that the parties would have added.[72] Then, the corporate con-

67. EASTERBROOK & FISCHEL, *supra* note 61, at 276.

68. "The articles may not be the only contractual terms of the relationship between the company and a shareholder. The company and a shareholder may establish additional contractual arrangements governing their relationship. These additional agreements are typical where a different class of shares created and issued, such as preference shares or redeemable shares. The terms of issue of these shares, typically contained in the issue document, supplement the provisions in the articles." SUSAN MCLAUGHLIN, UNLOCKING COMPANY LAW 148 (2d ed. 2012).

69. ALASTAIR HUDSON, SECURITIES LAW 329 (Sweet & Maxwell 2008). The historical evolution of securities law in England can be traced to recognize this nature of the securities law: "Even in the Victorian period of the promoters before the company acquired its distinct personality, there would be some advertising literature which sought to induce investors to spend their Money on acquiring securities of the given kind. This advertising material was known as a prospectus." (HUDSON at 23). Consequently, the common law dealing with investment contracts has dealt frequently with the provisions of prospectuses (HUDSON at 24). The offer of securities and their acquisition constituted a contract. The principal focus of the litigation, therefore, tended to focus on the question whether or not those promoters had committed fraud in the marketing of the company or had some negligent misrepresentation or misstatement in the formation of the contract for sale of the shares (HUDSON at 22). Similarly, advisors to the company, whether or not they were directors of that company or partners in a joint stock company, also faced similar liability for any involvement in the making or dissemination of such statements (HUDSON at 22).

70. Schaad v. Hotel Easton Co., 369 Pa. 486 (1952) ("The relation between a corporation and a preferred shareholder is one of contract, especially as to the preferential right secured by the terms of the issue.").

71. Ronald Coase outlines the concept of "transaction costs" as follows: "In order to carry out a market transaction it is necessary to discover who it is that one wishes to deal with, to inform people that one wishes to deal and on what terms, to conduct negotiations leading up to a bargain, to draw up the contract, to undertake the inspection needed to make sure the terms of the contract are being observed, and so on. These operations are costly, sufficiently costly at any rate to prevent many transactions that would be carried out in a world in which the pricing system worked without cost." R.H. Coase, *The Problem of Social Cost*, 3 J. LAW & ECON. 1, 15 (1960).

72. Harwell Wells, *The Rise of the Close Corporation and the Making of Corporation Law*, 5 BERKELEY BUS. L.J. 263, 287 (2008) ("The statutory norms were not problems for public corporations, because the norms themselves mirrored the governance structures favored by public corporations. They were, however, a problem for the close corporations participants who desired to change those governance mechanisms.").

tract regarding the publicly traded corporation "can be viewed as a standard form multiparty contract, some of the terms which are specified by statute."[73] As a result, it can be expressed that "a stockholder's right between himself and the corporation and the other stockholders are contractual, and that the terms of the contract are to be found in the agreement of association and the provisions of applicable statutes."[74]

One important function of the "default rules of corporate law is to provide a means of accommodating, over time, developments that cannot easily be foreseen at the outset."[75] After all, "transaction costs affect the ability of the parties to make exhaustive agreements capable of addressing all possible contingencies that may arise in the course of their relationship"[76] and it is understood that the parties in long-term transactions or contracts (i.e., relational contracts),[77] such as shareholders in corporations, do not adopt complete contracts which address all potential contingencies and conflicts.[78] As a corollary, it is generally assumed that issues such as "shareholder oppression" would have been bargained by shareholders if bargaining were costless,[79] and oppressive conduct "violates the agreement that the parties would have reached . . . if they had negoti-

73. Kirshnan S. Chittur, *Resolving Close Corporation Conflicts: A Fresh Approach*, 10 HARV. J.L. & PUB. POL'Y 129, 159 (1987); Western Foundry Co. v. Wicker, 403 III. 260 (1949) ("The terms of this contract are embodied in the charter of the corporation and in the appropriate provisions of the corporation statute in force at the time the articles of incorporation were adopted.").

74. Crocker v. Waltham Watch Co., 315 Mass. 397 (1994).

75. REINIER KRAAKMAN ET AL., ANATOMY OF CORPORATE LAW 21 (2d ed. 2009).

76. William J. Aceves, *The Economic Analysis of International Law: Transaction Cost Economics and the Concept of State Practice*, 17 U. PA. J. IN'L ECON. L. 995, 1002 (1996).

77. Melvin A. Eisenberg, *Why There is No Law of Relational Contracts,* 94 NW. U. L. REV. 805, 814 (2000) (The phrase "long-term contracts" is generally used as a synonym for relational contracts.).

78. Manuel A. Utset, *A Theory of Self-Control Problems and Incomplete Contracting: The Case of Shareholder Contracts,* 2003 UTAH L. REV. 1329, 1332 (2003); Charles J. Goetz, Robert E. Scott, *Principles of Relational Contracts*, 67 VA. L. REV. 1089, 1091-92 (1981) ("A contract is relational to the extent that the parties are incapable of reducing important terms of the arrangement to well-defined obligations. Such definitive obligations may be impractical because of inability to identify uncertain future conditions or because of inability to characterize complex adaptations adequately even when the contingencies themselves can be identified in advance. As the discussion below illustrates, long-term contracts are more likely than short-term agreements to fit this conceptualization, but temporal extension per se is not the defining characteristic . . . In conventional contracts, the parties generally are able to reduce performance standards to rather specific obligations. By contrast, relational contracts create unique, interdependent relationships, wherein unknown contingencies or the intricacy of the required responses may prevent the specification of precise performance standards. Complexity and uncertainty each play conceptually distinct roles, although they frequently operate in combination.").

79. Cheffins, *supra* note 66, at 789 ("It is generally assumed that participants in corporations would bargain for protection against oppression and unfair prejudice if bargaining were costless").

ated a solution to the disputed point."[80] In fact, this is the reason why the oppression statutes give the "shareholder the benefit of a hypothetical bargain that she never memorialized in an enforceable agreement."[81] Herein, the involuntary dissolution law is used as the umbrella concept which provides the statutory terms for the "corporate contract" on issues regarding contingencies that may arise in the course of the corporate relationship.

V. APPLYING THE THEORY

Relying on the contractual view, once it is acknowledged that the presence of a default involuntary dissolution rule is necessary for corporate law to fulfill its function, the enforcement of the statute should be construed through the principles of the contractual view as well. In this sense, under "a contractarian framework, the oppression action is a default contractual term embedded in any contract between a corporate stakeholder and the corporation" and the broad language of the statute "leaves it to the courts to determine what approach to contractual gap-filling should be undertaken when interpreting the oppression provisions."[82] As a consequence, using the most widely accepted standard as the touchstone, it can be said that jurisdictions that have adopted the "reasonable expectations" standard to define oppression "embrace the central tenet of the nexus of contracts theory of the firm, that the primary role of corporate law should be to enforce participants' contract."[83]

According to the contractual theory, an economic analysis does not solely focus on enforcement of expressly articulated bargains and pays attention to bargains never fully articulated as well, "because at some point the costs of setting out a bargain in writing will exceed the benefits."[84] In most instances, some parts of the agreement are left unwritten. Also, as the nature of the corporate contract is a long-term transaction rather than a discrete one, it is not possible to foresee and articulate every possible conflict that may arise in the contract in the future;[85] and "economically rational investors will often prefer to live with an incomplete

80. Michael E. DeBow, "*Oppression" of Minority Shareholders: Contract, Not Tort*, 54 ALA. L. REV. 128, 128 (1993).

81. Anupam Chander, *Minorities, Shareholder and Otherwise*, 113 YALE L.J. 119, 144 (2003).

82. Khimji & Viner, *supra* note 3, at 142.

83. Terry A. O'Neill, *Self-Interest and Concern for Others in the Owner-Managed Firm: A Suggested Approach to Dissolution and Fiduciary Obligation in Close Corporations*, 22 SETON HALL L. REV. 646, 691 (1992).

84. Cheffins, *supra* note 66, at 785.

85. O'Neill, *supra* note 83, at 659.

bargain, addressing problems later, if and when they arise."[86] In this regard, the "shareholder oppression doctrine reduces the need for expensive ex ante bargaining, allowing the participants to proceed with an incomplete agreement."[87]

Economic theory[88] suggests that both the express terms of the agreement, and the terms that the agreement would have included if the negotiations had been costless, should be equally considered to fully construe the parties' agreement (i.e., corporate contract).[89] Herein, the most widely accepted standard of the oppression ground, the "reasonable expectations" standard, exists to make the following construction: "reasonable expectations constitute the bargain of the parties in light of which subsequent conduct must be appraised."[90] In this sense, it appears as a method that is used to find or interpret the explicit or implicit terms of the contract.[91] Not surprisingly, the reasonable expectations standard is already in use in different contexts of corporate law for both close and publicly traded corporations.[92]

Then, to decide whether the involuntary dissolution remedy should be applied to a publicly traded corporation through a ground such as "oppression", the parties' bargains first have to be fully understood. Thus, the bargains' terms, so its sources, need to be located. In the close corporation context "the array of rights possessed by any particular shareholder may well vary from one corporation to the next, because shareholder rights may spring from many sources: (1) the corporations organic documents, (2) agreements between shareholders or between the corporation and shareholders, (3) statutory corporation law, and (4) decisional law governing the operation of corporations."[93]

86. Means, *supra* note 23, at 1187.

87. *Id.* at 1194.

88. Mary-Hunter Morris, *Only "The Punctilio" If I Say So: How Contractual Limitations on Fiduciary Duties Deny Protection to Victims of Oppressive Freeze-outs Within Private Business Entities*, 10 Duq. Bus. L.J. 73, 77 (2008) ("The view of the business entity as a "nexus of contracts" was conceptually born as a result of the avid acceptance that the law and economics theory found within business law.").

89. Cheffins, *supra* note 66, at 792-93.

90. Application of Topper, 433 N.Y.S.2d 359 (Sup. Ct. 1980).

91. Progressive Cas. Ins. Co. V. Marnel, 587 F. Supp. 622 (1983) ("The most likely resort to reasonable expectations . . . would be as an interpretative tool where the language of a policy is ambiguous. . . . There is logic to a reasonable expectation being used as a construction tool where there is ambiguity in policy language.").

92. For example, in *Elliott Associates, L.P. v. Avatex Corp.*, 715 A.2d 843 (1998), the Delaware court expressed that the reasonable expectations standard can be used to determine the rights of preferred shareholders if there is ambiguity in the contract.

93. Schautteet v. Chester Bank, 707 F. Supp. 885 (1988).

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However, as the contractual relationship between the publicly traded corporation and its shareholders is different than in the close corporation, the sources of the bargain would also be different. This is due to the following reason: In the context of close corporations, the nature of the corporate contract generally remains intact as if it is a partnership contract because both the parties and the understanding between them generally remains unchanged and the newcomers purchase the shares by most likely knowing both the implicit and explicit conditions of the membership.[94] However, once a corporation becomes a publicly traded one, newcomers purchase the shares from the market and the dispersed nature of the shareholders makes it impossible for the newcomer to know the implicit terms unless those are disclosed to the public (i.e., made explicit). While this fact does not prohibit the application of the oppression standards, such as the "reasonable expectations" standard, for investors of public securities in general,[95] it produces the requirement for a limitation on the sources of the bargain in the context of publicly traded corporations.[96]

Then, the determination of the sources which the oppression ground should consider depends on the acknowledgement of the following principle: The disclosure policy of capital market law (i.e., securities law), regarding publicly traded corporations, forces a limitation implementation on the sources of the oppression analysis, and accordingly, only the explicit sources should be considered. Otherwise, the certainty, stability and trustworthiness of the marketplace would be undermined[97] and the transaction costs would eventually increase since every allegation of an implicit term would require a deep judicial evaluation. For instance, the "reasonable expectations" should be structured from the following explicit sources: (1) the statutory provisions (both corporate and capital market law) and additional layer of regulations (particularly, the listing rules), (2) corporation's organic documents (e.g., articles of incorporation, bylaws) and general assembly (i.e., shareholders' meeting) or board of directors' resolutions,[98] and (3) public disclosures (i.e., announce-

94. Jaffe Commercial Finance Co. v. Harris, 119 Ill. App. 3d 136 (1983).

95. *See* Bank of New York Mellon v. Commerzbank Capital Funding Trust II, 65 A.3d 539 (2013) (applying the reasonable expectations theory for the benefit of the holders of public securities).

96. O'Neill, *supra* note 83, at 658 ("For publicly traded corporations, there is an obvious difficulty in determining whether the shareholders got what they bargained for").

97. After all, "clearly defined legal rules that enable people to 'know the nature of their rights and obligations and be able to plan their actions with some confidence about the legal consequences." John A. Lovett, *On the Principle of Legal Certainty in the Louisiana Civil Law Tradition: From the Manifesto to the Great Repealing Act and Beyond*, 63 La. L. Rev. 1397, 1397 (2003).

98. Royals v. Piedmont Elec. Repair Co., 137 N.C. App. 700 (2000).

ments).[99] Among these sources, the public disclosures deserve a special explanation due to its continuing nature and unique position in the operation of publicly traded corporations. Other explicit common sources present the same characteristics as in the close corporation.

VI. USING PUBLIC DISCLOSURES AS A BASIS FOR THE COMPLAINT

The connection between the contractual view of corporate law, involuntary dissolution and the sources for analysis can be better understood by discussing why and how a public disclosure can be accepted as a source for oppression. The "efficient capital market hypothesis" accepts that the market price of shares traded on well-developed markets reflects all publicly available information (including any material misrepresentations), and an investor who buys or sells shares at the price set by the market does so in reliance on the integrity of that price. Thus, an investor's reliance on any public representations (including misrepresentation) may be presumed.[100] Using the contractual theory, it can be said that the information mandatorily disclosed by the issuer statutorily supplements the terms of the corporate contract.[101] Once these disclosures are accepted as

99. Although not discussed in U.S. law, Canadian law accepts that public announcements of a publicly traded corporation are "promises" that can create reasonable expectations. For examples, see *Themadel Foundation v. Third Canadian Investment Trust Ltd.*, 1995 CanLII 7040 (Ca. Ont. Sec. Com.) ("It strikes me that once the "promise" has been made (in a corporate/securities legislation sense as we have here through the information circulars and press releases which are to be translated into the issuer bids), then this promise becomes a reasonable expectation which deserves protection through the oppression provisions. . . . I think it reasonable that shareholders be entitled to rely on written and public pronouncements of what corporations in which they hold shares will do. This is especially so in the case of corporations which offer their shares to the public as it is an offence for such corporations to be other than truthful in public pronouncements.") and *Ford Motor Co. Canada, Ltd. v. Ontario Mun. Emp. Ret. Bd.*, 2006 CanLII 15 (Can. Ont.). Similar grounds are also asserted in some U.K. law cases by claimants and courts. For an example by a claimant, see *Bradman v. Trinity Estates plc*, [1989] B.C.L.C. 757 (Eng.): "One of the grounds of the application under sec. 459 is said to be that the transaction is prejudicial to members in that it represents a departure from what was held out to them in the prospectus . . . ." For an example by a court, see *Re Leeds United Holdings plc*, [1997] B.C.C. 131 (Eng.): "It may be that in certain cases the court can find a relevant legitimate expectation outside the company's constitution that can be relied on for s. 459 purposes even in the case of a public company, but such circumstances must, it seems to me, be rare."

100. Basic Inc. v. Levinson, 485 U.S. 224 (1988).

101. One may assert that relying on a provision that has an administrative remedy, rather than civil remedy as a basis in oppression claim, can mean that a civil remedy is created for the provisions violation through judiciary. For example, see Chapman, *supra* note 16, 213 ("The expensive wording of the oppression remedy raises the question as to whether the oppression remedy can be used as a means of civil enforcement of the continuous disclosure provisions."). However, this is not accurate. The securities law provisions are added to the oppression equation through the contractual theory and does not by its own establish a civil liability.

a term of the contract, it is easier to say that these can be used as a source for the analysis of an oppression.[102]

Accordingly, it is fair to ask whether a simple media advertisement or coincidental communication (e.g., answering an inquiry of a newspaper, or a managers' speech given during a conference in a university, or an unauthorized officer's reply to an investor's inquiry e-mail), unrelated from an investor relations department or mandatory disclosures, would give rise to a source for oppression.[103] Applying the contractual theory once again, it should be underlined that the reason why a disclosure made in accordance with securities law would give rise to an oppression source is that these disclosures would act as a supplement to the terms of the contract between the corporation and the shareholders due to the statutory framework that ties certain liabilities and rights to these disclosures. On the other hand, any advertisement or coincidental

102. The court's reasoning in the U.S. case, *Bank of New York Mellon v. Commerzbank Capital Funding Trust II*, 65 A.3d 539 (2013), presents an analysis for this issue: "The reasonable expectation of the public investors —in this case, the holders of the Trust Preferred Securities—must therefore be given effect. The investors' reasonable expectation in this case is that the DresCap Trust Certificates are Parity Securities. That result is hardly novel or surprising, because the Bank itself created that expectation: (i) in various communications with its German regulators, (ii) in its own internal communications, and (iii) with third parties. Particularly telling is that in a November 2009 e-mail exchange, a Bank employee, in response to an investor's inquiry, confirmed that, '[Y]es, the [DresCap Trust I Certificates] is a hybrid Tier 1 instrument which would qualify as a parity instrument.' That communication and others like it confirm that of the two competing interpretations, the Trustee's interpretation is the more reasonable, because the Defendants themselves believed— and contributed to the investment community's reasonable belief—that the DresCap Trust Certificates were Parity Securities." Building on the reasoning in this case, it can be said that a response of the investor relations department of a corporation can play a role in the interpretation of an issue and contribute to the expectations of a shareholder and deem it a reasonable one. After all, this department speaks on behalf of the issuer, and the information it gives or discloses to the particular investor would be done in accordance with the securities law, and thus become a part of the contract between the corporation and the shareholder. While one can assert that this particular answer would stay in between the two parties and can only contribute to the specific reasonable expectations of an investor (which is not considered in the context of a publicly traded corporation), this argument will fail: The fact that any material information should be disclosed to the public obliges the issuer to announce the information given to a particular investor to the public, and failure to do this does not change the nature of the information. It just means that there is a violation of the disclosure requirement, and the material nature of the information is enough to elevate it to a level that would deem it a term between the corporation and the shareholders in general.

103. The Swissair/Wibru decision, represents an example of liability that a shareholder can have due to advertisements or coincidental communications. In that case, the court opined that the advertisement and project announcement letters created a legitimate expectation for the consumers who engage in a contractual relationship with a subsidiary, and the parent should be liable for the breach of trust in corporate groups. *See* Hasan Pulasli, *Turk Ticaret Kanunu Tasarisina Gore Sirketler Toplulugunun Temel Nitelikleri ve Hakim Sirketin Guven Sorumlulugu* [*Companies According to Turkish Commercial Law: The Basics of the Community and the Rights of the Company Trust Responsibility*], GAZI UNIVERSITESI HUKUK FAKULTESI DERGISI [GAZI UNIV. FACULTY L.J.] C. XI, Sa.1-2 270-75 (2007), *available at* http://webftp.gazi.edu.tr/hukuk/dergi/11_11.pdf.

communication that is not made as a part of the securities law requirements would not have this effect.[104] Although these might be used as extrinsic evidence that would establish the basis of the implied terms of the corporate contract in close corporations, granting their usage in the context of publicly traded corporations would greatly damage the integrity of the market. After all, in theory, investors make their investment decisions relying on the information disclosed in accordance with securities law because only these are given a legal effect and added as terms to their contracts with the corporation.[105]

VII. CONCLUSION

The construction of the involuntary dissolution statute is not incompatible with the nature of a publicly traded corporation. However, its compatibility depends on the approach used to interpret the statute. An involuntary dissolution statute would effectively remedy and restrain opportunistic behavior in the publicly traded corporation only if the statute is construed through a convenient doctrinal basis and analysis, such as the one suggested in this note.

Although the shareholder oppression is not the only ground for involuntary dissolution and so the discussions of this note is inconclusive, evaluating the issue through this most common ground proves that the policy considerations behind the involuntary dissolution statute is equally applicable to publicly traded corporations as well. Accordingly, this note claims that there is no need for judicial reluctance to apply the involuntary dissolution statute to these corporations. Shareholder opportunism is an institutional reality and corporate law should not be ignorant of the features, such as the involuntary dissolution law, the law inherently possesses.

104. However, this does not mean that these communications do not give rise to civil and criminal liability under securities laws' market manipulation rules.

105. For instance, under the U.S. securities law, Regulation Fair Disclosure, 17 C.F.R. §. 243.100, which "is aimed at prohibiting the selective disclosure of information in order to promote the full and fair disclosure of information to the public" (S.E.C. v. Siebel Systems, Inc., 384 F. Supp. 2d 694 (2005)), would support this qualification in cases such as disclosures made through social media platforms (Press Release, *SEC Says Social Media OK for Company Announcements if Investors Are Alerted*, U.S. Sec. & Exchange Comm'n (Apr. 2, 2013), https://www.sec.gov/news/press-release/2013-2013-51htm.