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## Ignoring Reality: Iowa Supreme Court Decides Case Involving “Oppression” by Majority Shareholder in Farm Corporation

-by Neil E. Harl\*

On June 14, 2013, the Iowa Supreme Court released an opinion dealing with what constitutes “fairness” among minority and majority shareholders in the setting of a second generation family farm corporation which had experienced disagreements between cousins in the second generation.<sup>1</sup> The facts of the case indicate that the parties had essentially ignored stock valuation for nearly 30-years while the value of assets was reaching record levels.<sup>2</sup> The minority shareholder succeeded in getting an adverse decision in the District Court reversed and remanded for further proceedings.

### The facts of the case

The facts of the case were that two brothers, who had farmed together, set up a farm corporation (with 1736 acres at the time) with minimal attention to the problems of stock valuation and the inevitable problem of succeeding generations all of whom are unlikely to continue in farming (or even want to continue ownership of farm assets). For the ownership of any farming operation, it is necessary for each generation to buy out the stock of those not wanting to be involved in farming or the ownership in a few generations becomes unmanageable. Moreover, different views as to stock valuation are likely to emerge unless there is a market for the stock to provide a value. Most commercial firms fall into the latter category but few farming operations have been able to rely on markets to handle the determination of fair market value.

Over the years, the stock ownership developed into a majority owner (the son of one of the two brothers) and a minority owner (a son of the other brother). After several years of intra-family skirmishing over stock values and other matters, the minority owner sued the corporation and its majority shareholder, alleging illegal, oppressive, malicious and fraudulent acts by the majority shareholder (and indirectly by the corporation). More precisely, the allegation was that the acts of the majority shareholder had resulted in waste of the corporation’s assets which amounted to a breach of fiduciary duty with relief requested in the form of dissolution of the corporation, payment of corporate dividends or a buy-out of the minority stock interest at a fair value.

The corporate bylaws had been amended in 1984 to include a buy-out provision (first option) and, unless a different price was agreed upon, the value was set at “book

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value per share of the shareholder's equity interest in the corporation as determined by the Board of Directors, for internal use only, as of the close of the most recent fiscal year."<sup>3</sup> The amendment in 1984 set a book value of \$686 per share. Footnote 1 of the case opinion indicates that there was no evidence of a different book value after that date. The record shows no dividends had ever been declared. Over a period of many years, the shareholders feuded over valuations and terms of any buy-out of the minority interest with no resolution.

#### The court decisions

The District Court dismissed the case following presentation of the plaintiff's case on the grounds that a five-year statute of limitations had expired. On appeal to the Iowa Court of Appeals, the court reversed and remanded for trial. At the trial, the District Court found no "oppressive" conduct.

The Iowa Supreme Court, after a review of the authorities<sup>4</sup> held that ". . . majority shareholders act oppressively when, having the corporate financial resources to do so, they fail to satisfy the reasonable expectations of a minority shareholder by paying no return on shareholder equity while declining the minority shareholder's repeated offers to sell shares for fair value."<sup>5</sup> The District Court decision was reversed and remanded "for further proceedings consistent with this opinion."<sup>6</sup>

#### Commentary

The decision has already generated a great deal of commentary but it is difficult to be critical of the court's decision. The facts of the case cried out for relief and the reasoning of the court is consistent with the progressive trend to recognize the position of economic disadvantage inherent in minority-majority power struggles.

However, the real culprit was the complete failure of the controlling parties to address – (1) the need for an annual determination of stock value; (2) the pay-out terms (immediate or deferred) of a properly drafted buy-sell or first option agreement; (3) a fall-back provision if valuations are not agreed upon each year; and (d) the situation if the majority owner or owners have the power to undervalue the stock consistently. The latter relates

to the percentage vote required to set annual values. Without a ready market for ownership interests, as is the case in farming and ranching, these steps are critical in every entity created to hold farmland or to carry on a farming or ranching operation.

Some have commented that there should have been more attention given to the intent of the two brothers who set up the corporation. The fact that their decisions (or lack of action) led to untold family turmoil for three decades substantially undercuts any inclination to attempt at this late date to ascertain what their intent might have been.

In short, the problem lies in the planning process. The Iowa Supreme Court is to be congratulated in providing a path to resolution of the conflicts that have festered for so long.

#### ENDNOTES

<sup>1</sup> Baur v. Baur Farms, Inc., No. 11-0601, June 14, 2013. See generally 6 Harl, *Agricultural Law*, Ch. 51, App. 51B, pp. 16-20 (2013).

<sup>2</sup> See Duffy, "Iowa Land Value Survey," Iowa Agriculture and Home Economics Experiment Station, Iowa State University, Dec. 2012 (average value of \$8,296 per acre as of November of 2012, representing an increase of 23.7 percent over 2011).

<sup>3</sup> Baur v. Baur Family Farms, Inc., No. 11-0601 (Iowa Sup. Ct., June 14, 2013).

<sup>4</sup> See, e.g., *Nw. Inv. Corp. v. Wallace*, 741 N.W.2d 782, 787-788 (Iowa 2007) (Iowa Supreme Court indicated its disapproval of share valuations incorporating a discount for a minority interest in a corporation).

<sup>5</sup> Baur v. Baur Family Farms, Inc., No. 11-0601 (Iowa Sup. Ct., June 14, 2013).

<sup>6</sup> *Id.*

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## CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

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### BANKRUPTCY

#### GENERAL

##### EXEMPTIONS

**CHILD TAX CREDIT.** The debtor claimed a portion of a federal income tax refund attributable to the child tax credit as exempt public assistance payments under Maine Stat. § 4422(13(A)). The trustee objected, arguing that the credit was not a refundable credit; therefore, the credit was meant only to reduce the overall tax on the debtor and not provide public assistance. The

Bankruptcy Court agreed and held that the portion of the refund attributable to the child tax credit was not eligible for the Maine public assistance exemption. *In re Tetrault*, 2013-2 U.S. Tax Cas. (CCH) ¶ 50,435 (Bankr. D. Maine 2013).

#### CHAPTER 12

**JURISDICTION.** The debtor filed a Chapter 12 case. During the case the debtor filed a complaint against a non-party in the bankruptcy case, alleging trespass, nuisance, negligence, and negligence per se arising out of defendant's use of the debtor's land. The debtor's complaint acknowledged that the action might not be a core proceeding in the bankruptcy and consented to the Bankruptcy Court's issuance of a judgment. Eight months later, the debtor filed a motion in the District Court to remove the action