

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

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APPEAL FROM SPARTANBURG COUNTY
Court of Common Pleas

SC Court of Appeals

J. Mark Hayes, II, Circuit Court Judge

Case No. 2008-CP-42-3397

Quentin S. Broom, Jr., Respondent,

v.

Ten State Street, LLP, Timothy D. Scranton,
Mark Broadwater, and H. Hugh Andrews, Defendants,

Of whom

H. Hugh Andrews, Individually
and on behalf of Tri-Star
Communications, Inc. is the, Appellant.

v.

Quentin S. Broom, Jr., Third-party Defendant.

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STATEMENT OF ISSUES ON APPEAL

- I. If a Corporation Only Has Two Shareholders and If One Suspects the Other Has Been Engaged in Self-dealing, Whether the Complaining Shareholder May Sue the Alleged Wrongdoer Directly, as Opposed to Bringing a Derivative Suit on Behalf of the Company.
- II. If Hugh Andrews Was Required to Bring His Claims in a Derivative Suit on Behalf of His Company, Whether the Circuit Court Erred in Dismissing the Claims Without Allowing Andrews the Opportunity to Amend Them.

STATEMENT OF THE CASE

This lawsuit arises out of a dispute between business partners. Hugh Andrews and Quentin Broom are the owners of Tri-Star Communications. They own equal shares in the company. At some point, says Andrews, Broom began to secretly pay himself an excessive salary. Broom also allegedly sold-off Tri-Star's inventory over Andrews' objection.

The primary issue in this appeal is whether Andrews may pursue a lawsuit directly against Broom for this alleged wrongdoing, or whether he must instead bring a shareholder derivative suit, which would be in Tri-Star's name. This question is significant because it implicates the pleading rules for derivative suits, and it also governs whether any money damages will go directly to Andrews, as opposed to Tri-Star.

Broom initiated this suit in September of 2005. In general, he alleged that he and Andrews were partners in several business entities and that Andrews conspired with a South Carolina law firm to reduce the value of some of Broom's business interests. Broom also alleged that he had been improperly charged for legal work done for Andrews individually. Broom named Andrews, the law firm, and two men who worked at the firm as defendants. See (Complaint). Andrews answered the complaint with a general denial. See (Answer).

In May of 2006, Andrews asked to amend his answer. In the amended answer, Andrews alleged several counterclaims against Broom. He captioned most of them both as counterclaims and as third-party claims, and he purported to bring the third-party claims on Tri-Star's behalf. See (R.p. ___) (the motion to amend) and (R.p. ___) (the amended answer).

In September of 2006, Broom filed a reply to the amended answer. The reply alleged several defenses to the counterclaims and third-party claims, but none of those defenses are relevant to the issues in this appeal. (Broom's Reply to Andrews' Counterclaims).

In September of 2011, Broom filed a motion to dismiss the counterclaims and the third-party claims. The grounds given to support the motion were that Andrews had not complied with the procedure for bringing a derivative suit; specifically, he never asked Tri-Star's board of directors to investigate any alleged wrongdoing, he never claimed such a request would be futile, he did not verify his counterclaims, and he did not allege that he could fairly represent the interests of Tri-Star's other shareholders. See (Motion to Dismiss).

Andrews opposed this motion, arguing that his claims were individual claims against Broom and that the rules for a derivative lawsuit did not apply. He also argued that if his claims fell technically within the definition of derivative claims, the court should follow the lead of several other jurisdictions that have allowed derivative claims to proceed as direct claims when the corporation in question is a small corporation with only a few shareholders. See (Memo in Opp. to the Mot. to Dismiss) (Andrews' memo in opposition).

In October of 2011, the circuit court conducted a hearing on the motion to dismiss. Shortly after the hearing, the court issued a form order that granted the motion. (R.p. ___). The court confirmed this ruling in a written order filed November 1, 2011. (R.p. ___).

The circuit court reasoned that all of Andrews' claims sought recovery for the misappropriation of corporate property. In the circuit court's view, such claims belonged in a derivative suit. *Id.* at 5.

The circuit court also recognized that Andrews had claimed Broom caused Tri-Star to be unable to pay a debt the corporation owed Andrews personally, but the court dismissed this claim because Andrews did not name Tri-Star as a defendant. *Id.* at 6.

The circuit court declined Andrews' request to relax the rule that derivative claims belong to the corporation and not to an individual shareholder. The court wrote that South Carolina courts had "rejected" this principle in the past and that "[t]his record" did not support the application of the exception some other jurisdictions have recognized.

Andrews asked the court to reconsider both the form order and the written order of dismissal. See (Supp. Mot. & Memo). He also requested leave to amend his answer a second time for the purpose of supplementing the factual allegations. See (Second Mot. to Amend Ans.). The court conducted a hearing on these motions in December of 2012.

On January 14, 2013, the circuit court issued a form order denying the motions to reconsider. (Jan 14, 2013 Form 4 Order). On February 1, 2013, the court issued a written order confirming this ruling. (Feb. 1, 2013 Order). Neither order expressly mentioned Andrews' motion to amend his answer, but the effect of the orders was to deny the motion.

On February 7, 2013, Andrews received written notice of the entry of the final order dismissing his claims. On March 8, 2013, Andrews initiated this appeal.

There is much more to the procedural history of this case, but this description is limited to that which is relevant to this appeal.

ARGUMENT

The first reason the Court should reverse is that Mr. Andrews' claims are not derivative. A hallmark of a derivative claim is that there is a class of shareholders who have suffered similar injuries as a result of the alleged wrongdoing. Such shareholders are "similarly situated," and one reason the law requires a derivative suit is that such a suit ensures all of the injured shareholders will enjoy the appropriate proportion of any recovery.

No one is similarly situated with Hugh Andrews. If Broom was stealing from Tri-Star, the only person he was stealing from was Andrews. When a corporation has only two shareholders, one's self-dealing necessarily correlates to the other's unique injury.

The second reason this Court should reverse is that the rules for derivative lawsuits cannot reasonably apply to these circumstances; the fact that this company has two equal owners results in too many oddities. Chief among these is the fact that it is impossible to ascertain Tri-Star's position in the case — one 50% owner thinks the company should sue the other. This is a classic case for relaxing the rules; applying them leads to absurd results. If the rules apply, Andrews must ask Broom to sue himself, Andrews must claim he can represent the interests of injured shareholders (he is the only one), and any money damages must go to Tri-Star, where they will be locked in a tug-of-war between equal shareholders.

The last reason this Court should reverse is that the law generally grants a party the chance to amend his pleadings if they are dismissed and the statute of limitations has expired. Again, this is a classic case for applying that principle. If the only defect in Mr. Andrews' claims is that he did not specifically state things that are obvious, he should be given the opportunity to amend his answer. In these circumstances, outright dismissal is unjust.

I. The Circuit Court Erred When it Held That Hugh Andrews Could Not Directly Sue His Business Partner for the Partner's Alleged Self-dealing.

The Court should hold that when a defunct corporation has two shareholders and one wishes to sue the other for alleged self-dealing, it is possible for those claims to be direct claims that belong to the complaining shareholder individually. Hugh Andrews is not really complaining about the depreciation of his stock value. Because Tri-Star is both defunct and caught between two shareholders who cannot agree, the company cannot function and effectively no longer exists. At its core, this is a dispute between Andrews and Broom individually; the claim is that when Broom stole from Tri-Star, he was stealing from no one else but Andrews. This view is supported by existing South Carolina law, and it is also supported by authority from other jurisdictions, which should be persuasive.

a. A Derivative Claim Involves a Corporate Injury; a Direct Claim Involves an Individual Injury.

If a stockholder brings a lawsuit concerning corporate mis-management, the stockholder is normally only a nominal party. Instead, the corporation is typically the real party in interest. The Supreme Court's decision in *Latimer v. Richmond & D.R. Co.* contains an early recognition of this principle, see 39 S.C. 44, 51-52, 17 S.E. 258, 260-61 (1893) (the "right of action" for mis-management "exists in the corporation itself"), and South Carolina courts have reiterated these principles on several other occasions. See, e.g., *Clearwater Trust v. Bunting*, 367 S.C. 340, 351, 626 S.E.2d 334, 339 (2006); *Davis v. Hamm*, 300 S.C. 284, 288, 387 S.E.2d 676, 678 (Ct. App. 1989); *Johnson v. Baldwin*, 221 S.C. 141, 149, 69 S.E.2d 585, 588 (1952).

Derivative suits are so-named because the plaintiff's standing derives from his status as a stockholder. The core of a derivative complaint thus does not allege a direct injury to the individual plaintiff; instead, it seeks redress for an injury to the corporation and, by extension, to *all* shareholders. This injury, the suit alleges, will not otherwise be redressed because the corporation's governing body is refusing to redress it. See *Jones v. H. F. Ahmanson & Co.*, 460 P.2d 464, 470 (Cal. 1969) (one definition of a derivative suit).

Special pleading rules apply to derivative suits because they represent a challenge to the principle that a corporation is primarily managed by its directors, not its shareholders. These rules include the requirement that the complaining shareholder verify the allegations of wrongdoing and describe the action he or she has taken to request that management remedy the problem. See Rule 23(b)(1), SCRCPP; see also S.C. Code Ann. § 33-7-400 (2006). This Court explained the rationale for these rules in *Carolina First Corp. v. Whittle*, 343 S.C. 176, 185-88, 539 S.E.2d 402, 407-09 (Ct. App. 2000), and another jurisdiction has explained that state's rules, which are similar to South Carolina's, as being "designed to create a balanced environment" that deters wasteful litigation based only a suspicion of wrongdoing, but permits litigation if a plaintiff can raise reasonable doubt about whether the people who control the corporation have abdicated their duties. *Brehm v. Eisner*, 746 A.2d 244, 255 (Del. 2000) (quoting *Grimes v. Donald*, 673 A.2d 1207, 1216-17 (Del. 1996)).

When, however, corporate action results in a loss that is unique to one particular shareholder, a claim related to that loss is not derivative. This is because the complaining shareholder's injury is not common to other shareholders — no one else has suffered similar harm as a result of the conduct at issue.

The Supreme Court's decision in *Hite v. Thomas & Howard Co. of Florence, Inc.* concerned one such scenario. There, the owner of 1/3 of the business alleged that his percentage of ownership had been reduced as a result of the majority owner's self-dealing. See 305 S.C. 358, 360-61; 409 S.E.2d 340, 341-42 (1991).

Hite was partially overruled by *Huntley v. Young*, which held that the denial of a motion to dismiss is not immediately appealable, see 319 S.C. 559, 560, 462 S.E.2d 860, 860-61 (1995), but nothing suggests that *Hite*'s discussion of corporate law is invalid.

This Court's decision in *Brown v. Stewart* references, but does not apply, another feature of this principle. *Brown* instructs that a complaining stockholder has an individual claim if the wrongdoer owes him a fiduciary duty and if recovery to the corporation will not provide him with full relief. 348 S.C. 33, 50, 557 S.E.2d 676, 685 (Ct. App. 2001).

The features that distinguish a derivative claim from a direct claim are easy enough to describe. Indeed, almost every case states them the same way. But describing the rules is one thing. Faithfully applying them is something else.

b. It Can Be Difficult to Distinguish a Derivative Claim from a Direct Claim, and That Difficulty Increases as the Number of Shareholders Shrinks.

A variety of jurisdictions have recognized that a single series of events can give rise to both direct and derivative litigation. *Norman v. Nash Johnson & Sons' Farms, Inc.*, 537 S.E.2d 248, 253 (N.C. Ct. App. 2000); *Bagdon v. Bridgestone/Firestone, Inc.*, 916 F.2d 379, 381 (7th Cir. 1990); *Sutter v. General Petroleum Corp.*, 170 P.2d 898, 901 (Cal. 1946). In the same vein, cases from several jurisdictions have recognized that as the number of the shareholders in a corporation diminish, the difficulty of applying the direct/derivative

distinction increases. One common illustration includes reciting that while a corporation with a large number of shareholders generally has a clear distinction between ownership (the shareholders) and management (the board), this is often absent in a corporation with a very small number of shareholders. Instead, the shareholders are likely the same individuals who manage the business. See, e.g., *Durham v. Durham*, 871 A.2d 41, 45 (N.H. 2005); *Aurora Credit Servs., Inc. v. Liberty West Dev., Inc.*, 970 P.2d 1273, 1280-81 (Utah 1998).

Another common illustration, closely related to ownership, is that corporations with a small number of shareholders may operate more like partnerships than corporations. *Johnson v. Gilbert*, 621 P.2d 916, 918 (Ariz. Ct. App. 1980); *Donahue v. Rodd Electrotype Co. of New England*, 328 N.E.2d 505, 512 (Mass. 1975). Several secondary authorities explore these issues in detail. See, e.g., Allan B. Cooper et al., *Too Close for Comfort: Application of Shareholder's Derivative Actions to Disputes Involving Closely Held Corporations*, 9 U.C. Davis Bus. L.J. 171 (2009); see also F. Hodge O'Neal & Robert B. Thompson, *O'Neal's Close Corporations*, §§ 1.02 & 9.22 (3d ed. 1994).¹

This should not be taken as an invitation to ignore the corporate form or disregard the fact that business partners have chosen to conduct business through a corporation. Far from it. Instead, this discussion observes the reality that unlike large corporations, corporations with a small number of shareholders often have no functional distinctions between ownership and management. Consider Tri-Star as an example. This corporation does not appear to have had a board of directors, and with ownership divided 50/50 between Broom and

¹Relevant sections in a more recent version of the *O'Neal* treatise include §§ 1.02, 9.2, and 9.26. O'Neal & Thompson, *O'Neal's Close Corporations* (rev. 3d ed. 2012)

Andrews, the corporation's management was tied directly to its ownership. Undoubtedly, there were some actions Tri-Star could not take if Broom and Andrews disagreed.

c. Faithfully Applying These Principles Leads to the Conclusion That Mr. Andrews' Claims Are Direct.

One defining characteristic of a derivative claim is that there is a class of shareholders who are similarly situated with the individual plaintiff. Because the injury is to the corporation in a derivative case, the injured shareholders find themselves in the same boat.

But when a company has only two shareholders and one alleges that the other has stolen from the business, the shareholders are *not* similarly situated. In this situation, the complaining shareholder has alleged a loss that is unique. This rule should control this case.

The complaining shareholder's loss is unique because he is the only party that has actually suffered a reduction in the value of his interest. If this case were a purported class action, Mr. Andrews would be a class of one. The alleged wrongdoer (Broom) has not suffered any injury, because while his stock may have decreased in book value, he has enjoyed the fruit of his alleged wrongdoing. This illustrates the absurdity of one of Rule 23's requirements and is one reason why that rule cannot apply: Rule 23 instructs that a plaintiff may not maintain a derivative suit if he does not fairly represent the interest of similarly situated shareholders. Here, there are no similarly situated shareholders. Other than Andrews, the only shareholder is Broom, and Broom is the alleged wrongdoer and defendant.

Other jurisdictions have applied this analysis to cases presenting similar circumstances. *Norman*, 537 S.E.2d at 260-61; *Noakes v. Schoenborn*, 841 P.2d 682, 687 (Or. Ct. App. 1992); *Yanow v. Teal Indus.*, 422 A.2d 311, 321-22 (Conn. 1979); *Funk v.*

Spalding, 246 P.2d 184, 187 (Ariz. 1952). This reasoning should be persuasive. The reason Mr. Andrews' claims should go forward is not because Tri-Star has not been injured — on paper, it has. The critical fact is that as compared to all other *shareholders*, Andrews is only shareholder bearing the alleged loss. O'Neal & Thompson, *supra* p.8, at §9.22 pp.115-117.

There do not appear to be any South Carolina cases illustrating a similar application of these principles, but that can only be because similar circumstances have not previously been present. On a number of occasions, South Carolina has recognized the “separate and distinct” rule — the rule allowing a direct suit against a manager if misconduct has caused a particular loss to an individual stockholder. *Hite*, 305 S.C. at 361-62, 409 S.E.2d at 342; *Ward v. Griffin*, 295 S.C. 219, 221, 367 S.E.2d 703, 704 (Ct. App. 1988). The general theory of Andrews' claims is that Broom has mis-managed the business, paid himself an excessive salary, and sold all of the inventory over Andrews' objection. While these would no doubt be derivative claims if Tri-Star was a large corporation with a clear division between ownership and management, it should be equally obvious that they are “separate and distinct” claims in the context of a corporation with only two owners. In such a situation, one shareholder's self-dealing will necessarily correspond to the other shareholder's unique loss.

None of this State's previous “close corporations” cases have presented this scenario.

Todd v. Zaldo involved a corporation with three shareholders, one of whom was not a party to the suit. The complaining party in *Todd* indicated that he believed his damages were personal because “my corporation is my money,” and this Court wrote in *Todd* that while this shareholder contended that the business operated as a partnership, “[the] record” did not support that contention. 304 S.C. 275, 403 S.E.2d 666 (Ct. App. 1991).

The present case cannot be fairly comparable. For one thing, there is no *record* to use in evaluating how this business operated. This Court's decision in *Todd* was the result of an appeal from a jury verdict, but in the present case, there not has been a trial. Here, the circuit court based its decision solely on the pleadings.

Other cases like *Brown v. Stewart* and *Clearwater Trust v. Bunting* are different for similar reasons. Like *Todd*, *Brown* presented a situation where the plaintiff's alleged injury was no different in character from that of a shareholder who was not a party to the lawsuit. *Brown*, 348 S.C. at 51, 557 S.E.2d at 685. Thus, the plaintiff's injury was not unique. In *Clearwater Trust*, there is no substantive discussion of whether any claims could have been brought directly. The court's opinion is silent as to whether all shareholders were parties and contains only a passing reference to the fact that in the normal case, a breach of fiduciary duty claim belongs in a derivative suit. 367 S.C. at 351, 626 S.E.2d at 339.

But when a business has only two shareholders, and when one alleges that the other has stolen from the business, all of the shareholders are not similarly situated. Because a complaining shareholder like Mr. Andrews has alleged a loss that is unique, this Court should reverse the circuit court's decision that he does not have standing to pursue his claim for corporate mis-management directly.

d. Even If Mr. Andrews' Claims Were Truly for a Corporate Harm, the Court Should Nevertheless Allow Him to Plead Those Claims Directly.

On at least four previous occasions, South Carolina's appellate courts have acknowledged that when the corporation in question has only a few shareholders, some foreign jurisdictions have applied an exception to the general rule that derivative claims

always belong to the corporation. From the oldest to the most recent, those cases are *Davis v. Hamm*, *Todd v. Zaldo*, *Babb v. Rothrock*, and *Brown v. Stewart*. None of these cases apply this exception, and none of them reject this exception. Instead, they each observe that the circumstances of the case in question were not appropriate for relaxing the rule that claims for corporate injuries are derivative claims. These cases are listed in the Appendix at the end of this brief, along with a brief paragraph describing each case's reasoning.

The American Law Institute proposed this exception in 1992, and one authority reported that as of 2009, 37 states had considered the exception with 16 states choosing to adopt it. Cooper et al., *supra* p.8, at 175, 182. The rationale of this exception is that when the purposes of a derivative suit are absent, proceeding derivatively forces litigants to comply with formalities that are cumbersome and futile. See *Principles of Corporate Governance: Analysis and Recommendations*, A.L.I., § 7.01(d), cmt. (e) (1994); *Durham*, 871 A.2d at 46.

For example, the demand requirement is designed to give the board of directors the first opportunity to redress a grievance. *Allison v. Gen. Motors Corp.*, 604 F. Supp. 1106, 1112 (D.Del. 1985). One jurist on the Seventh Circuit has described that “[t]he persuasive rationale for the demand requirement is that it allows directors to make a business decision about a business question: whether to invest the time and resources of the corporation in litigation.” *Starrels v. First Nat. Bank of Chicago*, 870 F.2d 1168, 1173 (7th Cir. 1989) (Easterbrook, J., concurring).

Nobody could seriously contend that there would be any point in asking Mr. Broom, in his capacity as a 50% owner of Tri-Star, to vote to sue himself. No one can expect Andrews to win the grant of that request.

Derivative cases often reference the need to raise doubts about whether the corporation's board can objectively decide whether to investigate the grievance or pursue a lawsuit. Many of these cases focus on asking if there is a reasonable question whether the challenged decision was tainted by board members looking out for their own self-interest. *Aurora Credit Servs.*, 970 P.2d at 1280; *Allison*, 604 F. Supp. at 1114, 1121 (1985).

That point has an interesting application to the circumstances of the present case. Here, there are *no* disinterested members of this corporation — one shareholder is the plaintiff, the other shareholder is the defendant. Tri-Star's official position is impossible to ascertain — it is a corporation in limbo. One 50% shareholder believes the corporation ought to sue the other shareholder. Not surprisingly, the alleged thief disagrees.

There are really two parts to the question whether to apply American Law Institute's proposed exception. The first is a pleading question. The second is a recovery question.

The pleading question should be easy to answer. The rules of civil procedure are designed to secure just and speedy outcomes, see Rule 1, SCRCP, and it seems odd to apply a rule for "class actions" to a lawsuit between 2 people. See Rule 23, SCRCP. Moreover, requiring Andrews to ask Broom to sue himself is, frankly, foolish. Decisions from other jurisdictions have recognized the futility of such a request. *Anderson v. Clemens Mobile Homes, Inc.*, 333 N.W.2d 900, 904 (Neb. 1983); *Funk*, 246 P.2d at 186. This point should not be controversial. When one partner alleges that the other is the wrongdoer, the claim for relief does nothing if it does not allege demand futility.

The Supreme Court of Texas took an interesting view of this question. It reasoned that when there is a derivative suit on behalf of a close corporation and all of the remaining

shareholders are named as defendants; that state's special pleading rules are deemed satisfied as a matter of law. *Eye Site, Inc. v. Blackburn*, 796 S.W.2d 160, 162-63 (Tex. 1990).

The recovery question posed by the ALI's exception is the question whether the money damages from the lawsuit should go to the corporation and its treasury, as opposed to the complaining shareholder personally. This question is harder to answer, and it may be impossible to answer it until later in the litigation. It may take discovery and a trial to determine whether the particular corporation has outside creditors who need to be protected or whether equity otherwise favors the corporation itself getting the recovery.

Concern for creditor's rights drove our Supreme Court's decision in *Babb*, but *Babb* differs from the present case because the Supreme Court had the benefit of reviewing a record that had been developed by a trial. 303 S.C. 462, 463, 401 S.E.2d 418, 419 (1991). This illustrates the error of the summary manner in which the circuit court rejected the ALI exception in the present case. The circuit court wrote that the "record" in this case did not support the application of the exception, see (Order, p.8), but at the 12(b)(6) stage, there is no substantive record. No one's *pleadings* will ever prove whether creditors need to be protected or whether the business, though a corporation on paper, ran as a partnership.

The argument for never allowing derivative suits to be brought directly is that the law prefers predictability and that a clean rule allows parties to avoid squabbles at the beginning of a suit. A well-written articulation of this reasoning can be found in the Seventh Circuit's decision in *Bagdon v. Bridgestone/Firestone, Inc.*. See 916 F.2d at 383-84.

The biggest problem with this view is that predictability proves to be an empty promise. Everyone agrees that corporate action can create both derivative and direct liability,

and there are plenty of cases, in this jurisdiction and others, that focus only the question whether the claims in a given case are truly derivative or direct. Predictability is not the ultimate goal — the law exists to vindicate the purposes behind the rules, not the rules themselves. One of the ultimate goals here is to protect the principle that a corporation is generally governed by its directors. Another goal is to limit the court system's role to adjudicating legitimate disputes. This is why derivative suits exist, and if these reasons do not exist in a particular case, the suit cannot legitimately be called derivative.

Hugh Andrews may not win any of his claims, but it ought to be obvious that he and his partner are embroiled in a non-trivial controversy. These men are 50/50 owners of the company in question, and unless they have a change of heart, no one but the court system can settle their dispute. This Court should accordingly reverse the decision dismissing Andrews' claims. The Court should explain that the requirements of Rule 23 either do not apply or have been functionally satisfied by the fact that Andrews named the only other shareholder as a defendant, and the Court should defer the question of whether the damages should be paid to Andrews personally, as opposed to Tri-Star, until after a record has been developed.

II. The Circuit Court Erred When it Dismissed Mr. Andrews' Claims Without Giving Him an Opportunity to Amend His Pleadings.

One of Andrews' claims arose out of a debt that Tri-Star allegedly owed him personally, and the circuit court dismissed this claim on the grounds that Andrews did not name Tri-Star as a defendant. See (Order, p.6).

In *Ward v. Griffin*, this Court wrote that “[a] stockholder may individually sue corporate directors, officers, or other persons when he has sustained a loss separate and

distinct from that of other stockholders generally.” 295 S.C. at 221, 367 S.E.2d at 704 (quoting 19 Am. Jur. 2d *Corporations* § 2245 (1986)). The circuit court’s order offers no authority for the proposition that in order to maintain this claim, Andrews had to sue Tri-Star instead of the officer who allegedly caused the debt to go unpaid. The reason why no authority is cited is that the proposition is not correct.

In *Spence v. Spence*, the Supreme Court instructed that “[w]hen a complaint is dismissed under Rule 12(b)(6) . . . [t]he plaintiff in most cases should be given an opportunity to file and serve an amended complaint.” 368 S.C. 106, 129, 628 S.E.2d 869, 881 (2006). *Spence* was a real estate case, and the issue of amended pleadings arose because the plaintiff asked for the chance to file an amended complaint before the trial court dismissed some of the parties with prejudice. *Id.* at 128, 628 S.E.2d at 880. The Court held that when the statute of limitations has expired, an appellate court which affirms a dismissal should grant a reasonable opportunity to amend the complaint if the aggrieved party presented additional allegations or a different theory of recovery which might state a claim upon which relief could be granted. *Id.* at 130, 628 S.E.2d at 881-82. The essence of this holding is that when the plaintiff shows that he or she can cure the defect that led to dismissal, the court should modify the dismissal to be without prejudice.

None of Broom’s arguments were directed to the merits of Andrews’ suit. Instead, they were all directed to the manner and sufficiency of pleading. Derivative cases inside and outside South Carolina reference parties having the opportunity to amend their pleadings. See *Carolina First Corp.*, 343 S.C. at 183, 539 S.E.2d at 406; *Allison*, 604 F.Supp. at 1119. Yet, when Andrews sought to amend his complaint, that request was denied.

outside South Carolina reference parties having the opportunity to amend their pleadings. See *Carolina First Corp.*, 343 S.C. at 183, 539 S.E.2d at 406; *Allison*, 604 F.Supp. at 1119. Yet, when Andrews sought to amend his complaint, that request was denied.

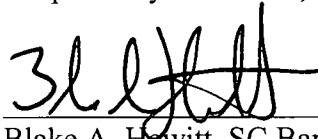
All of this has been so wasteful. Broom knows why Andrews never made a demand on Tri-Star's board of directors — there is no board. Broom knows why Andrews did not ask him to sue himself — the request would obviously have been futile. Broom knows that Andrews cannot and will not adequately represent the interests of all Tri-Star shareholders — Broom is the only other shareholder and he is the defendant. All of this is clear when everyone's pleadings are considered together, but if Andrews must specifically allege this in order for his claims to survive, *Spence* instructs that he should have that opportunity.

CONCLUSION

This Court should reverse the circuit court's decision and remand this case for proceedings consistent with the Court's decision.

June 10, 2013

Respectfully submitted,



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APPENDIX

Davis v. Hamm,

300 S.C. 284, 387 S.E.2d 676 (Ct. App. 1989)

Appeal from damages award after a bench trial. The award was in favor of a former stockholder and against a corporate director. This Court noted some of the foreign decisions applying special rules to derivative suits involving close corporations, but ultimately declined to apply the rule because the plaintiff was not a stockholder at the time she brought the case. This was a classic derivative suit. The claim was that one of the president's decisions had caused a reduction in the price of the business' stock.

Todd v. Zaldo,

304 S.C. 275, 403 S.E.2d 666 (Ct. App. 1991)

Appeal of a jury verdict in favor of the majority stockholder and against one of the two minority stockholders. The third stockholder was not a party to the lawsuit. This Court wrote that there was "no indication in the record the companies operated as *de facto* sole proprietorships or partnerships," and that the record did not present "a factual scenario" for "ignoring" the fact that the claim for mis-management was a corporate claim.

Babb v. Rothrock,

303 S.C. 462, 401 S.E.2d 418 (1991)

Appeal from a master's judgment on claims for set-off and mis-appropriation in a suit involving the 4 shareholders of a bankrupt corporation. The Supreme Court dismissed the case, relying on the general rule that individual shareholders may not sue corporate directors for losses suffered by the corporation. The court rejected the application of special rules for close corporations, writing "[a]ssuming we should adopt the [] exception . . . the record discloses the presence of a reason compelling a derivative action, to wit, protection of corporate creditors."

Brown v. Stewart,

348 S.C. 33, 557 S.E.2d 676 (Ct. App. 2001)

Appeal of a jury verdict in favor of an individual shareholder. This Court wrote that the plaintiff "[could] not rely on [the exception for close corporations]," because allowing the plaintiff to maintain an individual action would not protect the interests of other shareholders who were not parties to the suit.

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM SPARTANBURG COUNTY
Court of Common Pleas

J. Mark Hayes, II, Circuit Court Judge

Case No. 2008-CP-42-3397

RECEIVED
JUN 10 2013
SC Court of Appeals

Quentin S. Broom, Jr., Respondent,

v.

Ten State Street, LLP, Timothy D. Scranton,
Mark Broadwater, and H. Hugh Andrews, Defendants,

Of whom

H. Hugh Andrews, Individually
and on behalf of Tri-Star
Communications, Inc. is the, Appellant.

v.

Quentin S. Broom, Jr., Third-party Defendant.

**DESIGNATION OF MATTER
TO BE INCLUDED IN THE RECORD ON APPEAL**

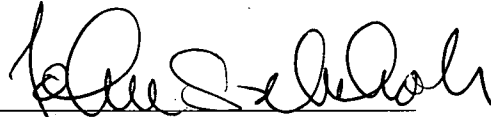
1. Form 4 of October 7, 2011;
2. Order of November 1, 2011;
3. Form 4 Order of January 14, 2013;
4. Order of February 1, 2013;
5. Complaint;
6. Answer;
7. Andrews' Motion to Amend Answer;
8. Andrews' Amended Answer;
9. Broom's Reply to Andrews' Counterclaims;
10. Broom's Motion to Dismiss;

11. Andrews' Memo in Opposition to the Motion to Dismiss;
12. Andrews' Supplemental Motion to Reconsider;
13. Andrews' Memo in Support of Supplemental Motion to Reconsider;
14. Andrews' Second Motion to Amend Answer.

I certify that this designation contains no matter which is irrelevant to this appeal.

June 10, 2013

Respectfully submitted,



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PROOF OF SERVICE

The undersigned hereby certifies that on the date indicated below she served counsel for the Respondent with a copy of the *Initial Brief of Appellant* and *Designation of Matter to be Included in the Record on Appeal* by mailing copies of the same by United States Mail with first class postage prepaid to the following addresses:

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June 10, 2013
Columbia, South Carolina

A handwritten signature in cursive script that reads "Erin Bridges". The signature is written in black ink and is positioned above a horizontal line.

Erin Bridges
BLUESTEIN, NICHOLS, THOMPSON
& DELGADO, LLC