STATE OF MINNESOTA
IN COURT OF APPEALS
A19-1592

Dustin Ward, et al.,
Appellants,

vs.

El Rancho Manana, Inc., et al.,
Respondents.

Filed May 18, 2020
Affirmed
Connolly, Judge

Stearns County District Court
File No. 73-CV-18-11033

Sarah R. Jewell, Kyle Murray, Franz Hultgren Evenson, P.A., St. Cloud, Minnesota (for appellants)

Christopher A. Wills, Eric Oelrich, Rajkowski Hansmeier, Ltd., St. Cloud, Minnesota (for respondents)

Considered and decided by Reilly, Presiding Judge; Connolly, Judge; and Hooten, Judge.

S Y L L A B U S

Under the doctrine of res judicata, shareholders of a closely held corporation who bring later derivative claims share privity with different shareholders of the same corporation that brought an earlier lawsuit alleging derivative claims when the two suits involve claims arising from the same set of factual circumstances.

O P I N I O N

CONNOLLY, Judge

In this dispute between shareholders in a closely held family business, appellants argue that the district court erred in dismissing their declaratory-judgment action. Because the district court did not err when it granted respondents' motions to dismiss and for summary judgment, we affirm.

FACTS

I. Background Information

In 1998, respondent Richard Ward formed Ward Family, Inc (WFI), with the stated purpose of giving his 1,200-acre property (the property) to his seven children while minimizing gift and estate tax burdens. *Blum v. Thompson*, 901 N.W.2d 203, 209-10 (Minn. App. 2017), *review denied* (Minn. Oct. 25, 2017).[1] Richard[2] then transferred his interest in the property to WFI through a quitclaim deed. *Id.* at 210. He became WFI's sole director and officer, and he gave each child about two percent of WFI's outstanding shares. *Id.* Appellants Dustin, Kayla, and Kelsie Ward own shares in WFI.[3]

Richard and his then-wife, Rosemary Ward, had purchased respondent El Rancho Manana, Inc. (ERMI) from Rosemary's parents in the 1960s or 1970s. *Id.* at 208. ERMI operates a commercial campground and horse stable on 200 acres of the property. *Id.*

[1] Other shareholders from WFI appealed an adverse grant of summary judgment to this court. We cite this prior decision to provide relevant factual information and analysis.
[2] We use first names for clarity and consistency with the district court's and parties' usage.
[3] Appellants are the children of Richard's son, Charles Ward. The record does not explain when or how they became shareholders in WFI.

When Richard and Rosemary divorced in 1985, they agreed that Richard would receive the entire 1,200-acre property and all shares of ERMI subject to certain restrictions. *Id.* at 208-09. After Richard formed WFI, ERMI continued to conduct business on the 200-acre portion of the property without a written lease agreement. *Id.* at 210. His son, respondent Kevin Ward, began managing ERMI in the 1990s.

Eventually, Richard began relinquishing more control of WFI to his children. By 2012, Richard owned 50.2% of the outstanding shares while each of his seven children owned about seven percent. *Id.* at 211. Also in 2012, the shareholders elected three directors: Richard and two of his daughters, respondents Ann Sullivan and Molly Thompson. *Id.*

WFI and ERMI executed a written lease agreement in 2012. *Id.* at 212. Under this agreement, ERMI can use the entire property for a 20-year term and holds the right to renew for another 20-year term. *Id.* After that, it may become a year-to-year tenant. *Id.* The lease requires ERMI to pay rent in an amount that covers WFI's administrative and professional fees, real estate taxes and assessments, mortgage payments, and debt payments on any future obligations for improvements that ERMI requests. *Id.* Three months after the lease's execution, Kevin purchased ERMI. *Id.* Upon assuming ownership, Kevin began restricting other WFI shareholders' access to the property. *Id.*

II. Prior Litigation

In February 2014, WFI shareholders Kathryn Ward Blum, Charles Ward, and Thomas Ward (the plaintiffs) sued Molly, Ann, Richard, Kevin, and WFI (the defendants), alleging various direct and derivative claims. *Id.* at 213. The three direct claims were:

(1) breach of fiduciary duty, (2) oppression of minority shareholders' rights in violation of Minn. Stat. § 302A.751 (2018), and (3) a request for litigation costs under Minn. Stat. § 302A.467 (2018).[4] *Id.* The four derivative claims asserted on WFI's behalf against the individual defendants included (1) breach of fiduciary duty, (2) corporate waste, (3) unjust enrichment, and (4) requests for litigation costs. *Id.*

In response to the suit, WFI formed a special litigation committee (the SLC) in 2014 to evaluate the derivative claims. *Id.* WFI, through the SLC, agreed with Kevin to "resolve[] . . . allegations against [him] in lieu of commencement of a lawsuit." *Id.* Based on this agreement, WFI renegotiated its lease with ERMI to prevent ERMI from encumbering WFI's property without prior approval. *Id.* And the renegotiated lease prohibited ERMI from unreasonably restricting WFI shareholders' access to the property. *Id.*

The SLC issued a 21-page report in April 2015 concluding that the defendants did not breach their fiduciary duties, did not commit corporate waste, and did not act fraudulently or illegally. *Id.* As a result, the SLC recommended against WFI pursuing any of the plaintiff's derivative claims. *Id.*

Following a grant of summary judgment to the defendants on the direct and derivative claims, the plaintiffs appealed. *Id.* at 213-14. This court affirmed in part, reversed in part, and remanded the case. *Id.* at 223. On remand, a jury and the district

[4] We cite the current version of these statutes because they have not been amended since the plaintiffs brought their lawsuit in 2014. *See Interstate Power Co. v. Nobles Cty. Bd. of Comm'rs*, 617 N.W.2d 566, 575 (Minn. 2000) (recognizing that, generally, "appellate courts apply the law as it exists at the time they rule on a case").

court ruled against the plaintiffs on their breach of fiduciary duty and shareholder-oppression claims following a bifurcated trial. *Blum v. Thompson*, A19-0938, 2020 WL 1983218, at *1 (Minn. App. Apr. 27, 2020) (*Blum II*). After the plaintiffs appealed the resulting judgment against them, this court affirmed. *Id.* at *12.

III. This Case

In December 2018, appellants brought a declaratory-judgment action against respondents seeking judicial review of the lease between WFI and ERMI. Count one of this action alleged that lease paragraph two violated the statutory rule against perpetuities. That paragraph states that WFI and ERMI's lease will expire in 2032, but it allows ERMI to renew the lease for another 20-year term and to become a year-to-year tenant in 2052 when the potential 40-year term ends.

Count two of the complaint sought a court order declaring lease paragraphs three and nine invalid as an equitable mortgage. Paragraph three defines ERMI's rent obligations, while paragraph nine addresses the parties' respective obligations for improvements to the property. Appellants alleged that the lease constitutes an equitable mortgage, claiming that WFI is essentially financing ERMI's purchase of the property over the lease term.

After answering, respondents moved to dismiss count one for failure to state a claim and sought summary judgment on count two. In their memorandum of law opposing the motions, appellants requested additional time to conduct discovery. Yet their attached declarations did not explain why they needed more time to conduct discovery or specify what evidence they would uncover with additional time.

The district court granted respondents' motions. In doing so, it reasoned that appellant's failed to state a claim on count one because they had no interest in the property. Alternatively, it held that count one presented a nonjusticiable controversy. On count two, the district court held that res judicata barred appellants' claim. As alternative reasons for granting summary judgment on count two, the district court cited laches and held that the lease did not constitute an equitable mortgage. This appeal follows.

ISSUES

I. Did the district court err in granting respondents' motion to dismiss count one for failure to state a claim?

II. Did the district court err in granting respondents' motion for summary judgment on count two by applying res judicata?

III. Did the district court err when it denied appellants' request for a scheduling order and more time to conduct discovery?

ANALYSIS

I. Dismissal of Count One for Failure to State a Claim

To begin, appellants argue that the district court erred in dismissing count one under Minn. R. Civ. P. 12.02(e) for failure to state a claim without first converting the motion to dismiss into a motion for summary judgment. But a district court may consider documents referenced in the complaint without transforming a motion to dismiss into one for summary judgment. *N. States Power Co. v. Minn. Metro. Council*, 684 N.W.2d 485, 490 (Minn. 2004).

Here, appellants attached the lease between WFI and ERMI to their complaint, which sought judicial review of the lease. Although respondents attached many documents to the memorandum supporting their motions, they referenced only the lease in arguing for dismissal of count one. Thus, the district court properly considered the lease without converting the motion to dismiss into a motion for summary judgment. *See In re Hennepin Cty. 1986 Recycling Bond Litig.*, 540 N.W.2d 494, 497 (Minn. 1995) (upholding district court's consideration of contract when deciding motion to dismiss because the complaint referenced parts of contract).

We turn now to the merits of the decision to dismiss count one. An appellate court reviews de novo a district court's dismissal of a claim under Minn. R. Civ. P. 12.02(e). *Bahr v. Capella Univ.*, 788 N.W.2d 76, 80 (Minn. 2010). In our review, we accept the pleaded allegations as true and construe all reasonable inferences in the nonmoving party's favor. *Walsh v. U.S. Bank, N.A.*, 851 N.W.2d 598, 606 (Minn. 2014). But legal conclusions in a complaint do not bind us. *Bahr*, 788 N.W.2d at 80.

Count one alleged that the lease between WFI and ERMI violated Minnesota's statutory rule against perpetuities. Under that statute, "a nonvested property interest is invalid unless (1) when the interest is created, it is certain to vest or terminate no more than 21 years after the death of an individual then alive; or (2) the interest either vests or terminates within 90 years after its creation." Minn. Stat. § 501A.01(a) (2018). This statutory section supersedes the common-law rule against perpetuities. Minn. Stat. § 501A.06 (2018).

Appellants argue that the lease between WFI and ERMI violates the statutory rule against perpetuities because their interest in the leased land will not vest within 21 years of the lease's creation. Because the complaint does not allege that appellants have individual interests in the property, we take this allegation to mean that WFI's interest in the land is too unclear under the lease. The lease began on December 31, 2012, and will expire in 40 years unless ERMI declines to renew it automatically. So the year 2052 marks the lease's endpoint. After that, ERMI may holdover and become a year-to-year tenant.

But count one never alleged that the claimed interest will fail to vest or terminate within 90 years after the lease's execution. *See* Minn. Stat. § 501A.01(a)(2). And we cannot see from the pleaded allegations how the lease would violate this second section. The lack of factual allegations asserting such a violation makes dismissal proper under Minn. R. Civ. P. 12.02(e). As a result, we need not address the district court's ruling that count one presented a nonjusticiable controversy.

II. Summary Judgment on Count Two Under Res Judicata

Appellants' second argument is that the district court erred in applying res judicata to grant summary judgment for respondents on count two. An appellate court reviews a district court's grant of summary judgment de novo. *Firefighters Union Local 4725 v. City of Brainerd*, 934 N.W.2d 101, 106 (Minn. 2019). Summary judgment is proper when "the movant shows that there is no genuine issue as to any material fact and the movant is entitled to judgment as a matter of law." Minn. R. Civ. P. 56.01.

The parties focus on the district court's application of res judicata[5] to grant summary judgment for respondents on count two of appellants' declaratory-judgment action. A district court's application of res judicata is reviewed de novo. *Rucker v. Schmidt*, 794 N.W.2d 114, 117 (Minn. 2011). The doctrine of res judicata involves facts giving rise to a claim and bars later litigation, no matter whether a party or its privy litigated a specific issue or legal theory. *Hauschildt v. Beckingham*, 686 N.W.2d 829, 840 (Minn. 2004). Res judicata is a doctrine of finality, and it applies to all claims that could have been litigated in an earlier action. *Id.* Courts should invoke res judicata carefully. *Wilson v. Comm'r of Revenue*, 619 N.W.2d 194, 198 (Minn. 2000).

Res judicata applies when four elements are met: "(1) the earlier claim involved the same set of factual circumstances; (2) the earlier claim involved the same parties or their privies; (3) there was a final judgment on the merits; [and] (4) the estopped party had a full and fair opportunity to litigate the matter." *Hauschildt*, 686 N.W.2d at 840. We examine these elements in turn.[6] And because the facts here satisfy all four elements, we conclude that the district court properly applied res judicata to count two.

[5] Minnesota courts use the term "res judicata" to describe claim preclusion. *See State v. Joseph*, 636 N.W.2d 322, 326 n.1 (Minn. 2001) (describing the supreme court's historical use of this term).

[6] In their brief, respondents also argue that collateral estoppel (issue preclusion) bars count two. But the district court did not rule on this argument, so we decline to address it. *See Hoyt Inv. Co. v. Bloomington Commerce & Trade Ctr. Assocs.*, 418 N.W.2d 173, 175 (Minn. 1988) ("[A]n undecided question is not usually amenable to appellate review.").

A. Same set of factual circumstances

Under the first res judicata prong, we consider whether the later claim involves the same set of factual circumstances as claims in the prior action. *Id.* Minnesota courts prohibit a plaintiff from dividing their causes of action involving the same factual circumstances into separate suits. *Hauser v. Mealey*, 263 N.W.2d 803, 807 (Minn. 1978). "A claim or cause of action is a group of operative facts giving rise to one or more bases for suing." *Hauschildt*, 686 N.W.2d at 840 (quotation omitted).

While appellants argued in their brief that count two alleged direct harm, their counsel conceded at oral argument that it was a derivative claim. In a derivative suit, the shareholder "step[s] into the corporation's shoes" and seeks redress that he could not demand for himself. *In re UnitedHealth Grp. Inc. S'holder Derivative Litig.*, 754 N.W.2d 544, 550 (Minn. 2008) (quotation omitted). But if a shareholder shows an injury that the corporation does not share, the shareholder has a direct claim. *In re Medtronic, Inc. S'holder Litig.*, 900 N.W.2d 401, 409 (Minn. 2017).

Our analysis of the claim involving the lease in the prior litigation clarifies this point. There, we held that the other WFI shareholders' claim about the lease agreement was derivative when they alleged that the lease harmed WFI. *Blum*, 901 N.W.2d at 215-16. But we also observed that the alleged injury was direct because the shareholders alleged that the lease agreement caused them individual harm. *Id.* at 216. Applying that reasoning here shows that count two of appellants' action is derivative because it does not allege that the lease has caused individual harm to appellants. In fact, appellants brought their action "as shareholders of Ward Family Incorporated."

In short, appellants are asserting another derivative claim on WFI's behalf about its lease agreement with ERMI. Other WFI shareholders already brought such a claim, which the SLC investigated. *See id.* at 213, 215-16. That appellants brought this case seeking a declaratory judgment does not preclude applying res judicata because appellants have simply restated the claim from the first suit under a different theory. *See Hauschildt*, 686 N.W.2d at 840 (explaining that res judicata applies to claims that a party could have asserted in an earlier action).

B. Same parties or their privies

The second res judicata element requires identical parties, or their privies, in the earlier and later actions. *Id.* In general, courts will find persons in privity with another party when (1) they control an action despite not being a named party to it, (2) a party represents their interests in an action, or (3) they are successors in interest to persons with derivative claims. *Rucker*, 794 N.W.2d at 118. But privity may also exist "when a person is otherwise so identified in interest with another that he represents the same legal right." *Id.* (quotation omitted). Because "privity" carries no prevailing definition for consistent application, courts must scrutinize the circumstances of each case to determine whether parties share privity. *Margo-Kraft Distribs., Inc. v. Minneapolis Gas Co.*, 200 N.W.2d 45, 47 (Minn. 1972).

Appellants argue that, because they were not parties in the prior case, res judicata cannot apply. In contrast, respondents ask this court to hold that shareholders from a closely held corporation bringing a later derivative claim share privity with different

shareholders from that corporation who brought a similar derivative claim. A review of Minnesota caselaw reveals that this is an issue of first impression.[7]

To start, we note the fundamental nature of a derivative suit. The corporation, rather than the individual shareholders, represents the real plaintiff in a derivative suit. *Ross v. Bernhard*, 396 U.S. 531, 538-39, 90 S. Ct. 733, 738 (1970); *In re UnitedHealth Grp.*, 754 N.W.2d at 550. This principle reveals that WFI represents the real plaintiff in both suits on any claims alleging harm to it based on the lease with ERMI.

Based on the corporation's role in a derivative action, we conclude that appellants shared privity with the other WFI shareholders in the earlier action. Indeed, it seems evident under Minnesota law that a corporation is bound by the results in a prior derivative suit in later litigation, even when different shareholders bring the new suit. Our research reveals that most courts have found that differing shareholders who bring successive derivative lawsuits on the same corporation's behalf share privity with one another. *See, e.g., Cal. State Teachers' Ret. Sys. v. Alvarez*, 179 A.3d 824, 848-49 (Del. 2018) (collecting cases).[8] The cases collected in *Alvarez* explain that privity exists between separate

[7] The supreme court addressed privity between shareholders and the Securities and Exchange Commission in *McMenomy v. Ryden*, 148 N.W.2d 804, 806-07 (Minn. 1967). We addressed privity in the res judicata context involving a professional association and its sole shareholder in *Bifulk v. Evans*, 353 N.W.2d 258, 261-62 (Minn. App. 1984). And we considered privity between a corporation and its majority owner in *Miller v. Nw. Nat'l Ins. Co.*, 354 N.W.2d 58, 62 (Minn. App. 1984). But none of these cases resolves the privity issue presented here.

[8] Although some of the foreign cases collected in *Alvarez* discuss collateral estoppel in a demand-futility context, the privity analysis does not differ under res judicata. *See Hauschildt*, 686 N.W.2d at 837, 840 (listing the elements for these concepts).

derivative plaintiffs because they are enforcing the corporation's right, and the corporation is the real party in interest. *Id.*

In sum, appellants are "so identified in interest" with the other WFI shareholders who brought the prior suit to support finding privity. *See Rucker*, 794 N.W.2d at 118. Both suits alleged derivative claims by different groups of shareholders within the same closely held corporation. While appellants correctly note that they played no individual role in the prior suit, this does not preclude application of res judicata. *See Nathan v. Rowan*, 651 F.2d 1223, 1226 (6th Cir. 1981) ("[N]onparty shareholders are bound by judgments if their interests were adequately represented.").[9]

C. Final judgment on the merits

In their brief, appellants conceded that this element was satisfied. But at oral argument, their counsel argued that there was no final judgment on the merits. We disagree. First, after a bifurcated trial in the other suit on the two remaining claims, we affirmed the judgment against the plaintiffs. *See Blum II*, 2020 WL 1983218, at *12. And a pending appeal "does not affect the preclusive nature of a judgment," unless the judgment is reversed or modified on appeal. *Brown-Wilbert, Inc. v. Copeland Buhl & Co.*, 732 N.W.2d 209, 220-21 (Minn. 2007).

Second, the supreme court denied review of our prior decision upholding the district court's grant of summary judgment on the derivative claims. The supreme court's denial

[9] Appellants do not argue that applying res judicata violates their due-process rights or that the prior WFI shareholders failed to adequately represent their interests. *See Restatement (Second) of Judgments* §§ 41-42, 59 (1984). We thus do not discuss those issues.

of a petition for review of a decision from this court causes this court's decision to become final. *Hoyt Inv. Co.*, 418 N.W.2d at 176. Thus, there has been a final judgment on all direct and derivative claims brought in the earlier suit. This element is met.

D. Full and fair opportunity to litigate the earlier case

The last res judicata factor considers "whether there were significant procedural limitations in the prior proceeding, whether the party had the incentive to litigate fully the issue, or whether effective litigation was limited by the nature or relationship of the parties." *Joseph*, 636 N.W.2d at 328 (quotation omitted). Here, the record reveals no procedural limitations in the earlier action. And the other WFI shareholders have extensively litigated that case, which now includes two appeals to this court. Thus, the final res judicata factor is satisfied.

III. Denial of Appellants' Request For a Scheduling Order and More Discovery

The final issue is whether the district court abused its discretion by denying appellants' request for a scheduling order and for more time to conduct discovery. But, as respondents observe, appellants do not discuss this issue in the argument section of their brief.

In general, parties forfeit any issues that they do not argue in their brief. *Balder v. Haley*, 399 N.W.2d 77, 80 (Minn. 1987). To prevent application of this rule, a party must at least address an issue in their brief's argument section. *In re Application of Olson for*

Payment of Servs., 648 N.W.2d 226, 228 (Minn. 2002). Here, appellants failed to argue this issue in their principal brief.[10] As a result, we decline to address it.

D E C I S I O N

Because count one of appellants' declaratory-judgment action failed to state a claim alleging a violation of the rule against perpetuities, the district court did not err by dismissing it. On count two, the district court correctly applied res judicata to grant respondents' summary-judgment motion. Appellants shared privity with fellow WFI shareholders who brought an earlier lawsuit alleging a derivative claim about the lease between WFI and ERMI. Thus, we affirm the district court in all respects.

Affirmed.

[10] In their reply brief, appellants offer a more detailed argument on this issue, contending that the district court violated their procedural due-process rights. An appellate court may deem forfeited issues that are argued for the first time in a reply brief. *Lund ex rel. Revocable Tr. of Kim A. Lund v. Lund*, 924 N.W.2d 274, 284 (Minn. App. 2019), *review denied* (Minn. Mar. 27, 2019). Thus, appellants have forfeited the newly raised arguments in their reply brief.