

The National Agricultural
Law Center



University of Arkansas
System Division of Agriculture

NatAgLaw@uark.edu | (479) 575-7646

An Agricultural Law Research Article

The Family Farm Corporation: A New Setting for the Doctrine of Corporate Opportunity

by

Mary E. Waite

Originally published in DRAKE LAW REVIEW
34 DRAKE L. REV. 537 (1984)

www.NationalAgLawCenter.org

THE FAMILY FARM CORPORATION: A NEW SETTING FOR THE DOCTRINE OF CORPORATE OPPORTUNITY

I. INTRODUCTION

As the popularity of traditional modes of farming operations—partnerships and individual or family organizations—declines in Iowa,¹ corporate farming is gaining momentum.² This Note focuses on the family farm corporation, Iowa's most prevalent corporate farming form.³ In 1982, family farm corporations encompassed nearly ninety-one percent of Iowa farm corporations and farmed 2,403,988 of the 2,541,848 acres operated by farm corporations that year.⁴

1. See 1 BUREAU OF THE CENSUS, U. S. DEP'T OF COMMERCE 1982 CENSUS OF AGRICULTURE, pt. 15, at 4 (1984) [hereinafter cited as 1982 CENSUS OF AGRICULTURE]. From 1978 to 1982, the number of Iowa farming corporations increased from 2,668 to 4,110. *Id.* Accompanying this increase was a corresponding rise in corporate acres farmed. *Id.* While the number of acres farmed by corporations accelerated from 1,621,982 in 1978 to 2,541,848 in 1982, a decline (albeit less dramatic) occurred in the number of farms and acres farmed by individual or family organizations and partnerships. *Id.* The Iowa farms operated by these entities decreased from 118,229 in 1978 to 110,823 in 1982. *Id.* The non-corporate acres farmed declined from 31,520,598 to 29,962,004. *Id.* Clearly the reason the percentage of increases in corporate farming are much sharper than the decreases in non-corporate farming is that approximately 78 percent of all Iowa farmland is still managed by individual or family organizations and partnerships. *Id.* at 4, 32.

2. Iowa's trend is a statewide manifestation of the national trend toward farming incorporation. SENATE COMM. ON AGRICULTURE, NUTRITION, AND FORESTRY, 97th Cong., 2d Sess., STATUS OF THE FAMILY FARM, FARM ORGANIZATION AND PERFORMANCE IN THE 1970's (Comm. Print 1982) [hereinafter cited as SENATE COMM. Report].

3. The Iowa definition of "family farm corporation" is a corporation:

a. Founded for the purpose of farming and the ownership of agricultural land in which the majority of the voting stock is held by and the majority of the stockholders are persons related to each other as spouse, parent, grandparent, lineal ascendants of grandparents or their spouses and other lineal descendants of the grandparents or their spouses, or persons acting in a fiduciary capacity for persons so related;

b. All of its stockholders are natural persons or persons acting in a fiduciary capacity for the benefit of natural persons or family trusts as defined in subsection 11 of this section; and

c. Sixty percent of the gross revenues of the corporation over the last consecutive three-year period comes from farming.

IOWA CODE § 172C (1983).

4. See 1982 CENSUS OF AGRICULTURE *supra* note 1, at 4. The growth in family farm corporations has been ongoing throughout the late 1970's. See Muhm, *Family Farm Corporations Gain in Iowa*, Des Moines Register & Tribune, Nov. 26, 1980, at 3B, col. 6. Nationally in 1978, family owned farming corporations constituted nearly 90 percent of the total 513,000 incorporated farms, with those having 10 or fewer shareholders predominating. SENATE COMM. REPORT, *supra* note 2, at 16. In Iowa, family farm corporations having 10 or fewer shareholders also predominated, in both 1978 and 1982. 1982 CENSUS OF AGRICULTURE, *supra* note 1, at 4. In 1982,

Since incorporation of the family farm is becoming increasingly attractive due to factors such as ease of ownership transfer through stock shares, continuity of operation, employee benefits for owners and limited liability,⁵ concern is necessarily engendered as to the rights and responsibilities of family farm shareholders. The formalities of incorporating the family farm in Iowa, as set forth by statute, may provide guidelines for technical requirements such as filing annual reports with the Iowa Secretary of State,⁶ but they fail to adequately address at least one area which should be of concern to any corporate shareholder—the fiduciary duties of directors with respect to corporate opportunity.⁷ The purpose of this Note is to evaluate the applicability of the doctrine of corporate opportunity in the context of the family farm corporation and to set forth workable proposals that shareholders of these corporations might utilize to prevent misappropriation of corporate opportunities by directors. Given the mounting number of family farm corporations nationally, the potential adverse impact of usurpation of corporate opportunity in these farm corporations and the lack of statutory or common law guidance with reference to corporate opportunity, shareholders should consider adapting these suggestions to their own operations.

This Note is not intended to set forth fool-proof solutions⁸ to the problems involving corporate opportunity that arise in the context of family farm corporations. Rather it is intended to generate ideas for farm incorporators which can be embodied in a contract, charter, or resolution. Such provisions should help shareholders settle disputes that will inevitably arise.⁹

3,638 of the 3,728 family farm corporations were held by fewer than 10 shareholders. *Id.* Additionally, 2,336,601 acres of 2,403,988 Iowa farmland acres were operated by these closely held family farm corporations. *Id.*

5. See generally E. HAYES, CORPORATE LAW AND PRACTICE §§ 1101-1108 (West 1969 & Supp. 1983); Harl, O'Byrne & Krausz, *The Farm Corporation*, in SELECTED READINGS IN FARM MANAGEMENT, 349-64 (1980).

6. See IOWA CODE § 496.1 (1983).

7. The fiduciary duty owed by a director to his corporation is that "responsibilities . . . be discharged in good faith and with that degree of care which ordinarily prudent persons would exercise under similar circumstances." 8 N. HARL, AGRICULTURAL LAW § 58.02 [1] [d], at 58-59.

8. Different problems and diverse facts surround each agricultural business, hence it is impossible to formulate general rules which will apply to every situation. See Shoemaker, *Incorporation of Family Agricultural Businesses*, 30 ROCKY MTN. L. REV. 401, 401 (1958); Davis, *From Agriculture to Agribusiness*, 34 HARV. BUS. REV. 107 (1956).

9. Failure to plan ahead has been cited as a primary reason only one-third of family-owned companies in the U.S. survive into the second generation. See Huntley & Thornton, *The Silent Strength of Family Businesses*, 94 U.S. NEWS & WORLD REPORT 47, 47 (April 25, 1983); cf. Nelton, *Shaky About Joining the Family Firm?*, 71 NATION'S BUSINESS 58, 58 (Nov. 25, 1983).

II. CORPORATE OPPORTUNITY

A. Definition

The corporate opportunity doctrine is an aspect of the fiduciary duty of loyalty owed to the corporation by those controlling its affairs.¹⁰ According to the doctrine, an officer, director, employee, or majority stockholder is prohibited from appropriating, for his own use, an opportunity that in fairness should have been offered his corporation.¹¹ The harm done to the corporation by the original seizure of the corporate opportunity is the issue, as distinguished from the problem of conflict of interest, which depends only upon the results of the seizure.¹² Only if consent is properly given by the shareholders may the fiduciary utilize a corporate opportunity for his own benefit.¹³

The case that laid the cornerstone for the corporate opportunity doctrine was *Guth v. Loft, Inc.*¹⁴ The Delaware Supreme Court in *Guth* summarized corporate opportunity as follows:

[I]f there is presented to a corporate officer or director a business opportunity which the corporation is financially able to undertake, [and it] is, from its nature, in the line of the corporation's business and is of practi-

10. Wadmond, *Seizure of Corporate Opportunity*, 17 *BUS. LAW.* 63, 63 (1961). See also *Science Accessories Corp. v. Summagraphics Corp.*, 425 A.2d 957, 961 (Del. 1980).

11. *Science Accessories Corp. v. Summagraphics Corp.*, 425 A.2d at 961.

12. *Id.*

13. Brudney & Clark, *A New Look at Corporate Opportunities*, 94 *HARV. L. REV.* 998, 998 (1981).

14. 23 Del. Ch. 255, 5 A.2d 503 (1939). The facts giving rise to the *Guth* litigation are as follows: Charles G. Guth was the president of Loft, Inc. (Loft), which manufactured and sold syrups, candies, beverages and foodstuffs. *Id.* at —, 5 A.2d at 505. Loft operated 115 stores for which it purchased about 30,000 gallons of Coca-Cola syrup annually. *Id.* Guth became embittered when the Coca-Cola Company refused to give him a jobber's discount in light of the fact that other purchasers of smaller quantities of the syrup received such a discount. *Id.* As a result, Guth decided to acquire an interest in a beverage company that had been adjudicated bankrupt in 1931. *Id.* at —, 5 A.2d at 506-07. Guth and one Megargel, who formerly controlled the bankrupt corporation, formed a new company beginning with an authorized capital of 300,000 shares. *Id.* at —, 5 A.2d at 507. One hundred thousand of these shares were issued to both Guth and Megargel, and it was agreed that the old company's secret syrup formula and trademark would be transferred to the new company. *Id.* The two shareholders organized the Pepsi-Cola Company under the laws of Delaware in August of 1931. *Id.* They then used the plants and facilities of Loft and the Grace Company, Inc. (the latter of which was owned by Guth and his family) to further the enterprise. *Id.* at —, 5 A.2d at 506. The suit in *Guth* was brought by Loft to impose a constructive trust in favor of the plaintiff on all shares of the Pepsi-Cola Company registered in the name of Guth and in the name of the Grace Company, Inc. *Id.* at —, 5 A.2d at 504. The Delaware Supreme Court held as follows:

[Guth's] cunning and craft supplanted sincerity [He] . . . commandeered for his own benefit and advantage the money, resources and facilities of his corporation and the services of its officials A genius in his line he may be, but the law makes no distinction between the wrong doing genius and the one less endowed.

Id. at —, 5 A.2d at 515.

cal advantage to it, is one in which the corporation has an interest or reasonable expectancy, and, by embracing the opportunity, the self-interest of the officer or director will be brought into conflict with that of his corporation, the law will not permit him to seize the corporate opportunity for himself . . . [T]he law will impress the trust in favor of the corporation upon the property, interests and profits so acquired.¹⁵

A year after the Delaware court decided *Guth*, the New Jersey Supreme Court decided *Solimine v. Hollander*,¹⁶ which further defined the corporate opportunity doctrine.¹⁷ The *Solimine* court held that a business opportunity was not a corporate one in these instances:

(a) wherever the fundamental fact of good faith is determined in favor of the director or officer charged with usurping the corporate opportunity, or (b) where the company is unable to avail itself of the opportunity or (c) where availing itself of the opportunity is not *essential* to the company's business, or (d) where the accused fiduciary does not exploit the opportunity by the employment of his company's resources, or (e) where by embracing the opportunity personally the director or officer is not brought into direct competition with his company and its business.¹⁸

Guth and *Solimine* suggested several general tests which are applied by the courts today in determining whether or not a corporate executive has usurped a business opportunity which should belong to the corporation.¹⁹ These tests are:

(1) "Interest or expectancy"—The corporation must have an equitable interest or reasonable expectancy in the opportunity stemming from a pre-existing right or relationship, and once this is established, the focus shifts to an appraisal of the degree to which the corporation needs the opportunity in order to survive.²⁰

(2) "Line of Business"—The opportunity must be intimately or substantially associated with the prospective or existing activities of the corporation.²¹

(3) "Employment of corporate resources"—If the opportunity is devel-

15. *Id.* at —, 5 A.2d 511 (citations omitted). See also *Schreiber v. Bryan*, 396 A.2d 512, 519 (Del. 1978).

16. 128 N.J. Eq. 228, 16 A.2d 203 (1940).

17. *Id.* at —, 16 A.2d at 215.

18. *Id.* (emphasis added). See also *Miller v. Miller*, 301 Minn. 207, —, 222 N.W.2d 71, 79 n.10 (1974). The *Miller* court, however, recognized that an all-inclusive standard for ascertaining wrongful appropriation was impossible to find since it is necessary to resolve each case according to "what is fair and equitable under the circumstances." *Id.* at —, 222 N.W.2d at 80.

19. *Guth v. Loft, Inc.* 23 Del. Ch. at —, 5 A.2d at 511; *Solimine v. Hollander*, 128 N.J. Eq. at —, 16 A.2d at 215.

20. *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 79-80 & n.10 (citing *Solimine v. Hollander*, 128 N.J. Eq. at 246, 16 A.2d at 215).

21. See *id.* at —, 222 N.W.2d at 80.

oped with corporate assets, it is deemed corporate.²²

(4) "Financial ability"—The corporation's financial inability to undertake the opportunity may create a presumption in favor of the usurping director, shareholder, or employee.²³

(5) "Intrinsic fairness"—It must be equitable for the corporate fiduciary to keep the opportunity under all the facts and circumstances.²⁴

The doctrine of corporate opportunity has been described as "among the least satisfactory limbs of doctrine in the corpus of corporate law."²⁵ Both courts²⁶ and commentators²⁷ have recognized that the doctrine is "not capable of precise definition."²⁸ Furthermore, it is impossible to conclusively state the law of corporate opportunity in the absence of a particular factual context.²⁹ A factual context is necessary because a determination of whether or not corporate opportunity has been wrongfully taken requires a balancing of multiple factors following application of the corporate opportunity "tests" to all the facts presented.³⁰

B. Corporate Opportunity in Iowa

Iowa law is elusive concerning fiduciary duties and ensuing liabilities of corporate fiduciaries when corporate business opportunities are misappropriated. The Iowa Code's proviso that directors act as reasonable persons would act under similar circumstances extends to matters involving dividends, asset and share distributions, and negligent financial statement submission.³¹ Statutory law is silent, however, with respect to acquisition of property by directors at the corporation's expense.³² In addition, two Iowa

22. See Brudney & Clark, *supra* note 13, at 1006.

23. See *Science Accessories Corp. v. Summagraphics Corp.*, 425 A.2d at 963.

24. See *Schreiber v. Bryan*, 396 A.2d at 519.

25. Brudney & Clark, *supra* note 13, at 998.

26. See *Miller v. Miller* 301 Minn. at —, 222 N.W.2d at 79. The court said: "We have searched the case law and commentary in vain for an all-inclusive or 'critical' test or standard by which a wrongful appropriation can be determined and are persuaded that the doctrine is not capable of precise definition." *Id.*

27. See Note, *Corporate Opportunity in the Close Corporation—A Different Result?* 56 GEO. L.J. 381, 382 (1967). The Note rejected "tests" for ascertaining corporate opportunity because "[a]side from concealing the true determinants—the underlying fact patterns—these conclusory tests have proved to be indistinguishable and meaningless." *Id.* In refusing to acknowledge the utility of these tests, however, the author seems to further confuse an already obscure area of the law. Although the tests which are generally applied to ascertain usurpation of corporate opportunity are indeed overlapping and inconclusive, they serve to thresh out determinative facts which judges weigh in making the ultimate equitable determination of "intrinsic fairness." See *infra* notes 138-58 and accompanying text.

28. *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 79.

29. See *Schreiber v. Bryan*, 396 A.2d at 519.

30. See *supra* notes 19-24 and accompanying text.

31. IOWA CODE § 496A.44 (1983).

32. *Id.*

Supreme Court cases are not only the touchstones of the law of corporate opportunity in Iowa; they also appear to be the only reported Iowa decisions which have even brushed the doctrine's surface.

In *Ontjes v. MacNider*,³³ a claim was filed on behalf of the stockholders of the Northwestern States Portland Cement Company for wrongful misappropriation of another company's stock against the estate of the deceased MacNider, who was president, general manager and director of the company.³⁴ The plaintiffs in this Iowa Supreme Court case sought to impose a constructive trust on the profits and earnings of the stock under the theory that MacNider had violated his fiduciary relationship with the cement company.³⁵ The court noted that neither the research of the parties, nor the court's efforts had disclosed a case that had ever been decided by the Iowa Supreme Court dealing with this proposition.³⁶ The *MacNider* court cited *Guth v. Loft*³⁷ and *Solimine v. Hollander*³⁸ in concluding that the nature of the enterprise into which MacNider entered was not one in which the cement company had any interest or expectancy, and since the other directors had indicated that they were not interested in purchasing the stock for the cement company, MacNider had not usurped a corporate opportunity.³⁹ Moreover, the court in *MacNider* held that the plaintiffs failed in their burden of proving by "clear, convincing and satisfactory" evidence that there was a need to impose a constructive trust.⁴⁰

Over twenty years later, the Iowa Supreme Court cited *MacNider* as the sole Iowa corporate opportunity precedent in *Schildberg Rock Products v. Brooks*.⁴¹ The defendants in *Schildberg* were officers, directors and the only owners of Missouri Valley Rock Quarry, Inc.⁴² Before they resigned as officers and directors, pursuant to a stock option which had been granted Schildberg Construction Co., the directors obtained a mineral lease on land within one and a half miles from a Schildberg quarry.⁴³ They had learned of test results following the company's drilling in the area and had represented to the lessor that they were working for the company.⁴⁴ The *Schildberg* court cited *MacNider* in holding as follows:

Plaintiff was financially able to enter into a utilize the . . . lease, the opportunity was in the line of plaintiff's business and of practical advan-

33. 232 Iowa 562, 5 N.W.2d 860 (1942).

34. *Id.* at 564-67, 5 N.W.2d at 862-63.

35. *Id.* at 575, 5 N.W.2d at 867.

36. *Id.*

37. *See supra* notes 14-15 and accompanying text.

38. *See supra* notes 16-18 and accompanying text.

39. *Ontjes v. MacNider*, 232 Iowa at 580-81, 5 N.W.2d at 870.

40. *Id.* at 586, 5 N.W.2d at 873.

41. 258 Iowa 759, 768-69, 140 N.W.2d 132, 137-38 (1966).

42. *Id.* at 761, 140 N.W.2d at 133.

43. *Id.* at 763, 140 N.W.2d at 134.

44. *Id.* at 764-65, 140 N.W.2d at 135.

tage to it, plaintiff had an interest and reasonable expectancy in the opportunity, by embracing it for themselves the self-interest of defendants was brought into direct conflict with that of plaintiff.⁴⁵

The Iowa Supreme Court thus affirmed the decree of the trial court's assignment of the mineral lease to the corporation.⁴⁶ The court followed the reasoning of the Pennsylvania Supreme Court in *Lutherland, Inc. v. Dahlen*⁴⁷ that the test of a corporate officer's liability upon seizure of a corporate business opportunity is whether or not the fiduciary has been unjustly enriched.⁴⁸

The question of corporate opportunity apparently has never been discussed in a reported Iowa case in which the corporate entity involved is a family farm corporation. Recently, however, the case of *Sauer v. Moffitt*⁴⁹ was decided by the Iowa Court of Appeals wherein this issue was presented.⁵⁰ One division of the complaint—a stockholder's derivative action brought on behalf of a family farm corporation (Moffitt Corp.)—asked

45. *Id.* at 769, 140 N.W.2d at 138.

46. *Id.* at 771, 140 N.W.2d at 139.

47. 357 Pa. 143, 53 A.2d 143 (1947).

48. *Schildberg Rock Prods. Co. v. Brooks*, 258 Iowa at 770-71, 140 N.W.2d at 139.

49. *Sauer v. Moffitt*, No. 8 slip op. (Iowa App. Nov. 20, 1984), *petition for further review filed*, No. 83-834 (Dec. 6, 1984).

50. *Id.* at 5-7. Two sisters, who were shareholders in Moffitt Corporation sued their mother, father, and brother, each of whom were directors of Moffitt Corporation alleging "illegal, or fraudulent acts" and misappropriation of waste of corporate assets within the meaning of the Iowa Code. *Id.* at 2. Plaintiffs relied on Iowa Code § 496A.94(1)(c). Plaintiffs sought any available equitable relief, including liquidation of the corporation, the appointment of a receiver, an accounting and temporary injunctive relief plus costs. Decree at 1, *Sauer v. Moffitt*, No. 90-270 (Iowa 5th Jud. Dist. filed Sept 2, 1981). Plaintiffs additionally sought \$500,000 of compensatory damages and \$500,000 of exemplary damages for defendants' conspiracy to defraud plaintiffs, and \$500,000 of compensatory damages for breach of fiduciary duties owed to plaintiffs. *Id.* at 1-2. Plaintiffs also sought \$500,000 and costs for breach of oral contract. *Id.* at 2. The last division of the complaint was a shareholder derivative action wherein the issue of usurpation of corporate opportunity arose. *Id.* at 1. The trial court found that the illegalities and breach of fiduciary duties exercised by the directors of the Moffitt Corporation were failure to provide notice of annual meetings over an eight-year period, improper corporate expenditures (including expenditures on a Cadillac and other cars and trucks, insurance premiums for the president's personal vehicles, and real estate taxes and insurance premiums on a home that had been held in the corporate name), and failure to issue stock certificates to plaintiffs pursuant to an oral contract. *Id.* at 34. The trial court indicated that directors of close corporations owed a higher fiduciary duty to minority stockholders than would the directors of other corporations, especially when the minority stockholders are family members. *Id.* at 38. The court concluded that the burden of proof shifted to the defendants to refute the plaintiff corporation's allegations of breach of fiduciary duty and self-dealing. *Id.* The defendants sustained their burden of proving that three farms were purchased with individual funds and were not corporate opportunities. *Id.* at 31. The trial court's decision regarding corporate opportunity was affirmed by the Iowa Court of Appeals. *Sauer v. Moffitt*, No. 83-834, slip. op. at 5-6 (quoting *Guth and Solimine*). The issue modified on appeal was not related to corporate opportunity. *Id.* at 11.

for damages and attorney's fees from the individual defendants "for waste, mismanagement, breach of fiduciary duties, self-dealing or unfair terms, and *appropriation of corporate opportunities*."⁵¹ The "corporate opportunity" allegedly usurped in *Moffitt* was the interest in three farms that had been acquired with the resources of the defendant shareholders.⁵²

The *Moffitt* case is of particular interest in that the the broader issue of fiduciary duties among family members as co-shareholders must be addressed in order to narrow the focus to corporate opportunity, which is "but one phase of the cardinal rule of undivided loyalty on the part of fiduciaries."⁵³ Traditionally, corporate law has imposed no duties among shareholders towards one another.⁵⁴ The modern view, however, is that a close corporation acquires the characteristics of an "incorporated partnership."⁵⁵ Therefore, shareholders of a closely held corporation owe one another the same fiduciary duty as partners owe one another in a partnership.⁵⁶ On the other hand, a sole shareholder has no fiduciary duties to co-shareholders, and consequently, none are owing his corporation.⁵⁷ It follows that the close corporation is personified in the form of shareholder "partners" among whom fiduciary duties are owing, and the personal activities of these partners are limited by "the duty of the finest loyalty."⁵⁸ *A fortiori*, the same degree of fiduciary loyalty should exist among members of the closely held family farm corporation, given both the initial consensual agreement to carry on business together *and* common bloodlines. Accordingly, any discussion of corporate opportunity in the family farm corporation setting should be viewed in light of especially high duties of loyalty owing among family members who are in business together.

III. EQUITABLE INTEREST OR REASONABLE EXPECTANCY

If a stockholder in a family farm corporation discovers a business opportunity which has not been developed with corporate assets, the answer to whether or not the corporation has an equitable interest or reasonable expectancy in the opportunity depends largely upon what the parties rati-

51. Decree at 1, *Sauer v. Moffitt*, No. 90-270 (Iowa 5th Jud. Dist. filed Sept. 2, 1981).

52. *Sauer v. Moffitt*, No. 83-834, slip op. at 5.

53. *Schildberg Rock Prods. Co. v. Brooks*, 258 Iowa at 768, 140 N.W.2d at 137.

54. *See Mairs v. Madden*, 307 Mass. 378, 380, 30 N.E.2d 242, 244 (1940). *See also Cardello v. Landau*, 329 Mass. 5, 9, 105 N.E.2d 843, 846 (1952); *Leventhal v. Atlantic Fin. Corp.*, 316 Mass. 194, 198-99, 55 N.E.2d 20, 23 (1944).

55. *Burg v. Horn*, 380 F.2d 897, 901 n.3 (2d Cir. 1967).

56. *See Burg v. Horn*, 380 F.2d at 901 n.3; *Donahue v. Rodd Electrotype Co.*, 367 Mass. 578, —, 328 N.E.2d 505, 517 (1975); *Russell v. First York Sav. Co.*, — Neb. —, —, 352 N.W.2d 871, 874 (1984).

57. *Canion v. Texas Cycle Supply, Inc.*, 537 S.W.2d 510, 513-14 (Tex. Civ. App. 1976). According to the *Canion* court, a sole shareholder does not usurp corporate opportunity when he ratifies his own act as director. *Id.* at 514.

58. *Meinhard v. Salmon*, 249 N.Y. 458, —, 164 N.E. 545, 546 (1928).

ally contemplated upon entering the venture.⁵⁹ It would be reasonable to impute to the corporation's shareholders anything within the firm's "functionally related operations."⁶⁰ A court might construe as continuing an interest in an opportunity that the corporation had initially contracted to obtain, such as a crop land lease which is to be renewed yearly.⁶¹ To limit what constitutes a reasonable expectation, the family farm corporation's directors might contract to exclude a particular commodity or additional quantities of this commodity from the purview of the corporation's reasonable expectations.⁶² If the directors agree that attaining a certain asset or that continuing an interest has some effect on the corporation's vitality, provided that acquisition of the opportunity is legal, it appears that the only limitation is that the harm that is caused by a fiduciary's misappropriation has "reasonably ascertainable monetary value."⁶³

According to case law, the determination of whether or not an opportunity should be a corporate one is sometimes dependent upon whether the opportunity is "essential" to the venture.⁶⁴ On other occasions, however, injury to the corporation is sufficient.⁶⁵ One commentator has suggested that

59. See Brudney & Clark, *supra* note 13, at 1010. *E.g.*, *Sauer v. Moffitt*, No. 83-834, slip op. at 7 (where corporation had no expectancy interest in acquiring farms, farms were not corporate opportunity).

60. See Brudney & Clark, *supra* note 13, at 1010. This premise suggests the relationship of the "reasonable expectations" and "line of business" tests. See *supra* text accompanying notes 19-21. It is proffered that an expectation cannot be reasonable if it is outside the sphere of the corporation's business.

61. See Brudney & Clark, *supra* note 13, at 1010. See also *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 80 n.11.

62. For example, in *Sauer*, a farm contract was executed by all the directors of Moffitt Corporation. Appendix for Appellants' Brief at 749, *Sauer v. Moffitt*, No. 83-834 (Iowa App. Nov. 20, 1984). The terms of the contract stated that "the operator may conduct a business of rising [sic] live-stock which shall not be a part of the business of said corporation." *Id.*

63. *BBF, Inc. v. Germanium Power Devices Corp.*, 13 Mass. App. 166, —, 430 N.E.2d 1221, 1227 (1982). The Massachusetts Appeals Court held that information can be a corporate opportunity. *Id.* at —, 430 N.E.2d at 1224. See also *General Automotive Mfg. Co. v. Singer*, 19 Wis. 2d 528, —, 120 N.W.2d 659, 661-62 (1963). In *Singer*, the general manager of business, who was under a contract which required him to devote full time and skill to his employment, turned over orders which the shop could not fill to other machine shops while he retained a secret profit. *General Automotive Mfg. Co. v. Singer*, 19 Wis. 2d at —, 120 N.W.2d at 661-62. In holding that *Singer's* activities were violative of his fiduciary duties to the corporation, the court stated that the corporate opportunity doctrine can apply to "tangible or intangible, present or future" property. *Id.* at —, 120 N.W. 2d at 663. A corporate opportunity, however, is not "a sale by a director of a business which the corporation had a right to expect would be offered it." *Rowen v. LeMars Mut. Ins. Co.*, 282 N.W.2d 639, 660 (1979).

64. See, *e.g.*, Brudney & Clark, *supra* note 13, at 1016. See also *Kaplan v. Fenton*, 278 A.2d 834, 836 (Del. 1971) (offer to sell stock was not essential to corporation).

65. See, *e.g.*, Brudney & Clark, *supra* note 13, at 1016-17. See also *Hartung v. Architects Hartung/Odle/Burke, Inc.*, 157 Ind. App. 546, —, 301 N.E.2d 240, 245 (1973). In this case, following his resignation from the corporation, Hartung informed the landlady of the corporate office that he desired to continue the month-to-month tenancy for his personal use. *Id.* at —,

in the context of a closely held corporation, if the opportunity is "functionally related to the business," the fiduciary may not take it, whether or not it is essential to the corporation's survival.⁶⁶ Certainly, given the high fiduciary duties owing among shareholders in "incorporated partnerships," it appears that it is not necessary to show a business opportunity is essential to the family farm corporation—a showing of harm should be sufficient.⁶⁷

A fiduciary of a closely held corporation may be found liable upon a mere showing of injury to the corporation. Thus, it becomes even more important for the shareholders to anticipate special problems that might arise. If a farmer is engaged in outside agricultural pursuits such as running a hatchery or a feed business, he should consider the effects of any purchases he makes towards the furtherance of such business on the family farm corporation. For instance, if a shareholder purchases a used tractor for less than the going rate with the intent to appropriate the proceeds to his personal use following resale by his implement dealership, he might be liable to his corporation for usurpation of corporate opportunity. The other shareholders could claim that he breached his fiduciary duties in failing to offer the chance to buy the tractor to the corporation. If this situation would have been foreseen, the following contractual provision might have eliminated at least some confusion as to what constitutes a corporate opportunity:

If (shareholder and/or director) in purchasing any chattel, represents to a third party that he is acting on behalf of said implement dealership in making such purchase,⁶⁸ and if such purchase is appropriated by said implement dealership in its line of business, such purchase will not constitute a corporate opportunity of (name of corporation).

Moreover, since it is not recommended that a farm owner transfer all his assets to the corporation,⁶⁹ and since farmers many times have become accustomed to the independence associated with sole proprietorships,⁷⁰ it is oftentimes difficult to separate the corporate entity from its shareholders. An attempt should be made to distinguish the two, however, by defining the scope of the individual farmers' (shareholders') activities as opposed to those of the corporation. This will not only aid the farmer in recognizing that the corporation's interests are distinct from his own, but it will also

301 N.E.2d at 244-45. The *Hartung* court held that his conduct was clearly against the corporation's interest. *Id.* at —, 301 N.E.2d at 245.

66. Brudney & Clark, *supra* note 13, at 1011.

67. See *Hartung v. Architects Hartung/Odle/Burke, Inc.*, 157 Ind. App. at —, 301 N.E.2d at 243.

68. It is necessary for the farmer to indicate to third parties that he is not representing the family farm corporation, because a corporate officer cannot acquire an interest adverse to the corporation by taking advantage of his inside knowledge. See *Schildberg Rock Prods. Co. v. Brooks*, 258 Iowa at 768, 140 N.W.2d at 136-37.

69. See HAYES, *supra* note 5, § 1108 at 653.

70. See Shoemaker, *Incorporation of Family Agricultural Businesses*, 30 ROCKY MTN. L.REV. 401, 402 (1958).

provide guidelines for the farmer to evaluate what opportunities the corporation can reasonably expect will be offered it in the future.

IV. LINE OF BUSINESS

If a corporate fiduciary desires to appropriate an asset to his own use, he must first define his corporation's "line of business," for purposes of deciding whether or not he must first offer the opportunity to the corporation. The fiduciary's argument that the phrase "line of business" is "so elastic as to furnish no basis for a useful inference" would carry little weight if he is sued by the balance of the shareholders for misappropriation of a corporate opportunity.⁷¹ The Minnesota Supreme Court in the leading case of *Miller v. Miller*⁷² considered such an argument.⁷³ The *Miller* court held that, although "the [corporate opportunity] doctrine is vague and subjects today's corporate management to the danger of unpredictable liability,"⁷⁴ workable standards should be set forth to quell at least some confusion in its application.⁷⁵ Accordingly, the court in *Miller* recognized the "line of business" test as one prong of a two-prong test for appraising corporate opportunity.⁷⁶ The "line of business" test, which the Minnesota court recognized as being more flexible than the more restrictive test of "interests or expectancy," is of practical value when applied to the facts and circumstances of each case.⁷⁷

According to the *Miller* court, an opportunity is within a corporation's "line of business" when:

the relationship of the opportunity to the corporation's business purposes and current activities—whether essential, necessary, or merely desirable to its reasonable needs and aspirations—; whether, within or without its corporate powers, the opportunity embraces areas adaptable to its business and into which the corporation might easily, naturally, or logically expand⁷⁸

71. *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 80 (quoting *Guth v. Loft, Inc.*, 23 Del. Ch. at 279, 5 A.2d at 514).

72. 301 Minn. 207, 222 N.W.2d 71 (1974). In *Miller*, a packing and wiping waste corporation prospered until the beginning of World War II, when its attempts to satisfy government war commitments caused substantial losses. *Id.* at —, 222 N.W.2d at 74. As a result, sideline businesses were formed which flourished. *Id.* at —, 222 N.W.2d at 74-75. A shareholder of the original corporation brought a derivative action, alleging usurpation of corporate opportunities by the sideline businesses. *Id.* at —, 222 N.W.2d at 72-73.

73. *Id.* at —, 222 N.W.2d at 80.

74. *Id.* at —, 222 N.W.2d at 81.

75. *Id.*

76. *Id.* The other prong is "intrinsic fairness." See *infra* notes 142-58 and accompanying text.

77. See *Miller v. Miller*, 301 Minn. at —, 222 N.W. 2d at 80 (citing *Guth v. Loft, Inc.*, 23 Del. Ch. 279, 5 A.2d 514).

78. *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 81; see also *Peterson Welding Supply v. Cryogas Prods.*, 126 Ill. App. 3d 759, —, 467 N.E.2d 1068, 1072 (1984) (business opportunity must be in line of business and of practical advantage to corporation).

In addition, the Minnesota court noted that application of this "line of business" test is particularly obscure because the phrase has been interpreted as broadly as the corporate charter, and as narrowly as the firm's actual operations.⁷⁹ Consequently, it becomes necessary for the shareholder in the family farm corporation, where a particularly hazy line is drawn between individual and corporate assets,⁸⁰ to designate as precisely as possible at the beginning of the venture the nature of the corporate business.⁸¹ For additional protection, individual shareholders should seek the consent of the other shareholders when entering into a transaction that might rightly belong to the corporation.⁸²

Some of the problems inherent in applying the "line of business" test to the family farm corporation surface when a shareholder purchases a tract of farmland with his own resources without consulting his fellow shareholders. If a corporate charter broadly defines the nature of the business, a court might resort to other means to determine whether or not the acquisition is in the corporation's line of business.⁸³

Considering the breadth of the corporate charter, a court's reasonable alternative would be to narrow its inquiry to the corporation's current activities to ascertain the functional relationship of those activities to the corporate opportunity.⁸⁴ Since there are apparently no reported cases which address corporate opportunity in the context of the family farm corporation, the "line of business" test has never been employed when farmland or chattels are alleged to be corporate opportunities. In light of this fact, to analyze whether or not farmland can be in the family farm corporation's line of business, it becomes necessary to expand the scope of inquiry to cases dealing with the question of whether or not realty can be within a corporation's "line of business."

The law in Iowa is that an interest in real estate can be a corporate opportunity when a corporation is financially able to undertake the venture, when the corporation has an interest and reasonable expectancy in the opportunity, and when the opportunity is in the corporation's line of busi-

79. See, e.g., *Brudney & Clark*, *supra* note 13, at 1012. Compare *Weismann v. Snyder*, 338 Mass. 502, —, 156 N.E.2d 21, 23 (1959) (corporate charter's broad grant of powers included sales activity in which president of corporation was engaged for his own benefit) with *Peterson Welding Supply v. Cryogas Prod.*, 126 Ill. App. 3d at —, 467 N.E.2d at 1072 (1984) (scope of "line of business" narrowed to include only activities which are "reasonably incident to the corporation's present or prospective business" and in which the corporation has the capacity to engage).

80. See *supra* text accompanying notes 69-70.

81. The "line of business" as set forth in the articles of incorporation or bylaws of the family farm corporation should fall within the general provisions of IOWA CODE § 172C.1 (8) (1983), which defines "family farm corporation." See *supra*, note 3.

82. See, e.g., *Hill v. Hill*, 279 Pa. Super. 154, —, 420 A.2d 1078, 1082 (1980).

83. See *infra* text accompanying notes 151-53.

84. *Schildberg Rock Prods. Co. v. Brooks*, 258 Iowa at 768, 140 N.W.2d at 137.

ness.⁸⁵ *Schildberg* is the only reported Iowa case which has characterized an interest in land as a corporate opportunity.⁸⁶ In *Schildberg*, the defendants were officers and directors of Missouri Valley Limestone Co. which later became Schildberg Rock Products Co.⁸⁷ The company was engaged in quarrying stone in seven counties in southwest Iowa.⁸⁸ When one of the defendants learned of mineral content test results through his position as director, he obtained a lease for the quarrying of limestone on the property that had been tested.⁸⁹ This defendant claimed that the corporation had refused the opportunity to purchase the land through the president who "appeared to lose interest in the thing" when he saw the test reports.⁹⁰ The property was within one and a half miles from lands on which the plaintiff's company held two leases.⁹¹ The court in *Schildberg* found that the interest in the stone deposits on the neighboring land was sufficiently within the scope of the quarrying corporation's activities so as to fall within its "line of business."⁹² Neither the company president's desire to do more drilling on the land before negotiating a lease on it nor the subjective belief of the defendant that the president had impliedly consented to the acquisition was sufficient to show the corporation had declined the opportunity.⁹³

It follows that under *Schildberg*, an Iowa court will look solely to the corporation's business activities to evaluate its line of business, absent an express agreement of the directors to the contrary. Therefore, if a shareholder of a grain-farming corporation wishes to lease or purchase adjoining cropland to operate himself, he should obtain unequivocal consent from the other shareholders. On the other hand, if the shareholder wishes to purchase adjoining pastureland, the court might not find the acquisition of the land to be in the corporation's line of business, but it could hold the shareholder liable for usurpation of a corporate opportunity upon the application of the other business opportunity tests⁹⁴ to the facts and circumstances. For example, if the acquisition of the parcel of land greatly increases the value of the corporation's land holdings as a "package"⁹⁵ and if the corporation is well able to afford the opportunity,⁹⁶ a court might designate it to be corporate.

85. *See id.*

86. *Id.*

87. *Id.* at 762-63, 140 N.W.2d at 134.

88. *Id.* at 761, 140 N.W.2d at 133.

89. *Id.* at 763-64, 140 N.W.2d at 134-35.

90. *Id.* at 763, 140 N.W.2d at 134.

91. *Id.* at 762, 140 N.W.2d at 134.

92. *Id.* at 765, 769, 140 N.W.2d at 136, 138.

93. *Id.* at 769, 140 N.W.2d at 138.

94. *See supra* text accompanying notes 19-24.

95. *See Farber v. Servan Land Co.*, 662 F.2d 371, 375 (5th Cir. 1981). The corporation has an "interest or expectancy" in acquiring land when such an acquisition greatly increases the value of the company's assets. *Id.*

96. *See A. C. Petters Co. v. St. Cloud Enters., Inc.*, 301 Minn. 261, ___, 222 N.W.2d 83, 86 (1974). The court's decision that a parcel of land was not a corporate opportunity rested almost

The same reasoning would extend to the acquisition of chattels such as machinery or livestock by a stockholder individually. Any personal property that is "reasonably incident" to the corporation's farming activities as detailed in its charter or as ascertained by the fact finder from evidence of daily activities should in fairness be offered first to the corporation.⁹⁷

V. EMPLOYMENT OF CORPORATE RESOURCES

Another point of inquiry is whether or not corporate resources may be used to acquire or maintain an individual opportunity. In *Sauer*, the trial court held that because the corporation's directors and majority stockholders had a "corporate business philosophy" that the farmland owned by the corporation should remain debt free, farm property which was purchased by directors with their own resources was not a corporate opportunity.⁹⁸ The problem in *Sauer* is that while the directors did not purchase the farms at issue with corporate funds, it seems likely that they will use corporate farm machinery to develop these assets; consequently, the question of whether or not the land might become a corporate opportunity arises.⁹⁹

In general, although a corporate fiduciary is under no obligation to use his personal funds to develop a corporate opportunity, a corporate fiduciary may not usurp such an opportunity by using corporate assets.¹⁰⁰ Such assets include "hard" assets, such as corporate funds and facilities,¹⁰¹ and "soft"

solely on the fact that the terms of the land contract were that the sale was to be cash, and that all the assets of the company were encumbered. *Id.* The *St. Cloud Enters.* court held:

Though Petters Company possessed the fundamental knowledge and practical experience required to utilize the opportunity, and the opportunity was admittedly intimately related and of "distinct, special value" to Petters Company and its reasonable needs and aspirations, the undisputed testimony conclusively establishes that the company was financially unable to avail itself of the business opportunity.

Id.

97. See *Boyd v. Cooper*, 269 Pa. Super. 594, —, 410 A.2d 860, 861 (1979) (shareholders in pizza business sued other shareholders to enjoin them from manufacturing pizza or pizza-related items at competing business); *Borden v. Sinskey*, 530 F.2d 478, 492-93, (3d Cir. 1976) (bank stock acquisitions held to be in holding company's "line of business" because the company was organized and incorporated for the purpose of buying and holding bank-related stocks and assets).

98. Decree at 31, *Sauer v. Moffitt*, No. 90-270 (Iowa 5th Jud. Dist. filed Sept. 2, 1981) *aff'd as modified*, No. 83-834 (Iowa App. Nov. 20, 1984). The corporation was formed pursuant to an estate plan so that defendants, husband and wife, could give their children (two of whom were plaintiffs) a debt-free corporation. *Id.* The court's finding of fact was that the only way Moffitt Corporation could purchase the farms in question was to mortgage land it already owned. *Id.*

99. *Cf. Sauer v. Moffitt*, No. 83-834, slip op. at 7.

100. See *Anderson v. Clemens Mobile Homes, Inc.*, 214 Neb. 283, —, 333 N.W.2d 900, 905 (1983). See *Brudney & Clark*, *supra* note 13, at 998.

101. *Ontjes v. MacNider*, 232 Iowa at 580, 5 N.W.2d at 870 (president purchased stock in individual, not corporate capacity); *Dolese Bros. Co. v. Brown*, 39 Del. Ch. 1, —, 157 A.2d 784, 787 (1960) (dominating director used corporate funds to purchase stock for himself); *Electronic*

assets, such as knowledge and good will.¹⁰² For example, if an officer obtains a loan from his corporation at an unreasonably low rate of interest and uses the money to procure a contract for himself without disclosing the facts to the other directors, the officer may be liable to the corporation for the profits resulting from such contract as well as the deficient loan interest.¹⁰³ Such liability can attach without a showing that the corporation had an "interest or expectancy" in the opportunity or that the opportunity was in the corporation's "line of business."¹⁰⁴

It appears that even if the Iowa Court of Appeals does not find usurpation of corporate opportunity in *Sauer*, Moffitt Corp. would later have a viable cause of action in equity for an accounting and for the recovery of damages if any shareholder uses, for instance, corporate equipment to develop an individual business opportunity.¹⁰⁵ Hence, if a shareholder uses the corporation's assets to generate his own profits, it appears he will be liable to the corporation for at least the reasonable cost of obtaining the asset somewhere else. Furthermore, a court may broaden the purview of the corporation's "reasonable interest or expectancy" and "line of business" so as to deem the opportunity corporate, or it may choose to ignore the corporate opportunity tests altogether in imposing liability.¹⁰⁶

In determining whether or not to hold a family farm corporation director liable on the sole basis of misappropriating a corporate asset in furtherance of his own ends, a court could raise at least two collateral issues which might prove particularly vexing in this situation: (1) If a farmer employs the "soft" resource of knowledge in obtaining a corporate resource, the court must somehow separate corporate knowledge from knowledge acquired in his individual capacity; and (2) Any distinction between fiduciary duties owed to the corporation by the shareholder director who has a management role in the farm corporation and a shareholder who merely has a pecuniary interest should be recognized in determining what corporate resources may be used to develop an outside opportunity.¹⁰⁷

Difficulty inheres in ascertaining when the farmer who is a director or shareholder is acting within the scope of his corporate employment. For instance, while a shareholder is authorized to carry on farm business pursuant to a farm contract which he and the corporation executed, he is not paid a

Dev. Co. v. Robson, 148 Neb. 526, —, 28 N.W.2d 130, 138 (1947) (managing officers used corporate facilities to secure government contract).

102. *Schildberg Rock Prods. Co. v. Brooks*, 258 Iowa at 763, 140 N.W.2d at 134 (directors relied upon inside knowledge of stone testing results in deciding to lease quarry); *Electronic Dev. Co. v. Robson*, 148 Neb. at —, 28 N.W.2d at 140 (court directed that goodwill be returned to the corporation). *See also* *Brudney & Clark*, *supra* note 13, at 1006-07.

103. *See* *Production Mach. Co. v. Howe*, 327 Mass. 372, —, 99 N.E.2d 32, 36 (1951).

104. *Id.* *See also* *Graham v. Mimms*, 111 Ill. App. 3d 751, —, 444 N.E.2d 549, 557 (1982).

105. *C.f.* *Production Mach. Co. v. Howe*, 327 Mass. at 372, 99 N.E.2d at 32.

106. *Id.*

107. *See supra* notes 101-04.

salary for either his services as director or "employee." Since his working hours are indefinite and he resides at his place of employment, it can be argued that he is always acting in his capacity as a corporate fiduciary, presuming he has no outside occupation. It follows that the farm shareholder can never acquire knowledge outside the scope of his duties as an officer, director and shareholder.¹⁰⁸ Accordingly, since he cannot escape his fiduciary capacity, and if acquisition of knowledge as a corporate asset conclusively establishes liability, the shareholder could never obtain any asset in his private capacity; hence, he would be amenable to the corporation for the value of virtually any asset he puts to his own use.¹⁰⁹

Invariably, however, when a fiduciary's abuse of his position as an insider is involved,¹¹⁰ additional tests¹¹¹ must be satisfied before a business opportunity will be deemed a corporate one.¹¹² Alternatively, when a corporation's hard assets, such as facilities, have been used together with a "soft" asset such as knowledge, liability might be imposed.¹¹³

If a director operated farms owned by the corporation as compared to a director who was a city dweller who acted in no management role, the law apparently makes no distinction in terms of freedom to use corporate assets for the furtherance of the director's own ends.¹¹⁴ Since the fiduciary duties that the shareholders owe to the corporation are indistinguishable for purpose of applying the corporate opportunity doctrine, the on-farm director has no more license to take corporate assets for himself than does the off-farm shareholder.¹¹⁵

108. See *Weiss v. Kay Jewelry Stores, Inc.*, 470 F.2d 1259, 1267-68 (D.C. Cir. 1972). In *Weiss*, the court held that there was a genuine issue of material fact in the defendant's claim that he purchased shares of stock in a non-corporate matter outside the scope of his duties as a director. *Id.* The case was reversed and remanded so the district court could distinguish between this defendant director's private rights and official obligations. *Id.* at 1271.

109. See Note, *supra* note 27, at 382.

110. See *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 78.

111. See *supra* text accompanying notes 19-24.

112. Cf. *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 78-79; see also *Schildberg Rock Prods. Co. v. Brooks*, 258 Iowa at 768, 140 N.W.2d at 137. In *Schildberg*, the interest in the quarry which was obtained by the defendant directors through their position as insiders was held by the court to be within the plaintiff corporation's "line of business." *Id.*

113. See *Electronic Dev. Co. v. Robson*, 148 Neb. at —, 28 N.W.2d at 140; *Science Accessories Corp. v. Summagraphics Corp.*, 425 A.2d at 963. The court in *Science Accessories* intimated that an officer's usurpation of corporate resources is conclusive as to wrongful acquisition of a business opportunity, irrespective of the corporation's interest in it. *Science Accessories Corp. v. Summagraphics Corp.*, 425 A.2d at 963.

114. See *Golden Rod Mining Co. v. Bukvich*, 108 Mont. 569, —, 92 P.2d 316, 319 (1939). In this case, the Montana Supreme Court held that a "dummy director" may be a mere figurehead with no responsibilities, but he has the same fiduciary duties as any other variety of director. *Id.* at —, 92 P.2d at 319. *But see Raines v. Toney*, 228 Ark. 1170, —, 313 S.W.2d 802, 808 (1958) (higher duty imposed upon fiduciary who was vice president, director and manager).

115. See *Golden Rod Mining Co. v. Bukvich*, 108 Mont. at —, 92 P.2d at 319.

VI. FINANCIAL ABILITY

A. *The Factor of Corporate Solvency*

Assuming a stockholder desires to acquire a farm to operate himself, he might question whether or not he is obligated to offer the opportunity to buy the farm to a land holding corporation if the "corporate business philosophy" is that the company should remain debt free, and if the purchase of the farm could only have been made by the corporation if it mortgaged its incorporated land.¹¹⁶

Iowa courts follow the *Guth* rule in holding that an opportunity is not a corporate one if the corporation is financially unable to undertake it,¹¹⁷ but apparently other jurisdictions are split on the issue.¹¹⁸ One view espoused by the courts is that if a corporation is solvent, its financial inability to undertake what is otherwise a business opportunity does not excuse a corporate fiduciary from diverting the opportunity toward his own purposes.¹¹⁹ The reason for this rule is that "[i]f directors are permitted to justify their conduct on such a theory, there will be a temptation to refrain from exerting their strongest efforts on behalf of the corporation since, if it does not meet the obligations, an opportunity of profit will be open to them personally."¹²⁰

The prevailing view, however, is that this ironclad rule is too extreme in that it prevents the fiduciary from taking advantage of a business opportunity regardless of the corporation's financial inability to afford the opportunity.¹²¹ Usually evidence must conclusively establish financial inability¹²² or the corporation must be technically or de facto insolvent in addition to such financial incapacity before the corporation has tacitly "refused" the opportunity.¹²³ An alternative approach is that the financial ability of a corpora-

116. See *supra* text accompanying note 98. The trial court in *Sauer* found that the incorporators' "corporate business philosophy" was that the farmland should not be mortgaged so it would remain unencumbered upon transfer to their children. Decree at 31, *Sauer v. Moffitt*, No. 90-270 (Iowa 5th Jud. Dist. filed Sept. 2, 1982).

117. Cf. *Rowen v. LeMars Mut. Ins. Co.*, 282 N.W.2d 639, 660 (Iowa 1979); *Schildberg Rock Prods. Co. v. Brooks*, 258 Iowa at 768, 140 N.W.2d at 138; *Ontjes v. MacNider*, 232 Iowa at 580, 5 N.W.2d at 870.

118. See, e.g., *Lussier v. Mau-Van Dev., Inc. I*, 667 P.2d 804, 813 (Hawaii Ct. App. 1983) (discussion of jurisdictional differences).

119. See *Irving Trust Co. v. Deutsch*, 73 F.2d 121, 124 (2d Cir.), cert. denied, 294 U.S. 708, reh'g denied, 294 U.S. 733 (1934) (financial inability due to failure of one of defendants to pay debt).

120. *Morad v. Coupounas*, 361 So. 2d 6, 9 (Ala. 1978) (quoting *Paulman v. Kritzer*, 17 Ill. App. 2d 284, —, 219 N.E.2d 541, 545-46 (1966), aff'd, 38 Ill. 2d 101, 230 N.E.2d 262 (1967)). See *Irving Trust Co. v. Deutsch*, 73 F.2d at 124.

121. See *Ellzey v. FYR-PRUF, Inc.*, 376 So. 2d 1328, 1334 (Miss. 1979).

122. See *A.C. Petters Co. v. St. Cloud Enters.*, 301 Minn. at —, 222 N.W.2d at 86; *Ellzey v. FYR-PRUF, Inc.*, 376 So. 2d at 1334.

123. See *Klinikci v. Lundgren*, 678 P.2d 1250, 1253 (Or. Ct. App. 1984).

tion to undertake a venture is one of numerous factors including the good faith of the officer and the degree of disclosure to the corporation, that are to be weighed on a case-by-case basis.¹²⁴

In addition, the burden of proving corporate financial incapacity is on the fiduciary.¹²⁵ If there is no evidence that indicates that a corporation cannot undertake a business opportunity which should be offered it, the presumption is that the corporation could undertake the opportunity.¹²⁶

Accordingly, a stockholder should conclusively prove either his family farm corporation's insolvency or financial inability to purchase a tract of land before he makes such a purchase for himself. Iowa courts have not discussed the "financial inability" test at length, but the decisions of other jurisdictions seem to indicate that a high quantum of evidence is necessary on the part of the defendant to prove his good faith in property acquisitions.¹²⁷ If a shareholder were to disclose the opportunity to his fellow shareholders and obtain their rejection of it, the shareholder might not have to furnish this overwhelming showing of corporate financial inability.¹²⁸

B. *Means of Proving Corporate Financial Inability or Insolvency*

If a director discloses a business opportunity to the other directors of the corporation to let them decide whether or not the corporation is solvent or able to avail itself of the opportunity,¹²⁹ on what factors do they base their decision?

A corporation's insolvency may be established in the balance sheet asset/liability sense just as temporary insolvency may be shown in the equity/debt sense.¹³⁰ Additionally, insolvency for purposes of inability to obtain a corporate opportunity may be argued if a corporation is unable to secure adequate financing given its financial position.¹³¹

124. See *Paulman v. Kritzer*, 17 Ill. App. 2d at —, 219 N.E.2d at 546 (president and 50 percent stockholder in corporation liable for misappropriation of real estate which he discovered while searching for real estate for corporation).

125. See *Klinicki v. Lundgren*, 678 P.2d at 1253.

126. See *Toledo Trust Co. v. Nye*, 426 F. Supp. 908, 912 (N.D. Ohio 1977).

127. See *supra* notes 122 and 123.

128. Cf. *Lussier v. Mau-Van Dev., Inc.*, 667 P.2d at 813. The *Lussier* court held that an opportunity is not corporate if "(1) the corporation is financially unable to undertake it and (2) before a director or officer seizes such opportunity for himself, he discloses the opportunity to the shareholders and obtains their consent to the acquisition of the opportunity and such action is not detrimental to the corporation creditors." *Id.* at 813 (citing *Hill v. Hill*, 279 Pa. Super. 154, 420 A.2d 1078 (1980)).

129. See, e.g., *Klinicki v. Lundgren*, 678 P.2d at 1254. If there is any uncertainty, "[d]isclosure is a fundamental fiduciary duty." *Id.*

130. *Ellzey v. FYR-PRUF, Inc.*, 376 So. 2d at 1334. See *Klinicki v. Lundgren*, 678 P.2d at 1254.

131. *Ellzey v. FYR-PRUF, Inc.*, 376 So. 2d at 1334. One suggestion is that a farm corporation probably has too "thin" a debt/equity ratio if the amount of debt issued to inside creditors is greater than the debt which could have been obtained from outside creditors. Comment,

Since there is no single test for determining corporate undercapitalization, such a determination is necessarily speculative.¹³² Although the debt to capital test is sometimes used, it is somewhat unreliable because of the wide range of ratios that have been approved by the courts.¹³³ Hence, the fact finder should direct his inquiry to all the surrounding circumstances to ascertain "whether the corporation, by reason of insolvency or lack of resources, has the financial ability to acquire the opportunity."¹³⁴ Courts have looked at anything from cash and liquid assets¹³⁵ to debts and delinquent liabilities¹³⁶ in reaching the conclusion that a corporation was either unquestionably financially unable, or too insolvent to obtain an opportunity. Additionally, a finding of corporate financial inability may be rebutted by the corporation's showing that the inability was due to either the fiduciary's delinquency as a corporate debtor or from failure to use good faith efforts in preventing or attempting to reverse such inability.¹³⁷

VII. INTRINSIC FAIRNESS

Suppose a family farm corporation's director went to a public auction with the purpose of purchasing a used corn planter and combine for the corporation. Since the weather was bad and no one was there that day, the director purchased the items for about half of what he thought they were worth. He then sold the items to his corporation for twice what he paid for them and kept the windfall profit.

During the ensuing litigation, the director would contend that the corporation would have to prove that the acquisition of the property is not only within its line of business, but is also an opportunity in which it had existing interest or expectancy.¹³⁸ Moreover, the corporation could not have an inter-

Considerations When Incorporating the Family Farm, 39 NEB. L. REV. 547, 549 (1960).

132. Comment, *Considerations When Incorporating the Family Farm*, 39 NEB. L. REV. at 548.

133. *Id.* at 549 n.9. Compare *John Kelly Co. v. Commissioner*, 326 U.S. 521, 524 (1946) (four to one ratio) with *Kraft Foods Co. v. Commissioner*, 232 F.2d 118, 127 n.17 (2d Cir. 1956) (thirteen to one ratio).

134. *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 81.

135. *Reiff v. Real Estate Comm'n*, 168 Conn. 201, —, 362 A.2d 975, 980 (1975). The finding that cash on hand and liquid assets were insufficient for the corporation to buy its own stock was coupled with the rule that a corporation ordinarily does not have an interest in its own stock; hence, an officer or director fails to usurp a corporate opportunity by purchasing such stock himself. *Id.*

136. *A. C. Petters Co. v. St. Cloud Enters.*, 301 Minn. at —, 222 N.W.2d at 86.

137. *Ellzey v. FYR-PRUF, Inc.*, 376 So. 2d at 1334.

138. See, e.g., *Durfee v. Durfee & Canning*, 323 Mass. 187, —, 80 N.E.2d 522, 529 (1948). The *Durfee* court held that the plaintiff corporation should be able to recover the profits that were reasonably capable of determination following a director's scheme to funnel money from the corporation to himself. *Id.* at —, 80 N.E.2d at 532. The defendant director had organized another company for the purpose of purchasing gasoline which it sold to the plaintiff corporation at a markup. *Id.* at —, 80 N.E.2d at 523-27.

est or expectancy unless the opportunity was "highly desirable if not absolutely necessary to the furtherance of [the corporate] . . . purpose."¹³⁹

The Massachusetts court refuted such an argument, however, rejecting the *Guth* "interest or expectancy" test.¹⁴⁰ The *Durfee* court held that "the true basis of the governing [corporate opportunity] doctrine rests fundamentally on the unfairness in the particular circumstances '[t]his calls for application of ethical standards of what is fair and equitable . . . [in] particular sets of facts'"¹⁴¹ Accordingly, even if the corporation would not have needed the corn planter and combine, in the example, the director would be responsible to the corporation because his act was fundamentally unfair.

The court in *Miller* has explicitly characterized how the intrinsic fairness test fits into the framework of corporate opportunity.¹⁴² Following a jurisdictional survey of various "tests," the Minnesota Supreme Court concluded that the most practical approach was the application of a bipartite line of a business/fairness test.¹⁴³ If a business opportunity has a reasonable or logical relation to the corporation's existing or prospective business, the acquiring officer should not be found liable if "the evidence establishes that . . . [he] did not violate his fiduciary duties of loyalty, good faith, and fair dealing toward the corporation."¹⁴⁴ Factors that the *Miller* court considered relevant in this equitable resolution were: (1) the nature of the officer's relationship to corporate management and control, (2) whether the officer was acting in his individual or official capacity when the offer was presented to him, (3) exploitation of corporate resources, (4) disclosure of the opportunity to the board and their response, (5) harm or benefit to the corporation of the acquisition, and (6) whether the officer's actions were in good faith and would have been exercised by a reasonable person under similar circumstances.¹⁴⁵

The factors which apparently carry the most weight in a court's finding of fundamental unfairness are exploitation of corporate resources, failure to obtain consent from the balance of directors, and lack of good faith. Exploitation of "hard" corporate resources is probably the only factor which is reprehensible enough to nearly always estop a fiduciary from acquiring a business opportunity.¹⁴⁶ Courts differ, however, in their views regarding the import of the consent and bad faith factors.

Generally, a corporate director may seize a corporate opportunity if the

139. *Id.* at __, 80 N.E.2d at 528.

140. *Id.* at __, 80 N.E.2d at 529.

141. *Id.* (quoting *BALLANTINE CORPORATIONS* 204-05 (rev. ed. 1946)).

142. *Miller v. Miller*, 301 Minn. at __, 222 N.W.2d at 81.

143. *Id.*

144. *Id.*

145. *Id.* at __, 222 N.W.2d at 81-82. See also *Ellzey v. FYR-PRUF, Inc.*, 376 So. 2d at 1333-34 (recent application of *Miller* two-prong test).

146. See *supra* notes 100-04 and accompanying text.

shareholders allow him to do so, provided the corporation's creditors are not harmed by such seizure.¹⁴⁷ The Delaware Court of Chancery, for example, has ruled that a corporation has implicitly rejected an opportunity if it has established that it is not in a position to take it; hence, the fiduciary is free to take the opportunity even if he learned about it in his fiduciary capacity.¹⁴⁸ On the other hand, according to the Pennsylvania Superior Court in *Hill v. Hill*,¹⁴⁹ a director must acquire the knowledge and approval of the shareholders, notwithstanding the fact that the corporation could not enjoy the opportunity because of its financial condition.¹⁵⁰

According to the last intrinsic fairness factor in *Miller*, a finding of bad faith is not necessary in imposing liability upon an officer who acquires a business opportunity.¹⁵¹ Conversely, good faith alone will not absolve the officer from liability.¹⁵² Moreover, there may be cases in which a business opportunity is so obviously essential to a corporation's continuing activities or is so intimately related to the corporation's business that bad faith is imputed to the director.¹⁵³

Since, "[i]n its overriding obligation to bring about substantial justice, a court of equity should not subject itself to the 'tyranny of a formula,'" ¹⁵⁴ courts have found it necessary to tailor the equitable doctrine of corporate opportunity to fit each case, especially in the context of close corporations.¹⁵⁵ Corporate fiduciaries have been found liable for the fruits of a continuing wrong.¹⁵⁶ Moreover, a fiduciary's passive role in the usurpation of a corporate opportunity will not exonerate him of liability if that role consisted of executing instruments necessary for the breaching fiduciary to further his ends.¹⁵⁷ When transactions involve corporate directors or officers, the heavy burden is on them to demonstrate that the transaction was fairly conducted.¹⁵⁸

147. *Hill v. Hill*, 279 Pa. Super. at —, 420 A.2d at 1082.

148. *Field v. Allyn*, 457 A.2d 1089, 1099 (Del. Ch. 1983).

149. 279 Pa. Super. 154, 420 A.2d 1078 (1980).

150. *Id.* at —, 420 A.2d at 1082. In his concurring opinion in *Hill*, Judge Lipez qualified the majority's interpretation with the caveat that no consent by shareholders does not necessarily mean an opportunity is corporate. *Id.* at —, 420 A.2d at 1084 (Lipez, J., concurring).

151. *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 82. *See also* *Production Mach. v. Howe*, 327 Mass. at —, 99 N.E.2d at 36 (1951).

152. *Miller v. Miller*, 301 Minn. at —, 222 N.W.2d at 82.

153. *Id.*

154. *Valle v. North Jersey Auto. Club*, 141 N.J. Super. 568, —, 359 A.2d 504, 511 (1976).

155. *See generally* Note, *Corporate Opportunity in the Close Corporation—A Different Result?* 56 GEO. L.J. 381 (1967).

156. *See Valle v. North Jersey Auto. Club*, 141 N.J. Super. at —, 359 A.2d at 510 (repercussions of wrongful acquisition not confined to date of occurrence).

157. *Borden v. Sinskey*, 530 F.2d 478, 483 (3rd Cir. 1976) (wife liable for usurpation of husband acting as her agent).

158. *Hill v. Hill*, 279 Pa. Super. at —, 420 A.2d at 1084 (Lipez, J., concurring). *See also* *Schreiber v. Bryan*, 396 A.2d at 519; *Robinson v. Brier*, 412 Pa. 255, —, 194 A.2d 204, 207

VIII. CONCLUSION

Anticipating every corporate opportunity that may arise in the context of the family farm corporation is an impossible task. This note should alert the farm incorporator that while the law in this area may be obscure, it should not be ignored.

Farmers should look beyond initial corporate formalities to prepare for future difficulties, especially when fellow shareholders are family members. One reason is that emotional strains of working with relatives are rooted in the earliest relationships among the shareholders.¹⁵⁹ Old rivalries in the classroom or on the football field will surely manifest themselves in corporate liquidation unless the proper precautions are taken.¹⁶⁰

Since family members usually know and trust each other, they will avoid planning ahead the way more dispassionate business venturers might. Given the peculiarities of the working relationship among related shareholders, however, family members should plan ahead *more* carefully than non-related shareholders.¹⁶¹

The purposes of the corporation should be stated with clarity in the articles and bylaws, or in a contract or resolution authorized by the directors. The clearer the statement of purpose, the less trouble a director will have in ascertaining what individual transactions he should rightfully first offer the corporation. For example, a farm contract which says that raising livestock will not be part of a land-holding corporation's activities may be specific enough to exempt livestock from being considered a corporate opportunity,¹⁶² but it does not disclose the intent of the parties regarding appropriation of additional land.¹⁶³

If there is any doubt as to whether or not an opportunity is corporate, it should be offered to the shareholders who embody the corporation. Approval by a majority of the owners of the "incorporated partnership"¹⁶⁴ should be sufficient to allow individual appropriation.¹⁶⁵

Additionally, shareholders should realistically plan ahead. If a divorce occurs, for instance, the court will look to the facts and circumstances surrounding the acquisition of the opportunity unless a previous arrangement has been made to establish the point in time beyond which there can be no

(1963).

159. Kinkead, *Family is a Passion Play*, 102 FORTUNE MAGAZINE 70, 71 (June 30, 1980).

160. *Id.*

161. *Id.* at 73. For instance, the founder's widow at one West Coast firm rotates presidents among her middle-aged sons "so they will know she loves them equally." *Id.*

162. See Decree at 8, *Sauer v. Moffitt*, No. 90-270, (Iowa 5th Jud. Dist. filed Sept. 2, 1981).

163. *Id.* at 31. The trial court based its decision upon the testimony of the parties as to "corporate philosophy." *Id.* There was apparently no written agreement to the contrary. *Id.*

164. *Burg v. Horn*, 380 F.2d at 901 n.3.

165. See *National Biscuit Co. v. Stroud*, 249 N.C. 467, —, 106 S.E.2d 692, 695 (1959) (the activities of a partnership may only be limited by the express will of the majority).

usurpation of corporate opportunity.¹⁶⁶

In Iowa, there is no statute that states that a corporation's director may not usurp an opportunity properly belonging to the corporation.¹⁶⁷ Nor do Iowa statutes address the close corporation specifically.¹⁶⁸ Family farm incorporators should not, however, mislead themselves by thinking that the issue does not exist. If a director is in doubt about whether or not an opportunity is corporate, the director should first seek the advice of fellow shareholders, and upon their approval, resolve to exclude the opportunity from corporate consideration.

Mary E. Waite

166. See *Borodinsky v. Borodinsky*, 162 N.J. Super. 437, —, 393 A.2d 583, 588-89 (1978). In *Borodinsky*, the husband, who was co-shareholder with his ex-wife, was not required to distribute among the shareholders assets which he had acquired since the date of a separation agreement. *Id.*

167. Liability has been imposed in other jurisdictions, however, and is predicated upon a breach of a general statutory duty. See e.g., *Sofate of America, Inc. v. Brown*, 171 Ga. App. 39, —, 318 S.E.2d 771, 776 (1984) (recognizing that appropriation of business opportunities is a violation of fiduciary duties); *Meiselman v. Meiselman*, 309 N.C. 279, —, 307 S.E.2d 551, 568-69 (1983) (recognizing that usurpation of a corporate opportunity constitutes a breach of the director's fiduciary duty); *Boyd v. Cooper*, 269 Pa. Super. 594, —, 410 A.2d 860, 861 (1979) (holding that an officer may be liable for damages resulting from a breach of his fiduciary duties when he acquires and uses for his benefit confidential information to the detriment of the corporation).

Georgia Code §22-714(a)(1)(C) (1983), which forbids officers or directors from appropriating "in violation of his duties . . . any business opportunity of the corporation," has been interpreted to mean that an opportunity must be the corporation's and obtained in violation of the fiduciary's duties. *Southeast Consultants, Inc. v. McCrary Eng'g Corp.*, 246 Ga. 503, —, 273 S.E.2d 112, 116 (1980). If such a statute were enacted in Iowa with the caveat that such a fiduciary duty is also imposed upon shareholders in close corporations, owners of family farm corporations would, at a minimum, be put on more explicit notice of the existence of corporate opportunity.

168. See generally IOWA CODE §§ 491.1-496A. 144 (1983). The vast majority of Iowa family farm corporations are closely held but Iowa statutory law does not distinguish between closely held corporations and those owned by more shareholders. *Id.* Some states, however, have statutes specifically applicable to close corporations. See ARIZ. REV. STAT. ANN. §§ 10-201 through 10-218 (West 1977 & Supp. 1984-85); CAL. CORP. CODE §§ 158, 202, 300, 421, 700, 706, 1111, 1201, 1800 (West 1977 & Supp. 1984) DEL. CODE ANN. tit. 8, §§ 341-356 (1983); ILL. ANN. STAT. ch. 32 §§ 1201-1216 (Smith-Hurd 1970 & Supp. 1984-85); KAN. STAT. ANN. §§ 17-7201 through 17-7216 (1983); ME. REV. STAT. ANN. tit. 13-A, §§ 102, 604, 606, 701 (Supp. 1984-85); MD. CORPS. & ASS'NS CODE ANN. §§ 4-101 through 4-603 (Supp. 1983); 15 PA. CONS. STAT. ANN. §§ 1371-1386 (Purdon Supp. 1984-85).