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A Survey of Recent Developments in the Law: Business Law

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BUSINESS LAW

A. States are Immune from Federal Patent-Infringement Suits in Federal Court

In Florida Prepaid Postsecondary Education Expense Board v. College Savings Bank, the U.S. Supreme Court held that, under the Eleventh Amendment, states are immune from patent infringement suits in federal court.\(^1\) The decision is the result of recent Eleventh Amendment jurisprudence effectively granting states complete sovereign immunity from private suits, based on federal rights, in both state and federal courts.\(^2\) An examination of College Savings Bank reveals that this jurisprudence renders businesses powerless to protect patents against state infringement.

College Savings Bank (College Savings), located in Princeton New Jersey, patented a financing method in which certificates of deposits were sold to finance college tuition.\(^3\) The investment, structured like an annuity, and known as “CollegeSure CD,” was designed to ensure sufficient funding for parents to meet future college tuition costs for their children.\(^4\) Florida Prepaid Postsecondary Education Expenses Board (Florida Prepaid), created as an entity of the State of Florida, began selling similar prepaid college investment annuities.\(^5\) College Savings sued Florida Prepaid, alleging that Florida’s investment contract infringed upon College Saving’s patent.\(^6\)

At trial, College Savings alleged that Florida Prepaid had violated the Patent Remedy Act\(^7\) by willfully infringing upon its

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4. See id.
5. See id.
6. See id.
patent. Florida Prepaid argued that based upon a recent Supreme Court decision, *Seminole Tribe v. Florida*, states could not be sued without their consent and therefore the suit should be dismissed. The crux of Florida Prepaid's argument was that Congress' use of its Article I powers to abrogate sovereign immunity was unconstitutional. The district court disagreed with this argument and denied Florida Prepaid's motion to dismiss. The Federal Court of Appeals affirmed, holding that Congress clearly intended to abrogate states' immunity, and that the power to abrogate was granted by section five of the Fourteenth Amendment.

Statute provides:

(a) Except as otherwise provided in this title, whoever without authority makes, uses, offers to sell, or sells any patented invention, within the United States or imports into the United States any patented invention during the term of the patent therefor, infringes the patent.
(b) Whoever actively induces infringement of a patent shall be liable as an infringer.
(c) Whoever offers to sell or sells within the United States or imports into the United States a component of a patented machine, manufacture, combination or composition, or a material or apparatus for use in practicing a patented process, constituting a material part of the invention, knowing the same to be especially made or especially adapted for use in an infringement of such patent, and not a staple article or commodity of commerce suitable for substantial noninfringing use, shall be liable as a contributory infringer.

Id.

9. *See id.* at 2204.
10. The Patent Clause of Article I provides that “Congress shall have Power . . . [t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.” U.S. CONST. art. I, § 8, cl. 8. The Commerce Clause provides that “Congress shall have Power . . . [t]o regulate Commerce with foreign Nations, and among the Several States, and with the Indian Tribes.” U.S. CONST. art. I, § 8, cl. 3.
The Supreme Court began its analysis by quoting the Eleventh Amendment which provides that, "[t]he Judicial Power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State." The Court went on to note that although taken literally, the text of the Eleventh Amendment restricts only the Article III diversity jurisdiction of the federal courts. The Eleventh Amendment has, for over one hundred years, not been taken for its literal meaning, but instead for what it was understood to mean when ratified, that "each State is a sovereign entity in our federal system; [and that] it is inherent in the nature of sovereignty not to be amenable to the suit of an individual without its consent." The Court thus framed the issue as "whether Congress has 'unequivocally express[e]' its intent to abrogate the immunity," and whether Congress has acted "pursuant to a valid exercise of power."

In resolving the issues, the Court agreed that Congress had unequivocally expressed its intention to abrogate sovereign immunity when it added to the Patent Remedy Act "[a]ny State... shall not be immune, under the eleventh amendment of the Constitution of the United States or under any other doctrine of sovereign immunity, from suit in federal court... for infringement of a patent." Although the Court noted that Congress clearly intended to abrogate states' sovereign immunity, whether Congress had the power to do so, was entirely another matter.

The Court noted that "Congress justified the Patent Remedy Act under three sources of constitutional authority: the Patent Clause... the Interstate Commerce Clause... and § 5 of the Fourteenth Amendment." The Court quickly noted that based on its decision in *Seminole Tribe of Florida v. Florida*, "Congress may not..."
abrogate state sovereign immunity pursuant to its Article I powers.\textsuperscript{21} As for abrogating states’ sovereign immunity powers under the Fourteenth Amendment, the Court noted that section five of the amendment allowed Congress to abrogate for appropriate legislation.\textsuperscript{22} But the court added, in order for legislation to be appropriate, and thus allow “Congress to invoke § 5, it must identify conduct transgressing the Fourteenth Amendment’s substantive provisions, and must tailor its legislative scheme to remedying or preventing such conduct.”\textsuperscript{23}

Here, the Court held that, “in enacting the Patent Remedy Act, however, Congress identified no pattern of patent infringement by the States, let alone a pattern of constitutional violations.”\textsuperscript{24} The Court reasoned that although the infringement of a patent interfered with the owner’s right to exclude others, it did not amount to a constitutional deprivation of property.\textsuperscript{25} Because the court concluded that the Congressional record does not support the notion that occasional infringement by states did not rise to the level of systematic deprivation of property, the legislation was “so out of proportion to a supposed remedial or preventive object that [they] cannot be understood as responsive to, or designed to prevent, unconstitutional behavior.”\textsuperscript{26}

Essentially, what \textit{Florida Prepaid Postsecondary Education Expense Board v. College Savings Bank} reveals is that so long as states only occasionally infringe upon patents where state remedies are not available, businesses are powerless in protecting their property. Indeed, so long as systematic infringement never occurs, Congress too, is powerless to provide a remedy for the taking of a federally granted property right.

\textbf{B. Baseball's Anti-Trust Exemption: Still Valid?}

In \textit{Minnesota Twins Partnership v. State}, the Minnesota Supreme Court examined the business of baseball and its unique exemption from antitrust suits.\textsuperscript{27} This action presented an opportunity to

\begin{footnotesize}
\begin{enumerate}
\item \textit{College Sav. Bank}, 119 S. Ct. at 2205.
\item \textit{See id.} at 2205-06.
\item \textit{See id.} at 2207.
\item \textit{Id.}
\item \textit{See id.} at 2208.
\item \textit{Id.} at 2210 (citing City of Boerne v. Flores, 521 U.S. 507, 532 (1997)).
\item \textit{See Minnesota Twins Partnership v. State}, 592 N.W.2d 847, 853 (Minn. 1999).
\end{enumerate}
\end{footnotesize}
clarify baseball’s exemption from antitrust legislation, specifically whether the Twin’s proposed sale and relocation of the team to another state fell within the exemption. 28

The ruling came after Minnesota’s Attorney General served the Twins with civil investigative demands (CIDs) designed to gather information to be used in the state’s investigation of possible state antitrust laws violation. 29 The Twins responded by filing a motion for a protective order in district court. 30 The district court denied the motion and granted the state’s motion to compel compliance with the CIDs. 31 The court of appeals denied review of the district court’s order, holding that the case presented premature issues and that the Twins were free to assert the antitrust exemption as an affirmative defense should prosecution occur. 32 On appeal, the Minnesota Supreme Court reversed the district court and held that the proposed sale and relocation of the team were exempt from federal and state antitrust laws. 33 Therefore, enforcement of the investigative demands was outside the Attorney General’s authority because no enforcement action could follow the investigation. 34

In October 1997, the Minnesota Twins announced that it had reached a deal to sell the team to a North Carolina group. 35 The deal was made contingent upon the Minnesota Legislature’s refusal to provide public funding of a new stadium. 36 All stadium-financing bills were refused by the legislature. 37 In December 1997, the Minnesota Attorney General served the Twins with civil investigation demands. 38 The demand requested a broad array of documents “concerning . . . the financial viability of the Metrodome, . . . the methods used by other professional baseball

28.  See id.
29.  See id. at 849.
30.  See id. at 850. A motion for a protective order is made under MINN. R. CIV. P. 26.03.
31.  See Minnesota Twins Partnership, 592 N.W.2d at 850.
32.  See id.
33.  See id. at 856.
34.  See id.
35.  See id. at 849.
36.  See id.
37.  See id.
38.  See id. “[T]he attorney General’s Office has the authority to demand discovery from persons suspected of violating state laws governing trade and commerce. MINN. STAT. § 8.31, subd. 2 (1998). This discovery is demanded through documents called civil investigative demands which issue directly from the Attorney General’s Office.” Id. at 849 n.2.
teams to obtain a new stadium, and the potential purchase of the Twins." The demand also requested information dating back to the Twins relocation from Washington in 1961, as well as information related to the governance, structure and revenues of Major League Baseball.

The Twins argued that the investigation was precluded by professional baseball’s exemption from antitrust laws; that the investigation was precluded by the commerce clause of the United States Constitution; and that the CIDs were overly broad and that compliance would be burdensome. The state argued that its concern regarding a possible Twin’s boycott of Minnesota justified the state’s investigation, saying, “it is reasonable to infer that the owners of MLB [Major League Baseball] teams are acting in concert to affect an illegal boycott and/or a price fixing agreement.” Furthermore, the state argued that MLB was “unlawfully exercising joint monopoly power.” The court framed the issue as an inquiry into the precise scope of professional baseball’s exemption from antitrust laws.

The court began its analysis by noting that Minnesota’s antitrust laws are interpreted with federal court’s construction of federal antitrust laws. Under federal construction, both federal and state laws are broadly construed. The court noted that “[t]his means that ‘exemptions from the antitrust laws must be construed narrowly.’” The court noted that since Federal Baseball Club of Baltimore, Inc. v. National League of Professional Baseball Clubs, Inc., baseball has been exempt from federal antitrust laws. In Federal Baseball, a suit was brought after the National League bought out seven of the eight teams of the Federal League, leaving Baltimore,

39. Id. at 849-50.
40. See id. at 850.
41. See id.
42. Id. at 851.
43. Id.
44. See id.
45. See id. (citing State of Minn. v. Alpine Air Prods., Inc., 490 N.W.2d 888, 894 (Minn. Ct. App. 1992)).
46. See id. at 851-52 (citing Minnesota-Iowa Television Co. v. Watonwan T.V. Improvement Ass’n, 294 N.W.2d 297, 305 (Minn. 1980)).
47. Id. at 852 (quoting Union Labor Life Ins. Co. v. Pireno, 458 U.S. 119, 126 (1982)).
49. See Minnesota Twins Partnership, 592 N.W.2d at 852.
the eighth team, without any competitors. The Supreme Court held that the Sherman Antitrust Act did not apply to baseball because baseball was not interstate commerce.

Another baseball case came to the Supreme Court thirty years later in *Toolson v. New York Yankees, Inc.* In *Toolson*, a pitcher argued that baseball’s reserve system violated antitrust law. The Court, per curiam, noted that Congress had declined to legislatively overrule professional baseball’s exemption since its ruling in *Federal Baseball* and that any change should come from Congress.

The next major case to come before the U.S. Supreme Court was also, according to the *Minnesota Twins Partnership* Court, the most thorough look at baseball’s exemption from antitrust. In *Flood v. Kuhn* another case involving a challenge to baseball’s reserve system, player Curt Flood sued after unwillingly being traded to a new team. The district court had held that baseball’s antitrust exemption applied and the court of appeals affirmed. On appeal, the U.S. Supreme Court affirmed. The Court’s opinion was consistent with the district court’s holding:

[T]he exemption set forth in *Federal Baseball* is limited strictly to professional baseball, and despite frequent invitations to review the issue, Congress has allowed the anomalous exemption to remain. The court acknowledged that the legal footings for the exemption were no longer valid, stating that “[p]rofessional baseball is business and it is engaged in interstate commerce,” but held that baseball remained exempt from federal antitrust

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50. See *Federal Baseball Club*, 259 U.S. at 207.
51. See id. at 208-09 (“The business is giving exhibitions of baseball, which are purely state affairs. . . . The transport [of teams] is a mere incident, not the essential thing. That to which it is incident, the exhibition, although made for money would not be called trade of commerce in the commonly accepted use of those words.”). The Minnesota Supreme Court noted that the reasoning in *Federal Baseball Club* would seem to apply to nearly all live performances. See *Minnesota Twins Partnership*, 592 N.W.2d at 852. The United States Supreme Court has declined to extend such an exemption. See id.
52. 346 U.S. 356 (1953).
53. See id. at 362-63. The reserve system is predicated on a reserve clause in a player’s contract that gives the team exclusive rights to a player. See id. at 364 n.10.
54. See id. at 357.
55. See *Minnesota Twins Partnership*, 592 N.W.2d at 853.
57. See id. at 264-65.
58. See id. at 266-67.
59. See id. at 285.
law under the stare decisis of *Federal Baseball* and *Toolson*. 60

The Minnesota Supreme Court opinion concluded by quoting *Toolson* 61 stating that “the business of baseball” is exempt from antitrust legislation based on *stare decisis* and congressional inaction. 62

Under federal construction, the *Twins* court concluded, “the great weight of federal cases” hold that *Flood* exempts the entire business of baseball from federal and state antitrust claims. 63 The court went on to say that it would follow the lead of these cases and “conclude the business of professional baseball is exempt from federal antitrust laws.” 64 The court then stated that the sale and relocation of the Twins was an integral part of the business of baseball and falls within the exemption. 65

The problem that emerges in baseball antitrust jurisprudence is clear. The United States Supreme Court granted exemption to baseball in a time when “gilded age” judges—judges who disagreed with federal intervention of business—sat on the court. From this judicially declared exemption, Congress has continually refused to override it. As a result, lower courts are forced to rely on *stare decisis* and congressional inaction, and thus uphold an exemption that is denied to all other professional sports or any other business entity.

C. Must a Lack of Marketability Discount be Applied when the Court Orders a Minority-Shareholder Buyout?

In *Advanced Communication Design, Inc. v. Follett*, the Minnesota Court of Appeals examined whether in a closed-corporation buyout, if the oppressive shareholder may apply a lack of marketability discount to a minority shareholder’s purchase price. 66 The court held, as a matter of first impression, that “a marketability discount cannot be used unfairly by controlling or oppressing shareholders to benefit themselves to the detriment of the minority

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60. See *Minnesota Twins Partnership*, 592 N.W.2d at 854.
63. *Minnesota Twins Partnership*, 592 N.W.2d at 854.
64. Id. at 856.
65. See id.
Marco Scibora formed Advanced Communication Design (ACD) in 1986. Mr. Scibora was the company's sole shareholder until 1990 when two others, including Brian Follett, each became one-third owners in ACD by each purchasing 1500 shares of nonvoting stock. The two investors also signed an agreement giving ACD the right of first refusal to purchase any departing stockholder's shares. In 1996, Fran Scibora, Marco Scibora's wife, became ACD's chief operating officer. Her compensation was to include 1500 shares of nonvoting stock, which would be converted to common stock provided she remained employed with ACD for one year.

Eight months after Mrs. Scibora became chief operating officer, she demoted Brian Follett, who was the only remaining shareholder besides her husband, from vice-president to manager. Mr. Follett's compensation was also substantially reduced. Mr. Follett subsequently resigned from ACD and sued after Mr. Scibora offered $24,646 for his 1500 shares. Mr. Follett alleged bad faith and a breach of fiduciary duty, and after a bench trial, the court ordered the Sciboras to buy back Mr. Follett's stock for $475,381.76 The Sciboras appealed, arguing that as a matter of law, the court must apply a lack of marketability discount in a forced buyout of a minority shareholder.

The court began its analysis by noting that "[t]here is no Minnesota law on the application of a lack of marketability discount." The court then examined two recent New Jersey cases addressing the issue. In Balsamides v. Protameen Chemicals, Inc., the district court ordered a forced oppressor shareholder buyout by an

67. Id. at 711.
68. See id. at 709.
69. See id.
70. See id.
71. See id.
72. See id.
73. See id.
74. See id. Mr. Follett's salary was reduced from $70,000 annually to $55,000 annually. See id.
75. See id.
76. See id.
77. See id.
78. See id. at 710.
79. See id.
oppressed shareholder. The district court also ordered that a thirty-five percent lack of marketability discount be applied to the sale. New Jersey's appellate court reversed, holding that a lack of marketability discount was inappropriate when the transaction resulted in the buyer obtaining total ownership of the corporation. New Jersey's Supreme Court reversed the appellate court's holding, stating "we find that courts in deciding whether to apply a marketability discount to determine the 'fair value' of shares of a shareholder forced to sell his stock in a judicially ordered buy-out must take into account what is fair and equitable."

The Balsamides court explained that allowing an oppressor shareholder, in a court ordered buyout, to receive a non-discounted value, would reward the oppressor shareholder for its oppressive actions. The court imposed a lack of marketability discount, stating, "to do otherwise would be unfair." In discussing the Balsamides case, the Minnesota Court of Appeals reasoned that the Balsamides court addressed an oppressed shareholder buying out an oppressive shareholder. The court noted that Balsamides was distinguishable from the issue before them, because the decision stated, "[w]hat to do when it is the oppressing shareholder who is given the buy-out option is a harder question that we need not decide."

The court then looked at a second case deciding the same issue, Lawson Mardon Wheaton, Inc. v. Smith, which involved a group of shareholders who owned fifteen percent of a corporation's stock and declined to approve a restructuring plan. The trial court found that a marketability discount should be applied because the dissenting shareholders had caused "extraordinary circumstances" that may have prevented an initial

81. See id. at 725.
82. See id. at 726.
83. Id. at 735.
84. See id. at 736 ("[T]he equities of the case quite clearly lie with [the oppressed shareholder], it would be unfair to allow [the oppressor shareholder] to receive [the corporation's] undiscounted value.").
85. Id. at 736.
87. Id. at 710 (quoting Balsamides, 734 A.2d at 738).
88. 734 A.2d 738 (N.J. 1999).
89. See id. at 741-42.
public offering. The appellate court affirmed. The New Jersey Supreme Court reversed, holding that:

The very nature or the term "fair value" suggests that courts must take fairness and equity into account in deciding whether to apply a discount to the value of the dissenting shareholder's stock. Marketability discounts should not be applied when determining the "fair value" of dissenting shareholders' stock in an appraisal action. The dissenters in this case wanted liquidity for their stock and wanted to sell their stock in a corporation now controlled by new management in whom they lacked confidence. That is not an "extraordinary circumstance."

The Minnesota Court of Appeals reasoned that the New Jersey Supreme Court reconciled decisions to erect a "guiding principle—a marketability discount cannot be used unfairly by controlling or oppressing shareholders to benefit themselves to the detriment of the minority or oppressed shareholders." Under current Minnesota law, if a majority shareholder oppresses a minority shareholder, equity demands a marketability discount not be applied to a valuation of stock in a forced buyout.

D. Court Reaffirms Restricted Review of Special Litigation Committees

In Driling v. Berman, the Minnesota Court of Appeals rejected an opportunity to expand current Minnesota law to scrutinize a special litigation committee's recommendation "by inquiring into the reasonableness of the committee's decision in addition to the committee's independence and good faith." The action, a derivative suit brought on behalf of Grand Casinos, alleged that members of Grand Casino's executive staff "breached their fiduciary duty and misused corporate assets by: (1) using Grand's

90. See id. at 744.
91. See id.
92. Id. at 748, 750.
94. See id.
95. 589 N.W.2d 503 (Minn. Ct. App. 1999).
96. Id. at 507.
funds to make ... investments in Stratosphere Corporation, (2) misappropriating and misusing material, nonpublic corporate information to profit personally through insider trading, and (3) exposing Grand to liability for violations of ... securities laws." In response to the suit, Grand appointed a special litigation committee. The committee, after reviewing numerous documents but offering no analysis, recommended none of the claims be pursued. Based on the committee's recommendation, the district court dismissed the suit.

On appeal, the court noted that this was not an issue of first impression, and that their review was strictly limited to whether the "committee was independent and conducted its investigation in good faith." The court rejected the contention that the brevity of a special litigation committee report is indicative of an investigation that was not conducted in good faith. As for the investigation, the court noted that when an investigation was conducted by competent members, and where the investigation was procedurally adequate, generally the investigation was conducted in good faith.

E. No Breach of Fiduciary Duty to Violate a Strict Confidentiality Agreement Leading to Failure of Proposed Public Offering and Subsequent Liquidation

In another derivative suit, St. James Capital Corp. v. Pallet Recycling Assoc., the court declined to extend a corporate director's duty of care to encompass compliance with a confidentiality agreement surrounding a proposed buyout of a corporation in order to protect the company's creditors. The suit began when Pallet Recycling Association of North America, Inc. (PRANA) was offered $10 million for the sale of the entire company. The purchase agreement was conditioned upon

97. Id. at 505.  
98. See id. at 506.  
99. See id.  
100. See id.  
101. Id. at 507.  
102. See id. at 509-10.  
103. See id. at 510.  
104. 589 N.W.2d 511 (Minn. Ct. App. 1999).  
105. See id. at 515.  
106. See id. at 514.
PRANA’s keeping the terms of the sale confidential. Despite the agreement, the terms of sale became public, resulting in the sale falling through, and PRANA’s liquidation of ten to twenty percent of the original sale price.

The court noted that Minnesota had never extended a corporate director’s duty of care to include completing a sale or public offering so as to protect the creditors of that particular company. To do so, the court noted, would defy the business judgment rule and instead interject a corporation’s creditors’ into the day-to-day management of a company.

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107. See id.
108. See id.
109. See id. at 515.
110. See id. at 516.