Tamakong v. Nakamura, 1 ROP Intrm. 608 (1989)

TAKEO TAMAKONG, HARUJI NGIRAKED, NGIRAKASAO TKEL, HASHINDA S. KEBEKOL, Individually and on behalf of all shareholders similarly situated and BELAU TRANSFER AND TERMINAL COMPANY,
Appellants,

v.

KUNIWO NAKAMURA,
Appellee.

CIVIL APPEAL NO. 12-87
Civil Action No. 66-84

Supreme Court, Appellate Division
Republic of Palau

Opinion
Decided: May 8, 1989

BEFORE: ARTHUR NGIRAKLSONG, Associate Justice; ROBERT A. HEFNER, Associate Justice; FREDERICK J. O'BRIEN, Associate Justice Pro Tem.

HEFNER, Associate Justice:

THE DOCK-ET

The record in this case reveals that this action was commenced by three shareholders and the corporation in which they hold shares, Belau Transfer & Terminal Company (the corporation). The sole defendant is the general manager of the corporation.

Belau Transfer & Terminal Company was incorporated in 1971 to provide stevedoring and warehousing services for the dock facilities serving Palau. It has an exclusive lease for ⊥609 the dock area. Over the years, it has expanded and diversified its operations beyond the services it provides at the dock area.

In 1972 the defendant, Kuniwo Nakamura, became the general manager of the corporation and has remained in that capacity to the present time. As general manager, he is the chief executive officer of the business.

The corporation has been profitable over the years. [1] However, in 1983 a group of shareholders joined together for the purpose of ousting the defendant as general manager. A

[1] The trial court found that the book value of each share increased from $10 to $123 per share and each shareholder received a return of 585% on his/her original investment.

"special shareholders meeting" was held on April 23, 1984, with 17 persons present. Among other actions taken at this meeting, the shareholders voted to remove the defendant from office. This meeting was found by the trial court to be ineffective because, in 1981, there was an amendment to the Articles and By-laws of the corporation which required 40% of the shareholders to be present at any special shareholders meeting. This requirement was not met at the April, 1981 meeting.

Since the defendant remained in his position, the plaintiffs filed this suit to remove the defendant, for damages and other relief. The trial court denied the plaintiffs any relief based on findings that the plaintiffs failed to prove that any acts of the defendant were detrimental to the ⊥610 corporation. This appeal followed.[2]

THE CARRIER - AT SEA OR ON FIRM GROUND?

The vehicle the plaintiffs chose to navigate these litigious waters is a shareholders derivative action - at least that's how the parties and the trial court treated it.[3]

Rule 23.1 of the Rules of Civil Procedure, sets forth the requirements for instituting a shareholders derivative suit and a review of plaintiffs' complaint reveals general compliance.[4]

Such an action is brought by one or more shareholders of a corporation to enforce a corporate right. *Lewis v. Chiles*, 719 F.2d 1044, 1047 (9th Cir. 1983). The term "derivative" is used because the alleged wrong to be redressed is against the ⊥611 corporation. The shareholder sues to recover for the corporation and not for him/herself. *Klopstock v. Superior Court of San Francisco*, 108 P.2d 906, 908 (Cal. 1941).

The purpose of a derivative action is to allow shareholders to protect the rights of the corporation where the corporation fails or refuses to take appropriate action for its own protection. *Daily Income Fund, Inc. v. Fox*, 464 U.S. 523, 529, 104 S.Ct. 831, 834-35 (1984). As such, the corporation is a necessary party to any derivative action but is named as a defendant based upon its failure or refusal to act. *Ross v. Bernard*, 396 U.S. 531, 539, 90 S.Ct. 733, 738 (1970). Although the corporation is the real party in interest in any derivative action, it is not

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[2] After the appeal was filed, the defendant moved to dismiss it as plaintiffs were late in payment of estimated transcript costs. A previous appellate panel denied this motion, finding no prejudice.

[3] Paragraph 2 of plaintiffs' complaint alleges the action is brought by the named shareholders and on behalf of all other shareholders of the corporation ". . . in the right of Belau Transfer & Terminal Company and for its benefit." The defendant has labeled the action as derivative (Statement of Case, p.-v-, Appellees brief).

[4] Rule 23.1 requires the complaint to be verified and must include allegations, inter alia, that the plaintiffs were shareholders at the time of the transaction of which they complain; and the efforts, if any, made by the plaintiffs to obtain the action they desire from the directors and the reasons for their failure to obtain the action or for not making the effort. The action cannot be maintained if it appears the shareholders cannot fairly or adequately represent the other shareholders similarly situated.

proper to name the corporation as a plaintiff because this would destroy the derivative nature of the shareholders action.

In the instant case, the corporation is named as a party plaintiff. This is clearly a misalignment of the parties. However, the parties have argued and the trial court decided this case based upon plaintiffs' original alignment of the parties and, therefore, we will proceed on the merits of this appeal.

STANDARD OF REVIEW

In reviewing the opinion of the trial court, the appellate court may only set aside findings and conclusions which are clearly erroneous. 14 PNC § 604(b).

⊥612 ISSUES ON APPEAL

The issues on appeal as framed by the plaintiffs/appellants are:

1) Whether defendant holds a fiduciary responsibility to the shareholders of BT&T;
and

2) whether defendant breached his fiduciary responsibilities to BT&T and its shareholders.

THE DEFENDANT - CAPTAIN OR CREWMAN?

The basic premise behind a shareholder's derivative suit is that some wrong has been done to the corporation itself thereby effecting the shareholders who own stock. *Haberman v. Washington Public Power Supply System*, 744 P.2d 1032, 1060, as amended 750 P.2d 254 (Wash. 1988). In this case, plaintiffs allege that to make a demand on the corporation through the officers or the Board of Directors that defendant be removed as a corporate employee would be futile as they are under the control of defendant.

Defendant is the general manager of BT&T and, as such, an employee of the corporation. It is without question that officers and directors of any corporation owe a fiduciary duty to the corporation. *Unicore, Inc. v. Thurman* , 599 P.2d 925, 927 (Colo. App. 1979). Here, plaintiffs argue that defendant likewise owes a fiduciary duty by virtue of his complete control over the board of directors and officers. However, plaintiffs have not brought forth any evidence, other than defendant's family relationship with some of the officers and board members, which would bear out this allegation.

⊥613 Abraham Lincoln once noted that if you call a dog's tail a "leg" the dog still only has four legs despite the labeling of his tail as a leg. Similarly, in this case, plaintiffs have made various allegations as to why defendant, an employee, should be considered as a fiduciary to BT&T. If such were the case, this would indeed be the tail wagging the dog. The uncontradicted evidence

is that the defendant was neither an officer nor a director of the corporation but only an employee and, as such, was subject to removal by the persons who are in an actual fiduciary relationship to the corporation - the officers and directors.

The trial court did not treat the defendant as a fiduciary and upon review we do not find this to be error.

IS THE CORPORATION SHIPSHAPE?

In light of what we have said as to the purpose of a shareholders derivative suit, we now determine if the trial court erred when it found that the corporation was not remiss in not removing the defendant and recovering from the defendant any losses assertedly suffered by the corporation.[5]

⊥614 The findings and conclusions of the trial court do not address specifically each and everyone of the plaintiffs' grievances but the lower court focused on the testimony about the discrepancies found by the auditors. Succinctly put, there was found to be irreconcilable differences between the inhouse audit and accounts and the audit done by an independent auditor (Calma).

It is the burden of the plaintiffs to show some damage to the corporation. *Goodman v. DeAzoulay*, 554 F. Supp. 1029, 1038 (E.D. Pa. 1983). The trial court found no damages to the corporation and in reviewing the court's findings on a clearly erroneous standard, we are not convinced that it erred. What plaintiffs have done is raise various questions about the propriety of defendant's activities vis-a-vis the corporation, but they have put forth nothing to show that the corporation has been damaged by defendant's management.

As noted above, the trial court found that there were discrepancies between the Calma audits for the years 1980-85 and those done inhouse for the same period. However, the court found that these discrepancies resulted "from differing treatment of accounts, adjustments and differing procedures between CPA's and lay bookkeepers." Calma testified that he found no "red flag" indicating fraud on defendant's part. The court noted that plaintiffs have the burden of proof but brought forth nothing other than "innuendo and suggestion" which would lead the court to believe the discrepancies encountered show conversion or misdealing.

⊥615 Examination of Calma by plaintiffs did not show any wrongdoing by defendant and numerous theories have been advanced as to the reason for the various discrepancies between the two audits. Plaintiffs are correct in their assertation that "we don't know the reason for these

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[5] The plaintiffs assert several acts by the defendant which, it is claimed, caused the corporation to lose money. These acts include: (1) the failure of the defendant to have audits of the corporate books done by "outside" auditors; (2) lost corporate opportunities because the defendant personally engaged in business which the corporation should have been involved in; (3) the failure of the defendant to pay taxes timely which resulted in a penalty to the corporation; (4) excessive compensation paid to the defendant; and (5) improper interlocking director relationships (even though the defendant was not a director of Belau Transfer).

discrepancies," however, the reason we don't is that the plaintiffs apparently never engaged in any discovery in order to ascertain the reasons for these discrepancies. Plaintiffs clearly have a right to the corporation's books and records and could have produced their own expert to analyze these books and testify as to the reasons for any discrepancies. Instead, plaintiffs chose to rely on defendant's expert.

FIXING THE RIGGING

Plaintiffs met on April 13, 1984, at a "special shareholders meeting" and attempted to elect new corporate officers. The trial court found this meeting "ineffective for the purpose of authorizing the actions taken" because the meeting did not conform with the requirements of the Amended Articles of Incorporation and By-Laws of the corporation. Specifically, the number of shareholders present was insufficient to call a special meeting and 30 days notice of such meeting was not given. The court found that plaintiffs were "estopped" from challenging the propriety of an amendment increasing the number of shareholders necessary to call a special meeting from 10% to 40% since "the Articles and By-Laws were properly amended in this regard some three (3) years ⊥616 before plaintiffs initiated this action." The court then found plaintiffs to have had constructive notice of this change as such was filed with the Registrar of Corporations. The court specifically found the challenged amendment proper and noted its filing. Since the corporation has an annual shareholder meeting every December and there is no evidence that plaintiffs ever challenged the amendment, such must be deemed ratified by acquiescence.

With regard to defendant's refusal to turn over the shareholder lists to plaintiffs upon demand, while these lists are clearly the property of the shareholders, the plaintiffs could have brought suit to compel the board to turn over those lists. Defendant's actions, as an employee of the corporation, did not preclude an action to compel the corporation itself to give plaintiffs the shareholder lists.

THE CORPORATE SHIP SAILS

Plaintiffs made various allegations against defendant contending that his actions as general manager somehow damaged the corporation. The trial court rejected these allegations since plaintiffs offered no proof as to damages on defendant's alleged self-dealing. The trial court found for defendant noting that it could not base any judgment on "conjecture, speculation or guess." Nothing before this court provides any basis for finding any of the trial court's findings erroneous. Rather, we are in complete accord. Plaintiffs made their ⊥617 allegations and failed to prove them. Under such circumstances, they must fail.

Based upon the foregoing, the judgment of the trial court in favor of defendant Kuniwo Nakamura is hereby AFFIRMED.