**IN THE**
**SUPREME COURT OF NORTH DAKOTA**

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**Supreme Court No. 990212**
**Cass County Civil No. 96-88**

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**State of North Dakota, ex rel.**
**Heidi Heitkamp, Attorney General,** **Plaintiff-Appellee,**

**-vs-**

**Family Life Services, Inc., d/b/a**
**Family Life Credit Services, et al.** **Defendants-Appellants.**

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**ON APPEAL FROM THE JUDGMENT**
**OF THE CASS COUNTY DISTRICT COURT**
**HONORABLE DONOVAN FOUGHTY, PRESIDING**

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# REPLY BRIEF FOR APPELLANT FAMILY LIFE SERVICES, INC.

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### I. THE RELEVANT POWERS OF BOTH THE ATTORNEY GENERAL AND THE TRIAL COURT IN THIS CASE ARE DEFINED BY STATUTE.

In its opening brief, Family Life Services, Inc. (FLS) demonstrated that the Attorney General had no statutory authority to bring this action to dissolve FLS or remove any member of its board, and that the trial court had no statutory authority to dismantle and reconstitute that Board. In her responsive brief, the Attorney General has attempted to escape from the statutory limits upon her powers with the bold claim that she possesses general "authority to represent and protect the public interest and general welfare of the citizens of this state," and that statutes enacted by the people's elected representatives in the North Dakota legislature merely "supplement" the "Attorney General's traditional public interest authority...." A.G. Br. 49-50.

According to her view, statutes are instruments to be selected or discarded at her discretion to implement the public interest and general welfare as the Attorney General determines them to be, **not** instruments designed by the state legislature to govern the Attorney General's pursuit of the public interest and general welfare. Only by inverting the executive power over the legislative can the Attorney General make the remarkable claim that the more expansive remedies available under N.D.C.C. ch. 10-33, enacted after the institution of this law suit, apply to this case, **but** that the limitations governing the filing of a law suit under N.D.C.C. Section 10-33-107 do not. A.G. Br. 52-54.

Not only has the Attorney General exalted the executive over the legislative department, but she also has claimed that the trial court had "inherent equitable powers...

independent of any statute" to dismantle and reconstitute the FLS Board. A.G. Br. 51, 57-58. Relying solely upon precedents from other states, she has asserted that "'a judge sitting in equity has **no limit** on his or her flexibility in devising remedies....'" (Emphasis added.) That is not the law in North Dakota. As this Court ruled in Burr v. Trinity Medical Center, 492 N.W. 2d 904, 908 (N.D. 1992): "it would be inappropriate for district courts to haphazardly fashion equitable remedies with no deference to codified law."

According to the "codified list of priorities of authoritative law in North Dakota," as set forth in N.D.C.C. 1-01-03 and 1-01-06, the trial judge should have dismissed this law suit for lack of subject matter jurisdiction, or in the alternative, declined to order the wholesale dismantling and reconstituting of the FLS Board.

## II. THE ATTORNEY GENERAL HAD NO STATUTORY AUTHORITY TO SEEK DISMANTLING AND RECONSTITUTION OF THE FLS BOARD.

According to her first amended complaint, the Attorney General brought this action "in the public interest pursuant [to] the common law and to authority granted under ... N.D.C.C. ch. 10-37, ch. 10-26 and ch. 32-13." I J.A. 125. All six claims for relief, however, were based solely upon alleged statutory violations. I J.A. 125, 136-39. Further, the trial court's Conclusions of Law found statutory violations, not breaches of any common law rule. I J.A. 504-11. Unlike State ex rel. Burgum v. Hooker, 87 N.W. 2d 337 (N.D. 1957), upon which the Attorney General has principally relied (A.G. Brief 49-50), there is neither allegation nor proof of a specific violation of the common law. Therefore, both the Attorney General's authority to bring this action and the trial court's

authority to fashion an order must be drawn from the statutes upon which the complaint and judgment rest, not an amorphous appeal to "the general welfare" or the "public interest." *Contrast* A.G. Br. 49-51, 57 *with* State ex rel. Miller v. District Court, 124 N.W. 417 (N.D. 1910).

In her struggle to find some precedent somewhere to support her action to transfer control of FLS to persons selected by a religious ministry of her preference, the Attorney General has conveniently forgotten that her prayer for relief calling for the removal of the FLS directors rested solely upon N.D.C.C. ch. 32-13. I J.A. 140 (Para. 4). As pointed out in the FLS opening brief, N.D.C.C. ch. 32-13 grants no such authority. FLS Br. 19-20. And the Attorney General has made absolutely no effort to rebut that fact.

The Attorney General has, however, attempted to refute FLS' contention that N.D.C.C. Section 10-26-08 requires notification to FLS and certification by the Secretary of State **before** the Attorney General may bring an action for dissolution of a nonprofit corporation. She has claimed that "the [statutory] language refers to the ministerial duties of the secretary of state having to do with documents and records that the statutes require be filed with his office." A.G. Br. 56-57. That reading directly conflicts with N.D.C.C. Section 10-28-07, which confers upon the secretary of state not only "the power and authority ... to perform **the duties therein imposed** on the secretary of state" (emphasis added), such as the filing of the articles of incorporation required by N.D.C.C. Section 10-24-13, but also "to administer chapters 10-24 through 10-28 efficiently," including the prohibition against corporate loans to its officers or directors as prescribed by N.D.C.C. Section 10-24-27. N.D.C.C. 10-28-05 confirms this, by conferring upon the Secretary of

State extensive investigative powers "to ascertain whether [a nonprofit] corporation has complied with **all the provisions** of chapters 10-24 through 10-28" (emphasis added).

N.D.C.C. chs. 10-24 through 10-28, enacted in 1959, were patterned after the Model Nonprofit Corporation Act originally drafted by the American Bar Association in 1952. That Act, like the ABA Model Business Corporation Act, conferred upon the secretary of state, not the attorney general, primary enforcement authority, limiting the attorney general's powers to instituting a court action only after proper certification by the secretary of state. *See Model Nonprofit Corporation Act,* Sec. 52, and Preface (ALI/ABA: rev. 1964). Not until 1988 did the ABA change its Model Nonprofit Corporation Act to reduce the powers of the secretary of state to ministerial ones. *Revised Model Nonprofit Corporation Act,* Official Comments to Sections 1.30 and 14.30 (rev. 1988). Although that change in the model act is now reflected in N.D.C.C. chs. 10-33, the Attorney General has conceded that this 1997 law was not in place at the time she commenced this action. *See* A.G. Br. 54.

This leaves N.D.C.C. ch. 13-07 as the only available statute authorizing the Attorney General to take action in this case. N.D.C.C. Section 13-07-07 authorizes only "a civil action ... for an injunction prohibiting any practice in violation of this chapter," not an action for dissolution or removal of directors for breach of fiduciary duties, much less for dismantling and reconstituting a nonprofit corporate board of directors. Yet, that is what the Attorney General did in this case. With no statutory authority for such action, the judgment entered by the district court dismantling and reconstituting the FLS Board is completely void. Larson v. Dunn, 474 N.W. 2d 34, 39 (N.D. 1991).

## III. THE TRIAL COURT HAD NO LAWFUL AUTHORITY TO TRANSFER CONTROL OF FLS.

The Attorney General has not cited a single case in which a court of equity has completely dismantled and reconstituted a nonprofit corporation's board of directors. Nor has she pointed to any statute expressly conferring such power. Yet, the Attorney General insists that, because N.D.C.C. Section 10-26-07 authorizes a court to dissolve a nonprofit corporation, the court had the power to choose the "less drastic" remedy of removal of **all** the directors, including those who had breached no fiduciary duty (FLS Br. 7-8), and to delegate the appointment of an entirely new board to the managers and employees of FLS and to the Board of the F-M Evangelical Ministerial Association (Ministerium). *See* A. G. Br. 54-56. To support her position, the Attorney General has relied upon Balvik v. Sylvester, 411 N.W.2d 383 (N.D. 1987).

Balvik does not support the Attorney General's position. In Balvik this Court reversed the trial court's order dissolving a business corporation on the grounds that requiring the majority stockholders, found guilty of wrongdoing, to buy out the wronged minority stockholder was "less drastic." In this case, however, the trial court has imposed an even more drastic remedy than either the dissolution rejected in Balvik or the buy-out approved in that case. It has decreed a government takeover of a religious nonprofit organization, completely ousting the FLS Board and turning FLS over to its branch managers and employees and an organization that had absolutely no interest in FLS. The remedy approved in Balvik, to be even reasonably comparable to the one imposed here, would not only have required the wrongdoing majority stockholder to buy out the

minority stockholder, but, thereafter, would have decreed a forced sale of the company "at a price determined by the court."

The remedy imposed in this case is "more drastic" than the one in Balvik for an additional reason. In Balvik, this Court rejected dissolution because "a forced dissolution allows minority shareholders to exercise retaliatory 'oppression' against the majority." Id., 411 N.W. 2d at 388. Similarly, the trial court here set the stage for "retaliatory oppression" by granting the FLS staff, and not members of the FLS Board, veto power over a proposal to reconfigure the board to keep the current directors, adding new ones acceptable to the managers and employees. I J.A. 451-63.

Rather than supporting the remedy employed by the court below, then, Balvik casts serious doubt upon any remedy that deprives even a wrongdoer of control of a company. Such a remedy "should be invoked," as Balvik has instructed, only "with extreme caution and only when justice requires it." Id., 411 N.W.2d at 388. In this case, justice requires just the opposite of what the trial court did. Not only did the trial court give no consideration whatsoever to the various alternative remedies set forth in detail in the Balvik opinion (*see* Id., 411 N.W.2d at 388-89), it also completely ignored the dangers of a governmentally-forced transfer of control over a private nonprofit corporation, especially when that corporation is intimately connected with a controversial prolife religious ministry. Allowing a government-ordered takeover of a nonprofit organization tempts government officials to seize an ongoing organization and convey it to persons considered acceptable to the government, a temptation not present if the organization is to be dissolved. Additionally, the exercise of such power risks the

appearance of impropriety when dealing with the takeover of organizations whose views are antithetical to those of the government official. If the trial court's order is permitted to stand, it opens the door to future government takeovers of such nonprofit endeavors upon the pretext of concern for financial irregularities, when the real reason is to transfer control to others whose views the government approves. It is for these reasons that the United States Supreme Court has laid down a set of strict rules governing the remedial power of courts in the redress of financial and property disputes in religious organizations, a point completely missed by the Attorney General in her attempt to refute FLS's reliance upon a line of cases dating back to 1872. *Compare* FLS Br. 27-32 *with* A.G. Br. 36-44.

## IV. THE TRIAL COURT USED UNCONSTITUTIONAL MEANS TO IMPLEMENT ITS REMEDY.

The Attorney General fails to address adequately the question whether the court's **remedy** meets applicable constitutional standards. Moreover, she has filled her brief with citations to cases involving government assistance to religious organizations, which are totally inapposite to **this** case which involves governmental **delegation of powers** to a religious organization as part of a judicial remedy invading the internal governing structure of another religious organization.

When the Attorney General finally addresses that issue, she chides FLS for relying "essentially on a single case, Larkin v. Grendel's Den, Inc., 459 U.S. 116 (1982)." A.G. Br. 34-36. There is reason for this reliance. That case is squarely on point, and requires reversal of the judgment below.

The Attorney General attempts to distinguish Grendel's Den first on the facts, making the startling claim that the rule in Grendel's Den applies only to a "specific religion, faith or congregation," not to the Ministerium which represents a cross-section of evangelical Christians. But the High Court stated in Grendel's Den that its ruling applied to delegations of such power to "religious institutions" generally. Grendel's Den, *supra,* 459 U.S. at 127.

Next, in one paragraph of her brief, the Attorney General makes the equally startling claim that the power delegated by the court to the Ministerium and to FLS branch managers and employees is not governmental at all, but "private"; yet, in the very next paragraph, she asserts that "the trial court retained the ultimate appointment authority and was free to reject any nominee selected by the Ministerium, branch managers and employees." A.G. Br. 35. If the court retained such power, then the selection of members of the FLS Board was not a "private" act. Indeed, there is nothing "private" about the power to select members of a board of directors of a nonprofit corporation when the bylaws of that corporation confer absolutely no power on the organization or persons doing the selecting! Moreover, Grendel's Den condemns not only the delegation of governmental power to a religious organization, but the "sharing" of such power with such an organization. Id., 459 U.S. at 127.

The Attorney General's third argument would dismiss Grendel's Den as having "limited precedential value." But that is because Grendel's Den "presented an example of united civic and religious authority, an establishment **rarely** found in such

straightforward form in modern America." Board of Education of Kiryas Joel v. Grumet, 512 U.S. 687, 697 (1994) (emphasis added).

Finally, the Attorney General has argued that, unlike in Grendel's Den, "the trial court's purpose could not be accomplished by other means." That misses the point completely. There are certain means that are unconstitutional no matter how compelling the government's case might appear. As the Court has recently explained the rule of Grendel's Den:

> The Act brought about a "'fusion of governmental and religious functions'" by delegating "important discretionary governmental powers" to religious bodies, thus impermissibly entangling government and religion. [Kiryas Joel, *supra,* 512 U.S. at 697.]

So long as the FLS Board partakes of a religious character and purpose, as both the Attorney General and the trial court recognized by enlisting the appointment services of the Ministerium, the trial court simply cannot replace the FLS Board without violating the Establishment and Free Exercise Clauses of the First Amendment.

## CONCLUSION

For all the reasons stated on appeal by FLS, the Judgment of the trial court removing and replacing the FLS directors should be reversed.

Respectfully submitted,


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