

## The Texas Supreme Court Overhauls the Minority Shareholder Oppression Doctrine

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Recent years have seen a sharp uptick in shareholder oppression claims. See 1 F. Hodge O'Neal & Robert B. Thompson, *Oppression of Minority Shareholders and LLC Members* iii (Rev. 2d ed. 2007). In the summer of 2014, the Texas Supreme Court issued an opinion changing the landscape of shareholder oppression law in the State of Texas—*Ritchie v. Rupe*. *Ritchie* heralds a new and unique framework for resolving complaints by a minority shareholder claiming mistreatment by the majority shareholders.

### ***Ritchie v. Rupe*, 443 S.W.3d 856 (Tex. 2014)**

In its landmark decision, a majority of the Texas Supreme Court reversed the lower court's buyout order in a minority shareholder oppression case and held: (1) the remedy for "oppressive" conduct is a rehabilitative receivership under the Texas oppression statute; a court-ordered buyout is not an available remedy; (2) in determining whether conduct was "oppressive," courts must take into account the business judgment rule; and (3) no common-law cause of action for shareholder oppression exists in Texas. *Ritchie v. Rupe*, 443 S.W.3d 856 (Tex. 2014).

### **The Facts**

The plaintiff in *Ritchie*, Ann Rupe, is trustee of a trust holding stock in a family business, stock previously owned by her deceased husband. *Id.* at 861. Rupe decided to sell the trust's minority stock interest to third parties. *Id.* at 862. Acting on the advice of counsel, the majority owners declined to meet with prospective buyers. *Id.* Rupe sued, claiming she had been oppressed. *Id.* Her main complaints were: (1) the majority owners would not meet with potential buyers of the trust's stock; (2) she allegedly was denied access to company records; and (3) although the majority owners offered to buy her stock back, the offered price was too low. The jury ultimately found that the majority owners had engaged in oppressive conduct. *Id.* The trial court agreed and ordered the corporation to redeem Rupe's shares for \$7.3 million. *Id.* at 862-63.

Texas's Fifth Court of Appeals upheld the oppression finding but remanded for a new trial on the buyout price so the jury could consider discounts that often apply to the value of a minority interest in a closely-held company for lack of marketability and control. *Id.* at 863. The Texas Supreme Court reversed. *Id.* at 892. In doing so, the Court gave Texas courts and litigants much-needed guidance on Texas shareholder oppression law.

### **The Court Defines "Oppressive"**

First, the Court considered the appropriate meaning and scope of the term "oppressive," as used in the rehabilitative receivership statute (Texas Business Organizations Code § 11.404)—the statute Rupe relied on for her oppression claim. *Id.* at 863-77. The Court's analysis was guided by fundamental statutory-construction principles. *Id.* at 863-66. Because the Legislature did not define "oppressive," the Court faced the task of ascertaining what the Legislature intended that term to encompass. *Id.* at 864.

Initially, the Court turned to case law construing the term, noting that two standards have dominated in shareholder-oppression cases: (1) the reasonable expectations test and (2) the fair dealing test. *Id.* at 864-65. The Court then considered the appropriate definition of “oppressive” in light of the receivership statute’s overall language. *Id.* at 866. The Court recognized that its task was to divine and effectuate the Legislature’s intent, rather than to make its own policy choices. *Id.* With “oppressive” left undefined by the Legislature, the Court sought out the term’s common meaning. *Id.* “Oppressive,” of course, has multiple meanings depending on the circumstances. Thus, the Court’s job was to find the definition most consistent with the statutory scheme. *Id.*

The Court turned to a “text-based approach,” which requires a court “to study the language of the specific provision at issue, within the context of the statute as a whole, endeavoring to give effect to every word, clause, and sentence.” *Id.* Under this approach, the Court examined not only the statutory term “oppressive,” but also the language and context of the entire receivership statute, including the other specific grounds for which it authorizes a receivership and the general requirements that apply to all of the specific grounds. *Id.*

Through this analysis, the Court concluded that conduct should be deemed oppressive only when: (1) the majority “abuse their authority over the corporation with the intent to harm the interests of one or more of the shareholders”; (2) “in a manner that does not comport with the honest exercise of business judgment”; and (3) “by doing so create a serious risk of harm to the corporation.” *Id.* at 871.

Although other states have adopted the “fair dealing” or “reasonable expectations” test, the Texas Supreme Court determined that neither adequately captured the Texas Legislature’s intended meaning of “oppressive” conduct. *Id.* at 870-71. While the Court agreed that its definition incorporated aspects of the fair-dealing and reasonable-expectations tests, the Court refused to embrace a definition that would find oppression under either test alone. *Id.* It thus disapproved of the appellate decisions that have done so. *Id.*

### **The Court Nixes a Buyout Remedy**

The Texas Supreme Court also rejected a court-ordered buyout for oppression, a remedy other states recognize. The Court held that the Texas receivership statute “creates a single cause of action with a single remedy.” *Id.* at 872. While the statute provides that a court may appoint a receiver only after finding that all other remedies available at law or in equity are inadequate, that proviso limits the availability of the receivership, rather than expanding the available remedies. *Id.* at 874-75. The Court appreciated that lesser remedies may be available under common law or other statutory provisions, and those remedies may be adequate. *Id.* If so, then no receiver need be appointed. *Id.* But for a claim asserted under the receivership statute, the sole remedy is the appointment of a rehabilitative receiver. *Id.* at 877.

The dissent chastised the majority, pointing out that numerous other states have approved a buyout remedy. *Id.* at 898, n. 25. But many of those states have a statute expressly allowing for a buyout remedy, while Texas does not. The Texas Legislature has not provided for a buyout remedy, and the Texas Supreme Court was unwilling to create new law. *Id.* at 872, n. 25. Moreover, the Court noted, a practical problem with court-ordered buyouts is that they can threaten the financial security of closely-held entities, even pushing them into bankruptcy or dissolution. *Id.* at 874, n. 26. Thus, the Court rejected the availability of a court-ordered buyout under the statute. *Id.* at 876.

## **The Court Rejects a Common-Law Shareholder Oppression Cause of Action**

The Court also determined that it would not recognize a common-law claim for minority shareholder oppression. *Id.* at 877-91. The Court undertook a complex analysis to find that Texas jurisprudence did not need a common-law cause of action for shareholder oppression when other legal protections exist to remedy complaints of the minority shareholder. *Id.*

## **The Court Advises Minority Shareholders to Protect Themselves**

The Court also offered guidance to minority shareholders by encouraging them to protect themselves before investing by negotiating shareholder agreements setting out remedies in the event of a dispute between the minority and majority shareholders. *Id.* at 881. The Court emphasized that the judicial system should afford citizens broad freedom in making choices about how to manage their business endeavors. *Id.* at n. 43. The Court also reasoned that it was “ill-suited to the task of second-guessing business decisions made by business people who typically have a more long-term perspective, access to more extensive information, greater experience in the industry, if not in business practices generally, and more interest in the outcome.” *Id.*

## **Texas Has Charted its Own Path for the Judicial Resolution of Minority Shareholder Oppression Claims**

The Texas Supreme Court has forged a different path for shareholder oppression law. Limiting its role to interpreting, rather than creating, the law, and recognizing individuals’ right to freely choose how to manage their own business affairs, the Court aligned Texas law with the Delaware Supreme Court’s view that it would “do violence to normal corporate practice and our corporation law to fashion an ad hoc ruling which would result in a court-imposed stockholder buyout for which the parties had not contracted.” *Nixon v. Blackwell*, 626 A.2d 1366, 1380 (Del. 1993).

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