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Texas Supreme Court Limits Rights of Minority Shareholders of Closely Held Corporations

In a recent ruling by the Texas Supreme Court in *Ritchie v. Rupe*, a six-justice majority concluded there is no common law claim for “minority shareholder oppression” in Texas. The decision signifies a sharp departure from the last 50 years, as several Texas appellate courts have permitted minority shareholders of closely held corporations to assert common law oppression claims. The court’s decision aligns Texas with Delaware, which does not recognize shareholder oppression claims.

In *Ritchie*, the plaintiff, a widow who became an 18 percent shareholder in Rupe Investment Corp. (RIC) through her late husband’s estate, claimed the majority owners aggressively offered to buy her interest in RIC for much less than it was worth, did not give her access to RIC’s books, and refused to meet with potential third party purchasers of her shares. The court concluded RIC’s conduct was not “oppressive” under Texas law, overturned the intermediate court of appeals’ ruling that required RIC to pay the plaintiff \$7.3 million for her shares, and limited the forms of redress minority shareholders can seek.

What This Means to You

After *Ritchie*, minority shareholders of closely held Texas corporations have limited, if any, legal recourse to assert minority shareholder oppression claims. In addition to giving close corporations greater control over the sale of shares by minority shareholders, *Ritchie* signals the court’s belief that directors and officers of close corporations should be afforded great deference in management and governance decisions. For minority shareholders, *Ritchie* emphasizes the importance of well-prepared shareholder agreements to ensure the interests of minority shareholders are adequately protected.

The *Ritchie* Decision

Overturning the ruling of the Dallas Court of Appeals and creating a more stringent definition of “oppression” in Texas, Justice Boyd, writing for the majority, ruled that the common law claim of oppression is not recognized in Texas law for minority shareholders of closely held corporations. The court concluded that forcing RIC to purchase the plaintiff’s shares at market rate is not a protection afforded by law. Finding that the majority owners in RIC were under no obligation or duty to meet with outside prospective purchasers, the court attributed the plaintiff’s difficulty in selling her shares to the intrinsic difficulty in selling shares of a closely held corporation.

The oppression standard articulated in *Ritchie* requires that a corporation’s directors or officers must “abuse their authority over the corporation with the intent to harm the interests of one or more of the shareholders, in a manner that does not comport with the honest exercise of their business judgment, and by doing so create a serious risk of harm to the corporation.” In applying this narrow standard, the court incorporated the business judgment rule, which is traditionally viewed as a very easy standard for corporate directors and officers to meet.

In refusing to acknowledge a common law claim of oppression, the court found that Texas law already affords minority shareholders sufficient protection. One of the protections acknowledged by the court is that a trial court may appoint a temporary rehabilitative receivership pursuant to Section 11.404 of the Texas Business Organizations Code. However, before granting relief under Section 11.404, a court must first find that all other available remedies are inadequate.

The court also found minority shareholders have the option of protecting themselves via contract by entering into shareholder agreements that include buy-sell clauses, rights of first refusal, or other redemptive provisions that would avoid many of the problems that could arise when it comes time to sell. In light of these existing protections, the court concluded the vagueness and circumstantial nature of the legal definition of “oppression” would make a ruling allowing for claims of shareholder oppression a difficult and inconsistent precedent for lower courts to apply.

Justice Guzman, joined by Justices Brown and Willett, offered a vigorous dissent, asserting “[t]he ultimate effect of [the] holding is to negate the very foundations of protection the legislatures and U.S. courts have long afforded to minority shareholders in closely held corporations.” According to the dissent, the court should have recognized the common law claim of oppression by upholding the appellate court’s finding of oppression on the facts presented.

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