

# Shareholder Agreements: Litigation Perspectives

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## ***I. INTRODUCTION***

It has been more than five years since the Texas Supreme Court declined to recognize a common-law cause of action for shareholder oppression.<sup>1</sup> In its holding, the Court narrowed the remedies available to shareholders harmed or oppressed by the corporation or majority

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

shareholders.<sup>2</sup> The Court relied in part on the statutory, contractual, and common-law causes of action and remedies already available to shareholders through litigation.<sup>3</sup> The Court also emphasized the importance of the use of shareholder agreements to protect the interests of the corporation and its shareholders and to avoid future disputes.<sup>4</sup>

Although it restricted shareholder common-law rights, *Ritchie* did not put an end to shareholder litigation.<sup>5</sup> As highlighted further below, recent cases reflect that shareholders continue to seek available judicial remedies, including through derivative actions and the various statutory and common-law causes of action and remedies outlined by the Court in *Ritchie*.<sup>6</sup> These cases provide insight into the types of claims practitioners should be cognizant of when advising their clients and drafting organizational documents. Through its repeated emphasis on the use of shareholder agreements for many situations, the Court in *Ritchie* left it to shareholders and corporations to protect their respective rights and interests and govern themselves by contract.<sup>7</sup> Thus, five years after *Ritchie*, the importance of well-drafted shareholder agreements cannot be understated. This article also discusses some of the potential provisions practitioners should strongly consider including in their organizational documents.

## **II. COMMON SHAREHOLDER DISPUTES AND AVAILABLE CAUSES OF ACTION**

In its analysis of shareholder oppression, the Court in *Ritchie* outlined some of the most common types of conduct that lead to shareholder disputes, including:

- Denial of access to corporate books and records;
- Withholding or refusing to declare dividends;
- Termination of employment;
- Misapplication of corporate funds and diversion of corporate opportunities;

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2. *See id.* at 889–91.

3. *See id.* at 879–89.

4. *Id.* at 871.

5. *See id.* at 879–82 (discussing the statutory and common-law causes of actions a shareholder may bring).

6. *See* cases cited *infra* notes 14–17.

7. *See Ritchie*, 443 S.W.3d at 871.

- Manipulation of stock values in relation to sales or purchases of minority interests.<sup>8</sup>

A review of Texas shareholder caselaw reflects those disputes referenced in *Ritchie*, and many other common scenarios in which shareholder disputes may arise, including:

- “Malicious suppression of dividends;”<sup>9</sup>
- Excessive pay;<sup>10</sup>
- Misuse of corporate funds and assets / loans to majority shareholders;<sup>11</sup>
- Profit distributions;<sup>12</sup>
- Demands for examination of books and records;<sup>13</sup>
- Forced or undervalued stock redemptions;<sup>14</sup>
- Disputes over right of first refusal;<sup>15</sup>

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8. *Id.* at 882–89.

9. *See Patton v. Nicholas*, 279 S.W.2d 848, 853–54 (Tex. 1955).

10. *See Cardiac Perfusion Servs., Inc. v. Hughes*, 436 S.W.3d 790, 791 (Tex. 2014) (allegations of excessive compensation and improper use of company funds to pay personal expenses); *Boehringer v. Konkel*, 404 S.W.3d 18, 22 (Tex. App.—Houston [1st Dist.] 2013, no pet.) (majority shareholder wrongfully awarded himself an excessive salary); *Gibney v. Culver*, No. 13-06-112-CV, 2008 WL 1822767, at \*1 (Tex. App.—Corpus Christi Apr. 24, 2008, pet. denied) (minority shareholder derivative action alleging excessive compensation paid to an officer).

11. *See In re LoneStar Logo & Signs, LLC*, 552 S.W.3d 342, 344 (Tex. App.—Austin 2018, no pet.) (minority LLC member derivative action alleging wrongful use of company’s assets); *Redmon v. Griffith*, 202 S.W.3d 225, 231 (Tex. App.—Tyler 2006, pet. denied) (minority shareholders sued alleging defendants diverted corporate opportunities, funds, and revenues and illegally disbursed corporate assets for personal use and benefit).

12. *Kohannim v. Katoli*, 440 S.W.3d 798, 813 (Tex. App.—El Paso 2013, pet. denied) (LLC owner filed suit alleging defendant shareholder failed to make profit distributions).

13. *Texas Ear Nose & Throat Consultants, PLLC v. Jones*, 470 S.W.3d 67, 73 (Tex. App.—Houston [14th Dist.] 2015, no pet.) (departing member brought suit against other members for breach of contract “and denial of access to . . . books and records”); *White Point Minerals, Inc., v. Swantner*, 464 S.W.3d 884, 886 (Tex. App.—Corpus Christi 2015, no pet.) (former shareholder brought suit alleging company wrongfully deprived him of access to “books, records of account, minutes, and share transfers”).

14. *See Herring Bancorp, Inc. v. Mikkelsen*, 529 S.W.3d 216, 218 (Tex. App.—Amarillo 2017, pet. denied) (minority shareholder alleged that involuntary stock redemption violated the articles of incorporation).

15. *Higginson v. Martin*, No. 07-15-00343-CV, 2017 WL 603626, at \*3 (Tex. App.—Amarillo Feb. 14, 2017, pet. denied) (minority shareholder sought declaration that

- Termination of employment;<sup>16</sup>
- Call rights disputes;<sup>17</sup>
- Share transfer disputes;<sup>18</sup>
- Merger disputes.<sup>19</sup>

The author regularly represents clients involved in shareholder lawsuits that highlight the importance of well-drafted shareholder (or partnership) agreements to reduce the potential for, or impact of, such disputes. In one such case involving a successful closely-held company, a retiring founder placed his son in charge of the business. In combination with his appointment of the son as president of the company, he sold shares of the company to the son. A dispute later ensued regarding the son's management of the company, and the board decided to terminate the son's employment. Seeking a complete separation, and based on the language of the shareholder agreement, the company then sought to repurchase the son's shares. Litigation ensued relating to the termination and the company's demand to repurchase the shares. The son threatened to market the shares to a third party. The son demanded access to the books and records and an accounting and accused board members and other executives of excessive distributions. Disputes over the value of the shares resulted in multiple appraisals and extensive discovery in the litigation. Expert witnesses were retained to opine

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shareholder agreement, which contained a right of first refusal concerning the transfer of shares, was unenforceable); *McAuley v. Flentge*, No. 06-15-00051-CV, 2016 WL 3182667, at \*1 (Tex. App.—Texarkana June 8, 2016, pet. denied) (shareholder dispute concerning whether transfer of stock was restricted by a right of first refusal).

16. *Guajardo v. Hitt*, 562 S.W.3d 768, 774 (Tex. App.—Houston [14th Dist.] 2018, pet. denied) (shareholder alleged claims arising from termination of his employment and removal of his salary despite certain provisions in the shareholder agreement).
17. *Baty v. Bowen, Miclette & Britt, Inc.*, 423 S.W.3d 427, 430–31 (Tex. App.—Houston [14th Dist.] 2013, pet. denied) (former employee and shareholder sued other shareholders alleging misappropriation of shares subject to shareholder agreement with call rights triggered by employment termination).
18. *Fishman v. C.O.D. Capital Corp.*, No. 05-16-00581-CV, 2017 WL 3033314, at \*2 (Tex. App.—Dallas July 18, 2017, no pet.) (company sued certain shareholders claiming transfer of shares violated shareholder agreement); *GM Oil Props., Inc. v. Wade*, No. 01-08-00757-CV, 2012 WL 246041, at \*2 (Tex. App.—Houston [1st Dist.] Jan. 26, 2012, no pet.) (shareholder sued corporate officer alleging breach of shareholder agreement for failing to transfer a certain percentage of his stock to the plaintiff).
19. *Hoggett v. Brown*, 971 S.W.2d 472, 475 (Tex. App.—Houston [14th Dist.] 1997, pet. denied) (“shareholder . . . [sued other shareholders] claiming that corporation’s merger with another company was fraudulent and violated shareholders agreement”).

regarding share valuation. The parties eventually settled their claims, but only after lengthy and expensive litigation. The shareholder agreement was reasonably robust but lacked, among others, certain provisions for valuation of shares in the event of a buy-back upon a triggering event (employment termination).

The allegations from this lawsuit undoubtedly sound familiar to Texas attorneys who regularly represent corporations and shareholders. Although this particular lawsuit likely could not have been avoided entirely, the litigation could have been substantially streamlined and more easily resolved by the inclusion of provisions governing the mechanism of share valuation and buy-back. To address the potential conflicts that may arise among shareholders, practitioners should possess a working knowledge of the types of claims available to and commonly asserted by dissatisfied shareholders in litigation.

### ***A. Direct Shareholder Claims***

#### ***1. Accounting and Statutory Access to Corporate Books and Records***

Demands for access to corporate information frequently underlie disputes between shareholders. The Court in *Ritchie* recognized that “denial of access to corporate[] books and records” may constitute a form of shareholder oppression.<sup>20</sup>

The Texas Business Organizations Code (“TBOC”) provides a comprehensive framework for shareholders to obtain information from the corporation.<sup>21</sup> The Court in *Ritchie* focused on the TBOC statutory framework that protects shareholders’ rights to access a corporation’s books and records and cited statutory accounting as an available remedy for minority shareholders claiming oppressive conduct.<sup>22</sup>

Cases decided since *Ritchie* reflect that disputes over access to information continue to generate shareholder litigation and confirm that shareholders have been able to obtain relief without a shareholder oppression claim. For example, in *Texas Ear Nose & Throat Consultants, PLLC v. Jones*,<sup>23</sup> the departing member of a medical PLLC prevailed at trial on his claims against other members for breach of contract and denial of access to the company’s books and records.<sup>24</sup> Interestingly, the

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20. *Ritchie v. Rupe*, 443 S.W.3d 856, 882 (Tex. 2014).

21. TEX. BUS. ORGS. CODE ANN. §§ 3.153, 21.218 (examination of records), 21.354 (inspection of voting list).

22. *Ritchie*, 443 S.W.3d at 882–83.

23. 470 S.W.3d 67 (Tex. App.—Houston [14th Dist.] 2015, no pet.).

24. *Id.* at 85.

court not only focused on the shareholder's presuit records demands but also noted that the shareholder served requests for production and filed motions to compel during the lawsuit that were relevant to the application of the statute and the jury's determination of liability.<sup>25</sup> Moreover, the court of appeals sustained the trial court's award of additional attorneys' fees for denial of access to books and records but determined that the additional fees must be properly segregated and paid by the LLC and not the individual defendant members.<sup>26</sup>

In *White Point Minerals, Inc., v. Swantner*,<sup>27</sup> a former shareholder brought suit "alleging the company had wrongfully deprived him of access to books, records of account, minutes, and share transfers."<sup>28</sup> The court discussed the standing requirements for a former shareholder bringing such a claim.<sup>29</sup> The court granted the former shareholder an opportunity to cure jurisdictional defects in his petition by pleading facts to establish his standing under TBOC section 21.218.<sup>30</sup>

The TBOC permits a shareholder to examine books and records "[o]n written demand stating a proper purpose."<sup>31</sup> A corporation that refuses to allow an examination "under Section 21.218 is liable to the shareholder for . . . costs . . . [and] attorney's fees," in addition to any other damages or remedies afforded the shareholder.<sup>32</sup> Shareholder litigation concerning requests for corporate records and information often focuses on whether the request was made in good faith and for a proper purpose, as required by the statute.<sup>33</sup> The burden is on the resisting party to plead and prove that the shareholder lacks a proper purpose in requesting an examination of records.<sup>34</sup> Once the resisting party has

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25. *Id.* at 86.

26. *Id.* at 89–91.

27. 464 S.W.3d 884 (Tex. App.—Corpus Christi 2015, no pet.).

28. *Id.* at 885, 886.

29. *Id.* at 889 ("[W]e hold that the statutory rights addressed in section 21.218 apply solely to a record or beneficial shareholder of a corporation at the time the demand is made or action is filed.").

30. *Id.* at 890.

31. TEX. BUS. ORGS. CODE ANN. § 21.218(b).

32. *Id.* § 21.222(a).

33. *See id.* §§ 21.218(b), 21.222(b)(4); *see also* Biolustre' Inc. v. Hair Ventures LLC, No. 04-10-00360-CV, 2011 WL 540574, at \*3 (Tex. App.—San Antonio Feb. 16, 2011, no pet.) (ordering access to books and records and finding proper purpose).

34. *See In re Dyer Custom Installation, Inc.*, 133 S.W.3d 878, 881 (Tex. App.—Dallas 2004, no pet.).

raised a fact issue regarding good faith or proper purpose, they are entitled to a jury trial on the issue.<sup>35</sup>

Given the frequency with which disputes arise over access, shareholder agreements can be drafted to include language regarding the scope of information, format, and mechanisms of providing information to shareholders. The shareholder agreement should not attempt to reduce a shareholder's statutory rights to access corporate information. However, a shareholder agreement can broaden, clarify, or specify those rights to reduce future conflicts over the company's books and records. For example, the shareholder agreement can specifically outline the types of reports that will be prepared and provided on a periodic basis, such as financial statements and other financial information. Inclusion of details on how the information will be maintained and made available in the event of a reasonable request can also avoid disputes and provide a defense to shareholder claims for more information. To avoid disputes over whether the demand was made for a proper purpose, shareholder agreements can also list potential bases and mechanisms for requesting books and records in the future.

## ***2. Breach of Contract***

The Court in *Ritchie* recognized that shareholders facing oppressive conduct may need to assert direct claims for breach of contract in order to obtain judicial relief.<sup>36</sup> The TBOC specifically authorizes a corporation that is not publicly traded to be governed by a shareholder agreement entered into by all "shareholders of a corporation."<sup>37</sup> The TBOC enumerates various provisions shareholders may include in a shareholder agreement concerning matters such as powers of directors, payment of dividends and distributions, authorizing arbitration, exercising voting powers, and that "otherwise govern[] . . . the management of the business and affairs of the corporation."<sup>38</sup> Additional sections of the TBOC expressly provide for contractual relationships among shareholders, including "written voting agreements"<sup>39</sup> and share transfer restrictions.<sup>40</sup> Ancillary to shareholder agreements, employment contracts are also frequently entered into by shareholders employed by the corporation.

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35. *Id.* (corporation was entitled to a jury trial on the issue of whether the shareholder had a proper purpose in requesting books and records).

36. *Ritchie*, 443 S.W.3d at 881, 888 n.55.

37. TEX. BUS. ORGS. CODE ANN. § 21.101(a).

38. *Id.*

39. *Id.* § 6.252.

40. *Id.* § 21.210.

Corporate formation, share transfer disputes, and redemptions are particularly common subjects of shareholder breach of contract claims.<sup>41</sup>

As indicated by these recent cases, share transfers made in breach of a shareholder agreement can cause significant damage. Breaches of other common shareholder provisions such as procedural or reporting obligations may be less significant and cause no damage. Whether a breach merits pursuit of litigation turns on the facts of each dispute. As for drafting considerations, the shareholder agreement is a contract and should be the product of principled and informed negotiations. The

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41. *See, e.g.*, *Texas First Inv. Mgmt. Co., v. Coorsh*, No. 01-17-00591-CV, 2018 WL 3352922, at \*1–2 (Tex. App.—Houston [1st Dist.] July 10, 2018, no pet.) (affirming grant of limited partner’s motion for partial summary judgment on his breach of contract claim against limited partnership for refusal to repurchase partner’s partnership units pursuant to partnership agreement); *APMD Holdings, Inc. v. Praesidium Med. Prof’l Liab. Ins. Co.*, 555 S.W.3d 697, 700 (Tex. App.—Houston [1st Dist.] 2018, no pet.) (affirming judgment for shareholder of proposed medical malpractice liability insurer on shareholder’s breach of contract claim against the insurer’s other shareholder for failure to finance the proposed insurer’s capital surplus as agreed to in memorandum of agreement); *Lowry v. Tarbox*, 537 S.W.3d 599, 605 (Tex. App.—San Antonio 2017, pet. denied) (affirming judgment on jury verdict for minority shareholder physician’s claim against medical practice for breach of compensation contract and failure to comply with stock redemption agreement); *Herring Bancorp, Inc. v. Mikkelsen*, 529 S.W.3d 216, 223–26 (Tex. App.—Amarillo 2017, pet. denied) (finding that corporation’s involuntary redemption of minority shareholder’s preferred stock as part of conversion to Subchapter S corporation did not breach articles of incorporation); *Gonzalez v. UniversalPegasus Int’l, Inc.*, 531 S.W.3d 276, 278 (Tex. App.—Houston [14th Dist.] 2017, no pet.) (affirming summary judgment for corporation and its board of directors on minority shareholders’ claim of breach of contract because shareholders failed to establish that cancellation of their shares was invalid and failed to present sufficient evidence that they were damaged by the alleged breach); *Fishman v. C.O.D. Capital Corp.*, No. 05-16-00581-CV, 2017 WL 3033314, at \*10–11 (Tex. App.—Dallas July 18, 2017, no pet.) (finding shareholder breached shareholder agreement transfer restrictions by failing to give required notice to other shareholders before transfer to a third-party trust in exchange for consideration); *McAuley v. Flentge*, No. 06-15-00051-CV, 2016 WL 3182667, at \*7–9 (Tex. App.—Texarkana June 8, 2016, pet. denied) (analyzing whether testamentary transfers were subject to a contractual right of first refusal in a shareholder agreement); *Texas Ear Nose & Throat Consultants, PLLC v. Jones*, 470 S.W.3d 67, 95–97 (Tex. App.—Houston [14th Dist.] 2015, no pet.) (upholding breach of employment agreement finding); *Aloysius v. Kislingbury*, No. 01-13-00147-CV, 2014 WL 4088145, at \*3–4 (Tex. App.—Houston [1st Dist.] Aug. 19, 2014, no pet.) (holding that majority shareholder had standing to bring breach of contract claim in his individual capacity against minority shareholder for breach of agreement to form the corporation); *GM Oil Props., Inc. v. Wade*, No. 01-08-00757-CV, 2012 WL 246041, at \*2 (Tex. App.—Houston [1st Dist.] Jan. 26, 2012, no pet.) (former shareholder sued a corporate officer in the officer’s individual capacity for breach of contract, alleging the defendant breached a shareholder agreement by failing to transfer a certain percentage of stock to the plaintiff).

corporation should try to limit its contractual obligations to shareholders while meeting the requirements of the governing statutes. On the other hand, minority shareholders should seek as many protections as they can reasonably negotiate, recognizing that they often may have less leverage.

### ***3. Common-Law Fraud, Statutory Fraud, Constructive Fraud***

Direct fraud claims typically arise from disputes over representations made relating to transactions such as share purchases or redemptions. Nondisclosure of facts may also be the basis of a claim if a duty to disclose is recognized by the law. *Ritchie* also noted the potential for common-law and statutory fraud claims to arise from manipulation of share values.<sup>42</sup>

Fraud under Texas law requires proof of the following, among other elements: (1) the defendant made a material false representation; (2) the representation was made knowingly or recklessly without knowledge of its truth; (3) the defendant made the representation with the intent that plaintiff act on it; (4) the plaintiff justifiably relied on the representation causing injury.<sup>43</sup> To be actionable under Texas law, a misrepresentation must be a statement “concerning a material fact.”<sup>44</sup> Shareholder complaints based on statements regarding future events or promises of future company performance may not support a fraud claim.<sup>45</sup>

Shareholders may assert that they were fraudulently induced to enter into a shareholder agreement or a transaction related to the shareholder agreement, such as a redemption agreement. The case *Allen v. Devon Energy Holdings, L.L.C.*<sup>46</sup> is instructive and outlines in detail the types of common law and statutory fraud claims that might be asserted by a shareholder in the context of share redemption.<sup>47</sup> In *Allen*, a minority shareholder claimed he was fraudulently induced to redeem his shares at a value that was twenty times less than the value at which a third party purchased the entity’s shares one and a half years later.<sup>48</sup> The court in *Allen* found that the majority shareholder’s statement in a letter to the minority shareholder that certain wells would be “non-

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42. See *Ritchie v. Rupe*, 443 S.W.3d 856, 888 n.56 (Tex. 2014).

43. *Zorrilla v. Aypco Constr. II, LLC*, 469 S.W.3d 143, 153 (Tex. 2015).

44. *Transp. Ins. Co. v. Faircloth*, 898 S.W.2d 269, 276 (Tex. 1995).

45. See *Allen v. Devon Energy Holdings, L.L.C.*, 367 S.W.3d 355, 370 (Tex. App.—Houston [1st Dist.] 2012, pet. granted, judgment vacated w.r.m.).

46. *Id.*

47. *Id.* at 369–76.

48. *Id.* at 367.

economic” was a material statement of fact and actionable for purposes of a fraudulent inducement claim.<sup>49</sup>

Fraud can take many forms, and the factual circumstances in reported cases vary widely. Here are some fairly recently reported shareholder-related fraud cases:

- *Abdu v. Hailu*,<sup>50</sup> affirming the trial court’s dismissal of a fraudulent lien claim by a shareholder in a closely-held corporation against another shareholder and third party because plaintiff shareholder asserted the claim individually, though it belonged to the corporation, and sought damages personally for the alleged wrong.
- *Lowry v. Tarbox*,<sup>51</sup> affirming the judgment on jury verdict for a minority shareholder physician’s claims against the co-owner of a neurology medical practice who was also the practice’s majority shareholder, for fraud against the physician.
- *Siddiqui v. Fancy Bites, LLC*,<sup>52</sup> affirming the district court’s judgment for two members of a four-member LLC on a claim that other LLC members fraudulently induced them to purchase their interests in the LLC.
- *Davis v. White*,<sup>53</sup> affirming judgment on a jury verdict for a former law partner on a claim against another partner for fraud in the failure to disclose the true nature of the partnership’s finances.
- *White v. Zhou Pei*,<sup>54</sup> affirming judgment for two shareholders of a closely-held corporation on a claim against the remaining shareholders for fraud by failure to disclose requested information regarding the corporation’s status and finances, but reversing judgment for shareholder’s claim that remaining shareholders violated fiduciary duties owed to him as a creditor of the corporation because there was insufficient evidence that the shareholder was in fact a creditor.

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49. *Id.* at 372, 376.

50. No. 05-17-01261-CV, 2018 WL 6716547 (Tex. App.—Dallas Dec. 21, 2018, no pet. h.).

51. 537 S.W.3d 599 (Tex. App.—San Antonio 2017, pet. denied).

52. 504 S.W.3d 349 (Tex. App.—Houston [14th Dist.] 2016, pet. denied).

53. No. 02-13-00191-CV, 2014 WL 7387045 (Tex. App.—Fort Worth Dec. 29, 2014, pet. granted), *judgment vacated on other grounds*, 475 S.W.3d 783 (Tex. 2015).

54. 452 S.W.3d 527 (Tex. App.—Houston [14th Dist.] 2014, no pet.).

In addition to supporting a common-law fraud claim, false representations may also be actionable as statutory fraud under the Texas Securities Act.<sup>55</sup>

The Texas Securities Act (“TSA”) provides,

A person who offers to buy or buys a security . . . by means of an untrue statement of a material fact or an omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading, is liable to the person selling the security to him, who may sue either at law or in equity for rescission or for damages if the buyer no longer owns the security.<sup>56</sup>

The TSA provides for recovery of damages, rescission, and recovery of costs and “attorney’s fees if the court finds that the recovery would be equitable in the circumstances.”<sup>57</sup>

Fraudulent conduct relating to shareholder agreements may also give rise to statutory fraud claims under the Texas Business and Commerce Code provisions governing stock transactions.<sup>58</sup> Actual

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55. See *Allen v. Devon Energy Holdings, L.L.C.*, 367 S.W.3d 355, 399–405 (Tex. App.—Houston [1st Dist.] 2012, pet. granted, judgm’t vacated w.r.m.) (trial court erred in granting summary judgment against the minority shareholder on his Texas Securities Act claims that he was misled by statements in redemption letter).

56. TEX. REV. CIV. STAT. ANN. art. 581-33B.

57. *Id.* art. 581-33D (outlining formulas for rescission and damages); see also *Allen*, 367 S.W.3d at 410 (finding that “any income the buyer received” recoverable as damages under the TSA does not include defrauding buyer’s proceeds from subsequent sale of the stock shares).

58. See TEX. BUS. & COM. CODE ANN. § 27.01 (“Fraud in Real Estate and Stock Transactions.”). Specifically,

Fraud in a transaction involving real estate or stock in a corporation or joint stock company consists of a

- (1) false representation of a past or existing material fact, when the false representation is
  - (A) made to a person for the purpose of inducing that person to enter into a contract; and
  - (B) relied on by that person in entering into that contract; or
- (2) false promise to do an act, when the false promise is
  - (A) material;
  - (B) made with the intention of not fulfilling it;
  - (C) made to a person for the purpose of inducing that person to enter into a contract; and
  - (D) relied on by that person in entering into that contract.

*Id.* § 27.01(a).

damages, attorney's fees, and costs (including expert witness fees) are recoverable if a shareholder prevails.<sup>59</sup> Exemplary damages may also be recoverable depending on proof of actual awareness of the false representation.<sup>60</sup>

Texas also recognizes a claim for constructive fraud, which requires a showing of a breach of trust or of a preexisting confidential relationship.<sup>61</sup> Actual fraud focuses on the wrongdoer's "intent to deceive, whereas constructive fraud is . . . [based on] breach of some legal or equitable duty which . . . the law declares fraudulent because of its tendency to deceive others, to violate confidence, or to injure public interests."<sup>62</sup> Where constructive fraud is found, a constructive trust over wrongfully obtained proceeds may be ordered.<sup>63</sup>

Fraud claims are often quite fact-dependent, and it may be difficult to anticipate them when drafting a shareholder agreement. Some provisions may prove helpful in reducing the likelihood of such claims or providing defenses to such claims. For example, because fraud claims require proof of reliance, a contractual disclaimer of reliance may be helpful in defending against a fraud claim.<sup>64</sup> Note that the contractual disclaimer must be "clear and unequivocal."<sup>65</sup>

A merger clause should be included in a shareholder agreement to establish there are no other understandings or agreements between the parties other than those specifically enumerated in the shareholder agreement (or other ancillary written agreements between the parties). A typical merger clause provides,

The agreement modifies and supersedes all other preceding agreements, oral or written, between the parties and constitutes the entire agreement of the parties regarding the subject matter of the contract.

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59. *Id.* § 27.01(b), (e).

60. *Id.* § 27.01(c), (d).

61. *Archer v. Griffith*, 390 S.W.2d 735, 740 (Tex. 1964).

62. *Id.*

63. *Meadows v. Bierschwale*, 516 S.W.2d 125, 128 (Tex. 1974).

64. *See Italian Cowboy Partners Ltd. v. Prudential Ins. Co.*, 341 S.W.3d 323, 332 (Tex. 2011) (clarifying existing case law relative to contractual waivers of fraudulent inducement claims).

65. *Id.* at 331, 336; *Schlumberger Tech. Corp. v. Swanson*, 959 S.W.2d 171, 179 (Tex. 1997) (Disclaimer of reliance clause had "requisite clear and unequivocal expression of intent necessary to disclaim reliance.").

A merger clause demonstrates that the parties to a contract intended the agreement to be a final integrated expression of their agreement.<sup>66</sup> If a dispute arises, the parol evidence rule bars attempts to introduce extrinsic evidence to vary, contradict, or add to the terms of the shareholder agreement.<sup>67</sup>

Note that a standard merger clause, without an expressed clear and unequivocal intent to disclaim reliance, is insufficient to foreclose a fraudulent inducement claim.<sup>68</sup> Thus, a drafter should not make the error of including a merger clause without also including a clear and unequivocal disclaimer of reliance. A comparison between the disclaimer clauses in *Schlumberger*<sup>69</sup> and *Forest Oil*,<sup>70</sup> which the Court found effective to disclaim reliance, and the clause in *Italian Cowboy*,<sup>71</sup> which the Court found insufficient to disclaim reliance, is instructive for drafting purposes:

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66. *See Italian Cowboy*, 341 S.W.3d at 334.

67. *See, e.g.*, RESTATEMENT (SECOND) OF CONTRACTS § 216 cmt. e (1981) (Merger clauses are “likely to conclude the issue [of] whether the agreement is completely integrated.”).

68. *Italian Cowboy*, 341 S.W.3d at 334.

69. *Schlumberger Tech. Corp. v. Swanson*, 959 S.W.2d 171, 180 (Tex. 1997).

70. *Forest Oil Corp. v. McAllen*, 268 S.W.3d 51, 54 n.4 (Tex. 2008).

71. *Italian Cowboy Partners Ltd. v. Prudential Ins. Co.*, 341 S.W.3d 323, 332 (Tex. 2011).

<i>Italian Cowboy</i>	<i>Schlumberger</i>	<i>Forest Oil</i>
<p>“Tenant acknowledges that neither Landlord nor Landlord’s agents, employees or contractors have made any representations or promises with respect to the Site, the Shopping Center or this Lease except as expressly set forth herein. . . . This lease constitutes the entire agreement between the parties hereto with respect to the subject matter hereof, and no subsequent amendment or agreement shall be binding upon either party unless it is signed by each party . . . .”<sup>72</sup></p>	<p>“[N]one of us is relying upon any statement or representation of any agent of the parties being released hereby. Each of us is relying on his or her own judgment . . . .”<sup>73</sup></p>	<p>“[I]n executing the releases contained in this Agreement, . . . [the parties are not] relying upon any statement or representation of any agent of the parties being released hereby. [We are] . . . relying on . . . [our] own judgment . . . .”<sup>74</sup></p>

Shareholder fraud claims often involve disputes over share valuation.<sup>75</sup> As outlined in the checklist below, shareholder agreements can include provisions regarding agreed-upon valuation methods that apply when a buy-sell provision is triggered or shares are redeemed. Among many options, valuation provisions may require fair market value

72. *Italian Cowboy*, 3341 S.W.3d at 328.

73. *Schlumberger*, 959 S.W.2d at 180 (emphasis omitted).

74. *Forest Oil*, 268 S.W.3d at 54 n.4.

75. See, e.g., *Allen v. Devon Energy Holdings, L.L.C.*, 367 S.W.3d 355 (Tex. App.—Houston [1st Dist.] 2012, pet. granted, judgment vacated w.r.m.); *N. Tex. Opportunity Fund, L.P. v. Hammerman & Gainer Int’l, Inc.*, 107 F. Supp. 3d 620, 627 (N.D. Tex. 2015) (shareholder fraud claims arising out of director’s effort to hide company’s true value so that shareholder would redeem its shares for less than they were worth).

as determined by qualified appraisers, a formula price specified in the shareholder agreement, book value, or a set price adjusted by specified indexes to account for the passage of time. Requiring an independent valuation by a valuation specialist may help assuage a shareholder's concerns about receiving fair market value for redeemed shares.

#### ***4. Breach of Fiduciary Duty Based on Informal Fiduciary Relationship***

The Court in *Ritchie* confirmed that shareholders do not generally owe each other fiduciary duties.<sup>76</sup> But the Court acknowledged that in some circumstances, a preexisting confidential relationship between shareholders may result in an “informal” fiduciary relationship that could be the basis for a shareholder’s claim for breach of fiduciary duty.<sup>77</sup>

The determination of whether an informal fiduciary duty exists is fact intensive and could arise from “a moral, social, domestic, or purely personal relationship of trust and confidence.”<sup>78</sup> No such relationship exists in a business transaction unless it “existed prior to, and . . . [separate] from[] the transaction[] at issue.”<sup>79</sup>

In *Cardiac Perfusion Services, Inc. v. Hughes*,<sup>80</sup> the claims included allegations that the majority shareholder engaged in oppressive conduct by suppressing payment of profit distributions, paying himself excessive compensation, and refusing to allow examination of the corporation’s books and records.<sup>81</sup> Although the Court reversed the buyout remedy ordered by the trial court (based on the holding in *Ritchie*), the parties did not challenge, and the court affirmed, the findings for breach of “informal” fiduciary duty.<sup>82</sup> Typically, the business judgment rule would apply to corporate decision-making such as payment of dividends. But where informal fiduciary duties are found separate and apart from the shareholders’ business relationship, the Court in *Ritchie* saw “no reason to assume that the [business judgment] rule would apply.”<sup>83</sup> Moreover,

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76. *Ritchie v. Rupe*, 443 S.W.3d 856, 874 n.27 (Tex. 2004) (citing *Willis v. Donnelly*, 199 S.W.3d 262, 276–77 (Tex. 2006)).

77. *Id.* at 874 n.27, 892 n.63.

78. *Id.*

79. *Id.* at 874 n.27 (citing *Meyer v. Cathey*, 167 S.W.3d 327, 331 (Tex. 2005)); *see also Cardiac Perfusion Servs., Inc. v. Hughes*, 436 S.W.3d 790, 791 n.1 (Tex. 2014) (discussing availability of direct claim by shareholder against majority shareholder for breach of informal fiduciary duty).

80. 436 S.W.3d 790 (Tex. 2014).

81. *Id.* at 791.

82. *Id.* at 792.

83. *Ritchie v. Rupe*, 443 S.W.3d 856, 874 n.27 (Tex. 2014).

the *Ritchie* Court indicated a court-ordered buyout remedy could be viable in the event the court of appeals on remand found a breach of an informal fiduciary relationship.<sup>84</sup> Notably, on remand, the court of appeals found no evidence of an informal fiduciary duty.<sup>85</sup>

In summary, a direct claim by shareholders based on an informal fiduciary relationship is unavailable to most plaintiff shareholders because it is narrowly limited to preexisting fiduciary or confidential relationships. Nevertheless, to reduce further the possibility of shareholder claims based on an informal fiduciary-like relationship, drafters and their clients can include prophylactic provisions in the shareholder agreement, such as reciprocal statements that the shareholders agree they are not fiduciaries and have no preexisting personal relationship of trust or confidence.

### ***5. Unjust Enrichment and Quantum Meruit***

Recovery for unjust enrichment is available “when one person has obtained a benefit from another by fraud, duress, or the taking of an undue advantage.”<sup>86</sup> It is often alleged in tandem with a direct fraud claim. However, depending on the circumstances of the claim, including from whom the benefit was obtained, the claim may belong to the corporation.<sup>87</sup>

Quantum meruit may be a viable claim in the context of disputes over services provided by a shareholder to a company. Quantum meruit requires a plaintiff to prove (1) “valuable services were rendered;” (2) “for the person sought to be charged;” (3) “which services were accepted . . .;” and (4) under such circumstances as reasonable notice to the person that the plaintiff performing the services expected compensation from the person sought to be charged.<sup>88</sup>

Some shareholders provide sweat equity to benefit a company but later feel underappreciated or shortchanged. For example, this may be particularly true in a family business where family members are expected to contribute their efforts to the greater good of the enterprise.

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84. *Id.* at 892.

85. *Ritchie v. Rupe*, No. 05-08-00615-CV, 2016 WL 145581, at \*4–6 (Tex. App.—Dallas Jan. 12, 2016, pet. denied).

86. *Heldenfels Bros., Inc. v. Corpus Christi*, 832 S.W.2d 39, 41 (Tex. 1992).

87. *See Hudgeons v. Hallmark*, No. 02-14-00194-CV, 2015 WL 5634395, at \*5 (Tex. App.—Fort Worth Sept. 24, 2015, no pet.) (affirming summary judgment for company’s senior vice president on claims by former stockholders for unjust enrichment and money had and received because representative lacked standing in his individual capacity to assert such claims; representative did not identify any duty owed directly to him contractually or otherwise by the vice president).

88. *Vortt Expl. Co. v. Chevron U.S.A., Inc.*, 787 S.W.2d 942, 944 (Tex. 1990).

Such organizations frequently lack formal planning or employment agreements documenting their shareholders' contributions. A quantum meruit claim may provide relief in such circumstances. This claim may also arise in the context of a start-up company that does not initially generate earnings or distribute dividends to its shareholders to compensate them for their efforts. A compensation dispute later invariably arises over the value of the shareholders' respective contributions to the company. These types of disputes may be avoided by shareholder employment agreements specifically delineating the parties' rights and obligations and the compensation shareholders will receive for their services.

### **6. Texas Theft Liability Act / Conversion**

Depending on the facts and circumstances (and the criminality, if any) surrounding purported oppressive conduct, shareholders may assert additional common-law tort claims such as conversion and statutory claims under the Texas Theft Liability Act ("TLA").<sup>89</sup>

Conversion requires a showing of unauthorized and wrongful assumption and exercise of control over the personal property of another, to the exclusion of the owner's rights.<sup>90</sup> An action for conversion of money will lie when identification of money is possible and there is a breach of an obligation to deliver the specific money in question or to otherwise treat specific money.<sup>91</sup>

A Texas Theft Liability Act ("TLA") claim hinges on a showing of theft under applicable Texas criminal statutes.<sup>92</sup> "Theft' means unlawfully appropriating property or unlawfully obtaining services as described by [Texas penal statutes]."<sup>93</sup>

In *North Texas Opportunity Fund L.P. v. Hammerman & Gainer International, Inc.*,<sup>94</sup> the plaintiff shareholder alleged claims arising out of a director's efforts setting up a shell company to hide the company's profits and true value so the shareholder would redeem its shares for less than their true value.<sup>95</sup> He alleged that he was entitled to possess, and

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89. See *Ritchie*, 443 S.W.3d at 883; TEX. CIV. PRAC. & REM. CODE ANN. §§ 134.001–.005 ("Texas Theft Liability Act").

90. *Green Int'l, Inc. v. Solis*, 951 S.W.2d 384, 391 (Tex. 1997).

91. *N. Tex. Opportunity Fund, L.P. v. Hammerman & Gainer Int'l, Inc.*, 107 F. Supp. 3d 620, 637 (N.D. Tex. 2015) (citing *Sw. Indus. Inv. Co. v. Berkley House Investors*, 695 S.W.2d 615, 617 (Tex. App.—Dallas 1983, writ ref'd n.r.e.)).

92. TEX. CIV. PRAC. & REM. CODE ANN. § 134.003.

93. *Id.* § 134.002.

94. 107 F. Supp. 3d 620 (N.D. Tex. 2015).

95. *Id.* at 626–27, 637.

the corporation had stolen, a portion of the true profits of the corporation that he otherwise would have received absent the wrongful conduct.<sup>96</sup> He alleged that the specific profits were specifically identifiable and had been fraudulently taken, and the court found those allegations sufficient to state claims for conversion and under the TLA.<sup>97</sup> The shareholder's primary claims were for fraud, but the addition of a TLA claim opened the door to recovery of attorney's fees.

### **7. Receiverships**

Shareholders frequently seek the juridical appointment of a receiver as part of shareholder litigation. Often this remedy is sought in the context of a claim for shareholder oppression. *Ritchie* adopted a three-part test for determining "oppression" under the TBOC:

[A] corporation's directors or managers engage in "oppressive" actions . . . when they 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.<sup>98</sup>

When this test for oppression is met, a minority shareholder may be entitled to a rehabilitative receivership, but not a buyout remedy.<sup>99</sup>

The TBOC has several provisions relating to the appointment of receivers. Depending on the circumstances and proof shown, the TBOC provides for (1) a rehabilitative receiver and (2) a receiver for specific property.<sup>100</sup> Receivers are often sought in circumstances such as deadlocks in management, but they are difficult to obtain.<sup>101</sup> "Receivership is an extraordinarily harsh remedy and one that courts are particularly loathe to utilize."<sup>102</sup> Thus, courts strictly construe the requirements for receivership and the burden is "on the party seeking

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96. *Id.* at 637.

97. *Id.* at 638.

98. *Ritchie v. Rupe*, 443 S.W.3d 856, 871 (Tex. 2014).

99. *Id.* at 872–73, 877; *Cardiac Perfusion Servs., Inc v. Hughes*, 436 S.W.3d 790, 791–92 (Tex. 2014).

100. TEX. BUS. ORGS. CODE ANN. §§ 11.403, 11.404.

101. *See Spiritas v. Davidoff*, 459 S.W.3d 224, 232 (Tex. App.—Dallas 2015, no pet.) (no irreparable harm shown for the appointment of a receiver even where proof showed that business entities were deadlocked and that the deadlock prevented the entity from responding to letters of intent regarding real property).

102. *See, e.g., id.* at 232 (internal citation omitted).

the appointment” to demonstrate that the circumstances meet the requirements.<sup>103</sup>

#### **a. Rehabilitative Receiver**

The TBOC lists specific grounds to appoint a rehabilitative receiver, and details several additional requirements that apply to each ground:

(a) Subject to Subsection (b), a court that has jurisdiction over the property and business of a domestic entity under Section 11.402(b) may appoint a receiver for the entity's property and business if:

(1) in an action by an owner or member of the domestic entity, it is established that:

(A) the entity is insolvent or in imminent danger of insolvency;

(B) the governing persons of the entity are deadlocked in the management of the entity's affairs, the owners or members of the entity are unable to break the deadlock, and irreparable injury to the entity is being suffered or is threatened because of the deadlock;

(C) the actions of the governing persons of the entity are illegal, oppressive, or fraudulent;

(D) the property of the entity is being misapplied or wasted; or

(E) with respect to a for-profit corporation, the shareholders of the entity are deadlocked in voting power and have failed, for a period of at least two years, to elect successors to the governing persons of the entity whose terms have expired or would have expired on the election and qualification of their successors;

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103. *Id.*

(2) in an action by a creditor of the domestic entity, it is established that:

(A) the entity is insolvent, the claim of the creditor has been reduced to judgment, and an execution on the judgment was returned unsatisfied; or

(B) the entity is insolvent and has admitted in writing that the claim of the creditor is due and owing; or

(3) in an action other than an action described by Subdivision (1) or (2), courts of equity have traditionally appointed a receiver.<sup>104</sup>

Even if one of the grounds listed in Section 11.404(a) is met, subsection (b) authorizes a receiver only if (1) appointment is necessary “to conserve the property and business of the . . . entity and avoid damage to the interested parties;” and (2) “all other available legal and equitable remedies . . . are inadequate.”<sup>105</sup>

In narrowly construing these requirements, the Texas Supreme Court explained the type of oppression that might warrant a rehabilitative receiver.<sup>106</sup> The Court cited to fraudulent and illegal conduct that must “create a serious risk of harm to the corporation.”<sup>107</sup> A rehabilitative receiver is the only remedy available under the statute for shareholder oppression.<sup>108</sup>

A rehabilitative receiver may not be the preferred remedy for a shareholder, who may in many cases prefer a buyout. However, the appointment of a rehabilitative receiver can apply significant pressure and may still advance litigation strategy to achieve a favorable outcome. The Court in *Ritchie* left undecided the question of “whether a trial court could properly appoint a rehabilitative receiver and authorize or order the receiver to implement a buyout of a shareholder’s interests.”<sup>109</sup> But it left the door slightly ajar provided the order complies with the statute’s

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104. TEX. BUS. ORGS. CODE ANN. § 11.404(a) (emphasis added).

105. *Id.* § 11.404(b).

106. *See Ritchie v. Rupe*, 443 S.W.3d 856, 866–71 (Tex. 2014).

107. *Id.* at 871; *see also Spiritas*, 459 S.W.3d at 236 (overturning receiver appointment for lack of evidence of “irreparable injury” from management deadlock).

108. *Ritchie*, 443 S.W.3d at 872–73, 877; *Cardiac Perfusion Servs. Inc. v. Hughes*, 436 S.W.3d 790, 791 (Tex. 2014) (holding buyout remedy not available under common-law claim for oppression or under statute).

109. *Ritchie*, 443 S.W.3d at 877 n.32

requirement that any appointment “conserve the property and business of the domestic entity and avoid damage to interested parties.”<sup>110</sup> The Court further noted without deciding the issue: “If the buyout would help the shareholder but hurt the corporation, an order authorizing the receiver to effectuate the buyout would likely not comply with the statute authorizing the appointment.”<sup>111</sup> Thus, *Ritchie* provides at least some basis for a shareholder to seek a rehabilitative receiver with the follow-on goal of seeking court authorization of the receiver to implement a buyout.

Moreover, while a rehabilitative receivership may not be fully satisfying, it can lead to a liquidating receivership if an acceptable rehabilitation plan is not presented within one year of the appointment of the receiver.<sup>112</sup>

Note that a party is entitled to an interlocutory appeal of an order “appoint[ing] a receiver or trustee.”<sup>113</sup> Thus, even if other claims remain to be litigated, an interlocutory appeal of the receivership appointment may proceed.<sup>114</sup> The prospect of an immediate interlocutory review is likely another reason that trial courts exercise caution before granting this extraordinary remedy.

### **b. Receivership for Specific Property**

TBOC section 11.403 provides for a receivership over specific assets or property of the corporation:

(a) Subject to Subsection (b), and on the application of a person whose right to or interest in any property or fund or the proceeds from the property or fund is probable, a court that has jurisdiction over specific property of a domestic or foreign entity may appoint a receiver in an action:

- (1) by a vendor to vacate a fraudulent purchase of the property;
- (2) by a creditor to subject the property or fund to the creditor's claim;

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110. *Id.* (citing TEX. BUS. ORGS. CODE ANN. § 11.404(b)(1)).

111. *Id.*

112. *See* TEX. BUS. ORGS. CODE ANN. § 11.405(a)(3).

113. TEX. CIV. PRAC. & REM. CODE ANN. § 51.014(a)(1).

114. *Spiritas v. Davidoff*, 459 S.W.3d 224, 234–37 (Tex. App.—Dallas 2015, no pet.) (on interlocutory appeal, reversing appointment of receiver).

(3) between partners or others jointly owning or interested in the property or fund;

(4) by a mortgagee of the property for the foreclosure of the mortgage and sale of the property, when:

(A) it appears that the mortgaged property is in danger of being lost, removed, or materially injured; or

(B) it appears that the mortgage is in default and that the property is probably insufficient to discharge the mortgage debt; or

(5) in which receivers for specific property have been previously appointed by courts of equity.

(b) A court may appoint a receiver for the property or fund under Subsection (a) only if:

(1) with respect to an action brought under Subsection (a)(1), (2), or (3), it is shown that the property or fund is in danger of being lost, removed, or materially injured;

(2) circumstances exist that are considered by the court to necessitate the appointment of a receiver to conserve the property or fund and avoid damage to interested parties;

(3) all other requirements of law are complied with; and

(4) the court determines that other available legal and equitable remedies are inadequate.

(c) The court appointing a receiver under this section has and shall retain exclusive jurisdiction over the specific property placed in receivership. The court shall determine the rights of the parties in the property or its proceeds.

(d) If the condition necessitating the appointment of a receiver under this section is remedied, the receivership shall be

terminated immediately, and the receiver shall redeliver to the domestic entity all of the property remaining in receivership.<sup>115</sup>

This type of statutory receivership is less onerous and, in theory, easier to obtain than a rehabilitative or liquidating receiver.<sup>116</sup> However, it still requires a judicial determination that damage to the property will occur and “other available legal and equitable remedies are inadequate.”<sup>117</sup> As a result, courts will strictly construe these statutory requirements.<sup>118</sup>

### ***B. Shareholder Derivative Claims for Breach of Duty to the Entity***

In addition to various direct shareholder causes of action, the Court in *Ritchie* identified derivative actions for breach of fiduciary duty as another potential remedy for oppressed shareholders.<sup>119</sup> The TBOC contains provisions that make it easier for shareholders to assert derivative actions in the context of closely held corporations and LLCs.<sup>120</sup>

Specifically, for closely held corporations and LLCs, the TBOC relieves shareholder plaintiffs of the burden of making a pre-suit demand and meeting other typical standing requirements.<sup>121</sup> It specifically states that the typical derivative action presuit demand requirements “do not apply to . . . a closely held corporation.”<sup>122</sup> In *Sneed v. Webre*,<sup>123</sup> the Texas Supreme Court reaffirmed that shareholders of a closely held corporation have derivative standing without making presuit demand, and do not need to overcome the business judgment rule to bring a derivative suit.<sup>124</sup>

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115. TEX. BUS. ORGS. CODE ANN. § 11.403.

116. See *Finger Contract Supply Co. v. Republic Nat. Bank of Dall.*, 412 S.W.2d 79, 84 (Tex. App.—Forth Worth 1967, writ ref'd n.r.e.) (“The instant receivership is the least harsh of those for which provision has been made by law as applied to corporations. It is one wherein the corporation has been left intact, but where only specific assets belonging to it are made the subject matter of the receivership.”).

117. TEX. BUS. ORGS. CODE ANN. § 11.403(b)(2), (3).

118. See, e.g., *Spiritas*, 459 S.W.3d at 234 (trial court’s receivership order failed to identify “specific property,” rendering Section 11.403 inapplicable); *Alert Synteks, Inc. v. Jerry Spencer, L.P.*, 151 S.W.3d 246, 251 (Tex. App.—Tyler 2004, no pet.) (trial court abused discretion in appointing receiver over corporation’s assets).

119. *Ritchie v. Rupe*, 443 S.W.3d 856, 880–81 (Tex. 2014).

120. See *id.* (“[T]he Legislature has enacted special rules to allow its shareholders to more easily bring a derivative suit on behalf of the corporation.”).

121. See TEX. BUS. ORGS. CODE ANN. § 21.563(b).

122. *Id.*

123. 465 S.W.3d 169 (Tex. 2015).

124. *Id.* at 181, 189–93.

The TBOC also provides that “if justice requires,” the court may treat a derivative action “as a direct action brought by the shareholder for the shareholder’s own benefit, . . . and . . . [award relief] directly to the [shareholder] . . . .”<sup>125</sup>

Officers and directors owe fiduciary duties to the corporation.<sup>126</sup> As a result, breach of fiduciary duty is a common shareholder derivative claim.<sup>127</sup> Depending on the factual circumstances, derivative claims for fraud or other intentional torts may also be asserted on behalf of the corporation.

Although the business judgment rule does not apply to a closely held corporation shareholder’s standing to initiate a derivative claim, it does apply to the merits of a derivative proceeding when officers’ or directors’ actions are being challenged.<sup>128</sup> Thus, in any derivative action, the business judgment rule applies as a defense to the merits of the claims that the officers or directors breached their duties to the corporation.<sup>129</sup> “The business judgment rule . . . generally protects corporate officers and directors, who owe fiduciary duties to the corporation, from liability for acts that are within the honest exercise of their business judgment and discretion.”<sup>130</sup> Citing from its opinion in *Cates v. Sparkman*,<sup>131</sup> the Court in *Sneed* stated “that courts will not interfere with the officers or directors in control of the corporation’s affairs based on allegations of mere mismanagement, neglect, or abuse of discretion.”<sup>132</sup> To overcome the business judgment rule, a claim for breach of fiduciary duty against an officer or director must be “characterized by *ultra vires*, fraudulent, and injurious practices, abuse of power, and oppression on the part of the company or its controlling agency clearly subversive of the rights of the minority, or of a shareholder, and which, without such interference, would leave the latter remediless.”<sup>133</sup>

A derivative claimant must show that the board or management failed to comply with their fiduciary duties owed the company.<sup>134</sup> A shareholder may bring a derivative fiduciary claim for “failure to declare dividends” when a director violates the duty to act solely for the benefit

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125. TEX. BUS. ORGS. CODE ANN. § 21.563(c).

126. *Ritchie v. Rupe*, 443 S.W.3d 856, 883 (Tex. 2014).

127. *See id.*

128. *Id.* at 869; *Sneed v. Webre*, 465 S.W.3d 169, 179 (Tex. 2015).

129. *Sneed*, 465 S.W.3d at 178–79.

130. *Id.* at 173 (citing *Cates v. Sparkman*, 11 S.W. 846, 848–49 (Tex. 1889)).

131. 11 S.W. 846 (Tex. 1889).

132. *Sneed*, 465 S.W.3d at 186 (citing *Cates*, 11 S.W. at 849).

133. *Sneed*, 465 S.W.3d at 180 (quoting *Cates*, 11 S.W. at 849).

134. *See Ritchie v. Rupe*, 443 S.W.3d 856, 868–69, 884 (Tex. 2014).

of the company and refuses to declare dividends for some other, improper purpose.<sup>135</sup> Derivative claims often include allegations that a majority shareholder awarded himself excessive pay or unwarranted bonuses while withholding dividends or failing to fund company initiatives.<sup>136</sup> Such conduct may amount to a “misapplication of corporate funds [or] diversion of corporate opportunities” which may be redressed through a derivative action for breach of fiduciary duty.<sup>137</sup>

The reasonableness of compensation is generally a fact question, and the burden is on the plaintiff to prove it was excessive.<sup>138</sup> Moreover, if the challenged conduct was undertaken “for the benefit of the corporation [and] in compliance with the duties of care and loyalty,” there is no derivative liability even if the conduct causes harm to the derivative shareholder’s interests.<sup>139</sup>

### ***1. Direct Recovery by a Derivative Plaintiff***

As noted above, the TBOC provides for direct recovery to a derivative claimant from a closely-held corporation or LLC “if justice requires.”<sup>140</sup> Thus, even if the damage is to the corporation, a derivative plaintiff may be able to show that he is entitled to a share of monetary damages based on his pro-rata ownership, financial or other contribution, or another financial metric that makes direct recovery just under the circumstances.

In *Saden v. Smith*,<sup>141</sup> a 50% shareholder brought a derivative claim based on another corporate officer’s diversion of company revenues into a personal bank account.<sup>142</sup> The court treated the derivative claim as a direct claim, found a breach of fiduciary duty to the corporation, and awarded damages directly to the plaintiff shareholder.<sup>143</sup> Conversely, direct recovery was denied by the court in *Guajardo v. Hitt*.<sup>144</sup> There, the

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135. *Id.* at 885.

136. *Id.* at 884; *Landon v. S&H Mktg. Grp., Inc.*, 82 S.W.3d 666, 677 (Tex. App.—Eastland 2002, no pet.).

137. *See Ritchie*, 443 S.W.3d at 887; *Boehringer v. Konkel*, 404 S.W.3d 18, 28–30 (Tex. App.—Houston [1st Dist.] 2013, no pet.) (majority shareholder wrongfully awarded himself an excessive salary).

138. *Boehringer*, 404 S.W.3d at 29; *Gibney v. Culver*, No. 13-06-112-CV, 2008 WL 1822767, at \*13 (Tex. App.—Corpus Christi Apr. 24, 2008, pet. denied) (minority shareholder derivative action alleging excessive compensation paid to an officer).

139. *Ritchie*, 443 S.W.3d at 884.

140. TEX. BUS. ORGS. CODE ANN. §§ 21.563(c), 101.463(c); *see supra* Part II B.

141. 413 S.W.3d 450 (Tex. App.—Houston [1st Dist.] 2013, pet. denied).

142. *Id.* at 462.

143. *Id.*

144. 562 S.W.3d 768 (Tex. App.—Houston [14th Dist.] 2018, pet. denied).

court affirmed the district court's denial of direct recovery to the derivative plaintiff shareholder based on disbursement of unauthorized bonuses and commissions.<sup>145</sup> The court found that the shareholder did not demonstrate his entitlement to recover the corporation's damages directly.<sup>146</sup>

Depending on the circumstances and the nature of the injury to the derivative plaintiff shareholder, other equitable remedies may be available.<sup>147</sup> The statutory receivership remedies discussed above may also be appropriate in the context of a derivative lawsuit.<sup>148</sup>

### ***2. Attorney's Fees and Costs***

A prevailing derivative plaintiff "may" be entitled to recover attorney's fees expended on claims asserted on behalf of the corporation if the court determines that "the proceeding . . . resulted in a substantial benefit to the corporation."<sup>149</sup> In *DeNucci v. Matthews*,<sup>150</sup> the court awarded fees to the derivative plaintiff who prevailed on fiduciary duty claims that management awarded wrongful excessive distributions.<sup>151</sup> The statute also places risk on a derivative plaintiff by providing that a derivative plaintiff must pay the fees and costs of the corporation or other defendant if a court finds that the derivative "proceeding [was] instituted or maintained without reasonable cause or for an improper purpose."<sup>152</sup>

### ***3. Disgorgement or other Equitable Remedies***

Where a breach of fiduciary duty has occurred but there are no direct damages to the company, disgorgement may be a potential equitable remedy.<sup>153</sup> In the shareholder litigation context, this remedy

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145. *Id.* at 771.

146. *Id.* at 779–81.

147. See *DeNucci v. Matthews*, 463 S.W.3d 200, 206 (Tex. App.—Austin 2015, no pet.) (affirming equitable remedies of reinstatement to board of directors and ordering access to records).

148. See *supra* Part II A(7).

149. TEX. BUS. ORGS. CODE ANN. § 21.561(b)(1).

150. 463 S.W.3d 200 (Tex. App.—Austin 2015, no pet.).

151. *Id.* at 209–10.

152. TEX. BUS. ORGS. CODE ANN. § 21.561(b)(2).

153. *Burrow v. Arce*, 997 S.W.2d 229, 243, 245 (Tex. 1999) (fee forfeiture as equitable remedy for breach of fiduciary duty).

would require the offending officer or director to disgorge the improper benefit received through their breach of duty.<sup>154</sup>

### **III. SHAREHOLDER AGREEMENT: A POTENTIAL ANTIDOTE TO FUTURE DISPUTES**

In *Ritchie*, the parties had failed to enter into a shareholder agreement.<sup>155</sup> The Court repeatedly suggested that shareholders enter into shareholder agreements to protect their respective interests and avoid common shareholder disputes:

Shareholders of closely held corporations may address and resolve such difficulties by entering into shareholder agreements that contain buy-sell, first refusal, or redemption provisions that reflect their mutual expectations and agreements.<sup>156</sup>

Sometimes, [shareholders in a closely held corporation] enter into shareholder agreements to define things like their respective management and voting powers, the apportionment of losses and profits, the payment of dividends, and their rights to buy or sell their shares from or to each other, the corporation, or an outside party. . . . When, as in this case, there is no shareholders' agreement, minority shareholders who lack both contractual rights and voting power may have no control over how those disputes are resolved.<sup>157</sup>

[S]hareholders may also prevent and resolve common disputes by entering into a shareholders' agreement to govern their respective rights and obligations. Importantly, the Legislature has granted corporate founders and owners broad freedom to dictate for themselves the rights, duties, and procedures that govern their relationship with each other and with the corporation. . . . [W]e note that although [the corporation]'s owners did not enter into a shareholders' agreement, they

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154. See *In re Life Partners Holdings, Inc. Derivative Litig.*, Consol. Case No. DR-11-CV-AM, 2015 WL 8523103, at \*17–18 (W.D. Tex. Nov. 9, 2015) (discussing various equitable remedies in shareholder lawsuit).

155. *Ritchie v. Rupe*, 443 S.W.3d 856, 861 (Tex. 2014).

156. *Id.* at 871.

157. *Id.* at 878–79.

certainly could have done so, and by doing so could have avoided the current dispute.<sup>158</sup>

A shareholder agreement may have little impact on the merits of, or defenses to, certain claims. If a corporate officer or director wrongfully diverts corporate funds to a personal account, a breach of loyalty and abuse of power is clear, and the provisions of a shareholder agreement would likely be immaterial to the claim. However, other claims may be significantly impacted by a shareholder agreement. For example, a derivative claim alleging suppression of dividends may be defeated by language in a shareholder agreement governing payment of dividends. If management complies (or attempts to do so in good faith) with provisions in a shareholder agreement regarding calculation or timing of dividends, a claim for breach of fiduciary duty by a disgruntled shareholder is more likely to fail under the business judgment rule. Thus, a well-drafted shareholder agreement can establish that allegedly wrongful conduct falls within the honest exercise of business judgment and discretion.

At least one leading commentator has suggested that a shareholder agreement can be drafted to limit fiduciary duties in the corporate context.<sup>159</sup> Based on the catchall provision of TBOC Section 21.101(a) regarding the permissible contents of a shareholder agreement, she posits that the “fiduciary duties of . . . management . . . may be modified or waived [in a shareholder agreement] . . . so long as such provisions would be permissible in the context of a partnership.”<sup>160</sup> However, a drafter must be careful to ensure that the shareholder agreement does not run afoul of the TBOC provisions that expressly prohibit the elimination or restriction of certain duties, such as the duty of loyalty.<sup>161</sup>

### ***A. Shareholder Agreement Under the Texas Statute***

Section 21.101 of the TBOC, entitled “Shareholders’ Agreement,” outlines the basic functions and contents of a shareholder agreement:

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158. *Id.* at 881 (citations omitted).

159. Elizabeth S. Miller, M. Stephen Beard & Alyce A. Beard, *Fiduciary Duties, Exculpation and Indemnification in Texas Business Organizations*, State Bar of Texas, 17th Annual Choice, Governance, & Acquisition of Entities, 9 (May 24, 2019), <https://www.baylor.edu/law/facultystaff/doc.php/117971.pdf>.

160. *Id.*

161. *See id.* at 8; *see also* TEX. BUS. ORGS. CODE ANN. §7.001 (“Limitation of Liability of Governing Person”).

(a) The shareholders of a corporation may enter into an agreement that:

- (1) restricts the discretion or powers of the board of directors;
- (2) eliminates the board of directors and authorizes the business and affairs of the corporation to be managed, wholly or partly, by one or more of its shareholders or other persons;
- (3) establishes the individuals who shall serve as directors or officers of the corporation;
- (4) determines the term of office, manner of selection or removal, or terms or conditions of employment of a director, officer, or other employee of the corporation, regardless of the length of employment;
- (5) governs the authorization or making of distributions whether in proportion to ownership of shares, subject to Section 21.303;
- (6) determines the manner in which profits and losses will be apportioned;
- (7) governs, in general or with regard to specific matters, the exercise or division of voting power by and between the shareholders, directors, or other persons, including use of disproportionate voting rights or director proxies;
- (8) establishes the terms of an agreement for the transfer or use of property or for the provision of services between the corporation and another person, including a shareholder, director, officer, or employee of the corporation;
- (9) authorizes arbitration or grants authority to a shareholder or other person to resolve any issue about which there is a deadlock among the directors, shareholders, or other persons authorized to manage the corporation;

(10) requires winding up and termination of the corporation at the request of one or more shareholders or on the occurrence of a specified event or contingency, in which case the winding up and termination of the corporation will proceed as if all of the shareholders had consented in writing to the winding up and termination as provided by Subchapter K;

(11) with regard to one or more social purposes specified in the corporation's certificate of formation, governs the exercise of corporate powers, the management of the operations and affairs of the corporation, the approval by shareholders or other persons of corporate actions, or the relationship among the shareholders, the directors, and the corporation; or

(12) otherwise governs the exercise of corporate powers, the management of the business and affairs of the corporation, or the relationship among the shareholders, the directors, and the corporation as if the corporation were a partnership or in a manner that would otherwise be appropriate only among partners and not contrary to public policy.

(b) A shareholders' agreement authorized by this section must be:

(1) contained in:

(A) the certificate of formation or bylaws if approved by all of the shareholders at the time of the agreement; or

(B) a written agreement that is:

(i) signed by all of the shareholders at the time of the agreement; and

(ii) made known to the corporation; and

(2) amended only by all of the shareholders at the time of the amendment, unless the agreement provides otherwise.<sup>162</sup>

Notably, provisions in a shareholder agreement are effective and enforceable “among the shareholders and between the shareholders and the corporation” even when inconsistent with the Texas Business Organizations Code.<sup>163</sup>

Section 21.101 provides guidance regarding provisions that can be included in a shareholder agreement.<sup>164</sup> But it is principally a starting point. Drafters should consider a detailed shareholder agreement that outlines the rights and obligations of a company, its shareholders, and management. There is no universally suitable form shareholder agreement, and practitioners face a difficult task in attempting to anticipate and prophylactically address all the potential disputes that may arise among the relevant parties. Two commentators described the difficult balance of rights that drafters must undertake:

Drafters of the organizing documents of a closely held corporation cannot avoid a tradeoff. On the one hand, they must provide some protection to minority investors to ensure that they receive an adequate return on the minority shareholder’s investment if the venture succeeds. On the other hand, they cannot give the minority too many rights, for the minority might exercise their rights in an opportunistic fashion to claim returns at the majority’s expense.<sup>165</sup>

### ***B. Checklist of Provisions that Should be Considered for Shareholder Agreements.***

The following are potential provisions that may be included in shareholder agreements to help avoid many common shareholder disputes.

- Stock transfer restrictions. Shareholders in privately held companies desire certainty and control over who may become a shareholder in the future. Transfer restrictions preclude shareholders from transferring (including selling, assigning, encumbering, pledging, or gifting) company stock without permission from some or all the other shareholders. The TBOC

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162. TEX. BUS. ORGS. CODE ANN. § 21.101.

163. *Id.* § 21.104.

164. *See id.* § 21.101.

165. Frank H. Easterbrook & Daniel R. Fischel, *Close Corporations and Agency Costs*, 38 STAN. L. REV. 271, 285 (1986).

contains various provisions relating to transferability and outlines the circumstances under which the transfer of a security is valid.<sup>166</sup> Section 21.213 provides that a transfer restriction is enforceable if “the restriction is reasonable and noted conspicuously on the certificate.”<sup>167</sup> A shareholder agreement often specifies those persons or categories of persons or entities (such as family partnerships or related entities) to whom shares may be transferred in the future and the mechanisms for such transfers. The transfer restrictions should require notice to all shareholders to ensure compliance.

- Pledges. Shareholders may wish to pledge their shares to secure the repayment of a corporation’s debt, or to secure personal indebtedness.
- Buy-Sell Provisions. These important provisions provide a mechanism for the purchase and sale of a shareholder’s interest upon the occurrence of specified trigger events. Trigger events commonly include death of a shareholder, divorce, termination of a shareholder’s employment, bankruptcy, and disability. Buy-sell provisions can be mandatory or voluntary.
  - Put right (voluntary). This provision allows a shareholder to sell their shares upon a trigger event. For example, a shareholder may wish to sell their shares in the event of a change in control of the company.
  - Call right (involuntary). This provision requires a shareholder to sell their shares upon a trigger event. For example, the company may wish to force a shareholder to sell their shares upon termination of employment or upon a finding of specified misconduct by a shareholder. Given the potential disputes that could arise from the exercise of such a provision, the shareholder agreement should outline in detail the mechanisms for exercise of the call right and for an agreed upon method for valuing the shares.
  - Drag along and tag along rights. A drag along right allows a majority shareholder to force a minority shareholder to sell their shares in the event the majority shareholder is selling shares. Drag along rights help prevent a minority shareholder from blocking a sale of the company. They can

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166. TEX. BUS. ORGS. CODE ANN. §§ 21.209, 21.211.

167. *Id.* § 21.213(a).

be complex provisions that include, for example, a minimum target sale price before the minority shareholder is forced to sell his shares. Tag along rights give a shareholder the right (but not the obligation) to sell shares at the same time and price as another shareholder. Typically, the minority shareholder possesses the tag along rights, but the provision can be drafted to go both ways and also permit a majority shareholder to tag along on a minority shareholder sale.

- Right of first refusal and first offer. These important provisions are a breed of transfer restriction in that they prevent a shareholder from selling shares to a third party without first offering them to the existing shareholders. A ROFR applies when a shareholder desires to accept an offer made by a third party to purchase their shares. A ROFO applies when a shareholder wishes to transfer his shares to a third party before an offer is made. In both cases, the shareholder must first offer the shares to the company and/or its shareholders on the same terms before the sale can occur. ROFRs can be linked to trigger events such as death or divorce of a shareholder.
- Preemptive rights. Contractual preemptive rights provide shareholders the right to purchase company stock which may be offered in the future, so as to maintain their percentage of ownership in the company. These can be complex provisions that should account for factors such as different classes of shares, shares issued as options or other compensation, and convertible securities. Note that TBOC Sections 21.203-21.208 provide additional statutory preemptive rights and restrictions in certain circumstances.
- Timing provisions. The shareholder agreements should specify the time for exercising rights generated by buy-sell provisions and transfer restrictions. For example, the shareholder agreement should impose a time deadline on a shareholder to exercise an option to purchase shares.
- Purchase Price / Share Valuation. As discussed further below, disputes over share valuation frequently arise in shareholder litigation. The shareholder's agreement should include provisions regarding the determination of purchase price in the event of a sale or transfer of shares. There are multiple options that can be tailored to account for the specific situation, nature

of the business and its assets (such as real estate assets), and the relationships of the shareholders. Some valuation options include (1) a fixed price; (2) fair market value determined by appraisal by a third party; (3) capitalization of historical earnings method; (4) book value; and (5) a formula price based on the company's financial metrics and performance. Adjustments for minority discount and lack of marketability may be appropriate. Book value may underestimate the true value of a business because assets are carried on the balance sheet at cost and without taking goodwill or going concern value of the business into account. A contract price may seem reasonable at the time a shareholder agreement occurs but may fall below fair value over time. However, courts typically uphold buy-sell provisions based on a stated price or book value even where fair value at the time of the triggering event exceeds the contract price or book value.<sup>168</sup> A capitalization of earnings method takes the average of historical earnings for some specified period and multiplies those earnings by a multiplier to arrive at a value. In theory this method may arrive at a value that better matches the true value of the company at the time of the trigger event. However, it involves far more complex drafting than the other methods.

- Dividends. A shareholder agreement may provide for payment of dividends in certain circumstances. For example, the agreement can provide for mandated dividends triggered by certain company financial metrics.
- Board representation. The shareholder agreement should address various governance matters, including board size, shareholder representation, voting power of the majority and minority shareholders, director designation rights, restrictions on removal of board members, and filling of board vacancies.
- Board committees. The shareholder agreement can provide for committees, possibly comprising independent directors, to make decisions on issues that, by their nature, may lead to disputes (such as management compensation).
- Board observer rights. The shareholder agreement can provide minority shareholders with board observer rights without giving them voting and decisionmaking power. Such a provision

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168. See *Dixie Pipe Sales, Inc. v. Perry*, 834 S.W.2d 491, 494 (Tex. App.—Houston [14th Dist.] 1992, writ denied) (enforcing a corporation's right to purchase shares at book value).

can help increase decisionmaking transparency and reduce the potential for conflict.

- Special voting rights. This provision may give minority shareholders veto power over certain significant events or decisions, which can be specified in the provision. Some examples of such events include committing the company to incur debt over a certain amount, loaning money over a certain amount, or entering into related-party transactions.
- Access to books, records, and information. As discussed above, shareholders have statutory rights to certain corporate information. The shareholder agreement can broaden or clarify those rights.
- Confidentiality. A business of any substance regularly produces confidential information. It may be confidential for multiple reasons, such as trade secret protection, business competitiveness, shareholder wealth management, or family or personal business privacy. A confidentiality provision can be used to protect such information as a matter of practice, and to prevent disgruntled minority shareholders from releasing sensitive information.
- Business / corporate opportunity clause. These provisions can either require shareholders to submit specific corporate opportunities to the company or explicitly provide that shareholders have no such obligation.<sup>169</sup>
- Arbitration. Shareholders can agree to arbitrate their disputes, and the specific language of an arbitration provision can be important in determining the procedures for deciding disputes.
  - Scope. Whether a claim falls within the scope of a shareholder agreement's arbitration provision turns on its language. In *Baty v. Bowen, Miellette & Britt, Inc.*,<sup>170</sup> the court construed the scope of an arbitration provision in a shareholder agreement to include a shareholder's claims for breach of fiduciary duty, oppression, and conversion arising out of an alleged forced sale of shares to the other shareholders.<sup>171</sup> The court focused on the specific language of the arbitration provision that "any controversy or claim

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169. See TEX. BUS. ORGS. CODE ANN. §§ 2.101(21), 21.101(a)(12), 152.002; Miller, Beard, & Beard, *supra* note 159.

170. 423 S.W.3d 427, 438–41 (Tex. App.—Houston [14th Dist.] 2013, pet. denied).

171. *Id.* at 440–41.

arising pursuant to this Agreement shall be submitted to and resolved by a single arbitrator.”<sup>172</sup> The court found that “pursuant to’ means ‘in carrying out’” the terms of the Shareholder Agreement.<sup>173</sup> The court concluded that the shareholder’s claims for breach of fiduciary duty, oppression, and conversion were “claims arising in ‘carrying out’ or ‘pursuant to’ the Shareholders’ Agreement” and must be arbitrated.<sup>174</sup>

- Arbitration procedures. Consideration should be given to how shareholder arbitration will be conducted. For example, arbitration clauses can specify the number of and method for selecting arbitrators, location of the arbitration, the amount of permitted discovery, arbitration timeline including time for issuing a decision, and other mechanics of an arbitration. Outlining these details in the shareholder agreement can ensure that the arbitration is streamlined and advances the goal of efficiently resolving shareholder disputes.
- Forum / venue selection. For various reasons, parties may prefer to preserve their rights to seek relief in the courts rather than arbitrate.<sup>175</sup> In such circumstances, the parties should consider agreeing to resolve any disputes in a specific judicial forum and thereby head off potential litigation forum shopping. Forum selection provisions can be particularly helpful where shareholders reside in different locations or the corporation has multiple offices and disparately located operations. A particularly business-friendly forum (such as Delaware) may also be a preferred forum for resolving disputes arising out of the shareholder agreement.
  - Subject to public policy constraints, forum selection clauses are generally enforceable in Texas. In *In re Lyon*

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172. *Id.* at 439 (emphasis supplied).

173. *Id.* at 440 (citing *Syntax, Inc. v. Hall*, 899 S.W.2d 189, 191–92 (Tex. 1995) (construing “pursuant to” language in an arbitration agreement as “carrying out” the terms of the agreement)).

174. *Id.* at 441.

175. The expense of arbitrator and arbitration filing fees, lack of dispositive motion practice, and the lack of appellate rights are some of the potential factors one may consider in avoiding arbitration. See David F. Johnson, *The Enforcement of Contractual Jury Waiver Clauses in Texas*, 62 BAYLOR L. REV. 649, 650–51 (2010) (discussing the potential downsides of arbitration clauses).

*Financial Services, Inc.*,<sup>176</sup> the Texas Supreme Court analyzed the scope of an arbitration provision in a shareholder agreement in the context of a minority shareholder dispute.<sup>177</sup> Specifically, in *Pinto Technology Ventures, L.P. v. Sheldon*,<sup>178</sup> the Court held that a minority shareholder's statutory, common-law tort, and fiduciary claims evidenced a "dispute arising out of" the shareholder agreement and therefore fell within the scope of the agreement's Delaware forum selection clause.<sup>179</sup> The subject forum selection clause contained commonly used "arising out of" language.<sup>180</sup> The Court noted that, in finding the subject claims within the scope of the forum selection provision, it refused to allow "artful pleading" to avoid the forum selection clause, and it "focus[ed] on the substance of the claims, not the labels, and avoid[ed] 'slavish adherence to a contract/tort distinction.'"<sup>181</sup>

- Shareholders can contractually agree that any litigation between them will be filed only in a particular forum (sovereign or state) and venue (location within that state). For example, a forum selection provision could require a lawsuit to be filed "in the courts of the State of Texas." A venue selection provision, in contrast, refers to the place within a forum where the case must be tried ("in the state courts of Harris County, Texas," for example). Some transactions may be subject to statutory venue provisions, including "Major Transactions" as defined by statute.<sup>182</sup>
- Jury Waiver. This provision may be included to require any disputes to be decided by a judge and not a jury. Jury waivers are enforceable if they are conspicuous and were entered into knowingly and voluntarily.<sup>183</sup>

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176. 257 S.W.3d 228 (Tex. 2008).

177. *Id.* at 231–32.

178. 526 S.W.3d 428 (Tex. 2017).

179. *Id.* at 439.

180. *Id.* at 434.

181. *Id.* at 441 (internal citations omitted).

182. See TEX. CIV. PRAC. & REM. CODE ANN. § 15.020(c).

183. *In re Gen. Elec. Capital Corp.*, 203 S.W.3d 314, 316 (Tex. 2006); *In re Prudential Ins. Co.*, 148 S.W.3d 124, 132–33 (Tex. 2004).

#### ***IV. CONCLUSION***

The Court in *Ritchie* significantly narrowed the litigation remedies available for oppressed minority shareholders. However, reported cases since *Ritchie* confirm that shareholder litigation continues to be pursued through several available statutory and common-law causes of action and remedies. The onus remains on practitioners to listen carefully to their clients and draft robust shareholder agreements tailored to their clients' current and—to the extent possible—future needs. Through a well-drafted shareholder agreement, many shareholder disputes may be more efficiently resolved, or avoided entirely.