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Getting around *Ritchie*: Choice-of-Law in Minority Oppression Claims

BY WADE L. MCCLURE AND BRANDON W. MAXEY

Since the Texas Supreme Court's clarification in *Ritchie v. Rupe*, finding there is no recognized common-law claim for minority shareholder oppression, much has been written of the hurdles facing minority shareholders now under Texas law. The limitations are apparent, but the creativity of the lawyers facing those hurdles is noteworthy.

One of the responses to *Ritchie* in this global economy is to assert that other state law applies. In today's environment, this is hardly a stretch. Even the smaller closely held entities have offices in multiple states, with employees, shareholders, and directors in different locations. Meetings occur by phone, via Skype or other modes available through the continued advancement in technology.

This new-age economy leads to a fundamental question. Which state law applies to the alleged oppressive activity? By examining analogous Texas case law and the Restatement, some guiding factors emerge.

Start With the Contract

A Texas court would start with any written contract between the parties. Often, this will be the Shareholders' Agreement—which may form the basis of any potential minority shareholder oppression claim. A choice-of-law provision may answer the question, if it is broad enough to encompass the oppression claim. But, a typical provision such as "Texas law governs the interpretation of the Shareholders' Agreement" may not control an independent claim of shareholder oppression.

Moreover, even a broadly drafted choice of law provision may be disregarded by the Court if: (1) the chosen state has no substantial relationship to the facts, or (2) the application of the law of the chosen state would violate public policy. *See Ennis, Inc. v. Dunbrooke Apparel Corp.*, 427 S.W.3d 527, 530-31 (Tex.App.—Dallas 2014).

But what happens when the agreement is silent on the applicable law or is not broad enough to cover alleged shareholder oppression claims?

What is the Choice-of-Law Standard?

There are two views on the classification of a minority shareholder oppression claim. Some courts have considered it a tort claim, but other courts and academic treatises characterize it as stemming from the internal governance of the company (or a "derivative" claim). This distinction is of interest because Texas courts apply a different standard for choice-of-law considerations with respect to these different claims.

For most causes of actions, including those sounding in tort, Texas follows the Restatement (Second) Conflict of Laws—which provides that, where a contract does not specify which law to apply, the Court will apply the law of the state with "the most significant relationship to the transaction and the parties…" *See Minnesota Min. and Mfg. Co. v. Nishika Ltd.*, 955 S.W.2d 853, 856 (Tex. 1996); *see also Ford Motor Co. v. Aguiniga*, 9 S.W.3d 252, 259-260 (Tex.App.—San Antonio 1999).

This analysis will focus first on "the place of injury," but will also consider (i) the place where the conduct causing the injury occurred, (ii) the place of incorporation and place of business of the parties, and (iii) the place where the parties' relationship is centered. *Alarcon v. Velazquez*, 552 S.W.3d 354, 362-63 (Tex.App.—Houston [14th Dist.] 2018). In minority shareholder oppression fact patterns, this could implicate several different states (and even countries). In short, this analysis will depend heavily on the facts of the case and the relationships of the parties.

In the pre-*Ritchie* case of *Chapa v. Chapa*, the Court of Appeals for San Antonio referred to a minority shareholder oppression claim as a tort. 2012 WL 6728242 *1 (Dec. 28, 2012). Later, the *Ritchie* Court found clearly that such a claim is one sounding in tort. *See* 443 S.W.3d 856, 889 (Tex. 2014). Thus, the multi-factor test discussed above is likely the operative standard.

On the other hand, derivative claims in Texas are generally litigated under the laws of the place of incorporation, as stated in Tex. Bus. Org. § 21.562 and in the newly added § 21.555. *See* 2019 Tex. Sess. Law Serv. Ch. 899 (H.B. 3603).

Why Does This Matter?

The "significant relationship" test gives counsel considerable room for argument and trial courts discretion on how to rule. Given the nature of minority shareholder oppression claims, it is often difficult to determine where the alleged injury took place. Further, given the global reach of today's companies, it can also be difficult to discern *where* the conduct giving rise to these injuries took place.

For example, which law would apply for a shareholder oppression claim filed by a Texas resident concerning alleged oppressive conduct of a foreign corporation with its main offices in New Mexico? While facts would need to be developed further, expect that a creative lawyer may argue New Mexico law would apply.

In sum, *Ritchie* is not necessarily the last word on all minority shareholder oppression claims in Texas. A creative lawyer, given the right facts, could convince a trial court to apply law from another state that still recognizes a common-law shareholder oppression cause of action. **HN**

Wade L. McClure is a partner at Mayer LLP and Brandon W. Maxey is an associate at the firm. They can be reached at wmcclure@mayerllp.com and bmaxey@mayerllp.com, respectively.