THE BANKRUPTCY IMPLICATIONS OF A COURT-ORDERED BUYOUT FOR SHAREHOLDER OPPRESSION: IS IT A REMEDY AT ALL?

Lydia Rogers*

Jim Spade, Jill Heart, and Jack Diamond decide to go into business together and form Aces Wild, Inc., a Texas corporation. At the beginning, the parties share common expectations about their business. Each party would share equally in the profits and losses of the business as shareholders. Each party would enjoy lifetime employment with the business. As members of the board of directors, the parties would make decisions on how to grow their idea into a successful business from which they would benefit as both owners and employees.

The business operates as planned for a while, but then something happens. Maybe a business opportunity arises that Jack and Jill support but Jim does not want to take the risk. Perhaps Jack and Jill no longer view Jim as a desirable business partner. Possibly Jim wants to sell the business to a larger company while Jack and Jill want to keep things the same. Whatever it is, the parties' once pleasant working relationship becomes hostile.

Jim begins to notice that Jack and Jill are treating him differently. The other two board members shoot down any idea Jim proposes. Once unanimous votes are now split 2-1, with Jim always on the losing end. Jack and Jill vote to adopt a new bonus policy where they receive disproportionately higher compensation than Jim. When Jim confronts Jack and Jill about the unfairness of these decisions, Jack and Jill state that they are doing nothing illegal, and if Jim does not like it, they would buy out his shares at a nominal price. Jim begins to feel like he has no say in the business he created.

This story is a common one in closely held corporations. Once friendly business partners become hostile, and a majority interest begins taking

---

*J.D. Candidate, Baylor University School of Law, Summer 2012; B.B.A. Baylor University, 2009. The author would like dedicate this article to her fiancé, Brandon Webb, who has shown her unconditional love and support throughout the author's law school experience. The author would like to thank Professor Elizabeth Miller for her guidance and oversight of this article. The author would also like to thank the staff of the Baylor Law Review for their tireless efforts in readying this article for publication.

actions that are unfair to the minority interest but do not rise to the level of illegality. The doctrine of shareholder oppression developed to grant minority shareholders relief from oppressive treatment by the majority. The most common remedy for shareholder oppression is a buyout, where the court orders the majority interest to "buy out" the minority interest by paying him the fair value of his shares. This appears to be an advantageous solution, since the minority interest can recover the value of his or her shares without forcing the dissolution of the business. However, if the business files bankruptcy, it is likely that the minority shareholder will never see a dime of the buyout money. The treatment of a buyout judgment in bankruptcy raises the question of whether it is a viable remedy at all.

This article will briefly summarize the shareholder oppression doctrine and its buyout remedy before considering the likely treatment of a buyout judgment in bankruptcy. Then the author will express her belief on how bankruptcy courts should handle buyout judgments in the future.

I. THE DOCTRINE OF SHAREHOLDER OPPRESSION

The doctrine of shareholder oppression developed in the context of the closely held corporation.[1] A closely held corporation is owned by a small number of shareholders that are actively involved in the management of the business.[2] Because closely held corporations are not typically publicly traded, it is unlikely that there is an active market for the company's shares.[3] Unlike the role of passive investor held by a shareholder in a

[1] Although this article addresses shareholder oppression in the context of the closely held corporation, it is generally accepted that the doctrine also applies to limited liability companies (LLCs). *See* TEX. BUS. ORGS. CODE ANN. § 11.404(a)(1)(C) (West 2008) (addressing shareholder oppression in Title 1, which applies to all domestic entities, including LLCs); Pinnacle Data Servs., Inc. v. Gillen, 104 S.W.3d 188, 191–92, 196 (Tex. App.—Texarkana 2003, no pet.) (suggesting that oppression applies in the LLC setting); Douglas K. Moll, *Minority Oppression & the Limited Liability Company: Learning (or Not) from Close Corporation History*, 40 WAKE FOREST L. REV. 883, 957 (2005) (concluding that the oppression doctrine should apply in the LLC context).

[2] *See* Donahue v. Rodd Electrotype Co. of New Eng., 328 N.E.2d 505, 511 (Mass. 1975). The closely held corporation discussed in this paper should not be confused with the statutory close corporation. *See generally* TEX. BUS. ORGS. CODE ANN. §§ 21.701–.732. A statutory close corporation must include in its certificate of formation: "This is a close corporation." *Id.* § 3.008. A closely held corporation may choose to but does not have to become a statutory close corporation for its shareholders to take advantage of the oppression doctrine.

[3] *Donahue*, 328 N.E.2d at 514 (stating that by definition the secondary market is unavailable for shares in the closely held corporation).

publicly traded company, shareholders in a closely held corporation must rely on their compensation as company employees and shareholder dividends to receive a return on their investment.[4] In many ways, a closely held corporation is more akin to a partnership than its larger, publicly traded, corporate brethren.[5]

The application of the conventional standard of majority rule to closely held corporations often leads to less than favorable consequences for the minority shareholder.[6] Because the majority shareholder, whether acting individually or in tandem with another shareholder, can control the board of directors,[7] the majority shareholder has free rein to act to the detriment of the minority.[8] Prior to the development of the oppression cause of action, the minority shareholder had inadequate means to protect his or her interest and was left to the mercy of the majority.[9] As previously mentioned, the lack of a secondary market prevented minority shareholders from selling their shares to cash out of the company.[10] Absent a buy-sell agreement, the minority shareholder could not force the company or the majority shareholders to redeem his or her shares for fair value.[11] Further, the

[4] *See* Wilkes v. Springside Nursing Home, Inc., 353 N.E.2d 657, 662 (Mass. 1976).

[5] *See* Redmon v. Griffith, 202 S.W.3d 225, 237 (Tex. App.—Tyler 2006, pet. denied) (citing Willis v. Donnelly, 118 S.W.3d 10, 31–32 (Tex. App.—Houston [14th Dist.] 2003), *rev'd on other grounds*, 199 S.W.3d 262 (Tex. 2006)).

[6] Douglas K. Moll, *Shareholder Oppression in Texas Close Corporations: Majority Rule (Still) Isn't What It Used to Be*, 43 TEX. J. BUS. L. 21, 22 (2009).

[7] *See* TEX. BUS. ORGS. CODE ANN. § 21.405 (stating that it is the duty of the shareholders to elect the board of directors for each term); *id.* § 21.359 (stating that directors shall be elected by a plurality of the votes cast by shareholders entitled to vote at a meeting in which a quorum is present). The majority interest can vote its shares to elect most, if not all, of the directors without regard to the minority interest. *See* Moll, *supra* note 6. However, if the certificate of formation authorizes cumulative voting in the election of directors, the minority shareholder has a greater opportunity to elect a representative to the board. *See* TEX. BUS. ORGS. CODE ANN. § 21.361.

[8] Moll, *supra* note 6. It is common for shareholders in a closely held corporations to elect themselves to positions on the board. 1 F. HODGE O'NEAL & ROBERT B. THOMPSON, O'NEAL & THOMPSON'S OPPRESSION OF MINORITY SHAREHOLDERS & LLC MEMBERS § 1:2, at 1-3 (rev. 2d ed. 2005). When relationships between the shareholders deteriorate, the majority interest, due to his or her superior voting power, has the ability to both fire the minority shareholder as an employee and either vote the minority shareholder off the board of directors or exclude him or her from participation in the management of the company. *See* Meiselman v. Meiselman, 307 S.E.2d 551, 558 (N.C. 1983).

[9] *See* Moll, *supra* note 6, at 22–23.

[10] *See* Brenner v. Berkowitz, 634 A.2d 1019, 1027 (N.J. 1993).

[11] *See* Goode v. Ryan, 489 N.E.2d 1001, 1004 (Mass. 1986).

minority shareholder lacks the voting power to compel the voluntary winding up and termination of the corporation to recover the value of his investment.[12] This lack of exit rights for injured minority shareholders led to the creation of a more viable alternative—the doctrine of shareholder oppression.[13]

A minority shareholder may assert violations of statutory and fiduciary duties in a shareholder oppression action.[14] First, the Texas Legislature adopted a statutory action for shareholder oppression in the Texas Business Organizations Code.[15] Under the code's winding up and termination provisions, a court may appoint a receiver for the entity if "in an action by an owner . . . it is established that . . . the actions of the governing persons of the entity are illegal, oppressive, or fraudulent . . . ."[16] Although, the receivership action is not the favored remedy to vindicate an oppressed shareholder,[17] this provision serves as the starting point for the development of the oppression standard as it exists in Texas today.[18] Second, the development of shareholder oppression as a cause of action has essentially imposed upon majority shareholders a duty to not oppress minority shareholders.[19] Traditionally, Texas courts have found that shareholders do not as a matter of law owe duties to one another.[20] However, the courts

---

[12] *See* TEX. BUS. ORGS. CODE ANN. §§ 21.364(a)(2), (b), .502–.503 (requiring at least a two-thirds shareholder vote to wind up and terminate the corporation).

[13] *See* Moll, *supra* note 6, at 25 n.18 ("It is primarily for this reason (lack of exit rights) that the shareholder oppression doctrine is generally considered to be a close corporation doctrine.").

[14] *See, e.g.*, Redmon v. Griffith, 202 S.W.3d 225, 235 n.4 (Tex. App.—Tyler 2006, pet. denied) (stating that the same underlying facts may support both a cause of action for statutory shareholder oppression and breach of a fiduciary duty owed to a minority shareholder).

[15] TEX. BUS. ORGS. CODE ANN. § 11.404(a)(1)(C).

[16] *Id.*

[17] *See* Moll, *supra* note 6, at 39–40. Due to the harsh effects of the appointment of a receiver and a potential liquidation, an equitable, court-ordered buyout of the minority's shares has developed as the preferred remedy. *See id.*

[18] *See* Davis v. Sheerin, 754 S.W.2d 375, 381 (Tex. App.—Houston [1st Dist.] 1988, writ denied) (looking to decisions in states with similar statutes to determine what constitutes oppressive conduct).

[19] *See Redmon*, 202 S.W.3d at 236; Allchin v. Chemic, Inc., No. 14-01-00433-CV, 2002 WL 1608616, at *7 (Tex. App.—Houston [14th Dist.] July 18, 2002, no pet.) (not designated for publication) (citing Hoggett v. Brown, 971 S.W.2d 472, 488 n.13 (Tex. App.—Houston [14th Dist.] 1997, pet. denied)).

[20] *E.g.*, *Redmon*, 202 S.W.3d at 237; Willis v. Donnelly, 118 S.W.3d 10, 31–32 (Tex. App.—Houston [14th Dist.] 2003), *rev'd on other grounds*, 199 S.W.3d 262 (Tex. 2006); *Hoggett*, 971 S.W.2d at 488; Kaspar v. Thorne, 755 S.W.2d 151, 155 (Tex. App.—Dallas 1988, no writ);

have noted that in some situations such a duty may exist.[21] Fiduciary duties to shareholders may be created "in certain circumstances in which a majority shareholder in a closely held corporation dominates control over the business, and in closely held corporations in which the shareholders operate more as partners than in strict compliance with the corporate form."[22] In the typical shareholder oppression case, the plaintiff will allege both the statutory and fiduciary duty bases for the cause of action.[23]

As the Texas Supreme Court has yet to recognize the cause of action, there is no clear standard for oppression.[24] Nonetheless, the Texas courts of appeals have defined shareholder oppression in two ways:

> 1. majority shareholders' conduct that substantially defeats the minority's expectations that, objectively viewed, were both reasonable under the circumstances and central to the minority shareholder's decision to join the venture; or
>
> 2. burdensome, harsh, or wrongful conduct; a lack of probity and fair dealing in the company's affairs to the prejudice of some members; or a visible departure from the standards of fair dealing and a violation of fair play on which each shareholder is entitled to rely.[25]

Schoellkopf v. Pledger, 739 S.W.2d 914, 920 (Tex. App.—Dallas 1987), *rev'd on other grounds*, 762 S.W.2d 145 (Tex. 1988).

[21] *See supra* note 20.

[22] *Redmon*, 202 S.W.3d at 237 (citing *Willis*, 118 S.W.3d at 31–32).

[23] A trap for the unwary exists when asserting a shareholder oppression claim against a Delaware corporation. Delaware does not expressly recognize a cause of action for shareholder oppression. In *Nixon v. Blackwell*, 626 A.2d 1366, 1379 (Del. 1993), the Delaware Supreme Court expresses a lack of sympathy for minority shareholders who do not bargain for their protection upfront through appropriate provisions in the corporate bylaws or a shareholder's agreement. However, Delaware does recognize that controlling shareholders owe fiduciary duties to minority shareholders. Sterling v. Mayflower Hotel Corp., 93 A.2d 107, 109–10 (Del. 1952). Thus, a Texas plaintiff seeking to assert a claim against a Delaware corporation must be vigilant in pleading breach of fiduciary duty rather than shareholder oppression.

[24] *See* Moll, *supra* note 6, at 21. Most recently, the Texas Supreme Court denied review of *Ritchie v. Rupe*, a major shareholder oppression case out of the Dallas court of appeals. 339 S.W.3d 275 (Tex. App.—Dallas 2011) (petition for review denied Aug. 12, 2011).

[25] *Ritchie*, 339 S.W.3d at 289 (quoting Willis v. Bydalek, 997 S.W.2d 798, 801 (Tex. App.—Houston [1st Dist.] 1999, pet. denied)); *Redmon*, 202 S.W.3d at 234 (quoting *Bydalek*, 997 S.W.2d at 801); Pinnacle Data Servs., Inc. v. Gillen, 104 S.W.3d 188, 196 (Tex. App.—Texarkana 2003, no pet.) (quoting *Bydalek*, 997 S.W.2d at 801).

These definitions were intended to be broad and expansive in order to bring a wide array of improper conduct within the scope of the cause of action.[26] Further, the definitions are not mutually exclusive and conduct may be found to be oppressive under either or both standards.[27]

Courts have found a variety of majority shareholder conduct to be oppressive.[28] Most oppressive conduct aims to deprive the minority shareholder of her reasonable expectations to share in the management and profits of the company.[29] Typical wrongdoings in shareholder oppression actions include: denied access to the company's books and records;[30] malicious suppression of dividends;[31] using corporate funds for personal purposes;[32] "squeeze-out" techniques such as diverting corporate opportunities,[33] payment of inadequate dividends,[34] and attempting to deprive the minority shareholder of the fair value of his or her shares;[35] wrongful termination of the minority shareholder from employment;[36]

[26] *Ritchie*, 339 S.W.3d at 289 (quoting Davis v. Sheerin, 754 S.W.2d 375, 381 (Tex. App.—Houston [1st Dist.] 1988, writ denied)).

[27] *Id.* (citing Scott v. Trans-Sys., Inc., 64 P.3d 1, 6 (Wash. 2003)).

[28] *Redmon*, 202 S.W.3d at 234 & n.3 ("[A] claim of oppressive conduct can be independently supported by evidence of a variety of conduct.").

[29] *See* Moll, *supra* note 6, at 22–23.

[30] *See Ritchie*, 339 S.W.3d at 292; Gibney v. Culver, No. 13-06-112-CV, 2008 WL 1822767, at *18 (Tex. App.—Corpus Christi Apr. 24, 2008, pet. denied) (mem. op.); *Redmon*, 202 S.W.3d at 236.

[31] *See Redmon*, 202 S.W.3d at 235. *See also* Patton v. Nicholas, 279 S.W.2d 848, 854 (Tex. 1955). Although *Patton* was decided before the development of the shareholder oppression doctrine, the Texas Supreme Court recognized that the malicious suppression of dividends by the controlling majority was "akin to a breach of trust, for which the courts will afford a remedy." *Id.*

[32] *See Redmon*, 202 S.W.3d at 235–36; Davis v. Sheerin, 754 S.W.2d 375, 382 (Tex. App.—Houston [1st Dist.] 1988, writ denied).

[33] *See Redmon*, 202 S.W.3d at 235; Advance Marine, Inc. v. Kelley, No. 01-90-00645-CV, 1991 WL 114463, at *1–2 (Tex. App.—Houston [1st Dist.] June 27, 1991, no writ) (not designated for publication). *See also* Donahue v. Rodd Electrotype Co. of New Eng., 328 N.E.2d 505, 515 (Mass. 1975) ("Majority 'freeze-out' schemes which withhold dividends are designed to compel the minority to relinquish stock at inadequate prices. When the minority stockholder agrees to sell out at less than fair value, the majority has won." (citations omitted)).

[34] *See Advance Marine, Inc.*, 1991 WL 114463, at *1–2.

[35] *See Redmon*, 202 S.W.3d at 235.

[36] *Id.* at 239; Gonzalez v. Greyhound Lines, Inc., 181 S.W.3d 386, 392 (Tex. App.—El Paso 2005, pet. denied). *But see* Willis v. Bydalek, 997 S.W.2d 798, 802 (Tex. App.—Houston [1st Dist.] 1999, pet. denied) (holding that termination of a minority shareholder is not oppressive when the corporation was profitless both before and after the firing, there is no further evidence of majority misconduct, and the minority was an at-will employee).

disguised dividends paid to the majority through excessive compensation;[37] and restricting the minority's ability to sell his or her shares to a third party.[38]

A final but important note: under Texas law, a shareholder oppression claim is considered to be a direct, not a derivative, cause of action.[39] A derivative action belongs to the corporation,[40] and the claimant bringing the suit on the corporation's behalf must comply with stringent procedural rules.[41] For injured shareholders, the drawbacks of bringing a derivative suit make it less desirable than a direct cause of action.[42] Because a plaintiff in an oppression action must allege conduct that would also be found in a derivative action on behalf of the corporation,[43] there has been some debate over whether an oppression action must be brought derivatively.[44] However, Texas courts of appeals recognize that because oppression claims arise out of the duty that a majority shareholder owes to

[37] *See* Four Seasons Equip. v. White (*In re* White), 429 B.R. 201, 214 (Bankr. S.D. Tex. 2010); *Redmon*, 202 S.W.3d at 235.

[38] *See* Ritchie v. Rupe, 339 S.W.3d 275, 296 (Tex. App.—Dallas 2011, pet. denied) (holding that the majority's refusal to meet or allow an officer or director to meet with prospective purchasers of the minority's shares constitutes oppressive conduct).

[39] *See Redmon*, 202 S.W.3d at 235–38.

[40] *See* TEX. BUS. ORGS. CODE ANN. § 21.551(1) (West 2008); Johnson v. Jackson Walker, L.L.P., 247 S.W.3d 765, 772 (Tex. App.—Dallas 2008, pet. denied).

[41] *See* TEX. BUS. ORGS. CODE ANN. §§ 21.551–.563; *Johnson*, 247 S.W.3d at 772–73 (discussing the procedural requirements of the predecessor statute, Act of May 21, 1965, 59th Leg., R.S., ch. 332 § 1, 1965 Tex. Gen. Laws 698, 698–99 (expired Jan. 1, 2010) (former Texas Business Corporation Act, replaced by the Texas Business Organizations Code)); *See* TEX. BUS. ORGS. CODE ANN. § 402 (explaining transition from the Texas Business Corporation Act to the Texas Business Organizations Code).

[42] Eric Fryar, *Direct vs. Derivative: Significant Opinion on Shareholder Oppression as a Direct Claim*, SHAREHOLDER OPPRESSION BLOG (Feb. 19, 2011, 3:27 PM), http://blog.shareholderoppression.com/2011/02/direct-vs-derivative-significant.html. A shareholder typically cannot recover for personal damages in a derivative suit. *Id.* *But see* TEX. BUS. ORGS. CODE ANN. § 21.563(c) (stating that a court, in its discretion, may treat "a derivative proceeding brought by a shareholder of a closely held corporation . . . as a direct action brought by the shareholder for the shareholder's own benefit"). Moreover, if the corporation files bankruptcy, the shareholders lose their rights to assert the claim because derivative claims are controlled by the bankruptcy estate. *See* Fryar, *supra*.

[43] *See* Schautteet v. Chester State Bank, 707 F. Supp. 885, 889 (E.D. Tex. 1988) ("[M]ost abuses of majority control constitute breaches of the fiduciary duties the majority owes the corporation . . . .").

[44] *Id.*; *see Redmon*, 202 S.W.3d at 233–34.

the minority shareholders,[45] they are individual claims of the minority shareholder and not the corporation.[46] Accordingly, a minority shareholder may assert an oppression claim in his or her individual capacity and recover directly for injuries sustained, while bypassing the complicated statutory requirements of a derivative suit.[47]

II. THE BUYOUT REMEDY

If the court finds that one of the grounds for shareholder oppression has been met, various remedies are available to the injured shareholder.[48] The traditional remedy for oppression is court-ordered dissolution of the corporation.[49] Over time, courts have moved away from dissolution and toward the alternate remedy of the judicially ordered buyout.[50] "This movement from dissolution to buyout as a remedy for oppression . . . reflects dissatisfaction with the traditional view of dissolution or the appointment of a receiver as harsh or extreme or as corporate death."[51] Though some state legislatures have codified the buyout remedy, many courts across the country have ordered buyouts under their general equitable powers, even in the absence of express statutory or contractual authority.[52]

[45] *See Redmon*, 202 S.W.3d at 234 ("It is the nature of the wrong, whether directed against the corporation only or against the shareholder personally, not the existence of injury, which determines who may sue." (citing Faour v. Faour, 789 S.W.2d 620, 622 (Tex. App.—Texarkana 1990, writ denied))).

[46] *Id.*

[47] *See id.* However, not all courts have come to the conclusion that oppression claims are inherently direct. In *Skyport Global Communications, Inc. v. Centurytel, Inc.*, a Texas bankruptcy court had to determine whether Delaware law recognized a direct cause of action for shareholder oppression. No. 08-36737, 2011 WL 111427, at *36 (Bankr. S.D. Tex. Jan. 13, 2011). Because the Delaware courts had not previously ruled that an oppression action is inherently direct, the Texas court had to apply the Delaware test for derivative claims to each factual component of the oppression claim. *Id.* at *37.

[48] *See* 1 O'NEAL & THOMPSON, *supra* note 8, § 7:17.

[49] *Id.*; *see also* MODEL BUS. CORP. ACT § 14.30(a)(2)(ii) (2010) (stating that in a proceeding brought by a shareholder, a court may dissolve a corporation if "the directors . . . have acted . . . in a manner that is illegal, oppressive, or fraudulent").

[50] Douglas K. Moll, *Shareholder Oppression in Close Corporations: The Unanswered Question of Perspective*, 53 VAND. L. REV. 749, 792 (2000) ("The most prevalent alternative remedy is the buy-out of the oppressed investor's holdings.").

[51] 1 O'NEAL & THOMPSON, *supra* note 8, § 7:17.

[52] *See, e.g.*, Orchard v. Covelli, 590 F. Supp. 1548, 1560 (W.D. Pa. 1984) (applying Pennsylvania law); Belcher v. Birmingham Trust Nat'l Bank, 348 F. Supp. 61, 148 (N.D. Ala. 1968) (applying Alabama law); Alaska Plastics, Inc. v. Coppock, 621 P.2d 270, 274 (Alaska

When a court orders a buyout, it requires the corporation or the majority shareholders to buy back the shares of the oppressed minority shareholder at a "fair value" set by the court.[53] The buyout remedy was first recognized in Texas in *Davis v. Sheerin*.[54] The Texas Business Organizations Code does not expressly provide for a buyout remedy for oppressed shareholders.[55] Nevertheless, the *Davis* court recognized that "less harsh" alternatives, such as a buyout, could exist outside of the Texas Business Organizations Code.[56] The court held, "Texas courts, under their general equity power, may decree a 'buy-out' in an appropriate case where less harsh remedies are inadequate to protect the rights of the parties."[57] The court determined that lesser remedies would not adequately protect the oppressed shareholder's interest.[58] While damages and certain injunctions might be sufficient to remedy a breach of fiduciary duty, in this case, these remedies would not prevent the majority from denying the minority any interest or voice in the corporation.[59] The court upheld the trial court's grant of a buyout and set the foundation for the buyout remedy in Texas.[60]

1980); G&N Aircraft, Inc. v. Boehm, 743 N.E.2d 227, 244 (Ind. 2001); Sauer v. Moffitt, 363 N.W.2d 269, 275 (Iowa Ct. App. 1984); Maddox v. Norman, 669 P.2d 230, 237 (Mont. 1983); 21 West, Inc. v. Meadowgreen Trails, Inc., 913 S.W.2d 858, 867 (Mo. Ct. App. E.D. 1995); McCauley v. Tom McCauley & Son, Inc., 724 P.2d 232, 243 (N.M. Ct. App. 1986); Delaney v. Ga.-Pac. Corp., 564 P.2d 277, 288 (Or. 1977); Baker v. Commercial Body Builders, Inc., 507 P.2d 387, 393 (Or. 1973); Landstrom v. Shaver, 561 N.W.2d 1, 9 (S.D. 1997); Davis v. Sheerin, 754 S.W.2d 375, 380 (Tex. App.—Houston [1st Dist.] 1988, writ denied). *But see* Schirmer v. Bear, 672 N.E.2d 1171, 1176 (Ill. 1996) (holding that when a statutory remedy is provided, asserting alternative equitable remedies is contrary to legislative intent); Brodie v. Jordan, 857 N.E.2d 1076, 1080 (Mass. 2006) (holding that without statutory authorization, a court-ordered buyout was inappropriate).

[53] *See* Moll, *supra* note 6, at 39.

[54] 754 S.W.2d at 378.

[55] *Id.* (stating that the predecessor statute, Act of March 30, 1955, 54th Leg., R.S., ch. 64, art. 7.05, 1954 Tex. Gen. Laws 239, 290 (expired Jan. 1, 2010) (former Texas Business Corporation Act, replaced by the Texas Business Organizations Code), does not provide for a buyout remedy). Rather, the statutory remedy for oppression is the appointment of a receiver with the eventual possibility of liquidation. *See* TEX. BUS. ORGS. CODE ANN. § 11.405 (West 2008); *Davis*, 754 S.W.2d at 378.

[56] *See* 754 S.W.2d at 380.

[57] *Id.*

[58] *Id.* at 383 (applying the lesser remedy analysis from Patton v. Nicholas, 279 S.W.2d 848, 857 (Tex. 1955)).

[59] *Id.*

[60] *Id.*

The Dallas court of appeals in *Ritchie v. Rupe* recognized a limit upon the buyout remedy.[61] Legal commentators have developed two conflicting approaches to the "fair value" of the oppressed shareholder's stock: enterprise value and fair market value.[62] The enterprise approach values the company as a whole and assigns the minority shareholder a pro rata portion of that value, without discounting for lack of marketability and minority status.[63] The fair market value approach considers "'the price at which the stock would change hands between a willing seller, under no compulsion to sell, and a willing buyer, under no compulsion to buy, with both parties having reasonable knowledge of relevant facts[,]'" which would reflect discounting for lack of marketability and minority status.[64] *Ritchie* was the first Texas case to directly address which approach should be used when valuing a buyout. The court determined that the relevant case-by-case inquiry was: did the shareholder desire to leave the corporation, or was the shareholder forced to relinquish his ownership by the oppressive conduct of the majority?[65] In *Ritchie*, because the shareholder was attempting to sell her shares, her shares should be discounted according to the fair market value approach.[66]

Even after allowing for discounts, the buyout appears to be an attractive remedy because it allows an oppressed shareholder to recoup his or her investment without forcing the winding up of the company.[67] Professor Moll, a leading scholar in the area of shareholder oppression, notes that the buyout is advantageous because:

[61] 339 S.W.3d 275, 299–302 (Tex. App.—Dallas 2011, pet. denied).

[62] *See id.* at 300; Moll, *supra* note 6, at 40–41.

[63] *Ritchie*, 339 S.W.3d at 300 (citing Douglas K. Moll, *Shareholder Oppression and "Fair Value": Of Discounts, Dates, and Dastardly Deeds in the Close Corporation*, 54 DUKE L.J. 293, 313 (2004)).

[64] *Id.* (quoting Fisher v. Yates, 953 S.W.2d 370, 379 (Tex. App.—Texarkana 1997, pet. denied)). Discounting is necessary in the fair market value approach to ensure the minority shareholder does not receive "excessive relief." *See id.* at 301. The minority discount reflects the fact that because a minority shareholder lacks the ability to control the corporation, a buyer would not be willing to pay as much for the shares. Moll, *supra* note 63, at 315–16. The majority discount reflects the fact that shares in a closely held corporation lack a secondary market and are difficult to liquidate. *Id.* at 316–17.

[65] *See Ritchie*, 339 S.W.3d at 301–02.

[66] *Id.*

[67] *See* Moll, *supra* note 6, at 39–40.

> The remaining shareholders continue to operate the business and to participate in the company's successes and failures, while the departing shareholder recovers the value of his invested capital and removes himself from the company's affairs. This equitable "parting" avoids a number of practical problems that often arise when more conventional remedies (e.g., injunctions, damages) are considered.[68]

Despite these benefits, a buyout can leave the oppressed shareholder unsatisfied in practice. The reality is that a court-ordered buyout judgment could force closely held corporations to declare bankruptcy.[69] Buyout judgments, even after discounts, can easily exceed one million dollars.[70] Such an amount is not likely to be readily available to a closely held corporation, and after a judgment, it would be unlikely that the corporation would be able to obtain outside financing to pay the debt.[71] Even before a judgment is rendered, the majority can vote to place the corporation into bankruptcy, effectively cutting off an avenue of recovery for the minority to recoup its investment.[72] The remainder of this article examines the

---

[68] *Id.*

[69] *See, e.g.*, *Ritchie*, 339 S.W.3d at 298 (noting that the majority shareholders argued that the buyout was an "unduly harsh 'remedy'" that would bring the corporation "to its knees" and place it "at risk of bankruptcy"). *See also* Edward B. Rock & Michael L. Wachter, *Waiting for the Omelet to Set: Match-Specific Assets and Minority Oppression in Close Corporations*, 24 J. CORP. L. 913, 920 (1999) (stating that the availability of a buyout remedy for an oppressed shareholder increases the corporation's risk of bankruptcy).

[70] *See Ritchie*, 339 S.W.3d at 283. The trial court ordered that the majority buyout the minority's shares for $7.3 million. *Id.* Although the court remanded the issue to the trial court to discount the minority's shares for lack of marketability, even the majority's expert valued the minority's shares at $4 million. *Id.* at 298. The buyout in *Davis v. Sheerin* was $550,000 in 1988. 754 S.W.2d 375, 378 (Tex. App.—Houston [1st Dist.] 1988, writ denied). Adjusting for inflation, the *Davis* buyout award in 2012 would be worth $1,069,710.48. US INFLATION CALCULATOR, http://www.usinflationcalculator.com (last visited May 21, 2012).

[71] *See* Rock & Wachter, *supra* note 69, at 920 (stating that the availability of a buyout remedy reduces the creditworthiness of a corporation facing an oppression claim); 1 O'NEAL & THOMPSON, *supra* note 8, § 1:4, at 1-7 n.2 ("In discussing a minority shareholder suit which eventually led to the bankruptcy of the corporation, a Pennsylvania attorney noted: 'No responsible bank would extend credit to a close[] corporation embroiled in a shareholder controversy. Without credit, most such corporations simply die.'" (quoting Letter to author, June 15, 1981)).

[72] *See, e.g.*, Redmon v. Griffith, 202 S.W.3d 225, 231 (Tex. App.—Tyler 2006, pet. denied). Less than a year after the minority filed suit alleging shareholder oppression, the controlling

consequences an oppressed shareholder faces when his or her corporation is placed into bankruptcy and proposes a solution that would ensure the buyout remedy's continued viability.

III. BANKRUPTCY CONSEQUENCES FOR THE OPPRESSED SHAREHOLDER

Suppose Jim is able to obtain a judgment against Jack, Jill, and Aces Wild, and the court orders a buyout of Jim's shares. During the course of the trial, Jack and Jill have been siphoning off corporate assets via disproportionately high compensation and bonuses. By the time Jim is able to assert his buyout remedy, the corporation is but a shell of its former self. Shortly after Jim obtains the judgment, Jack and Jill, serving in their capacity as directors, vote to put the company into voluntary bankruptcy. What can Jim do to ensure that Jack, Jill, and Aces Wild follow through with their legal obligations imposed by the buyout?

A. A Very Basic Overview of Bankruptcy

Bankruptcy is a special area of federal law authorized by Article I, Section 8 of the U.S. Constitution.[73] Its purpose is to alleviate the effects of financial failure.[74] Both individuals and businesses may take advantage of the bankruptcy provisions.[75] A common misconception is that a debtor must be insolvent to be eligible to file for bankruptcy.[76] However, there is no provision of the Bankruptcy Code that contains an insolvency requirement for a debtor that voluntarily files bankruptcy.[77] "[A]

majority voted to place the corporation into bankruptcy. *Id.* Due to the imposition of the automatic stay, the minority was forced to abandon all claims against the corporation and proceed only against the majority shareholders. *Id.*

[73] U.S. CONST. art. I, § 8, cl. 4 (granting Congress the power to pass "uniform Laws on the subject of Bankruptcies throughout the United States"). The current version of bankruptcy law, found in title 11 of the United States Code, was passed in 1978 and is commonly known as the Bankruptcy Code.

[74] 1 COLLIER ON BANKRUPTCY ¶ 1.01 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2011).

[75] 11 U.S.C. § 109(a) (2006). A "person," as used in Section 109, includes both individuals and corporations. *Id.* § 101(41).

[76] Neil E. Colmenares, *Top 10 Misconceptions About Bankruptcy*, THE CPA JOURNAL (May 2005), http://www.nysscpa.org/cpajournal/2005/505/perspectives/p18.htm.

[77] Richard H. George, Note, *Bankruptcy for Nonbankruptcy Purposes: Are There Any Limits?*, 6 REV. LITIG. 95, 114 (1987). However, the Code does require that a debtor be insolvent in order

financially beleaguered debtor with real debt and real creditors should not be required to wait until the economic situation is beyond repair" in order to file a bankruptcy petition.[78]

Two main features of bankruptcy are the automatic stay[79] and the discharge.[80] The automatic stay is a temporary injunction effective the instant the bankruptcy petition is filed.[81] The scope of the automatic stay is extremely broad and stops almost all actions taken against the debtor or his property, whether formal or informal.[82] All claims or suits against the debtor are stayed as long as the property remains in the estate, until the case is dismissed, or until the debtor obtains or is denied a discharge.[83] The discharge is the most important consequence of a bankruptcy action.[84] If granted, a discharge voids any judgment or claim against the debtor that arose prior to the filing of the bankruptcy petition.[85] The discharge effectuates the principal purpose of bankruptcy, to "grant a fresh start to the honest but unfortunate debtor."[86]

The two most common bankruptcy filings are Chapter 7 liquidations and Chapter 11 reorganizations.[87] Liquidation involves the "collection, liquidation, and distribution" of the debtor's property to satisfy the claims of eligible creditors.[88] While a corporation is eligible to file for Chapter 7

to file an involuntary bankruptcy petition. *Id.* at 115. Even this requirement does not conform to the traditional "balance sheet" test for insolvency where liabilities exceed assets. *Id.* Rather, the test is whether "the debtor is generally not paying such debtor's debts as such debts become due . . . ." *See* 11 U.S.C. § 303(h)(1).

[78] *In re* Johns-Manville Corp., 36 B.R. 727, 736 (Bankr. S.D.N.Y. 1984) (confirming a Fortune 500 company's reorganization plan because it faced tens of thousands of asbestos tort claims).

[79] 11 U.S.C. § 362(a) (2006 & Supp. IV 2011).

[80] *Id.* §§ 362(a), 524, 727.

[81] *Id.* § 362(a) ("[A] petition filed under . . . this title . . . operates as a stay, applicable to all entities . . . ."). For an example of how immediately the automatic stay takes effect, *see Elbar Invs., Inc. v. Pierce* (*In re Pierce*), 91 F. App'x 927, 928–29 (5th Cir. 2004) (voiding a constable's sale that occurred 30 minutes after the bankruptcy petition was filed).

[82] *See* 11 U.S.C. § 362(a); 3 COLLIER ON BANKRUPTCY, *supra* note 74, ¶ 362.03.

[83] *See* 11 U.S.C. § 362(c); 3 COLLIER ON BANKRUPTCY, *supra* note 74, ¶ 362.06.

[84] 1 COLLIER ON BANKRUPTCY, *supra* note 74, ¶ 1.02.

[85] *See* 11 U.S.C. § 524(a)(2)–(3) (2006); 1 COLLIER ON BANKRUPTCY, *supra* note 74, ¶ 1.02.

[86] Marrama v. Citizens Bank of Mass., 549 U.S. 365, 367 (2007) (internal quotation marks omitted).

[87] *See* 1 COLLIER ON BANKRUPTCY, *supra* note 74, ¶ 1.02.

[88] *See* 6 COLLIER ON BANKRUPTCY, *supra* note 74, ¶ 700.01.

liquidation,[89] it is not eligible for a discharge under this chapter.[90] If a business does file for liquidation, it ceases to be a going concern.[91] In sharp contrast to liquidation, Chapter 11 reorganization envisions that a business will survive the bankruptcy proceeding.[92] The crux of reorganization is the reorganization plan that allows a debtor to restructure both debts and equity interests while maintaining control of business affairs.[93] If the bankruptcy court confirms the reorganization plan,[94] the debtor will be discharged of all debts incurred prior to the filing of the bankruptcy petition.[95]

To participate in distributions from the bankruptcy estate, a party must be a creditor.[96] A creditor is an "entity that has a claim against the debtor that arose at the time of or before" the bankruptcy petition was filed.[97] A claim is broadly defined to ensure that "all legal obligations of the debtor, no matter how remote or contingent, will be able to be dealt with in the bankruptcy case."[98] To determine a creditor's share in the bankruptcy estate, the creditor must file a proof of claim.[99] Once a proof of claim is

---

[89] 11 U.S.C. § 109(b).

[90] *Id.* § 727(a)(1) ("The court shall grant the debtor a discharge, unless . . . the debtor is not an individual . . . .").

[91] Arturo Bris et al., *The Costs of Bankruptcy: Chapter 7 Liquidation Versus Chapter 11 Reorganization*, 61 J. FIN. 1253, 1256 (2006).

[92] 7 COLLIER ON BANKRUPTCY, *supra* note 74, ¶ 1100.01 ("Chapter 11 embodies a policy that it is generally preferable to enable a debtor to continue to operate and to reorganize or sell its business as a going concern rather than simply to liquidate a troubled business.").

[93] *See* W. HOMER DRAKE, JR. & CHRISTOPHER S. STRICKLAND, CHAPTER 11 REORGANIZATIONS § 12:1 (2d ed. 2011) ("[T]he plan represents that vehicle by which the debtor accomplishes its rehabilitation . . . .").

[94] 11 U.S.C. § 1129(b).

[95] *Id.* § 1141(d)(1)(A); Bosiger v. U.S. Airways, Inc., 510 F.3d 442, 448 (4th Cir. 2007) ("[S]uccessful completion of the reorganization process allows a debtor, burdened with 'the weight of oppressive indebtedness,' to restructure its financial obligations, discharge its pre-existing debt, and emerge from bankruptcy with a new capital structure that better reflects financial reality." (quoting Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934))).

[96] 1 COLLIER ON BANKRUPTCY, *supra* note 74, ¶ 1.03.

[97] 11 U.S.C. § 101(10)(A).

[98] United States v. LTV Corp. (*In re* Chateaugay Corp.), 944 F.2d 997, 1003 (2d Cir. 1991) (quoting H.R. REP. NO. 95-595, at 309 (1977)); *see* 11 U.S.C. § 101(5)(A). A "claim" is defined as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured . . . ." 11 U.S.C. § 101(5)(A). The term "claim" also extends to equitable remedies that give rise to a right to payment. *Id.* § 101(5)(B).

[99] *See* 11 U.S.C. § 501; *see also* Official Bankruptcy Form 10 (2011),

filed, the claim is typically deemed "allowed"[100] unless a specific objection is made.[101] A creditor that fails to file a proof of claim generally cannot participate in the bankruptcy estate.[102]

For purposes of this discussion, it is assumed that the corporation will file for Chapter 11 reorganization to take advantage of the discharge.[103] The minority shareholder's rights differ depending on whether he or she is attempting to enforce the buyout judgment against the corporation or the majority shareholders.[104] Both situations will be considered in turn.

B. *Effect of Bankruptcy on Oppressed Shareholder's Claims Against the Corporation: The Subordination Problem*

If Aces Wild had filed for bankruptcy during the pendency of Jim's suit, the automatic stay would have prevented Jim from proceeding with his shareholder oppression cause of action.[105] Jim would have to file a proof of claim in Aces Wild's bankruptcy case that, if unobjected, would result in an allowed claim.[106] Jim would have an unliquidated, unsecured claim among the last to be paid from the bankruptcy estate.[107] If Jim receives anything

http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/BK_Forms_Current/B_010.pdf. The proof of claim identifies the debtor and creditor in addition to stating the amount of the claim as of petition date, the basis for the claim, and the value of the collateral if the claim is secured. *See* Official Bankruptcy Form 10, *supra*. Further, the creditor must submit documents that support the claim. *See id.*

[100] 11 U.S.C. § 502(a). The amount of the allowed claim determines what portion of the bankruptcy estate a creditor can receive. *See id.* However, the allowance of a claim does not ensure that the creditor will receive the full amount of its claim. *See infra* notes 106–08 and accompanying text.

[101] 11 U.S.C. § 502(a). Objections to a claim may be raised by the debtor, the bankruptcy trustee, or another creditor. *See id.* § 502(a)–(b). Typical objections include unenforceability under agreement or law, untimely filing, and claims for unmatured interest. *See id.* § 502(b).

[102] *See* 4 COLLIER ON BANKRUPTCY, *supra* note 74, ¶ 501.01[1]. Further, the discharge prevents a creditor from trying to assert pre-existing claims against the debtor after the close of the bankruptcy case. *See* 11 U.S.C. § 1141(d)(1)(A).

[103] *See supra* notes 90–95 and accompanying text.

[104] *See* Fryar, *supra* note 42.

[105] *See* 11 U.S.C. § 362(a) (2006 & Supp. IV 2011).

[106] *See id.* §§ 101(5)(B) (2006). An oppressed shareholder seeking a buyout satisfies the definition of a claim, even though its origin is equitable and not legal relief. *See id.* § 101(5)(B). Because the grant of a buyout results in a right to payment for the "fair value" of the minority's shares, it would fall under the second definition of "claim." *Id.*; *see supra* note 53 and accompanying text.

[107] *See id.* § 1129(b).

from the bankruptcy estate, it would be pennies on the dollar.[108] After the case is closed and the discharge is in place,[109] Jim would be barred from attempting to further satisfy his debt.[110] This result is inevitable unless Jim can successfully obtain relief from the automatic stay.[111]

If Jim is able to secure a buyout judgment against Aces Wild prior to its bankruptcy filing, the automatic stay prevents Jim from collecting on the judgment.[112] When Jim files a proof of claim, he will run into the subordination problem discussed below. Unless Jim is able to overcome mandatory subordination, he will likely be in a worse position than if he had not obtained the buyout judgment at all.[113]

Generally, Section 510(b) subordinates claims "arising from the purchase or sale" of the debtor's securities.[114] One of the pillars of corporate bankruptcy law is that "creditors are entitled to be paid ahead of

[108] *See, e.g.*, Yoder v. Ohio Bureau of Workers' Comp. (*In re* Suburban Motor Freight, Inc.), 998 F.2d 338, 342 (6th Cir. 1993) (noting the probability that, in Chapter 11 cases, non-priority unsecured claims will receive pennies on the dollar); *In re* U.S. Airways Grp., Inc., 303 B.R. 784, 792 (Bankr. E.D. Va. 2003) (noting that, in Chapter 11 cases, general unsecured claims may receive only pennies on the dollar).

[109] *See* 11 U.S.C. § 1141(d)(1)(A).

[110] *See id.* §§ 523(a), 524(a) (2006 & Supp. IV 2011). It should be noted that the concept of non-dischargeability does not apply to corporate debtors filing for Chapter 11 reorganization. *See id.* § 523(a) ("A discharge . . . does not discharge an *individual* debtor from [the following] debt[s] . . . ." (emphasis added)).

[111] *See id.* § 362(d). A discussion of a motion for relief from stay is beyond the scope of this article. However, if the minority shareholder is able to prove that the corporation falls into one of the four categories of Section 362(d), the bankruptcy court shall grant relief "by terminating, annulling, modifying, or conditioning such stay." *Id.*

[112] *See id.* § 362(a)(2).

[113] *See* Weissmann v. Pre-Press Graphics Co. (*In re* Pre-Press Graphics Co.), 307 B.R. 65, 71 (N.D. Ill. 2004) (commenting that the determination that an oppressed shareholder's claim is subject to mandatory subordination "will have a significant impact on his potential distribution in Debtor's bankruptcy proceedings").

[114] 11 U.S.C. § 510(b) (2006). Section 510(b) provides in full text:

> For the purpose of distribution under this title, a claim arising from rescission of a purchase or sale of a security of the debtor or of an affiliate of the debtor, for damages arising from the purchase or sale of such a security, or for reimbursement or contribution allowed under section 502 on account of such a claim, shall be subordinated to all claims or interests that are senior to or equal the claim or interest represented by such security, except that if such security is common stock, such claim has the same priority as common stock.

Id.

shareholders in the distribution of corporate assets."[115] Section 510(b) was enacted to prevent disappointed shareholders from bootstrapping their position to share on parity with unsecured creditors by claiming corporate illegality in the issuance of securities.[116] The effect is to shift the risk of loss from creditors to the shareholders who willingly chose to invest in the successes and failures of the debtor corporation.[117]

The scope of Section 510(b) has been debated since its enactment in 1978.[118] Some courts have narrowly construed the statutory language to only require subordination if the illegality occurred during the issuance of the securities and not to post-issuance misconduct.[119] However, the Second,[120] Third,[121] Fifth,[122] Ninth,[123] and Tenth[124] Circuits have used a

[115] Racusin v. Am. Wagering, Inc. (*In re* Am. Wagering, Inc.), 493 F.3d 1067, 1071 (9th Cir. 2007). Under Chapter 11's absolute priority rule, equity holders may not receive any distributions from the bankruptcy plan until the debts of unsecured creditors have been satisfied. *See* 11 U.S.C. § 1129(b)(2)(B); H.R. REP. NO. 95-595, at 413–18 (1977) ("[Section 1129] codifies the absolute priority rule from the dissenting class on down.").

[116] *See* Hollace Topol Cohen, *Mandatory Subordination Has Its Limits*, *in* NORTON ANNUAL SURVEY OF BANKRUPTCY LAW 1, 1 (William L. Norton, Jr. ed., 2007).

[117] *See* John J. Slain & Homer Kripke, *The Interface Between Securities Regulation and Bankruptcy—Allocating the Risk of Illegal Securities Issuance Between Securityholders and the Issuer's Creditors*, 48 N.Y.U. L. REV. 261, 288 (1973) ("It is difficult to conceive of any reason for shifting even a small portion of the risk of illegality from the stockholder, since it is to the stockholder, and not to the creditor, that the stock is offered."). This seminal article by Professors Slain and Kripke is considered to be the inspiration for Section 510(b). *See* Baroda Hill Invs., Ltd. v. Telegroup, Inc. (*In re* Telegroup, Inc.), 281 F.3d 133, 139 (3d Cir. 2002) ("In enacting § 510(b), Congress relied heavily on a law review article written by Professors John J. Slain and Homer Kripke . . . ."); *see also* Cohen, *supra* note 116, at 2–3.

[118] Cohen, *supra* note 116, at 1.

[119] *See, e.g.*, Montgomery Ward Holding Corp. v. Schoeberl (*In re* Montgomery Ward Holding Corp.), 272 B.R. 836, 844 (Bankr. D. Del. 2001) (holding that a claim only "arises from the purchase or sale of a security" if there is an allegation of fraud in the purchase, sale, or issuance of the security); *In re* Angeles Corp., 177 B.R. 920, 926–27 (Bankr. C.D. Cal. 1995) (holding that the scope of Section 510(b) is limited to fraudulent inducement claims), *aff'd*, 199 B.R. 220 (B.A.P. 9th Cir. 1996).

[120] Rombro v. Dufrayne (*In re* Med Diversified, Inc.), 461 F.3d 251, 255–56 (2d Cir. 2006).

[121] *Telegroup*, 281 F.3d at 141–42; *see also In re* Int'l Wireless Commc'ns Holdings, Inc., 68 F. App'x 275, 278 (3d Cir. 2003).

[122] SeaQuest Diving, LP v. S&J Diving, Inc. (*In re* SeaQuest Diving, LP), 579 F.3d 411, 421 (5th Cir. 2009), *implicit adoption recognized by* Official Comm. of Unsecured Creditors v. FLI Deep Marine LLC (*In re* Deep Marine Holdings, Inc.), 65 Collier Bankr. Cas. 2d (MB) 406, 412–13 (Bankr. S.D. Tex. Jan. 19, 2011).

[123] Racusin v. Am. Wagering, Inc. (*In re* Am. Wagering, Inc.), 493 F.3d 1067, 1072 (9th Cir.

perceived "ambiguity" in the language of Section 510(b) to broadly apply subordination to post-issuance illegality.[125] Under this broad approach, mandatory subordination has been applied to claims beyond the traditional scope of securities fraud, including damages arising from breach of contract, mismanagement, and breach of fiduciary duty.[126] Such a claim is subject to mandatory subordination if there is "some nexus or causal relationship between the claim and the sale [or purchase] of the security."[127]

An issue that has arisen upon the application of this test is when must a court recognize that a claim is really a debt and not a wrongful assertion of an equity interest?[128] A shareholder oppression buyout judgment squarely implicates this concern.[129] In *In re Pre-Press Graphics Co.*, a minority shareholder brought a successful shareholder oppression action against the corporation in state court.[130] As a remedy, the court ordered the corporation to buy out the minority's shares at "fair value," which the court determined was $1,383,350.[131] Rather than appeal the judgment, the corporation filed a

2007); Am. Broad. Sys., Inc. v. Nugent (*In re* Betacom of Phx., Inc.), 240 F.3d 823, 829 (9th Cir. 2001).

[124] Allen v. Geneva Steel Co. (*In re* Geneva Steel Co.), 281 F.3d 1173, 1178, 1182–83 (10th Cir. 2002).

[125] *See Deep Marine Holdings, Inc.*, 65 Collier Bankr. Cas. 2d (MB) at 412–13. The phrase that has caused the most ambiguity is "'damages *arising from* the purchase or sale of such a security.'" *See* Cohen, *supra* note 116, at 1, 4 (emphasis added) (quoting 11 U.S.C. § 510(b) (2006)). Courts have construed this language to mean either the issuance of a security or damages that would not have arisen but for the issuance of a security. *See supra* notes 119–24 and accompanying text.

[126] *See* Cohen, *supra* note 116, at 4. In *Telegroup*, the Third Circuit articulated its rationale for this broad approach as follows: "[B]ecause claimants retained the right to participate in corporate profits if [the corporation] succeeded, we believe that § 510(b) prevents them from using their breach of contract claim to recover the value of their equity investment in parity with general unsecured creditors." 281 F.3d at 142.

[127] *Telegroup*, 281 F.3d at 138.

[128] Cohen, *supra* note 116, at 5.

[129] *See* Weissmann v. Pre-Press Graphics Co. (*In re* Pre-Press Graphics Co.), 307 B.R. 65, 71 (N.D. Ill. 2004).

[130] *Id.* at 69. The court found that the following actions of the majority constituted oppressive conduct: (1) demanding that the minority shareholder resign as director; (2) conducting secret capital transactions that resulted in the reduction of the minority shareholder's ownership interest from 38% to 6%; and (3) purchasing stock to increase the majority's ownership at a price of $106.14 per share despite receiving offers ranging from $2,000 to $9,000 per share. *Id.* at 69, 79.

[131] *Id.* at 69. The judgment was reduced by $25,000 that the minority had received as a partial down payment on a repurchase agreement, and subject to a further reduction of $75,000 if the corporation cured the breached agreement. *Id.*

voluntary Chapter 11 bankruptcy petition.[132] The minority shareholder filed a proof of claim approximately in the amount of the buyout judgment.[133] The corporation and its largest creditor objected to the claim and argued that because it arose from the sale of securities, it must be subordinated under Section 510(b).[134] The bankruptcy court agreed and ordered that the shareholder's claim be subordinated to the claims of the unsecured creditors.[135]

On appeal, the district court had to determine whether a buyout judgment arises from the purchase or sale of the debtor's securities.[136] The court first analyzed the nature of the minority shareholder's claim and held that it can look behind the judgment to the shareholder oppression claims on which the claim was based.[137] The court then considered whether the language of Section 510(b) allowed for subordination of claims that arose from post-investment conduct by the corporate debtor.[138] Following the logic of the Third[139] and Tenth[140] Circuits, the court adopted the broad approach and concluded that "some causal link must exist between the purchase or sale and the claim at issue, but . . . the causal link need not arise contemporaneously with the purchase or sale of a security."[141]

Finally, the *Pre-Press Graphics* court considered whether a claim for shareholder oppression satisfied the test set out above, thus resulting in

---

[132] *Id.* at 70.

[133] *Id.*

[134] *Id.*

[135] *Id.*

[136] *Id.* at 71.

[137] *Id.* at 71–73. The corporation argued that the claim is the state court order forcing the repurchase of the minority's shares. *Id.* at 71. Such a construction would squarely fall within the "purchase or sale of a security" language of Section 510(b). *See id.* The court rejected this approach based on the broad definition of "claim" and a pair of Supreme Court decisions instructing courts to look beyond the terms of an order or settlement agreement and examine the substantive claims when determining whether a debt is non-dischargeable. *See id.* at 71–73; *see* 11 U.S.C § 101(5)(A) (2006) (defining "claim"); Brown v. Felsen, 442 U.S. 127, 138–39 (1979) (instructing courts to look beyond the terms of a settlement agreement to classify whether a debt is non-dischargeable); Archer v. Warner, 538 U.S. 314, 322–23 (2003) (instructing the same).

[138] *Pre-Press Graphics*, 307 B.R. at 73.

[139] Baroda Hill Invs., Ltd. v. Telegroup, Inc. (*In re* Telegroup, Inc.), 281 F.3d 133, 141–42 (3d Cir. 2002).

[140] Allen v. Geneva Steel Co. (*In re* Geneva Steel Co.), 281 F.3d 1173, 1178–79, 1182 (10th Cir. 2002).

[141] *Pre-Press Graphics*, 307 B.R. at 78 (citing *Telegroup*, 281 F.3d at 144 n.2).

mandatory subordination.[142] The court afforded great weight to Professors Slain and Kripke's concerns of unhappy shareholders "bootstrapping" claims to enjoy the status of unsecured creditor.[143] The court concluded that the claimant must be viewed as a disaffected shareholder seeking to recoup his investment ahead of unsecured creditors.[144] Accordingly, the shareholder's buyout judgment was inextricably intertwined with his status as shareholder, satisfying the "causal link" to a purchase or sale of a security required to trigger mandatory subordination.[145] The fact that the shareholder's claims were reduced to a money judgment prior to the filing of the bankruptcy petition[146] did not persuade the court that the shareholder's equity position had transformed into that of a creditor.[147]

Arguably, the result in *Pre-Press Graphics* was wrong. First, the decision ignores the entire purpose of the oppression doctrine.[148] The court repeatedly characterized the oppressed shareholder's harm as a decrease in value to his shares.[149] Although loss of share value can figure into the minority shareholder's harm, the true harm that oppression seeks to remedy is a defeat of the minority shareholder's expectations.[150] The court's focus on the minority's loss in value of shares ignores the difference between an investor in a publicly held corporation and an investor in a closely held corporation.[151] An investor in a publicly held corporation invests with the

[142] *Id.* The court noted that in deciding this case it was "writing on a completely blank slate." *Id.* "No court has yet addressed whether a [shareholder oppression claim] falls within the scope of § 510(b)." *Id.*

[143] *Id.* at 79. *See* Slain & Kripke, *supra* note 117, at 261.

[144] *Pre-Press Graphics*, 307 B.R. at 79.

[145] *Id.* at 80; *see* Cohen, *supra* note 116, at 8–9.

[146] *Pre-Press Graphics*, 307 B.R. at 69–70.

[147] *See id.* at 80; *see* Cohen, *supra* note 116, at 9.

[148] *See* Ritchie v. Rupe, 339 S.W.3d 275, 289 (Tex. App.—Dallas 2011, pet. denied); Moll, *supra* note 6, at 26. *See also supra* Part I for a discussion of the oppression doctrine.

[149] *See Pre-Press Graphics*, 307 B.R. at 79 ("[Claimant] must be viewed as a disaffected shareholder who brought suit because the value of his stock was diluted . . . ."); *id.* ("Those shares simply became less valuable due to Pre-Press' misconduct."); *id.* at 80 ("Here, Pre-Press' misconduct resulted in [the minority shareholder] receiving a smaller percentage of profits from his 500 shares, and those shares became worth less money.").

[150] *See Ritchie*, 339 S.W.3d at 289; Moll, *supra* note 6, at 26–27. The broad definition of "oppression" was meant to encompass the complex and varied harms suffered by a minority shareholder. *See Ritchie*, 339 S.W.3d at 289.

[151] *See* Moll, *supra* note 63, at 338 ("The components of a close corporation shareholder's investment, however, differ significantly from the components of a public corporation shareholder's investment.").

expectation that he or she will receive a proportionate share of the company's value.[152] On the other hand, an investor in a closely held corporation does not expect his or her investment to be limited to a mere financial sum.[153] Rather, a shareholder in a closely held corporation often expects that his or her investment entitles him or her to employment and a role in the management of the corporation.[154] Because the doctrine of shareholder oppression seeks to protect more than the minority shareholder's mere financial interest in the corporation, it should not be unilaterally viewed as a claim "arising from the purchase or sale of securities."[155]

More egregiously, the court mischaracterized the minority shareholder's relationship with the corporation once the buyout was ordered. In support of its conclusion that the minority shareholder was "bootstrapping" his claim, the court remarked that at all times, the minority shareholder "continued to enjoy the benefit of sharing in the company's success—and bore the risk of the company's failure."[156] The court missed the point that once the buyout was ordered there was an "equitable parting," and the minority shareholder relinquished all rights to participate in corporate affairs and distributions.[157] Thus, the shareholder ceased to be a shareholder and took on the role of creditor.[158] When a claimant exchanged his or her equity interest for a debt interest, the "nexus or causal connection

[152] *See id.* In layman's terms, the publicly held investor invests money to make money. *See id.* at 338–39.

[153] *See id.* at 339.

[154] *See id. See also* Wilkes v. Springside Nursing Home, Inc., 353 N.E.2d 657, 662 (Mass. 1976) ("The minority stockholder typically depends on his salary as the principal return on his investment . . . ."); Ingle v. Glamore Motor Sales, Inc., 535 N.E.2d 1311, 1319 (N.Y. 1989) (Hancock, J., dissenting) ("A person who . . . buys a minority interest in a close corporation does so not only in the hope of enjoying an increase in value of his stake in the business but for the assurance of employment in the business in a managerial position.").

[155] 11 U.S.C. § 510(b) (2006); *see supra* notes 25–26 and accompanying text. The *Pre-Press Graphics* court attempted to address this concern:

> Nothing in the legislative history of § 510(b) or the case law suggests that the rationale for subordinating shareholder claims—i.e., that shareholders bear a greater risk of insolvency because they enjoy the benefit of sharing in the profits—does not apply where shareholders own a relatively small number or percentage of shares.

Weissmann v. Pre-Press Graphics Co. (*In re* Pre-Press Graphics), 307 B.R. 65, 79 (N.D. Ill. 2004).

[156] *Pre-Press Graphics*, 307 B.R. at 80.

[157] *See* Moll, *supra* note 6, at 39–40.

[158] *See infra* note 173.

required to employ [S]ection 510(b) cease[d] to exist."[159] This mischaracterization struck a fatal blow to the oppressed shareholder's expectation of recovery; even the court recognized that subordination means the minority shareholder "likely will never recover under the state court judgment."[160]

C. A Proposed Solution: Applying the Limits of American Wagering to Shareholder Oppression Buyouts

Without limitations, the broad approach to Section 510(b) could extend subordination to situations where Congress never intended it to apply.[161] However, a return to the strict construction of Section 510(b)[162] would overrule a significant amount of case law where the application of the broad approach came to the appropriate conclusion.[163] The Ninth Circuit was able to split the difference between these concerns in *In re American Wagering, Inc.*[164] In its opinion, the court set forth a limit on the application of Section 510(b) to prepetition money judgments without disavowing the broad approach.[165] This limitation allows for the continued viability of the buyout remedy after the debtor corporation has filed bankruptcy.

The *American Wagering* court pointed out that in cases where "arising from" was construed to include claims other than fraud, there was a concern that such claims tried to re-characterize what would otherwise be subordinated securities claims.[166] In an earlier decision, the court identified

[159] Burtch v. Gannon (*In re* Cybersight LLC), No. 02-11033, Civ.A.04-112 JJF., 2004 WL 2713098, at *3 (D. Del. Nov. 17, 2004) (quoting Official Comm. of Unsecured Creditors v. Am. Capital Fin. Servs., Inc. (*In re* Mobile Tool Int'l, Inc.), 306 B.R. 778, 781 (Bankr. D. Del. 2004)) (internal quotation marks omitted).

[160] *See Pre-Press Graphics*, 307 B.R. at 80.

[161] *See, e.g.*, Am. Wagering, Inc. v. Racusin (*In re* Am. Wagering, Inc.), 326 B.R. 449, 450, 458 (B.A.P. 9th Cir. 2005), *rev'd*, 493 F.3d 1067 (9th Cir. 2007) (applying mandatory subordination to a claim when the claimant never actually owned stock in the debtor corporation); *see also* Cohen, *supra* note 116, at 10 ("The BAP's decision in *American Wagering* illustrates how the reliance on cases that adopt the broad approach to the application of section 510(b) may allow a court to subordinate a claim that was not grounded in fraud, illegality, or misconduct in the issuance (or retention) of a security . . . .").

[162] *See* Cohen, *supra* note 116, at 1, 4; *see also supra* note 119 and accompanying text.

[163] *See supra* notes 120–24 and accompanying text.

[164] Racusin v. Am. Wagering, Inc. (*In re* Am. Wagering, Inc.), 493 F.3d 1067, 1072–73 (9th Cir. 2007).

[165] *See id.*; Cohen, *supra* note 116, at 10.

[166] *Am. Wagering*, 493 F.3d at 1072.

two reasons to subordinate these claims: (1) different expectations of risk and return for shareholders and creditors and (2) reliance of creditors on the equity cushion created by shareholder investment.[167] "Neither rationale applies" to a claimant whose right to share in profits ceased to exist by means of a prepetition money judgment.[168] The fact that the judgment was obtained before the onset of the bankruptcy filing rebuts an allegation that the claimant was trying to convert an equity interest into an unsecured claim only after the corporation's stock started to decline in value.[169] The money judgment "established a fixed, pre-petition debt due and owing [claimant] as a creditor, not the risk/return position of an equity investor in the now-bankrupt corporation."[170] Accordingly, the claim in *American Wagering* was not subject to subordination under Section 510(b).[171]

Whether the claimant once owned stock in the debtor corporation should not contribute to the decision of whether a claim should be treated as debt or subordinated as an equity interest.[172] The causal connection required to trigger Section 510(b) subordination is eliminated when a prepetition judgment transforms the claimant's equity interest into a debt interest.[173] The claim no longer arises from the purchase or sale of the

[167] *Id.* (looking to Am. Broad. Sys., Inc. v. Nugent (*In re* Betacom of Phx., Inc.), 240 F.3d 823, 829 (9th Cir. 2001)).

[168] *See id.*; Cohen, *supra* note 116, at 11. The claimant in *American Wagering* was a corporate agent that did not receive the stock compensation promised in an employment agreement. 493 F.3d at 1069. The agent sued for breach of contract and obtained an order requiring the corporation to pay the value of the promised stock. *Id.* at 1070. The corporation filed bankruptcy and argued that the agent's claim should be subordinated because it related to the purchase or sale of the debtor's security. *Id.* The court reversed the bankruptcy court's order to subordinate the claim based on the debt/equity distinction. *Id.* at 1073.

[169] *Cf. Betacom of Phx.*, 240 F.3d at 826, 832. In *Betacom of Phoenix*, a lawsuit was filed three years before the bankruptcy petition, but the suit had not concluded and no judgment had yet issued at the time of the bankruptcy filing. *Id.* at 826. The Ninth Circuit ordered that the claim be subordinated under Section 510(b). *Id.* at 832.

[170] *Am. Wagering*, 493 F.3d at 1073.

[171] *Id.* at 1069, 1073.

[172] *See* Cohen, *supra* note 116, at 13.

[173] *See, e.g.*, Official Comm. of Unsecured Creditors v. Am. Capital Fin. Servs., Inc. (*In re* Mobile Tool Int'l, Inc.), 306 B.R. 778, 782 (Bankr. D. Del. 2004) (noting that the surrender of the equity interest as evidenced by the receipt of a debt instrument is crucial to establishing that the rights to share in profits are eliminated and hence the purposes of Section 510(b) are not violated). Several courts have recognized that an equity interest may become a debt obligation that cannot be subordinated under Section 510(b). *See* Burtch v. Gannon (*In re* Cybersight LLC), No. 02-11033, Civ.A.04-112 JJF., 2004 WL 2713098, at *3–4 (D. Del. Nov. 17, 2004); Raven Media Invs. LLC

debtor's security; rather, the right to payment arises from the debt obligation created by the money judgment.[174] This is the exact issue that the court in *Pre-Press Graphics* failed to see when it applied Section 510(b) to a buyout based on shareholder oppression.[175]

Bankruptcy courts considering whether to subordinate a buyout judgment based on shareholder oppression should follow the logic of *American Wagering* and not *Pre-Press Graphics*. The legislative history of Section 510(b) supports the view that a prepetition judgment would not be subject to mandatory subordination even if it arose from securities fraud claims.[176] During congressional hearings considering the passage of Section 510(b), the Securities and Exchange Commission expressed its opposition to mandatory subordination of securities claims because "[m]andatory subordination would result in different treatment to security holders whose fraud claims were reduced to judgment before bankruptcy, and those security holders whose claim had not reached that point."[177] Though Congress ultimately rejected these concerns, the quoted language indicates congressional acceptance that a claim reduced to prepetition judgment, even when predicated on illegal shareholder action, should not be subject to mandatory subordination.[178] This conclusion supports the application of the *American Wagering* limitation to the buyout judgment.[179]

---

v. DirecTV Latin Am., LLC (*In re* DirecTV Latin Am., LLC), 42 Bankr. Ct. Dec. (LRP) No. 169, at 737 (D. Del. Feb. 4, 2004); *In re* Wyeth Co., 134 B.R. 920, 922 (Bankr. W.D. Mo. 1991). In *Cybersight*, a member's dispute over a contractual buyout resulted in an arbitration award that was entered as judgment prepetition. 2004 WL 2713089, at *1. The court refused to subordinate the claim, noting that once the state court entered judgment, the judgment became a fixed debt obligation of the LLC and the former shareholder was entitled to general unsecured creditor status. *Id.* at *3. "[S]ubordinating [the member's] claim would not further the legislative prerogatives of Section 510(b)." *Id.* Expanding on the *Mobile Tool* decision, the court also held that the issuance of a debt instrument is not required to break the causal connection. *Id.* at *4. A judgment entered by a court requiring the buyout of the membership interest had the same effect of eliminating the benefits and risks associated with equity ownership and acquiring a position as creditor. *See id.*

[174] *See supra* note 173.

[175] *See supra* notes 156–60 and accompanying text.

[176] *See* H.R. REP. NO. 95-595, at 196 (1977).

[177] *Id.* The SEC believed that subordination should be considered on a case-by-case basis. *Id.* "[A] security holder who has been defrauded should be treated the same as any other tort victim . . . ." *Id.*

[178] Cohen, *supra* note 116, at 24.

[179] *See id.* "Since section 510(b) has been applied to other claims for illegality and misconduct asserted by holders of securities, by analogy, a prepetition judgment with respect to damages arising from such illegality or misconduct would not be subject to mandatory

In order for it to continue to be a viable remedy for shareholder oppression, bankruptcy courts must recognize that a prepetition judgment ordering a buyout of the minority's shares creates a debt interest and does not arise out of the purchase or sale of the debtor's securities.[180]

D. Effect of Bankruptcy on Oppressed Shareholder's Claims Against the Majority Shareholders

Suppose that after considering the headache of mandatory subordination, Jim decides to drop Aces Wild as a party to the lawsuit and proceed solely against Jack and Jill. Since shareholder oppression is considered to be a direct claim in Texas,[181] Jim does not have to relinquish his claims to the bankruptcy trustee.[182] Does the pendency of Aces Wild's bankruptcy case affect Jim's ability to sue for and enforce a buyout for shareholder oppression against the majority shareholders?

Though a minority shareholder may initially sue both the corporation and the majority shareholder for oppression,[183] it is unlikely that the court will order that the corporation and majority are jointly and severally liable for the buyout. Rather, as the litigation progresses, the minority will elect against which party to seek the buyout.[184] The bankruptcy implications

subordination." *Id.* The oppressive conduct and the resulting buyout judgment are an appropriate application of this principle. *See* Moll, *supra* note 6, at 39.

[180] *See supra* note 173 and accompanying text.

[181] *See supra* notes 39–47 and accompanying text.

[182] *See* Fryar, *supra* note 42. Upon bankruptcy, any derivative claims now belong to the bankruptcy trustee. *See id.*

[183] *See, e.g.*, Mueller v. Cedar Shore Resort, Inc., 643 N.W.2d 56, 59, 63 (S.D. 2002) (exemplifying situation where petitioner brings an oppression claim against both the majority shareholders and the corporation). *See also* Moll, *supra* note 6, at 39 ("[A] buyout typically involves a court ordering *the corporation or the majority shareholder* to purchase the shares of an aggrieved minority investor . . . ." (emphasis added)).

[184] *See* BP Am. Prod. Co. v. Marshall, 288 S.W.3d 430, 456 (Tex. App.—San Antonio 2008), *rev'd on other grounds*, 342 S.W.3d 59 (Tex. 2011) (holding that the one-satisfaction rule "applies when multiple defendants commit the same act or when multiple defendants commit different acts that result in a single injury"). *See also* Tony Gullo Motors I, L.P. v. Chapa, 212 S.W.3d 299, 303, 314 (Tex. 2006). The Texas Supreme Court in *Tony Gullo Motors* enumerated the one-satisfaction rule: "There can be but one recovery for one injury, and the fact that . . . there may be more than one theory of liability[] does not modify this rule." *Id.* at 303 (quoting Stewart Title Guar. Co. v. Sterling, 822 S.W.2d 1, 8 (Tex. 1991)) (internal quotation marks omitted). The court explained that "[w]hile [the plaintiff] could certainly plead more than one theory of liability, she could not recover on more than one." *Id.* Ultimately, the court held that the plaintiff was "entitled to recover on the most favorable theory the verdict would support" but that she was "not required

make pursuing the corporation the less desirable choice if the corporation is in financial jeopardy.[185] On the other hand, the majority shareholder is often flush with cash he or she has siphoned off as disguised dividends.[186]

If the minority is able to secure a buyout judgment against the majority shareholders, then a subsequent corporate bankruptcy does not stand in the way of the minority enforcing the judgment against the majority.[187] If the corporation does file bankruptcy during the pendency of the oppression lawsuit, it has no effect on the minority's claims against the majority shareholder.[188] Because the majority shareholder owes a duty to act with fairness toward the minority,[189] the majority's liability runs to the minority and not the corporation.[190] Accordingly, the wrongs complained of in the oppression suit are not swept up in the bankruptcy proceeding and are not subject to the automatic stay.[191]

However, if the minority is pursuing a buyout judgment against the corporation and then attempts to enforce the judgment against the majority shareholder, bankruptcy does come into play.[192] In *Weil v. Express Container Corporation*, the minority shareholder sued the corporation and majority shareholder for shareholder oppression.[193] The corporation filed for Chapter 11 reorganization during the pendency of the suit.[194] After the

to make that election until she [knew] her choices." *Id.* at 314.

[185] *See supra* Part III.B.

[186] *See, e.g.*, Four Seasons Equip., Inc. v. White (*In re* White), 429 B.R. 201, 210 (Bankr. S.D. Tex. 2010).

[187] *See* Fryar, *supra* note 42.

[188] *See id.*

[189] *See supra* notes 19–22 and accompanying text.

[190] *See* Fryar, *supra* note 42 (noting that a shareholder oppression claim is not a derivative claim but is "entirely a direct and individual claim based on the breach of duties owed directly to the shareholder").

[191] *See id. See also supra* notes 81–83 and accompanying text for a discussion on the consequences of the automatic stay.

[192] *See* Weil v. Express Container Corp., 824 A.2d 174, 180–81 (N.J. Super. Ct. App. Div. 2003).

[193] *Id.* at 178. New Jersey has a statutory remedy for shareholder oppression. *See* N.J. STAT. ANN. § 14A:12–7 (West 2003) (allowing an oppressed shareholder to pursue both involuntary dissolution and forced buyout proceedings). However, the court in *Weil* states that a court may impose other equitable remedies and that its analysis of the immediate issue is consistent with those remedies. *See Weil*, 824 A.2d at 181.

[194] *Weil*, 824 A.2d at 179. As part of the reorganization plan, the assets of the corporation were sold to a third party. *Id.* After the sale, the corporation dissolved. *See id.* at 181.

reorganization plan was confirmed, the minority shareholder attempted to proceed with her remaining claims against the majority shareholder in state court.[195] However, the court refused to impose personal liability upon the majority shareholder after the corporation's bankruptcy was final.[196]

The *Weil* court based its conclusion on the fact that each of the potential remedies for shareholder oppression "contemplates the existence of an on-going or successor corporation."[197] The court recognized that in all cases where a court assessed a buyout judgment against a majority shareholder, the remedy was always imposed while the corporation or its successor continued to exist.[198] "No precedent cited suggests that, following a dissolution of the corporation in bankruptcy, any remedy can appropriately be asserted against a former majority shareholder personally."[199] Unwilling to expand the buyout remedy to this new context, the court prevented the minority shareholder from proceeding against the majority.[200]

The *Weil* case highlights some lingering concerns about pursuing a shareholder oppression action against a majority shareholder. If the corporation encounters financial trouble that results in Chapter 7 dissolution or Chapter 11 reorganization followed by a subsequent acquisition of corporate assets, the minority shareholder could be barred from asserting her oppression claims against the majority.[201] If such a situation were to arise, the minority shareholder might have better luck with establishing his or her right as a creditor in the bankruptcy estate.[202]

IV. CONCLUSION

Shareholder oppression, though recognized in many jurisdictions, is still a developing area of law with many unanswered questions. One of those questions is treatment of its buyout remedy after the corporation has filed bankruptcy. Given the likelihood of financial failure in such a situation, it

---

[195] *Id.* at 180. The bankruptcy court determined that some of the minority's claims were actually derivative in nature and thus belonged to the trustee. *Id.* at 179–80. Those that were not considered derivative were remanded to state court. *Id.* at 180.

[196] *Id.* at 181.

[197] *Id.*

[198] *Id.*

[199] *Id.*

[200] *Id.*

[201] *See id.* at 181.

[202] *See id.*

is an important issue that practitioners should consider when determining how to proceed with an oppression cause of action.

Moreover, courts considering the treatment of a buyout judgment rendered against a now bankrupt corporation should remember the policy behind the creation of the oppression doctrine and its departure from majority rule. If a buyout judgment is subordinated under Section 510(b), it essentially renders the minority's remedy meaningless. Courts should apply the limitation the Ninth Circuit recognized in *American Wagering*, where equity interests converted to debt interests prepetition are not subject to mandatory subordination. Otherwise, minority shareholders like Jim would be left wondering whether a court-ordered buyout is a remedy at all.