Whose Harm Is It Anyway?—The Feasibility of Direct Claims By Minority Shareholders Following Cash-Out Mergers in Texas Corporations

JP Haskins*

I. INTRODUCTION

Conflicts between the owners of closely-held corporations are commonplace.¹ A closely-held corporation is usually marked by characteristics such as relatively few shareholders, substantial participation by shareholders in the management of the corporation, and limited or no market for the corporation’s stock. Despite appearing more analogous to a partnership than a traditional public corporation, a closely-held corporation often retains traditional corporate characteristics, including centralized management, whereby power may easily become concentrated in the hands of a majority shareholder or group. As a result, the majority has the ability to utilize various business combination methods—including cash-out mergers—in a way that allows the majority to retain an interest in the surviving corporation or entity while forcing minority shareholders to relinquish their equity in exchange for cash, debt securities, or other non-equity consideration.

To illustrate, consider a simple hypothetical. Shareholder A, Shareholder B, and Shareholder C are equal owners of a privately-held Texas corporation (Company X). Shareholders A and B receive a very generous offer from a third-party interested in acquiring Company X. Without telling Shareholder C about the offer, Shareholders A and B offer to buy Shareholder C’s stock. After Shareholder C refuses to sell,

---

¹A closely-held corporation is generally viewed as a corporation owned by a small number of shareholders. In Texas, closely-held corporations are statutorily defined (for derivative suit purposes) as those having fewer than thirty-five shareholders and “no shares listed on a national securities exchange or regularly quoted in an over-the-counter market by one or more members of a national securities association.” TEX. BUS. ORGS. CODE ANN. § 21.563(a) (West 2012).
Shareholders A and B form a new Texas corporation (NewCo) and contribute all of their Company X shares to NewCo so that NewCo becomes the majority owner of Company X. NewCo then causes Company X to merge with and into NewCo, with NewCo surviving the merger. Under the plan of merger, Shareholder C will be given some cash and a long-term note in exchange for his shares of Company X. Shareholders A and B then receive all the benefits from the subsequent third-party acquisition of NewCo. Shareholder C then has a decision: accept the cash and note, or contest the offer and seek a judicial appraisal.2

As it stands, Texas law provides minority shareholders with very limited meaningful recourse following a cash-out merger based on unfair dealing and/or unfair consideration. Chiefly, minority shareholders are often stuck in a situation where they (1) are limited to statutory appraisal rights, (2) lack an actionable fiduciary duty to bring a direct suit, (3) are unable to successfully assert a derivative suit because the transaction in question deprived them of standing, or (4) maintain the standing necessary to bring a derivative suit, but are unable to demonstrate that the conduct in question harmed the corporation.3 In contrast, other jurisdictions, including Delaware, have provided minority shareholders with a direct cause of action to challenge an unfair merger process.4 At least one Texas court applying Delaware law has held that shareholders can bring an action directly against the controlling persons of a corporation to challenge the validity of the merger itself.5

---

2 The same result, i.e., the elimination of a minority owner’s interest, may be accomplished using various merger and business combination mechanisms. See 20A ELIZABETH S. MILLER & ROBERT A. RAGAZZO, TEXAS PRACTICE SERIES: BUSINESS ORGANIZATIONS § 40:9 (3d ed. 2015) (providing examples).


4 See, e.g., Parnes v. Bally Entm’t Corp., 722 A.2d 1243, 1244–45 (Del. 1999); see also 2 O‘NEAL & THOMPSON, O’NEAL AND THOMPSON’S CLOSE CORPORATIONS AND LLCS: LAW AND PRACTICE § 9:26 (Rev. 3d ed. 2015) (“Fiduciary duties increasingly can be enforced as direct suits brought by individual shareholders, particularly in closely held [entities].”). Such suits are also increasingly being held as viable through the use of class action proceedings. See generally Robert B. Thompson & Randall S. Thomas, The New Look of Shareholder Litigation: Acquisition-Oriented Class Actions, 57 VAND. L. REV. 133 (2004).

5 See Elloway v. Pate, 238 S.W.3d 882, 900 (Tex. App.—Houston [14th Dist.] 2007, no pet.).
Nonetheless, recent Texas cases have recognized related claims and additional circumstances where a fiduciary relationship might arise, suggesting that Texas courts are cognizant that current remedial options can leave real and potentially grave abuses of power unredressed.\(^6\) Additionally, the Texas Supreme Court has suggested in dicta that when competing bids exist, the decision to accept a lower price does not harm the corporation, but the shareholders, implying that a claim based on inadequate price belongs to the shareholders directly.\(^7\) Thus, in light of the aforementioned, Texas courts may be willing to provide a minority owner who receives inadequate or unfair consideration in a cash-out merger a direct claim against the controlling owner or owners to challenge the validity of the merger by charging the controlling owner or owners with breaches of fiduciary duty in unfair dealing and/or unfair price.

This Comment will address the current status of minority shareholder recourse as it relates to cash-out mergers based on unfair consideration or unfair dealing, primarily in the context of Texas closely-held corporations. Section II will provide a general background on cash-out mergers, mechanisms generally used to challenge such mergers, and commonly available remedies. Section III will focus on minority shareholders’ current remedies under Texas law, more specifically, the primary road-blocks that have hindered aggrieved minority shareholders in Texas corporations, including limitations on actionable fiduciary duties, limitations on the availability of derivative actions, the availability of various “freeze-out” mechanisms for controlling parties to force minority shareholders to relinquish their ownership interests, and the exclusivity of the statutory appraisal remedy. Section IV discusses the approaches utilized in other jurisdictions, primarily the approach used by Delaware courts, which provides aggrieved minority shareholders with a direct claim in the context of a merger based on unfair dealing or consideration. Finally, Section V focuses on the feasibility of a direct claim in Texas, primarily in an attempt to provide practitioners with arguments to deal with current limitations under Texas law.

---

\(^6\) See, e.g., Vejara v. Levior Int’l, LLC, No. 04-11-00595-CV, 2012 WL 5354681, at *4–5 (Tex. App.—San Antonio Oct. 31, 2012, pet. denied) (mem. op.) (holding that former majority owner of a limited liability company owed fiduciary duties to the purchaser of a controlling interest in the company, despite lack of evidence of any prior relationship of trust and confidence, because the former owner’s “control and intimate knowledge of the company’s affairs and plans gave rise to the existence of an informal fiduciary duty.”).

\(^7\) See In re Schmitz, 285 S.W.3d at 458 n.34.
II. BACKGROUND: CASH-OUT Mergers, COMMON CHALLENGES TO UNFAIR Mergers and TRANSACTIONS & POTENTIAL RELIEF

A. Cash-Out Mergers Generally

Cash-out mergers, often additionally characterized as “freeze-outs” or “squeeze-outs,” are mergers or transactions structured by majority shareholders in such a way that the majority retains an interest in the surviving corporation or entity, while minority shareholders are forced to relinquish their equity in the corporation in exchange for cash, debt securities, or other non-equity consideration that effectively eliminates the minority from participation in the surviving corporation. Indeed, such transactions are coercive by definition. In effect, “minority stockholders are bound by [majority stockholders] to accept cash or debt in exchange for their common shares, even though the price they receive may be less than the value they assign to those shares.” Depending on the jurisdiction and assuming the requisite voting power is present, a variety of mechanisms can be utilized to eliminate a minority owner’s interest, including: statutory

8The term “cash-out merger” in the strictest sense is a transaction in which the consideration paid to the shareholders of the merging corporation is cash rather than securities of the surviving corporation. This article utilizes the term “cash-out” because the ramifications experienced by minority shareholders in Texas following the consummation of a merger based on unfair dealing and/or price are most apparent or acute in the context of a cash-out merger; however, because the elimination of a minority owner’s interest can be effectuated by alternative mechanisms, any reference to “cash-out” is intended to refer more generally to the forced relinquishment of minority ownership based on unfair dealing and/or price. See 20A MILLER & RAGAZZO, supra note 2, § 40:9; Fernán Restrepo & Guhan Subramanian, The Effect of Delaware Doctrine on Freezeout Structure & Outcomes: Evidence on the Unified Approach, 5 HARV. BUS. L. REV. 205, 208 (2015) (“A freezeout (also known, with some occasional loss of precision, as a ‘going-private merger,’ a ‘squeeze-out,’ a ‘parent-subsidiary merger,’ a ‘minority buyout,’ a ‘take-out,’ or a ‘cash-out merger’) is a transaction in which a controlling shareholder buys out the minority shareholders for cash or the controller’s stock.”); McCann v. McCann, 275 P.3d 824, 830 (Idaho 2012) (“Squeeze-outs, sometimes called freeze-outs, are actions taken by the controlling shareholders to deprive a minority shareholder of his interest in the business or a fair return on his investment.”).


10Crago, supra note 9, at 4.

mergers, share exchanges, two-step tender offers (a tender offer followed by a short-form merger), an asset acquisition, or even a reverse stock split.  

**B. Challenging Unfair Cash-Out Mergers and Transactions & Sources of Relief**

An aggrieved shareholder has two judicial avenues to attempt to challenge an allegedly unfair transaction involving a corporation in which the shareholder owns stock: a derivative or a direct claim. A derivative action is an action by a shareholder on behalf of a corporation to enforce a corporate right that the corporation has refused for one reason or another to assert, whereas a direct action is a suit by a shareholder to remedy wrongs done to him individually where the wrongdoer violates a duty owed directly to the shareholder. The Delaware Supreme Court has attempted to clarify the easily muddled distinction between direct and derivative claims with a two-prong framework: “(1) who suffered the alleged harm (the corporation or the suing stockholders, individually); and (2) who would receive the benefit of any recovery or other remedy (the corporation or the stockholders, individually)?” Other jurisdictions, however, have long relied on the so-called “special injury” test, which, as the name indicates, focuses on the injury alleged in the complaint.

Despite the analytical methodology used, the result is that in most jurisdictions, shareholders must establish a personal cause of action and

---


14 Tooley v. Donaldson, Lufkin, & Jenrette, Inc., 845 A.2d 1031, 1033 (Del. 2004). In a different opinion, the Delaware Supreme Court expanded on Tooley, providing that: “If the corporation alone, rather than the individual stockholder, suffered the alleged harm, the corporation alone is entitled to recover, and the claim in question is derivative. Conversely, if the stockholder suffered harm independent of any injury to the corporation that would entitle him to an individualized recovery, the cause of action is direct.” Feldman v. Cutaia, 951 A.2d 727, 732 (Del. 2008) (footnote omitted).

15 See, e.g., Lewis v. Seneff, 654 F. Supp. 2d 1349, 1362 (M.D. Fla. 2009); Casden v. Burns, 504 F. Supp. 2d 272, 277 (N.D. Ohio 2007); Estate of Browne v. Thompson, 727 S.E.2d 573, 575 (N.C. Ct. App. 2012). The “special injury” test requires “an injury which is separate and distinct from that suffered by other shareholders, or a wrong involving a contractual right of a shareholder, such as the right to vote, or to assert majority control, which exists independently of any right of the corporation.” Moran v. Household Int’l, Inc. 490 A.2d 1059, 1070 (Del. Ch. 1985) (citations omitted).
injury to their personal interests to bring direct actions against majority owners and/or officers and directors. However, it is only when shareholders suffer injury to their interests resulting from injury to the corporation (i.e., a derivative injury) that they may file a derivative action. It is important to note that a class action is a direct suit. That is, a class action is treated as direct in nature because the class is essentially alleging that it was injured by an act that was not an injury to the corporation. Class action lawsuits filed under state law challenging the conduct of the person or group in control in the mergers and acquisitions context have emerged as “the dominant form of corporate litigation and outnumber derivative suits by a wide margin.”

As will be discussed, whether the conduct in question provides a shareholder with the ability to bring a direct or derivative action is crucial in the cash-out merger context because of, among other things, the applicable substantive and procedural rules, the effect of a merger on a shareholder’s standing to pursue a claim for relief, and assuming liability is found, whether the recipient of any recovery is the corporation or shareholder.

The claims or causes of action available to aggrieved shareholders to challenge the consummation of a merger may be statutorily created or common-law based, subject to limitations based on the character of the action (i.e., whether the action is direct or derivative in nature) and the state of the law in a particular jurisdiction. Some of the applicable common-law causes of action include: an accounting, breach of fiduciary duty, breach of

16 Warden, Beene, & Frawley, supra note 13; see also Brodsky & Adamski, supra note 9, § 9:2 ("Although the line between a derivative and a direct suit is sometimes hazy, the gravamen of a derivative suit is injury to the corporation rather than to the individual stockholder."); Elizabeth J. Thompson, Direct Harm, Special Injury, or Duty Owed: Which Test Allows for the Most Shareholder Success in Direct Shareholder Litigation?, 35 J. Corp. L. 215, 235 (2009) ("While courts in [various jurisdictions] apply different standards to determine whether a claim is direct or derivative, the results tend to be similar.").


18 See Richard A. Booth, Direct and Derivative Claims in Securities Fraud Litigation, 4 Va. L. & Bus. Rev. 277, 295 (2009) ("Indeed, the phrase class action essentially connotes that the action is a direct action.").

19 See Thompson & Thomas, supra note 4, at 135.

20 See 2 O’Neal & Thompson, Close Corporations and LLCs, supra note 4, § 9:26.
contract, conspiracy, conversion, fraud and constructive fraud, fraudulent transfer, shareholder oppression, unjust enrichment, and quantum meruit.\textsuperscript{21}

Suits alleging breach of fiduciary duty provide, arguably, the most flexible mechanism to challenge mergers allegedly based on unfair price or unfair dealing. Indeed, in many jurisdictions an alleged breach of fiduciary duty may serve as the basis of a direct suit or a derivative suit in the name of, and on behalf of, the corporation.\textsuperscript{22} The typical elements of a claim for breach of fiduciary duty are: (1) a fiduciary relationship between the plaintiff and defendant; (2) the defendant must have breached his fiduciary duty to the plaintiff; and (3) the defendant’s breach must result in injury to the plaintiff or benefit to the defendant.\textsuperscript{23} Assuming that an actionable duty is owed to the minority shareholder, direct suits alleging breach of fiduciary duty are common and viable means of attacking the fairness or validity of a merger.\textsuperscript{24}

A majority of states recognize claims for shareholder oppression, such claims being primarily creatures of statute.\textsuperscript{25} Claims for shareholder oppression are closely related to breach of fiduciary duty claims; in fact, the two are often equated.\textsuperscript{26} Even in jurisdictions that do not recognize a separate shareholder oppression cause of action, courts have noted that the concept relates closely to the fiduciary duty of loyalty, illustrating the general notion that because minority shareholders in closely-held


\textsuperscript{22}See 2 O’NEAL & THOMPSON, CLOSE CORPORATIONS AND LLCS, supra note 4, § 9:19.

\textsuperscript{23}See, e.g., Anderton v. Cawley, 378 S.W.3d 38, 51 (Tex. App.—Dallas 2012, no pet.).


\textsuperscript{25}See Bittle & Hinson, supra note 21, at 386–87.

\textsuperscript{26}See 2 O’NEAL & THOMPSON, O’NEAL AND THOMPSON’S OPPRESSION OF MINORITY SHAREHOLDERS AND LLC MEMBERS § 7:8 (Rev. 2d ed. 2015); Robert C. Art, SHAREHOLDER RIGHTS AND REMEDIES IN CLOSE CORPORATIONS: OPPRESSION, FIDUCIARY DUTIES, AND REASONABLE EXPECTATIONS, 28 J. CORP. L. 371, 377–78 (2003); Douglas K. Moll, SHAREHOLDER OPPRESSION & DIVIDEND POLICY IN THE CLOSE CORPORATION, 60 WASH. & LEE L. REV. 841, 852 (2003) (“The development of the statutory cause of action and the enhanced fiduciary duty ‘reflect the same underlying concerns for the position of minority shareholders, particularly in close corporations after harmony no longer reigns.’ Because of the similarities between the two remedial schemes, it has been suggested that ‘it makes sense to think of them as two manifestations of a minority shareholder’s cause of action for oppression’ . . . [or] as two sides of the same coin . . . .’”) (footnotes omitted).
corporations are extremely vulnerable, majority and controlling shareholders have a special duty to refrain from abusing their position and engaging in self-dealing.\textsuperscript{27} Importantly, whether characterized as shareholder oppression or breach of fiduciary duty, viewing the relationship between shareholders in a closely-held corporation as more akin to that of partners in a partnership has opened the door for minority shareholders to bring direct claims in many jurisdictions.\textsuperscript{28}

As a general rule, the remedies available in both direct suits and derivative actions do not differ from those in other civil suits.\textsuperscript{29} Recovery may come in the form of money damages or equitable relief, and includes—for example—restitution, unjust enrichment, injunctive relief, constructive trusts, disgorgement of profits, an accounting, and even punitive damages.\textsuperscript{30} Moreover, many jurisdictions provide statutorily created remedies, including the right of dissent and appraisal, corporate book and record inspection rights, dissolution, and court ordered buy-outs.\textsuperscript{31} Again, the scope, availability, and particular relief afforded by the remedies differs significantly from jurisdiction to jurisdiction and may depend on the nature of the suit (i.e., direct or derivative).\textsuperscript{32}

The corporate statutes of each state contain provisions permitting shareholders to dissent from certain corporate actions and to seek a court directed appraisal of their shares under certain circumstances by following specified procedures.\textsuperscript{33} The principal purpose of dissent and appraisal rights

\footnotesize{\textsuperscript{27}See Gentile v. Rossette, 906 A.2d 91, 100 (Del. 2006); Abraham v. Emerson Radio Corp., 901 A.2d 751, 752 (Del. Ch. 2006); Donahue v. Rodd Electrotypo Co. of New Eng., Inc., 328 N.E.2d 505, 515 (Mass. 1975); Byron F. Egan, How Recent Fiduciary Duty Cases Affect Advice to Directors and Officers of Delaware and Texas Corporations, State Bar of Texas 1, 456 (2015).}

\footnotesize{\textsuperscript{28}See 2 O’Neal & Thompson, Oppression, supra note 26, § 7:7 (“A challenge to action taken by controlling shareholders or directors based on breach of fiduciary duty traditionally was brought as a derivative suit, but now is more likely to be brought as a direct suit.”).}

\footnotesize{\textsuperscript{29}DeMott & Cavers, supra note 17, § 7:6.}

\footnotesize{\textsuperscript{30}See, e.g., Bostic v. Goodnight, 443 F.3d 1044, 1048–49 (8th Cir. 2006); Am. Family Care, Inc. v. Irwin, 571 So.2d 1053, 1061 (Ala. 1990) (constructive trust); T. Rowe Price Recovery Fund, L.P. v. Rubin, 770 A.2d 536, 552 (Del. Ch. 2000) (granting preliminary injunction); G&N Aircraft, Inc. v. Boehm, 743 N.E.2d 227, 245 (Ind. 2001) (concluding award of punitive damages was appropriate when controlling shareholder engaged in oppressive and malicious conduct to freeze out plaintiffs).}

\footnotesize{\textsuperscript{31}See Art, supra note 26, at 402.}

\footnotesize{\textsuperscript{32}See DeMott & Cavers, supra note 17, § 2:7.}

\footnotesize{\textsuperscript{33}Byron F. Egan, Fiduciary Duties of Corporate Directors and Officers in Texas, 43 Tex. J. Bus. L. 45, 326 (2009).}
is to provide minority shareholders with recourse following majority approval of an undesirable fundamental corporate action. Many jurisdictions designate statutory appraisal rights as the exclusive remedy for dissenting shareholders, such that aggrieved shareholders may not otherwise seek relief stemming from the consummation of a fundamental corporate transaction; however, in other jurisdictions, challenges based on breach of fiduciary duty, among other theories, may be asserted alternatively or in addition to the appraisal remedy.

III. MINORITY SHAREHOLDER RECOUSE UNDER TEXAS LAW

Prior to the Texas Supreme Court’s holding in Ritchie v. Rupe, shareholder oppression claims provided aggrieved minority shareholders with a direct avenue for relief, which included flexible equitable remedies. While the ramifications of Ritchie v. Rupe will likely present a multitude of issues for minority shareholders generally, the current void left in Texas law leaves minority shareholders with very limited meaningful recourse following an unfair merger. To begin, the general rules in Texas are that officers and directors owe their duties to the corporation itself, and that majority shareholder status does not, by itself, give rise to actionable fiduciary duties owed to minority shareholders. Likewise, the availability of a derivative suit to a shareholder following a transaction based on unfair dealing or inadequate consideration poses several issues, namely whether a “cashed-out” shareholder can even retain standing to assert a claim and the

35 See Egan, supra note 33, at 336.
37 For a more thorough overview of Ritchie v. Rupe and the potential consequences, see generally Miller, supra note 36; Bittle & Hinson, supra note 21; James Dawson, Ritchie v. Rupe and the Future of Shareholder Oppression, 124 YALE L.J. 89, 90 (2014); DeMott & Cavers, supra note 17, § 2:7 (“[B]y disallowing remedies lesser than receivership, the [Ritchie v. Rupe] court became the only (or the first) of the 37 with comparable statutory provisions to preclude other remedies.”).
39 See Allen v. Devon Energy Holdings, L.L.C., 367 S.W.3d 355, 391 (Tex. App.—Houston [1st Dist.] 2012, pet. granted, judgm’t vacated w.r.m.).
fact that a merger alleged to be executed unfairly or for an inadequate price is unlikely to cause harm to the corporation.  

What is more, despite the clear potential for self-dealing in connection with such transactions, majority shareholders may legally and explicitly effectuate fundamental business transactions for the sole purpose of “cashing-out” or “freezing-out” minority shareholders as long as the requisite statutory procedures are complied with. Lastly, under the Texas Business Organizations Code, statutory appraisal rights are the exclusive remedy for shareholders to seek relief following an allegedly unfair transaction, and because of the process used to determine fair value, the exclusivity of the appraisal remedy often results in minority shareholders receiving inadequate or unfair compensation.

A. Limitations on Actionable Fiduciary Duties

The general rule regarding fiduciary duties is that corporate officers and directors owe their fiduciary duties to the corporation itself and owe no formal fiduciary duties to a company’s individual shareholders in the absence of a confidential relationship or other independent ground for asserting the existence of a fiduciary relationship.

Likewise, with regard to the relationship between majority and minority owners, the general rule is that majority shareholder status does not, by itself, give rise to fiduciary duties to minority shareholders. Moreover, despite the fact that all Texas courts agree that a special relationship

---


41 See, e.g., Farnsworth v. Massey, 365 S.W.2d 1, 5 (Tex. 1963) (“However, as above pointed out, this action characterized by the plaintiff as a ‘freeze out’ is one which the law permits, providing such action is authorized by four-fifths of the outstanding capital stock of the corporation which is selling its assets.”).

42 See TEX. BUS. ORGS. CODE ANN. § 10.368 (West 2012 & Supp. 2015); see also 20A MILLER & RAGAZZO, supra note 2, § 40:17 (“[i]t remains to be seen whether courts will permit minority shareholders to bring damages actions challenging freeze-out transactions despite the appraisal exclusivity statute.”).

43 See, e.g., Redmon, 202 S.W.2d at 236–37; Hoggett, 971 S.W.2d at 487–88. For a thorough overview of Texas law regarding the fiduciary duties of corporate directors and officers, see Egan, supra note 33, at 55–61.

44 See Allen, 367 S.W.3d at 391.
sufficient to trigger fiduciary duties can arise informally, the overwhelming majority of case law shows rejection of such claims based on business relationships alone.  

The effect of these rules in the cash-out merger context was exemplified in *Somers v. Crane*, where the court held that:

> Because fiduciary relationships are of an ‘extraordinary nature’ and should not be recognized lightly, and because of the abundant authority stating that a director’s or officer’s fiduciary duty runs only to the corporation, not to individual shareholders, we decline to recognize the existence of a fiduciary relationship owed directly by a director to a shareholder in the context of a cash-out merger.

Thus, the court precluded the aggrieved shareholders from asserting a direct class action against the directors and officers for their role in an allegedly unfair cash-out merger. Under this proposition, fiduciary claims in connection with a merger are the right of the corporation itself, not

---

45 See, e.g., Meyer v. Cathey, 167 S.W.3d 327, 330–31 (Tex. 2005) (holding that an informal fiduciary duty is not owed in a business transaction absent a moral, social, domestic, or purely personal relationship of trust and confidence that existed prior to and independent from the parties’ business relationship); Ritchie v. Rupe, No. 05-08-00615-CV, 2016 WL 145581, at *1 (Tex. App.—Dallas Jan. 12, 2016, pet. filed) (“We conclude there is no evidence of a relationship of trust and confidence to support the finding of an informal fiduciary relationship.”). But see *In re TSC Sieber Servs., LC*, No. 09-61042, 2012 WL 5046820, at *6 (Bankr. E.D. Tex. Oct. 18, 2012) (finding individual who took over managerial control of LLC but had no formal office or ownership interest owed LLC a formal fiduciary duty based on agency law and an informal fiduciary duty based on circumstances giving rise to control.).


47 It should be noted for purposes of this article that the factual context of *Somers* involved conduct that would most accurately be described as harm to the corporation. Specifically, the class of shareholders complained that the controlling shareholder (who served as CEO) and members of the board of directors breached fiduciary duties to the shareholders by entering into a multi-million dollar termination agreement with a potential buyer that included the controlling shareholder. *Id.* at 8–9. The corporation ultimately accepted a higher offer from a third-party, but was obligated to pay the termination fee, 51% of which was payable to the controlling shareholder. *Id.* Thus, the factual circumstances of *Somers* do not directly mirror the scenario contemplated in this article because the payment of the termination fee is likely more properly seen as harm to the corporation; however, the propositions stated by the court are important in considering both the lack of a directly owed fiduciary duty to minority shareholders as well as the general effect of a merger on standing for derivative suit purposes.
individual shareholders.\textsuperscript{48} As a result, shareholders must sue derivatively so that recovery flows to all shareholders through an award of damages or equitable relief to the corporation as a whole. However, as will be discussed, in the context of a cash-out merger, shareholders have been denied statutory standing to sue derivatively because the cash-out relieves them of shareholder status.\textsuperscript{49} Moreover, even assuming a claim based on inadequate consideration could be brought derivatively, the shareholders would need to overcome authority suggesting that the corporation itself is likely not harmed, as well as the existence of statutory appraisal rights, which provide the exclusive remedy for dissenting shareholders absent fraud in the transaction.

\textbf{B. Limitations on the Availability of Derivative Suits}

As indicated, the general rule is that financial harm to shareholders resulting from alleged corporate mismanagement or violation of some duty owed to the corporation provides the corporation with a cause of action that may only be asserted by one or more shareholders derivatively.\textsuperscript{50} Derivative actions in Texas are governed by the applicable provisions of the Texas Business Organizations Code, which contains numerous requirements that must be satisfied prior to assertion of the suit.\textsuperscript{51}

Under Section 21.552, a shareholder must have been “a shareholder of the corporation at the time of the act or omission complained of.”\textsuperscript{52} On the face of the statute, it appears to contemplate only whether the plaintiff shareholder can establish “contemporaneous ownership”—however,

\textsuperscript{48} See Gearhart Indus., Inc. v. Smith Int’l, Inc., 741 F.2d 707, 721 (5th Cir. 1984) (noting that while Delaware law explicitly allows for direct suit in cash-out merger cases, under Texas law fiduciary claims in connection with a merger are the right of the corporation itself, not individual shareholders).

\textsuperscript{49} See discussion infra Part III.B.


\textsuperscript{52} Id. § 21.552(a)(1)(A). This requirement is also present in Rule 23.1 of the Federal Rules of Civil Procedure, which governs derivative actions brought in federal court. See FED. R. CIV. P. 23.1(b)(1).
 implicit in Section 21.552 is the requirement that the plaintiff maintain such ownership “continuously” through completion of the suit.53 Only one Texas court has ruled on the merger survival issue under the statutory derivative provisions, holding that, at least in a cash-out merger, the right of a shareholder to bring a derivative action on behalf of the non-surviving corporation does not survive the merger.54 The court also noted that assuming Texas would recognize exceptions to the general rule, shareholders would have to show either that (1) the merger was fraudulently perpetrated to deprive shareholders of the standing to bring a derivative action; or (2) the merger is merely a reorganization, which does not affect the plaintiff’s ownership in the business enterprise.55

Moreover, it is unclear under Texas law whether a shareholder retains derivative standing if the transaction in question confers upon the shareholder a new ownership interest in the same corporation (i.e., a reorganization affecting the shareholder’s ownership interest) or a successor entity (i.e., a business combination transaction).56 At least one Texas court has recognized an equitable exception to the continuous ownership rule where a shareholder’s ownership interest is involuntarily destroyed without a valid business purpose, distinguishing a situation where a shareholder has voluntarily disposed of his or her shares and thereby consciously destroyed the technical foundation of his or her right to maintain the action.57 With regard to a transaction that provides a minority shareholder with a new ownership interest, it would be logical that the shareholder would retain standing following the transaction given that such a shareholder would have continuously maintained a financial interest. This, however, is questionable in light of the legislative history surrounding the 2011 amendment to Section 21.552 of the Texas Business Organizations Code, which indicates the intent of the legislature to clarify that a derivative-suit plaintiff must

53 See 20A MILLER & RAGAZZO, supra note 2, § 39:9 (“Although the statute speaks only to ownership at the time of the alleged violation, it is well accepted that a plaintiff must continuously own stock through completion of the suit to have derivative standing.”). 
55 Id. at 14 n.5.
56 See 20A MILLER & RAGAZZO, supra note 2, § 39:9 n.14.
57 See Zauber v. Murray Sav. Ass’n, 591 S.W.2d 932, 937–38 (Tex. Civ. App.—Dallas 1979, writ ref’d n.r.e.) (holding that minority shareholder alleging usurpation of business opportunities retained standing to bring derivative action where the majority eliminated the minority shareholder’s ownership interest during the pendency of the suit by effecting a reverse stock split).
have been a shareholder at the time of filing suit through the completion of the proceedings.\textsuperscript{58} Thus, the “continuous ownership” rule clearly extinguishes shareholder standing following the consummation of a traditional cash-out merger and may even preclude derivative standing where the transaction giving rise to the suit confers an ownership interest in the new entity as consideration.

In addition to the problems associated with the continuous ownership rule, because a derivative cause of action belongs to the corporation, a shareholder cannot maintain a derivative suit that the corporation itself could not maintain.\textsuperscript{59} Indeed, even assuming that a derivative action was asserted in the context of a closely-held corporation—where the court is authorized under the Texas Business Organizations Code, “if justice requires,”\textsuperscript{60} to treat a derivative proceeding like a direct action and allow the shareholder to recover directly—the action is still derivative in nature.\textsuperscript{61} To be clear, suits by shareholders in closely-held corporations are exempt from most of the procedural requirements applicable to derivative suits.\textsuperscript{62} It is in addition to the exemptions from some of the procedural requirements that the court may treat a derivative action brought by a shareholder of a closely-held corporation as a direct action “if justice requires.”\textsuperscript{63} But, as indicated, the ability of a court to treat a derivative proceeding as a direct action in order to allow the plaintiff shareholder to recover directly is slightly misleading, at least in the context of a cash-out merger. That is,
2016] WHOSE HARM IS IT ANYWAY? 577

because the proceeding is still derivative in nature, the shareholder must still show injury to the corporation, and commonly the acts complained of do not harm the corporation; rather they harm the minority shareholder(s) alone. While it may be argued that the corporation is injured as a result of a merger based on unfair consideration, the existing authority in Texas suggests that the corporation is not always harmed in this context.64 However, as will be discussed, this notion—that a merger based on unfair consideration injures the shareholder(s) and not the corporation—provides tremendous support for the argument that a minority owner who receives inadequate or unfair consideration in a cash-out merger should be able to assert a direct claim against the controlling persons to challenge the validity of the merger.65

C. Availability of Explicit Cash-Out [Freeze-Out and Squeeze-Out] Transactions

A majority owner or group of owners in a Texas corporation, assuming such owner or owners control an adequate number of the board-of-director votes and shares to effectuate the transaction and to comply with the applicable-statutory requirements, can freely utilize various business-combination methods to explicitly “squeeze-out”66 minority shareholders, thereby forcing minority owners to sell their shares.67 Some jurisdictions have precluded majority shareholders from effecting a transaction for the sole purpose of eliminating a minority interest, absent a showing of an

64 See In re Schmitz, 285 S.W.3d 451, 458 n.34 (Tex. 2009).
65 See discussion infra Part V.
66 As previously indicated, the distinction between “freeze-out” and “squeeze-out” mergers can be somewhat muddled. See Restrepo & Subramanian, supra note 8, at 208. Despite the characterization used, it should be noted that the scenario contemplated in this article primarily focuses on the use of a cash-out merger to eliminate the minority, as opposed to an arms-length acquisition structured as a cash merger where all shareholders receive cash. The importance of the distinction is not in the terminology used, rather the scope of the underlying fiduciary duty (or lack thereof) serving as the catalyst for potential shareholder action. That is, in the arms-length context, the majority’s conduct will likely be analyzed more on the duty-of-care spectrum, while in the true minority “squeeze-out” scenario, the majority’s conduct is generally scrutinized under the duty of loyalty. See 2 O’NEAL & THOMPSON, OPPRESSION, supra note 26, § 5:1. Nonetheless, much of the uncertainty and potential solutions discussed in this article apply in either situation.
67 See, e.g., Farnsworth v. Massey, 365 S.W.2d 1, 5 (Tex. 1963) (“However, as above pointed out, this action characterized by the plaintiff as a ‘freeze out’ is one which the law permits, providing such action is authorized by four-fifths of the outstanding capital stock of the corporation which is selling its assets.”).
independent-business purpose. Setting aside, for now, the clear tension between forcing minority owners to relinquish their stock and the potential for self-dealing, a minority shareholder forced to sell his or her shares following a freeze-out transaction is limited to statutory dissent and appraisal rights, which, as will be discussed, often fail to provide adequate compensation to minority shareholders.

D. Right of Dissent & Appraisal: The Exclusivity Principle

Section 10.368 of the Texas Business Organizations Code states:

In the absence of fraud in the transaction, any right of an owner of an ownership interest to dissent from an action and obtain the fair value of the ownership interest under this subchapter is the exclusive remedy for recovery of: (1) the value of the ownership interest; or (2) money damages to the owner with respect to the action.

The so-called “exclusivity principle” applies broadly, and includes “[a]ny merger on which the shareholder is entitled to vote,” and “[a]ny short-form merger on which the shareholder is entitled to vote or in which the shareholder’s interest is converted or exchanged.” In order to exercise any right to an appraisal, shareholders must comply with the intricate procedures required under the Texas Business Organizations Code. The failure of a shareholder to strictly comply with the statutory procedures can easily result in the loss of the right altogether. Moreover, in moving forward with the appraisal remedy, it is likely that the shareholder will have effectively abandoned the requisite shareholder status for purposes of a derivative suit.

---

70 20A MILLER & RAGAZZO, supra note 2, § 40:13.
71 See generally TEX. BUS. ORGS. CODE ANN. §§ 10.351–358.
72 See, e.g., Holt v. D’Hanis State Bank, 993 S.W.2d 237, 242 (Tex. App.—San Antonio 1999, no pet.) (holding that a corporation could elect to terminate a shareholder’s right to appraisal where the corporation raised the shareholder’s failure to submit stock certificates within the statutory time period for the first time in a motion for summary judgment).
73 See, e.g., Breed v. Barton, 429 N.E.2d 128, 129 (N.Y. 1981) (holding that by exercising their rights of dissent to the merger, the plaintiffs had abandoned their status as shareholders).
Commentators have noted that the exclusivity of dissent and appraisal rights poses unique ramifications in “transactions in which a controlling person or persons force the minority to accept cash for its stock.” Specifically, assuming the minority shareholder complied with all of the procedural hurdles contained in the Texas Business Organizations Code, the issue then becomes determining the fair value of the shares. The “fair value” of the minority’s shares, for purposes of establishing a valuation in connection with an appraisal proceeding, is defined as “the value of the [shares] on the date preceding the date of the action that is the subject of the appraisal.” Notably, the calculation excludes any value created by the transaction that gave rise to the appraisal. In other jurisdictions, analogous fair value provisions have been interpreted in a way that also prohibits consideration of pre-transaction wrongs in determining fair value. Thus, not only can minority shareholders be forced to relinquish their ownership interest, they are also effectively precluded from any benefits or synergies that may have arisen from that transaction and may be prohibited from recovering value associated with (or lost as a result of) pre-transaction wrongdoing.

E. Texas Law is Unfavorable for Minority Shareholders

As it stands, minority shareholders in Texas corporations seeking recourse following a cash-out merger executed unfairly or for inadequate consideration must overcome tremendous obstacles. Indeed, given the

74 See 20A MILLER & RAGAZZO, supra note 2, § 40:17 (“[I]t remains to be seen whether courts will permit minority shareholders to bring damages actions challenging freeze-out transactions despite the appraisal exclusivity statute.”); see also Andra v. Blount, 772 A.2d 183, 193 (Del. Ch. 2000) (providing an example, in the context of a publicly held corporation, where an appraisal remedy might not fully compensate shareholders).

75 TEX. BUS. ORGS. CODE ANN. § 10.362.

76 See id. It is important to note that the Texas Business Organizations Code does provide that the fair value shall not be discounted because of the minority status of the owner or any potential lack of marketability. See id. § 10.362(b).

77 See, e.g., Gonsalves v. Straight Arrow Publishers, Inc., 701 A.2d 357, 363 (Del. 1997) (holding that the lower court properly excluded evidence offered to establish that the corporation’s chief executive officer had been excessively compensated prior to a short form merger that cashed out the corporation’s minority shareholders).

78 See Dawson, supra note 37, at 92; Robin Gibbs & Angus J. Dodson, Corporate Fiduciary Duties, 68 ADVOC. 13, 15 (2014) (“[S]trict application of the rule limiting standing to sue on a breach of fiduciary duty to the corporation itself would have perverse effects because a corporation often loses its separate existence following a merger, resulting in a situation in which
limited and often insufficient options available to minority shareholders, freeze-outs and squeeze-outs will likely become highly attractive to majority shareholders. Some commentators have gone as far as saying that if the available recourse for minority shareholders in closely-held corporations remains unchanged, the result is “likely to disincentivize investment in close corporations, ramp up the frequency of shareholder oppression, and imperil the financial health of many small businesses.”

The Texas Supreme Court acknowledged as much in Ritchie v. Rupe where the majority stated, “[w]e recognize that our conclusion leaves a ‘gap’ in the protection that the law affords to individual minority shareholders . . . .”

Nonetheless, recent Texas cases suggest that courts are cognizant that these limitations, strictly applied, would leave minority shareholders with limited recourse. For example, despite the seemingly clear limitations on fiduciary duty claims under Texas law, several intermediate Texas courts have recognized related claims and additional circumstances where a fiduciary relationship might arise. Likewise, a Texas appellate court recently issued an opinion indicating that a claim for aiding and abetting shareholder oppression may be valid.

there is no surviving entity left to bring claims for breaches that diminished the value of the corporation as a whole.”).

79 Dawson, supra note 37, at 90.
80 Ritchie v. Rupe, 443 S.W.3d 856, 889 (Tex. 2014).
81 For example, the Texas Supreme Court has acknowledged that closely-held corporations pose difficulties for minority shareholders seeking to resolve disputes. See Sneed v. Webre, 465 S.W.3d 169, 178 (Tex. 2015) (quoting Ritchie, 443 S.W.3d at 878–79 (footnotes omitted)) (“[M]inority shareholders who lack both contractual rights and voting power may have no control over how those disputes are resolved. . . . [M]inority shareholders in closely held corporations have ‘no statutory right to exit the venture and receive a return of capital’ like partners in a partnership do, and ‘usually have no ability to sell their shares’ like shareholders in a publicly held corporation do; thus, if they fail to contract for shareholder rights, they will be ‘uniquely subject to potential abuse by a majority or controlling shareholder or group.’ Unhappy with the situation and unable to change it, they are often unable to extract themselves from the business relationship, at least without financial loss.”).

83 See generally Brown v. Pennington, No. 05-14-01349-CV, 2015 WL 3958618 (Tex. App.—Dallas June 30, 2015, no pet.). The Brown court dismissed the action for lack of personal jurisdiction, but its analysis assumed the existence of an aiding and abetting shareholder
IV. DIRECT SHAREHOLDER CLAIMS CHALLENGING THE FAIRNESS OR VALIDITY OF A MERGER

The vulnerability of minority shareholders resulting from the ability of majority shareholders to abuse their power by consummating a transaction based on unfair price and/or dealing is not unique to Texas. However, as will be discussed, there is a clear movement in other jurisdictions in favor of allowing minority shareholders to challenge such transactions using a direct suit.\(^{84}\) A number of states protect minority shareholders by imposing special fiduciary duties on majority shareholders in closely-held corporations.\(^{85}\) This trend illustrates the apparent awareness of courts that the ability of majority or controlling shareholders to abuse their position leaves minority shareholders with substantial exposure, which would likely go without redress absent the availability of a direct claim for relief. In fact, direct suits challenging the fairness or validity of a merger have been the basis for a key area of state-based-class-action litigation.\(^{86}\)

---


\(^{85}\) Estes v. Idea Eng’g & Fabricating, Inc., 649 N.W.2d 84, 88 (Mich. 2002) (discussing Michigan statute that creates cause of action with discretionary remedies for shareholder of closely held corporation based on showing that acts of directors or those in control of corporation “are illegal, fraudulent, or willfully unfair and oppressive to the corporation or to the shareholder.”); Ballard v. Roberson, 733 S.E.2d 107, 112 (S.C. 2012) (reasoning that controlling shareholders acted oppressively under South Carolina statute when they fulfilled their stated intention to oust plaintiff by issuing additional shares in conflict with terms of corporation’s articles of incorporation and the stock purchase agreement among themselves and plaintiff); Reget v. Paige, 626 N.W.2d 302, 311–12 (Wis. 2001) (noting that shareholders may bring direct suit under Wisconsin statute where the controlling owners of a corporation inflicted direct injury on complaining shareholder that benefited shareholders who were not injured); 2 O’NEAL & THOMPSON, OPPRESSION, supra note 26, § 7:8.

\(^{86}\) Pennington, by asserting Brown committed a tort in Texas, met his initial burden of alleging jurisdiction under the Texas long-arm statute. Id. at *9; see also Michael A. Grill, Aiding and Abetting Shareholder Oppression?, HOLLAND & KNIGHT SHAREHOLDER RIGHTS BLOG (Sept. 8, 2015), https://www.hklaw.com/ShareholderRightsBlog/Aiding-and-Abetting-Shareholder-Oppression-09-08-2015.

See also Thompson & Thomas, supra note 4, at 178.
A. Delaware’s Direct Claim Fills the “Gap”

Delaware is one of the many jurisdictions that provides minority shareholders with direct claims to challenge transactions alleged to inadequately compensate or otherwise disadvantage the minority.\(^{87}\) A brief comparison of Texas and Delaware law as it relates to available recourse for minority shareholders following a merger based on unfair dealing or unfair consideration is useful to garner an understanding of the rationale utilized by Delaware courts in allowing direct claims. Practically, evaluating the manner in which Delaware’s laws regarding fiduciary duties have served as the catalyst for allowing such claims may be helpful in light of the fact that Delaware law is often cited by the Texas Supreme Court for its recognized corporate jurisprudence.\(^{88}\)

Consistent with Texas, under Delaware law, the general rule is that a plaintiff who ceases to be a shareholder—whether by reason of a merger or otherwise—loses standing to continue and/or maintain a derivative suit.\(^{89}\) Thus, absent fraud, a derivative shareholder must not only be a shareholder at the time of the alleged wrong and at the time of commencement of suit, but he must also maintain shareholder status throughout the litigation.\(^{90}\) Likewise, Delaware law does not formally recognize shareholder

---

\(^{87}\)As indicated, a number of jurisdictions provide shareholders with direct causes of action to challenge the fairness or validity of a merger. See 2 O’NEAL & THOMPSON, CLOSE CORPORATIONS AND LLCs, supra note 4, § 9:26 (providing a chart of the states allowing direct suits). However, because of other similarities between Texas and Delaware, namely the limitations on shareholder oppression claims, comparing Delaware provides insight into the policy or rationale that may be useful for practitioners attempting to persuade a Texas court to allow a direct claim. Moreover, many commentators have written on the similarities and differences between Texas and Delaware law, such literature often regarding the so-called “Delaware advantage,” with opinions landing on both sides of the aisle. For a more thorough comparison of Texas and Delaware corporate law see Egan, supra note 33; Byron F. Egan, Choice of Entity Decision Tree After Margin Tax and Texas Business Organizations Code, 42 TEX. J. BUS. L. 71 (2007); Byron F. Egan & Curtis W. Huff, Choice of State of Incorporation-Texas Versus Delaware: Is It Now Time to Rethink Traditional Notions?, 54 SMU L. REV. 249 (2001); David Mace Roberts & Rob Pivnick, Tale of the Corporate Tape: Delaware, Nevada and Texas, 52 BAYLOR L. REV. 45 (2000); George Parker Young, Vincent P. Circelli & Kelli L. Walter, Fiduciary Duties and Minority Shareholder Oppression from the Defense Perspective: Differing Approaches in Texas, Delaware, and Nevada, 45 TEX. J. BUS. L 257 (2013); Stephanie S. Rojo, Comment, Delaware Versus Texas Corporate Law: How Does Texas Compare?, 3 HOUS. BUS. & TAX L.J. 290 (2003).

\(^{88}\)See, e.g., Grant Thornton LLP v. Prospect High Income Fund, 314 S.W.3d 913, 927 n.19 (Tex. 2010); In re Schmitz, 285 S.W.3d 451, 457 n.32 (Tex. 2009).


oppression as a separate cause of action—with the Delaware Supreme Court going as far as saying that no special rules protect minority shareholders in closely-held corporations.\footnote{Nixon v. Blackwell, 626 A.2d 1366, 1380 (Del. 1993); Harbor Fin. Partners v. Huizenga, 751 A.2d 879, 899–900 (Del. Ch. 1999); see also Egan, supra note 27, at 442 (“Shareholder oppression has not been recognized as a cause of action by the Supreme Courts of either Delaware or Texas.”).} As with Texas, Delaware courts have reasoned that the available remedies adequately protect minority shareholders.\footnote{Nixon, 626 A.2d at 1380–81.}

Despite the seeming consistency of both jurisdictions, the substance of the “available remedies” cited by Texas and Delaware courts as adequately protecting minority shareholders are in stark contrast.

To begin, the Texas Supreme Court has pointed to the availability of relief “through a derivative action, or through a direct action” based on breach of fiduciary duty, as a means of recourse for minority shareholders.\footnote{Ritchie v. Rupe, 443 S.W.3d 856, 882, 887 (Tex. 2014).} Yet, because Texas courts have held that fiduciary claims in connection with a merger are the right of the corporation itself, not individual shareholders, inevitably the effectuation of a merger and subsequent loss of derivative standing is the end of the road.\footnote{See Ritchie, 443 S.W.3d at 882 (derivative suit based on merger for “grossly inadequate consideration” dismissed for lack of standing); Somers ex rel. EGL, Inc. v. Crane, 295 S.W.3d 5, 12 (Tex. App.—Houston [1st Dist.] 2009, pet. denied).}

Delaware, in contrast, explicitly allows for a direct suit in such cases.\footnote{See Parnes v. Bally Entm’t Corp., 722 A.2d 1243, 1245 (Del. 1999); Lewis, 477 A.2d at 1046.} Specifically, Delaware law provides that a “stockholder who directly attacks the fairness or validity of a merger alleges an injury to the stockholders, not the corporation, and may pursue such a claim even after the merger at issue has been consummated.”\footnote{Parnes, 722 A.2d at 1245.} Although it has been characterized as an exception to the general rule regarding loss of derivative standing,\footnote{In re Primedia, Inc. Shareholders Litig., 67 A.3d 455, 477 (Del. Ch. 2013); In re NYMEX S’holder Litig., Nos. CIV.A.3621-VCN & 3835-VCN, 2009 WL 3206051, at *49 (Del. Ch. Sept. 30, 2009).} it is more important to note that the rule recognizes that in the context of a merger involving unfair dealing and unfair price, the resulting
injury is to the shareholders, not the corporation.\textsuperscript{98} From a practical standpoint, the rule acknowledges the reality that following a cash-out merger effectuated to eliminate minority ownership interests, the surviving corporation or entity (comprised of at least some former majority owners) is extremely unlikely to institute a derivative action based on conduct that ultimately benefitted it.\textsuperscript{99}

Texas courts have also suggested that “[a] corporate shareholder may have an individual action for wrongs done to him where the wrongdoer violates a duty arising from a contract or otherwise and owing directly by him to the shareholder.”\textsuperscript{100} But, Texas courts have never recognized a formal fiduciary duty between majority and minority shareholders in a closely-held corporation.\textsuperscript{101} Without a legally recognized duty, direct claims are virtually impossible. Likewise, as indicated, even assuming a derivative claim was procedurally available, it would likely fail because typical acts of the majority that harm or oppress minority shareholders, such as an unfair cash-out merger, usually benefit the corporation and rarely harm it.\textsuperscript{102}

In contrast, Delaware courts have recognized that minority-majority relationships are ripe for abuse and the conduct most likely to constitute abuse of that relationship does not harm the corporation, but the minority shareholder(s) in question.\textsuperscript{103} Thus, despite declining to recognize a formal shareholder oppression cause of action, Delaware imposes an actionable fiduciary duty where (1) a shareholder owns more than 50 percent of the shares, or (2) a shareholder (or group of controlling shareholders) exercises control over the business affairs of the corporation.\textsuperscript{104} The recognition of such a duty reflects an understanding that certain transactions, undoubtedly cash-out mergers based on unfair dealing and/or unfair consideration, harm the minority shareholders. Indeed, Delaware courts have expanded on the scope of the duty owed to shareholders by officers and directors (whom often are also majority owners, or conduits thereof) in the context of a sale

\textsuperscript{98}See generally Peter V. Letsou & Steven M. Haas, The Dilemma That Should Never Have Been: Minority Freeze Outs in Delaware, 61 BUS. LAW. 25 (2005).

\textsuperscript{99}Gibbs & Dodson, supra note 78, at 13.

\textsuperscript{100}Faour v. Faour, 789 S.W.2d 620, 622 (Tex. App.—Texarkana 1990, writ denied).

\textsuperscript{101}Willis v. Donnelly, 199 S.W.3d 262, 276 (Tex. 2006).

\textsuperscript{102}See supra Part III.B.


or break-up, consistently holding that officers and directors may discharge their heightened duty by establishing that they sought out the best value reasonably available to shareholders.\(^{105}\) Moreover, in transactions involving a majority or controlling shareholder—who stands on both sides of the transaction—Delaware courts employ the “entire fairness” standard of review, placing the burden on the majority shareholder to affirmatively demonstrate both fair dealing and fair price.\(^{106}\) While Delaware, like Texas, has endorsed the legitimacy of cash-out or freeze-out mergers to eliminate the minority, Delaware applies the entire fairness standard to such self-interested mergers.\(^{107}\)

**B. Mechanics of a Direct Claim**

As indicated, under Delaware law, a shareholder who directly attacks the fairness or validity of a merger generally alleges an injury to the shareholders, not the corporation, and may pursue such a claim even after the merger at issue has been consummated.\(^{108}\) Whether characterized as an exception to the continuous ownership rule of derivative actions or as a generally available direct claim, in order to state a direct claim, there must be (1) the existence of an actionable fiduciary duty and (2) breach of such duty—based on unfair dealing and/or unfair price in a manner that places the fairness or validity of the merger in question. Thus, the substance of a complaint must “question the fairness of the price offered in the merger or the manner in which the merger agreement was negotiated.”\(^{109}\) With respect to fair dealing, minority shareholders have successfully established breaches of fiduciary duty in situations where (1) the majority fails to apply procedures that replicate independent, arms-length bargaining; (2) the majority fails to make full disclosure; or (3) the majority uses its power to place the minority in an unfavorable bargaining position with respect to a


\(^{107}\) Id. at 711.

\(^{108}\) Parnes v. Bally Entm’t Corp., 722 A.2d 1243, 1244–45 (Del. 1999) (reversing lower court decision that stockholders’ action challenging the fairness of the company’s merger was a derivative claim and holding that the complaint adequately alleged a direct claim because a stockholder who directly attacks the fairness of a merger alleges an injury to the stockholders, not the corporation); Elloway, 238 S.W.3d at 900.

\(^{109}\) Parnes, 722 A.2d at 1245; see also Kramer v. W. Pac. Indus., 546 A.2d 348, 351–52 (Del. 1988).
freeze-out merger. Establishing unfair price is less susceptible to categorical classification. In fact the techniques used in determining the fair value of shares are inconsistent, but nonetheless minority shareholders are given substantial leeway to argue that the price in question was unfair in light of the Delaware Supreme Court’s decision to allow consideration of “any techniques or methods which are generally considered acceptable by the financial community.”

V. FEASIBILITY OF A DIRECT SHAREHOLDER CLAIM IN TEXAS

As indicated, the remedial scheme available to minority shareholders in Texas closely-held corporations fails to recognize that “typical acts of minority shareholder oppression,” including cash-out mergers based on unfair dealing or price, “usually operate to benefit the corporation and hardly ever harm it.” As a result, minority shareholders seeking to assert a direct claim against the majority or controlling owners following a cash-out merger based on unfair dealing and/or unfair consideration must overcome a number of barriers, the most pronounced of which is the lack of a formally-owed, actionable fiduciary duty imposed on the majority or controlling shareholders (whether officers/directors or not). Nonetheless, because of the specific quandary faced by minority shareholders forced to relinquish their ownership in an unfair cash-out merger, Texas courts may

---


111 Id. at 1141 (quoting Weinberger, 457 A.2d at 712–13).

112 The discussion regarding the feasibility of a direct claim in this article is focused on the corporate context. However, it is important to note that similar considerations can and should apply in the context of other entities, e.g., limited liability companies and limited partnerships. Texas courts generally analogize to corporate law in dealing with other entities, thus much of the foregoing discussion would likely translate. See, e.g., In re Hardee, No. 11-60242, 2013 WL 1084494, at *9 (Bankr. E.D. Tex. Mar. 14, 2013). In fact, under the Texas Business Organizations Code, members of an LLC do not have statutory dissent and appraisal rights unless and to the extent that the governing documents of the LLC provide for such rights. See TEX. BUS. ORGS. CODE ANN. § 10.351(b)–(c) (West 2012 & Supp. 2015). Thus, given that some of the barriers being discussed, such as the exclusivity principle, do not apply outside the corporate context it may be that standing to bring a direct claim is actually easier to establish by a minority owner of an LLC.

113 Ritchie v. Rupe, 443 S.W.3d 856, 893 (Tex. 2014) (Guzman, J., dissenting).

be willing to recognize at least a limited exception to the traditional restrictions placed on claims for breach of fiduciary duty. At least one Texas court, albeit applying Delaware law, has held that “[a] stockholder who directly attacks the fairness or validity of a merger alleges an injury to the stockholders, not the corporation, and may pursue such claim even after the merger at issue has been consummated.”

Some commentators have suggested that “[i]t seems likely that courts would apply the same rule in a case governed by Texas law.” That prediction finds support in recent Texas decisions which seem to recognize that strict application of the traditional rules governing fiduciary duty claims would leave significant injuries without a remedy. In light of the aforementioned, the Texas Supreme Court’s implicit recognition that a claim based on inadequate price or unfair dealing in connection with a cash-out merger belongs to the shareholder(s), and the authority suggesting that a minority shareholder may overcome the exclusivity principle by challenging the transaction using a claim for breach of fiduciary duty (which Texas courts have equated to fraud)—minority shareholders may find relief by way of a direct action to challenge a cash-out merger premised on the majority’s breach of fiduciary duty.

A. Direct Claims Are Generally Viable in Texas Where a Personal Cause of Action and Personal Injury Are Established

Texas courts have allowed shareholders to bring direct causes of action “where the wrongdoer violates a duty arising from contract or otherwise, and owing directly by him to the [shareholder].” Indeed, the Texas Supreme Court recently acknowledged the long-standing availability of direct actions where a shareholder can show a personal cause of action and

---

116 Gibbs & Dodson, supra note 78, at 15.
117 See supra Part III.E.
119 See Farnsworth v. Massey, 365 S.W.2d 1, 5 (Tex. 1963); 20A MILLER & RAGAZZO, supra note 2, § 40:17 (citing Carl David Adams, Benefiting from Fiduciary Office: A Presumption of Fraud, 47 Tex. B.J. 648, 649 (1984)).
personal injury. Stated another way, Texas law is clear that a shareholder who suffers “special injury” distinct from any injury to the corporation has standing to bring a direct action.

Therefore, a shareholder in Texas attempting to challenge the validity of a cash-out merger using a direct claim must establish (1) a personal cause of action and (2) personal injury. Aggrieved shareholders can potentially overcome the various issues that have stymied direct recovery by characterizing a merger based on unfair dealing or consideration as a breach of fiduciary duty owed to the shareholder (in light of the fact that the resulting harm is clearly to the shareholder and not the corporation).

B. Establishing a Personal Cause of Action and Personal Injury

The key to establishing standing to bring a direct action, is the existence of a personal cause of action and personal injury. Given that a claim in this context will likely rely on a claim for breach of fiduciary duty, the analysis will focus primarily on the elements of that claim.

1. Establishing the Existence of a Fiduciary Duty Owed to Minority Shareholders

Texas courts have long acknowledged that a fiduciary duty may arise informally, but have nonetheless been reluctant to give such claims merit under most circumstances. Given the fact-specific limitations inherent in establishing an informal duty, the focus of this article is primarily on the possibility of establishing a formally owed (i.e., status-based) duty to minority shareholders. In addition to the distinctive source of an informal fiduciary duty, it is also important to note that the scope of an informal, relationship-based duty would likewise be different. The status-based duty between shareholders recognized by courts is not always a “true” fiduciary duty, i.e., an obligation to act in the best interests of the other; rather a

---

123 The elements of a claim for breach of fiduciary duty are: (1) a fiduciary relationship between the plaintiff and defendant; (2) the defendant must have breached his fiduciary duty to the plaintiff; and (3) the defendant’s breach must result in injury to the plaintiff or benefit to the defendant. Lundy v. Masson, 260 S.W.3d 482, 501 (Tex. App.—Houston [14th Dist.] 2008, pet. denied).
124 See supra note 45 and accompanying text.
formal, status-based duty imposes a more narrow obligation to act fairly and honestly. In contrast, where a duty arises from a relationship of trust and confidence ("informal duty"), such a duty will likely encompass the aspects of a true fiduciary duty, that is, the duty to act selflessly in the best interests of the other.

Nonetheless, under the right circumstances commentators have noted that despite the traditional rule precluding majority shareholder status alone from creating fiduciary duties to minority shareholders—"courts are increasingly finding that an informal fiduciary relationship can arise based purely on [one’s] intimate knowledge of and control over an entity in comparison to minority or passive investors." Thus, minority shareholders who can establish a special relationship sufficient to create an informal fiduciary duty owed by the majority to the minority may be successful in asserting direct claims to challenge an unfair cash-out merger.

Despite the longstanding proposition that shareholders generally do not owe one another a formal fiduciary duty, there is Texas authority suggesting that a controlling shareholder owes a fiduciary duty to a minority shareholder in the context of the communication of an offer to purchase the minority shareholder’s shares including an offer to redeem the

---

125 See 20 MILLER & RAGAZZO, TEXAS PRACTICE SERIES: BUSINESS ORGANIZATIONS § 30:32 n.13 (3d ed. 2015) ("[A]ny ‘fiduciary duty’ imposed on shareholders is a duty to treat their co-investors fairly rather than a duty to act selflessly. To the extent that one seeks to impose a true fiduciary duty upon a controlling shareholder—the duty to act selflessly in the best interests of other shareholders—there is no question that such a duty may only be based on a sufficient relationship of trust and confidence. However, the duty of a controlling shareholder not to misappropriate the value of the enterprise by freezing out the minority would seem to be based on status.").

126 See id.


128 See Thompson v. Hambrick, 508 S.W.2d 949, 954 (Tex. Civ. App.—Dallas 1974, writ ref’d n.r.e.) (holding fact issues existed regarding the breach of fiduciary duty where the directors joined in the rejection of the $45 per share offer, secretly agreed to sell their stock at $55 per share to the same people who had made the previous offer, without notice to the minority shareholders, the right of first refusal, or any participation in the transaction).
shares where the redemption will result in an increase in the controlling shareholder’s ownership of the corporation. Specifically, in Allen v. Devon Energy Holdings, L.L.C., the First Court of Appeals, analogizing in part to corporate case law, applied a “special facts” test to hold that a fiduciary relationship existed as a matter of law in the limited liability company (LLC) context where (1) the alleged-fiduciary has a legal right of control and exercises the control by virtue of his status as the majority owner and sole member-manager of a closely-held LLC and (2) either purchases a minority shareholder’s interest or causes the LLC to do so through a redemption when the result of the redemption is an increased ownership interest for the majority owner and sole manager.

While the Allen court declined to recognize a broad formal fiduciary duty on the part of a majority owner to a minority owner—reiterating the general rule that Texas courts will not impose such a duty between majority and minority shareholders in closely-held corporations—the court concluded that corporate case law supported imposing a fiduciary duty in a situation like that at issue, i.e., where a majority member’s position enables the effectuation of a transaction that results in the redemption of a minority member’s interest (thus increasing the ownership of the majority member). Thus, notwithstanding the court’s recognition that the overwhelming Texas authority on the subject rejects the imposition of a broad formal fiduciary duty on the part of a majority shareholder to a minority shareholder, the conduct in question (a challenge of a share redemption orchestrated by the majority member of an LLC) coupled with the court’s application of the “special facts” test, may have broad implications. For example, in Vejara v. Levior International, LLC, the Fourth Court of Appeals held that a minority owner owed an informal fiduciary duty because of the owner’s “control and intimate knowledge of the company’s affairs and plans . . . .” While the court characterized the duty in question as an informal fiduciary duty, there was no evidence of any prior relationship of trust and confidence as is typically required to establish an informal fiduciary relationship. Thus, this case exemplifies the apparent sympathy felt by Texas appellate courts regarding disputes involving minority owners and may even ultimately

130 Id. at 395–96.
132 See id. at *1–2.
WHOSE HARM IS IT ANYWAY?

illustrate the gradual expansion of fiduciary claims to new contexts that would not be protected under previously existing law.

Likewise, aggrieved minority shareholders may find relief in characterizing the fiduciary duty owed by the majority as a limited, “controlling shareholder duty.” While such a duty would resemble that contemplated by the Allen court, the focus would shift slightly towards the historical conflation by Texas courts of shareholder oppression actions and fiduciary duty law. That is, Texas courts that have been hesitant to recognize and apply a shareholder oppression cause of action to the facts before them have instead turned to fiduciary duties as a source of relief for plaintiffs. Most commonly, this has arisen in situations where a majority shareholder dominates control over the business. Established Texas precedent has recognized that “in certain limited circumstances, a majority shareholder who dominates control over the business may owe a [fiduciary duty] to the minority shareholder[s].” Such controlling shareholder duties flow from the power the majority has to unilaterally direct corporate affairs and typically arise in self-dealing transactions and sales of the controlling interest. Of course, it would be misguided to suggest that controlling shareholders should not be able to exercise the rights inherent in majority ownership. But, with regard to cash-out mergers where, under the specific circumstances, the majority has retained some disproportionate benefit at the expense of the minority, it does not make sense for the

---

133 See, e.g., Faour v. Faour, 789 S.W.2d 620, 622–23 (Tex. App.—Texarkana 1990, writ denied); Morgan v. Box, 449 S.W.2d 499, 502 (Tex. App.—Dallas 1969, no writ); 20 MILLER & RAGAZZO, supra note 125, § 30:32 n.14 (noting that the concepts of shareholder oppression and fiduciary duty law are often equated).
134 Egan, supra note 27, at 451; see also Allen, 367 S.W.3d at 365; Davis v. Sheerin, 754 S.W.2d 375 (Tex. App.—Houston [1st Dist.] 1988, writ denied) (court-ordered buy-out of minority shareholder where majority shareholder engaged in oppressive conduct).
137 20A MILLER & RAGAZZO, supra note 2, § 36:14.
138 See, e.g., Thompson v. Hambrick, 508 S.W.2d 949, 952–53 (Tex. Civ. App.—Dallas 1974, writ ref’d n.r.e.) (“The right of control is ordinarily a right inherent in ownership or control of a majority of the stock . . . “).
traditional rules to apply. As a matter of policy, imposing controlling shareholder duties would reflect the common-sense notion that the usual default rules of corporate law affect closely-held corporations differently from large publicly held corporations.\textsuperscript{139}

Moreover, consider that in \textit{Ritchie v. Rupe}, the Texas Supreme Court indicated that the vague standard for determining “oppressive” conduct was a key factor in the Court’s decision to decline to recognize a common-law cause of action for oppression.\textsuperscript{140} However, the Court stated:

\begin{quote}
Although we do not foreclose the possibility that a proper case might justify our recognition of a new common-law cause of action to address a “gap” in protection for minority shareholders, any such theory of liability will need to be based on a standard that is far more concrete than the meaning of ‘oppressive.’\textsuperscript{141}
\end{quote}

Again, a cash-out merger effectuated in order to eliminate a minority interest epitomizes the “gap” left by the current remedial scheme available to Texas minority shareholders because ultimately the minority, not the corporation, bears the injury. Likewise, as the \textit{Ritchie} dissent noted, “[t]he remedy that comes closest to affording some relief to the oppressed minority shareholder is a common-law claim for breach of fiduciary duty.”\textsuperscript{142}

Against this backdrop, it would make sense to provide minority shareholders with a direct claim for breach of fiduciary duty in the limited circumstance where the majority has dominated control over the business either by engaging in self-dealing such that they enjoy a disproportionate benefit at the expense of the minority or likewise where the majority sells or transfers control to the minority’s detriment. Despite the “fiduciary” connotation, such a “controlling shareholder duty” would not require the majority to act as a “true” fiduciary, rather, the duty imposed on the controlling shareholder would require fairness and honesty.\textsuperscript{143}

\begin{flushleft}
\textsuperscript{139} See McLaughlin v. Schenk, 220 P.3d 146, 155 (Utah 2009) (“[T]o require the same fiduciary duties for publicly held and closely held corporate shareholders would not adequately protect close corporation shareholders.”); see also 20A \textsc{Miller & Ragazzo}, supra note 2, § 36:14.
\textsuperscript{140} Ritchie v. Rupe, 443 S.W.3d 856, 890 (Tex. 2014).
\textsuperscript{141} \textit{Id.}
\textsuperscript{142} \textit{Id.} at 905 (Guzman, J., dissenting).
\textsuperscript{143} See supra notes 125–26 and accompanying text.
\end{flushleft}
duty would not only be consistent with the scope of the duty recognized under Delaware law, but would also be consistent with prior Texas decisions. Likewise, the limited nature of a controlling shareholder duty could dispel concerns regarding the ambiguity surrounding oppression claims. That is, the proposed duty could facilitate a concrete, workable standard that would apply primarily to situations where a derivative suit would be inapplicable (because the minority alone has suffered the injury) while simultaneously foreclosing the “gap” in minority shareholder protection.

Therefore, in light of recent decisions and established precedent recognizing that majority shareholders may improperly exert control over closely-held corporations, minority shareholders in closely-held corporations have multiple avenues to persuade a Texas court that a fiduciary duty exists sufficient to give rise to a direct cause of action.

2. A Claim Based On Unfair Dealing or Inadequate Price
Belongs to the Shareholders

It is well established that where all shareholders are harmed in proportion to share ownership, fiduciary claims in connection with a merger are generally seen as belonging to the corporation itself. But, a

---

144 Hoggett v. Brown, 971 S.W.2d 472, 488 n.13 (Tex. App.—Houston [14th Dist.] 1997, pet. denied) (“We note that a majority shareholder’s fiduciary duty ordinarily runs to the corporation . . . [h]owever, in certain limited circumstances, a majority shareholder who dominates control over the business may owe such a duty to the minority shareholder. See e.g., Patton v. Nicholas, 279 S.W.2d 848 (Tex. 1955) (injunction issued against majority shareholder maliciously suppressed dividends); Davis v. Sheerin, 754 S.W.2d 375 (Tex. App.—Houston [1st Dist.] 1988, writ denied) (court-ordered buy-out of minority shareholder where majority shareholder engaged in oppressive conduct); Duncan v. Lichtenberger, 671 S.W.2d 948 (Tex. App.—Fort Worth 1984, writ ref’d n.r.e.) (minority shareholders entitled to reimbursement of monetary contribution to corporation where majority shareholder completely excluded minority shareholders from management of business); Thompson v. Hambrick, 508 S.W.2d 949 (Tex. Civ. App.—Dallas 1974, writ ref’d n.r.e.) (fact issue existed as to whether majority shareholders wrongfully obtained premium for selling control of the corporation); Morrison v. St. Anthony Hotel, 295 S.W.2d 246 (Tex. Civ. App.—San Antonio 1956, writ ref’d n.r.e.) (former minority shareholder entitled to sue majority shareholder for malicious suppression of dividends). None of these circumstances are present because [the defendant] was never a controlling shareholder of the corporation.”).

145 See Gearhart Indus., Inc. v. Smith Int’l, Inc., 741 F.2d 707, 721 (5th Cir. 1984); Egan, supra note 33, at 178; see also City of Inkster Policeman & Fireman Ret. Sys. v. Kinder, No. 01-08-00308-CV, 2009 WL 1562909, at *3 (Tex. App.—Houston [1st Dist.] June 4, 2009, no pet.)
shareholder who suffers “special injury” distinct from any injury to the corporation has standing to bring a direct action.\textsuperscript{146} For example, direct suits have been allowed for claims challenging the withholding of dividends, discriminatory distribution of corporate assets, dilution and interference with voting power, the denial of preemptive rights, refusal to allow inspection of corporate books and records, and breach of the duty that a controlling shareholder owes to minority shareholders.\textsuperscript{147}

In the context of a merger with competing bids, the Texas Supreme Court has expressed doubt as to whether the decision to accept a lower price “would harm the corporation as opposed to the shareholders.”\textsuperscript{148} While the statement itself is dicta, it provides room for argument that in a cash-out merger a claim based on inadequate price belongs to the shareholders directly, and therefore should be available for assertion as a direct claim. Thus, again considering that the “gap” in minority shareholder protection applies primarily where the harm in question flows to only the minority shareholders, it seems logical that such a situation would clearly satisfy the personal injury aspect of a direct action.

C. Overcoming the Exclusivity Principle

As discussed, shareholders seeking to recover directly for unfair mergers must overcome the exclusivity principle, i.e., the status of the statutory appraisal procedure as the exclusive remedy for recovery of the fair value of the shares or money damages to the shareholder with respect to the transaction in question. Nonetheless, the exclusivity principle does not apply where there are allegations of fraud in the transaction.\textsuperscript{149} The statute likely does not preclude suits against officers or directors for misconduct.\textsuperscript{150}

\textsuperscript{146} See Thompson, 508 S.W.2d at 954; 20A MILLER & RAGAZZO, supra note 2, § 39:7.

\textsuperscript{147} 20A MILLER & RAGAZZO, supra note 2, § 39:7.

\textsuperscript{148} In re Schmitz, 285 S.W.3d 451, 458 n.34 (Tex. 2009) (“We also note that the letter does not specify why accepting $22 rather than $23 per share would harm the corporation as opposed to the shareholders.”); see also Marron \textit{ex rel.} Stewart & Stevenson Servs., Inc. v. Ream, No. CIVAH–06–1394, 2006 WL 2734267, at *7 (S.D. Tex. May 5, 2006) (questioning whether claim that board should have accepted offer for $35.50 rather than offer for $35.00 per share was derivative claim belonging to corporation).

\textsuperscript{149} TEX. BUS. ORGS. CODE ANN. § 10.368 (West 2012 & Supp. 2015).

\textsuperscript{150} 20A MILLER & RAGAZZO, supra note 2, § 40:17 (“Presumably, shareholders injured by conduct that depressed the value of the corporation’s shares prior to the transaction with respect to
Moreover, given that the statute applies on its face to money damages, suits requesting equitable relief should not be precluded.

With regard to the fraud exception, claims for breach of fiduciary duty are often described as a form of constructive fraud. For example, in *Gannon v. Baker*, the court stated that the “allegations that [the majority shareholder] failed to disclose material information and engaged in self-dealing in distributing the corporate assets are allegations of fraud in the transaction.” In light of this authority, there is support for allowing a minority shareholder to bypass the appraisal statute and directly challenge a cash-out transaction. Likewise, with regard to suits requesting equitable relief, Texas courts have broad discretion to fashion equitable remedies such as profit disgorgement, fee forfeiture, injunctions, and receivership to remedy a breach of fiduciary duty. Thus, if a minority shareholder can establish the existence of a directly owed fiduciary duty, the exclusivity principle should not prohibit direct suits to rectify the consummation of transactions based on unfair price or unfair dealing.

**VI. CONCLUSION**

As it stands, minority shareholders in Texas closely-held corporations following cash-out mergers are faced with a unique quagmire of barriers, including: (1) the exclusivity of statutory appraisal rights, (2) the non-
existence of an actionable fiduciary duty to bring a direct suit, (3) the loss of derivative standing following the consummation of the transaction giving rise to the action, and (4) the inability to successfully assert a derivative suit, even where such shareholders can maintain the requisite standing, because of the fact that the conduct in question likely did not harm the corporation itself. Nonetheless, Texas courts may be willing to provide a minority owner who receives inadequate or unfair consideration in a cash-out merger a direct claim against the controlling persons to challenge the validity of the merger by charging the controlling persons with breaches of fiduciary duty in unfair dealing and/or unfair price. In order to overcome barriers in Texas law, shareholders will need to establish both personal injury and a personal cause of action. Recent trends in Texas case law and established precedent recognizing that majority shareholders may improperly exert control over closely-held corporations provide multiple avenues for shareholders to successfully assert the existence of an actionable fiduciary duty. Likewise, the personal injury aspect should logically be satisfied considering that in the context of a cash-out merger allegedly based on unfair dealing and/or unfair price, not only is the surviving corporation or entity (comprised of at least some former majority owners) unharmed, but it is likely a beneficiary of such conduct.

Ultimately, the “gap” in minority shareholder protection will require Texas courts to recognize that, with regard to unfair cash-out mergers, the shareholders are suffering the injury—not the corporation. Thus, future attempts by minority shareholders to challenge such transactions may benefit from analogizing to the framework utilized in Delaware. That is, a stockholder should challenge the validity of the merger itself, usually by charging the directors with breaches of fiduciary duty resulting in unfair dealing and/or unfair price.\footnote{Parnes v. Bally Entm’t Corp., 722 A.2d 1243, 1245 (Del. 1999).} In doing so, minority shareholders may preempt or curtail concerns regarding the scope of the duty by limiting it to situations where a majority shareholder (or controlling group) dominates control over the business affairs of the corporation. As indicated, limiting the existence of the duty to situations where a majority shareholder dominates control over the business would be consistent with prior Texas decisions.\footnote{See supra note 144.} Likewise, the limited nature of this proposed duty could dispel concerns regarding the ambiguity surrounding the scope of shareholder oppression claims, thereby foreclosing the “gap” and providing a workable
standard that would apply primarily to situations where a derivative suit would be inapplicable. While establishing the existence of a fiduciary duty, the breach of which is maintainable as a direct cause of action is crucial, it may be persuasive on that front to emphasize the distinction between a derivative claim for mismanagement related to a merger and a direct claim for unfairness in the merger terms.157 By illuminating this distinction, minority shareholders may be able to demonstrate the limitations on current remedial options in the specific context of an unfair merger, namely the fact that in the cash-out context, the harm is to the minority.