Interoffice Memorandum of Law
Appellant's Brief

TO: Mr. Dudley Knox; Advanced Legal Research and Writing LGLA-2331-53500
FROM: Mr. Chris Rainbolt
DATE: May 7, 2015
IN RE: *Argo Data Resource Corp. v. Shagrithaya*, 380 S.W.3d 249 (Tex.App.—Dallas 2012).

Assignment: To draft an Appellant's Brief arguing on behalf of one of the parties in the matter above.

APPELLATE COURT CASE NO. 05-10-00690-CV

STATE OF TEXAS

IN COURT OF APPEALS

Balkrishna Shagrithaya,
Plaintiff-Respondent,

vs.

Argo Data Resource Corporation and Max Martin,
Defendant-Appellants

APPELLANT'S BRIEF

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES:

STATUTES:

ENCYCLOPEDIAS:

COMMENTARY:

LAW REVIEW ARTICLES:

ISSUES

Did the defendant's act of withholding dividends for the purpose of buying out minority interest constitute minority shareholder oppression?

The district court ruled in the affirmative.

Tex. Bus. Orgs. Code Ann. § 11.404 (West).
Ritchie v. Rupe, 443 S.W.3d 856, 871 (Tex. 2014).

Did an implied contract exist between the parties that they would maintain equal salaries?

The district court ruled in the affirmative.

Effel v. McGarry, 339 S.W.3d 789, (Tex.App.-Dallas 2011).

STATEMENT OF CASE AND FACTS

The Case

On December 28, 2007, the Respondent, Balkrishna Shagrithaya, sued the Appellants, Argo Data Resource Corporation and majority shareholder Max Martin, in the 162nd Judicial District Court, Dallas County, for minority shareholder oppression, breach of contract, and other causes of action. Mr. Shagrithaya sought judgment in his favor and monetary relief. At trial, the jury found in favor of Mr. Shagrithaya on all claims submitted and Lorraine Raggio, J. entered judgment ordering Argo to issue a one-time dividend of $85 million for its shareholder oppression and pay additional damages of $1,361,100 for breach of contract. Argo and Martin appeal.

The Facts

Max Martin and Balkrishna Shagrithaya formed Argo in 1980 to provide software services to the retail financial services industry. The two men were the only members of the board of directors and had an equal vote. Because Martin was the majority shareholder, he retained a tie-

breaking option. Initially, Martin was the president and handled business matters while Shagrithaya was in charge of developing the company's technology. During the early stages of the business, the board elected to pay themselves no salary and reinvest all earnings in order to grow the company and eventually sell it.

Around 2000, Martin became CEO and succession plans for the founders of the company became a concern. Martin urged Shagrithaya to take on a managerial role, a proposal that Shagrithaya resisted.

In 2004, the first dividend was issued in the amount of $160,000 which was distributed proportionately to the shareholders' percentage of ownership.

Initially, the men took no salaries but, when they eventually did, they voted each year for equal salaries. By 2006, their annual salaries had reached nearly $1 million. Around this time, Martin cut Shagrithaya's salary to $300,000 claiming his duties did not warrant executive compensation. Efforts to divest Shagrithaya of his interest in the corporation began. Several options were explored; including a repurchase by Argo and purchases by various third party purchasers. Each plan was rejected, some by Martin and some by Shagrithaya.

In 2007, an IRS protest included indications that the company was retaining earnings as early as 2003 anticipating a possible repurchase of Shagrithaya's shares. Shagrithaya was unaware at the time of the IRS protest and that retained earnings were a likely source for funds of a potential repurchase of his shares.

In 2007 and 2008, the board issued a dividends of $250,000 and $25 million respectively, both of which were distributed proportionately.

No resolution regarding salaries or divestiture options was reached.

SUMMARY OF ARGUMENT

Max Martin, and therefore Argo, did not act oppressively towards Balkrishna Shagrithaya, the lone minority shareholder by suppressing dividends. Because Martin's actions did not constitute an abuse of authority with intent to harm Shagrithaya's interest to the detriment of the corporation, they did not constitute minority shareholder oppression.

Testimony at trial indicated there was no agreement that salaries for Martin and Shagrithaya would remain equal. Since no contract existed regarding salaries, Martin was not in breach of contract when he reduced Shagrithaya's salary.

The trial court erroneously ruled that Martin, and therefore Argo, committed minority shareholder oppression and breach of contract. That judgment should be reversed and Shagrithaya should receive no relief on either claim.

ARGUMENT

I

This Court should reverse the trial court's judgment in favor of Respondent and should instead find that there was no minority shareholder oppression of Respondent.

The construction of a statute is a question of law that is decided by the court. *R.R. Comm'n of Tex. V. Tex. Citizens for a Safe Future & Clean Water*, 336 S.W.3d 619, 624 (Tex.2011). When reviewing an appeal, questions of law are to be decided de novo. *Id.*

Argo did not commit minority shareholder oppression when it withheld dividends.

In Texas:

> … a court that has jurisdiction over the property and business of a domestic entity under Section 11.402(b) may appoint a receiver for the entity's property and business if (1) in an action by an owner or member of the domestic entity, it is established that … (C) the actions of the governing persons of the entity are illegal, oppressive, or fraudulent …

Tex. Bus. Orgs. Code Ann. § 11.404 (West).

Subsection C allows a remedy if the actions of the controlling body of a corporation are oppressive. The statute, however, does not define "oppressive." The Texas Supreme Court recently redefined the term and found that a corporation's controlling body engages in oppressive conduct "when they abuse their authority over the corporation with the intent to harm the interests of one or more of the shareholders, in a manner that does not comport with the honest exercise of

their business judgment, and by doing so create a serious risk of harm to the corporation." *Ritchie v. Rupe*, 443 S.W.3d 856, 871 (Tex. 2014).

The Supreme Court's definition of oppressive conduct requires an "abuse of authority over the corporation." *Ritchie v. Rupe*, 443 S.W.3d 856, at 871 (Tex. 2014). Texas law allows, but does not require, the board of directors to authorize a distribution of earnings. Tex. Bus. Orgs. Code Ann. § 21.302 (West). The decision to retain earnings or issue dividends falls within the purview of a board of directors' business judgment. When the Court redefined "oppressive", it "emphasized the 'business judgment' test as capturing the legislative effect of shareholder oppression under the Statute." Jill Yaziji, *The Texas Supreme Court Revises the Definition and Remedies of Shareholder Oppression*, 52-OCT Hous. Law., 42 (2014). "The business judgment rule is a basic principle of corporate law that precludes courts from interfering with the discretion of the directors in operating the company." 20A *Tex. Prac., Business Organizations* § 36:5 (3d ed.). "Examples of acts which may fall within the directors' discretion under the business judgment rule include: (2) deciding whether to pay, and the amount of dividends…" *Id*. Martin's decision to retain earnings is consistent with the business judgment rule. Thus, the decision to suppress dividends did not constitute an "abuse of power."

Additionally, Shagrithaya testified that when he and Martin formed Argo, their plan was to grow the company by retaining earnings and reap the return on their investment by selling the company at some point in the future. By doing so, Shagrithaya concedes that the decision to retain earnings is consistent with the "honest exercise of business judgment."

The new definition of "oppressive" requires an "intent to harm the interests of one or more of the shareholders." *Ritchie v. Rupe*, 443 S.W.3d 856, at 871 (Tex. 2014). Although Martin and Shagrithaya planned to retain earnings, evidence presented at trial indicates that by the end of 2008, dividends exceeding $25 million had been issued which were distributed to all shareholders proportionately to their ownership of the company. So, to the extent that Martin received dividends, so too did Shagrithaya and to the extent that Shagrithaya's dividends were suppressed, so too were Martin's. "Actions that uniformly affect all shareholders typically will not satisfy this aspect of the term's meaning because, collectively, the shareholders of a business are not at the mercy of the business's directors." *Ritchie v. Rupe*, 443 S.W.3d 856, 871 (Tex. 2014). Therefore,

Martin's suppression of dividends was not done with "intent to harm the interests of one or more of the shareholders."

As mentioned before, retention of earnings is an option available to the governing body of a corporation. Tex. Bus. Orgs. Code Ann. § 21.302 (West). Retaining earnings rather than distributing them in the form of a dividend leaves more cash available to the company, increasing the overall strength and position of the corporation. Therefore, Martin's decision to retain earnings did not "create a serious risk of harm to the corporation."

In summary, Martin did not commit minority shareholder oppression when he suppressed dividends because retaining earnings was an honest exercise of business judgment, not an abuse of power, was applied to all shareholders equally, and did not create a serious risk of harm to the corporation. The district court's judgment that Martin's suppression of dividends constituted minority shareholder oppression should be reversed.

ARGUMENT

II

This Court should reverse the trial court's judgment in favor of Respondent and should instead find that there was no breach of contract by Appellant.

In reviewing a verdict for legal sufficiency, this court credits evidence that supports the verdict if reasonable jurors could, and disregards contrary evidence unless reasonable jurors could not. *Kroger Texas Ltd. P'ship v. Suberu*, 216 S.W.3d 788, 793 (Tex. 2006). A challenge to the legal sufficiency of evidence is successful when the evidence offered to establish a vital fact does not exceed a scintilla. *Id*. "Evidence does not exceed a scintilla if it is so weak as to do no more than create a mere surmise or suspicion that the fact exists." *Id.*

There was legally insufficient evidence to prove the existence of an implied contract between the parties to maintain equal salaries.

When Martin reduced Shagrithaya's salary, over his objection, he did not breach a contract requiring that their salaries would remain equal because there was no such contract. "The element of mutual intent to contract or actual assent is an essential element of a contract implied in fact just

as in the case of an express contract." 14 Tex. Jur. 3d *Contracts* § 11 (2013). "To constitute a contract, the minds of the parties must meet with respect to the subject matter of the agreement, and as to all of its essential terms." *Effel v. McGarry*, 339 S.W.3d 789, at 792 (Tex.App.-Dallas 2011), citing *Finley v. Hundley*, 252 S.W.2d 958, at 962 (Tex.Civ.App.-Dallas 1952, no writ).

At trial, Shagrithaya conceded that he never had any discussions with Martin about compensation when Argo was formed and that he made no oral or written agreements with Martin regarding salaries. No evidence of a contract was admitted at trial. The sole basis of Shagrithaya's contract claim is that, once he and Martin began receiving compensation from Argo, they voted each year as board members to receive the same amount. The simple fact that a party has consistently done something in the past does not, standing alone, demonstrate an agreement to continue performing the same act in the future.

In summary, Shagrithaya admitted that there was no agreement, or even any discussion, regarding their compensation and the only evidence submitted fails to exceed a scintilla. Because there was no agreement that Martin and Shagrithaya would maintain equal salaries, the district court's judgment that Martin was in breach of contract when he reduced Shagrithaya's salary should be reversed.

CONCLUSION

Argo Data Resource Corporation and Max Martin respectfully request this Court to vacate the district court's judgment in favor of Mr. Shagrithaya and render judgment that Shagrithaya take nothing by his claims.

Dated: _____

Respectfully submitted,

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