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Get Involved: Second Department Upholds Denial of Passive Shareholder's Judicial Dissolution Claim

One of the most common disputes we encounter as commercial litigators is thebusiness divorce. This occurs when shareholders of a closely held corporation, – often family members, suffer a total relationship breakdown and can no longer own a business together. In these cases, one potential avenue of relief is New York's Business Corporation Law Section 1104-a, which authorizes minority shareholders to seek judicial dissolution of a closely held corporation. To succeed on a Section 1104-a claim, the minority shareholder must demonstrate that the controlling shareholders have engaged in,*inter alia*, "oppressive actions." A recent decision by the Appellate Division, Second Department examines the availability of Section 1104-a relief for a passive shareholder who has not been involved in the company business but one day wakes up and claims dissatisfaction with the majority's operations.

The Case: ***In the Matter of Hoffman v. S.T.H.M. Realty Corp.***

The appeal arose out of a bench trial in New York Supreme, Kings County involving three family-owned real estate companies controlled equally by four individuals: the petitioner, her brother and two cousins. The record evidence showed the petitioner "did not seek employment or responsibilities in the day-to-day management of the corporations, or express an interest in shareholders' meetings," but instead remained a passive shareholder for years. When the petitioner finally decided to get involved, the majority shareholders rejected her demand for the corporation to sell its real estate holdings. The petitioner then filed suit under BCL 1104-a and the trial court dismissed the actions, finding "[n]o credible evidence" of the allegations, and holding that, "New York law permits the three (3) shareholders controlling 75% of the shares to block the remaining shareholder, with whom they profoundly disagree, from corporate management."

On appeal, the Appellate Division Second Department affirmed, holding, "oppression should be deemed to arise only when the majority conduct substantially defeats expectations that, objectively viewed, were both reasonable under the circumstances and were central to the petitioner's decision to join the venture." Because "the petitioner did not evince a reasonable expectation of actively participating in the management of the corporations," "while the petitioner might now disagree with the manner in which the corporations' assets are being managed, the conduct of the majority shareholders was not oppressive."

Takeaway

BCL 1104-a can offer important protection to minority shareholders of closely held corporations that are dominated by the decision-making power of a malfeasant majority. But that protection is only available if that minority shareholder has actively participated (or attempted to participate) in the corporation's governance. Shareholders who sit idly do so at their peril should they one day seek to dissolve the corporation on grounds of majority oppression.