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When a shareholder dispute results in the judicial dissolution of the company

Despite its prominence, the issue of how to manage a potential dispute among shareholders or blocks of shareholders during the company's life is rarely anticipated. Yet, such a situation, quite common nowadays, can have major implications and even entail, in case of paralysis of the business, the dissolution of the company.

This is precisely what has been recently recalled by the *Cour de Cassation*[1] (French Supreme Court) in a case where, after having found that the dispute between the two equal blocks of shareholders of a holding company jeopardized the survival of the entire group, it ordered the judicial dissolution of the holding company and its subsidiary.

In the commented case, the capital of the company *Saumuroise de participations* was majority-owned by the company *Les Terres Froides*, itself owned in equal parts by two blocks of shareholders members of the same family (hereinafter "block A" and "block B").

Because of major disagreements between the two blocks of shareholders, a court officer was appointed in 2008 to serve as mediator. An agreement was reached in July 2009 and the mediation continued.

Arguing that the dispute between the shareholders had entailed, despite the aforementioned agreement and the mediation procedure, a paralysis in the running of *Les Terres Froides* and, consequently, of *Saumuroise de participations*, a member of the Block A petitioned the Court for the dissolution of these companies, as per Article 1844-7, 5 of the French Civil Code[2].

Two Block B shareholders opposed the request for dissolution and put forth the following arguments:

- The renewal of the members of the companies' corporate bodies through the appointment of external members, in order to resume the operation of said companies and promote the search for a potential acquirer of the whole group;
- The resumption of the normal operation of the corporate bodies of both companies, as notably attested to by the minutes of general meetings and Executive Board meetings held since 2009, despites the

temporary suspension of the aforementioned contemplated sale.

The *Cour de Cassation* rejected the appeal of the two Block B shareholders and confirmed the judgment of the Grenoble Court of Appeals[3] that had ordered the dissolution of the two companies, after having pointed out that:

- The failure of the mediation procedure had showed that the terms of the 2009 agreement were not, or no longer, enforceable;
- The fact that the conflicting shareholders, each on their own and on behalf of both companies, had filed submissions before the Court of Appeals revealed the persistence of two antagonistic blocks;
- The discussions on corporate governance held at the end of 2010 and at the beginning of 2011, showed that disagreements remain and that this deadlock situation concerning the shareholding structure "*had the effect of jeopardizing the survival of the group*".

This decision confirms the need for designing, at the time the company is incorporated, adequate contractual mechanisms that would apply in the event of a deadlock situation. Such mechanisms, stipulated in a shareholders' agreement, can take the form of unilateral promises to sell/buy, exclusion/withdrawal clauses, or so-called "buy or sell" clauses.

The "*buy or sell*" clause (also referred to as alternative offer clause, Texan clause or even "shot-gun" clause) remains the most suitable solution in the presence of two antagonistic blocks of shareholders, like in the commented case.

The implementation of a "buy or sell" clause is quite simple:

In a crisis situation (that must be defined very precisely), one of the shareholders or blocks of shareholders may offer to acquire the shares of the other shareholder or block of shareholders at a specific price per share that is most of the time determined by applying a pre-agreed calculation formula. The other shareholder or block of shareholders may then either (i) accept the offer and sell the shares in the conditions set forth therein, or (ii) refuse the offer and buy the offering shareholder's or block of shareholders' shares at the determined price per share.

This type of clause, because of its effects and its uncertain outcome, has the merit of "provoking" amicable negotiations and is a simple method for settling disputes between equal shareholders or blocks of shareholders.

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[1] Commercial Chamber of the *Cour de Cassation*, October 9, 2012, n° 11-21.761, n° 989 F-D.

[2] "*The company shall be terminated:* […]

5° By way of early dissolution ordered by the Court at the request of a shareholder and for legitimate reasons, in particular in case of […] *a dispute between shareholders that paralyses the running of the company."*

[3] Court of Appeals of Grenoble, March 31, 2011