

Lawyer Insights

Limited Partner's Standing: New Texas Supreme Court Ruling

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In June 2020, the Texas Supreme Court clarified whether a limited partner has constitutional standing to sue and seek damages individually for injuries to the value of the partnership. *Pike v. Tex. EMC Mgmt., LLC*, 17-0557, 2020 WL 3405812 (Tex. June 19, 2020). The case signals a shift from Texas precedent and is destined to impact partnership disputes in the future.

In *Pike*, EMC Cement BV (EMC), a limited partner, obtained a \$7 million damage award for the other partners' (collectively, Walker) breach of the partnership agreement. On appeal, Walker challenged the award, claiming EMC lacked standing to recover damages because Walker's breach caused harm to the partnership and not to EMC. According to Walker, the partnership was the only party that could maintain a cause of action for breach.

For years, defendants relied on the Texas Supreme Court's decision in *Wingate v. Hajdik*, 795 S.W.2d 717 (Tex. 1990) to halt individual partners from asserting claims for injuries suffered by the partnership. In *Wingate*, the court explained that stockholders lack standing to maintain suit or recover for wrongs done solely to the corporation. Courts have applied the same logic in partnership disputes. Several Texas appellate courts, relying on the so-called "*Wingate* prohibition," held that limited partners did not have an individual right to sue for the diminished value of their ownership interests in the partnership.

Wingate and its progeny allowed courts to block at the outset of the lawsuit a limited partner's attempt to recover damages for harm suffered by the partnership. Defendants typically argued that limited partners had no standing to recover for the diminished value of his or her interest in the partnership because the partnership suffered the harm. Further, defendants claimed that, even though partners may have been injured by the diminished value to his or her interest, they would be made whole if the partnership recovered compensation for the wrong.

Looking to federal case law and the Texas partnership statutes, the *Pike* court addressed whether the "*Wingate* prohibition" implicates a constitutional standing issue and requires courts to find a limited partner lacks standing for harm suffered by the partnership. The court held it did not, finding that "a partner or other stakeholder in a business organization has constitutional standing to sue for an alleged loss in the value of its interest in the organization." In the majority's view, *Wingate* does not implicate a court's subject matter jurisdiction, and partners' or stakeholders' claims should be decided on the merits. This holding departs from decades of Texas jurisprudence interpreting the "*Wingate* prohibition."

Justice Bland vehemently disagreed with the majority. She remarked that the court's holding allows a limited partner to circumvent the partnership, and despite lacking personal injury, recover directly for the partnership's injury. In her mind, the court blurred the basic principal that entities are separate from their individual partners. The court also ignored the derivative standing rights the Texas Business

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Organizations Code affords limited partners by allowing them to bring a claim on behalf of the partnership. Further, she cited Texas precedent finding that the “standing inquiry begins with determining whether the plaintiff has *personally* been injured” and a reduction in value to the partnership constitutes an injury to the partnership, not its limited partners. According to Justice Bland, EMC had no standing to bring a claim for a reduction in the value of the partnership and the court should have dismissed its claim for lack of jurisdiction.

Pike may trigger a potential flood of litigation by limited partners seeking individual redress for the lost value of interests in a partnership. Trial courts may no longer dismiss a limited partner's claim on standing grounds. The “*Wingate* prohibition” appears to have lost its teeth because limited partners can individually assert claims without fear of swift dismissal. Limited partners now have the ability to engage in motion practice and attempt to establish the merits of the case. At a minimum, defendants will likely incur more costs in fending off such claims.

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