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# CORPORATIONS AND PARTNERSHIPS

by

Barbara Bader Aldave\*

**D**URING the survey period the Texas courts decided a number of cases that raised important issues concerning partnerships, limited partnerships, and corporations. There were also many significant developments, both state and federal, in the law of securities regulation. These cases and developments are discussed in this Article.

## I. PARTNERSHIPS

*Elements of Partnerships and Joint Ventures.* The Texas courts are frequently asked to decide whether two or more persons are or are not co-partners or joint venturers. Section 6 of the Texas Uniform Partnership Act (TUPA)<sup>1</sup> defines a "partnership" as "an association of two or more persons to carry on as co-owners a business for profit."<sup>2</sup> Because the governing definition is broad, and because important consequences attach to the conclusion that persons are partners, it is hardly surprising that there is a great deal of litigation to determine whether particular business relationships constitute partnerships.

In deciding whether a partnership has been created, a Texas court should be guided by the rules set out in section 7 of the TUPA.<sup>3</sup> Section 7 stresses the critical importance of profit-sharing. Except in enumerated circumstances, "[t]he receipt by a person of a share of the profits of a business is prima facie evidence that he is a partner in the business."<sup>4</sup> On the other hand, section 7 says nothing about the sharing of losses. Profit-sharing is an essential element of business co-ownership, and thus of partnership,<sup>5</sup> but loss-sharing is not.<sup>6</sup>

Because a "joint venture" is simply a partnership formed for a limited

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1. TEX. REV. CIV. STAT. ANN. art. 6132b (Vernon 1970).

2. *Id.* § 6(1).

3. *Id.* § 7 (rules for determining the existence of a partnership).

4. *Id.* § 7(4). No such inference is to be drawn when the profits of a business are received in the following circumstances: (1) as payment of a debt; (2) as wages of an employee or rent to a landlord; (3) as an annuity to a widow or representative of a deceased partner; (4) as interest on a loan; or (5) as consideration for the sale of the goodwill of a business or other property by installments or otherwise. *Id.*

5. A. BROMBERG, CRANE AND BROMBERG ON PARTNERSHIP §§ 14(a)-(b) (1968).

6. *See id.* § 14(e). One of the usual consequences of a finding that a partnership exists is that each partner will be required to contribute toward the losses of the business, but the partners may agree to allocate the losses among themselves as they wish. *Id.*; *see* TEX. REV. CIV. STAT. ANN. art. 6132b, § 18(1) (Vernon 1964).

purpose,<sup>7</sup> section 7 of the TUPA provides an appropriate mode of analysis for determining the existence of a joint venture. However, Texas courts seldom refer to section 7 when deciding whether particular persons are joint venturers. More often, they invoke a four-part formula that sets forth the following as the "essential elements" of a joint venture: (1) a community of interest in the venture, (2) an agreement to share profits, (3) an agreement to share losses, and (4) a mutual right of control or management of the enterprise.<sup>8</sup> The Texas Supreme Court reiterated and applied this formula in *Coastal Plains Development Corp. v. Micrea, Inc.*<sup>9</sup>

Micrea, Inc. brought suit against Coastal Plains Development Corporation for breach of a contract concerning the development and sale of subdivision lots. Under the contract, Coastal Plains was to subdivide and plat a tract that it owned and have roads built on it, while Micrea was to conduct a promotion campaign and sell the lots. The parties agreed that all contracts pertaining to the development were to be approved and executed jointly, and that the net profits were to be divided equally. They also agreed that the performance of their respective obligations would not constitute them partners or joint venturers.<sup>10</sup> In its action against Coastal Plains, Micrea argued that the two companies had been engaged in a joint venture despite the contrary expression of intent in their contract.<sup>11</sup> The Texas Supreme Court, however, rejected Micrea's argument. The court found that the contract between the parties "did not have any agreement for sharing the losses,"<sup>12</sup> and insisted that such an agreement is an essential element of a joint venture.<sup>13</sup>

In *Micrea* the court appears to have asked the wrong question, and then to have given the wrong answer to the question it asked. An express agreement to share losses should not be regarded as an essential element of a joint venture.<sup>14</sup> Because they are likely to be optimistic about the prospects of their business, co-partners and joint venturers may overlook the possibility that their enterprise will prove unsuccessful, and therefore neglect to provide for the allocation of losses.<sup>15</sup> In any event, Micrea and Coastal Plains *had* expressly provided for the allocation of losses, or unrecovered costs: Coastal Plains was to bear the ultimate burden of them.<sup>16</sup> In its decision the supreme court emphasized that Coastal Plains was

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7. See generally A. BROMBERG, *supra* note 5, § 35; 19 R. HAMILTON, TEXAS PRACTICE: BUSINESS ORGANIZATIONS § 4 (1973).

8. See, e.g., *Chandler v. Herndon*, 450 S.W.2d 703, 706 (Tex. Civ. App.—Corpus Christi 1970, writ ref'd n.r.e.).

9. 572 S.W.2d 285 (Tex. 1978).

10. *Id.* at 286-87.

11. Micrea contended that the contractual provisions requiring an equal division of the profits and joint approval and execution of all contracts, along with certain advertising material that stated that the project was a joint venture between the parties, established the existence of a joint venture. *Id.* at 288.

12. *Id.*

13. *Id.*

14. A. BROMBERG, *supra* note 5, § 35.

15. *Id.* § 14(e).

16. 572 S.W.2d at 288.

solely responsible for the costs of road construction, and was obliged to reimburse Micrea for the costs of advertising and selling, but these facts do not lead to the conclusion that the parties were not joint venturers. Rather, the parties had entered into a specific agreement respecting the allocation of costs, or losses, as permitted by the TUPA.<sup>17</sup>

Perhaps the court's reluctance to find that the parties in *Micrea* were joint venturers simply reflected a policy of strict enforcement of the Real Estate License Act (RELA),<sup>18</sup> which prohibits suits for compensation for enumerated kinds of services by a person or company not duly licensed as a real estate broker or salesman.<sup>19</sup> The Beaumont court of civil appeals had held that Micrea and Coastal Plains were joint venturers, so that Micrea did not have to prove that it was a licensed broker in order to recover damages for Coastal Plains' breach of contract, because a person or company need not have a license to sell his or its own land.<sup>20</sup> The lower court may or may not have been correct in concluding that transactions between joint venturers are exempt from the requirements of the RELA. If the supreme court disapproved of the lower court's construction of the RELA, however, it should have reversed on that ground, instead of holding that an agreement to share losses is an essential element of a joint venture.

The *Micrea* decision was cited and followed in *Raybourn v. Lewis*.<sup>21</sup> Raybourn brought suit against Lewis and others for breach of an oral contract under which Raybourn had acted as a real estate advisor to the defendants. According to Raybourn, the contract provided that he was to receive a fixed salary plus ten percent of the profits earned from the parties' purchase, development, and sale of real estate. The court of civil appeals affirmed a judgment for the defendants on the ground that the provisions of the RELA precluded Raybourn, who did not hold a license to sell real estate, from recovering any compensation for his services.<sup>22</sup> In

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17. See TEX. REV. CIV. STAT. ANN. art. 6132b, § 18(1) (Vernon 1970). Although § 18(1) permits the allocation of costs or losses as between partners, *id.* § 15 provides that all partners are jointly and severally liable for all partnership obligations. Thus, even though a partnership agreement between *A* and *B* allocates all costs to *A*, *B* may still be held liable for those costs to third parties. Of course, *B* can compel the partnership or *A* to reimburse him pursuant to the partnership agreement.

18. *Id.* art. 6573a (Vernon 1969).

19. In 1975 the regular session of the 64th Legislature substantially amended the RELA. See 1975 Tex. Gen. Laws ch. 216, § 20, at 549. The *Micrea* case was governed by the predecessor of § 20(a) of the amended RELA. Section 20(a), which is substantially the same as its predecessor, provides as follows:

A person may not bring or maintain an action for the collection of compensation for the performance in this state of an act set forth in Section 2 of this Act without alleging and proving that the person performing the brokerage services was a duly licensed real estate broker or salesman at the time the alleged services were commenced, or was a duly licensed attorney at law in this state or in any other state.

TEX. REV. CIV. STAT. ANN. art. 6573a, § 20(a) (Vernon Supp. 1978-79).

20. Coastal Plains Dev. Corp. v. Micrea, Inc., 553 S.W.2d 816, 818 (Tex. Civ. App.—Beaumont 1977), *rev'd*, 572 S.W.2d 285 (Tex. 1978).

21. 567 S.W.2d 908, 911 (Tex. Civ. App.—San Antonio 1978, writ *ref'd n.r.e.*).

22. *Id.* at 912.

answer to Raybourn's argument that he had been engaged in a partnership or joint venture with the defendants, the court cited *Micrea* and listed the four "essential elements" of a joint venture.<sup>23</sup> While the court acknowledged that there was some evidence of an intent to share profits, it stressed that there was no evidence of an agreement to share losses,<sup>24</sup> and noted that there had been testimony that control was solely in the defendants.<sup>25</sup> On this record, the court bluntly concluded that "[t]here is no evidence whatsoever establishing a joint venture or partnership."<sup>26</sup>

The pre-*Micrea* decision of *Heinrich v. Wharton County Livestock, Inc.*<sup>27</sup> also listed an "agreement to share losses, costs or expenses" as one of the four essential elements of a joint venture.<sup>28</sup> Nevertheless, without referring to any evidence of a loss-sharing agreement between the parties in the case before it, the court concluded that they were joint venturers.<sup>29</sup> Under a "working agreement," Truchard was to purchase, pasture, and care for some cattle, while Heinrich was to provide the funds necessary to pay for the cattle. When the cattle were sold, the profits were to be divided equally between the parties. In furtherance of the venture, Truchard purchased some cattle at an auction with a series of drafts, and promptly resold the cattle to Heinrich. However, the drafts given by Truchard were dishonored, and the auction company repossessed the cattle. Heinrich then sued the auction company to recover the value of the cattle. In a well-reasoned opinion, the court affirmed a judgment for the auction company. Truchard had known that his drafts would be dishonored when he bought the cattle from the auction company and when he resold them to Heinrich. Because Truchard and Heinrich were joint venturers, Truchard's knowledge was imputed to Heinrich, and Heinrich could not claim the status of a bona fide purchaser.<sup>30</sup>

While some Texas courts invoke a questionable formula to determine whether a partnership or joint venture has been created, other courts fail to make clear just what legal standards they apply. For example, in *Nueces Trust Co. v. White*<sup>31</sup> one of the central issues was whether a person who had used an automobile as security for a loan, and had delivered the ownership papers for the automobile to the lender, was a partner in the company that was the registered owner of the car. The court acknowledged that there was a conflict in the testimony as to whether the borrower was a partner in the company or had authority to use the car as collateral, but ultimately treated the questions as issues of fact that had been resolved by

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23. *Id.* at 911; see text accompanying note 8 *supra*.

24. *Id.*

25. *Id.* A mutual right of control is one of the essential elements of a joint venture. See text accompanying note 8 *supra*.

26. 567 S.W.2d at 912.

27. 557 S.W.2d 830 (Tex. Civ. App.—Corpus Christi 1977, writ ref'd n.r.e.).

28. *Id.* at 833.

29. *Id.*

30. *Id.* at 834.

31. 564 S.W.2d 798 (Tex. Civ. App.—Corpus Christi 1978, no writ).

the trial judge.<sup>32</sup> An award of damages against the lending institution for the wrongful withholding of the ownership papers was affirmed.

During the survey period there was one case in which the Texas Supreme Court relied in part on the provisions of section 7 of the TUPA<sup>33</sup> in concluding that no partnership had been created. In *Rankin v. Naftalis*<sup>34</sup> the plaintiffs sought to impress a constructive trust on an oil and gas lease that Rankin had taken in his own name. Rankin and the plaintiffs had jointly engaged in the business of operating the "Melton" oil and gas lease. After the completion of the first well on the Melton lease, Rankin bought another lease, the "Orsak" lease, with his own funds. A well on the Orsak lease proved to be a producer, and the plaintiffs sought to share in its production. The plaintiffs based their claim to an interest in the Orsak lease and well on the theory that Rankin had violated his fiduciary duties to them as joint venturers when he acquired the lease for his own benefit. The court held, however, that the fiduciary duties that Rankin owed to the plaintiffs extended only to dealings within the scope of their joint venture, which embraced only the development of the original Melton lease.<sup>35</sup> The court also rejected the argument that the plaintiffs and Rankin had entered into "a broader partnership arrangement."<sup>36</sup> The plaintiffs had proved no more than the type of arrangement described in section 7(5) of the TUPA, which provides that "[o]peration of a mineral property under a joint operating agreement does not of itself establish a partnership."<sup>37</sup>

*Arbitration Agreements.* In *Wydel Associates v. Thermasol, Ltd.*<sup>38</sup> a federal district court was called upon to decide the operative scope of TUPA section 9(3)(e),<sup>39</sup> which no prior case had construed.<sup>40</sup> Wydel Associates, a Texas partnership, sued a Delaware corporation for breach of contract and deceptive trade practices. The contract upon which the suit was brought provided that all disputes relating to the contract were to be decided by arbitration in the State of New York. The plaintiff partnership argued that it was not bound by the arbitration clause because the contract containing it had been executed by a single partner, while section 9(3)(e) requires the unanimous authorization of the partners to "submit a partnership claim or liability to arbitration or reference."<sup>41</sup> The court assumed, for purposes of argument, that section 9(3)(e) limits the authority of partners to agree to

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32. *Id.* at 806.

33. TEX. REV. CIV. STAT. ANN. art. 6132b, § 7 (Vernon 1970).

34. 557 S.W.2d 940 (Tex. 1977).

35. *Id.* at 944.

36. *Id.* at 945.

37. TEX. REV. CIV. STAT. ANN. art. 6132b, § 7(5) (Vernon 1970).

38. 452 F. Supp. 739 (W.D. Tex. 1978).

39. TEX. REV. CIV. STAT. ANN. art. 6132b, § 9(3)(e) (Vernon 1970). This section provides as follows: "Unless authorized by the other partners or unless they have abandoned the business, one or more but less than all the partners have no authority to . . . [s]ubmit a partnership claim or liability to arbitration or reference."

40. 452 F. Supp. at 739, 741, 742.

41. TEX. REV. CIV. STAT. ANN. art. 6132b, § 9(3)(e) (Vernon 1970).

arbitrate future disputes,<sup>42</sup> but nevertheless concluded that the partnership was bound by the arbitration clause.<sup>43</sup> First, the court held that the Federal Arbitration Act,<sup>44</sup> which validates arbitration provisions in contracts concerning transactions involving interstate commerce,<sup>45</sup> overcame the effect of section 9(3)(e).<sup>46</sup> The court reasoned that in cases covered by the federal act, it was not "bound to apply those state statutes which limit arbitration agreements with rules not applicable to other contracts."<sup>47</sup> Second, the court held that the plaintiff partnership had ratified the entire contract, including the arbitration clause, by accepting benefits under the contract and bringing suit upon it.<sup>48</sup>

*Dissolution and Its Consequences.* Two cases decided during the survey period dealt with questions regarding the rights and duties that arise upon the withdrawal of a partner from a partnership. Pursuant to section 29 of the TUPA,<sup>49</sup> which defines a dissolution as "the change in the relation of the partners caused by any partner ceasing to be associated in the carrying on as distinguished from the winding up of the business,"<sup>50</sup> the actual withdrawal of a partner causes a technical "dissolution" of a partnership. A dissolution of a partnership, however, does not necessarily entail a termination of the business. The partnership agreement may provide that some or all of the remaining partners will have the right to continue the business after a dissolution.<sup>51</sup> In addition, when a dissolution is caused in contravention of the partnership agreement, the TUPA permits all the partners who were not responsible for the dissolution to continue the business under specified conditions.<sup>52</sup> Even if the business is to terminate, the partnership will continue to exist until the "winding up" of its affairs has been completed.<sup>53</sup>

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42. 452 F. Supp. at 741-42.

43. *Id.*

44. 9 U.S.C. §§ 1-14 (1976).

45. *Id.* § 2. This section provides as follows:

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

46. 452 F. Supp. at 742.

47. *Id.* See *Collins Radio Co. v. Ex-Cell-O Corp.*, 467 F.2d 995, 998 (8th Cir. 1972).

48. 452 F. Supp. at 742.

49. TEX. REV. CIV. STAT. ANN. art. 6132b, § 29 (Vernon 1970).

50. *Id.*

51. 19 R. HAMILTON, *supra* note 7, § 188.

52. TEX. REV. CIV. STAT. ANN. art. 6132b, § 38(2)(b) (Vernon 1970). This section allows the nonresponsible partners to possess partnership property for purposes of carrying on the business as long as they secure payment by a bond approved by the court, or pay any party causing the dissolution the value of his interest in the partnership at the time of dissolution less damages for the breach of the agreement, and indemnify the dissolution-causing party against all present and future partnership liabilities.

53. *Id.* §§ 29-30.

*Woodruff v. Bryant*<sup>54</sup> involved a determination of whether and when a particular partnership had been dissolved. At one time the plaintiffs and Lillie Bryant were all partners in the Flour Bluff Finance Company, which was managed by Bryant. In 1971, a dispute arose between Bryant and the other partners, and she wrote them a letter in which she tendered her resignation as company manager and offered to sell her partnership interest. The other partners did not respond to the letter. Bryant left her employment with the company, but continued to receive her share of the partnership profits. In 1972 Bryant became the manager of a competing loan company. The other partners in Flour Bluff sued Bryant for breach of her fiduciary duty to refrain from engaging in a competing business, and she cross-claimed for her share of the partnership assets. The jury found that Bryant had intended to dissolve the partnership on the date of her letter to the other partners, and that she had ceased to be associated with the partnership prior to her association with its competitor. The trial court then entered judgment against the plaintiffs on their cause of action, and for Bryant on her cross-claim.

The court of civil appeals held that there was insufficient evidence to support the critical findings of the jury.<sup>55</sup> While recognizing that any partner has the power to dissolve a partnership at any time,<sup>56</sup> the court noted that Bryant had participated in the partnership business to the same extent as the other "silent partners" after her resignation as manager, and that she had still considered herself a partner at the time of trial.<sup>57</sup> The case was remanded for a reconsideration of whether Bryant had breached her fiduciary duties by her employment with the competing business, and for a redetermination of the value of her partnership interest at the date of the actual dissolution of the finance company.<sup>58</sup>

*Ordway-Saunders Co. v. Little*<sup>59</sup> illustrates the value of including in a partnership agreement a carefully drafted section defining the rights of a withdrawing partner. The agreement in this case provided that when a partner withdrew from the partnership, his interest in "the assets, records, business and all other property"<sup>60</sup> of the partnership would become the property of the partnership, and that he would receive in exchange for his interest the amount of his capital account, as reflected on the books of the

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54. 558 S.W.2d 535 (Tex. Civ. App.—Corpus Christi 1977, writ ref'd n.r.e.).

55. *Id.* at 542.

56. The court stated that the TUPA "codifies the common law rule so that every partner has the inherent *power* to dissolve his partnership even though the partnership agreement might attempt to limit that partner's *right* to dissolve the partnership." *Id.* at 539 (emphasis added).

57. Since its inception, the partnership had had a managing partner and two or three silent partners who participated by voting only when management decisions were necessary. The managing partner testified that he did not discuss partnership business with any of the silent partners during the period in question. Also, Bryant testified at trial that she was still a partner of Flour Bluff Finance Co. and had not sold her partnership interest. *Id.* at 541.

58. *Id.* at 544.

59. 568 S.W.2d 711 (Tex. Civ. App.—Amarillo 1978, writ ref'd n.r.e.).

60. *Id.* at 713.



partnership, plus his allocable share of profits and salary.<sup>61</sup> When the plaintiff withdrew from the partnership, he received a payment which he regarded as insufficient, and brought suit for an additional sum. The plaintiff conceded that the amount that he had been paid was correct according to the partnership books, but he insisted that his capital account was understated because it reflected only the cost and not the market value of certain assets and included no allowance for the value of good will. The Amarillo court of civil appeals held that the partnership agreement was unambiguous, and that the partnership's accounting procedures were consistent with generally accepted accounting principles.<sup>62</sup> The plaintiff had received the full payment to which he was entitled under the agreement, and he could not thereafter demand a greater amount from the partnership.<sup>63</sup>

*Procedure in Suits By or Against Partnerships.* In *Hammonds v. Holmes*<sup>64</sup> the Texas Supreme Court held that a judgment of dismissal with prejudice in a suit by two individuals for wrongful foreclosure of a deed of trust on their business property precluded a subsequent action against the same defendant by a partnership comprised of the same two individuals to redress the same wrong. Two weeks after the *Hammonds* opinion was issued, it was cited as dispositive of the question in *Corsicana Ready Mix v. Trinity Metroplex Division, General Portland, Inc.*<sup>65</sup> The *Corsicana Ready Mix* case held that a default judgment could not be entered against a partnership when each of the individual partners had filed an answer to the petition naming the partnership as defendant.<sup>66</sup> The court reasoned that "[s]ince res judicata bars a suit in the partnership name after the individual partners' suit on the same claim had been dismissed with prejudice, it logically follows that an answer for all of the individual partners is equivalent to an answer for the partnership."<sup>67</sup> Both of these decisions, refusing to elevate form over substance, seem entirely correct. Despite the outcome in *Corsicana Ready Mix*, however, a careful practitioner should file pleadings on behalf of the partnership itself, even though pleadings are also filed on behalf of the individual partners, whenever a petition names the partnership entity as a defendant.

## II. LIMITED PARTNERSHIPS

*Attorney General Opinion H-1229.* A major controversy concerning the law of limited partnerships was created during the survey period by an opinion of the Texas attorney general. The final portion of Opinion H-1229 concluded that a corporation may not serve as the sole general part-

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61. *Id.*

62. *Id.* at 718.

63. *Id.* at 719.

64. 559 S.W.2d 345 (Tex. 1977).

65. 559 S.W.2d 423 (Tex. Civ. App.—Dallas 1977, no writ).

66. *Id.* at 424.

67. *Id.*

ner of a Texas limited partnership.<sup>68</sup> One week after H-1229 was issued, its final portion was withdrawn "pending reconsideration."<sup>69</sup> The withdrawal, however, did not allay all the concerns raised by the original opinion. In order to assist practitioners in advising limited partnerships, five law professors published a letter that they had sent to the attorney general prior to the withdrawal of the last portion of H-1229.<sup>70</sup> The letter argued convincingly that a corporation may indeed serve as the sole general partner of a Texas limited partnership.

Opinion H-1229 contained another unsettling portion in which the attorney general read section 26 of the Texas Uniform Limited Partnership Act (TULPA)<sup>71</sup> as requiring the unanimous approval of the limited partners for any acts leading to amendment or cancellation of the limited partnership certificate.<sup>72</sup> If this interpretation were correct, section 26 would invalidate provisions in a limited partnership agreement for amendment of the certificate, or dissolution of the partnership, by a majority vote of the limited partners. The same five professors who published their objections to the now-withdrawn portion of H-1229 also published a detailed criticism of the opinion's conclusion that section 26 establishes a unanimity requirement.<sup>73</sup>

*Defective Formation of Limited Partnerships.* Two cases decided during the survey period examined the consequences of defects in the formation of a limited partnership. In *Voudouris v. Walter E. Heller & Co.*<sup>74</sup> a creditor sued the defendant on a debt incurred by a business in which the defendant had allegedly become a general partner. The defendant and his brother had entered into a limited partnership agreement under which the defendant was to be the limited partner and his brother the general partner in a carpet company. Neither the limited partnership agreement nor any certificate of limited partnership was ever filed with the Texas secretary of state.<sup>75</sup> The defendant cosigned and later paid a promissory note to obtain funds for the business, but he never participated in the management of the enterprise. The limited partnership agreement recited that the defendant was entitled to twenty percent of the profits of the business, but there was no evidence that any profits had actually been distributed to him. Upon discovering that his brother had not been paying the bills, the defendant gave up his interest in the partnership and obtained his brother's agree-

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68. TEX. ATT'Y GEN. OP. NO. H-1229 (1978).

69. *Id.* H-1229A.

70. Bromberg, Bateman, Hamilton, Lebowitz & Winship, *Corporate General Partners*, 16 TEX. ST. B. BULL. SECTION CORP., BANKING & BUS. L., No. 1, Sept. 1978, at 24.

71. TEX. REV. CIV. STAT. ANN. art. 6132a, § 26 (Vernon 1970).

72. TEX. ATT'Y GEN. OP. NO. H-1229 (1978).

73. Bromberg, Bateman, Hamilton, Lebowitz & Winship, *Unanimity Requirements in Limited Partnerships*, 16 TEX. ST. B. BULL. SECTION CORP., BANKING & BUS. L., No. 2, Dec. 1978, at 3.

74. 560 S.W.2d 202 (Tex. Civ. App.—Houston [1st Dist.] 1977, no writ).

75. Persons seeking to form a limited partnership are required by statute to file with the secretary of state a certificate that sets out specified information. See TEX. REV. CIV. STAT. ANN. art. 6132a, § 3 (Vernon 1970).

ment to indemnify him against liability. He also informed the creditors of the carpet company that he had sold his interest in the company and was no longer responsible for its debts.

In a rather disjointed opinion, the Houston court of civil appeals held that the defendant was not liable for the obligations of the carpet company. The court ruled that the limited partnership agreement never became effective because it was never filed with the secretary of state,<sup>76</sup> but concluded that the failure to file the agreement did not result in the formation of a general partnership.<sup>77</sup> The court emphasized that the brothers had not intended to enter into a general partnership, and that the defendant had not taken part in the management and control of the business.<sup>78</sup> In addition, the court held that the defendant had "renounced the partnership" immediately upon learning that the partnership agreement had not been filed, so that section 12 of the TULPA prevented the imposition of liability.<sup>79</sup> The provisions of this section seem fully to support the result in the case.

The subsequent case, *Garrett v. Koepke*,<sup>80</sup> decided by the Dallas court of civil appeals, goes substantially beyond *Voudouris* in protecting the ostensible limited partners in a defectively organized limited partnership. In *Garrett* the defendants had been designated as limited partners in a limited partnership agreement, but, as in *Voudouris*, neither the agreement nor any certificate of limited partnership had been filed with the secretary of state. The plaintiffs, who had entered into a contract with the ostensible limited partnership, argued that the failure to file the statutorily required certificate rendered the defendants liable as general partners. The court held, however, that since the plaintiffs "were on notice that the entity with which they were dealing was in fact a limited partnership,"<sup>81</sup> the defendants' failure to file a limited partnership certificate was "immaterial."<sup>82</sup> Reasoning that the purpose of the filing requirement is to provide third persons with notice of the essential features of the partnership arrangement, the court concluded that the plaintiffs "were in no way prejudiced by the failure to comply with the statute."<sup>83</sup> The court saw "no compelling policy reason"<sup>84</sup> for insisting upon "technical compliance with these notice

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76. 560 S.W.2d at 206.

77. *Id.* at 207.

78. *Id.* at 206.

79. *Id.* at 208. TEX. REV. CIV. STAT. ANN art. 6132a, § 12 (Vernon 1970) provides as follows:

A person who has contributed to the capital of a business conducted by a person or partnership erroneously believing that he has become a limited partner in a limited partnership, is not, by reason of his exercise of the right of a limited partner, a general partner with the person or in the partnership carrying on the business, or bound by the obligations of such person or partnership; provided that on ascertaining the mistake he promptly renounces his interest in the profits of the business, or other compensation by way of income.

80. 569 S.W.2d 568 (Tex. Civ. App.—Dallas 1978, writ ref'd n.r.e.).

81. *Id.* at 570.

82. *Id.*

83. *Id.*

84. *Id.*

provisions.”<sup>85</sup>

It is difficult to square the holding in *Garrett* with the provisions of the TULPA. Section 3(a)<sup>86</sup> of the TULPA explicitly requires that persons desiring to form a limited partnership file a certificate containing designated information in the office of the secretary of state, and section 3(b) declares that “[a] limited partnership is formed if there has been substantial compliance in good faith with the requirements of paragraph (a).”<sup>87</sup> When no limited partnership certificate has been filed, there can hardly have been “substantial compliance” with the requirements of section 3(a), and it would seem to follow that no limited partnership has been formed. Nevertheless, the court that decided *Garrett* asserted, without discussing the provisions of section 3, that “the entity” with which the plaintiffs had dealt “was in fact a limited partnership.”<sup>88</sup>

The *Garrett* court appears to have acknowledged the existence of a “de facto limited partnership” or a “limited partnership by estoppel,” just as other courts have occasionally granted recognition to a “de facto corporation” or “corporation by estoppel.” Although the de facto and estoppel doctrines as developed in corporate law may be highly artificial, their use has often served the ends of fairness and justice. Many cases have held that a plaintiff who has dealt with a business association on the understanding that it is a corporation, but who subsequently discovers that the corporation was defectively formed, should not be awarded a recovery against a shareholder who was not aware of or responsible for the defect.<sup>89</sup> Thus, even in states that have abandoned the doctrine of de facto corporations, a person who has dealt with a business association as if it were a corporation may be estopped to deny the corporation’s existence.<sup>90</sup>

Whatever the merits of particular applications of the estoppel doctrine in corporate law, there is less need for a similar doctrine to protect the members of defectively organized limited partnerships. The TULPA itself provides an escape hatch for a person who thinks that he is a limited partner in a limited partnership, but then discovers that no limited partnership certificate has been filed. The statutory scheme is relatively clear. A de jure limited partnership is formed when there is substantial compliance in good faith with the section 3 requirements for the execution and filing of a

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85. *Id.* In a secondary holding, the court concluded that the limited partners had not become personally liable to the plaintiffs by taking control of the partnership business, because the debt to the plaintiffs had been incurred prior to the limited partners’ exercise of control. *Id.* at 571. See TEX. REV. CIV. STAT. ANN. art. 6132a, § 8 (Vernon 1970). The court noted that the limited partners’ liability for obligations incurred before they became general partners could only be satisfied out of partnership property. 569 S.W.2d at 571. See *Miller v. Doughty*, 520 S.W.2d 586 (Tex. Civ. App.—Corpus Christi 1975, no writ); TEX. REV. CIV. STAT. ANN. art. 6132b, § 17 (Vernon 1970) (liability of incoming partner).

86. TEX. REV. CIV. STAT. ANN. art. 6132a, § 3(a)(2) (Vernon Supp. 1978-79).

87. *Id.* § 3(b) (Vernon 1970).

88. 569 S.W.2d at 570.

89. See, e.g., *American Salt Co. v. Heidenheimer*, 80 Tex. 344, 15 S.W. 1038 (1891). See also 19 R. HAMILTON, *supra* note 7, §§ 330, 331; I. HILDEBRAND, I THE LAW OF TEXAS CORPORATIONS § 185 (1942).

90. See 19 R. HAMILTON, *supra* note 7, §§ 330, 331.

limited partnership certificate.<sup>91</sup> When no certificate has been filed, section 12 allows one who intended to become a limited partner to avoid personal liability by promptly renouncing his interest in profits or compensation after the failure to file becomes known to him.<sup>92</sup> The difficulty with the *Garrett* opinion is that it ignores the statute. To grant the privilege of limited liability to all persons who represent that they are limited partners in a limited partnership, whether or not they have filed a limited partnership certificate, effectively negates the filing requirement enacted by the legislature.

*Breach of Fiduciary Duty.* One of the remedies available to limited partners against a general partner who breaches his fiduciary duties was discussed in *Watson v. Limited Partners of WCKT, Ltd.*<sup>93</sup> In *Watson* the limited partners sought recovery of their capital investment, on the theory of money had and received, from the general partner. The limited partners had contributed most of the capital of the limited partnership, which was formed to own and rent out five fourplexes. According to the findings of the trial court, the general partner "failed to manage the affairs of the limited partnership as a fiduciary,"<sup>94</sup> and the plaintiffs' contributions to capital were dissipated. The limited partnership was dissolved, a receiver was appointed, and the fourplexes were sold at a trustee's sale. The general partner subsequently repurchased the fourplexes for his own account. On these facts the appellate court held that the limited partners were entitled to restitution of the full amount of their contributions to the capital of the limited partnership.<sup>95</sup> The court concluded that when the general partner breached his fiduciary duties to the limited partners, he automatically forfeited the money that had been advanced to him.<sup>96</sup> The case serves as a reminder that restitution is a recognized remedy for a violation of the duties arising out of a fiduciary relationship.<sup>97</sup>

### III. CORPORATIONS

*Recognition or Disregard of the Corporate Entity.* Cases in which the courts were asked to "pierce the corporate veil" continued to arise during the survey period. In *Inesco, Inc. v. Sears*<sup>98</sup> the seller of a barge sought to recover the unpaid portion of the purchase price from Inesco, the purchasing corporation, Trans-Mex Leasing Company, a subsidiary of Inesco, and Gray, the former chairman of the board and controlling shareholder of Inesco. Gray had made the initial payments on the barge, although title was taken in Inesco's name and later transferred to Trans-Mex. Following

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91. TEX. REV. CIV. STAT. ANN. art. 6132a, § 3(b) (Vernon 1970).

92. *Id.* § 12; see note 79 *supra*.

93. 570 S.W.2d 179 (Tex. Civ. App.—Austin 1978, no writ).

94. *Id.* at 181.

95. *Id.* at 182.

96. *Id.* at 183.

97. *Id.* at 182.

98. 567 S.W.2d 827 (Tex. Civ. App.—Beaumont 1978, writ ref'd n.r.e.).

a dispute among the corporations' shareholders, the barge was ultimately transferred to Gray in exchange for all his stock in Inesco and Trans-Mex. The trial court found that Gray was the alter ego of Inesco and Trans-Mex, and held all three defendants liable for the amount owed on the barge. The court of civil appeals affirmed on two alternative theories. First, the court noted that there was evidence that Gray had contributed all the funds of Inesco, that he had controlled all the financial affairs of the corporations, that he originally had intended to acquire title to the barge in his own name, and that he had told the other shareholders and directors that he would pay for the barge. These facts convinced the court that Gray had used the corporate entity of Inesco to transact his personal business, and that he should be held liable as the alter ego of the corporation.<sup>99</sup> Second, the court concluded that Gray should be required to pay the plaintiff's claim because he had "denuded" Inesco of its only asset when he had acquired title to the barge in exchange for his worthless stock.<sup>100</sup> This alternative ground of the decision seems fully adequate to support the result: neither a corporation nor an individual will be permitted to evade creditors by gratuitously conveying assets to another person or entity.<sup>101</sup>

*Angus v. Air Coils, Inc.*<sup>102</sup> also involved an action brought by a creditor seeking to hold an individual shareholder responsible for a corporate debt. Texas Refrigeration and Engineering Company was founded in 1958 by the defendant, F.M. Angus. Angus and his wife and son were the sole shareholders and directors of Texas Refrigeration; in addition, Angus served as the president of the corporation. In 1970 the plaintiff, Air Coils, invoiced Texas Refrigeration for some repair costs, but Angus did not pay the bill because he thought that Air Coils had collected the amount in question from a third party. Angus dissolved the corporation in 1971, but he failed to send any notice of dissolution to Air Coils, and swore in the articles of dissolution that all liabilities of Texas Refrigeration had been discharged or adequate provision made for their payment. The trial court reviewed the foregoing facts, noted that Angus and his wife and son had made loans to Texas Refrigeration without receiving any evidence of indebtedness from it, and concluded that Angus was individually liable to Air Coils because he had "treated the corporation as his alter ego."<sup>103</sup>

The court of civil appeals reversed. At the outset the court concluded that, "as a matter of law," Texas Refrigeration was not the alter ego of Angus.<sup>104</sup> Emphasizing that Air Coils had voluntarily contracted with Texas Refrigeration as a corporate entity, the court found none of the "extraordinary circumstances" that could justify holding a shareholder indi-

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99. *Id.* at 830. For a discussion of the alter ego doctrine, see *Fagan v. LaGloria Oil & Gas Co.*, 494 S.W.2d 624 (Tex. Civ. App.—Houston [14th Dist.] 1973, no writ).

100. 567 S.W.2d at 830.

101. See *World Broadcasting Sys., Inc. v. Bass*, 160 Tex. 261, 328 S.W.2d 863 (1959).

102. 567 S.W.2d 931 (Tex. Civ. App.—Dallas 1978, no writ).

103. *Id.* at 932.

104. *Id.* at 933.

vidually liable on a corporation's debt.<sup>105</sup> Neither the fact that the majority of the corporation's stock was owned by one person, nor the fact that Angus and his family had provided funds to the corporation to keep it solvent, was regarded as a sufficient basis for piercing the corporate veil.<sup>106</sup> Furthermore, the court dismissed Air Coils' argument that Angus's violations of certain provisions of the Texas Business Corporation Act (TBCA)<sup>107</sup> made him liable for the corporation's debts. Assuming, arguendo, that Angus had violated article 6.04(A)(2)<sup>108</sup> by failing to send a notice of dissolution to Air Coils, and had violated article 6.06(A)(4)<sup>109</sup> by swearing that no debts of the corporation remained unpaid, the court nevertheless concluded that "violations of these provisions of the Texas Business Corporation Act are not grounds, in and of themselves, to disregard the corporate entity on an alter-ego theory and to impose liability individually for a corporate debt on a former shareholder."<sup>110</sup>

Although the *Angus* opinion contains a thoughtful discussion of the alter ego doctrine, the court's discussion of the dissolution statutes and the consequences of a failure to comply with them is much less satisfactory. Some confusion results from the court's characterization of the determinative issue in the case. While the question was stated to be whether violations of certain provisions of the Texas Business Corporation Act made the corporation Angus's alter ego,<sup>111</sup> it might have been more appropriate to ask whether the alleged violations of the TBCA gave Air Coils an independent basis for a suit against Angus. TBCA article 6.04(A)(2) requires that a corporation send written notice of its intention to dissolve to "each known creditor of and claimant against the corporation."<sup>112</sup> The obvious purpose of this statutory requirement is to afford all creditors an opportunity to press their claims against the corporation,<sup>113</sup> either before it distributes its assets to its shareholders or within the three-year period allowed for the prosecution of actions against the corporation after the date of dissolu-

105. The court considered "extraordinary circumstances" to include the use of a corporate entity to defraud existing creditors of shareholders, to circumvent a statute, to evade an existing obligation, or to achieve a monopoly. *Id.*; see, e.g., *Pace Corp. v. Jackson*, 155 Tex. 179, 284 S.W.2d 340 (1955); *Hanson Southwest Corp. v. Dal-Mac Constr. Co.*, 554 S.W.2d 712 (Tex. Civ. App.—Dallas 1971, writ ref'd n.r.e.).

106. 567 S.W.2d at 933.

107. TEX. BUS. CORP. ACT ANN. arts. 6.04(A)(2), .06(A)(4) (Vernon Supp. 1978-79).

108. *Id.* art. 6.04(A)(2). Article 6.04(A)(2) provides that before filing articles of dissolution, "[t]he corporation shall cause written notice by registered mail of its intention to dissolve to be mailed to each known creditor of and claimant against the corporation."

109. *Id.* art. 6.06(A)(4). This article requires the articles of dissolution to state the following:

That all debts, obligations and liabilities of the corporation have been paid or discharged or that adequate provision has been made therefor, or . . . that all property and assets have been applied so far as they would go to the payment thereof in a just and equitable manner and that no property or assets remained available for distribution among its shareholders.

110. 567 S.W.2d at 934.

111. *Id.* at 933.

112. TEX. BUS. CORP. ACT ANN. art. 6.04(A)(2) (Vernon Supp. 1978-79).

113. *Id.* art. 6.04, comment (Vernon 1956).

tion.<sup>114</sup> If a creditor or claimant is not notified as required by article 6.04(A)(2), and his claim is not paid or provided for prior to the dissolution of the corporation, he might have a cause of action against the corporation's directors under TBCA article 2.41(A)(3),<sup>115</sup> or against the corporation's shareholders on the common-law theory that allows an unsatisfied creditor of a dissolved corporation to pursue its assets into the hands of the shareholders.<sup>116</sup> The *Angus* opinion obliquely indicates that "the statute of limitations and the period of corporate survival had run" before Air Coils learned that Texas Refrigeration had ceased to exist.<sup>117</sup> The opinion, however, does not identify the particular statute of limitations to which it refers, and it is not immediately obvious which statute of limitations should be applicable when a creditor brings suit against a shareholder or director after discovering that the corporate debtor has been dissolved.<sup>118</sup> If the statute of limitations had run on Air Coils' original contract claim against Texas Refrigeration before Air Coils commenced suit against Angus, the suit against Angus should probably have been barred. On the other hand, if Air Coils would still have had an enforceable claim against Texas Refrigeration but for the dissolution of the corporation and the expiration of the three-year survival period, Air Coils probably should have had an enforceable claim against Angus and the other former shareholders and directors of Texas Refrigeration. In any event, the decision left unanswered many questions concerning the liabilities of the former shareholders and directors of a dissolved corporation. The best protection against such liabilities is strict compliance with the dissolution statutes.

During the survey period, there were some rather unusual cases in which the issue was whether or not a corporation should be recognized as an independent entity. In *Houston Furniture Distributors, Inc. v. Bank of Woodlake, N.A.*<sup>119</sup> the plaintiff bank brought suit against the corporate maker of a promissory note and Edward Gibbons, a guarantor of the indebtedness under a pre-existing guaranty agreement, for the unpaid principal amount of the note, interest, and attorney's fees. Both the corporation and Gibbons asserted the defense of usury. Although the defendants conceded that the rate of interest that the bank had charged could legally be

114. The three-year period for the survival of remedies is established by *id.* art. 7.12. See also TEX. REV. CIV. STAT. ANN. art. 1302—2.07 (Vernon 1962).

115. TEX. BUS. CORP. ACT ANN. art. 2.41A(3) (Vernon 1956) provides as follows:

The directors of a corporation who vote for or assent to any distribution of assets of a corporation to its shareholders during the liquidation of the corporation without the payment and discharge of, or making adequate provision for, all known debts, obligations, and liabilities of the corporation shall be jointly and severally liable to the corporation for the value of such assets which are distributed, to the extent that such debts, obligations and liabilities of the corporation are not thereafter paid and discharged.

116. See, e.g., N. LATTIN, LATTIN ON CORPORATIONS § 185 (2d ed. 1971); Schoone, *Shareholder Liability upon Voluntary Dissolution of Corporation*, 44 MARQ. L. REV. 415, 416 (1961).

117. 567 S.W.2d at 934.

118. See generally Schoone, *supra* note 116, at 428.

119. 562 S.W.2d 880 (Tex. Civ. App.—Houston [1st Dist.] 1978, no writ).



charged to a corporate borrower, they argued that the loan had actually been made to Gibbons rather than to the corporation. In particular, the defendants pointed out that a bank officer had suggested that the note be executed by the corporation, even though he knew that Gibbons planned to use the borrowed funds for an investment scheme unrelated to the corporation's business. In affirming a summary judgment for the bank, the court of civil appeals held that the foregoing facts did not constitute proof of an "agreement, device or subterfuge to charge interest at a usurious rate."<sup>120</sup> The court noted that an earlier Texas case<sup>121</sup> had held that "a lender may lawfully require, as a condition to making a loan, that the loan be made to a corporation rather than to an individual borrower, and such a condition does not, in itself, make the transaction usurious, even though the purpose of the requirement is to permit the lender to charge a higher rate of interest."<sup>122</sup> While the court may have reached a correct result in the case before it, the broad rule that it cited is difficult to reconcile with the oft-repeated warning that a corporate entity cannot be used to evade the policy of a statute.<sup>123</sup>

*Navarro v. Collora*<sup>124</sup> was a very unusual case. The minor children of the decedent, Joe Collora, sought to require the defendant, Navarro, to assign his interest in certain land to the decedent's estate. In 1962 Collora owed Navarro, his attorney, the sum of \$4,000. In exchange for Navarro's cancellation of the \$4,000 debt, Collora deeded the land in question to the Camille Corporation, of which Navarro was the president and his minor children the sole stockholders. At the time of the conveyance, the land was worth approximately \$23,000, and only \$5,500 remained due on the original purchase price. Three years later, Camille Corporation transferred the land to Navarro. On these facts, the trial court instructed a verdict for the Collora children, apparently on the ground that Navarro had acquired the land unfairly.

The court of civil appeals reversed and remanded for a new trial. The appellate court recognized that "the attorney-client relationship is highly fiduciary in nature,"<sup>125</sup> and that "the attorney owes his client the highest of good faith and honest dealing."<sup>126</sup> Further, the court declared that "[t]here is a presumption of unfairness which attaches to a transaction between an attorney and his client, and once it is shown that the attorney-

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120. *Id.* at 883.

121. *American Century Mortgage Investors v. Regional Center, Ltd.*, 529 S.W.2d 528 (Tex. Civ. App.—Dallas 1975, writ *ref'd n.r.e.*).

122. 562 S.W.2d at 883.

123. *See, e.g., Anderson v. Abbott*, 321 U.S. 349, 362-63 (1944) (dealing with Federal Reserve Act); *United States v. Lehigh Valley R.R.*, 220 U.S. 257, 259 (1911) (dealing with Interstate Commerce Act).

124. 566 S.W.2d 304 (Tex. Civ. App.—Corpus Christi 1978), *rev'd in part*, 22 Tex. Sup. Ct. J. 120 (Nov. 29, 1978). The supreme court reversed the judgment of the court of civil appeals with respect to a party whose claim was distinct from that of the Collora children. The Collora children did not appeal to the supreme court, which therefore did not address the issue discussed in the text.

125. 566 S.W.2d at 311.

126. *Id.*

client relationship existed at the time of the transfer of property from the client to the attorney, the burden of proving its fairness is on the attorney."<sup>127</sup> The court, however, did not apply the rule that it announced. Rather, it emphasized that the transfer in question was not a transfer directly from the client to his attorney, but was instead a transfer from the client to his attorney's family-owned corporation.<sup>128</sup> In the view of the court, the jury should have determined whether the conveyance to Camille Corporation "was in fact a transaction between the defendant and Joe M. Collora,"<sup>129</sup> either because the corporation was the defendant's alter ego, or because the defendant had designedly used the corporation as a device to acquire the property for himself.<sup>130</sup> In the absence of a jury finding that the conveyance to the corporation was a transaction between the attorney and his client, the court deemed it unnecessary to decide whether or not the transaction was fair.<sup>131</sup>

The portion of the court's opinion summarized above is extremely puzzling. It is impossible to see the relevance of the fact that Joe Collora had conveyed the property in question to the defendant's family-owned corporation rather than to the defendant himself. The critical fact was that the defendant attorney had agreed to cancel his client's indebtedness in consideration of the client's transfer of property to some person or entity specified by the defendant. There obviously was a transaction between the attorney and his client, whether the attorney chose to give the benefit of that transaction to himself, to a corporation, to his children, or to a person selected at random. The Collora children should not have been required to demonstrate that Camille Corporation was the defendant's alter ego, or that other circumstances justified piercing the corporate veil. On the contrary, as soon as the children had proved that their father had given up his land in exchange for his attorney's cancellation of a debt, the attorney should have been required to prove the intrinsic fairness of the arrangement.

*Christopher v. General Computer Systems, Inc.*<sup>132</sup> was another case reaching a very questionable result. General Computer Systems brought suit against Surety Industries, Inc. and Christopher, Surety's president and sole shareholder, for the misappropriation of some funds that Surety had collected as General's agent, but that Christopher had diverted to his personal use. Judgment was entered against Christopher for \$117,000 in actual damages and \$150,000 in exemplary damages. The award of exemplary damages was predicated on the jury's findings that Christopher and Surety had conspired to withhold maintenance funds from General and that the conspiracy had been willful and deliberate.<sup>133</sup> On appeal,

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127. *Id.*

128. *Id.* at 311-12.

129. *Id.* at 312.

130. *Id.*

131. *Id.*

132. 560 S.W.2d 698 (Tex. Civ. App.—Dallas 1977, writ ref'd n.r.e.).

133. *Id.* at 704.

Christopher attacked the award of exemplary damages on the ground that there was no evidence of a conspiracy, since there was no evidence that he had combined with any other identifiable individual to commit an unlawful act. The court of civil appeals held, however, that there was ample evidence to support the jury's findings and the award of exemplary damages.<sup>134</sup> While the court apparently acknowledged that it takes two or more persons to conspire, it considered Christopher and Surety to be the requisite two persons. According to the court, the evidence supported a finding that Christopher, acting in his individual capacity, had conspired with Surety, acting through Christopher as its chief executive officer, to withhold funds from General.<sup>135</sup>

In overruling a motion for rehearing, the majority reaffirmed its original decision, but appeared to concede that the evidence in the case may have been inadequate to establish a common-law conspiracy for any purpose other than to support an award of exemplary damages.<sup>136</sup> Further, the majority expressly limited its original ruling "to the peculiar circumstances of this case and the language of the issues and accompanying definitions, as submitted to the jury without objection."<sup>137</sup> Thus, while the *Christopher* decision is rather bizarre, it is unlikely to have much impact as precedent.

*Authority of Officers.* Texas courts are frequently asked to decide whether or not particular acts fall within the authority of a corporate officer. In *Square 67 Development Corp. v. Red Oak State Bank*,<sup>138</sup> the question was whether the president of a corporation had the inherent authority to employ an attorney and initiate a suit against a bank for conversion. The court held that "the president of a corporation is not authorized to employ an attorney to conduct litigation for the company absent express authority or implied authority (such as entrustment with broad powers of management of the corporate business) set forth in the bylaws or by proper action of the board of directors."<sup>139</sup> The court also noted that, in the case before it, the board of directors had passed a resolution that negated any authority that the president might otherwise have had to prosecute the suit in question.<sup>140</sup>

While a corporation's president has very limited implied authority under Texas law, a case decided during the past year recognized that a general manager has much broader powers. In *W.B. Dunavant & Co. v. Southmost Growers, Inc.*<sup>141</sup> the general manager of Southmost Growers, a corporation that operated a cotton gin, executed a written contract under

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134. *Id.* at 705.

135. *Id.* In a vigorous dissent, Justice Akin argued that there can be no meeting of the minds when only one mind exists, so that two natural persons are necessary to the existence of a conspiracy. *Id.* at 708.

136. *Id.* at 709.

137. *Id.*

138. 559 S.W.2d 136 (Tex. Civ. App.—Waco 1977, writ ref'd n.r.e.).

139. *Id.* at 138.

140. *Id.*

141. 561 S.W.2d 578 (Tex. Civ. App.—Corpus Christi 1978, writ ref'd n.r.e.).

which Southmost agreed to sell a particular farmer's cotton crop to W.B. Dunavant & Company. In fact, the farmer had not authorized Southmost to sell his cotton, and he refused to deliver his crop to Dunavant at the price that had been negotiated by Southmost's general manager. After buying the cotton directly from the farmer at a higher price, Dunavant sued Southmost for damages for breach of contract. The court held that the general manager of Southmost had authority to bind Southmost by contract, and rendered judgment for Dunavant. The governing rule was stated as follows:

Where a corporation transacts its business by, through or under a general manager, the conduct of such business by the general manager binds the corporation, if the transaction under scrutiny is within the scope of the corporation's business. . . . [I]n the ordinary business affairs of a corporation, as a general rule, the acts of a corporation's general manager are the acts of the corporation itself.<sup>142</sup>

*American Bank & Trust Co. v. Freeman*<sup>143</sup> arose out of the commission of a fraud by the chairman of the board of directors of a bank. The board chairman agreed to sell the plaintiff 12,500 shares of his bank stock and to see that the plaintiff was elected to the board of directors. The plaintiff borrowed a large sum from the bank to finance the stock purchase. The board chairman went bankrupt, however, and failed to transfer any stock to the plaintiff or to obtain a seat on the board for him. The plaintiff then sued the bank for fraud in the inducement. In reversing a judgment for the plaintiff, the court of civil appeals noted that there was no evidence that the board of directors of the bank had ever expressly or impliedly authorized the board chairman to contract for the sale of his personal stock to the plaintiff or to promise the plaintiff a directorship.<sup>144</sup> As the court recognized, the plaintiff had been "sorely abused,"<sup>145</sup> but not by the defendant bank.

Three cases decided during the survey period discussed what kinds of facts will support a finding that a corporation has ratified an originally unauthorized act. In *Bowers Steel, Inc. v. DeBrooke*<sup>146</sup> the president of a corporation offered the plaintiff twenty percent of the company's stock as consideration for his accepting employment as vice president. After the plaintiff was terminated without having received the stock, he sued the corporation for breach of contract. The court acknowledged that the general powers of the president of a corporation do not ordinarily include the right to offer one-fifth of the corporation's stock to someone as an inducement to enter into an employment contract.<sup>147</sup> Nevertheless, the court affirmed a judgment for the plaintiff, because the evidence supported the finding that the corporation's directors and shareholders knew of the

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142. *Id.* at 582.

143. 560 S.W.2d 444 (Tex. Civ. App.—Beaumont 1977, writ ref'd n.r.e.).

144. *Id.* at 446.

145. *Id.* at 447.

146. 557 S.W.2d 369 (Tex. Civ. App.—San Antonio 1977, no writ).

147. *Id.* at 372.

promise to the plaintiff and did nothing to repudiate it prior to the decision to terminate him.<sup>148</sup> The case illustrates the general rule that "the directors or stockholders may ratify any act or contract of any other body or agency of the corporation which they might have authorized in the first instance."<sup>149</sup>

*Jackson v. Gray*<sup>150</sup> held that the board of directors of a bank had ratified the dismissal of the executive vice-president by the chief executive officer. The court recognized that a valid ratification requires knowledge by the principal of all the relevant facts, but concluded that the record established that the board had acted with the requisite knowledge.<sup>151</sup> Alternatively, the court held that the board's attempt to ratify the dismissal of the vice-president was tantamount to his dismissal by the board itself.<sup>152</sup>

The final case involving a question of ratification was *Reece v. First State Bank*.<sup>153</sup> The plaintiff bank sued Reece, the vice-president of a corporation, on his "continuing guaranty for corporate indebtedness."<sup>154</sup> The bank had made a loan in return for a promissory note purportedly signed by Reece on behalf of the corporation, but Reece's signature on the note was forged. The corporation made several payments on the note, and took title to some vehicles purchased with the proceeds of the loan. Finding that the corporation had ratified the execution of the note, the court held that the note had become a "corporate indebtedness" on which Reece was liable as guarantor.<sup>155</sup>

*Shareholder's Petition for Annual Meeting. Valley International Properties, Inc. v. Los Campeones, Inc.*<sup>156</sup> presented a number of interesting issues, one of which was whether an unregistered owner of shares may seek a court order for a shareholders' meeting. Article 2.24(B) of the TBCA<sup>157</sup> authorizes a proper court, "on the application of any shareholder," to order a shareholders' meeting if no annual meeting has been held within a thirteen-month period. Los Campeones purchased a majority of the shares of Valley International Properties (V.I.P.) at a public foreclosure sale, and then filed a petition for a meeting under article 2.24(B). On appeal from a judgment ordering the meeting, V.I.P. argued that Los Campeones had no right to seek relief under article 2.24(B) because it had not registered its stock with V.I.P. in accordance with section 8.207 of the Texas Business and Commerce Code.<sup>158</sup> The court concluded, however, that section 8.207 merely affords protection to a corporation that identifies its shareholders

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148. *Id.* at 373.

149. *Id.* at 371-72.

150. 558 S.W.2d 138 (Tex. Civ. App.—Tyler 1977, writ ref'd n.r.e.).

151. *Id.* at 139.

152. *Id.*

153. 566 S.W.2d 296 (Tex. 1978).

154. *Id.* at 296.

155. *Id.* at 298.

156. 568 S.W.2d 680 (Tex. Civ. App.—Corpus Christi 1978, writ ref'd n.r.e.).

157. TEX. BUS. CORP. ACT ANN. art. 2.24(B) (Vernon Supp. 1978-79).

158. TEX. BUS. & COM. CODE ANN. § 8.207(a) (Vernon 1968). This subsection provides that "[p]rior to due presentment for registration of transfer of a security in registered form

by reference to its record of ownership, and does not govern how a court is to treat an unregistered shareholder.<sup>159</sup> Further, the court reasoned that if the legislature had intended the word "shareholder" in article 2.24(B) to mean "shareholder of record," it would have used the phrase "shareholder of record," as it did in other sections of the TBCA.<sup>160</sup> Finally, the court found that Los Campeones had a protectable property interest that entitled it to demand a shareholders' meeting regardless of its ability or desire to vote.<sup>161</sup>

*Oral Contracts for the Sale of Securities.* Two cases decided during the survey period presented questions concerning the scope and meaning of section 8.319 of the Texas Business and Commerce Code,<sup>162</sup> which establishes a statute of frauds for contracts for the sale of securities. In *Kenney v. Porter*<sup>163</sup> the plaintiff sued for specific performance of an alleged contract for the purchase and sale of stock. The plaintiff and the defendant were the sole shareholders of the Valley Plumbing Supply Company. In accordance with a pre-existing buy-sell agreement, the plaintiff made a written offer to sell his shares to the defendant or, alternatively, to buy the defendant's shares. The plaintiff alleged, and the defendant denied, that the defendant had orally accepted the plaintiff's offer. The trial court granted a summary judgment for the defendant on the ground that there was no written contract, as required by section 8.319 of the Texas Business and Commerce Code, for the sale of either party's stock. The Corpus Christi court of civil appeals, however, reversed the judgment and remanded the cause for trial. After reviewing the definition of the term "security" in section 8.102(a) of the Texas Business and Commerce Code,<sup>164</sup>

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the issuer . . . may treat the registered owner as the person exclusively entitled to vote, to receive notifications and otherwise to exercise all the rights and power of an owner." *Id.*

159. 568 S.W.2d at 687.

160. *Id.*; see TEX. BUS. CORP. ACT ANN. art. 2.25 (Vernon 1956).

161. 568 S.W.2d at 687.

162. TEX. BUS. & COM. CODE ANN. § 8.319 (Vernon 1968) provides as follows:

A contract for the sale of securities is not enforceable by way of action or defense unless

- (1) there is some writing signed by the party against whom enforcement is sought or by his authorized agent or broker sufficient to indicate that a contract has been made for sale of a stated quantity of described securities at a defined or stated price; or
- (2) delivery of the security has been accepted or payment has been made but the contract is enforceable under this provision only to the extent of such delivery or payment . . . .

163. 557 S.W.2d 589 (Tex. Civ. App.—Corpus Christi 1977, no writ).

164. TEX. BUS. & COM. CODE ANN. § 8.102(a)(1) (Vernon 1968) defines a "security" as an instrument which

- (A) is issued in bearer or registered form; and
- (B) is of a type commonly dealt in upon securities exchanges or markets or commonly recognized in any area in which it is issued or dealt in as a medium for investment; and
- (C) is either one of a class or series or by its terms is divisible into a class or series of instruments; and
- (D) evidences a share, participation or other interest in property or in an enterprise or evidences an obligation of the issuer.

the appellate court held that there was an issue of fact as to whether or not the stock in Valley Plumbing fell within the definition.<sup>165</sup> The decision demonstrates that the term "security" has a much more limited and technical meaning in the Business and Commerce Code than in state and federal securities laws.<sup>166</sup>

The interpretation of section 8.319 was also at issue in *Bowers Steel, Inc. v. DeBrooke*,<sup>167</sup> in which one of the questions was whether the statute rendered unenforceable an oral contract of employment for which the consideration was to be corporate stock.<sup>168</sup> The jury had found that the plaintiff was offered stock in the defendant corporation as consideration for his acceptance of employment with the corporation. Reasoning that the plaintiff had made "payment" for the stock when he accepted a position with the company, the court concluded that the terms of section 8.319(2) were satisfied, and that the plaintiff could enforce his contract.<sup>169</sup>

#### IV. SECURITIES REGULATION

*Texas Securities Law.* During the survey period the Texas courts decided three cases that presented important questions concerning the scope and meaning of the Texas Securities Act (TSA).<sup>170</sup> In *Searsy v. Commercial Trading Corp.*<sup>171</sup> the Texas Supreme Court held that certain "naked" commodities options were "both investment contracts and evidence of indebtedness,"<sup>172</sup> and thus "securities" as defined in article 581—4(A) of the TSA.<sup>173</sup> Since the defendants had not registered the options before selling them to the plaintiffs, the plaintiffs were allowed to rescind their purchases and recover the consideration paid.<sup>174</sup> In *Enntex Oil & Gas Co. v. State*<sup>175</sup> the principal question was whether the defendant corporations, which were either incorporated in or authorized to do business in Texas, could constitutionally be required to comply with the registration and licensing provisions of the TSA before selling interests in Texas oil and gas leases to persons who resided in other states. Noting that "the State of Texas has a legitimate local public interest in taking precautions that oil and gas leases covering its lands are not the subject of fraudulent security practices," the Texarkana court of civil appeals held that the State's regulation of the de-

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165. 557 S.W.2d at 591.

166. Compare TEX. BUS. & COM. CODE ANN. § 8.102(a) (Vernon 1968) with TEX. REV. CIV. STAT. ANN. art. 581—4A (Vernon 1964), 15 U.S.C. § 77b(1) (1976), and 15 U.S.C. § 78c(a)(10) (1976).

167. 557 S.W.2d 369 (Tex. Civ. App.—San Antonio 1977, no writ). This case is also discussed in the text accompanying notes 146-49 *supra*.

168. 557 S.W.2d at 374.

169. *Id.*

170. TEX. REV. CIV. STAT. ANN. arts. 581—1 to —39, 582—1 (Vernon 1964 & Supp. 1978-79).

171. 560 S.W.2d 637 (Tex. 1977).

172. *Id.* at 642.

173. TEX. REV. CIV. STAT. ANN. art. 581—4A (Vernon 1964).

174. 560 S.W.2d at 642.

175. 560 S.W.2d 494 (Tex. Civ. App.—Texarkana 1977), *appeal dismissed*, 99 S. Ct. 445, 58 L. Ed. 2d 419 (1978).

fendants' activities did not violate the commerce clause of the United States Constitution.<sup>176</sup> The court also concluded that a defendant that did not engage in any sales activities, but that did manage the wells drilled by another defendant, was a "dealer" under the TSA.<sup>177</sup> Finally, in *Simmons v. Danco, Inc.*<sup>178</sup> the Dallas court of civil appeals held that a private party had "no right, as a matter of law, to apply to a court for an injunction" against another party's alleged violation of the tender offer guidelines issued by the Texas Securities Commissioner.<sup>179</sup> The court reasoned that a controversy concerning the enforcement of the guidelines must be submitted to the Texas Securities Board or the Texas Securities Commissioner for an initial decision,<sup>180</sup> because the Board and the Commissioner have primary jurisdiction over the interpretation and enforcement of rules and regulations promulgated under article 581—28-1 of the TSA.<sup>181</sup>

*Federal Securities Law.* Congress made some important changes in and additions to the federal securities laws during the survey period. The Securities Exchange Act of 1934<sup>182</sup> was amended by the Foreign Corrupt Practices Act of 1977,<sup>183</sup> which outlaws the making of certain payments designed to influence foreign officials<sup>184</sup> and requires reporting companies to meet specified accounting standards,<sup>185</sup> and by the Domestic and Foreign Investment Improved Disclosure Act of 1977,<sup>186</sup> which authorizes the Securities and Exchange Commission to require disclosures from each beneficial owner of more than five percent of a covered class of equity securities.<sup>187</sup> Section 3(b) of the Securities Act of 1933<sup>188</sup> was amended twice during 1978, as Congress raised the limit on the exemptions that may be created under the section first to \$1,500,000<sup>189</sup> and then to \$2,000,000.<sup>190</sup> The Securities Investor Protection Act<sup>191</sup> was also

176. 560 S.W.2d at 497.

177. *Id.* at 498. "Dealer" is defined in TEX. REV. CIV. STAT. ANN. art. 581—4C (Vernon 1964) (emphasis added) to include

every person or company, other than a salesman, who engages in this state, either for all or part of his or its time, directly or through an agent, in selling, offering for sale or delivery or soliciting subscriptions to or orders for, or undertaking to dispose of, or to invite offers for, or rendering services as an investment adviser, or *dealing in any other manner in any security or securities within this state.*

In concluding that the defendant was a dealer, the court stated that the defendant "*was dealing with securities that should have been licensed and regulated under the Act.*" 560 S.W.2d at 498 (emphasis added).

178. 563 S.W.2d 376 (Tex. Civ. App.—Dallas 1978, writ *ref'd n.r.e.*).

179. *Id.* at 378.

180. *Id.* at 378-79.

181. TEX. REV. CIV. STAT. ANN. art. 581—28—1 (Vernon Supp. 1978-79).

182. 15 U.S.C.A. § 78 (1971 & Supps. 1972-77, 1978).

183. Pub. L. No. 95-213, §§ 101-104, 91 Stat. 1494 (1977).

184. *Id.* § 103(a) (codified at 15 U.S.C.A. § 78dd—1 (Supp. 1978)).

185. *Id.* § 102 (codified at 15 U.S.C.A. § 78m(b)(2) (Supp. 1972-77)).

186. Pub. L. No. 95-213, §§ 201-204, 91 Stat. 1494 (1977).

187. *Id.* § 203 (codified at 15 U.S.C.A. § 78m(g) (Supp. 1972-77)).

188. 15 U.S.C. § 77c(b) (1976).

189. Pub. L. No. 95-283, § 18, 92 Stat. 249, 275 (1978).

190. Pub. L. No. 95-425, § 2, 92 Stat. 962 (1978).

191. Pub. L. No. 91-598, 84 Stat. 1636 (1970) (codified at 15 U.S.C.A. § 78aaa-III (1971 &



amended,<sup>192</sup> in part to double the insurance coverage for securities and cash left on deposit with a member broker-dealer.<sup>193</sup>

The Securities and Exchange Commission issued a number of important releases during the survey period. When Congress raised the limit on exemptions under section 3(b) of the 1933 Act from \$500,000 to \$1,500,000,<sup>194</sup> the Commission responded by increasing the maximum amount of securities that may be sold in a regulation A<sup>195</sup> offering to \$1,500,000.<sup>196</sup> The Commission also expanded the availability of form S-16, the short form for the registration of securities under the 1933 Act.<sup>197</sup> The Commission amended schedule 14A<sup>198</sup> under the 1934 Act to require disclosures in proxy statements of the services provided to corporations by their principal independent accountants;<sup>199</sup> and, in an unusual move, the Division of Corporation Finance published its staff instructions for the review of proxy materials containing anti-takeover proposals.<sup>200</sup> The Commission also adopted new beneficial ownership disclosure rules under the 1934 Act.<sup>201</sup>

A new rule was added to the "140 series," and three others were amended. The Commission adopted rule 148,<sup>202</sup> which it modeled after rule 144,<sup>203</sup> in order to provide a "safe harbor" for the resale of bankruptcy-related securities. Subsequently, rules 144 and 148 were amended to increase the amount of securities that may be sold under their provisions, and to permit sellers to deal directly with market makers.<sup>204</sup> The Commission amended rule 146<sup>205</sup> to require issuers to file reports of non-public offerings under the rule,<sup>206</sup> and to allow simplified disclosures in offerings of \$1,500,000 or less.<sup>207</sup> Rule 145<sup>208</sup> was amended to permit a person deemed to be an "underwriter" of securities acquired in a rule 145 business combination to resell the securities without limitation after holding them for two years, provided that the person is not an affiliate of the

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Supp. 1978)).

192. Pub. L. No. 95-283, 92 Stat. 249 (1978).

193. *Id.*, § 9, 92 Stat. 249, 265 (1978).

194. Pub. L. No. 95-283, § 18, 92 Stat. 249, 275 (1978); *see text accompanying note 189 supra.*

195. 17 C.F.R. §§ 230.251-264 (1978).

196. 43 Fed. Reg. 41,383, 41,385 (1978) (to be codified at 17 C.F.R. § 230.254).

197. 43 Fed. Reg. 16,672, 16,677 (1978). Form S-16 is found at 17 C.F.R. § 239.27 (1978).

198. 17 C.F.R. § 240.14a-101 (1978).

199. 43 Fed. Reg. 29,109, 29,111 (1978).

200. 43 Fed. Reg. 49,863 (1978).

201. 43 Fed. Reg. 18,484, 18,495 (1978); 43 Fed. Reg. 55,751, 55,755 (1978) (to be codified at 17 C.F.R. §§ 240.13d-1 to -7).

202. 43 Fed. Reg. 14,445, 14,449 (1978) (to be codified at 17 C.F.R. § 230.148).

203. 17 C.F.R. § 230.144 (1978).

204. 43 Fed. Reg. 43,709, 43,711 (1978); 43 Fed. Reg. 54,229, 54,230 (1978).

205. 17 C.F.R. § 230.146 (1978).

206. 43 Fed. Reg. 10,548, 10,550 (1978).

207. 43 Fed. Reg. 41,193, 41,194.

208. 17 C.F.R. § 230.145 (1978).

issuer and that the issuer is a reporting company.<sup>209</sup>

During 1978 the United States Court of Appeals for the Fifth Circuit addressed many important issues of securities regulation. One of the most significant decisions was *Great Western United Corp. v. Kidwell*,<sup>210</sup> in which the court held that the Idaho takeover statute was invalid because it was pre-empted by the Williams Act,<sup>211</sup> and because it imposed an unconstitutional burden on interstate commerce.<sup>212</sup> The United States Supreme Court has granted certiorari in the case. Another important decision was *Wilson v. First Houston Investment Corp.*,<sup>213</sup> in which the Fifth Circuit held that an aggrieved investor has an implied right of action for damages against an investment adviser for the adviser's violation of the antifraud provisions of the Investment Advisers Act of 1940.<sup>214</sup> The Supreme Court has granted certiorari in a Ninth Circuit case reaching the same conclusion.<sup>215</sup>

During its 1977-1978 Term, the United States Supreme Court decided only one case arising under the federal securities laws. In *Securities & Exchange Commission v. Sloan*<sup>216</sup> the Court held that the SEC lacks the statutory authority to issue, on the basis of a single set of events, a series of summary orders suspending trading in a corporation's stock for consecutive ten-day periods. During its present Term, the Court may produce a large number of securities opinions. In January 1979 the Court decided *Parklane Hosiery Co. v. Shore*,<sup>217</sup> which held that the determination of factual issues against the defendants in an SEC injunctive proceeding could estop the defendants from relitigating the issues before a jury in a subsequent action for damages, and *International Brotherhood of Teamsters v. Daniel*,<sup>218</sup> which held that the provisions of the Securities Act and Securities Exchange Act are inapplicable to a noncontributory, compulsory pension plan. Among the questions still facing the Court are: whether the independent directors of a mutual fund registered under the Investment Company Act of 1940<sup>219</sup> have the power to foreclose a nonfrivolous derivative suit against the majority directors of the fund and its investment adviser;<sup>220</sup> whether section 17 of the Securities Exchange Act of 1934<sup>221</sup>

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209. 43 Fed. Reg. 21,660, 21,661 (1978).

210. 577 F.2d 1256 (5th Cir. 1978), *cert. granted*, 47 U.S.L.W. 3450 (U.S. Jan. 9, 1979) (No. 78-759).

211. 15 U.S.C.A. §§ 78m(d), (e) (1971 & Supp. 1972-1977); 15 U.S.C.A. §§ 78n(d)-(f) (1971).

212. 577 F.2d at 1279, 1286.

213. 566 F.2d 1235 (5th Cir. 1978), *petition for cert filed*, 46 U.S.L.W. 3766 (U.S. June 1, 1978) (No. 77-1717).

214. 566 F.2d at 1243. The antifraud section of the Investment Advisers Act is codified at 15 U.S.C. § 80b-6 (1976).

215. *Lewis v. Transamerica Corp.*, 575 F.2d 237 (9th Cir.), *cert. granted sub nom. Transamerica Mortgage Advisors, Inc. v. Lewis*, 99 S. Ct. 348 (1978) (No. 77-1645).

216. 436 U.S. 103 (1978).

217. 47 U.S.L.W. 4079 (U.S. Jan. 9, 1979) (No. 77-1305).

218. 47 U.S.L.W. 4135 (U.S. Jan. 16, 1979) (Nos. 77-753 and 77-754).

219. 15 U.S.C.A. §§ 80a-1 to -52 (1971 & Supp. 1978).

220. *Lasker v. Burks*, 567 F.2d 1208 (2d Cir.), *cert. granted*, 99 S. Ct. 75 (1978) (No. 77-1724).

221. 15 U.S.C. § 78q (1976).

creates an implied right of action against an accounting firm that prepares a misleading report of a broker's financial affairs;<sup>222</sup> and whether a fraud perpetrated on brokers who are intermediaries in securities transactions, and not investors, can be found to violate section 17(a)(1) of the Securities Act of 1933.<sup>223</sup>

One development anticipated during the coming year may eventually prove to have an enormous impact on securities regulation. Before the end of 1979, Congress is expected to begin consideration of the proposed Federal Securities Code, which was approved by the American Law Institute at its last annual meeting. If enacted, the Code will integrate the six inter-related federal securities statutes into a single piece of legislation in an attempt to simplify the law, eliminate duplicate regulation, and increase the efficiency of the entire scheme of investor protection.<sup>224</sup>

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222. *Touche Ross & Co. v. Redington*, 46 U.S.L.W. 2598 (2d Cir. 1978), *cert. granted*, 47 U.S.L.W. 3360 (U.S. Nov. 28, 1978) (No. 78-309).

223. *United States v. Naftalin*, 579 F.2d 444 (8th Cir.), *cert. granted*, 47 U.S.L.W. 3402 (U.S. Dec. 12, 1978) (No. 78-561).

224. The Introduction to the proposed Code is reproduced at [78 Decisions] FED. SEC. L. REP. (CCH) ¶81,563.