
January 1985

Corporations and Partnerships

David Simon Sokolow

Recommended Citation

David Simon Sokolow, *Corporations and Partnerships*, 39 Sw L.J. 203 (1985)
<https://scholar.smu.edu/smulr/vol39/iss1/9>

This Article is brought to you for free and open access by the Law Journals at SMU Scholar. It has been accepted for inclusion in SMU Law Review by an authorized administrator of SMU Scholar. For more information, please visit <http://digitalrepository.smu.edu>.

CORPORATIONS AND PARTNERSHIPS

by

David Simon Sokolow*

I. PARTNERSHIPS

A. *Rights of Partners*

IN *Shindler v. Harris*¹ the court held that a joint venturer was not entitled to recover from his coventurers the value of his interest in the venture under section 42 of the Texas Uniform Partnership Act (TUPA).² In March 1973, a joint venture formed by the parties purchased a tract of land and gave the seller several lien notes as partial payment. The venturers orally agreed that they would periodically contribute money in proportion to their ownership interests to pay off the notes, cover operating expenses, and purchase additional land. In September 1973, they reduced their agreement to writing in a detailed joint venture agreement.

On February 20, 1975, three weeks before a payment on one of the notes fell due, the venture's property manager sent a letter to each venturer requesting that he pay his proportionate share of the amount due. H.B. Harris, one of the venturers, had previously informed the other venturers that he would not pay his share of future assessments. When Harris failed to pay his share by the specified date, the manager delivered a written notice to Harris informing him that he had ten days to remedy his default. When Harris failed to do so, the manager reduced Harris's interest in the venture from approximately \$776,000 to zero. The written agreement specifically authorized all of the property manager's actions.³ The day after Harris's default, one of the other venturers, acting as Harris's attorney-in-fact pursuant to the terms of the joint venture agreement, executed a deed conveying Harris's interest in the venture to a third party.⁴ The property was ultimately sold

Copyright 1985 David Simon Sokolow.

* B.A., M.A., J.D., Columbia University. Assistant Professor of Law, University of Texas School of Law.

The author wishes to thank Robert W. Hamilton and Leon Lebowitz for their insightful comments on drafts of this Article and Brenda Heinold for her diligent and cheerful research assistance.

1. 673 S.W.2d 600 (Tex. App.—Houston [1st Dist.] 1984, writ ref'd n.r.e.).

2. TEX. REV. CIV. STAT. ANN. art. 6132b, § 42 (Vernon 1970). Although it is possible to distinguish between a joint venture and a partnership, joint ventures are governed by the rules applicable to partners, including partnership statutes. See J. CRANE & A. BROMBERG, LAW OF PARTNERSHIPS § 35, at 192 (1968).

3. 673 S.W.2d at 604.

4. Harris's interest in the venture was conveyed to Mrs. Vivian Smith, the mother-in-law of one of the other venturers. At trial, Harris contended that his coventurers had breached

for a profit, which was apportioned among the remaining venturers.

Harris sued to recover the value of his interest in the venture and his proportionate share of the profits. Despite a jury verdict that Harris had abandoned his interest in the venture, the trial court awarded Harris his interest in the venture and land under TUPA section 42. On appeal the court reversed and barred Harris from recovering against his coventurers because he had intentionally relinquished his interest in the venture.⁵ The court held that Harris was not entitled to judgment based on TUPA section 42.⁶ The court correctly observed that section 42 applies only when the parties have not otherwise agreed on how to settle the account of a partner who withdraws, which the parties did here.⁷ Section 42 expressly permits partners to override the settlement provisions set out there by agreeing to settle accounts in some other manner.⁸ The court ruled that because the joint venture agreement clearly and unequivocally provided for the forfeiture of Harris's interest in the event of default,⁹ Harris could not recover from his coventurers.¹⁰

The court further reasoned that section 42 did not apply because Harris had neither retired from the venture nor died, but had been expelled by his coventurers.¹¹ Although section 42 expressly refers only to a partner who "retires or dies,"¹² a partner who is expelled should be able to exercise his section 42 option¹³ unless he has clearly agreed to forfeit his interest in the partnership.¹⁴ Of course, if he is expelled for breaching the partnership agreement, the remaining partners can maintain a suit against him to recover damages they suffered as a result of his breach.

In *Dunn v. Summerville*¹⁵ the Texas Supreme Court reiterated the general rule that partners share partnership profits equally even if they have contrib-

their fiduciary duty to him by concealing from him Mrs. Smith's willingness to contribute to the venture in exchange for Harris's interest in the venture. The appellate court, however, found it unnecessary to decide whether the venturers' financing activities constituted a breach of their fiduciary duty to Harris because of the jury findings that those activities did not cause any damage to Harris and that Harris had abandoned his interest in the venture. *Id.* at 606.

5. *Id.* at 606-07.

6. *Id.* at 607-08.

7. *Id.* at 608; see TEX. REV. CIV. STAT. ANN. art. 6132b, § 42 (Vernon 1970).

8. TEX. REV. CIV. STAT. ANN. art. 6132b, § 42 (Vernon 1970).

9. See 673 S.W.2d at 608-09 (quoting from the joint venture agreement).

10. *Id.* at 609. In assessing whether forfeiture would be equitable in this case, the court noted that the joint venture agreement also protected a defaulting venturer by providing that the other venturers would not have any recourse against him other than the reduction of his percentage interest in the venture to zero. *Id.*

11. *Id.* at 608.

12. TEX. REV. CIV. STAT. ANN. art. 6132b, § 42 (Vernon 1970).

13. Section 42 permits a partner who retires or the legal representative of a partner who dies to elect to receive from the partners who continue the partnership business either the value of the partner's interest in the partnership as of the date of dissolution with interest or the "profits attributable to the use of his right in the property of the dissolved partnership," unless otherwise agreed. *Id.*

14. *Cf.* *Stone City Attractions, Inc. v. Henderson*, 571 S.W.2d 206, 210 (Tex. Civ. App.—Austin 1978, writ ref'd n.r.e.) (section 42 governs the rights of "outgoing partners" when the partnership business is continued after dissolution).

15. 669 S.W.2d 319 (Tex. 1984) (per curiam).

uted unequal amounts of capital to the partnership, unless they have agreed to split the profits in some other fashion.¹⁶ Because the two partners in *Dunn* had not agreed on how to split the profits, the supreme court held that Summerville could recover one-half of the excess draws taken by Dunn, but not the entire difference between their draws as awarded by the lower court.¹⁷

B. Intrapartnership Liability for Negligence

Partners owe a fiduciary duty to one another that requires "the utmost degree of good faith and honesty in dealing with one another."¹⁸ When a partner breaches his fiduciary duty, as by appropriating partnership property and partnership employees for his personal use, he may be held liable to the injured partners.¹⁹ But what if a partner is simply negligent in conducting partnership affairs? Will he be liable to the other members of the partnership? Surprisingly, virtually no authority on this question exists. In *Ferguson v. Williams*,²⁰ however, the Austin court of appeals held as a matter of law that a partner is not liable to other members of the partnership for negligence in the management or operation of the partnership.²¹

The court's holding signifies that a person who enters into a partnership assumes the risk that one or more of his partners may be negligent. Such a result makes sense; to hold otherwise would require a partner, in effect, to guarantee his capability as a businessman to the other members of the partnership.²²

C. Noncompetition Clauses

In *Henshaw v. Kroenecke*²³ the Texas Supreme Court upheld Henshaw's right to recover liquidated damages from his former partner for breach of a noncompetition clause contained in their original partnership agreement.²⁴ Before forming the partnership Henshaw operated a sole proprietorship offering management consulting services. Henshaw invited Kroenecke to join his business, and in April 1972 they executed a partnership agreement. That agreement contained a clause providing that Kroenecke would not compete with Henshaw by servicing clients of the partnership for three years after the termination of the agreement. If he did, Kroenecke would have to pay Hen-

16. *Id.* (citing *Johnston v. Ballard*, 83 Tex. 486, 487-89, 18 S.W. 686, 686-88 (1892); TEX. REV. CIV. STAT. ANN. art. 6132b, § 18 (Vernon 1970)).

17. 669 S.W.2d at 319.

18. *Veale v. Rose*, 657 S.W.2d 834, 837 (Tex. App.—Corpus Christi 1983, writ ref'd n.r.e.) (citing *Huffington v. Upchurch*, 532 S.W.2d 576, 579 (Tex. 1976); *Fitz-Gerald v. Hull*, 150 Tex. 39, 49-50, 237 S.W.2d 256, 264 (1951)).

19. *Veale v. Rose*, 657 S.W.2d 834, 837 (Tex. App.—Corpus Christi 1983, writ ref'd n.r.e.).

20. 670 S.W.2d 327 (Tex. App.—Austin 1984, writ ref'd n.r.e.).

21. *Id.* at 331.

22. See J. CRANE & A. BROMBERG, *supra* note 2, § 68, at 395 ("In the absence of special agreement, no partner guarantees his own capacity.").

23. 656 S.W.2d 416 (Tex. 1983).

24. *Id.* at 419.

shaw liquidated damages calculated according to a formula set out in the clause.

In October 1974, Henshaw and Kroenecke each formed his own professional corporation. By amendment to the partnership agreement, the corporations were substituted as partners for Henshaw and Kroenecke, but the partnership agreement was otherwise ratified and affirmed. At the same time, the corporations executed a new partnership agreement (the 1974 agreement). The 1974 agreement stated that it did not "alter or amend" the original partnership agreement; however, it contained a separate covenant preventing employees of the two corporations from competing with the new partnership. None of the individuals or corporations involved ever signed this covenant. When a dispute arose in 1976,²⁵ Kroenecke left the firm and took clients with him. After dissolution of the partnership, Henshaw sued Kroenecke to recover liquidated damages for breach of the covenant not to compete contained in the original partnership agreement.

The court of appeals held that only the partnership could enforce the covenant, but the supreme court ruled that Henshaw individually was entitled to the protection of the noncompetition clause.²⁶ In the supreme court's view, the covenant constituted an agreement between Kroenecke and Henshaw individually and not between Kroenecke and the partnership.²⁷ The court reasoned that Henshaw was the business entity both before the partnership began and after it terminated;²⁸ consequently, Henshaw had a legitimate interest in protecting himself from the possibility that Kroenecke would establish rapport with his clients and take them with him upon termination.²⁹ Public policy was also a factor in the decision. The court was concerned that if only the partnership could enforce the covenant, the members of a two-man partnership could never enter into an enforceable non-competition clause; after termination no partnership would remain to enforce the covenant.³⁰ For these reasons, the court determined that the covenant in the original partnership agreement was reasonable and that Henshaw could enforce it.³¹

Over the objection of two dissenting justices,³² the court also held that the original partnership agreement, including the covenant, was integrated into

25. The dispute concerned the original covenant not to compete. Apparently, Kroenecke demanded that the covenant be changed to bind Henshaw as well as himself and that the liquidated damages be fixed in a lump sum. He left a note to that effect for Henshaw, who construed it as a termination of the partnership. *See id.* at 417-18. For a more detailed discussion of the dispute, see *Henshaw v. Kroenecke*, 671 S.W.2d 117, 118-19 (Tex. App.—Houston [1st Dist.] 1984, writ ref'd n.r.e.) (on remand).

26. 656 S.W.2d at 418.

27. *Id.*

28. *Id.*

29. *Id.* (citing *Hospital Consultants, Inc. v. Potyka*, 531 S.W.2d 657, 662 (Tex. Civ. App.—San Antonio 1975, writ ref'd n.r.e.)).

30. 656 S.W.2d at 418.

31. *Id.* The court also held that the liquidated damages provision was reasonable and enforceable. *Id.* at 419.

32. *Id.* at 420-21 (Wallace, J., dissenting). Justice Kilgarlin joined in Justice Wallace's dissent.

the 1974 agreement.³³ Thus, even though the covenant attached to the 1974 agreement had never been signed, the majority concluded that the original covenant continued to bind Kroenecke.³⁴

Although one can quibble with certain aspects of the majority opinion,³⁵ the court clearly reaches a sensible result. The majority's reasoning leaves no doubt that the parties designed the noncompetition clause in the original partnership agreement to protect Henshaw against competition from Kroenecke, and the express language of the original covenant reinforces that conclusion.³⁶ Furthermore, even if the original covenant was not integrated into the 1974 agreement, as the dissent contended,³⁷ the language of the 1974 agreement suggests that the parties intended to supplement, rather than supersede, the original partnership agreement.³⁸ Finally, the circumstances surrounding termination of the partnership in 1976³⁹ indicate that Kroenecke himself recognized Henshaw's right to enforce the original covenant against him. Overall, in terms of policy, the decision in *Henshaw* encourages the judicious use of reasonable noncompetition clauses.

D. Assignment of Interest in a Lease

*Heflin v. Stiles*⁴⁰ involved a landlord-tenant dispute that may have significant ramifications for partnerships that are tenants in Texas. In 1973, Hyden and Stiles, doing business as Hyden-Stiles, G.M.C., Inc., leased a piece of property for a ten-year term from John King. The lease agreement provided that the "Lessee" would not assign the agreement without the written consent of the lessor. Subsequently, Hyden and Stiles sublet the premises to Joe Heflin. Several years later, Heflin purchased the property from King, thereby becoming lessor to Hyden and Stiles under the 1973 lease

33. The majority cited language in both the 1974 agreement ("This agreement does not alter or amend [the original partnership agreement] . . .") and the 1974 amendment to the original partnership agreement ("The parties hereby ratify and reaffirm all provisions of [the original partnership agreement] . . .") to support its holding that the original covenant had been integrated into the 1974 agreement. *Id.* at 419. This language, however, failed to convince the dissent that the parties had intended an integration. Justice Wallace stated that integration was permissible only when it is shown that the parties clearly intended an integration or when it is necessary to clarify the meaning of an ambiguous writing. *Id.* at 421 (Wallace, J., dissenting). Because the 1974 agreement, which contained no signed covenant, was clear and unambiguous, and because neither of the parties suggested otherwise, Justice Wallace concluded that no integration had occurred. *Id.*

34. *Id.* at 419.

35. Despite the court's statement that Henshaw had "substituted his own personal corporation as a partner," *id.* at 417, under the original partnership agreement, the court never entertained the possibility that the corporation was the proper plaintiff in this case. Perhaps this issue had not been argued to the court.

36. The covenant provided in part: "Kroenecke agrees that upon his voluntary termination of this agreement he will not compete with *Henshaw* . . ." *Id.* (quoting the partnership agreement) (emphasis added).

37. See *id.* at 420-21 (Wallace, J., dissenting). For a discussion of the dissenting opinion, see *supra* note 33.

38. The language cited by the majority to show that an integration had occurred, see *supra* note 33, can also be read as evidencing an intent to ensure that the original partnership agreement have continued vitality.

39. See *supra* note 25.

40. 663 S.W.2d 131 (Tex. App.—Fort Worth 1983, no writ).

while continuing as their sublessee. On August 9, 1978, pursuant to a winding up of the partnership, Hyden assigned all of his interest in the 1973 lease to Stiles without obtaining Heflin's consent, written or otherwise. When Heflin learned of the assignment, he stopped paying rent under the sublease and refused to accept rental payments from Stiles. Stiles sued for the back rent. Heflin counterclaimed for termination of the 1973 lease on the ground that Hyden's assignment without consent constituted a breach of the 1973 lease and a violation of Texas landlord and tenant law, article 5237,⁴¹ which also prohibits the assignment of a lease without the lessor's consent.⁴²

Stiles argued that the purported assignment merely effected a dissolution of a partnership between co-lessees, as a result of which he had succeeded to his partner's interest under the lease. Despite the absence of Texas case law on point,⁴³ the court rejected Stiles's interpretation of his written agreement with Hyden.⁴⁴ The court characterized the purpose of both the statute and the similar provision in the lease⁴⁵ as being solely for the benefit of the landlord.⁴⁶ In the court's view, both were intended to allow landlords to determine who would occupy their property and to ensure that landlords would not have impecunious tenants thrust upon them without their consent.⁴⁷ The court also quoted language from two contracts cases to the effect that a party has the right to determine with whom he will contract.⁴⁸ Without further explication,⁴⁹ the court held that the agreement between Hyden and Stiles was an assignment violating both the lease and the statute.⁵⁰

On the surface, the court's decision appears equitable.⁵¹ Arguably, it would have been unfair to Heflin to allow Hyden to substitute Stiles as the sole lessee without Heflin's consent, when Heflin had previously been able to

41. TEX. REV. CIV. STAT. ANN. art. 5237 (Vernon 1962), *repealed by* Act of June 19, 1983, ch. 576, § 6, 1983 Tex. Gen. Laws 3729, 3729-30, *recodified at* TEX. PROP. CODE ANN. § 91.005 (Vernon 1984).

42. The lease went beyond the statute in requiring that the lessor's consent to any assignment be in writing.

43. *See* 663 S.W.2d at 134.

44. *Id.* at 135.

45. *See supra* note 42.

46. 663 S.W.2d at 134 (citing *Fair West Bldg. Corp. v. Trice Floor Coverings*, 394 S.W.2d 707, 708 (Tex. Civ. App.—Fort Worth 1965, no writ)).

47. 663 S.W.2d at 134.

48. *Id.* at 134-35 (quoting *Moore v. Mohon*, 514 S.W.2d 508, 513 (Tex. Civ. App.—Waco 1974, no writ); *Arkansas Valley Smelting Co. v. Belden Mining Co.*, 127 U.S. 379, 387 (1888)).

49. *See infra* note 53.

50. 663 S.W.2d at 135.

51. Although the result in *Heflin* protects lessors from having undesirable lessees foisted upon them by assignment, certain aspects of this case suggest that Heflin himself may not have merited such protection. First, Heflin was not the original lessor in the 1973 lease; thus, this case is not really analogous to the cited cases, in which transferees of contract rights sought to enforce those rights against a party to the original agreement. Heflin conceivably relied on the creditworthiness of both Hyden and Stiles when he purchased the property from King in 1977, but no evidence to that effect was presented. Moreover, Heflin had a strong economic incentive to seek termination of the 1973 lease that derived from his peculiar status as both lessor and sublessee of the property. As sublessee, Heflin paid Hyden and Stiles \$575 per month, while as lessor of the property he received only \$335 per month from them. These facts suggest that Heflin may have been less a victim of an unwanted lessee than a shrewd businessman with a strong desire to escape from a bad bargain. If so, the court's solicitude is misplaced.

rely on the "skill, character or credit"⁵² of both Hyden and Stiles. Nevertheless, the court's emphasis on the landlord-tenant aspects of the case undercuts the importance of the fact that *Heflin* involved a partnership.⁵³ A hypothetical will help to illustrate the possible consequences of the court's holding. Assume that a lessor rents property to a partnership composed of thirty individuals and that one of the partners subsequently retires and assigns his interest in the lease to the other members of the firm. Under the rationale of *Heflin*, the lessor could terminate the lease. One could attempt to distinguish this situation from *Heflin* on the ground that in the hypothetical the partnership as an entity⁵⁴ remained as lessee after the assignment, whereas in *Heflin* no partnership remained after Hyden had withdrawn. A court might not choose, however, to recognize this distinction. In light of these considerations, the legislature should reconsider the effect of article 5237 on assignments of leases among partners.

E. Formation

In *Hasslocher v. Heger*⁵⁵ the primary issue was whether the parties had formed a joint venture to resell a costly diamond. In February 1977 Heger, a jeweler, apprised Hasslocher that the "North Star Diamond" could be purchased for \$300,000. Heger and Hasslocher traveled to Florida where Hasslocher purchased the stone for that amount. One month later, the parties signed a handwritten agreement, drafted by Hasslocher, providing that they would share equally the profits from the resale of the diamond; that Heger would keep the diamond in a safety deposit box while it was in his possession and show it to prospective customers; and that they would sell the diamond for the highest price possible to gain the greatest profit.⁵⁶ Initially, Hasslocher kept the diamond in his safe deposit box; later, he moved it to another box, which both parties were authorized to open. On March 6, 1978, Hasslocher moved the stone to yet another safe deposit box; after that, Heger could show the diamond only if Hasslocher or his wife accompanied him. The stone was never sold.

Heger sought a declaratory judgment that he and Hasslocher had formed a joint venture.⁵⁷ The jury found in Heger's favor, but the appellate court reversed.⁵⁸ Essentially, the court applied the four-prong test for a joint ven-

52. *Moore v. Mohon*, 514 S.W.2d 508, 513 (Tex. Civ. App.—Waco 1974, no writ).

53. The court did consider a case involving a partnership, *Demming v. Republic Nat'l Bank Bldg. Co.*, 294 S.W.2d 888 (Tex. Civ. App.—Dallas 1956, writ ref'd n.r.e.), but distinguished that case as involving the addition, rather than the removal, of a partner. 663 S.W.2d at 134. The court's discussion of *Demming*, however, had no bearing on its ultimate disposition of the instant case.

54. Texas partnership law recognizes a partnership as a distinct legal entity, separate from its partners for most purposes. *Haney v. Fenley, Bate, Deaton & Porter*, 618 S.W.2d 541, 542 (Tex. 1981).

55. 670 S.W.2d 689 (Tex. App.—San Antonio 1984, writ ref'd n.r.e.).

56. *Id.* at 691.

57. Heger also brought suit against Hasslocher for breach of contract, specific performance, and attorney's fees.

58. 670 S.W.2d at 694.

ture⁵⁹ and found that evidence to support three of the four necessary elements was wanting.⁶⁰ First, the court found insufficient evidence of an agreement to share losses.⁶¹ The written agreement was silent as to the sharing of losses; furthermore, Hasslocher had testified that he expected to bear any losses and that he and Heger had never discussed Heger's paying any part of the loss. Second, the court found some evidence that the parties shared a community of interest in the undertaking, but not enough to support the jury's finding.⁶² Apparently, the court was swayed by Heger's testimony that his objective was to gain prominence as a jeweler as well as to derive a profit.⁶³ Finally, the court found little, if any, evidence to support the proposition that the parties had a mutual right of control over the diamond.⁶⁴ Hasslocher's moving the stone to a safe deposit box to which only he had access, his desire to control who saw the stone, and his intention not to sell the stone for a year because of tax considerations demonstrated to the court that Hasslocher alone controlled the diamond.⁶⁵ The court, therefore, held that the parties had not entered into a joint venture and remanded for trial on Heger's other claims.⁶⁶

The court arguably erred in concluding that the parties shared no community of interest. They clearly had a mutual interest in reselling the diamond

59. The four elements of a joint venture are: "(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." *Coastal Plains Dev. Corp. v. Micrea, Inc.*, 572 S.W.2d 285, 287 (Tex. 1978) (citing *Brown v. Cole*, 155 Tex. 624, 631, 291 S.W.2d 704, 709 (1956); *Luling Oil & Gas Co. v. Humble Oil & Ref. Co.*, 144 Tex. 475, 483-84, 191 S.W.2d 716, 722 (1945); *Chandler v. Herndon*, 450 S.W.2d 703, 706 (Tex. Civ. App.—Corpus Christi 1970, writ ref'd n.r.e.)).

60. 670 S.W.2d at 692.

61. *Id.* at 692-93.

62. *Id.* at 693.

63. *Id.*

64. *Id.* at 693-94.

65. *Id.* at 693.

66. See *supra* note 57. The court also considered the propriety of the special issue on joint venture, which recited as an element of a joint venture an "agreement to share losses, costs or expenses." *Id.* at 691 (emphasis added). Based on this special issue, the jury found that the parties had indeed entered into a joint venture agreement. Hasslocher contended that the court's framing of this element in the disjunctive made it impossible to determine whether the jury had in fact found "an agreement to share losses," as required by the Texas Supreme Court. See *supra* note 59. The court acknowledged that the jury had to find that the parties agreed to share the losses, but concluded that the jury could have made such a finding based on the issue submitted. 670 S.W.2d at 692.

Given the disjunctive wording of the issue, however, the jury could have concluded that the parties had entered into a joint venture without finding that they had agreed to share losses. Under the issue submitted, a finding that the parties had agreed to share costs or expenses would have satisfied this element of a joint venture. Although the court noted that the issue had been similarly defined in other cases, *id.* at 691 (citing *Gray v. West*, 608 S.W.2d 771, 777 (Tex. Civ. App.—Amarillo 1980, writ ref'd n.r.e.); *Heinrich v. Wharton County Livestock, Inc.*, 557 S.W.2d 830, 833 (Tex. Civ. App.—Corpus Christi 1977, writ ref'd n.r.e.); *Patton v. Calloway*, 522 S.W.2d 252, 256 (Tex. Civ. App.—El Paso 1975, writ ref'd n.r.e.); *Fry v. Shaw*, 508 S.W.2d 142, 145 (Tex. Civ. App.—Dallas 1974, writ ref'd n.r.e.)), in none of those cases was the wording of the special issue challenged, as it was here. Despite the court's machinations, 670 S.W.2d at 691-92, the charge as submitted was faulty.

for the greatest possible profit;⁶⁷ financially, each expected to derive the same benefit from the resale.⁶⁸ That Heger may have had some additional motivation for participating in the undertaking does not alter that fundamental community of interest. Even so, a contrary finding on this issue would not have changed the result, as two of the other elements of a joint venture were missing.

F. Interest in Partnership Property

A partner's interest in partnership property is "personal property for all purposes" under TUPA.⁶⁹ Consequently, even for purposes of descent and probate distribution, a deceased partner's interest in partnership realty is treated as personal property under TUPA and, as such, is includable in his Texas taxable estate.⁷⁰ In *Humphrey v. Bullock*,⁷¹ however, the decedent's executors contended that Texas common law, rather than TUPA, should apply because the partnership of which the decedent was a partner had been formed before the effective date of TUPA.⁷²

As a preliminary matter, the court focused on the partnership interest that passed under the probate laws,⁷³ rather than on the partnership interest held by the decedent during his lifetime,⁷⁴ because inheritance tax is imposed on the right of succession rather than on the property itself.⁷⁵ Accordingly, the court sought to ascertain how Texas courts had characterized a partner's interest for probate purposes prior to the adoption of TUPA. The court concluded that Texas common law, in contrast to TUPA,⁷⁶ treated real partnership property as realty for probate purposes.⁷⁷ Given this disparity in

67. That interest was manifested in the parties' written agreement. See *supra* text accompanying note 56.

68. Cf. *Brown v. Cole*, 155 Tex. 624, 642, 291 S.W.2d 704, 716 (1956) (Smith, J., dissenting) (suggesting that when all parties derive a material benefit they have a community of interest).

69. TEX. REV. CIV. STAT. ANN. art. 6132b, § 26 (Vernon 1970).

70. Bromberg, *Commentary on the Texas Uniform Partnership Act*, 17 TEX. REV. CIV. STAT. ANN. 360-61 (Vernon 1970).

71. 666 S.W.2d 586 (Tex. App.—Austin 1984, writ ref'd n.r.e.).

72. The executors also contended that the partnership to which the decedent belonged was a mining partnership rather than a general partnership. The distinction is significant because of authority that the assets of a mining partnership should be treated as the partners' individual property. See *id.* at 589 (citing *Munsey v. Mills & Garitty*, 115 Tex. 469, 482-86, 283 S.W. 754, 759-61 (1926)). The court concluded, however, that the partnership was a general partnership. 666 S.W.2d at 590. The court determined that the parties intended to form a general partnership based upon a provision in their written agreement that the partnership would terminate on the death of one of the partners. *Id.* at 589-90. A mining partnership does not dissolve on the death of a partner. *Id.* at 590 (citing *Munsey*, 115 Tex. at 484-86, 283 S.W. at 760-61; W. SUMMERS, *THE LAW OF OIL AND GAS* §§ 742, 735 (1962)).

73. 666 S.W.2d at 589-90 (citing *Blodgett v. Silberman*, 277 U.S. 1 (1928); *Lynch v. Kentucky Tax Comm'n*, 333 S.W.2d 257 (Ky. 1960); *Perkins v. Oklahoma Tax Comm'n*, 428 P.2d 328 (Okla. 1967)).

74. In an earlier portion of its opinion, the court concluded that a partner's interest in partnership property during his lifetime was treated as personalty at common law. 666 S.W.2d at 590-91.

75. *Id.* at 591 (citing *Calvert v. Coke*, 458 S.W.2d 913, 916 (Tex. 1970)).

76. *Id.*; see *supra* text accompanying note 70.

77. *Id.* (citing *Miller v. Howell*, 234 S.W.2d 925, 930 (Tex. Civ. App.—Fort Worth 1950,

treatment, the court had to determine whether it should apply TUPA to the instant facts. As the court noted, partnerships formed before the adoption of TUPA are generally subject to its provisions,⁷⁸ except where the application of TUPA will "impair the partnership contract or affect any right accrued before the [T]UPA took effect."⁷⁹ Because the partnership agreement was silent on how partnership property should descend upon the death of a partner,⁸⁰ the court presumably concluded that the change in the law did not interfere with the partnership agreement.⁸¹ Furthermore, because rights acquired by will⁸² or inheritance⁸³ do not vest until a testator's death, and because the decedent did not die until after TUPA was enacted, the court reasoned that no right had vested before TUPA took effect.⁸⁴ The court, therefore, ruled that it was proper to treat the decedent's partnership interest for estate tax purposes as personalty in accord with the dictates of TUPA.⁸⁵

G. Venue

Before it was revised in 1983, the Texas venue statute did not expressly provide where venue would lie against a partnership.⁸⁶ Courts confronted with this issue had to decide whether a partnership was an association for venue purposes, because the statute did provide where venue would lie against an "association."⁸⁷ There were conflicting results, depending upon whether the court viewed a partnership as an entity separate from the partners, or as an aggregate of individuals. If the court viewed the partnership as an entity and thus an association, venue would lie against the partnership;⁸⁸ if, however, the court viewed it as an aggregate, venue would not lie

no writ); *Ramon v. Ramon*, 10 S.W.2d 584, 585 (Tex. Civ. App.—San Antonio 1928, writ ref'd). The surviving partner could, however, have the property appropriated to settle partnership affairs. See 666 S.W.2d at 591 (citing *Williams v. Dovell*, 202 Md. 351, 96 A.2d 484 (1953); *Wharf v. Wharf*, 306 Ill. 79, 137 N.E. 446 (1922)).

78. 666 S.W.2d at 592 (citing *Smoot v. Smoot*, 568 S.W.2d 177, 180 (Tex. Civ. App.—Dallas 1978, no writ); *McKinney v. Nacogdoches Indep. School Dist.*, 489 S.W.2d 161, 168-69 (Tex. Civ. App.—Tyler 1972), *rev'd on other grounds*, 504 S.W.2d 832, 837-38 (Tex. 1974); *Kelly v. Kelly*, 411 S.W.2d 953, 955 (Tex. Civ. App.—Houston 1967, writ ref'd n.r.e.)).

79. 666 S.W.2d at 591. The quoted language is based on TUPA § 4(5), TEX. REV. CIV. STAT. ANN. art. 6132b, § 4(5) (Vernon 1970), but differs slightly from the wording of that section. Section 4(5) states that TUPA "shall not be construed so as to impair the obligations of any contract existing when [TUPA] goes into effect, nor to affect any . . . right accrued before [TUPA] takes effect." *Id.* (emphasis added).

80. 666 S.W.2d at 592.

81. Although the court did not explicitly discuss the significance of the silence of the partnership agreement on the matter of descent, it apparently found no impairment of the partnership contract because of this silence.

82. 666 S.W.2d at 592 (citing TEX. PROB. CODE ANN. § 37 (Vernon Supp. 1982); *Casey v. Kelly*, 185 S.W.2d 492, 493-94 (Tex. Civ. App.—Fort Worth 1945, writ ref'd)).

83. 666 S.W.2d at 592 (citing *Davis v. First Nat'l Bank*, 139 Tex. 36, 44-45, 161 S.W.2d 467, 472-73 (1942)).

84. 666 S.W.2d at 592 (citing *McCain v. Yost*, 155 Tex. 174, 284 S.W.2d 898 (1955)).

85. 666 S.W.2d at 592.

86. TEX. REV. CIV. STAT. ANN. art. 1995 (Vernon 1964).

87. *Id.* art. 1995(23).

88. See *Haney v. Fenley, Bate, Deaton & Porter*, 618 S.W.2d 541, 542 (Tex. 1981) (per curiam) (interpreting subdivision 23); *Jacox v. Cobb*, 659 S.W.2d 743, 745 (Tex. App.—Tyler 1983, no writ) (interpreting subdivision 4).

against the partnership.⁸⁹ By amending the statute expressly to include the word "partnership," the legislature codified the view that a partnership is an entity for venue purposes and relieved the courts of the burden of making this difficult determination.⁹⁰

In *Seidman & Seidman v. Schwartz*⁹¹ the court held that a partnership's choice of venue against a defendant did not preclude a partner who was being sued as a third-party defendant from asserting his right to be sued in his county of residence. The court correctly reasoned that although the partnership as an entity⁹² owned the cause of action against Schwartz and could choose where to institute its suit against him, that choice did not abrogate the venue rights of a partner being sued as a third-party defendant in his individual capacity.⁹³

H. Miscellaneous Partnership Cases

*Lowry v. Crimmins*⁹⁴ is apparently the first reported case involving TUPA section 36,⁹⁵ which addresses the effect of dissolution on a partner's existing liability for a partnership debt. Unfortunately, the opinion contains only cursory discussion of the statute. The court simply concluded in a footnote that Lowry was not discharged from his liability on a partnership note upon dissolution because he and his partner had never agreed that he would be discharged, as section 36(2) requires.⁹⁶

In *Vick v. George*⁹⁷ the procedural posture of the case on appeal required the court to ascertain whether the plaintiff had presented probative evidence of a partnership or joint venture of which Calvin Vick was a member.⁹⁸ Vick, however, had apparently represented himself, or had allowed himself to be represented, as a partner in an oil drilling venture to prospective investors in the venture.⁹⁹ If such a representation had been made to the investors, Vick would be liable to them as a partner by estoppel under section 16 of TUPA¹⁰⁰ regardless of whether a partnership existed.¹⁰¹ The opinion does

89. See *Noguess v. Border Motor Co.*, 238 S.W.2d 302, 303-04 (Tex. Civ. App.—Beaumont 1951, no writ); *Heid Bros. v. Mueller-Huber Grain Co.*, 185 S.W.2d 470, 471-73 (Tex. Civ. App.—El Paso 1944, no writ).

90. TEX. REV. CIV. STAT. ANN. art. 1995, § 3(f) (Vernon Pam. Supp. 1964-1984).

91. 665 S.W.2d 214 (Tex. App.—San Antonio 1984, writ dismissed w.o.j.).

92. The court recognized that a partnership is "an entity legally distinct from its partners for most purposes" under TUPA. *Id.* at 218 (citing *Haney v. Fenley, Bate, Deaton & Porter*, 618 S.W.2d 541, 542 (Tex. 1981) (per curiam), which in turn cited Bromberg, *Commentary on the Texas Uniform Partnership Act*, 17 TEX. REV. CIV. STAT. ANN. 299, 300 (Vernon 1970)).

93. 665 S.W.2d at 218.

94. 665 S.W.2d 230 (Tex. App.—Eastland 1984, writ granted).

95. TEX. REV. CIV. STAT. ANN. art. 6132b, § 36 (Vernon 1970).

96. 665 S.W.2d at 232 n.4.

97. 671 S.W.2d 541 (Tex. App.—San Antonio 1983), *aff'd in part, rev'd in part and remanded*, 28 Tex. Sup. Ct. J. 168 (Dec. 19, 1984) (per curiam).

98. 671 S.W.2d at 547.

99. *Id.* at 548.

100. TEX. REV. CIV. STAT. ANN. art. 6132b, § 16 (Vernon 1970); see also J. CRANE & A. BROMBERG, *supra* note 2, § 36, at 200 (joint venture may exist by estoppel).

101. Section 16 provides redress to a person who has given credit to the actual or alleged partnership in reliance on the misrepresentation. TEX. REV. CIV. STAT. ANN. art. 6132b,

not clearly show whether this theory was argued to the court.¹⁰²

Finally, in *Corinth Joint Venture v. Lomas & Nettleton Financial Corp.*¹⁰³ the court concluded that a partner had authority to enter into a settlement agreement extending the maturity date of a partnership note, where the agreement effectively preserved the partnership's primary asset from foreclosure.¹⁰⁴ The court reasoned that extending the date of a partnership obligation resembled other actions that courts have deemed to be within a partner's authority, including his borrowing money or giving promissory notes on behalf of the partnership.¹⁰⁵

II. CORPORATIONS

A. Trust Fund Doctrine

In *Henry I. Siegel Co. v. Holliday*¹⁰⁶ the Texas Supreme Court addressed the scope of the trust fund doctrine, which concerns the right of a creditor of a dissolved corporation to recover from those who received the corporation's assets upon dissolution.¹⁰⁷ Edna Holliday and Alfred and Barbara Graham were the officers and directors of Holly Gram, Inc., a Texas corporation that operated a shoe store and two dress shops. Siegel sold merchandise on credit to the dress shops. After approximately one year in business, Mrs. Holliday and the Grahams agreed to dissolve the corporation, but to continue the business as separate proprietorships. Mrs. Holliday took the assets and liabilities of the shoe store and the Grahams took those of the dress shops. None of the creditors of the dress shops, including the plaintiff Siegel, were notified of the dissolution. Holly Gram's assets at the time of dissolution were worth \$20,000; Mrs. Holliday received assets worth \$10,000. After dissolution, Mrs. Holliday paid a total of \$26,000 to various Holly Gram creditors, but did not pay Siegel.¹⁰⁸

Siegel sued Mrs. Holliday and the Grahams on the Holly Gram debt. Although the Grahams had assumed responsibility for the debt under their agreement with Mrs. Holliday, Siegel argued that Mrs. Holliday was personally liable for the debt based on the trust fund doctrine as embodied in article 6.04(A)(3) of the Texas Business Corporation Act (TBCA)¹⁰⁹ and article

§ 16(1) (Vernon 1970). Although the investors in *Vick* gave money rather than credit to the purported partnership in reliance on the representation that Vick was a partner, there is no policy reason to deny them recovery under section 16.

102. The court cited to TUPA § 16, but never discussed § 16's application to the facts. 671 S.W.2d at 547.

103. 667 S.W.2d 593 (Tex. App.—Dallas 1984, writ dismissed w.o.j.).

104. *Id.* at 597.

105. *Id.* (citing *J. CRANE & A. BROMBERG*, *supra* note 2, § 50, at 281). Despite the fact that a judgment implementing certain features of this agreement was later entered, the court held that the partner had not confessed a judgment against the partnership merely by entering into the settlement agreement. 667 S.W.2d at 597; *cf.* TEX. REV. CIV. STAT. ANN. art. 6132b, § 9(3)(d) (Vernon 1970) (partner cannot confess a judgment against the partnership unless authorized by the other partners or unless the partnership business has been abandoned).

106. 663 S.W.2d 824 (Tex. 1984).

107. *See generally* *Hunter v. Fort Worth Capital Corp.*, 620 S.W.2d 547 (Tex. 1981).

108. Siegel's claim was for \$2087.98.

109. TEX. BUS. CORP. ACT ANN. art. 6.04(A)(3) (Vernon 1980). Article 6.04(A)(3) directs

1302—2.07(B) of the Miscellaneous Corporation Laws Act.¹¹⁰ In essence, Siegel contended that Mrs. Holliday, as a director of the dissolved corporation, was a trustee of the corporation's assets for the benefit of its creditors and thus had a fiduciary duty to see that those assets were applied to the creditors' claims on a pro rata basis.¹¹¹ Siegel concluded that Mrs. Holliday was personally liable to it for the full amount of its claim for breaching the duty owed to it as creditor.

A majority of the court rejected Siegel's interpretation of the relevant statutes. The majority construed article 6.04(A)(3) to require that the last board of directors of a dissolved corporation "make a just and equitable distribution of corporate assets to the creditors first and then to the stockholders."¹¹² For the purpose of deciding this case, the majority *assumed* that this language required the directors to distribute the corporate assets pro rata to creditors.¹¹³ According to the majority, the trust fund doctrine creates an equitable lien in favor of creditors on any assets that the directors have preferentially transferred, but does not ordinarily provide a basis for imposing personal liability on the directors.¹¹⁴ The majority recognized, however, that a director may be held personally liable under article 1302—2.07(B) for breach of his duty to make a just and equitable distribution, but only to the extent of the corporate assets that have come into the directors' hands by virtue of the dissolution.¹¹⁵ The majority therefore concluded that Siegel was not entitled to recover against Mrs. Holliday because she had already paid out sums exceeding the value of corporate assets distributed to the Holly Gram directors.¹¹⁶

Justice Ray's dissent characterized this result as patently inequitable¹¹⁷ because it allows directors of a dissolved corporation:

to pick and choose among the creditors they wish to pay, secure in the knowledge that creditors who do not receive their pro rata share will have no claim against them individually so long as the directors pay out at least an amount equal to the corporate assets on hand at dissolution.¹¹⁸

At the core of the dissent is the notion that directors of a dissolving corpora-

that if the assets of a dissolved corporation are inadequate to pay all the corporation's debts, the corporation must apply those assets "so far as they will go to the just and equitable payment" of the debts.

110. TEX. REV. CIV. STAT. ANN. art. 1302—2.07(B) (Vernon 1980). Article 1302—2.07(B) requires the directors and officers, in winding up corporate affairs, to act as trustees for the benefit of creditors.

111. 663 S.W.2d at 826.

112. *Id.* at 827.

113. *Id.* at 826. The court expressly pretermitted the question of whether article 6.04(A)(3) requires a pro rata distribution of assets. The court assumed it did since the issue was not material to the case. *Id.*

114. *Id.* at 827-28. A creditor would have to trace the assets and subject them to his claim. He would be unable to claim the assets, however, if they were held by a bona fide purchaser. *Id.* at 828.

115. *Id.* at 828; see TEX. REV. CIV. STAT. ANN. art. 1302—2.07(B) (Vernon 1980).

116. 663 S.W.2d at 828.

117. *Id.* (Ray, J., dissenting).

118. *Id.*

tion are trustees who are bound as fiduciaries "to administer the corporate assets for the benefit of the creditors";¹¹⁹ as such, they must use reasonable care to pay creditors equally or risk personal liability in excess of the corporate assets distributed to the directors upon dissolution.¹²⁰

Although the language of article 1302—2.07(B) supports the majority's conclusion,¹²¹ the equities weigh heavily in favor of Justice Ray's interpretation. The majority opinion countenances the unequal treatment of corporate creditors. Under the rule adopted in *Siegel*, creditors who learn of a corporation's dissolution and receive payment from the corporation benefit at the expense of creditors who are unaware of the dissolution, even if there has been no fraud or favoritism in payment.¹²² This result is particularly unfair to creditors like *Siegel* who are not informed of the dissolution by the corporation's board of directors as required by statute.¹²³ Furthermore, the majority's concern for the plight of corporate directors seems misplaced. A director ordinarily risks unlimited personal liability for a breach of his fiduciary duty to the corporation and there is no compelling policy reason to constrict that liability in the context of dissolution. Finally, if state law permits the disparate treatment of corporate creditors, the creditors may force the corporation into federal bankruptcy court where equal treatment is assured.¹²⁴ In light of these considerations, the legislature should amend article 1302—2.07(B) to require that the directors of a dissolved corporation ratably distribute the corporation's assets to its creditors.

B. Piercing the Corporate Veil

Cases involving the doctrine of piercing the corporate veil are susceptible of two generalizations: (1) courts are more likely to pierce the corporate veil when the defendant is a corporation than when it is an individual;¹²⁵ and (2) courts are more willing to pierce the corporate veil in a tort case than in a breach of contract case.¹²⁶ In *Lucas v. Texas Industries, Inc.*,¹²⁷ however, the Texas Supreme Court refused to hold a parent corporation liable for the tortious act of its subsidiary. A beam manufactured by Texas Structural Products, Inc. (Structural) had injured Randall Lucas. He sued Texas Industries, Inc. (TXI), Structural's corporate parent, to recover for his injuries.

119. *Id.*

120. *Id.* at 828-29.

121. See *supra* note 115 and accompanying text. Justice Ray argued that the language "merely restates the basic principle that in normal circumstances the officers and directors of a dissolved corporation need only ratably distribute the assets at dissolution and nothing more." 663 S.W.2d at 830 (Ray, J., dissenting).

122. *Siegel* did not allege fraud or favoritism in this instance. 663 S.W.2d at 826.

123. See TEX. BUS. CORP. ACT ANN. art. 6.04(A)(2) (Vernon 1980); 663 S.W.2d at 826.

124. 11 U.S.C. § 303 (1982).

125. 19 R. HAMILTON, BUSINESS ORGANIZATIONS § 234, at 235 (Texas Practice 1973).

126. *Lucas v. Texas Indus., Inc.*, 27 Tex. Sup. Ct. J. 491, 492 (July 11, 1984) (citing 1 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 43 (Supp. 1982)). The theory underlying this generalization is that a contract plaintiff voluntarily dealt with an undercapitalized corporation, but a tort plaintiff did not. See 19 R. HAMILTON, *supra* note 125, § 234, at 226-27.

127. 27 Tex. Sup. Ct. J. 491 (July 11, 1984).

Lucas presented evidence at trial that TXI and Structural had several common officers and directors, filed a consolidated income tax return, and used the same corporate logo. Lucas further showed that TXI suggested the safety procedures to be used in Structural's plants, loaned Structural money, and delivered the injury-causing beam to the jobsite. He also demonstrated that the Structural officer who had signed a contract related to the job on which Lucas was injured signed on a line labeled "Texas Industries, Inc."¹²⁸ Based on this evidence, the trial court held that Structural was the alter ego of TXI and awarded Lucas damages against TXI. The court of appeals affirmed,¹²⁹ and TXI appealed.

The Texas Supreme Court initially observed that a parent corporation will not be liable for the obligations of a subsidiary merely because of a unity of financial interest, ownership, and control.¹³⁰ Liability will be imposed on the parent only if "the subsidiary is being used as a sham to perpetrate a fraud, to avoid liability, to avoid the effect of a statute, or in other exceptional circumstances."¹³¹ The court then distinguished alter ego cases based on tort claims from those based on contract claims. The court stated that in a tort case like *Lucas*, "the financial strength or weakness of the corporate tortfeasor is an important consideration."¹³² Other language in the opinion suggested, however, that the financial strength or weakness of the subsidiary is virtually the only consideration in assessing whether the corporate veil of the parent should be pierced.¹³³ The court concluded that no evidence was presented to show "that Structural was undercapitalized or was incapable of paying a possible judgment."¹³⁴

The court also concluded that neither the companies' common directors, nor their consolidated tax return, nor their shared logo, nor their intercorporate business transactions "induce[d] Lucas to fall victim to a basically unfair device by which Structural's corporate entity was used to achieve an inequitable result."¹³⁵ Although the truth of this conclusion cannot be gainsaid, the court's use of the concept of "inducement" in an alter ego case

128. *Id.* at 493.

129. *Texas Indus., Inc. v. Lucas*, 634 S.W.2d 748 (Tex. App.—Houston [14th Dist.] 1982), *rev'd in part, remanded in part*, 27 Tex. Sup. Ct. J. 491 (July 11, 1984).

130. 27 Tex. Sup. Ct. J. at 492 (citing *Hanson Sw. Corp. v. Dal-Mac Constr. Co.*, 554 S.W.2d 712, 716-17 (Tex. Civ. App.—Dallas 1977, writ *ref'd n.r.e.*)).

131. 27 Tex. Sup. Ct. J. at 492 (citing *Torregrossa v. Szalc*, 603 S.W.2d 803, 804 (Tex. 1980); *Pace Corp. v. Jackson*, 155 Tex. 179, 194-95, 284 S.W.2d 340, 351 (1955)).

132. 27 Tex. Sup. Ct. J. at 492 (citing *Gentry v. Credit Plan Corp.*, 528 S.W.2d 571, 573 (Tex. 1975)).

133. The court stated:

If the corporation responsible for the plaintiff's injury is capable of paying a judgment upon proof of liability, then no reason would exist to attempt to pierce the corporate veil and have shareholders pay for the injury. If, however, the corporat[ion] sued is not reasonably capitalized in light of the nature and risk of its business, the need might arise to attempt to pierce the corporate veil and hold the parent corporation liable.

27 Tex. Sup. Ct. J. at 492.

134. *Id.* at 493.

135. *Id.* (citing *Torregrossa v. Szalc*, 603 S.W.2d 803, 804 (Tex. 1980)).

based on a tort claim is inappropriate.¹³⁶ Tort victims are rarely induced to be the victim of one tortfeasor rather than another.

As a final matter, the court disapproved of the wording of the special issue on alter ego liability. The special issue asked the jury whether the activities of TXI and Structural had become "so blended that [Structural] for all practical purposes became the alter ego of [TXI]."¹³⁷ The court concluded that a blending of activities alone cannot support the imposition of alter ego liability on the parent corporation.¹³⁸

The tone as well as the language of *Lucas* suggest that it may be more difficult in the future for plaintiffs to recover in tort cases on an alter ego theory than it has been in the past. After *Lucas* a tort plaintiff will probably be unable to reach the parent corporation's assets if the subsidiary corporation is adequately capitalized.

In *Edwards Co. v. Monogram Industries, Inc.*,¹³⁹ discussed in last year's *Survey*,¹⁴⁰ a Fifth Circuit panel concluded that a creditor may sue a parent corporation for the debts of its subsidiary when the parent uses the subsidiary as a mere conduit.¹⁴¹ Applying this standard, the panel held Monogram liable for the contractual obligation of its subsidiary. Recently, however, a majority of the Fifth Circuit, sitting en banc, ruled that the panel had applied the wrong legal standard and reversed.¹⁴² The court reviewed at length the decisions of the Texas courts in this area,¹⁴³ and held that in order to pierce a parent corporation's corporate veil on a contract claim in Texas, a plaintiff must show either that the parent used the subsidiary for fraud or that some other injustice is present.¹⁴⁴ The court concluded that the plaintiff could not recover from the parent on its contract claim since it had failed to make such a showing.¹⁴⁵

Judge Jolly, author of the original panel opinion, dissented. He claimed that the majority had not merely interpreted Texas law, but had decided doubtful legal questions that the Texas courts had clearly avoided deciding.¹⁴⁶ Judge Jolly also observed that one could cite the Texas cases in this area as authority for nearly any position advanced on the issue.¹⁴⁷

Although cases in this area are difficult to reconcile, the majority opinion

136. Inducement seems more appropriate in a contract context, where the parties are bargaining with one another in an attempt to strike a deal.

137. 27 Tex. Sup. Ct. J. at 493.

138. *Id.*

139. 700 F.2d 994 (5th Cir. 1983), *rev'd en banc*, 730 F.2d 977 (5th Cir. 1984).

140. See Hamilton, *Corporations and Partnerships, Annual Survey of Texas Law*, 38 Sw. L.J. 235, 264-65 (1984).

141. 700 F.2d at 995.

142. 730 F.2d 977 (5th Cir. 1984) (en banc).

143. *Id.* at 980-83; see, e.g., *Gentry v. Credit Plan Corp.*, 528 S.W.2d 571 (Tex. 1975); *Bell Oil & Gas Co. v. Allied Chem. Corp.*, 431 S.W.2d 336 (Tex. 1968); *First Nat'l Bank v. Gamble*, 134 Tex. 112, 132 S.W.2d 100 (1939).

144. 730 F.2d at 983-84.

145. *Id.* at 984. The court also stated in a dictum that the panel had erred in concluding that the subsidiary had no separate existence from the parent. *Id.* at 984-87.

146. *Id.* at 987 (Jolly, J., dissenting).

147. *Id.*

accurately mirrors the unwillingness of the Texas courts to pierce the corporate veil in contracts cases in the absence of fraud or other exceptional circumstances.¹⁴⁸ The language of the majority opinion is perhaps more categorical than Texas decisions in this area, but is entirely consistent with their spirit.

In *Sabine Towing & Transportation Co. v. Merit Ventures, Inc.*¹⁴⁹ the federal district court permitted the creditor of a bankrupt subsidiary to recover from the parent corporation on a contract debt. Applying fifteen factors developed from existing case law,¹⁵⁰ the court concluded that the subsidiary was not a "full fledged" corporate entity.¹⁵¹ To avoid fundamental injustice to the creditor, the court pierced the parent's corporate veil.¹⁵² Although the court was not bound by Texas law because it sat as a court of admiralty,¹⁵³ the court cited the panel in *Edwards* on several occasions.¹⁵⁴ Under the stricter standard for alter ego liability in contract cases subsequently adopted in the Fifth Circuit's en banc opinion in *Edwards*,¹⁵⁵ however, the parent corporation in this case would not have been liable.¹⁵⁶

In *Nelson v. International Paint Co.*¹⁵⁷ the plaintiff sought to hold a parent corporation liable on a products liability claim against the subsidiary. Although the parent owned 100% of the subsidiary's stock and had several directors in common with the subsidiary, the Fifth Circuit affirmed the sum-

148. See, e.g., *Torregrossa v. Szelc*, 603 S.W.2d 803, 804 (Tex. 1980); *Bell Oil & Gas Co. v. Allied Chem. Corp.*, 431 S.W.2d 336, 339 (Tex. 1975) (quoting *State v. Swift & Co.*, 187 S.W.2d 127, 131-32 (Tex. Civ. App.—Austin 1945, writ ref'd)).

149. 575 F. Supp. 1442 (E.D. Tex. 1983).

150. *Id.* at 1446-48 (citing *Andrew Martin Marine Corp. v. Stork-Werkspoor Diesel B.V.*, 480 F. Supp. 1270, 1276-77 (E.D. La. 1979); *Bay Sound Transp. Co. v. United States*, 350 F. Supp. 420, 426-27 (S.D. Tex. 1972)). The fifteen factors cited were: (1) common or overlapping stock ownership between the parent and the subsidiary; (2) common or overlapping directors and officers; (3) use of the same corporate office; (4) inadequate capitalization of the subsidiary; (5) financing of the subsidiary by the parent; (6) whether the parent existed solely as a holding company for its subsidiaries; (7) the parent's use of the subsidiary's property and assets as its own; (8) the nature of intercorporate loan transactions; (9) incorporation of the subsidiary being caused by the parent; (10) whether the parent and the subsidiary file consolidated income tax returns; (11) decision-making for the subsidiary by the parent and its principals; (12) whether the directors of the subsidiary act independently in the interest of the subsidiary; (13) the making of contracts between the parent and subsidiary that are more favorable to the parent; (14) observance of formal legal requirements; (15) the existence of fraud, wrong-doing, or injustice to third parties. 575 F. Supp. at 1446-48.

151. 575 F. Supp. at 1448.

152. *Id.* at 1449.

153. *Id.* at 1446. The court applied federal common law, rather than the law of any particular state. *Id.* (citing *Talen's Landing Inc. v. M/V Venture*, 656 F.2d 1157, 1160 (5th Cir. 1981)).

154. 575 F. Supp. at 1446, 1448; see *Edwards Co. v. Monogram Indus., Inc.*, 713 F.2d 139 (5th Cir. 1983) (panel's denial of rehearing after its initial decision published in 700 F.2d 994 (5th Cir. 1983), *rev'd en banc*, 730 F.2d 977 (5th Cir. 1984)).

155. 730 F.2d 977 (5th Cir. 1984); see *supra* notes 142-48 and accompanying text.

156. Some evidence presented at the trial indicated that the initial capitalization of the subsidiary was inadequate to cover the corporation's expected liabilities. 575 F. Supp. at 1447. Other evidence, however, revealed that the subsidiary had enough money during several years of its operation to make loans to sister corporations, *id.*, and to pay off a \$1,000,000 bank note, *id.* at 1445.

157. 734 F.2d 1084 (5th Cir. 1984).

mary judgment in favor of the parent.¹⁵⁸ The parent did not finance the subsidiary, nor did any evidence show that the subsidiary was undercapitalized. The companies kept separate financial records, had separate operating officers, had no mutual employees, maintained their own factories, and secured their own raw materials. Furthermore, the subsidiary paid the parent for any research and development information it received and bore its share of joint advertising expenses. The court thus concluded that the two companies were operated as separate entities and refused to pierce the corporate veil.¹⁵⁹

C. Procedural Considerations

Pleading

Failure to plead properly may have untoward consequences for both plaintiffs and defendants in suits involving corporations. A corporate officer who is sued in his individual capacity and who fails to make a verified denial of liability in his individual capacity under rule 93(c)¹⁶⁰ runs the risk that a court will find him individually liable even in the absence of a finding that the corporation functioned as his alter ego.¹⁶¹ In such a case, the court is not required to pierce the corporate veil because the plaintiff has not alleged that the individual defendant was hiding behind one.¹⁶² On the other hand, when individual liability is predicated on an alter ego theory the plaintiff must plead that theory.¹⁶³ Regardless of the theory upon which the plaintiff bases his claim, he must prove his right to recover from the defendant in the capacity in which the defendant is sued in order to prevail on the merits.¹⁶⁴

158. *Id.* at 1093-94. The court cited *Gentry v. Credit Plan Corp.*, 528 S.W.2d 571, 573 (Tex. 1975), for the proposition that a subsidiary will not be considered the alter ego of its parent "merely because of stock ownership, a duplication of some or all of the directors or officers, or an exercise of the control that stock ownership gives to stockholders." 734 F.2d at 1092.

159. 734 F.2d at 1093.

160. TEX. R. CIV. P. 93(c) (Vernon 1979), amended by and recodified at TEX. R. CIV. P. 93(2) (Supp. 1985).

161. See *Kersh & Sons, Inc. v. Texas Employers' Ins. Ass'n*, 675 S.W.2d 775, 776 (Tex. App.—Beaumont 1984, no writ) (citing *Butler v. Joseph's Wine Shop, Inc.*, 633 S.W.2d 926, 930 (Tex. App.—Houston [14th Dist.] 1982, writ ref'd n.r.e.); *Robertson v. Bland*, 517 S.W.2d 676, 680 (Tex. Civ. App.—Houston [1st Dist.] 1974, writ dismissed). *Kersh* held that the corporation's officers could be individually liable for premiums due on workers' compensation insurance, even though they had signed the application in their capacity as officers, since they had failed to make a verified denial of individual liability. 675 S.W.2d at 776; see also *Duval County Ranch Co. v. Wooldridge*, 674 S.W.2d 332, 337 (Tex. App.—Austin 1984, no writ) (also citing *Butler*).

162. See, e.g., *Light v. Wilson*, 663 S.W.2d 813, 814 (Tex. 1984); *Butler v. Joseph's Wine Shop, Inc.*, 633 S.W.2d 926, 929 (Tex. App.—Houston [14th Dist.] 1982, writ ref'd n.r.e.); *Gray v. West*, 608 S.W.2d 771, 778 (Tex. Civ. App.—Amarillo 1980, writ ref'd n.r.e.).

163. *Light v. Wilson*, 663 S.W.2d 813, 814 (Tex. 1984). The Texas Supreme Court in *Light* held that a corporation's sole owner could not be personally liable for the corporation's fraud when the owner did not individually violate the law and the plaintiff had failed to plead the alter ego theory. *Id.*

164. See *id.* at 814-15.

Jurisdiction

In *Helicopteros Nacionales de Colombia, S.A. v. Hall*¹⁶⁵ the United States Supreme Court held that a Colombian corporation was not amenable to the jurisdiction of Texas courts because the corporation's contacts with Texas were insufficient to satisfy the requirements of due process.¹⁶⁶ Defendant Helicol did not have a place of business in Texas and had never been authorized to do business there. Helicol did, however, have numerous contacts with Texas including: sending its chief executive officer to Houston for a contract-negotiating session; accepting into its New York bank account checks drawn on a Texas bank; purchasing more than \$4,000,000 worth of equipment from a firm in Texas; and sending personnel to the Texas firm for training. The parties conceded that the plaintiffs' wrongful death action "did not 'arise out of,' and [was] not related to, Helicol's activities in Texas."¹⁶⁷ The only question before the Court, therefore, was whether Helicol's contacts with Texas constituted "the kind of continuous and systematic general business contacts"¹⁶⁸ that would justify the exercise of jurisdiction over Helicol.

The Supreme Court concluded they did not. The executive's single trip to Texas was not continuous and systematic enough contact in the Court's view to support an assertion of jurisdiction.¹⁶⁹ Moreover, the Court observed that the bank on which a check is drawn is ordinarily determined by the unilateral act of the drawer;¹⁷⁰ thus, the Texas checks were not an appropriate consideration in determining whether a drawee had sufficient contacts with a forum to justify the assertion of jurisdiction.¹⁷¹ Finally, relying on a 1923 precedent, *Rosenberg Bros. & Co. v. Curtis Brown Co.*,¹⁷² the Court determined that Helicol's purchases from the Texas firm and related trips to Texas taken by Helicol's employees were not a sufficient basis to assert jurisdiction.¹⁷³ The Court, therefore, concluded that Helicol was not subject to

165. 104 S. Ct. 1868, 80 L. Ed. 2d 404 (1984).

166. *Id.* at 1874, 80 L. Ed. 2d at 414.

167. *Id.* at 1872-73, 80 L. Ed. 2d at 410. Because the parties had not argued any relationship between the plaintiffs' claim and Helicol's contacts with Texas, and the majority expressed no view with respect to that issue. *Id.* at 1873 n.10, 80 L. Ed. 2d at 411-12 n.10.

The Court also refrained from addressing the conclusion of the Texas Supreme Court, *Hall v. Helicopteros Nacionales de Colombia, S.A.*, 638 S.W.2d 870, 872 (Tex. 1982), that Texas's long-arm statute, TEX. REV. CIV. STAT. ANN. art. 2031b (Vernon 1964 & Supp. 1985), reaches as far as the due process clause permits. 104 S. Ct. at 1871 n.7, 80 L. Ed. 2d at 410 n.7. For a discussion of that issue, see Sokolow, *Corporations and Partnerships, Annual Survey of Texas Law*, 37 Sw. L.J. 165, 176-77 (1983) and the articles cited at 177 n.107.

168. 104 S. Ct. at 1873, 80 L. Ed. 2d at 412 (applying the test set out in *Perkins v. Benguet Consol. Mining Co.*, 342 U.S. 437, 438 (1952)).

169. 104 S. Ct. at 1873, 80 L. Ed. 2d at 412.

170. *Id.* at 1873, 80 L. Ed. 2d at 412.

171. *Id.* at 1873, 80 L. Ed. 2d at 412-13 (citing *Kulko v. California Superior Court*, 436 U.S. 84, 92 (1978); *Hansen v. Denckla*, 357 U.S. 235, 238 (1958)).

172. 260 U.S. 516, 518 (1923).

173. 104 S. Ct. at 1873-74, 80 L. Ed. 2d at 412-13 (visits on business unrelated to the cause of action "even if occurring at regular intervals, would not warrant the inference that the corporate defendant was present within the [forum] jurisdiction") (citing *Rosenberg Bros. & Co. v. Curtis Brown Co.*, 260 U.S. 516, 518 (1923)).

suit in Texas courts.¹⁷⁴

Justice Brennan, in dissent, questioned whether the narrow view of in personam jurisdiction embodied in *Rosenberg* continued to have vitality in light of the trend toward expanding the scope of permissible jurisdiction over non-resident defendants that began with *International Shoe Co. v. Washington* in 1945.¹⁷⁵ In his view, the exercise of jurisdiction was proper because of Helicol's continuous commercial contacts with Texas.¹⁷⁶ A noted authority on jurisdictional matters concurs.¹⁷⁷

In *C&H Transportation Co. v. Jensen & Reynolds Construction Co.*¹⁷⁸ the Fifth Circuit held that the exercise of jurisdiction over a California corporation under article 2031b¹⁷⁹ did not comport with the due process requirement that a defendant have some minimum contacts with the forum state resulting from an affirmative act on its part.¹⁸⁰ The defendant had contracted to have the plaintiff, a Texas corporation, transport equipment from Louisiana to Washington. The defendant's only contacts with Texas consisted of: a single three-way telephone conference call between defendant's president in Washington and the plaintiff's representatives in Washington and Texas; movement of the equipment through Texas; and defendant's mailing a payment check to plaintiff's office in Dallas. Relying on *Hydrokinetics, Inc. v. Alaska Mechanical, Inc.*,¹⁸¹ the court concluded that the totality of these contacts—a single telephone call involving Texas, the fortuitous routing of equipment through Texas,¹⁸² and the mailing of a single payment check to Texas—did not support an inference that the defendant had purposely availed itself of the privilege of conducting business in Texas.¹⁸³ As in *Hydrokinetics*, the significant factor was that only a single, isolated transaction was involved. Assuming that the contract was formed during the conference call,¹⁸⁴ it is curious that the court did not consider whether the contract had been formed in Texas. Texas state courts and the Fifth Circuit both have considered the place of formation important in assessing whether the exercise of jurisdiction is proper.¹⁸⁵

174. 104 S. Ct. at 1874, 80 L. Ed. 2d at 414.

175. *Id.* at 1875-77, 80 L. Ed. 2d at 415-17 (Brennan, J., dissenting); see *International Shoe Co. v. Washington*, 326 U.S. 310 (1945).

176. 104 S. Ct. at 1877, 80 L. Ed. 2d at 417 (Brennan, J., dissenting). Justice Brennan also argued that Helicol was subject to suit in Texas because the plaintiffs' claim was directly and significantly related to Helicol's Texas contacts. *Id.* at 1878, 80 L. Ed. 2d at 418.

177. See Weintraub, *Due Process Limitations on the Personal Jurisdiction of State Courts: Time for a Change*, 63 ORE. L. REV. 485, 528-30 (1984).

178. 719 F.2d 1267 (5th Cir. 1983), *cert. denied*, 104 S. Ct. 1930, 80 L. Ed. 2d 475 (1984).

179. TEX. REV. CIV. STAT. ANN. art. 2031b (Vernon 1964) (Texas long-arm statute).

180. 719 F.2d at 1269 (citing *Hydrokinetics, Inc. v. Alaska Mechanical, Inc.*, 700 F.2d 1026, 1028 (5th Cir. 1983), *cert. denied*, 104 S. Ct. 2180, 80 L. Ed. 2d 561 (1984); *S.W. Offset, Inc. v. Hudco Publishing Co.*, 622 F.2d 149, 152 (5th Cir. 1980)).

181. 700 F.2d 1026 (5th Cir. 1983), *cert. denied*, 104 S. Ct. 2180, 80 L. Ed. 2d 561 (1984).

182. The court pointed out that performance of the plaintiff's duty under the contract—delivery of the equipment—was to occur not in Texas, but in the state of Washington. 719 F.2d at 1270.

183. *Id.*

184. *Id.* at 1269 n.5.

185. See, e.g., *Product Promotions, Inc. v. Cousteau*, 495 F.2d 483, 495 (5th Cir. 1974); U-

In *C.W. Brown Machine Shop, Inc. v. Stanley Machinery Co.*¹⁸⁶ the Fort Worth court of appeals held that a Massachusetts corporation did not subject itself to jurisdiction in Texas merely by advertising in national publications distributed in Texas.¹⁸⁷ The court's opinion tracked the Fifth Circuit's reasoning in *Loumar, Inc. v. Smith*,¹⁸⁸ which the court characterized as a "strikingly similar" case.¹⁸⁹ Insofar as the nonresident defendant in *Stanley Machinery* had not solicited business in Texas by direct mailings to Texas residents or advertised in Texas publications,¹⁹⁰ its position is analogous to that of the defendant in *Loumar*. The cases are distinguishable, however, in one significant respect. The defendant seller in *Stanley Machinery* had paid freight charges for shipment to Texas. This suggests that performance under the contract—delivery of the goods—was to take place in Texas. In *Loumar* the goods were shipped "F.O.B. Maryland"; thus, delivery was to be in Maryland. The fact that a contract is to be performed in Texas has long been considered significant in assessing whether the assertion of jurisdiction over a nonresident defendant comports with due process.¹⁹¹ Consequently, one may argue that subjecting the defendant in *Stanley Machinery* to suit in Texas would not have offended "notions of fair play and substantial justice."¹⁹² The court, however, held otherwise.

In *Stabler v. New York Times Co.*¹⁹³ the federal district court rejected the argument that subjecting the New York Times Company to jurisdiction in Texas would chill constitutionally protected speech and violate due process, when the allegedly defamatory article would have a foreseeable adverse effect on the plaintiff's reputation in Texas.¹⁹⁴ While acknowledging that a court should consider the first amendment rights of a nonresident media

Anchor Advertising, Inc. v. Burt, 553 S.W.2d 760, 763 (Tex. 1977), cert. denied, 434 U.S. 1063 (1978).

186. 670 S.W.2d 791 (Tex. App.—Fort Worth 1984, no writ).

187. *Id.* at 793-94.

188. 698 F.2d 759 (5th Cir. 1983). In *Loumar* the Fifth Circuit acknowledged that advertising in nationally circulated trade publications might be sufficient to subject a corporate defendant to suit in a state in which the publication circulates. *Id.* at 763 (citing *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 295 (1980)). The court concluded, however, that the Supreme Court in *Woodson* had not held that "advertising reasonably calculated to reach the state would, without more, permit assertion of personal jurisdiction over the advertiser." 698 F.2d at 764. Furthermore, because the nonresident defendant in *Loumar* had not advertised in Texas telephone directories or local Texas publications, the Fifth Circuit was not constrained by a decision of the Texas Supreme Court upholding the assertion of jurisdiction over a nonresident defendant who had advertised in national publications circulated in Texas as well as in Texas telephone directories. *Id.*; see *Siskind v. Villa Foundation*, 642 S.W.2d 434, 436-37 (Tex. 1982).

189. 670 S.W.2d at 793.

190. *Id.*

191. See, e.g., *C&H Transp. Co. v. Jensen & Reynolds Constr. Co.*, 719 F.2d 1267, 1271 (5th Cir. 1983); *Hydrokinetics, Inc. v. Alaska Mechanical, Inc.*, 700 F.2d 1026, 1029 (5th Cir. 1983); *Product Promotions, Inc. v. Cousteau*, 495 F.2d 483, 496 (5th Cir. 1974); *Gubitosi v. Buddy Schoellkopf Prod., Inc.*, 545 S.W.2d 528, 535 (Tex. Civ. App.—Tyler 1976, no writ).

192. *International Shoe Co. v. Washington*, 326 U.S. 310, 320 (1945).

193. 569 F. Supp. 1131 (S.D. Tex. 1983).

194. *Id.* at 1135 (citing *Edwards v. Associated Press*, 512 F.2d 258, 263 (5th Cir. 1975); *Curtis Publishing Co. v. Golino*, 383 F.2d 586, 588 (5th Cir. 1967); *Buckley v. New York Times Co.*, 338 F.2d 470, 472 (5th Cir. 1964)).

defendant in determining whether the exercise of jurisdiction is proper, the court concluded that those rights are not controlling.¹⁹⁵

Several cases decided during the survey period involved a default judgment entered against a corporate defendant who had failed to make an appearance. In *Dan Edge Motors, Inc. v. Scott*¹⁹⁶ Scott filed suit against Dan Edge Motors, Inc., a Texas corporation. A citation was issued to "Dan Edge, Dan Edge Motors, Inc." and was served by leaving a copy with Edge, the corporation's president. Although the court recognized that a domestic corporation may be served by delivering the citation to its president,¹⁹⁷ the court held that the citation was insufficient to confer jurisdiction over the corporation because the citation was not issued in the name of the corporation, but in the name of its agent.¹⁹⁸

In *General Office Outfitters, Inc. v. Holt*¹⁹⁹ the plaintiff had secured a default judgment based on substituted service on the secretary of state under section 2.11(B) of the TBCA.²⁰⁰ The plaintiff in her petition alleged that she had used due diligence to serve the corporation's registered agent and incorporated the affidavit of a deputy constable stating that he had attempted service on the corporation's registered agent but had been unable to locate the agent at the corporation's registered address. On appeal, the court held that the affidavit would not support substituted service because it failed to detail the actual diligence the constable had used.²⁰¹

The Houston court of appeals upheld a default judgment based on substituted service in *Tankard-Smith, Inc. v. Thursby*.²⁰² Having tried unsuccessfully to serve in person the corporation's registered agent at its registered address, the plaintiff made substituted service on the secretary of state. The secretary in turn mailed a copy of plaintiff's citation to the corporation's registered address in accordance with section 2.11(B),²⁰³ but the copy was returned bearing the notation "address insufficient." The trial court entered a default judgment against the defendant. The defendant argued on appeal that the substituted service was improper because defendant had not received a copy of the citation. The court, however, concluded that the defendant itself was responsible for this situation since it had failed to notify

195. 569 F. Supp. at 1136. The court in *Stabler* found significant the fact that the *Times* maintained a permanent news bureau in Texas, staffed by two reporters and a secretary, and sold more than one million copies of the newspaper in Texas every year. *Id.* at 1135. The court distinguished *New York Times Co. v. Connor*, 365 F.2d 567 (5th Cir. 1966), on the ground that the *Times*'s circulation in Texas was much greater in *Stabler* than in *Connor*. 569 F. Supp. at 1135.

196. 657 S.W.2d 822 (Tex. App.—Texarkana 1983, no writ).

197. *Id.* at 823 (citing TEX. BUS. CORP. ACT ANN. art. 2.11 (Vernon 1980)).

198. 657 S.W.2d at 823 (citing *Temple Lumber Co. v. McDaniel*, 24 S.W.2d 518, 519 (Tex. Civ. App.—Beaumont 1930, no writ)).

199. 670 S.W.2d 748 (Tex. App.—Dallas 1984, no writ).

200. TEX. BUS. CORP. ACT ANN. art. 2.11(B) (Vernon 1980).

201. *Id.* at 749-50. The court suggested that the affidavit should describe each attempt made to serve the agent. *Id.*; see *Harrison v. Dallas Court Reporting College*, 589 S.W.2d 813, 815 (Tex. Civ. App.—Dallas 1979, no writ) (suggesting in a dictum that an affidavit ought to show how many attempts of service were made and the times at which service was attempted).

202. 663 S.W.2d 473 (Tex. App.—Houston [14th Dist.] 1983, writ ref'd n.r.e.).

203. TEX. BUS. CORP. ACT ANN. art. 2.11(B) (Vernon 1980).

the secretary of state of a change in its registered address, as section 8.09 of the TBCA requires.²⁰⁴ The court thus affirmed the default judgment.²⁰⁵

Finally, in *Minexa Arizona, Inc. v. Staubach*²⁰⁶ an Arizona corporation failed to convince the court that the plaintiffs were required to serve process on the corporation by serving the secretary of state under article 2031b(3).²⁰⁷ The plaintiffs' pleadings alleged that the defendant corporation, though not registered to do business in Texas, maintained a regular place of business in Texas. For this reason, the court correctly held that the plaintiffs had properly served the corporation under article 2031b(2)²⁰⁸ by leaving a copy of the process with the corporation's vice-president, who was in charge of the corporation's business in Texas at the time of service.²⁰⁹

Venue

One of the more significant changes wrought by the legislature in its 1983 revision of the Texas venue statute was the elimination of interlocutory appeals of venue questions.²¹⁰ The legislature provided, however, that the statutory revisions would not apply to appeals of venue questions "pending" on September 1, 1983, the effective date of the revisions.²¹¹ In *Grubbs v. Mercantile Texas Corp.*²¹² the court refused to hear an interlocutory venue appeal on the ground that the appeal was not "pending" on September 1, 1983.²¹³ A hearing on the corporate defendant's plea of privilege had been held on July 28, 1983, but the order sustaining the plea was not signed until October 3, 1983. The court in *Graue Haws v. Fuller*²¹⁴ reached the same result on similar facts.²¹⁵ Although one may argue that this result is unfair to the plaintiffs because the "rules [were] changed in the middle of the game,"²¹⁶ the courts' interpretation comports with the plain meaning of the

204. 663 S.W.2d at 475-76; TEX. BUS. CORP. ACT ANN. art. 8.09 (Vernon 1980).

205. 663 S.W.2d at 476; cf. *Roland Communications, Inc. v. American Communications Corpus Christi, Inc.*, 662 S.W.2d 145 (Tex. App.—Corpus Christi 1983, no writ) (default judgment improper when no showing in the record that the secretary of state had forwarded a copy of process to defendant). In rejecting defendant's claim that the default judgment was void because the form of notice the plaintiff had used did not meet the due process requirements of the federal and state constitutions, the court reasoned that "the failure of the method of service was the result of the [defendant] corporation's own failure to comply with the statutory requirements which are designed to assure it of notice of pending suits." 663 S.W.2d at 476 (citing *TXXN, Inc. v. D/FW Steel Co.*, 632 S.W.2d 706, 708 (Tex. App.—Fort Worth 1982, no writ)).

206. 667 S.W.2d 563 (Tex. App.—Dallas 1984, no writ).

207. TEX. REV. CIV. STAT. ANN. art. 2031b(3) (Vernon 1964 & Supp. 1985).

208. *Id.* art. 2031b(2).

209. 667 S.W.2d at 565-66. The plaintiffs failed to allege expressly in their pleadings that their cause of action arose from the defendant's business in Texas, as required by article 2031b(2). TEX. REV. CIV. STAT. ANN. art. 2031b(2) (Vernon 1964 & Supp. 1985). The court, however, concluded that the pleadings were sufficient to give the defendant notice that it was being sued in a Texas court under article 2031b(2). 667 S.W.2d at 566.

210. See TEX. REV. CIV. STAT. ANN. art. 2008 (1964) (repealed 1983).

211. Act of June 17, 1983, ch. 385, § 3, 1983 Tex. Sess. Law Serv. 2124-25 (Vernon).

212. 668 S.W.2d 429 (Tex. App.—Eastland 1984, no writ).

213. *Id.* at 430.

214. 666 S.W.2d 238 (Tex. App.—El Paso 1984, no writ).

215. *Id.* at 239.

216. *Id.* (Preslar, C.J., dissenting).

statute.²¹⁷

Cases interpreting the repealed venue statute²¹⁸ will continue to have vitality in construing analogous sections of the statute as revised. For that reason, several cases decided under the repealed statute during the survey period are worth noting. In *Champlin Petroleum Co. v. Heinz*²¹⁹ the court held that a foreign corporation had no "agency or representative" in the county of suit as required by subdivision 27,²²⁰ despite the presence of two employees who took care of the corporation's oil and gas operations. The employees did not have management discretion or authority to conduct business of any nature with third parties on behalf of the corporation. The corporation, however, owned and operated 37 gas wells in the county of suit, and owned two compressor stations there worth more than \$400,000.²²¹ In light of these facts, it would not have been unfair to allow the suit to proceed.²²² Nevertheless, courts have held that subdivision 27 does not authorize maintenance of a suit in any county where the defendant merely does business.²²³ Instead, an agent or representative whose duties involve more than matters of manual or mechanical execution must be present.²²⁴ The court in *Heinz*, therefore, held venue improper.²²⁵

In *First Gibraltar Mortgage Corp. v. Gibraltar Savings Association*²²⁶ the court held that a plaintiff who brought suit under the Declaratory Judgment Act (DJA)²²⁷ was entitled to venue where he resided under subdivision 23.²²⁸ Although the court held that the showing of a justiciable controversy under the DJA "in and of itself . . . [meets] the requirements of subdivision 23,"²²⁹ the holding should not be construed to mean that a plaintiff who

217. As the majority in *Graue Haws* observed: "Here, the legislature made one exception to the applicability of the new statute: 'shall not apply to pending appeals on venue questions.' To add an additional exception: 'shall not apply to venue matters in lawsuits pending when the act took effect' would be repugnant to the statute." *Id.*

218. TEX. REV. CIV. STAT. ANN. art. 1995 (Vernon 1964) (repealed 1983).

219. 665 S.W.2d 544 (Tex. App.—Corpus Christi 1983, writ ref'd n.r.e.).

220. TEX. REV. CIV. STAT. ANN. art. 1995(27) (Vernon 1964) (repealed 1983).

221. 665 S.W.2d at 547.

222. The jury found that the defendant's business "was, in more or less permanent form, actually conducted" in the county of suit. *Id.* at 546. This finding satisfies the test for "agency" set out in *Milligan v. Southern Express, Inc.*, 151 Tex. 315, 322-23, 250 S.W.2d 194, 198 (1952) ("agency" involves a situation in which "the business of the defendant is, in more or less regular and permanent form, actually conducted in the county of suit").

For the view that it would not be fair to allow the suit to proceed against the defendant on these facts, see Guittard & Tyler, *Revision of the Texas Venue Statute: A Reform Long Overdue*, 30 BAYLOR L. REV. 563, 574-75 (1980).

223. See *Rouse v. Shell Oil Co.*, 577 S.W.2d 787, 789 (Tex. Civ. App.—Corpus Christi 1979, writ dism'd); *Colorado Interstate Gas Co. v. Mapco, Inc.*, 570 S.W.2d 164, 170 (Tex. Civ. App.—Amarillo 1978, no writ).

224. *Rouse v. Shell Oil Co.*, 577 S.W.2d 787, 789 (Tex. Civ. App.—Corpus Christi 1979, writ dism'd).

225. 665 S.W.2d at 549.

226. 658 S.W.2d 709 (Tex. App.—Dallas 1983, no writ).

227. TEX. REV. CIV. STAT. ANN. art. 2524—1 (Vernon 1965).

228. 658 S.W.2d at 711 (citing *Bituminous Casualty Corp. v. Commercial Standard Ins. Co.*, 639 S.W.2d 25, 26 (Tex. App.—Tyler 1982, no writ); *Amoco Prod. Co. v. Texas Elec. Serv. Co.*, 614 S.W.2d 194, 198 (Tex. Civ. App.—Houston [14th Dist.] 1981, no writ)).

229. 658 S.W.2d at 711.

asserts a claim under the DJA need not prove venue facts sufficient to satisfy the requirements of subdivision 23. To the contrary, plaintiff must prove such facts to avail himself of the general exceptions to article 1995.²³⁰ The court's language merely signifies that a plaintiff who proves such facts can acquire venue under subdivision 23 even though he seeks no remedy other than a declaratory judgment.²³¹

In *Houston Chronicle Publishing Co. v. Stewart*²³² the court held that a cause of action for libel could be brought against a newspaper corporation in the county where the plaintiff resided at the time the cause of action arose. The court, however, sustained the plea of privilege of corporate officers who were not shown to be personally connected with the publication of the allegedly libelous article on the ground that a corporate officer cannot be held personally liable for corporate wrongs merely by reason of his corporate office.²³³

D. Nonprofit Corporations

Two recent cases required the courts to interpret the rarely construed Texas Non-Profit Corporation Act (TNPCA).²³⁴ In accordance with article 1396—2.09 of the TNPCA,²³⁵ the court in *Aldrich v. State*²³⁶ held that the corporation's board of directors lacked the authority to adopt a new set of bylaws because the members of the corporation had not delegated that authority to the board.²³⁷ Alternatively, the court held that even if the board had validly adopted new bylaws, the board could not have caused those bylaws to operate retroactively.²³⁸ Despite the dearth of authority on the question of retroactivity of bylaws,²³⁹ the court's alternative holding is sensible.

In *Governing Board v. Pannill*²⁴⁰ certain local chapters of the Texas Society of the Daughters of the American Revolution (TSDAR) challenged the sale by the TSDAR, a nonprofit corporation, of a piece of property known as

230. See *Amoco Prod. Co. v. Texas Elec. Serv. Co.*, 614 S.W.2d 194, 196 (Tex. Civ. App.—Houston [14th Dist.] 1981, no writ). Plaintiff in *First Gibraltar* was entitled under the third clause of subdivision 23 to venue in Dallas County, where it resided at the time the cause of action arose, because it proved that the defendant corporation maintained an agent in Dallas County.

231. See 658 S.W.2d at 711.

232. 668 S.W.2d 727 (Tex. App.—Houston [1st Dist.] 1983, writ dismissed).

233. *Id.* at 730 (citing *Belo v. Fuller*, 84 Tex. 450, 452, 19 S.W. 616, 617 (1892); *K & G Oil Tool & Serv. Co. v. G & G Fishing Tool Serv.*, 158 Tex. 594, 596, 314 S.W.2d 782, 793 (1958)).

234. TEX. REV. CIV. STAT. ANN. art. 1396—1.01 to —11.01 (Vernon 1980).

235. Article 1396—2.09 vests in the members of a nonprofit corporation the power to "alter, amend, or repeal the by-laws [of the corporation] or to adopt new by-laws," but allows the members to delegate that power to the board of directors. *Id.* art. 1396—2.09.

236. 658 S.W.2d 323 (Tex. App.—Tyler 1983, no writ).

237. *Id.* at 326; see *supra* note 235.

238. 658 S.W.2d at 326-27. The court found that bylaws are ordinarily limited to future cases and cannot have a retroactive operation. *Id.* at 327 (citing 18 AM. JUR. 2D *Contracts* § 168 (1965)).

239. To buttress its conclusion that the bylaws could not be applied retroactively, the court cited only one case, *Steger v. Davis*, 27 S.W. 1068, 1070 (Tex. Civ. App.—1894, writ refused). 658 S.W.2d at 327.

240. 659 S.W.2d 670 (Tex. App.—Beaumont 1983, writ refused n.r.e.).

the Freeman Plantation. The chapters contended that although the sale had been approved by a majority of the votes actually cast by TSDAR members at the TSDAR State Conference in 1975 (158 in favor, 142 against), the sale had not been approved by a "vote of the majority of the votes entitled to be cast by the members present" as required by article 1396—2.12(A) of the TNPCA.²⁴¹ Evidence showed that 342 voting delegates had registered for the conference as of the day preceding the vote, but only 158 voted for the sale. The court, however, held that other evidence enabled the jury reasonably to conclude that 42 of the voting delegates were not present at the session when the motion to sell the Freeman Plantation was actually voted on.²⁴² Thus, the court concluded that the sale had been approved in accordance with the dictates of article 1396—2.12(A).

The chapters also contended that the sale of the Freeman Plantation was governed by article 1396—5.09(A), which requires that a sale of "all, or substantially all, the property and assets of a corporation" be approved by two-thirds of the members entitled to vote and present at the meeting at which the vote is conducted.²⁴³ Considering the other significant assets owned by the TSDAR, including stocks, bonds, certificates of deposit, and real estate, the court reasoned that the jury could have justifiably concluded that the sale of the Freeman Plantation did not constitute a sale of substantially all of the society's assets.²⁴⁴ The court rejected the chapters' argument that article 1396—5.09 should be read to govern "the sale of any significant asset unless made for an express purpose of the non-profit corporation."²⁴⁵ The court found such a reading inconsistent with the language of article 1396—5.09(A).²⁴⁶

In a third case involving nonprofit corporations, *Texas Farm Bureau v. United States*,²⁴⁷ the Fifth Circuit was called upon to decide whether advances made by one nonprofit corporation to a separate but affiliated nonprofit corporation constituted loans or contributions to capital for tax purposes. The court found this situation analogous to traditional debt-equity cases involving for-profit corporations and their shareholders.²⁴⁸ Applying a list of objective factors developed by the courts in the context of traditional debt-equity cases,²⁴⁹ the court concluded that the advances were

241. TEX. REV. CIV. STAT. ANN. art. 1396—2.12(A) (Vernon 1980).

242. 659 S.W.2d at 677. The state historian of the TSDAR testified that to the best of her knowledge, everyone present at the session voted.

243. TEX. REV. CIV. STAT. ANN. art. 1396—5.09(A) (Vernon 1980).

244. 659 S.W.2d at 683.

245. *Id.* at 684 (emphasis deleted).

246. *Id.* "Any significant asset" is substantially different from "all, or substantially all, the property and assets." See *supra* text accompanying note 243.

247. 725 F.2d 307 (5th Cir.), *reh'g denied*, 732 F.2d 437 (5th Cir. 1984) (per curiam).

248. 725 F.2d at 310.

249. *Id.* at 311 (quoting *Estate of Mixon v. United States*, 464 F.2d 394, 402 (5th Cir. 1972)). Factors included names given to certificates, presence of fixed maturity, source of payments, right to enforce payment, participation in management, status of contribution in relation to regular corporate creditors, intent of parties, adequate capitalization, source of interest payments, ability to obtain outside loans, extent advances are used to acquire capital assets, and failure of debtor to repay on due date.

contributions to capital rather than loans and, therefore, were not deductible as bad debts.²⁵⁰

E. *Rights of a Foreign Corporation to Sue*

Article 8.18 of the TBCA bars a foreign corporation that is transacting or has transacted business in Texas without a certificate of authority from maintaining a suit in a Texas court on a cause of action arising out of such business until it has obtained a certificate of authority.²⁵¹ Article 8.01 provides, however, that this restriction does not apply to a foreign corporation that has merely transacted business in interstate commerce in Texas.²⁵² In *Killian v. Trans Union Leasing Corp.*²⁵³ a Texas couple, acting through an intermediary, leased an irrigation sprinkler system that was installed on their farm in Frio County, Texas. The lessor was Trans Union, a foreign corporation. Subsequently, Killian purchased the farm at a foreclosure sale. When Killian refused to return the irrigation system, Trans Union sued Killian for conversion. Killian contended that Trans Union could not maintain its suit because Trans Union had never obtained a certificate of authority. The court held that Trans Union had simply transacted business in interstate commerce.²⁵⁴ The lease agreement provided that it had been made and accepted in Illinois and provided for payments at Trans Union's Chicago office. Furthermore, no evidence showed that the Texas company that had arranged the transaction for the couple was acting as an agent of Trans Union. Accordingly, the court concluded that Trans Union could maintain its suit even though it had not obtained a certificate of authority.²⁵⁵

250. 725 F.2d at 314. The court was persuaded that the advances constituted contributions to capital because: (1) the parties had failed to comply with the repayment provision in their agreement concerning the advances; (2) the corporation that had received the advances was thinly capitalized; (3) the complete overlap in the boards of directors of the two corporations had precluded any arm's-length relationship between them; (4) the advances had been used to cover basic operating costs of the recipient corporation; and (5) the recipient corporation had never made a single interest payment. *Id.* at 313-14. Because the objective factors pointed overwhelmingly toward a finding that the advances constituted contributions to capital, the court found it unnecessary to consider the parties' subjective intent. *Id.* at 312 (citing *Estate of Mixon v. United States*, 464 F.2d 394, 407 (5th Cir. 1972)) & 314. The court subsequently qualified the relevance of subjective intent in its opinion denying rehearing. *See Texas Farm Bureau v. United States*, 732 F.2d 437 (5th Cir. 1984) (per curiam).

251. TEX. BUS. CORP. ACT ANN. art. 8.18(A) (Vernon 1980).

252. Article 8.01(B) states that "a foreign corporation shall not be considered to be transacting business in this state, for the purposes of this Act, by reason of carrying on in this state one (1) or more of the following activities: . . . (9) Transacting any business in interstate commerce." *Id.* art. 8.01(B)(9).

253. 657 S.W.2d 189 (Tex. App.—San Antonio 1983, writ ref'd n.r.e.).

254. *Id.* at 191.

255. *Id.* at 192. The court also determined that the lease agreement was evidence of the couple's indebtedness. *Id.* Creating evidence of debt does not constitute transacting business in Texas for purposes of the TBCA. TEX. BUS. CORP. ACT ANN. art. 8.01(B)(7) (Vernon 1980). Consequently, the court held that Trans Union had merely transacted business interstate by entering into the lease. 657 S.W.2d at 192. Because no permit or certificate of authority is required for a foreign corporation to transact interstate business, Trans Union was allowed to bring suit. *Id.*

F. Miscellaneous Corporate Issues

In *Leck v. Pugh*²⁵⁶ one of two equal shareholders in a Texas corporation sought a court-ordered liquidation of the corporation pursuant to article 7.06 of the TBCA.²⁵⁷ The shareholders had been involved in litigation since 1972 and the corporation had been in receivership since 1979. The court affirmed the order instructing the receiver to liquidate the corporate assets since no plan for remedying the condition that had necessitated the appointment of a receiver had been presented within twelve months after the receiver was appointed.²⁵⁸

In *De Anda v. De Anda*²⁵⁹ Mr. De Anda endorsed and transferred shares of stock in a Texas state bank to his ex-wife pursuant to a divorce decree, but she failed to notify the bank of the transfer. As a result, the bank continued to pay dividends on the shares to Mr. De Anda. Mrs. De Anda sued her former husband to recover the dividends. Mr. De Anda contended that he was entitled to the dividends because the shares had never been transferred on the books of the bank, as required by state banking law²⁶⁰ and the bank's bylaws. The court observed that the statutory provision requiring a stock transfer to be recorded on the bank corporation's books was intended to protect the bank from suit by the transferee in cases like this one, and did not invalidate the transfer of stock as between Mr. and Mrs. De Anda.²⁶¹ The court concluded that Mrs. De Anda was entitled to the dividends issued on the disputed shares since the transfer was valid.²⁶²

The validity of a stock transfer was also at issue in *Estate of Bridges v. Mosebrook*.²⁶³ At the request of W.L. Bridges, Sr., Agri-Place, Inc., a closely held corporation, issued stock certificates in the names of individuals to whom Bridges intended to make a gift of the stock.²⁶⁴ Bridges later handed the donees their respective stock certificates and told them that the stock belonged to them, adding that he would retain possession of the stock certificates. The beneficiaries of the will of Bridges' second wife asserted that the gifts had not been consummated because the donor had neither relinquished control over the certificates nor properly delivered them to the donees.²⁶⁵ Recognizing that what constitutes delivery will depend on the

256. 676 S.W.2d 180 (Tex. App.—Waco 1984, no writ).

257. TEX. BUS. CORP. ACT ANN. art. 7.06(A)(3) (Vernon 1980). Article 7.06(A)(3) allows a district court to order a liquidation if a corporation is in receivership and no plan for remedying the condition requiring appointment of a receiver has been presented within 12 months after the appointment of the receiver. *Id.*

258. 676 S.W.2d at 181.

259. 662 S.W.2d 107 (Tex. App.—San Antonio 1983, no writ).

260. See TEX. REV. CIV. STAT. ANN. art. 342—401 (Vernon 1973).

261. 662 S.W.2d at 109 (quoting *Cooper v. Citizens Nat'l Bank*, 267 S.W.2d 848, 853 (Tex. Civ. App.—Waco 1954, writ ref'd n.r.e.)).

262. 662 S.W.2d at 109.

263. 662 S.W.2d 116 (Tex. App.—Fort Worth 1983, writ ref'd n.r.e.).

264. Bridges conveyed a farm to his brother-in-law who conveyed the property in turn to a newly formed, closely held corporation. Stock issued to the brother-in-law was cancelled and 20,000 shares were issued to members of Bridges' family and relatives of his second wife. None of the stock was issued in Bridges' name.

265. 662 S.W.2d at 121.

circumstances of the case,²⁶⁶ the court concluded that the gift transfers had been completed.²⁶⁷

The beneficiaries in *Mosebrook* also argued that the shares of stock had not actually been issued because they were not signed by the president or vice-president of the corporation, as required by article 2.19 of the TBCA.²⁶⁸ The court, however, rejected that argument as well. Stating that "a stock certificate is not the actual ownership of a corporation," the court construed article 2.19 as simply affording the owner of stock a right to demand that the corporation provide the signatures omitted from the certificates.²⁶⁹ The provision does not, the court reasoned, require the signatures as a condition precedent to issuance of stock.²⁷⁰

In *Duncan v. Lichtenberger*²⁷¹ two of the three shareholders in a closely held corporation sued Duncan, the corporation's president and remaining shareholder. The suit alleged two independent causes of action, one based on fraud and the other based on Duncan's breach of fiduciary duty. The jury found that Duncan had not committed fraud, but that he had breached his fiduciary duty to the other shareholders.²⁷² On appeal, Duncan contended that the plaintiffs were not entitled to recover on their fiduciary duty claim since they had failed to prove fraud. The court rejected this contention, however, stating that it could find no authority for the proposition that a cause of action based on breach of fiduciary duty requires an element of fraud.²⁷³ The court, therefore, affirmed the trial court's judgment awarding the plaintiffs restoration of the consideration that they had paid to Duncan for their shares of stock in the corporation.²⁷⁴

In *Ratner v. Sioux Natural Gas Corp.*²⁷⁵ the Grant Company sued two individuals, Elliot Powers and J.F. Freel, and two corporations, Sioux Natural Gas Corporation (SNGC) and Sioux Pipeline Corporation (SPC), for fraud. Powers and Freel were the directors, officers, and sole shareholders of both corporations. After a jury verdict in Grant's favor, the trial court held

266. *Id.* (citing *Webb v. Webb*, 184 S.W.2d 153, 156-57 (Tex. Civ. App.—Eastland 1944, writ ref'd)).

267. 662 S.W.2d at 121.

268. TEX. BUS. CORP. ACT ANN. art. 2.19(A) (Vernon 1980). Article 2.19(A) provides that a corporation shall deliver stock certificates to shareholders that are signed by "the president or a vice president and either the secretary or assistant secretary or such officer or officers" as the corporation's bylaws prescribe. *Id.*

269. 662 S.W.2d at 121. The court recognized that complete ownership of stock does not even require a certificate to be issued. *Id.* at 120 (citing *Yeaman v. Galveston City Co.*, 106 Tex. 389, 398, 167 S.W. 710, 720 (1914)).

270. 662 S.W.2d at 121.

271. 671 S.W.2d 948 (Tex. App.—Fort Worth 1984, writ ref'd n.r.e.).

272. Duncan took control of a corporation formed by conveyances from a limited partnership and proceeded to fire his previous partners. The cause of action focused on their exclusion from management of the corporation.

273. 671 S.W.2d at 954. The court did, however, cite one authority for the proposition that the existence of fraud is not required for a breach of fiduciary duty to occur. *Id.* at 954 n.1 (citing *F. O'NEAL, OPPRESSION OF MINORITY SHAREHOLDERS* §§ 7.13, 9.04 (1975)).

274. 671 S.W.2d at 954. The court had previously noted that equitable relief is available for a breach of fiduciary duty in Texas. *Id.* at 952 (citing *International Bankers Life Ins. Co. v. Holloway*, 368 S.W.2d 567 (Tex. 1963)).

275. 719 F.2d 801 (5th Cir. 1983).

the four defendants jointly and severally liable to Grant for \$11,900,000 in actual damages and \$1,100,000 in punitive damages, plus prejudgment interest.²⁷⁶ Shortly before the Fifth Circuit heard oral argument on appeal, Powers and Freel settled with Grant; the settlement agreement, however, provided that the judgment would remain in effect against SNGC and SPC.

The issue before the Fifth Circuit in *Ratner* was the effect of the settlement on the nonsettling corporate tortfeasors. The court initially recognized that under Texas law an injured party must apply any amount received in settlement from one defendant against the amount to be recovered from the other defendants in order to prevent a windfall to the plaintiff.²⁷⁷ The court acknowledged, however, that "the rationale of the 'one satisfaction' rule is usually inapposite to punitive damages."²⁷⁸ The Court nevertheless held that because all four defendants had been found jointly liable for both actual and punitive damages, the amount Grant received from Powers and Freel should be credited against the entire judgment, including punitive damages.²⁷⁹

III. SECURITIES

A. *Insider Trading Sanctions Act*

The major development in federal securities law during the survey period was the passage of the Insider Trading Sanctions Act of 1984 (the Act).²⁸⁰ Insider trading involves the purchase or sale of securities based upon inside information unavailable to the investing public. According to the legislative history of the Act, insider trading "undermin[es] the public's expectations of honest and fair securities markets where all participants play by the same rules."²⁸¹ Congress observed that the remedies available to the Securities and Exchange Commission were insufficient to deter many potential violators from trading on the basis of inside information.²⁸² To curb the increasingly widespread incidence of insider trading,²⁸³ Congress passed the Insider Trading Sanctions Act of 1984.

276. The final judgment was for \$18,385,307.80.

277. 719 F.2d at 803 (quoting *Gill v. United States*, 429 F.2d 1072, 1079 (5th Cir. 1970)).

278. 719 F.2d at 804.

279. *Id.* at 805. The court distinguished two cases holding that amounts received in settlement should not be credited against awards of punitive damages, on the ground that in those cases the punitive damages were not common to all of the defendants. *Id.* at 804 (distinguishing *Howard v. General Cable Corp.*, 674 F.2d 351, 358 (5th Cir. 1982); *Hill v. Budget Fin. & Thrift Co.*, 383 S.W.2d 79, 81-82 (Tex. Civ. App.—Dallas 1964, no writ)).

280. Pub. L. No. 98-376, 98 Stat. 1264 (to be codified in scattered subsections of 15 U.S.C. § 78).

281. H.R. REP. NO. 355, 98th Cong., 2d Sess. 2, reprinted in 1984 U.S. CODE CONG. & AD. NEWS 2274, 2275.

282. *Id.* at 7, reprinted in 1984 U.S. CODE CONG. & AD. NEWS 2274, 2280. Prior to the passage of the Act, the primary remedies available to the SEC were an injunction against further violations of the securities laws and disgorgement of illicitly obtained profits. *Id.*

283. See *id.* at 5, reprinted in 1984 U.S. CODE CONG. & AD. NEWS 2274, 2278. In one instance, for example, the SEC alleged that an individual had purchased about \$3000 in call options of a corporation that was subject to a takeover proposal. The individual realized approximately \$430,000 in 48 hours. *Wall St. J.*, Mar. 2, 1984, at 1, col. 6.

At the core of the Act is a provision that gives the Securities and Exchange Commission the authority to bring suit for a civil penalty in a federal district court against a person who purchases or sells securities "while in possession of material nonpublic information,"²⁸⁴ or a person "aiding and abetting" such a purchase or sale.²⁸⁵ The size of the penalty is left to the discretion of the court, but it may not exceed three times the profit gained or loss avoided as a consequence of the prohibited transaction.²⁸⁶ A five-year statute of limitations applies.²⁸⁷ The Act also raises the maximum criminal penalty for violations from \$10,000 to \$100,000.²⁸⁸

The aiding and abetting provision is intended to snag the "tipper" who communicates inside information to other persons who trade on the basis of that information, even though the tipper himself may not trade on the basis of it.²⁸⁹ One who does not communicate material nonpublic information cannot be held liable as an aider or abetter;²⁹⁰ thus, broker-dealers who merely execute trades for their customers who are trading unlawfully are excluded from the coverage of the Act.²⁹¹ The Act also excludes liability based solely on the doctrine of respondeat superior.²⁹² Curiously, the Act contains no definition of "insider trading." Congress apparently believed that the caselaw pertaining to insider trading was sufficiently well-developed to provide the courts with adequate guidance in construing the Act.²⁹³

B. Sale of Business Doctrine

In 1983 the Fifth Circuit joined the Second and Fourth Circuits in rejecting the "sale of business" doctrine,²⁹⁴ which holds that a transfer of all the stock in a corporation is not within the purview of the federal securities laws.²⁹⁵ In the 1984 case of *Siebel v. Scott*²⁹⁶ the Fifth Circuit clarified its

284. Pub. L. No. 98-376, § 2, 98 Stat. 1264, 1264 (to be codified at 15 U.S.C. § 78u(d)(2)(A)).

285. *Id.*

286. *Id.* The Act defines "profit gained or loss avoided" as "the difference between the purchase or sale price of the security and the value of that security as measured by the trading price of the security a reasonable period after public dissemination of the nonpublic information." *Id.* (to be codified at 15 U.S.C. § 78u(d)(2)(C)).

287. *Id.* (to be codified at 15 U.S.C. § 78u(d)(2)(D)).

288. *Id.* § 3, 98 Stat. 1264, 1265 (to be codified at 15 U.S.C. § 78ff).

289. H.R. REP. NO. 355, 98th Cong., 2d Sess. 9, reprinted in 1984 U.S. CODE CONG. & AD. NEWS 2274, 2282.

290. See Pub. L. No. 98-376, § 2, 98 Stat. 1264, 1264 (1984) (to be codified at 15 U.S.C. § 78u(d)(2)(B)) ("No person shall be subject to a [civil penalty under the Act] solely because that person aided and abetted a transaction covered by [section 2(A) of the Act] in a manner other than by communicating material nonpublic information.").

291. H.R. REP. NO. 355, 98th Cong., 2d Sess. 10, reprinted in 1984 U.S. CODE CONG. & AD. NEWS 2274, 2283.

292. See Pub. L. No. 98-376, § 2, 98 Stat. 1264, 1264 (1984) (to be codified at 15 U.S.C. § 78u(d)(2)(B)).

293. See H.R. REP. NO. 355, 98th Cong., 2d Sess. 13, reprinted in 1984 U.S. CODE CONG. & AD. NEWS 2274, 2286.

294. *Daily v. Morgan*, 701 F.2d 496, 504 (5th Cir. 1983); see *Golden v. Garafalo*, 678 F.2d 1139, 1146 (2d Cir. 1982); *Coffin v. Polishing Mach., Inc.*, 596 F.2d 1202, 1204 (4th Cir.), cert. denied, 444 U.S. 868 (1979).

295. *But cf. Christison v. Groen*, 740 F.2d 593, 595 (7th Cir. 1984) (sale of business doc-

view.

In *Siebel* all the limited partners in a cable television system sold their interests in the limited partnership to Jim Scott and Associates (JSA), the general partner. The limited partners later sued JSA for fraud in connection with the sale under section 10(b) of the Securities Exchange Act of 1934²⁹⁷ and rule 10b-5.²⁹⁸ JSA contended that the transaction did not involve the sale of securities because the net effect of the sale was a transfer to JSA of all the business assets of the cable television system rather than any interest that could be characterized as a "security." The Fifth Circuit disagreed. The court acknowledged that the partnership interests were not securities in JSA's hands.²⁹⁹ The court held, however, that the limited partners' interests were securities in the hands of the sellers.³⁰⁰ The court thus concluded that the sellers could maintain their suit under the Exchange Act. The court observed that the sale of business doctrine, even in circuits where it has been endorsed, is implicated only when the interest transferred takes a traditional form such as ordinary corporate stock;³⁰¹ therefore, the doctrine would not have applied in *Siebel* in any event, because the interest took the form of an investment contract.³⁰² The United States Supreme Court has granted writs of certiorari in two cases to resolve the conflict among the circuits concerning the "sale of business" doctrine.³⁰³

C. Texas Securities Act

Several cases construing the Texas Securities Act (TSA)³⁰⁴ are worthy of note. In *Weisz v. Spindletop Oil & Gas Co.*³⁰⁵ the court held that an action by the state for the appointment of a receiver did not toll the statute of limitations with respect to private claims based on purported violations of the TSA.³⁰⁶ The court cited two cases, including one from the Texas Supreme Court, to support the proposition that the TSA's three-year statute

trine presumed to apply where purchaser acquires a *controlling* interest in a business even if he has not acquired all of its stock) (citing *Sutter v. Groen*, 687 F.2d 197, 199 (7th Cir. 1982)).

296. 725 F.2d 995 (5th Cir. 1984).

297. 15 U.S.C. § 78j(b) (1982).

298. 17 C.F.R. § 240.10b-5 (1984).

299. 725 F.2d at 999.

300. *Id.*

301. *Id.*; see *King v. Winkler*, 673 F.2d 342 (11th Cir. 1982); *Frederiksen v. Poloway*, 637 F.2d 1147 (7th Cir.), *cert. denied*, 451 U.S. 1017 (1981); *Chandler v. Kew, Inc.*, 691 F.2d 443 (10th Cir. 1977) (opinion ordered published 1982).

302. 725 F.2d at 999. The characterization of an interest as a security varies with the relationship of its holder to the venture. An investment contract is only a security if the holder is relying on the managerial skills of others to generate his profit. If the holder is relying on his own entrepreneurial talents to generate his profit, his interest does not fall within the coverage of the securities laws. *Id.*; see *SEC v. Howey Co.*, 328 U.S. 293 (1946) (test for determining if investment contract exists is whether scheme involves investment in common enterprise with profits derived solely from efforts of others).

303. *Landreth Timber Co. v. Landreth*, 731 F.2d 1348 (9th Cir. 1984), *cert. granted*, 53 U.S.L.W. 3355 (U.S. Nov. 13, 1984) (No. 83-1963); *Ruefenacht v. O'Halloran*, 737 F.2d 320 (3d Cir. 1984), *cert. granted*, 53 U.S.L.W. 3355 (U.S. Nov. 13, 1984) (No. 84-165).

304. TEX. REV. CIV. STAT. ANN. arts. 581—1 to —39 (Vernon 1964 & Supp. 1985).

305. 664 S.W.2d 423 (Tex. App.—Corpus Christi 1983, no writ).

306. *Id.* at 425.

of limitations should be rigorously enforced.³⁰⁷

In *Jones v. Latham*³⁰⁸ the court of appeals held that the state securities commissioner was entitled to an order requiring a securities dealer to produce certain business records pursuant to an administrative subpoena.³⁰⁹ The dealer argued that the order was appropriate only if the commissioner could prove that he was unable to perform his duties without the subpoena, but the court rejected that standard.³¹⁰ The court stated that section 3 of the TSA³¹¹ authorizes the commissioner to inspect and copy the records of dealers to prevent or detect a violation of the Act.³¹² On that basis, the court of appeals upheld the lower court's order.³¹³

In *Star Supply Co. v. Jones*³¹⁴ the court held that a broker who had agreed to find a buyer for a Texas corporation was not required to register as a securities broker in order to effectuate the sale of the corporation.³¹⁵ The court reasoned that since all the corporate stock was transferred, the transaction did not constitute a sale of securities as contemplated by the TSA.³¹⁶ Although the court purported to look to federal court decisions to interpret the TSA,³¹⁷ it neglected to look closely enough. In essence, the court treated the transaction as the sale of a business rather than the sale of securities. The court, however, failed to recognize that the Fifth Circuit had repudiated the sale of business doctrine under federal securities law.³¹⁸

D. Texas Securities Board

During the survey period the Texas State Securities Board adopted a new set of rules³¹⁹ governing the registration in Texas of securities previously registered with the Securities and Exchange Commission pursuant to the SEC's "shelf registration" provision, rule 415.³²⁰ The board also adopted new rules governing the procedure to be used in contested cases³²¹ and adopted a sixty-day time limit for the filing of a complaint challenging denial

307. *Id.* (citing *Dillon v. Lintz*, 582 S.W.2d 394, 397 (Tex. 1979); *Stone v. Enstam*, 541 S.W.2d 473, 477 (Tex. Civ. App.—Dallas 1976, no writ)).

308. 671 S.W.2d 612 (Tex. App.—Eastland 1984, writ ref'd n.r.e.).

309. *Id.* at 614.

310. *Id.*

311. TEX. REV. CIV. STAT. ANN. art. 581—3 (Vernon 1964).

312. 671 S.W.2d at 614.

313. *Id.* The court also rejected the dealer's argument that his business records were privileged under the fifth amendment. *Id.* at 613 (citing *United States v. Doe*, 104 S. Ct. 1237, 1239, 79 L. Ed. 2d 552, 559 (1984)).

314. 665 S.W.2d 194 (Tex. App.—San Antonio 1984, no writ).

315. *Id.* at 196.

316. *Id.*

317. *Id.* (citing *Searsy v. Commercial Trading Corp.*, 560 S.W.2d 637, 640 (Tex. 1977)).

318. See *Daily v. Morgan*, 701 F.2d 496 (5th Cir. 1983); see also *supra* notes 296-303 and accompanying text (discussion of recent case clarifying the circuit's position).

319. Tex. Sec. Bd., 9 Tex. Reg. 4074 (1984) (codified at 7 TEX. ADMIN. CODE § 113.11).

320. 17 C.F.R. § 230.415 (1984). The SEC has now adopted rule 415 on a permanent basis.

321. Tex. Sec. Bd., 9 Tex. Reg. 1436 (1984) (codified at 7 TEX. ADMIN. CODE §§ 105.1-.10).

of a permit for the sale of securities.³²² In a third development of note, the board adopted a rule exempting from the TSA registration requirements³²³ and the TSA dealer registration requirements³²⁴ the offer, sale, or distribution of securities under employee plans.³²⁵

322. *Id.* at 2773 (codified at 7 TEX. ADMIN. CODE § 105.3).

323. TEX. REV. CIV. STAT. ANN. art. 581—7 (Vernon 1964 & Supp. 1985).

324. *Id.* art. 581—12 (Vernon 1964).

325. Tex. Sec. Bd., 9 Tex. Reg. 2776 (1984) (codified at 7 TEX. ADMIN. CODE § 139.11).