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Glenn D. West
Sarah E. Stasny

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The purpose of this annual survey of Texas corporate law is to provide Texas lawyers an analysis of the latest court decisions affecting corporate practice. In the last few years, we have focused our Texas Corporations Surveys principally on (1) specific considerations of importance to attorneys drafting corporate agreements governed by Texas law; and (2) the interplay between (a) the vulnerability of corporate officers under Texas common law to personal tort liability arising from the negotiation and execution of agreements entered into solely on behalf of their corporation, and (b) the Texas Legislature’s seemingly firm commitment to exonerate corporate officers from any liabilities arising from a contractual obligation created by a Texas corporation. A number of Texas cases de-
cided during 2004 continue to underscore these issues of Texas law and the need for specific drafting to avoid unintended consequences in corporate acquisition or other agreements. This year we provide specific suggested contractual provisions to address these issues in our discussion of drafting corporate agreements in Part II of this Survey.

Last year's discussion of Benchmark Electronics, Inc. v. J.M. Huber Corp. provided an opportunity to explore specific differences between New York and Texas law on the availability of extra-contractual tort claims based upon contractual representations in a stock purchase agreement. In Part III of this Survey, Rudisill v. Arnold White & Durkee, P.C. provides us an opportunity to discuss specific differences between Delaware and Texas corporate law in connection with the question of when stockholders' approval is required to sell "all or substantially all" of the assets of a corporation. Despite the fact that many corporate lawyers in Texas find that they are more familiar with Delaware corporate law than Texas (given the dominance of Delaware as the state of incorporation for many of the corporations based in Texas), and despite the fact that both the Delaware and Texas corporate statutes were originally based on the same Model Business Corporation Act, it is a mistake to assume that the statutory frameworks are the same.

II. DRAFTING CORPORATE AGREEMENTS

As noted in last year's Texas Corporations Survey, the Texas courts continue to demonstrate "a refreshingly clear commitment to the sanctity of the written agreement." That commitment was reinforced during this Survey period by a pair of decisions by the Texas Supreme Court specifically upholding a forum selection clause in an insurance policy and a contractual jury waiver clause in a commercial lease. The Texas courts' commitment to the sanctity of contract means that Texas courts will enforce an unambiguous agreement as written because the parties "are entitled to select what terms and provisions to include in a contract before executing it ... [and] each is entitled to rely upon the words selected to demarcate their respective obligations and rights." 8

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8. ASI Techs., Inc. v. Johnson Equip. Co., 75 S.W.3d 545, 549 (Tex. App.—San Antonio 2002, pet. denied). See West & Chao, supra note 2, at 1416 n.61; see also Burke v. Union Pac. Res. Co., 138 S.W.3d 46, 62 (Tex. App.—Texarkana 2004, pet. filed) ("The agreement will be enforced as created regardless of whether the parties contracted wisely."); Breitenfeld v. SAS Inst., Inc., 147 S.W.3d 672, 678 (Tex. App.—Dallas 2004, no pet. h.) ("In an unambiguous contract, we will not imply language, add to language, or interpret it other than pursuant to its plain meaning."); The Frost Nat'l Bank v. L&P Distribrs., Ltd., 122 S.W.3d 922, 932 (Tex. App.—Corpus Christi 2003, pet. filed) ("[I]t is not
Despite the Texas courts’ strong commitment to holding contracting parties to their written, signed agreements, we have identified in past Texas Corporations Surveys at least three areas of extra-contractual exposure arising from the negotiation and execution of those contractual agreements by the contracting corporate parties and their officers. Those three areas of extra-contractual exposure are (1) the vulnerability of contracting parties to tort claims for fraud and negligent misrepresentation arising from extra-contractual representations, as well as from the representations expressly set forth in the contract; (2) the vulnerability of corporate officers, as agents of their corporate principals, to tort liability arising from the negotiation and execution of corporate contractual agreements; and (3) the vulnerability of contracting parties to being bound by preliminary corporate agreements intended as mere letters of intent.

Last year we suggested that each of these areas of potential extra-contractual exposure could paradoxically be mitigated by precise drafting in the very corporate agreements from which these extra-contractual exposures arise. This year we take each of those extra-contractual exposures in turn and provide suggested contractual provisions to address that exposure.

A. Contractually Avoiding Extra-Contractual Claims

Last year we identified a peculiarity of Texas law that permits a party to a contract to disclaim reliance on extra-contractual representations but to nonetheless pursue tort claims outside of the contract for fraud or negligent misrepresentation based upon the specific representations set within the province of the court to vary contractual terms in order to protect parties from the consequences of their own oversights and failures in nonobservance of obligations assumed. As noted in last year’s Texas Corporations Survey, however, there is a requirement that the agreement must have been “freely bargained,” and mutual mistake, duress, unconscionability or the breach of fiduciary duty will eviscerate that free bargain. See West & Nelson, supra note 2, at 813, 820 n.81. During this Survey period, the effect of making a heavily one-sided agreement with a person of limited bargaining power and thereby rendering it “substantively unconscionable” was addressed at length in In re Luna, No. 01-03-01055-CV, 2004 WL 2005935, at *2-5 (Tex. App.—Houston [1st Dist.] Sept. 9, 2004, orig. proceeding [mand. pending]). On the other hand, as noted by one Texas court during this Survey period, “illiteracy” alone is not a basis for avoiding enforcement of a contract as written. In re Ledet, No. 04-04-00411-CV, 2004 WL 2945699, at *5 (Tex. App.—San Antonio Dec. 22, 2004, no pet. h.).

9. See West & Chao, supra note 2, at 1416, 1429 n.161.
11. West, supra note 2, at 1226-30; West & Treadway, supra note 2, at 811-16; West & Chao, supra note 2 at 1403-08; West & Nelson, supra note 2, at 804-09.
12. West, supra note 2, at 1233-38; West & Treadway, supra note 2, at 818-23; West & Chao, supra note 2 at 1411-15; West & Nelson, supra note 2, at 818-19.
13. West & Nelson, supra note 2, at 817, 820 n.106.
forth in that contract.\textsuperscript{15} Most contractual disclaimer clauses involve the
buyer declaring reliance on any representations not expressly set forth in the contract. As to those representations that are expressly set forth in the contract, the parties obviously intend that the buyer be able to rely upon them and seek contractual remedies against the seller for their breach. The possibility that the buyer could bring claims for contractual breach, as well as extra-contractual tort claims against the seller based on the agreed contractual representations set forth in the contract that disclaimed reliance on extra-contractual representations is, we suspect, not fully appreciated and seldom addressed.

Our discussion of \textit{Benchmark Electronics} in last year's Texas Corporations Survey revealed that New York law is significantly different from Texas law in this respect.\textsuperscript{16} New York law apparently does not permit tort claims for fraud or negligent misrepresentation based solely upon representations set forth in a contract. Rather, a buyer's claims, to the extent they relate to contractual representations, are limited to breach of contract.\textsuperscript{17} Texas, on the other hand, does allow such tort claims on the theory that there is a duty, independent of the contract, not to fraudulently or negligently make misrepresentations. The fact that the misrepresentations are limited to those specifically set forth in a contract (by virtue of the disclaimer clause respecting representations not set forth in the contract) does not change or eliminate that separate, independent duty or the remedy in tort for its breach.\textsuperscript{18} Accordingly, under Texas law, the standard disclaimer of reliance on extra-contractual representations will foreclose both contract and tort liability for claims based on any representation not expressly set forth in the contract,\textsuperscript{19} it but will leave the

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\textsuperscript{15} West & Nelson \textit{supra} note 2, at 817, 820 n.106; see also F.S. New Prods., Inc. v. Strong Indus., 129 S.W.3d 606, 619-20 (Tex. App.—Houston [1st Dist.] 2004, pet. granted).
\textsuperscript{16} West & Nelson \textit{supra} note 2, at 817, 820 n.105.
\textsuperscript{17} Id.
\textsuperscript{18} Id. at 814-816; see also Dallas Fire Ins. Co. v. Tex. Contractors Sur. & Cas. Agency, 128 S.W.3d 279, 294 (Tex. App.—Fort Worth 2004), rev'd on other grounds, No. 04-0215, 2004 WL 2913657 (Tex. 2004) ("[A]n independent duty is imposed on the general public to abstain from inducing others to enter into contracts by the use of fraudulent misrepresentations, irrespective of whether the misrepresentations are later subsumed into the contract or whether the damages suffered are only the economic loss related to the subject matter of the contract."); Conquest Drilling Fluids v. Tri-Flo Int'l, 137 S.W.3d 299, 309-10 (Tex. App.—Beaumont 2004) ("A duty to not act illegally to procure a contract is separate and independent from the duties established by the contract itself."). \textit{But see} Castle Pro. Ltd. P'ship v. The Long Trusts, 134 S.W.3d 267, 274 (Tex. App.—Tyler 2003, pet. denied) (Except with respect to contracts "creating fiduciary relationships ... and in the absence of independent injury, if a contract spells out the parties' respective rights regarding a particular matter, the contract, not common law tort principles, governs any dispute about that matter.").
\textsuperscript{19} West & Nelson \textit{supra} note 2, at 817, 820 n.105; see also Cherry v. McCall, 138 S.W.3d 35 (Tex. App.—San Antonio 2004); Cronus Offshore, Inc. v. Kerr McGee Oil & Gas Corp., 2004 WL 3330786 (E.D. Tex. 2004). As noted last year, however, standard disclaimer of reliance on extra-contractual representation clauses will not be effective against an "unsophisticated party." See \textit{id}. at 814, 820 n.85; see also Carousel's Creamery, L.L.C. v. Marble Slab Creamery, Inc., 134 S.W.3d 385, 394 (Tex. App.—Houston [1st Dist.] 2004, pet. granted). Disclaimer clauses procured by fraud are likewise not enforceable. Nelson v. Najm, 127 S.W.3d 170, 175-76 (Tex. App.—Houston [1st Dist.] 2003, pet. de-
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door open for both contract and tort liability based on representations that are contained in the contract.\(^{20}\)

To address this issue, we suggest that corporate sellers consider adding the following provision (in addition to the typical provision whereby the buyer disclaims reliance upon any representations not expressly set forth in the contract) to their purchase and sale agreements:

**Exclusivity of Agreement.** The parties hereto have voluntarily agreed to define their rights, liabilities and obligations respecting the subject matter of this Agreement exclusively in contract pursuant to the express terms and provisions of this Agreement; and the parties hereto expressly disclaim that they are owed any duties not expressly set forth in this Agreement. The sole and exclusive remedies for any breach of the terms and provisions of this Agreement (including any representations and warranties set forth herein) shall be those remedies available at law or in equity for breach of contract only (as such contract remedies may be further limited or excluded pursuant to the express terms of this Agreement); and the parties hereto hereby waive and release any and all tort claims and causes of action that may be based upon, arise out of or relate to this Agreement, or the negotiation, execution or performance of this Agreement (including any tort claim or cause of action based upon, arising out of or related to any representation or warranty made in or in connection with this Agreement or as an inducement to enter into this Agreement).\(^{21}\)

Given the fact that the ability of buyers to bring extra-contractual tort claims for breaches of contractual representations does not exist in some other states, such as New York, we also suggest that special attention be paid to the choice of law clause in purchase and sale agreements.\(^{22}\) The typical choice of law clause in a purchase and sale agreement is very similar to the clause in the stock purchase agreement reviewed by the court in *Benchmark Electronics*, which reads, “This Agreement shall be governed by, and construed in accordance with, the laws of the State of New

\(^{20}\) West & Nelson *supra* note 2, at 817, 820 n.104. Of course this raises the specter of exemplary damages which are not supposed to be available for breach of contract. See *Lisanti* v. *Dixon*, 147 S.W.3d 638, 645 (Tex. App.—Dallas 2004, no pet. h.) (“Even if the breach [of contract] is malicious, intentional, or capricious, exemplary damages may not be awarded unless the plaintiff proves a distinct tort.”).

\(^{21}\) This clause is not a substitute for, but is an addition to, the negotiations that should occur with respect to limitations on consequential damages or lost profits, as well as the exclusivity of contractual indemnification claims as the sole contractual remedy under the contract. See SAVA Gumarska in Kemijska Industra D.D. v. Advanced Polymer Scis., Inc., 128 S.W.3d 304, 317 (Tex. App.—Dallas 2004, no pet. h.) (“[P]arties to a contract are free to limit or modify the remedies available for breach of their agreement.”).

\(^{22}\) Issues related to the requirements for properly selecting another state's law to apply to a contract are beyond the scope of this Survey; another Survey article addresses choice of law issues.
Unfortunately, as noted by the Fifth Circuit in *Benchmark Electronics*, this formulation of a choice of law clause "is narrow because it deals only with the construction and interpretation of the contract." It does not address the law that will be applicable to extra-contractual tort claims arising out of or related to the contract. Accordingly, even where parties agree that the contract will be governed by the laws of a particular state (such as New York) that does not permit tort claims based on breach of contractual representations, the choice of law clause must be carefully drafted to avoid application of Texas law to tort claims arising out of the contract.

During this Survey period, a Texas court specifically upheld the applicability of another jurisdiction's law to tort claims arising from a contractual relationship because of the expansive language used in the choice of law clause selecting that jurisdiction. We suggest using a similar formulation for choice of law provisions in purchase and sale agreements:

**Governing Law.** This Agreement, and all claims or causes of action (whether in contract or tort) that may be based upon, arise out of or relate to this Agreement or the negotiation, execution or performance of this Agreement (including any claim or cause of action based upon, arising out of or related to any representation or warranty made in or in connection with this Agreement or as an inducement to enter into this Agreement), shall be governed by the internal laws of the State of ____.

Finally, in fairness to buyers who have agreed to have their rights determined and limited by the terms of the contract, some consideration should be given to assuring the buyer that the contractual representations for which the buyer bargained are not forfeited by the seller's subsequent claim of extra-contractual waiver based on the buyer's own investigation or knowledge. A few courts have held that, in the absence of an express reservation of rights, a buyer waives its right to enforce a contractual representation that the buyer knows was untrue when made or that the

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24. *Id*.
25. *See id. at 727*.
26. *El Pollo Loco, S.A. de C.V. v. El Pollo Loco, Inc.*, 344 F. Supp. 2d 986 (S.D. Tex. 2004). The choice of law clause required the application of the laws of Mexico to "[a]ll disputes which may arise in connection with the performance of this Agreement." *Id.* at 988. According to the court, all of the plaintiff's tort claims were disputes that were connected with the performance of the Agreement. *Id.* at 989. *But see Loy v. Harter*, 128 S.W.3d 397, 403-05 (Tex. App.—Texarkana 2004, pet. denied) (holding that an arbitration clause covering all claims "arising under or in connection with" an employment agreement did not cover tort claims arising from alleged breach of fiduciary duty of employee when he was acting in his capacity as director of the corporate employer); *In re All Trac Transp.*, Inc., 306 B.R. 859, 910 (Bankr. N.D. Tex. 2004) (tortious interference with contract claim governed by Texas law, not Utah law, despite a clause in the contract that stated "This Agreement and all transactions contemplated hereunder and/or evidenced hereby shall be governed by, construed under and enforced in accordance with the internal laws of the State of Utah.").
27. For additional suggestions for drafting an effective choice of law clause, see Tina L. Stark, *Negotiating and Drafting Contract Boilerplate § 6.02* (2003).
buyer learns was untrue after signing the contract but before closing. These cases seem to be based upon the notion that "reliance" is a necessary element of a breach of contract claim based upon an express warranty in the same way "reliance" is a necessary element of a tort action for fraud or negligent misrepresentation. While some of these cases appear to be based entirely upon an analysis of the Uniform Commercial Code, the requirement of proof of reliance to recover under an express contractual warranty appears to be a common law concept and, therefore, is potentially applicable whether or not the transaction involves a sale of goods. To address this issue, we suggest that corporate buyers consider adding the following provision to their acquisition agreements:

**No Waiver of Representations and Warranties.** Because Buyer has agreed to limit its rights to those specifically set forth in this Agreement, and to disclaim any extra-contractual representations and warranties or claims, Seller has agreed that Buyer's rights to indemnification for the express representations and warranties set forth herein are part of the basis of the bargain contemplated by this Agreement; and, except to the extent specifically set forth in the Schedules to this Agreement, Buyer's rights to indemnification (as specifically set forth in and limited by Paragraph ___) shall not be affected or waived by virtue of (and Buyer shall be deemed to have relied upon the express representations and warranties set forth herein notwithstanding) any knowledge on the part of Buyer of any untruth of any such representation or warranty of Seller expressly set forth in this Agreement, regardless of whether such knowledge was obtained through Buyer's own investigation or through disclosure by Seller or another person, and regardless of whether such knowledge was obtained before or after the execution and delivery of this Agreement.

28. See Coastal Power Int'l, Ltd. v. Transcon. Capital Corp., 10 F. Supp. 2d 345 (S.D.N.Y. 1998); Rogath v. Siebenmann, 129 F.3d 261 (2d Cir. 1997); Galli v. Mertz, 973 F.2d 145 (2d Cir. 1992). These cases are cited and discussed in Robert F. Quaintaince, Can You Sandbag? When a Buyer Knows Seller's Reps and Warranties are Untrue, 5 THE M&A LAWYER 8 (2002). Of course, sometimes it is the parties' express intention that the buyer will be deemed to have waived its indemnification right for a particular breach if it closes while having knowledge of that breach. In such cases, the parties include a so-called "anti-sandbagging" clause in the acquisition agreement to make this intention clear. A buyer should carefully consider the implications of agreeing to such a provision, however, because the seller may create an issue of fact in response to any buyer indemnification claim simply by claiming that the buyer must have known about the breach. In any event, a buyer should be aware, as described above, that the buyer might be deemed to have waived its rights even if no "anti-sandbagging" provision is included. See Quaintaince, supra.


30. See Ziff Davis Publ'g, 553 N.E.2d at 1002 n.2; Am. Tobacco Co. v. Grinnell, 951 S.W.2d 420, 436 (Tex. 1997) ("Though not a fraud-based claim, an express warranty claim also requires a form of reliance . . . [and the Uniform Commercial Code's requirement that express warranties be] part of the 'basis of the bargain' loosely reflects the common-law express warranty requirement of reliance.").
B. CONTRACTUALLY EXONERATING CORPORATE OFFICERS FROM PERSONAL EXPOSURE FOR TORT LIABILITIES ARISING OUT OF CORPORATE CONTRACTUAL OBLIGATIONS

We were reminded during this Survey period that "a corporate agent can be held individually liable for fraudulent statements or knowing misrepresentations even when they are made in the capacity of a corporate representative." Our repeated calls for the Texas courts to properly apply Article 2.21 of the Texas Business Corporation Act and to preempt the application of this common-law agency principal in the context of corporate officers negotiating and executing corporate contractual obligations were unheeded in the past and were unheeded during this Survey period. The possibility that corporate officers could be held personally liable for torts arising from the negotiation and execution of corporate

31. A.C.S. Wright v. Sage Eng'g, Inc., 137 S.W.3d 238, 250 (Tex. App.—Houston [1st Dist.] 2004, pet. denied); see also Cimarron Hydrocarbons Corp. v. Carpenter, 143 S.W.3d 560, 564 (Tex. App.—Dallas 2004, pet. filed) ("[A] corporate agent is personally liable for his own fraudulent or tortious acts, even when acting within the course and scope of his employment."); Morris v. Powell, 150 S.W.3d 212, 220-21 (Tex. App.—San Antonio 2004, no pet. h.) ("Corporate agents are individually liable for fraudulent or tortious acts committed while in the service of their corporation."). This result applies to the corporate officer even though he is acting solely on behalf of his corporate principal and "regardless of whether he receives any personal benefit from the tortious act." See Cass v. Stephens, 156 S.W.3d 38 (Tex. App.—El Paso 2004, orig. proceeding [mand. pending]); see also West & Treadway, supra note 2, at 812, 820 n.65.

32. Article 2.21 provides in pertinent part that
A holder of shares, . . . or any affiliate thereof or of the corporation, shall be under no obligation to the corporation or to its obliges with respect to . . . any contractual obligation of the corporation or any matter relating to or arising from the obligation on the basis that the holder . . . or affiliate is or was the alter ego of the corporation, or on the basis of actual fraud or constructive fraud, a sham to perpetrate a fraud, or other similar theory, unless the obligee demonstrates that the holder . . . or affiliate caused the corporation to be used for the purpose of perpetrating and did not perpetrate an actual fraud on the obligee primarily for the direct personal benefit of the holder, . . . or affiliate; . . . (emphasis supplied).

33. See West, supra note 2, at 1226-31; West & Treadway, supra note 2, at 814-16; West & Chao, supra note 2, at 1403-08; West & Nelson, supra note 2, at 804-09. As noted in past Texas Corporations Surveys, and reaffirmed during this Survey period, the Texas courts appear prepared to accept the applicability of Article 2.21 in veil piercing cases directed at corporate shareholders. See West & Chao, supra note 2, at 1403-08; West & Nelson, supra note 2, at 804-09; Rimade Ltd. v. Hubbard Enters., Inc., 388 F.3d 138 (5th Cir. 2004); Signal Peak Enters. of Tex., Inc. v. Bettina Inv., Inc., 138 S.W.3d 915 (Tex. App.—Dallas 2004, pet. struck). The Texas courts do not, however, appear prepared to accept the idea that a corporate officer, acting as an agent and fiduciary at the direction and under the authority and control of her corporation, is an affiliate of the corporation for the purpose of Article 2.21 and therefore entitled to its protections. See West & Chao, supra note 2, at 1403-08; West & Nelson, supra note 2, at 804-09. For further support for the idea that a corporate officer is an affiliate of her corporation because, as an agent and fiduciary, she is under the control of her corporate principal see Nat'l Plan Adm'rs, Inc. v. Nat'l Health Ins. Co., 150 S.W.3d 718, 730 (Tex. App.—Austin 2004, pet. filed) ("A true fiduciary is bound to serve the primary interests of the principal and to subvert his own self-interests when they are in conflict."); Loy v. Harter, 128 S.W.3d 397, 407 (Tex. App.—Texarkana 2004, pet. denied) ("Obedience" is one of the "broad duties [that] stem from the fiduciary status of corporate officers . . ."); Crooks v. Moses, 138 S.W.3d 629, 637 (Tex. App.—Dallas 2004, no pet. h.) ("Agency is the consensual relationship between two parties when one, the agent, acts on behalf of the other, the principal, and is subject to the principal's control.").
contracts is particularly troublesome given our discussion in Section II, Part A. In an effort to contractually exonerate corporate officers from liability for fraud or negligent misrepresentation arising from statements made on behalf of their corporate principal in connection with the negotiation and execution of a corporate contractual obligation (whether such statements are made outside or inside the four corners of the contract), we suggest the inclusion of the following provision in purchase and sale agreements between corporate parties:

**No Third Party Liability.** This Agreement may only be enforced against the named parties hereto. All claims or causes of action (whether in contract or tort) that may be based upon, arise out of or relate to this Agreement, or the negotiation, execution or performance of this Agreement (including any representation or warranty made in or in connection with this Agreement or as an inducement to enter into this Agreement), may be made only against the entities that are expressly identified as parties hereto; and no officer, director, shareholder, employee or affiliate of any party hereto (including any person negotiating or executing this Agreement on behalf of a party hereto) shall have any liability or obligation with respect to this Agreement or with respect to any claim or cause of action (whether in contract or tort) that may arise out of or relate to this Agreement, or the negotiation, execution or performance of this Agreement (including a representation or warranty made in or in connection with this Agreement or as an inducement to enter into this Agreement).  

C. **Ensuring that a Letter of Intent Remains a Letter of Intent**

Whether a particular memorandum, letter, or other document constitutes an enforceable obligation or a mere expression of intent continues to be the focus of a number of decisions by the Texas courts. The absolute necessity of clearly stating that a letter of intent is not intended to be enforceable has been emphasized repeatedly during each of the last four Survey periods. In the absence of an express intent to be nonbinding, Texas courts repeatedly hold "that 'a binding contract may be formed if the parties agree on the material terms, even though they leave open other provisions for later negotiation,' and that 'a letter of intent may be binding even though it refers to the drafting of a future, more formal,

34. One could also consider adding this provision as an additional sentence to the "No Third Party Beneficiary" clause and simply change the caption to "No Third Party Beneficiary or Liability." One should make clear in the "no third party beneficiary" language, however, that this provision is in fact intended to benefit third parties (i.e., the officers, directors, shareholders, employees and affiliates of the corporate parties) in the same manner as exceptions are customarily made for indemnification provisions that benefit officers, directors or employees.

35. We believe this clause will also help defeat "alter ego," "single business enterprise" and similar "piercing the corporate veil" claims.

36. See generally West, supra note 2, at 1233-38; West & Treadway, supra note 2, at 818-23; West & Chao, supra note 2, at 1411-15; West & Nelson, supra note 2, at 818-19.
agreement." Last year, however, we highlighted a case which declared, "when subsequent actions by the parties suggest that they did intend to be bound by an agreement that was expressly nonbinding, Texas courts have held that the intent of the parties to be bound becomes a question of fact." We suggested, therefore, that in addition to a provision clearly stating that the letter of intent was intended to be nonbinding, "consideration may also be given to including in a letter of intent a provision disclaiming any intention to be subsequently bound by a nonbinding letter of intent as a result of actions taken in furtherance thereof." During this Survey period, COC Services, Ltd. v. CompUSA, Inc. provided an opportunity for a more thorough discussion of this purported "partial performance" exception to the nonbinding nature of letters of intent that clearly state they are nonbinding.

COC Services involved a proposed master franchise agreement involving CompUSA stores in Mexico. The parties entered into a letter of intent that granted "COC the exclusive right to negotiate to establish stores in Mexico, subject to expiration on a set date." The specified expiration date was ultimately extended until December 31, 1999. Attached to the letter of intent were detailed forms of each of the proposed master franchise agreements ("MFA") and the proposed license agreement for the initial licensee operating under that MFA. The letter of intent further specified that "if both the MFA and a license agreement were not timely executed, COC's exclusive negotiation rights expired with no further obligations between the parties." In other words, the letter of intent contemplated only an exclusive right for COC to negotiate to in-

37. West & Chao, supra note 2, at 1411 (quoting John Wood Group USA, Inc. v. ICO, Inc., 26 S.W.3d 12, 19-20 (Tex. App.—Houston [1st Dist.] 2000, pet. denied), as reviewed in West, supra note 2 at 1233-38). During this Survey period, in Kelly v. Rio Grande Computerland Group, 128 S.W.3d 759 (Tex. App.—El Paso 2004, no pet.), the court found that it was a fact question whether a letter of intent that was "explicitly made subject to 'approval of counsel for all parties and to the preparation and execution of a final binding agreement prepared by counsel to all parties'" was an enforceable agreement even though a subsequent purchase agreement that did not cover all of the terms of the letter of intent was executed by the parties. Id. at 764. The court noted that the letter of intent did not have a provision "clearly stating that the letter is nonbinding, as such negations of liability have been held to be effective." Id. at 767. The court also held that it was a fact question "whether the Purchase Agreement was only the first in a series of agreements to be executed by the parties as memorialized in the Letter of Intent." Id. at 769. Moreover, the entire agreement clause in the purchase agreement was not considered to dispose of the issue because it was, as many entire agreement clauses are, limited to "the subject matter of this Agreement," which did not cover all the subjects covered by the letter of intent. Id. at 768. The obvious fix here would have been specific mention of the letter of intent as having been superseded by the purchase agreement if that was in fact the intent. See also Castano v. San Felipe Agric., Mfg. & Irrigation Co., 147 S.W.3d 444, 449-51 (Tex. App.—San Antonio 2004, no pet.).


41. Id. at 660.

42. Id. at 662.

43. Id. at 664.
introduce a third party to CompUSA as the initial licensee for a specified period, with the proviso that if the MFA and the initial license were not executed before December 31, 1999, there would be no further obligations of any kind under the letter of intent or the MFA.\footnote{44}

The letter of intent was executed in January of 1999. In early September 1999, Grupo Carso, a Mexican company with a fifteen percent stake in CompUSA, began discussions with COC about its franchising of CompUSA stores in Mexico. COC, Carso, and CompUSA met a few weeks later concerning the proposed franchise arrangement whereby Carso would presumably become the initial licensee. No further discussions were held between COC and Carso; thereafter, CompUSA and Carso periodically discussed Carso’s interest in acquiring CompUSA in its entirety. After the September meetings between Carso, COC and CompUSA, COC had several conversations with the CEO of CompUSA concerning the lack of responsiveness by Carso. About two weeks before the letter of intent would expire, COC sent a proposal to CompUSA for a new licensee candidate from Mexico. CompUSA responded that it had insufficient information to evaluate the new candidate. In the first week of January 2000, immediately following the expiration of the letter of intent, Carso and CompUSA again began negotiations regarding the acquisition of CompUSA by Carso. By the end of January 2000, those negotiations led to the acquisition of CompUSA by Carso.\footnote{45}

COC filed suit against CompUSA claiming that the unexecuted MFA attached to the letter of intent was a binding, enforceable agreement that CompUSA breached. COC also sued Carso for tortious interference with the MFA. The jury found in favor of COC against both Carso and CompUSA and awarded substantial damages for lost profits and punitive damages.\footnote{46}

On appeal, the court focused on whether there was any issue of fact that was properly submitted to the jury respecting the parties’ intent to be bound by the MFA. Among the issues considered by the court was whether the parties’ actions subsequent to the execution of the letter of intent raised a fact issue of the parties’ intent to be bound by the unexecuted MFA.\footnote{47} Among the evidence suggesting that CompUSA intended to be bound by the MFA were statements made by the CompUSA CEO

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\item \footnote{44}{Id.}
\item \footnote{45}{Id. at 661.}
\item \footnote{46}{Id. at 661-62.}
\item \footnote{47}{The court also noted that the MFA, which despite its detail had left several terms blank to be negotiated after the initial licensee was determined, lacked at least one essential term necessary to make it enforceable—the minimum revenue stream payable to CompUSA. \textit{Id.} at 665. The court also suggested that Texas actually recognizes “a five-factor test” for determining whether the binding nature of a letter of intent is a question of law for the court or a question of fact for the jury. Those five factors, which derive from a Second Circuit case applying New York law and which the \textit{John Wood} court cited with approval, are “(1) the language of the agreement, (2) the context of the negotiations, (3) the existence of open terms, (4) partial performance, and (5) the necessity of putting the agreement in final form, as indicated by the customary form of such transactions.” \textit{Id.} at 668 (citing Arcadian Phosphates, Inc. v. Arcadian Corp., 884 F.2d 69 (2d Cir. 1989)). As
\end{itemize}
and materials sent to prospective licensees approved by CompUSA suggesting that “COC currently owns a CompUSA Master Franchise.”

COC also argued that it expended substantial “efforts to locate a suitable licensee,” which was one of the main obligations of COC under the MFA. According to the court, however, “COC’s efforts to locate a licensee were consistent with performance of the [letter of intent] and not unequivocally referable to COC’s performing under the MFA” because the letter of intent and COC’s exclusive negotiation rights would terminate if both the MFA and an initial license agreement were not executed prior to December 31, 1999. Accordingly, the court refused to “consider conduct consistent with performance of the [letter of intent] as probative of performance under the MFA.”

Likewise, the court noted that COC never performed any of the primary obligations specified in the MFA, such as opening stores or paying the initial fee. More importantly, the CEO’s statements and his acquiescence in the preparation of materials for prospective licensees, and any of the other actions purported to be in furtherance of the MFA, were insufficient to overcome the express language in the letter of intent. Therefore, there was no fact issue as to whether the parties intended to be bound by the unexecuted MFA.

We suspect that, given the court’s substantial deference to the language of the letter of intent, the court’s analysis would have been simplified if the language of the letter of intent was clearer. We have set forth below our suggested clause to clearly express that a letter of intent is not binding and that subsequent actions will not be deemed to alter that intent:

**Non Binding Obligations.** This letter is nonbinding and is intended only to memorialize certain preliminary terms related to a proposed transaction between the parties hereto; and the terms set forth herein do not constitute all of the material terms upon which agreement must be reached. This letter is not intended to create and shall not create any binding, enforceable obligations between the parties hereto; and no prior or subsequent conduct or action by the parties hereto, whether in furtherance of the proposed transaction or otherwise, shall abrogate the foregoing disclaimer of intent to be bound hereby or create any binding obligations respecting the proposed transaction. A binding obligation respecting the proposed transaction shall arise, if at all, only upon the execution of a subsequent formal agreement by all the parties hereto, the terms of which shall supersede this letter and all prior negotiations, discussions, representations, agreements and understandings, whether written or oral, respecting the proposed transaction.

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48. *Id.* at 669.
49. *Id.*
50. *See id.*
51. *Id.* at 668-69.
52. *Id.* at 670.
53. Obviously a letter of intent may include certain binding provisions such as expense reimbursement, exclusivity of negotiations and confidentiality. If there are binding provi-
Corporations (in this case, a law firm organized as a professional corporation) continued to engage in the legal services business,\(^6\) the concurring opinion emphasized that the legislative intent behind Article 5.09(B) was to treat an asset sale as one in the usual and regular course of business if the corporation engaged in any business following the sale—“even if the corporation did not engage in that business before the sale.”\(^7\)

The relevant facts of the case are as follows. In 1999, two law firms—Arnold White & Durkee, P.C. (“AWD”) and Howrey & Simon (“H&S”)—negotiated a Combination Agreement under which AWD transferred all of its assets (other than a few that were specifically excluded) to H&S in exchange for becoming a “Level II Partner” in H&S. H&S subsequently changed its name to Howrey Simon Arnold & White, L.L.P. (“HSAW”). The assets specifically excluded were three vacation condominiums, two insurance policies, and several automobile leases.\(^8\)

AWD, a Texas professional corporation, held a shareholders’ meeting to vote on the proposed combination with H&S, and the meeting notice stated that a two-thirds majority of Class B and Class C shares would be required for passage. At the meeting, the combination was approved by a two-thirds vote. The three plaintiff-appellants in *Rudisill* were holders of Class B or Class C shares. Each submitted a written objection to the combination prior to the meeting and then voted against the combination at the meeting, pursuant to the procedures for dissenting found in Article 5.12 of the Texas Business Corporation Act.\(^9\)

AWD argued that, despite the fact that the transaction was submitted for approval by a two-thirds majority shareholder vote, the sale was in the usual and regular course of business pursuant to Article 5.09(B), and thus dissenters’ rights were not available.\(^10\) The trial court agreed, and the Fourteenth District Court of Appeals affirmed, holding that AWD continued to engage in business following the sale of nearly all of its assets to H&S, even though AWD was essentially a passive owner of a partnership interest in the new firm, HSAW.\(^11\)

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67. Id. at 561 n.7.
68. Id. at 566 (Frost, J., concurring).
69. Id. at 558.
70. Id.
71. The majority noted that AWD did in fact submit the transaction to a shareholder vote and indicated in the meeting notice that a two-thirds majority vote was required for approval. The majority found that this was irrelevant to its determination of whether dissenters’ rights were available. See id. at 563. Pursuant to Article 5.11(A)(2), dissenters’ rights are available only in cases where a two-thirds majority shareholder vote is required, which is not the case if Article 5.09(B) applies. See id.
72. Id. at 561. The majority added the following in a footnote, which puts an interesting gloss on the above discussion regarding whether, for purposes of Article 5.09(B), the majority believed that a corporation must continue in the same business following the transaction.

It is also important to note that, although the statute provides that a corporation can continue in business if it applies a portion of the consideration received from the transaction to the conduct of a business in which it engages following the transaction, the parties have, for the most part, limited their
The plaintiff shareholders cited the following facts in support of their argument that AWD did not engage in any business following the transaction. AWD had no income other than what it received as a partner in HSAW, had no clients separate from HSAW and did not market itself as a separate firm. Indeed, as the plaintiffs noted, AWD transferred to H&S all the assets it had previously used to operate a legal services business. Moreover, following the combination, all of the shareholders of AWD were eligible to become partners in HSAW; many shareholders began holding themselves out as partners of HSAW. The number of shareholders and employees of AWD dwindled after the transaction, and as existing shareholders of AWD retired, withdrew or otherwise terminated their relationship, AWD's partnership interest in HSAW was reduced by the same percentage as the departing shareholder's equity interest in AWD.\footnote{See \textit{id.} at 574 (Frost, J., concurring).} It is difficult to conceive of a practical difference between the business combination crafted by AWD and H&S and one in which AWD had been liquidated and its shareholders given direct partnership interests in HSAW.

The Fourteenth District Court of Appeals disagreed with the plaintiffs, however, holding that AWD did continue to engage in business following its combination with H&S. In fact, the majority opinion concluded that AWD continued to engage in the \textit{legal services business},\footnote{\textit{id.} at 558, 562 n.10, 573 n.7 (Frost, J., concurring).} a conclusion that the concurring justice found unnecessary to reach.\footnote{\textit{id.} at 574 (Frost, J., concurring).}

The majority indicated that "[i]t is clear that AWD remained in the legal services business, at least indirectly, in that (1) its shareholders and employees continued to practice law under the auspices of HSAW, and (2) it held an ownership interest in HSAW, which unquestionably contin-
ues directly in the business.” The concurrence expressed some doubt that AWD continued in the legal services business but concluded, without any analysis, that AWD did continue to engage in some business following its combination with H&S, which was enough for the concurrence to hold that Article 5.09(B) applied to the transaction.

This outcome is surprising to corporate practitioners who are familiar with traditional formulations of the “sale of all or substantially all assets” provision. The concurrence highlighted the irregularity of Article 5.09(B) among corporation laws:

Texas . . . is unique in defining “usual and regular course of business” in a way that includes the most unusual, irregular, and extraordinary events in the life of a corporation. Texas’ singular definition of this well-worn term in Article 5.09(B) of the Texas Business Corporation Act effectively eliminates the necessity for shareholder approval in many transactions that, even in the common parlance and understanding, would never be considered in the “usual and regular course of business.”

Additionally, an official comment to the Model Business Corporation Act (on which the Texas Business Corporation Act is based) provides quite narrow circumstances in which it would be in the usual and regular course of business for a corporation to sell all of its assets, including, for example, the sale of a corporation’s only business where the corporation was formed to buy and sell businesses and the proceeds are to be reinvested in another business. Article 5.09(B), however, was not drawn from the Model Act, and the concurrence noted that a comparison of the Texas provision to other similar statutes “suggests the Texas legislature intended a major departure in the definition of ‘usual and regular course of business.’”

What is unclear is whether the legislature intended this departure to

76. Id. at 563.
77. The concurrence pointed out that “[s]ince the effective date of the combination, Arnold White & Durkee has been nothing more than a passive partner in Howrey Simon.” Id. at 573 n.7 (Frost, J., concurring). The concurrence further noted that: [t]he majority finds that Arnold White & Durkee needs no more than lawyers themselves to engage in the legal-services business. The record shows that when Arnold White & Durkee had clients, the firm used a great deal more than lawyers to engage in the legal-services business, including leasehold interests, books, computers, furniture, equipment, and many other operating assets. Though it may be technically possible to engage in the legal-services business with no operating assets, as the majority suggests, Arnold White & Durkee clearly did not do so before the asset transfer, when the firm still had clients. With no “tools of the trade” it would seem that the firm’s few remaining lawyers and support staff would be ill-equipped to service clients even if there were some. Likewise, with no clients to consume legal services, it is questionable whether Arnold White & Durkee could, directly or indirectly, continue in the legal-services business.

Id. at 573 n.8 (Frost, J., concurring).
78. See id. at 566, 573, 574 (Frost, J., concurring).
79. Id. at 566 (Frost, J., concurring).
80. Id. at 570 (Frost, J., concurring).
81. Id. at 57-71 (Frost, J., concurring).
extend as far as the *Rudisill* decision. In the *Rudisill* transaction, the selling corporation retained no useful assets and continued only as the owner of a partnership interest in the surviving entity. This raises the question whether a selling corporation in Texas, in order to avoid the shareholder approval and dissenters' rights provisions of the Texas Business Corporation Act, need only structure a transaction such that a portion of its consideration is in the form of an ownership interest (e.g., preferred stock representing a right to payment of a certain amount if certain financial targets are reached). The *Rudisill* concurrence indirectly suggested that this would be the case.

Arguably, all the board of directors of a corporation would have to do to avoid these statutory shareholder protections is to arrange for the corporation to continue in some business—even though very different from the corporation's prior business—so that the corporation can "engage in a business" after the sale of all or substantially all of the corporation's assets. Given the relative ease of structuring a transaction in this manner, a corporation in Arnold White & Durkee's position could avoid triggering the statutory shareholder protections, leaving minority shareholders vulnerable to fundamental corporate change without shareholder approval or an appraisal remedy for dissenting shareholders.

Thus, as the *Rudisill* decision makes clear, the Texas Legislature, in its attempt to provide certainty to corporations engaging in significant asset sales, has left the door wide open for Texas corporations to structure transactions to avoid shareholder approval and dissenters' rights even in the case of a transaction that is, in essence, a complete liquidation of the corporation's assets.

82. One law professor, commenting on the *Rudisill* decision, disagreed with the court that the Texas Legislature intended so broad an exception when it enacted Article 5.09(B). See Jill Schachner Chanen, *Dissenting Partners Lose Out in Merger Ruling: Texas Case Seen as Boost to Corporations Over Appraisal Rights*, 41 A.B.A. J. E-REPORT 1 (2004). Chanen pointed out that the 1987 amendment to the Texas Business Corporation Act was made after two notable Delaware cases indicated that "substantially all" might mean less than fifty percent of a business's assets. *Id.* (citing *Katz v. Bregman*, 431 A.2d 1275 (Del. Ch. 1981) and *Gimbel v. Signal Cos., Inc.*, 316 A.2d 599 (Del. Ch. 1974)). Indeed, both prior to and after the 1987 enactment of Article 5.09(B), Delaware courts struggled to determine whether a particular asset sale by a corporation was a sale of all or substantially all of the corporation's assets. *See supra* note 59. It seems that the Texas Legislature, in enacting Article 5.09(B), intended to avoid similar uncertainty in the case of a significant asset sale by a Texas corporation.

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83. Rudisill, 148 S.W.3d at 572 (Frost, J., concurring).