SMU | Dedman School of Law

SMU Law Review

Volume 49
Issue 4 *Annual Survey of Texas Law*

Article 8

1996

Corporations

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I. INTRODUCTION

THERE were several interesting cases decided by Texas courts during the Survey period.[1] These cases are organized into the general categories of: (1) shareholder, director, and officer liability, (2) corporate status after merger, (3) corporate procedural rights, and (4) conduct of shareholder meetings. In addition, a bill amending several provisions of the Texas Business Corporation Act ("TBCA") was favorably considered by the Texas Legislature.[2] Although the bill did not pass, it is expected to pass early in the 1997 legislative session. A summary of the most significant provisions of the bill is included in the final section of this article.

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1. October 1, 1994 through September 30, 1995.

2. Letter from Curtis W. Huff, Chairman, *Corporation Law Committee of the Business Law Section of the State Bar of Texas*, to Alan W. Tompkins (Aug. 10, 1995) (on file with author).

II. JUDICIAL DEVELOPMENTS

A. PERSONAL LIABILITY OF OFFICERS, DIRECTORS, AND SHAREHOLDERS

1. Holloway v. Skinner[3]

In one of the most significant Texas decisions of the year, the Texas Supreme Court addressed whether Graham Holloway, the president, director, and largest shareholder of Holligan, Inc., could be held personally liable in tort for causing the corporation to breach its contracts with Rick Skinner. In 1981, Skinner contributed his Alvin Ord's sandwich shop franchise business to Holligan, Inc. in return for a promissory note, a royalty on the gross sales of the shops, and a management position with the corporation. Holloway served as president of the corporation and held forty percent of its common stock. During the next three years, Holligan failed to pay some of the amounts due Skinner, and Skinner's relationship with Holloway deteriorated. Skinner left his position with Holligan in 1984; the corporation defaulted entirely on its obligations to him in 1985.

Skinner successfully sued Holligan for the amounts owed under the contracts, but the corporation filed for bankruptcy before satisfying the judgment. Skinner then sued Holloway, claiming that he had tortiously interfered with the contracts by inducing the corporation's default. The trial court rendered judgment in favor of Skinner on the tortious interference claim. The Austin Court of Appeals affirmed, holding that Holloway was not immune from the claim of tortious interference and that he had used his position to gain a personal benefit at the expense of the corporation's creditors.[4]

Citing *Maxey v. Citizen's National Bank*,[5] the court stated the general rule that a corporate officer who causes the corporation to breach a contract cannot be held personally liable in tort if the decision was made in good faith and in the best interests of the corporation.[6] The court listed the elements of a cause of action for tortious interference as: "(1) the existence of a contract subject to interference, (2) the occurrence of an act of interference that was willful and intentional, (3) the act was a proximate cause of the plaintiff's damage, and (4) actual damage or loss occurred."[7] Regarding the first element, the majority noted that "[w]hen there is a complete identity of interests [between a corporation and its stockholder], there can be no interference as a matter of law."[8] The ma-

3. 898 S.W.2d 793 (Tex. 1995).

4. *See* Holloway v. Skinner, 860 S.W.2d 217 (Tex. App.—Austin 1993) (affirming trial court decision in favor of Rick Skinner); John D. Jackson & Alan W. Tompkins, *Annual Survey of Texas Law: Corporations and Limited Liability Companies*, 47 SMU L. Rev. 901, 915 (1994) [hereinafter *Jackson & Tompkins*] (discussing Holloway v. Skinner).

5. 507 S.W.2d 722 (Tex. 1974).

6. 898 S.W.2d at 795.

7. *Id.* at 795-96 (citing Browning-Ferris Indus. v. Reyna, 865 S.W.2d 925, 926 (Tex. 1993).

8. *Id.* at 797.

jority held that the first element was satisfied, despite the "substantial alignment" of Holloway's interests with those of the corporation, because Holloway owned only forty percent of its stock.[9]

The majority then held that in order to establish the second element when the defendant is both a corporate officer and the breach-inducing party, the plaintiff must prove that "the defendant acted in a fashion so contrary to the corporation's best interests that his actions could only have been motivated by personal interests."[10] The majority reasoned that:

> [T]he mere existence of a personal stake in the outcome, especially when any personal benefit is derivative of the improved financial condition of the corporation or consists of the continued entitlement to draw a salary, cannot alone constitute proof that the defendant committed an act of willful or intentional interference. . . . Were this not the rule, virtually every failure to pay a corporate debt would constitute a prima facie case of tortious interference against the corporate officer who decided not to pay the debt.[11]

In reviewing the facts, the majority noted that the corporation had severe cash flow problems and current liabilities far in excess of current assets at the time of the defaults.[12] The majority concluded that although Skinner was required to prove "more than the fact that [Holloway] benefitted from the breach," no evidence indicated that the breach was motivated by Holloway's pursuit of his own interests.[13] The decision of the Austin Court of Appeals was reversed, and judgment was rendered that Skinner take nothing.[14]

Justice Hecht, joined by Justice Owen, concurred in the judgment but disagreed strongly with the majority's approach to concluding that Holloway was not liable. His principle criticism was that the law should not burden an agent with potential liability to third parties when the principal is not dissatisfied with the agent's actions. His rationale is summarized in the following quotation:

> An agent who acts to better his own interests cannot be held liable for tortious interference if his actions are also in his principal's best interests. . . . The rule [adopted by the majority] allows a third party to show that an agent's conduct was contrary to his principal's interest, even if the principal asserts the opposite position . . . . [U]nder the Court's rule, Skinner can argue that Holloway did not act in Holligan's best interests when Skinner does not share those interests and when Holligan itself has no complaint . . . .[15]

Justice Hecht wrote that the better rule, in the context of a contract between a third party and an agent's principal, is that the agent should be

9. *Id.*
10. *Id.* at 796.
11. 898 S.W.2d at 796.
12. *Id.* at 798.
13. *Id.*
14. *Id.*
15. *Id.* at 799.

held liable for tortious interference only if the agent has exceeded the scope of his authority.[16] Hecht pointed out that Holloway would have been better situated if he had personally guaranteed the corporation's obligations to Skinner because he could have avoided $100,000 in punitive damages.[17] He cited numerous cases to support his view that the majority's rule is flawed and "prone to mischief," but ultimately concurred in the court's judgment.[18]

In a separate concurrence, Justice Enoch wrote that the majority was trying to place a "square peg into a round hole" by focusing on the second element of the tortious interference claim.[19] His view, which was shared by Justice Hecht, was that Holloway's authority to act on behalf of the corporation was the decisive issue. Enoch wrote that "[u]nder the first element of the tortious interference with contract cause of action, there must be a contract that was subjected to interference. If the interferer is a party, then there was no contract subjected to interference because a party cannot interfere with himself."[20] Enoch reasoned that in the case of a contract with a corporation, the plaintiff must establish that the corporate officer should be treated as a stranger to the contract and not as the contracting party. In other words, the plaintiff has the burden of proving that the corporate agent acted outside his scope of authority.[21] Enoch agreed that Skinner had presented no evidence establishing that Holloway acted to serve his own interests to the detriment of the corporation, and concurred in the court's judgment.[22]

2. *Ex Parte Chambers*[23]

A leading contender for the 1995 "Miscarriage of Texas Justice Award"[24] was the Texas Supreme Court's decision in *Ex Parte Chambers*. This case involved the issue of whether a corporation's sole officer, director, and shareholder could properly be held in contempt of court for his failure to cause the corporation to pay a contempt fine levied against it. As the basis for the appeal, Franklin Delano Chambers sought a writ of habeas corpus. The facts indicated that in early 1992, Chambers was employed by a business brokerage firm known as International Business Exchange Corporation ("Exchange"). Chambers left Exchange and, in April of 1992, formed International Business Search, Inc. ("IBS") to op-

16. 898 S.W.2d at 798.
17. *Id.* at 800.
18. *Id.* at 803 (citing Wagenseller v. Scottsdale Memorial Hosp. 710 P.2d 1025, 1043-44 (Ariz. 1985); Morriss v. Coleman Co., 738 P.2d 841 (Kan. 1987)).
19. *Id.* at 804.
20. *Id.*
21. 898 S.W.2d at 804.
22. *Id.*
23. 898 S.W.2d 257 (Tex. 1995).
24. This award was inspired by a passage from Justice Enoch's concurrence in *Ex Parte Chambers*. *See id.* at 263. The award is dedicated to those who believe that even though the procedural formalities of the law exist for our mutual benefit and protection, sometimes things just don't turn out right. *See, e.g.*, People v. Orenthal James Simpson, Cause No. BA097211, Super. Ct. for the State of California, County of Los Angeles.

erate in direct competition with Exchange. IBS employed Chambers and several other former Exchange employees. Exchange sued Chambers, IBS, and the former Exchange employees for violating the non-disclosure and non-competition agreements that they had signed while working for Exchange. In mid-1992, Exchange obtained an injunction restraining the defendants from using Exchange's trade secrets and confidential information.

In early 1993, Chambers and the individual defendants were found in contempt of court for violating the injunction. Small fines were imposed and paid. Chambers then transferred all the assets of IBS to his new sole proprietorship ("IBS II"). The proprietorship engaged in the same business practices as IBS. In June of 1993, another contempt order was issued against IBS alone, which by that time had no assets. The contempt order against IBS required payment of a $3,000 fine within 10 days. At a hearing approximately four months after the second contempt order was issued, Chambers argued that IBS was unable to pay the fine. The court found both Chambers and IBS to be in contempt, and ordered Chambers to personally pay a $6,000 fine and spend seven days in jail. Chambers sought a writ of habeas corpus, which the Third Court of Appeals denied.[25]

The Texas Supreme Court granted Chamber's writ of habeas corpus because Chambers established that IBS was unable to pay the fine.[26] In its analysis, the court focused on whether an officer, director and shareholder can be held in contempt of court when the violated order is directed only to the corporation. The court noted that for a corporate agent to be charged with contempt, there must be evidence that the agent was personally connected with defying the decree.[27] The court had no difficulty finding that because Chambers controlled IBS, he had personally participated in the violation and had notice of the contempt order. Thus, the contempt order was held to be valid on those grounds.[28] The court found, however, that because IBS did not have sufficient assets to pay the fine at any time after the second contempt order was entered, the failure to pay by Chambers and IBS was involuntary.[29] The court noted that the involuntary inability to comply is a valid defense to criminal contempt.[30]

Although Exchange argued that IBS was Chamber's alter ego and that the fine should be paid out of Chamber's personal assets, the court took Exchange to task for failing to allege the alter ego theory in its motion for contempt.[31] The court found that Chambers had no duty to preserve the assets of IBS for the payment of fines "which hypothetically would be

25. *Id.* at 259.
26. *Id.*
27. *Id.* at 259-61.
28. 898 S.W.2d at 261.
29. *Id.* at 261-62.
30. *Id.* at 262.
31. *Id.*

levied in the future."[32] The majority stated that it could not justify Chambers' imprisonment when Exchange's motion for contempt did not allege the alter ego theory, and granted the writ of habeas corpus.[33] In concurring in the judgment, Justice Enoch disagreed with the majority's basic premise that a corporate agent could be held in contempt for the violation of a contempt order directed only against the corporation.[34] He also chastised the trial court for its June, 1993 contempt judgment because it implicitly found that the corporation was Chambers' alter ego without having provided him with adequate notice of the charges.[35]

In dissent, Justice Raul Gonzalez correctly argued that the Court should have refused to allow Chambers to "brazenly flout[ ] the orders of the trial court [and make] a mockery of the judicial system."[36] He felt that it was clear that Chambers had repeatedly violated the trial court's injunctions and had only challenged the trial court after the issuance of the second contempt order.[37] Gonzalez opined that IBS's inability to pay was not involuntary because IBS had sufficient assets to pay the fine at one time, and was unable to comply with the contempt order only because of Chamber's voluntary dissipation of the corporation's assets.[38] Additionally, Gonzalez noted that piercing the corporate veil was not necessary in order to hold Chambers personally liable because he was the only person who could have caused IBS to pay its fine.[39] Gonzalez reasoned that "[t]he power to hold parties in contempt and to sanction noncompliance is an essential element of judicial independence and authority,"[40] and stated that he would have affirmed the trial court's judgment of contempt.[41]

3. *Valley Mechanical Contractors, Inc. v. Gonzales*[42]

In this case, the Corpus Christi Court of Appeals addressed whether the alter ego and corporate disregard doctrines could be used to reach corporate funds in order to satisfy the obligations of the corporation's president. In 1988, attorney Ernesto Gonzales represented Isidora Wabler in her divorce from David Wabler. The divorce decree ordered Mr. Wabler to pay Gonzales $13,075 in attorney's fees. In 1991, while the judgment was outstanding, Mr. Wabler formed Valley Mechanical Contractors, Inc. ("VMC"). The corporation was purportedly formed for the operation of a commercial air conditioning business. Wabler personally paid the costs of incorporating VMC, appointed himself president, and

32. *Id.*
33. 898 S.W.2d at 266.
34. *Id.* at 262-63.
35. *Id.* at 263.
36. *Id.* at 263.
37. *Id.* at 263.
38. 898 S.W.2d at 266.
39. 898 S.W.2d at 267-68.
40. *Id.* at 267.
41. *Id.* at 269.
42. 894 S.W.2d 832 (Tex. App.—Corpus Christi 1995, no writ).

opened two corporate banks accounts on which he was the sole signatory. Wabler made his brother, Raymond, the sole shareholder of VMC even though Raymond paid no consideration for the shares.

Gonzales applied for a writ of garnishment against VMC's funds in 1993, alleging that VMC was Wabler's alter ego. Gonzales presented evidence that VMC's bank accounts were not properly maintained and that VMC made several payments to Wabler for which there was no adequate documentation. Further, although Wabler testified that his VMC salary was his only source of income, the evidence indicated that deposits to his personal bank account far exceeded his salary. Finally, the evidence showed that VMC had paid Wabler's home telephone bill. Based on the record, the trial court found that VMC was Wabler's alter ego and ordered garnishment against VMC's bank accounts.[43] VMC appealed on the grounds of evidentiary insufficiency.[44]

In affirming the judgment, the Corpus Christi Court of Appeals reviewed the operative differences between the *Castleberry v. Branscum*[45] corporate disregard doctrine and the alter ego doctrine. Citing *Castleberry*, the court noted that Texas courts will disregard the corporate fiction when it has been used as part of an unfair device to achieve an inequitable result.[46] The court stated that the third *Castleberry* circumstance justifying disregard of the corporate form—when it is used to evade an existing legal obligation—was implicated in the case at hand.[47]

The court wrote that the alter ego doctrine is used to disregard the corporate fiction when there is "such unity between a corporation and an individual that an adherence to the fiction of a separate existence would . . . sanction a fraud or promote an injustice."[48] An alter ego relationship can be shown when: (1) corporate formalities have not been followed or when corporate and personal property have been commingled, (2) an individual maintains an excessive financial interest, ownership, and control over the entity, or (3) the corporation has been used for personal purposes.[49] The rationale is if shareholders disregard the corporate form, the law will also disregard the form when necessary to protect corporate creditors.[50] Based on the evidence presented in the trial court, the court of appeals held that Wabler had created VMC as a means of avoiding his obligation to Gonzales, that he maintained total control over the corporation, and that the alter ego finding was proper.[51] The trial court's judgment was affirmed.[52]

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43. *Id.* at 833-34.
44. *Id.* at 833.
45. 721 S.W.2d 270 (Tex. 1986).
46. 894 S.W.2d at 834.
47. *Id.*
48. *Id.*
49. *Id.* at 835.
50. *Id.*
51. 894 S.W.2d at 836.
52. *Id.*

B. Corporate Status After Merger

The Texas Supreme Court's 1995 decision in *Bailey v. Vanscot Concrete Co.*[53] marked the second time in two years that the court has dealt with issues relating to the 1986 accident involving Wallace Bailey, Jr. and a batch of contaminated concrete.[54] In July of 1986, Vanscot Concrete ("Vanscot") merged into a corporation that subsequently changed its name to Tarmac Texas, Inc. The appropriate filings were made in the Texas Secretary of State's office to reflect the merger. Prior to the merger, Vanscot conducted business under the assumed names of Express Concrete Company ("Express") and Pennington Concrete Company ("Pennington"). Assumed name certificates were filed of record in Tarrant County. Three months after the merger, Bailey was injured by concrete from a truck bearing the name "Express/Pennington." Bailey sued Vanscot after he learned that both Express and Pennington were assumed names of Vanscot. Vanscot moved for summary judgment on the grounds that it had ceased to exist, as a result of the merger, approximately three months before the accident. The motion was denied, but Bailey made no effort to join Tarmac as a party. The case went to trial, during which Bailey amended his pleadings to name Vanscot d/b/a Express/Pennington as defendant. The jury found for Bailey.

Bailey sought judgment against Tarmac in a post-verdict motion, but the trial court rendered judgment only against Vanscot. On appeal, Vanscot successfully argued that it was not liable to Bailey because its existence had ended three months before Bailey's accident, and that the real party in interest—Tarmac—had never been joined as a party to the suit. The Fort Worth Court of Appeals held that Vanscot was not a correct party and dismissed the appeal. The Texas Supreme Court reversed the dismissal, holding that a corporation may still appeal a trial court judgment after the corporation has ceased to exist.[55] The Supreme Court remanded the case to the Fort Worth Court of Appeals, which rendered judgment that Bailey take nothing.

In his appeal, Bailey claimed that Vanscot continued to exist within Tarmac for the purpose of legal liability. Citing Article 5.06(A)(1) of the TBCA, the Supreme Court confirmed that Vanscot's actual and legal existence had ended upon the merger.[56] The court summarized the case in a footnote: "This is not a successor liability case in which a corporation commits a tort and thereafter either dissolves or merges. Rather, in Bailey's case, the corporation merged and then allegedly committed a tort. Therefore, Bailey was required to sue the corporation which injured

53. 894 S.W.2d 757 (Tex. 1995).

54. *See* Vanscot Concrete Co. v. Bailey, 853 S.W.2d 525 (Tex. 1993) (holding that a corporation which has ceased to exist as a result of merger has the right to appeal a trial court's judgment against it); *Jackson & Tompkins*, *supra* note 4, at 915 (discussing Vanscot Concrete Co. v. Bailey).

55. 853 S.W.2d at 526.

56. 894 S.W.2d at 759.

him—the post merger entity."[57]

Bailey also argued that Vanscot could not assert a lack of existence because it had failed to withdraw the assumed name certificates after the merger. The court held that there was no authority for imposing tort liability on Vanscot because of a failure to withdraw misleading certificates, and reasoned that the failure did not change the fact that Vanscot did not exist on the date of the accident.[58] The court noted that Bailey should have added Tarmac as a defendant after Vanscot identified it as the real party in interest, and "decline[d] to correct Bailey's error by retroactively substituting the correct party on his behalf."[59]

C. Corporate Procedural Rights

1. Disco Machine of Liberal Co. v. Payton[60]

This case dealt with the application of the statutory limitations period of TBCA Article 2.22-1[61] to a preemptive rights violation. In August of 1985, while George Payton was a shareholder of Diversified Industrial Service Company ("Diversified"), the corporation sold 355 shares to Disco Machine of Liberal Company ("Disco"). After several attempts to gain access to Diversified's books and records, Payton was permitted to review the books in April of 1990. At that time, he discovered the corporation's sale of shares to Disco. In August of 1991, Payton filed suit against the corporation and several other defendants in order to enforce his preemptive rights. The defendants moved for summary judgment, claiming that Payton's claim should have been brought within the four years after the violation occurred—or by August of 1989. Payton based his argument on Section C of TBCA Article 2.22-1, which became effective on August 28, 1989[62] and provides as follows:

> An action may not be brought . . . on account of any violation of any preemptive right . . . unless such action is brought within the earlier of: (1) One year after the date on which written notice is given to each shareholder whose preemptive right was violated . . . which notice shall . . . inform the shareholder that the issuance, sale, or other distribution . . . was in violation of the preemptive right of the shareholder; and (2) Four years after the date on which the corporation issued, sold, or otherwise distributed those shares or securities *or the effective date of this provision, whichever is later.*[63] (Emphasis added).

Because the statutory provision became effective in August of 1989, Payton argued that the limitations period for his claim ended in August of 1993 and, therefore, that his suit was timely filed. The trial court agreed and granted summary judgment for Payton.

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57. *Id.* at 759 n.1.
58. *Id.* at 759.
59. *Id.* at 761.
60. 900 S.W.2d 124 (Tex.App.—Amarillo 1995, writ requested).
61. Tex. Bus. Corp. Act. Ann. art. 2.22-1, § C (Vernon Supp. 1995).
62. *Id.*
63. *Id.*

In affirming the trial court decision, the Amarillo Court of Appeals held that the trial court's literal interpretation of the statutory language was consistent with the Texas Legislature's intent to make an "otherwise indefinite limitations period finite."[64] The appellate court noted that no evidence indicated that Payton knew, or should have known, about Diversified's sale of shares to Disco,[65] and that Payton had only found the preemptive rights violation because he sought access to the corporate records for valuation purposes.[66] Amazingly, the appellants argued that because Payton had been repeatedly (and possibly wrongly) denied access to Diversified's records since as early as the mid-1970s, he had effectively been put on notice about the preemptive rights violation.[67] The appellate court was not convinced, and overruled the appellant's point of error.[68]

2. State v. Empak, Inc[69]

In this case, Houston's Fourteenth District Court of Appeals considered whether a Texas corporation has a right to a speedy trial under both federal and state law. The opinion is significant because, as the case demonstrates, a corporation's right to a speedy trial can have a serious impact when regulatory enforcement actions are involved.

Empak operated a hazardous waste treatment facility in Harris County. Its customers were major chemical companies who routinely reviewed Empak's environmental compliance status and requested information about any pending criminal environmental actions against the company. In 1990 and 1991, the Harris County Pollution Control Department ("HCPCD") sent three notices of alleged water pollution violations to Empak, and the company responded to each notice within ten days of receipt. On April 29, 1991, Empak was charged with misdemeanor offenses of water pollution. It was not until over two years later, however, (on August 10, 1993) that Empak was served with a summons. Prior to the arraignment, Empak moved to dismiss the action based on the State's violation of Empak's right to a speedy trial under the United States and Texas Constitutions.

At the hearing on the motion to dismiss, Empak officials testified that despite the notices of violation, Empak had not disclosed to potential customers that it was subject to any ongoing environmental enforcement actions. Empak explained that this was because most violation notices did not result in enforcement action, and that during the long period between the violation notice and the summons, HCPCD gave no indication that Empak would be subject to any enforcement action.[70] Further, Empak

64. 900 S.W.2d at 126.
65. *Id.* at 127.
66. *Id.*
67. *Id.*
68. *Id.*
69. 889 S.W.2d 618 (Tex. App.—Houston [14th Dist] 1994, no writ).
70. *Id.* at 621.

had closed its files concerning the alleged violations because of the lapse of time.[71] The State offered no testimony or opposition to the motion to dismiss, and the trial court granted the motion.

In reviewing the trial court's decision, the appellate court noted that under both the state and federal constitutions, an accused is entitled to a speedy public trial.[72] While state and federal rights are independent, Texas courts generally look to federal courts to determine state constitutional rights.[73] While the State argued that the right to a speedy trial was "purely personal" to an individual citizen, the court found that "a corporation faced with pending criminal charges is vulnerable to many of the interests that have been recognized historically as being protected by the speedy trial right . . . ."[74] These interests include being forced to exist under a cloud of anxiety and suspicion as well as the loss of customers and goodwill. In examining the issue, the court found that numerous federal courts and courts in other states had determined that a corporate defendant was entitled to a speedy trial.[75] After discussing the logic of cases inside and outside the jurisdiction, the court concluded that corporations have a right to a speedy trial under the federal and state constitutions as well as the Texas Code of Criminal Procedure.[76] Based on this finding, the court was required to determine whether Empak's right to a speedy trial had been violated.[77]

In reviewing the facts, the appellate court found that the delay was not justified, particularly because the State had offered no evidence for the delay and because the charges could have adversely affected Empak's business.[78] While the court stated that the analysis of whether a defendant's right to a speedy trial had been violated is often difficult, the twenty-eight month delay by the State in this case was unreasonable.[79] Had the State offered some viable reason for the delay, the court's determination may have been different. Regardless of that fact, *Empak* confirms that Texas corporations have the right to a speedy trial when a criminal enforcement action is involved.

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71. *Id.*
72. *Id.*
73. *Id.*, (citing Harris v. State, 827 S.W.2d 949, 956 (Tex. Crim. App.) (en banc), *cert. denied*, 113 S.Ct. 381 (1992)).
74. 889 S.W.2d at 622.
75. *Id.*
76. *Id.* at 623; *see* TEX. CODE CRIM. PROC. ANN. art. 1.05 (Vernon 1977).
77. *Id.*; *see also* Barker v. Wingo, 407 U.S. 514, 531 (1972) (applying a balancing test to determine whether a defendant has been denied his right to a speedy trial). Under the *Barker* balancing test, the court reviews: (1) the length of the delay, (2) the government's justification for the delay, (3) whether the accused asserted his right to a speedy trial, and (4) prejudice to the accused caused by the delay. *Id.*
78. 889 S.W.2d at 623-24.
79. *Id.* at 625.

3. *El T. Mexican Restaurants, Inc. v. Bacon*[80]

Houston's First District Court of Appeals addressed the issues of corporate standing, capacity, and the right to sue in Texas courts in *El T.* The case centered around J. Roland Bacon, an insurance agent who incorporated his insurance business and became the sole shareholder of J. Roland Bacon, Inc. ("JRBI"). In 1981, El T. Mexican Restaurants, Inc. ("ET") entered into an agreement with JRBI for the purchase of insurance. As part of the agreement, JRBI paid for the insurance and billed ET. When ET failed to pay the amounts due, JRBI sued. During the litigation, an issue was raised regarding JRBI's corporate status.

In 1984, Bacon decided to cease doing business as a corporation and stopped paying corporate franchise taxes. As a result, the Texas Secretary of State forfeited JRBI's corporate charter. Bacon did not, however, dissolve the corporation. Bacon claimed that the cause of action accrued in 1983, when ET failed to pay its debt. He filed suit on behalf of JRBI in 1985. In 1990, Bacon amended his pleadings to delete JRBI and designate himself as successor in interest to the corporation's cause of action. ET sought a directed verdict at trial on the basis that Bacon had no right to recover on the corporation's claim. The motion was denied.

On appeal, ET asserted that Bacon had no right to recover as a shareholder on JRBI's cause of action and that JRBI's suit was void because it lacked the capacity to file suit.[81] Bacon argued that he was the successor in interest to JRBI which, if true, would give him standing to personally recover on the corporation's cause of action.[82] In an excellent analysis, the court explained that when a corporation forfeits its right to sue in Texas courts due to the failure to pay franchise taxes, the sole shareholder does not automatically become a successor in interest who may personally recover on the corporation's causes of action.[83] In reviewing JRBI's situation, the court noted that a corporation that fails to pay its franchise taxes loses the right—and capacity—to sue in Texas courts.[84] This lack of capacity, however, did not make JRBI's suit void. A lack of capacity must be challenged by a verified plea in abatement.[85] Although ET did not directly challenge JRBI's capacity, it had challenged Bacon's right to individually recover on JRBI's cause of action at trial.[86] This was construed by the appellate court as "a challenge to Bacon's standing as an individual shareholder of an incapacitated, but still existing, corporation."[87]

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80. 1995 Tex. App. LEXIS 5 (Tex. App.—Houston [1st Dist] Jan. 5, 1995, no writ) (not yet released for publication, subject to revision or withdrawal).

81. *Id.* at *3-*4.

82. *Id.* at *5-*6.

83. *Id.* at *6-*10.

84. *Id.* at *6-*8.

85. 1995 Tex. App. LEXIS 5 at *6.

86. *Id.* at *7-*8.

87. *Id.* at *8.

The court next recognized that when a corporation forfeits its privileges to sue in Texas courts, the title to its assets is bifurcated so that legal title remains with the corporation while beneficial title vests in the shareholders.[88] As the holder of beneficial title to JRBI's assets, Bacon was entitled to prosecute and defend JRBI's actions in Texas courts.[89] He did not have standing to sue in his own name, however, as the court explained: "Capacity to sue devolves upon the shareholders of a corporation when that corporation becomes incapacitated. Standing to sue, however, does not devolve upon the shareholders, and they must sue as representatives of the corporation, which still owns legal title to its cause of action."[90] In this situation, Bacon should have sued in JRBI's name on the corporate cause of action. After reviewing the stages of corporate decay, the court concluded that neither Bacon nor JRBI had the requisite combination of standing and capacity that was necessary to pursue the claim. Judgment was rendered that Bacon take nothing.[91]

The court provided a footnote on how Bacon could have successfully pursued the claim against ET. First, he could have paid the past-due franchise taxes, along with penalties and interest, and revived JRBI's charter and right to sue.[92] Second, he could have dissolved JRBI, taken title to its assets and liabilities, and maintained the action in his own name.[93] Finally, Bacon could have sued ET in a representative capacity on behalf of JRBI.[94] While the court's decision may seem harsh, it is clear that Texas courts have little sympathy for plaintiffs who fail to observe basic corporate formalities.

D. Conduct of Shareholder Meetings

In *ITC Cellular, Inc. v. Morris*,[95] the Texarkana Court of Appeals considered whether proper formalities were followed in the shareholder meetings of a closely held corporation. ITC Cellular, Inc. ("ITC") was founded by Walker Morris. Fifty-three percent of its outstanding shares were held by the Morris Children's Trust, of which Walker Morris served as trustee. Eighteen percent of the company was later acquired by Fred and David Neal. The Neals brought a stockholder derivative suit in 1990. As part of the settlement of the suit, the Neals obtained a proxy to vote the shares held by the trust. After they gained control of the trust shares, the Neals appointed themselves as corporate officers. In 1993, Morris attempted to revoke the proxy in favor of the Neals. Each faction called a shareholder's meeting at approximately the same time; the Neals set the annual meeting for January 8, 1994, and Morris scheduled a special meet-

88. *Id.* at *11.
89. *Id.*
90. 1995 Tex. App. LEXIS 5 at *11.
91. *Id.* at *20.
92. *Id.* at *19 n.10.
93. *Id.*
94. *Id.*
95. 909 S.W.2d 182 (Tex. App.—Texarkana 1995, no writ).

ing on January 13 for the purpose of electing directors. At the annual meeting, the Neals voted the trust shares and amended the bylaws to reduce the number of directors from two to one. Fred Neal was elected the sole director and president of ITC, and David Neal was appointed as corporate secretary.

The events of the special meeting on January 13 gave rise to the controversy in this case. When Dallas attorney Jon Sparling attempted to call the meeting to order, Charles Chapman, ITC's corporate counsel, objected. Chapman pointed out that Section 2.12 of ITC's bylaws required that the presiding official at a shareholder's meeting be either the corporate president or the person elected by a majority of the shares. After Sparling examined the proxy for the trust shares and determined that a quorum was present, he called a vote to determine who should preside. Chapman argued that no vote could be taken because the meeting had not been properly convened. At that point, Sparling nominated himself to preside over the meeting. Chapman and the Neals promptly walked out. Sparling proceeded to conduct the meeting, which resulted in the removal of the Neals and the election of Morris and his nominee to the board of directors. ITC sought a declaratory judgment to prohibit Morris and his nominee from holding themselves out as directors. Morris moved for summary judgment on the basis that he and his nominee were duly elected at a valid meeting. The trial court concluded that the meeting was valid and granted summary judgment for Morris.[96]

The Neals appealed the summary judgment. The Texarkana Court of Appeals compared the facts to those of *Duffy v. Loft*.[97] In *Duffy*, a corporate president refused to call a vote for the election of a presiding officer for the meeting, as provided in the bylaws. The shareholders elected someone other than the president to run the meeting. The Delaware Chancery Court held that the meeting was valid because the stockholders had no other choice than to act as they did. The Texarkana court held that in this case, because Fred Neal failed to take control of the meeting, it "was not fatal for someone else to temporarily conduct the meeting until a presiding officer could be elected."[98] The court noted that if Neal had sought to preside, he would have been entitled to do so unless someone else was elected. He could not, however, "thwart the will of the majority by refusing to allow an election of a new chairperson as provided for in the bylaws."[99] Because Neal failed to take charge of the meeting, the court found that the meeting had been properly convened.

The Neals also questioned whether a quorum was present when Morris and his nominee were elected to the board. The court cited Article 2.28 of the TBCA for the proposition that a quorum is present when a majority of the shares entitled to vote are represented at a meeting in person or

96. *Id.* at 184.
97. *See* Duffy v. Loft, 152 A. 849 (Del. 1930).
98. 909 S.W.2d at 185.
99. *Id.*

by proxy, and stated that a quorum attaches when the meeting commences.[100] Further, because both Article 2.28(A) of the TBCA and the ITC bylaws provide that a quorum is not affected by the withdrawal of shareholders after a meeting has begun, the court held that the quorum was not broken by the Neals' departure.[101] Finally, the Neals argued that a quorum is broken when shareholders have good cause to leave a meeting. The court recognized that if a shareholder is forced to leave a meeting or denied the right to participate, their withdrawal is not voluntary and a quorum can be broken.[102] The court found, however, that although the Neals were not satisfied with the number of shares they were allowed to vote, they left the meeting voluntarily. Their voluntary departure meant that the quorum was not broken. Therefore, the trial court's summary judgment was affirmed.[103]

III. LEGISLATIVE HIGHLIGHTS

During the 1995 legislative session, the Texas Business Law Foundation proposed House Bill 1425,[104] which contained numerous amendments to the Texas corporation, limited liability company, and partnership statutes. The bill was developed by the Corporation Law Committee of the State Bar Section of Business Law and was intended to update Texas business entity laws in order to make the state a more attractive jurisdiction for incorporation.[105] The bill was passed by the Texas House of Representatives and approved by the Economic Development Committee of the Texas Senate. Unfortunately, filibusters and a last-minute political squabble kept the bill from passing the Senate.[106] Due to the bill's noncontroversial nature, however, it is expected to pass during the early days of the 1997 legislative session. A summary of the bill's more significant provisions is included here as a preview and planning guide for business lawyers. Caution is encouraged, however, since there is no assurance that the bill will pass or that it will pass without modification.

One of most interesting features of the bill is its provision for a new form of corporate transaction known as a conversion. A conversion differs from a merger in that there is no combination or division of the corporation, but simply a change in organizational form with no interruption of the organization's existence.[107] The procedures to effect a conversion are similar to those required for a merger.[108] Because a conversion represents only an uninterrupted change in the form of the organization, it

100. *Id.*; *see also* TEX. BUS. CORP. ACT ANN. art. 2.28 (Vernon Supp. 1995).
101. *Id.*
102. *Id.* at 185-86.
103. 909 S.W.2d at 186.
104. Tex. H.B. 1425, 74th Leg., C.S. (1995).
105. HOUSE COMM. ON BUS. AND INDUSTRY, BILL ANALYSIS, Background, Tex. C.S.H.B. 1425, 74th Leg., R.S. (1995).
106. *Id.*
107. H.B. 1425 § 28.
108. *Id.*

cannot be used in lieu of a merger of two pre-existing operating entities.[109]

A new Part Thirteen is proposed for the TBCA which will impose special voting requirements for certain related-party transactions involving publicly-held Texas corporations and their shareholders.[110] This Part will prohibit self-dealing transactions between the corporation and shareholders holding more than twenty percent of its shares, for a period of three years after the shareholder acquired its interest, unless the transaction is approved by two-thirds of the remaining shareholders.[111] The prohibition will not apply if the board of directors approved the transaction before the shareholder acquired its interest or if the shareholder held its interest from a specified date through the date of the transaction.[112] Part Thirteen also includes a provision expressly permitting directors to "consider the long term interest of a corporation and its shareholders when considering actions that affect the interest of their corporations."[113]

If the bill passes in 1997, Part Two of the TBCA will be amended to include, among other things, a new Section 2.30-1 dealing with shareholder agreements. This section will permit the shareholders of a business corporation to modify, by agreement, governance provisions such as the board's discretion and powers, the means for authorizing and making distributions, and the terms of the directors and officers.[114] The section is based on a similar provision in the Revised Model Business Corporation Act.[115] Article 2.21, dealing with the personal liability of shareholders and subscribers, will be amended to provide that the affiliates of a shareholder or subscribers will enjoy the same statutory protection as the shareholder or subscriber.[116] Article 2.29 will be amended to provide that if a corporation holds shares of its own stock through a trust or otherwise, the corporation may vote those shares.[117] Article 2.31 will also be amended to permit a modification to the general rule that a corporation will be managed by its board of directors.[118]

If passed, the bill will amend Article 3.05 to delete the requirement that the $1,000 in consideration to be received by the corporation before it begins to transact business be in the form of money, labor done, or property received.[119] This change results from the elimination of the restriction in the Texas Constitution regarding the form of consideration to be received by Texas corporations prior to first transacting business.[120]

109. *Id.*
110. *Id.* § 39.
111. *Id.*
112. H.B. 1425 § 39.
113. *Id.*
114. *Id.* § 8.
115. *Id.* § 8.
116. *Id.* § 5.
117. H.B. 1425 § 7.
118. *Id.* § 9.
119. *Id.* § 17.
120. *Id.*

The change will also conform Article 3.05 to Article 2.16, which allows consideration consisting of any tangible or intangible benefit.[121] A similar conforming change will be made to Article 3.02A.[122] Finally, Article 5.14 will be amended to provide updated procedures for the disposition of stockholder derivative actions, including rules for the appointment, by a court, of a group of disinterested directors or other persons to consider issues raised in the derivative proceeding.[123] The derivative rules are based on similar provisions in the Revised Model Business Corporation Act.[124]

121. *Id.*
122. H.B. 1425 § 14.
123. *Id.* § 27.
124. *Id.*