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Professional Liability

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I. INTRODUCTION

During the Survey period, Texas courts issued important decisions in various professional liability actions. In the medical field, the Texas Supreme Court weighed in on the application of the Texas Civil Practice and Remedies Code to the Texas Medicaid Fraud Prevention Act, as well as the "analytical gap" inherent in expert opinions. In the legal malpractice context, the San Antonio Court of Appeals analyzed the effects of

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criminal proceedings on the tolling of legal malpractice claims. Finally, courts addressed a wide-ranging set of issues related to director and officer liability, including the imposition of a corporate default on an entity's former officer, the availability of entity protection for Texas Water Code liability, and the high evidentiary burden required to hold a parent company liable for the obligations of its subsidiary under the "alter ego" theory.

II. HEALTHCARE LIABILITY

In the past year, Texas courts addressed an array of novel issues including whether a Texas Medicaid Fraud Prevention Act (TMFPA) civil-remedy action is an action for recovery of damages subject to apportionment or a civil-penalty guided exclusively by the TMFPA's statutory penalty scheme, and whether an expert report sufficiently closes the "analytical gap" when it constitutes a "good faith effort" to comply with the statutory requirements and explains "how and why" the negligence caused the alleged injury.

A. Supreme Court of Texas Determines Proportionate Fault Scheme Does Not Apply to TMFPA Actions

On December 6, 2017, the Texas Supreme Court issued a well-reasoned opinion that changed, or at the very least qualified, a TMFPA defendant's ability to spread liabilities between other responsible parties via Texas's proportionate-responsibility statutes—namely Chapter 33 of the Texas Civil Practice and Remedies Code. The upshot—Section 36.052 of the TMFPA is a "civil penalty" and its mitigated-fault provision conflicts with the Civil Practice and Remedies Code's proportionate-responsibility statute. TMFPA defendants must pay the entire penalty as prescribed by the statute: no splitting.

In re Xerox Corporation and Xerox State HealthCare, LLC f/k/a/ ACS State HealthCare, Relators is a prime example of the Texas Supreme Court identifying jurisprudential principles and applying those principles with exactness. Justice Guzman's opinion is airtight. The supreme court was presented with the following controversy: Xerox Corporation, a third-party administrator of the Texas Medicaid program, defrauded the State of Texas, and by extension, citizens of the State, by (1) misrepresenting, concealing, and failing "to disclose that it was not processing orthodontic prior-authorization requests in accordance with Medicaid policy"; (2) failing to review evaluation documentation; and (3) failing to supervise otherwise unqualified clerical employees who "routinely 'rubber stamped' orthodontic prior-authorization requests."[1] The State sued Xerox under the TMFPA[2] and urged the trial court to award a civil rem-

1. *In re* Xerox Corp. and Xerox State HealthCare, LLC f/k/a/ ACS State HealthCare, Relators, 555 S.W.3d 518, 521 (Tex. 2018) (orig. proceeding).

2. Tex. Hum. Res. Code Ann. §§ 36.001–.132.

edy: (1) treble the amount of fraudulently procured Medicaid payments; (2) civil penalties of not less than $5,500 per unlawful act; (3) interest on the payments; and (4) expenses and attorneys' fees.[3] Xerox urged the trial court to consolidate its TMFPA actions with TMFPA actions arising from the same set of operative facts and to shift liability proportionately between all culpable parties.[4] The trial court refused[5] and the Austin Court of Appeals denied mandamus relief.[6] Xerox filed its mandamus petition on the issue of whether Chapter 33's proportionate-responsibility scheme encompasses a civil-remedy action under the TMFPA.[7]

The supreme court immediately understood the issue on appeal as one of statutory interpretation and legislative intent.[8] As such, the supreme court's analysis departed from, journeyed through, and arrived at the same destination—the text of Chapter 33 and TMFPA Section 36. Chapter 33 applies to Deceptive Trade Practices Act (DTPA) actions, statutory torts,[9] "any cause of action based on tort," and "any other conduct" violative of applicable legal standards.[10] Notably, TMFPA actions are not expressly addressed in Chapter 33.

The parties' arguments could not have been less similar in their approach and conclusion. Xerox urged the supreme court to treat the TMFPA as a statutory tort based on fraud for the recovery of damages, therefore rightly and necessarily applying Chapter 33 "to prevent the State from seeking damages for the same injury from multiple tortfeasors."[11] It asked the supreme court to analyze each component part of TMFPA Section 36.052(a) and to find that the provisions award civil damages rather than civil penalties.[12]

The State insisted the supreme court treat the TMFPA as a civil-enforcement statute for civil penalties, where separate violations of the statute necessarily produce separate injuries that cannot and should not be allocated between multiple violators.[13] Under this logic, the State contended the supreme court need not look for an express exemption in Chapter 33 because the comparative fault statute is inapplicable by its own terms—the violations are not unitary.[14] In the alternative, the State

3. *In re Xerox Corp.*, 555 S.W.3d at 521.
4. *Id.*
5. *Id.* at 521–22.
6. *In re* Xerox Corp., 550 S.W.3d 640, 642 (Tex. App.—Austin 2016) (orig. proceeding) (mem. op.), *mand. granted*, 555 S.W.3d 518 (Tex. 2018).
7. *In re Xerox Corp.*, 555 S.W.3d at 522.
8. *Id.*
9. *See* Dugger v. Arredondo, 408 S.W.3d 825, 827 (Tex. 2013); Sw. Bank v. Info. Support Concepts, Inc., 149 S.W.3d 104, 110–11 (Tex. 2004) (holding the proportionate-responsibility statute is inapplicable to conversion claims under Article 3 of the Uniform Commercial Code, which adopts its own comparative-responsibility scheme that is comprehensive, uniform with other jurisdictions, and more specific than Chapter 33).
10. TEX. CIV. PRAC. & REM. CODE ANN. § 33.002(a)(1).
11. *In re Xerox Corp.*, 555 S.W.3d at 524.
12. *Id.* at 526.
13. *Id.* at 524.
14. *Id.*

asked the supreme court to recognize the conflict between the TMFPA and Chapter 33, particularly the statutes' methods of punishment and reward and their differing "carrot-and-stick" regimes.[15] In any event, the State asked the supreme court to analyze TMFPA Section 36.052(a) in the aggregate, finding that the provision awards civil penalties rather than civil damages.[16]

As a matter of background, Section 36.052(a) is comprised of four component damages provisions. A person who violates the TMFPA is liable to the state for: (1) the amount of any payment or benefit provided under the Medicaid program as a result of the unlawful act; (2) interest on the amount of the payment or benefit; (3) a "civil penalty of . . . not less than $5,500 . . . and [up to $15,000 depending on the circumstances] for each unlawful act . . .; "and (4) two times the amount of the payment or value of the benefit."[17]

Diving into the issue, the supreme court first concluded that the "civil remedy in [S]ection 36.052(a) is undeniably punitive in the aggregate, imposing monetary liability far surpassing the amount of Medicaid funds the State may have actually expended due to an unlawful act."[18] Still, the supreme court accepted Xerox's challenge of analyzing Section 36.052(a) piecemeal—in "elemental fashion."[19] First, the supreme court juxtaposed the legislature's reference to Section 36.052 as a "civil remedy" to the more commonly used, "damages," concluding that the legislature's peculiar designation proves it did not intend Section 36 to operate as a typical damages provision.[20] Interestingly, however, the supreme court later seemed to recant its reliance on labels, proclaiming, "[t]he use or absence of labels may suggest legislative intent, but labels are not dispositive of underlying character."[21]

The supreme court laid the predicate for the balance of its opinion by distinguishing between "damages" and "penalties." "Damages" were determined to be "[m]oney claimed by, or ordered to be paid to, a person as compensation for loss or injury."[22] A "penalty," on the other hand, was determined to be a "'[p]unishment imposed on a wrongdoer,' especially, 'a sum of money exacted as punishment for either a wrong to the state or a civil wrong (as distinguished from compensation for an injured party's loss).'"[23] The supreme court paid specific attention to its prior holdings

15. *Id.* at 536.
16. *Id.* at 526.
17. TEX. HUM. RES. CODE ANN. § 36.052(a)(1)–(4).
18. *In re Xerox Corp.*, 555 S.W.3d at 527 ("The very idea of treble damages reveals an intent to punish past, and to deter future, unlawful conduct, not to ameliorate the liability of wrongdoers."); *see* Vt. Agency of Nat. Res. v. Stevens, 529 U.S. 765, 784 (2000) (describing the civil-penalty and treble-damages remedy in the federal False Claims Act as "essentially punitive in nature").
19. *In re Xerox Corp.*, 555 S.W.3d at 527.
20. *Id.* at 527–28.
21. *Id.* at 529.
22. *Id.* (quoting *Damages*, BLACK'S LAW DICTIONARY (10th ed. 2014)).
23. *Id.* at 530 (quoting *Penalty*, BLACK'S LAW DICTIONARY (10th ed. 2014) (citation omitted)).

concerning compensatory schemes and whether or not a penalty could ever be, in part, compensatory.[24] The supreme court determined that, based on a long line of case law, penalties could have "compensatory traits."[25]

Having distinguished between "damages" and "penalties," the supreme court addressed Section 36, subsection by subsection, reasoning whether any of the component subsections transformed Section 36 from a "penalties" provision to a damages "provision" subject to the machinations of Chapter 33's proportionate-responsibility scheme. The supreme court immediately determined that subsections 36.052(a)(2) [interest on the payment or benefit] and (a)(3) [civil penalty of . . . not less than $5,500] were undoubtedly penalties. Section 36's interest provision, (a)(2), was found to be in conflict with common law and alternative statutory interpretations of interest, which normally state that "interest . . . begins to accrue on the earlier of 180 days after the date a defendant receives written notice of a claim or the date suit is filed."[26] Here, the so called "interest as interest" accrues as allowed by statute—"at the prejudgment interest rate in effect on the day the payment or benefit was received or paid [accruing from that day until] the state recovers the amount of the payment or value of the benefit."[27] Therefore, the supreme court determined that (a)(2) had "no significance to the present inquiry independent of the characterization of the principle amount in (a)(1)," addressed later in the opinion.[28] It did not operate as an independent damages provision or transform Section 36 into a damages provision. And, the supreme court determined subsection (a)(3) to be a penalty provision on its face—employing the term of art, "civil penalty."[29]

Subsections (a)(1) and (a)(4) proved more difficult to categorize. The supreme court determined subsection (a)(4) was properly characterized as a penalty provision despite Xerox's insistence that the payment multiplier functioned as a liquidated damages provision.[30] It rejected Xerox's argument, reasoning that liquidated damages provisions are necessarily penalties, "unless (1) the harm caused by the breach is incapable or difficult of estimation and (2) the amount of liquidated damages is a reasonable forecast of just compensation."[31] Here, subsection (a)(4) was found to be "tethered" to actual damages and therefore fails "because it (1) assumes actual damages can and will be determined and (2) instead of attempting to forecast actual damages, it calls for them to be determined and multiplied."[32] Because (a)(4) was fixed to the penalty assessed in

24. *Id.*
25. *Id.* (citing Cavnar v. Quality Control Parking, Inc., 696 S.W.2d 549, 551–52 (Tex. 1985)).
26. *Id.* at 532.
27. *Id.*; TEX. HUM. RES. CODE ANN. § 36.052(a)(2).
28. *In re Xerox Corp.*, 555 S.W.3d at 532.
29. *Id.* at 529; TEX. HUM. RES. CODE ANN. § 36.052(a)(3).
30. *In re Xerox Corp.*, 555 S.W.3d at 532.
31. *Id.* at 533.
32. *Id.*

(a)(1), it was necessarily a penalty itself.[33]

Subsection (a)(1), the crux of the entire debate, proved most difficult for the supreme court to categorize. The supreme court's first and decidedly best argument was that because subsection (a)(1) assesses the amount of payment based on *either* the amount of harm done *or* the amount of benefit received, the remedy is clearly "unrelated to actual loss" and therefore a penalty.[34] Still, the subsection does not use terms like "harm," "damages," "overpayment," "loss," "actual damages," "unauthorized amount," "compensation," or any other words implying a loss measurement.[35] No matter the type of fraud or the damage caused, the remedy in Section 36.052(a) "is always fixed at the payment amount."[36] The supreme court commented that, "Subsection (a)(1) reflects a deliberate shift away from actual loss to the fact of disbursement, obviating the need for the government to prove actual damages unless doing so is required to prove an unlawful act."[37] Because TMFPA Section 36 was found to be a penalty provision both when considered in its totality and when considered in its component subsections, Chapter 33 was deemed inapplicable because it was patently not "an action to recover damages."[38]

However, just to be sure, the supreme court also opined on Chapter 33's "irreconcilable tension" with the TMFPA.[39] This conflict arises from the TMFPA's "carrot-and-stick approach" which is "designed to root out fraud in the system by rewarding those who report unlawful activities and severely punishing those who do not."[40] The carrot-and-stick approach was found to operate to the exclusion of any other statutory reduction or elimination of liability.[41] The only way to limit liability under the TMFPA is by "prompt disclosure."[42] As such, the supreme court held that "[t]he TMFPA's strong public policy of encouraging insiders and whistleblowers to come forward cannot be squared with the powerful disincentive that would ensue if a contribution counterclaim were permitted."[43]

The Texas Supreme Court's *In re Xerox Corp.* decision is significant because it forecloses any TMFPA defendant's ability to shift liability to other responsible parties. If you are alleged to have defrauded the State under the TMFPA, you can expect to be penalized in the amount of the actual payment disbursed or benefit received, interest on the amount of the payment or benefit, a civil penalty between $5,500 and $15,000 for

33. *Id.*
34. *Id.* (citing Flores v. Millennium Interests, Ltd., 185 S.W.3d 427, 434 (Tex. 2005)).
35. *Id.*
36. *Id.* at 534.
37. *Id.*
38. *Id.* at 535.
39. *Id.*
40. *Id.* at 536.
41. *Id.*
42. *Id.*
43. *Id.* at 538.

each unlawful act, and two times the amount of the payment or value of the benefit. The supreme court's holdings give the TMFPA more bite.

B. Texas Supreme Court Bridges the "Analytical Gap" Inherent in Expert Opinions on Causation

In previous years, this Survey has documented the ongoing efforts of Texas courts to clarify compliance with standards set out in the Texas Medical Liability Act (TMLA), codified as Texas Civil Practice and Remedies Code Chapter 74. The TMLA requires plaintiffs asserting a "health care liability claim" (HCLC) to serve each defendant with an expert report within 120 days after the defendant's original answer or risk dismissal of the case with prejudice.[44] The report must include "a fair summary of the expert's opinions as of the date of the report regarding applicable standards of care . . . and the causal relationship between" the asserted failure to meet the standard of care and the claimed injury.[45] Last year's Survey concluded that disagreements and confusion, specifically with regards to what courts find to be acceptable causation evidence in the expert reports, would lead to less than mechanical results in the future. This hypothesis proved true in 2018, and in exemplary fashion, in the case of *Abshire v. Christus Health Southeast Texas*.[46]

Sue Abshire, reporting chest and back pains, checked into the emergency room of Christus Hospital-St. Elizabeth (Christus) on November 19, 2012.[47] Following two EKGs, which produced standard results, Abshire was discharged and directed to follow up with a cardiologist.[48] However, "[n]o spinal evaluation was conducted" and, consequently, Christus staff did not record that Abshire "suffered from osteogenesis imperfecta (OI)—commonly known as brittle bone disease" in Abshire's medical history.[49]

Abshire was not away from Christus long, returning just two days later with chest pain and difficulty breathing.[50] Her OI was noted this time, but the hospital immediately discharged her after a simple chest x-ray.[51] Abshire would return to the emergency room several times. A day later, she entered with chest, shoulder, neck, and back pains. Again, her OI was noted and she was sent away "with a diagnosis of constipation, musculoskeletal pain, and pleurisy."[52] A few days later, Abshire entered via ambulance for back and chest pain and shortness of breath—her OI was *not* documented, but an additional x-ray showed degenerative changes to both her spine and her shoulders. Later, a physician noted probable bone

44. Tex. Civ. Prac. & Rem. Code Ann. § 74.351(a), (b)(2).
45. *Id.* § 74.351(a), (r)(6).
46. 563 S.W.3d 219, 221 (Tex. 2018) (per curiam).
47. *Id.*
48. *Id.*
49. *Id.*
50. *Id.*
51. *Id.*
52. *Id.*

necrosis but eventually discharged her.[53]

The day after this discharge, Abshire returned to the Christus emergency room for the fifth time with weakness in her legs and difficulty walking.[54] She was transferred to a rehabilitation hospital where she was put on a physical therapy plan.[55] Her rehab physician documented her OI and planned to have an MRI performed, but Abshire was sent to Christus for additional review after her symptoms failed to improve.[56] When Christus attempted to send Abshire back to rehab, the rehab clinic intervened and had Abshire sent to Baptist Beaumont where an MRI was ordered. The results revealed a compression fracture of Abshire's T-5 vertebrae, an injury which ultimately rendered her a paraplegic and incontinent.[57]

Abshire sued for negligence. In the opinion at issue, the courts addressed a claim against the Christus nurses for failing to "recognize the signs and symptoms of a spinal compression fracture resulting in a delay in treatment which caused [her] paraplegia and missed the history of [OI] that predisposes one to fractures."[58] Abshire included an expert report in which a board-certified physician in internal medicine, geriatrics, and rheumatology stated that if Christus had "followed the Standard of Care for patients with OI, Ms. Abshire in medical probability would not have developed paraplegia and bowel and bladder incontinence."[59]

Christus challenged the report in several ways, objecting that the report did not adequately set out "the applicable standards of care, the manner in which Christus breached the standards, and the causal link between Christus's conduct and Abshire's injuries."[60] Christus filed a motion to dismiss stating that the report was deficient in showing either the hospital's responsibility for the breach through its nurses or adequately demonstrating causation.[61] The trial court gave Abshire thirty days to address the deficiencies, prompting her to file a supplementary report and an additional report "discussing the standard of care and breach by Christus's nursing staff."[62] The trial court found the supplemental reports to be a "good faith effort to comply with the statutory requirements" and denied the motion to dismiss.[63]

The Beaumont Court of Appeals reversed and dismissed the claims, finding that the reports suffered from an "analytical gap" because they did not demonstrate how the nurses' failure to document Abshire's OI

53. *Id.* (emphasis added).
54. *Id.* at 222.
55. *Id.*
56. *Id.*
57. *Id.*
58. *Id.*
59. *Id.*
60. *Id.*
61. *Id.*
62. *Id.* at 223.
63. *Id.*

caused her paraplegia.[64] However, the Texas Supreme Court reversed and found "the report sufficiently addresse[d] both causation and the standard of care."[65]

The supreme court called attention to the requirement referenced by the trial court that it "need only find that the report constitute a good faith effort to comply with the statutory requirements."[66] The supreme court then took on the central issue of causation, asking whether the report "explain[ed] 'how and why' the alleged negligence caused the injury."[67] The supreme court cited multiple paragraphs from the report, highlighting the nurses' failure to document the OI and stated that if the nurses had "linked [her symptoms] to the [OI] diagnosis then [Abshire] could have been admitted . . . on absolute bed rest," had scans ordered, and had "treatment started to preserve[ ] the integrity of her spine" and that failure to do so "allowed the injury to progress to . . . paraplegia."[68] Though somewhat couched in terms of what *could* have happened, the supreme court found this to be a "straightforward link between the nurses' alleged breach of the standard of care and Abshire's spinal injury."[69]

The supreme court's characterization of the link as "straightforward" is interesting, because the court of appeals deemed the report conclusory. The court of appeals reasoned that when Abshire's OI *was* noted, the physicians did not order tests or provide spinal treatment, and thus the opinion that failing to chart her OI led to the injury was built on an analytical gap. The supreme court was critical of this analysis, stating that "it appears the court of appeals simply did not agree with [the expert's] conclusions."[70] This is, one could argue, a rather ungenerous reading of the appellate decision. All "analytical gaps" concern, to a certain degree, the believability of a conclusion; whether it is possible at all that one item can lead to the next. Though the supreme court found that the court of appeals' analysis veered too close to actual weighing the credibility of the report,[71] the supreme court did not merely state that it is not the job of the court to determine if there is an analytical gap in the report's analysis. Instead, the supreme court affirmatively stated that it did not believe such an analytical gap existed.[72] Without setting out a guiding principle or rule, one could argue that finding that no analytical gap existed also weighed the credibility of the expert report. The supreme court leaves trial and appellate courts with the mandate to determine whether there are analytical gaps, but not to weigh credibility—a difference, perhaps, without a true distinction.

64. *Id.*
65. *Id.*
66. *Id.* (citing TEX. CIV. PRAC. & REM. CODE ANN. § 74.351(l)).
67. *See id.* at 224.
68. *Id.* at 224–25
69. *Id.* at 225.
70. *Id.* at 226.
71. *Id.*
72. *Id.* at 225.

The supreme court also addressed whether the report identified the standard of care, despite the court of appeals failing to consider arguments on the issue.[73] The supreme court cited the nurses' omission exactly as described in the report.[74] The supreme court found it sufficient to describe the standard of care as requiring full and accurate documentation of Abshire's medical history even without a complete articulation of what this documentation procedure should entail.[75] Though not as contentious of an issue, this auxiliary issue underscores that much of the analysis relies on a less-than-mechanical determination of which arguments and statements are too conclusory and which are sufficient on their face.

III. LEGAL MALPRACTICE

Unlike 2017 and previous years, the Texas Supreme Court has been silent on issues related to legal malpractice. It failed to issue a single opinion analyzing the legal standards of a professional negligence claim in 2018. Yet, the courts of appeals in Texas were fairly busy with legal malpractice cases, adjudicating almost fifty claims against attorneys, most of which focused on the nuances of summary-judgment motions.[76] Undoubtedly, there is a sea of sufficiency-of-the-evidence claims stemming from those motions for summary judgment analyzed by the Texas courts of appeal, but, as a practical matter, cases are not the most helpful because their analysis is almost entirely fact-dependent.

As such, this section of the article will solely focus on one not-so-common legal malpractice case where the San Antonio Court of Appeals branched out from the sea of run-of-the-mill summary judgment appeals and resolved one of the more "unique" legal malpractice cases. More specifically, the court of appeals delved into the facts of a case involving the complex maze of tolling the limitations period for a legal malpractice cause of action amidst a criminal conviction. This case is important to the legal-malpractice jurisprudence because it focuses on issues that seem straight-forward but are actually quite nuanced. The case is *Skelton v. Gray*.[77]

In *Skelton*, the San Antonio Court of Appeals closely analyzed the effects of criminal proceedings on the tolling of legal malpractice claims. Skelton, the plaintiff, was an attorney who was "charged with forging the will of her deceased client."[78] Skelton drafted a will for her client, Ysidro Canales, in her office, but the original remained in Canales's possession until his death.[79] After Canales died, "the original will could not be lo-

73. *See id.*
74. *See id.* at 227.
75. *See id.*
76. *See, e.g.*, Renda v. Erikson, 547 S.W.3d 901, 908 (Tex. App.—Amarillo 2018, pet. granted).
77. 547 S.W.3d 272 (Tex. App.—San Antonio 2018, pet. granted).
78. *Id.* at 274.
79. *Id.*

cated," and Skelton took matters into her own hands.[80] Skelton printed a clean copy of the original will (the executed version was water damaged), cut the signatures from the water-damaged copy, and pasted the signatures onto the clean printed copy.[81] Skelton's secretary informed the authorities in 2003, and in late 2004, Skelton was charged with forgery.[82]

Skelton's forgery case went to trial in 2007, during which she was represented by Guy James Gray.[83] Ultimately, Skelton was convicted of forgery and was sentenced to a suspended one-year term of imprisonment and two years of community supervision.[84] After the conviction, Gray's representation of Skelton ended and Skelton hired new counsel to represent her during the appeals process.[85] On direct appeal through her new counsel, Skelton argued that Gray's representation was ineffective and that the jury charge improperly allowed conviction for a theory not included in the indictment.[86] The San Antonio Court of Appeals affirmed the conviction in 2010.[87]

During the pendency of the direct appeal, a civil trial was held on the will contest brought by Canales's family members.[88] The jury determined that "Skelton did not act with the intent to defraud or harm another when she physically altered the will," and the trial court "order[ed] that the will contestants take nothing."[89] Thereafter, on September 26, 2011, Skelton sought a writ of habeas corpus from the San Antonio Court of Appeals, claiming, *inter alia*, that (1) Gray rendered her ineffective assistance of counsel and (2) she was actually innocent based on the conflicting verdicts between the criminal and will contest trials.[90] The court of appeals granted Skelton habeas relief as to her ineffective assistance assertions, vacating the judgment of the criminal court, and remanding the case for a new trial.[91] However, instead of retrying the case, the State ultimately dismissed Skelton's forgery charge on February 6, 2015.[92]

Then, "[o]n May 27, 2016, Skelton filed suit against Gray for legal malpractice and breach of fiduciary duty."[93] "In response, Gray filed a Rule 91a motion to dismiss" on two bases: (1) "Skelton's legal malpractice claim was 'barred by the *Peeler*[94] doctrine because she ha[d] not been exonerated from the underlying [forgery charge]'"; and (2) "the statute

80. *Id.*
81. *Id.*
82. *Id.*
83. *Id.*
84. *Id.*
85. *Id.*
86. *Id.*
87. *Id.*; *see* Skelton v. State, No. 04-08-00720-CR, 2010 WL 2298859 (Tex. App.—San Antonio June 9, 2010, pet. ref'd) (mem. op., not designated for publication).
88. *Skelton*, 547 S.W.3d at 274.
89. *Id.*
90. *Id.*
91. *Id.*
92. *Id.*
93. *Id.*
94. 909 S.W.2d 494 (Tex. 1995).

of limitations barred her claims."[95] The trial court dismissed Skelton's claims, "finding the legal malpractice claim failed for lack of exoneration and the breach of fiduciary duty claim was barred by limitations." Skelton appealed, introducing the following issues: (1) whether Skelton can sue Gray, given the habeas determination and the State's dismissal of Skelton's charges; (2) whether the *Hughes*[96] tolling rule permits Skelton to sue within two years of being exonerated; and (3) whether the *Hughes* tolling rule applies when fiduciary duty and tolled malpractice claims are intertwined.[97]

To prove legal malpractice, a plaintiff must show: "(1) the attorney owed the plaintiff a duty, (2) the attorney breached that duty, (3) the breach proximately caused the plaintiff's injuries, and (4) damages occurred."[98] In *Peeler*, the Texas Supreme Court "considered whether a convict can sue her criminal defense attorney for legal malpractice."[99] The supreme court held that generally, because defendants' own actions are "the sole cause of any damages flowing from [their] indictment and conviction," they likely cannot establish the proximate cause requirement of a legal malpractice claim.[100] Yet, if the convict has been exonerated—or, in other words, the criminal conviction has been overturned—then and only then can the plaintiff who has been convicted of a criminal offense establish the causation necessary to establish a legal malpractice claim.[101]

On appeal, Skelton argued that *Peeler* was distinguishable and did not apply to her factual circumstances. More specifically, Skelton argued that the *Peeler* doctrine only applied to convicted criminals and, because her forgery conviction was dismissed, *Peeler* was inapplicable.[102] Further, Skelton argued that because she was "effectively exonerated"—by the State's dismissal of her conviction and the jury's finding that she did not act with intent to defraud or harm—the *Peeler* analysis did not apply to her.[103]

The San Antonio Court of Appeals agreed. In a short, ten-sentence analysis, the court of appeals distinguished *Peeler* from Skelton's circumstances. It held that, at the time Peeler sued her attorney for malpractice, her conviction was still intact.[104] To the contrary, Skelton's conviction was dismissed by the underlying court *and then* she sued her attorney for malpractice.[105] Therefore, at the time that Skelton's legal malpractice suit

95. *Skelton*, 547 S.W.3d at 274–75.
96. 821 S.W.2d 154, 157 (Tex. 1991).
97. *Skelton*, 547 S.W.3d at 275.
98. *Id.* at 276 (citing Joe v. Two Thirty Nine Joint Venture, 145 S.W.3d 150, 159 (Tex. 2004)).
99. *Id.* (citing *Peeler*, 909 S.W.2d at 497–98).
100. *Id.* (citing *Peeler*, 909 S.W.2d at 497–98).
101. *Id.*
102. *Id.*
103. *Id.*
104. *Id.*
105. *Id.* at 276–77.

was filed, she was not a plaintiff convicted of a criminal offense as required under *Peeler*.[106] Consequently, the court of appeals held that "the trial court erred in applying the *Peeler* doctrine to the facts" and should not have dismissed her legal malpractice claim.[107]

In turn, the court of appeals discussed the statute-of-limitations arguments related to both the legal malpractice and the breach of fiduciary duty claims. First, it discussed the *Hughes* tolling rule as applied to the two-year statute of limitations for Skelton's legal malpractice tort claim. In effect, the Texas Supreme Court established a tolling rule in *Hughes* for legal malpractice statutes of limitations for scenarios "when an attorney commits malpractice in the prosecution or defense of a claim that results in litigation."[108] In those cases, "the statute of limitations . . . is tolled until all appeals on the underlying claim are exhausted."[109] More importantly, the *Hughes* rule applies even where, as here, the attorney's representation ends after the negligent act occurs but before the litigation ends.[110]

The date upon which a claim accrues is particularly important in legal malpractice cases, especially when tolling is at issue. "A legal malpractice claim accrues when the client sustains a legal injury or, in cases governed by the discovery rule, when the client discovers, or should have discovered through the exercise of reasonable care and diligence, the facts establishing the elements of the claim."[111] Regarding the accrual date in this case, there are several key dates:

(1) December 13, 2007: Jury verdict on fraud charge; Gray's representation concluded
(2) March 25, 2011: Court of Criminal Appeals issued mandate denying Skelton's petition for discretionary review
(3) September 26, 2011: Skelton filed application for writ of habeas corpus
(4) November 6, 2014: Fourth Court of Appeals issued mandate in habeas proceeding
(5) February 6, 2015: forgery charge dismissed by State
(6) May 27, 2016: Skelton filed suit against Gray[112]

Based on these dates, Gray contended that Skelton's legal malpractice claim accrued on March 25, 2011, the date upon which the mandate was issued denying Skelton's petition for discretionary review,[113] arguing "that in a criminal case, the end of a direct appeal ends the tolling of the

106. *Id.*
107. *Id.* at 277.
108. *Id.* (quoting Hughes v. Mahaney & Higgins, 821 S.W.2d 154, 157 (Tex. 1991)).
109. *Id.* (quoting *Hughes*, 821 S.W.2d at 157 (citation omitted)).
110. Apex Towing Co. v. Tolin, 41 S.W.3d 118, 121–22 (Tex. 2001).
111. *Skelton*, 547 S.W.3d at 277 (citing TEX. CIV. PRAC. & REM. CODE ANN. § 16.003); *see* S.V. v. R.V., 933 S.W.2d 1, 4 (Tex. 1996) (legal injury rule); Willis v Maverick, 760 S.W.2d 642, 646 (Tex. 1988) (discovery rule).
112. *Skelton*, 547 S.W.3d at 277.
113. *Id.* at 278.

statute of limitations for malpractice claims related to the underlying representation."[114] Skelton disagreed, reasoning that the malpractice claim did not accrue until either (1) the court issued its mandate in the habeas proceeding on November 6, 2014; or (2) Skelton's charges were dismissed on February 6, 2015, as Skelton sued Gray within two years of either date.[115] These arguments were based on an additional reference date crafted by the court in *Apex Towing*, which is the date "when litigation is 'otherwise finally concluded.'"[116] In Skelton's opinion, "a habeas corpus application 'relates to and flows from the original conviction,'"[117] and as such, the conclusion of litigation is only marked by the final order in a habeas corpus proceeding.[118]

Additionally—"from a public policy perspective"—Skelton asserted that limitations could not begin to "accrue on a legal malpractice claim . . . until after the [criminal defense] attorney's former client has had a reasonable opportunity to seek habeas corpus relief to challenge the conviction."[119] Otherwise, she would never "[have] the opportunity to obtain exoneration."[120]

The court of appeals agreed with Skelton. In short, the court of appeals relied on public policy and on the fact that, given the strict requirements of the *Peeler* doctrine, Skelton could not have ever sued Gray for malpractice if she did not first contest the criminal conviction via the habeas corpus proceeding.[121] Ultimately, the case was remanded to the trial court for further proceedings because the court of appeals held that Skelton's legal malpractice claim was timely, as it was filed within two years of November 6, 2014, the date on which the habeas corpus proceeding was completed and served to overturn her conviction.[122]

Skelton is important to the field of legal malpractice because of its thorough analysis of the intricacies and potential missteps of tolling laws related to malpractice claims arising from criminal convictions.

IV. DIRECTOR AND OFFICER LIABILITY

During the Survey period, Texas courts addressed two novel issues. The first dealt with whether a default judgment imposed against an entity may bind that entity's answering corporate officer in the same suit. The second focused on whether a member of a limited liability company may be held personally liable for a violation of the Texas Water Code even where the member purportedly acts as an agent of the entity. Additionally, during

114. *Id.*
115. *Id.*
116. *Id.* (quoting *Apex Towing*, 41 S.W.3d at 119).
117. *Id.* (quoting Falby v. Percely, No. 09-04-422 CV, 2005 WL 1038776, at *2 (Tex. App.—Beaumont May 5, 2005, no pet.) (mem. op.)).
118. *Id.*
119. *Id.*
120. *Id.*
121. *Id.* ("Had she tried to sue him any sooner, her claim would have been barred by *Peeler*.").
122. *Id.* at 279–80.

the Survey period, one appellate court provided further guidance on the degree of evidence that must be demonstrated in order to pierce the corporate veil under an alter ego theory.

A. The Dallas Court of Appeals Rejects the Imposition of a Corporate Default on the Entity's Former President

On November 27, 2018, the Dallas Court of Appeals was tasked with determining whether a default entered against a corporation may be used as summary judgment evidence against the directors and officers of that entity.[123] In *Christian v. Venefits, LLC*, the court of appeals answered this question in the negative where the director or officer has individually answered and has no authority to cause the entity to answer the suit.

The factual setting begins with a stock purchase agreement whereby Venefits, LLC (Venefits) was to acquire a fifty-one percent interest in VIPCO Advisors, Inc. (VIPCO), an entity whose principal business involved the underwriting of insurance policies.[124] Subsequent to the stock purchase, Mack Christian continued to serve as president of VIPCO and maintained his twenty-one to twenty-two percent ownership interest.[125] For the two months following the close of the stock purchase, Venefits made monthly payments pursuant to its terms.[126] However, three months after the closing date, Venefits discovered that VIPCO failed to file a franchise tax report due the month before the closing, the consequence being that VIPCO forfeited its right to transact business in Texas.[127]

Seeking redress for VIPCO's forfeiture to transact business, Venefits filed suit against VIPCO, Christian, and multiple officers of VIPCO, alleging breach of fiduciary duty, breach of contract, and fraud.[128] Venefits specifically alleged that "VIPCO was a forfeited Texas corporation as defined by [S]ection 171.2515 of the tax code and the named officers/directors, including Christian, were liable for its debts under [S]ection 171.255."[129] Significantly, according to Chapter 171 of the Tax Code, if a corporation's right to transact business is forfeited for its failure to file an annual report, the corporation is "denied the right to sue or defend in a court of this State, and each director or officer . . . is liable for a debt of the corporation."[130]

While multiple defendants were named in the suit, Christian was the only defendant to file an answer.[131] Following the filing of his general denial and affirmative defenses, Christian moved for summary judgment

123. Christian v. Venefits, LLC, No. 05-17-01218-CV, 2018 WL 6187612 (Tex. Civ. App.—Dallas Nov. 27, 2018) (mem. op.).
124. *Id.* at *1.
125. *Id.*
126. *Id.*
127. *Id.*
128. *Id.*
129. *Id.*
130. *Id.* (citing Tex. Tax Code Ann. §§ 171.252, 171.255).
131. *See Venefits*, 2018 WL 6187612, at *1.

on each of Venefits' claims.[132] The trial court granted Christian's motion on two of the claims, leaving only Venefits' breach of contract claim for resolution.[133]

Following the trial court's partial grant of Christian's summary judgment, Venefits filed a motion for default judgment on its fraud and breach of contract claims against the defendants that had not answered the original suit.[134] The trial court granted Venefits' motion for default judgment against VIPCO and its non-answering officers and directors, and rendered a final judgment rescinding the stock purchase agreement.[135]

Now left with the trial court's entry of default against VIPCO, Venefits moved for summary judgment on its remaining breach of contract claim against Christian.[136] Its theory in support of its motion was that "the [trial court] ha[d] already established the existence of a breach [of contract] by VIPCO Advisors Inc., and [ ] Christian, as an owner and the President of VIPCO, [was] not entitled to the protection of a corporation because no corporation existed at the time of the breach," due to the forfeiture.[137]

While Christian made numerous arguments in opposition to Venefits' motion for summary judgment, most important was Christian's argument that because Venefits ceased to pay VIPCO pursuant to the stock purchase agreement, it was Venefits, rather than VIPCO, who was in breach of the stock purchase agreement.[138] Accordingly, "Christian argued the default judgment rendered against VIPCO did not preclude him from contending that VIPCO did not breach the stock purchase agreement."[139] He further noted that because Section 171.255 of the Tax Code:

> provides that a director or officer's liability is determined "in the same manner and to the same extent as if the director or officer were a partner and the corporation were a partnership," he should be permitted to contend and offer evidence that VIPCO did not breach the contract and that no debt was created or incurred for purposes of [S]ection 171.255.[140]

Nevertheless, the trial court granted the motion for summary judgment against Christian, reasoning that Christian's defense amounted to "an 'argument to essentially disregard' [S]ection 171.255 and 'apply general

132. *See id.*
133. *See id.*
134. *Id.* at *2.
135. *Id.*
136. *Id.*
137. *Id.* ("Attached to the motion was Christian's deposition establishing he was president of VIPCO at the time the stock purchase agreement was entered; affidavits by [an officer of VIPCO] attaching Christian's third-party petition and the stock purchase agreement; an affidavit by . . . the registered agent for VIPCO, attaching the state comptroller's notice of forfeiture to VIPCO; and the trial court's default judgment rescinding the stock purchase agreement and awarding damages to Venefits.").
138. *Id.* at *3.
139. *Id.*
140. *Id.* (quoting TEX. TAX CODE ANN. § 171.255(b)).

partnership law.'"[141]

Appealing the trial court's grant of summary judgment in favor of Venefits, "Christian argue[d] the trial court erred in concluding he is personally liable under Section 171.255 of the tax code for the default judgment Venefits obtained against VIPCO."[142] Thus, the issue presented to the Dallas Court of Appeals was whether the default of a non-answering corporate defendant may bind an answering director or officer of that entity in the same suit.[143]

In reversing the trial court's grant of summary judgment,[144] the court of appeals rooted its rationale on principles of fairness. Specifically, the court of appeals cited a line of Texas case law stating that it would result in fundamental unfairness to impose default liability on an answering defendant where the answering defendant has no authority to answer on behalf of the defaulting defendant.[145] While the cases that the court of appeals cited to mainly arise from an employer/employee relationship, the court of appeals expressed no reservation in expanding such rationale to non-answering corporate defendants and their former officers under Section 171.255.[146]

Fueling the court of appeals' rationale was the penal nature of Chapter 171, a fact that led the court of appeals to cite the common adage that punitive statutes are to be "strictly construed to protect those individuals against whom liability is sought."[147] In accordance with a strict construction of Section 171.255, the court of appeals stated that even if it were to construe Section 171.251 so as to allow VIPCO to defend itself, the plain fact remained that there was no evidence in the record that Christian had authority to answer on behalf of the company.[148] For the sake of argument, the court of appeals further posited that even if, as president, Christian had authority to answer, that authority would have no longer existed as he resigned from the position before Venefits' suit was filed.[149] Thus, the court of appeals found that Christian, as the only answering

141. *Id.*
142. *Id.* at *4.
143. *Id.*
144. *Id.*
145. *See id.*; Winnard v. J. Grogan Enters., LLC, No. 05-10-00802-CV, 2012 WL 1604907, at *2 (Tex. App.—Dallas Apr. 30, 2012, no pet.) (mem. op.) (holding deemed admissions of an employee may not be imputed on an employer where employer answered and participated in trial); Brazos Valley Cmty. Action Agency v. Robinson, 900 S.W.2d 843, 845–46 (Tex. App.—Corpus Christi 1995, writ denied) (holding that employer was not to be bound by employee's default where employer answered and employer possessed no authority to answer on behalf of employee); Mayfield v. Hicks, 575 S.W.2d 571 (Tex. App.—Dallas 1978, writ ref'd n.r.e.) (holding that where a guarantor has notice of a suit against his or her principal and answers in that suit, the guarantor will not be bound by the default of the principal, as the guarantor may not possess authority to answer on behalf of the principal).
146. *See Venefits*, 2018 WL 6187612, at *6.
147. *Id.* (quoting Rossman v. Bishop Colo. Retail Plaza, L.P., 455 S.W.3d 797, 802 (Tex. App.—Dallas 2015, pet. denied)).
148. *See id.*
149. *Id.*

defendant who had already fought off two of Venefits' causes of action, would have been unfairly prejudiced by the imposition of VIPCO's default judgment against him in his individual capacity.[150]

The *Venefits* decision is significant in that it demonstrates at least one court's hesitance to impose an entity's default judgment on its directors or officers. While the expansiveness of the decision has yet to be seen outside the context of Chapter 171 of the Tax Code, the case still alludes to the fact that, under statutory schemes permitting individual liability, the failure of an entity to answer suit may not subsequently bar its officers and directors from individually raising their defenses.

B. The Texas Supreme Court Disregards Entity Protection and Imposes Texas Water Code Liability on the Sole Member of a Limited Liability Company

On June 22, 2018, by rehearing, the Texas Supreme Court held that a sole member of a limited liability company (LLC) could be personally liable under Section 7.102 of the Texas Water Code for causing the company to violate the statute.[151] Pursuant to Section 7.102 of the Texas Water Code, a "person who causes, suffers, allows, or permits a violation of a statute . . . within the [Texas Commission on Environmental Quality's (TCEQ)] jurisdiction . . . shall be assessed" certain civil penalties.[152] Accordingly, the supreme court found that the term "person" as used in Section 7.102 encompasses individual conduct, even where the individual acts as an agent of the entity.[153]

In 2004, Bernard Morello purchased a tract of land previously owned by Vision Metals, Inc. (Vision).[154] During the course of Vision's ownership, its operations caused certain contaminants to escape into the property's groundwater.[155] To remain in compliance with applicable environmental laws, Vision obtained a "hazardous waste permit and compliance plan," requiring Vision to "(1) implement a corrective action program, (2) reduce the groundwater contamination as well as monitor and file reports detailing corrective actions . . . , and (3) provide assurance to the TCEQ that Vision was financially capable of conducting the corrective action program."[156] In closing on the property, Morello remained aware of Vision's obligations to the TCEQ.[157]

When Morello eventually closed on Vision's former site, he assigned all of his interests and obligations in the property to White Lion Holdings, LLC (White Lion), an entity that he formed for the sole purpose of hold-

150. *Id.* at *7.
151. State v. Morello, 547 S.W.3d 881, 888 (Tex. 2018); *see* Tex. Water Code Ann. § 7.102.
152. Water Code § 7.102.
153. *Morello*, 547 S.W.3d at 886.
154. *Id.* at 883.
155. *See id.*
156. *Id.*
157. *See id.*

ing title to the property.[158] Just months following this closing, the TCEQ sent notices to White Lion, informing Morello that White Lion failed to remain in compliance with Vision's original compliance plan.[159] However, Morello ignored these notices and two years later, in April 2006, the State filed suit against White Lion, alleging the aforementioned violations of the compliance plan.[160] Shortly thereafter, the State added Morello as a defendant to its suit, alleging that Morello was individually culpable for the violation of the TCEQ compliance plan.[161]

Seven years following the filing of the State's original petition against White Lion, it moved for summary judgment on its claim that "for over nine years, White Lion had deliberately failed to maintain and monitor the groundwater remediation system."[162] The trial court granted the State's motion and severed its remaining claim against Morello in his individual capacity.[163] Subsequently, the State moved for summary judgment against Morello, arguing that Morello caused White Lion to violate a statute within the jurisdiction of the TCEQ and was therefore liable as a "person" under Section 7.102 of the Water Code.[164] Morello vehemently maintained the State's theory on the ground that regardless of whether he was the sole member of White Lion and made all decisions for the entity, "his actions were performed in his capacity as White Lion's agent, and not in his individual capacity."[165] Accordingly, Morello asserted that he could not be found personally liable for any violation of Section 7.102.[166] Nevertheless, the trial court granted the state's motion against Morello.[167]

On appeal, the Austin Court of Appeals reversed the trial court, reasoning that the State failed to demonstrate that "the alleged failures to satisfy the terms of the compliance plan . . . are tortious or fraudulent conduct of Morello individually or that those failures to comply should somehow be treated as if they were."[168] Thus, the court of appeals found that the State made no showing that, as a matter of law, Morello could be held individually liable under Section 7.102.[169]

The State, not to be deterred by the court of appeals' holding, brought its appeal before the Texas Supreme Court.[170] In its appeal, the State

158. *See id.* Note that while Morello personally paid the purchase price, title to the property and the TCEQ compliance plan were transferred to White Lion.

159. *Id.* Specifically, the TCEQ alleged that White Lion failed to "perform a groundwater monitoring program and fail[ed] to comply with reporting requirements." *Id.*

160. *See id.*

161. *See id.*

162. *Id.* at 883–84.

163. *See id.* at 884.

164. *See id.*

165. *Id.*

166. *Id.*

167. *See id.*

168. *See* State v. Morello, 539 S.W.3d 330, 340 (Tex. App.—Austin 2016), *rev'd*, 547 S.W.3d 880, 881 (Tex. 2018)).

169. *See id.* at 339.

170. *See Morello*, 547 S.W.3d at 885.

maintained that pursuant to the "plain language of the Water Code," Morello could be found individually liable, regardless of whether he acted as an agent of White Lion.[171] Under this rationale, because Section 7.102 simply reads that a "person" may be liable if such "person" causes the violation of another, Morello could be found individually liable as the "person" who caused White Lion's violation.[172] In response, Morello furthered three arguments relevant to this discussion, namely that he could not be individually liable because (1) White Lion was the sole party to the compliance plan; (2) any of his violative conduct was performed in his capacity as an agent of White Lion; and (3) that the term "person" found in Sections 7.101 and 7.102 did not encompass individuals.[173]

In addressing the respective merits of the arguments, the supreme court first recognized that the State's position did not rest upon the Texas Business Organizations Code.[174] Instead, the supreme court noted that the State's argument was made solely pursuant to the Water Code.[175] As such, the supreme court found no need to explore the premise found in the Business Organizations Code that "a member . . . is not liable for a debt, obligation, or liability of a limited liability company."[176] Under the supreme court's rationale, the determination of Morello's liability rested solely on an analysis of Sections 7.101 and 7.102 of the Water Code.[177]

Turning to the language of the Water Code, the supreme court acknowledged the omission of a definition of the term "person" within the statute.[178] To this end, the supreme court furthered two arguments in holding that the term "person" found in the Water Code encompasses individuals. First, the supreme court noted that Black's Law Dictionary specifically defines the term "person" as "[a] human being."[179] Second, the supreme court reasoned that because it could find "no statutory definition *excluding* individuals from the definition of person," it was unpersuaded to exclude individuals with respect to the Water Code.[180] Accordingly, the supreme court was left with the determination of whether Morello, as a "person," caused White Lion's violation of the TCEQ compliance plan.

With respect to the remaining issue, Morello's first two previously mentioned arguments were relevant to the analysis. First, with respect to fact that White Lion was Vision's sole transferee, the supreme court found it

171. *See id.*
172. *See id.*
173. *See id.*
174. *See id.*
175. *See id.* (recognizing "the State's position is not based on the Business Organizations Code; it is based on the Water Code").
176. *See id.* (quoting TEX. BUS. ORGS. CODE ANN. § 101.114). The supreme court went on to explain that the Business Organizations Code was further inapplicable as Morello "was not held liable for the debt, obligation, or liability of [White Lion.]" *Id.* at 888.
177. *See id.*; *see* TEX. WATER CODE ANN. §§ 7.101, 7.102.
178. *See Morello*, 547 S.W.3d at 886.
179. *Id.* (quoting *Person*, BLACK'S LAW DICTIONARY (10th ed. 2014)).
180. *Id.* (emphasis in original).

of no significance that Morello never *individually* assumed any obligations under the compliance plan.[181] In the view of the supreme court, the plain language of Sections 7.101 and 7.102 makes those Sections applicable to any "person," not merely "the person holding the permit."[182] Therefore, because Morello caused White Lion's violation of the compliance plan, he was a "person" causing a violation.

Moving to Morello's agency argument, the supreme court similarly rejected Morello's assertions. Specifically, Morello argued that corporate agents "may only be held [personally] liable for 'tortious' or 'fraudulent' acts."[183] To this end, the supreme court found that there existed no such limitation. Instead, the supreme court cited to case law reasoning that corporate agents may be held personally liable for their own violations of statutory schemes.[184] As such, the supreme court found no reason that a corporate agent should be personally protected from individual liability when that agent "personally participated in the wrongful conduct."[185]

The supreme court's holding in *Morello* is significant in that it demonstrates that corporate agents will sometimes be unable to hide behind the "corporate shield." Recall that generally, members and managers of limited liability companies are not personally liable for the debts, obligations, or liabilities of the company. Nevertheless, *Morello* reiterates that such individuals must remain cognizant of the varying statutory schemes describing broad violative conduct. It is in these instances that a court may find the agent is not answering for the debts or obligations of the entity and is instead answering for his or her personal violation.

C. The First Houston Court of Appeals Reaffirms the High Evidentiary Burden Required to Hold a Parent Company Liable for the Obligations of its Subsidiary Under an "Alter Ego" Theory

Since the enactment of Texas Business Organizations Code Section 21.223, it is without question that Texas law affords a high degree of deference to the corporate form and its protections.[186] Accordingly, to disregard the corporate form and hold a shareholder or member[187] liable for the contractual obligations of the entity, two findings must be met. First,

181. *See id.*
182. *Id.*
183. *Id.*
184. *See id.* at 887 (citing Miller v. Keyser, 90 S.W.3d 712, 716 (Tex. 2002) (holding corporate agent could be held personally liable under the DTPA for making false statements); State v. Malone Service Co., 853 S.W.2d 82, 84 (Tex. App.—Houston [14th Dist.] 1993, writ denied) (holding violations of the Water Code are analogous to an "environmental tort" and therefore corporate officers may be individually liable for their participation in those environmental torts)).
185. *See Morello*, 547 S.W.3d at 888. The supreme court further bolstered this holding by citing to numerous out-of-state and federal cases declining to provide individual protection to corporate agents when that agent personally participates in violative conduct.
186. Tex. Bus. Orgs. Code Ann. § 21.223.
187. Section 21.223 of the Code applies with the same force and effect to limited liability companies as it does to corporations. *Id.* § 101.002(a).

the plaintiff must demonstrate "that the entity on which it seeks to impose liability is the alter ego of the debtor."[188] Second, the plaintiff must establish "that the corporate fiction was used . . . to perpetrate an actual fraud on the plaintiff for the defendant's direct personal benefit."[189] The First Houston Court of Appeals decision in *KingKing, LLC v. Precision Energy Servs., Inc.*[190] demonstrates the high-degree of proof necessary to conclusively establish this two-part factual inquiry.

Turning to the relevant facts, KingKing, LLC (KingKing), the United States subsidiary of a Chinese corporation, was one of the members of Amerril, a limited liability company engaged in oil and gas exploration.[191] In essence, the relationship between KingKing and Amerril was analogous to a holding company and its subsidiary operating company. KingKing would hold the mineral leases and Amerril would act as operator on the leasehold.[192] Eventually, in 2013, Amerril required certain "goods and services" to perform its operations on one of the leases held by KingKing.[193] To obtain such items, Amerril engaged Weatherford International, Inc. (Weatherford) and its relevant subsidiaries.[194] As a requisite to obtaining a line of credit for the goods and services, Amerril sent Weatherford a "Confidential Credit Account Application with Terms and Conditions" identifying KingKing as its "principal owner."[195] Amerril's application was subsequently accepted and Weatherford began supplying Amerril with oilfield items and services.[196]

Four months following the initial engagement, the relationship between Amerril and Weatherford swiftly deteriorated when one of the items supplied by Weatherford "allegedly failed, causing a delay in drilling operations and damage to the [w]ell."[197] While Weatherford continued to perform under the parties' contract, Amerril supposedly ceased paying Weatherford's invoices.[198] After Weatherford escalated matters by filing for a lien in the county property records, Weatherford and Amerril filed various suits against each other, with venue ultimately lying in Harris County.[199]

In the district court, Weatherford asserted that "KingKing was liable for Amerril's contractual obligations to Weatherford pursuant to Business Organizations Code Section 21.223 because Amerril was an alter ego

188. KingKing, LLC v. Precision Energy Servs., Inc., 555 S.W.3d 200, 213 (Tex. App.—Houston [1st Dist.] 2018, no pet.) (citing Tryco Enters., Inc. v. Robinson, 390 S.W.3d 497, 508 (Tex. App.—Houston [1st Dist.] 2012, pet. dism'd)).
189. *Id.* at 213–14.
190. *Id.*
191. *See id.* at 204.
192. *See id.*
193. *Id.*
194. *See id.*
195. *Id.* at 204–05.
196. *See id.* at 205.
197. *Id.*
198. *See id.*
199. *See id.*

of KingKing."[200] Further, Weatherford specifically alleged that:

> KingKing used Amerril to perpetrate an actual fraud on Weatherford by "purposefully creating Amerril as a shell entity with no control of any funds with which to pay Weatherford and by failing to disclose the extent of KingKing's control at the time of contracting and throughout the course of the lawsuit."[201]

Accordingly, Weatherford asserted the two requisite elements to pierce the corporate veil, that there existed an alter ego relationship and that such relationship was used to perpetrate an actual fraud. On these two points, Weatherford moved for summary judgment.[202]

Weatherford's summary judgment evidence on its veil piercing argument consisted primarily of two depositions. The first of these came from Amerril's former accounting manager, Jacque Bateman, who testified that KingKing possessed full control over Amerril's bank accounts.[203] To this point, Bateman specifically testified that: (1) all incoming Amerril funds from the well's operations would be deposited into an account controlled by KingKing; and (2) all funding requests made by Amerril would require KingKing approval.[204] These two facts led Bateman, when pressed, to conclude that Amerril relied "solely on funds it obtained from U.S. KingKing"[205] and held "no local control" over its funds.[206]

Weatherford's second deposition, attached as summary judgment evidence, came from Robert Hadlow, a corporate representative of KingKing and Amerril's interim financial officer.[207] In parts relevant to alter ego, Hadlow testified that KingKing and Amerril shared a mailing address, shared two corporate officers, and that the web address www.uskingking.com contained the statement "Welcome to Amerril Energy."[208] Further, Hadlow made reference to the fact that KingKing had been transferring its mineral leases to Amerril, without remuneration, who would then act as both owner and operator.[209]

Turning to Weatherford's claim of actual fraud, Weatherford's counsel provided Hadlow with a copy of Amerril's balance sheet which had allegedly been supplied to Weatherford as part of its initial line of credit application.[210] When presenting Hadlow with the document, Weatherford's counsel queried whether Hadlow had any reason to believe the amounts reflected in the balance sheet were inaccurate.[211] To this, he responded that he "had to make several adjustments" to the sheet and that some of

200. *Id.* at 206.
201. *Id.*
202. *Id.* at 206–07.
203. *Id.* at 207.
204. *Id.* at 207–08.
205. *Id.* at 208.
206. *Id.*
207. *See id.*
208. *Id.*
209. *See id.*
210. *See id.*
211. *See id.*

the values were "way too high."[212] For example, the balance sheet reflected Amerril's annual net income as $92 million, where that number should have been closer to $72 million.[213] On this ground, coupled with Bateman's testimony relating to alter ego, Weatherford argued there was no issue of material fact on both of the requisite showings needed for Weatherford to hold KingKing liable for Amerril's obligations. After KingKing made no response, the trial court ultimately granted Weatherford's motion two months later.[214]

On appeal, the First Houston Court of Appeals first recognized the seeming presumption against disregarding the corporate form.[215] Citing both recent and longstanding Texas case law, the court of appeals noted that "[g]enerally, a corporation is a separate legal entity that insulates its owners and shareholders from personal liability for its corporate obligations."[216] Therefore, a court will pierce the corporate veil under an alter ego theory only where "there is such unity between corporation and individual that the separateness of the corporation has ceased and holding only the corporation liable would result in injustice."[217] This requisite showing, in the words of the court of appeals, "involves two considerations: (1) the relationship between the entities, and (2) whether the entities' use of limited liability was illegitimate."[218] Importantly, these two considerations are distinct, thus "[e]vidence that a company was used as an alter ego does not, by itself create an issue regarding whether it was used to commit an actual fraud on the plaintiff."[219]

In accordance with the independent relationship between the two veil piercing considerations, the court of appeals first analyzed whether Weatherford met its burden in demonstrating that Amerril was the alter ego of KingKing. On this point, the court of appeals considered the following factors in examining the relationship between the allegedly intertwined entities:

> (1) whether the entities shared a common business name, common offices, common employees, or centralized accounting; (2) whether one entity paid the wages of the other entity's employees; (3) whether one entity's employees rendered services on behalf of the

212. *Id.*

213. *Id.* Such other items included inflated values for "stock, leasehold costs, and accounts receivable." *Id.*

214. *Id.* at 209.

215. *See id.* at 213.

216. *See id.* (citing Nichols v. Tseng Hsiang Lin, 282 S.W.3d 743, 747 (Tex. App.—Dallas 2009, no pet.)); *see also* Willis v. Donnelly, 199 S.W.3d 262, 271 (Tex. 2006) ("A bedrock principle of corporate law is that an individual can incorporate a business and thereby normally shield himself from personal liability for the corporation's contractual obligations.").

217. *KingKing*, 555 S.W.3d at 213 (quoting Tryco Enters., Inc. v. Robinson, 390 S.W.3d 497, 508 (Tex. App.—Houston [1st Dist.] 2012, pet. dism'd)).

218. *Id.* (citing SSP Partners v. Gladstrong Invs. (USA) Corp., 275 S.W.3d 444, 455 (Tex. 2008)).

219. *Id.* at 214 (quoting Metroplex Mailing Servs., LLC v. RR Donnelley & Sons Co., 410 S.W.3d 889, 896–97 (Tex. App.—Dallas 2013, no pet.)).

> other entity; (4) whether one entity made undocumented transfers of funds to the other entity; and (5) whether the allocation of profits and losses between the entities is unclear.[220]

On these factors, Weatherford first argued that, pursuant to factor three, it had established that "KingKing's employees rendered services for Amerril."[221] As evidence, Weatherford pointed to Hadlow's status as Amerril's interim chief financial officer, his assistance in the preparation of KingKing's tax returns, that KingKing and Amerril shared two officers, and that KingKing approved Amerril's funding requests.[222] Turning to the other factors, Weatherford asserted that the shared website, the commonality of mailing addresses between the entities, and their routine swapping of assets without consideration conclusively "establishe[d] that Amerril is the alter ego of US KingKing."[223]

While Weatherford appeared to make a showing under multiple of the above-listed factors, the court of appeals' swift rejection of such arguments firmly demonstrates the degree of proof necessary to find that a factor weighs in favor of piercing the protections of the corporate veil. On the commonality of officers and financial control, the court of appeals cited to the Texas Supreme Court, reasoning that the courts of this state have "never held corporations liable for each other's obligations merely because of centralized control, mutual purposes, and shared finances."[224] Additionally, the court of appeals disregarded Hadlow's commonality of roles as "Weatherford presented no evidence that *any other* employee of Amerril . . . render[ed] services for KingKing."[225]

Turning to Weatherford's remaining arguments, the court of appeals first found it unpersuasive that the two entities shared a mailing address. Here, the court of appeals reasoned that "the companies ha[d] offices in different suites," "d[id] not share the same business name," and there was no evidence that either entity paid the wages of the other entity's employees.[226] Last, that KingKing transferred properties to Amerril without consideration was similarly lacking in consequence. In that respect, the court of appeals noted that there was no evidence that any of those transactions went undocumented.[227] The court of appeals also commented that the lack of frequency of these types of asset transfers similarly harmed Weatherford's argument.[228] Therefore, the court of appeals concluded that while Weatherford may have made some showing under the enumerated factors, its evidence lacked the degree necessary to conclusively es-

220. *Id.* (citing *Tryco Enters.*, 390 S.W.3d at 509).
221. *Id.*
222. *Id.*
223. *Id.* at 215.
224. *Id.* (quoting SSP Partners v. Gladstrong Invs. (USA) Corp., 275 S.W.3d 444, 455 (Tex. 2008)).
225. *Id.* (emphasis added).
226. *Id.*
227. *Id.*
228. *Id.* at 215–16.

tablish that Amerril was merely the alter ego of KingKing.[229]

While the court of appeals rejected Amerril's alter ego arguments, the court, assuming *arguendo* that it had not, addressed whether Amerril had made the requisite showing of actual fraud. Again, Weatherford pointed to the overinflated Amerril balance sheet.[230] However, in Texas, a demonstration of actual fraud requires that the defendant acted with "dishonesty of *purpose or intent to deceive*."[231] Accordingly, the court of appeals found that the plain fact that "Weatherford presented Hadlow's testimony that several values on KingKing's balance sheet were too high . . . does not establish, as a matter of law, that . . . KingKing acted fraudulently."[232] To have made such a showing, the court of appeals would have required Weatherford to demonstrate that "KingKing *knew* that th[e] balance sheet was inaccurate at the time it was . . . submitted to Weatherford or at any time before Hadlow discovered the error."[233] Therefore, collectively with the court of appeals' negative finding on Weatherford's alter ego evidence, the First Houston Court of Appeals reversed and remanded the district court's grant of summary judgment in favor of Weatherford.[234]

The KingKing case is significant as it demonstrates the degree of evidence and proof necessary to establish, as a matter of law, both alter ego and actual fraud. While Weatherford appeared to make somewhat compelling arguments as to the interconnectedness of Amerril and KingKing, the court of appeals' swift rejection gives guidance that one-off dual employees, shared entity addresses, and a commonality of officers and financial accounts will not suffice when attempting to disregard the protections of incorporation. Last, the court of appeals' opinion speaks to the burden with respect to actual fraud. With the enactment of Section 21.223, constructive fraud will no longer be sufficient.[235] Therefore, a complainant must be ready to provide evidence beyond the mere fact a false statement was submitted or made.

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229. *Id.* at 216. The court went on to explain that "[e]vidence is conclusive only if reasonable people could not differ in their conclusions . . . [therefore, in] considering the record and the applicable law, Weatherford has not established, as a matter of law, that 'there is such unity between Amerril and KingKing that the separateness of the corporation has ceased and holding only the corporation liable would result in injustice.'" *Id.* (citing Tryco Enters., Inc. v. Robinson, 390 S.W.3d 497, 508 (Tex. App.—Houston [1st Dist.] 2012, pet. dism'd) (internal brackets omitted)).

230. *See id.* at 217.

231. *Id.* (emphasis added).

232. *Id.* at 217–18.

233. *Id.* at 218 (emphasis added).

234. *See id.* at 220 ("We therefore reverse the portions of the trial court's judgment that hold KingKing liable for Amerril's obligations . . . [and] remand for further proceedings.").

235. Prior to the enactment of Section 21.223, the Texas Supreme Court held that "tort claimants and contract creditors must show only constructive fraud." Castleberry v. Branscum, 721 S.W.2d 270, 273 (Tex. 1986).