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Dallas Court of Appeals Reverses Partnership Verdict: Preliminary Agreements Precluded Partnership

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On Tuesday, July 18, 2017, the Dallas Court of Appeals reversed a \$535 million judgment against Enterprise Products Partners, L.P. (Enterprise), finding that unfulfilled conditions precedent in Enterprise's written agreements with Energy Transfer Partners, L.P. (ETP) precluded the formation of a partnership between the parties. The jury verdict had generated concerns in the business community that parties could unwittingly form a partnership and be subject to the attendant fiduciary duties. The court of appeals' decision signals that the risk of an inadvertent partnership can be minimized through appropriate drafting of preliminary agreements.

The court's opinion recites that during 2011, Enterprise and ETP discussed potentially working together to build a crude oil pipeline from Cushing, Oklahoma to Houston, Texas. The parties signed three agreements: a confidentiality agreement, a letter agreement with a term sheet for the potential transaction, and a reimbursement agreement by which the parties agreed to share certain expenses while negotiating definitive agreements. Each of these agreements contained customary provisions that limited the parties' obligations to one another.

After efforts to obtain commitments from oil shippers during the open season fell short of stated goals, Enterprise contacted ETP and terminated its participation in the project. But prior to that time, the court noted, Enterprise had been in discussions with another company about an alternative pipeline project to transport oil from Cushing to Houston. Enterprise subsequently built the pipeline with the other company.

ETP claimed that it and Enterprise had formed a partnership and that Enterprise breached its fiduciary duties to ETP by teaming with the other company on the alternative project. In March 2014, a Dallas jury found in favor of ETP, awarding actual damages of \$319,375,000 and disgorgement of \$150 million. Including interest, the final judgment totaled \$535 million.

While acknowledging that a partnership can be created under Texas law when parties associate "to carry on a business for profit as owners ... regardless of whether ... the persons intended to create a partnership" (Texas Business Organizations Code § 152.051(b)), the Dallas Court of Appeals found no partnership was formed in this case. In reversing the trial court judgment, the court relied on protective terms in the letter agreement providing that no binding or enforceable obligations would arise unless and until (1) the parties received board approvals

and (2) there were executed definitive agreements. ETP acknowledged that these two conditions were not met, but it argued that the failure of these conditions was only one factor in a five-factor statutory test for determination of the existence of a partnership (Texas Business Organization Code § 152.052). The court of appeals disagreed, ruling that the five factors in the statute were not exclusive and that the law of conditions precedent is one of the “principles of law and equity” that, according to Section 152.003 of the Texas Business Organizations Code, supplement the statutory provisions.

According to the court, the failure of these conditions precedent precluded formation of a partnership unless they were waived. The court also found that ETP had the burden of either obtaining a jury finding of waiver or establishing by conclusive evidence that a waiver had occurred. Because ETP did not request a jury finding, and because the court found that there was no conclusive evidence of waiver, the court found that the jury’s verdict could not stand. It reversed and rendered judgment in favor of Enterprise.

It seems likely that ETP will ask the Texas Supreme Court to accept review of the case. Regardless of the ultimate outcome of the litigation, the verdict remains a cautionary tale for parties considering joint business opportunities to take appropriate precautions to avoid inadvertently creating a partnership where none is intended.