Business Associations

By Joseph Epps Claxton*

This survey article deals with recent Georgia cases and statutes in the areas of partnerships, corporations, and securities regulation.

I. Partnerships

In determining the potential liability of a member of a partnership, obviously it is necessary to make certain that the defendant is in fact a partner. The Georgia courts have insisted for many years that finding an actual partnership agreement is not always essential in order to conclude that a person is a member of a partnership. As long ago as 1895 the Georgia Supreme Court stated that "[a]s to third persons, [one] may assume such a liability by inducing them to extend a credit upon the faith of representations made by him, either express or implied, to the effect that he was a partner and as such liable."[1] A person who makes such representations is estopped to argue that he is not really filling the role of a partner.[2]

In *Time Financial Services, Inc. v. Hewitt*,[3] decided by the court of appeals during the current survey period, these basic principles were reaffirmed. The defendant had signed certain documents, checks, and promissory notes in a manner that indicated that he was functioning as a partner. He also allowed himself to be held out as a partner at various meetings. In light of these circumstances, the mere fact that there was no express partnership agreement naming the defendant clearly did not entitle him to summary judgment.

II. Corporations

A. *The Corporation as a Legal Entity*

A corporation is a legal entity, an institution which "the law has seen fit to clothe . . . with legal personality."[4] On occasion, the concept is abused to such an extent that courts have no choice other than to pierce

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1. Carlton v. Grissom & Co., 98 Ga. 118, 121, 26 S.E. 77, 78 (1895).
2. Mims v. Brooks & Co., 3 Ga. App. 247, 59 S.E. 711 (1907).
3. 139 Ga. App. 270, 228 S.E.2d 176 (1976).
4. N. Lattin, The Law of Corporations 65 (2d ed. 1971).

the corporate veil. Liability then is imposed on the corporate shareholders, or on another corporation the affairs of which are so interrelated with those of the first corporation as to be inseparable. There are numerous instances in which this has occurred in Georgia.[5] Nevertheless, as in most jurisdictions, the Georgia judiciary is extremely reluctant to take such a step, and generally will not do so even if only the technical attributes of separateness are preserved.

For example, in the recent case of *Cornwell v. Williams Brothers Lumber Co.*[6] the court of appeals considered a number of relatively minor points that together indicated that one corporation involved in the case was not the mere alter ego[7] of another.

> The corporations are located in the same building but on different floors leased separately from the landlord; there is no commingling of corporate assets; there are separate banking accounts; separate equipment was maintained; separate tax returns were filed; separate minute books, by-laws and corporate records were maintained; the companies had separate liability insurance policies; separate personnel were employed and separate payrolls maintained; out of eight directors only two are common to both corporations while only three of eight shareholders are common to both.[8]

Obviously, the mere observance of a normal corporate routine will usually be enough to preserve the legitimacy of the entity concept.

In *Byrd v. Brand*,[9] the court of appeals again emphasized the distinctiveness of the corporate entity, with specific reference to the line that should be drawn between a corporation and its shareholder or shareholders. The court reaffirmed the concept that "[o]ne person may own all the stock of a corporation, and still such individual shareholder and the corporation would, in law, be two separate and distinct persons."[10]

The sole stockholder who was involved in *Byrd* had been careful to preserve the legal integrity of the corporation he owned. This is sometimes extremely difficult for a person who is the sole owner of a corporation, or one of a small number of owners. In such situations, there is a constant

5. *See, e.g.*, Trans-American Communications, Inc. v. Nolle, 134 Ga. App. 457, 214 S.E.2d 717 (1975); Lincoln Land Co. v. Palfrey, 130 Ga. App. 407, 203 S.E.2d 597 (1973); Ashburn Air Service, Inc. v. Ashburn Bank, 127 Ga. App. 872, 195 S.E.2d 272 (1973).

6. 139 Ga. App. 773, 229 S.E.2d 551 (1976).

7. The alter ego doctrine involves two factors: "(1) [T]hat there be such unity of interest and ownership that the separate personalities of the corporation and the individual [or another corporation] no longer exist and (2) that, if the acts are treated as those of the corporation alone, an inequitable result will follow." Automotriz Del Golfo De California v. Resnick, 47 Cal.2d 792, 796, 306 P.2d 1, 3 (1957).

8. 139 Ga. App. at 774, 229 S.E.2d at 552.

9. 140 Ga. App. 135, 230 S.E.2d 113 (1976).

10. Waycross Air-Line R.R. Co. v. Offerman & W. R.R. Co., 109 Ga. 827, 828, 35 S.E. 275 (1900).

temptation for the shareholder to treat the corporation as a mere extension of himself. That mistake must be avoided, for "[i]t is clear that if the managers and owners of a corporation desire to have creditors and the courts treat the corporation as a true legal entity, then those managers and owners cannot wholly ignore the legal entity concept themselves."[11]

Of course, even if someone establishes a corporation and operates it in a fundamentally legitimate manner, the owner will not always be released from liability in future business dealings with others. For example, in *Goad v. L & W Supply Corp.*,[12] the court of appeals noted that

> [s]imply because Mr. Goad formed a corporation, it was not required that all businesses would automatically cease to deal with Mr. Goad as an individual and begin to deal instead with the corporation. All of the evidence indicates that. . .[L & W] intended at all times to deal with Mr. Goad as an individual not with his limited liability company.[13]

Goad was compelled to accept personal responsibility for the debts under consideration in the case.[14]

B. *Corporation by Estoppel*

The doctrine of corporation by estoppel represents the converse of the *Goad* situation. The doctrine is based on the proposition that "a person who has contracted or otherwise dealt with a body purporting to be a corporation, is, by reason of having dealt with it as such, estopped from denying its corporate existence."[15] After a period in which the validity of the estoppel approach had fallen into some doubt, the doctrine was given strong support by the Georgia Supreme Court in the 1974 case of *Cahoon v. Ward*.[16] Shortly afterward, the court of appeals adopted the *Cahoon* analysis in *Walker v. Joanna M. Knox & Associates, Inc.*[17]

The doctrine of corporation by estoppel was accorded additional support during the current survey period in *Lamas v. Baldwin*.[18] That case emphasized that

> one who deals with a corporation as such an entity cannot, in the absence of fraud, deny the legality of the corporate existence for the purpose of holding the owner liable. Having dealt with the corporation as his debtor,

11. Claxton, *Annual Survey of Georgia Law: Agency and Business Associations*, 25 MERCER L. REV. 21, 36 (1974).

12. 141 Ga. App. 427, 233 S.E.2d 503 (1977).

13. *Id.* at 428, 233 S.E.2d at 503-04.

14. For another recent case taking a similar approach, *see* Cook v. Van Deren Hardware, Inc., 129 Ga. App. 768, 201 S.E.2d 328 (1973).

15. Cason v. State, 16 Ga. App. 820, 829, 86 S.E. 644, 649 (1914).

16. 231 Ga. 872, 204 S.E.2d 622 (1974).

17. 132 Ga. App. 12, 207 S.E.2d 570 (1974).

18. 140 Ga. App. 37, 230 S.E.2d 13 (1976).

> [one] cannot claim [that the corporate shareholder] is personally liable for its debts. It is well settled that persons who contract with or otherwise deal with a company as a corporation are estopped to deny its corporate existence.[19]

It is hardly possible for a court to state its views more clearly.

C. *Arbitration of Intra-Corporation Disputes*

The use of arbitration to settle intra-corporate disputes has become widespread in the last twenty-five years. Although this trend has encountered some resistance from the courts, that resistance seems to be disappearing. In the words of one leading authority:

> Judicial opposition to the use of arbitration for settling intra-corporate disputes is slowly yielding as businessmen and their lawyers continue to resort to arbitration as a preferable alternative to dissolution or litigation for settling disputes and breaking deadlocks in otherwise useful and profitable enterprises. After all, there is really no sound reason why all the shareholders of a corporation should not be permitted by unanimous agreement to arrange for the settlement of intra-corporate disputes by arbitration, and if an arbitration arrangement is established to meet a legitimate business need in a closely held enterprise and if it is approved by all interested persons, a court can hardly justify a refusal to sustain it.[20]

Certainly the Georgia courts appear to have no qualms about relying upon arbitration as a substitute for long and tiresome litigation. In *Fisher v. Gause*,[21] the supreme court upheld the decisions of an arbitrator to whom the trial court had submitted a dispute between the only two shareholders of a corporation. The only qualification in the *Fisher* opinion was that the arbitrator could not impair any rights of third parties against one of the shareholders. *Fisher v. Gause* appears to reflect full judicial confidence in the arbitration process.

D. *Defamation of a Corporation*

In *Eason Publications, Inc. v. Atlanta Gazette, Inc.*,[22] the question of whether a corporation may be considered as a matter of law to be the object of defamation was considered for the first time in Georgia. The traditional rule in this area is that

> [a] corporation is regarded as having no reputation in any personal sense, so that it cannot be defamed by words, such as those imputing unchastity,

19. *Id.* at 40-41, 230 S.E.2d at 15-16.
20. F. O'NEAL, CLOSE CORPORATIONS: LAW AND PRACTICE §9.26, at 94 (1971).
21. 236 Ga. 663, 225 S.E.2d 2 (1976).
22. 141 Ga. App. 321, 233 S.E.2d 232 (1977).

> which would affect the purely personal repute of an individual. But it has prestige and standing in the business in which it is engaged, and language which casts an aspersion upon its honesty, credit, efficiency or other business character may be actionable.[23]

The court of appeals accepted this approach in *Eason Publications.*

E. Procedure

A number of procedural issues having a direct impact in the corporate area were subjected to appellate review in Georgia during the current survey period. One of the simplest but most basic of these issues revolved around the statutory rule that the right of a foreign corporation to conduct business in Georgia is dependent upon the procurement of a certificate of authority to transact business.[24] In general, a foreign corporation that has failed to obtain such a certificate may not maintain an action in any Georgia court.[25] There are certain exceptions to the certificate requirement, however; among them is the rule that a foreign corporation shall not be considered to be transacting business in Georgia if it only engages in "[e]ffecting transactions in interstate or foreign commerce."[26] In *Dekalb Cablevision Corp. v. Press Association,*[27] the plaintiff was a New York corporation which had contracted to furnish a news compilation to the Georgia cable television company on a daily basis for broadcast purposes. The contract was entered into in New York. The court of appeals affirmed the trial court's denial of the defendant's motion to dismiss the complaint of the New York corporation. The motion had been based on the fact that the foreign corporation had not obtained a certificate of authority, but the interstate exemption was deemed controlling. The court of appeals set forth what appears to be a workable balancing test in its resolution of the case.

> Transactions in Georgia between a foreign corporation and a local entity, which exhibit both interstate and intrastate features, must be examined to determine its dominant characteristics. . . . If the transaction is exclusively or dominantly interstate in nature, it will be characterized as "interstate" and the foreign corporation need not comply with the state statute. . . . However, where the local activities of the foreign corporation are not merely ancillary to the interstate features, but constitute a substantial local and domestic business separate from its interstate business, the foreign corporation must comply with the state statute.[28]

23. W. PROSSER, HANDBOOK OF THE LAW OF TORTS §111, at 745 (4th ed. 1971).
24. GA. CODE ANN. §22-1401(a) (1977).
25. GA. CODE ANN. §22-1421(b) (1977).
26. GA. CODE ANN. §22-1401(b)(9) (1977).
27. 141 Ga. App. 1, 232 S.E.2d 353 (1977).
28. *Id.* at 2-3, 232 S.E.2d at 354.

Relying upon this test, the court concluded that the business activities in question were entirely interstate in character, and thus "squarely within the exception granted foreign corporations from registration."[29]

Another basic procedural matter was dealt with by the court of appeals in *Rosing v. Dwoskin Decorating Co.*[30] The court analyzed the question whether a corporate plaintiff in a pending action may continue as at least a nominal plaintiff in the event of formal dissolution, merger, or consolidation. This problem is governed directly by Georgia's Civil Practice Act,[31] which specifically states that "[i]n case of any transfer of interest the action may be continued by or against the original party, unless the court upon motion directs the person to whom the interest is transferred to be substituted in the action or joined with the original party."[32] In light of this statutory approach, the court of appeals held in *Rosing* that dissolution did not affect the procedural status of the corporate plaintiff. The result would be entirely different, of course, in a situation in which the dissolution, merger, or consolidation had occurred *prior* to the filing of the action. In such an instance, the corporation would not be a proper plaintiff.[33]

In *Davis v. Ben O'Callaghan Co.*,[34] one of the more important cases decided during the current survey period, the Georgia Supreme Court set out "to determine whether a judgment creditor of a corporation could bring an action for his own benefit against a corporate officer or director under Code Ann. §22-714 (Rev. 1970), and, if so, whether punitive damages are allowable in such an action."[35] Section 22-714(a) plainly states that an action of this sort is to be brought for the purpose of procurring a judgment "for the benefit of the corporation. . . ." Section 22-714(b) provides, however, that "[a]n action may be brought for the relief provided in this section, and in the provisions of section 22-715 relating to the liability of directors in certain cases, by the corporation, or a receiver, trustee in bankruptcy, officer, director or judgment creditor thereof, *or by a shareholder in accordance with sections 22-614 and 22-615 relating to derivative actions.*" (Emphasis added.)

In reliance upon the latter part of §22-714, the plaintiff-appellee in *Davis* argued that the section

> requires only shareholders to bring a derivative action, and, therefore, by negative implication judgment creditors may bring an action for their own benefit. [The Georgia Supreme Court construed] the statutory language

29. *Id.* at 3, 232 S.E.2d at 355.
30. 141 Ga. App. 617, 234 S.E.2d 128 (1977).
31. GA. CODE ANN., tit. 81A (1972).
32. GA. CODE ANN. §81A-125(c) (1972).
33. *See, e.g.*, Employers' Liability Assurance Corp. v. Keelin, 132 Ga. App. 459, 208 S.E.2d 328 (1974).
34. 238 Ga. 218, 232 S.E.2d 53 (1977).
35. *Id.* at 218-219, 232 S.E.2d at 54.

> to mean that a judgment creditor must generally sue for the benefit of the corporation, that is, derivatively, but need not comply with *all* of the procedural requirements which must be satisfied in shareholder derivative actions under §22-615 of the Business Corporation Code and §81A-123(b) of the Civil Practice Act.[36]

In its conclusion, the supreme court adopted the position taken by the court of appeals that "[s]ince the corporation, under the terms of its own agreement, was required to pay these particular dollars to this specific creditor, we see no reason, under these peculiar facts, to deny recovery by the creditor directly against the corporate officer. . . ."[37] This result is in accord with the approach taken by the New York courts to that section[38] of the New York Business Corporation Law upon which §22-714 of the Georgia Code is based.[39]

Probably the most significant decision affecting the corporate area during the last year was that in *Value Engineering Co. v. Gisell,*[40] which dealt with Georgia's Long Arm Statute.[41] *Value Engineering* arose out of a complaint by a passenger on a Delta Air Lines flight that she had been harmed by exposure to negligently packed radioactive material being shipped on the plane in which she was traveling from Washington, D.C. to Atlanta, Georgia. The radioactive material was on its way from Washington to Baton Rouge, Louisiana, and had been routed through Atlanta so that it could be switched from one plane to another. The Value Engineering Company, which had shipped the material, challenged the jurisdiction of the Georgia courts with the argument that

> the radioactive material was delivered to Delta for shipment to Louisiana and not to Georgia and that it [Value Engineering] had no control over when or where the flight might land or stop. Based on this, it argues that any contact between itself and [Georgia] is "fortuitous," is not based upon any "purposeful activity" here and thus should not be the basis for an exercise of personal jurisdicton over it in Georgia Courts.[42]

This position was a logical outgrowth of Value Engineering's insistence that the only portion of the Georgia Long Arm Statute which could possibly apply to it was that subsection which provides for jurisdiction over any nonresident who "[c]ommits a tortious injury in this State caused by an

36. 238 Ga. at 221, 232 S.E.2d at 55 (emphasis in original).

37. *Id.* at 222-23, 232 S.E.2d at 56, *quoting from* Davis v. Ben O'Callaghan Co., 139 Ga. App. 22, 25, 227 S.E.2d 837, 840 (1976).

38. N.Y. BUS. CORP. LAW §720 (McKinney 1963).

39. *See, e.g.,* Trionics Research Sales Corp. v. Nautec Corp., 28 App. Div. 2d 664, 280 N.Y.S.2d 630 (1967), *rev'd on other grounds,* 21 N.Y.2d 574, 237 N.E.2d 68, 289 N.Y.S.2d 745 (1968).

40. 140 Ga. App. 44, 230 S.E.2d 29 (1976).

41. *See* GA. CODE ANN. §24-113.1 (1971).

42. 140 Ga. App. at 46, 230 S.E.2d at 30.

act or omission outside this State, *if the tortfeasor regularly does or solicits business, or engages in any other persistent course of conduct, or derives substantial revenue from goods used or consumed or services rendered in this State. . . .*"[43] Obviously, the capacity of the Georgia courts to extend jurisdiction to nonresident defendants is limited under this language. Another subsection of the Long Arm Statute, however, provides for personal jurisdiction over any nonresident who "[c]ommits a tortious act or omission within this State. . . ."[44] The application of this aspect of the Long Arm Statute was reviewed in detail by the Georgia Supreme Court in 1973 in the well-known case of *Coe & Payne Co. v. Wood-Mosaic Corp.*[45]

> [T]he court [in *Coe & Payne*] reviewed a situation in which a corporate defendant had committed a negligent act outside Georgia, with the damage from the act occurring in Georgia. The issue was whether jurisdiction could be predicated on that portion of the Long Arm Statute which refers to the commission of "a tortious act or omission within this State. . ." For the first time ever, the court held in the affirmative. In taking this position it adopted the so-called Illinois Rule, which embodies the proposition that "the negligence occurring outside the state cannot be separated from the resulting injury occurring within the state."[46]

In the *Value Engineering* case the court of appeals expressly followed the *Coe & Payne* approach that "jurisdiction shall be exercised over nonresident parties to the maximum extent permitted by procedural due process."[47] The *Value Engineering* decision is in accord with the developing standard that "within the bounds of fairness and substantial justice to the defendant, the Long Arm Statute will be applied to the limits of due process so that those who invoke the protection or benefits of the laws of Georgia, or who injure citizens or property here, will be made to answer therefore in the Georgia courts."[48] This trend has tremendous significance in the corporate sphere.

III. SECURITIES REGULATION

The present Georgia securities law is the Georgia Securities Act of 1973,[49] which became effective on April 1, 1974. However, cases governed by the Securities Act of 1957,[50] the predecessor of the present law, are still handled

43. GA. CODE ANN. §24-113.1(c) (1971) (emphasis added).
44. GA. CODE ANN. §24-113.1(b) (1971).
45. 230 Ga. 58, 195 S.E.2d 399 (1973).
46. Claxton, *supra* note 11, at 42. The reference to the Illinois Rule may be found in the *Coe & Payne* opinion, 230 Ga. at 60, 195 S.E.2d at 400.
47. 230 Ga. at 60, 195 S.E.2d at 401. The reference in *Value Engineering* to this approach is found at 140 Ga. App. at 46, 230 S.E.2d at 30.
48. Beaird & Ellington, *Annual Survey of Georgia Law: Trial Practice and Procedure*, 25 MERCER L. REV. 265, 275 (1974), *quoted in* 140 Ga. App. at 48, 230 S.E.2d at 31.
49. GA. CODE ANN., tit. 97 (1976).
50. 1957 Ga. Laws 134.

by the Georgia courts. Ordinarily, these cases have major implications with reference not only to the old securities law but also the new one. This is true of *Meason v. Gilbert*,[51] decided during the current survey period by the supreme court. The central issue in *Meason* was "what effect is to be given to an integration clause in a stock purchase agreement that no representations other than those contained in the prospectus induced the purchaser to buy certain securities."[52] With the protection of the investor clearly a prime consideration, the court stated:

> We consider this clause as merely having evidentiary value on the question of whether representations were made to the purchaser inducing the stock purchase other than those contained in the prospectus. This provision in the contract states there were no such representations but the purchaser now says there were representations outside the prospectus which induced the purchase. This creates an issue of fact that cannot be resolved as a matter of law. We also reject the seller's contention that the clause as a matter of law estops the purchaser from raising any alleged oral misrepresentations.[53]

The *Meason* decision indicates the investor-oriented judicial philosophy that has been evident in recent Georgia securities cases.[54] The Securities Act of 1973, with its emphasis on protecting the rights of the public,[55] will certainly reinforce this developing judicial approach.

IV. LEGISLATION

The 1977 session of the Georgia General Assembly enacted important new legislation dealing with corporate takeovers.[56] The new statutory material, which is included in the Georgia Corporations Code[57] as Chapter 22-19, provides vitally needed guidelines for the control of takeover efforts, which are notoriously susceptible to abuse.

The heart of the legislation requires the registration of takeover bids with the Commissioner of Securities.[58] The disclosure entailed in the filing of the registration statement is vital to the welfare of the investing public.

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51. 236 Ga. 862, 226 S.E.2d 49 (1976).

52. *Id.*

53. *Id.* at 864, 226 S.E.2d at 150.

54. *See, e.g.*, Fortier v. Ramsey, 136 Ga. App. 203, 220 S.E.2d 753 (1975) (holding that limited partnership interests are securities); Jaciewicki v. Gordarl Assoc.,132 Ga. App. 888, 209 S.E.2d 693 (1974) (broadly defining the term "security"); Boddy v. Theiling, 129 Ga. App. 273, 199 S.E.2e 379 (1973) (emphasizing the duties of directors in corporate securities transactions).

55. For discussions of the 1973 Act, see Claxton, *supra* note 11, at 44; Trotter & Poe, *A Survey of the Securities Act of 1973*, 10 GA. ST. B.J. 219 (1973), and *A Survey of the Georgia Securities Act of 1973: Addendum*, 25 MERCER L. REV. 601, 625 (1974).

56. GA. CODE ANN., ch. 22-19 (1977).

57. GA. CODE ANN., tit. 22 (1977).

58. GA. CODE ANN. §22-1902 (1977).

Included in the information which the offeror must set forth in the registration statement are the following items: identification of all persons who fit the definition of offeror;[59] a statement of any beneficial interest in the equity securities of the offeree company held by the offeror, its officers and directors, and any associates thereof;[60] the source and amount of funds to be used in acquiring any equity securities of the offeree company; a statement of any plans to make material changes in the business, corporate structure, management, or personnel of the offeree company; all material facts regarding any existing or proposed contracts, arrangements, or understandings which the offeror has with any person with respect to the takeover bid; all material information concerning the organization and operations of a corporate offeror; an up-to-date balance sheet; and copies of all written materials to be used in connection with the takeover bid. The legislation also has a strong civil liability section,[61] as well as serious criminal penalties in the event of a willful violation of the chapter.[62]

The chapter on corporate takeovers is a vital addition to the Georgia Corporations Code and can only serve to improve what was already a good set of statutes for the regulation of the activities of corporations.

59. For the definition of offeror *see* GA. CODE ANN. §22-1901(c) (1977).
60. For the definition of associate *see* GA. CODE ANN. §22-1901(d) (1977).
61. GA. CODE ANN. §22-1913 (1977).
62. GA. CODE ANN. §22-1912 (1977).