TEXAS LAW ON DISSOLUTION OF ENTITIES

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TEXAS LAW ON DISSOLUTION OF ENTITIES

I. INTRODUCTION

In the current market conditions of the energy markets that are significant contributors to the economy of this state, the next few years will have to necessarily focus on "downside" issues of entity formation – namely insolvency and dissolution. This paper will focus on the statutory and case law in Texas concerning the dissolution of entities, in particular the "filing entities," corporations, LLCs and limited partnerships (I am going to skip over general partnerships). I will start with the statutory rules and procedures, to review the rules and procedures for the process, along with a discussion of what is "not there" in the statute (especially in comparison to other states), and follow with the glosses to the statutory rules that have been added by case law. At the end, I hope you will have an excellent technical grasp of the process of dissolving an entity.

II. STATUTORY PROCESS – THE "HUB" PROVISIONS

A. TBOC Structure.

In the TBOC, the "HUB" sections of the TBOC contain provisions for the dissolution process that are common to all filing entities. Naturally, there are specific rules for each type of entity in both the main "H**UB**" TBOC section, as well as in each "Spoke" TBOC Section applicable to the specific entity. The "Hub" TBOC provision on dissolution is Section 11, which contains the requirements for winding up of the entity, filing the Certificate of Termination and matters concerning procedures and rights during the winding up and termination process.

B. Timing of the Process under the TBOC.

The kernel of the process of winding up and terminating a filing entity in Texas is set forth in Section 11.052, "Winding Up Procedures." In Texas, an entity must conduct its winding up process prior to filing the Certificate of Termination. The statute §11.052(a)(1) requires that the filing entity to:

i. Cease doing business, except to the extent necessary to wind up;
ii. Send a written notice to each known claimant of the winding up (except for a general partnership);
iii. Collect and sell its property, to the extent the property is not to be distributed in kind; and
iv. Perform and other act required to wind up its business.

The timing of the winding up process requires that the creditors and related claimants be dealt with prior to any filing with the Secretary of State of the State of Texas.

C. Events Requiring a Winding Up.

Under §11.051, the process of winding up and termination may be voluntary, may be an event or a time specified in the governing documents, or may result from action instituted (a) the Secretary of State, (b) the courts, through a process with the Attorney General of the State of Texas, or (c) the provisions for charter forfeiture in the Texas Tax Code. Most importantly, for the claims process, the forms of involuntary forfeiture (Secretary of State, Attorney General and Tax Code) are governed by the same procedures and result (at least with respect to the filing entity) in the same results as a voluntary termination, or termination in accordance with the provisions of the governing documents. *Landrum v. Thunderbird Speedway, Inc*., 97 SW 3d 756, 758-759 (Tex App – Dallas 2003, no pet.).

D. Discharge of Liabilities and Obligations – Prior to the filing of the Certificate of Termination.

Under §11.053, there are two provisions for dealing with the discharge of liabilities in the winding up process. First, under §11.053(a), if the assets are sufficient, they shall be applied to discharge all liabilities. While paying the pending accounts receivable is obvious, contingent or unliquidated obligations may prove more difficult. Second, under §11.053(b), there is a provision concerning resolution of claims when the "property of the domestic entity is not sufficient to discharge all of the domestic entity's liabilities and obligations." Under this provision, the filing entity is to apply its property "to the extent possible to the just and equitable discharge of its liabilities and obligations, including liabilities and obligations to its owners or members, other than for distributions." In *Siegel v. Holliday*, 663 SW2d 824, 826 (Tex. 1984), the Texas Supreme Court in dicta said that it assumed this language meant pro rata. The Court noted that "statutes existing since 1871 have been interpreted as requiring a defunct corporation to make a pro rata distribution of assets to creditors."[1] The court went on to say, however, that the change to "just and equitable" when the TBOC was adopted in 1955 may give a dissolved entity more flexibility.[2]

[1] 663 SW2d at 831, note 1.
[2] *Id*.

i. Strategies for Unliquidated or Contingent Liabilities.

On an elementary level, it is possible to establish a fund or a trust for the unliquidated creditors to have a source of payment for their claims. See II D, below.

ii. Escheat.

The TBOC dissolution provisions also invoke the Texas provisions concerning escheat to the State Comptroller, §11.354, which is a provision that is useful if you have an amount that is certain, but cannot locate the creditor.

iii. Accelerated Procedure for Existing Claims.

The TBOC provisions also have an "Accelerated Procedure for Existing Claims," §11.358. Under this provision, you may shorten the statutory period (three years) for claims resolution by sending a specified form of notice. If the claimant agrees and accepts, you are done. If they do not, the dissolving entity may "reject" and if the claimant does not respond (seem highly unlikely in the circumstances), then again you are done. If the claimant agrees or fails to respond, the procedure takes 180 days. If the claimant disagrees, you at least have set the stage for a "resolution," likely litigation or more hopefully a mediation and settlement.

This accelerated procedure only applies to "existing claims" which are defined in §11.001(3) to be claims that existed before the entity's termination and not barred by a statute of limitations (so what would a claim about the viability of a statute of limitations defense be???), or a contractual claim (not a tort claim) that arises any time three years after the termination. *Anderson Petro-Equip, Inc. v. State of Texas*, 317 SW 3d 812 (Tex App. – Austin 2010, pet denied). §11.00 (i) defined 'Claims" as a "right to payment, damages or property, whether liquidated or unliquidated, accrued or contingent, matured or unmatured." As a result, if there are any allegations of liabilities that exist prior to or during the winding up process, they are likely to be "existing claims." See Section V, below, for a discussion of the details about those provisions that have been established about the claims process.

E. Handling contingent assets or liabilities.

A dissolving entity may have either assets or liabilities that are contingent or uncertain as to final amount at the time of dissolution. A common technique for handing either contingent assets or contingent liabilities is a liquidating trust. If this technique is used, the dissolving entity establishes a trust to hold the contingent assets or to hold cash to discharge the contingent liabilities. The beneficiaries of the trust will be the owners of the dissolving entity—to the extent of any residual assets in the case of a trust established to handle contingent liabilities. A liquidating trust must be established in a certain way so as to avoid it being classified as a taxable entity. Treasury Regulation § 301.7701-4(d) provides that a liquidating trust will be treated as a trust, and therefore not taxable, if—

> [I]t is organized for the primary purpose of liquidating and distributing the assets transferred to it, and if all its activities are all reasonably necessary to, and consistent with, the accomplishment of that purpose. A liquidating trust is treated as a trust for purposes of the Internal Revenue Code because it is formed with the objective of liquidating particular assets and not as an organization having as its purpose the carrying on of a profit-making business which would normally be carried on through business organizations classified as corporations or partnerships.

The IRS provided some guidance on liquidating trusts in Private Letter Ruling 2012244004. In that ruling, a limited partnership (the "LP") sold all its assets and terminated its business activities. The LP desired to distribute the sale proceeds and dissolve, but it had two significant contingent liabilities that might be asserted against it.

The LP established a liquidating trust with an affiliate of its general partner as trustee (the "Trustee"). The trust agreement authorized the Trustee to resolve the contingent liabilities by payment, defense, or compromise, to invest the assets of the trust in short-term investments (subject to several limitations) and to perform administrative tasks. The trust agreement explicitly prohibited the Trustee from making investments other than short-term cash equivalents, from retaining cash in excess of an amount reasonable necessary to provide for the contingent liabilities, and from holding assets such as publically-traded stock or partnership interests. The trust's term was three years, and the taxpayer represented that the three-year term was selected to match the statute of limitations applicable to the contingent liabilities. However, the Trustee was authorized to extend the term if a claim was asserted during the three-year period and more time was need to resolve it. However, the trust agreement provided that in no event would its term be extended past five years from the date it was established, Upon termination of the trust, all of its remaining assets would be distributed to the partners of the LP.

The IRS granted several favorable rulings, including:

- The trust would be classified as a liquidating trust; and
- The trust would be treated as a grantor trust for federal income tax purposes, meaning that any taxable income it had would be taxable to the beneficiaries.

The IRS has established conditions under which a ruling will be issued that a trust is a liquidating trust in Rev. Proc. 82-58, 1982-2 C.B. 847, as amplified by Rev. Proc. 91-15, 1991 C.B. 484, which includes a checklist for requesting a ruling on a trust that it is intended to be a liquidating trust.

F. The Certificate of Termination.

The statute, §11.101 has mandated information for the Certificate of Termination that may be filed after the winding up process. Rather than regurgitate the list in the statutory provision, I recommend that you google the Secretary of State's website to obtain the WORD or pdf version the form of Certificate of Termination from the Secretary of State that has the mandated information. I also commend to your review the commentary that accompanies the form concerning the procedures and rules followed by the Secretary of State in accepting Certificates of Termination for filing. Unless otherwise provided in the certificate, the Certificate of Termination is effective upon filing, §11.102.

Texas, like all other states, requires that before you exit the filing system that the filing entity satisfy its franchise tax obligations. This is evidenced by a special form of good standing certificate issued by the Comptroller certifying that taxes have been paid sufficient to allow for dissolution (or merger or other transaction where the entity may leave the state's system). This certificate may only be obtained upon the acceptance by the Comptroller (which usually requires a tax payment) of a final franchise tax return, which is not, generally, a simple matter. It can be further complicated if the entity dissolving has been filing as part of a combined group for Texas Franchise Tax purposes. This is an area where significant advance planning is required, because the completion of the final tax return is regularly a complicated process.

G. Three Year Period after the Certificate of Termination is Filed.

Once the Certificate of Termination has been filed, there is a three year transition period before the filing entity is completely extinguished. Under §11.356, the terminated entity has a limited life, in that claimants may raise "Existing Claims," which was defined above, and which includes claims pending (contingent and unliquidated claims are specifically enumerated) prior to the filing of the Certificate of Termination, or claims on contracts that entered into during this three year transition period. Once the Certificate of Termination is properly filed, new tort claims a barred. *Landrum v. Thunderbird Speedway, Inc*., 97 SW 3d 756 (Tex App – Dallas 2003, no pet.). Similarly to the period of the winding up, the authorized activities of the terminated entity are restricted to prosecuting or defending claims brought against the entity, permitting the survival of an existing claim by or against the terminated filing entity, holding title to or liquidating property of the terminated entity, applying or distributing property or otherwise settling affairs not completed prior to termination. To the extent after the three year period that the entity continues to be involved in any actions on "existing claims," its existence for that purpose will continue until resolution of such claims.

H. Governing Persons during the Three Year Limited Survival Period.

Once the Certificate of Termination has been filed, the governing persons of the terminated entity that were the governing persons before the filing will continue in their capacities thereafter, as may be affected by death or resignation. The governing persons, however, can replace themselves, so that no owner/member vote is required to replace a governing person, §11.357. The governing persons serve during this post filing period with the same authority (as limited by the limited purposes of a terminated entity) and subject to the same duties that were in place prior to the termination.

I. Reinstatement.

During the three years after the filing of the Termination, the filing entity may be revived through reinstatement. The most common reason for reinstatement is the forfeiture of a charter for failure to pay taxes or make required filings (e.g. Annual Reports). Reinstatement is also used when the filing entity needs to execute a conveyancing document (e.g. real estate deed or assignment of oil and gas lease) that was missed in the dissolution process. There are two important details of note, as follows: (1) reinstatement may only occur in the three years after the filing of the Certificate of Termination, and (2) if the filing entity has lost its name, it has to formally file an amendment to reinstate under a different name.

Reinstatement requires the same "levels" of approval as were required for winding up and termination (e.g. shareholder vote, member vote, general partner approval). While there are the usual requirements for the contents of the certificate filed for the reinstatement, there is a requirement for a tax clearance letter from the comptroller to certify that the filing entity has paid all the franchise taxes it owes.

III. SUPPLEMENTAL PROVISIONS – THE "HUB" AND "SPOKE" PROVISIONS FOR EACH TYPE OF ENTITY.

Each form of entity governed by the TBOC has supplemental provisions applicable to that particular entity form in two locations in the TBOC, first in Section 11, the "HUB" and second in each section affecting the particular type of entity. Set forth below are the provisions and their respective citations for each juridical entity.

A. Corporations.

The Section 11 "HUB" provision governing dissolution of corporations is §11.059, that provides that an event that requires a winding up (this is a reference to §11.051(3)) may be contained in each of the Certificate of Formation or a bylaw, provided that the bylaw was adopted by approval of the shareholders.

§§21.501 through 504, are the "Spoke" provisions that specifically govern dissolutions of corporations. These provisions concern the shareholder approval process for the winding up and dissolution, and the related processes of reinstatement or cancellation or revocation of a voluntary decision to wind up. The quick summary of the rule is that, unless you have provided to the contrary in accordance with the TBOC provisions concerning non-unanimous consents, a written consent to dissolve (reinstate, revoke, cancel) requires a unanimous vote, and if you use the shareholder meeting process, there must be a formal board of directors approval, and the matter put to a vote in a shareholders meeting, where (in accordance with the rules in §11.364) it may be adopted by a vote of 2/3s of the outstanding shares (unless the required percentage vote, again, has been altered by the Certificate of Formation). §11.504 provides that the Board of Directors will manage the process of winding up and dissolution (see §11.357 concerning how to manage any changes in personnel during the process).

B. Limited Liability Companies.

§11.056 is the "HUB" provision applicable to LLCs, and it contains the provisions about the ability to continue an LLC without a member. As you will recall, LLCs are a hybrid entity, and as an entity that is taxed as a partnership, has to deal with the issue of "no partners." Accordingly, if an LLC has no members, it must wind up and dissolve. §11.056 establishes a ninety day mechanism that gives successors in interest to members a period of time to properly to assign the membership interest and become a de facto member to forestall the termination of the LLC. The Texas provision, however, has a statutory defect, cured by Delaware. Under Texas law, if a member transfers its interest, the transferee is only an assignee of the interest unless and until that Member is admitted to the Company as a member. That may prove to be difficult in the event of the death of a sole member. Delaware law cures this issue by providing that if you transfer your interest, you cease to be a member with respect to the interest transferred, which means the transferee becomes the member with respect to that interest, not an assignee. § 18-702(b)(3) of the Delaware LLC Act. Obviously, in both Delaware and Texas, these issues may be both fixed or circumvented by the LLC Agreement, so that the Delaware provision is a default rule.

In the "Spoke" provisions, §§101.551 and 552 provide the rules for the governing persons eligible to wind up the LLC, and the requirements for owner approval of the winding up and dissolution. For an LLC, because of the flexibility of the management arrangements, the TBOC simply provides that the "governing authority," or persons or persons designated by the governing authority may conduct the process. The TBOC has defined "governing authority" to include the various permutations of management structures available to an LLC. §101.551 also included provisions concerning (1) who is authorized to wind up an LLC that has no members, when the successors have determined to not continue, and (2) the authority of a court appointed representative. Section 101.552 provides the rule for approval of the process, which is unanimous, unless the LLC agreement provides to the contrary.

C. Limited Partnerships.

§11.058 is the "HUB" provisions for limited partnerships, and it provides for the unanimous written consent of all partners of a limited partnership to approve a winding up and termination (unless provided to the contrary in the partnership agreement), and is the place concerning the rules requiring that the withdrawal of a general partner, or the elimination of all limited partners of a limited partnership are events requiring a winding up and termination of the limited partnership (unless provided to the contrary in the partnership agreement).

The "Spoke" provisions are found in §§153.501-505 which contain the rules specific to limited partnerships concerning the rules to continue in a limited partnership if the entity loses its general partner, which is like the LLC provision that gives the remaining partners 90 days to determine to continue and make sure that there is at least one general partner. Additionally, it is much more common for limited partnerships to have a term or a specified purpose, and events related to each (time limit passed, or purpose fulfilled) is an event that would require a winding up under the Hub provision of §11.051. As a result, §153.501 has rules for continuing, and similarly, for revoking a winding up that has commenced.

IV. LIABILITY OF A TERMINATED FILING ENTITY.

A. In General - Statutory Provisions.

The TBOC has an express provision that states that a terminated entity is liable only for "existing claims." §11.351. Once again, "existing claim" is expressly defined in §11.001(3) as a "claim that existed before the termination of the entity and is not barred by limitations, or a contractual obligation incurred after termination." First, termination occurs when the Certificate of Termination is properly filed. §11.102. Next, recall that the Certificate of Termination is not to be filed until after the winding up period. Once the determination has been made to wind up (and that is an issue that does require a vote of owners, see Section III above for the rules on numerosity), Section 11.052 prescribes those limited activities that may be conducted during this time. In theory, by the time that the business has been wound down, the statutory structure anticipates that no new business would have been commenced, and that the assets and income has been collected and distributed to pay known claims, and that reserves for contingent or unknown claims have been created, or that the accelerated process for liquidating claims has been undertaken. Thus, the statute contemplates that as you file the Certificate of Termination, you have paid your bills and provided a reserve for those bills not liquidated, and the remainder may be distributed to owners, who may "ride off in to the sunset."

Notwithstanding, once the Certificate of Termination is filed, there is a three (3) year period for claimants to come forward, either because they were not known, or they subsequently dispute the payment or provision in payment made to them. Under case law, any distribution to shareholders is returnable to the creditors during this three year period if there is a claim that was not adequately resolved, or for contract claims that could arise after the Certificate of Termination pursuant to the powers of the governing persons in effect during the three years after the filing of the Certificate of Termination. Unlike Delaware, 8 Del. C. §282, Texas has no express statutory provision on the limits of liability for shareholders to the amount distributed to them, and relies on case law, and related laws of fraudulent conveyance. The rules concerning distributions from entities (i.e., dividends) expressly do not apply to distributions upon termination under Chapter 11, §21.303(b), §153.210(a) and §101.206(a).

B. Forfeiture Under Tax Code.

In addition to the rules concerning the obligations of an entity in dissolution, the Texas Tax Code adds a layer of personal liability for officers and directors of entities that are dissolved through this administrative proceeding. The Texas Tax Code §§ 171.251, 2515(b) provide for the forfeiture of a corporation's corporate privileges or the forfeiture of the right to transact business in Texas of other "taxable entities." A taxable entity includes partnerships (with some exceptions) and LLCs. If a forfeiture for franchise tax occurs, Tax Code § 171.255 provides that each director or officer of the corporation is liable "for each debt of the corporation that is created or incurred in this state after the date on which the report, tax, or penalty is due and before the corporate privileges are revived. Tax Code § 171.2515(b) makes § 171.255 applicable in the case of the forfeiture of a taxable entity's right to transact business in Texas.

Case law is instructive on how the franchise tax provisions fit in with the state entity law provisions on liabilities in the dissolution process. In *Landrum et al. v. Thunderbird Speedway, Inc.*, 97 SW 3d 756 (Tex. App – Dallas 2003), an accident killed a man at Thunderbird Speedway, Inc. on June 22, 1996. The corporation had forfeited its charter under the Tax Code on February 14, 1995. The appeals court upheld a summary judgment in favor of the corporation, reasoning that the accident occurred after dissolutions, and therefore was not an existing claim. This case did include or discuss the issue of the personal liability of any officer or director.

In *Jonnet v. State*, 877 SW2d 520 (Tex. App. Austin 1994), the court held that the directors of a dissolved corporation were liable for penalties assessed against the corporation for failure to plug abandoned oil wells. The corporation had notice, as operator of record that it was not in compliance with Texas Railroad Commission rules in December 1989. The corporation forfeited its charter for failure to pay taxes in June 1990. The Railroad Commission commenced its proceedings in 1990 and obtained judgment against the corporation and its officers, personally. The Court of Appeals upheld the judgment. In an interesting twist, the court found that although the debt was pre-existing at the time of the forfeiture, Section 81.0531 of the Natural Resources Code characterizes each day that a violation continues as a separate violation for purposes of penalty assessments, and therefore the liabilities were incurred after the forfeiture.

With a similar result to *Jonnet*, above, in *Anderson Petro-Equipment, Inc. v. State of Texas*, 317 SW 3d 812 (Tex App – Austin 2010), the president of a corporation was held liable for costs and penalties for failing to properly plug wells. Anderson Petro-Equipment, Inc. forfeited its charter on October 13, 2004 for failure to pay franchise taxes. The Texas Railroad Commission entered three separate orders for failure to properly plug will on May 11, 2004, October 4, 2005 and April 11, 2006. The appellate court affirmed the district court's holding that the corporation was liable for all three judgments, and that the president was personally liable for the two judgments that were entered after the date of the

forfeiture (no mention of the tax code provision cited in *Jonnet)*. The court reasoned that the claims were contingent claims at the time of forfeiture, since the corporation had notice of these violations beginning in 2002, and therefore the claims did not "arise" after the forfeiture.

In *Macyoti Corporation v. Sea Oats Investments IV, LP*, No. 13-10-00010-CV (Tex. App. Corpus Christi-Edinburg, August 23, 2011), the appellate court reversed a summary judgment award against officers of a corporation, stating that there was a question of fact whether a liability under a letter agreement was created or incurred when it was entered into on August 16, 2007. The corporation had forfeited its charter for failure to pay franchise taxes on August 9, 2009. Although it is not clear from the court's opinion, the parsing of the case would indicate that the issue was whether the liability arose on execution of the contract, or on the date it was breached.

V. CASE LAW ON DISSOLUTIONS – GENERALLY.

Understandably, there is a body of case law exploring the liabilities remaining after the dissolution of an entity. Cases focus on the passage of the three (3) year period and types of claims that have arisen after the completion of the three years, in attempts to circumvent the TBOC by other federal, state or constitutional provisions. Of course, I find that the case law is a little muddled, and bears some analysis to understand the potential litigation risks of the process of dissolution. The core issue litigated is the ability of creditors of an entity after dissolution to reach officers, directors and equity owners of the dissolved entity. Apart from the statutory provisions discussed above, common law doctrines have been applied over the years to permit creditors redress against shareholders of dissolved corporations. The primary equitable theory is called the "trust fund doctrine," which was equitable relief that permitted creditors to trace assets of the dissolved corporation in the hands of former shareholders and impress a trust, or an "in rem" liability on the shareholders to the extent of the value of the assets distributed to them in liquidation. This theory is not a theory of personal liability, as much as a theory to permit the tracing of assets in the hands of former shareholders.

A reading of the existing statutory provisions, as well as the antecedents to the TBOC, demonstrate that the legislature was intent on revising the open ended nature of shareholder liability to the current three year liability for existing claims and contract claims incurred after filing the Certificate of Termination. As is not surprising, lawsuits are filed alleging this equitable theory notwithstanding the express statutory provisions.

For example, as is evident by the cases arising with respect to forfeitures for failure to pay franchise taxes, the single most litigated issue is when the cause of action arose, and whether a liability that was liquidated and became fixed in time and amount after the Certificate of Dissolution was in fact an "existing liability" because it was a contingent claim prior to the Certificate of Dissolution. The tax cases set forth above consistently hold that claims that are contingent prior to dissolution that are liquidated within the three years thereafter are existing claims for which there is recourse, although in the tax cases, the recourse is against officers and directors, not shareholders. The full amount of the liability is assessed against the officers and directors personally under a tax dissolution. This is to be distinguished from the "in rem" theory of the trust fund doctrine that only holds shareholders liable to the extent of a distribution, and limited to the assets of the corporation. In this circumstance, the officers and directors are fully personally liable. Even though the persons held liable are not the same, the judicial reasoning on the definition of "existing claims" should be directly applicable outside the context of franchise taxes.

The "source" case explaining the liabilities of shareholders in dissolution is *Hunter v. Fort Worth Capital Corp*. 620 SW2nd 547 (Tex 1981). In this case, an elevator company installed an allegedly defective elevator in 1960. The corporation that installed it sold its assets and dissolved in 1964. In 1975, the elevator permanently injured a man when the hydraulic system failed and the elevator fell on top of him. The Supreme Court found that the common law trust fund doctrine had been supplanted by the then provisions of the Texas Business Corporations Act (largely the same as the TBOC), and that since the accident had occurred more than three years after the dissolution, there was no cause of action against the shareholders. Cases have generally upheld the TBOC provisions, although not with the clarity one would wish.

One question to note that will be interesting in the coming litigation from the oil patch recession are the cases that look at liability of shareholders that did not, in fact, receive distributions in liquidation. In *Siegel v. Holliday* 663 SW 2nd 824 (Texas 1984), creditors were denied their claims against shareholders, who dissolved a corporation after it had failed, and had, in fact, personally paid some creditors in excess of the assets of the corporation. Similarly, in *Angus v. Air Coils, Inc.* 567 SW 2nd 931 (Tex App – Dallas 1978), a creditor sued the sole shareholder, officer and director for an invoice that was not paid by a failed corporation. While the court held that the shareholder was protected by the corporate veil, it went on to add that since the shareholder did not in fact receive any distributions, there were not assets on which to impress the trust for

the benefit of the creditors. As importantly, the fact that the shareholder had forgotten to send the notices to creditors required in dissolution did not give rise to an action severe enough to constitute fraud for a veil piercing argument. The Fifth Circuit, based on the Texas statute and case law, has also held that there must be evidence that assets were distributed to the shareholders to hold them liable. *North American Savings Association v. MetroFlex Development Partnership*, 931 F2d 1073, 1079 (5th Cir. 1991)

Further challenges to the TBOC provisions have arisen to question the applicability of the TBOC in light of statutes that permit minors an extended statute of limitations to sue for injuries under the Medical Liability and Insurance Improvement Act, and such challenges have failed to date. See: *Gomez v. Pasadena Health Care Mgmt* 246 SW3d 311 (Tex App Houston, 14th Dist, 2008, no petition). *Durham Clinic, P.A. v. Mittierene Jane Barrett, as Guardian,* 107 SW3d 761 (Tex App – Waco, 2003). Courts have generally held that the TBOC dissolution provisions "trump" the statutes concerning extensions of statutes of limitations. The reasoning is that under the TBOC provisions, the cause of action is completely extinguished. The cases label the TBOC provisions as "survival statutes," with the result that the cause of action goes away entirely, and distinguish that concept from a statute of limitations. A statute of limitations does NOT make the cause of action go away, it just says it is too late to prosecute the cause of action.

A related challenge to the TBOC provisions is under grounds based on the Texas constitution. Cases, including *Gomez*, above, have challenged the TBOC provisions on the grounds that the extinguishment of the cause of action by the TBOC violates Texas constitutional provision called the "Open Courts Provision." The cases argue that the TBOC cuts off access to the judicial system guaranteed by the Texas constitution. See: "A Vanishing Remedy: Questioning the Constitutionality of the Current State of Sale of Assets, Post-Dissolution Tort Liability in Texas, Matt Acosta, 60 Baylor Law Review 655, 2008. Most cases, again, have held that the Open Courts Provision does not serve to deny the terms of the TBOC. *Gomez,* supra, *Anderson v. Hodge Boats & Motors, Inc*. 814 SW2d 894 (Tex App. – Beaumont, 1991)

Finally, there are many cases where plaintiffs further allege other piercing arguments. Many cases include, in addition to the challenge under the trust fund doctrine, alter ego and veil piercing arguments. As a result, you will see confusion over the reasoning to hold shareholders or officers and directors liable. For example, as pointed out in *Angus*, above, the creditor alleged veil piercing and trust fund doctrine. My favorite of the confusing cases is *Smith v. Chapman*, 897 SW.2d 399 (Tex App, Eastland 1999), in which a corporation forfeited its charter, and the plaintiff sued the directors under the dividend provision of the TBCA. The court held that the directors were not liable because the statute of limitations for breach of fiduciary duty was two years, and the plaintiff had sued more than two years after the forfeiture. Suffice it to say, that fiduciary duties are not involved in either the trust fund doctrine, or director's liability for faulty dividends under the then TBCA or the current TBOC. If, however, you have potential veil piercing exposure, the case law on the TBOC provisions concerning trust fund theory will not be of any assistance in the instance of a fraud against a creditor of any entity. Also, remember there are both federal and state laws that have both personal liability for control persons and successor liability, including federal tax, federal securities, federal and state environmental, and so forth.

VI. CONCLUSION.

In light of the current economic conditions of the State of Texas, it is likely that there will be additional attention to the relevant Texas statutes and case law for those entities with failed businesses that simply need to be cleaned up and terminated. The statute is relatively clear, and absent successor liability issues such as a veil piercing argument, the path to dissolution is viable. The tax cases, and payment of franchise taxes due would also point to the efficacy of voluntary dissolution of an entity to avoid potential personal liability of officers, directors and correlative governing persons. You will also note, that the vast majority of cases cited in this paper are from the period of the early nineties, which were appeals from cases that derived from the circumstances of the last great drop in oil prices in the state of Texas. History would caution lawyers to be alert for further developments that are highly likely in turbulent economic times in this area of law.