

**PARTNERSHIP FORMATION LAW – DOES TEXAS LAW PERMIT CONTRACTUAL CONDITIONS  
PRECEDENT TO PRECLUDE PARTNERSHIP FORMATION?**

By Madison Hastings\*

*Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P.*, 593 S.W.3d 732 (Tex. 2020).

In *Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P.*,<sup>1</sup> the Supreme Court of Texas recently affirmed a decision of the Court of Appeals for the Fifth District of Texas, in which the Court of Appeals held Texas law permits parties to conclusively agree that certain contractual conditions must be satisfied before a partnership can form.<sup>2</sup> The Supreme Court of Texas’s opinion is significant because it instructs lower courts that an agreement not to be partners unless certain conditions are met will be conclusive on the issue of partnership formation as between the parties.<sup>3</sup> Importantly, before this opinion, the Court had never “squarely addressed whether parties’ freedom to contract for conditions precedent to partnership formation can override the statutory default test, in which intent is a mere factor.”<sup>4</sup>

Energy Transfer Partners, L.P. and Energy Transfer Fuel, L.P. (together, “ETP”) as well as Enterprise Products Partners, L.P. and Enterprise Products Operating LLC (together, “Enterprise”) are among the ten largest energy companies in the United States.<sup>5</sup> In 2011, Enterprise and ETP agreed to explore the viability of converting a pipeline called Old Ocean into one that would transport natural gas from Cushing, Oklahoma, to Houston, Texas.<sup>6</sup> In three separate written agreements, ETP and Enterprise expressed their intent that neither party would be bound to proceed without the execution of a formal contract approved by each company’s board of directors.<sup>7</sup> First, in a Confidentiality Agreement, signed in March 2011, ETP and Enterprise agreed:

[U]nless and until a definitive agreement between the Parties with respect to the Potential Transaction has been executed and delivered, and then only to the extent of the specific terms of such definitive agreement, no Party hereto will be under any legal obligation of any kind whatsoever with respect to any transaction by virtue of this Agreement or any written or oral expression with respect to such a transaction by any Party or their respective Representatives, except, in the case of this Agreement, for the matters specifically agreed to herein . . . .<sup>8</sup>

\* J.D. 2020 South Texas College of Law Houston.

<sup>1</sup> *Energy Transfer Partners, L.P. v. Enter. Prods. Partners*, 593 S.W.3d 732 (Tex. 2020).

<sup>2</sup> *Id.* at 734.

<sup>3</sup> *Id.* at 741.

<sup>4</sup> *Id.* at 739.

<sup>5</sup> *Id.* at 734.

<sup>6</sup> *Id.* at 734-35.

<sup>7</sup> *Id.* at 734.

<sup>8</sup> *Id.* at 734-35.

Second, in April 2011, ETP and Enterprise executed a Letter Agreement including a “Non-Binding Term Sheet” envisioning a “mutually agreeable Limited Liability Company Agreement would be entered into” to govern the joint venture.<sup>9</sup> The Letter Agreement stated:

[N]o binding or enforceable obligations shall exist between the Parties with respect to the Transaction unless and until the Parties have received their respective board approvals and definitive agreements memorializing the term and conditions of the Transaction have been negotiated, executed and delivered by both of the Parties. Unless and until such definitive agreements are executed and delivered by both of the Parties, either [Enterprise] or ETP, for any reason, may depart from or terminate the negotiations with respect to the Transaction at any time without any liability or obligation to the other, whether arising in contract, tort, strict liability or otherwise.<sup>10</sup>

Third, in April 2011, ETP and Enterprise also signed a Reimbursement Agreement providing the terms by which ETP would reimburse Enterprise for the cost of half of the project’s engineering work.<sup>11</sup> The Reimbursement Agreement stated ETP and Enterprise were “in the process of negotiating mutually agreeable definitive agreements” and that nothing should “be deemed to create or constitute a joint venture, a partnership, a corporation, or any entity taxable as a corporation, partnership or otherwise.”<sup>12</sup>

By May 2011, ETP and Enterprise began seeking sufficient shipping commitments.<sup>13</sup> The project was marketed to potential customers as a “50/50 JV.”<sup>14</sup> For the project to be viable, ETP and Enterprise needed shipping commitments of at least 250,000 barrels a day for ten years at a tariff of \$3.00 per barrel.<sup>15</sup> Initially, ETP and Enterprise were unable to secure these commitments.<sup>16</sup> They continued their attempts and on August 12, 2011, received a commitment for 100,000 barrels daily.<sup>17</sup> ETP hoped other commitments would follow, but Enterprise had already resumed negotiations with another entity and prepared to exit.<sup>18</sup> On August 15, 2011, Enterprise orally terminated its relationship with ETP.<sup>19</sup> A few days later, Enterprise confirmed this termination in writing.<sup>20</sup> Ultimately, Enterprise and another entity invested billions of dollars into the pipeline, now called “Wrangler.”<sup>21</sup> Wrangler opened in 2012, achieving great financial success.<sup>22</sup> ETP brought suit against Enterprise.<sup>23</sup>

<sup>9</sup> *Id.* at 735.

<sup>10</sup> *Id.*

<sup>11</sup> *Id.*

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

<sup>14</sup> *Id.*

<sup>15</sup> *Id.* at 736.

<sup>16</sup> *Id.*

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

<sup>21</sup> *Id.*

<sup>22</sup> *Id.*

<sup>23</sup> *Id.*

At trial, ETP argued that despite the disclaimers in the parties' written agreements, they formed a partnership through their conduct for the purpose of marketing and pursuing a pipeline.<sup>24</sup> Further, ETP argued Enterprise breached its statutory duty of loyalty by pursuing the Wrangler project with another entity.<sup>25</sup> The jury agreed with ETP, answering "yes" to whether "ETP and Enterprise [had] create[d] a partnership to market and pursue a pipeline project to transport crude oil from Cushing, Oklahoma to the Gulf Coast."<sup>26</sup> The jury further agreed that Enterprise breached its duty of loyalty to ETP.<sup>27</sup> The jury found ETP should recover \$319,375,000.00 in damages and that Enterprise should be disgorged of the benefit gained as a result of misconduct in the amount of \$595,257,433.00.<sup>28</sup> The trial court rendered judgment on the verdict in the amount of \$535,794,777.40 plus prejudgment interest (after reducing the disgorgement amount to \$150,000,000.00).<sup>29</sup>

The Court of Appeals reversed and rendered judgment for Enterprise.<sup>30</sup> The Court of Appeals held the Texas Business Organizations Code ("TBOC") allows parties to contract for conditions precedent to partnership formation.<sup>31</sup> Further, the Court of Appeals held the Letter Agreement created two unmet conditions precedent to partnership formation.<sup>32</sup> First, the Letter Agreement required the execution of "definitive agreements memorializing the terms and conditions of the Transaction."<sup>33</sup> Second, the Letter Agreement required that these definitive agreements receive each party's "respective board approvals."<sup>34</sup> The court concluded that because these conditions were unmet and ETP did not prove waiver of these conditions, ETP could not recover.<sup>35</sup> The Supreme Court of Texas granted ETP's petition for review.<sup>36</sup>

The Supreme Court of Texas agreed with the Court of Appeals' conclusion that the Letter Agreement imposed two unmet conditions precedent to the formation of a partnership between ETP and Enterprise, and that ETP failed to establish any waiver of these conditions.<sup>37</sup>

The Supreme Court of Texas began its analysis with TBOC § 152.051(b), providing "an association of two or more persons to carry on a business for profit as owners creates a partnership, regardless of whether: (1) the persons intended to create a partnership; or (2) the association is called a 'partnership,' 'joint venture' or other name."<sup>38</sup> The Court then discussed the non-exclusive factors indicating partnership formation under TBOC § 152.052(a),<sup>39</sup> emphasizing "'expression of

<sup>24</sup> *Id.*

<sup>25</sup> *Id.*

<sup>26</sup> *Id.*

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> *Id.*

<sup>30</sup> *Id.*

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

<sup>33</sup> *Id.*

<sup>34</sup> *Id.*

<sup>35</sup> *Id.* at 736-37.

<sup>36</sup> *Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P.*, 593 S.W.3d 732, 737 (Tex. 2020).

<sup>37</sup> *Id.* at 742.

<sup>38</sup> *Id.* at 737.

<sup>39</sup> TBOC § 152.052(a) ("Factors indicating that persons have created a partnership include the persons': (1) receipt of right to receive a share of profits of the business; (2) expression of an intent to be partners in the business; (3)

an intent to be partners in the business’ is just one factor within the totality-of-the-circumstances test.”<sup>40</sup> The Court highlighted the reality that pursuant to TBOC § 152.051(b), “persons can create a partnership regardless of whether they intend to.”<sup>41</sup> However, the Court then referenced *Ingram v. Deere*,<sup>42</sup> where it expressed skepticism that the Legislature “intended to spring surprise or accidental partnerships on independent business persons.”<sup>43</sup>

The Court turned to TBOC § 152.003, asserting, “[t]he principles of law and equity” are properly considered in the partnership-formation analysis.<sup>44</sup> The Court reasoned the “well-developed body of common law” strongly supporting parties’ freedom of contract, “decades older than the TBOC or its predecessor statute,” should govern.<sup>45</sup> In support of this notion, the Court emphasized, “perhaps no principle of law is as deeply engrained in Texas jurisprudence as freedom of contract.”<sup>46</sup>

Finally, the Court held parties can contract for conditions precedent to preclude the unintentional formation of a partnership because the Legislature did not intend parties to end up in surprise or accidental partnerships and TBOC § 152.003 expressly authorizes “principles of law and equity” such as freedom of contract to supplement the partnership-formation analysis.<sup>47</sup>

The Court concluded, as a matter of law, ETP and Enterprise did not create a partnership because the conditions precedent in their contract remained unmet.<sup>48</sup> The Court went on the hold these conditions precedent could be waived or modified by word or deed of the party to whom the obligation was due.<sup>49</sup> However, ETP did not provide any evidence that Enterprise specifically disavowed or acted inconsistently with the Letter Agreement’s requirement of definitive, board-of-directors-approved agreements.<sup>50</sup> Therefore, ETP provided no evidence of waiver of the conditions precedent.<sup>51</sup>

participation or right to participate in the control of the business; (4) agreement to share or sharing: (A) losses of the business; or (B) liability for claims by third parties against the business; and (5) agreement to contribute or contributing money or property to the business.”).

<sup>40</sup> *Energy Transfer Partners, L.P.*, 593 S.W.3d at 737.

<sup>41</sup> *Id.* at 737-38 and nn.12 & 13 (noting comment 1 to the Revised Uniform Partnership Act § 202(a), serving as the basis for the relevant TBOC provisions, provides parties “may inadvertently create a partnership despite their expressed subjective intention not to do so.”).

<sup>42</sup> *Ingram v. Deere*, 288 S.W.3d 886 (Tex. 2009).

<sup>43</sup> *Energy Transfer Partners, L.P.*, 593 S.W.3d at 738.

<sup>44</sup> *Id.*

<sup>45</sup> *Id.*

<sup>46</sup> *Id.* at 740.

<sup>47</sup> *Id.*

<sup>48</sup> *Id.*

<sup>49</sup> *Id.* at 741.

<sup>50</sup> *Id.*

<sup>51</sup> *Id.* at 742.