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SURVEY ARTICLES

Business Associations

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This Article surveys recent developments in Georgia’s corporate, securities, partnership and banking law. It covers noteworthy cases decided during the survey period¹ by the Georgia appellate courts, United States district courts located in Georgia, and the Eleventh Circuit

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¹ The survey period is June 1, 1999 through May 31, 2000.
Court of Appeals. Also included in this Article are highlights of recent revisions to the Official Code of Georgia Annotated ("O.C.G.A.").

I. CORPORATIONS

A. Piercing the Corporate Veil

A corporation is a legal entity separate from its shareholders, officers and agents. The corporation's owners and managers act as mere agents of the corporation and are not personally liable for the corporation's debts. However, this so-called corporate shield is not impenetrable; it may be pierced. In determining whether to pierce the corporate veil, the most fundamental analysis focuses on whether the corporate structure has been so abused that injustice can only be avoided by holding the agents of the corporation liable for its debts. More often than not, Georgia courts did not pierce the corporate veil when presented with the issue during this survey period. However, the courts pierced the corporate veil under circumstances in which the corporation's officers or directors paid for their own personal apartments with corporate funds, commingled funds, and personally collected insurance proceeds for damages specifically caused by the officer making the claim. Notwithstanding the continued proliferation of veil-piercing claims, the Georgia courts have failed to provide concrete guidance for evaluating disparate factual situations. The courts have continued to use a variety of theories to justify piercing the corporate veil, including alter ego, apparent or ostensible agency, fraud, abuse, and joint venturer. As a result, appellate review has been inconsistent, and potential appellants are more apt to try their fortune at the appellate level.

Courts generally frame the issue of piercing the corporate veil as whether the corporation is the alter ego or business conduit of its shareholders. The main inquiry does not focus on the composition of

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2. See generally Jerome L. Kaplan et al., Kaplan's Nadler, Georgia Corporations, Limited Partnerships and Limited Liability Companies § 3-4 (1999).
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corporate ownership or control because, under Georgia law, a corporation and its shareholders or officers are separate entities even if wholly owned and controlled by a sole shareholder. To pierce the corporate veil in Georgia, a plaintiff must show the following: (1) that the shareholder's disregard of the corporate entity made the corporation a mere instrumentality for the transaction of the shareholder's own affairs; (2) that there is such unity of interest and ownership that the separate personalities of the corporate form and the shareholder or officer cease to exist; and (3) that to adhere to the doctrine of a separate corporate entity would promote injustice or perpetrate fraud. More specifically, before a veil-piercing claim is submitted to a jury, courts will require substantive evidence demonstrating that the corporate arrangement represented simply a sham used "to defeat justice, to perpetuate fraud, or to evade statutory, contractual or tort responsibility."  

1. Court of Appeals of Georgia Affirms Grant of Summary Judgment and Provides Review of Georgia Law. The controversy in Clark v. Cauthen began in 1987 as a result of an automobile accident. Carolyn Clark (formerly Carolyn Tibbs) brought suit against Studebaker's of Savannah, Inc. ("Studebaker's"), seeking damages she incurred in a head-on collision with Janice Carter, a patron of Studebaker's. Because the accident occurred within fifteen minutes after Carter departed Studebaker's and because Carter was allegedly intoxicated at the time of the collision, Clark sought to hold Studebaker's liable for Carter's negligence. A jury returned a verdict in favor of Clark in the amount of $250,000 and against Carter and Studebaker's jointly and
The court of appeals affirmed the verdict and certiorari was denied. Unable to collect on her judgment, Clark initiated suit against Victor Cauthen, a former shareholder and owner of Studebaker's, in an effort to pierce the corporate veil and collect against him personally. The trial court granted summary judgment in favor of Cauthen, and Clark appealed.

The Court of Appeals of Georgia reiterated principles of corporate law rooted in the nineteenth century: "[E]ach corporation is a separate entity, distinct and apart from its stockholders, and insulation from liability is an inherent purpose of incorporation." Adhering to these principles, Georgia courts are reluctant to disregard the corporate structure and hold individual stockholders liable for any corporate debt. In determining whether to pierce the corporate veil, Georgia courts have long upheld the following: "Sole ownership of a corporation by one person or another corporation is not a factor, and neither is the fact that the sole owner uses and controls it to promote his ends. There must be evidence of abuse of the corporate form." This abuse is not determined by any rigid formula although certain abuses may be more condemning than others.

The record showed that "Cauthen sold his interest in Studebaker's to a corporation that had been administratively dissolved, received a $20,000 loan from Studebaker's that was later characterized as salary, and forgave royalty payments that were to be paid [to] him." However, the acts were justified, and none of these facts resulted in, or resulted from, a disregard for the legal entity. The court found that Cauthen was not aware of the administrative dissolution, that the $20,000 loan "was consistent with Studebaker's usual practice regarding the owner's compensation," and that forgiveness of the royalty payments "did not affect Studebaker's financial condition."

While Clark amassed a record ripe with "questionable behavior, inaccurate information and inconsistent testimony," she produced no evidence "of triable jury issues which would result in the corporate veil being pierced." In veil-piercing claims, summary judgment is only appropriate "if no evidence exists that shows, or from which it might be

13. Id. at 142, 392 S.E.2d at 908.
14. 239 Ga. App. at 226, 520 S.E.2d at 479.
15. Id. at 227, 520 S.E.2d at 479 (citations omitted).
16. Id. (citing Fuda v. Kroen, 204 Ga. App. 836, 837, 420 S.E.2d 767, 768 (1992)).
17. Id. at 226, 520 S.E.2d at 479.
18. Id. at 228, 520 S.E.2d at 480.
19. Id. at 228-29, 250 S.E.2d at 480.
inferred, that 'the corporate arrangement was a sham, used to defeat justice, to perpetuate fraud, or to evade statutory, contractual or tort responsibility.' As a result, the court of appeals found no error and affirmed the superior court's grant of summary judgment.

2. Application of the National Labor Relations Act Obligated the Eleventh Circuit to Apply Federal Law in Lieu of State Law Regarding Piercing the Corporate Veil. In National Labor Relations Board v. West Dixie Enterprises, Inc., the International Brotherhood of Electrical Workers filed a charge of unfair labor practices against West Dixie Enterprises, Inc. ("West Dixie"), which prompted the National Labor Relations Board ("NLRB") to conduct an investigation of the matter. Following its investigation, the NLRB filed a complaint against West Dixie based on violations of sections 8(1) and 8(3) of the National Labor Relations Act ("NLRA"). The NLRB subsequently added West Dixie's owner, sole shareholder and president, Carole Paolicelli, and her husband, Paul Paolicelli, West Dixie's director of operations, as defendants because the NLRB believed that "the Paolicellis were alter egos of West Dixie and were therefore also liable for the violations." Congress intended for the scope of the NLRB's statutory jurisdiction to be broad. "In passing the [NLRA], Congress intended to and did vest in the [NLRB] the fullest jurisdictional breadth constitutionally permissible under the Commerce Clause." As a practical matter, it is easiest to determine whether jurisdiction is present under the NLRA by using the following test: "[J]urisdiction exists when gross interstate inflow (purchases) or outflow (sales), whether direct or indirect, exceeds $50,000.00 [in a one-year period]." West Dixie did not contest that it made purchases in excess of $50,000 during 1994 and that the alleged violations took place in 1994. Therefore, the Eleventh Circuit Court of Appeals held that the NLRB appropriately exercised its jurisdiction over West Dixie and the Paolicellis, but from a purely corporate perspective, the intriguing aspect of this case rests in the NLRB's application of the NLRA to pierce the corporate veil.

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20. Id. at 228, 520 S.E.2d at 480 (quoting J & J Materials, 214 Ga. App. at 65, 446 S.E.2d at 783).
21. Id. at 229, 520 S.E.2d at 481.
22. 190 F.3d 1191 (11th Cir. 1999).
24. 190 F.3d at 1193.
25. Id. (quoting NLRB v. Reliance Fuel Oil Corp., 371 U.S. 224, 226 (1963)).
26. Id. (quoting NLRB v. Jerry Durham Drywall, 974 F.2d 1000, 1002 (8th Cir. 1992)).
27. Id.
The Paolicellis argued that under applicable state law veil-piercing theories, they would not be personally liable for the NLRA violations.\(^{28}\) However, the NLRB refused to apply state law and instead applied "the Tenth Circuit's two-pronged test for determining whether owners or operators of a corporation are personally liable for the unfair labor practices of the corporation."\(^{29}\) Under the Tenth Circuit's test:

> the corporate veil may be pierced when: (1) there is such unity of interest, and lack of respect given to the separate identity of the corporation by its shareholders, that the personalities and assets of the corporation and the individuals are indistinct, and (2) adherence to the corporate form would sanction a fraud, promote injustice, or lead to an evasion of legal obligations.\(^{30}\)

The first prong required the NLRB to consider "(a) the degree to which the corporate legal formalities [had] been maintained, and (b) the degree to which individual and corporate funds, other assets, and affairs [had] been commingled."\(^{31}\) According to the record, "[t]he Paolicellis often used personal checks or credit cards to pay for West Dixie's supplies and payroll . . . [and] produced no records indicating that any of [the] payments were bona fide loans or repayments, or that the individual and corporate entities were kept separate."\(^{32}\) While a failure to maintain adequate records may have justified piercing the corporate veil alone, the discovery of commingled funds provided an even stronger case.\(^{33}\)

Moreover, the second prong provided a strong policy-based argument that to find the Paolicellis not personally liable "would sanction a fraud, promote injustice, or lead to an evasion of legal obligations."\(^{34}\) The Paolicellis "[paid] rent on Mr. Paolicelli's personal apartment for six months, . . . [and they] continued to operate their electrical contracting business under the name West Dixie after the corporation was administratively dissolved."\(^{35}\) The diversion of corporate funds and the failure to maintain corporate formalities and separate identities directly resulted in West Dixie's inability to "meet its remedial obligations" under the NLRA.\(^{36}\) As a result, the Eleventh Circuit Court of Appeals found

\(^{28}\) *Id.* at 1194. The Paolicellis argued that Florida Statute § 607.1421(4) was applicable. *Id.*

\(^{29}\) *Id.*

\(^{30}\) *Id.* (quoting White Oak Coal Co., 318 N.L.R.B. 732, 735, 1995 WL 526356 (1995)).

\(^{31}\) *Id.*

\(^{32}\) *Id.*

\(^{33}\) *Id.*

\(^{34}\) *Id.*

\(^{35}\) *Id.*

\(^{36}\) *Id.* at 1194-95.
no error and affirmed the NLRB's holding that the Paolicellis were personally liable.  

Any time the NLRA is pleaded and applies, the Federal Court's exclusive jurisdiction will make it possible for a plaintiff to have the benefit of the Tenth Circuit's test, as adopted by the Eleventh Circuit, to pierce the corporate veil.

3. A Corporation with a Single Stockholder and Insufficient Funds, Without More, Does Not Create a Jury Question. In Wynn v. Arias, Ethel Wynn and Arias Properties, Inc. ("API") entered into a contract for the construction of Wynn's home. When the agreement fell apart, Wynn demanded the return of her earnest money, but API argued that Wynn had prevented the completion of the project and, therefore, she was not entitled to the return of the earnest money. After API sold the house to a third party, Wynn sued for breach of contract and additional tort claims. Wynn claimed that the corporation was a sham and that Arias, as API's president, should be personally liable because (1) API's office and phone were in Arias' home and (2) Arias controlled API. Additionally, API had no funds to repay the earnest money. The court stated:

[T]he mere operation of a corporation does not render one personally liable for corporate acts. Sole ownership of a corporation by one person, is not a factor and neither is the fact that the sole owner uses and controls it to promote his ends. There must be evidence of abuse.

The Court of Appeals of Georgia upheld the trial court's grant of summary judgment because Wynn had presented no evidence of a sham, fraud or inappropriate handling of corporate funds. Furthermore, the court noted that the mere fact the corporation had little cash on hand was not dispositive of the fraud issue. To be considered a sham, the low cash balance must be coupled with intent to avoid future debts of the corporation.

37. Id. at 1195.
39. Id. at 718-20, 531 S.E.2d at 132-34.
40. Id. at 719, 531 S.E.2d at 133.
41. Id. at 719-20, 531 S.E.2d at 133-34.
42. Id. at 719, 531 S.E.2d at 133.
43. Id.
4. United States District Court for the Middle District of Georgia Permits Joinder and Amendment of Counterclaim Based on Veil-Piercing Theory. In Blitch Ford, Inc. v. MIC Property & Casualty Insurance Corp.,\textsuperscript{44} Brett Blitch, on behalf of Blitch Ford, filed an insurance claim with MIC Property and Casualty Insurance Corporation ("MIC") to cover more than $450,000 of damages that resulted from a fire at the Blitch Ford car dealership. MIC paid on all the claims. After payment of the claims, Brett Blitch was convicted of arson, and MIC sought to amend its answer to assert counterclaims based on misrepresentation and fraud against both shareholders, Margaret and Brett Blitch.\textsuperscript{45} The court held the claim against Margaret Blitch for misrepresentation "would be futile and insufficient as a matter of law."\textsuperscript{46} However, the court held the corporate veil could be pierced to find Brett Blitch personally liable.\textsuperscript{47} As identified in the record, Brett Blitch not only "co-mingled funds for his personal benefit," but more importantly, he used the corporation "to perpetuate fraud against defendant."\textsuperscript{48}

5. Absent Fraud, One Who Deals with a Corporation as a Corporate Entity Cannot Deny the Corporate Form and Hold the Owner Liable. In Garrett v. Women's Health Care of Gwinnett,\textsuperscript{49} Dr. Garrett sued Dr. Salvino and Women's Healthcare of Gwinnett, P.C. ("WHCG") for breach of her employment agreement. Dr. Garrett attempted to pierce the corporate veil of WHCG and hold Dr. Salvino individually liable for the alleged breach of her employment agreement. Among its numerous holdings, the trial court granted summary judgment in favor of Dr. Salvino on all individual claims against her. On appeal, Dr. Garrett argued that the trial court erred by dismissing Dr. Salvino as a defendant in her individual capacity and that the corporate veil should be pierced to hold Dr. Salvino personally liable for the actions of WHCG.\textsuperscript{50}

Dr. Garrett's employment agreement provided that if she did not become a co-owner of WHCG after her first year of employment, WHCG would pay her a production bonus after the end of her second year. Dr. Garrett did not become a co-owner, left WHCG after two years, and was

\textsuperscript{44} No. 7:97-CV-21, 2000 WL 352353 (M.D. Ga., Mar. 31, 2000).
\textsuperscript{45} Id. at *1-2.
\textsuperscript{46} Id. at *2.
\textsuperscript{47} Id.
\textsuperscript{48} Id.
\textsuperscript{50} Id. at 55, 532 S.E.2d at 168.
therefore entitled to the production bonus. The employment agreement clearly stated the production bonus was to equal twenty-five percent of the gross profits directly attributable to Dr. Garrett's work minus $300,000, but the agreement was unclear as to calculation of gross profits.\(^{51}\) When WHCG's corporate accountant asked if the term gross profits was to include a deduction for costs, Dr. Salvino answered that "that was her intent."\(^{52}\) The difference was substantial. Dr. Garrett's bonus as calculated with a deduction for costs equaled $6,504.27 versus a bonus without a deduction for costs equal to $50,973.07. Although the trial court agreed that Dr. Garrett's bonus should have equaled the latter, the trial court also found that Dr. Salvino could not be held liable in a personal capacity and granted summary judgment in favor of Dr. Salvino.\(^{53}\)

In affirming the trial court's decision, the court of appeals held that "[o]ne 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."\(^{54}\) The court of appeals reiterated that piercing the corporate veil will not be justified absent fraud or injustices or absent abuse of the corporate form.\(^{55}\) Noting that the "record [was] devoid of evidence that would warrant piercing the corporate veil," the court of appeals affirmed the trial court's holding.\(^{56}\)

B. Statutorily Created Corporation Cannot Utilize Its Subsidiary to Circumvent Statutory Restrictions

In *Flint Electric Membership Corp. v. Barrow*,\(^{57}\) the Georgia Supreme Court addressed whether a rural electric membership corporation could sell propane gas in violation of O.C.G.A. sections 46-3-170 to -541.\(^{58}\) Flint Electric Membership Corporation ("Flint") was incorporated under the Georgia Electric Membership Corporation Act ("GEMCA") and had a wholly owned subsidiary, FlintErgy, Inc. ("FlintErgy"). Unlike Flint, FlintErgy was not incorporated under the GEMCA and therefore was not, by statute, restricted from selling forms of energy other than electrical energy.\(^{59}\) Thus, Flint and its board of directors intended to

\(^{51}\) *Id.* at 53, 532 S.E.2d at 166.

\(^{52}\) *Id.* at 53-54, 532 S.E.2d at 166-67.

\(^{53}\) *Id.* at 55-56, 532 S.E.2d at 168.

\(^{54}\) *Id.* at 55, 532 S.E.2d at 168.

\(^{55}\) *Id.* at 56, 532 S.E.2d at 168.

\(^{56}\) *Id.*

\(^{57}\) 271 Ga. 636, 523 S.E.2d 10 (1999).

\(^{58}\) See O.C.G.A. § 46-3-200 (1992).

\(^{59}\) 271 Ga. at 637, 523 S.E.2d at 12.
sell propane gas "either directly, or indirectly, through FlintErgy." At trial the court held that "the GEMCA does not authorize an electric membership corporation to sell or distribute propane gas." Moreover, because "FlintErgy was the alter ego of Flint, the trial court also enjoined Flint from selling propane gas indirectly through FlintErgy.

On appeal, Flint argued that because the O.C.G.A. encouraged electric membership corporations to assist, promote and develop other "methods of conserving, producing, converting, and delivering energy," Flint could sell propane gas through its subsidiary. The Georgia Supreme Court disagreed with Flint and affirmed the trial court's decision. Using traditional veil-piercing language, the Georgia Supreme Court noted: "Whether a subsidiary company is the alter ego of a parent company and whether the subsidiary company was formed to promote injustice or protect fraud are generally questions for the trier of fact." Holding the trial court's findings were supported by the evidence, the Georgia Supreme Court concluded that "Flint created FlintErgy as a shell and solely for its own convenience and benefit"; thus, "Flint cannot engage in the sale of propane gas indirectly through FlintErgy.

C. Even without a Certificate of Authority, a Foreign Corporation's Claim Is Not Void

In the only other true corporate case to reach the Supreme Court of Georgia during the survey period, the Supreme Court of Georgia granted certiorari in Transportation Insurance Co. v. El Chico Restaurants, Inc. to interpret O.C.G.A. section 14-2-1502(a). The sole issue on appeal to the supreme court concerned whether the phrase "maintain a proceeding" under the statutory language included the commencement of that action, so that the failure of a foreign corporation to obtain a certificate of authority prior to the commencement of the action would render it void ab initio. The supreme court held that "[b]ased on the

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60. Id., 523 S.E.2d at 11.
61. Id., 523 S.E.2d at 12.
62. Id.
63. Id.
64. Id.
65. Id. at 638, 523 S.E.2d at 12 (citations and internal quotations omitted).
68. O.C.G.A. § 14-2-1502 (1994) (titled "Consequences of transacting business without authority").
69. 271 Ga. at 775, 524 S.E.2d at 487. Void ab initio is translated as follows: "Null from the beginning, as from the moment when a contract is entered into." BLACK'S LAW DICTIONARY 1568 (7th ed. 1999).
language of O.C.G.A. section 14-2-1502(a) and its legislative history, . . . a foreign corporation’s action is not void for failure to obtain a certificate of authority [either before or after commencement] and thus the court of appeals correctly held that El Chico’s action could be amended.”

O.C.G.A. section 14-2-1502(a) provides that “[a] foreign corporation transacting business in this state without a certificate of authority may not maintain a proceeding in any court in this state until it obtains a certificate of authority.” In her opinion, Justice Hunstein utilized classic statutory interpretation analyses. Referring to Black’s Law Dictionary, the American Heritage Dictionary, Webster’s Third New International Dictionary, and Ballentine’s Law Dictionary, the majority held that (1) the word “maintain” does not include the “commencement of the item to be maintained”; (2) most commonly “maintain” means “the continuation of a pre-existing condition”; and (3) “to ‘maintain an action’ most commonly means the continuation of a lawsuit already begun.”

The majority also reviewed legislative history and found the 1969 legislature included the phrase “unless before commencement of the action it shall have obtained such a certificate” in a previous version of the statute, but the 1988 legislature removed any reference to the word “commencement.” Therefore, the Georgia Supreme Court concluded that because the legislature removed the 1969 language, which had required foreign corporations to obtain a certificate of authority “before commencement of the action,” El Chico could obtain its certificate of authority and amend its claim.

In any event, it is clear that in order to maintain a claim (which includes the time period after commencement), a foreign corporation will need to obtain a certificate at some time during the litigation.

D. Inspection of Corporate Documents Denied

Two cases appeared before the Court of Appeals of Georgia that reaffirmed which corporate documents members or shareholders could demand to inspect and under which circumstances they could do so. In Parker v. Clary Lakes Recreation Ass’n, the Cobb County Superior Court denied Parker’s application to compel Clary Lakes Recreation Association, Inc. (“CLRA”) to produce corporate documents. Parker originally sued CLRA, his neighborhood’s homeowner’s association, in

70. 271 Ga. at 775, 524 S.E.2d at 487.
71. O.C.G.A. § 14-2-1502(a).
72. 271 Ga. at 775, 524 S.E.2d at 487.
73. Id. at 775-76, 524 S.E.2d at 487-88.
74. Id. at 777, 524 S.E.2d at 488.
After discovery was closed, Parker requested to “inspect all accounting and/or corporate records of [CLRA] for the purpose of determining the performance of management and the condition of the corporation.” CLRA refused Parker’s request for the additional documents, and Parker sought an order to compel production. After deciding that Parker’s primary motive behind the request was to continue discovery beyond the applicable period, the trial court ordered CLRA to produce only one of nine categories that Parker requested.

Under Georgia law, two categories of corporate records may be inspected. The first category, which consists of basic corporate structuring documents and includes by-laws, minutes, resolutions and the articles of incorporation, is described in O.C.G.A. section 14-2-1602(a). The second category, which consists of more specific requests and includes accounting records and other minutes or records that are not covered under O.C.G.A. section 14-2-1602(a), is described in O.C.G.A. section 14-2-1602(c). Any shareholder may inspect and copy documents in the first category upon giving written notice to the company and waiting five business days before inspection. However, a shareholder may inspect documents in the second category only if:

1. His demand is made in good faith and for a proper purpose that is reasonably relevant to his legitimate interest as a shareholder;
2. He describes with reasonable particularity his purpose and the records he desires to inspect;
3. The records are directly connected with his purpose; and
4. The records are to be used only for the stated purpose.

If a shareholder satisfies the requirements in O.C.G.A. section 14-2-1602, and a corporation does not permit inspection or copying, the shareholder “may apply to the superior court for an order permitting inspection and copying of the requested records.” And, “unless the corporation proves that it refused inspection in good faith because it had a reasonable basis for doubt about the right of the [shareholder] to inspect the records demanded,” the corporation will be liable for costs and attorney fees.

76. Id. at 681, 534 S.E.2d at 155.
77. Id. at 682, 534 S.E.2d at 155.
78. Id. The judge ordered CLRA to produce “any minutes as required by O.C.G.A. § 14-3-1602(a)(5).” Id. at 684, 534 S.E.2d at 156.
80. Id. § 14-2-1602(b).
81. Id. § 14-2-1602(d).
82. Parker, 243 Ga. App. at 683, 534 S.E.2d at 156.
83. Id. (quoting O.C.G.A. § 14-3-1604(c)).
Because Parker requested documents that mainly fell into the second category, the trial court had to determine whether Parker had requested the documents for a "proper purpose." The burden of proof was on Parker, and he did not sufficiently demonstrate that his request was anything other than "an attempt to obtain discovery for [his lawsuit against CLRA] after the expiration of the discovery period." Without proof that this request was for a proper purpose, the superior court also refused to impose costs and attorney fees. In its holding, the court of appeals specifically noted that (1) the trial judge was "in the best position to evaluate Parker's motives for seeking the documents" and (2) the trial judge's findings were not clearly erroneous. Therefore, the court of appeals affirmed the Cobb County Superior Court's holding.

Similarly, in JarAllah v. American Culinary Federation, Inc., JarAllah sought to inspect and copy records of American Culinary Federation, Inc. ("ACF") pursuant to an alleged refusal by ACF to produce the requested documents. However, the Court of Appeals of Georgia held that "ACF never refused to permit JarAllah to inspect its records" and that in reality "ACF did not respond, due to 'simple oversight.'" Accordingly, ACF never "refused inspection" and could not be liable for costs or attorney fees under O.C.G.A. section 14-2-1604.

E. Defective Service of Process on Non-Resident Corporation

In Teledata World Services, Inc. v. Tele-Mart, Inc., Tele-Mart, Inc. ("Tele-Mart"), a Nevada corporation, was authorized to transact business in the state of Georgia. Teledata World Services, Inc. ("Teledata") attempted to serve process on Tele-Mart for breach of contract. After attempting to serve process on Tele-Mart at its Atlanta and New York City registered addresses, Teledata "argue[d] that it then perfected service under the Georgia Long Arm Statute" by personally serving a
Teledata employee in New York. The trial court granted Tele-Mart's motion to dismiss for insufficiency of service of process, and the Court of Appeals of Georgia affirmed.

In a succinct statement of law the court held:

Georgia's Long Arm Statute may be used to serve nonresident defendants. To be considered a 'nonresident' under the Long Arm Statute, a corporation must neither be a Georgia corporation nor a foreign corporation authorized to do or transact business in Georgia. Because Tele-Mart is authorized to transact business in Georgia, the Long Arm Statute is not applicable here.

F. Direct Versus Derivative Suit

In Matthews v. Tele-Systems, Inc., Tele-Systems was a closely-held corporation. Originally, Tele-Systems had four director/shareholders. Charles Matthews was one of the director/shareholders and owned approximately one-third of Tele-Systems' stock. After the other three directors convinced him that one of Tele-Systems' largest, most substantial clients did not want Matthews on the board of directors, Matthews resigned as a board member. After Matthews' resignation, he voted his shares to re-elect the three remaining board members. Once the three were in control of the board, Tele-Systems issued enough new stock so that Matthews would own less than one-quarter of the outstanding stock. Tele-Systems then fired Matthews and executed a reverse stock split. An effect, and presumably the intent, of the reverse stock split was to force Matthews' holdings in Tele-Systems to revert to a simple claim for cash. Matthews then filed suit against Tele-Systems and its remaining three director/shareholders for breach of fiduciary duty. The trial court granted summary judgment in favor of Tele-Systems on all counts of the breach of fiduciary duty claim, and Matthews appealed. The Court of Appeals of Georgia affirmed the trial court's grant of summary judgment.

Regarding Matthews' claim for breach of fiduciary duty based on the grant and payment of excessive salaries, the court held the following: (1) "[A] shareholder seeking to recover misappropriated corporate funds may only bring a derivative suit"; (2) Matthews "acquiesced in and ratified the salaries" and, therefore, was "estopped from complaining";

95. Id.
96. Id. at 843, 529 S.E.2d at 373.
97. Id. at 842, 529 S.E.2d at 373.
99. Id. at 871-72, 525 S.E.2d at 414.
100. Id. at 872, 525 S.E.2d at 414.
and (3) "Matthews' exclusive remedy for matters affecting the price of his stock" rested in the stock appraisal action that was currently pending and brought by Tele-Systems in the DeKalb Superior Court. The claim that the director/shareholders had been paid an excessive salary was, essentially, a claim for waste of corporate assets. Because Matthews initiated a direct action instead of a derivative action and because Matthews could not prove that he sustained any special injuries separate and distinct from those suffered by any other shareholders of the corporation, his action failed.

In the second count, Matthews alleged the other director/shareholders deceived him by forcing him to resign from the board of directors and, as a result, he suffered his injury and loss. The court of appeals held that because Matthews owned less than one-third of the shares at the time he resigned from the board, the other owners, who as a group held more than two-thirds of the outstanding stock, "had the right and power to vote Matthews out of office." The court likened Matthews' situation to that of an employer that deceives an at-will employee to induce resignation: "[T]he employer could have fired the employee at will at any time, the choosing of more palatable yet deceitful means does not harm the employee in the end analysis."

G. Legislative Changes

The 1999 session of the General Assembly of Georgia passed several amendments to the Business Code, the most notable of which are summarized below.

1. Rights Plans—Deviation From Delaware. O.C.G.A. section 14-2-624 substantially revises the Georgia Business Corporation Code ("GBCC") with regard to rights plans. Over the past several years, Georgia case law has begun to deviate from Delaware case law with regard to certain provisions in rights plans. Rights plans (1) are designed to preserve control by the target board during the process relating to potential takeover transactions and (2) operate to make it prohibitively expensive for an acquiror to acquire enough shares to exceed a specified threshold without the approval of the target board.

101. Id. at 872-74, 525 S.E.2d at 414-15.
102. Id. at 872-73, 525 S.E.2d at 415.
103. Id. at 874, 525 S.E.2d at 415.
104. Id., 525 S.E.2d at 415-16.
105. Id., 525 S.E.2d at 416.
In *Invacare Corp. v. Healthdyne Technologies, Inc.*,\(^{107}\) the United States District Court for the Northern District of Georgia upheld a dead hand provision that was part of Invacare's rights plan.\(^{108}\) Essentially, the dead hand provision operates to protect against proxy contests by allowing an incumbent board that is actually voted out to retain control over the rights plan or poison pill. Several Delaware cases have rejected the dead hand provision.\(^{109}\) In the 1999 session, the GBCC was revised to codify the holding in *Invacare Corp.* and permit dead hand provisions—subject to certain limitations. The language as revised in O.C.G.A. section 14-2-624 reads as follows:

(d) The terms and conditions of rights, options, or warrants issuable pursuant to this Code section may include provisions that:

(1) Preclude or limit the exercise, transfer, or receipt of such rights, options, or warrants by, or invalidate or void any such rights, options, or warrants held by, any person that is a beneficial owner of a specified amount of the outstanding equity securities or percentage of the outstanding voting power of the corporation, or by any transferee of such person, except that such provisions shall not affect any person whose beneficial ownership at the date of adoption of any such provision exceeds such specified amount or percentage, unless the amount of outstanding equity securities beneficially owned by such person is subsequently increased; and

(2) Limit, restrict, or condition the power of a future director to vote for the redemption, modification, or termination of the rights, options, or warrants for a period not to exceed 180 days from the initial election of the director; provided that, such 180 day time limitation shall not apply to any such limitation, restriction, or condition that is based solely on a director's current or former status as an employee or officer of the corporation; as a director, officer, employee, affiliate, or associate of any interested shareholder or person seeking to become an interested shareholder; or as a director, officer, or employee of an affiliate of an interested shareholder or person seeking to become an interested shareholder.\(^{110}\)

Essentially, new directors will be prohibited from withdrawing or changing a rights plan for a maximum of 180 days; provided, however, the prohibition may continue beyond 180 days if the prohibition is based solely on certain current or former positions or relationships by the director with (1) the target, (2) an interested shareholder or person

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108. Id. at 1578.
110. O.C.G.A. § 14-2-624(d).
seeking to become an interested shareholder, or (3) an affiliate of an interested shareholder or person seeking to become an interested shareholder. Additionally, the revisions significantly expanded the types of items that may be included in a shareholder agreement and, specifically, allow shareholder agreements to eliminate the board of directors or restrict its powers under certain circumstances.

2. Revisions to Statutory Governance of Architects. Act 901 comprehensively revised the law relating to the practice of architecture and created the Georgia State Board of Architects and Interior Designers as a successor to the State Board of Architects. The Act increased board membership to include two qualified interior designers, and created the position of vice president. It redefined the practice of architecture and changed qualifications of registered architects, restrictions on their practice, and registration renewals. The Act defined what structures need the seal of an architect and provided for exceptions, enforcement, and penalties. The Act also amended O.C.G.A. section 43-14-2, relating the State Construction Industry Licensing Board, to redefine “utility system” to include leachate collection and treatment systems associated with landfills. The Act also amended O.C.G.A. ch. 43-39A, relating to Georgia Real Estate Appraisers Board (“the Board”), and O.C.G.A. ch. 43-40, relating to real estate brokers and sales persons, to require certain applicants and persons under investigation by the Board to submit fingerprints and to authorize the Board to obtain records of criminal convictions of applicants and certain licensees.

II. SECURITIES

A. Sturm v. Marriott Marquis Part II

On February 7, 2000, the United States District Court in the Northern District of Georgia decided round two of Sturm v. Marriott Marquis Corp. On November 16, 1998, the district court granted Marriott Marquis’ motion to dismiss for failure to state a claim as to the federal claims because Sturm had failed to meet the heightened standard for pleading scienter under the Private Securities Litigation Reform Act (“PSLRA”). Thereafter, Sturm amended his complaint and Marriott

111. Id. § 14-2-624(d)(2).
112. Id. §§ 14-2-731 and -732.
Marquis moved to dismiss his amended complaint. In a well-structured and lengthy opinion, District Judge Thrash again granted the motion to dismiss in part and denied the motion to dismiss in part.

In the first count, the court addressed Sturm's claims that Marriott Marquis had committed securities fraud under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10(b)-5 promulgated thereunder. Sturm claimed that Marriott Marquis made false statements and concealed material facts during the proposed restructuring of the limited partnership. To succeed with his claim under Rule 10(b)-5, Sturm had to allege with specificity that "the [Marriott Marquis] (1) made a misstatement or omission, (2) of material fact, (3) with scienter, (4) in connection with the purchase or sale of securities, (5) upon which [Sturm] relied, and (6) that reliance approximately caused [Sturm's] injury." On the other hand, Marriott Marquis argued it could not be sued for securities fraud at the same time it was accused of mismanagement. Disagreeing with Marriott Marquis' argument, the court held that "[a]llegations of mismanagement and breach of fiduciary duty do not, however, bar a claim for securities fraud if the elements of such a claim are adequately pleaded.

Regarding Sturm's argument that Marriott Marquis failed to disclose the consideration connected with the contemplated real estate investment trust ("REIT") conversion when the merger was being considered by and offered to the partnership, the court held Sturm adequately pleaded with particularity that Marriott Marquis had provided misleading information. However, because Sturm had not alleged Marriott Marquis took any action beyond a preliminary internal consideration of the REIT conversion, the omission did not rise to the level of materiality required to state a claim for securities fraud. Next, the court addressed Sturm's argument that the limited partners should have been issued a short term bridge loan instead of losing their equity position, holding the "central thrust" of its argument rested on

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116. 85 F. Supp. at 1360.
117. Id.
120. 85 F. Supp. 2d at 1364.
121. Id.
122. Id. at 1365 (citing Robbins v. Koger Properties, Inc., 116 F.3d 1441, 1447 (11th Cir. 1997)).
123. Id.
124. Id.
125. Id. at 1370.
126. Id.
corporate mismanagement and "such claims are not cognizable under federal securities laws." Additionally, the court held Sturm's argument that Marriott Marquis had understated the appraisal value by roughly $20 million was not material because "the hypothetical reasonable investor would understand that the value he or she received from the REIT conversion depended upon a number of variables, only one of which was the appraised value of the Hotel." Additionally, the court held Sturm's argument that Marriott Marquis had understated the appraisal value by roughly $20 million was not material because "the hypothetical reasonable investor would understand that the value he or she received from the REIT conversion depended upon a number of variables, only one of which was the appraised value of the Hotel." Sturm also failed to prove Marriott Marquis possessed a mental state that embraced an "intent to deceive, manipulate or defraud." Although Sturm provided numerous facts establishing the limited partnership merger had benefitted Marriott Marquis to the detriment of plaintiffs, those facts alone were not enough to establish scienter. Sturm, however, presented more persuasive evidence alleging Marriott Marquis had identified two lenders willing to refinance the hotel mortgage. Therefore, Marriott Marquis affirmatively lied about availability during its solicitation for approval of the merger. While the facts alleged by Sturm had yet to be proven, the court held scienter was adequately pleaded to allow Sturm's Section 10(b) claims to proceed as to the alleged misrepresentation.

B. Shares of Closely-Held Corporation Held to Be "Securities" Under the Georgia Securities Act

In Bell v. Sasser, Robert Sasser and his son John Sasser founded and owned one hundred percent of Sundance Boats, Inc. ("Sundance"). After only a few months of operation, the Sassers were approached by Seaborne Bell, who wanted to acquire their company. After some negotiation, the parties drafted an agreement pursuant to which Bell purchased the outstanding shares of Sundance for $200,000. After the sale, Robert Sasser went to work for a boat manufacturing company he had worked with prior to founding Sundance. Several years later, and apparently because Sundance did not turn a profit, Bell and Sundance filed suit against Robert Sasser, John Sasser, and Robert Sasser's employer, Carolina Skiff, Inc. ("Carolina Skiff"). Both parties filed cross-motions for partial summary judgment, and the trial court granted

127. Id.
128. Id. at 1370-71.
129. Id. at 1371 (quoting Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 (1976)).
130. Id. at 1372.
131. Id.
summary judgment in favor of Robert Sasser, John Sasser, and Carolina Skiff.\textsuperscript{133}

Two separate cases were at issue in the appeal. In the first case, Bell and Sundance appealed the entry of summary judgment against them regarding whether the Sassers sold Bell unregistered securities in violation of Georgia law.\textsuperscript{134} In the second case, the Sassers and Carolina Skiff appealed the trial court's failure to grant summary judgment in their favor regarding the allegation that Robert Sasser fraudulently misrepresented to Bell that he would personally take care of any warranty work required on Sundance boats and that Robert Sasser and Carolina Skiff conspired to drive Sundance out of business.\textsuperscript{135}

In ruling for the Sassers, the trial court held that the Georgia Securities Act ("the Act") was not applicable, and that even if it had been applicable, Bell himself had violated the Act.\textsuperscript{136} The court of appeals relied on a two-pronged analysis established by the Georgia Supreme Court for determining whether stock is a security within the meaning of the Act.\textsuperscript{137} The initial prong was set forth in \textit{Landreth Timber Co. v. Landreth},\textsuperscript{138} and is commonly known as the stock characterization test. The second prong is commonly known as the \textit{Howey economic reality test}.\textsuperscript{139} The Georgia Supreme Court has adopted both prongs of the test, first in \textit{Tech Resources v. Estate of Hubbard}\textsuperscript{140} and more recently in \textit{Cohen v. William Goldberg & Co.}\textsuperscript{141} Under the stock characterization test, when an instrument (1) is called "stock" and (2) bears usual characteristics of stock, the purchaser justifiably may assume the federal securities laws apply.\textsuperscript{142} The characteristics usually associated with common stock are "(i) the right to receive dividends contingent upon an apportionment of the profits, (ii) negotiability, (iii) the ability to be pledged or hypothecated, (iv) the conferring of voting rights in proportion to the number of shares owned, and (v) the capacity to appreciate in value."\textsuperscript{143} Only if stock does not satisfy the criteria outlined in the stock characterization test should a court analyze whether the economic

\textsuperscript{133.} \textit{Id.} at 843-44, 520 S.E.2d at 290.
\textsuperscript{134.} \textit{Id.} at 844, 520 S.E.2d at 290.
\textsuperscript{135.} \textit{Id.} at 850, 520 S.E.2d at 294.
\textsuperscript{136.} \textit{Id.} at 845, 520 S.E.2d at 291.
\textsuperscript{137.} \textit{Id.}
\textsuperscript{139.} See \textit{SEC v. W.J. Howey Co.}, 328 U.S. 293, 298-99 (1946).
\textsuperscript{140.} 246 Ga. 583, 584, 272 S.E.2d 314, 316 (1980).
\textsuperscript{142.} \textit{Id.} at 607-08, 423 S.E.2d at 232 (citing \textit{Landreth}, 471 U.S. at 685-86).
\textsuperscript{143.} 238 Ga. App. at 845, 520 S.E.2d at 291 (quoting \textit{Landreth}, 471 U.S. at 686).
Under the economic reality test, a transaction constitutes a securities transaction if there is (1) an investment, (2) a reasonable expectation of profits, and (3) reliance on the management of another party to create the profits.\textsuperscript{145}

The trial court concluded that it was "difficult, if not impossible, to analyze [this case] under the \textit{Landreth} stock characterization test" and, therefore, immediately applied the "economic reality" test.\textsuperscript{146} Under the framework of the stock characterization test, the court of appeals affirmed the trial court's denial of Bell's motion for summary judgment and reversed the trial court's grant of the Sassers' motion for summary judgment.\textsuperscript{147} The court held that this case was similar to \textit{Landreth} and \textit{Cohen} and that the "transaction clearly involved stock."\textsuperscript{148}

As evidence under the stock characterization test that Sundance stock was a security, the court noted that: (1) Sundance had only one class of stock in its articles of incorporation and, therefore, all stockholders were entitled to dividends; (2) Sundance by-laws permitted transfers of the stock, and Bell had in fact purchased the stock, so the shares were negotiable; (3) no evidence was presented to demonstrate that the shares could not be pledged; (4) each stockholder was entitled to one vote per share; and (5) Sundance stock could appreciate in value.\textsuperscript{149}

Next, the court reversed the Sassers' motion for summary judgment.\textsuperscript{150} The court rejected the Sassers' arguments that Bell lacked standing, that Sundance stock was exempt from registration, that Bell equally violated Georgia securities laws, and that Bell had failed to tender the stock.\textsuperscript{151} Consequently, "the Sassers [were] liable to Bell under OCGA § 10-5-14(a) for the sale of unregistered securities, but the amount of recovery to which Bell [was] entitled remain[ed] in dispute."\textsuperscript{152}

With regard to Bell's conspiracy claim, the court held Bell failed to carry his burden of proof; therefore, the Sassers and Carolina Skiff should have been granted summary judgment.\textsuperscript{153}

\textsuperscript{144} Id.
\textsuperscript{146} 238 Ga. App. at 845, 520 S.E.2d at 291.
\textsuperscript{147} Id. at 850, 520 S.E.2d at 294.
\textsuperscript{148} Id. at 846, 520 S.E.2d at 292.
\textsuperscript{149} Id.
\textsuperscript{150} Id. at 847, 520 S.E.2d at 292.
\textsuperscript{151} Id. at 847-48, 520 S.E.2d at 292-93.
\textsuperscript{152} Id. at 850, 520 S.E.2d at 294.
\textsuperscript{153} Id. at 853, 520 S.E.2d at 296.
Similar to the analysis in *Bell*, in *Cox v. Edelson*, the Court of Appeals of Georgia was presented with the issue of whether a security had been sold. Although the case set forth few facts, the record showed Gerald Cox invested in Hank and Sue Ann Edelson’s office furniture business. Soon thereafter Cox filed suit “alleging that the Edelson’s knowingly made false statements that induced him to invest in their [business] to his detriment.”

In three separate orders, the trial court (1) denied Cox’s motion for summary judgment as to his claim for breach of contract and violation of securities laws; (2) granted Edelson’s motion for summary judgment as to Cox’s claim for breach of contract and violation of securities laws; and (3) granted summary judgment to the Edelsons on five of the seven counts raised in Cox’s amended complaint. Cox appealed the grant of summary judgment to the Edelsons regarding breach of contract and violation of securities laws, and the Edelsons cross-appealed to challenge the denial of summary judgment as to Cox’s claim for fraud and misrepresentation.

While the trial court held Cox’s investment in the Edelsons’ company did not “meet the definition of a security,” the Court of Appeals of Georgia reversed, holding the stock Cox purchased was a security subject to the Georgia Securities Act (“Act”). The trial court applied the economic reality test, but the court of appeals did not “[b]ecause Cox’s investment meets the definition of a security.” As stated above in the review of *Bell*, the Georgia Supreme Court adopted a two-part test in *Cohen* to analyze when an investment equals a security: “[T]he initial test must be the ‘stock characterization’ test,” and “[o]nly if it does not meet the requirements of that test must we apply the ‘economic’ reality test.”

Under the stock characterization test, there is a two-part analysis. The first question is whether the instrument sold is called “stock,” and the second question is whether the instrument sold “bears the usual characteristics of stock.” If both questions are answered in the affirmative, “a purchaser justifiably may assume that securities laws apply.” Under the Act, a security is defined as:

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155. *Id.* at 5, 530 S.E.2d at 251.
156. *Id.*
157. *Id.*
158. *Id.* at 7, 530 S.E.2d at 252.
159. *Id.*
160. *Id.* at 6, 530 S.E.2d at 251-52.
161. *Id.*, 530 S.E.2d at 252.
162. *Id.*
any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of indebtedness, investment certificate, certificate of interest or participation in any profit sharing agreement, . . . transferable share, investment contract, voting-trust certificate, limited partnership interest, or beneficial interest in profits or earnings, or any other instrument commonly known as a security . . . .

Even though both courts noted that Cox’s purchase was a “stock purchase,” the court of appeals found it necessary to analyze the characteristics of the particular investment vehicle sold to Cox. Typical characteristics associated with common stock are “(1) the right to receive dividends contingent upon an apportionment of profits; (2) negotiability; (3) the ability to be pledged or hypothecated; (4) the conferring of voting rights in proportion to the number of shares owned; and (5) the capacity to appreciate in value.” Additionally, any investment that qualifies as a security must be registered unless there is an applicable exemption for the sale.

In the subscription agreement under which Cox purchased his shares, he acknowledged that the shares were not registered and that the company was not obligated to register the shares or make an exemption. Cox also agreed to strict limitations on his right to resell or transfer the shares. Furthermore, Cox made a representation that he would not present evidence to show he had any right to receive dividends, to participate in voting, or to gain value in the stock. Although these facts do not, on their face, embody the characteristics of stock, “the [Georgia] Supreme Court found that neither restrictions on the negotiability of stock in a closely-held corporation, nor its unregistered status negated the stock’s character as a security.” Therefore, “the Georgia securities laws contemplate that stock may be a security and yet be unregistered.” Once the court determined Cox’s investment met the stock characterization test, there was no need for the court to apply the economic reality test; however, genuine issues of material facts still existed regarding whether the Edelsons made fraudulent statements. Therefore, the court of appeals remanded the case to the

163. Id.
164. Id.
165. Id. at 7, 530 S.E.2d at 252.
167. 243 Ga. App. at 7, 530 S.E.2d at 252.
168. Id.
169. Id. (internal quotations omitted).
170. Id. at 7-8, 530 S.E.2d at 252-53.
trial court for determination of count seven—Cox's allegation that the Edelsons had violated the securities laws.\footnote{171}

\section*{C. Forward Looking Statements Accompanied by Cautionary Statements Did Not Violate the Georgia Securities Act}

\textit{Harris v. Ivax Corp.}\footnote{172} involved a class action suit alleging that Ivax Corp. ("Ivax"), its chairman and CEO, and its CFO had committed fraud under the Securities Exchange Act Section 10(b) and Securities and Exchange Commission Rule 10(b)-5. The complaint filed by a group of investors in Ivax stemmed from several press releases issued by Ivax and the subsequent announcement of a $179 million loss. Ivax issued press releases in both August and September 1996. Those press releases stated optimism and specifically set forth an anticipated loss of $43 million. However, in November 1999, Ivax announced a $179 million loss with the greatest portion of the loss being derived from a reduction in goodwill associated with certain Ivax businesses. The $104 million attributed to the goodwill reduction was not mentioned in either press release, and Ivax's stock price plummeted.\footnote{173}

Ivax's investors claimed that the economic projections for the company were fraudulent and that Ivax knew the omission of the possible goodwill writedown was misleading. Ivax defended its position by claiming protection under the safe harbor provisions of the Securities Exchange Act and arguing that Ivax's investors had not met the newly enacted heightened pleading standard under the Private Securities Litigation Reform Act ("PSLRA"). The district court dismissed Ivax's investors claims, and the investors appealed seeking a review of the dismissal of the complaint and arguing the district court should have granted them leave to amend their complaint if they had not met the heightened pleading standards under the PSLRA.\footnote{174}

The PSLRA provides a safe harbor for forward-looking statements if the statements are "accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement."\footnote{175} If the safe harbor requirement is met, an individual or corporation will not be held liable if the forward-looking statement ultimately proves to have been false.\footnote{176} Additionally, the safe harbor requires that even if a forward-

\begin{itemize}
\item \textit{Id.} at 9, 530 S.E.2d at 254.
\item \textit{Id.} at 802.
\item \textit{Id.}
\item \textit{Id.}
\item \textit{Id.}
\end{itemize}
looking statement does not have the appropriate cautionary language, a plaintiff must prove defendant had actual knowledge that the forward-looking statement was in fact false or misleading.\textsuperscript{177} As was required in \textit{Sturm}, the heightened pleading standards mandate that a plaintiff seeking to obtain recovery for securities fraud must "allege specific facts that raise a 'strong inference' of the 'required state of mind' on the part of the officers responsible for an allegedly fraudulent statement."\textsuperscript{178} Not only did the district court conclude all statements were forward-looking and were accompanied by appropriate cautionary language, but the district court also held plaintiffs had failed to satisfy the new pleading standards required under the PSLRA.\textsuperscript{179}

The Eleventh Circuit Court of Appeals, affirming the district court's decision, held Ivax's statements were all forward-looking and accompanied by "meaningful cautionary language."\textsuperscript{180} Additionally, the court held that because the press releases issued by Ivax were covered under the safe harbor provision, there was no need to "enter the thicket of the PSLRA's new pleading requirements for scienter; if a statement is accompanied by meaningful cautionary language, 'the defendant's statement of mind is irrelevant.'\textsuperscript{181} A forward-looking statement is defined as

\begin{itemize}
\item[(A)] a statement containing a projection of revenues, income (including income lost), earnings, (including earnings lost) per share, capital expenditures, dividends, capital structure, or other financial items;
\item[(B)] a statement of the plans and objectives of management for future operations, including plans or objectives relating to the products or services of the issuer;
\item[(C)] a statement of future economic performance, including any such statement contained in a discussion and analysis of financial condition by the management or in the results of operations included pursuant to the rules and regulations of the commission;
\item[(D)] any statement of the assumptions underlying or relating to any statement described in sub-paragraph (A), (B), or (C);
\item[(E)] any report issued by an outside reviewer retained by an issuer, to the extent that the report assesses a forward-looking statement made by the issuer;
\item[(F)] a statement containing a projection or estimate of such other items as may be specified by rule or regulation of the Commission.\textsuperscript{182}
\end{itemize}

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\textsuperscript{177} Id. (quoting 15 U.S.C. § 78u-5(c)(1)(B)).
\textsuperscript{178} Id.
\textsuperscript{179} Id.
\textsuperscript{180} Id.
\textsuperscript{181} Id.
\textsuperscript{182} Id. at 805 (quoting 15 U.S.C. § 78u-5(i)(1)).
The Eleventh Circuit then scrutinized several statements under the framework and definition of a forward-looking statement. The court concluded each statement it analyzed fell comfortably within one of the subsections defining a forward-looking statement.

The first forward-looking statement analyzed was "reorders are expected to improve as customer inventories are depleted." Because "the test makes clear that an expected increase in reorders was one of the bases of the optimism," the court held this sort of statement was indeed "a statement of the assumptions underlying a statement of future economic performance." The second statement analyzed by the court was "the challenges unique to this period in our history are now behind us." Although plaintiffs argued the CEO's use of present tense in his statement made the statement fall outside the scope of the forward-looking safe harbor, the court was not persuaded and held a statement "about the state of a company whose truth or falsity is discernable only after it is made necessarily refers only to future performance." Therefore, the statement was based on future economic performance as provided under subsection (C) of the definition of a "forward-looking" statement.

The third statement by Ivax was the following: "Our fundamental business and its underlying strategies remain intact. Only a limited number of companies are positioned to meaningfully participate in this rapidly growing market and, among them, IVAX is certainly very well positioned." As with the second statement, the court held that while the CEO's choice of words involved language identifying a present condition, the use of the word "intact" and "well-positioned" is language "whose truth can only be known after seeing how Ivax's future plays out."

Finally, in the fourth statement examined by the court, Ivax listed multiple factors that could influence third quarter results for the company. Because the factors included both forward-looking statements and statements that were not forward-looking, the question presented was whether "the safe harbor benefits the entire statement or only parts

183. Id. at 804.
184. Id. at 803.
185. Id. at 804.
186. Id.
187. Id. at 805.
188. Id.
189. Id.
190. Id.
191. Id.
of it." Plaintiffs argued the whole statement was misleading because it is the whole statement that omits the expectation of a goodwill writedown. For the purposes of analyzing the entire statement, the court pointed to extrinsic sources of congressional intent and stated the "safe harbor provision was enacted in order to loosen the 'muzzling effect' of potential liability for forward-looking statements which often kept investors in the dark about what management foresaw for the company." Therefore, if the court were to hold an entire statement that contains both forward-looking and non-forward-looking statements as outside of the safe harbor, the intent of Congress to foster communication would be hindered. Moreover, the court recognized that because that holding could create a potential loop hole:

a list or explanation would only qualify for this treatment if it contained assumptions underlying a forward-looking statement. Investors should know, under the statutory scheme, that relying on assumptions is dangerous; there will often be no legal recourse even if the assumption is false. Second, a defendant can fully benefit from the safe harbor's shelter only when it is disclosed risk factors in a warning accompanying the forward-looking statement. This disclosure as well should warn investors against blind reliance on mixed lists.

After determining that all statements were in fact forward-looking statements, the Eleventh Circuit then analyzed the district court's conclusion that adequate cautionary language accompanied the forward-looking statements. The press releases included "detailed and informative" cautionary provisions, but did not include specific warnings about a potential goodwill writedown. Therefore, the question presented was whether cautionary language must "explicitly mention the factor that ultimately belies a forward-looking statement." The Eleventh Circuit held it did not and further annunciated that the statute only required "important factors that could cause actual results to differ materially from those in the forward-looking statement" be addressed and not "all factors." Additionally, a conference report that accompanied the PSLRA clearly specified that "failure to include the particular

192. Id. at 806.
193. Id.
194. Id.
195. Id. at 806-07.
196. Id. at 807.
197. Id.
198. Id.
199. Id.
200. Id.
factor that ultimately causes the forward-looking statement not to come true will not mean that the statement is not protected by the safe harbor."201

When claiming fraud under the Securities Exchange Act of 1934 and Rule 10b-5, the decision in Harris provides sound guidance to any Georgia corporation and its counsel with regard to forward-looking statements and the applicable safe harbor provided under the securities laws. Harris also provides guidance in the delicate arena of the heightened pleading requirements of the PSLRA.

III. PARTNERSHIP

A. Court of Appeals of Georgia Upholds Substance Over Form and Protects Partnership Assets From Judgment Creditor

In Aaron Rents Inc. v. Fourteenth Street Venture, L.P.,202 Aaron Rents was granted a $559,114 judgment against Shepherd. Shepherd and others had breached warranties contained in the sale of his company to Aaron Rents. Two years later, Fourteenth Street Associates, which was fifty percent owned by Shepherd, conveyed essentially all of its property to Fourteenth Street Venture, L.P. ("L.P."). Aaron Rents filed a declaratory judgment to secure its debt on the transferred property, and L.P. and Life of Virginia, a secured creditor that held a 1994 deed on the property to secure debt, filed for summary judgment. The trial court granted summary judgment in favor of L.P. and Life of Virginia, and Aaron Rents appealed.203

Aaron Rents argued Shepherd and his partner did not form a partnership when they originally created Fourteenth Street Associates, but instead formed a joint venture. Although the language in the contract that formed Fourteenth Street Associates identified Fourteenth Street Associates as a "joint venture" instead of a "partnership," the substance of the agreement proved the intent of the parties to be otherwise.204 The agreement set forth the following:

Fourteenth Street Associates was formed to acquire property for profit, that both Shepherd and Stalker had to consent to any other business by the association, that neither Shepherd nor Stalker had any authority to act alone on behalf of the association, that Shepherd and Stalker each had a 50% interest in the association's assets and profits

201. Id.
203. Id. at 747, 533 S.E.2d at 761.
204. Id.
and losses, that Shepherd and Stalker each contributed $25,000 in capital to the association, that each of them bore the risks of the association’s business.205

The court of appeals held that as a matter of law Shepherd and Stalker had an intent to contribute equal amounts to share risks, control, and assets; therefore, they essentially formed a partnership.206 Additionally, as may be common with distinctions between joint ventures and partnerships, no distinction was met in this case. Stalker and Shepherd intended to participate and share jointly in property, profits, losses, and control.207 As such, the court held the partnership property was in the partnership’s name and was not individual real property owned by a single partner and, therefore, was not subject to Aaron Rents’ lien against the individual partner.208

B. Conveyance of Property to a Joint Venture is Insufficient to Give Notice of Partnership’s Interests in the Property

In Accolades Apartments, L.P. v. Fulton County,209 which was decided before Aaron Rents, the court of appeals addressed the issue of whether certain real property had been placed into a partnership or whether the property, which was transferred to “the joint venture by its name alone,” was not partnership property.210 If the property had been transferred into the partnership, it would have been protected from condemnation proceedings by the IRS, the Georgia Department of Revenue, and Coyote Portfolio, LLC (collectively, “the Creditors”), but if the property merely was transferred to the joint venture, the Creditors would be entitled to reach the property.211 The court reiterated that “when title to property is placed in the name of the partnership, the question of individual shielding assets and secret partnerships is eliminated.”212

After reviewing the record, the court held the transfer of property to the joint venture name alone was “insufficient to give notice of a partnership interest therein.”213 Moreover, the court noted that Georgia law does not recognize a joint venture as a distinct legal entity

205. Id. at 748, 533 S.E.2d at 761-62.
206. Id.
207. Id.
208. Id. at 748-49, 533 S.E.2d at 762.
210. Id. at 215, 528 S.E.2d at 270.
211. Id.
212. Id.
213. Id.
separate from its owners. For these reasons, the court held that the Creditors were entitled to disbursements from the property and that Accolades Apartments, as the successor in interest to the joint venture, was not.

C. Limited Partners Are Liable for State Taxes

In Department of Revenue v. Sledge, the Georgia Department of Revenue denied Tennessee residents' application for a refund of income taxes assessed against them. The Tennessee residents were William and Mary Sledge. The Sledges were limited partners in two separate Georgia limited partnerships. The Georgia limited partnerships had their principal place of business in Georgia, and all partnership-related activities were conducted in Georgia by the general partners, who were Georgia residents. Even though the Sledges were merely passive limited partners and the partnership only invested in a New York brokerage account, the partnership withheld Georgia income taxes on the Sledges' share of profits.

At trial, the Fulton County Superior Court reversed the Georgia Department of Revenue's denial to refund Georgia income taxes withheld from the Sledges during the years 1992 through 1994. On appeal, "[t]he Sledges contend that O.C.G.A. § 48-7-24 taxes the profits of a partnership only if the individual member does business in Georgia and that, because they personally did not do business in Georgia, they owed no income tax on their share of the partnership profits." However, the Court of Appeals of Georgia held that the "statute is plain." O.C.G.A. section 48-7-24 states: "When one or more of the individual members of a partnership doing business in the state are nonresidents of this state, the nonresidents shall be taxable on their share of the net profits of the partnership." The literal meaning of the statute contradicted the Sledges' argument, and the court held that "where a partnership does business in Georgia, its individual members are taxable on their share of the net profits of the partnership—regardless of whether the individual members qualify as doing business in Geor-

214. Id.
215. Id. at 216, 528 S.E.2d at 270.
217. Id. at 833, 528 S.E.2d at 261.
218. Id.
219. Id. at 834, 528 S.E.2d at 261.
220. Id.
221. Id. at 833, 528 S.E.2d at 261; see also O.C.G.A. § 48-7-24(a) (1995 & Supp. 2000).
The Sledges also contended the limited partnership did not do business in Georgia because it merely invested in the New York brokerage account. However, the court of appeals disagreed and held that it “must be guided by the general principle of Georgia law that the phrase ‘doing business’ means any activity or transaction for the purpose of financial profit or gain.” Therefore, because a partnership by definition will be formed to achieve profits, it is inevitable that a limited partnership engaged in the activity of financial profit or gain will always be doing business under Georgia law.

D. Partner Liability for Partnership Debts

In *McCollum v. O'Dell*, Glenn McCollum, Robert O'Dell, and Basile Antonelli entered into a handwritten agreement prepared by Antonelli and McCollum. The agreement was three sentences long and essentially set forth a $25,000 loan agreement. The Court of Appeals of Georgia stated, “This case presents a perfect example of what happens when lay persons exercise their right to draft a legal document.” Under the agreement, Glenn McCollum loaned $25,000 to Antonelli's Restaurant, Inc., and in return, McCollum was to receive an option to buy into Antonelli's as a full partner. However, after depositing $25,000 into a business checking account, the restaurant failed, and McCollum was not repaid for his loan. McCollum then brought suit against what he claimed to be the partnership with O'Dell and Antonelli. As a partner, O'Dell would be liable for any partnership debts due and payable. O'Dell, on the other hand, argued the loan was made to Basile Antonelli, individually, and not the partnership. At trial, the court ruled in favor of O'Dell, holding the money was a loan to

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222. 241 Ga. App. at 834, 528 S.E.2d at 261.
223. *Id.*, 528 S.E.2d at 262.
225. *Id.* at 6-7, 525 S.E.2d at 722. The full text of the agreement is as follows:

This agreement between Glenn McCollum and Antonelli’s Restaurant Inc. is borrowing [sic] the sum of twenty-five thousand dollars from Glenn McCollum. Payment agreement between parties is monthly payment of 650.00 per month starting with the first payment due Jan. 1, 1996 for the total payments of 48 months for total amount of thirty one thousand and two hundred dollars. Antonelli’s Inc is giving a 6 month option for Glenn McCollum to come in as a full partner starting date Jan. 1, 1996 expiring July 1, 1996 for the total sum fee of one hundred and twenty five thousand dollars paid into Antonelli’s corp. as Glenn McCollum options if during 6 month grace period expires Glenn McCollum has the option to refuse partnership and Antonelli will continue to make payments to 48 month contract.

*Id.* at 7, 525 S.E.2d at 722.
226. *Id.* at 6, 525 S.E.2d at 722.
Antonelli personally. On appeal, the Court of Appeals of Georgia held the trial court's ruling rested on "erroneous legal theory" and reversed and remanded the decision to the trial court to determine "whether the parties intended that the loan be made to the business or to Antonelli individually."  

The difficulty in this decision rested on the "inexpertly drafted," "ambiguous" and "poorly worded" nature of the agreement. The contract referred to Antonelli in several different respects. First, Antonelli signed in his individual capacity as Basile Antonelli; second, McCollum loaned the money to an entity referred to as "Antonelli's Restaurant, Inc.,” “Antonelli's, Inc.,” “Antonelli's corp.,” and the "partnership." If the loan was a "business" loan as opposed to a personal loan to Antonelli, then "all partners [would be] jointly and severally liable for all debts, obligations, and liabilities of the partnership," including McCollum's $25,000.

O'Dell also attempted to hide behind the corporate veil by claiming he believed the business had been incorporated when he signed the agreement. If the business actually had been a corporation, O'Dell would have been protected as an officer or director of the corporation, free from personal liability on corporate debts. The court of appeals, however, held that "there [was] no evidence supporting the trial court's finding that O'Dell thought the business had been incorporated when he signed the contract," and, in fact, "O'Dell [had] testified unequivocally that the business was never incorporated and that he knew, at the time he signed the contract, that the business was operating as a partnership." While this case provides little new guidance with regard to Georgia partnership law, it emphasizes the importance of competent legal counsel in forming the legal relationship intended by the parties.

IV. RESTRICTIVE COVENANTS

In Georgia, as is common in other states, the courts have adopted a fairly straightforward analytical structure regarding noncompetition and nonsolicitation agreements. Courts analyze three factors when

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227. Id. at 7-8, 525 S.E.2d at 722.
228. Id. at 10, 525 S.E.2d at 724.
229. Id. at 9, 525 S.E.2d at 723.
230. Id.
231. Id. at 10, 525 S.E.2d at 724.
232. Id. at 8, 525 S.E.2d at 723.
233. Id.
234. The authors would like to thank Michael E. Ross, Partner in the firm of King & Spalding, Atlanta, Georgia, for his guidance in the preparation of this section.
determining the reasonableness of the challenged restrictions, including (1) duration, (2) territorial coverage, and (3) scope of the prohibited activity.\textsuperscript{235} The question of reasonableness of the imposed restraint is a question of law for the court.\textsuperscript{236}

It is worth noting that "blue penciling" of an offending restrictive covenant in a pure employment agreement (as opposed to restrictive covenants incorporated in the sale of a business) is prohibited under Georgia law, even if the contract includes a severability clause.\textsuperscript{237} In an employment agreement, a covenant not to compete or a nonsolicitation agreement must stand on its own or fail in its entirety; thus, it is advisable to scrutinize these clauses and reference the prevailing law prior to committing to specific language.

A. NonCompete Covenants

In \textit{Herndon v. Waller},\textsuperscript{238} the Court of Appeals of Georgia struck down a noncompete covenant in a veterinarian's lease agreement.\textsuperscript{239} Waller, the veterinarian, brought a declaratory judgment action to invalidate the noncompete covenant.\textsuperscript{240} The court of appeals first held the noncompete covenant should be analyzed under the strict scrutiny accorded to restrictive covenants in employment contracts rather than under the relaxed standard, including blue-penciling, which is allowed with restrictive covenants in connection with the sale of a business.\textsuperscript{241} The court reasoned the noncompete covenant reflected the unequal bargaining power inherent in employment contracts because (1) Waller, as lessee, was essentially in the same position as the buyer of a business, not the seller, and (2) Waller received no separate consider-


\textsuperscript{236} Rollins Protective Servs. Co. v. Palermo, 249 Ga. 138, 139, 287 S.E.2d 546, 548 (1982). The reasonableness analysis is informed by the following structure: A court will apply (1) strict scrutiny to restrictive covenants ancillary to employment agreements; (2) a middle level of scrutiny to restrictive covenants found in professional partnership agreements; and (3) a much lesser degree of scrutiny to restrictive covenants ancillary to the sale of a business. See Habif, Arogeti & Wynne, P.C. v. Baggett, 231 Ga. App. 289, 289-90, 498 S.E.2d 346, 349 (1998).


\textsuperscript{239} Id. at 495, 525 S.E.2d at 160.

\textsuperscript{240} Id. at 494, 525 S.E.2d at 160.

\textsuperscript{241} Id. at 495, 525 S.E.2d at 161 (citing \textit{Baggett}, 231 Ga. App. at 289-90, 498 S.E.2d at 349).
ation for the noncompete covenant. Curiously, however, even though the lessor, Herndon, was also a veterinarian, the court of appeals did not analyze this case using the new middle tier level of review for restrictive covenants ancillary to professional partnership agreements.

Waller prevailed in the trial court on the ground that the geographic term of the noncompete covenant was too vague to be enforced. Nonetheless, the court of appeals concluded the noncompete covenant "was not reasonable in light of the nature of the business and the parties' situation." In reaching this conclusion it pointed out that (1) Herndon had not practiced veterinary medicine at the leased premises for more than six years when he leased it to Waller; (2) while the tenant immediately prior to Waller was also a veterinarian, he defaulted on the lease, and the office had been in disrepair for several months before it was leased to Waller; and (3) less than ten percent of Waller's clients were carryovers from this previous tenant or any other veterinarians who had worked out of the office earlier. The court of appeals found that "[t]he customers serviced at the leased premises, therefore, were Waller's and not Herndon's."

In Ceramic & Metal Coatings Corp. v. Hizer, the Court of Appeals of Georgia struck down a noncompete covenant in an employment contract for a sales representative because it was overly broad in its territory and scope of prohibited activities. Specifically, the noncompete covenant failed because it: (1) applied to all of Georgia and Florida even though Hizer sold to customers only in five counties in Florida and three counties in Georgia; (2) provided that the territory would be expanded to include "any territory added during the course of [his] Agreement"; and (3) imposed a paradigm "in any capacity" restriction on Hizer's ability to go to work for a competitor. In short, this opinion was routine as analyzed by the court, and CMC could not have prevailed under the current noncompete law in Georgia. It is interesting to note that CMC was seeking to have the court apply the new "middle tier" level of review which it refused to do.

242. Id.
243. Id.
244. Id. at 494-95, 525 S.E.2d at 160. The noncompete agreement reads as follows: "[Waller] agrees not to operate as a Veterinarian for a distance of fifteen (15) miles." Id. at 494, 525 S.E.2d at 160.
245. Id. at 496, 525 S.E.2d at 161.
246. Id.
247. Id.
249. Id. at 391, 529 S.E.2d at 162.
250. Id. at 393-94, 529 S.E.2d at 163-64.
In Hogan Management Services, P.C. v. Martino, a nonsolicitation agreement in a physician's services contract was plainly unenforceable because it lacked any time limitation, had no territorial limitation, and prohibited Martino from soliciting any patients. Additionally, the court emphasized its lack of authority to alter or "blue-pencil" the nonsolicitation clause.

In Kuehn v. Selton & Associates, Brad Kuehn was a commercial real estate agent and broker whose noncompete agreement with Selton & Associates likewise failed because it had neither a specified territory nor a definite expiration date. Notably, however, the court of appeals suggested that this noncompete covenant might have passed muster if it had been confined to real estate clients served by Kuehn. This dictum may help remove any lingering doubt after Mouyal that both noncompete and nonsolicitation covenants in Georgia can define their territories by reference to the actual or prospective customers contacted by the ex-employee instead of by reference to geographical terms.

In AGA, LLC v. Rubin, the court of appeals struck down a noncompete covenant that prohibited an employee-gastroenterologist, for eighteen months after termination of his employment, from rendering gastroenterology services, except in an emergency situation, at or within five miles of any hospital where he regularly performed services for his employer-group at any time during the term of his employment. The court of appeals held this noncompete covenant was facially invalid "because the territory was not determinable until the time of the employee's termination." In doing so, the court overruled its earlier opinion, which upheld a noncompete covenant with a similarly "moving"
Thus, Rubin confirms that drafting an enforceable noncompete covenant under Georgia law will continue to be plagued by the difficulty of defining a territory that accurately reflects the geographic area in which the employee works not only at the time of entering into the noncompete covenant, but also when the employee is terminated, which could be years later.

In *Iero v. Mohawk Finishing Products, Inc.*, David Iero was a former salesman for Mohawk who lived and was based in Georgia for twelve years. He quit and went to work for a competitor, which prompted a sword rattling letter from Mohawk reminding him of his noncompete and nondisclosure covenants. Iero then filed suit in Fulton Superior Court seeking a declaratory judgment and injunctive relief against enforcement of the covenants. Mohawk moved to dismiss pursuant to the New York forum selection clause in Iero's employment agreement.

The trial court dismissed the case, and the court of appeals affirmed. Although it was undisputed that the covenants were invalid under Georgia law, the court held it would not violate Georgia public policy to enforce the "freely negotiated forum selection clause," at least so far as Iero "does not even address whether the New York court would apply New York law." In reaching this conclusion, the court of appeals held it was not enough that litigating in New York would be inconvenient for Iero absent any contention, much less any proof, that "enforcement of the forum selection clause would deprive him of his day in court."

To be sure, the court of appeals left open the possibility that it might have ruled differently upon a showing that a New York court would uphold the covenants. Moreover, *Iero* does not indicate whether a Georgia court would honor a judgment or injunction entered by a New York court enforcing the covenants.

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263. *Id.* at 670, 534 S.E.2d at 137.
264. *Id.* at 672, 534 S.E.2d at 139.
265. *Id.*
266. *Id.*
267. *Id.*
B. Nonsolicitation Covenants

In Gill v. Poe & Brown of Georgia, Inc., the Court of Appeals of Georgia struck down an eighteen month nonsolicitation-of-customers covenant under Georgia law. In doing so, the court of appeals reversed the trial court's order granting partial summary judgment to Poe & Brown and denying Gill's cross-motion for summary judgment on the enforceability of the nonsolicitation covenant.

Gill was an insurance agent who signed the nonsolicitation covenant in 1992 while he was employed by the predecessor of Poe & Brown. The nonsolicitation covenant was assigned to Poe & Brown without Gill's consent when it purchased the assets of his previous employer. With this background, the court held as follows: (1) The assignment of the nonsolicitation covenant was valid even without Gill's consent, and (2) relying primarily on Smith Adcock & Co. v. Rosenbohm, the nonsolicitation covenant was overbroad and unenforceable because it prohibited Gill from seeking business in competition with his ex-employer from any persons or entities that were his actual or actively sought customers at any time during Gill's employment even though they may have ended their relationship with Poe & Brown or its predecessor as many as four years before Gill was terminated in 1996. As to former clients, the court of appeals found that "Gill's employer had no legitimate business interest in preventing Gill's solicitation." Moreover, the court of appeals suggested that nonsolicitation-of-customers covenants will not pass muster, unless, like the nonsolicitation covenant that was at issue in Rosenbohm, they are limited to customers or prospects with which the employee, or perhaps the employer for existing accounts set up by the employee, had some business contact within at least the two years immediately prior to termination of employment.

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269. Id. at 580, 524 S.E.2d at 329.
270. Id.
271. Id. at 580-81, 524 S.E.2d at 329-30.
274. 241 Ga. App. at 583, 524 S.E.2d at 331.
275. Id.
276. Id. at 582, 524 S.E.2d at 331; see also W.R. Grace & Co. v. Mouyal, 262 Ga. 464, 466, 422 S.E.2d 529, 532 (1992).
V. AGENCY

A. CEO Possessed “Inherent Agency”

In *Family Partners Worldwide, Inc. v. SunTrust Bank, Atlanta*, Family Partners Worldwide, Inc. operated under a corporate structure with two corporations: one arranged and facilitated international adoptions (“Family Partners Worldwide”) and the second operated as a foundation raising funds for the adoptions (“Family Partners Foundation,” and together with Family Partners Worldwide “Family Partners”). Both corporations had the same corporate governance with identical boards of directors and with Keith McGrew as their CEO. McGrew allegedly embezzled funds from Family Partners Worldwide. After McGrew set up a bank account with SunTrust Bank under the Family Partners Foundation name, he “allegedly used [that account] to convert funds from Family Partners.” In its attempt to recover the embezzled funds, Family Partners sued SunTrust, “contending SunTrust was liable because it did not require a corporate resolution or certificate of authority to open either account.” In granting summary judgment in favor of SunTrust, the trial court held the CEO had “inherent agency power to open the accounts.”

On appeal, the court of appeals held SunTrust did not know of the alleged embezzlement; therefore, the only issue to be determined was “whether McGrew as CEO had either the authority or inherent agency power to open the account and designate himself as the authorized signatory for withdrawals.” Inherent agency power is defined as “the power of an agent which is derived not from authority, apparent authority or estoppel, but solely from the agency relation and exists for the protection of persons harmed by or dealing with a servant or other agent.” As CEO, McGrew had the following powers and characteristics: (1) He was the most senior executive in both corporations; (2) he had uncontested power to operate the corporation on a daily basis; (3) he had the authority to execute contracts on behalf of the corporation; and

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278. *Id.* at 618, 530 S.E.2d at 743.
279. *Id.*
280. *Id.*
281. *Id.*
282. *Id.* at 619, 530 S.E.2d at 743.
(4) he had the authority to hire and fire employees. Additionally, "McGrew sat on the finance committee of the boards and had complete authority to oversee and supervise the financial end of the businesses, including the authority to communicate with outside accountants and attorneys." McGrew "had the implied power to interact with banks by obtaining information in receiving and reconciling monthly bank statements," and "he had the authority to endorse and deposit checks in Family Partners' other three accounts at NationsBank, wire monies from those accounts, and serve as an authorized sole signatory on corporate checks and payroll checks drawn at NationsBank." He had the "implied authority to incur reasonable business expenses, purchase supplies, and pay invoices and other corporate debts such as payroll taxes, refunds, liability insurance, and repair bills." In light of the overwhelming evidence and "plenary scope of his power," McGrew's actions to withdraw the monies from the SunTrust accounts "would be within the ordinary course of business of Family Partners and the foundation."

Regardless of the overwhelming evidence, Family Partners argued SunTrust remained liable even though McGrew had inherent agency power "because SunTrust failed to follow its own internal policy requiring a corporate resolution or Certificate of Authority to establish a corporate account." In finding for SunTrust, the court of appeals held Family Partners' argument failed because the United States District Court for the Northern District of Georgia has held "that 'a bank's failure to follow its own internal operating procedures [regarding opening accounts] cannot give rise to legal liability' for embezzlements from that account." Moreover, the Georgia Supreme Court has held that even though "the bank could easily protect its interest by requiring a proper corporate resolution showing the agent's authority to act for the corporation, that method is not the exclusive one for establishing the existence either of authority or of inherent agency power to open a bank account for the corporation."

284. Id., 530 S.E.2d at 743-44.
285. Id., 530 S.E.2d at 744.
286. Id. at 619-20, 530 S.E.2d at 744.
287. Id. at 620, 530 S.E.2d at 744.
288. Id.
289. Id.
291. Id.
VI. BANKING

A. Breach of Duty

In Wachovia Bank of Georgia, N.A. v. Reynolds, Frances Reynolds purchased a certificate of deposit ("CD") from Wachovia Bank of Georgia, N.A. ("Wachovia"). Reynolds purchased the CD as attorney-in-fact for her brother, Bernard S. Bailey, Jr., who was mentally incapacitated and vulnerable to criminal activity. When Reynolds purchased the $64,000 CD, Reynolds unequivocally instructed Wachovia that "everything pertaining to him comes to my address," and Wachovia issued an initial deposit receipt listing "Bernard S. Bailey, Jr. by Francis B. Reynolds, POA" as the bank's customers. However, Wachovia did not follow Reynolds' instructions and "opened Mr. Bailey's CD account in his name alone and sent everything pertaining to the account to Mr. Bailey directly based on his existing customer profile as one of the bank's credit card customers." Not surprisingly, when Mr. Bailey's CD matured, he went to Wachovia and withdrew his entire account in cash. After receiving the $66,722 cash in a canvas bag, Mr. Bailey walked out of the bank. When Reynolds attempted to renew the CD, she was told Bailey had withdrawn all of his money. When Reynolds asked Bailey about the money, he told her "that he had asked a maintenance man to hide the money in the attic of his apartment." After a search of Bailey's attic proved futile, Reynolds and Bailey filed suit against Wachovia for recovery of the money plus attorney fees. After a jury verdict, the trial court entered a judgment in favor of Reynolds and Bailey that included an award of bad faith attorney fees. On appeal, Wachovia argued that

(a) its duty of care extended to Mr. Bailey alone as its sole depositor-customer and the principle for whom Ms. Reynolds acted as agent in establishing his CD account; (b) Mr. Bailey's damages resulted from an unforeseeable intervening criminal act of a third party foreclosing

293. Id. at 1, 533 S.E.2d at 744.
294. Id.
295. Id.
296. Id. at 1-2, 533 S.E.2d at 744.
297. Id. at 2, 533 S.E.2d at 744.
298. Id.
299. Id.
recovery against Wachovia; and (c) there was no evidence that Mr. Bailey was entitled to OCGA § 13-6-11 attorney's fees for bad faith.  

The Court of Appeals of Georgia affirmed the trial court's holding and affirmed the jury verdict, which totaled $95,598.34.  

On appeal, Wachovia attempted to shift the analysis to its "duties owed when the CD was withdrawn" as opposed to its "obligations and duties owed when Ms. Reynolds originally set up the CD." However, the court of appeals was quick to identify that, as a financial institution, Wachovia had a duty to issue the CD

in a manner that complied with the wishes of the customer, so long as the wishes of the customer were not contrary to applicable law, and that the financial institution maybe liable to the customer or third party beneficiary for mishandling the transaction including improperly advising the customer how the certificate should be established or changed to comply with the wishes of the customer.

The court of appeals concluded that Ms. Reynolds' actions in opening the account were clear and that there was no evidence contrary to applicable law. The court not only highlighted Ms. Reynolds' precision in instructing Wachovia about the ownership and information flow regarding the CD, but also noted that Wachovia had breached its duty by failing to produce a signature card before permitting Bailey to withdraw his money.  

Addressing Wachovia's claim that the superior court should have granted its motion for a directed verdict based on "the unforeseeable intervening criminal act of a third party," the Court of Appeals of Georgia specified that the intervening criminal act was, in fact, foreseeable by Wachovia and therefore could not operate to bar recovery by Reynolds and Bailey.  

Lastly, the Court of Appeals of Georgia affirmed the trial court's denial of Wachovia's motion for directed verdict as to bad faith attorney fees under O.C.G.A. section 13-6-11. The record revealed expert testimony had been presented to determine reasonable banking practices, and "[c]ontrary to [the expert testimony], Wachovia opened Mr.
Bailey's CD account in his name alone not annotating its records to reflect that the account was established pursuant to a power of attorney or otherwise noting special circumstances.\footnote{308}

B. Although Bank Failed to Adhere to Internal Procedures, Because it Strictly Complied With the International Chamber of Commerce Rules, Bank Was Not Liable

In Banco Surinvest, S.A. v. SunTrust Bank,\footnote{309} the United States District Court for the Northern District of Georgia issued an opinion regarding the International Chamber of Commerce's Uniform Rules for Collections as detailed in ICC Publication No. 522 ("URC 522") and Georgia's Commercial Code as set forth in O.C.G.A. sections 11-4-501 to -504.\footnote{310} Banco Surinvest, S.A. ("Banco") helped finance a peanut trade between Herbert A. H. Behrens, S.R.L. ("Behrens") and the Collins Brokerage Company, LLC ("Collins Brokerage"). SunTrust Bank, Atlanta ("SunTrust") was appointed to be the collecting bank and to forward Collins Brokerage's payments to Banco. After Collins Brokerage failed to make full payment under its agreement with Banco, Banco brought suit against Collins Brokerage and SunTrust. Banco's claim against SunTrust alleged that SunTrust violated its duties under the agreement with Banco.\footnote{311} SunTrust allegedly breached its duties

by (1) failing to procure payment in full and failing to perfect security interests in the shipments before delivering the title documents, (2) allowing Collins Brokerage to draft and sign inadequate trust receipts and commitment letters, and (3) failing to monitor Collins Brokerage's payments and notify Banco when Collins Brokerage did not pay the Remittances in full.\footnote{312}

However, "[n]either the contract, URC 522, nor Georgia Law imposed upon SunTrust any duties to perform the aforementioned tasks."\footnote{313} SunTrust was not required to perfect a security interest or to accept only payments in full before transferring any title documents, and no facts in the complaint support a claim that SunTrust "breached the contract or exceeded the bounds of reasonableness by failing to perform these tasks."\footnote{314} Additionally, the court held SunTrust should not have

\begin{footnotes}
\footnotetext{308}{Id.}
\footnotetext{309}{78 F. Supp. 2d 1366 (1999).}
\footnotetext{310}{Id. at 1368-71.}
\footnotetext{311}{Id. at 1368.}
\footnotetext{312}{Id.}
\footnotetext{313}{Id.}
\footnotetext{314}{Id. at 1368-69.}
\end{footnotes}
been required to look beyond the contract because URC 522 specifically “instructs collecting banks to act only upon the instructions given by the remitting bank,” and the comments to URC 522 warn banks they should “not look elsewhere for instructions.” Article 8 of the URC 522 further provides:

Where the remitting bank instructs that either the collecting bank or drawee is to create documents (bills of exchange, promissory notes, trust receipts, letters of undertaking or other documents) that were not included in the collection, the form and wording of such documents shall be provided by the remitting bank, [sic] otherwise the collecting bank shall not be liable or responsible for the form and wording of any such document provided by the collecting bank and/or the drawee.

SunTrust had no liability under Article 8 because Banco in fact had not provided specific wording for the trust receipts to be collected. SunTrust also was “otherwise instructed to release the title documents before receiving full or even partial payment.” Furthermore, SunTrust’s failure to notify Banco of Collins Brokerage’s failure to pay the remittances in full did not impose liability on SunTrust. Collins Brokerage honored the documentary drafts by executing the trust receipts and commitment letters, accepting the title documents from SunTrust, and accepting the peanut shipments. Therefore, SunTrust did not violate the contract, which did not describe when honor or dishonor occurred. Although Collins Brokerage’s failure to pay under the trust receipts may have constituted a default, the default did not “amount to dishonor of the documentary drafts.”

C. Title V of the Gramm-Leach-Bliley Act

The Gramm-Leach-Bliley Act, which is commonly referred to as the Financial Services Modernization Act (“FSMA” or “the Act”) was enacted on November 12, 1999, and all rules will technically take effect on November 12, 2000. Because of the significant burden that the Act places on financial institutions, a period of voluntary compliance has been established and will be in effect from November 12, 2000 until July

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315. Id. at 1369; see also ICC Uniform Rules for Collection: A Commentary of 13 (1995).

316. 78 F. Supp. at 1369.

317. Id.

318. Id.

319. Id. at 1369-70.

320. Id. at 1370.

1, 2001. Essentially, the Act provides sweeping changes to the Glass-Stegall Act of 1933 and outlines privacy policy standards that will govern the use of consumer information that is collected by financial institutions. The Act covers a wide range of financial institutions and dictates that these financial institutions must protect and safeguard customer information and records. At its core, the privacy policy standards require a financial institution to provide notice of the privacy policy to its consumer customers and to provide opt-out notice before sharing any consumer information with third parties. Additionally, any company receiving nonpublic personal information is automatically subjected to limitation on re-use of that information.

Financial institutions are defined to include all entities in banking, lending, financial or investment advisory; mutual fund, securities, insurance, or trust services; as well as activities simply deemed “financial in nature” or incidental to a financial activity. The Act is intended to cover all “personally identifiable financial information” and information other than “publicly available information.” The Act is broadly drafted to include that all information received in connection with a financial transaction including personal information that is not intrinsically financial. Financial institutions must provide annual notice of the privacy policies, which must be clear and conspicuous and inform customers (1) of the categories of information collected and disclosed, (2) the sources of such information, (3) the usage of the information, and (4) to whom the information is disclosed or may be disclosed in the future. Although the restrictions are broad and wide within the Act, leeway is provided to the financial institutions regarding use of the protected information. As an example, financial institutions may release the account numbers of current customers to that same financial institution’s own credit card company.

As with every other financial institution covered by the Act, Georgia banks will need to wade through the massive revisions in the Act and prepare for the modernization of the financial services industry.

323. Tit. V(A) § 501.
324. Id. § 502.
325. Id.
326. Id. § 503.
327. Id. § 505.
328. Id. § 503.
329. Id. § 502.
D. Legislative Changes

The 1999 session of the General Assembly of Georgia passed several amendments to the Code as it relates to financial institutions. The most notable are summarized below.

1. Modification to Specific Limitations on Financial Institution Operations or Powers. To highlight discretion permitted by the Code, and to provide parity with other federally insured financial institutions, the Commissioner may modify or amend qualifying or limiting requirements imposed on financial institutions including: collateral requirements and limits on the amounts of obligations owing to it from any one person or corporation, loan to value or other limitations in real estate lending, limitations on the amount of investments and stock or other capital securities of a corporation or other entity, and limitations on the amount of bank acceptances to be issued. Before any order ratifying or amending limitations is issued, the Commissioner must determine "that such activity will not present undue safety and soundness risks to the financial institution or institutions involved."

2. Ownership of Certain Public Property. O.C.G.A. section 7-1-282 was further amended to include specific reference to permit a bank to own or lease certain public real property and facilities. The amended Code section specifically references purchase of or construction of a municipal building, school building, or other similar state, local, or other governmental authority facility if, as holder of legal title, the purchases for the purposes of leasing the facility to a municipality or other public or governmental authority that has the authority to enter into the lease and the resources sufficient to make lease payments as they come due, is authorized to levy taxes or is backed by the taxing authority of another political subdivision.

3. Acquisition of Out-of-State Banking Institutions. O.C.G.A. section 7-1-288(c) was revised to remove the limitation providing that a bank could only acquire and hold for its own accounts banking institutions that were located primarily within Georgia. As revised, the
statute now only limits a bank's ownership to consist primarily of depository financial institutions.336

4. Bank's Board of Directors. O.C.G.A. section 7-1-480,337 which outlines the requirements for the board of directors of a bank or trust company, was amended to provide a carve-out in the situation involving a bank that has branches in states other than Georgia. Whereas the prior language required each director to live within forty miles of any bank office located in Georgia, the new language requires that "the residency of directors [be] consistent with the bank's articles of incorporation and bylaws."338 Additionally, banks may now establish "non policy-making regional boards of directors" that will operate and exercise certain powers, duties and responsibilities delegated to it by the board.339

5. Bank Branch Offices. The various provisions for the establishment of bank branch offices were amended to include a new listing of factors that the department will use in its consideration of the application for establishing any new branch office.340 The revised language in O.C.G.A. sections 7-1-628.7(e) and (f)341 provides for heightened cooperation, regulation, supervision and reporting by branches established in interstate banking and branching by merger.

7. Mortgage Brokers and Mortgage Lenders. The revisions to Chapter 1 of Title VII also included a substantial revision of the code sections regarding mortgage brokers and mortgage lenders to impose new licensing, educational, and other requirements.342

VI. PROFESSIONAL ASSOCIATIONS: LEGISLATIVE CHANGES

The 1999 session of the General Assembly of Georgia passed several amendments to Title 43—The Professions and Businesses title of the Code. The most notable are summarized below.

336. Id.
337. Id. § 7-1-480.
338. Id.
339. Id. § 7-1-482(d).
340. Id. § 7-1-602(a)(2).
341. Id. § 7-1-628.7(e) and (f).
342. Id. § 7-1-1000 to -1018.
A. Athlete Agents

The revisions amended provisions affecting the regulation of athlete agents, provided additional grounds for refusing to register or discipline an athlete agent, amended the provisions relating to notice of the signing of an agent contract that is given to an institution of higher education and to the Georgia Athlete Agent Regulatory Commission, provided for certain terms to be included in agent contracts, and authorized an institution of higher education to bring a civil action against an athlete agent for the recovery of damages.\(^3\)\(^4\)

B. Professional Licensing

The revisions to Title 43 also included revisions to the licensing and regulatory practices of various professions. These professions included the practice of chiropractic, the regulation of cosmetology, the education and qualifications for dental hygienist, the licensing requirements of licensed practical nurses, the licensing to practice acupuncture, the licensing and registration qualifications of private detectives and security agencies, and the regulation of athlete agents.\(^3\)\(^4\)

C. Charitable Solicitations

The Act also amended the "Georgia Charitable Solicitations Act of 1988"\(^3\)\(^4\) to change the definition of charitable organization, define solicitor agent, provide for electronic filing of certain registration forms by paid solicitors with the Secretary of State, require written consent to a criminal background investigation, change certain requirements in financial statements filed by paid solicitors, establish a time limit for the Secretary of State to register applicants as paid solicitors, require a paid solicitor to provide a charitable organization detailed records regarding solicitation campaigns, change the bonding requirements, change provisions relating to record keeping by registered charitable organizations, and require certain disclosures by paid solicitors to contributors.\(^3\)\(^4\)

D. Snow Skiing Safety

Revisions to this Title also included certain requirements with respect to snow skiing safety. The Act enumerated inherent dangers of skiing

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344. Id. ch. 43.
345. Id. §§ 43-17-1 to -23.
346. Id. §§ 43-17-2 to -5, -7 to -9, and -12.
and provided for the assumption of risk and responsibilities and duties as passengers on tramways.\textsuperscript{347} It required the posting of signs designating trails and slopes by degree of difficulty, posting of a warning notice relating to the inherent dangers of skiing, addition of snow grooming equipment and snowmobiles, and it provided for the revocation of skiing privileges of persons in violation of the Act.\textsuperscript{348}

\textsuperscript{347} Id. ch. 43-43A.
\textsuperscript{348} Id.