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ARTICLES

Business Associations

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This Article surveys noteworthy cases that the Georgia appellate courts, the United States district courts located in Georgia, and the Eleventh Circuit Court of Appeals decided during the survey period¹ as they relate to Georgia corporate, partnership, securities, and banking

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¹ The survey period is June 1, 1997 through May 31, 1998.
laws. It also highlights certain enactments by the Georgia General Assembly revising the Official Code of Georgia Annotated ("O.C.G.A.").

I. CORPORATIONS

A. Piercing the Corporate Veil

The concept of "piercing the corporate veil," to hold shareholders personally liable for the debts of the corporation, has been used by the Georgia courts in an attempt to remedy fraud or injustice. The courts, however, have failed to define precise standards to apply to rather predictable factual scenarios. Consequently, the results often seem contradictory and confused.²

Georgia courts generally frame the issue as whether the corporation is the alter ego or business conduit of its owner.³ The principal inquiry is not the composition of corporate ownership or control because, under Georgia law, a corporation and its shareholders or officers are distinct entities even if wholly-owned and controlled by an individual.⁴

To establish a claim to pierce the corporate veil, the plaintiff must show: (1) that the shareholder’s disregard of the corporate entity made it 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 personality of the corporation and the shareholder or officer no longer exist; and (3) that to adhere to the doctrine of a separate corporate entity would promote injustice or protect fraud.⁵

For the issue to be submitted to a jury, Georgia courts require evidence that the corporate arrangement is a sham used “to defeat justice, to perpetuate fraud, or to evade statutory, contractual or tort responsibility.”⁶

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⁵ J & J Materials, 214 Ga. App. at 64-65, 446 S.E.2d at 782-83. See also Derbyshire, 194 Ga. App. at 844, 392 S.E.2d at 40; Amason, 186 Ga. App. at 321, 367 S.E.2d at 108.
Every year there are a number of reported cases in which a claimant seeks to pierce the corporate veil to reach the assets of a corporation's shareholders. The inquiry is a jury question, and often these claims are tried in the course of litigation, although they may not be the main claim in a case. This activity will continue and be encouraged so long as the legislature and the courts do not develop a more workable set of legal standards to apply to veil-piercing claims.

1. The United States District Court for the Southern District of Georgia Invokes the Veil-Piercing Theory to Hold a Principal Liable for Acts of a Corporation. In Chemtall, Inc. v. Citi-Chem, Inc., the United States district court refused to allow a New Jersey corporation's sole shareholder and chief executive officer to hide behind the corporate veil and avoid liability for his fraudulent acts. Plaintiffs, Chemtall, Inc. and Pearl River Polymers, Inc., sued Citi-Chem and Calvin M. King (individually as chief executive officer of Citi-Chem) for failing to abide by a lockbox payment agreement entered into by the parties.

Chemtall, a Riceboro, Georgia company, and Pearl River Polymers, a corporation owned by Chemtall, manufactured water-treatment polymer products. Citi-Chem had an agreement with both companies to buy their products and distribute the products under the "Citi-Chem" trade name. Under a lockbox payment agreement, Citi-Chem would invoice its customers with instructions to remit their payments to a Georgia bank lockbox. From there the money would be divided pursuant to the parties' agreement. The arrangement provided that a "managing agent" would remove the funds from the lockbox and send each of the parties their appropriate share. Although King originally acted as the lockbox's managing agent, Chemtall and Pearl River soon realized that King was slow in forwarding their share, and they replaced him as managing agent with Chemtall. After the change, Chemtall and Pearl River "performed all lockbox accounting activity in Georgia, and from there sent checks to Citi-Chem in New Jersey."

A few years after Chemtall took over as managing agent of the lockbox, King began violating the original payment agreement. King,

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8. Id. at 1413.
9. Id. at 1397.
10. Id. at 1392.
11. Id. at 1393.
12. Id.
13. Id.
14. Id.
without the knowledge of Chemtall, directed its customers to send their payments to a New Jersey address.\textsuperscript{15} According to testimony from former Citi-Chem employees, Citi-Chem would send an invoice to its customers directing them to send all payments directly to a bank account set up by Citi-Chem in New Jersey.\textsuperscript{16} A copy of the invoice showing the correct lockbox address would be sent to Chemtall and Pearl River to cover up the scheme.\textsuperscript{17}

During the same period that King was diverting the customer payments to Citi-Chem, he was also diverting corporate resources to himself. King directed his employees to set up a bank account in the name of Citi-Chem, Inc., D.C. ("CCI-DC") to receive the diverted customer payments. From this account King transferred to himself a "consulting fee" of $45,000, which he used to fund a separate business, King's Liquors.\textsuperscript{18} He also used $6,000 of the funds in the CCI-DC account to purchase a BMW and "transferred two [new] automobiles out of Citi-Chem and into his own name."\textsuperscript{19}

Claiming a $152,082.80 arrearage and breach of contract, Chemtall and Pearl River sued Citi-Chem and King in a Georgia state court and obtained several Temporary Restraining Orders ("TROs").\textsuperscript{20} Citi-Chem notified its customers to disregard the TROs and to continue sending payments to the CCI-DC account.\textsuperscript{21} Shortly thereafter, Citi-Chem filed for bankruptcy protection in New Jersey.\textsuperscript{22} King invoked the corporate veil defense claiming that he signed the lockbox agreement in his capacity as Citi-Chem's president and that only the bankrupt corporation was subject to liability.\textsuperscript{23}

In order for a plaintiff to be successful in a veil-piercing claim, the plaintiff must show that the defendant disregarded the corporate form.\textsuperscript{24} In the past, Georgia courts have held that the corporate veil is sufficiently pierced when "a corporate officer participates with his

\textsuperscript{15} Id.
\textsuperscript{16} Id. at 1396.
\textsuperscript{17} Id.
\textsuperscript{18} Id. at 1397.
\textsuperscript{19} Id.
\textsuperscript{20} Id.
\textsuperscript{21} Id.
\textsuperscript{22} Id.
\textsuperscript{23} Id. at 1400.
\textsuperscript{24} Id. at 1402 (citing Heyde v. Xtraman, Inc., 199 Ga. App. 303, 306, 404 S.E.2d 607, 610 (1991)). "There must be some evidence of abuse of the corporate form. [In other words,] [p]laintiff[s] must show that the defendant disregarded the separateness of legal entities by commingling on an interchangeable or joint basis or confusing the otherwise separate properties, records or control." Id.
corporation in wrongfully converting another's property.\textsuperscript{25} Under this analogy, the district court refused to allow King the protection of the corporate veil.\textsuperscript{26} The court held that Chemtall and Pearl River produced sufficient evidence to prove that King abused the corporate veil and subjected himself to personal liability by commingling the corporation's funds with his own and directing the corporation to perpetrate fraud upon its creditors and to evade contractual responsibility.\textsuperscript{27}

2. Court Finds Sole Shareholder Individually Liable for Executing Bad Check. In Kolodkin v. Cohen,\textsuperscript{28} the Georgia Court of Appeals held that the president of a corporation can be held personally liable under O.C.G.A. section 13-6-15\textsuperscript{29} for drafting a corporate check when the account contains insufficient funds to cover the check.\textsuperscript{30} Cohen was the president, sole shareholder, and director of Amalgamated T-Shirts, Inc.\textsuperscript{31} Kolodkin and Amalgamated entered into a real property lease agreement. Amalgamated stopped doing business in October of 1995, when the corporate account did not have sufficient funds to cover the lease payment. As expected, the November payment was returned for insufficient funds. Kolodkin sued Cohen in his individual capacity under O.C.G.A. section 13-6-15 for drafting the check.\textsuperscript{32} O.C.G.A. section 13-6-15 provides as follows:

\begin{quote}
Notwithstanding any criminal sanctions which may apply, any person who makes, utters, draws, or delivers any check, draft, or order upon any bank, depository, person, firm, or corporation for the payment of money, which drawee refuses to honor the instrument for lack of funds or credit in the account from which to pay the instrument or because the maker has no account with the drawee, and who fails to pay the same amount in cash to the payee named in the instrument within ten days after a written demand therefor, as provided in subsection (c) of this Code section, has been delivered to the maker by certified mail shall be liable to the payee, in addition to the amount owing upon such check, draft, or order, for damages of double the amount so owing, but
\end{quote}

\textsuperscript{25} Id. (citing DCA Architects, Inc. v. American Bldg. Consultants, 203 Ga. App. 598, 600, 417 S.E.2d 386, 388-89 (1992)).
\textsuperscript{26} Id. at 1413.
\textsuperscript{27} Id. at 1403-04.
\textsuperscript{29} O.C.G.A. § 13-6-15 (Supp. 1998).
\textsuperscript{30} 230 Ga. App. at 387, 496 S.E.2d at 518.
\textsuperscript{31} Id. at 385, 496 S.E.2d at 517.
\textsuperscript{32} Id., 496 S.E.2d at 516-17.
in no case more than $500.00, and any court costs incurred by the
payee in taking the action. 33

Although this Code section had not been interpreted in Georgia, the
court found that the statute appeared to create a limited exception to the
general corporate principle that an individual who signs in a representa-
tive capacity is not personally liable. 34 The court reasoned that
nowhere in the Code was there any "language limiting liability for a
maker acting in a representative capacity." 35 The court felt that had
the Georgia General Assembly intended to limit liability of persons
signing in a representative capacity, it would have done so in the
Code. 36

3. Court Refuses to Pierce the Corporate Veil Without
Evidence of Fraud. In General Insurance Services, Inc. v. Marcola, 37
the Georgia Court of Appeals was asked to reverse a grant of judgment
notwithstanding the verdict for defendant, Karl Byers. 38 Plaintiff sued
Karl Byers individually as president of a corporation that had breached
a contract to purchase plaintiff's corporation. 39 Plaintiff claimed that
"Karl Byers agreed to purchase plaintiff's [corporation] while concealing
from her his intent to transfer his interest immediately to the third
parties, ... to whom [she] had previously refused to sell her [busi-
ness]." 40

The court refused to pierce the corporate veil and impose liability upon
the buyer of a business. 41 In its explanation the court argued that
"[t]he corporation is prima facie a distinct legal entity with rights and
liabilities which are separate from those of [its shareholders]." 42 "One
who deals with a corporation as such an entity cannot, in the absence of

34. 230 Ga. App. at 386, 496 S.E.2d at 517.
35. Id. (citing O.C.G.A. § 11-3-404 (1994 & Supp. 1998) (pertaining "to all persons
purporting to act as or on behalf of a corporation without authority to do so"); O.C.G.A.
signs his or her own name to an instrument").
36. Id.
38. Id. at 145, 497 S.E.2d at 680.
39. Id. at 144, 497 S.E.2d at 680.
40. Id. at 149, 497 S.E.2d at 683.
41. Id., 497 S.E.2d at 684.
42. Id., 497 S.E.2d at 683 (citing Midtown Properties, Inc. v. George F. Richardson, 139
Ga. App. 182, 185, 228 S.E.2d 303, 308 (1976); Jones v. Adamson's, Inc., 147 Ga. App. 282,
283, 248 S.E.2d 514, 516 (1978)).
fraud, deny the legality of the corporate existence for the purpose of holding the owner liable."\(^4\)

According to the court, the circumstances did not lend themselves to a conclusion that the defendant corporation (GIS) was a sham or that defendant Karl Byers made false or misleading representations to plaintiff that would amount to fraud.\(^4\) Thus, the court concluded that the trial court correctly granted a judgment notwithstanding the verdict in favor of Karl Byers.\(^4\)

B. Personal Liability for Preincorporation Transactions

In Zuberi v. Gimbert,\(^46\) the Georgia Court of Appeals held that an individual who signed a commercial lease on behalf of a nonexistent corporation was personally liable for damages to the warehouse.\(^47\)

Under O.C.G.A. section 14-2-204, all persons purporting to act as or on behalf of a corporation, with actual knowledge there was no incorporation, are jointly and severally liable for all liabilities created while so acting.\(^48\)

In Zuberi, defendant signed a commercial lease for the use of a warehouse "as the purported representative of a non-existent corporation, 'ATM Manufacturing, Inc.'\(^49\) Although Zuberi testified that he was acting on behalf of ATM America, no evidence indicated that ATM America existed as a corporation, and regardless, the name on the lease was ATM Manufacturing, Inc., not ATM America Corp.\(^50\) The attorneys for Zuberi argued that he acted on behalf of ATM Enterprises, Inc. and "meant to sign on behalf of this existing corporation."\(^51\)

Whether Zuberi made a simple mistake in his signature was not relevant to the issue of liability.\(^52\) The court of appeals found the difference in names substantial and did not involve the mere abbreviation of a longer official corporate name.\(^53\) Zuberi tried to apply a

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44. *Id.* (quoting Hickman v. Hyzer, 261 Ga. 38, 41, 401 S.E.2d 738, 740 (1991)).

45. *Id.*


47. *Id.* at 473, 496 S.E.2d at 742.


49. 230 Ga. App. at 472, 496 S.E.2d at 741.

50. *Id.* at 472-73, 496 S.E.2d at 742.

51. *Id.* at 473, 496 S.E.2d at 742.

52. *Id.*

53. *Id.* (distinguishing Pinson v. Hartsfeld Ctr., 191 Ga. App. 459, 461, 382 S.E.2d 136, 138 (1989), which held that a mere "misnomer" is not enough to impose personal liability
corporation by estoppel argument, suggesting that plaintiffs believed they were dealing with a corporation.\textsuperscript{54} The court found that Zuberi signed on behalf of a nonexistent corporation and, regardless of plaintiffs' belief, he was precluded from asserting the defense of corporation by estoppel.\textsuperscript{55}

\textbf{C. Successor Liability: Product Liability for Products Manufactured by Predecessor Corporation}

In \textit{Farmex, Inc. v. Wainwright},\textsuperscript{56} the Georgia Supreme Court faced the issue of imposing liability on a corporation based upon the "continuation theory" of liability. Third-party plaintiffs were sued when their trailer became unhitched and struck a vehicle. They alleged that a hitch pin caused the accident and filed a third-party complaint against Farmex, even though the hitch pin involved had been designed and manufactured by JA-BIL, Inc. Farmex purchased JA-BIL, Inc. in an asset purchase transaction and continued selling the hitch pins manufactured by JA-BIL, Inc.\textsuperscript{57}

The trial court granted summary judgment in favor of Farmex, concluding that, under the continuation theory, Farmex was not the "manufacturer" of the hitch pin for purposes of strict liability.\textsuperscript{58} The court of appeals reversed, imposing liability on Farmex, even though it did not find present the elements of "the continuation theory, as traditionally applied."\textsuperscript{59}

An asset sale generally will not produce liability upon the purchaser for the acts of the seller unless one of four exceptions is present: "(1) there is an agreement to assume liabilities; (2) the transaction is, in fact, a merger; (3) the transaction is a fraudulent attempt to avoid liabilities; or (4) the purchaser is a mere continuation of the predecessor corporation."\textsuperscript{60} Departing from any of the foregoing recognized exceptions, the court of appeals reversed the trial court's grant of summary judgment reasoning that (1) the manufacturer is better able to protect itself and bear the cost while the consumer is helpless; and (2) the manufacturer

\begin{itemize}
\item \textsuperscript{54} \textit{Id.}
\item \textsuperscript{55} \textit{Id.}
\item \textsuperscript{56} 269 Ga. 548, S.E.2d 802 (1998).
\item \textsuperscript{57} \textit{Id.} at 548-49, 501 S.E.2d at 803-04.
\item \textsuperscript{58} \textit{Id.} at 548, 501 S.E.2d at 803.
\item \textsuperscript{59} \textit{Id.} (citing Corbin v. Farmex, 227 Ga. App. 620, 622, 490 S.E.2d 395, 399 (1997)).
\item \textsuperscript{60} 227 Ga. App. at 621, 490 S.E.2d at 397 (citing Bullington v. Union Tool Corp., 254 Ga. 283, 284, 328 S.E.2d 726, 727 (1985)).
\end{itemize}
is the instrumentality to look to for improvement of the product's quality.\textsuperscript{61}

Judge Smith dissented from the court of appeals decision reversing the trial court's grant of summary judgment.\textsuperscript{62} Judge Smith argued that the court was bound by the Georgia Supreme Court's decision in \textit{Bullington v. Union Tool Corp.},\textsuperscript{63} and that the majority opinion here did not apply because the new corporation never produced the product.\textsuperscript{64}

The Georgia Supreme Court granted certiorari to review the opinion of the court of appeals.\textsuperscript{65} The court found that strict liability applies only to the "manufacturer of any personal property sold as new property" and not to a "product seller."\textsuperscript{66} The common law continuation theory applies only when there is some identity of ownership.\textsuperscript{67} The supreme court agreed with the court of appeals that there was no identity of ownership with respect to the assets purchased from JA-BIL by Farmex and, thus, the common law continuation theory did not apply.\textsuperscript{68}

The supreme court found that although Farmex continued the general business of manufacturing, warehousing, and selling hitch parts, it "did not continue to design or manufacture hitch pins of the type that it acquired from JA-BIL."\textsuperscript{69} The court distinguished a "manufacturer" from a "product seller," holding that the purpose behind strict liability, to protect defenseless victims from manufacturing defects, could not be advanced by imposing strict liability upon a "product seller."\textsuperscript{70}

\subsection*{D. Dissenting Shareholder's Rights}

In \textit{Croxton v. MSC Holding, Inc.},\textsuperscript{71} the Georgia Court of Appeals faced the question of how the statutory appraisal remedy for valuation of shares of dissenting shareholders applies when a dissenting shareholder has an independent contract requiring the corporation to buy his shares. Plaintiff Croxton was an employee and a fifty percent shareholder of defendant corporation for a number of years. Croxton's employment agreement provided that, upon his termination without cause, the

\begin{itemize}
\item[61.] Id. at 622, 490 S.E.2d at 398 (quoting Cyr v. B. Offen & Co., 501 F.2d 1145, 1154 (1st Cir. 1974)).
\item[62.] Id. at 624, 490 S.E.2d at 399 (Smith, J., dissenting).
\item[63.] 254 Ga. 283, 328 S.E.2d 726 (1985).
\item[64.] 227 Ga. App. at 624, 490 S.E.2d at 399.
\item[65.] Farmex, 269 Ga. at 549, 501 S.E.2d at 803.
\item[66.] Id. (quoting O.C.G.A. §§ 51-1-11, -11.1 (Supp. 1998)).
\item[67.] Id., 501 S.E.2d at 803-04.
\item[68.] Id., 501 S.E.2d at 804.
\item[69.] Id.
\item[70.] Id. at 550, 501 S.E.2d at 804.
\end{itemize}
company would purchase his shares. Under the contract the purchase price for the shares was predetermined.72

The corporation terminated Croxton without cause in August 1995.73 In September 1995, the company "announced its intent to sell certain corporate assets."74 Soon thereafter, Croxton's attorney sent notice to the corporation stating that, if the proposed sale took place, the shareholder "intended to demand payment for his shares as provided in Article 13 of the Georgia Business Corporation Code (the statutory appraisal procedure)."75 Croxton sent a "dissenting shareholder's form" to the corporation in December, demanding the "fair value" of his stock pursuant to O.C.G.A. section 14-2-1302.76

When the corporation determined that the value of Croxton's shares was zero, defendant demanded his contractually-set price of $400,000.77 In March 1996, the corporation filed a petition pursuant to O.C.G.A. section 14-2-1330 which it denominated as a "nonjury equitable valuation proceeding to determine the fair value of [plaintiff's] shares."78 The corporation claimed that, under Grace Bros. v. Farley Industry,79 the statutory proceeding for a dissenting shareholder's demand constituted Croxton's exclusive remedy.80 The trial court agreed with the corporation, "finding that Croxton's election to pursue dissenter's rights barred any claim he might have had under his contract."81

The court of appeals disagreed with the trial court's understanding of Grace Bros.82 According to the court of appeals, Grace Bros. specifically recognized that individual shareholders may have individual, independent claims and may have a status which differs from other shareholders.83 For those who occupy the status of dissenting shareholders, the only remedy is the statutory appraisal remedy if the shareholder's objection is essentially a complaint regarding the price of his shares.84

The court of appeals reversed the trial court's holding reasoning that Croxton's claim constituted an independent contract claim, not merely

72. Id. at 179, 489 S.E.2d at 77.
73. Id., 489 S.E.2d at 78.
74. Id.
75. Id.
76. Id.
77. Id. at 179-80, 489 S.E.2d at 78.
78. Id. at 180, 489 S.E.2d at 78.
80. 227 Ga. App. at 180, 489 S.E.2d at 78.
81. Id.
82. Id. at 180-81, 489 S.E.2d at 78.
83. Id. at 181, 489 S.E.2d at 79.
84. Id.
a derivative claim. Croxton did have standing as a dissenting shareholder because he notified the corporation that, if they sold the assets, he would demand payment under O.C.G.A. section 14-2-1320(b). However, this demand did not constitute an "exclusive" election of remedies of a dissenting shareholder. Further, the court of appeals found that Title 13 contained no statutory provision that could deprive Croxton of his contractual right to payment for his shares as provided in his contract.

E. Shareholders Rights Plan: Georgia Law Gives Board of Directors Sole Discretion

The United States District Court for the Northern District of Georgia determined in Invacare Corp. v. Healthdyne Technologies, Inc. that adopting bylaws proposed by tender offeror, requiring removal of the poison pill provision, would violate a Georgia statute vesting in the board of directors discretion to determine terms and conditions of a shareholders rights plan. In Invacare Healthdyne's Board of Directors implemented a shareholders rights plan ("poison pill") to help protect against hostile takeovers. Under the plan, each shareholder, with the exception of the hostile bidder, would have the right to purchase additional shares of common stock at half-price in takeover situations. Healthdyne's rights plan also had a "continuing director" feature, which required that any redemption or amendment of the rights plan be approved by one or more directors who were members of the Board prior to the adoption of the rights plan, or who were subsequently elected to the Board with the recommendation and approval of the other continuing directors.

Invacare sought a preliminary injunction to have the continuing director provision declared invalid. In addition, Invacare proposed a bylaw that would require the current Board of Directors of Healthdyne to amend the rights plan to eliminate the continuing director feature. Invacare argued that the continuing director provision was illegal under

85. Id. at 181-82, 183, 489 S.E.2d at 79, 80.
86. Id. at 182, 489 S.E.2d at 79.
87. Id.
88. Id.
90. Id. at 1582.
91. Id. at 1579.
92. Id.
93. Id.
94. Id.
95. Id.
section 801(b) of the Georgia Code because it was a significant limitation on the Board of Directors' powers, not included in the articles of incorporation or the bylaws.96 Additionally, Invacare argued that the continuing director provision of the rights plan violated the directors' fiduciary duties.97

The court, relying on the Georgia Business Corporation Code (the "Business Code"),98 made a determination that the implementation of the shareholders rights plan was within the authority of the Board of Directors and not a violation of the directors' fiduciary duties.99 The Business Code provides that:

A corporation may issue rights, options, or warrants with respect to the shares of the corporation whether or not in connection with the issuance and sale of any of its shares or other securities. The board of directors shall determine the terms upon which the rights, options, or warrants are issued, their form and content, the consideration for which they are to be issued, and the terms and conditions relating to their exercise, including the time or times, the conditions precedent, and the prices at which and the holders by whom the rights, options, or warrants may be exercised.100

In addition, O.C.G.A. section 14-2-624(c) states that:

[n]othing contained in Code section 14-2-601 shall be deemed to limit the board of directors' authority to determine, in its sole discretion, the terms and conditions of the rights, options, or warrants issuable pursuant to this Code section. Such terms and conditions need not be set forth in the articles of incorporation.101

Invacare relied primarily on a decision handed down by the New York Supreme Court.102 In Bank of New York v. Irving Bank Corp.,103 the court invalidated a continuing director provision because it restricted the power of the board of directors to manage the corporation.104 The New

96. Id. at 1580 (quoting O.C.G.A. § 14-2-801(b) (1994) which provides: All corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, its board of directors, subject to any limitation set forth in the articles of incorporation, bylaws approved by the shareholders, or agreements among the shareholders which are otherwise lawful.).
97. Id. at 1581.
100. O.C.G.A. § 14-2-624(a) (1994).
101. Id. § 14-2-624(c).
102. 968 F. Supp. at 1580.
103. 528 N.Y.S.2d 482 (Sup. Ct. 1988).
104. 968 F. Supp. at 1580.
York court's holding was based on a New York statute which provided that "a restriction of the board's power to manage the business of the corporation is invalid unless . . . all of the incorporators or all of the shareholders of record have authorized such provision on the certificate of incorporation . . . ." The district court in Invacare found that no such limitation exists under the Georgia Business Code and that O.C.G.A. section 14-2-624(c) granted the board of directors sole discretion to determine the terms and conditions of shareholder rights agreement.

The district court went even further to note that Georgia corporate law embraced the concept of continuing directors as part of a defense against hostile takeover. The concept of the continuing directors approval is set forth in the Georgia Fair Price Statute. Additionally, the Georgia Business Combination Statute specifically provides that a bylaw opting into the statute cannot be repealed without "the affirmative vote of at least two-thirds of the continuing directors." Based on this analysis, the court found Invacare's proposed bylaw invalid as a matter of law in Georgia.

F. Legislative Changes

The 1997 Session of the General Assembly of Georgia enacted several amendments to the Business Code, the most notable of which are summarized below.

1. Share Exchanges. The legislature amended O.C.G.A. section 14-2-1103(h) to include references to share exchanges. This amend-
ment makes all the rules for action by the shareholders of the acquiring corporation in a share exchange parallel to those for action by the shareholders of the surviving corporation in a merger.\textsuperscript{114}

\section*{2. Dividend on Treasury Shares.} The legislature added subsection (d) to O.C.G.A. section 14-2-623 to allow for dividends on treasury shares.\textsuperscript{115} This amendment will allow a corporation to preserve the relative value of its treasury shares.\textsuperscript{116}

\section*{3. Pledge of Treasury Shares.} The legislature added O.C.G.A. section 14-2-640(e) to allow a corporation to pledge its own treasury shares as collateral for corporate obligations.\textsuperscript{117}

\section*{4. Voting of Treasury Shares.} The legislature amended O.C.G.A. section 14-2-721(b) to prohibit a corporation from having the ability to vote its own shares.\textsuperscript{118}

\section*{5. Appointment of Inspectors.} The legislature added O.C.G.A. section 14-2-729.1 to the Business Code to require publicly traded companies to appoint an inspector to be present at all meetings of the corporation.\textsuperscript{119} The inspector is charged with the duties of (1) ascertaining the number of shares outstanding; (2) determining the shares represented at the meeting; (3) determining the validity of proxies and ballots; (4) counting all votes; and (5) determining the result.\textsuperscript{120}

\section*{II. PARTNERSHIPS}

\subsection*{A. Oral Partnership Agreement Extinguishes as a Matter of Law upon Incorporation}

In \textit{Jamal v. Pirani},\textsuperscript{121} the court of appeals determined that any oral partnership agreement between three shareholders of a corporation terminated when the corporation was formed.\textsuperscript{122} Jamal, a one-third shareholder of a corporation formed for the purpose of operating convenience stores, sued another one-third shareholder, alleging that the

\begin{footnotesize}
\textsuperscript{114} Id.
\textsuperscript{115} Id. § 14-2-623(d) cmt.
\textsuperscript{116} Id.
\textsuperscript{117} Id. § 14-2-640(e) cmt.
\textsuperscript{118} Id. § 14-2-721(b) cmt.
\textsuperscript{119} Id. § 14-2-729.1.
\textsuperscript{120} Id. § 14-2-729.1(b)(1)-(5).
\textsuperscript{121} 227 Ga. App. 713, 490 S.E.2d 140 (1997).
\textsuperscript{122} Id. at 714, 490 S.E.2d at 141.
\end{footnotesize}
shareholder breached an oral partnership agreement by purchasing two
convenience stores for himself rather than for the corporation. Jamal argued that all three shareholders entered into an oral partner-
ship agreement to purchase and operate convenience stores. The oral
agreement required them to purchase as many additional stores as
possible. Under the agreement, each of them would have a one-third
interest in each store. The trial court found, and the court of appeals agreed, that the
purported agreement to purchase unspecified stores in the future
terminated as a matter of law when all three individuals incorporated
their business and began operating their venture under the corporate
form. Thus, the court found Jamal’s claim against the other
shareholder without merit.

B. Partnership Agreement Controls a Partner’s Rights

In Bumgarner v. Green, the court of appeals found that a partner-
ship agreement allowed partners of a limited partnership to borrow
money against partnership property as well as to reimburse themselves
for property acquisition costs. Green, a limited partner, sued the
other two limited partners and the sole general partner of Wauka, a
limited partnership. Green alleged that the other partners breached a
duty of good faith by encumbering partnership property and reimbursing
themselves for expenses of acquisition of partnership property.

Green entered into a partnership agreement with Bumgarner and
Bruce to subdivide and develop real estate owned by Green and his two
brothers. Bumgarner and Bruce borrowed money on personal lines of
credit and purchased the property from Green’s brothers. Subsequently,
they transferred their property to the partnership, and Green trans-
ferred property he owned to the partnership. The three each received a
33.3% interest in the partnership. All three individuals read and signed
the partnership agreement. After the transfer of the property to the
partnership, the general partner, Senson, Inc., through its president,
Bumgarner, borrowed $342,000 secured by a deed encumbering the
partnership property. The borrowed money reimbursed both Bumgarner

123. Id. at 713, 490 S.E.2d at 140.
124. Id.
125. Id. at 714, 490 S.E.2d at 141 (citing Carnes v. McNeal, 224 Ga. App. 88, 89, 479
S.E.2d 474, 476 (1996); Baker v. Schneider, 210 Ga. 493, 494, 80 S.E.2d 783, 785 (1954)).
126. Id.
128. Id. at 159, 489 S.E.2d at 46.
129. Id. at 157-59, 489 S.E.2d at 44-46.
and Bruce for their initial investment in the property, plus interest. The business of the partnership proved to be very slow and the income produced did not equal the costs of the interest on the borrowed funds. The partnership had to sell the property at a loss in order to pay back the money borrowed against the property.\footnote{130}{Id. at 157-58, 489 S.E.2d at 44-45.} Green sued Bumgarner and Bruce, alleging inter alia, breach of duty of good faith, fraud, mental distress, and conversion.\footnote{131}{Id. at 158, 489 S.E.2d at 45.}

The trial court found the partnership agreement ambiguous on whether Bumgarner and Bruce had authority to reimburse themselves for their initial investment.\footnote{132}{Id.} A jury returned a verdict in favor of Green, and Bumgarner and Bruce appealed, arguing that a directed verdict was required because the partnership agreement specifically allowed their actions.\footnote{133}{Id.}

The court of appeals found that the partnership agreement expressly authorized the General Partner to encumber the underlying property and to reimburse Bumgarner and Bruce for their expenses.\footnote{134}{Id. at 159, 489 S.E.2d at 46 (citing Section 14.02 of the Partnership Agreement: "The Property may be encumbered, sold, or otherwise transferred by the General Partner.")} Under rules of contract construction, where an agreement is clear and unambiguous, no construction is required or permitted by the trial court.\footnote{135}{Id. at 158-59, 489 S.E.2d at 46.} In this case, the court of appeals reversed the trial court's holding, finding that Bumgarner and Bruce never violated their fiduciary duty to either Green or the partnership.\footnote{136}{Id.} The court of appeals reasoned that the partnership agreement, which controlled the operations of the partnership, expressly allowed the actions taken by Bumgarner and Bruce and thus precluded any finding of a breach of fiduciary duty.\footnote{137}{Id.}

Paragraph VI of the Agreement also states:

the Special Original Limited Partner [Green] shall be entitled to receive or be allocated from profit and loss in accordance with his respective percentage interest only after the Original Limited Partners [Bumgarner and Bruce] and the General Partner [Senson, Inc.] have been reimbursed all additional funds which the General Partner and the Original Limited Partners shall advance from time to time to the Limited Partnership for the purposes of paying the acquisition costs of the real property, title insurance premiums, recording charges, and any and all other acquisition cost expenses incurred in connection with the acquisition of the real property . . . .

III. BANKS AND BANKING

A. Duties of Bank Officers

In *Construction Lender, Inc. v. Sutter*, the court of appeals faced the task of determining the fiduciary duty owed by a construction lender to a borrower. The Sutters entered into a loan agreement with The Construction Lender, Inc. ("TCL") to finance the construction of their house and to pay off the purchase price for the underlying land. Under the agreement, TCL would make advances on the construction as long as TCL was "satisfied" with the progress of the construction. The agreement also provided that "all periodic inspections and any appraisals made by [TCL] [were] for the sole purpose of protecting [TCL's] security interest in the real estate and determining that progress [had] been made for the disbursement of construction loan funds as work [had] been completed."

After construction began, the Sutters began having problems with the builder's work. At that point, the Sutters asked Joe Ray, president of TCL, not to make any further payments to the builder without first obtaining their approval. For the next three advances, Ray obtained the approval of the Sutters. However, for the fourth advance, Ray examined the builder's work himself and paid the builder $47,500 without first obtaining the Sutters' approval. Soon thereafter, the builder abandoned the job and declared bankruptcy.

The trial court found Ray and TCL liable to the Sutters on two separate theories of negligence. First, the trial court held that Ray and TCL breached a duty to ensure that payments made on the loan were timely and for work actually done. Second, the trial court found that Ray and TCL negligently failed to discharge the duty they voluntarily undertook to obtain the Sutters' approval before disbursing the final $47,500 to the builder.

The court of appeals agreed with the trial court on one finding and disagreed on the other. The court of appeals held that the trial court properly determined that Ray and TCL undertook a duty to obtain

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139. Id. at 405-06, 491 S.E.2d at 855.
140. Id. at 406, 491 S.E.2d at 855.
141. Id.
142. Id. at 407, 491 S.E.2d at 856.
143. Id.
144. Id.
145. Id. at 410, 491 S.E.2d at 858.
prior approval when they agreed to do so and then complied with the request three times. TCL breached that duty when it paid the builder $47,500 without approval from the Sutters. The court of appeals disagreed with the trial court that Ray and TCL had a duty to ensure that payments were for work actually performed. The court of appeals found that generally, "a construction lender has no independent duty to protect the borrower-homeowner from problems associated with the builder's work, such as construction defects or the builder's failure to pay materialmen."

Additionally, the contract between TCL and the Sutters specified that all appraisals and inspections were provided solely for TCL's benefit, disclaimed any liability on the part of TCL for the builder's work, and described TCL's relationship as that of a mortgage lender. Under this analysis, the court of appeals found that Ray and TCL never undertook a duty of ensuring that work was performed.

B. Usurious Rates: National Banks Without Branches in Georgia are not Subject to Georgia Usury Laws

In Christiansen v. Beneficial National Bank, the United States District Court for the Southern District of Georgia held that, although Beneficial National Bank was loaning money to consumers in Georgia, it did not have a "branch" in Georgia and, thus, was not subject to Georgia's usury laws. The Christiansens filed their tax return with H&R Block and received a refund anticipation loan ("RAL") through Beneficial National Bank. After receiving the loan, the Christiansens filed suit claiming that Beneficial, through H&R Block as agent, violated Georgia's usury laws by charging them 245.249% interest on the loan. The Christiansens claimed that Georgia law applied because

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146. Id. at 407, 491 S.E.2d at 856 (citing Stelts v. Epperson, 201 Ga. App. 405, 407, 411 S.E.2d 281, 282 (1991) ("Where one undertakes an act which he has no duty to perform and another reasonably relies upon that undertaking, the act must generally be performed with ordinary and reasonable care.
147. Id.
148. Id. at 410, 491 S.E.2d at 858.
150. Id.
151. Id.
153. Id. at 684-85.
154. Id. at 683.
155. Id.
Beneficial, by obtaining the loans through a local H&R Block office, was operating a branch office in Georgia.\[^{156}\]

The court disagreed with the Christiansens' analysis.\[^{157}\] First, the court found clear precedent holding that national banks without interstate branches may charge the interest rate allowable in their home state to customers located outside of their home state.\[^{158}\] In addition, the court found that the loan agreement had a Delaware choice-of-law clause that was valid under O.C.G.A. section 7-4-13.\[^{159}\] As a result of its findings, the district court dismissed the Christiansens' claim against Beneficial for failure to state a claim upon which relief could be granted.\[^{160}\]

IV. SECURITIES

A. Punitive Damages Awarded in Arbitration

In *Greenway Capital Corp. v. Schneider*,\[^{161}\] the Georgia Court of Appeals held that, unless expressly barred by the parties' contract, punitive damage awards are permissible in arbitration of federal securities laws cases, even where expressly precluded by state law.\[^{162}\] Schneider instituted an arbitration action before the National Association of Securities Dealers, Inc. ("NASD") after she lost $49,525 entrusted to Greenway.\[^{163}\] Schneider alleged violations of federal securities laws, violations of the Georgia Securities Act,\[^{164}\] common law fraud, breach of fiduciary duty and negligence.\[^{165}\] Concluding that Greenway "exhibited such an entire want of care as to raise the presumption of a conscious indifference to the rights of the claimant," the arbitrators awarded Schneider $100,000 in punitive damages pursuant to O.C.G.A. § 51-12-5.1.\[^{166}\]

Greenway argued in the court of appeals that Georgia law prohibited punitive damages in negligence cases and, thus, foreclosed any punitive

\[^{156}\] Id.

\[^{157}\] Id. at 684.


\[^{159}\] Id. at 684; O.C.G.A. § 7-4-13 (1997).

\[^{160}\] 972 F. Supp. at 685.


\[^{162}\] Id. at 486, 494 S.E.2d at 289.

\[^{163}\] Id. at 485, 494 S.E.2d at 288.


\[^{165}\] 229 Ga. App. at 485, 494 S.E.2d at 288.

\[^{166}\] Id. at 485-86, 494 S.E.2d at 288; O.C.G.A. § 51-12-5.1 (Supp. 1998).
damage award by the arbitrators. The court of appeals found Greenway's argument to be without merit. The court held that when there has been no agreement by the parties to be bound by state arbitration law, and when the transaction involved interstate commerce within the meaning of the Federal Arbitration Act, state law is preempted by federal law.

The court of appeals also found that *Hilton Construction Co. v. Martin Mechanical Contractors* controlled its decision in this case. "Whenever a superior court vacates or confirms an award obtained under the Federal Arbitration Act, that court must apply federal substantive law." The court of appeals upheld the arbitrators' decision because, under current federal law, punitive damages are permissible.

**B. Binding Effect of Trial Court Decision**

In *Mitcham v. Blalock*, the Georgia Supreme Court held that a trial court in Georgia was empowered to protect a judgment it had entered by enjoining an investor's subsequent arbitration proceeding. Mitcham filed an arbitration claim against Atlanta Securities & Investments ("ASI"), his broker, Jones, and the corporate officers of ASI, asserting that they had bought and sold high risk securities without his consent. Mitcham received an award against ASI and Jones; however, the arbitrators dismissed from the suit the officers of ASI due to lack of notice. Mitcham later filed suit in the Superior Court of Dekalb County against the officers. The trial court granted summary judgment for all three officers, and the court of appeals affirmed.

After the grant of summary judgment, Mitcham sought arbitration of the same claim by filing a statement of claim against the officers with

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168. Id.
172. Id. (citing Hilton Constr. Co. v. Martin Mechanical Contractors, 251 Ga. 701, 703, 308 S.E.2d 830, 832 (1983)).
173. Id.
175. Id. at 648, 491 S.E.2d at 785.
176. Id. at 644, 491 S.E.2d at 783.
177. Id.
178. Id. at 645, 491 S.E.2d at 783.
179. Id.
the National Association of Securities Dealers. The trial court enjoined Mitcham’s arbitration claim on the grounds of res judicata and collateral estoppel. Mitcham appealed that decision to the Supreme Court of Georgia. The court found that the Georgia Constitution authorized a court to exercise “such powers as necessary . . . to protect or effectuate its judgments.” The court also held that O.C.G.A. section 15-6-8 gives a superior court judge the authority to grant writs of injunction to protect the judgments it has entered.

180. Id.
181. Id.
182. Id., 491 S.E.2d at 783-84.
183. Id., 491 S.E.2d at 784 (citing Ga. Const. art. VI, § I, para. IV (1983)).
185. 268 Ga. at 645, 491 S.E.2d at 784 (citing O.C.G.A. § 15-6-8 (1994)).