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## REPORT



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**EDITOR'S NOTE: IN THE STATES**

Victoria Prussen Spears

**PROTECTING MUTUAL INDEMNITY PROVISIONS FROM THE NEW MEXICO OILFIELD ANTI-INDEMNITY ACT**

Tom Donaho

**CALIFORNIA TAKES ACTION TO AVOID ELECTRICITY SHORTAGES AND RELIABILITY CHALLENGES**

Monica A. Schwabs, Neeraj Arora, F. Jackson Stoddard, and Levi McAllister

**SITTING STILL (OR HOW STATE ANTI-IDLING LAWS ARE LANDING TRANSIT AND TRANSPORTATION COMPANIES IN FEDERAL COURT)**

Aaron M. Flynn, Christopher J. Cunio, Michael J. Altieri, and Lauren Bachtel

**TEXAS SUPREME COURT REJECTS "ACCIDENTAL PARTNERSHIPS" AND AFFIRMS REVERSAL OF \$535 MILLION PIPELINE JUDGMENT**

Timothy S. Durst, Louis Layrison, Liam O'Rourke, and Shayna M. Goldblatt

**CUTTING CARBON, SAVING DOLLARS? PHILADELPHIA ADOPTS BUILDING ENERGY EFFICIENCY TUNEUP REQUIREMENT**

Brad A. Molotsky and David Amerikaner

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VOLUME 20

NUMBER 4

April 2020

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**Editor's Note: In the States**

Victoria Prussen Spears

109

**Protecting Mutual Indemnity Provisions from the New Mexico Oilfield Anti-Indemnity Act**

Tom Donaho

111

**California Takes Action to Avoid Electricity Shortages and Reliability Challenges**

Monica A. Schwebs, Neeraj Arora, F. Jackson Stoddard, and Levi McAllister

120

**Sitting Still (or How State Anti-Idling Laws Are Landing Transit and Transportation Companies in Federal Court)**

Aaron M. Flynn, Christopher J. Cunio, Michael J. Altieri, and Lauren Bachtel

127

**Texas Supreme Court Rejects "Accidental Partnerships" and Affirms Reversal of \$535 Million Pipeline Judgment**

Timothy S. Durst, Louis Layrisson, Liam O'Rourke, and Shayna M. Goldblatt

132

**Cutting Carbon, Saving Dollars? Philadelphia Adopts Building Energy Efficiency Tuneup Requirement**

Brad A. Molotsky and David Amerikaner

136

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# Texas Supreme Court Rejects “Accidental Partnerships” and Affirms Reversal of \$535 Million Pipeline Judgment

*By Timothy S. Durst, Louis Layrisson, Liam O’Rourke, and Shayna M. Goldblatt\**

*The latest decision in Energy Transfer Partners, L.P. v. Enterprise Products Partners, L.P., likely provides finality to hotly contested litigation between two of the largest pipeline companies in the United States. The Texas Supreme Court left in place a lower court’s reversal of a \$535 million judgment, and held that an “agreement not to be partners unless certain conditions are met will ordinarily be conclusive on the issue of partnership formation as between the parties.” The authors of this article explain the decision, which has major implications for energy companies doing business in Texas.*

Ending a long running and widely watched dispute over partnership formation in Texas, the Texas Supreme Court recently held “that parties can conclusively negate the formation of a partnership . . . through contractual conditions precedent.” The latest decision in *Energy Transfer Partners, L.P. v. Enterprise Products Partners, L.P.*, likely provides finality to hotly contested litigation between two of the largest pipeline companies in the United States.

The Supreme Court left in place a lower court’s reversal of a \$535 million judgment; the trial court judgment had been based on a jury’s finding that a partnership was formed by the conduct of the parties. The jury concluded that a partnership had been formed without a written partnership agreement and despite contractual conditions precedent that required a written agreement to form a partnership. This led some commentators to refer to the case as the “accidental partnership” litigation.

In a concise 15 page opinion, the Texas Supreme Court confirmed its prior holdings regarding the importance of freedom of contract. It elevated the

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\* Timothy S. Durst (tim.durst@bakerbotts.com), a partner at Baker Botts L.L.P., is a first chair trial lawyer handling complex and high stakes disputes in a wide range of cases. Louis “Louie” Layrisson (louie.layrisson@bakerbotts.com) is a partner at the firm counseling clients in a range of civil disputes, and his trial practice includes energy litigation, complex commercial disputes, and products liability litigation. Liam O’Rourke (liam.orourke@bakerbotts.com) is an associate at the firm focusing his practice on energy litigation, securities and shareholder litigation, and a broad range of tort litigation. Shayna M. Goldblatt (shayna.goldblatt@bakerbotts.com) is an associate at the firm representing energy, finance, and transportation clients in state and federal court.

importance of written contracts in partnership formation, holding that an “agreement not to be partners unless certain conditions are met will ordinarily be conclusive on the issue of partnership formation as between the parties.” We have been following this case through its eight year lifespan because, as discussed below, it has major implications for energy companies doing business in Texas.

## **THE FAILED JOINT VENTURE, \$535 MILLION JUDGMENT, AND APPEALS**

This much anticipated decision concludes eight years of litigation pitting Dallas-based Energy Transfer Partners, L.P. and Energy Transfer Fuel, L.P. (collectively, “ETP”) against Houston-based Enterprise Products Partners, L.P. and Enterprise Products Operating LLC (collectively, “Enterprise”) regarding a joint venture pipeline project.

In March 2014, a Dallas jury sided with ETP, finding that the parties created a partnership for the pipeline project through their conduct despite conditions precedent in preliminary agreements. The trial court ultimately entered a judgment for \$535 million.

In July 2017, a three judge panel on the Dallas Court of Appeals unanimously reversed and rendered judgment for Enterprise. The panel found it was undisputed that the parties had not preformed the conditions precedent in the preliminary agreements (that is, definitive agreements and board approvals); because ETP failed to prove a waiver of those conditions, the appellate court held that the partnership was precluded under Texas law.

On October 8, 2019, the Texas Supreme Court heard oral argument. ETP argued that the intermediate court’s decision effectively abrogated the five factor statutory partnership test set out in the Texas Business Organizations Code (“TBOC”), and an early stage, non-binding letter should not nullify later conduct of the parties evidencing a partnership.

Enterprise argued that a reversal would endanger freedom of contract and the ability of sophisticated parties to bargain for conditions precedent to avoid accidental partnerships. Enterprise also argued that ETP needed, but failed, to prove that the parties’ conduct “waived” the conditions precedent.

Fourteen amici from academia, trade associations, and businesses also weighed in, largely echoing the briefing of the parties that they supported.

## THE COURT'S DECISION

On January 31, 2020, the Texas Supreme Court issued its opinion<sup>1</sup> affirming judgment for Enterprise. Focusing on the longstanding Texas policy strongly favoring freedom of contract, the court held that parties, as a matter of law, “can contract for conditions precedent to preclude the unintentional formation of a partnership.”

The court explained that its decisions “recognizing this policy are decades older than the TBOC or its predecessor statute.” Consistent with its previous decision in *Ingram v. Deere*,<sup>2</sup> the court reiterated its view that “the Legislature did not ‘intend[] to spring surprise or accidental partnerships’ on parties.” And, the court highlighted that the TBOC expressly authorizes supplementation of the partnership formation rules with “principles of law and equity.” In that regard, the court noted that “perhaps no principle of law is as deeply engrained in Texas jurisprudence as freedom of contract.”

Although an agreement not-to-be-partners would ordinarily preclude the partnership formation analysis, the court held open the possibility that conduct can waive conditions precedent. The court held that ETP needed—yet failed—to “obtain a jury finding on waiver or to prove it conclusively.” The court clarified that, “where waiver of a condition precedent to partnership formation is at issue, only evidence directly tied to the condition precedent is relevant.”

Evidence generally probative of the five partnership factors “is not relevant,” because, “otherwise, a party in ETP’s position could claim waiver in virtually every case.” ETP ultimately needed to demonstrate that “Enterprise specifically disavowed the Letter Agreement’s requirement of definitive, board-of-directors-approved agreements or that Enterprise intentionally acted inconsistently with that requirement.”

The court rejected ETP’s evidence, that the “parties held themselves out as partners and worked closely together on the [pipeline] project” as irrelevant “to the issue of waiver of definitive, board-approved agreement[s].”

## LESSONS LEARNED

It is no surprise that the Texas Supreme Court, like the Dallas Court of Appeals, closely scrutinized this judgment, which attracted amicus briefs warning of the “uncertainty” and “chilling effect” that the judgment would have on energy joint venture projects in Texas. The *Enterprise* decision clarifies Texas partnership law in two important respects.

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<sup>1</sup> <https://www.txcourts.gov/media/1445666/170862.pdf>.

<sup>2</sup> 288 S.W.3d 886, 898 (Tex. 2009).



First, it affirms the enforceability—and importance—of contractual provisions like conditions precedent in preliminary agreements associated with partnerships and joint ventures. Given the prevalence of joint ventures for midstream infrastructure transporting oil, gas, and more recently produced water, this decision offers a clear roadmap to avoid accidental partnerships. As a practical matter, this decision will prompt parties to pursue dismissals at earlier stages of litigation because conditions precedent can be enforced “as a matter of law.”

Second, although the decision acknowledges that certain circumstances might waive conditions precedent, the court took a narrow view of what evidence would be relevant. The narrow exception sets a high bar for any party seeking to avoid the enforcement of such provisions, and, as a result, it may discourage challenges to the enforcement of conditions precedent.

With the court’s guidance in hand, companies doing business in Texas should consider the following steps when preparing initial joint venture documents:

- Carefully identify and define: (i) the parties, scope, and timing of a potential joint venture project; and (ii) the specific conditions that must be met prior to enforceable obligations (i.e., avoid non-specific boilerplate). The *Enterprise* decision confirms that conditions precedent will be enforced as written.
- Although not directly addressed in the *Enterprise* decision, companies should consider additional provisions to mitigate the risk of accidental partnership through conduct, including:
  - (i) Express statements negating the intention to become partners;
  - (ii) Specific disclaimers of fiduciary duties and duties of loyalty;
  - (iii) Disclaimers specifying certain joint activities (i.e., third party marketing) that do not give rise to a partnership;
  - (iv) Mutual waivers of causes of action based on partnership or joint venture theories; and
  - (v) A specific end date for negotiations if no definitive agreement is executed or other condition precedent is not satisfied.
- Work closely with project teams and business clients to ensure that business structure, internal documents, and third party communications accurately reflect the current commercial arrangement.

The *Enterprise* decision provides certainty on partnership formation by signaling that contract provisions will be enforced as written, meaning that parties can avoid accidental partnerships through the use of conditions precedent.