

**FEBRUARY 5, 2020**

For more information,
contact:

Stuart Zisman
+1 713 751 3260
szisman@kslaw.com

Alyssa Ladd
+1 713 751 3273
aladd@kslaw.com

King & Spalding

Houston
1100 Louisiana Street
Suite 4000
Houston, Texas 77002-5213
Tel: +1 713 751 3200

Freedom of Contract Cited as the Reason for Texas Supreme Court's Affirmation of Court of Appeals Judgment in ETP v. Enterprise

On January 31, 2020, the Texas Supreme Court (the “Court”) affirmed the 2017 judgment of the Dallas Court of Appeals that Texas law upholds the rights of contracting parties to agree not to be partners unless certain conditions precedent are satisfied or waived. The Court held that “parties can conclusively negate the formation of a partnership under Chapter 152 of the [Texas Business Organizations Code (“TBOC”)] through contractual conditions precedent.”¹

BACKGROUND

In early 2011, Enterprise Products Partners L.P. (“Enterprise”) and Energy Transfer Partners, L.P. (“ETP”), both builders and operators of oil and gas pipelines, began discussing a potential pipeline to transport crude oil from Cushing, Oklahoma to Houston, Texas. The parties agreed to explore the viability of such a pipeline and, to this end, negotiated and executed three written agreements, including a Nonbinding Term Sheet and Letter Agreement (the “Letter Agreement”). The Letter Agreement provided that *“no binding or enforceable obligations shall exist between the Parties with respect to the Transaction unless and until the Parties have received their respective board approvals and definitive agreements...have been executed.”* Thereafter, representatives of each of ETP and Enterprise participated in an “open season” to attract long-term shipping commitments on their potential pipeline. The commitments obtained during open season ultimately fell short of the parties’ agreed minimum commitment requirement. Shortly after open season closed, Enterprise contacted ETP and terminated its participation in the project.

Two weeks before open season ended, Enterprise had discussions with Enbridge (US) Inc. (“Enbridge”) regarding a Cushing-to-Houston pipeline. These conversations were not disclosed to ETP. The day after Enterprise terminated its participation in the project with ETP, Enterprise agreed to



work with Enbridge on a Cushing-to-Houston pipeline. Shortly thereafter, ETP sued Enterprise for breach of joint enterprise and fiduciary duty.

TRIAL COURT

In 2014, a Dallas jury found that a partnership had been formed and that Enterprise failed to comply with its duty of loyalty as a partner and awarded ETP damages of \$535.8 million. The TBOC provides five factors that indicate whether a partnership (an “association...to carry on a business for profit”) has been formed: (1) receipt or right to receive a share of profits of the business; (2) expression of an intent to be partners in the business; (3) participation or right to participate in control of the business; (4) agreement to share or sharing: (A) losses of the business; or (B) liability for claims by third parties against the business; and (5) agreement to contribute or contributing money or property to the business.² Looking to the parties’ conduct, and applying these five factors in a totality of the circumstances test, the jury found that a partnership was formed notwithstanding the limiting language of the Letter Agreement. The jury further concluded that, as a partner to ETP, Enterprise breached its duty of loyalty by pursuing a similar pipeline project with Enbridge.

COURT OF APPEALS

In 2017, the Dallas Court of Appeals (“Appeals Court”) considered whether “the trial court erred by denying Enterprise’s motions for directed verdict and JNOV because the parties’ written agreements contained unperformed conditions precedent that as a matter of law precluded the forming of the disputed partnership.”³ While the trial court instructed the jury to determine whether the parties formed a partnership using the five-factor test, the Appeals Court noted that those five factors are not exclusive. The Appeals Court looked also to Section 152.003 of the TBOC, which says that principles of law and equity – including the law of conditions precedent – supplement statutory principles of partnership law. The Letter Agreement between Enterprise and ETP required the satisfaction of two conditions precedent before a partnership would be created: (1) approvals of the respective parties’ boards and (2) the negotiation, execution and delivery of definitive agreements. The Appeals Court concluded that “unperformed conditions precedent to forming a partnership will prevent the partnership from forming unless the parties waive the performance of the conditions precedent or other rules of law or equity nullify them.”⁴

It was undisputed that the conditions precedent were not satisfied and the Appeals Court found that the testimony did not conclusively establish that the parties waived the two conditions precedent to the formation of a partnership. Accordingly, on July 18, 2017 the Appeals Court reversed the trial court’s judgment as to ETP’s claims and rendered judgment that ETP take nothing.

TEXAS SUPREME COURT

The issue the Court considered on appeal was whether “Texas law permits parties to conclusively agree that, as between themselves, no partnership will exist unless certain conditions are satisfied.”⁵ The Court affirmed the Appeals Court’s holding that the five-factor test was not exclusive and Section 152.003 of the TBOC expressly authorizes that the test be supplemented with “principles of law and equity,” chief among them the freedom of contract.⁶ The Court pointed to its “well-developed body of common law” and public policy in upholding the parties’ freedom of contract: “We hold that parties can contract for conditions precedent to preclude the unintentional formation of a partnership under Chapter 152 and that, as a matter of law, they did so here.”⁷ The Court went on to find that conditions precedent can be waived (by word or deed), but that in this case ETP failed to either obtain a jury finding of waiver or prove conclusively that the parties waived the conditions precedent.⁸ Importantly, the Court noted that evidence of the other five partnership factors is irrelevant when there are conditions precedent that have not been satisfied or waived.⁹

KEY TAKEAWAYS



Texas courts will go to great lengths to protect a party’s ability to dictate the terms of its own contracts (i.e., the freedom of contract), particularly in arms’ length negotiations between sophisticated parties. To be clear, Texas courts will continue to use the five-factor test to determine whether a partnership has been formed under Texas law, as contemplated in the TBOC. Companies should be cognizant that they may find themselves in situations where they unintentionally become “partners”. Nonetheless, the Court has made it very clear that if parties negotiate specific conditions to the efficacy of partnership formation, then those conditions will be honored unless they are either satisfied or waived. As a result, parties seeking to avoid an inadvertent partnership should always include clear and unambiguous conditions to partnership formation, along with a standard “no waiver” provision that requires any waiver of the conditions precedent to be made in writing.

ABOUT KING & SPALDING

Celebrating more than 130 years of service, King & Spalding is an international law firm that represents a broad array of clients, including half of the Fortune Global 100, with 1,100 lawyers in 21 offices in the United States, Europe, the Middle East and Asia. The firm has handled matters in over 160 countries on six continents and is consistently recognized for the results it obtains, uncompromising commitment to quality, and dedication to understanding the business and culture of its clients.

This alert provides a general summary of recent legal developments. It is not intended to be and should not be relied upon as legal advice. In some jurisdictions, this may be considered “Attorney Advertising.” View our [Privacy Notice](#).

ABU DHABI	BRUSSELS	DUBAI	HOUSTON	MOSCOW	RIYADH	SINGAPORE
ATLANTA	CHARLOTTE	FRANKFURT	LONDON	NEW YORK	SAN FRANCISCO	TOKYO
AUSTIN	CHICAGO	GENEVA	LOS ANGELES	PARIS	SILICON VALLEY	WASHINGTON, D.C.

¹ *Energy Transfer Partners, L.P. v. Enterprise Prod. Partners, L.P.*, No. 17-0862, 2020 WL 500259, at *1 (Tex. Jan. 31, 2020).

² TEX. BUS. ORGS. CODE ANN. § 152.052(a) (West 2012).

³ *Enterprise Prod. Partners, L.P. v. Energy Transfer Partners, L.P.*, No. 05-14-01383-CV, 2017 WL 3033312, at *1, (Tex. App. – Dallas July 18, 2017) (mem. op.).

⁴ *Id.* at *7.

⁵ *ETP v. Enterprise*, 2020 WL 500259, at *1.

⁶ *Id.* at *6.

⁷ *Id.* at *5-6.

⁸ *Id.* at *7.

⁹ *Id.*