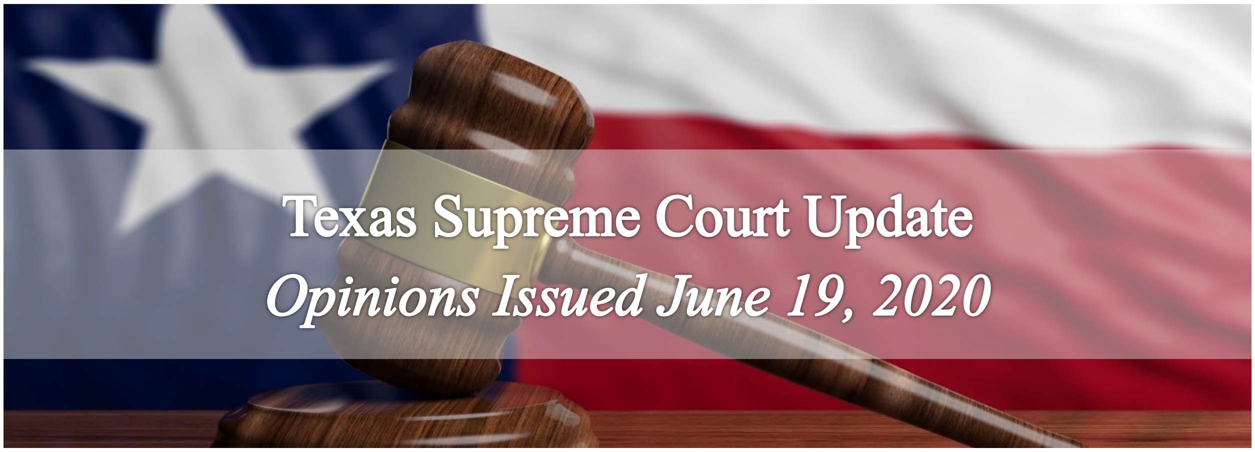

By Stephen Gibson
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Limited Partnership: *Limited partner has standing to sue for alleged loss to the value of the limited partner's partnership interest that is separate from the damages sustained by the partnership itself so long as there is an injury in fact and there is no valid objection to whether the limited partner is a proper person to recover for that injury.*

Necessity of Verified Denial to Challenge Lack of Capacity: *Lack of capacity to recover under existing law, as opposed to lack of standing to sue, is waived if not established by the allegations of the petition and there is no timely verified denial.*

Necessity of Cross-Appeal: *Failure to cross-appeal decision to disregard alternative damage finding meant that finding could not be used to support recovery for misappropriation of trade secrets.*

No Evidence Post-Judgment Challenges are sufficient to preserve complaints that damages testimony is conclusory but complaints about valuation methodology is waived if no timely objection is lodged to the testimony when presented at trial.

Conclusory Future Damages Testimony: *Failure of witnesses to provide objective data to support their assumptions or correlate those assumptions to existing data was legally insufficient to support a jury verdict awarding damages for lost value of partnership business.*

Injunctive Relief: Failure to prove actual damages for the misappropriation of trade secrets does not establish that there is no adequate remedy at law as required to permit injunctive relief.

In Pike v. Texas EMC Management, LLC, individual investors and a limited partnership, "EMC Cement," organized EMC Products to manufacture and market a new type of cement under a license agreement with a Dutch technology company. EMC Products was a limited partnership with EMC Management acting as its general partner. The business was not as lucrative as anticipated and failed after the individual investors, Walker and Wilson, refused further funding. Unbeknownst to EMC Products and EMC Management, Wilson and Walker had engaged in clandestine discussions about EMC Product's business with affiliates of VHSC.

VHSC later purchased EMC Products' manufacturing plant and equipment after foreclosure. VHSC also hired EMC Products' former president, Pike, and other EMC Products employees to continue producing the new cement and improve methods for its manufacture. EMC Products, EMC Cement, and EMC Management successfully sued VHSC, Pike, and Wilson and Walker for breach of fiduciary duties, trade secret misappropriation, breach of management agreements, and tortious interference with the management and partnership agreements.

Traditionally, standing to recover for losses in the value of the assets of a business entity with a legal identity separate from its inventors was traditionally limited to the business entity itself, not its investors.

Three decades earlier, *Wingate v. Hajdik*, 795 S.W.2d 717, 719 (Tex. 1990), held claims for losses to a corporation belonged to corporation, not the shareholders. The shareholders' derivative loss in the form of reduced stock value was compensated indirectly when the corporation recovered the loss. Based on this rule, Wilson and Walker argued the limited partners had no "standing" to assert individual damages claims because loss of value to the partnership, EMC Products in this case, was a claim that belonged to the partnership and not separately to its partners.

Jurisdictional standing is a function of alleged injury in fact, regardless of whether there is a formal legal right of recovery. Standing to recover, on the other hand, is a defensive matter that can be waived if not timely raised by a verified denial.

The lengthy 8:1 opinion by Justice Busby in Pike v. Texas EMC Management, LLC, first decided whether this "standing" challenge was directed to the existence of a justiciable case or controversy essential to the trial court's subject-matter jurisdiction, or was instead an attack on the plaintiffs' right to prevail on the merits. Relying on parallel federal authorities, the opinion posited that shareholders and partners had standing in the jurisdictional sense because they had in fact suffered a loss, which is all that "jurisdictional" standing requires. But whether a party can recover due to statutory restrictions on the right of recovery is not a matter of the existence of an actual injury but rather whether a claimant has a right to recover for that injury. Limitations on the right of recovery notwithstanding the existence of an injury in fact is not a jurisdictional concern, but a question that goes to the merits of the claim: whether the claimant has the capacity to recover for that loss. The opinion analyzed the relevant sections of the Business Organizations Code and concluded that they too were germane to the right of recovery, not injury in fact. Thus, it held the *Wingate* rule for corporate shareholders also applied to partners in a limited partnership and that this limitation was a matter of capacity to recover on the merits. According to the majority, the ability to satisfy statutory restrictions designed to protect the separate identities of certain types of business entities are not jurisdictional if there is an injury in fact.

Justice Bland not convinced there is a meaningful distinction between jurisdictional standing and right-of-recovery standing.

As Justice Bland's partial dissent highlights, the majority's distinction of injury-in-fact standing from capacity standing presents a chicken-and-egg dilemma. The dissent maintains that there can be no injury in fact to a partner because the loss belonged to the partnership in the first place, just as the loss in the value of a corporate asset is a claim that belongs to the corporation instead of individual shareholders. According to the dissent, a partner's inability to assert the claim permitted by statute divests the partner of jurisdictional standing so courts have no power to decide such claims when asserted by partners.

Editorial observation: Ability to waive substantive defects in the right of recovery may explain the difference between jurisdictional standing and right-of-recovery standing.

Though not couched as such, the dispute between the majority and the dissent appears to be over whether jurisdictional standing can exist when the claimant has no substantive right of recovery. Enter a unique and, in this writer's opinion, underappreciated feature of Texas procedural law: the special exception. Recovery in a jury trial is determined by the issues made by the pleadings in which defects of form and substance are waived pursuant to Texas Rule of Civil Procedure 90 if not pointed out *in writing* before submission to the jury.

A party pleading for a right of recovery that does not satisfy substantive law is nonetheless entitled to recover on proof of those allegations if the opposing party poses no timely written objection to the pleading defect. This possibility is sufficient to confer jurisdictional standing without satisfying the substantive capacity requirement. Neither opinion discusses special exceptions, but it is the only way this writer can think of to explain the majority's resolution of the standing issue. As the majority opinion would later observe on another issue, "[o]ur adversary system of justice generally depends 'on the parties to frame the issues for decision and assign[s] to courts the role of neutral arbiter of *matters the parties present*." (Emphasis added). This feature, the majority observed, "distinguishes our adversary system … from the inquisitorial one." If that rationale applies to the standing issue, then treating the opinion as implicit approval of a general right of partnership members to recover separately from the partnership for loss in the value of partnership assets reads too much into it. The opinion is simply addressing the standing question in the procedural posture presented by the parties, it was not addressing the greater substantive issues presented by treating limited partnerships and corporations as separate legal entities.

Lack of capacity to recover under existing law, as opposed to lack of standing to sue, is waived if not established by the allegations of the petition and there is no timely verified denial.

The distinction between jurisdictional standing and capacity-to-recover standing was important because plaintiffs argued that Wilson and Walker waived their right to assert lack of the latter by failing to assert it in a verified denial as required under Texas Rule of Civil Procedure 93. If the “standing” argument had been deemed one that attacked injury in fact and, thereby, subject-matter jurisdiction, that complaint required no error preservation and could be raised for the first time during the appeal. The opinion agreed generally that failure to raise lack of a sufficient allegation of capacity by verified plea means the issue is not before the court.

The limited partners’ request for damages separate from those to the limited partnership did not become apparent until the charge conference and after the time for additional pleading asserting a verified denial.

However, the opinion avoided deciding whether filing a verified denial was necessary. The majority reasoned the partners’ claim for separate damages did not arise until plaintiffs tendered their requested damage issue at the jury charge to which the defendants timely objected as required under rule 274. “Because EMC Cement … alleged that it sustained damages as a result of Walker and Wilson’s breaches, Walker had no reason … to file a verified denial.” Thus, it concluded that the capacity-to-recover question did not arise when the defendants could have asserted a verified denial.

But pleading general and special damages is necessary under Texas law. Tex. R. Civ. P. 45, 47, 56. The majority did not explain how pleadings could be so open-ended to support the submission of such a theory without also obliging the defendant to timely specially except. This lack of explanation may rest in the fact that the majority determined that the plaintiff’s recovery was substantively foreclosed because “there [wa]s insufficient evidentiary support for EMC Cement[]’s damages even if it had capacity.”

Failure to cross-appeal decision to disregard alternative damage finding meant that finding could not be used to support recovery for misappropriation of trade secrets.

The claim for damages for misappropriation of trade secrets was based on two alternate measures: value of the right to use the trade secrets or costs saved by the use of the trade secrets. The jury found the same amount under both measures, but the trial court disregarded the finding based on the value of the trade secret’s use for lack of probative evidence. The opinion determined that there was no probative evidence to support an award of damages under the costs-savings measure. Further, the majority ruled that the court of appeals could not uphold recovery on the use valuation alternative because the plaintiffs did not challenge on appeal the trial court’s decision to disregard the jury’s finding on that measure of damages. Citing the nature of an adversary justice system, the majority ruled that the damage award for trade secret misappropriation could not be upheld by overturning trial court ruling that was unchallenged on appeal.[1]

There was no evidence of lost value to partnership interest from tortious interference or breach of the management agreement.

Plaintiffs also recovered damages based on jury findings about the loss of market value of the partnership or the partner’s interest therein due to defendant’s tortious interference and breach of management agreements. One

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[1] Under Texas Rule of Appellate Procedure 38.2(b), “When the trial court renders judgment notwithstanding the verdict …, the appellee must bring forward by cross-point any issue … that would have prevented an affirmance of the judgment if the trial court had rendered judgment on the verdict.” Here, the cross-point rule does not strictly apply because the sufficiency of the evidence to support the alternate finding was not one that would have *prevented* affirmance. It would have *permitted* affirmance.

component of this recovery was based on the difference in the value of the plant and equipment before and after foreclosure.

Evidence based on the original purchase price of plant and equipment alone, without depreciation for wear and tear from use, will not support recovery when damages to be measured by market value under the question submitted to the jury.

Plaintiffs sought to uphold recovery for this difference by testimony from the engineer who designed and built the plant. His calculation was based on its original cost plus 20% due to increased costs of labor and materials. His calculation included no reduction for wear, tear, or depreciation from the intervening use of the plant and its equipment. This testimony lacked any probative value for three reasons. First, purchase price can be a starting point for calculating actual value but, standing alone, is insufficient to support damages based on *market* value. Second, the charge submitted to the jury inquired about the fair market value, so testimony about purchase price was not probative of the question the jury was asked to decide. Third, the witness's testimony about the value of the plant and equipment was never "tie[d]" to the market value of the partnership, which was the only damages measure the jury was asked to decide.

An owner's testimony about the value of property is probative only when based on the owner's opinion of market *value, not book value.*

Testimony from an owner about the plant and equipment's book value" could not salvage the jury finding because an owner's estimate is probative only when based on *market* value. Book value is different. Evidence of the foreclosure sale price could not be used as a basis for treating the award as based on market value because foreclosure sales do not involve a willing seller, which is essential to market valuation. Thus, the majority determined there was no evidence supporting a damage award for diminution in the market value of the partnership based on the value of the plant and equipment.

There was no legally sufficient evidence of the value of the business operation exclusive of plant and equipment because the witnesses could not relate assumptions to any supporting objective data.

As to the value of the business operation *excluding* plant and equipment, plaintiffs adduced testimony from one of EMC Products' limited partners. This witness based his valuation in part on projected ten-year earnings before interest, taxes, depreciation, and amortization then assumed a percentage increase in future sales volume reduced to present value by a similar discount rate. Defendants challenged whether the witness applied the correct formula in calculating present value because he failed to make certain deductions, but the court refused to entertain a challenge to the witness's methodology because the defendants failed to object during trial to the admissibility of the testimony on grounds of improper methodology.

However, defendants also urged that his testimony was based on assumptions about future sales that were entirely without supporting sales data or market analysis. In particular, the witness assumed increasing sales and increasing prices without in any way accounting for a known economic recession of providing any explanation supporting his assumption contrary to known facts. This complaint about the analytical gap between the actual sales data and the assumptions underlying the witness's valuations were "no evidence" objections preserved by defendants' post-trial legal sufficiency challenge in their motion for judgment notwithstanding the verdict. The majority further agreed these objections were valid and, therefore, the witness's testimony failed to connect his valuations to any data, which was required to allow that testimony to support the jury's damage award.

The future value of the business also could not be supported by evidence of a non-binding letter of intent under which it was hoped that the market for the cement product could be expanded to California. The evidence showed the parties to the letter of intent never closed their transaction. The witness did not explain how that incomplete transaction could provide any factual support for valuation of EMC Products' Texas business. Thus, the majority ruled that this testimony was also entirely conclusory and incapable of supporting the verdict.

The opinion then turned to whether an expert witness's estimate of future business valuation under the standards of two relevant professional associations could support the verdict. That witness, however, assumed a positive growth rate for future income when EMC Products' historical sales data showed a zero sales growth rate over its four years of operations. Without an objective data-supported explanation of how there would have been a growth in sales had the business continued in operation, the expert's testimony also lacked probative value.

However, the plaintiffs' failure to adduce probative evidence of the future value of the business did not itself establish that it was *impossible* to prove that there could be no remedy in the form of damages for the alleged misappropriation of trade secrets. Because the majority was convinced that it would have been impossible to prove damages for this alleged misappropriation, it ruled that the trial court did not abuse its discretion in denying injunctive relief because such relief is available only if there is no adequate legal remedy for the harm. Because of these evidentiary deficiencies, the court reversed the judgment for the plaintiffs and rendered a take-nothing judgment.

Special Warranty Deeds: A party that accepts a special warranty deed cannot recover for breach of an implied covenant of seisen for defects of title to which the special warranty does not apply.

Merger Doctrine: The acceptance of a deed that does not fully comply with the requirements of the sales contract is deemed to satisfy the contract nevertheless under the doctrine that the requirements of the contract are merged with the accepted performance.

Except for quitclaim deeds, the grantor in any real property conveyance impliedly covenants ownership of the interest purportedly conveyed unless the covenant is specifically disclaimed. In [Chicago Title Insurance Company v. Cochran Investments, Inc.](), the grantor purchased property in a foreclosure sale. The grantor entered into a contract of sale that required conveyance by general warranty deed, but the grantor conveyed ownership by *special* warranty deed limiting the grantor's obligation to defend title to those who claimed ownership through him. After this conveyance, the bankruptcy trustee claimed the foreclosure sale violated a bankruptcy stay and was invalid. The purchaser's title insurer settled the claim and brought a subrogation suit against the grantor.

The bankruptcy trustee did not claim ownership *through* the grantor but challenged whether the grantor acquired valid ownership to begin with. Because the special warranty did not apply, the title insurer asserted that the grantor was liable for breach of the covenant of seisen. Ostensibly, the first question was whether the special warranty deed's limitation of the grantor's liability to defend title overrode any obligation of an implied seisen covenant – a subject on which the lower courts had been divided.

Without deciding that whether a covenant of seisen could be implied in a special warranty deed, the court held in a unanimous opinion by Justice Lehrmann that the limitation of the special warranty to persons claiming through the grantor was a disclaimer sufficient to foreclose explicitly any greater implied obligation under any covenant of seisen. "[T]he special warranty here expressly disclaims liability for a failure of title unless that failure arises from someone claiming the property by, through, and under [the grantor]," the opinion explains.

According to cases cited in the opinion, when a grantee accepts a *special* warranty deed, the grantee is presumably acting on the grantee's own evaluation of title and cannot complain of defects beyond those protected by the special warranty. Because the bankruptcy trustee's claim was not through the grantor, there was no breach of either warranty or any implied covenant. *Caveat emptor* apparently applies to grantees who accept special warranty deeds.

Moreover, it does not appear that the parties can "contract around" the effect of the special warranty in the deed by attempting to generally preserve rights in the sales contract itself. The opinion in *Cochran Investments* invoked the merger doctrine to deny the title insurer's claim for breach of contract of sale based on the delivery of special warranty deed instead of the general warranty deed called for in the sales contract. The merger doctrine provides that "[w]hen a deed is delivered and accepted as performance of a contract to convey, the contract is merged in the deed." Apparently, this doctrine cannot be disclaimed. In this case, the contract provided that its obligations "survive[d] closing" but the court held the doctrine prevented the title insurer from recovering under the sales contract. "To the extent the special warranty deed limits [the grantor's] liability for failures of title in a way the contract does not, …

the merger doctrine forecloses the contract claim. Thus, it behooves grantees to carefully inspect the deed to be received to make sure that it complies with the underlying sales contract.

Texas Prompt Payment Claims Act: *Insurers are not insulated from liability under the Act by payment of appraisal awards determining the amount of the covered claim.*

Last year, the court held in *Barbara Technologies Corp. v. State Farm Lloyds* that "payment in accordance with an appraisal of a claim [under a policy of property insurance] is neither an acknowledgment … nor a determination of liability under the policy for purposes of" the Texas Prompt Payment of Claims Act. Before the decision in *Barbara Technologies* was handed down, the courts of appeals ruled in two cases that insurance companies which paid the appraisal awards could not be liable to policyholders under the prompt payment statute. In *Marchbanks v. Liberty Ins. Corp.* and *Perry v. U. S. Automobile Assoc.*, the court reversed these holdings in two *per curiam* opinions because they were contrary to the holding in *Barbara Technologies.*

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