By Stephen Gibson[1]

***Statutory Construction*: Statutes Must Be Interpreted By Reading Language in the Context of the Intended Objective.**

***Alcoholic Beverage Regulation*: The Tied House Statutes Prohibits Retail Permits When a Brewer Owns a Substantial Interest in the Retailer's Corporate Owner.**

In *Cadena Comercial USA Corp. v. Texas Alcoholic Beverage Comm'n*, the Texas Supreme Court ruled on the applicability of the "tied house" statute. This statute prevents an entity with "an interest" in any alcoholic beverage manufacturer from also having "a direct or indirect interest" in an alcoholic beverage retailer. *See* Tex. Alcoholic Bev. Code § 102.07. It was originally enacted shortly after the repeal of Prohibition to prevent the creation of incentives for widespread over indulgence.

In *Cadena*, the would-be retailer was a wholly-owned subsidiary of a company that also indirectly owned a 20% interest in a brewer. The ownership interest was separated by several layers of corporate structure between the brewer and corporation. In a 6:2 opinion by Justice Johnson, the Texas Supreme Court ruled that this remote cross-ownership was enough to authorize the TABC to deny an alcoholic beverage permit to the retailer.

Proper Interpretation Depends on the Overall Statutory Purpose, Not Isolated Definitions.

Statutory interpretation was front and center. *Cadena* exemplifies looking to the plain text of the entire statute, not just isolated provisions, to arrive at a proper interpretation. The court determined the legislative objective was preserving public health and safety by strictly separating manufacture and distribution. In light of that objective, the court considered what the statute meant when it proscribed issuing a permit to any entity that also held "an interest in the business of a . . . brewer." The court agreed that the Legislature intended "interest" to be defined very broadly to include *any* commercial or economic interest, not just formal, legally recognizable, ownership interests.

The court also rejected the argument that "interest" was impermissibly vague. It reasoned the statute applied to "an interest in the business of a . . . brewer" that included "any stake in the financial performance of an entity engaged in the manufacture . . . of alcoholic beverages." The court generally disapproves of interpreting a statute merely by stringing together isolated definitions. However, this approach was deemed appropriate in light of the statutory objective. Thus, the appropriate interpretive method depends on the overall purpose as ascertained from the entire statutory scheme.

Interest Sufficient to Trigger Application of Police Power Statute Not Confined by Civil Limitations on Piercing the Corporate Veil.

Having broadly defined "interest" to capture virtually any interest, the court rejected the applicant's argument that "interest" was limited to consideration of only the retailer's immediate owner. Instead, "interest" was deemed to be

[1] The opinions expressed are solely those of the author. They do not necessarily represent the views of Munsch, Hardt Kopf & Harr, P.C. or its clients.

broad enough that the TABC could look beyond corporate formalities and consider the brewer's stock ownership in the retailer's ultimate corporate parent.

Again, context was key. Given the purpose of the statute, the court was not constrained by limits on corporate veil-piercing that prevent litigants from disregarding legally separate entities. It also didn't hurt that the statute explicitly makes both "direct" and "indirect" interests disqualifying. In *Cadena*, the stock ownership was 20% -- less than a controlling interest, but "substantial" nonetheless. That was enough to trigger application of the tied house statute. The court refused to render an advisory opinion whether ownership of a "single share" would have been enough.

Dodging the "single share" argument was crucial to disposition of Cadena's claim that the statute's application denied it equal protection. Cadena showed the state had pension funds that owned mutual funds that held stock in both brewers and retailers. The court deflected the argument by ruling that this indirect ownership did not "come close" to the magnitude of the cross-ownership of the brewer in the retailer's corporate parent. Further, the opinion points out that a mutual fund manager is obliged to diversify fund holdings. The magnitude of the pension fund investments are capped at 1% of the fund's assets and 5% of any corporation's stock – a much lower percentage than the interest owned by the brewer in the retailer's corporate parent. In short, a 20% ownership is disqualifying but 5% is not.

The Dissent's "Fly" In the Majority's Statutory Construction "Ointment."

Nothing in the statute's text suggests that existence of a disqualifying "interest" is a matter of degree or magnitude. The majority simply reads into the statute a requirement that the interest be "significant." Ironically, the majority rebuffs the dissenting opinion of Justice Willett and Chief Justice Hecht for doing exactly the same thing: reading into the statute a similar requirement of "significant" ownership.[2] The real dispute between these factions is that the majority deems the ownership interest at issue significant; the dissent does not.

The dissenters relied on the declaration that the objective the tied house statute was "to assure the independence of members of the [retailer – distributer – manufacturer] system." They reasoned that "an interest" sufficient to trigger the tied house statute had to be beyond that necessary to preserve "independence." In their view, the remote minority corporate ownership in this case did not meet that threshold because nothing showed that the brewer's remote minority interest could influence the retailer's operations or *vice versa*.

***Environmental Liability*: The Texas Railroad Commission Does Not Have Primary Jurisdiction Over Environmental Claims.**

***Arbitration*: There Can Be No Disqualifying Partiality If There is No Evidence the Arbitrator Was Aware of the Alleged Cause for Partiality; Arbitration Awards Cannot Be Set Aside for Manifest Disregard of Texas Law Merely for An Erroneous Application of That Law; A "Clear Agreement" Is Required to Authorize Expansion of the Judicial Review Permitted by Statute.**

As part of a previous settlement, the mineral lessee in *Forest Oil Corp. v. El Rucio Land & Cattle Co.* agreed: 1) not to bring or store hazardous material on the lease; 2) to remove hazardous material when legally required; 3) to remediate in accordance with state and federal law; and 4) to arbitrate lessor-lessee disputes. In its operations, the lessee used pipe containing normally occurring radioactive materials (NORM). The lessor alleged the use of these pipes caused personal injuries and contamination. A divided three-arbitrator panel awarded the lessor actual damages, punitive damages, and attorney's fees totaling approximately $22 million and declared the lessee's future remediation responsibilities.

The lessee first sought to vacate the arbitration award by contending that the Texas Railroad Commission (RRC) had primary, if not exclusive, jurisdiction over the environmental claims. Giving an agency *exclusive* jurisdiction divests

[2] *In this writer's opinion*, both majority and dissent fail to candidly acknowledge the limits of strict adherence to statutory text as interpretive dogma. If proper consideration of "context" is necessary to effectuate legislative intent, it will be impossible *not* to read words into the statute. If doing so were unnecessary, the Legislature would have expressed itself perfectly for all purposes and all situations. This is a patently unrealistic expectation, especially considering that the Texas Legislature must accomplish its work in a highly compressed, biennial session.

the courts of subject-matter jurisdiction except as allowed under administrative procedure laws. *Primary* jurisdiction, on the other hand, simply allocates decision-making priority when both courts and agencies have the authority to initially resolve disputes.

To support its contention that RRC jurisdiction was exclusive, the lessee pointed to statutes giving the RRC *sole responsibility* for preventing water pollution from production activities and regulating disposal of oil and gas waste containing NORM. Again, resorting to context, Chief Justice Hecht's unanimous opinion[3] viewed these as allocations of administrative responsibility not intended to usurp judicial authority over civil suits. The lessee argued, however, that a statute authorizing suit for violation of RRC orders negatively implied the RRC had primary authority to resolve contamination claims before a litigant could seek judicial relief. The court disagreed because intent to supplant civil jurisdiction could only be implied when absolutely necessary. Here, it was merely possible, not necessary, to read the statute to preclude judicial jurisdiction. The primary jurisdiction doctrine does not apply to "inherently judicial" claims such as actions for trespass, negligence, intentional tort and breach of contract. The possibility that a court and the RRC might impose differing or double liability was a matter for the Legislature, not the court, to resolve.

There Was No Evident Partiality By One of the Arbitrators, Manifest Disregard of Texas Law or Clear Agreement Authorizing Expanded Judicial Review.

The court also rejected the lessee's effort to set the arbitration award aside for evident partiality and manifest disregard of Texas law. The lessee claimed arbitrator bias because the lessee objected to an arbitrator serving as mediator in another case. There was no direct evidence the arbitrator knew of the objection, however. Consequently, the court ruled that it could not have caused any partiality.

The court also rejected the claim that the damage award was invalid because it assessed damages not permitted under Texas law. An arbitration award can only be set aside if there is no authority to decide the issue, not because that issue was incorrectly decided. The clause giving arbitrators authority to resolve scope-of-arbitration disputes authorized them to decide, rightly or wrongly, recoverable damages under Texas law.

Further, the court was not convinced by the lessee's argument that authorizing "punitive damages where allowed by Texas substantive law" was a "clear agreement" that overcame the Texas Arbitration Act's restrictions on judicial review. The court pointed to a more specific directive for judicial review of discovery orders and concluded that lack of a similarly clear agreement about the arbitration award meant the agreement was not intended to expand judicial review.

***Exemplary Damages*: Error to Consider on Appeal Highly Improbable Consequences When Reviewing Punitive Damage Awards.**

***Mental Anguish Damages*: The Evidence Adequately Showed Substantial Disruption of Daily Routine.**

***Frivolous Litigation Sanctions*: Attorney's Fees Incurred Defending Frivolous Litigation Are Appropriate Measure for Sanctions Provided Case Was Not Terminable Earlier Regardless of Resolution of Disputed Fact Questions.**

Bennett v. Grant is a malicious prosecution case arising from an attempt to prefer criminal blackmail charges. The criminal charges were the latest chapter of an escalating feud between two ranchers. The dispute started when one rancher captured the other's stray cattle. The seizure spawned a cattle theft criminal trial in which Grant was acquitted. Grant then sued for malicious prosecution. He recovered $5000 for mental anguish, $5700 in attorney's fees, and a whopping $1.25 million in punitive damages from Bennett and a related corporation. An additional $250,000-plus sanction was assessed against Bennett for a frivolous slander counterclaim.[4]

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[3] Justice Brown did not participate in the case.
[4] These litigants forgot that when the hole is deeper than you are tall, it's a good idea to stop digging.

The Evidence Adequately Showed Substantial Disruption of Daily Routine Sufficient to Make the Mental Anguish Compensable and to Support the $5000 Actual Damage Award.

Justice Willett's unanimous opinion began by upholding the award of $5000 mental anguish damages award. The court found that moving four times, building a security fence, fear of leaving home, headaches, weak stomach, sleep deprivation and loss of appetite were more than adequate to prove a high degree of compensable mental pain and anguish necessary to recover for mental anguish.

Because the Conduct Involved a Felony, Chapter 41's Punitive Damages Statutory Caps Do Not Apply.

The court then addressed punitive damages. It began by ruling that Chapter 41's punitive damages caps did not apply because malicious prosecution involves deception to obtain a felony indictment affecting another's pecuniary interests – i.e., the cost of hiring attorneys to quash the indictment and the $10,000 bond to avoid confinement pending the criminal trial. Because obtaining the indictment affected a pecuniary interest, the deception in doing so was a felony under Penal Code §32.36. Chapter 41's punitive damage caps, therefore, did not apply.

Punitive Damages of 48 Times Actual Damages Were Unconstitutionally Excessive.

However, the punitive damage award was found to violate due process after considering the three *BMW v. Gore* factors: (1) reprehensibility of the misconduct; (2) the disparity between the exemplary damages and actual or likely harm; and (3) the difference between the exemplary damages and civil or criminal penalties for comparable conduct. The court agreed that the conduct was reprehensible and that the exemplary damages were not out of line with the criminal penalties of up to $46,000 in fines and 22 years of incarceration. The second factor was the trouble spot. A 48:1 punitive damage ratio was far above the 4:1 ratio demeed "close to the line of constitutional impropriety."

Economic Harm or Value of Wrongful Incarceration Was Not a Likely Result of the Tortious Conduct and Cannot Be Considered in the Ratio of Actual to Exemplary Damages.

The significant feature of the proportionality analysis was the clarification that the relevant relationship is between the punitive damages and the harm that was *likely* to result from the tortious conduct had it been successful, *not* the harm that *actually* resulted. The Texas Supreme Court disagreed with the court of appeals' conclusion that if the prosecution had resulted in a conviction, damages to the plaintiff based on compensation rates paid by the state for wrongful convictions would have been not less than $160,000 and perhaps more than a million, depending on the sentence imposed. But, the Texas Supreme Court ruled that the court of appeals erred in considering the value of the criminal penalty because incarceration was no longer possible. The criminal indictments had been quashed and limitations had run. Thus, incarceration should not have been considered when fixing the constitutional limit on punitive damages.[5]

Joinder Was Proper and the Joined Defendant Waived Any Error by Failing to Object in the Trial Court.

The related corporate entity was joined as a defendant by motion after trial court's suggested joinder "under rule 38." Grant did not specify the basis for the joinder motion. Rule 38 applies to third-party defendants and would not have permitted the joinder of an additional defendant. However, joinder was permitted under rules 37(proper parties), 39 (necessary for complete relief) and 40 (relief from the same transaction). When neither the motion nor the trial court limited joinder to an improper basis, allowing the additional defendant to be added to the litigation was not an abuse of discretion. Moreover, any error would not have been preserved because there was no objection in the trial court.

[5] This observer questions whether it is appropriate to assume the limitations defense was certain to have been successful. The opinion does not address this issue. The test for excessiveness is based on the likely harm had the tortious conduct *been successful*. Unless limitations barred prosecution as a matter of law, assuming it would have been a successful defense to prosecution seems incompatible with the excessiveness test.

Attorney's Fees Incurred Defending Frivolous Litigation Are a Proper Consideration for Sanction Amount and May Include All Defense Fees If Case Cannot Be Adjudicated Earlier on Summary or Other Legal Basis.

The sanction award was based on the attorney's fees Grant incurred in defending Bennett's defamation counterclaim. Bennett challenged the sanctions amount as excessive. The court disagreed because it deemed attorney's fees was not an inappropriate sanctions yardstick when there was no way for Grant to earlier terminate the defamation claim for legal invalidity.

The Texas Supreme Court upheld all of the judgment except the punitive damage award. Treating that recovery as a separate, severable action, it remanded that aspect of the case to the court of appeals for re-evaluation of constitutional excessiveness without considering the consequences of a conviction that, with near certainty, could have never occurred.