

Question 3 – July 2014 – Selected Answer 1

Part 1

ABP is liable to Motorist, but Abner and Blake are not. The issue is an limited liability company's liability for torts of its employees, and managers' liability for torts of employees.

A limited liability company (LLC) is an entity of limited liability. In other words, members and managers of an LLC do not incur personal liability for debts and obligations of the LLC except in certain circumstances (e.g. if they commit the tort at issue). The LLC, however, will be liable for torts of its members, managers, and employees if the torts are committed within the scope of employment. However, just because the LLC is liable does not automatically make the members or managers liable. They must actually participate in or commit the tort in order to incur personal liability.

It is undisputed that the ABP employee who ran the red light was acting in the scope of his employment. ABP is therefore liable for the employee's tort, and Motorist can validly recover from ABP. However, there is no evidence that Abner or Blake participated in the tort themselves. They therefore are not personally liable for the employee's tort. They maximum amount they could lose is their capital contributions to ABP, which are subject to Motorist's claim. However, their monies not tied up in the LLC are not subject to recovery. Note, however, that the language in the LLC agreement exempting Abner and Blake from personal liability to third parties would be ineffective had Abner and Blake personally committed the tort at issue. LLC members by law are not allowed to shield themselves from liability for their *own* torts.

In sum, Motorist can sue and recover from ABP, but not Abner or Blake.

Part 2

ABP and Blake will be liable to Customer, but Abner will not. As noted above, LLC members enjoy limited liability for LLC debts and obligations. Further, LLC members who sign contracts on behalf of the LLC do not incur personal liability simply because they signed the contract. However, members *may* incur personal liability if they do not make it clear that they are signing in their representative capacity, rather than their personal capacity. Again, however, members and managers who commit a tort are personally liable for their own tort, even if it occurs during the scope of their employment.

In this case, both Abner and Blake signed the contract as "Managing Members." This language is sufficient to notify Customer that the two were signing in their representative capacity (i.e. they were not agreeing to be personally liable on the contract). Further, the LLC agreement gave them actual authority to enter into contracts on ABP's behalf. At this point, neither is liable on the contract. However, Blake committed the tort in question (negligence) that injured Customer. On the way to delivering the order to Customer, Blake got drunk and, due to his intoxication, crashed the truck, destroying both the truck and Customer's order. Blake was at the least negligent (a tort), and was more likely grossly negligent. Customer can therefore sue Blake and recover personally from him. LLC members and managers cannot limit their liability to third parties for their own torts. Blake is therefore liable.

ABP will also be liable because the contract has been breached. LLCs are liable on all contracts signed on their behalf. This contract was breached-due to Blake's tort-and Customer could recover from ABP. Further, ABP is vicariously liable for torts committed by members, managers, and employees if the torts are committed during the scope of their employment. Blake may have been on a frolic here, which would exempt ABP from tort liability, but he may not (because the crash occurred while he was on his way to deliver the order). Regardless of tort liability, Customer can definitely sue ABP for breach of contract.

Abner will not be personally liable for Customer's damages. As noted above, LLC members and managers enjoy limited liability for LLC debts and obligations. This debt is ABP's debt, and Abner will not be liable for it unless he participated in the tort himself. However, Abner had no knowledge of Blake's drinking problem. He therefore

was not negligent in letting Blake personally deliver the order. Further, the crash was caused by Blake, not Abner. Abner therefore did not participate in the tort, and was not negligent in letting Blake drive the truck, and Customer cannot sue Abner for her damages.

Part 3

Yes, ABP should prevail on its cross-claim against Blake. The issue is an LLC member's liability to the LLC for torts the member commits.

An LLC member is liable to an LLC for torts the member commits. The LLC member must reimburse the LLC for any damages he causes through breaches of his duty of care or duty of loyalty. However, LLC members and managers may limit their liability to the LLC, but only for mere negligence. Under the Texas Business Organizations Code, LLC members and managers cannot limit their liability to the LLC for gross or willful misconduct.

The LLC agreement here explicitly excludes liability to the LLC for breach of fiduciary duty, but does not exclude liability for gross negligence or intentional misconduct. The tort here was not committed intentionally, as Blake did not purposefully drive off the road. However, it was likely committed in a grossly negligent manner, as driving drunk is usually considered gross negligence. Blake's blood alcohol content was three times the legal limit, which is extremely high (further contributing to his gross negligence). An LLC manager owes a fiduciary duty of care to the LLC, which includes an obligation to make reasonable business decisions. It appears highly likely that driving a company truck while drunk is an unreasonable decision. Under Texas law, and explicitly under this LLC agreement, Blake likely breached his fiduciary duty of care in a grossly negligent manner, and would be personally liable to ABP for the damages he caused (loss of the truck and the Customer's order).

Question 3 – July 2014 – Selected Answer 2

1. In motorist's lawsuit, only ABP is liable to motorist. At issue is the liability of the company and members for torts committed in the ordinary course of an LLC's business.

Under the doctrine of respondeat superior a principal is vicariously liable for the torts of employees acting within the scope of their employment. On the other hand, under the TBOC, members of an LLC enjoy limited liability for the debts of the company. They are not personally liable for claims against the company that do not arise from their own negligence. Here, motorist has sued ABP, Blake, and Abner but will only recover against ABP. ABP is vicariously liable to the motorist. First the driver was negligent because he ran a red light and collided with the motorist. Second, as a delivery truck driver he was an employee acting within the scope of employment. Thus, all of the elements of respondeat superior are met and ABP will be liable to the motorist.

On the other hand Abner and Blake will not be personally liable. As members of ABP they enjoy the limited liability protection of the entity. Motorist has no claim against either of them for their own negligence. Additionally, there is no indication that it would be appropriate to pierce the corporate veil in this situation as there has been no fraudulent conduct. Thus, the most Abner or Blake stand to lose in this situation is any capital contribution they have made to ABP.

2. In the customer's suit only ABP and Blake are liable to customer. At issue is the liability of an LLC and its members for contracts made by the LLC and of the member of an LLC for his own negligence. LLCs are liable for any contract entered into by agents with actual authority. Typically, the members of an LLC are not liable of contracts of the company if they sign the contracts in their capacity of members on behalf of the LLC. On the other hand, the general rule of limited liability for LLCs does not limit the liability of members to third parties for their own negligence.

ABP will be liable to customer on the contract signed by Abner and Blake. The partnership agreement grants both of them "actual authority to enter into agreements on behalf of ABP." This

grants each of them actual authority as agents to bind the company. By signing the contract as "managing members" they bound the company to the contract. When the contract was breached by nonperformance due to Blake's antics, the company was liable for damages. Even if only one of the members had signed the contract, the company would still be liable as the company agreement granted actual authority to both members. Thus, ABP is liable on the contract with customer.

Here, Abner will not be found liable on the customer's suit. The only bases on which liability could be found are that he signed the contract and is a member of the LLC. As discussed above, the limited liability protection of the LLC prevents Abner's liability by solely being a member. Additionally, Abner's signing of the contract in his capacity as a "managing member" does not make him liable on the contract. He was acting as an agent of the company with actual authority per the company agreement and disclosed both his agent status and his principal. Thus he cannot be held liable simply by having signed the contract.

Blake, on the other hand, can be found liable for his own negligence to customer. He will not be found liable on any of the bases discussed above with respect to Abner. On the other hand, because he was personally responsible for the crash of the truck and the resulting damages the customer can file suit for Blake's personal negligence. Nothing in the TBOC allows a member of an LLC to shield himself from liability on this basis.

3. ABP should prevail against Blake in its claim for breach of fiduciary duty. Members of an LLC owe the company a duty of care to act in a manner that a reasonably prudent member would act. This duty can be limited by agreement of the members.

Here, the members agreed to limit their fiduciary duties to the company but expressly did not include matters of gross negligence or intentional misconduct. Blake's conduct constituted at least gross negligence and perhaps intentional misconduct. He was sent to deliver a large order for which time was of the essence. Instead of promptly delivering his goods, he stopped at a bar where he became extremely intoxicated (three times the legal limit). He then crashed the truck causing significant damage to the company due to the destroyed truck and breached contract. Given all of these facts, Blake was at least grossly negligent with respect to his duty of care and is thus liable to the LLC.

Question 3 – July 2014 – Selected Answer 3

1. In the motorist's suit, ABP will be held liable, but Abner and Blake will not be held liable. At issue here is the liability of a limited liability company (LLC) and its members for the torts committed by the LLC's employees. Under Texas law (the Texas Business Organizations Code), members of an LLC are shielded from any of the LLC's debts. The LLC will be held liable for any torts committed by employees of the LLC when the torts are committed within the course and scope of the employee's employment.

Here, the ABP employee was driving the delivery truck--and the facts state it was in the course and scope of his employment to do so. Because the employee ran the red light and hit the motorist while he was acting in the course and scope of his employment, LLC will be liable for the debt to motorist.

Abner and Blake will not be liable because they are members of the LLC, and the LLC will shield them from liability. The fact that they are managing members and have the authority to bind ABP to contracts does not waive their liability shield because both of these duties are within the safe harbor of the statute.

2. In the customer's suit, Blake and ABP will be held liable; Abner will not be held liable. At issue here is the liability of an LLC and its members for contracts signed by the members, and torts committed by a member.

Under Texas law, an agent is not liable on a contract he signed for the principal where the agent has actual authority to sign a contract on the principal's behalf. Here, the written company agreement of the LLC stated that the managing members (Abner and Blake) would have the "authority to enter into agreements on behalf of ABP." Further, both signed their name to the contract with customer including the words "as Managing Members." Abner and Blake will not be liable on the underlying contract with customer because they had actual

authority to make the contract, and they signed the contract in their capacity as agents. ABP will be liable on the contract because it is the principal, and principals are liable for the contracts that agents sign on their behalf, when the agents have the authority to make those contracts.

While members of an LLC are not liable for the torts committed by employees of the LLC, they are liable for their own torts they commit while working within the course and scope of the LLC. An employee who is on a frolic is not considered to be within the course and scope of the employment. The frolic occurs where the employee deviates from the business of its employer for period of time that is extensive. When an employee is on a detour, he will still be considered to be acting within the course and scope of his employment. A detour is a brief period of time where the employee is not engaged in business for the employer.

Here, Blake will be personally liable for the tort he committed. While delivering an order to customer, he was extremely intoxicated. He wrecked the company vehicle and destroyed the customer's order as a result of his intoxication. He will be liable to customer for damages.

Abner will not be personally liable for Blake's tort. Members have no duty to supervise other members. Abner did not know that Blake had a drinking problem, or that Blake was delivering the order while his blood alcohol level was three times the legal limit. As a result, Abner will bear no liability.

ABP will be liable to customer for Blake's tort. Although Blake did not act within the scope of his employment by stopping at the bar on the way to deliver the order, it appears that his stop was brief. Additionally, the tort was committed once he was again acting in the scope of the employment--delivering the customer's order in the company van. Because Blake committed a tort within the scope of the employment ABP will be held vicariously liable.

3. ABP should prevail on its cross-claim against Blake. At issue here is whether managing members can waive their fiduciary duties to the LLC.

Under Texas law, while managing members are permitted to limit their liability to the LLC, they may not completely waive their fiduciary duties to the LLC. Such unwaivable fiduciary duties include the duty of care, good faith, and duty of loyalty. The duty of care requires that a managing member act as would a prudent person.

Here, Blake has breached his duty of care. A prudent person would not consume copious amounts of alcohol, then proceed to drive a company delivery van to deliver an order to a customer. Blake's blood alcohol level was three times the legal limit when he was driving the van. He was not acting prudently and breached the duty of care. Alternatively, ABP can argue that Blake was "grossly negligent" within the terms of the Company Agreement such that would allow ABP to recover.

ABP will be able to prevail on its cross-claim against Blake for breaching his fiduciary duty.