



Counsel's Corner

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Typically forming a new entity to serve as a commercial tenant or buyer is a good idea.... But not always!

In 1986 Dick's Last Resort, as tenant, signed a Lease for Dallas property located in the West End District. In 1999 the Landlord allowed Dick's Last Resort to use a newly formed, related entity (Dick's West End) to replace the old one and serve as the new tenant.

Presumably the Landlord did not recognize the Tenant's intentions.

In 2005 the restaurant relocated without the Landlord's consent and rent payments ceased. The Landlord sued Dick's West End for breach of the lease, but also alleged that Dick's Last Resort was liable under a little-used legal theory called "*piercing the corporate veil*." That theory imposes liability by ignoring the corporate structure, when the corporate form has been used as part of an unfair device to achieve an inequitable result. Typical allegations include fraud and evasion of existing legal obligations.

The 44th Judicial District Court of Dallas, in a jury trial, awarded Judgment to the Landlord against all defendants. Dick's Last Resort, Dick's West End and various other defendants appealed.

Testimony from a Dick's principal indicated that Dick's West End was purposefully formed as a no-asset company, so that it could close the restaurant and leave the Landlord with the remedy of pursuing an insolvent tenant. The jury, after receiving evidence that Dick's: (i) moved the restaurant only three blocks away, (ii) was paying rent at half the cost of the initial Lease, and (iii) was in continual operation with the same employees, equipment and operating company from the date of the relocation through the date of trial, concluded that Dick's Last Resort had perpetrated a fraud. The jury would not let Dick's Last Resort escape liability by forming a shell entity and transferring to it the tenant's interest in the Lease.

The Judgment of the trial court was upheld in a recent appellate decision.

Bottom line:

1. Be careful when you form a new entity for a singular purpose.
2. Be careful when you give deposition testimony, written statements or Court testimony.
3. Juries and Judges do not favor escaping liability by playing the entity shell game.

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