ment Security Review Board's decisions: All findings of fact are conclusive and binding on the reviewing court; the court can only consider the evidence and reasonable inferences therefrom that are most favorable to the Review Board's decision.[36] On its face, this rule is contrary to the "substantial evidence on the whole record" rule enunciated by the Second District Court of Appeals in *City of Evansville.* However, it should not be viewed as contrary to that decision due to the specific statutory restrictions on the scope of review for Employment Security Review Board decisions, which make the decisions of the Review Board conclusive and binding as to all questions of fact.[37] Therefore, reviewing the record as a whole to determine if substantial evidence existed to support the agency's findings of fact would have been beyond the limitation placed upon reviewing courts.

III. Business Associations

*Paul J. Galanti**

During the survey period five cases were decided that warrant discussion,[1] and there were several significant legislative developments.

---

[36] *Id.* at 428.

[37] IND. CODE § 22-4-17-12 (1976).

*Professor of Law, Indiana University School of Law—Indianapolis. A.B., Bowdoin College, 1960; J.D., University of Chicago, 1963.

[1] There were three other decisions worth a passing reference. The first is Johnson v. Motors Dispatch, Inc., 360 N.E.2d 224 (Ind. Ct. App. 1977), affirming in part and reversing in part summary judgment for two trucking companies in a personal injury suit. The two companies were the owner and lessee of the rig. In turn the lessee's driver was on a "trip lease" from Motors Dispatch when the accident occurred. Under Interstate Commerce Commission rules, 49 C.F.R. § 1057.4(a)(4) (1976), Motors Dispatch was responsible for the driver's torts during the lease. However, a lessor can operate a truck for a lessee, Transamerican Freight Lines v. Brada Miller Freight Systems, 423 U.S. 28, 39 (1975), and the lessor can be liable under the doctrine of respondeat superior if it maintains a right to control the driver. Vance Trucking Co. v. Canal Ins. Co., 249 F. Supp. 33 (D. S.C. 1966), *aff'd,* 395 F.2d 391 (4th Cir.), *cert. denied,* 393 U.S. 845 (1968). The issue in *Johnson* was whether the two defendants possessed the right to control the driver's actions. The Court of Appeals held that the owner of the rig unquestionably had no right of control, so summary judgment in his favor was proper, but there was a genuine question of fact as to whether the lessee had surrendered control to Motors Dispatch under the borrowed servant doctrine. Under this doctrine the lending employer escapes liability if there is a transfer of control from the servant to the transferee. *See* W. SEAVEY, AGENCY § 86 (1964); RESTATEMENT (SECOND) OF AGENCY § 227 (1958). However, the court might have been contemplating the slightly different

A. Securities Law Fraud

A case that appears deceptively simple, but which has, or more accurately had, some interesting ramifications is *B & T Distributors, Inc. v. Riehle.*[2] In *Riehle*, the First District Court of Appeals reversed and remanded a decision of the Tippecanoe Circuit Court adverse to individual defendants Kingery and Schilling, and remanded with instructions to enter judgment in favor of their counterclaim and to rescind the purchase of the corporate stock of B & T from the Riehles.[3]

The action was filed by the Riehles to recover approximately $13,000 that the defendants had agreed to pay as part of the transaction. Kingery and Schilling counterclaimed, seeking rescission on two theories: (1) common law fraud; or (2) fraud as defined under the Indiana Securities Act,[4] commonly known as the Blue Sky Act. The

---

situation where there is dual employment and both masters are liable. *See* Gordon v. S.M. Byers Motor Car Co., 309 Pa. 453, 164 A. 334 (1932). *See generally* RESTATEMENT (SECOND) OF AGENCY § 226 (1958); W. SEAVEY, *supra* § 85.

The second decision is Burger Man, Inc. v. Jordan Paper Prods., Inc., 352 N.E.2d 821 (Ind. Ct. App. 1976), where the court recognized that corporations can only act through agents and that such agents can be clothed with apparent authority. Soft Water Utils., Inc. v. Le Fevre, 308 N.E.2d 395 (Ind. Ct. App. 1974); Storm v. Marsischke, 304 N.E.2d 840 (Ind. Ct. App. 1974). The court correctly stated the general rule: The third person must reasonably rely on a manifestation by the principal that the agent has authority. 352 N.E.2d at 832. However, since the manifestation seemed to result from the corporate positions of the agents the court more accurately might have been contemplating the distinct but overlapping concept of inherent authority. Under this concept the agent possesses authority simply by being employed in a position that would normally carry the authority perceived by the third party. *See* Farm Bureau Mut. Ins. Co. v. Coffin, 136 Ind. App. 12, 186 N.E.2d 180 (1962). *See generally* RESTATEMENT (SECOND) OF AGENCY §§ 8A, 161A (1958); W. SEAVEY, *supra* § 59D.

[2]359 N.E.2d 622 (Ind. Ct. App. 1977).

[3]The court also awarded interest at 6% from the date of payment for the shares, costs, and reasonable attorneys' fees as provided by the civil penalty section of the Indiana Securities Act in effect when the suit was filed. Indiana Securities Act, ch. 333, § 507, 1961 Ind. Acts 984 (amended 1975). In 1975, the interest rate was increased to 8%. IND. CODE § 23-2-1-19(a) (1976).

[4]IND. CODE §§ 23-2-1-1 to -21 (1976). The anti-fraud provision of the Act, in pertinent part, makes it "unlawful for any person in connection with the offer, indirectly . . . to make any untrue statements of a material fact necessary or *to omit to state a material fact necessary in order to make the statements made in the light of circumstances under which they are made, not misleading . . . .*" *Id.* § 23-2-1-12 (emphasis added). The civil penalty provision then in effect provided for rescission by purchasers of securities, or damages if the securities had been sold, against a seller who

> offers or sells a security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading (the buyer not knowing of the untruth or omission), and who does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the untruth or omission . . . .

trial court rejected both grounds in entering judgment for the Riehles, but the appellate court only discussed the securities law contention. Of course, if a cause of action was properly stated under the Blue Sky Act, it was unnecessary to discuss the other ground.

The appellate court first considered the Riehles' argument that the sale of the B & T shares was exempt from the Blue Sky anti-fraud provision as either an isolated nonissuer transaction[5] or a small offering.[6] It correctly rejected this argument because section 23-2-1-2(b)[7] on its face only exempts certain transactions from the Act's requirement that securities be registered with the Indiana

---

Indiana Securities Act, ch. 333, § 507, 1961 Ind. Acts 1023 (amended 1975). The 1975 amendments to the Indiana Securities Act also made rescission available to sellers of securities, and § 23-2-1-19(a) now reads as follows:

> Any person who offers, purchases or sells a security in violation of any of the provisions of this chapter, and who does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the violation, is liable to any other party to the transaction, who did not knowingly participate in the violation or who did not have, at the time of the transaction, knowledge of the violation, who may sue either at law or in equity to rescind the transaction or to recover the consideration paid, together, in either case, with interest at eight percent (8%) per year from the date of payment, costs, and reasonable attorneys' fees, upon the tender of the security or consideration received by the person bringing the action.

IND. CODE § 23-2-1-19(a) (1976). For discussions of the Indiana Securities Act, *see generally* Doxsee, *Securities Problems in Indiana*, 17 RES GESTAE 6 (1973); Pasmas, *Securities Issuance and Regulation: The New Indiana Securities Law*, 38 IND. L.J. 38 (1963); Note, *Securities Registration Requirements in Indiana*, 3 IND. LEGAL F. 270 (1969).

[5]IND. CODE § 23-2-1-2(b)(1) (1976) exempts "any isolated nonissuer transaction, whether effected through a broker-dealer or not."

[6]The provision in effect at the time of the suit exempted *offers* of securities to no more than 20 persons, provided certain conditions were met. Indiana Securities Act, ch. 333, § 102, 1961 Ind. Acts 984 (amended 1975). The 1975 amendments broadened the scope of this transactional exemption by making it available for *sales* to no more than 35 persons. IND. CODE § 23-2-1-2(b)(10)(i) (1976). *See generally* Galanti, *Business Associations, 1975 Survey of Recent Developments in Indiana Law*, 9 IND. L. REV. 33, 59-60 (1975). The § 23-2-1-2(b)(1) and (10) transactional exemptions were the focus of Hippensteel v. Karol, 304 N.E.2d 796 (Ind. Ct. App. 1973), *discussed in* Galanti, *Business Associations, 1974 Survey of Recent Developments in Indiana Law*, 8 IND. L. REV. 24, 29-35 (1974).

[7]The current language of the exemption is as follows: "[T]he following transactions are exempted from the registration requirements of Section 3 of this chapter." IND. CODE § 23-2-1-2(b) (1976). The former language, in effect when *Riehle* was filed, exempted the transaction "from section 201." Indiana Securities Act, ch. 190, § 1, 1969 Ind. Acts 541 (amended 1975). Although indirect, the reference was to § 3 of the Act, which makes it "unlawful for any person to offer or sell any security in this state unless (1) it is registered under this act or (2) the security or transaction is exempted . . . ." IND. CODE § 23-2-1-3 (1976). The criminal liability provision of the Act, *id.*, § 23-2-1-18.1, also applies even if the security or transaction is exempt.

Securities Commissioner before they are offered or sold to the public.[8] Thus, even if a particular transaction is exempt from registration, the anti-fraud proscription still applies. This approach to securities regulation is not unique with Indiana. The Federal Securities Act of 1933[9] also exempts particular types of securities[10] and transactions[11] from the registration requirement of the Act but not the anti-fraud provisions.[12] Limiting exemptions to the registration requirement is also the norm of other state Blue Sky Laws.[13]

The legislative rationale is clear. The registration process[14]

---

[8]Indiana provides two registration procedures: registration by coordination for any security for which a registration statement has been filed under the Securities Act of 1933, 15 U.S.C. §§ 77a - 77aa (1970 & Supp. V 1975), in connection with the same offering, IND. CODE § 23-2-1-4 (1976), and registration by qualification for all other securities, *id.* § 23-2-1-5. *See generally* authorities cited note 4 *supra.* IND. CODE § 23-2-1-2(a) (1976) exempts certain types of securities from the registration requirements.

[9]15 U.S.C. §§ 77a - 77aa (1970 & Supp. V 1975). The registration requirement is imposed by § 5 of the Act. *Id.* § 77e (1970). The commentary on federal securities regulation is legion. The classic reference is L. LOSS, SECURITIES REGULATION (2d ed. 1961 & Supp. 1969), but other selected references can be found in D. RATNER, SECURITIES REGULATION (1975).

[10]15 U.S.C. § 77c(a) (1970). The parallel is not complete. Section 3 provides that the provisions of the 1933 Act do not apply to exempted securities "[e]xcept as hereinafter expressly provided." *Id.* The general civil liability and the anti-fraud provisions of the Act expressly apply to any person who uses the instruments of interstate commerce to sell securities. *Id.* §§ 77*l*, 77q. The provision exempts securities, but certain classes of exempt securities are in reality transactional exemptions if they are securities issued in exchange for other securities, *id.* § 77c(a)(9), (10); securities sold in intrastate offerings, *id.* § 77c(a)(11); and small offerings made pursuant to § 3(b), *id.* § 77c(b). *See generally* D. RATNER, *supra* note 9, at 220. Indiana also treats as a security exemption what might be considered transactional. *See* IND. CODE § 23-2-1-2(a)(8) (1976).

[11]15 U.S.C. § 77d (1970 & Supp. V 1975). Unlike § 3, § 4 of the 1933 Act specifically provides that the exemption is limited to the registration requirement of § 5. *Id.* § 77e (1970).

[12]*Id.* §§ 77*l*(2), 77q(a) (1970).

[13]Section 402 of the Uniform Securities Act, 7 UNIFORM LAWS ANNOTATED § 402 (1970), exempts specified securities from § 301 of the Act, the registration provision, but not §§ 101, 409 and 410, which are the anti-fraud, criminal and civil liability provisions respectively. The Uniform Securities Act has been adopted in part or in whole in 32 jurisdictions, and certain provisions of the Indiana Securities Act are based on the Uniform Securities Act. *See generally* 1 L. LOSS, *supra* note 9, at 42 (1961); 1 F. O'NEAL, CLOSE CORPORATIONS § 1.16, at 85 (1971). Blue Sky laws have been prolific generators of legal writing. Professors Jennings and Marsh use almost two full pages to list articles. R. JENNINGS & H. MARSH, SECURITIES REGULATION 1271-72 (4th ed. 1977).

[14]One of the basic purposes of all securities regulation is to provide investors with material financial and other information about issuers of securities. SEC v. Ralston Purina Co., 346 U.S. 119 (1953). *See generally* R. JENNINGS & H. MARSH, *supra* note 13, at 53; 1 L. LOSS, *supra* note 9, at 121-28, 178-86 (1961); H. SOWARDS, THE FEDERAL SECURITIES ACT (11 Business Organizations) pt. 1, § 1.02 (1977). To this end, the term

results in formalized disclosure of information about an issuer that is essential to an honest securities market. However, in some situations the expensive process would not add to the protection of investors or benefit the public, that is, a transaction between two purchasers and two sellers, as in *Riehle*. This does not mean such purchasers should be left to the mercies of the seller or to whatever rights they might have at common law. Quite the contrary, it is essential to the scheme of regulation that a buyer of unregistered securities have recourse against a seller[15] who has engaged in any fraudulent practices.[16]

Thus, the issue in *Riehle* was whether the sellers had violated section 23-2-1-12. Mr. Riehle had given the plaintiffs an estimated profit and loss statement wherein B & T showed a profit for the first six months of 1971 of approximately $5,800 and a gross profit margin on sales of approximately 33.4%. For the subsequent equivalent period in 1975, Kingery and Schilling had an actual net loss somewhat over $100 and a gross profit margin on sales of approximately 26.2% for the equivalent period in 1972. Although Kingery and Schilling had asked to see the corporation's books of account, the Riehles did not comply.[17] These books presumably would have shown that Riehle had grossly overstated the profitability of the business.

The court held that the Riehles' failure to comply with this request was an "omission" of a material fact needed to clarify statements made about the B & T shares and consequently violated the Blue Sky Act. The result would seem appropriate because section 23-2-1-12(2) specifically prohibits such omissions,[18] just as section

---

"security" is always broadly defined, IND. CODE § 23-2-1-1(k) (1976), 15 U.S.C. § 77b(1) (1970), and liberally construed, SEC v. W.J. Howey Co., 328 U.S. 293 (1946). *But see* United Housing Foundation, Inc. v. Forman, 421 U.S. 837 (1975) (strict construction).

[15]Although fraud by a *purchaser* of securities has always been proscribed, IND. CODE § 23-2-1-12 (1976), rescission by a defrauded seller was not authorized until 1975, *id.* § 23-2-1-19(a).

[16]Assuming that the mails or some facilities of interstate commerce were involved, such as a telephone call, Kingery and Schilling could have also brought an action under the Securities Act of 1933 as well. Section 22(a) of the 1933 Act grants state courts concurrent jurisdiction to enforce the Act. 15 U.S.C. § 77v(a) (1970). *See* Wilko v. Swan, 346 U.S. 427 (1953). They could not have sued in an Indiana court for a violation of the Securities Exchange Act of 1934 because § 27 grants exclusive jurisdiction to federal courts. 15 U.S.C. § 78aa (1970). *See* American Distilling Co. v. Brown, 295 N.Y. 36, 64 N.E.2d 347 (1945), *aff'g* 269 App. Div. 763, 54 N.Y.S.2d 855 (1945), *aff'g* 184 Misc. 431, 51 N.Y.S.2d 614 (Sup. Ct. 1944). *See generally* Galanti, *Business Associations, 1976 Survey of Recent Developments in Indiana Law*, 10 IND. L. REV. 57, 67-76 (1976).

[17]359 N.E.2d at 623, 625.

[18]15 U.S.C. § 77g(a)(2) (1970).

17a(2) of the Federal Securities Act of 1933[19] and rule 10b-5 promulgated under the Securities Exchange Act of 1934.[20] However, what the court, and maybe the parties, overlooked is whether there is an obligation on the part of purchasers or sellers of securities seeking rescission under the Indiana Blue Sky Act to act with due diligence in protecting their interests, and, if so, whether Kingery and Schilling exercised sufficient care.

The opinion states that Kingery and Schilling unsuccessfully sought to obtain the books and records of B & T before purchasing the stock but did not insist on seeing them before making a $70,000 investment. It would not be unreasonable to deny rescission to parties to a securities transaction who act so cavalierly. In other words, perhaps the purchaser of securities should be required to take *some* steps to check out an assertion of fact or at least follow through on an inquiry. After all, this was a face-to-face transaction initiated by Kingery and not a faceless transaction over a stock exchange. This certainly is not a plea for the return of the rule of caveat emptor, nor does it ignore that the elements of common law fraud have been liberalized in recent years.[21] It simply recognizes that a securities buyer might properly be expected to look out for his or her interests rather than relying on rescission if an investment goes sour.

The civil penalty provision authorizing rescission appears neutral on this point in its current form and as in effect at the time of *Riehle*.[22] It clearly bars relief where the buyer knows of the omission or has knowledge of the violation, as provided by the 1975 amendments. Construing the statute literally, Kingery and Schilling should have been denied rescission because they obviously knew they had not received the books and records and so were aware of the "omission." The court would then have had to consider the common law fraud claim. However, even if form is ignored in favor of

---

[19]17 C.F.R. § 240.10b-5 (1977). The rule was promulgated pursuant to § 10(b) of the 1934 Act. 15 U.S.C. § 78j(b) (1970). Courts and commentators have at time placed the rule on a pedestal of honor, as in SEC v. Texas Gulf Sulfur Co., 401 F.2d 833, 847-48 (2d Cir. 1968), *cert. denied*, 394 U.S. 976 (1969), where the court stated the rule was promulgated "to prevent inequitable and unfair practices and to insure fairness in securities transactions generally, whether conducted face-to-face, over the counter or on exchanges . . . ." *Id.* at 847-48 (citing 3 L. LOSS, *supra* note 9, at 1455-56 (1961)). However, its origins were very modest. *See* Comments of Milton V. Freeman in the *Conference on Codification of the Federal Securities Laws*, 22 BUS. LAW. 793, 922 (1967). The judicial attitude has changed since *Texas Gulf*. *See, e.g.*, Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 736 n.8 (1975).

[20]IND. CODE § 23-2-1-12(2) (1976) is clearly based on federal rule 10b-5, which in turn was based on § 17a(2) of the Federal Securities Act of 1933, 15 U.S.C. § 77g(a)(2) (1970). *See* Freeman, *supra* note 19.

[21]W. PROSSER, HANDBOOK OF THE LAW OF TORTS § 108, at 715-16 (4th ed. 1971).

[22]*See* discussion in note 4 *supra*.

substance and the "omission" was not of the books of account, but of their contents, it would not strain the statute to say that persons like Kingery and Schilling, who knew that B & T's books might not support the Riehles' claim, but who did not insist on examining them, had constructive knowledge of the omissions. To be sure, there is a countervailing argument: Section 23-2-1-19 provides a due diligence defense for a defendant who can prove he "did not know, and in the exercise of reasonable care could not have known, of the violation,"[23] and if the legislature had intended to impose a due diligence obligation on a plaintiff, it would have so provided.

Under the federal securities laws some courts have obligated plaintiffs in anti-fraud actions to act with diligence. For example, in *Kaplan v. Vornado, Inc.*[24] plaintiff was denied relief in a rule 10b-5 action alleging that a convertible debenture should have stated on its face that the issuer could force conversion by calling the security because he had done nothing to learn the basic nature of the security. An even clearer example was *Mitchell v. Texas Gulf Sulphur Co.*,[25] denying recovery to a plaintiff who sold Texas Gulf stock almost a week after the company announced its famous Canadian ore strike. Plaintiff claimed reliance on the earlier infamous "gloomy" press release of April 12, 1964, discounting rumors of the strike. In rejecting the claim the court stated:

> At some point in time after the publication of a curative statement such as that of April 16, stockholders should no longer be able to claim reliance on the deceptive release, sell, and then sue for damages when the stock value continues to rise. *This is but a requirement that stockholders too act in good faith and with due diligence in purchasing and selling stock.*[26]

---

[23]In effect this provision makes actionable all intentional and negligent misrepresentations and omissions but not innocent and non-negligent ones. *See generally* 3 A. BROMBERG, SECURITIES LAW: FRAUD § 8.4(210) (1977). Professor Bromberg doubts that § 410(a)(2) of the Uniform Securities Act, 7 UNIFORM LAWS ANNOTATED § 410(a)(2) (1970), which is similar to § 23-2-1-19(a)(2) of the Indiana Code before the 1975 amendments, ch. 333, § 507, 1961 Ind. Acts 1023, imposes a duty of inquiry on a plaintiff or bars recovery on the basis of constructive rather than actual knowledge. Based upon the similarity of the language to § 12(2) of the Securities Act of 1933, 15 U.S.C. § 77*l*(2) (1970), and the authority construing that provision, he reasons that constructive knowledge does not bar recovery. His assertion is carefully couched, but then the authority is less than clear. *See* 3 A. BROMBERG, *supra* §§ 8.4(220), (317).

[24][1972-73 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 93,585 (N.D. Ill. 1971).

[25]446 F.2d 90 (10th Cir.), *cert. denied*, 404 U.S. 1004 (1971), *rehearing denied*, 404 U.S. 1064 (1972).

[26]446 F.2d at 103 (emphasis added). In Financial Indus. Fund, Inc. v. McDonnell-Douglas Corp., 474 F.2d 514, 516 (10th Cir. 1973), the court in dictum imposed a duty

The degree of care a plaintiff must exercise would of course vary with the circumstances, such as the nature of the omission and the sophistication of the plaintiff.

Admittedly, as noted in *McLean v. Alexander*,[27] the due diligence requirement arose as a defensive response to the ballooning number of private actions brought under rule 10b-5. Now that *Ernst & Ernst v. Hochfelder*[28] establishes scienter as an element of a rule 10b-5 suit, *McLean* indicates that the "plaintiff's diligence" defense might not be appropriate if an actual intent to defraud has been established. The Seventh Circuit in *Sundstrand Corp. v. Sun Chemical Corp.*[29] agreed with the *McLean* proposition by observing that under a *Hochfelder* standard, only gross conduct somewhat comparable to that of defendant's should cancel out wanton or intentional fraud.

However, as Professor Bloomenthal points out, a plaintiff's care might still be an appropriate inquiry in the "uncharted area of liability between negligence and specific intent to defraud,"[30] and the diligence of a plaintiff as a defense is "more likely to arise in the context of nondisclosure and in transactions as to which a court concludes defendant had no duty to make disclosure to the plaintiff, because the information was generally available or because plaintiff had equal access to the information."[31] Even the most sophisticated investor can be defrauded where there is nondisclosure of material information,[32] but it is questionable if Kingery and Schilling were

---

on a securities purchaser to investigate the stock adequately before purchasing. However, holding the particular plaintiff, a mutual fund, to a higher standard than the ordinary investor is not surprising. *See* 3A H. BLOOMENTHAL, SECURITIES AND FEDERAL CORPORATE LAW § 9.21(6), at 9-109 n.420.2 (rev. 1976).

[27]420 F. Supp. 1057, 1077-79 (D. Del. 1976). For a general discussion of the due diligence requirement, or the bar of constructive knowledge as it may be called, *see* 3 A. BROMBERG, *supra* note 23, § 8.4(652); 3A H. BLOOMENTHAL, *supra* note 26, § 9.21(6); Wheeler, *Plaintiff's Duty of Due Care Under Rule 10b-5: An Implied Defense to an Implied Remedy*, 70 NW. L. REV. 561 (1976); Comment, *Negligent Misrepresentations Under Rule 10b-5*, 32 U. CHI. L. REV. 824, 844 (1965).

[28]425 U.S. 185 (1976).

[29]553 F.2d 1033 (7th Cir. 1977), *cert. denied*, 46 U.S.L.W. 3207 (U.S. Oct. 4, 1977) (No. 77-255). *See also* Dupuy v. Dupuy, 551 F.2d 1005 (5th Cir. 1977); Holdsworth v. Strong, 545 F.2d 687, 693 (10th Cir. 1976). Perhaps involvement by a plaintiff that would justify an in pari delecto defense might be required. *See* Tarasi v. Pittsburgh Nat'l Bank, [1977] FED. SEC. L. REP. (CCH) ¶ 96,050 (3rd Cir. 1977), *cert. denied*, 98 S. Ct. 505 (1977). Plaintiffs who were active participants in forming the corporation that violated the Indiana Securities Act have been denied rescission. Theye v. Bates, 337 N.E.2d 837 (Ind. Ct. App. 1975). *Theye* is discussed in Galanti, *Business Associations, 1976 Survey of Recent Developments in Indiana Law*, 10 IND. L. REV. 57, 76-79 (1976).

[30]H. BLOOMENTHAL, SECURITIES LAW IN PERSPECTIVE 87 (1977).

[31]*Id.*

[32]*See* Straub v. Vaisman & Co., 540 F.2d 591 (3rd Cir. 1976).

true fraud victims where they asked for, but did not insist on, seeing B & T's books. Although the Riehles were less than candid, they did not appear to be guilty of intentional fraud, or at least the trial court so found.

Riehle appears to obligate the seller of corporate shares to furnish the purchaser with the books of account, without request, whenever any representation about an enterprise's profitability has been made. This may or may not be an undue burden, since books of account can well contain material information;[33] but as a matter of policy, a purchaser of securities in a face-to-face transaction should be obligated to follow through on a request to examine books and records before an unprofitable transaction can be rescinded. Of course, the whole problem with *Riehle* might hinge on the trial court's finding that the Riehles had not made false representations of fact and the court's silence as to whether there were omissions of material facts. The court of appeals might have felt there were misrepresentations but did not want to disturb the findings of fact.[34]

B. Covenants Not to Compete

Another decision of interest is *Peters v. Davidson, Inc.*[35] The First District Court of Appeals affirmed an order of the Boone Superior Court enforcing a covenant not to compete and granting Davidson preliminary injunctive relief against its former employee Peters. The disputed covenant was not between Peters and Davidson, as such, but was in an employment agreement between Peters and Avels, Inc., Davidson's predecessor, where Peters was a sales engineer. The particular provision prohibited Peters from divulging or using trade secrets, shop drawings, customer lists or other confidential information of Avels and prohibited him (1) from being connected with or operating a competing business for one year following his employment; and (2) from referring to Avels or its affiliates to their detriment, diverting or attempting to divert business from them, or hiring or attempting to hire any Avels employee for two years following his employment.

Peters worked for Avels until January 1, 1973, when it merged

---

[33]Neidermeyer v. Neidermeyer, [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,123 (D. Ore. 1973). *See generally* Holdsworth v. Strong, 545 F.2d 687 (10th Cir. 1976).

[34]Indiana Trial Rule 52A provides that a court on appeal shall not set aside a finding of the trial court unless it is clearly erroneous. This has been interpreted to require the reviewing court to hold a firm conviction that a mistake has been made, notwithstanding evidence to support the finding. *See* United States v. United States Gypsum Co., 333 U.S. 364, 395 (1948) (construing FED. R. CIV. P. 52(a)).

[35]359 N.E.2d 556 (Ind. Ct. App. 1977).

with another company under the Indiana General Corporation Act[36] to form Davidson, Inc. He continued with Davidson in the same capacity and in the same territories until he resigned in December, 1975. One week later he formed a corporation to compete with Davidson in the same area.[37] Davidson then filed suit alleging the breach of the covenant not to compete, and the trial court granted the application for preliminary injunction phrased in the terms of the covenant.

Although the court considered Peters' contention that the trial court incorrectly determined the question of law involved as the crux of the case, the bulk of the opinion dealt with whether the interlocutory order should be treated as a decision on the merits of the case. Because there was no showing that the hearing for the preliminary injunction was to be treated as a trial on the merits,[38] the court did not treat the order as one on the merits and only reviewed the trial court's decision for an abuse of discretion.[39]

The appellate court started from the premise that covenants not to compete in employment contracts are enforced if they are (1) reasonably necessary for the protection of the employer's business, (2) not unreasonably restrictive of the employee's rights, and (3) not against public policy;[40] but the court recognized that covenants of

---

[36]IND. CODE §§ 23-1-5-1 to -8 (1976). The court referred to the transaction as a merger, but it appears from the facts that it might have been a consolidation where the constituent companies cease to exist and a new consolidated company emerges. *See* H. HENN, HANDBOOK OF THE LAW OF CORPORATIONS § 346 (2d ed. 1970). The Indiana General Corporation Act recognizes the distinction between the two procedures, *compare* IND. CODE § 23-1-5-2 (1976) *with id.* § 23-1-5-3, but for purposes of deciding *Peters*, the distinction was irrelevant. For a general discussion of the rights of the surviving corporation in a merger or of the new corporation in a consolidation, *see* Z. CAVITCH, BUSINESS ORGANIZATIONS §§ 67.01-67.04 (rev. ed. 1977); A. CONARD, CORPORATIONS IN PERSPECTIVE § 119 (1976); 15 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS §§ 7040-7041, 7075-7083.1 (perm ed. 1973); H. HENN, *supra* § 346; N. LATTIN, THE LAW OF CORPORATIONS § 170 (2d ed. 1971).

[37]It was clear that Peters felt he was no longer bound by the covenants. He did not even make an effort to avoid competing with his former employer. 359 N.E.2d at 559.

[38]The application for the preliminary injunction could have been consolidated with a trial on the merits under Indiana Trial Rule 65(A)(2). *See generally* 4 W. HARVEY & R. TOWNSEND, INDIANA PRACTICE 388 (1971).

[39]359 N.E.2d at 560 (citing Rosenburg v. Village Shopping Center, Inc., 251 Ind. 1, 238 N.E.2d 642 (1968), and Angel v. Behnke, 337 N.E.2d 503 (Ind. Ct. App. 1975)).

[40]*Id.* (citing Miller v. Frankfort Bottle Gas, Inc., 136 Ind. App. 456, 202 N.E.2d 395 (1964), and Welcome Wagon, Inc. v. Haschert, 125 Ind. App. 503, 127 N.E.2d 103 (1955)). For a general discussion of the validity of covenants not to compete, *see* 6A A. CORBIN, CORBIN ON CONTRACTS § 1394 (1962); RESTATEMENT (SECOND) OF AGENCY § 396 (1958); RESTATEMENT OF CONTRACTS § 516 (1932); Blake, *Employee Agreements Not to Compete*, 73 HARV. L. REV. 625 (1960). For a refreshing, albeit lengthy, judicial analysis of this area, *see* Arthur Murray Dance Studios, Inc. v. Witter, 105 N.E.2d 685 (Ohio Ct. App. 1952).

this nature are strictly construed.[41] It concluded that the trial court did not abuse its discretion within these guidelines. Davidson had pleaded and proved enough to establish the irreparable harm necessary for injunctive relief[42] by showing Peters' continuing competition.[43]

On the merits of the case—and the court for all intents and purposes decided the merits—the court rejected Peters' argument that the restrictive covenants lapsed on January 1, 1974, and January 1, 1975, because the merger was the triggering event. According to the court, this point was argued "cogently,"[44] but not cogently enough. The flaw in the argument was section 23-1-5-5 of the Indiana General Corporation Act. The court cited the entire section, but it clearly was contemplating subsection (d), which provides "all and every other interest, of or belonging to or due to each of the corporations so merged or consolidated shall be taken and deemed to be transferred to and vested in such single corporation without further act or deed,"[45] and subsection (e) which provides that the single corporation resulting from the merger or consolidation is liable for all the liabilities and obligations of the constituent companies.[46] Thus, the contractual rights and obligations of Avels became those of Davidson by operation of law on January 1, 1973.[47]

Of course, the parties conceivably could have intended a merger to trigger the covenant, but this would make little sense from the employer's point of view. There is no question but that the court

---

[41]Struever v. Monitor Coach Co., 156 Ind. App. 6, 294 N.E.2d 654 (1973). *See generally* authorities cited note 40 *supra*.

[42]The court posited that irreparable harm could be established, even if the damages could not be measured in dollars. 359 N.E.2d at 561 (citing Welcome Wagon, Inc. v. Haschert, 125 Ind. App. 503, 127 N.E.2d 103 (1955)).

[43]Indiana Trial Rule 65(C) provides that the trial court must fix the amount of a security bond before a preliminary injunction can issue. Peters complained about the adequacy of the bond, but this was held to be within the discretion of the trial court. The court stated that if Peters should prevail and show damages exceeding the bond, he could recover the excess from Davidson, 359 N.E.2d at 561-62 (citing Howard D. Johnson Co. v. Parkside Dev. Corp., 348 N.E.2d 656 (Ind. Ct. App. 1976)), but it is not absolutely clear this is true in absence of a showing of malicious prosecution or abuse of process. *See* Jones Drilling Corp. v. Rotman, 245 Ind. 10, 15, 195 N.E.2d 857, 860 (1964).

[44]359 N.E.2d at 562. The dictionary defines "cogent" as something "appealing strongly to the reason or conscience; compelling belief, assent, or action; forcibly convincing as a *cogent* argument or discourse." FUNK & WAGNALL'S NEW STANDARD DICTIONARY OF THE ENGLISH LANGUAGE 517 (1974).

[45]IND. CODE § 23-1-5-5(d) (1976). *See generally* authorities cited note 36 *supra*.

[46]*Id.* § 23-1-5-5(e). *See generally* authorities cited note 36 *supra*.

[47]The merger agreement apparently provided for the assignment of contract rights to Davidson. 359 N.E.2d at 562.

correctly construed the particular agreement.[48] The purpose of the covenant, as with all restrictive covenants, was to protect Avels within reasonable limits from competition from a former employee. Certainly if Avels had simply changed its name to Davidson, it would clearly want to continue protection of the covenant and as far as Peters was concerned all the merger did was change Avels' name. His activities did not change after the merger, and he continued to accept the benefits of his employment agreement. Thus, Davidson was entitled to have its interests protected just as was Avels. Peters freely entered into an employment contract containing an apparently enforceable covenant not to compete, and it was proper not to relieve him of his contractual responsibilities simply because Avels was now Davidson.

C. Employment Contracts

A violinist discharged by the Indianapolis Symphony Orchestra for missing two tour concerts was partially successful in his damage action in *Indiana State Symphony Society, Inc. v. Ziedonis.*[49] In *Ziedonis*, the Second District Court of Appeals affirmed the judgment of the Marion Superior Court that the discharge was in violation of his contract[50] but reversed and remanded with directions as to recoverable damages.

Ziedonis' contract obligated him to attend concerts, and the Symphony argued that his absences constituted a breach justifying immediate discharge. Ziedonis responded that the discharge for cause provision of the Symphony's Master Agreement did not apply because his individual contract provided a penalty for his absences—a deduction from his weekly salary. He claimed they were justified.[51] The court concluded there was sufficient evidence

---

[48]The court cited its own decision in Struever v. Monitor Coach Co., 156 Ind. App. 6, 294 N.E.2d 654 (1973), for the proposition that covenants not to compete are strictly construed. 359 N.E.2d at 362. *See generally* authorities cited note 40 *supra.* However, *Struever* is not completely apposite because it involved a covenant not to compete ancillary to the sale of a business. The *Struever* court struck down the covenant because it did not contain adequate spatial or geographic limitations. This was particularly unfortunate for the corporate plaintiff, which had paid Struever for his shares in the business and now was faced with his competition. Perhaps the *Struever* court erred in not holding defendant to his bargain. At least Peters had not been "bought out" by Davidson and was using the money to start a competing business.

[49]359 N.E.2d 253 (Ind. Ct. App. 1976) (White & Buchanan, JJ., concurring).

[50]Ziedonis was discharged twice. The first discharge was to be effective at the end of the subsequent symphony season and the second discharge was effective immediately. He did not complain of the first discharge but only sought damages for what he would have earned until it became effective. *Id.* at 254.

[51]The court concluded the Symphony could not use evidence of Ziedonis' conduct before his first discharge in attempting to justify the subsequent discharge for cause. *Id.* at 255.

to sustain the judgment for Ziedonis.[52]

However, the court also concluded that the damage award was excessive because it did not take into account what Ziedonis had earned while playing with two other orchestras following his discharge. The court divided on which party had the burden of proving whether those earnings actually reduced his losses. Judge White, who wrote the opinion on the breach issue, took the position that the burden of proving mitigation was on the Symphony, and he would not have deducted the earnings because it did not show Ziedonis' earnings actually reduced his loss.[53] Judge White recognized that Ziedonis had a duty to use reasonable efforts to avoid loss by securing employment elsewhere but felt that by testifying about his two other jobs Ziedonis did not assume the burden of showing whether his gross earnings exceeded his expenses. He also observed that the Symphony had not objected to a jury instruction recognizing Ziedonis' duty to mitigate damages by making reasonable efforts to obtain work elsewhere but which did not mention that the sums earned should be considered in assessing damages.[54]

Judge Buchanan, with Judge Hoffman concurring, took the position that a discharged employee must mitigate damages and must establish any expenses that would offset the earnings. He recognized that the Symphony had the burden of showing the availability of other employment,[55] even though the duty to mitigate is on the employee.[56] Ziedonis in effect satisfied the Symphony's obligation, but he did not establish any offsetting expenses, so the entire amount earned should be treated as mitigation.[57] Although imposing

---

[52]Consequently the denial of the Symphony's motion for a directed verdict under Trial Rule 50(A) was not in error. *See* Miller v. Griesel, 261 Ind. 604, 308 N.E.2d 701 (1974); Mamula v. Ford Motor Co., 150 Ind. App. 179, 275 N.E.2d 849 (1971).

[53]Both Judge White and Judge Buchanan found support in Hamilton v. Love, 152 Ind. 641, 643, 53 N.E. 181, 181 (1899); Hinchcliffe v. Koontz, 121 Ind. 422, 426, 23 N.E. 271, 272 (1890); and Pennsylvania Co. v. Dolan, 6 Ind. App. 109, 124, 32 N.E. 802, 807 (1892). They disagreed on the interpretation of Milhollen v. Adams, 66 Ind. App. 376, 115 N.E. 803 (1917). Judge Buchanan read it as recognizing that allowances should be made for the employee's expenses but not for imposing the burden of proof on the employer. 359 N.E.2d at 255-56.

[54]Ziedonis was upheld on the calculation of his prospective earnings for the summer and subsequent concert season. 359 N.E.2d at 256.

[55]*See* note 53 *supra.*

[56]359 N.E.2d at 257 (Buchanan & Hoffman, JJ., concurring). Mitigation limits the recovery by a discharged employee to what his or her actual loss might have been if employment had been sought, as an inducement to find new jobs. Inland Steel Co. v. Harris, 49 Ind. App. 157, 163, 95 N.E. 271, 273 (1911).

[57]In essence Judge Buchanan bifurcated the burden of proof on mitigation. The employer has to establish that the employee could find alternative work, and the employee must establish that any amounts so earned did not reduce the damages suf-

this burden on the employee seems somewhat inconsistent with the rule that the employer must show the availability of other employment or a lack of diligence in seeking other employment, it makes eminent sense because the employee and not the employer would know what expenses were incurred in obtaining other work.[58] Ziedonis was given the option of either a remittance of the entire amount earned or a new trial on the issue of damages, presumably with the burden of establishing any expenses to offset his earnings upon Ziedonis.

D. Respondeat Superior and Independent Contractors

Another interesting decision is *Burkett v. Crulo Trucking Co.*,[59] reversing a judgment of the Lawrence Circuit Court against Crulo Trucking in a wrongful death action. The primary issue on appeal was whether Crulo was entitled to a separate trial under Indiana Trial Rule 42(b)[60] because plaintiff, decedent's administrator, had entered into a loan receipt agreement with the estate of the truck driver, a co-defendant. The court recognized the propriety of loan receipt agreements[61] but concluded that the admission of the driver's negligence prejudiced Crulo's right to a fair trial even though the truck driver's estate could recover the amount of the loan exceeding a judgment against Crulo.[62]

---

fered by reason of the breach. 359 N.E.2d at 257 (Buchanan & Hoffman, JJ., concurring).

[58]The suggestion that the employees should have the burden of proof on either the mitigation of damages or the issue of avoidable consequences has not met with much success. *See* D. DOBBS, HANDBOOK ON THE LAW OF REMEDIES § 12.25, at 925 (1973) (citing C. MCCORMICK, HANDBOOK ON THE LAW OF DAMAGES § 159, at 628 (1935)). However, Judge Buchanan suggested that it is more reasonable to shift the burden when offsetting damages. In support of his position, he cited Annot., 22 A.L.R.3d 1047, 1071 (1968), *cited in* 359 N.E.2d at 257 (Buchanan, J., concurring), but his concurrent citation to MCCORMICK, *supra* §§ 58-60, does not relate to the issue and must be erroneous.

[59]355 N.E.2d 253 (Ind. Ct. App. 1976).

[60]It is appropriate for a court to order a separate trial under this rule in order to avoid prejudice.

[61]American Transp. Co. v. Central Ind. Ry., 255 Ind. 319, 264 N.E.2d 64 (1970); Northern Ind. Pub. Serv. Co. v. Otis, 145 Ind. App. 159, 250 N.E.2d 378 (1969). *See generally* 44 AM. JUR. 2d *Insurance* §§ 1824, 1855 (1969); Thornton & Wick, *Loan Receipt Agreements: Are They Loans, Settlements, Wagering Contracts, or Unholy Alliances?*, 43 INS. COUNSEL J. 226 (1976); McKay, *Loan Agreement: A Settlement Device that Deserves Close Scrutiny*, 10 VAL. L. REV. 231 (1976).

[62]The decision to grant separate trials is within the discretion of the trial court, Holt v. Granite City Steel Co., 22 F.R.D. 65 (E.D. Ill. 1957), but here there was an abuse of discretion because of the damning nature of the co-defendant's admissions. 355 N.E.2d at 260.

What is interesting for purposes of this survey is the court's conclusion that the trial court erred in refusing to give Crulo's tendered instruction on an independent contractor defense. In other words, Crulo claimed the driver was an independent contractor and not an employee, so the doctrine of respondeat superior, holding an employer liable for the torts of an employee, would be inapplicable.[63] Except for certain exceptions primarily based on policy grounds,[64] a person is not liable for the torts of an independent contractor who controls the means, methods, and manners of achieving the desired result.

The trial court apparently refused the instruction because plaintiff referred to the truck driver as an agent and not an employee, and the jury could be confused. The appellate court recognized that any problem was not with the instruction but with the semantics of agency law that blur the distinction between the terms "agent," "servant," and "employee" when considering the doctrine of respondeat superior.[65] Unfortunately, courts often fail to recognize that the term "agent" is an umbrella term covering employees and servants, which are basically synonymous, as well as independent contractors. In fact, to an agency purist, an agent is either a servant or a non-servant independent contractor.[66] Plaintiff viewed "agent" and "independent contractor" as mutually exclusive terms. This was clearly wrong, as the appellate court pointed out. The driver was no doubt Crulo's agent. He may have been a servant or employee, making Crulo liable for the driver's torts under the respondeat superior doctrine; or he may have been an independent contractor, in which case the doctrine did not apply.

Crulo had argued and presented evidence that the driver was an independent contractor so it was reversible error to refuse the instruction.[67] Crulo had the right to an instruction on its defense even

---

[63]*See* Prest-O-Lite Co. v. Skeel, 182 Ind. 593, 106 N.E. 365 (1914); Hale v. Peabody Coal Co., 343 N.E.2d 316 (Ind. Ct. App. 1976); Stewart v. Huff, 105 Ind. App. 447, 14 N.E.2d 322 (1938). *See generally* RESTATEMENT (SECOND) OF AGENCY §§ 2(3), 214, 220, 250-251 (1958); RESTATEMENT (SECOND) OF TORTS §§ 409-429 (1965); W. SEAVEY, *supra* note 1, §§ 6, 82, 91; W. PROSSER, HANDBOOK OF THE LAW OF TORTS § 71 (4th ed. 1971).

[64]For example, a person hiring an independent contractor can be held liable for the latter's torts if the work is intrinsically dangerous. Denneau v. Indiana & Mich. Elec. Co., 150 Ind. App. 615, 277 N.E.2d 8 (1971). *See generally* authorities cited note 63 *supra*.

[65]*See* W. SEAVEY, *supra* note 1, §§ 1, 6. The *Burkett* court even observed that Instruction 13.21 of the *Indiana Pattern Jury Instructions* was misleading. 355 N.E.2d at 261.

[66]W. SEAVEY, *supra* note 1, § 6, at 8. To compound matters, Professor Seavey recognizes that there can be independent contractors who are not agents and hence cannot bind the principal on contractual matters. *Id.* §§ 6, 11E.

[67]Jackman v. Montgomery, 320 N.E.2d 770 (Ind. Ct. App. 1974).

if plaintiff's case was founded on the erroneous premise that a showing of agency alone brings into play respondeat superior with no additional showing of servant or employee status.

E. Partnership Duties

A decision raising interesting partnership questions is *Pearson v. Hahn*[68] in which the First District Court of Appeals reversed and remanded a decision of the Morgan Circuit Court against a deceased partner's widow, who sought the appointment of a receiver for two partnerships and an accounting by the surviving partners. The two partnerships involved, Martinsville Leasing Company (MLC) and Martinsville Plaza Company (MPC), were organized to engage in real estate development. The partnership agreements were similar and contemplated the businesses would continue after the partnerships were dissolved. The MPC agreement was a better drafted document because it clearly provided for continuation on the death of a partner and provided two methods for valuing the interests, which the surviving partners could purchase.[69] The earlier MLC agreement was silent as to dissolution by death and did not provide for valuation of the partnership. It only gave the remaining partners the right to purchase the interest of a former partner.

The MPC continuation agreement obligated the partners wishing to continue the business to notify the former partner or his estate within sixty days after his disassociation from the firm. The problem in *Pearson* was that defendant Hahn was the deceased partner's executor; and even though the notice was given to the attorney for the estate, Hahn and the other surviving partner, McDaniel, in effect notified Hahn in his executory capacity of their intention to purchase the interest. Thus, one issue in the case was whether this notice complied with the provision in the MPC agreement.[70] The notice was specifically given to the MPC partnership, but it appears the parties and the court considered it applicable to the MLC partnership as well. Because of the similarity in the partnership businesses and agreements, and their close proximity in time, this is not an unreasonable result for reflecting the intentions of the three partners.

---

[68]352 N.E.2d 767 (Ind. Ct. App. 1976).

[69]The purchase price was to be the lower of the fair market value or the book value of the interest. *Id.* at 768. For a discussion of continuation agreements and the valuation of a deceased partner's interest, see A. BROMBERG, CRANE & BROMBERG ON PARTNERSHIP §§ 83A(c), 86(a), 90A (1968) [hereinafter cited as CRANE & BROMBERG]; M. VOLZ & A. BROMBERG, THE DRAFTING OF PARTNERSHIP AGREEMENTS 26-33, 97-103, 109-19 (6th ed. 1976).

[70]Sometime after the suit was filed, Hahn resigned as executor and was replaced by a bank as administrator d.b.n. 352 N.E.2d at 769.

Defendants had the assets of MPC appraised, as did the widow. Both appraisals were limited to one small parcel of land, transferred to MPC by defendant McDaniel, and showed liabilities exceeding assets. Myers' widow, now Mrs. Pearson, was dissatisfied and sought a financial accounting of both partnerships. The suit seeking the appointment of a receiver and an accounting pursuant to the Indiana Accounting by Surviving Partners Act[71] followed Hahn's failure to respond to Mrs. Pearson's request.

The trial court found that the title to all real estate, except for the one parcel, was held in the names of the partners and their wives as individuals. Accordingly, any interest Pearson had in those properties was as a surviving tenant by the entirety and not as an heir. Since the tract in MPC's name had a negative value, the trial court ordered the conveying of Myers' interest in MPC to the surviving partners without consideration. The trial judge obviously accepted the propriety of the notice.

The appellate court treated the case as having two issues: (1) whether it was proper for Hahn to give notice to himself; and (2) whether the notice made inapplicable the provisions of the Indiana Accounting by Surviving Partners Act and, although the court was not clear, the Indiana Uniform Partnership Act[72] pertaining to the dissolution of a partnership. The court said it would discuss the issues concurrently but seems to have ignored the second. However, it did reach a result congruent to the Indiana Uniform Partnership Act when it held that the inherent conflict of interest between Hahn as a surviving partner and Pearson as the beneficiary of the deceased partner's estate obligated him to fully disclose to her, upon request, all assets arguably belonging to the partnerships.[73]

Interestingly, the court based its decision on common law and ignored the Indiana Uniform Partnership Act. It relied primarily on cases discussed in an A.L.R. annotation and *Moorman v. Moorman.*[74] These cases establish that a surviving partner dealing with a deceased partner's estate has an affirmative obligation to fully inform the estate of the assets of the partnership.[75] As the Indiana Supreme Court recognized in *Moorman*, the heirs of a deceased partner are at a disadvantage in dealing with a surviving partner concerning the partnership.[76] Normally, disclosure would be to the

---

[71]IND. CODE §§ 23-4-3-1 to -8 (1976).

[72]*Id.* §§ 23-4-1-1 to -43.

[73]352 N.E.2d at 773-74.

[74]*Id.* at 772-73 (citing Annot., 45 A.L.R.2d 1009 (1956), and Moorman v. Moorman, 226 Ind. 192, 79 N.E.2d 112 (1948)).

[75]*See, e.g.*, Tennant v. Dunlop, 97 Va. 234, 33 S.E. 620 (1899), *cited in* Pearson v. Hahn, 352 N.E.2d at 772.

[76]226 Ind. at 196, 79 N.E.2d at 114. *Moorman*, decided before the Uniform Partnership Act was adopted, held that the appointment of a receiver under the Indiana

representative of the estate; but where, as here, a partner represents the estate, the disclosure has to be to the beneficiaries themselves.

The obligation to disclose upon demand has been codified in the Indiana Uniform Partnership Act. Section 20 compels partners to render on demand "true and full information of all things affecting the partnership to . . . the legal representative of any deceased partner."[77] Section 22 gives a partner the right to an accounting as to partnership affairs,[78] and this right accrues to the legal representative under section 43 when dissolution is caused by death.[79] Section 42 of the Act gives the estate of a deceased partner certain rights where the business is continued, subject to any continuation agreement.[80] The *Pearson* court did recognize that partners can make binding agreements to allow surviving partners to buy out a deceased partner's interests and stated that partners can serve as executors or administrators, even if Hahn's conduct here was improper.

Unfortunately, the court failed to give any guidance to the trial court as to what constitutes partnership property when it remanded the case for a complete audit of the assets of the two partnerships. The trial judge apparently thought that the legal title held by the partners and their wives was controlling and that the various business properties involved, except for the one parcel, were not partnership property. What is not clear is whether he considered the possibility that the properties were thought to be partnership property by the partners, even though title was in their names as individuals as a carry-over from the common law rule that a partnership was not an entity capable of holding title.[81] They might have followed the traditional partnership practice, even though section 8 of the Indiana Uniform Partnership Act[82] changes the common law.

Accounting by Surviving Partners Act was within the discretion of the trial court. *Id.* at 195-96, 79 N.E.2d at 114.

[77]IND. CODE § 23-4-1-20 (1976).

[78]*Id.* § 23-4-1-22.

[79]*Id.* § 23-4-1-43. This right exists subject to any agreement to the contrary. For a discussion of the right to an accounting under the Uniform Partnership Act, see CRANE & BROMBERG, *supra* note 69, § 72.

[80]IND. CODE § 23-4-1-42 (1976). *See generally* CRANE & BROMBERG, *supra* note 69, §§ 86, 90A.

[81]*See, e.g.*, Adams v. Blumenshine, 27 N.M. 643, 204 P. 66 (1922). *See generally* Powell, *Land Capacity of Natural Persons as Unincorporated Groups*, 49 COLUM. L. REV. 297, 314-15 (1949).

[82]IND. CODE § 23-4-1-8 (1976). The Uniform Partnership Act did not entirely reject the aggregate theory of partnerships, CRANE & BROMBERG, *supra* note 69, § 3, but it clearly adopted the entity theory with respect to real property in § 8(3). CRANE & BROMBERG, *supra* note 69, § 38.

In effect, the statute recognizes the partnership as an entity apart from the partners for holding title. The question of whether the real estate was partnership property or the individual property of the partners is one of intent.[83] The fact that title was in the individual names does not preclude a finding that it is partnership property and vice versa,[84] although the interest of the partnership is equitable and the creditors of the legal titleholders would have priority.[85]

The appellate court could not be expected to determine the partners' intent, but the trial court should have been advised to consider the possibility that more than the small tract was partnership property. The evidence, at least as it appears in the opinion, is not conclusive. For example, McDaniel bought the property before the partnership was formed and kept the balance after conveying the small tract. This would be evidence that the property was McDaniel's individual property, based on section 8 of the Indiana Uniform Partnership Act. Title to the real estate managed by MLC was in their individual names, the financing was obtained in their names, and they signed leases as lessors. This would tend to support the conclusion that MLC did not have any property. However, lending sources might have insisted on their borrowing as individuals, even though partners are personally liable for partnership debts.[86] However, they did form partnerships pursuant to written agreements and so contemplated conducting business as partners. It would not be illogical for them to consider the property as partnership property regardless of who held title.

In fact, it is not clear what the appellate court expected of the trial court. If it merely wanted the disclosure of partnership property, or arguably partnership property, it was compelling an exercise in futility. All information is now known. Perhaps it was direc-

---

[83]*See* Roberts v. McCarty, 9 Ind. 16 (1857). *See generally* CRANE & BROMBERG, *supra* note 69, § 38.

[84]However, courts are less inclined to find property held in the name of the partnership to be individual property because it presumably has been used in the firm's business, CRANE & BROMBERG, *supra* note 69, § 37, but mere use in the business might not be enough to support a finding that it was to be partnership property. *See* Ellis v. Mihelis, 60 Cal. 2d 206, 384 P.2d 7, 32 Cal. Rptr. 415 (1963).

[85]*See* Roy E. Hays & Co. v. Pierson, 32 Wyo. 416, 234 P. 494 (1925). *See generally* CRANE & BROMBERG, *supra* note 69, §§ 37(d), 38.

[86]Conceivably the lenders desired to be personal as well as partnership creditors in order to enjoy a higher priority in the event of the bankruptcy of the firm and the partners. *See* Rodgers v. Meranda, 7 Ohio St. 180 (1857); IND. CODE § 23-4-1-40 (1976). *See generally* CRANE & BROMBERG, *supra* note 69, §§ 90, 91-94. It is interesting to note that the Annotation relied on by the *Pearson* court on the first issue discussed situations where property owned by the individuals before the partnership was formed became an asset of the partnership. Annot., 45 A.L.R.2d 1009 (1956).

ting the trial court to treat the balance of the tract from which the parcel was conveyed as MPC property. This puts the trial court in a dilemma. It might very well have considered the issue and simply rejected the assertion that the property belonged to the partnership.

F. Statutory Developments

Although the 1977 session of the Indiana General Assembly produced several noteworthy statutory developments,[87] probably the most significant development occurred in *Great Western United Corp. v. Kidwell*,[88] where a federal district court declared the Idaho Corporate Takeover Act[89] unconstitutional. The ruling, if upheld on appeal, could affect all state laws regulating corporate tender offers, including the Indiana Business Takeover Act passed in 1975.[90]

The rationale of *Great Western* was twofold. The first ground was that the Idaho statute conflicted with and frustrated the clear purpose of the Williams Act amendments to the Securities Exchange Act of 1934,[91] requiring certain disclosures of companies making tender offers. The Williams Act was intended to protect shareholders of target companies without unduly impeding cash takeover bids, and the court concluded the Idaho statute destroyed the careful balance between the interests of the offeror and those of the management of the target company. Judge Hill emphasized that the Idaho statute primarily benefited managements of target companies by permitting lengthy hearing procedures for tender offers opposed

---

[87]Other enactments worth noting are IND. CODE § 23-1-10-2 (1976), relating to the corporate director's liability, amended to conform more closely to the language of 2 ABA-ALI MODEL BUS. CORP. ACT ANN. § 48 (2d ed. 1971); IND. CODE §§ 23-1-11-4, -8, -9 (Supp. 1977), amended to permit filing of certified copies of corporate documents by foreign corporations qualified to do business in Indiana; *id.* §§ 6-2-1-30, 22-4-32-22, amended to require that notice of a pending corporate dissolution need only be given to the Indiana Department of Revenue and the Employment Security Division when incorporators are dissolving a corporation that has not commenced business; *id.* § 23-3-2-2, amended to afford the surviving corporation in a merger a fee credit, based on the fees the nonsurviving corporation had paid on its authorized shares; and *id.* § 23-2-1-1(k), amended to exclude from the definition of "security" certain contracts or trusts that comply with specified provisions of the Federal Internal Revenue Code.

[88][1977] FED. SEC. L. REP. (CCH) ¶ 96,187 (N.D. Tex. 1977).

[89]5A IDAHO CODE §§ 13-1501 to -1513 (Supp. 1977).

[90]IND. CODE §§ 23-2-3-1 to -12 (1976). For a discussion of this Act, see Galanti, *Business Associations, 1975 Survey of Recent Developments in Indiana Law*, 9 IND. L. REV. 33, 52-59 (1975); Note, *The Indiana Business Takeover Act*, 51 IND. L.J. 1051 (1976). For a discussion of tender offers in general, see authorities cited in Galanti, *supra*, at 53 nn.92 & 94, and Note, *supra*, at 1053 n.5.

[91]15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1970).

by management.[92] These statutes definitely can be detrimental to shareholders by discouraging tender offers or by reducing the tender price.[93] Although federal law has not and cannot totally occupy the field of securities regulation,[94] federal law had to prevail here because the purposes were in opposition. The court also held the statute unconstitutional under the Commerce Clause.[95] The statute had a substantial effect on interstate commerce and did not accomplish a legitimate "local purpose." Certainly compliance with many potentially conflicting state statutes would have such an effect, even if compliance with one did not.

It is, of course, too early to tell if Judge Hill's ruling will be upheld on appeal, but it is significant that the Supreme Court emphasized the "balance" of the Williams Act in *Piper v. Chris-Craft Industries, Inc.*[96] Certainly little support for the state acts can be expected from the SEC because its attitude towards business takeover statutes is hostile.[97] Without doubt, *Great Western* adds a new dimension to the already mind-boggling tender offer game.

The most significant actual legislative development was the adoption of section 35 of the Model Business Corporation Act,[98] which defines the duties and standards of care of corporate directors. Section 23-1-2-11(a) formerly provided, in part, that "the business of every corporation shall be managed by a board of directors." This is the so-called "corporate norm" where directors of a corporation are expected to manage its affairs. It is also the concept

---

[92]The Indiana Act is similar. IND. CODE § 23-2-3-1(i)(5) (1976) excludes tender offers that have been approved by the board of directors of the target company from the definition of offers subject to the Indiana Securities Act.

[93]In the tender offer involved in *Great Western*, the company reduced its bid for Sunshine Mining by $1 because of management's opposition. *See* BUS. WEEK, Oct. 3, 1977, at 40. The bid was eventually raised when Great Western and Sunshine Mining reached an accord. Wall St. J., Oct. 6, 1977, at 16, col. 3. Opposition by management backfired even more when the Gerber Products Co. was sued for $100 million after its opposition caused an offeror to reduce its bid by $3. The bid was ultimately dropped. BUS. WEEK, Aug. 29, 1977, at 25; *id.*, Oct. 3, 1977, at 50.

[94]Section 18 of the 1933 Act, 15 U.S.C. § 77r (1970), and § 28 of the 1934 Act, 15 U.S.C. § 78bb(a) (1970), specifically allow for state regulation of securities. SEC v. National Sec. Inc., 393 U.S. 453, 461 (1969). The terms of § 28 permit state regulation only to the extent it does not conflict with the federal regulatory scheme. 15 U.S.C. § 78bb(a) (1970).

[95]U.S. CONST. art. I, § 8, cl. 3.

[96]97 S. Ct. 926 (1977).

[97]Wall St. J., Aug. 3, 1977, at 1, col. 1. When the SEC recently amended schedule 14D-1, 2 FED. SEC. L. REP. ¶ 24,284C (1977) (to be codified in 17 C.F.R. § 240.14d-100), and rule 14d-1, 2 FED. SEC. L. REP. ¶ 24,281A (1977) (to be codified in 17 C.F.R. § 240.14d-1), it emphasized that efforts to benefit shareholders in the context of tender offers should not unnecessarily tip the balance in favor of either side.

[98]1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 35 (2d ed. 1971).

that has plagued the principals of closely held corporations who wished to operate an enterprise more as a chartered partnership than as a publicly held corporation like General Motors.[99] Unfortunately, other jurisdictions have construed the model act's statutory charge to restrict the rights of owners of a corporation to agree among themselves as to how they will vote and otherwise manage its affairs.[100] However, some recent cases recognize the *sui generis* nature of close corporations and have allowed more flexibility in their structuring.[101]

Section 23-1-2-11(a) now reads in pertinent part: "[C]orporate powers shall be exercised by or under the authority of, and the business and affairs of a corporation shall be managed under the direction of, a board of directors except as may be otherwise provided in this article or *the articles of incorporation.*"[102] Thus, the legislature has sanctioned arrangements for managing close corporations, provided they are contained in the articles of incorporation. In fact, shareholders can eliminate the board of directors and manage the corporation's affairs directly.[103] It would seem, then, that Indiana has "modernized" its General Corporation Act. By eliminating the old inflexible "norm," it now reflects a common practice for closely held corporations "in the real world."[104]

However, it is also possible to characterize the new provision as evidence that Indiana has joined what Justice Brandeis characterized in his dissent in *Liggett v. Lee*[105] as a "race of the lax." The

---

[99]For an interesting discourse on the typology of corporations, see A. CONARD, *supra* note 36, at 152-74.

[100]*See, e.g.*, Clark v. Dodge, 269 N.Y. 410, 199 N.E. 641 (1936); McQuade v. Stoneham, 263 N.Y. 323, 189 N.E. 234 (1934). *See generally* Delaney, *The Corporate Director: Can His Hands Be Tied in Advance*, 50 COLUM. L. REV. 52 (1950).

[101]*See, e.g.*, Galler v. Galler, 32 Ill. 2d 16, 203 N.E.2d 577 (1965); Donahue v. Rodd Electrotype Co., 328 N.E.2d 505 (Mass. 1975). *But see* Somers v. AAA Temporary Serv., Inc., 5 Ill. App. 3d 931, 934, 284 N.E.2d 462, 465 (1972), which construed *Galler* as permitting slight deviations from corporate norms, but forbidding shareholder agreements that are in direct contravention of the statute.

[102]IND. CODE § 23-1-2-11(a) (Supp. 1977) (emphasis added). Attempting to accomplish the goal of flexibility by means of bylaws, unless specifically authorized by the Indiana General Corporation Act, appears risky, because the Act specifies that such matters must be accomplished in the articles of incorporation. *See In re* William Faehndrich, Inc., 2 N.Y.2d 468, 141 N.E.2d 597 (1957).

[103]IND. CODE § 23-1-2-11(a)(1) provides that persons acting in lieu of a board of directors shall have the powers and duties of directors. *See generally* 1 ABA-ALI MODEL BUS. CORP. ACT. ANN. § 35, ¶ 2, at 755-59 (2d ed. 1971).

[104]One potential problem with a custom-tailored flexible corporation is that it increases the risk that a court might disregard the corporate fiction and impose personal liability on the shareholders.

[105]288 U.S. 517, 541-79 (1933). If the legislature had been interested only in aiding Indiana close corporations, it could have adopted the language of § 35 as liberalized in 1969, 1 ABA-ALI MODEL BUS. CORP. ACT. ANN. § 35, at 755 (2d ed. 1971).

reference here is to section 23-1-2-11(a)(2), which affirmatively states that the duty of care of a director is to serve "in good faith, in a manner he reasonably believes to be in the best interests of the corporation, and with such care as an ordinarily prudent person in a like position would use under similar circumstances."

According to the comments on the most recent amendments to section 35 of the Model Business Corporation Act, this standard "reflects the good faith concept embodied in the so-called 'business judgment rule.' "[106] These comments recognize that the traditional corporate norm could require outside directors who are not otherwise actively involved with the corporation to become involved in the detailed administration of its affairs. The comments observe that this expectation can "no longer be viewed to be reasonable. Indeed, such involvement is clearly neither practical nor feasible insofar as today's complex corporation, other than perhaps the closely-held corporation, is concerned."[107] To the contrary, when reports of corporate misdeeds are still making news, it is inappropriate for the legislature to lower the duty of outside directors who might be the only people able to police management.

The amendment has broadened the right to rely on reports and documents furnished by corporate personnel, professionals, or other committees of the board of directors.[108] If a director reasonably believes in the reliability and competence of the persons giving such reports, there is no liability for being or having been a director. The provision does state that a director "shall not be considered to be acting in good faith if he has knowledge concerning the matter in question that would cause such reliance to be unwarranted,"[109] but this could well be an invitation for directors *not* to examine operations in case some questionable conduct might be disclosed.

In an article on director reliance on counsel, the model act's authors favorably note that the revision of section 35

> constitutes the most comprehensive definition of a director's right of reliance yet attempted. In sweeping language it now makes the right of reliance available not only for legal questions but also for factual information covering virtually

---

[106]*See* the report that proposed the current language of § 35. Committee on Corporate Laws, *Changes in the Model Business Corporation Act*, 29 BUS. LAW. 947, 951 (1974).

[107]*Id.* at 952.

[108]Ch. 275, § 41, 1967 Ind. Acts 866, 867-68 (formerly codified at IND. CODE § 23-1-10-2(e) (1976)), allowed reliance on financial statements as a defense to three described violations involving pay outs of corporate funds. This provision was deleted in the current version of IND. CODE § 23-1-10-2 (1976) and superseded by the far broader language of *id.* § 23-1-2-11(a) (Supp. 1977).

[109]IND. CODE § 23-1-2-11(a)(2) (Supp. 1977).

> every aspect of corporate activity for which the board of directors may be responsible.[110]

They recognize the trend in the revision of corporation codes towards a general "enabling" philosophy, but argue:

> Nonetheless, granting management the right to rely on counsel and others does not reduce management's traditional accountability. The general requirements of good faith and due care inherent in the statutory provisions are sufficient assurance of this. Instead, the salutory development merely recognizes the facts of life in the operation of a complex corporate enterprise.[111]

This is possibly true, but a court might not diligently scrutinize the conduct of a director when faced with statutory language as broad as that of section 23-1-2-11(a)(2). This does not mean shareholders' interests will be ignored, but they may be given short shrift.[112] Considering the recent trend of the Supreme Court in interpreting the federal securities laws,[113] shareholders of publicly held corporations have precious little protection. Perhaps that is why the individual investor has left the market.

A second significant change to the General Corporation Act was the adoption of new section 23-3-4-1.6 governing reinstatement of corporations whose terms of existence have expired or whose articles have been revoked for failing to file annual reports.[114] The statute, which applies to not-for-profit corporations as well, now provides for the reinstatement of such corporations upon application to the Secretary of State and the satisfaction of certain specified requirements. The amendment provides that the "corporation shall be

---

[110]Hawes & Sherrard, *Model Act Section 35 — New Vigor for the Defense of Reliance on Counsel*, 32 BUS. LAW. 119, 119 (1976). *See also Report of the Committee on Corporate Law Departments On Corporate Director's Guidebook*, 32 BUS. LAW. 1841 (1977).

[111]Hawes & Sherrard, *supra* note 110, at 145-46.

[112]As Hawes & Sherrard point out, proof of reliance on counsel should be permitted where good faith is an element of a director's duty of loyalty or where the duty is measured under the business judgment rule. Hawes & Sherrard, *supra* note 110, at 136.

[113]*See, e.g.*, Santa Fe Indus., Inc. v. Green, 97 S. Ct. 1292 (1977); Piper v. Chris-Craft Indus., Inc., 97 S. Ct. 926 (1977); TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438 (1976); Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976); Rondeau v. Mosinee Paper Corp., 422 U.S. 49 (1975); United Hous. Foundation, Inc. v. Forman, 421 U.S. 837 (1975); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975).

[114]IND. CODE § 23-3-4-1.6 (Supp. 1977). This section replaced IND. CODE § 23-3-4-1.5 (1976).

deemed to have continuously existed since the date"[115] of its termination or revocation, thus eliminating any questions about the validity of corporate acts during the hiatus. A conforming amendment was made to section 23-1-7-4 to eliminate the prior procedure of reinstating a corporation whose existence has terminated pursuant to its articles by amending its articles to extend its duration.

There is no quarrel with a procedure streamlining the process of reinstating corporations that have failed to file annual reports, since it is a common occurrence. The only question that this author has is that the Act does not indicate the duration of the reinstated corporation. There is no problem for a corporation with a perpetual duration whose articles were revoked, but there is for a corporation whose existence was limited to, for example, five years. Is its duration perpetual? The statute is silent and should be clarified. However, a strong argument can be made that by deleting the language in section 23-1-7-4 concerning amending the articles, the legislature has demonstrated an intent that the newly reinstated corporation would have perpetual duration. Those responsible for reinstating such a corporation could, of course, amend the articles pursuant to the regular amendment process[116] if they wished to limit its duration.

IV. Civil Procedure and Jurisdiction

*William F. Harvey**

A. Jurisdiction and Service of Process

1. Quasi in Rem Jurisdiction.—A fitting introduction to this section is the penetrating opinion of the United States Supreme

---

[115]IND. CODE § 23-3-4-1.6(c) (Supp. 1977). The courts are divided as to whether a corporation with a revoked charter had de facto status during the period of revocation. *Compare* Spector v. Hart, 139 So. 2d 923 (Fla. Ct. App. 1962) *with* Moore v. Rommel, 233 Ark. 989, 350 S.W.2d 190 (1961). A statutory provision granting de facto status has been declared unconstitutional. *See* Gano v. Filter-Aid Co., 414 S.W.2d 480 (Tex. Ct. App. 1967). An interesting question is whether the new provision would make the penalty provision of IND. CODE § 23-1-10-5(a) (1976) inapplicable where the business was conducted "knowingly and willfully and with intent to defraud" during the period the articles were revoked.

[116]IND. CODE § 23-1-4-1 (1976).

*Dean, Indiana University School of Law—Indianapolis. A.B., University of Missouri, 1954; J.D., Georgetown University, 1959; LL.M., Georgetown University, 1961.

The author wishes to extend appreciation to Gary Price for his assistance in the preparation of this discussion.