FIDUCIARY FOLLY LEADS TO FIASCO: THE CASE OF CONSOLIDATED PIPELINE AND EQUIPMENT CORPORATION (CPEC)

Laura Sullivan, Sam Houston State University
Robert Stretcher, Sam Houston State University
Joey Robertson, Sam Houston State University

CASE DESCRIPTION

The primary subject matter of this case involves the agency relationship between Steve Shelton, a fiduciary (the accountant) and his client and friend, Paul Jameson. Paul's son, Jim Jameson, has brought a lawsuit against Paul and Steve, because of his dissatisfaction with the recent sale of his property. Secondary issues include gratuitous agent issues, agent liability, and confidential relationship liability. The case has a difficulty level appropriate for undergraduate Business Law or Accounting courses. The case can be taught in 1-2 class hours, depending on the desired detail level for the discussion. It should take approximately one hour of outside preparation by students.

CASE SYNOPSIS

Jim Jameson, former president of CPEC Pipeline and Equipment Corporation (CPEC) has brought an action against his father and his father's accountant. His father, Paul, is the 100% owner of CPEC, and has arranged the sale of the business to a third party for $65 million. One year earlier Jim's employment as CPEC president had been terminated for alleged mismanagement. After Jim's termination Paul resumed duties as president of CPEC during the structuring of the sale of the business.

Following his termination, but prior to the sale of CPEC Jim was paid $3.8 million by CPEC (at his father's direction) for a parcel of land Paul had essentially given to Jim five years earlier. The fair market value of the land at the time of this transaction was about $1.2 million. The purpose of the purchase in excess of the actual value was to transfer an "inheritance" of sorts to Jim while avoiding the tax consequences of a gift tax. The burden of the tax was then Jim's, a further irritating aspect of the transaction.

Following the sale of CPEC Jim now claims the $3.8 million he received for the land did not represent an amount acceptable for an inheritance. Jim also felt that the land was of substantially higher value to the firm, and that the sale of the business was somehow tied to the inclusion of the *land. His conclusion was that the land is actually worth substantially more than the $3.8 million he was paid.*

Interestingly, if Jim's conclusion is correct, then the amount paid does not exceed the value of the land, and there would be less suspicion of a fraudulent avoidance of taxes by Paul. If Jim is wrong in his conclusion, Paul and the firm would be suspected of fraudulent avoidance of taxes, but would have greater wealth to offer the firm's purchaser. The main question addressed by the case is whether Steve, the accountant for CPEC, owes a fiduciary duty to Jim in connection with this land sale.

BACKGROUND

The Jameson family lived in Dallas, Texas. Paul Jameson worked as a welder. Paul and his son Jim Jameson have always had a volatile relationship. Paul divorced Jim's mother when Jim was very young. Jim Jameson was raised by his mother in Oregon. Shortly before high school the family moved back to Dallas, Texas. While his son lived in Oregon, Paul Jameson built a successful business from the ground up. Paul had spent years growing and developing product lines and customers. The work was time consuming and Paul had little time for anything but work.

After Jim's arrival back in Dallas, his father tried to mend their broken relationship. After high school graduation Paul offered Jim a job a CPEC. Jim began his career as a floor sweeper. It was Paul's dream that Jim would start at the bottom and work his way up the ladder. Someday he hoped that Jim would take over the company. Through time Jim advanced in the company. He became vice president of marketing and client development. Later, Paul had a health problem that required him to take time away from CPEC. Paul turned CPEC over to Jim, making Jim president.

For a brief period all seemed well. Paul regained his health but allowed Jim to continue as president. However, one day Paul went to lunch with a couple of employees and serious concerns regarding Jim's performance arose. Paul decided to investigate the situation. He pulled previous month's financial statements. He reviewed payments made to vendors. He realized that there were several payments to companies he had never heard of before. After further investigation he realized that the companies did not exist and that the checks were in fact cashed by Jim Jameson. At this point Paul had a very serious decision to make, he had to terminate his own son's employment with CPEC.

After Jim's termination, Paul decided to sell CPEC. At his advanced age he no longer wanted the stress of running a large company. He began to look for buyers. Paul knew that he would need assistance with the sale of CPEC, so he hired his longtime accountant and friend, Steve Shelton. Steve would assist in the accounting work and serve as a liaison between the attorneys and Paul.

As negotiations began between several potential buyers Steve coordinated and structured the deal. He continued to pursue the most advantageous deal for his clients, Paul and CPEC. After almost a year of negotiations the final deal was hammered out with the internationally known

Halliburg, Inc. It was an excellent deal for Paul. Steve constructed a primarily cash deal. As CPEC's sole shareholder, Paul stood to net approximately sixty-five million dollars.

There was one final issue that needed to be resolved. Originally there were two parcels of land that CPEC owned. Parcel A was where the original facility was located. This four acre parcel has a small three thousand square foot warehouse. Parcel B was the main parcel, which included the current seventy thousand square foot office, warehouse and welding facility. At the time, Parcel A was not being used by CPEC. Parcel A was owned by CPEC. However, Paul essentially gave the parcel to Jim when he sold it to him for one dollar. As part of the original deal CPEC was supposed to include Parcel A with its sale. Paul asked Steve to talk to Jim about selling his parcel.

Steve contacted Jim regarding the sale of Parcel A. Jim was aware that Paul was in the process of selling CPEC. Jim informed Steve that he would sell, if the price was right. Through several conversations with Jim, Steve realized that Jim was trying to extort the situation. Steve informed Paul and Halliburg of the situation. Halliburg stated that owning Parcel A was not a deal breaker. It was at this point that Jim ceased to have any leverage in the sale of CPEC.

Steve had an idea. The relationship between father and son had degenerated to the point that they were almost completely estranged. Steve did not want to see Paul completely end his relationship with Jim. Steve contacted Paul regarding giving Jim an inheritance through the sale of Parcel A. If Paul purchased Parcel A, it would not be considered a gift and Jim would have to pay any tax on the profit. Paul did enjoy his relationship with his grandchildren. He believed that if he could somehow appease Jim maybe their relationship could be salvaged. Paul authorized Steve to begin negotiations with Jim.

Steve contacted Jim regarding the purchase of Parcel A. Jim appeared agreeable to selling the land. Conversations continued and a deal came together. Steve contacted an attorney to draft the sale documents. Steve calculated that even in the best real estate marked that the value of Parcel A was worth $1.2 million. He realized that the value of the land could not be too far from the sale price or the Internal Revenue Service could potentially have an issue with the transaction. The other issue that Steve had to contend with was Jim's greed. Steve believed that Jim saw this as his one last opportunity to make some money off his father.

Jim was holding fast to the belief that he could make ten million dollars from the sale of Parcel A. This was considerably more than Paul was willing to pay. Steve had a couple of very intense conversations with Jim. The conversations centered on the fact that Paul no longer required Parcel A to complete the sale of CPEC. If Jim was to make any money from the sale he needed to be reasonable. Finally, after months of negotiations the deal was finalized. Jim walked away with a check for $3.8 million from the sale of Parcel A. Jim made more than three times the fair market value of Parcel A.

After the sale of CPEC and Parcel A were completed, Jim and Paul had a major disagreement. Jim was very angry and felt that he could have made more money from his father. He sought the counsel of an attorney. He later filed suit against Paul and Steve. The suit against Paul was severed from Steve's suit. Jim lost his suit against his father. However, it seemed that Jim was enjoying hurting anyone associated with his father.

Jim claimed in his lawsuit that Steve was his agent with relation to the sale of Parcel A. Thus, Steve owed to him all fiduciary duties that an agent owes to his master. Further, he claimed that there was a confidential relationship between the parties. The final claim centers on a charge of fraud relating to a fiduciary duty Jim believes he was owed by Steve.

THE TASK

Assume that you are an assistant to Steve's attorney. Answer the following questions in detail.

1. What duty does an accountant owe his client?

2. What is an agency relationship?

    a. How does an agency relationship begin?

    b. Who bears the burden to prove that an agency relationship existed?

    c. What liability does that pose to the agent?

3. What is a fiduciary duty?

    a. When does one owe a fiduciary duty?

    b. Can one owe a fiduciary duty even if one is not paid for his or her services?

    c. If "yes" what is the name for this duty?

4. Did Jim appoint Steve as his agent?

5. If Steve was, in fact, Jim's agent – what type of agent was he?

6. If Steve was not Jim's agent, was there any relationship between the accountant and son at all?

7. What is fraud?

8. Is there any evidence of fraud on Jim's part?

9. Is there any evidence of fraud on Paul's part?

10. If the sale of the parcel of land from Jim to CPEC for 3 times its actual value is fraud, who is liable?

11. If Paul relied on Steve's expertise in setting up the sale of the land, does Paul have any recourse against Steve?

12. Is it possible that a court could find there was no agency relationship in the sale of land in excess of its true value?