IN THE COURT OF APPEALS OF TENNESSEE, WESTERN SECTION AT JACKSON

H. PATRICK HEFFERNAN,	)	Shelby County Chancery Court No. 96510-3 R.D.
Plaintiff/Appellee.	)	
VS.	)	C. A. No. 02A01-9504-CH-00080
HEFFERNAN, BALLINGER, POUNDS, AND YARBROUGH, INC. and LYNN H. BALLINGER, CHARLES O. POUNDS and ROBERT A. YARBROUGH,	)	
Defendant/Appellant.	)	

FILED

September 11, 1996

Cecil Crowson, Jr.
Appellate Court Clerk

From the Chancery Court of Shelby County at Memphis.
Honorable D. J. Alissandratos, Chancellor

Carl H. Langschmidt, Jr.,
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OPINION FILED:

REVERSED AND REMANDED

FARMER, J.

HIGHERS, J. : (Concurs)
LILLARD, J. : (Concurs)

This litigation was initiated by Appellee, H. Patrick Heffernan, against Ballinger, Pounds and Yarbrough, Inc., formerly Heffernan, Ballinger, Pounds and Yarbrough, Inc.,[1] and Glen H. Ballinger, Charles O. Pounds and Robert A. Yarbrough, to recover the earned commissions and share of corporate profits allegedly due him. The trial court referred the matter to the clerk and master who, after a hearing, determined that Heffernan was entitled to compensation in the amount of $44,242.92.[2] The master's report was affirmed by the chancellor who entered judgment for Heffernan accordingly.[3] The Corporation has appealed, presenting the following issues for our review:

> 1. Whether the Chancellor and the Clerk and Master erred in concluding that Heffernan did not owe Heffernan, Ballinger, Pounds and Yarbrough, Inc. $15,620.01 for commissions he placed in his own agency for his personal benefit while he was still an employee of Heffernan, Ballinger, Pounds and Yarbrough, Inc.
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> 2. Whether the Chancellor and Clerk and Master erred in holding that the corporation should have given Heffernan a partial distribution of profit of $22,680.
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> 3. Whether the Chancellor and the Clerk and Master erred in concluding that the plaintiff was entitled to receive commissions which the corporation owed him for the fiscal year ending May 31, 1987.
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> 4. Whether the Chancellor and Clerk and Master erred in concluding that Heffernan did not have to repay his loan of $15,000 to the corporation.

For reasons hereinafter discussed, we reverse the judgment of the trial court.

The proof establishes that the Corporation was formed in October 1979 to operate as an insurance agency. Heffernan and the individually named defendants were its officers and

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[1]For answer, it was asserted that the proper corporate defendant "is Heffernan, Ballinger, Pounds and Yarbrough, Inc. and it has not changed its name."

[2]After filing of the master's report, Heffernan amended his complaint to allege, ***inter alia***, conspiracy and wrongful conversion against the individual defendants.

[3]The judgment was rendered as against "Heffernan, Ballinger, Pounds and Yarbrough, Inc." and made final pursuant to Rule 54.02 T.R.C.P. By separate order, the trial court referred the matter back to the clerk and master for further hearing to determine the liability, if any, of "Ballinger, Pounds and Yarbrough, Inc. and Lynn H. Ballinger, Charles O. Pounds and Robert A. Yarbrough." The suit as to Ballinger, Pounds and Yarbrough, Inc. was subsequently nonsuited. For our purposes, the only appellant in this action is Heffernan, Ballinger, Pounds and Yarbrough, Inc., which we refer to throughout this opinion as "Appellant" or "the Corporation."

directors, with Heffernan serving as president. Each owned 25% of the corporate stock. Each had been insurance agents prior thereto and had developed their own "book of business." They did not execute a no-compete agreement. The Corporation operated under a fiscal year ending May 31.

Problems arose among the four when all did not agree to Heffernan's suggestion that they enter into a buy-sell agreement. The three other stockholders, however, offered to buy out Heffernan in a February 1987 meeting with him. According to Heffernan, he informed the others at this meeting that he was unsure of his future plans regarding the company and would let them know his decision on April 1. The parties agree that sometime around April 1, Heffernan made known his intentions to leave the business. He testified: "[o]n April first I met [with] them and I said . . . I would not want to continue in business with you . . . . I will take my business and you keep your business." Mr. Pounds testified that he recalled Heffernan announcing that "he was going to leave in several months."

Heffernan testified that the stockholders met again in May and that "it was laid out very intelligently how I would take my accounts." He said that prior to the completion of his proposal as to how they would "split," Pounds strongly suggested that he "get out right now." According to Heffernan, he replied, "I have no intention of getting out. I own 25 percent of this agency and 25 percent of . . . the building[4] and my book of business. And when I get my deal set up and we get through the end of this month, then I will depart." He continued, "my goal [was] to move over at the end of May and all the business up to that date was being placed with [the Corporation]."

Heffernan's plans did not materialize, however, as the record establishes that he physically vacated the premises no later than May 7. Mr. Ballinger testified that on April 13, 1987, he first learned that Heffernan was renewing business in his new agency while continuing to work for the Corporation. He and Yarbrough confronted Heffernan who, according to Ballinger, denied the allegations. According to Heffernan, he admitted that he was "writing some business with [his]

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[4]The record establishes that the four, as partners, purchased the building occupied by the Corporation.

new agency."[5] Ballinger and Pounds requested that he leave, prompting his early departure. Heffernan testified that prior to the conversation with Ballinger and Yarbrough, he believed that he had effectively ended his relationship with and his obligations to the Corporation and further believed that he was entitled to stay on the premises because of his ownership of part of the building and agency. Heffernan testified that his last paycheck from Appellant was for the month of April 1987.

The board of directors did not declare Heffernan a bonus in 1987, according to Pounds, "because at the time we did it he left before the year was out and if he would have stayed, we would have looked at it differently, but in the meantime he was diverting business away from our shop two months before he was to leave. And a lot of that business expired April one and affected the bottom line of the company, and I couldn't see giving a bonus in that kind of situation."

The record includes a letter dated April 8, 1987 from Pounds to an insurance company represented by the Corporation informing the latter of Heffernan's "decision to leave" and requesting that any future contacts regarding the Corporation be directed to either Pounds, Yarbrough or Ballinger. It was Pounds' testimony that he wrote similar letters to all companies doing business with the Corporation. Pounds further testified that at that point in time he had no idea that Heffernan would be taking business in a new agency before the end of the fiscal year. The corporate charter for Heffernan's new agency, H. P. Heffernan Insurance, Inc. was signed by him on April 14, 1987 and filed by the State of Tennessee on the following day. A letter dated April 1, 1987 from a customer of the Corporation to CNA Insurance identifies its "agent of record" as Heffernan Insurance.

On cross-examination, Heffernan admitted that he renewed certain policies handled by the Corporation through his new agency. He insisted, however, that such policies would never have been issued without Pounds' approval. When questioned further, "[b]ut you didn't tell [Pounds] you were soliciting this to go into another agency; right?", Heffernan replied, "[n]ot on April first, no . . . . I told him I was leaving and he would have been awfully naive if he thought

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[5]When questioned about this conversation on cross-examination, Heffernan stated that he did not recall admitting or denying the allegation.

everything that came after that date was going back into their pockets." Heffernan explained that the policies were originally ordered April 1 for the Corporation and the order from his new agency did not take place until sometime in May, with the policies actually being issued in June. The policies, however, were "back dated" to April 1 for continuous coverage. He was questioned:

> Q. You are totally satisfied they were covered though?
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> A. Absolutely, April first.
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> Q. Through what agency were they covered?
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> A. Through my agency.
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> Q. April one through your agency Heffernan, Inc.?
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> A. That is right.

On redirect examination, Heffernan insisted that all of the accounts renewed through his new agency were those he developed prior to the formation of the Corporation. He agreed that the premiums and commissions earned by the Corporation from the accounts subsequently placed with his new agency totaled approximately $15,000 in the year preceding their removal.

Heffernan further admitted that he wrote new business for his new agency while president of the Corporation. He was asked:

> Q. You sold a new policy in your new agency while you still were president of Heffernan, Ballinger, Pounds and Yarbrough for West Pools; right?
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> A. After I had made my commitment.
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> Q. While you were still president?
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> A. Well, yes, I guess.

Upon hearing the evidence, the master awarded Heffernan $22,680 for his share of distributed corporate profits and approximately $33,000[6] in earned commissions for the year ending

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[6]This amount was subsequently reduced by the master for sums that were determined due Appellant from Heffernan.

May 31, 1987. The method of computation was based on the master's determination that for several years prior to 1987, the parties operated under an agreement wherein each individual producer of commission income was compensated based upon the percentage of what he produced compared to total commissions. When year end profit was computed, each producer received their established percentage of profit.

Although it was determined that prior to May 31, 1987, "Heffernan began seeking and filing agent of record letters with the insurance companies on insurance he had written . . . . to insure that he or his new agency would be entitled to future commissions rather than the corporation. . . ," the master concluded that such action did not violate Heffernan's fiduciary duties to the Corporation. The master reasoned:

> The other shareholders knew a breakup was in progress and Mr. Heffernan was extremely displeased and knew that he was going to leave. His decision to seek agent of record letters on insurance he had written, that was being renewed, was not unreasonable or improper.
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> . . . .
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> . . . . Mr. Heffernan did not breach his duty to the corporation by directing business to himself.

It was further concluded that Heffernan was neither obligated to Appellant for any commissions placed in his own agency prior to his departure or a $15,000 loan from the Corporation to him. These findings, as hereinabove noted, were concurred in by the chancellor.

We begin our review cognizant of the general rule that concurrent findings by the master and trial court are conclusive on appeal. Four exceptions render the rule inapplicable: (1) the issue should not have been referred to a master; (2) the findings are based on an error of law; (3) the findings involve a question of law or a mixed question of law and fact; or (4) the findings are not supported by substantial and material evidence. ***See In re Estate of Wallace***, 829 S.W.2d 696, 700 (Tenn. App. 1992); ***Crouch v. Crouch***, 385 S.W.2d 288, 291 (Tenn. App. 1964).

It is well established that officers and directors of a corporation owe a fiduciary duty to the corporation and its members or shareholders and, while occupying such a position of trust,

must act in the utmost good faith. ***E.g., State ex rel. Oliver v. Society for Preservation of Common Prayer***, 693 S.W.2d 340, 343 (Tenn. 1985). In ***Knox-Tenn Rental Co. v. Jenkins Ins., Inc.***, 755 S.W.2d 33 (Tenn. 1988), our supreme court further observed:

> In a broad sense, the directors and officers of a corporation are its agents. While they may not be in a strict sense trustees, it is well established that they occupy a fiduciary, or more exactly a quasi-fiduciary, relation to the corporation and its stockholders. 18B Am.Jur.2d, Corporations, § 1689, p. 541. An agent is a fiduciary with respect to the matters within the scope of his agency. The very relationship implies that the principal has reposed some trust or confidence in the agent and the agent or employee is bound to the exercise of the utmost good faith, loyalty, and honesty toward his principal or employer. 3 Am.Jur.2d Agency, § 210, p. 713. The correct rule on the status of a corporate officer as a fiduciary is found in ***Hayes v. Schweikart's Upholstering Co.***, 402 S.W.2d 472, 483, 55 Tenn.App. 442 (1965), citing from 19 C.J.S., p. 107, as follows:
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> > "A corporate officer must at all times be loyal to his trust and act in good faith and unselfishly toward the corporation and its stockholders, and cannot assume positions in conflict with the interests of the corporation; but the restrictions on their activities growing out of the fiduciary status extend only to such corporate interests as exist at the time or may reasonably be expected in the development of the corporate business. If the officers transcend or abuse their powers, they are as much responsible to their principal as the agent of an individual is to him."
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> > "A mere employee does not ordinarily occupy a position of trust or confidence toward the corporation unless he is also an agent. . . ." Vol. 19 C.J.S. Corporations § 761b, p. 107.

Knox-Tenn Rental, 755 S.W.2d at 36-37. The ***Hayes*** court further held that such "obligation of loyalty" by directors and officers to the corporation "extend[s] up until the very last day of their terms of office." ***Hayes v. Schweikart's Upholstering Co.***, 402 S.W.2d 472, 482 (Tenn. App. 1965).

Having addressed the applicable law, we turn attention to the facts of our case. On April 1, Heffernan informed the other directors/shareholders of his intention to leave the Corporation. He physically vacated the premises in early May, although the record suggests that his original intention was to remain with Appellant until the end of the fiscal year. Heffernan was admittedly compensated by the Corporation through the month of April and he, undoubtedly, remained an employee, officer and director of the Corporation at least through the end of this month.

As enunciated in ***Hayes***, his fiduciary duty to Appellant extended until this time. As a result, and in accordance with the foregoing law, Heffernan could not direct business toward his own agency during this period without violating his fiduciary duty to Appellant. It is abundantly clear, however, that Heffernan did just this; it being never more apparent than when Heffernan himself testified that he wrote new business for his own agency while president of the Corporation.

The master, likewise, found that Heffernan "direct[ed] business to himself" prior to May 31 and that his purpose for doing so was to ensure that his new agency would be allowed the future commissions rather than the Corporation. The master nonetheless concluded that Heffernan was not in breach of his fiduciary duty because the other shareholders "knew a breakup was in progress" and that Heffernan was "going to leave." Inasmuch as the master's findings in this regard involved mixed questions of law and fact, we do not find ourselves bound by the concurrent finding rule and, therefore, hold that Heffernan breached his fiduciary duty to the Corporation. As a consequence thereof, he must forfeit a portion of the compensation otherwise due him.

In ***Wilshire Oil Co. v. Riffe***, 406 F.2d 1061 (10th Cir. 1969), the plaintiff corporation filed suit against its former corporate officer to recover compensation paid the officer "during the period he was interested in a competitive corporation." ***Wilshire Oil***, 406 F.2d at 1062. ***Wilshire*** quoted the general rule that corporate officers who engage in activities which constitute a breach of their duty of loyalty or who willfully breached their contract of employment are not entitled to compensation for services performed during that time period even though part of their services were properly performed. ***Id***. ***See In re Omni Mechanical Contractors, Inc.***, 114 B.R. 518 (Bankr. E.D. Tenn. 1990); 5A William M. Fletcher, ***Fletcher Cyclopedia of the Law of Private Corporations*** § 2145 (perm. ed. rev. vol. 1995). The court, in quoting from the Restatement (Second) of Agency § 469, further acknowledged that "[a]n agent, who, without the acquiescence of his principal, acts for his own benefit or for the benefit of another in antagonism to or in competition with the principal in a transaction is not entitled to compensation which otherwise be due him." ***Wilshire*** found the foregoing rule applicable to the facts before it and allowed the plaintiff to recoup the compensation paid the corporate officer during the period of time that the "failure commenced" to its end. ***Id***. ***Wilshire*** determined that the period of violation was seven months and awarded the plaintiff an

amount equal to seven-twelfths of all compensation paid the officer for that particular calendar year.[7] ***Id***. at 1062-63.

Heffernan's complaint seeks earned commissions and his share of corporate profits through May 31, 1987. The chancellor's award to Heffernan was based on earned commissions and profits for the entire fiscal year. As heretofore stated, Heffernan is not entitled to any compensation for the period in which he was in breach of his fiduciary duty to Appellant. Clearly, Heffernan was in violation of this fiduciary duty no later than April 1. We, therefore, find a remand of this cause to the trial court necessary to determine the commissions and profit share rightfully due Heffernan, with no compensation allotted for the two months prior to the end of the fiscal year.

As to the commissions allegedly due the Corporation from Heffernan, ***Central Bus Lines, Inc. v. Hamilton Nat'l Bank***, 239 S.W.2d 583, (Tenn. App. 1951), holds:

> [Corporate officers] are not permitted to deal with the corporation or its assets for their own private gain and cannot deal for themselves and for the corporation at one and the same time . . . . If they do so act in violation of their trust, they must account for any profits made by use of corporate assets.

Central Bus Lines, 239 S.W.2d at 585. Based upon the foregoing, we believe Appellant entitled to the approximately $15,000 in commissions that were placed in Heffernan's own agency.[8]

We now address Appellant's final issue regarding whether Heffernan should be obligated to the Corporation for the $15,000 loaned to him.[9] The Master determined the following in regard to this issue:

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[7]This decision is the second of two appeals. On remand from the first appeal, the trial court awarded the plaintiff corporation the profits made by the officer by participating in competitive enterprises. ***See Wilshire Oil***, 406 F.2d at 1062.

[8]We note here that Appellant has not sought recovery of these funds by way of counterclaim or setoff. However, we agree that the issue was in fact tried by the parties in accordance with Rule 15.02 T.R.C.P.

[9]This issue was also tried by consent of the parties pursuant to Rule 15.02 T.R.C.P.

> There were a number of loans made by the corporation to various principals over a period of years. These loans were paid off May 25, 1986 and each of the principals' loans were renewed in the amount of $15,000 on June 25, 1986 . . . In the spring of 1987, at the time Mr. Heffernan left to form his own agency, each of the principals owed the corporation $15,000. . . . Mr. Ballinger, Mr. Pounds, and Mr. Yarbrough continued using the old corporate structure for operation of business for another year and perhaps a little longer at which [time] they formed the new corporation Ballinger, Pounds, and Yarbrough, Inc. During that next fiscal year which began after May 31, 1987 the remaining principals borrowed an additional $10,000 from HBP&Y, and then . . . on May 31, 1988 they each paid back $25,000. Mr. Heffernan never paid the $15,000 he had borrowed, and the question is, does he owe this money to HBP&Y which still exists as a shell corporation. The proof is not clear, but presumably the $75,000 which was paid into the corporation by the three principals and other assets still belong to the old corporation. The answer to the question of whether Mr. Heffernan should pay the old corporation $15,000 depends on whether or not Mr. Heffernan is making claim to any of the $75,000 which was paid back. If he is not making any claim to the $75,000 paid in by the defendants, then there would be no reason for him to pay back the $15,000 he borrowed since the defendants had the power to draw the $75,000 out at any time. Also it does not appear that the money was used to pay corporate debts existing at the time Mr. Heffernan left. If he is making claim to part of the $75,000, then he should pay back the money.
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> It should be noted that Mr. Heffernan is not required to pay back the $15,000. It should be treated as income and presumably he should show this as income on his tax return.

Heffernan does not dispute that the Corporation loaned him $15,000 which he has not repaid. We believe he remains obligated to the Corporation for this amount. Our holding in this regard is not meant to preclude Heffernan's recoupment of a portion of this amount, should the trial court ultimately deem him entitled after its reconsideration of the proper amount of compensation due Heffernan.

It results that the judgment of the trial court is reversed, with this cause remanded to the trial court with instructions to recalculate the amount of compensation due Heffernan in light of the breach of his fiduciary duty to the Corporation. Costs are assessed against H. Patrick Heffernan, for which execution may issue if necessary.

FARMER, J.

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HIGHERS, J. (Concurs)

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LILLARD, J. (Concurs)