

Monterey College of Law

Business Organizations (Agency & Partnerships)

Fall 2024

Prof. D. Bean

Instructions:

Time Allotted: Three (3) Hours

Allocate your time according to the points for each question:

Question 1

Randy owns and operates Integral Cannabis, a large growery and dispensary chain. Randy hires Towlie, a cannabis expert, to test the merchandise and market to significant customers including distributors and celebrity consumers. Unbeknownst to Towlie, Randy also wishes to expand into the restaurant business.

During the course of his employment, Towlie becomes acquainted with Snoopy Pupp, a hip-hop icon and significant celebrity cannabis consumer who has long endorsed Integral.

While on vacation to the Chartreuse Triangle, a known cannabis growing area, Towlie meets Trey and Matt. They inform Towlie that (1) they have created a new strain, "North Park," which cultivates quickly and has higher yields than known current strains and (2) Trey and Matt are going to purchase Casa Feo, a run-down restaurant, and renovate it. Towlie invests in both ventures using his own funds and does not disclose either opportunity to Randy.

When Towlie returns to Integral, Randy comments that Randy is interested in purchasing some of the North Park strain.

The infinite access to cannabis is too much of a temptation for Towlie, who ingests at least several hundred dollars' worth of cannabis per day at Integral and Randy's expense. Randy learns of Towlie's excessive consumption and fires Towlie; Randy tells Towlie he has four hours to clear his things. During those four hours, Towlie calls Trey and Matt, asks to buy all the North Park so Randy cannot buy any, and then calls Snoopy Pupp and asks if Snoopy Pupp will become his client and endorse Towlie's new venture. Snoopy Pupp agrees.

1. Discuss any claims Randy may have against Towlie.

Question 2

Olaf One and Tommy Two form a partnership, a car dealership. Tommy is obsessed with Porsches and orders several, but customers do not buy them. Olaf then sends a letter to Porsche, "No more Porsches please we can't sell them."

About three months later, Tommy contacts Porsche and orders several more Porsches. When they are delivered, Olaf refuses to pay.

Frustrated, Olaf finds a buyer for the business, Ted Thirdparty. Ted is aware that Olaf and Tommy are equal partners in the business. Olaf sells Ted every car, the underlying lot and any building and fixture thereon, any furniture, signs, or other property associated with the business, and the customer list. When Tommy finds out, he objects and refuses to transfer any items to Ted.

Porsche then sues Ted for the still uncollected debt.

1. Discuss any claims Porsche may have against the partnership or Olaf.
2. Discuss any claims Ted may have against the partnership or Olaf.
3. Assume Ted convinces Tommy to transfer his interest and Ted becomes the owner of the dealership. Discuss any claims Porsche may have against Ted.

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Question 3

Aaron Able comes to you and informs you that he has been operating a profitable business for the last five years. He has not filed any kind of documents with any government office. He tells you that he is considering bringing in a friend, Brianna, as a co-manager of the business, but Brianna does not want to be personally liable for any debts of the business. Carl has also offered to fund the business but does not want to partake in management, and similarly does not want to have personal liability.

1. Advise Aaron of what entities have been or could be created and the pros and cons of each.

Question 1:

1. **A principle-agent relationship is formed when both parties consent to a relationship wherein the agent agrees to act on behalf of, and under the supervision of, the principal.** Here, Towlie is hired to test the cannabis and market to significant customers. Towlie is an agent of Randy/Integral
2. **An agent owes the principle a duty of loyalty. The agent cannot act in a manner adverse to the principal and the agent cannot undertake business opportunities learned about via the agency and reasonably related to (material to) the agency.**
 - a. Here, Towlie learns about "North Park" while on vacation. He is not acting as an agent. However, the opportunity is sufficiently related to Randy's business that Towlie should disclose it to Randy.
 - b. The restaurant business, however, does not appear to be related to Integral. Therefore Towlie's investment in the restaurant is not a breach of the duty of loyalty.
 - c. Towlie's excess cannabis consumption is materially adverse to the business and a breach.
 - d. Towlie became acquainted with Snoopy Pupp during his employment; furthermore, asking for an endorsement is materially adverse to Integral. This is a further breach.
 - e. When Towlie purchases all the North Park with the specific purpose of obstructing Randy's business, this is a further breach.

Question 2

1. **All partners are agents of the partnership. The partnership is liable for transactions any partner makes, even if that partner lacked authority, provided the third party did not know the transaction was beyond the scope of the partner's authority.**
 - a. Here, Tommy is a partner and therefore an agent. Olaf will assert that Olaf's letter to Porsche put Porsche on notice that the partnership would not buy any more Porsches. Porsche will assert that the letter is vague, and that Tommy had authority to override the letter. Porsche has the better argument.
2. **Disposition of all or nearly all assets of the partnership is not a normal transaction of the partnership. Such a transaction puts a third party on notice that the partner lacks authority for that transaction.** Ted has no recourse against Tommy because Ted could not reasonably believe that Olaf had authority for the transaction.
3. **Normally, purchasing assets of a partnership does not subject the purchaser to the liabilities of the partnership. However, when the purchaser essentially carries on the business, the purchaser is liable.** Here, because Ted is essentially continuing the business, he will be liable to Porsche for the debt.

Question 3

1. **A solo proprietorship is the default form of business, it is formed whenever a person carries on a business; no filing is required. The proprietor has personal liability for the debts of the proprietorship.** Here, Aaron has already formed a solo proprietorship by carrying on a business. He has no liability shield.
2. **A partnership is formed when two or more people agree to carry on a business for profit. It is formed by operation of law when those elements are met, no filing is required, Each partner is personally liable for the debts of the partnership.** Here, if Brienne joins as co-manager or Carl as investor or both, a partnership will be formed, with all partners having personal liability and no liability shield.
3. **A limited partnership requires a filing with the Secretary of State naming the general and limited partners. The general partners have personal liability for partnership debts, but the limited partners do not. However, a limited partner who takes part in the management of the business will be deemed a general partner and have personal liability.** Here, the parties could form an LP. The LP would likely protect Carl from personal liability, but not Brianna, as she would be a manager.
4. **A limited liability partnership requires a filing. All partners have a liability shield.** Here, the LLP is a better choice than a SP, GP, or LP because it will protect all partners.
5. **A limited liability company requires a filing. All members have a liability shield.** The LLC is also a good choice because of the liability shield.
6. **All entities discussed have flow-through taxation, that is, the partners/members will be taxed on earnings regardless of actual distributions.**
7. The three should opt for an LLP or LLC.

1)

Agency

Agency is a relationship between the agent acting upon the benefit of the principal. For agency to exist there must be mutual assent, the agent must be acting for the benefit of the principal, and the agent must be subject to the control of the principal.

Here Towlie is acting as the agent for Randy who is acting as the principal. The reason for this is due to Randy hiring Towlie to test the merchandise and market it to customers, celebrity, and distributors. Thus Towlie is acting for Randy's benefit and is subject to Randy's control. Thus an agency has been formed between Towlie the agent and Randy the principal.

Duty to Inform

An agent has a duty to inform the Principal about things that apply to the agent carrying out the task for the principal that pertain to the business which they are carrying out.

Here Towlie should have informed Randy about the new strain "north park" since this would fall in line with his duties towards Randy and his cannabis operation, thus this information would have been important for Randy to know since he works at a growery and dispensary chain and even commented about how he is interested about buying the strain from Towlie after his vacation where he learned about the strain. Along with this Towlie invests his own funds into the new strain which could create a problem which he is not acting within his own self interest instead of Randy's benefit and did not mention any of this to Randy. As for the second statement about Casa Feo, Towlie did not know that Randy wished to expand into the restaurant business so he has no duty to inform Randy about this statement.

Duty of Loyalty

An agent must act within the interest of the principal and do so with good faith and fair dealing and not act adversely to the principal interests.

Here Towlie breached this principal on two occasions when he first acted in his self interest and 2nd where he acted adversely to Randy interest. First Towlie acted in his self interest when he knew information about the North Park strain and not only didn't tell Randy but also purchased some for his own benefit thus acting in his self interest and not for Randy's interest. Second when he was left with 4 hours to clear out his thing he then calls Trey and Matt and buys all of the North Park strain so that Randy cannot buy any and also asks Snoopy if he will be his own client within Towlie's new venture. With this Towlie knows that Snoopy has long endorsed Integral and knowing acts adversely to Randy while still technically within the scope of his agency since he was doing this within his four hours to clear out his things along with buying out all of the North Park strain within this four hours.

Duty of Due Care

An agent must act with due care when carrying out business on behalf of the principal.

Towlie could have breached this duty by ingesting several hundred dollars worth of cannabis per day while at Integral and on Randy's expense. Randy fired once he learned about the excessive consumption thus showing that he should not have been ingesting this amount while working and thus not exercising due care within his agency.

Duty to Obey

An agent must obey the principal when carrying out task for the purpose of agency relationship and so long as the principal is not asking anything illegal to be done.

Here Towlie breached the duty to obey through multiple different actions within the agency with Randy. Towlie was tasked with marketing to customers and testing merchandise. However he abused this task and ended up consuming several hundred of dollars worth of cannabis per day on Randy's expense as well as not informing him about possible business ventures of the new strain when he told Towlie that he was interested in buying North Parl strain after Towlie had knowledge of vendors who created the strain.

Conclusion

Randy can claim that Towlie his agent breached duties that were owed to Randy the Principal. The duties that were breached are duty to inform, duty to obey, duty of loyalty, and duty of due care.

Question Two

Claims Porsche may have against the partnership or Olat.

Partnership: A partnership is an association of two or more persons who carry on as co-owners of a business for profit.

Here, the facts do not state that Olat and Tommy ever submitted a filing that would allow them to form a type of partnership that would provide one or both of them with a liability shield, so presumably they have formed (either intentionally or unintentionally) a general partnership.

General Partnership: Under a general partnership each partner may be jointly and severally liable for obligation incurred on behalf of the partnership.

Each partner is an agent of the partnership, meaning that each partner has the power to bind the partnership.

Here, in purchasing the orders from Porsche Tommy likely had the power to bind the partnership. Olat will likely try to argue that his letter to Porsche,

instructing them to not fill anymore orders because the partnership was unable to sell the cars, serves as notice that Tommy did not have the authority to purchase any more cars from them.

~~Apparent~~ Apparent Authority of a General Partner:

In circumstances in which a partner contracts with a third party without the express authority to do so but does so within the ordinary course of business and without the third party knowing or having reason to know that the partner lacked such authority, then the third party may still enforce the contract.

Here, Tommy and Olat run a car dealership, so the purchasing and selling of cars is presumably within the ordinary course of business. Olat will likely attempt to argue that, Porsche, at the time Tommy placed the second order, was on notice that Tommy lacked the authority to do so. Porsche will likely respond by arguing that because Tommy and Olat are general partners

and without any facts to suggest they did not share equal management and control of the business, Olat did not have the power to strip his partner of his authority to purchase the vehicles.

Porsche may bring a claim against both the partnership and Olat for breach of contract after the refusal to pay for the vehicles. As a general rule, however, Porsche will likely have ^{to} bring suit against the partnership first and if the assets of the partnership are insufficient to satisfy the judgment then Olat will be personally liable. In either event Porsche will likely be successful in a claim for breach of contract.

Any claims Ted may have against the partnership or Olat partnership: See above

General Partnership: See above

Partnership Assets: Assets are presumed to be partnership assets provided that they are purchased with partnership money or they are purchased by one of the

partners under the name of or holding themselves out as a member of the partnership.

Here, there are no facts to suggest that any of the assets which Olat attempted to sell to Ted were Olat's separate property, so they are presumably assets of the partnership.

In attempting to sell the totality of the partnership assets, Olat is effectively selling the business itself which is well outside the ordinary course of the business of running a car dealership.

Apparent Partnership Authority: See above

Even if Ted was not on notice that Olat lacked the authority to sell the partnership assets, Olat's actions are likely so far outside the bounds of the ordinary course of business that the court would find that Ted may not be justified in believing Olat had such authority. Alternatively a court may also find that the differences between Olat and Tommy are so irreconcilable that the court forces the dissolution

of the partnership. Ted may still be able to acquire the assets through the dissolution and liquidation of the partnership. Absent a dissolution however, Ted will likely be unsuccessful in enforcing the sale of the partnership without Tommy's consent. Ted may still have a personal claim against Olaf for breach of contract and misrepresentation if Olaf did in fact represent to Ted that he actually had the authority to sell the business.

Olaf may choose to sell his interest in the partnership to Ted, but not the partnership assets as listed in the facts.

Claims Porsche may have
against Ted

If Olaf is successful in convincing Ted Tommy to sell the business to Ted, Porsche may still be able to recover from Ted under the doctrine of successor liability.

Successor liability: In a circumstance ^{where} a partnership no longer exists but the new owner of the partnership assets carry on business and effectively hold

themselves out as the same business the new owner may still be held liable for the debt of the partnership.

Here, if Ted carries on do business as effectively the same entity and holds himself ~~as~~ out as the same business, then Porsche may seek to recover the debt incurred by the general partnership.

3)

1) Advise Aaron of what entities have been or could be created and the pros and cons of each

GENERAL PARTNERSHIP

A general partnership ("GP") is formed when two or more people come together to operate a business for profit. Each of the partners is general partner with equal rights to control and management. The partners also share equally in profit and loss.

PROS

A GP is easy to form. It is the default partnership and requires no official filing with the Secretary of State.

CONS

General partners are jointly and severally liable for partnership debt. If a GP has insufficient funds to cover debts, a creditor may satisfy the debt once GP funds have been exhausted with the partner's personal assets.

General partners are bound by the actions taken by a general partner if they had apparent authority and acted in the ordinary course of business.

LIMITED PARTNERSHIP

A limited partnership consists of at least one general partner and one limited partner. It requires a filing with the Secretary of State to be formed. The general partner is responsible for management and control, whereas the limited partner provides capital investments for ownership and does not participate in much management or control.

PROS

Limited partners are only liable for up to their capital contribution amount.

CONS

Limited partners can become general partners by exercising too much control.

Limited partners have the power, but not the right, to leave a limited partnership. As a result, if they leave, they will be sued.

General partners are jointly and severally liable for debts and contracts incurred by a general partner with agency and acting within the ordinary course of business.

LIMITED LIABILITY PARTNERSHIP

A limited liability partnership ("LLP"), like a general partnership, makes no distinction between partners. It requires a filing with the Secretary of State to be formed. Of the three forms of entities, a LLP provides the most protection to partners.

PROS

Partners are shielded from personal liability for partnership debts.

CONS

The partnership is bound by the actions taken by a partner if they had apparent authority and acted in the ordinary course of business.

Partners remain liable for two years after terminating the partnership if the liability arises from business taken on during the partnership.

CONCLUSION

Based on Aaron's likely current status as a sole proprietorship, if he chooses to bring in partners to his profitable business, he should form a limited liability partnership or a limited partnership.

Brianna's desire to serve as a co-manager of the business and avoid personal liability for any business debts would be in line with a formation of a limited liability partnership. However, Carl's desire to offer funds but not partake in management and not be personal liable for business debts puts him more in line with a formation of a limited partnership.

If Aaron needs more capital, it will be appealing to get Carl's support and funds by opening the limited partnership. However, if capital is not an issue, Aaron's personal assets will be best protected by the limited liability partnership.

END OF EXAM