

BUSINESS ASSOCIATIONS

Professor John Orcutt
Spring Semester 2010

MIDTERM EXAMINATION – IN CLASS

INSTRUCTIONS:

1. This is a closed-book, closed-note examination. You may not bring any materials to the examination.
2. This is a 60-minute examination and is worth 50 points (or 10% of your final grade). I have provided you with 26 multiple choice questions (each worth 2 points). The maximum score on the exam, however, will be 50 points. In effect, you get one free wrong answer for the exam.
3. The grading of examinations is anonymous. So, you must write your examination number on the examination, and your Scantron sheet. **YOU MAY NOT WRITE YOUR NAME ON ANYTHING – YOU MAY ONLY USE YOUR EXAM NUMBER.**
4. The multiple choice questions are to be answered on a Scantron sheet. Your proctor will provide you with specific instructions regarding the filling out of the Scantron sheet.
5. I have tried my best to write and proofread the exam so that there are no distracting typos or other errors – but, I may not have been totally successful. If you believe there is a typo or other error that makes it difficult to answer a particular question, make your best selection and write out the error on the back of the Scantron sheet (for the multiple choice questions) or in your blue book (for the essay questions) and any assumption you used to answer the question. Be sure to indicate the number of the question involved.

Good luck on the examination!

DO NOT TURN TO PAGE 2 UNTIL THE PROCTOR TELLS YOU TO BEGIN

30 MULTIPLE CHOICE QUESTIONS
(2 points each – 2 minutes per MC question suggested)

Question 1

Giselle is a loan officer at TownBank, Inc. ("TownBank"). TownBank's internal procedures provide that loan officers can enter into loan agreements of up to \$200,000. For loan agreements above \$200,000, TownBank loan officers must get approval from the Credit Department before signing the contract.

Brady walked into the TownBank branch and asked to speak with someone about getting a loan. Brady was walked to Giselle's desk, where her nameplate identified her as a loan officer. Brady sought a loan for \$300,000 and Giselle approved Brady's request. Giselle pulled out a loan agreement from her desk, filled in the \$300,000 principal amount and the interest rate and signed the agreement. Brady also signed the agreement. Giselle did not get approval from the Credit Department. TownBank found out about the loan two days later and refused to honor the agreement.

If Brady sues TownBank, what is the most accurate statement about TownBank's liability under the loan agreement?

- (A) TownBank could be liable under the loan agreement under a theory of implied authority.
- (B) TownBank could be liable under the loan agreement under a theory of apparent authority.
- (C) Both (A) and (B).
- (D) TownBank is not liable under the loan agreement because Giselle exceeded her actual authority when she signed the loan agreement.

Questions 2 and 3 are based on the following fact situation:

Snooki was a teacher at Shore High School. The school's curling team was going to another school to play a game and was to be transported in private cars. Snooki asked Ronnie, the coach for the school's curling team, if he had enough cars. Ronnie responded that he needed one more car. Snooki told Ronnie that he could use her car for the game if Ronnie drove it. Snooki did not ask for, nor was she promised, any compensation for the use of her car. On the drive back from the game, Ronnie crashed the car. Ronnie died in the accident and Mike, one of the members of the curling team, was terribly injured. Ronnie's negligent driving was the cause of the car accident.

Mike sues Snooki for the damages he has suffered from the car accident.

2. What is the most accurate statement regarding Snooki's potential liability for Mike's damages?
 - (A) If Snooki is found to have had a principal/agent relationship with Ronnie, she will be liable because principals are liable for torts committed by their agents.
 - (B) If Snooki is found to have a master/servant relationship with Ronnie, she could be liable.
 - (C) If Snooki is found to have a principal/independent contractor relationship with Ronnie, she will be liable if Ronnie's tort was committed within the scope of his agency.
 - (D) It is highly unlikely that Snooki could be found liable for Mike's damages. Irrespective of the nature of her relationship with Ronnie, Ronnie's accident exceeded his authority.

3. Which of the following are valid arguments for Snooki NOT being liable for Mike's damages?
 - (A) Ronnie is not Snooki's agent because there was no consideration to bind an agency agreement between them.
 - (B) Ronnie is not Snooki's agent because his agency relationship is barred by the Statute of Frauds.
 - (C) Snooki could not be Ronnie's principal because she did not receive any financial gain from the relationship.
 - (D) None of the above.

Questions 4 and 5 are based on the following fact situation:

Allison, Bill, Charles and Donna formed a partnership ("ABCD Partnership") about two years ago to open and operate a grocery store. In accordance with their initial understanding, Allison has served as general manager, Bill has served as assistant general manager and producer manager, Charles has run the meat department, and Donna has run the bakery. About six months ago, Charles decided that he needed help in the meat department so he hired Edgar to work under a one-year contract (the "Employment Contract"). Edgar knew that was Charles one of the partners for ABCD Partnership and Edgar had no reason to believe that Charles could not hire him. None of Allison, Bill or Donna ever approved Edgar's hiring. Allison and Bill believe that Edgar is surly and slow and that he is driving customers away. They have asked Charles to fire him, but Charles has refused to do so. He thinks Edgar is brash but lovable and that many customers like his style. Charles is satisfied that Edgar works fast enough to get his job done. Donna does not have a strong opinion on Edgar and wants to stay out of the matter.

The partnership agreement for ABCD Partnership includes the following distribution of profits: Allison is entitled to 50% of partnership profits, Bill 30%, Charles 10% and Donna 10%. The partnership agreement, however, is silent as to both management and voting matters.

Allison and Bill have come to you for advice on getting rid of Edgar.

4. Allison and Bill would like to assert that ABCD Partnership is not responsible for the Employment Contract. What is the most accurate statement regarding ABCD Partnership's liability for the Employment Contract?
- (A) ABCD Partnership is likely contractually bound by the Employment Contract.
 - (B) ABCD Partnership is likely not contractually bound by the Employment Contract because Charles did not have actual express authority to hire Edgar.
 - (C) ABCD Partnership is likely contractually bound by the Employment Contract because Charles had actual implied authority to hire Edgar.
 - (D) ABCD Partnership is likely not contractually bound by the Employment Contract. Because hiring Edgar was an "ordinary matter connected with the partnership business," it required a majority of the partners to approve the transaction.
5. If it turns out that ABCD Partnership is responsible for the Employment Contract, Allison and Bill would like to terminate the Employment Contract and fire Edgar. Charles will not approve any firing. In addition, you have spoken with Donna. Donna has told you that she is staying out of the dispute and will neither vote to fire Edgar, nor will she vote to keep him. You can assume that any vote for ABCD Partnership to terminate Edgar will be as follows:
- Allison will vote to terminate
 - Bill will vote to terminate

- Charles will vote NOT to terminate
- Donna will abstain from the vote

What is the most accurate statement regarding Allison's and Bill's ability to cause ABCD Partnership to terminate Edgar?

- (A) Allison and Bill hold 80% of the voting rights for ABCD Partnership. If Allison and Bill vote for ABCD Partnership to terminate Edgar's contract, the contract will be terminated.
- (B) Allison and Bill voting to terminate Edgar's contract provides a 2-to-1 vote for termination over Charles's vote not to terminate. That 2-to-1 vote is sufficient to cause ABCD Partnership to terminate Edgar's contract.
- (C) Without cooperation from Charles or Donna, Allison and Bill cannot force ABCD Partnership to terminate Edgar.
- (D) Terminating Edgar will require a unanimous vote from all of the partners.

Question 6

Generally speaking, a corporation must be solvent in order to pay a dividend, and still be solvent after the dividend has been paid. A dividend violating this rule will be deemed to be illegal. This is not an entirely accurate summary of the law – there are a few approaches that states take to deal with this issue and a number of different tests for determining whether a corporation is in a proper financial position for paying dividends. It is, however, an accurate statement of the basic concept: no dividends unless the corporation is solvent.

What is the purpose for this rule that a corporation must be solvent in order pay a dividend (and still be solvent after the dividend has been paid)?

- (A) The solvency rule is a default rule and may be contractually modified by the shareholders through the corporation's certificate of incorporation and/or by-laws.
- (B) Shareholders do not own the corporation's assets. Shareholders only have a right to what we referred to in class as the "residual".
- (C) The rule is grounded in historical precedent and is not based on any underlying purpose.
- (D) It helps to alleviate the problems that arise from the separation of ownership from management in a corporation.

Questions 7 – 10 are based on the following fact situation:

Acme Corporation operates close to 1,000 family-style restaurants throughout the United States. Of the 1,000 restaurants, Acme Corporation directly owns and operates roughly 100 of them (they will be called "Acme-owned" restaurants). The other roughly 900 restaurants are independently-owned restaurants and operate through a franchise arrangement (they will be called "Acme-branded" restaurants).

Not surprisingly, torts occur at Acme-owned and Acme-branded restaurants from time-to-time. You have been asked to consider two specific incidents that took place in the last six months.

- **Incident No. 1:** This incident occurred at an Acme-owned restaurant. A group of customers of middle-eastern descent were subjected to racial and ethnic discrimination while trying to buy a meal at an Acme-owned restaurant. Nermien (who was born in Egypt, but now lives in the United States) and her children stopped at an Acme-owned restaurant for dinner. When Nermien asked for a table, Smith (the restaurant's manager) told Nermien and her children, "We do not serve your kind here." A brief argument ensued, during which time Smith insulted Nermien and her children with various racial epithets. After Nermien left the restaurant, Smith used the store's intercom system to continue yelling racial epithets. Nermien has sued Acme Corporation for damages that she suffered from Smith's tortious behavior. For purposes of these questions, you are to assume that Smith has committed numerous torts against Nermien.
- **Incident No. 2:** This incident occurred at an Acme-branded restaurant. Paula has sued Acme Corporation for injuries that she suffered when she bit into a sapphire stone while eating a hamburger she had purchased at an Acme-branded restaurant.

Questions Regarding Incident No.1:

7. If Acme Corporation is found to be liable for damages that Smith caused to Nermien, which of the following statements provides the most likely, and the most complete, explanation?
- (A) Because Smith was an employee of Acme Corporation, Acme Corporation has a master/servant relationship with Smith.
 - (B) The court found Acme Corporation directly liable for the tort under a theory of respondeat superior.
 - (C) The court found Acme Corporation vicariously liable because it found that Smith was an employee of Acme Corporation and that Smith's actions were within the scope of her employment.
 - (D) The court found Acme Corporation vicariously liable under a theory of apparent agency.

8. If Acme Corporation is found NOT to be liable for damages that Smith caused to Nermien, which of the following statements provides the most likely explanation?
- (A) The court must have rejected the apparent agency doctrine.
 - (B) The court found that Acme Corporation did not have sufficient control over Smith's behavior to create a master/servant relationship.
 - (C) The court found that Smith's actions were not within the scope of her employment because Smith was not given actual authority to commit the tort.
 - (D) The court found that Smith's actions were not within the scope of her employment because Smith's actions were motivated purely by personal reasons and had no purpose to serve Acme Corporation.

Questions Regarding Incident No.2

For the questions relating to Incident No. 2, please consider the following additional facts. Acme Corporation did not own or operate the restaurant where Incident No. 2 took place. Instead, that particular restaurant was an Acme-branded restaurant that was owned by NPH Restaurants Inc. ("NPH"). NPH owned and operated the restaurant under a License Agreement with Acme Corporation. Among other things, the License Agreement included the following agreements:

- Acme Corporation agreed to license the name "Acme Restaurant" to NPH;
 - Acme Corporation was required to conduct national and regional advertising for the benefit of NPH;
 - NPH agreed to operate the restaurant in a manner consistent with the "Acme System." The Acme System requires that all licensees operate their restaurants in a consistent manner. The Acme System covers the operation of Acme-branded restaurants in considerable detail, including setting forth required standards, policies, practices, and procedures for preparing and serving food; and
 - The License Agreement also includes a disclaimer that expressly states that NPH is not an agent of Acme Corporation for any purpose.
9. If Acme Corporation is found to be liable for damages caused to Paula when she bit into the sapphire, which of the following statements provides the best explanation?
- (A) The court could have found that Acme Corporation exercised sufficient control over NPH to form a master/servant relationship.
 - (B) The court could have found that the doctrine of apparent agency was applicable.
 - (C) Both (A) and (B).
 - (D) None of the above.

10. If Acme Corporation is found NOT to be liable for damages caused to Paula when she bit into the sapphire, which of the following statements provides the best explanation?

- (A) Parties have the ability to contract out of agency relationships, which is what Acme Corporation and NPH did with the disclaimer.
- (B) The court could have found that Acme Corporation did not exercise sufficient control over NPH to form a master/servant relationship.
- (C) The court must have respected NPH's corporate shield.
- (D) None of the above.

Question 11

Suppose you are outside counsel to a public corporation engaged in the manufacture and sale of automobile replacement parts. The CEO calls you for advice about having the corporation make a charitable gift of \$1 million to a private school for poor children that has had considerable success over a number of years in motivating and educating children who might otherwise not have had much of a chance to succeed academically. The school is in difficult financial straits and will likely have to close unless it receives this \$1 million charitable gift. The corporation's profits last year were roughly \$10 million, and will probably be the same this year. The CEO says that he is besieged by requests for charitable donations. To avoid more requests and to avoid creating ill will with people seeking funds for other causes (some of whom are important customers), the CEO wants the corporation's charitable gift to the school to be anonymous.

Is there any problem with the corporation making the charitable gift as envisioned by the CEO?

- (A) Yes. There is a substantial risk that the dividend would be ultra vires.
- (B) No. So long as the corporation's current residual is in excess of \$1 million, there should be no problem with the corporation providing a charitable donation to a very worthy cause.
- (C) Yes. Because of the size of the gift and the fact that it is anonymous, the dividend appears to violate the internal affairs doctrine unless approved by a majority of the corporation's shareholders.
- (D) No. States long ago recognized the social welfare benefits that stem from permitting corporations to make charitable gifts.

Question No. 12

Lawson & Dawson is a general partnership. At the latest partnership meeting, 11 of the 21 partners were present. Two matters were voted on at that meeting: First, the admission of a new partner. Second, the purchase of \$500 worth of office supplies. The vote on both matters was 10 in favor, one opposed. The partnership agreement was silent as to both management and voting matters. After the meeting, one of the absent partners challenged the actions taken at the meeting.

Which of the following statements is most accurate?

- (A) No action should have been taken at the meeting, because not all partners were present.
- (B) The admission of a new partner is invalid, but the purchase of office supplies is valid.
- (C) Both actions taken at the meeting are invalid.
- (D) Both actions taken at the meeting are valid.

Question 13

ARod is widely viewed in his community as being a businessperson with very questionable ethics and little concern for his customers. ARod operates a taxicab business that consists of 10 taxis. To minimize his potential liability, ARod has structured his business as 10 separate corporations. Each corporation owns one taxi and carries only the legally mandated minimum liability insurance. ARod is the sole shareholder of each corporation. Each of the taxis operates out of a single garage (which is held by an 11th corporation owned by ARod).

One of ARod's cabs, owned by PED Corp. ("PED"), injured Derek. Derek's injuries far exceed PED's assets, so he would like to sue, and hold personally liable, ARod. What is Derek's most persuasive argument that the court should pierce the corporate veil and hold ARod personally liable for Derek's injuries?

- (A) The corporate form should be disregarded because PED was insufficiently capitalized.
- (B) ARod's use of corporate vehicles to shield himself from personal liability is per se fraudulent behavior.
- (C) ARod did not respect PED's corporate formalities, which resulted in ARod and PED having a master/servant relationship.
- (D) ARod did not respect PED's corporate formalities, which resulted in ARod treating PED as a *de jure* corporation.

Questions 14 and 15 are based on the following fact situation:

Paula is a film producer who runs Xanadu Movie Productions Inc. ("Xanadu"). Paula has the authority to make all hiring decisions on behalf of Xanadu. Paula hired Amy as project manager for an upcoming movie. During a Monday morning meeting, Paula says to Amy, "Go out and hire a camera person. Get somebody really good. We need to get this done this week."

The very next day, and without any further consultation with Paula, Amy hires Tom. Tom is one of the best camera people in the business. Amy uses Xanadu's standard employment agreement, fills in Tom's compensation of \$50,000 for the project (which is the standard fee for this type of camera work) and signs the agreement (the "Employment Agreement") on behalf of Xanadu. Tom also signs the Employment Agreement. After the Employment Agreement is signed, Amy tells Paula. Paula is furious, and says, "I hate Tom. He is not hired. I am not using him on the film and I am not paying him."

14. If a court finds that Xanadu is contractually bound under the Employment Agreement, which of the following statements provides the most likely explanation?
- (A) Amy had actual implied authority to enter into the Employment Agreement on behalf of Xanadu.
 - (B) Amy had apparent authority to enter into the Employment Agreement on behalf of Xanadu.
 - (C) Amy had inherent agency power to enter into the Employment Agreement on behalf of Xanadu.
 - (D) Xanadu is contractually bound under the Employment Agreement under the doctrine of agency by estoppel.
15. If a court finds that Xanadu is NOT contractually bound under the Employment Agreement, which of the following statements provides the most likely explanation?
- (A) Because Xanadu was a fully-disclosed principal, Tom was on notice to verify Amy's actual authority.
 - (B) The doctrine of inherent agency power is generally applicable only in the case of undisclosed principals.
 - (C) Amy lacked authority to enter into the Employment Agreement.
 - (D) Xanadu failed to expressly ratify the Employment Agreement.

Questions 16 and 17 are based on the following fact situation:

Harold operated an herbal supplement shop, at which Kumar worked as the receptionist. Kumar demanded an increase in his weekly wage of \$500. Harold countered with an offer to make Kumar a partner. Kumar liked the idea, so Harold and Kumar entered into a written agreement that provided:

- The parties shall associate themselves to operate a business called "We're Not Low" (WNL)
- Kumar shall make no capital investment in the business
- All control and management of the business shall be vested in Harold
- Harold alone is to be liable for debts of the business
- Kumar is to act as cashier and receptionist at a salary of \$500 per week and a bonus at the end of the year of 20% of the net profits
- Harold shall receive a salary of \$2,000 per week and a bonus at the end of the year of 80% of the net profits
- The business arrangement shall continue until either party gives ten days' notice of termination

Harold and Kumar operated under this agreement for a number of years. Harold and Kumar never filed partnership income tax returns, but did tend to refer to each as "partners."

One day, Harold caught Kumar improperly taking money from the cash register. Harold told Kumar he was "fired," and kicked him out of the store. On his way out of the store, Kumar yelled, "You can't just fire me. I'm a partner. I better get my share of the business."

In answering these questions, please assume that the Uniform Partnership Act applies.

16. Harold asserts that WNL was not a partnership under the law. Harold claims that Kumar was a mere employee of WNL. Which statement provides an accurate description of whether Harold and Kumar were "partners" in a legal sense?
- (A) Because Harold and Kumar were sharing profits, WNL was definitely a partnership.
 - (B) Because Harold maintained all control over WNL's business, bore all losses, and contributed all of the capital to the business, WNL was definitely not a partnership.
 - (C) Because Harold and Kumar were sharing profits and referred to each other as partners, WNL was definitely a partnership.
 - (D) None of the above.

17. If you could advise Harold about how best to terminate Kumar, which of the following statements provides the best advice?
- (A) Because there is a risk that WNL is a partnership, Harold should make certain that his termination of Kumar does not violate the partnership agreement.
 - (B) Because there is no chance that WNL is a partnership, Harold can freely terminate Kumar as an at-will employee.
 - (C) Even if WNL is a partnership, Harold can freely terminate Kumar as an at-will partner.
 - (D) Because there is no chance that WNL is a partnership, Harold can terminate Kumar as an at-will employee. Moreover, because Kumar stole money from Harold, Kumar should not be able to claim that his firing was in violation of an implied duty of good faith and fair dealing.

Question 18

Hillary is a serial entrepreneur who has developed a number of successful start-up companies. Hillary just finished the business plan for her latest venture and plans on forming a corporation soon. Prior to forming the corporation, however, Hillary was presented with an opportunity to sign a 5-year lease (the "Lease") that Hillary found enticing for her new venture. Hillary told the Landlord that she was signing the Lease on behalf of Khosla Corp. ("Khosla"), a corporation that was "to be formed," and the Lease reflected this fact. A few weeks after the Lease was executed, Hillary formed Khosla, which immediately moved its operations into the leased premises. Khosla also paid the rent called for under the Lease. Khosla's board of directors, however, never took any formal action regarding the Lease.

Roughly six months after the Lease was executed, Landlord decided that it was not happy with the Lease. Commercial rental prices have increased substantially in the last six months, so Landlord would like to get out of the Lease so that it can re-lease the premises for a better price. What is the most accurate statement regarding the Landlord's ability to get out of the Lease?

- (A) Because Khosla did not formally adopt the Lease, Landlord can treat the Lease as an offer that Khosla never accepted. As a result, Landlord can rescind its offer and be free from the Lease.
- (B) Promoters can bind their future corporations to contracts. As a result, it is highly unlikely that Landlord can get out of the Lease.
- (C) If Hillary had agreed to be personally bound under the Lease, then Landlord would have been prevented from getting out of the Lease. Since Hillary did not agree to be personally bound, Landlord is free to get out of the Lease.
- (D) None of the above.

Questions 19 and 20 are based on the following fact situation:

Eric is a well known collector of baseball cards. Eric recently learned that Seller was in possession of a Barry Bonds rookie baseball card and that Seller would be interested to sell it for \$400. Eric very much wanted to acquire the card, but he did not want his identity known to Seller for fear that Seller would substantially increase her asking price for the card if she knew that Eric were the buyer. As a result, Eric hired Karen to act as his agent to purchase the card. Eric gave Karen explicit instructions on how to make the offer, when to make the offer, and how much to pay for the card. Eric also instructed Karen not to disclose Eric's identity when making the purchase, and instead to simply state she was making the purchase on behalf of an "interested party."

Karen followed Eric's instructions and entered into an oral agreement (the "Agreement") with Seller pursuant to which Seller promised to deliver the baseball card and Karen promised to deliver the \$400 from the "interested party." The exchange was to take place on March 15th. On March 15th, Seller showed up with the baseball card, but Karen did not have the \$400. It turns out that Eric changed his mind and no longer wanted to buy the Barry Bonds rookie baseball card.

19. What is the most correct statement regarding whether Eric is liable under the Agreement?
- (A) Eric is an undisclosed principal and he will be liable under the Agreement if a court finds that Karen had authority to enter into the Agreement.
 - (B) Eric is a partially-disclosed principal and he will be liable under the Agreement if a court finds that Karen had authority to enter into the Agreement.
 - (C) Eric has sufficient control over Karen's behavior to create a master/servant relationship. As a result, Eric will be liable under the Agreement.
 - (D) Eric does not have sufficient control over Karen's behavior to create a master/servant relationship. As a result, Eric will only be liable under the agreement if Karen had authority to enter into the Agreement.
20. What is the most correct statement regarding whether Seller can hold Karen liable under the Agreement?
- (A) Seller cannot hold Karen liable under the Agreement.
 - (B) Seller should be able to hold Karen liable under the Agreement based on apparent breach of the implied warranty of authority.
 - (C) It is inferred that Karen will be liable under Agreement unless she disclaimed such liability to Seller prior to entering into the Agreement.
 - (D) Karen should not be liable under the Agreement unless Eric and Karen intended for such liability.

Question 21

Jen and Harry are both ice cream entrepreneurs and social activists. Jen and Harry created a corporation, Jen & Harry Inc. ("J&H"), that now has millions of shareholders. J&H has a three-part mission that considers profits as only one measure of success – and not the "highest" measure of success. The three parts of J&H's mission are:

1. **Social Mission:** J&H shall operate in a way that recognizes its influence on society, and the importance of improving the quality of life all over the world.
2. **Product Mission:** J&H will always strive to make the finest quality products, working to use natural, wholesome ingredients that respect the Earth.
3. **Economic Mission:** J&H shall operate on a sustainable financial basis of profitable growth. But, profit motives are not to interfere with J&H's social or product missions, nor are profit motives to interfere with J&H's healthy relationships with its employees and the local community.

Dodge v. Ford provides the classic statement on the fundamental purpose of corporations:

"A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of the directors is to be exercised in the choice of means to attain that end, and does not extend to change in the end itself . . ."

Please assume that Dodge v. Ford is good law in J&H's state of incorporation. Is J&H's mission legally permissible? What is the most correct statement?

- (A) J&H's mission is not legally permissible because it is ultra vires.
- (B) J&H's mission could be legally permissible if shareholders were given proper notice of the mission before investing in J&H. It would be best if the mission were included in the certificate of incorporation.
- (C) J&H's mission is unlikely to be legally permissible. The purpose of corporations is to pursue profits, not humanitarian agendas.
- (D) J&H's mission is likely legally permissible because pursuing a humanitarian agenda is likely in the best interests of the shareholders.

Questions 22 and 23 are based on the following fact situation:

Brad and Jen entered into an oral agreement whereby they contracted to become partners in the operation of a restaurant. The parties did not expressly fix any definite period of time for the duration of this undertaking. For the purpose of purchasing necessary restaurant equipment, Jen loaned \$100,000 to the partnership, with the understanding that the loan was to be repaid to Jen out of the prospective profits of the partnership as soon as the partnership could reasonably do so.

Shortly after formation of the partnership, it became clear that Brad and Jen would have trouble co-existing as partners as they had fundamentally different views on how to operate the partnership and general disharmony. In particular, Jen persisted on being the dominating figure of the enterprise and frequently took to humiliating and belittling Brad in front of the restaurant employees. Jen also refused to do any work (claiming she had not worked in 30 years and she didn't plan to start now) and she took small sums of money from the partnership without Brad's knowledge or consent. Finally, Brad and Jen had fundamental differences on how the partnership should operate. Brad offered to buy out Jen's interest, but Jen refused.

22. Brad would like to dissolve the partnership. Does Brad have the right to kick Jen out of the partnership? What is the most accurate statement?
- (A) Because the partnership is an "at-will" partnership, Brad has the right to dissolve the partnership with impunity.
 - (B) Brad must show that Jen was in breach of the partnership agreement in order to dissolve the partnership.
 - (C) Of course Brad can dissolve the partnership. The relevant question is not whether Brad can dissolve the partnership, the more relevant question is whether Brad can dissolve the partnership without breaching the partnership agreement.
 - (D) Of course Brad can dissolve the partnership. Based on the facts in the question, however, it is highly unlikely that Brad can dissolve the partnership without breaching the partnership agreement.
23. Why might Brad decide to seek a dissolution by decree of court? What is the most accurate statement?
- (A) A court decree is always required to dissolve a partnership.
 - (B) A court decree ensures against a charge that Brad's dissolution is in contravention of the partnership agreement.
 - (C) A court decree is required to break the deadlock between Brad and Jen since each holds 50% of the partnership's voting rights.
 - (D) Brad does not need to seek a dissolution by decree of court. It is a waste of resources for Brad to seek such a dissolution since the partnership is an "at will" partnership.

Questions 24 and 25 are based on the following fact situation:

A venture capital firm decided to form a limited partnership (the "LP") in order to raise money to invest in high-technology start-up companies. The structure of the LP would be as follows:

- A corporation would be created to serve as the general partner; and
- Investors in the LP would be brought in as limited partners

The venture capital firm would like your advice on the legality/consequences of the structure.

24. Will the LP be a legally-permissible limited partnership? What is the most accurate statement?

- (A) No.
- (B) Yes.
- (C) No. Legal entities cannot serve as general partners. Only human persons can serve as general partners for a limited partnership.
- (D) Yes. So long as all the formalities are followed for forming a limited partnership (e.g., a certificate of limited partnership is filed in the office of the Secretary of State), there is nothing about the proposed structure that sounds troubling.

25. Assuming that the LP is a valid limited partnership, what would be the liability exposure for the general partner and the limited partners? What is the most correct statement?

- (A) The general partner is personally liable for the obligations of the limited partnership. The limited partners have limited liability (i.e., their liability is limited to the amount of their investment in the partnership, which they may lose) so long as they do not participate in the control of the business of the partnership.
- (B) Because the general partner is a limited-liability entity, the limited partners are personally liable for the obligations of the limited partnership.
- (C) The general partner is personally liable for the obligations of the limited partnership. The limited partners have limited liability (i.e., their liability is limited to the amount of their investment in the partnership, which they may lose) regarding any contractual obligations. Limited partners have joint and several personal liability, however, for any tort obligations of the partnership.
- (D) None of the above.

Question 26

Large corporations frequently use a “quarantine” strategy when acquiring new businesses. The acquisition by Bristol-Myers of Medial Engineering Corp. in the In re Silicone Gel Breast Implants Product Liability Litigation is a good example of the strategy. The large corporation does not merge the new business into the large corporation, but instead holds the new business as a 100%-owned subsidiary. That means the large corporation is a shareholder of the new business. The goal of this quarantine strategy is to provide the large corporation with the benefits of shareholder limited liability.

In class, I explained that the parent corporation “respecting corporate formalities” for the 100%-owned subsidiary can greatly strengthen the success of a “quarantine” strategy – i.e., it strengthens the corporate shield.

Which of the following statements does NOT help to explain why “respecting corporate formalities” is important to the “quarantine strategy”?

- (A) Respecting corporate formalities helps to prevent a court from finding that the large corporation and the 100%-owned subsidiary have a principal/agent relationship.
- (B) Respecting corporate formalities helps to prevent a court from finding that the 100%-owned subsidiary is the “alter ego” of the large corporation.
- (C) Respecting corporate formalities helps the large corporation to demonstrate that its actions with the 100%-owned subsidiary are not ultra vires.
- (D) Respecting corporate formalities helps to show a separate existence between the large corporation and the 100%-owned subsidiary.

*** * * * * END OF EXAM * * * * ***

