Kern County College of Law

Business Organizations I Examination

Fall 2025

Prof. J. Harvey

Instructions:

Answer three (3) essay questions. 100 points per question.

Time Allotted: Three (3) hours.

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Question 1

Sarah and Tom have been friends since college and both work in the landscaping industry. In March 2024, they met for coffee and Sarah proposed that they "go into business together" doing high-end residential landscape design. Tom agreed, and they shook hands on the deal. They agreed to split profits 60-40, with Sarah taking the larger share because she would contribute more initial capital. Over the next two months, Sarah purchased $15,000 worth of design software and equipment using her personal credit card. Tom began meeting with potential clients and secured three contracts, signing them "Tom Chen, Green Spaces Design" without consulting Sarah.

In May, Tom entered into a $40,000 contract with the Johnsons to redesign their backyard, including installing a koi pond and imported Japanese maples. He told the Johnsons he was "one of the owners of Green Spaces Design." Tom never discussed this contract with Sarah. When Sarah learned about it, she was furious because they had never taken on such a large project and she believed Tom lacked the expertise for water features. She immediately called the Johnsons and told them Tom had "no authority" to enter into the contract and that Green Spaces Design would not perform the work. The Johnsons have now sued both Sarah and Tom for breach of contract, seeking $25,000 in damages. Meanwhile, Sarah is demanding that Tom reimburse her for half of the $15,000 she spent on equipment.

1. **Can the Johnsons enforce the contract? If so, against who and why? Explain your analysis.**
2. **What is likely to be the result if Tom refuses to reimburse Sarah and she sues? Explain your analysis.**

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Question 2

Martinez & Associates is a general partnership consisting of three partners: Elena Martinez, David Wu, and Jennifer Ross. The partnership agreement, signed in 2023, states that partnership decisions require a majority vote and that partners will devote their "primary business efforts" to the partnership. The partnership specializes in providing IT consulting services to mid-sized manufacturing companies in the Midwest.

In September 2024, Elena was approached by Apex Manufacturing, a longtime client of the partnership, about a lucrative opportunity to develop a proprietary software system for managing Apex's supply chain. Elena believed this project was outside the partnership's usual scope of work and would require her to learn new programming skills. Without informing David or Jennifer, Elena agreed to do the project personally for a $200,000 fee, which she would receive over twelve months. Elena worked on the Apex project during evenings and weekends. In November, David discovered the arrangement when he ran into an Apex executive at a conference. David and Jennifer are now demanding that Elena turn over all fees received from Apex to the partnership.

Elena argues that she acted properly because: (1) the project was outside the partnership's expertise, (2) she worked on it during her own time, and (3) David and Jennifer would have voted against taking it on anyway since it would have required hiring additional staff. David and Jennifer maintain that any opportunity arising from a partnership client belongs to the partnership.

1. **Suppose you are a newly-hired associate at a law firm. David and Jennifer come to you for assistance. Do they have a claim? If so, against who and on what basis? Who would be the appropriate plaintiff and why? Explain your analysis.**

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Question 3

Baker & Sullivan was formed as a general partnership in 2020 by childhood friends Alice Baker and Mike Sullivan, with the stated goal of operating a craft brewery. They had no written partnership agreement. Each contributed $50,000 initially and agreed to share profits equally. The brewery became moderately successful, generating about $120,000 in annual profits. In January 2024, Alice told Mike she wanted to "retire from the partnership" and pursue other interests. Mike said he wanted to keep the brewery running and offered to pay Alice $50,000 for her interest—the amount of her initial contribution. Alice rejected this offer, stating that her interest was worth much more given the brewery's profitability and that the partnership property, including the customer list and brand name, should be sold to determine the true value.

In March 2024, while Alice and Mike were arguing about the terms of her departure, Mike signed a two-year supply contract with Hop Growers Co-op worth $180,000. He never told Alice about this contract. In April, Alice learned about the contract and told Hop Growers that the partnership was "dissolved" and therefore the contract was void. Hop Growers has now sued the partnership for breach of contract.

Meanwhile, Mike has been operating the brewery and taking the full amount of profits for himself since February, claiming that Alice "quit" and therefore has no right to ongoing profits. Alice is demanding an accounting and claims she is entitled to half of all profits earned through the date the partnership is formally wound up.

1. **Has the partnership been dissolved? If so, when did dissolution occur? Explain your analysis.**

2. **Is the partnership bound by the March 2024 contract with Hop Growers? Why or why not? In your answer, analyze:**

   (a) whether Mike had actual authority to enter the contract,
   (b) whether Mike had apparent authority to bind the partnership, and
   (c) whether it matters that Hop Growers had no knowledge of Alice's intention to leave the partnership.

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1)

Question 1:

The Johnsons can enforce the contract against Sarah, Tom, and Green Space Designs because Tom acted with implied and apparent authority when he contract with the Johnsons.

General Partnership

A general partnership is formed when two or more people form an agreement to start a business for profit. These agreements can be express or implied and do not require any specific formalities. A verbal agreement will suffice. In order to meet the RUPA standards of a partnership, the partners would have to: (1) agree on how to share profits (2) agree on how to share losses (3) mutually agree on management and control and (4) there must be a community interest in the venture. General partnerships do not shield partners from liability. General partners are liable for the partnerships contracts, torts, and losses. If there is a suit against a partnership and the partnership can not pay, the partner's personal assets could be used to pay.

The facts state that Sarah and Tom share experience in the landscaping industry. With this in common, they had a meeting where Sarah made and Tom accepted a business proposition. Although it was not formal, Sarah and Tom expressly agreed to start a business together that they hoped would be profitable doing high-end residential landscape design. An unofficial, verbal agreement is sufficient to start a general partnership. Sarah and Tom also agreed they would split the profits of their venture with Sarah getting a larger share (60), and Tom getting a smaller share (40). The facts do not indicate that Sarah and Tom entered into an agreement as to how to share the losses of the business however, the law states that if the agreement is silent as to the losses, the partnership will split the losses in the same manner as they split the profits.

Sarah and Tom have formed a general partnership. They are each partners and are each liable for the contracts, torts, and losses of the partnership.

Agency

An agency relationship exists where an agent and a principal mutually assent to the relationship, there is benefit to the principal, and the principal maintains control over the agent's actions. An agent owes a duty of care, duty of loyalty, and a duty to disclose to the principal.

Based on the facts, Tom and Sarah are both agents of the partnership they just formed, Green Space Designs. Tom and Sarah both agreed to work together and took on roles to further the buisness. The work that Sarah and Tom are doing is benefiting the business/principal, Green Space Designs, and not Sarah and Tom individually. The principal controls Sarah and Tom's actions and is bound by them. Here, both Sarah and Tom owe a duty of care to the business meaning they must act in the best interest of the business. They also owe a duty of loyalty meaning they must not work against the principal and in favor of a third party. They also must disclose to each other what is going on with the business.

An agency relationship exists between Tom, Sarah, and their principal, Green Spaces Design.

Authority to Bind

Authority can be actual or apparent. Actual authority can be express or implied. Actual express authority exists when a principal expressly gives authority to an agent verbally or in writing. Actual implied authority exists when the agent believes they have authority because they are doing things that are necessary to complete their duties. Also, implied authority can exist based on custom or past acts of the agent that the principal has approved of. Apparent authority exists when a third party reasonably believes the agent has authority because the principal has cloaked the agent with the appearance of authority.

A principal can be bound to an agents acts when authority actual authority (express or implied) is present. A principal can also be bound if apparent authority exists however, if the agent was acting outside of their actual authority, they will have to indemnify the principal for any loss caused by their actions.

Tom entered into a 40k contract with the Johnsons to redesign their backyard, including installing a koi pond and imported Japanese maples. During contract negotiations, Tom stated that he was "one of the owners of Green Spaces Design." Based on the analysis above, we know that Tom is a partner and an agent of Green Space Designs. As a partner, Tom has implied authority to bind the partnership to an agreement that is within the normal scope of business that the partnership partakes in. When Tom contracted with the Johnson's he had already secured contracts with three other potential clients. The facts state that Sarah was not consulted when the contracts were signed but the facts are silent as to whether Sarah was aware of these contracts after they were secured. If Sarah found out about the contracts later, and did nothing to try to rescind the contracts, Tom could see this as a ratification of his acts. If Sarah ratified Tom's acts in the past, he has a strong

argument for having implied authority in his dealings with the Johnsons.Tom acted with implied authority when he signed the contract with the Johnsons.

Sarah will likely attempt to argue that Tom did not have authority to contract on behalf of Green Space Designs because he did not consult her first. She will state that Tom's actions were not in the usual course of business because the contract for 40k was much larger than any other project they had ever worked on. Also, Tom did not have the expertise for water features meaning that they could not properly complete the project.

The Johnson's are seeking to enforce the contract and they have a great argument to do so. In addition to the implied authority that Tom had, the Johnson's will argue that Tom had apparent authority as well. Tom stated that he was one of the owners of Green Spaces Designs which would reasonably indicate to the Johnsons that Tom had the authority to contract with them. This means that Tom bound the partnership and they are liable to the Johnsons. The Johnson's can enforce the contract and sue for breach of contract.

Based on the analysis above, the Johnson's can enforce the contract because Tom was acting with implied and apparent authority when he entered into contract with the Johnsons. If the partnership can not pay for the breach of contract suit from the Johnson's, a court can order a judgement against Tom and Sarah's personal assets to make the Johnson's whole.

Question 2:

Sarah will likely win in a suit against Tom to collect a portion of her $15k in expenses because they were a purchase on behalf of the partnership they shared. However, if Sarah tries to sue Tom for losses from the Johnson suit, she will fail.

As stated above, Tom and Sarah, as co-partners, were agents of the partnership and had the implied authority to bind the partnership in contracts and purchases that were in the normal course of business for their partnership. The facts indicate that Sarah spent $15k in design software and equipment using her personal credit card. These expenses seem reasonable and are within the normal course of the partnership business because Sarah and Tom were starting a new high-end landscaping business from scratch. The software and equipment would help the business be profitable.

A partnership agreement dictates how profits are shared and losses are shared within a partnership. The facts do not state exactly how the expenses or losses of Tom and Sarah's partnership would be shared but the law states that if their agreement was silent regarding the losses, they would be

shared in the same way the profits are. Sarah was to take 60% of the profits because she was contributing more initial capital and Tom would take 40% of the profits.

Sarah will have to pay 60% of the $15k that she contracted for because that is her share of the losses/expenses of the business. Tom will have to pay 40% of the $15k that Sarah spent because that is his share of the business.

If Sarah attempts to sue Tom for indemnity regarding the Johnson's breach of contract claim, her argument will fail. This is so because Tom had authority to bind the partnership and Sarah's actions caused a breach of that contract.

2)

General Partnerships

A general partnership consists of two or more individuals who act as co-owners for a business for profit and do not meet any other requirements for another form of association. They equally share profits, losses (proportional to their contribution), and controlling and managing the partnership. As a partnership they owe fiduciary obligations to the partners and partnership as its own entity (duty of loyalty, care, and obedience which will be defined in the analysis). The partnership can be created **at will** (both the partners enter into a partnership with no duration specified), by a **definitive term** (for a specific duration), or by j**oint venture** until the completion of the specific particular undertaking). The partnership can also be created impliedly, expressly, or written in the **partnership agreement.**

Here**,** there is a partnership at will since there is no definitive term nor is there a particularized undertaking. There was a written partnership agreement that bound the partnership to their specific obligations and duties to each other and their partnerships. Therefore, there is a general partnership at will where there is an existing written partnership agreement that requires majority vote of partner for conducting new business and requiring primary business efforts to the partnership. Thus any breach of those agreements is not in compliance to the partnership agreement.

Agency:

An agency relationship is created if there is an agent (a) the person who is acton in behalf of or for the principal (P) who is the individual whom the agent is acting in behalf of. The agent and the principal must have capacity to enter into the agency relationship through mutual assent, meaning that both the P and the A have mutual manifestations to enter into the agency relation where the A acts for the P's benefit and is subject to the P's control. Much like the general partnership, there are fiduciary obligations of duty of loyalty, care, and obedience.

Here, there is general partnership relationship between all three partners. However, there was an agency relationship between Elena and Apex since Elena was acting for the benefit and control of Apex where there was mutual assent by both parties. Thus there is an agency relationship between Elena and Apex.

Authority:

Actual Authority- occurs either by express or implied. expressed actual authority exists if the partners were given an oral or written instructions. Implied exists if the partner/Principal had reason to believe they had authority based on the P's conduct or manifestations.

Inherent Authority: the agent reasonably inferred they had authority to act based on the specific agency relationship established.

Apparent Authority occurs based on the outwards perceptive of the third party. The third party reasonably believed that the agent had actual authority based on the P's conduct or manifestations.

Estoppel Authority: where a third party reasonably believes that the agent has authority to act, the principal carelessly permits the act, and the third party has detrimentally relied.

Here, Elena has actual authority to only conduct business for Martinez and Assoc. as stated per their partnership agreement. She stated there was no actual not apparent authority to conduct business with Apex per authority granted by the partnership. However, there can be an argument made by Apex that hiring Elena was within the scope of her apparent authority, and there can be an argument made that Elena and Apex had an agency relatioiinship where there was actual authorty. (see analysis below)

1. David and Jennifer v. Elena (Martinez & Associates) for Breach of Fiduciary Duty of Loyalty, Care, and Obedience

Here, David, Jennifer, and Elena entered into a partnership entered into a written partnership agreement where they explicitly stated that any decisions of the partnership would require a majority vote and that they are to devote their "primary business efforts" to the partnership. Every partner owes their partners and their partnership the **fiduciary duties of care, loyalty, and obedience.** Duty of loyalty signifies that the partners must not act adversely to the other partners or partnership and not compete. Duty of care signifies that the partners must act as carefully, diligently, and competently as any reasonable partner would. Duty of Obedience means that the partner must obey all legal obligations and not go beyond the scope of their duty.

Breached Duty of Loyalty:

Elena broke her fiduciary **duty of loyalty** by competing adversely with her partnership with Jennifer and David. She argues that the work was outside of the partnerships usual scope of the work, and she had to learns different programming skills. She states that the project was outside of the partnership's expertise, she worked on her own time, and her other partners would have voted

against her wishes. She may argue that she is able to conduct her own separate business outside the scope, but she is NOT entitled to individual benefits. Elena was not loyal to her other partners in Martinez & Assoc. because she conducted business with an already existing client for her own benefit, not for the benefit of the partnership as a whole. David and Jennifer could argue that Elena was unloyal to the purpose of the partnership which was to be put their primary efforts to the business. In addition, she decided to selfishly contract with an existing client of their partnership to individual benefit from a separate and secretive business. Any benefit she retained with her business from Apex Manufacturing is to be be fully given back to the entire partnership. In addition, she was also contracting and creating an agency relationship with Apex where she is subject to there control and working for their benefit (which is alos agasint her loyalty to Maritnez and Assoc).

Despite Elena not conducting with Apex within the scope of the business, she breached her duty of loyalty by working adversely with an already existing client of Martinez & Associates.

Breached Duty of Care:

Elena breached **her duty of care** by failing to act as carefully, diligently, and competently as any other partner would. Elena was to behave as a reasonable partner would in her circumstance. Here she did not. She conspired to work with an already existing client of Maritnez and Assoc. therefore, not acting as a diligent or competent partner. She could argue that she was careful in not letting her obligations to this secret venture with Apex Manufacturing not interfere with her partnership obligations to Martinez and Assoc. She worked on weekends and evening while not on the clock at Martinez & Assoc. However, she breached her duty of loyalty and obedience (below) by not devoting her primary efforts to Martinez and Associates. Instead of working on a secret venture with Apex, she could have devoted her full attention to her already existing obligation to Martinez and Assoc. In addition, she was not acting careful, since she evidently was discovered working secrelty with an already existing client, which is besides the point.

Therefore, Elena breached her duty of care by not being careful or a reasonable partner and conducting business with an already existing partner.

Breached Duty of Obedience:

Elena also breached her **duty of obedience** by not complying to the terms of their written partnership agreement and superseding the majority vote requirement. Here, Elena breached her duty of obedience by going against their partnership agreement. Any decisions required a majority vote, which she did not do, and she was to focus primarily on the business, which again she did not

do by conspiring with an already existing client. She disobeyed her contractual obligation and her fiduciary obligations to her partnership with David and with Jennifer. Therefore, any individual benefits that she retained while conducting work for Apex is to be given to Martinez and Assoc and will be apportioned equally among David, Jennifer, and Elena.

In conclusion, Elena had breached her fiduciary duties to David and Jennifer, and the partnership as a whole, thus any benefits she retained individually ($200,000) is to be given to Martinez & Associates and will be distributed proportionally.

2. David and Jennifer v. Apex Manufacturing will be <u>unsuccessful</u>

Agency Relationship and Authority between Apex and Elena

Here, Jennifer and David do not have a claim against Apex because they are not a partner to Martinez & Assoc. However, they may argue that Elena had apparent authority to act on behalf of Martinez and Assoc. to help Apex with their proprietary software since she is a partner to the Martinez and Ass, whom they already have an existing contractual relationship with. They can argue that they simply asked Elena, had **apparent authority** based on their reasonable belief that she had **actual authority** to conduct business with them for consulting services for manufacturing companies (which is within the partnership's conduct). Here, however, Apex approached Elena, on her own, without consulting the entire partnership first, and entered into their own contractual agreement. Therefore, there any argument made for apparent authority is moot since Apex knew that the other partners were not aware of this service. There is however, an existing **contractual obligation** of **actual authority between Elena and Apex** since they entered into an agency relationship where she is subject to Apex control and working for their benefit.

In conclusion, David and Jennifer (Martinez & Assoc.) have no claim against Apex, only Elena, as they are not a partner to Martinez and Assoc, but they may recover and proportionally distribute the 200,000 given to Elena.

3)

The partnership has not been officially dissolved because that is a process that has not been completed. The dissolution began when Alice notified Mike that she wanted to retire from the partnership.

The partnership is bound by the March 2024 contract with Hop Growers. There was apparent authority that Mike could still act on behalf of the partnership. Hop Growers were not aware of Alice's desire to end the partnership and therefore they reasonably relied on the apparent authority.

General Partnership

A general partnership is formed when two or more people form an agreement to start a business for profit. These agreements can be express or implied and do not require any specific formalities. A verbal agreement will suffice. In order to meet the RUPA standards of a partnership, the partners would have to: (1) agree on how to share profits (2) agree on how to share losses (3) mutually agree on management and control and (4) there must be a community interest in the venture. General partnerships do not shield partners from liability. General partners are liable for the partnerships contracts, torts, and losses. If there is a suit against a partnership and the partnership can not pay, the partner's personal assets could be used to pay.

Here, Alice and Mike agreed to start a craft brewery for profit. Although they did not have a partnership agreement, this is not required to form a general partnership. They had a verbal agreement which is sufficient to form the partnership. Alice and Mike agreed to share profits equally and they each contributed $50k to get the business started. If the agreement is silent as to how to share the losses, the partnership will share the losses in the same way they share their profits, in this case 50/50. It can be assumed that Alice and Mike agreed that they would both manage and control the business. Communities generally have an interest in business like a craft brewery because it can lead to jobs and can also be a great place for communities members to patron.

The general partnership was formed and both Alice and Mike, as well as the partnership are liable for the partnerships contract, torts, and losses. There is no shield for liability for the partners in a general partnership.

Partnership Duties

Partners have a fiduciary duty to each other and to the partnership. Partners have a duty of care, duty of loyalty, and a duty to not compete with the partnership or usurp partnership business opportunities.

Here both Alice and Mike were bound by these duties. They had to pursue buisness ventures for the benefit of the partnership and not compete with the partnership. They also had a duty to comply with the partnership agreement.

Agency

An agency relationship exists where an agent and a principal mutually assent to the relationship, there is benefit to the principal, and the principal maintains control over the agent's actions. An agent owes a duty of care, duty of loyalty, and a duty to disclose to the principal.

Mike and Alice are both in a fiduciary relationship with each other and the partnership/Brewery which is the principal in this situation. Mike and Alice are both working to benefit the brewery by investing in it and generating 120k in annual profits. Mike and Alice must demonstrate a duty of care and loyalty to the brewery and they must disclose all information regarding the partnership to each other.

Authority to Bind

Authority can be actual or apparent. Actual authority can be express or implied. Actual express authority exists when a principal expressly gives authority to an agent verbally or in writing. Actual implied authority exists when the agent believes they have authority because they are doing things that are necessary to complete their duties. Also, implied authority can exist based on custom or past acts of the agent that the principal has approved of. Apparent authority exists when a third party reasonably believes the agent has authority because the principal has cloaked the agent with the appearance of authority.

A principal can be bound to an agents acts when authority actual authority (express or implied) is present. A principal can also be bound if apparent authority exists however, if the agent was acting outside of their actual authority, they will have to indemnify the principal for any loss caused by their actions.

In this case, Mike will argue that he had authority to bind the partnership because all partners have implied authority. Mike has likely entered into contracts to benefit the partnership in the past and these actions have been ratified by the partnership. However, Mike knew of Alice's wishes so he

was acting outside of the scope of the authority he held with the partnership at this time (see analysis below).

Based on the facts above Hop Growers, the third party in this case, would have reasonably believed that the agent, Mike, had authority to contract on behalf of the partnership because he was one of the owners of the brewery. At this time, there are no facts to indicate that Alice announced to the community that she was interested in dissolving the partnership. Therefore, Hop Grower's reasonbly believed that Mike still had authority and the Brewery could take on new business.

The partnership is bound by the March 2024 contract with Hop Growers based on apparent authority. The fact that Hop Growers was unaware of Alice's desire tot end the partnership matters because they had no reason to know that Mike did not have the authority to bind the partnership. If the partnership fails to follow through with this contract, Hop Growers could bring a claim for breach of contract. If they are found liable by a court, the partnership would have to pay Hop Growers. However, Alice would be able to seek indemnification from Mike as he was acting outside of authority because they partnership should have been winding up and not taking on any new business.

Dissolution

If a partnership agreement does not state how or when the partnership should be dissolved, it is an at-will partnership that will continue in perpetuity until any or all of the partners decide to not conduct business together anymore. A partner has the authority to dissociate from the partnership and dissolve the partnership. Dissolution is a legal process that partnership must go through when the partnership is coming to an end. At dissolution, the business is no longer engaged in the normal course of business. This means that the partnership can not take on any new business; they must wrap up old business and only engage in the business of winding up. During this time, partners lose the authority to bind the partnership with any new business that is not winding up. When winding up, the partnership assets may be liquidated and the funds go to pay outside creditors, inside creditors, and partner capital contributions in that order. If there is anything else left, the partners divide the value based on their partnership agreement. If the partnership can not afford to pay all of their creditors, the partners may be held personally liable to pay for the partnership debts.

Here the facts state that Alice told Mike that she wanted to "retire from the partnership" and pursue other interests. Alice began the process of dissociating from the business when she expressed this information to Mike. These words began the dissolution process of the partnership. A partner, Alice, has the authority to dissolve the partnership absent an agreement to the contrary. Even if Alice and

Mike had contracted on how to dissolve the partnership, Alice could still dissolve it my unequivocally stating her desire to do so. However, Alice would be subject to a breach of contract claim in that instance.

At this point Mike and Alice did not have the actual authority to bind the partnership in a new agreement. They had to wrap up old business and only engage in winding up the partnership (i.e. liquidating assets, paying creditors, etc.) Mike was acting outside of the scope of his authority when he contracted with Hop Growers. Even if Mike wanted to continue the venture without Alice, he would have had to dissolve the partnership first then start new again because Alice did not agree to share her interest for only 50k. Buisness acquire goodwill and her share of the business would likely be much higher than 50k. If Alice did not want to carry on the buisness, the partnership had to be sold and wound up and the profits shared amongst Mike and Alice equally after paying off any outside creditors and returning both of their initial investments.

END OF EXAM