

Business Associations Fall 2020 midterm assignment: draft memo

The question asks you to discuss the legal issues raised by the facts described, giving your reasoning, and, in particular to answer the questions: 1. Who has the right to decide whether or not to accept Elly's offer to acquire a half interest in the business? And 2. What issues are raised by Billy's interactions with XYZ Media and what can Ally do about these issues?

Question 1.

For question 1, we need to think about the legal characteristics of the relationships between the various parties. The facts describe a relationship in which A and B agree to work together to raise money to buy a business, run it for a few years, and then sell it. They borrow money from C and D in return for a market rate of interest and a share of profits (for which they might need to wait). A and B seem to have formed either a joint venture or a partnership. They are either carrying on as co-owners a business for profit under RUPA §202 or involved in a more limited relationship as in *Sandvick v La Crosse* or *Meinhard v Salmon*. But, bearing in mind that *Owen v Cohen* suggests that you can have a partnership for a term for the achievement of a particular objective (here getting to the point of being able to sell the restaurant business) I think the argument that there is a partnership between A and B is a strong one.

C and D may also be partners, as co-owners of the business for profit (e.g. *Martin v Peyton*). In addition to sharing in profits they go to the restaurant regularly and promote it on their social media. This is much less clear than the situation with respect to A and B. But it matters in terms of decisionmaking. If A and B are the partners, under RUPA default rules they would have an equal say in the management of the business and therefore all decisions about changes in the business (not otherwise within the authority of a particular partner) would have to be decided by unanimity (RUPA §§401(6)(equal rights in management) and 401(10) (ordinary matters majority, extraordinary matters unanimity)). If A, B, C and D are the partners, then an ordinary matter could be decided by any 3 of the partners. But E's offer to buy half of the business looks like the admission of a new partner which would require unanimity under RUPA §401 (9) (consent of all partners necessary for admission of new partners). Whether or not C and D are partners matters in terms of which people agree to admitting E as a partner (A and B or A, C, B, C and D), but either way, B would need to agree (and perhaps E's suggestions about how the business should be run will lead to B objecting).

Question 2:

B and XYZ. First, there is the question of authority. A and B focus on different aspects of running the restaurant business: A deals with day to day management and B deals with external relations. They may have displaced the RUPA default rules about decision-making, or they may not. This is unclear. So, does B have authority to make decisions about advertising spending or not? We know that authority is actual (express, implied, incidental) or apparent.

The fact that Billy has been allowed to manage external relations suggests that he may be able to argue he has implied actual authority with respect to this contract (based on his reasonable interpretation of the authority he and A agreed he would have). And XYZ may be able to argue he has apparent authority (based on their reasonable interpretation). A partner has apparent authority with respect to matters in the ordinary course of the partnership business (RUPA §301)

and there is an argument that B has authority here. However, this is a new and very expensive campaign, which suggests that it could be argued that it is not in the ordinary course of business. In addition, B's decision was influenced by the hiring of his sister. So he suffered from a conflict of interest when he agreed to the contract, which is a problem from the perspective of the fiduciary duties he owes to his partners and the partnership, and also raises questions about the reasonableness of his interpretation of his authority.

The circumstances are different from those of the agency/partnership cases we have read which focused on benefits a partner derived or diverted to themselves (e.g. *Meinhard v Salmon*), but there is a conflict of interest here and B should have disclosed it to his partners before agreeing to the contract, if he had authority to agree to the contract. At the time you answered this question we had not studied directors' conflicting interest transactions but you had read enough to know that secrecy could be an issue for fiduciaries.

A could challenge the contract for lack of authority, or on the basis of the conflict of interest. With respect to the issue of limiting B's powers to affect the business in future, that issue could be tied up in the questions about how the decision as to admitting a new member would be carried out. The existing partnership could be dissolved (subject to the *Owen v Cohen* partnership for a term issue and also subject to the need to pay to B the value of B's interest in the business) and a new business entity set up. If some thought were given to issues of management rights and financial participation that would be a good idea. Also the issue of liability.

Given the uncertainties about whether the partnership would be seen as a partnership for a term it would be advisable to apply to dissociate B as a partner. Here also, B would need to be bought out.