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1) Advantages/Disadvantages

General Partnership:

There are few advantages to forming a general partnership. One advantage is that the partners need not file anything with the state in order to establish a general partnership. For Beth and Mike, they can just agree to go into business together to make and sell cupcakes. They will be able to determine how profits and losses should be shared without an agreement and will both be able to equally manage the business. The disadvantages of a general partnership far outweigh the advantages. The main disadvantage is that each partner is jointly and severally and personally liable for the losses of the partnership. That means that both Beth and Mike will be personally liable to the partnership's creditors for any debt owed by the partnership. The creditor can get to the partners' personal assets once the partnership's assets are used up. Additionally, each partner will be liable for the torts of the partnership and the other partner. Again, this makes the partners personally liable for the torts the other partner commits while in the scope of the agency relationship.

Limited Liability Partnership:

Unlike a general partnership, each partner in a limited liability partnership (LLP) is not personally liable for the debts of the partnership or the torts committed by the other partners. Each partner is only liable to the amount of the contribution he/she made to the partnership. Additionally, like a general partnership, the partners will be able to decide who will manage or they can decide to manage equally. A disadvantage of forming a LLP is that while each partner is not liable for the debts of the partnership, a partner can be personally liable if he guarantees a partnership loan. Further, a partner can be personally liable for the torts of another partner or employee if the partner supervised the tortfeasor, encouraged or aided the tortfeasor, or knew of the tort and did nothing to correct the action. Another disadvantage is that in order to form a LLP, the partnership must file the required documentation with the state.

Limited Liability Company:

Similar to a partnership, each member of a limited liability company (LLC) is not personally liable for the debts of the LLC or the torts committed by other members. Each

member is only liable for the amount that he contributed to the company. Another advantage of an LLC is the taxation treatment. An LLC can elect to be treated like a partnership for taxation purposes rather than treated like a corporation. This election eliminates the double taxation of corporations. Further, a LLC has another tax benefit of not having to follow the rules of an S Corporation. The S corporation rules are very stringent with regard to who can be a shareholder, the number of shareholders, etc. A LLC on the other hand can have members of all types including individuals, partnership, corporations, etc. Like the LLP, a disadvantage of the LLC is that fact that a member can be held personally liable if he personally guarantees a loan of the LLC. To form an LLC also requires filing that a general partnership does not.

2) Lawful Formation

General Partnership:

To form a general partnership Beth and Mike need only agree to carry on the business for profit. There is no need for them to file anything with the state to form the partnership. A partnership agreement is not required either. Beth and Mike can choose to allocate income and losses however they choose. Absent an agreement to the contrary, the partners will share profits (and losses) equally. However, in order for Beth and Mike to conduct business as "The Best Cupcakes" they will need to file an Assumed Name document with the Secretary of State. The assumed name filing is required if a partnership is not going by the surnames of the partners.

Limited Liability Partnership:

In order for Beth and Mike to form a limited liability partnership, Beth and Mike will need to file articles of formation with the Secretary of State. It will need to include the names of the partners, the address of the partnership and the registered agent of the partnership. Also, they will need to pay the filing fee of \$250 per partner. The state also requires that a LLP obtain insurance of at least \$100,000 to cover the partnership or have assets set aside of at least \$100,000. The name of the LLP must include "limited liability partnership" or "LLP" or "L.L.P." after the name to indicate to the public that it is operating as an LLP. Therefore, the name of the business must be something like "The Best Cupcakes, LLP."

Limited Liability Company:

Similar to forming a LLP, Beth and Mike will have to file articles of formation with the

Secretary of State to form a limited liability company. The filing must contain the members names, address of the company, and the registered agent for the company. A filing fee must also be included which is \$500. The state also requires a LLC to obtain insurance of \$100,000 or instead set aside assets of \$100,000 for liability. The LLC must also contain required language in the name: "limited liability company," "LLC," or "L.L.C." Therefore, Beth and Mike's company's name should be something like "The Best Cupcakes, LLC."

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1. General partnership: A general partnership is an entity involving two or more partners operating a business. As compared with limited liability entities, the primary advantage of a general partnership is the ease of setup and operation. There is no requirement to file forms with the State in order to establish a general partnership. Thus, it can begin operating immediately on agreement of the parties. It also does not involve the payment of any fees to the state, which represents a cost savings for the business. All three types of entities have the benefit of pass-through tax status, which means that only the partners are taxed (rather than taxing the entity first and then also taxing the owners). Similarly, it is also advantageous that each type of entity can be managed by all of the partners. Conversely, the significant disadvantage associated with general partnerships is that each partner is jointly and severally liable on a personal basis for all of the partnerships debts, whether a contract or tort debt. Thus, if the partnership is insolvent, partnership creditors can obtain payment from any partner's personal funds (though partners are entitled to indemnification from the partnership to the extent solvent, and contribution from the other partners if one partner bears a disproportionate amount of the debt). Likewise, partners are even vicariously liable for each other's torts and for contracts (even if not authorized if there is a substitute for actual authority) that one partner enters into on behalf of the partnership.

Limited liability partnership (LLP): An LLP is a partnership that has obtained special limited liability status from the State by filing certain documents and paying certain fees. Unlike a general partnership, an LLP is advantageous in that it provides limited liability for the partners. The partnership itself remains liable on all contracts and is vicariously liable for the torts of employees and partners in the scope of business. However, the partners cannot be held personally liable even if the partnership is insolvent (though their contributions to the partnership are at risk and they remain liable for their own torts). There is an important exception to the limited liability, which makes an LLP disadvantageous as compared with an LLC: a partner is personally liable for torts committed by an employee the partner is supervising the employee or authorizes/encourages his tortious acts. Another disadvantage of an LLP as compared with a general partnership is the filing and fee requirements. State-mandated forms and fees must be paid both before an LLP can begin operating and annually. A failure to comply with these requirements could result in losing limited liability status, money claims by the State, and even

involuntary termination of the entity.

Limited liability company (LLC): An LLC is an entity that may be operated as either a corporation or partnership and receives limited liability status from the State. The individuals who own the LLC are called members. The primary advantage of an LLC is that it offers the maximum liability protection for members. Although the LLC is liable on contracts and vicariously liable for torts committed by members and employees, the members are not personally liable for any contractual obligations or torts (except a member remains liable for his own torts). Unlike an LLP, this protection extends to all vicarious liability, even where an employee's tortious actions are authorized or supervised by a member. Another advantage of an LLC is the ease with which new members may be admitted: there is no requirement for additional capital contributions to admit a new member. On the other hand, an LLC's primary disadvantage is the same as that of the LLP: members must file forms and pay fees at startup and annually thereafter. Failure to pay those fees results in a loss of limited liability and possibly involuntary termination.

2. General partnership: To create and commence operation as a general partnership, the only requirement is that the partners execute an agreement among themselves. The agreement need not be in writing (unless otherwise required under the Statute of Frauds) and merely must state the obligations of the partners, discuss how profits and losses should be apportioned, and set a duration (could be for a limited purpose/time or perpetual). Although the partnership need not file anything with the State, they may wish to do file an assumed name certificate to make transacting business easier (e.g., to open a bank account in the partnership's name) and to reserve their desired name.

LLP: The partners must file a specific LLP form with the Secretary of State before they can commence operations. The form must specify the name and address of the partners, the duration and purpose of the partnership, and the name of the partnership. By law, the name must give notice of limited liability status by including "Limited Liability Partnership" or "LLP" in the name. The LLP must also make an annual filing with the State.

LLC: The members must file a specific LLC form with the Secretary of State before they can

commence operations. The form must specify the name and address of the members, the duration and purpose of the LLC, the name and address of a registered agent in Texas for service of process, and the name of the LLC. The name is statutorily required to include "Limited Liability Company," "LLC," or "LC" in the name. The LLC also must make an annual filing and pay franchise taxes each year.

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Partnership:

Recognized by the TBOC, a general partnership provides various advantages based on its informality. A GP may be formed with relatively ease, and requires no formal management structure or requirements. As simple as GPs are to form they are equally as easy to dissolve. Modifications of the partnership agreement require only the consent of the partners involved, and there are no required documents to be filed with the state. The general partnership operates as a pass through tax entity, therefore the partners will only be taxed on profits distributed to them, and the partnership will pay no tax. There are however, several negatives to a general partnership, particularly with respect to liability. General partners are all jointly and severally liable for any debts or other liabilities of the partnership. The general rule requires a creditor or tort victim to exhaust the partnership's assets prior to looking to the individual partners, however once satisfied, the creditor may look personally to the partner. Therefore, the partner's personal property could be subject to the claim. Partners who satisfy partnership debts will have a claim against the partnership for contribution. Because this appears to be a small operation, a GP might make sense for Beth and Mike, however, the liability exposure is not worth the simplicity.

Limited Liability Partnership:

The limited liability partnership is essentially identical to the general partnership as far as advantages are concerned (except for a few minor formalities discussed in part 2), however it differs from the partnership with respect to liability of the partners. An entity formed as an LLP provides a total shield of liability to partners from the LLP's liabilities unless the partner was the cause of the tort or debt OR was supervising another who individually incurred liability. Thus partners are still liable for their own torts, however, their liability for overall debts of the partnership is limited to their invested interests. A LLP is thus, much more appealing than a GP, however, Beth and Mike will be required to keep \$100,000 on hand or obtain insurance for \$100,000, which might be difficult given the nature of their small business.

LLCs

LLC's provides an excellent balance between simplicity, control, and tax planning while maintaining a shield against personal liability for investors. Much more formal than an LLP or GP, the LLC typically falls in line with a corporation with respect to corporate formalities. An entity organized under an LLC is given the choice of being either manager managed or member managed, which offers a great deal of flexibility. The LLC

is also permitted to elect pass through taxation which, like a LLP and GP, avoids the double taxation issues which corporations face. Much like the LLP, the LLC provides a liability shield for members. While a member would be liable for their own liabilities/torts, they only stand to lose the value of their interest in the LLC and are faced with no personal liability (unless the corporate veil is pierced). The major downside to the LLC is that it is somewhat more formal, there are filing requirements (see below), and termination is more complicated than it would be under a GP or LLP. Additionally, there is less case law surrounding the LLC, thus it might make it more difficult to predict how courts will rule on issues such as liability.

2)

Formation of a general partnership requires no formalities whatsoever. There need only be an agreement between 2 or more partners to form the partnership. This agreement may even be oral unless it violates the statute of frauds (can't be performed in one year). Beth and Mike simply need to intend to form a partnership.

An LLP requires Beth and Mike to file a document with the Texas Secretary of State indicating the names and addresses of the partners, the address of the principal place of business (Dallas), and payment of a \$200 filing fee. In addition, Beth and Mike will be required to maintain \$100,000 in insurance or reserve this amount. Also, the business must include the phrase limited liability partnership or LLP, otherwise it may be considered a general partnership.

LLC's also require a filing with the secretary of state including the \$500 filing fee, certificate of formation (which indicates the number, names and addresses of the members involved). Once the state has accepted the application the LLC could hold a meeting to adopt bylaws, however this is not required. The LLC must use the phrase limited liability company or "LLC" when referring to the name of the company.

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