

Question 4 – July 2014 – Selected Answer 1

1) RPL is a general partnership. A general partnership is presumed for an entity that is created among partners for the purpose of doing business and making a profit, unless there is an affirmative showing that a different entity has been created. In this case, there are 6 total partners, Ashley included, conducting business in Texas together, so they are definitely a partnership of some sort. To be a limited partnership or limited liability partnership, a certificate must be filed with Secretary of State stating that the entity has been formed and is being used in the conduct of the partners' business and the name must include "limited" or "limited liability" or other similar phrases or abbreviations. In this case the word Limited is included in the title, but the partners have agreed not to disclose RPL's existence or file any information containing RPL's name address or business purpose with any government agency so the entity cannot be a limited or limited liability partnership.

2) Which of the provisions below are valid and which are not?

a) Access to books and records: Valid. All partners must have access to an entities books and records, but the access can be limited in reasonable fashion. In this case, inspecting during normal business hours, under Ashley's supervision, after reimbursing for reasonable costs are all reasonable limits on the partners' access.

b) Limited liability for partners: Invalid. If RPL was an LP or LLP this would be valid for the limited partners. However, because RPL is a general partnership, all partners are completely liable for all actions of the company and they may not limit their liability by internal agreement.

c) No liability for breach of duty of care or good faith except for willful or intentional misconduct: Valid. Although the duty of care and duty of good faith may not be completely eliminated even by agreement, defining what constitutes a breach of those duties is allowed. Defining a breach as willful or intentional misconduct is a valid definition of the duties.

d) No partner may sell... to any person not already a partner: Valid. Although a partnership cannot completely restrict the ability to sell or transfer its shares, it is allowed to place some restrictions on alienation.

e) RPL's affairs are to be governed by Louisiana law: Invalid. For internal governance of an entity, the laws of the state of Texas apply to entities created within Texas. In the present case, all partners reside in Texas, the only office is in Texas and all of RPL's business is in Texas, so even though Ashley was born in Louisiana, Louisiana law cannot be applied to govern the affairs of RPL.

Question 4 – July 2014 – Selected Answer 2

1. RPL is a general partnership

A general partnership is the association of two or more persons to carry on a business for profit as co-owners. A general partnership can be formed without intent to form a partnership or any other formalities such as writing or filing documents with the Secretary of State. In a general partnership, partners share profits and losses equally and have equal rights to management, though a managing partner may be appointed to manage the partnership primarily. In a general partnership, each partner is personally liable for any obligations or debts of the partnership. This liability cannot be disclaimed. A limited partnership ("LP") is a partnership that includes one or more general partners and one or more limited partners. A LP is formed by filing documents with the Secretary of State that state, among other things, the name of the LP that must include some form of the words "limited partnership," the names and addresses of the general partners and limited partners, and state the purpose of the LP. The document must also state that the intent is to form a LP. In a LP, general partners are personally liable for the obligations and debts of the LP, however limited partners are only liable up to the amount they invested in the LP, unless the limited partner exercises control over the LP, in which case the limited partner can be treated as a general partner and become liable for the LP's debts and obligations.

A Limited Liability Partnership ("LLP") is a partnership in which none of the partners are liable for the

debts or obligations of the LLP or for the actions of other partners. The formation of an LLP requires the filing of documents with the Secretary of State stating, among other things, the name of the LLP that must include "LLP," the names and addresses of the partners, the intent to be an LLP and the purpose of the LLP. Here, RPL has decided to not disclose RPL's existence to the public or file any information containing RPL's name, address or business purpose with any government agency. Since RPL has not filed anything with the Secretary of State which would specify what type of organization it is, RPL is a general partnership, despite the word "Limited" in its name.

2. RPL's partnership agreement provisions

A partnership agreement is the document that determines how a partnership will be run. In a general partnership, a partnership agreement is not required, however without one, the partnership is subject to the default rules of the TBOC. A partnership agreement may modify the TBOC default rules.

A. Access to RPL's Books and Records

In a partnership, partners have the right to equal access to the books and records of the partnership. A partnership agreement may restrict this right, but only if it is reasonable. Here, these conditions to viewing RPL's books and records would be considered reasonable because they limit the time to business hours, require the presence of the managing partner as a person who knows the books, and the reasonable costs of making the books and records available. All of these conditions are allowed on the access to books and records, so this provision is valid.

B. Partner Liability to Creditor

As stated above, in a general partnership, all partners are personally liable for the obligations and debts of the partnership. This rule cannot be modified by a partnership agreement because it is one of the basic tenants of a general partnership. Since the partnership agreement tries to limit the partner's liability to creditors for only the amount of his investment, this provision is void. If RPL wanted this limitation of liability to creditors, it should have formed a LP or LLP, in which the limited partners are only liable up to the amount of their investment.

C. Partner's Liability to RPL for Breach of Duty of Care or Duty of Good Faith

Each partner owes a duty of loyalty, care and good faith to the partnership and the other partners. The duties of care and good faith cannot be disclaimed by a partnership agreement. However, a partnership agreement may include factors to be used in order to determine whether a breach of the duty of care has occurred. Here, the partnership agreement states that there is no partner liability to RPL for the breach of duty of care or good faith, unless the partner has engaged in willful or intentional misconduct. The initial attempt to disclaim these duties would fail, however the provision provides that the duty of care or good faith is breached by willful or intentional misconduct. These qualifications may be considered factors for a court or partnership to use in order to determine when a breach has occurred. Therefore, this provision may be valid if the qualifications are considered as factors.

D. Sale or Assignment of Interest

Generally, in a partnership, a partner may sell, transfer or assign his interest in the partnership. However, a partnership agreement may limit the transferability of partnership interest by requiring the partner to offer the interests to the partnership first, or specifying people who it can be sold to, as long as it includes some way for the partner to get rid of the shares fairly. Here, this provision is valid because it requires the partner sell the interest only to current partners.

E. Governing Law

A partnership agreement may specify under which state's law it will be governed, but there must be some connection or reason for the choice of that state's law. Here, all of the partners are Texas residents, RPL's only office is in Texas and all business is conducted in Texas. The only connection from the facts is that Ashley was born and raised in Louisiana. Since there is no connection between the partnership and Louisiana, this provision is probably invalid.

Question 4 – July 2014 – Selected Answer 3

1. RPL is a general partnership. A general partnership is an agreement between two or more people to carry on a business for profit, sharing in control and profits or losses. No paperwork needs to be filed in

order to form a partnership and the partners do not need to intend to form a partnership specifically. All that is needed is an intent to carry on a business together. Partners in a partnership can assent to a partnership agreement to establish the terms of their partnership, but if no such agreement exists, then the Texas Business Organization Code contains a set of default rules which will apply to the partnership. In a partnership, all partners are personally liable for the debts and obligations of the partnerships.

A limited partnership is a partnership in which there are general partners and limited partners. Limited partners are partners who are not personally liable for the obligations of the partnership, while general partners are personally liable. A limited liability partnership is a partnership in which none of the partners are personally liable for the obligations of the partnership. In order to form a limited partnership or a limited liability partnership, a certificate of formation must be filed with the Texas Secretary of State stating that the organization is a limited partnership or a limited liability partnership, respectively. Furthermore, the name of the organization must include the phrase "limited partnership" (or "LP") or "limited liability partnership (or "LLP") respectively. Here, Ashley and the five partners decided to need the existence of RPL a secret to the general public. They did not file any information containing RPL's name or address or business purpose with any government agency. RPL cannot be a limited partnership or limited liability partnership because it failed to file a certificate of formation with the Texas Secretary of State. General partnerships, on the other hand, do not need to file any information with any government agency in order to be formed. Therefore, RPL is a general partnership.

2. As stated earlier, partners can create a partnership agreement to govern their partnership and change the default rules in the Texas Business Organization Code, but some rules cannot be changed and some changes must be reasonable.

a. The provision that any partner who wishes to access RPL's books and records may do so but only during normal business hours, under Ashley's control, and after reimbursing RPL for the reasonable cost of making the books and records available is likely valid. Under the default rules, all partners have the right of access to a partnership's books and records. However, the right is subject to a rule of reasonableness whereby the access can be reasonably limited to such things as normal business hours. It is reasonable to require partners to reimburse the partnership for the costs of accessing the books. This provision would be valid since it still allows the partners their right of access to the books (which cannot be entirely eliminated), but provides for reasonable restrictions.

b. The provision that no partner will be liable to RPL's creditors beyond the amount of his or her investment in RPL will be not valid against any RPL creditor. In a partnership, all partners are personally liable for the obligations of the partnership. That is, a partnership creditor can bring an action and name the partnership and all individual partners as defendants, and collect any judgment from the partners. A partnership agreement cannot limit this liability. If the partners want to limit their liability, they need to form a business organization which permits such limited liability, by filing a certificate of formation with the Texas Secretary of State. This filing puts creditors on notice that the partners are not personally liable.

c. The provision that no partner can be held liable to RPL for breach of the duty of care or good faith unless the partner has engaged in willful or intentional misconduct is likely valid. Under the Texas Business Organization Code, partners owe each other a duty of care and good faith. This duty cannot be eliminated by a partnership agreement, but a partnership agreement can establish the terms under which breach will be evaluated. Here, the partners have determined that breach will not be found unless the partners engaged in willful or intentional misconduct. This provision is likely valid since it is a reasonable limitation but does not completely eliminate the duty of care or good faith.

d. The provision that no partner may sell, transfer, or assign his interest in RPL to any person who is not already a partner in RPL is likely valid, but will not affect the ability of certain creditors to reach a partner's partnership interest payment of certain debts, such as child support obligations. A partnership agreement can limit the ways in which partners can transfer their partnership interest. This ability to restrain alienability exists so that partners are not forced to be partners with someone who they have not consented to be in business with. A partner can be restricted from transferring his management rights in the partnership. However, a partner's partnership interest - that is, his right to receive distributions from

the partnership - may be involuntarily alienated by some creditors. This provision of the RPL partnership agreement will not prevent such actions. However, these transferees do not become partners in the partnership. They do not have the management rights of partners unless the partners agree to admit a new partner. The transferees merely have the right to receive monetary distributions in the same manner in which the transferor-partner would receive such distributions.

e. The provision that RPL's affairs are to be governed by Louisiana law will not be valid. A partnership agreement can decide which law will apply to the partnership, but only if there is a reasonable basis for the selection of that forum state law. The partnership must have some connection to the state whose law they choose to govern their affairs. Here, while Ashley was born and raised in Louisiana, she is a Texas resident now and all five of the other partners are Texas residents. The business only has one office which is in Texas and it conducts all of its business in Texas. Under these facts, RPL does not have sufficient contacts with Louisiana such that its affairs should be governed by Louisiana law. This provision is invalid.