

AGN:  
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SPRING SEMESTER 2012

# **BUSINESS ASSOCIATIONS**

**THREE HOURS.  
THIS IS A CLOSED-BOOK EXAM.**

Try to show thought and critical analysis of the materials and issues dealt with in the course.

DO read the questions carefully and think about your answers before beginning to write.

DO refer to statutory provisions, cases and other materials where appropriate. If you make general statements, try to back them up with specific references.

DO NOT use abbreviations unless you explain what you are using them to stand for.

DO NOT make assumptions in answering the hypothetical.

DO explain what further information you might need in order to answer the question properly.

DO write legibly and clearly.

**You will get credit for following these instructions, and may be penalized for failing to do so.**

Azeroth and Skyrim are both states in the US which have corporations statutes in the form of the Delaware General Corporation Law (DGCL) and partnership statutes in the form of the Revised Uniform Partnership Act (1997) (RUPA).

Joe is the CEO of Infinity Gaming Corporation (IGC) , a corporation incorporated in Azeroth. IGC owns and operates casinos in Azeroth, and its shares trade on the Azeroth Stock Exchange (ASX). Some time ago IGC began to expand its operations outside the US, and it entered into a partnership agreement with Endless Gaming Inc. (EGI), a corporation incorporated in Skyrim whose shares are also traded on the ASX. Joe negotiated the partnership agreement with Frieda, who is the CEO of EGI. The Boards of Directors of both corporations approved the partnership agreement after Joe and Frieda explained their vision of how the two corporations could work together profitably in opening new casinos in Elbonia, a developing country far from the US. Joe and Frieda have been friends for years. The Boards agreed that in order to strengthen links between the two partners Joe would become a director of EGI and Frieda would become a director of IGC.

The partnership agreement provided that Petra, IGC's Vice President for Business Development, would be in charge of developing a plan for the partnership's business and George, EGI's Corporate Counsel was to be in charge of the partnership's legal issues. The partners would share profits equally and each partner agreed to contribute capital and expertise to the partnership. IGC and EGI agreed that Petra and George would have the authority to make ordinary business decisions for the partnership. Extraordinary decisions would require the consent of IGC and EGI. Because Joe and Frieda had known each other for such a long time and trusted each other the partnership agreement also limited the partners' fiduciary duties "to the maximum extent permitted by law."

The Board of IGC authorized Joe to consent to extraordinary decisions of the partnership on its behalf. The Board of EGI said to Frieda that they wanted her to be involved in monitoring what the partnership was doing but that she and George should

consult EGI's Board on any extraordinary decisions of the partnership.

The partnership established its main offices in Azeroth because the largest airport in Azeroth had very good connections to Elbonia. Petra persuaded George to hire her younger sister, Cara, to design the office premises. Cara had just graduated from design school at the time and this was her first job. She was very pleased to be hired because there was a shortage of interesting jobs at the time and the partnership agreed to pay her very well for her work. Cara designed a very glamorous (and expensive) office suite. Petra and George agreed that it made sense for the offices to look luxurious because the partnership was in the business of luxury gaming. They did not consult Joe and Frieda about these expenses.

When IGC and EGI announced the establishment of the partnership the shares of both corporations increased significantly in price. At the time many commentators on the gaming industry thought that IGC and EGI were the two most innovative gaming businesses around and the market seemed to like the idea of the investment in Elbonian gaming.

Joe, Frieda, Petra and George went on a number of trips to Elbonia separately and together to negotiate access to the gaming market in Elbonia. After a while they began to delegate the details of negotiation with the Elbonian authorities to Petra. Joe, Frieda and George emphasized to Petra that she must consult with George with respect to any legal issues. Petra was determined to show that she could succeed in the negotiations, so, when the Elbonian Minister for Investment told Petra that she could have the gaming licenses the partnership would need if she arranged for him to travel with his (large) family to stay for two weeks at EGI's most luxurious casino in Skyrim at EGI's expense, she agreed without stopping to think. Petra paid for the vacation from the partnership's bank account. A payment such as this constitutes criminal bribery in Skyrim and in Azeroth.

Joe happened to be visiting the same EGI casino as the Minister at the same

time, and they happened to meet at a poker game there. After the game was over they had a long conversation. The Minister explained to Joe that he wanted to bring outside expertise into Elbonia to help develop the gaming industry, including developing state-owned casinos, because he was offended at the idea that the profits from Elbonian gaming would be going to the shareholders in foreign corporations. Joe agreed to sign a very lucrative contract to act as a consultant to the Elbonian Government. He did not tell anyone at IGC or EGI about this contract.

The Azeroth Integrity Commission learns about the Minister's vacation and informs Petra that she, the partnership, IGC and EGI are under investigation. Before telling anyone else Petra informs her husband who tells a friend of his who owns shares in EGI that the friend should sell his shares. The Azeroth Integrity Commission announces that it is investigating the Elbonian bribery, and that it is determined to stamp out such behavior. Elbonia informs the partnership that it will not be allowed to open a casino in Elbonia. The market price of shares in IGC and EGI collapses.

**Answer the following 5 questions, explaining (where applicable) what further facts you would need to know and giving reasons for your answers:**

1. (25 points) What claims do you think EGI has against IGC under the partnership agreement? Does IGC have any claims against EGI under the partnership agreement?
2. (25 points) If minority shareholders in IGC and EGI want to sue directors and officers of those corporations what should they argue? What problems will they face ?
3. (20 points) If the partnership has insufficient assets to satisfy the claims of its creditors can the creditors look to the partners for payment ? Would it make a difference if the partners had decided to establish an LLP or LLC instead (and they had become limited liability partners or member/managers)?

4. (15 points) If a partnership agreement governed by RUPA limits the partners' fiduciary duties "to the maximum extent permitted by law," how do you think a court should go about defining the maximum extent?
5. (15 points) Under what circumstances would Petra's husband, and/or his friend, incur liability based on these facts? Do the facts raise any other legal issues?

**RUPA § 103**

(a) Except as otherwise provided in subsection (b), relations among the partners and between the partners and the partnership are governed by the partnership agreement. To the extent the partnership agreement does not otherwise provide, this [Act] governs relations among the partners and between the partners and the partnership.

(b) The partnership agreement may not:...

(3) eliminate the duty of loyalty under Section 404(b) or 603(b)(3), but:

(i) the partnership agreement may identify specific types or categories of activities that do not violate the duty of loyalty, if not manifestly unreasonable; or

(ii) all of the partners or a number or percentage specified in the partnership agreement may authorize or ratify, after full disclosure of all material facts, a specific act or transaction that otherwise would violate the duty of loyalty;

(4) unreasonably reduce the duty of care under Section 404(c) or 603(b)(3);

(5) eliminate the obligation of good faith and fair dealing under Section 404(d), but the partnership agreement may prescribe the standards by which the performance of the obligation is to be measured, if the standards are not manifestly unreasonable...

**RUPA § 404**

(a) The only fiduciary duties a partner owes to the partnership and the other partners are the duty of loyalty and the duty of care set forth in subsections (b) and (c).

(b) A partner's duty of loyalty to the partnership and the other partners is limited to the following:

(1) to account to the partnership and hold as trustee for it any property, profit, or benefit derived by the partner in the conduct and winding up of the partnership business or derived from a use by the partner of partnership property, including the appropriation of a partnership opportunity;

(2) to refrain from dealing with the partnership in the conduct or winding up of the partnership business as or on behalf of a party having an interest adverse to the partnership; and

(3) to refrain from competing with the partnership in the conduct of the partnership business before the dissolution of the partnership.

(c) A partner's duty of care to the partnership and the other partners in the conduct and winding up of the partnership business is limited to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law.

(d) A partner shall discharge the duties to the partnership and the other partners under this [Act] or under the partnership agreement and exercise any rights consistently with the obligation of good faith and fair dealing.

(e) A partner does not violate a duty or obligation under this [Act] or under the partnership agreement merely because the partner's conduct furthers the partner's own interest.

(f) A partner may lend money to and transact other business with the partnership, and as to each loan or transaction the rights and obligations of the partner are the same as those of a person who is not a partner, subject to other applicable law.

(g) This section applies to a person winding up the partnership business as the personal or legal representative of the last surviving partner as if the person were a partner.