

## 12.4: Summary and Exercises

### Summary

The basic law of partnership is found in the Uniform Partnership Act and Revised Uniform Partnership Act. The latter has been adopted by thirty-five states. At common law, a partnership was not a legal entity and could not sue or be sued in the partnership name. Partnership law defines a partnership as “an association of two or more persons to carry on as co-owners a business for profit.” The Uniform Partnership Act (UPA) assumes that a partnership is an aggregation of individuals, but it also applies a number of rules characteristic of the legal entity theory. The Revised Uniform Partnership Act (RUPA) assumes a partnership is an entity, but it applies one crucial rule characteristic of the aggregate theory: the partners are ultimately liable for the partnership’s obligations. Thus a partnership may keep business records as if it were a legal entity, may hold real estate in the partnership name, and may sue and be sued in federal court and in many state courts in the partnership name.

Partnerships may be created informally. Among the clues to the existence of a partnership are (1) co-ownership of a business, (2) sharing of profits, (3) right to participate in decision making, (4) duty to share liabilities, and (5) manner in which the business is operated. A partnership may also be formed by implication; it may be formed by estoppel when a third party reasonably relies on a representation that a partnership in fact exists.

No special rules govern the partnership agreement. As a practical matter, it should sufficiently spell out who the partners are, under what name they will conduct their business, the nature and scope of the business, capital contributions of each partner, how profits are to be divided, and similar pertinent provisions. An oral agreement to form a partnership is valid unless the business cannot be performed wholly within one year from the time that the agreement is made. However, most partnerships have no fixed terms and hence are “at-will” partnerships not subject to the Statute of Frauds.

### Exercises

1. Able, Baker, and Carr own, as partners, a warehouse. The income from the warehouse during the current year is \$300,000, two-thirds of which goes to Able. Who must file a tax return listing this as income, the partnership or Able? Who pays the tax, the partnership or Able?
2. The Havana Club operated in Salt Lake City under a lease running to defendant Dale Bowen, who owned the equipment, furnishings, and inventory. He did not himself work in operating the club. He made an oral agreement with Frances Cutler, who had been working for him as a bartender, that she take over the management of the club. She was to have the authority and the responsibility for the entire active management and operation: to purchase the supplies, pay the bills, keep the books, hire and fire employees, and do whatever else was necessary to run the business. As compensation, the arrangement was for a down-the-middle split; each was to receive \$300 per week plus one half of the net profits. This went on for four years until the city took over the building for a redevelopment project. The city offered Bowen \$30,000 as compensation for loss of business while a new location was found for the club. Failing to find a suitable location, the parties decided to terminate the business. Bowen then contended he was entitled to the entire \$30,000 as the owner, Cutler being an employee only. She sued to recover half as a partner. What was the result? Decide and discuss.
3. Raul, a business student, decided to lease and operate an ice cream stand during his summer vacation. Because he could not afford rent payments, his lessor agreed to take 30 percent of the profits as rent and provide the stand and the parcel of real estate on which it stood. Are the two partners?
4. Able, Baker, and Carr formed the ABC Partnership in 2001. In 2002 Able gave her three sons, Duncan, Eldon, and Frederick, a gift of her 41 percent interest in the partnership to provide money to pay for their college expenses. The sons reported income from the partnership on their individual tax returns, and the partnership reported the payment to them on its information return. The sons were listed as partners on unaudited balance sheets in 2003, and the 2004 income statement listed them as partners. The sons never requested information about the management of the firm, never attended any meetings or voted, and never attempted to withdraw the firm’s money or even speak with the other partners about the firm. Two of the sons didn’t know where the firm was located, but they all once received “management fees” totaling \$3,000, without any showing of what the “fees” were for. In 2005, the partnership incurred liability for pension-fund contributions to an employee, and a trustee for the fund asserted that Able’s sons were personally liable under federal law for the money owing because they were partners. The sons moved for summary judgment denying liability. How should the court rule?
5. The Volkman wanted to build a house and contacted David McNamee for construction advice. He told them that he was doing business with Phillip Carroll. Later the Volkman got a letter from McNamee on stationery that read “DP Associates,” which they assumed was derived from the first names of David and Phillip. At the DP Associates office McNamee introduced Mr.

Volkman to Carroll, who said to Volkman, “I hope we’ll be working together.” At one point during the signing process a question arose and McNamee said, “I will ask Phil.” He returned with the answer to the question. After the contract was signed but before construction began, Mr. Volkman visited the DP Associates office where the two men chatted; Carroll said to him, “I am happy that we will be working with you.” The Volkman never saw Carroll on the construction site and knew of no other construction supervised by Carroll. They understood they were purchasing Carroll’s services and construction expertise through DP Associates. During construction, Mr. Volkman visited the DP offices several times and saw Carroll there. During one visit, Mr. Volkman expressed concerns about delays and expressed the same to Carroll, who replied, “Don’t worry. David will take care of it.” But David did not, and the Volkman sued DP Associates, McNamee, and Carroll. Carroll asserted he could not be liable because he and McNamee were not partners. The trial court dismissed Carroll on summary judgment; the Volkman appealed. How should the court rule on appeal?

6. Wilson and VanBeek want to form a partnership. Wilson is seventeen and VanBeek is twenty-two. May they form a partnership? Explain.
7. Diane and Rachel operate a restaurant at the county fair every year to raise money for the local 4-H Club. They decide together what to serve, what hours to operate, and generally how to run the business. Do they have a partnership?

### SELF CHECK QUESTIONS

1. The basic law of partnership is currently found in
  1. common law
  2. constitutional law
  3. statutory law
  4. none of the above
2. Existence of a partnership may be established by
  1. co-ownership of a business for profit
  2. estoppel
  3. a formal agreement
  4. all of the above
3. Which is false?
  1. An oral agreement to form a partnership is valid.
  2. Most partnerships have no fixed terms and are thus not subject to the Statute of Frauds.
  3. Strict statutory rules govern partnership agreements.
  4. A partnership may be formed by estoppel.
4. Partnerships
  1. are not taxable entities
  2. may buy, sell, or hold real property in the partnership name
  3. may file for bankruptcy
  4. have all of the above characteristics
5. Partnerships
  1. are free to select any name not used by another partnership
  2. must include the partners’ names in the partnership name
  3. can be formed by two corporations
  4. cannot be formed by two partnerships

### Answers

1. c
2. d
3. c
4. d
5. c

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