ESSAY QUESTION NO. 7

Answer this question in booklet No. 7

Sarah and Ginger decided to form a business to clean up dog poop from yards on a monthly subscription basis. They called their business "Ziggy Poop Service." They agreed to split the costs and profits 50/50. Ginger transferred her van to the business and they repainted it with the business name on all sides. The cost of all other start up equipment was shared evenly by Ginger and Sarah. They had no written agreement governing their business arrangement. The business took off and soon they had more customers than the two could handle. They approached Joe, an old high school friend, and in lieu of wages, he agreed to handle one third of the Ziggy Poop customers in exchange for 10% of the profits. Joe had no responsibility to contribute to the costs of the business should expenses exceed revenues.

While scooping poop, Ginger accidentally let loose a customer's rare pedigree dog and it was never recovered. The customer demanded that Ginger reimburse him for the value of the dog, $3,000. Ginger paid the customer immediately to avoid legal action, and then submitted the cost for inclusion in the business' monthly calculation of costs at the end of the month. Sarah objected, she said it was Ginger's fault that the dog was lost, not hers, and that therefore Ginger should bear the cost alone.

Sarah and Ginger each received an equal share of the profits at the end of each month. While Sarah was doing as much poop pick-up as Ginger, she was also handling all of the book keeping and business correspondence. Sarah asked Ginger to pay her an additional administration fee based on the number of hours she performed such additional duties. Ginger did not agree to Sarah's request. Sarah is now disillusioned with being in business with Ginger and considers calling it quits. She comes to you to find out how the business assets would be split up if she ended the business. She specifically wants half the value of all of the business assets remaining after the business is closed, plus an additional payment to make up for the extra administrative duties she has performed.

1. What form of business enterprise is Ziggy Poop Service and what is the relationship of Sarah, Ginger and Joe to that business?

2. How should the cost of the lost dog be handled in order to comply with Alaska law?

3. What advice will you give Sarah with respect to her rights to half of the business' remaining assets and extra compensation should the business be terminated?

GRADERS GUIDE

***** QUESTION NO. 7 *****

SUBJECT: BUSINESS LAW

1. What form of business enterprise is Ziggy Poop Service and what is the relationship of Sarah, Ginger and Joe to that business? (40 points)

Ziggy Poop Service is a general partnership at will. It was formed when Sarah and Ginger agreed to carry on a business for profit and share the costs and profits. Partnerships at will can be formed without written agreement or the filing of paperwork with the state. AS 32.06.202. Sarah and Ginger are therefore partners. They could not have formed a corporation, limited liability corporation or limited partnership since those business entities require the filing of organizational paperwork with the state as a precondition to formation.

Joe began working with the business after it was formed. He is receiving a 10% share of the profits but has no responsibility for the costs. While Sarah and Ginger could have admitted him as a partner, they did not do so. Instead his receipt of a share of the profits is in lieu of wages or compensation for acting as an employee of the business. The fact that Joe has no responsibility for sharing in the costs of the business bolsters the conclusion that he is acting as an employee or independent contractor and not as a partner in the business. Under AS 32.06.202, the sharing in the profits of a partnership gives rise to the presumption that the individual is a partner; but an exception to that presumption is where the individual receives the profit share in lieu of wages or compensation as an independent contractor or employee. AS 32.06.202(b)(3).

2. How should the cost of the lost dog be handled in order to comply with Alaska law? (20 Points)

A partnership is liable for loss or injury caused to a person as a result of a wrongful act or omission by a partner acting in the ordinary course of business of the partnership. AS 32.06.305. In addition, a partnership is required to indemnify a partner for liabilities incurred by the partner in the ordinary course of the business of the partnership. AS 32.06.401. Because the facts do not suggest that Ginger was not acting in the ordinary course of Ziggy Poop Services when the customer's dog escaped and was lost, the partnership is liable for that loss. Because Ginger fronted the cost of the loss, she is correctly asking that the partnership revenues for the month be used to cover that loss.

> Some applicants may also discuss the legal right of one partner to enter into a settlement agreement that binds the partnership. Pursuant to AS 32.06.301, a partner is an agent of the partnership and can bind the partnership when appearing to be carrying on the business of the partnership. The only exception to the partnership being bound by the acts of the partner apparently acting in the ordinary course of business is where the partner expressly lacks the authority to engage in the conduct and the person with whom the partner is dealing has actual knowledge of that lack of authority.

3. What advice will you give Sarah with respect to her rights to a share of the business assets and extra compensation should the business be terminated? (40 Points)

Each partner is entitled to an equal share of the partnership profits absent agreement otherwise. AS32.06.401(b). There are no facts to suggest that Ginger and Sarah agreed that the profit sharing would be other than equal between them. Further, under AS 32.06.401, a partner is not entitled to compensation for services performed for the partnership. Therefore, Sarah has no right to demand compensation for her administrative services.

When a partnership is set up, each partner is considered to have an account that is credited with the value of the money and assets the partner contributes to the partnership and the partner's share of profits. The account is charged with the value of any partnership assets distributed to the partner and the partner's share of liabilities and losses. AS 32.06.401(a). The balance of that account is what the partner is entitled to receive on winding up the partnership business. AS 32.06.807. If the $3000 payment for the lost dog that was paid by Ginger has not yet been reimbursed by the partnership, then Ginger's account will be credited with ½ of the $3,000 payment and Sarah's account will be debited for ½ of the $3,000 payment.

The Ziggy Poop Service partnership assets consist of the van which Ginger contributed and the other equipment, the cost of which was evenly shared by Ginger and Sarah. Upon the winding up of the partnership, Ginger will be credited with the value of the van and Sarah and Ginger will each be credited for contributing half of the remaining business equipment acquired at start up. They will also each be credited with one half of the profits (less Joe's 10%) since they are sharing profits equally. Sarah would not be entitled to receive half the value of the partnership assets since she did not contribute the van. Ginger will receive the value of the van she contributed to the partnership upon winding up the business. Ginger and Sarah would then evenly divide the remaining partnership assets.