

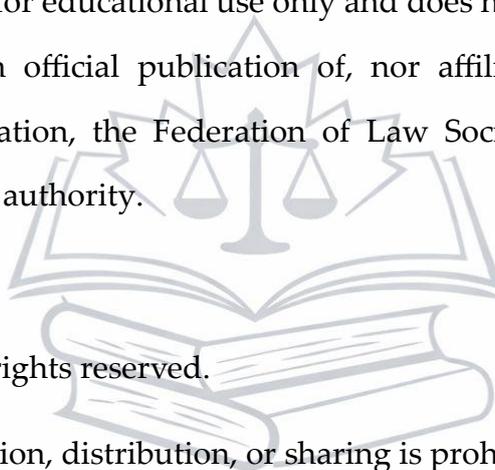
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## CHAPTER I: INTRODUCTION TO BUSINESS ORGANIZATIONS

### What is a Business?

A business refers to an organization engaged in activities that are commercial, industrial, or professional in nature. It can operate for profit or as a non-profit entity with a charitable or social purpose. There are three main forms of business structures: sole proprietorship, partnership, and corporation. Partnerships can be categorized further into General Partnerships, Limited Partnerships (LPs), and Limited Liability Partnerships (LLPs).

### Basic Forms of Business Organization

#### 1. Sole Proprietorship:

This is the simplest and oldest type of business structure. A sole proprietorship is owned and operated by a single individual, who makes all key decisions and bears full responsibility for the business. There is no legal distinction between the owner and the business, meaning they share the same identity under the law. This structure is attractive because it is straightforward to set up, inexpensive to operate, and easy to dissolve. Additionally, under Ontario's Business Names Act, a sole proprietor using their own name is not required to register the business name.

Despite its simplicity, this form of business carries significant risks, as the owner is personally liable for all debts and obligations incurred by the business. This lack of separation can expose personal assets to creditors. Furthermore, it may be challenging for sole proprietors to secure loans or other forms of financing due to the limited credibility of the structure.

#### Advantages:

- Easy and cost-effective setup.
- Flexibility in management and operations.
- Simplified dissolution process.

**Disadvantages:**

- Unlimited personal liability.
- Limited access to financial resources.
- No distinction between personal and business assets.

**2. Partnerships:**

Partnerships involve two or more individuals working together to run a business with the goal of generating profit. This structure allows for shared responsibility and flexibility in managing the business. Partnerships are relatively easy to establish and dissolve, though they require adherence to legal requirements, such as registration under the Business Names Act and notifying creditors when a partner leaves.

General partnerships have the drawback of unlimited liability for all partners, meaning that personal assets are at risk. However, Limited Liability Partnerships (LLPs) offer professionals the ability to limit their liability for the actions of other partners while maintaining active participation in the business.

Limited Partnership: Types of partners: 1. General Partner (unlimited liability), 2. Limited Partner (Limited Liability)

**3. Corporations:**

Corporations are created under laws such as the *Canada Business Corporations Act* or equivalent provincial statutes. The primary feature that distinguishes a corporation from other business structures is its recognition as a separate legal entity. This means the corporation has its own legal identity, independent of its shareholders, directors, or officers.

This separation provides numerous benefits, including:

- The ability to sue and be sued in its own name.
- Entering into contracts independently.
- Perpetual existence regardless of changes in ownership or management.
- Limited liability for shareholders, protecting their personal assets.

While corporations enjoy easier access to capital and tax advantages, they face higher administrative costs and obligations, such as filing annual returns and holding regular meetings. Incorporation also requires compliance with statutory procedures and regulations.

#### 4. Other Methods of Carrying on Business:

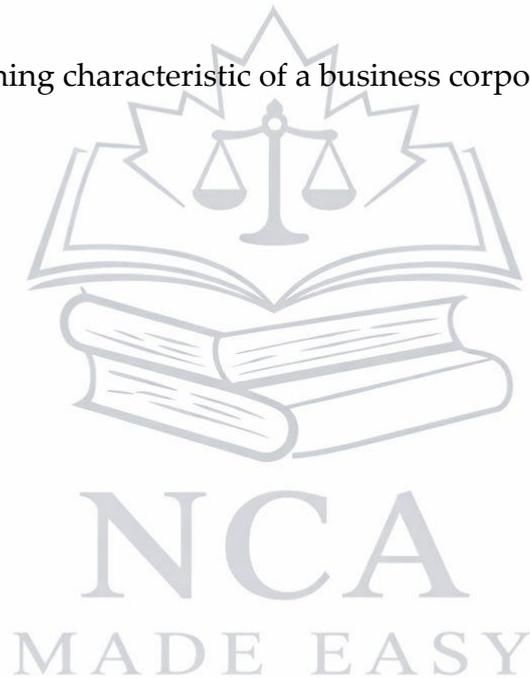
- **Unique Corporations:** Examples include banks governed by the Federal Bank Act and insurance companies regulated under the Insurance Act.
- **Joint Ventures:** Collaborative projects between two or more parties pooling resources for a specific goal, such as research and development. – Limited Period.
- **Strategic Alliances:** Agreements between independent entities to achieve mutual objectives, without creating a separate legal entity.
- **Licensing Agreements:** Contracts granting one party the right to use another's property, distinct from franchising. -IP
- **Franchising:** A business model where a brand is expanded through third-party operators under specific guidelines, as governed by laws like the *Arthur Wishart Act* in Ontario.
- **Distribution Relationships:** Agreements for selling another company's products.
- **Business Trusts:** Legal arrangements where trustees manage assets for beneficiaries, similar in some respects to corporations.

#### Conclusion:

In summary, the choice of business structure plays a crucial role in determining the legal and financial responsibilities of the owners. While sole proprietorships offer simplicity, partnerships provide shared management, and corporations ensure limited liability and perpetual existence. Alternative forms like joint ventures, strategic alliances, and business trusts cater to specific business needs. Understanding these structures is essential for effectively navigating the legal and operational aspects of business organizations.

**POTENTIAL EXAM QUESTIONS:**

1. **Sam** is debating whether to incorporate their business. They currently operate a sole proprietorship; however, they would like to grow their brand and require more capital to do so. Sam has attended the bank, and they expressed reservations about lending money to a sole proprietorship. Advise Sam.
2. **Alex** is a licensee. The licensor in the arrangement has become very involved in Alex's business operations. Alex is concerned, as they originally contracted into the license agreement to maintain autonomy and conduct their business without interference. Is it possible that although a license agreement was entered into, this relationship may be legally deemed a different form of business?
3. What is the defining characteristic of a business corporation?



## NCA SAMPLE QUESTION AND ANSWER

### Question 1: 40 Marks

After the untimely death of his partner Miles Archer, Sam Spade continued his Vancouver agency under the name of Sam Spade. Several years later, one Sarah Spade visited his office claiming to be his daughter. Sarah demanded that Sam make her a partner in his agency, but Sam refused. "Archer and his wife were such a nuisance. I'll never take on another partner as long as I can walk. But if you want to work for me, I'll buy you a yellow trench coat and all the cigars you want, and pay you 20 bucks a week plus expenses and 20% of the profits."

Sam Spade continued to carry on the agency's business in the name of Sam Spade. Nevertheless, when occasional bills arrived in the name of Spade & Spade, he was as likely to pay those bills as any others. Sarah never complained. "Maybe someday he'll really treat me like a partner after all," she mused.

Ten years later, Sam had taken to drink. Business fell off and creditors called. After Sam had hounded Sarah for weeks to pay the creditors ("You'll find it pays off, kid, we'll work together to make sure it'll pay off for you once business picks up again"), Sarah began paying the creditors with her personal funds. One day when Sam became particularly abusive, Sarah finally left. On her way through the door, she yelled, "You were never a father to me, you faked the agency books for years, and you never do any work, though you were never any good anyway, you rat. I know you've siphoned off thousands to Archer's widow for you two to use later, and I'll get my share of it. You'll send my lawyer a certified check for my share of this filthy business or I'll see you in court."

### Answer the Following Questions:

- (a) Does Sarah have any share coming to her? How big a share?
- (b) The agency has no funds that a court can locate, and Sam has disappeared with Archer's widow. Can the creditor that sent its bills to Spade & Spade collect from Sarah?
- (c) If Sarah were a partner, would she be liable for Sam's liquor bills? What if Sam charged the liquor to the office account?

### Sample Answer

#### **Issues:**

- (a) Does Sarah have any share coming to her? How big a share?
- (b) The agency has no funds that a court can locate, and Sam has disappeared with Archer's widow. Can the creditor that sent its bills to Spade & Spade collect from Sarah?
- (c) If Sarah were a partner, would she be liable for Sam's liquor bills? What if Sam charged the liquor to the office account?

#### **Rules:**

##### Statutory Framework – Ontario Partnership Act (PA):

- s. 2 – Definition of partnership: carrying on business in common with a view to profit.
- s. 3(1) – Rules for determining existence of partnership.
- s. 3(1)(c) – Profit-sharing as remuneration for services is not by itself proof of partnership.
- s. 6 – Mutual agency: acts of a partner in the usual course bind the firm.
- s. 10(1) – Partners are jointly liable for debts/obligations incurred in ordinary course while they are partners.
- s. 15(1) – Holding-out: liability where a person represents or knowingly allows themselves to be represented as a partner and credit is given in reliance.
- s. 24(1) – Equal share in capital and profits unless otherwise agreed.
- s. 24(2) – Right to indemnification for payments made in ordinary/proper conduct of business.
- s. 29 – Duty to account for private benefits from use of partnership property, name, or business connection.

Case Laws:

- *Cox v. Hickman* – Mutual agency is the decisive test for partnership.
- *Waugh v. Carver* – Profit-sharing is strong evidence of partnership but not conclusive.
- *Tower Cabinet Co. Ltd. v. Ingram* – Holding-out requires knowledge of representation.
- *Volzke Construction Ltd. v. Westlock Foods Ltd.* – Control is not determinative; conduct and agreement are key.
- *Pooley v. Driver* – Courts may find a partnership despite stated intentions if conduct supports it.
- *Continental Bank v. R.* – Examine total relationship; conduct and intention matter more than labels.

**Analysis:**

(a) Share Entitlement

Under s. 2 PA, partnership requires (i) a business, (ii) carried on in common, (iii) with a view to profit. The detective agency is clearly a business. The real issue is whether Sarah carried it on “in common” with Sam as a partner.

Sarah’s \$20/week plus expenses and 20% of profits falls under s. 3(1)(c), profit-sharing as remuneration for services. This is an explicit statutory exception, so profit-sharing alone is not conclusive (*Waugh v. Carver*). Applying *Cox v. Hickman*, mutual agency is decisive, and there is no evidence Sarah had authority to bind the firm or deal with third parties on its behalf (s. 6 PA). Sam’s refusal to take her as a partner and his unilateral control indicate no mutual agency.

The “in common” requirement is absent. *Continental Bank* and *Volzke* show we must look to conduct: Sarah hoped “maybe someday” to be a partner, showing she knew she was not one at the time. Her later payment of firm debts was voluntary. If she were a partner, s. 24(2) would entitle her to indemnification; as a non-partner, she is merely a creditor.

However, a contrary argument exists under *Pooley v. Driver*: the use of “Spade & Spade” over ten years, her awareness of it, and Sam’s occasional statements about “working together” could allow a court to infer a de facto partnership. If so, s. 24(1) applies, equal (50%) share in profits and capital in absence of contrary agreement.

(b) Creditor Recovery

If Sarah is not a partner, s. 15(1) PA provides that a person who represents themselves or knowingly allows themselves to be represented as a partner is liable to anyone who gives credit in reliance on that representation. Here, Sarah saw invoices addressed to “Spade & Spade” and never objected, which can be passive acquiescence (Tower Cabinet). If the creditor proves reliance on that belief, she is liable even without actual partnership.

If she is a partner, s. 10(1) makes partners jointly liable for debts incurred in the ordinary course. Agency service bills are clearly within the ordinary business of a detective agency (s. 6 PA), so she would be liable automatically.

(c) Liability for Liquor Bills

Under s. 6 PA, the firm is only bound by acts done in the usual course of its business. Buying liquor for personal consumption is plainly outside the usual scope of a detective agency’s operations. Even if charged to the office account, the key question is whether the supplier could reasonably believe it was for firm purposes. If it was for entertaining clients or otherwise connected to the business, it could bind the firm; otherwise, s. 29 PA requires Sam to account for personal benefits, and the other partners (including Sarah) would not be liable.

**Conclusion:**

Therefore, based on the facts and the above analysis:

- (a) Most likely no partnership and no share; Sarah is entitled only to repayment of advances. However, if a partnership is found, s. 24(1) gives her a 50% share.
- (b) Creditor can recover if holding-out and reliance are proven, or automatically if partnership exists.
- (c) Sarah is not liable for Sam’s personal liquor bills unless they were genuinely within the firm’s business expenses.