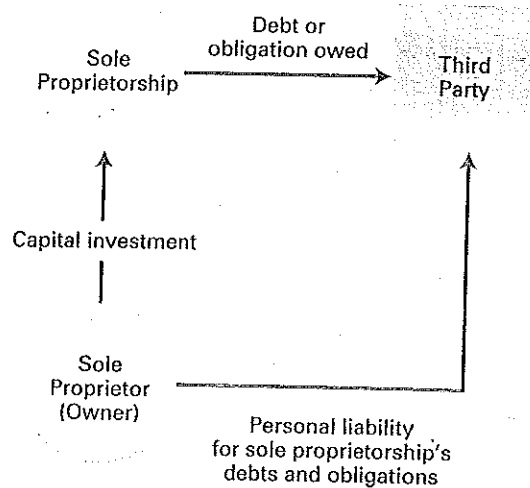


Exhibit 14.1 SOLE PROPRIETORSHIP



Assume that after several months, Nathan closes the business because it is unsuccessful. At the time it is closed, the business has no assets, owes the bank \$100,000, and owes other debts of \$25,000. Here, Nathan, the sole proprietor, is personally liable to pay the bank and all the debts of the sole proprietorship from his personal assets.

In the following case, the court had to decide the liability of a sole proprietor.

CASE 14.1 *Sole Proprietorship***Bank of America, N.A. v. Barr**

9 A.3d 816 (2010)

Supreme Judicial Court of Maine

"An individual doing business as a sole proprietor, even when business is done under a different name, remains personally liable for all of the obligations of the sole proprietorship."

—Alexander, Judge

Facts

Constance Barr was the sole owner of The Stone Scone, a business operated as a sole proprietorship. Based on documents signed by Barr on behalf of The Stone Scone, Fleet Bank approved a \$100,000 unsecured small business line of credit for The Stone Scone. Fleet Bank sent a letter addressed to Barr and The Stone Scone, which stated, "Dear Constance H Barr: Congratulations! Your company has been approved for a \$100000 Small Business Credit Express Line of Credit." The bank sent

account statements addressed to both The Stone Scone and Barr. For four years, Fleet Bank provided funds to The Stone Scone. After that time, however, The Stone Scone did not make any further payments on the loan, leaving \$91,444 unpaid principal. Pursuant to the loan agreement, interest on the unpaid principal balance continued to accrue at a rate of 6.5 percent per year. Bank of America, N.A., which had acquired Fleet Bank, sued The Stone Scone and Barr to recover the unpaid principal and interest. Barr stipulated to a judgment against The Stone Scone, which she had converted to an limited liability company, but denied personal responsibility for the unpaid debt. The trial court found Barr personally liable for the debt. Barr appealed.

Issue

Is Barr, the sole owner of The Stone Scone, personally liable for the unpaid debt?

(continued)

Language of the Court

The trial record contains sufficient evidence that Barr is personally liable for the debt owed to Bank of America. The evidence demonstrates that, at the time Barr acted on The Stone Scone's behalf to procure the small business line of credit, she was the owner of The Stone Scone and the sole proprietor of that business. An individual doing business as a sole proprietor, even when business is done under a different name, remains personally liable for all of the obligations of the sole proprietorship. As the sole proprietor of The Stone Scone when that sole proprietorship entered into the agreement for a line of credit with Fleet Bank, Barr became personally liable for the debts incurred on that line of credit account.

Decision

The supreme judicial court affirmed the trial court's judgment that held Barr personally liable, as the sole proprietor of The Stone Scone, for the sole proprietorship's unpaid debt owed to Bank of America.

Case Questions

Critical Legal Thinking

What is a sole proprietorship? What are the main attributes of sole proprietorship?

Ethics

Did Barr act ethically in denying responsibility for The Stone Scone's debts?

Contemporary Business

Why are sole proprietors held personally liable for the debts of their businesses?

Taxation of a Sole Proprietorship

A sole proprietorship is not a separate legal entity, so it does not pay taxes at the business level. Instead, the earnings and losses from a sole proprietorship are reported on each sole proprietor's personal income tax return. A sole proprietor has to file tax returns and pay taxes to state and federal governments.

General Partnership

General partnership, or ordinary partnership, has been recognized since ancient times. The English common law of partnerships governed early U.S. partnerships. The individual states expanded the body of partnership law.

A general partnership, commonly referred to as a partnership, is a voluntary association of two or more persons for carrying on a business as co-owners for profit. The formation of a general partnership creates certain rights and duties among partners and with third parties. These rights and duties are established in the partnership agreement and by law. General partners, or partners, are personally liable for the debts and obligations of the partnership (see Exhibit 14.2).

Formation of a General Partnership

A business must meet four criteria to qualify as a general partnership under the UPA [UPA Section 6(1)]. It must be (1) an association of two or more persons (2) carrying on a business (3) as co-owners (4) for profit. A general partnership is a voluntary association of two or more persons. All partners must agree to the participation of each co-partner. A person cannot be forced to be a partner or to accept another person as a partner. The UPA's definition of *person* who may be a general partner includes natural persons, partnerships (including limited partnerships), corporations, and other associations. A business—a trade, an occupation, or a profession—must be carried on. The organization or venture must have a profit motive in order to qualify as a partnership, even though the business does not actually have to make a profit.

general partnership
(ordinary partnership)

An association of two or more persons to carry on as co-owners of a business for profit [UPA Section 6(1)].

general partners (partners)

Persons liable for the debts and obligations of a general partnership.

Uniform Partnership
Act (UPA)

A model act that codifies partnership law. Most states have adopted the UPA in whole or in part.