



Business Relationships and the Law

Introduction to Bus Orgs
The Law of Partnership
Reading – CACL Chapter 15, 16

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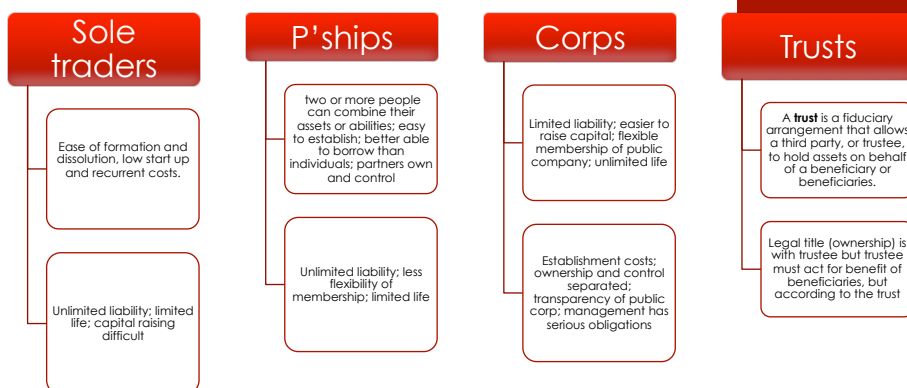
Introduction to Business Relationships

- See the brief introduction to each of the forms of business organizations
 - Agency- NOT EXAMINABLE CHAPTER 15
 - Sole trader- NOT EXAMINABLE
 - Trust- NOT EXAMINABLE
 - Partnership
 - Corporation

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Comparisons: see CACL 16.65

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Intro to law of agency

- The key point is that the **law of agency** allows one person to authorise another person to do any act that he or she has capacity to do themselves. *And when the agent does act, the principal has to bear the consequences:* see CACL 15.10
- We will only deal with agency as it affects partnerships and corporations

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The Law of Partnerships

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Major learning outcomes

- Broadly
 - to appreciate the role of both the Partnership Act and the common law in the creation and management of partnerships
- Specifically
 - To understand **what a partnership is** and **how it can be created**
 - To understand the **special relationship** that exists **between partners**
 - To understand the **liability of partners is unlimited**
 - **To analyze the liability of partners** a) under contract or b) in tort
 - To understand what occurs when a partnership dissolves, particularly in relation to liability and **property**
 - To understand the concept of the **limited partnership** and why they are now increasingly common

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1. Creation and definition

■ Introduction: see CACL 16.10

- **Relevance:** eclipsed by the rise of the corporation (and its main feature of *limited liability*) but still common in relation to:
 - Small family businesses
 - By design or default
 - Professional associations like lawyers and accountants
 - Mandatory
 - Some are now “limited partnerships” and “limited liability” partnerships
- **Legal relationship:** Partners are **both principals and agents** of each other
 - A partner is **able to bind his/her other partners** (as an agent) and
 - A partner **may be bound by the acts of the other partners** (as a principal is)

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■ Formation (CACL 16.20)

- Partnership is **created by agreement** - express (oral or written) or implied
 - A **formal partnership agreement** (accountants, doctors, lawyers etc) might deal with membership, capital, entitlement, management, accounts, dissolution, dispute resolution, goodwill etc (see CACL 16.210)
 - Many p'ship agreements are **less formal** (eg H-W run café)
 - **PA has an *interstitial*** (filling the gap in the partnership agreement if any, but can be chosen if the partnership act should convene or not) **role – that is, it plugs gaps in any partnership agreement**

■ Number and name (CACL 16.60)

- **Corps Act s115** – max no. is 20 except where it is **professional** (see footnote 9 p451)
- **Name** _ (CACL 16.100) - Reg'n required under **BN Reg'n Act** unless the name consists of the full name of each partner

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2. Nature and definition: CACL 16.110

- If **no agreement by the parties** the **courts** have to decide **if a partnership exists**.

- The courts look to **ss5 and 6 of the Act**:

1. **Section 5** defines a partnership as **'the relation that exists between persons:**

- **carrying on a business**
- **in common**
- **with a view of profit'**

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■ 1. **'Carrying on a business'**- cannot be one-off

- *repetitive or regular acts* done in relation to 'any trade, occupation or profession'
- **'business'** is any 'trade, occupation or profession' (cf hobby) see tax cases
- **'carrying on'**
 - **Smith v Anderson** – CACL 16.120
 - > 20 investors in shares owned by a trust tried to wind up the trust because it was not registered as a p'ship BUT as there were no **mutual rights and obligations** between subscribers = no partnership.
 - repetition is the key—one-off is more likely to be a joint venture

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- need a pattern or series of acts....but **when does it start?**:
 - **Khan v Miah** (CA 16.130)
 - Study facts carefully
 - Why was it important whether a p'ship existed?
 - If partnership exists, K entitled to a distribution of p'ship assets on dissolution.
 - HL said premises were p'ship property, ordered sale of the property and distribution of proceeds.
 - ie no rule of law that no p'ship cannot exist until trading commences...
 - **Goudberg v Herniman Associates** (CA 16.135)
 - Study facts
 - Why was it important whether a p'ship existed? If p'ship exists, G and W, respectively, jointly liable for fees/price.
 - No p'ship – only W liable because they were not "carrying on a business" when HA did the work. Not "preparatory" (as it was in K v M).
 - **Keith Spicer Ltd v Mansell** (CA 16.140)
 - Study facts carefully
 - Why was there not a partnership? What was the consequence?

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- **2. 'in common' – needs to be a "mutuality of rights and obligations"**
- the business must be operated by or on behalf of all the partners.
 - All members need *not* be active in management as long as it is being carried on on their behalf.
 - **Degorgio v Dunn (CA 16.150)**
 - Facts: rock band re-formed.
 - Issue: partnership ?
 - Decision: not a partnership.
 - Why did it matter whether it was a partnership?
 - **Re Ruddock (CA 16.155)**
 - Even though R and B said that B was **not** a partner, the court said she was. There was *in fact* a "mutuality of rights and obligations". Therefore not entitled to priority as a creditor.

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- **3. 'with a view to profit'** (CACL 17.57)
 - Need to intend to make a profit – even if you don't
 - members of sporting clubs, societies or charitable orgs are not 'partners'.
 - Why does it matter?
 - Even though these orgs make profits these are not shared among the members and *the members are not liable for the debts incurred by the committee in excess of their subscriptions*

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2. Section 6: the Statutory Rules

- The Partnership Act provides that in determining whether *or not* a p'ship exists "regard shall be had" to the following rules (CACL 16.170)

Rule 1—common ownership: s6(1) – CACL 16.175

- Common or joint ownership of property (like land or buildings) does **not** necessarily mean that the common owners are in a partnership....must be *carrying on business in common* (see s5)

Rule 2—sharing of gross returns: s6(2)

- Sharing of **gross returns** does **not** mean the sharers are in a partnership (eg real estate agents who receive a wage based on the annual gross profits of the agency): **Cribb v Korn** (CACL 16.180)
 - Farmer – Owner (Cribb) – Worker (Korn)
 - Why was it important for K to show that C was a partner with K's employer?

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Rule 3—profit sharing: s6(3)

- **Sharing of profits** is **not conclusive proof of p'ship** but creates a **strong presumption** (*prima facie evidence*) that there is a partnership; the other party has the **onus** of proving there is **not** a partnership
- See, for example, **Cox v Hickman** (CACL 16.185)
 - Smith and Co owe \$ to creditors inc Cox
 - Under Deed, trustees to run business and pay all profits to C et al until debt paid off - then hand back business to S
 - H supplied materials - became trade creditor making firm liable to pay
 - Issue – Was Cox et al “partners” with S and therefore liable for debts of the business?
 - Decision ?

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- The Act gives examples where the presumption does **not** operate (because there is no ‘mutuality of rights and obligations’):
 - **s6(3)(a)**-a **debt repaid in instalments out of profits** (eg **Cox v Hickman** CACL 16.185)
 - **s6(3)(b)**-a **wage paid on the basis of a share of profits** (eg **Plummer v Thomas** CACL 16.186)
 - **s6(3)(c)**-payment of an annuity to a widow or child of a deceased partner
 - **s6(3)(d)**-loan with the interest dependent on profits
 - **s6(3)(e)**-annuity for goodwill part of sale of business dependent on profits

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3. Rights and Duties of partners to each other

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1. **Partnership Agreement** (CACL 16.210)
2. **General rights and duties under PA: s28** (CACL 16.211):
 - Share equally in capital and profits and losses: s28(1)
– see *Popat v Schonchhatra* CACL 16.212
 - Firm indemnifies every partner for firm-related expenses: s28(2)
 - Every partner may take part in management: s28(5)
 - No partner entitled to remuneration: s28(6)
 - No person can be introduced without consent of all: s28(7)
 - Decisions to be decided by majority: s28(8)
 - Books to be kept at the place of business and all have access: s28(9)
3. **Restriction on right to expel a partner: s29** (CACL 11.23)

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4. Fiduciary obligations to each other

- P'ship is founded on **mutual trust and confidence** – gives rise to a **fiduciary duty** of full disclosure towards each other. Partners bound to exercise good faith which continues right through to dissolution:
- **Chan v Zacharia** (CACL 16.215)
 - C and Z were medical practitioners
 - Option to renew in lease
 - On dissolution, C negotiated new lease in his own name
 - Held: partnership is a fiduciary relationship – it continues until winding up – C had breached this fiduciary duty
- **Scotts v Lewarne** (CACL 16.230)
 - W agreed to sell a hotel to a company owned by S. S needed about \$400k and approached L asking for \$300k. L agreed, in exchange for equity and profits. S used the money to discharge his mother's mortgage, transferred that property into his name and used the property as security for a loan which he used to purchase the hotel business
 - it was a breach of fiduciary duty to use L's \$300,000 in that way.

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5. Statutory duties (reflecting common law fiduciary duties)

CACL 16.213

- Partners must **render true accounts and full information** of all things affecting the partnership: s32
- Duty to **account for benefits** derived from dealings with partnership without consent or for use by any of them of the p'ship property, name or business connection: s33(1)
- Duty **not to compete** with partnership: s34

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4. Partnership property (CACL 16.270)

- **Issue: determining what is the property of the p'ship is important particularly at the end of the p'ship relationship.**
 - For example, when p'ship ends one partner may demand the return of the van or the computer or the expensive painting....can have it only if it is *his or her* property (and not *p'ship* property).
- **Under s24** p'ship property includes:
 - items *brought into* the partnership property as *partnership* property. Whether property has been brought in as p'ship property depends on **intention**;
 - items acquired *on account* of the firm;
 - items acquired *for the purposes of* and in the course of the partnership business
- **Under s25:**
 - items bought with p'ship money are deemed to have been bought on account of the firm unless contrary intention appears.

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- **What right does each partner have to the p'ship property?**
 - Partners have **no title to specific property** (eg the painting on the wall or the car) but a **right to his/her proportion of the surplus after the realisation of assets and the payment of debts**: CACL 16.290
 - See **Harvey v Harvey** (CACL 16.280)
 - Land never became part of the p'ship property. Why?
 - 'Goodwill' – also part of the p'ship property (CACL 16.320)

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5. Liability of partners to third parties

5.1. Liability for debts and obligations (contracts): ss 9 & 13

- Each partner is liable *jointly* with the other partners for all debts and obligations of the firm incurred while he/she is a partner: **s13**.
- A partner (acting as an agent) will bind co-partners where
 - he/she *does any act or enters into a transaction*
 - That is within the scope of *kind of business carried on by the partnership*; and
 - is carried out in *the usual way* that partnerships of that kind conduct business;
 - UNLESS the partner had no authority to so act and
 - the third party knew this, or
 - the third party did not know or believe that the partner was a partner: **s9**.

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- **Two limbs**

- 1. Ask: 'what is the **kind of business** of the partnership?'
 - **Mercantile v Garrod** (CACL 16.390)
- 2. Even if the action of the partner was within the scope of what the partnership normally does, it must be done in **the usual way** if it is to bind the other partners.
 - **Goldberg v Jenkins** (CACL 16.393)

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- 3. Did the other person know or believe there was no authority or did not believe him to be a partner
 - **Construction Engineering v Hexyl** (CACL 16.395)

- **Joint liability: s13** (CACL 16.400)

- **The creditor would sue each and every partner jointly up to the full amount - but creditor can only sue once**
 - A partner or partners who is sued can insist that other members be 'joined' in the one (and only) action.

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5.2 Liability of partners to third party for wrongful acts of a partner: ss14-15

- Each partner is liable for any loss or harm caused to a third person while acting 'in the ordinary course of the business of the partnership' or 'with the authority of the co-partners': **s14**.
- This needs to be answered by looking at the p'ship agreement and the business of the p'ship
 - **Walker v European Electronics** (CACL 16.480)
 - See the facts
 - G was acting in the "ordinary course of the business" and therefore the other partners were jointly and severally liable.
 - **National Bank v Batty** (CACL 16.490)
 - See the facts
 - Davis was *not* acting in the course of the firm's business or within authority when he fraudulently deposited cheques into the firm's account and then misappropriated them
 - **Polkinghorne v Holland & Whittington** (CACL 16.500)
 - See the facts
 - Why were the solicitors liable to P even though H provided investment advice and *not* legal advice?
- **Joint and several liability:** P could sue one (or more) partners and receive the full amount and leave it to the partner/s who has/have been sued to get the others to contribute according to their share of the liability

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6. Dissolution of a partnership

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- Overview (CACL 16.550)
- A partnership may be terminated by
 - Operation of law (s37) (CACL 16.560)
 - The partners – 5 circumstances (CACL 16.570)
 - The courts (s39) – 6 circumstances (CACL 16.580)
- Partners remain jointly liable for debts even after dissolution of a partnership: (CACL 16.590) **Hammersmith v Ogge** (CACL 16.430)
- Application of p'ship property on dissolution: s48 (CACL 17.570)
- Final settlement of accounts on dissolution: s48 (CACL 16.640)

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7. Limited Partnerships

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- The concept: CACL 16.660
 - Must be one partner who has unlimited liability
 - And one who has limited liability – usually a partner who invests money in the partnership – but cannot take part in management
- The legislation: CACL 16.660
- Incidents of limited partnerships: CACL 16.670

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