Partnership Agreements: changing them needs partners' consent

Section 19 of the Partnership Act 1890 provides:

"The mutual rights and duties of partners, whether ascertained by agreement or defined by this Act, may be varied by the consent of all the partners, and such consent may be either express or inferred from a course of dealing."

It often happens that during the course of a partnership business the partners' practices diverge from the strict provisions of the partnership agreement they may have signed some years ago. The question is whether such a practice has had the effect of changing (varying) the terms of the partnership agreement for the future as opposed to on a one-off basis.

In *Patel v. Patel* [2019] EWHC 298 (Ch), the English High Court found that the dealing of the partners in relation to the allocation of profits did not infer a consent of the partners to vary permanently the written partnership agreement provisions on equal sharing.

FACTS

The two parties had entered into two separate partnership agreements for the running of two separate dental practices. The Claimant was the uncle of the Respondent's then husband. The Claimant had provided most of the capital for each partnership. However it was the understanding that the Respondent would carry out the work at the practices. Both partnership agreements provided that the parties would share the profits and losses equally. That was in any event the default position under section 24 rule (1) of the Partnership Act 1890.

For the first two years of business the Claimant agreed in each year that the Respondent could have 100% of the profits of practice A. Both parties had signed the partnership accounts to that effect. After the Respondent and the Claimant's nephew divorced a dispute arose over the division of the profits. It was submitted to arbitration. The Claimant sought a binding decision that he was entitled to half of the profits of both practice A and practice B.

The Respondent claimed that in respect of the partnership for practice A, there had been a course of dealing from which it could be taken that the partnership agreement had been varied to give her 100% of the profits.

At the end of the hearing, in his award the arbitrator found that the allocation of profits over 2 years to the Respondent alone amounted to an agreement between the parties to change the profit sharing provisions of the partnership agreement for practice A to 100% to the Respondent and 0% to the Claimant and made an award to that effect.

The Claimant sought to annul the award in Court on a number of grounds, including

1. an "obvious error of law" in finding that the agreed allocation over 2 years could amount to a consent to change the partnership agreement for the future.

The Court found that the arbitrator had obviously erred in law in finding that the 2 years' alteration of profits applied to the future.

It found that for there to be a change in the partnership agreement under section 19 through a course of dealing, the dealing had to be objectively capable of an 'unambiguous interpretation' showing consent to alter the terms of the partnership agreement.

Applying this legal principle to the conduct over 2 years in this case, there could be no objective basis for a conclusion of consent to change the partnership agreement for the future. The arbitrator had therefore erred in his application of the law and the award fell to be altered.

DISCUSSION

Course of Dealing Altering Partnership Agreement

The court made it clear that the focus on a course of dealing must be to see if it amounts to a consent to vary for the future indefinitely, and that this should not readily be inferred.

However each case will have to be decided on its own facts.

It was always going to be difficult for the Respondent partner to argue that merely because the Claimant had agreed to give her 100% of the profits over each of two years, that this meant that he had renounced to ever have a share of the profits in the future.

A couple of factors made this contention difficult :

- the fact that the Claimant was to have no profits at all despite having made a very substantial capital contribution
- the fact that the consents stretched only over 2 years.

Lessons

When considering the effect of dealing which has diverged from a partnership agreement, the key is to have regard to what, if any consent, there was in nature of the dealing, objectively assessed.