

The risk of uncertain partnership arrangements

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The risks for partnerships operating without a written partnership agreement in place are well known. A recent Court of Appeal case is a useful reminder that these risks can arise in the period after new partners join a business but before a new formal agreement is signed.

Cheema v. Jones and others

In *Cheema v. Jones and others* [2017] EWCA Civ 1706, the Court of Appeal considered a dispute in relation to a medical practice. Two doctors had a written partnership agreement (the Original Agreement) and invited three further doctors to join them in the practice. The new doctors started working at the practice whilst the terms of a new partnership agreement were negotiated.

Prior to signing the new agreement a dispute arose. Cheema (the Appellant), who was one of the original partners, apparently suggested (to one of the new partners) that the other original partner, Jones, should retire. Jones was informed and "berated [the Appellant] in unflattering terms". The dispute escalated. The Appellant was ultimately prevented from seeing patients and accessing medical records. He issued proceedings, based on the Original Agreement, to enable him to return to the practice.

The crux of the claim, by the time it came in front of the Court of Appeal, was which agreement governed the relationship between the five doctors.

The Original Agreement needed the Appellant to agree to dissolve it. The Appellant argued that the Original Agreement still existed and the three new partners were not admitted as new partners. The other four doctors argued that a "partnership at will" was created between the five doctors. In the absence of an express or implied agreement as to how it will come to an end, a partnership at will exists indefinitely, but can be dissolved at any time by one partner serving notice on the other partners. As a result, the four doctors argued that the new partnership was dissolved by a notice they had served, and they were therefore free to set up another partnership without the Appellant.

The Court of Appeal agreed with the four doctors. Put simply, the new doctors had started working at the practice and on the facts in this particular dispute this created a new partnership between the five partners. As the negotiations focused on a new partnership agreement between all five doctors, and there was never a reference in those negotiations to the Original Agreement as a fallback position, the court concluded it should infer that the original partners intended to abandon the Original Agreement. The fact that the new agreement was never signed did not change this. Given that the partnership existed between the five doctors without a formal written agreement, it was deemed to be a partnership at will. Therefore, contrary to what the Appellant had presumably expected before the dispute arose, it could be easily dissolved without his consent.

What this means

In situations where someone is invited to join existing partners in a business, if the new partner is unaware of the existing agreement or claims not to be bound by it (the obvious example is that those involved started negotiating new terms), then the new partner's arrival may well create a new partnership between all of the partners and cause the existing written agreement to cease to be effective.

The terms of such a new agreement will depend on the facts. It is understandable that existing partners may assume that until a new written agreement is in place the old terms will apply, but that may well not be the case. The *Cheema* case is a salient reminder of the importance of formalising the partnership agreement in writing as quickly as possible. Such an agreement needs to accurately reflect the key arrangements and negotiating these can take time. If this negotiation process occurs concurrently with the new partners taking part in the business then a new unwritten partnership arrangement may well arise.

As this case shows, unintended consequences can follow. Given the assets, liabilities and goodwill involved in a medical practice, the original partners understandably wanted to ensure the partnership could not be easily brought to an end. The Original Agreement required unanimity on key decisions, including dissolving the partnership, and the original partners may well have presumed (before the dispute arose) this continued until the new agreement was in place. However, the court decided that a partnership at will applied prior to the new written agreement being in place, and this significantly lowered the threshold to dissolve the partnership.

The absence of a written partnership agreement can have other uncertain consequences. These will depend on the facts of any situation. When a partnership is dissolved its assets are pooled and after paying off the partnership's debts and liabilities anything remaining is distributed between the partners. If one partner brought substantially more assets into the partnership, yet it comes to light that the other partner had incurred significant liabilities on behalf of the partnership, the first partner may receive far less than he expected on dissolution.

In conclusion, when a partnership is formed or new partners join the business, it is in the best interests of all involved to ensure (if at all possible) the formal written agreement is in place prior to those involved carrying on the business together. Otherwise, a dispute arising whilst the new terms are negotiated could well produce unforeseen and unpleasant outcomes.

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