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REFORM OF GENERAL PARTNERSHIP LAW: THE AGGREGATE VERSUS ENTITY DEBATE

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I. THE CONTEXT FOR REFORM

1. Introduction

[1] In 2005, the Uniform Law Conference of Canada embarked on the following inquiry: what, if anything, should be done to reform partnership law in Canada? The timeliness of this inquiry is evident. In 1994 the National Conference of the Commissioners on Uniform State Law (NCCUSL) adopted the Revised Uniform Partnership Act (RUPA)[1]. The RUPA substantially revised the 1914 Uniform Partnership Act that had been adopted by all States, with the exception of Louisiana. In 1997, further amendments to the RUPA included provisions pertaining to limited liability partnerships (RUPLA). As of 2005, three (3) States have enacted RUPA (1994),[2] twenty-nine (29) States have enacted the RUPLA[3] and two (2) States were in the process of adoption.[4]

[2] In 2003, the United Kingdom (UK) Law Commission and the Scottish Law Commission authored a report on Partnership Law, which report included a revised Partnership Act (Draft Bill).[5] To date, the reforms proposed in the Law Commission's joint report have not been implemented. This report is of particular interest in Canada as the provincial and territorial Partnership Acts are essentially an adoption of the United Kingdom's 1890 Partnership Act.[6] As a result, Canadian partnership law, with the exception of Quebec, enjoys a high degree of uniformity.

[3] Partnership law predates its statutory regulation as one of the simplest and oldest forms of business association. To operate in partnership, two or more persons must agree to carry on business with one another, with a view to a profit.[7] Although the concept is simple, since its inception, civil jurisdictions and common law jurisdictions have characterized the partnership business form differently. Both the UK 1890 Partnership Act and the United States 1914 Uniform Partnership Act adhered to an 'aggregate' approach to partnership. The aggregate approach characterizes a partnership as a mere aggregation of its individual partners; it is not an entity separate and distinct from its partners. In the absence of other statutory entitlements to do so, the partnership is not an

entity capable of holding property, entering into contracts, suing or being sued it is own name or continuing after the removal, death or disassociation from the partnership of one of the partners. Rather, it is a merely a collection of the rights and liabilities of the partners.

[4] The debate over entity and aggregate status of the partnership business form is not new.[8] In fact, Canadian common law jurisdictions have not strictly adhered to the aggregate approach to partnerships but have enacted procedural law allowing partnership with a registered business name to sue and be sued in its own name[9], allowing for execution against partnership assets held in the name of the partnership,[10] allowing for the registration of interests in personal property in the business name of the partnership and the ability to enforce those interests.[11]

[5] In both the RUPA (US) and the Law Commission Draft Bill, the drafters have continued along the path of abandoning strict adherence the 'aggregate' view of the partnership in favour of a partnership being granting separate legal entity status.[12] However, in both cases, the reforms do not completely abandon the attributes of the aggregate status of partnership. In both the US and the UK, the aggregate approach is being retained for tax purposes.[13]

2. Motivations for Reform (US and UK)

[6] So what are the motivations for reform of partnership law and do they resonate in the Canadian context? In both the US and the UK, two practical problems were identified with continuing to conceptualize partnerships as an aggregate of partners rather than a separate legal entity. As an aggregate of the partners, when the composition of the partnership changes (e.g. death, retirement) the partnership terminates, with either the formation of a new partnership to continue the partnership business, or the partnership business being wound-up. The decision to change a partnership to its own separate legal entity facilitates the continuation of the business upon change in composition of the partnership, rather that resulting in a winding-up of the business.[14]

[7] The second motivation to change from entity to aggregate status is to avoid problems with property ownership, particularly related to the ownership of real property.[15] As the partnership is not an entity, it has no ability to own property. Rather, partnership property is the joint property of all partners. There are some difficulties associated with registration of the partnership interests in title-based property registries and difficulties in determining rights to or against the assets of the partnership when the composition of the partnership changes. As an entity, a partnership would be capable of holding title to property. However, entity status would not solve the difficulty in determining whether property is partnership property or separate property of the partners.

[8] In Canada, the law applicable to general partnerships has never undertaken a substantial revision. Reforms to date have resulted in the creation of new business forms such as the limited partnership,[16] and, in many jurisdictions, professional limited liability partnerships.[17]

[9] In the United States, the project for reform was motivated in large part by interest from the Business Law Section of the American Bar Association (ABA). The consultation process commenced in 1984 with an initial report of the ABA published two years later in 1986. After receipt of the Report, NCCUSL adopted a drafting committee in 1987 to review the 1914 Uniform Partnership Act. This resulted in a 1992 Revised Uniform Partnership Act, which was adopted unanimously. Subsequently, there was further consultation and revision, resulting in the unanimous adoption in 1994 RUPA. However, the reform experience in the United States has been criticized for failing to proceed with an underlying theory to guide the structures of the reform resulting in a failure to identify the social costs associated with the adopted reforms.[18]

[10] In the UK, the Partnership Act of 1890 has been largely unchanged since its enactment.[19] In the mid to late 1990s several reviews were being undertaken by the Law Commission and the Department of Trade and Industry to determine the appropriateness of existing forms of business association and whether there was a need to create new forms.[20] Although these reviews did not identify a pressing need for reform initiatives, it has been identified that political pressure from professional firms for limited liability

resulted in the 2001 enactment of legislation to create a limited liability partnership.[21] A review of general partnership law was undertaken by the UK and Scottish Law Reform Commission's in 2000, culminating in its 2003 report (hereinafter the "Law Commission Report"). It should be noted that Scottish law had always differed from the UK aggregate characterization of a partnership and instead adopted an entity approach to partnership. The reforms being proposed in the Law Commission Report are substantively similar to those contained in the RUPA.

[11] The recommendation by the Law Commission to change partnership from an aggregate of partners to a separate legal entity was not supported by the Chancery Bar Association, the Law Reform Committee of the Bar Council or the Law Society.[22] It did, however, receive significant support from a number of other industry, business and professional organizations.[23]

[12] In the Canadian context, the fundamental question is: Do we have a significant need to reform general partnership law? Are those needs being met by other strategies or other business forms? If there is a need, what objectives should a reform project achieve?

[13] In this paper I have focused on the single most important reform contained in both the RUPA and the Law Commission Report - the decision to grant separate legal entity status to partnership and abandon the concept of partnership as an aggregate of its partners. The rationale for this focus is that this crucial decision will directly impacts all other reform initiatives. Accordingly, examining the principles upon which current partnership law is based and looking at proposed reforms from the perspective of applying (or not applying) these principles is important in the law reform process.

[14] Part II of this paper contains a summary of the current partnership law in Canada and the principles of contract, agency and aggregate-status that have combined to form our current partnership law system. Part III examines the motivations and rationales for reform coming from the US and the UK, particularly the ability of entities to have a continued existence upon a change in composition of the partnership and the ability of entities to hold title to property. Part IV considers the impact a change to entity status

would have on the liability structure of the partnership vis-à-vis third parties and partners, as well as the tax implications of moving from aggregate to entity status.

II. SUMMARY OF CURRENT LAW

1. Aggregate of Partners

[15] With the exception of Quebec, partnership law in Canada enjoys a high degree of uniformity, as provincial partnership legislation is modeled on the provisions contained in the 1890 Partnership Act (UK). In Canada and the UK, partnerships are not separate legal persons. As a result, partnerships are categorized as an 'aggregate' of partners, rather than its own 'entity'. The aggregate status of the partnership has been its defining feature, contrasting partnerships from entity forms of business organization. It is from the aggregate status of partnership that the relationship between the partners themselves and between the partnership and third parties is defined.

[16] The common law system does not treat partnership as an entity. However, it does refer to the partnership collectively as a "firm".[24] Agency duties owed to partners by other partners are also owed to the firm[25] and the partnership as a firm is also liable in situations of wrongful conduct by the partners.[26] There are also provisions in the ***Income Tax Act*** that deems continued existence of partnerships after dissolution.[27] However, these instances of entity-like treatment do not create a separate entity as has been adopted in the RUPA or contained in the Law Commission's Draft Bill. Rather, they are more akin to a nomenclature or a convenient method of referencing the partners as a collective.

2. Contract and Agency

[17] The partnership relationship is contractual, premised on the mutual agreement of the partners to engage in a business venture. The terms of the contract may be express, such as in the case of a formal, written partnership agreement, or implied by the conduct and dealings of the parties. Because of this contractual basis, a partnership is an inherently flexible business form. It can be created between small groups of individuals

on an informal basis, or by large number of partners with detailed written terms. The flexibility in content of the contractual arrangement is tempered only by legislation composed of a few mandatory rules governing the partnership relationship and, more commonly, default rules available to 'fill gaps' in the agreement between the partners.

[18] As the partnership is formed by contract, the responsibility for management of the business and entitlement to its financial rewards are determined by the contractual agreement. In the absence of agreement, the statute provides default rules governing these important issues, which rules are premised on equality of responsibility between partners and majority decision-making.[28]

[19] The mutuality of the contract is destroyed when there is a change in partner composition. As a result, partnership legislation provides, subject to agreement by the parties, that a new partner cannot be admitted to the firm without unanimous consent of all other partners.[29] Similarly, when a partner dies or assigns into bankruptcy, unless the partnership agreement otherwise provides, the partnership is dissolved.[30] When a partnership is dissolved, two things may occur: a new partnership may be created immediately upon dissolution of the old, either expressly or by implication; or the partnership may be wound-up and partnership property distributed among the partners.[31] If a new partnership is formed, the partnership business is continued by the new firm, subject to the entitlements of the departing partner.[32] Dissolution has implications for third-party contracts, requiring a new partnership to be assigned the rights and obligations incurred by the old partnership and the third-party consenting to such assignment. This consent may be express but is often implied by reference to the course of dealings between the third-parties and the new partnership.

[20] The relationship between each partner is that of agency; each partner is agent of all other partners and, each partner a principal of each agent.[33] This enables each partner to enter into contractual obligations that bind themselves and all other partners. It also has the effect of making all partners primarily liable for these obligations in the event of default.[34]

[21] Partners are also jointly and severally liable to third-parties for loss or injury caused by the wrongful act or omission of a partner,[35] for misrepresentation by a partner acting with actual or apparent authority,[36] and for the improper use of money or property which a partner receives in the course of carrying on the partnership business or which is in the custody of the partnership.[37]

[22] Given this simple liability regime, there is incentive for each partner to carefully choose its other partners, monitor the activities undertaken by the partnership through its partners and/or or enter into partnership agreements that contractually define each partners' scope of authority, obligations, liability for contribution or terms of indemnification.[38] Depending on the size or sophistication of the partnership some or all of these techniques may be employed.

[23] This agency relationship also extends to the partnership. Partnership legislation provides that partners are also agents of the partnership (although the partnership is not an agent of the partners).[39] Without the partnership being a principal is it difficult to conceptualize how a partner could be an agent of a non-existent principle. The answer to this may be that the legislation has attempted to find a mechanism to bind the partnership as a collective, so as to ensure that partnership assets could be used to satisfy third-party claims.

[24] The aggregate status of partnership also dictates that each partner owes fiduciary duties to one another. As agents of one another, there is a duty to act in good faith in relation to all dealings with other partners.[40] The legislation also sets out fiduciary duties, requiring all partners to refrain from using partnership property to obtain a personal profit and to account for those profits to the other partners.[41] The obligation to account for profits extends to partners who, without consent of the other partners, compete with the business of the partnership.[42] This relationship between partners differs from corporate law where directors, as agents, owe agency and fiduciary duties to the corporation.[43] The corporation, as an entity, is the principal in the agency relationship. Unlike in a partnership where both ownership and control are vested in the partners, in a corporation, ownership is vested in the shareholders who do not owe duties to either the corporation or

to each other.[44] Control is vested in the directors. Because directors have control over the assets of the entity (the corporation), directors owe agency and fiduciary duties to the corporation.

3. Dissolution and Continuity

[25] Dissolution and formation of new partnerships provides a simple scheme for determining liabilities of partners to third parties and to each other. Subject to agreement between the parties, departing partners stop being liable for obligations incurred after dissolution and new partners are not liable for obligations incurred prior to joining the partnership.[45] However, a departing partner continues to be liable for the debts and obligations incurred by the partnership prior to his departure.[46] Furthermore, subject to the partnership agreement, departing partners are entitled to their share in the division of partnership assets.[47]

4. Ability to Dissolve the Partnership

[26] Subject to any agreement to the contrary, a partnership will dissolve upon expiration of the term fixed in the partnership agreement,[48] termination of the undertaking or adventure for which the partnership was formed,[49] notice given by a partner of his intention to dissolve the partnership,[50] death of a partner,[51]or by a partner making an assignment in bankruptcy.[52]

[27] If a partner allows his share of partnership property to be charged for his separate debts, the Act provides partners with the option of dissolving the partnership.[53] A partnership is automatically dissolved if the partnership becomes illegal, in that either the business of the partnership becomes unlawful, or it becomes unlawful to carry on the business in partnership form.[54]

[28] The court may also decree a dissolution of the partnership: if a partner is shown to be of unsound mind;[55] if a partner is permanently incapable of performing the terms of the partnership contract;[56] if a partner is guilty of misconduct which is calculated to prejudicially effect that firm;[57] if a partner wilfully or persistently commits a breach of

the partnership agreement;[58] if a partner otherwise conducts himself in such as way that it is not reasonably practicable to continue the operation of the partnership;[59] when the business of the firm can only be carried on at a loss;[60] and, when the court determines it would be just and equitable to do so.[61]

5. Consequences of Dissolution

[29] In the absence of agreement to the contrary, when the partnership dissolves, legislation grants rights to the departing partner, or the partner's estate, to have the partnership business wound-up and proceeds distributed in accordance with the partner's share of the partnership.[62] This form of dissolution followed by a winding-up of the business is referred to as a 'general dissolution'. Alternatively, a new partnership may be formed immediately after dissolution of the old firm and the partnership business carried on by the new firm.[63] This situation is referred to as a 'technical dissolution'. The ability to carry on the business of the firm by a new partnership is governed by express or implied agreement between the parties. In the event there is no agreement, however, the ability to demand a winding-up of the partnership business ensures that a departing partner or its estate receive its share of the partnership assets and proceeds.

[30] The timing of dissolution and the winding-up of the business differs between partnerships and corporations. In a corporate dissolution, winding-up occurs prior to dissolution of the corporation. In the partnership context, the agency relationship between the partners ceases upon dissolution, but the business is wound-up after dissolution. The reason for this is related to the entity status of the corporation and the aggregate status of the partnership.

[31] A corporation, as a separate legal entity, incurs its own obligations. The owners of the entity (its shareholders) and its managers (directors), as a general rule, do not have the rights or liabilities of the entity. As a result, prior to dissolution of the entity, the creditors of the entity must have their debts satisfied by the assets of the entity and, conversely, any claims of the corporation against third-party also must be settled prior to its termination.

[32] In contrast, a partnership is an aggregate of its partners, with each partner being a co-agent of each other. The consequence of the agency relationship is for each partner to be jointly and severally liable for the debts and obligations entered into by its other partners in operating the partnership business. Accordingly, creditors of the partnership are creditors of the partners. When a partnership dissolves, the agency relationship ceases to exist. Because dissolution of a partnership terminates the agency relationship between the partners, legislation is required to make former partners liable for transactions entered into during the winding-up process.[64]

[33] However, creditors' rights are not affected upon dissolution as creditors have the ability to claim against partnership property, or against the assets of individual partners. Partners that have satisfied the claims of partnership creditors have rights of indemnification by the partnership[65] and/or are entitled to contribution from other partners.[66]

6. Impact of Dissolving Partnerships and forming New Partnerships

[34] When a partnership is dissolved, if the business is not wound-up, the continuation of the business by the new partnership raises a couple of potential difficulties. The first is the valuation of each partners' share in the partnership assets and proceeds. The payout received by the partner is subject to agreement between the parties, with the ability of the departing partner to insist on winding-up of the business if no satisfactory resolution is reached. The second is a determination of the liabilities of the old partners and the new partners for existing and new debt obligations. A third consideration is the existing contractual obligations of the partnership and the ability to transfer these contractual obligations and liabilities to the new partnership.

a. Partners' Rights on Dissolution

[35] Upon dissolution, a partner is entitled to have the debts and obligations of the partnership satisfied by partnership property and to receive its share of any surplus assets or proceeds.[67] If a partner has entered into a fixed term partnership and paid a premium

for entering the partnership and the partnership is dissolved prior to the expiration of the fixed term (except by virtue of the death of a partner), the partner may be entitled to a court ordered repayment of part or all of the premium.[68] If a partnership continues after dissolution, in the absence of agreement to the contrary, a departing partner or its estate is entitled to a share of the profits made on the departing partner's share of the assets.[69] Partnership legislation also sets out rules for the final distribution of partnership assets, in the event the partners have not entered into an agreement for such distribution.[70]

b. Liability of Partners for Partnership Obligations

[36] When a partnership dissolves and a partner leaves the partnership, subject to an agreement to the contrary, a partner's liability for old debts of the partnership continues,[71] but liability for new debts only continues so long as the other partners have the authority to bind the partner. As co-agents, partners bind each other through the exercise of actual or apparent authority. Upon dissolution, a partner only has the actual authority to bind partners in so far as such obligations are necessary to facilitate the winding-up on the business.[72] However, partners could exercise apparent authority and enter into obligations after dissolution, if third-parties dealing with the partner do not have knowledge that the partnership has dissolved.[73] To avoid incurring new liabilities after dissolution, notice of dissolution may be given publicly,[74] and publication of a change in partnership in official gazettes is used to provide notice to all third-parties that did not have previous dealings with the firm.[75] Thus, dissolution and subsequent notice to third-parties provides a simple mechanism of determining the on-going liabilities of partners, both former and existing.

[37] The primary liability of partners for partnership liabilities enables creditors of partnerships to sue and recover partnership debts from individual partners without the necessity of exhausting remedies against partnership assets prior to seeking enforcement against individual partners. Partners are also protected in this scheme, as they are entitled to indemnification from the firm and/or contribution from other partners in respect of satisfying partnership debts. Procedural rules in various jurisdictions also allow creditors to sue partnerships, or partnerships to sue, in the business name of the partnership.[76] In

order to ascertain which partners were partners at the time a liability arises, if the partners operate under a business name, certificates filed pursuant to partnership and/or business names registration legislation provide conclusive evidence against signatories of their partner status, without effecting the status of non-signatories.[77]

c. Assignment of Third-Party Contracts

[38] Because a partnership is not an entity, contracts entered into by a partnership cannot be transferred to the new partnership without the consent of the parties to the contract. That means both the new partners and the third-party with rights vis-à-vis the old partners must consent to release the old partners from liability and consent to bind new partners to these obligations. This consent may be express or implied. For example, in a large firm, the consent to transfer contractual rights and obligations from the old partners to the partners of the new firm is commonly implied by the course of dealings, or set out in a formal written agreement.

[39] Contracts of guarantee pose specific difficulties as a surety's obligation is coextensive with the debtor's obligation. A change in the composition of the firm may relieve the surety from obligations unless he consents to the change. Legislation has expressly provided that upon a change in the composition of the firm, unless there is an agreement to the contrary, any continuing guarantee is revoked as to future transactions.[78]

7. Ownership of Partnership Property

[40] In both Canada and the UK, each partner is the holder of an undivided joint interest in all property of the partnership.[79] As a partnership is not a separate entity, it is not capable of holding title to property in the name of the partnership. Rather, title is vested in the name of the individual partners, or in the name of an entity (e.g. a corporation) formed for the purpose of holding title.

[41] The distinction between partnership property and the property that is co-owned or individually owed by partners is defined by the partnership agreement. In the absence of such agreement, the legislation provides few default rules to govern this determination.

[42] All property brought into the partnership business or subsequently acquired in the course of operations is to be partnership property and must be applied exclusively for the purpose of the partnership.[80] If the purchase of property is made using partnership funds, it is deemed to be property of the firm.[81]

[43] The statute also contains particular provisions concerning interests held in real property. There is no presumption that land held by partners is 'partnership property'. Rather, unless there is an agreement to the contrary, the land belongs to them as co-owners.[82] The statute also provides that in the event that land is held as partnership property, unless there is an agreement to the contrary it is to be treated as moveable or personal property.[83]

8. Seizure of Partnership Property

[44] Whether property is 'partnership property', co-owned by the partners or is separate property of an individual partner is an important determination. Partnership property may be seized in satisfaction of any judgment against the partnership[84], but it may not be seized in respect of private debts of individual partners. Only a partner's interest in partnership property (namely the right to receive its share of the profits) may be the subject of a charging order arising out of a proceeding against an individual partner.[85]

[45] In Canadian jurisdictions with personal property security legislation, a partnership carrying on business under a registered business name is entitled to use its business name for the purposes of registration and subsequent enforcement proceedings against personal property.[86] As a result, registration of the property in the name of the partnership is evidence that the property is partnership property, rather than privately owned.

[46] In the context of real property, land registry systems guaranteeing security of title do not allow for title to be registered in the business name of the partnership. Rather, it is held in the name of the partners or a corporation controlled by the partnership. In jurisdictions with no restriction on the number of individual names that can be placed on

title, partnerships can register title naming all partners. The land registry system in the UK, however, poses a unique problem in that it prohibits the naming of more than four individuals on title.[87] In registry systems that do not guarantee security of title, but are 'notice' based systems (akin to personal property security registries), allowing registration in the business name of a partnership does not undermine the system.[88]

9. Dissolution and Transfer of Title

[47] Partnership property poses two challenges upon dissolution of the partnership. The registration of partnership property in the name of individual partners will necessitate transfer of title upon change in composition of the partnership. This may be an administrative burden for firms where there is frequent turn-over in partnership composition. However, in such cases, if the real property is not co-owned, it is more common for the partnership to use a corporation for the purpose of holding title.

[48] The second challenge is determining whether property is partnership property for the purposes of winding-up the business and distributing to each partner its share of the proceeds and for enforcement of judgments by creditors.

III. SIGNIFICANT REFORM INITIATIVES IN THE US AND UK

[49] In both the RUPA (US) and the Law Commission Draft Bill, the aggregate status of partnership has been replaced with partnerships being granted separate entity status.[89] The two most significant reasons noted for this change were to allow for the continuity of the partnership after change of membership and to enable the partnership to hold title to property. As an entity, the partnership would continue to exist after the departure of a partner or admission of a new partner without the necessity of dissolution of the old partnership and creation of a new partnership. As an entity it would also be able to hold title to property in the name of the partnership, rather in the name of the individual partners or the name of a corporation controlled by the partnership. In reviewing possibilities for reform, careful consideration must be given to these rationales.

1. Continuity of the Partnership: Changing the Default Rule

[50] In the US, the change of partnership status from an aggregate of partners to a separate legal entity provides a conceptual basis for continuing the firm despite a partner's departure from the firm.[90] Thus, the continuity of a partnership's life has been noted by NCCUSL as an achievement of the RUPA.[91]

[51] The Law Commission identified the importance of facilitating the continuity of partnerships as an important principle guiding partnership reform.[92] This resulted in a recommendation to change the default rules pertaining to dissolution of an 'at will' partnership upon the death or retirement of a partner.[93] The result of this recommendation is that a departing partner would not have the right to insist on a winding-up of the partnership business, but would, instead be entitled to receive the value of its share in the partnership.

[52] The Law Commission's recommendation to allow for continuity of the partnership is accompanied by a recommendation to give a different meaning to the term 'dissolution'.[94] Dissolution would no longer mark the end of the partnership and the beginning of a new partnership or the commencement of winding-up proceedings, it would occur at the end of the winding-up process. The first step of terminating the partnership would be the 'break-up' of the partnership, the second step, the 'winding-up' process and the final step, 'dissolution'.[95] This recommendation is consistent with the entity status of the partnership. Dissolution would only occur after the liabilities of the partnership have been satisfied and the assets distributed. It would be at that stage that the partnership would cease to exist.

[53] RUPA also changed the law governing partnership break-ups and dissolution. It has used the term 'dissociation' to explain the change in the relationship caused by a partner's ceasing to be associated with the partnership business as a result of retirement, expulsion in accordance with the partnership agreement, death of a partner or upon judicial determination that an individual partner has become incapacitated and unable to perform its duties.[96] Upon dissociation a partner's right to participate in the management

of the partnership business ceases and duties of loyalty terminate.[97] In a case of dissociation, the right of a partner to insist on a winding-up of the partnership has been replaced with the requirement that the partnership purchase the departing partner's interest in the partnership for a buyout price determined by the partnership agreement, or in accordance with the Act.[98] The term 'dissolution', however, continues to be used to describe the termination of the partnership relationship caused by expiration of a fixed term partnership, agreement of the partners to wind-up the partnership business, court ordered termination or termination occurring upon dissociation when at least one-half of the remaining partners elect to wind-up the partnership business.[99] Winding-up of the partnership business will continue after the event causing dissolution.

a. No Right to Wind-up the Partnership Business

[54] Both the RUPA and the Law Commission Report recommendations alter the default rule in the event of a voluntary departure of a partner to an 'at will' partnership. In the case of fixed term partnerships, the partners themselves have agreed that the partnership business is to cease at the expiration of the term. Under existing partnership law, for partnerships that do not expire after a fixed term, a retiring partner may insist on a winding-up of the business upon giving notice of dissolution. Granting partnerships entity status and changing the default rule would allow for the continuation of the business by existing partners.

[55] Changing the default rule to prevent a departing partner from having the right to insist on a winding-up of the business is consistent with the entity status of the partnership. If partnerships were granted entity status, the partners of the partnership would not (subject to legislative intervention), be agents of one another. With no agency relationship, the departure of a partner would not terminate the agency relationship. However, the departure of a partner could still be the point in time when certain liabilities for partnership debts and obligations could cease.

[56] It is not clear whether the problems experienced by the application of the current default rule necessitate a change in legislation. Currently, the change in the default rule is already exercised contractually when partners enter into a partnership agreement which

provide for the continuity of the partnership upon retirement and subsequent valuation and buyout of a partner's interest. The Law Commission's report has suggested that, in the case of a viable business where there is no contractual agreement to continue the business after the departure of a partner, there is some reluctance by the courts to facilitate the continuation of the partnership business.[100] The reason for this reluctance is likely the contractual basis of the partnership itself. If partners have agreed to a continuation of the partnership business after departure of a partner, then the agreement of the parties governs. If they have not, unless such an agreement can be implied from their conduct, there is no basis to find such an agreement. As a result, the default rule is consistent with the expectations of the parties and facilitates the exit of the partner and acquisition of its share of the partnership assets through winding-up. This rule is rational, as it enables partners to contract out of its provisions, but provides an effective means of facilitating the payment of debts and distribution of partnership assets among the partners in the event they have not contracted for continuation.

[57] One concern with changing the default rule is that the departing partner may be prejudiced by the change. In the UK, this concern was raised by the Chancery Bar Association, and the Law Reform Committee of the General Council of the Bar.[101]

[58] The Law Commission recognized that replacing the default rule would necessitate the enactment of additional rules to govern the rights of departing partners including a new set of rules setting out a mechanism and timetable for a partner to withdraw and for the other partners to respond to the withdrawal.[102] These rules would be very important and provide for the ability of the departing partner to seek appropriate relief from the court in the event of significant valuation or distribution disagreements.

[59] A concern was also raised that many individuals operating in 'inadvertent partnerships' (unaware their business relationship is one of partnership) would not be aware of the default regime, particularly in relation to the timing of the break-up provisions proposed in the new Act, and would consistently find themselves in contravention of the legislation.[103]

[60] The Law Commission considered this issue but responded that in most cases, inadvertent partnerships would be partnerships composed of two persons, which partnerships would break-up upon the departure of the one of the partners in any event and the new 'continuation' default rule would not apply.[104] Second, under current rules, unaware partners conduct themselves in violation of existing default rules and it falls to the court to look to the parties conduct to determine what was intended by the partners' acts, particularly in relation to the requirement of giving notice of dissolution in partnership where they are not for a fixed term. The role of the court to work through these situations would continue if the default rule was changed.[105] Third, in the case of an inadvertent partnership, the courts will likely be able to infer from the conduct of the parties whether they intended to contract out of the new default continuity regime and order the winding-up of the partnership business.[106] Fourth, the Commission believes that their role is to create a regime to address the interests of persons who know that they are in partnership and need a workable and efficient default regime to govern their relationship as well as consider the impact on inadvertent partnerships.[107] As a result, they were not convinced that the concern was important enough to change their recommendation.

b. Liability of Old and New Partnerships for Existing Obligations

[61] One of the benefits of entity status being granted to a partnership is that the partnership would continue to be bound by third-party contracts even after a change in composition of the partnership. Under the current regime, during a technical dissolution, the old partnership dissolves and new partnership is created and carries on the partnership business. However, contracts formed between the old partnership and third parties would be binding on the old partners, but not on the new partners without mutual consent to an assignment of rights and liabilities.[108] In many cases, this is achieved expressly through agreement between the old and new partners of the partnership to acquire the rights and liabilities of the business and indemnify former partners.

[62] Under a 'continuity' default regime, the partnership entity would be bound by the existing contractual obligations. A regime that entitled departing partners to a buy-out of

their interest from the partnership would have to determine a point in time when liabilities cease for old partners and when they exist for new partners.

c. Assignment of Third-Party Contracts

[63] During a technical dissolution, where a new partnership is formed and carries on the partnership business, in order for existing contracts to be binding on the new firm, third-parties must consent to the assignment of those rights and a release from liability of the old firm. Under current practice, the consent by third-parties is either expressly provided for in the contract or, more often, implied from conduct. With entity status, a partnership would enter into a contract and a change in composition of the partners would not alter the parties to the contract.

[64] It is unlikely that the change in partnership status would provide more protection to third-party creditors of the corporation. Under the existing regime, dissolution does not reduce the liability of a partner for existing debts or obligations.[109] It also requires partners to give notice to third-parties dealing with the firm of their departure to prevent further liability from accruing.[110] This notice provides information to third-parties about the composition of the firm which will enable them to make decisions about their contractual relationship with the firm (such as continuing to supply goods and services to the firm or contracting for additional security). The ability of a partner to insist on the winding-up of the partnership business upon dissolution also protects third-parties as the claims of partnership creditors must first be satisfied prior to partnership assets being distributed.[111]

[65] With continuity of the entity, no new partnership will be formed and the partnership will continue to be bound by the existing contracts. While the effect of this may be neutral in terms of whether it poses greater risks to third-parties dealing with the firm, the impact of notice (or no notice) upon a change in partners of the partnership should be considered.[112]

[66] In this context, the status of a continuing guarantee should also be reviewed. The partnership as an entity would continue to exist and there would not be a principled reason for the continuing guarantee to terminate. Rather, it would be policy decision as to whether to retain the current rule. The Law Commission has recommended that the rule not be re-enacted because the terms of the guarantee usually determine the extent to which the obligation will continue after a change in composition of the partnership and a change in composition of the partnership was not perceived to alter the risk to the guarantor.[113]

d. Should the 'Winding-up' Default Rule be Changed?

[67] Under the current system, dissolution arises upon death, retirement, bankruptcy, notice or expiration of the agreement. As partnership is contractually based, dissolution marks the end of the mutual consent to be bound together in the partnership relationship. It also brings about the end of the actual agency relationship between the partners. The default rules pertaining to partners' rights and obligations during winding-up, however, are necessary to protect third-parties dealing with the partnership and to facilitate the winding-up process.

[68] With a change to entity status, unless the legislation provides otherwise, there is no requirement that partners would be agents of one another. As an entity, the partnership would be primarily liable to creditors of the partnership and would have to continue to exist until debts and other liabilities were satisfied.

[69] There does not appear to be a compelling reason to change the default rule. This is because there are no obvious benefits for third-parties contracting with the partnership or for partners (existing or remaining) that are not already solved through the application of contract law principles. In the vast majority of cases, a partnership agreement has defined the circumstances for continuity of the partnership and for dissolution and winding-up. In the case of a technical dissolution, courts imply assignment of contractual rights by reference to parties conduct. The obvious benefit the current rule provides is greater protection to the departing partner. Even in the absence of a prior agreement, the

partners may reach an agreement on valuation and buyout after dissolution, such that the default rule will not apply in the vast majority of cases.

2. Termination and Winding-up of the Partnership: A Change in Process

[70] The Law Commission has recommended that if a partnership is to be granted separate entity status, the partnership would continue to exist until the partnership business is wound-up.[114] The proposal is for a three step process, with the first step referred to as the 'break-up' of the partnership, the second step the process of winding-up the partnership and the third step, the termination of the partnership on completion of winding-up. This final stage would be 'dissolution'.[115]

[71] In the RUPA, the term 'dissolution' continues to be used to describe the commencement of the winding-up process.[116] This has been the subject to criticism since it was adopted.[117] The Law Commission has recommended the retention of the term 'dissolution', but has proposed that it be used to refer to the termination of the partnership rather than the commencement of the winding-up process. The reason for this change is because dissolution suitably describes the final termination of the partnership entity, and because it is consistent with the use of the term in the corporate law context.[118]

[72] The Law Commission has further recommended that if the partnership is reduced to a single individual, break-up of the partnership would occur and there would not be a 'grace' period granted to the individual to find a new partner for the purpose of carrying on the business.[119] However, the partnership would not terminate immediately, but continue to exist during the winding-up process.[120]

[73] The Law Commission has further recommended that during the break-up and winding-up stages of a partnership, the partners do not cease being partners. As a result, liabilities and obligations continue until winding-up is complete and the partnership is terminated.[121]

[74] Under existing law, dissolution marks the end of the actual agency relationship between the partners. Accordingly, dissolution of the partnership followed by winding-up of the partnership business is in accordance with the aggregate status of partnerships. If a partnership has separate entity status, it is consistent with the entity concept to provide for the continued existence of the entity until the claims of third-party creditors are satisfied. As a result, dissolution of the partnership must be preceded by a winding-up of the business, in the same manner as a corporate winding-up and dissolution.

[75] The important decision, therefore, is not whether to change the order of dissolution and winding-up or change the use of the 'dissolution' terminology, but rather whether to grant entity status to the partnership or retain its aggregate status. Once that determination is made, then the processes may be properly ordered and defined.

a. Should Continuity be the Motivation for Reform?

[76] It is not apparent whether ensuring continuity of 'at will' partnerships should be a motivating force behind partnership reform. While continuity has been adopted as a principle by the Law Commission, it is not clear whether lack of continuity has been problematic in Canada. Most sophisticated partnerships are governed by partnership agreements which will provide for continuity in certain circumstances and specify the financial and other entitlements of a departing partner. In smaller, less formal partnerships or inadvertent partnerships, it is unlikely that individuals jointly engaging in a business enterprise would intend that the business should be carried on in the event the partners leave the firm. However, the ability to arrive at an agreement after dissolution of the partnership, places this decision in the hands of the parties.

[77] The continuity of the partnership was an important objective to be achieved by the UK Law Commission when it drafted its recommendations for reform of partnership law. The decision to grant partnerships' entity status allows for this objective to be achieved. In the Canadian context, is continuity of 'at will' partnerships an important objective?

3. Property Ownership

[78] The Law Commission proposal to grant entity status to a partnership attempts to solve problems associated with the inability of a partnership to hold title to property, including land, in its own name. [122]

[79] Granting partnerships entity status would allow registration of title in land registries in the business name of the partnership. This would provide judgment creditors with judgments against the firm or judgment creditors with judgments against private partners to better identify which property is subject to seizure and/or whether property would be subject to a charging order only. In the case of personal property, this issue has already been solved in the context of the registry system which allows for registration and enforcement of interests in the business name of the partnership.

[80] Entity status would solve the problems associated with requiring a transfer of title on the change in the composition of the partners. However, in practice this problem has been solved by partnerships that intend to continue after change in partnership composition utilizing corporations for the purpose of holding title to real property.

[81] Granting entity status to a partnership will not solve the problems associated with attempting to clearly distinguish partnership property from separate property of the partners. This may be important in the context of a winding-up of a partnership business upon dissolution, particularly if there is no express agreement evidencing the partners' intention in this regard. However, if partnerships were granted entity status, legislative amendments would have to be included to clarify whether partnership property that is contributed to the partnership by a partner, but held in a partners name, or property acquired by one or more of the partners, would be deemed to be partnership property.

[82] The Law Commission proposal has recommended that in the case where a partner contributes property to the partnership but continues to hold it in his personal name, such property would be deemed to be held in trust for the partnership.[123] It also recommends a rule that if property is acquired by one of more of the partners for the partnership, the

partnership should be deemed to be held in trust for the partnership.[124] Such provisions would adapt the current legislation to entity status. It has also recommended re-acting a rebuttable presumption that, absent agreement to the contrary, property acquired with partnership funds would be partnership property.[125]

[83] RUPA also provides for partnership property ownership by the partnership entity rather than the individual partners.[126] When property is acquired in the name of the partnership, or when the partnership's name is referenced in the instrument transferring title or is purchased using partnership funds.[127] Property acquired in the name of one or more of the partners, without reference to the partnership, is presumed to be separate property, even if used for partnership purposes.[128]

[84] Problems associated with property ownership and registration in Canada may be sufficient to motivate a change in partnership from aggregate to entity status. Alternatively, changes to the registry systems may mitigate problems. As a result, further consultation with the appropriate interest groups should be undertaken to determine whether such problems exist. If so, the next step would be to consider the most appropriate reforms to rectify those deficiencies.

IV. ADDITIONAL IMPACTS OF REFORM

1. Tax Treatment Considerations

[85] The tax treatment of business entities is a significant consideration to be taken into account when deciding what form of business association to utilize when undertaking a business venture. Whether a partnership is taxed at the 'entity' level of the partnership or at the level of the individual partners is an important consideration.

[86] In Canada, a partnership is not taxed as a separate legal entity and does pay tax on its income at the entity level. It may, however, be required to file an informational return setting out various elections made by the partners.[129] However, a partnership's taxable income is calculated 'as if' it were a separate legal person. Income or losses, the capital cost allowance and various reserves are claimed by the partnership, which deducts

employee wages and is responsible for source deductions. The net income or losses are then allocated to the partners and taxed at the level of the partners. Investment tax credits, resource expenditures and charitable donations are also allocated and deducted by the partners.

[87] The ability of partnership losses to flow through to an individual partner's income tax return is viewed as a benefit for many business ventures. Generally, the computation of partnership income is the same as computing income for other business organizations, such as proprietorships and corporations. Section 96 of the Act, however, provides some special adjustments for the income of partnerships.

[88] In contrast, corporate income is taxed that the entity level, with shareholders being taxed on the dividends received.[130] This has been characterized as 'double taxation' by some commentators, and regularly criticized.[131] The popularity of business income trusts as an investment vehicle is due, almost entirely, to the ability to achieve more favourable tax treatment on income than is available either through the use of a partnership, or through the creation of a corporation. Current consultations by the federal government on the taxation of flow-through entities should be watched to determine any implications it may have on changes in tax treatment to be afforded to limited partnerships or to income trusts.[132]

[89] In the United States, there are two possible tax treatments for partnerships. A partnership with 100 or more partners can elect to be taxed at the partnership level (termed an electing large partnership).[133] Any partnership with less than 100 partners or a partnership with 100 or more partners that has not elected to be taxed at the entity level is taxed at the aggregate level with profits and losses passing through to the general partners.[134] It should be noted that the deductions available when taxed at the entity level or the individual partner level differ significantly.[135] This is a significant difference from Canadian law where there is no ability to elect to be taxed at the entity level.

[90] Partnerships are entitled to file an informational return with the IRS setting out the distributive amount of tax income, and illustrate the income, deductions and other information about the partnership that is requested.

[91] In the Internal Revenue Code, all existing partnerships are considered as continuing, unless they are terminated.[136] Termination occurring only if no part of the business, financial operation, or venture of the partnership continues to be carried on by any of the partners in partnership, or within a year there is a sale or exchange of 50% of more of the total interest in partnership capital and profits.[137]

[92] In the UK, the income tax system has undergone significant changes since the 1990s. Historically, partnerships were taxed at the level of the partnership, with the tax liability being a debt of the partnership and each partner being jointly liable for the debt.[138] With the most recent amendments to the ITCA, unless the contrary intention appears, a partnership is not treated as an entity for tax purposes and the profits and losses of the partnership flow through to the individual partners with each partner being personally liable for tax only on his share.[139] For capital gains purposes, however, the partnership form is disregarded with all dealings of partnership property being treated as dealings by individual partners.[140] This differs from Canadian law where capital gains or losses are calculated at the partnership level for the purposes of determining the total net income of the partnership, the share of which flows through to the partner level.

[93] The Law Commission Report makes it clear that in the event the reforms to partnership law are adopted, it will rely on a statement authorized for publication by Inland Revenue (the UK equivalent of the Canada Revenue Agency) committing itself "to bring forward any tax legislation necessary to maintain the present policy of generally treating partnerships as transparent for tax purposes."[141]

[94] If a decision is made to change partnership from an aggregate of its partners to an entity, the tax policy applicable to partnerships would have to be negotiated with the federal and provincial governments. As the ability to flow through losses to individual partners is a particularly attractive feature of the partnership form, it is most likely that industry would not want to lose such an important taxation feature. In both the US and

UK, this feature appears to have been retained although it is not clear whether there is a principled rationale for such retention, or whether it has been retained due to political pressure. In any event, if such a change is proposed, work will have to be done with taxation authorities to work out the implications of such a change.

2. Agency and Personal Liability for Partnership Obligations

[95] In both the UK and Canada, a partner is an agent of the other partners and an agent of the firm. A partner acting within the scope of his actual authority will bind both the firm and the partners. Even if the actual authority of a partner is revoked, the partner will still bind the firm and the partners if he has apparent authority to act and the third party dealing with the partner had no knowledge of the revocation of actual authority.

[96] The existence of agency duties between partners is due to the fact that a partnership does not have a separate legal personality. As such, the partnership cannot be a 'principal'. An aggregate of partners, however, must have a method available to enter into contracts on behalf of the business enterprise that would bind all partners to the risks and rewards of the contract. This is achieve through contracts of agency, with each partner being an agent of one another, and each act of the partner undertaken with the authority of the other partners or in the ordinary course of business, being binding on the co-agents.

[97] The decision to continue the agency relationship between partners with the granting of entity status to a partnership would be a question of policy and not an application of legal principle. This is because with entity status, the partners do not stand in the same relationship to one another. Conceptually, the separate entity of the partnership would provide a solid rationale for partners acting on behalf of the partnership, to bind the partnership entity and for primary liability to rest with the entity.

[98] In Canada, limited liability currently exists for shareholders of corporations.[142] In limited partnerships, limited partners have been granted limited liability status,[143] and in several jurisdictions, the unit-holders in income trusts have been granted limited

liability.[144] It is probable that with a change to entity status, there would be political pressure to grant partners limited liability status as a default rule, similar to that provided to shareholders of a corporation.

[99] Under RUPA, partners are agents of the partnership.[145] The liability of a partner for partnership obligations is continued under the RUPA,[146] but the Act requires creditors to first exhaust remedies against the partnership before executing against the separate assets of the partners.[147]

[100] The Law Commission Report also recommends that a partner is made an agent of the partnership entity and not the partners.[148] However, this recommendation was not unanimously received. Inland Revenue suggested that the basis for the tax treatment of partnerships was premised on mutual agency.[149] Another consultant observed that the agency relationship between partners reflected the collective and several liability of partners for partnership debts.[150]

[101] Under current law, partners are jointly and severally liable for the obligations of the partnership.[151] Creditors of the partnership are also able to recover a partnership debt by enforcement against a partner's assets without having to first enforce against and exhaust the assets of the partnership. A partner that satisfies a partnership liability is entitled to be indemnified by the partnership,[152]or receive contribution from its other partners.[153] The legislation also grants priority to the private creditors of a deceased partner, allowing for prior payment of the deceased partner's private debts over payment from the estate of partnership debts.[154]

[102] The Law Commission Report has proposed that each partner would continue to be liable for obligations of the partnership and that such liability would be joint and several.[155] The Law Commission's has also recommended the continuance of unlimited liability for all general partners of a partnership.[156] However, in contrast to RUPA, a creditor would not be required to exhaust remedies against the firm prior to enforcing claims against the property of partners, provided that the partnership creditor had properly established the existence and amount of the firm's liability in the proceedings. If a partner pays the debt, he would be entitled to indemnity from the partnership, or

contribution from the other partners. However, if the creditors' claim was successfully enforced against partnership assets, the partnership would not be entitled to claim contribution or indemnity from the partnership.

[103] Under current partnership law, partners are liable for partnership obligations because of the agency relationship between the partners. With a separate legal personality, the partnership entity would be bound by acts of its agents, but it would be a policy decision whether to make the partners agents of one another and whether to make partners liable for the obligations of the entity. The Law Commission and RUPA have made that policy choice and continue to make partners liable for the obligations of the partnership, even though the partners are no longer agents of each other.

3. Duties of Good Faith and Fiduciary Duties

[104] Partners are fiduciaries of one another. The duty to act in good faith is an incident of the agency relationship between the partners. The duty to account for personal profit made using partnership property without the consent of the partners, and the duty to disgorge profits acquired by a partner engaging in a competing business without the consent of the partners are an expression of the fiduciary duty. With a change from aggregate to entity status, the question arises as to whether these duties will continue to be owed to the other partners or to the partnership.

[105] The Law Commission has recommended that the duty of good faith should continue to be owed to the partners, but that other duties, such as the duty to account for profits and not compete with the partnership would be owed to the partnership.[157]

[106] The RUPA has provided default rules expressing that certain fiduciary duties will be owed to the partnership[158] and good faith and fair dealing obligations will be owed to the partners.[159] However, RUPA also grants partners the ability to contract around the strict application of these duties.[160]

[107] If a partnership were granted entity status, the fiduciary duties should be owed to the partnership as an entity. Fiduciary duties arise when one party grants to another party the access to their assets for a limited purpose. In the trust context, a trustee owes a fiduciary duty to the beneficiary of the estate, as the trustee has been granted access to those assets for the purpose of benefiting the beneficiary not for the purpose of benefiting himself. If a partnership were granted entity status, access to the partnership property would be granted to partners for the purpose of benefiting the partnership. Defection from that purpose without the consent of the partnership would result in a breach of the duty.

[108] As with any duties owed, an important issue to be resolved should be whether or not by agreement, the parties can contract out of the fiduciary duties or good faith duties. The Law Commission has recommended making the duty of good faith mandatory, with the other duties default to the extent that contracting-out would not violate the duty of good faith.[161] This is consistent with the approach taken in RUPA.

4. Consistency of Partnership Law in Canada

[109] The provinces currently enjoy a high degree of uniformity in general partnership law. This means limited regulatory competition between jurisdictions. There is the possibility for increased regulatory competition if some jurisdictions decide to grant partnerships entity status and others retain the aggregate approach to partnership. Furthermore, the duty and liability regimes applicable to partners of the entities could differ between jurisdictions depending on the policy choices of the provinces.

[110] Are the benefits of our current uniform system sufficient to outweigh any benefits that may arise from reforming partnership law? If there was a decision to embark on a reform project, is there a consensus on which approach to take? Unless it is agreed that regulatory competition is preferred to uniformity, it is preferable for general partnerships to be accorded similar treatment.

5. Freedom of Contract

[111] The current partnership legislation allows for freedom of contract in the partnership relationship. For certain issues related to dissolution and continuity, parties already have the freedom to contract for the terms they wish to govern their relationship. The current default rules contained in the legislation are premised on contract and agency principles. In light of the ability to contract out of the default rules, it would not appear necessary to alter those rules, unless the conceptual framework of partnership was altered.

6. Existence of other Forms of Business Association

[112] The most significant issue is whether a partnership should continue to be an aggregate of its partners or treated as a separate entity. Currently, there are a number of existing forms of business organization available to choose from, each with its unique entity or aggregate status, tax treatment, and liability structure. For example, business corporations, non-profit corporations and unlimited liability corporations have legal personalities separate from their shareholders. Business trusts and limited partnerships have flow-through tax treatment and limited liability options. Has the lack of a separate legal personality for partnerships resulted in significant problems for persons operating in partnership? Is the only motivation for reform to create a corporate-like entity with the tax consequences of a partnership? Alternatively, are there real problems with the ability of the partners to effectively operate businesses that can only be resolved through significant reform of partnership law?

V. CONCLUSION: FUTURE CONSULTATIONS

[113] This paper has sought to highlight and consider the most significant reforms and proposals for reform that have arising from the US and the UK in recent years. The most significant issue is whether a partnership should retain its aggregate status, or acquire a separate legal entity. The current aggregate system of partnership has applied contract and agency principles to create a rationale system of default rules while retaining the

ability of partners to contract out of their various applications. In this context, one must identify the problems with the current system that would justify change before blindly following either the US or UK reforms. The desire to provide continuity of 'at will' partnerships, does not, in my opinion, justify such drastic reform. However, whether the inability to hold title to property in the name of the partnership and the inability to register such ownership in land titles registry systems, is sufficiently problematic to justify granting entity status to partnerships must be considered.

[114] Future consideration of partnership reform could focus on whether Canadian law should grant entity status to partnerships. Consultations similar to those conducted by NCCUSL and the Law Commission could be undertaken. However, in such a process, the political pressure of industry lobby groups should be anticipated.

[115] A second option would be to undertake more discrete inquiries particularly in relation to the issue of holding title to property. Provinces could consult with their respective land titles registries to determine if ownership and registration problems are prevalent before embarking on larger scale consultations.

[116] The federal government should also be consulted to determine whether the tax treatment of a partnership would change if it were granted entity status. This consultation is likely the single most important variable in the context of significant reform.

[117] If it is decided to retain the aggregate status of partnership, a project focused on updating the antiquated language of the existing legislation could still be undertaken as a project by the Uniform Law Conference of Canada.

[1] Uniform Partnership Act (1994), http://www.nccusl.org/nccusl/uniformact_summaries/uniformacts-s-upa1994.asp (hereinafter RUPA).
[2] Connecticut, West Virginia and Wyoming adopted the RUPA (1994).
[3] Alabama, Alaska, Arizona, Arkansas, California, Colorado, Delaware, District of Columbia, Florida, Hawaii, Idaho, Illinois, Iowa, Kansas, Maryland, Minnesota, Mississippi, Montana, Nebraska, New Jersey, New Mexico, North Dakota, Oklahoma, Oregon, South Dakota (substantially similar), Tennessee, Texas, Vermont, Virginia and Washington have enacted the RUPA with the 1997 amendments. In addition both Puerto Rico and the U.S. Virgin Islands have adopted the Act. South Dakota has also adopted legislation considered substantially similar.
[4] Indiana and Kentucky.
[5] Report on a Reference under Section 3(1)(e) of the Law Commissions Act, 1965, Partnership Law, Law Com No. 283 and Scot Law Com No. 192 (2003), http://www.lawcom.gov.uk/lc_reports.htm (hereinafter the Law Commission Report).
[6] The provincial and territorial legislation applicable to general partnerships is as follows: Partnership Act, RSA 2000, P-3; Partnership Act, RSBC 1996, c. 348 (BCPA); Partnership Act, CCSM c.P30; Partnership Act, RSNB c. P-4; Partnership Act, RSNL 1990, c. P-3; Partnership Act, RSNS 1989, s. 334; Partnership Act, RSO 1990, c. P.5 (OPA); Partnership Act, RSPEI 1988, P-1; Civil Code of Quebec, RSQ c. C-1991; Partnership and Business Names Act, RSY 2002, c. 166. In this paper, references are made to the Saskatchewan (SPA), Ontario (OPA) and British Columbia (BCPA) form of the legislation.
[7] SPA s. 3;OPA s. 2; BCPA s. 2.
[8] In fact, in the United States a rigorous debate can be traced in several academic articles of the time. (See: Lewis, ***The Uniform Partnership Act,*** 24 Yale L.J. 617 (1915); Crane, ***The Uniform Partnership Act – A Criticism***, 28 Harv. L. Rev. 762 (1915); Lewis, ***The Uniform Partnership Act – A Reply to Mr. Crane's Criticism, Part I***. 29 Harv. L. Rev. 158 (1915) and ***Part II***, 29 Harv. L. Rev. 291 (1916); Crane, ***The Uniform Partnership Act and Legal Persons***, 29 Harv. L. Rev. 838 (1916); Williston, ***The Uniform Partnership Act, with Some Remarks on Other Uniform Commercial Laws,*** 63 U. Pa. L. Rev. (1914); Drake, ***Partnership Entity and Tenancy in Partnership: The Struggle for Definition***, 15 Mich. L. Rev. 609 (1917).
[9] Queens' Bench Rules of Court (Sask.), ss. 51 and 52; Ontario Rules of Court s. 8.01; Supreme Court Civil Rules (B.C.) rule 7(1).
[10] SPA s. 25(1); OPA s. 26(1); BCPA; Ontario Rules of Court s. 8.06.
[11].Personal Property Security Regulations, P-6.2, Reg. 1, s. 11; Personal Property Security Regulations, R.R.O. 1990, Regulation 912, s. 16(4); Personal Property Security Regulations, B.C. Reg. 227/2002, s.8(f).
[12] Law Commission Report Part V; Draft Bill cl. 1(3); RUPA s. 201(a).
[13] See UPA Revision Subcommittee on Partnerships and Unincorporated Business Organizations, Section of Business Law, American Bar Association, ***Should the Uniform Partnership Act be Revised?*** 43 Bus. Law. 121 (1987) at 124; Law Commission Report para 3.53 setting out the statement of Inland Revenue which has been interpreted by the Commission as a commitment to retain the aggregate tax treatment of partners.
[14] NCCUSL identified several benefits of the RUPA including, the continuity of life of the partnership by changing the rules on dissolution of the partnership. See RUPA ss. 701 & 801. The Law Commission, at para 3.2 of its Report, identified 'continuity' as an important aim of reform. The other objectives identified were: (1) to preserve partnership as a flexible, informal and private business vehicle; (3) to preserve mutual trust and good faith as critical components of the relationship between partners; and (4) to provide a modern law of partnership based on consistent and straightforward concepts, which are readily understandable by advisers and clients alike.
[15] NCCUSL identified that the creation of a 'cohesive entity' would allow for a distinct body to be placed between the partners and the partnership assets, thereby allowing the partnership to sue and be sued in its own name and allowing property to be acquired in the partnership name. See commentary at http://www.nccusl.org/nccusl/uniformact_why/uniformacts-why-upa.asp; The Law Commission Report Part V sets out difficulties with property ownership, including transference between old and new partnerships.
[16] In Alberta, British Columbia, Manitoba, Saskatchewan and the Yukon, limited partnerships are provided for within the general partnership legislation. In New Brunswick, Newfoundland & Labrador, Nova Scotia, Northwest Territories and Ontario, limited liability partnerships are regulated pursuant to a separate Limited Partnership Acts. While the U.K.'s 1890 Partnership Act was adopted in almost all provinces and territories, the U.K.'s 1907 Limited Partnership Act was not so adopted.
[17] Alberta, British Columbia, Manitoba, New Brunswick, Newfoundland & Labrador, Nova Scotia, Ontario and Saskatchewan allow for the creation of limited liability partnerships (LLPs). Statutory regulation of LLPs if found

within the general partnership acts of these provinces. In jurisdictions allowing LLPs, partners of an eligible profession are not liable for the negligent acts of co-partners, but continue to be personally liable for the trade debts and obligations of the partnership.

[18] See Allan Walker Vestal, 'Drawing Near the Fastness?': The Failed US Experiment in Unincorporated Business Entity Reform in McCahery, Raaijmakers and Vermeulen (eds.) ***The Governance of Close Corporations and Partnerships***, (Oxford University Press, 2004);

[19] Legislation pertaining to partnerships in the UK date back to 1865 with "Bovill's Act" which was debtor-creditor legislation aimed at clarifying differences between partnership and other forms of debt relationship. In 1879 Sir Fredrick Pollock drafted the first comprehensive bill codifying the common law applicable to partnership, which draft led to the enactment of the 1890 statute.

[20] Company Law Review (1994) – Law Commission and Department of Industry and Trade (1997) review concluded no need create new form of business association with limited liability as the UK limited company was sufficiently flexible to meet the needs of large and small, private and public firms.

[21] Although impetus for LLPs came from professional groups, it was ultimately decided that enabling only certain regulated groups of professionals to enjoy the privilege of a limited liability partnership could not be sustained. As a result, in the UK the use of the legal form is not restricted to professionals only.

[22] Law Commission Report, footnote 4.

[23] Law Commission Report, footnote 3.

[24] SPA s. 6; OPA s. 5; BCPA s. 1.

[25] SPA s. 7; OPA s. 6; BCPA s. 7.

[26] SPA ss. 12 & 13; OPA ss. 11 & 12; BCPA s. 12 & 13.

[27] Section 98(1).

[28] SPA s. 26; OPA s. 24; BCPA s. 27.

[29] SPA s. 26 (7); OPA s. 24(7); BCPA s. 27(g).

[30] SPA s. 35(1); OPA s. 33; BCPA s. 36.

[31] Lindley & Banks, at para 24-02 refers to a dissolution where the business is carried on by a new partnership without a winding-up as a 'technical' dissolution, while a dissolution followed by a winding-up of the business as a 'general' dissolution.

[32] Upon dissolution, a partner is entitled to his share of the division of profits and capital of the partnership after settlement of the partnership liabilities. SPA s. 41; OPA s. 39; BCPA s. 42 If the partnership business is not wound-up, the partner is entitled to receive his share of the profits based on the profits generated through use of his share of the partnership assets in the on-going business. SPA s. 44; OPA s.42; BCPA s. 45.

[33] SPA s. 7; OPA s. 6; BCPA s. 7.

[34] SPA s. 11; OPA s. 10; BCPA s. 11.

[35] SPA ss. 12 & 14; OPA ss. 11 & 13; BCPA ss. 12 & 14.

[36] SPA s. 16; OPA s. 15; BCPA s. 16.

[37] SPA s. 13; OPA s. 12; BCPA s. 15.

[38] It has been the separation of ownership and control over the business that is often cited as leading to the development of legislation granting limited liability to those owners of the business that are not vested with control authority. For example, in the corporate context, shareholder's as residual owners of the business have limit liability, but are not vested with the authority to manage the business and affairs of the corporation. Rather, the corporation has a separate entity status; the corporation is its own principal and its agents are the directors and officers vested with control authority. In the context of limited liability partnerships, limited partners have limited liability because they do not engage in the management and/or control of the business. In a corporation, shareholders are not liable for contractual or tort obligations of the corporation, and are only liability for their own personal tortuous acts. In the context of a limited partnership, the partnership does not have separate entity status, so the liability of the limited partner is 'limited' by the amount the limited partner has invested in the firm.

[39] SPA s. 7; OPA s. 6; BCPA s. 7

[40] BCPA s. 22. The Saskatchewan and Ontario Acts do not have good faith provisions in their legislation.

[41] SPA s. 31; OPA s. 29; BCPA s. 32. Property of the partnership includes any physical or informational property of the partnership.

[42] SPA s. 32; OPA s. 30; BCPA s. 33.

[43] Business Corporations Act, RSS 1978, c. B-10, s.117; Business Corporations Act , RSO 1990, c. B.16 s.134(1);Business Corporations Act. SBC 2002, c.57, s. 142.

[44] In Canada there are two reasons that the law does not yet recognize agency or fiduciary duties between shareholders. The first being that shareholders are not agents of one another and, as a result, there is no corresponding authority to enter into arrangements that would bind each other. Secondly, the fiduciary duty is

premised on one party being granted access to the assets of another party for a limited purpose. Again, shareholders do not vest authority over their assets to another shareholder. In the corporate context, any assets of the corporation are not assets of the shareholder. Rather, the shareholder is, in fact, only a residual beneficiary of the assets of the corporation upon dissolution, if the corporation is solvent at the time of dissolution. There are some regulatory decisions in Canada which would suggest that in the context of large, controlling shareholders, the law may be developing to find agency and fiduciary duties owed by the controlling shareholder to the minority shareholder; however, such decisions do not properly conceptualize the basis of the fiduciary duty. Furthermore, it is unlikely such a development is necessary given the existence of the statutory oppression remedy which enables minority shareholders to seek court ordered relief against, ***inter alia***, other shareholders in the even of oppressive or unfairly prejudicial treatment by the corporation.

[45] SPA s. 19; OPA s. 18; BCPA s. 19. Partners may be liable for obligations that incur after dissolution on the basis of apparent authority if notice has not been given.

[46] Ibid.

[47] SPA s. 41; OPA s. 39; BCPA s. 42.

[48] SPA s. 34 (a); OPA s. 32(a); BCPA contains no similar legislative provision.

[49] SPA s. 34 (b); OPA s. 32(b); BCPA contains no similar legislative provision.

[50] SPA s. 34 (c); OPA s. 32(c); BCPA s. 29. The ability to dissolve a partnership upon giving notice is reserved for 'at will' partnership (those partnerships that do have fixed terms or whether the fixed term has expired and the partnership continues to carry on business in partnership.) If the partnership agreement provides for a fixed term, a partner is not entitled to unilaterally change the terms of the partnership agreement by giving notice to dissolve. Rather, a partner would have to apply to court to be granted such relief.

[51] SPA s. 35(1); OPA s. 33(1); BCPA s. 36(1).

[52] Ibid.

[53] SPA s. 35 (2); OPA s. 33(2); BCPA s. 36(2).

[54] SPA s. 36; OPA s. 34; BCPA s. 37.

[55] SPA s. 37(a); OPA s. 35(a); BCPA s 38(1)(a).

[56] SPA s. 37(b); OPA s. 35(b); BCPA s. 38(1)(b).

[57] SPA s. 37(c); OPA s. 35(c); BCPA s. 38(1)(c).

[58] SPA s. 37(d); OPA s. 35(d); BCPA s. 38(1)(d).

[59] Ibid.

[60] SPA s. 37(e); OPA s. 35(e); BCPA s. 38(1)(e).

[61] SPA s. 37(f); OPA s. 35(f); BCPA s. 38(1)(f).

[62] SPA s. 41; OPA s. 39; BCPA s. 42.

[63] SPA s. 29(2); OPA s. 27(2); BCPA s. 30(2).

[64] SPA s. 40; OPA s. 38; BCPA s. 41.

[65] SPA s. 26 (2); OPA s. 24(2); BCPA s. 27(b).

[66] SPA s. 26 (1); OPA s. 24(1) BCPA s. 27(a).

[67] SPA ss. 41 & 46; OPA ss. 39 & 44; BCPA ss. 42 & 47.

[68] SPA s. 42; OPA s. 40; BCPA s.43.

[69] SPA s. 44; OPA s. 42; BCPA s. 45.

[70] SPA s. 46; OPA s. 44; BCPA s. 47.

[71] SPA s. 19; OPA s. 18; BCPA s. 19.

[72] SPA s. 40; OPA s. 38; BCPA s. 41.

[73] SPA s. 38(1); OPA s. 36(1); BCPA s.39(1).

[74] SPA s. 39; OPA s. 37; BCPA s. 40.

[75] SPA s. 38(2); OPA s. 36(2); BCPA s. 39(2).

[76] Queens' Bench Rules of Court (Saskatchewan), ss. 52 and 54; Ontario Rules of Practice, Rules 8.01 & 8.02; Supreme Court Rules (British Columbia) Rule 7(1).

[77] SPA ss. 47 & 48; BCPA ss. 84 & 85; OPA does not contain a similar provision.

[78] SPA s. 20; OPA s. 19; BCPA 20.

[79] This conclusion that partners held a joint tenancy interest in all partnership property was first reached in the case of ***Heydon v. Heydon***, 1 Salk. 392 (1693).

[80] SPA s. 22; OPA s. 21; BCPA s. 23.

[81] SPA s. 23; OPA s. 22; BCPA s. 24.

[82] SPA s. 22(2); OPA s.21(3); BCPA s. 23(3).

[83] SPA s. 24; OPA s.23; BCPA s.25.

[84] SPA s. 25(1); Ontario Rules of Practice, Rule 8.06; BCPA s.26.
[85] SPA s. 25(2); OPA does not contain an equivalent section; BCPA s. 26(2). Legislation also grants partners the option of redeeming the charging order, or if a sale is ordered, to purchase the share of the delinquent partner's interest (SPA s.25(3); OPA s. 33(2); BCPA s. 26(3).
[86]Personal Property Security Regulations, P-6.2, Reg. 1, s. 11; Personal Property Security Regulations, R.R.O. 1990, Regulation 912, s. 16(4); Personal Property Security Regulations, B.C. Reg. 227/2002, s.8(f). The difference between real property registry systems and personal property registry systems are that in Torrens real property registry systems, security of title is a fundamental principal. As a result, one need not look beyond the title for confirmation of ownership. Personal property registry systems are 'notice' systems. Registrants claim to have an interest in the property, but the registry system does not provide proof of that interest.
[87] In the UK, land held by a partnership can be vested in no more than four partners (Trustee Act 1925, s. 34(2); Law of Property Act 1925, s. 34(2).
[88] In Saskatchewan for example, title cannot vest in the business name of the partnership, but 'interests' in land may be registered in the name of the partnership, as the registration of an interest on title is not conclusive proof of the validity of the interest. Rather, the registration of an interest provides a notice to third-parties that others claim an interest in the property.
[89] Law Commission Report Part V; Draft Bill cl. 1(3); RUPA s. 201(a).
[90] RUPA s. 601, Comment 1.
[91] http://www.nccusl.org/nccusl/uniformact_why/uniformacts-why-upa.asp
[92] Law Commission Report para 3.2.
[93] Law Commission Report para 8.30, Draft Bill, cl. 38.
[94] Law Commission Report para 12.23.
[95] Law Commission Report, Draft Bill cls. 38, 39, 43 and 45.
[96] RUPA s. 601.
[97] RUPA s. 602.
[98] RUPA s. 701. In contrast, the Law Commission Report does not recommend adoption of expulsion rights or any change to the current expulsion rights contained in the legislation. See SPA s. 27; OPA s. 25; BCPA s. 28.
[99] RUPA s. 801
[100] See the discussion of ***Syers v. Syers*** orders in the Law Commission Report paras 8.9 to 8.12.
[101] Law Commission Report, para 8.17
[102] Law Commission Report para 8.20, Draft Bill cl. 32(1), (2)(a) and (3). The partner would be entitled to be paid the value of his share in the partnership calculated on the hypothesis that the partnership had broken up and its assets were sold on the date of his withdrawal at a price equal to the greater of (i) the liquidation value and (ii) the value based on a sale of the entire business as a going concern without the outgoing partner. The partner wishing to resign from the partnership would also be required to give eight weeks notice of his resignation, and all other partners would then have the right to resign from the partnership by giving two weeks notice and, if not less than half of the partners vote to break-up the partnership, such a vote would supersede the resignation notice. (see para 8.100; Draft Bill, cls 30, 34(5) and 38(2)-(4).)
[103] Law Commission Report para 8.21.
[104] Law Commission Report para 8.22.
[105] Law Commission Report para 8.23.
[106] Law Commission Report para 8.24.
[107] Law Commission Report para 8.25.
[108] Law Commission Report paras 5.11 to 5.23 and 8.13.
[109] SPA s. 19(2); OPA s. 18(2);BCPA s. 19(2).
[110] SPA ss. 38 & 39; OPA ss.36 & 37; BCPA ss. 38 & 39.
[111] SPA s.41; OPA s. 39; BCPA s. 42.
[112] RUPA s. 301 provides that every partner has apparent authority to bind the partnership unless the other party knows that the partner has no authority or has received notification of the partner's lack of authority. Pursuant to s. 102(b), a person has notice of a fact if he knows or has reason to know it exists from all the facts that are known to him or he has received a notification. Accordingly, RUPA allows a partnership to protect itself by sending a notification of the dissociation to a third party. Furthermore, s. 704(c) of the RUPA provides for the filing of a statement of dissociation and the filing of such a statement operates as constructive notice of the dissociated partners lack of authority effective 90 days after filing. In contrast, the Law Commission Report did not recommend that adoption of a similar constructive notice filing system.
[113] Law Commission Report paras 13.6 to 13.9.
[114] Law Commission Report para 12.13, 12.16 & 12.17.

[115] Law Commission Report, para 12.13; Draft Bill, cls. 38, 39(1), (2) and 45.
[116] RUPA s. 801.
[117] D. Weidner, "Pitfalls in Partnership Law Reform: some United States Experience" [2001] 26 Journal of Corporation Law 1031.
[118] Law Commission Report, para 12.14, footnote 20.
[119] Law Commission Report, para 12.18.
[120]Law Commission Report, paras 12.19 & 12.20.
[121] Law Commission Report para 12.25.
[122] Law Commission Report, Part IX.
[123] Law Commission Report para 9.73 & 9.80, Draft Bill cl. 18(2).
[124] Ibid.
[125] Law Commission Report para 9.76, Draft Bill cl. 18(1).
[126] RUPA s. 203.
[127] RUPA s. 204 (a) through (c).
[128] RUPA s. 204(d).
[129] Income Tax Act. s. 96. Partnerships consisting of six (6) or more partners must file a partnership information return setting out the Capital Cost Allowance Schedule, reconciliation of the capital account, tax shelters or renounced resource expenditures and a calculation of the cumulative eligible capital account (CEC): See IC 89-5R and IC89-5RSR.
[130] There is some indication that the federal government is considering introducing an enhanced scheme of dividend tax credits to satisfy thee critics of double taxation.
[131] See for example: J. Clemens, "Canada Needs a Bush-Like Tax Cut" (Jan. 3, 2003) The Fraser Institute http://www.fraserinstitute.ca/shared/readmore1.asp?sNAV=ed&id=131. For an opposing view see: K. Books, Learning to Live with an Imperfect Tax: A Defense of the Corporate Tax (2003), 36 UBCL. Rev. 621.
[132] Department of Finance Canada, Tax and Other Issues Related to Publicly Listed Flow-Through Entities (Income Trusts and Limited Partnerships), Consultation Paper, September 2005. http://www.fin.gc.ca/activty/pubs/toirplf_1e.html.
[133] Internal Revenue Code, Title 26, Subtitle A, Chapter 1, Subchapter K, Part IV, ss. 771 through 775. (Form 1065-B)
[134] Internal Revenue Code, Title 26, Subtitle A, Chapter 1, Subchapter K, Part I, s. 701. (Form 1065)
[135] Ibid, s. 773(B) (b).
[136] Ibid, s. 708(a)
[137] Ibid, s. 708(b)(1)(A) and (B).
[138] Income and Corporation Taxes Act 1998 (ICTA) s. 111: the total sum was treated as "one sum … separate and distinct from any other tax chargeable on those persons … and a joint assessment shall be made in the partnership name".
[139] ICTA 1988, s. 111 (new form).
[140] Taxation of Chargeable Gains Act 1992 s 59: "tax in respect of chargeable gains accruing (to partners) shall, in Scotland as well as elsewhere in the United Kingdom, be assessed and charged on them separately." The Law Commission Report notes difficulties with the application of this rule in practice at para. 3.51.
[141] Law Commission Report, para. 3.53.
[142] Business Corporations Act, RSS 1978, c. B -10, s. 43(1); Business Corporations Act, RSO 1990, c. B.16, s.92(1).
[143] SPA s.64; Limited Partnership Act, RSO 1990, c. L.16, s. 9; BCPA s.57.
[144] Limited liability for beneficiaries of income trusts has been granted in Alberta, Ontario and Manitoba. Saskatchewan has followed this trend by the introduction of Bill No. 40 (2005-2006), The Income Trust Liability Act, which Bill received Royal Assent on May 19, 2006.
[145] RUPA s. 301(1).
[146] RUPA s. 306(a).
[147] RUPA s. 307(d).
[148]Law Commission Report para 6.10, Draft Bill, cl. 6(3). It also recommended that partners would continue to be liable to third parties for partnership debts and obligations (see: paras 6.54 through 6.58, Draft Bill cls. 3, 23(1),(3),(4) & (5).).
[149] Law Commission Report para. 6.7.

[150] Ibid.
[151] SPA s. 11; OPA s. 10(1); BCPA s.11.
[152] SPA s. 26(2); OPA s. 24(2); BCPA s.27(b).
[153] SPA, s. 26(1). OPA s. 24(1); BCPA s. 27(a).
[154] SPA s.11; OPA s. 10(1); BCPA s.11.
[155] Law Commission Report para. 6.58, Draft Bill cl.23(1), (3), (4) and (5).
[156] Law Commission Report para 6.59, Draft Bill cl. 3.
[157] Law Commission Report, para 11.22. In addition, duties of care would be owed to the partnership and not the partners.
[158] RUPA ss. 103(b) (3), 404(b) or 603(b)(3).
[159] RUPA s. 103(b)(5).
[160] RUPA s. 103(3) states that: The partnership agreement may not: (3) eliminate the duty of loyalty under section 404(b) or 603(b)(3), but: (i) the partnership agreement may identify specific types or categories of activities that do not violate the duty of loyalty, if not manifestly unreasonable; or (ii) all of the partners or a number or percentage specified in the partnership agreement may authorize or ratify, after full disclosure of all material facts, a specific act or transaction that otherwise would violate the duty of loyalty. Section. 103(b)(5) states: the partnership agreement may not: eliminate the obligation of good faith and fair dealing under Section 404(d), but the partnership agreement may prescribe the standards by which the performance of the obligation is to be measured, if the standards are not manifestly unreasonable.
[161] Law Commission Report para 11.29, Draft Bill cl. 9.