

AGENCY QUESTION

A man and a woman were equal partners in a neighborhood natural-foods store. The store had been at the same location for many years and had developed a loyal following. Under their informal arrangement, the man had managed the business and the woman had supplied capital to the business as needed.

They leased the building in which the store was located and had regularly sought to purchase the building for the partnership, but the landlord had always refused. Six months ago, however, the landlord called the man and said, "I thought you would want to know that I'm planning to sell the building." The next day, the man sent the woman an email: "I am leaving our partnership. I will wind up the business and send you a check for your half share." Without informing the woman, the man then contacted the landlord and offered to buy the building. The landlord accepted, and the two entered into a binding purchase agreement. One month later, the man took title to the building.

Three months ago, the man sent the woman a check for half of the store's inventory and other business assets. Instead of cashing the check, the woman sent the man an email stating that she regarded the partnership as still in existence and demanded that the man convey title to the building to the partnership. The man replied that their partnership was dissolved and that he had moved on. He then began to operate the store as a natural-foods store with a name different from that of the original store, but with the same product offerings and the same employees.

The woman has sued the man for withdrawing from the partnership and for breaching his duties by buying the building from the landlord.

1. Did the man properly withdraw from the partnership? Explain.
2. Assuming that the man's withdrawal was not wrongful, what was the legal effect of the man's withdrawal from the partnership? Explain.
3. What duties, if any, did the man breach by purchasing the building? Explain.

AGENCY ANALYSIS

AGENCY VI.; VII.; VIII.

ANALYSIS

Legal Problems:

- (1) May a partner properly withdraw from a partnership that has no definite term or specific undertaking?
- (2) What is the legal effect of a partner's withdrawal from an at-will partnership—both on the partnership and on the withdrawing partner's duties?
- (3) What are the duties of a withdrawing partner during the winding up of a dissolved partnership with respect to business opportunities that came to the partner's attention during the partnership?

DISCUSSION

Summary

The man had the right to withdraw from the partnership, and his email stating that he was “leaving” expressed his will to withdraw. His withdrawal was not wrongful, given that the partnership had no definite term or particular undertaking.

The man's withdrawal from the partnership caused the partnership to be dissolved, but this dissolution did not terminate the man's duties to the woman during the winding up of the partnership business. During the winding up of the partnership business, the man continued to owe fiduciary duties to the partnership and the woman, as well as duties of good faith and fair dealing.

The opportunity to purchase the building was a partnership opportunity because of the partnership's prior interest in owning the building and because the opportunity was presented to the man while the partnership was still in existence and prior to its dissolution. The man's purchase of the building violated his duty of loyalty not to appropriate partnership opportunities during the winding-up process, and the purchase was not in good faith because the man failed to inform the woman of the opportunity when he learned of it before he withdrew from the partnership.

[NOTE: An examinee may analyze this question under either the Uniform Partnership Act (1914) (UPA) or the Revised Uniform Partnership Act (1997, as amended in 2013) (RUPA). Although the terminology regarding partnership dissolution and winding up are somewhat different under the two Acts, the legal ramifications of the partner's withdrawal in this two-person, at-will partnership are essentially the same under both Acts. In addition, the revised Act codifies and clarifies the fiduciary duties of partners, and the analysis on this topic cites both the RUPA provisions and applicable case law.

Agency Analysis

All states, except Louisiana, have adopted a version of the Uniform Partnership Act. As of 2017, most states (37) have adopted the revised Act, though only a handful have adopted the 2013 amendments. The original Act, however, remains applicable in the following MEE jurisdictions: Missouri, New Hampshire, New York, Rhode Island, and Wisconsin. *See* Uniform Law Commission, Partnership Act.]

Point One (25%)

The man's email to the woman constituted a withdrawal from the partnership and did not violate the partnership agreement.

A partner may withdraw from a partnership by giving notice at any time. UPA § 31; RUPA § 601(1) (partner is “disassociated” from partnership upon partnership having notice of partner’s “express will to withdraw”). A partner always has the power to withdraw by express will, even if such withdrawal is wrongful or in contravention of the partnership agreement, such as early withdrawal from a partnership with a definite term. UPA § 31(2); RUPA § 601; *see also* Comment 1 to RUPA § 601 (partnership cannot eliminate *power* of partner to dissociate, but can eliminate *right* to dissociate and make such dissociation wrongful).

Dissolution is caused without any violation of the partnership agreement when, among other circumstances, a partner withdraws from an at-will partnership. UPA § 31(1)(b); RUPA § 801(1). In the absence of a definite term or particular undertaking, a partnership is deemed to be at will. *See* Comment, RUPA § 102(13) (partnership at will is “default mode,” unless partners have agreed to definite term or particular undertaking). *See also Girard Bank v. Haley*, 332 A.2d 443, 447 (Pa. 1975) (explaining that “particular undertaking” must be capable of accomplishment at some time, although the exact time may be unknown).

Here, the man’s email to the woman constituted a withdrawal from the partnership and did not violate the partnership agreement, given that there is no indication that the partners (who had been carrying on the business for many years) had agreed on a definite term or particular undertaking for their natural-foods store partnership. Thus, the man’s withdrawal from their at-will partnership was proper.

Point Two (25%)

The man's withdrawal from the partnership caused the partnership to be dissolved, but did not terminate the man's duties to the woman during the winding-up process.

Dissolution of a partnership results in a change in the legal relation of the partners but does not immediately terminate the partnership or the rights and powers of the partners. *See* UPA § 29; RUPA § 801(1) (in at-will partnership, notice of partner’s withdrawal causes partnership to be dissolved, and business must be wound up). Upon dissolution, the partnership continues until the winding up of partnership affairs is completed. UPA § 30; RUPA § 802(a) (partnership continues only for purposes of winding up).

Thus, dissolution marks the point when the partners cease carrying on the partnership business together and begin a process of settling the partnership affairs. The partners' rights, powers, and duties continue during the winding-up process that follows dissolution, during which the partnership liabilities are paid, the business is settled and closed, and the partnership assets are distributed. *See* RUPA § 802(b)(1). The partners' legal relationship and the partnership terminate only when all of the partnership affairs are completely wound up. UPA § 30; RUPA § 802(a).

Under the Uniform Partnership Act (1914), a partnership at will is dissolved by the express will of any partner, and any partner of the dissolved partnership has the right to have the partnership business wound up. UPA §§ 31(1)(b), 38(1). A similar result follows under the Revised Uniform Partnership Act, which provides that a partner in a partnership at will can dissociate from the partnership by that partner's express will, and upon dissociation the partnership is dissolved and its business must be wound up. *See* RUPA §§ 601(1), 801(1); *see also Fleming v. Hagen Estate*, 702 N.W.2d 786, 789 (Minn. Ct. App. 2005) (under revised act, withdrawal from partnership results in dissolution only in at-will partnership).

Here, although the man's withdrawal (or dissociation) caused their at-will partnership to be dissolved, the man continued to have duties to the woman and the partnership during the winding-up process. Because the man's withdrawal (dissociation) from the partnership was not wrongful, he had the power and the right to participate in the winding up of the partnership business, and his actions during that period bound the partnership. *See* UPA § 37; RUPA § 804(a) (dissolved partnership bound by acts of partner "appropriate for winding up the partnership business").

Point Three (50%)

During the winding-up process, the man owed the woman a fiduciary duty to account to the partnership for any benefit derived from the appropriation of a partnership opportunity, as well as duties of good faith and fair dealing. The man's purchase of the building for himself, without telling the woman, breached these duties.

During the winding-up process, partners who participate in the winding up of partnership business continue to have a fiduciary relationship to the partnership and the other partners. *See* RUPA § 409 (except for duty not to compete with partnership, all of partner's fiduciary duties continue to apply during "winding up of the partnership business").

Among the partner's fiduciary duties is a duty to account to the partnership for any benefit derived by the partner from the appropriation of any partnership opportunities. *See* RUPA § 409(b)(1)(C) (duty arises "in the conduct or the winding up of the partnership's business"). The duty not to appropriate partnership opportunities continues during the winding-up process, although "the scope of the partnership opportunities inevitably narrows." *See* Comment to RUPA § 409(b)(1)(C); *see also Bayer v. Bayer*, 215 App. Div. 454, 214 N.Y.S. 322 (1926) (partner's fiduciary duties in a dissolved partnership no longer extend to looking to the future of the business).

Agency Analysis

A partnership opportunity includes one that is “closely related to the entity’s existing or prospective line of business, [that] would competitively advantage the partnership, and . . . that the partnership has the financial ability, knowledge and experience to pursue” *Triple Five of Minn., Inc. v. Simon*, 404 F.3d 1088, 1096 (8th Cir. 2005). A partner who learns of a business opportunity during the term of a partnership may not appropriate that opportunity (without sharing with his co-partners) during the winding-up process or after the partnership term ends. *See Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928) (lease extension and expansion beyond term of original joint venture); *Fouchek v. Janicek*, 225 P.2d 783 (Ore. Sup. Ct. 1950).

In addition, the partner must perform his duties during the winding up of the partnership business “consistently with the contractual obligation of good faith and fair dealing.” RUPA § 409(d). The obligations of good faith and fair dealing encompass a disclosure duty. *See* Comment 4 to RUPA (1997) § 404; *see also Hamilton Co. v. Hamilton Tile Corp.*, 23 Misc.2d 589, 197 N.Y.S.2d 384 (N.Y. Sup. Ct. 1960) (partner’s dealings during the winding-up process include continuing duties of “good faith and full disclosure”); 59A Am. Jur. 2d Partnership § 291, Termination of Partnership (2015) (dissociated partner may not use confidential partnership information after dissociation).

Here, the opportunity to purchase the building in which the store was located constituted a partnership opportunity. The partners’ prior interest in purchasing the building indicates that ownership of the building was an expectancy of the partnership, and there is no indication that the partnership lacked the financial resources to buy the building. Further, given the goodwill that the store had gained at its location, ownership of the building would likely be a partnership opportunity because owning and not having to lease the building would enhance the value of the partnership’s ongoing business. *See* Comment to RUPA (1997) § 803 (recognizing value of preserving partnership business as a going concern during winding-up process); *see also Paciaroni v. Crane*, 408 A.2d 946 (Del. Ch. 1979). In fact, the man’s eagerness to purchase the building provides evidence that ownership of the building created value for the ongoing business of operating the natural-foods store at that location.

The man breached his fiduciary duty to the partnership and the woman by not informing the woman of the opportunity to purchase the building so that their partnership could have acquired the goodwill (customer loyalty) that attached to the building’s location. In addition, the man breached his duty of good faith and fair dealing by not informing the woman of this business opportunity.

The man breached his duties to the partnership and the woman even though he did not begin negotiations for the building’s purchase and did not purchase the building until after withdrawing from the partnership. Courts have found a breach of fiduciary duties even when final negotiations and purchase of the partnership opportunity occur after withdrawal. *See Dzen v. Dzen*, 1999 WL 130545 (Conn. Super. Ct. 1999) (breach of fiduciary duty when partner, after withdrawal and during winding up of partnership, purchased property that had been leased to partnership); *Lavin v. Ehrlich*, 363 N.Y.S.2d 50 (Sup. Ct. 1974) (same).

[NOTE: An examinee might conclude that the man's continuation of the natural-foods store with the same customers, suppliers, and employees of the partnership also constituted a breach of duties to the partnership and the woman. These continuing dealings, however, are not raised in the question.

An examinee might also point out that the proper remedy in this case would be for the man to hold the building in trust as a partnership asset, thus allowing the woman to participate in the building's special value to the partnership. But the proper remedy for the man's breach of his duties is not raised in the question.]

