

EXPULSION AND COMPULSORY RETIREMENT: THE NASTY SIDE OF LIFE

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TEMPERS RAGE. BLOOD BOILS AND FLOWS. AMONG THE HARDEST FOUGHT BATTLES IN THE PARTNERSHIP FIELD ARE THOSE ARISING FROM EXPULSION AND COMPULSORY RETIREMENT.

Starting at the beginning: general principles of expulsion

In order to be able to expel, a power must have been expressly agreed between the partners, typically set out in a partnership agreement. Absent express agreement, there is no power to expel¹ (likewise for compulsory retirement).

Expulsion clauses are strictly construed and in the event of ambiguity, construed against the partners seeking to expel. The Courts are conscious that when a partner is expelled, his share of the business may be ‘confiscated’ (typically for less than he would have received on a general dissolution) and conscious also of the summary nature and stigma of expulsion².

Doing (and undoing) the deed: exercising the power of expulsion

Expulsion clauses list grounds upon which a partner may be expelled and the agreement generally contains a procedure for expulsion. Those expelling need to be sure to follow assiduously the procedure set out, and to draw up carefully the notice (including identifying³ the grounds relied upon)⁴.

The expelled partner may challenge his expulsion by arbitration or Court proceedings⁵, asserting that the expulsion

was wrongful. The Judge scrutinises the facts and asks whether, on the facts, the grounds relied upon are made out. Most grounds contain a qualitative element.

Common grounds contained in agreements include:

- **Misconduct:** this must be more than merely trivial. The older cases talk of “studied omission”. A useful modern case (Thakrar v Vadera [unrep 31.3.99]) relies upon impropriety, a failure to put it right and seriousness, as hallmarks of the more than trivial.
- **Material breach:** per Dillon LJ in DB Rare Books Ltd v Antiqubooks [1995] 2 BCLC 306: “It is enough if a breach goes to the root of the confidence and good faith which should exist between partners.”

Motives for expulsion: the good, the bad and the downright ugly

The expulsion may be challenged, even if justified on the wording of the expulsion clause, on the basis of bad faith/improper motive. Per Lindley & Banks at 10-120⁶:

“A power of expulsion must not be exercised with an ulterior motive, financial or otherwise. Lord Lindley put it in this way:



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'The Court cannot control the exercise of a power to expel if it is exercised bona fide. But all clauses conferring such a power are construed strictly, on account of the abuse which may be made of them, and of the hardship of expulsion; and the Court will never allow a partner to be expelled if he can show that his co-partners, though justified by the wording of the expulsion clause, have, in fact, taken advantage of it for base and unworthy purposes of their own, and contrary to that truth and honour which every partner has a right to demand on the part of his co-partners'.

Equally, an expulsion will not be struck down merely because it happens to fit in with the continuing partners' wish to be rid of the expelled partner: the fact that they have previously been actively looking for a means to remove him from the partnership does not⁷ call their bona fides into question if grounds for the exercise of the power exist."

The new kid on the block: compulsory retirement clauses

Compulsory retirement clauses⁸ are becoming more prevalent. Typically along these lines:

"Any Partner may be required to retire from the Partnership by not less than 6 months' notice in writing requiring such retirement served upon him by the other Partners and any Partner on whom any such notice is served shall forthwith retire from the Partnership on the expiry of the said notice."

In principle, being akin to expulsion (albeit with little or no stigma attached), similar principles ought to apply as to construction and exercise. That said, significantly, no ground needs to be identified or relied upon. This makes it very hard to challenge, as

per The Encyclopaedia of Professional Partnerships:

"if they [the continuing partners] choose to keep their own counsel, the prospects of such exercise being successfully impugned in anything other than an extreme case are remote".

The overriding requirement of good faith must still apply. It may be that by alleging bad faith (with some basis) the expelled partner will 'flush out' the facts and matters relied upon. However, when then seeking to impugn reliance on those facts and matters, one would probably have to show that no reasonable group of partners faced with those circumstances could have reached the decision that they did. A high hurdle indeed.

The price of the majority partners being wrong

If you do establish the expulsion or compulsory retirement was wrongful, then it is as if you had never ceased to be a partner. You are entitled to the drawings you did not receive after the purported expulsion/compulsory retirement.

In principle, if you can show consequential loss which is not too remote, then damages can be claimed. This might be direct loss, eg a partner not being eligible to share in an incentive profit pool. In *Mullins v Laughton* [2003] Ch 250, the then Neuberger J (now elevated to the Lords), accepted in principle that damages for loss of reputation and career disruption could be recoverable.

Applying first principles, the wrongfully expelled/compulsorily retired partner cannot end up in a better position than he would have been had he remained a partner.

The wronged partner may also have a claim under discrimination legislation⁹.

The wronged partner may well also be able to use the failed attempt to remove him as grounds to seek a dissolution of the partnership under s.35 of the Partnership Act 1890.

A cautionary note

Given the venomous fights that regularly follow expulsions and compulsory retirements, those faced with errant (or inept) partners would often be well advised to explore ways of managing the problem (good old fashioned 'discussions', or new fangled 're-training') or failing that, to try and agree a retirement on terms (and avoid potentially substantial costs). Of course, sometimes the circumstances are such that the only option is throwing him overboard. Once done, be prepared for a big splash!

- 1 See s.25 Partnership Act 1890. Partners seeking to be rid of one of their number, but lacking the necessary power, will either need to negotiate his departure or seek to dissolve the partnership (grounds (c), (d) and (f) may be of particular assistance in circumstances typically associated with expulsion).
- 2 See as an example of this approach and as to expulsion generally, *Blisset v Daniel* (1853) 10 Hare 493.
- 3 Whether the identification of grounds is a necessity or merely good practice is debatable. In practice it would be unusual (and potentially legally problematic) not to do so.
- 4 When seeking to establish that the expulsion was not wrongful, it may be possible to rely as justification upon additional misdeeds of the expelled partner that came to light after the expulsion. It will be more difficult to seek to rely as additional grounds upon matters known about at the time of expulsion, but not then relied upon. The expelled partner may be able to rely upon waiver.
- 5 For simplicity's sake, I refer below simply to the Court/Judge. Whether or not to go to arbitration, rather than Court, depends on whether the agreement contains an arbitration clause and if so, its scope.
- 6 See also *Blisset v Daniel* (supra).
- 7 When the Court considers an expulsion it will however, take into account the entire factual matrix. Previous attempts to expel may colour the way that a Court assesses the genuineness of the grounds purportedly relied upon.
- 8 Again an expressly agreed power is required.
- 9 See among other relevant legislation, s.6A(1)(d)(ii) of the Disability Discrimination Act 1995 and see also *Dave v Robinska* [2003] ICR 1248.