



Partnership

By Mark C. Rossman and Brendan H. Frey

and the Fiduciary Component

Duties, Obligations, Rights, and Remedies

Not honesty alone, but the punctilio
of an honor the most sensitive,
is then the standard of behavior.

—J. Benjamin Cardozo¹

The standards for establishing a partnership may reasonably be viewed as somewhat relaxed. In fact, neither a written nor even an oral agreement is required to create a partnership. Moreover, a partnership may exist independent of the parties' intent, and a partnership can be found even when the parties expressly did not intend to form a partnership.

Given the broad definition in Michigan of what constitutes a "partnership," the partnership penumbra is applied to a wide array of factual scenarios in the caselaw and should be considered by the business law practitioner when someone has been wronged

by another member of a business enterprise. If a partnership is not desired at the onset of a business relationship, one must be careful not only to appropriately define the relationship in agreements, but also to conduct the business affairs so as not to permit a finding of a partnership should litigation arise.

The consideration of a partnership claim in litigation is particularly important when the elements of a contract claim or business tort may be lacking. For instance, your client may have had an understanding with another person to equally divide the proceeds of a business endeavor, but there was no written contract between them and they now disagree on what their intentions were. There may be evidence that the parties appeared to be equals in running the business, but your client's business "partner" is paying himself an inordinate amount of the profits as purported salary or claiming certain of the business's assets as his own, preferring himself over your client. Another example may be that a business that two people founded and grew into a profitable enterprise is sold and one partner claims a much greater portion of the proceeds.

Fast Facts

Under *Byker v Mannes*, a partnership can be found to exist even if the parties did not intend to form a partnership.

Even after *Byker*, recent decisions show that some courts still give weight to the parties' intent to form, or not form, a partnership.

The fiduciary duties among partners are strict and require the utmost good faith and honesty.

Without clear agreements defining who is entitled to what, or what the parties' respective roles in the enterprise are, claims based on contract or tort theories will present some challenges that may ultimately leave the aggrieved party without a remedy. Claims based on the Uniform Partnership Act can be particularly valuable when the elements of traditional contract or business tort claims may be difficult to establish. Once established, the partnership gives rise to very strict fiduciary duties, the breach of which triggers significant remedies available to the aggrieved partner.

A Partnership Can Arise Even When There is No Intent

The concept of a partnership is statutorily defined in Michigan. Michigan's Uniform Partnership Act (Partnership Act)² provides that "[a] partnership is an association of 2 or more persons...to carry on as co-owners a business for profit[.]"³ In *Byker v Mannes*, the Michigan Supreme Court held that even absent the intent to create a partnership, a partnership can nonetheless arise.⁴ Thus, the analysis is not one of subjective intent to form a partnership. Rather, it is of the parties' objectively manifested conduct toward one another with respect to the parties' business, and whether such conduct meets the statutory definition of a partnership.

In deciding whether a partnership exists, courts are directed by the caselaw to engage in a broad, intensely factual review of "all the attendant circumstances," and no single factor in the analysis will be conclusive.⁵ For example, even a signed partnership agreement is not conclusive proof that a partnership existed.⁶ Similarly, registering a business as a partnership merely creates a presumption that there is a partnership.⁷

In *Byker*, the Supreme Court held that a partnership may underlie a corporate entity's business affairs and stand independent of formal shareholder relationships within the corporate entity.⁸ In some cases, this holding will undercut a defense asserted pursuant to MCL 449.6(2), which provides that "any association formed under any other statute of this state...is not a partnership[.]" The plaintiff and the defendant in *Byker*, to facilitate investments for their partnership, created separate corporate entities and individual partnerships in which they were shareholders for the purpose

of operating each separate entity.⁹ The defendant took the position that the formalized shareholder relationships established by the separate entities defined the nature of his obligations to the plaintiff and, therefore, he could have no liability under the Partnership Act. The Court disagreed and held that there was a "general"¹⁰ partnership underlying all of the separate corporate entities. Despite the existence of the parties' well-defined relationships in the separate entities, the Partnership Act applied with full force in *Byker*, and the Court clarified that the focus of any intent analysis, as one factor out of many, is only "on whether the parties intended to carry on as co-owners a business for profit" and not "on whether the parties intended to form a partnership."¹¹

Even After *Byker*, Partnership Intent Still Plays a Role in the Analysis

Despite the declaration in *Byker* that intent to form a partnership is irrelevant, recent appellate decisions illustrate that some courts still hold the intent factor in high esteem. In *Gunnnett v Brooks*, a 2007 unpublished decision, the Court of Appeals affirmed a trial court's holding that no partnership was formed, focusing on the fact that "the evidence presented at trial supported the trial court's finding that neither plaintiff nor defendant intended to form a partnership when they signed the umbrella distribution agreement."¹² In holding as such, the Court noted, "[i]n considering whether a partnership exists, the intention of the parties is of prime importance."¹³ While the Court of Appeals went on to apply the *Byker* analysis and held that the various indicia of a partnership was lacking, it is clear that the intent of both parties to not form a partnership was an important factor in the analysis.¹⁴

Similarly, in the 2007 published decision of *Kay Investment Co, LLC v Brody Realty No 1, LLC*, the Court of Appeals, in a 2–1 decision, held that the intent of the parties as embodied in a "joint venture agreement" supported the finding that the parties did not form a partnership.¹⁵ In finding a joint venture and rejecting the partnership claim, the Court of Appeals cited to the fact that the parties' agreement "does not contain language that suggests the formation of a partnership," as it "does not contain the word 'partnership.'¹⁶ In his dissent, Judge Schuette sharply criticized and characterized the majority's opinion as a departure from the mandates of the Michigan Supreme Court in *Byker*.¹⁷ He wrote that *Byker* "clearly outlined the differences between individuals' subjective intent and their conduct in a business relationship," as was articulated by Justice Cooley, who was quoted extensively in *Byker*:

It is nevertheless possible for parties to intend no partnership and yet to form one. If they agree upon an arrangement which is a partnership in fact, it is of no importance that they call it something else, or that they even expressly declare that they are not to be partners. The law must declare what is the legal import of their agreements, and names go for nothing when the substance of the arrangement shows them to be inapplicable.¹⁸

While both the *Kay Investment* and *Gunnnett* decisions also analyzed several of the non-subjective partnership factors enunciated by the Partnership Act, these recent decisions show that intent to form, or not form, a partnership will not always be disregarded by the courts.

What Kind of Conduct Gives Rise to a Finding of a Partnership?

In establishing whether a partnership exists, several factors are delineated by the Partnership Act and by caselaw. In Michigan, indications of a partnership may include any of the following:

- The sharing of profits (this constitutes prima facie evidence of a partnership)¹⁹
- A party rendering services while also possessing rights of management, such as the authority to enter into contracts²⁰
- The use of the term “partner” by the parties²¹
- The belief of third parties that they were dealing with a partnership²²
- The contribution of experience “in more than an advisory or consulting capacity”²³
- The contribution of “capital, consisting of money, merchandise, et cetera, or credit, skill, or labor”²⁴

Factors that may cut against the finding of a partnership include any of the following:

- Tax returns that do not list the business as a partnership²⁵
- Title to property involved in the operation of the partnership that is not in the partnership’s name²⁶
- All business contracts in the name of the party denying the existence of a partnership²⁷
- No agreement to share losses²⁸
- Receivable checks payable to the party denying the existence of a partnership²⁹
- No partnership bank account³⁰
- No filed statutory certificate³¹

As these non-exhaustive lists illustrate, most breach-of-partnership disputes will be fact-intensive in terms of establishing whether a partnership exists.

The Fiduciary Duties are Expansive and Strict

Michigan courts universally recognize the fiduciary relationship of partners and impose on them obligations of the utmost good faith and integrity, requiring the full and honest disclosure of information to one another.³² The Court in *Band v Livonia Assoc* held that “[e]ach partner has the right to know all that the others know, and each is required to make full disclosure of all material facts within his knowledge in any way relating to the partnership affairs.”³³ Partners also have a right to access partnership books and a right to an account of partnership affairs.³⁴

Several holdings in Michigan jurisprudence have defined the type of conduct that constitutes a breach of these duties. For example, partners are prohibited from engaging in competing businesses without accounting to co-partners.³⁵ Partners breach their fiduciary duties when they exclude the other partner from working in the partnership and earning a salary, or by operating the business without the other partner’s consent.³⁶ The fiduciary obligation requires partners to fully disclose partnership affairs and obtain consent of the partners before conveying partnership property to themselves.³⁷ Disclosure of material facts to some partners but not others is a fiduciary breach.³⁸

Absent an agreement to operate the partnership for an express term or to terminate the partnership after a particular undertaking, partners dissatisfied with the status quo can dissolve the partnership at will.³⁹ However, dissolution of the partnership alone does not immediately end the partnership, and fiduciary duties remain until a winding-up phase is complete and the partnership’s assets are distributed.⁴⁰

The Remedies for a Breach

Even when there is an agreement establishing an express term for the partnership, a partner who has been wronged by another partner’s breach of fiduciary duties may petition the court for a decree of dissolution.⁴¹ Dissolution must be ordered if the court finds that the breach of fiduciary duties prejudicially affects the continuation of the partnership or if it is not reasonably practicable to carry on the partnership.⁴² In addition to the dissolution of the partnership, under MCL 449.38(2)(a)(II), an aggrieved partner is entitled to damages against each partner who wrongfully

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caused the dissolution.⁴³ The aggrieved partner's damages remedy is for him or her to be made economically whole.⁴⁴ Put another way, the remedy consists of "placing the wronged partners in the economic position that they would have enjoyed but for the breach."⁴⁵ Exemplary damages are not available for a breach of a fiduciary duty claim in the context of a partnership, because the fiduciary duties are held to arise from the partnership "contract," which is implied under the Partnership Act.⁴⁶

Conclusion

The possibility of a partnership claim may be based on myriad facts and circumstances and should not be overlooked by the business law practitioner, either in litigating business disputes or in explicitly defining in agreements the parties' expectations and duties. To avoid partnership standards of accountability and disclosure in a business enterprise, participants should ensure that organizational documents clearly disclaim the existence of a partnership, and they should conduct their business affairs in such a manner as to avoid any presumption of a partnership. On the other hand, when one faction of a business is aggrieved by the conduct of the other, the Partnership Act may give rise to a viable claim. ■



Mark C. Rossman is a partner in the law firm of Mantese and Rossman, P.C., in Troy (www.manteseandrossman.com). He concentrates his practice in complex commercial and business litigation, shareholder and partnership disputes, business transactions, and distressed loan workouts and related litigation. He has previously written about the role of fiduciary duties in the context of reinsurance contracts (86 Mich BJ 5 (May 2007)). In 2007, he was profiled in Lawyers Weekly as one of Michigan's "Up and Coming Lawyers."



Brendan H. Frey is an associate with Mantese and Rossman, P.C., concentrating in complex commercial and business litigation and shareholder and partnership disputes. He graduated cum laude from Wayne State University Law School in 2007, where he earned a Silver Key Certificate and was president of the Environmental Law Society. Mr. Frey earned his undergraduate degree from the University of Michigan (BA, 2002).

FOOTNOTES

1. *Meinhard v Salmon*, 249 NY 458, 464 (1928) [emphasis added]; see also *Band v Livonia Assoc.*, 176 Mich App 95, 113; 439 NW2d 285 (1989), citing 59A Am Jur 2d, Partnership, § 420, p 453 ("The courts universally recognize the fiduciary relationship of partners and impose on them obligations of the utmost good faith and integrity in their dealings with one another in partnership affairs.")
2. MCL 449.1 *et seq.*
3. MCL 449.6(1).
4. *Byker v Mannes*, 465 Mich 637, 653; 641 NW2d 210 (2002).
5. *Hynansky v Vietri*, unpublished opinion of the Court of Chancery of Delaware, issued August 7, 2003 (Docket No. 14645-NC), p 6 (holding based on a Delaware statute with language identical to Michigan's Uniform Partnership Act).
6. *Hynansky*, *supra*.
7. *Miller v City Bank & Trust Co, N A*, 82 Mich App 120; 266 NW2d 687 (1978).
8. *Byker*, *supra* at 641-642.
9. *Id.* at 639.
10. The Court of Appeals deemed it a "general" or "super" partnership. The Michigan Supreme Court removed the modifiers and simply referred to the business relationship as a partnership.
11. *Byker*, *supra* at 653 n 9.
12. *Gunnett v Brooks*, unpublished opinion per curiam of the Court of Appeals, issued January 18, 2007 (Docket No. 263838), p 3.
13. *Id.*, citing *Lobato v Paulino*, 304 Mich 668, 670-671; 8 NW2d 873 (1943).
14. *Id.* at 4.
15. *Kay Investment Co, LLC v Brody Realty No 1, LLC*, 273 Mich App 432, 443; 731 NW2d 777 (2007).
16. *Id.* at 443.
17. *Id.* at 446-447.
18. *Id.* at 447, citing *Byker v Mannes*, 465 Mich 637, 648-649, 641 NW2d 210 (2002), quoting *Beecher v Bush*, 45 Mich 188, 193-194; 7 NW 785 (1881).
19. MCL 449.7(4); *Falkner v Falkner*, 24 Mich App 633, 643; 180 NW2d 491 (1970); *Lobato v Paulino*, 304 Mich 668, 670-671; 8 NW2d 873 (1943); *Klein v Kirschbaum*, 240 Mich 368; 215 NW 289 (1927); 137 ALR 33.
20. *Falkner*, *supra* at 642-644; 137 ALR at 64; *Runo v Rothschild*, 219 Mich 560; 189 NW 183 (1922).
21. *Falkner*, *supra* at 642-644; 137 ALR at 86.
22. *Falkner*, *supra* at 642-644; 137 ALR at 79.
23. *Shacket Developments, Inc v Labana*, unpublished opinion per curiam of the Court of Appeals, issued February 28, 2003 (Docket No. 237232), p 2.
24. *Michigan Employment Security Comm v Crane*, 334 Mich 411, 416; 54 NW2d 616 (1952).
25. *Miller*, *supra*.
26. *Id.*
27. *Moore v Du Bard*, 318 Mich 578; 29 NW2d 94 (1947).
28. *Id.*
29. *Id.*
30. *Id.*
31. *Id.*
32. *Penner v De Nike*, 288 Mich 488; 285 NW 33 (1939).
33. *Band*, *supra* at 113-114.
34. MCL 449.19 and 449.22.
35. *Johnson v Ironside*, 249 Mich 35; 227 NW 732 (1929).
36. *Yager v Howard*, unpublished opinion per curiam of the Court of Appeals, issued August 2, 2007 (Docket No. 269120), p 2.
37. MCL 449.20 and 449.21(1); *Carto v Underwood Prop*, unpublished opinion per curiam of the Court of Appeals, issued June 12, 2008 (Docket No. 272747), pp 4-5.
38. *Band*, *supra* at 113-114.
39. MCL 449.31; *Fall v Loudon*, unpublished opinion per curiam of the Court of Appeals, issued February 12, 2008 (Docket No. 275519), p 3, n 2.
40. MCL 449.30, 449.37, 449.38, and 449.40; *Fall*, *supra* at 3, n 4, citing *Howe v Weibert*, 332 Mich 84, 95; 50 NW2d 75 (1952); *Brooks v Rose*, 191 Mich App 565, 570-571; 478 NW2d 731 (1991), citing *Gilroy v Conway*, 151 Mich App 628, 637; 391 NW2d 419 (1986).
41. MCL 449.32; *Band*, *supra* at 114.
42. MCL 449.32; *Band*, *supra*.
43. MCL 449.38(2)(a)(iii); *Brooks*, *supra* at 570-571.
44. *Gilroy v Conway*, 151 Mich App 628, 637; 391 NW2d 419 (1986), citing MCL 449.21.
45. *Gilroy*, *supra* at 637-638, citing *Lynn v Arehart*, 231 Mich 144; 203 NW 834 (1925); *Penner v De Nike*, 288 Mich 488; 285 NW 33 (1939); *Van Stee v Ransford*, 346 Mich 116; 77 NW2d 346 (1956).
46. *Gilroy*, *supra* at 637 ("There is no tortious conduct here existing independent of the breach of the partnership contract.")