FIRST DIVISION, INNER HOUSE, COURT OF SESSION

[2018] CSIH 68
XA7/19

Lord President
Lord Brodie
Lord Drummond Young

OPINION OF THE COURT

delivered by LORD BRODIE

in the Appeal from the Sheriff Appeal Court

by

DR ANDREI SHEVELEU

Pursuer and Appellant

against

DRS ANDREW BROWN AND CHRISTOPHER DUCKER

Defenders and Respondents

Pursuer and Appellant: Isla Davie, Advocate; Young & Partners, Dunfermline
Defenders and Respondents; McIlvride QC; Harper Macleod LLP

31 October 2018

Introduction

[1] This is an appeal from the Sheriff Appeal Court ("SAC") with the permission of this court. Whereas initially it appeared to raise questions about the proper function and scope of sections 38 and 42 of the Partnership Act 1890 in the winding-up of a partnership, as the

argument developed it came more to focus on the proper import of sheriff's (unchallenged) findings-in-fact.

[2] The action was raised in the Sheriff Court of South Strathclyde, Dumfries and Galloway at Stranraer. It is for count, reckoning and payment. It is at the instance of one former partner of a dissolved firm of general medical practitioners (the Southern Machars Group Practice) against the other two former partners. After proof on a Note of Objection to Accounts and Answers, the sheriff, in terms of an interlocutor dated 20 December 2016, found the defenders liable to make payment to the pursuer in the sum of £15,949, together with certain payments of interest. The sheriff held that in so far as the pursuer had any claim for profits arising subsequent to the date of dissolution of the partnership that fell to be quantified by reference to section 42 of the Act.

[3] The pursuer appealed to the SAC on the grounds that the sheriff had left out of account certain income accruing subsequent to the date of dissolution of the partnership and paid to the defenders but which fell to be treated as belonging to the partnership and therefore, by virtue of sections 24 and 29 of the 1890 Act, shared between the former partners as part of the settlement on winding-up. It was the pursuer's contention that the income arose from an uncompleted transaction of the former partnership which must be taken to have been completed by the defenders by virtue of the authority conferred on them by section 38 of the 1890 Act. It was further contended that the defenders were therefore obliged to account to the pursuer for his share of what properly were profits of the former partnership. The SAC rejected that contention and on 25 August 2017 refused the appeal. Permission to appeal having been refused by the SAC, it was granted by this court on 7 December 2017.

[4] The appeal to the SAC had also included an appeal against the sheriff's decision on expenses. That point is not renewed in the appeal to this court.

The relevant statutory provisions

[5] The Partnership Act 1890 provides, *inter alia*:

> **4. Meaning of firm.**
>
> (1) Persons who have entered into partnership with one another are for the purposes of this Act called collectively a firm, and the name under which their business is carried on is called the firm-name.
>
> (2) In Scotland a firm is a legal person distinct from the partners of whom it is composed, but an individual partner may be charged on a decree or diligence directed against the firm, and on payment of the debts is entitled to relief *pro ratâ* from the firm and its other members.
>
> **9. Liability of partners.**
>
> Every partner in a firm is liable jointly with the other partners, and in Scotland severally also, for all debts and obligations of the firm incurred while he is a partner; and after his death his estate is also severally liable in a due course of administration for such debts and obligations, so far as they remain unsatisfied …
>
> **20. Partnership property.**
>
> (1) All property and rights and interests in property originally brought into the partnership stock or acquired, whether by purchase or otherwise, on account of the firm, or for the purposes and in the course of the partnership business, are called in this Act partnership property, and must be held and applied by the partners exclusively for the purposes of the partnership and in accordance with the partnership agreement.
>
> …
>
> **24. Rules as to interests and duties of partners subject to special agreement.**
>
> The interests of partners in the partnership property and their rights and duties in relation to the partnership shall be determined, subject to any agreement express or implied between the partners, by the following rules:—

(1) All the partners are entitled to share equally in the capital and profits of the business, and must contribute equally towards the losses whether of capital or otherwise sustained by the firm.

(2) The firm must indemnify every partner in respect of payments made and personal liabilities incurred by him –

(a) in the ordinary and proper conduct of the business of the firm; or,

(b) in or about anything necessarily done for the preservation of the business or property of the firm.

…

(5) Every partner may take part in the management of the partnership business.

(6) No partner shall be entitled to remuneration for acting in the partnership business.

…

29. Accountability of partners for private profits.

(1) Every partner must account to the firm for any benefit derived by him without the consent of the other partners from any transaction concerning the partnership, or from any use by him of the partnership property name or business connexion.

(2) This section applies also to transactions undertaken after a partnership has been dissolved by the death of a partner, and before the affairs thereof have been completely wound up, either by any surviving partner or by the representatives of the deceased partner.

...

38. Continuing authority of partners for purposes of winding up.

After the dissolution of a partnership the authority of each partner to bind the firm, and the other rights and obligations of the partners, continue notwithstanding the dissolution so far as may be necessary to wind up the affairs of the partnership, and to complete transactions begun but unfinished at the time of the dissolution … but not otherwise.

…

42. Right of outgoing partner in certain cases to share profits made after dissolution.

(1) Where any member of a firm has died or otherwise ceased to be a partner, and the surviving or continuing partners carry on the business of the firm with its capital or assets without any final settlement of accounts as between the firm and the outgoing partner or his estate, then, in the absence of any agreement to the contrary, the outgoing partner or his estate is entitled at the option of himself or his representatives to such share of the profits made since the dissolution as the Court may find to be attributable to the use of his share of the partnership assets, or to interest at the rate of five per cent. per annum on the amount of his share of the partnership assets.

…

44. Rule for distribution of assets on final settlement of accounts.

In settling accounts between the partners after a dissolution of partnership, the following rules shall, subject to any agreement, be observed:

(a) Losses, including losses and deficiencies of capital, shall be paid first out of profits, next out of capital, and lastly, if necessary, by the partners individually in the proportion in which they were entitled to share profits:

(b) The assets of the firm including the sums, if any, contributed by the partners to make up losses or deficiencies of capital, shall be applied in the following manner and order:

In paying the debts and liabilities of the firm to persons who are not partners therein: In paying to each partner rateably what is due from the firm to him for advances as distinguished from capital:

In paying to each partner rateably what is due from the firm to him in respect of capital: The ultimate residue, if any, shall be divided among the partners in the proportion in which profits are divisible."

The pleadings and the accounting

[6] The pleadings in the case consist of a Closed Record on the initial writ and defences, as amended and closed of new on 19 November 2015, and a Note of Objection to Accounts and Answers, received on 18 June 2015.

[7] In terms of the Closed Record the pursuer seeks production of the whole books and accounts of the former firm of the Southern Machars Group Practice together with a full

account by the defenders of their intromissions with the assets of the firm so that the true balance due to the pursuer may be ascertained and for payment by the defenders to the pursuer of the balance found due. It is averred by the pursuer and admitted by the defenders that the parties were partners in the partnership of the Southern Machars Group Practice, that the pursuer was entitled to receive a third of the profits of that partnership and that the partnership was dissolved on 12 March 2014.

[8] It was further admitted that at the date of the dissolution of the Southern Machars Group Practice the firm was party to a general medical services contract with NHS Dumfries & Galloway (a trading style of Dumfries & Galloway Health Board) (the "DGNHS contract"). In terms of the DGNHS contract, the firm required to give six months' notice of its intention to cease providing services.

[9] At article 4 of condescendence the pursuer averred that the firm continued to provide services under the DGNHS contract until 30 June 2014. In answer 4 the defenders denied that averment and in response averred:

> "Explained and averred that the dissolved partnership did not trade or provide services after that date. By letters to the pursuer and each of the defenders all dated 20 February 2014, NHS Dumfries & Galloway required the individual partners of the dissolved partnership to continue to provide medical services in accordance with the contract until the earlier of 30 September 2014 or the date of a new contractual arrangement being established. The defenders provided medical services in accordance with the provisions of the contract until 30 June 2014, when new contractual arrangements were established in accordance with the requirements of NHS Dumfries & Galloway."

[10] In article 5 of condescendence the pursuer avers that he has called upon the defenders to produce an accounting of their intromissions with the assets of the firm up to and including 30 June 2014. In answer the defenders explained that the "accounts of the dissolved partnership for the period 12 March to 30 June 2014 shall be made available to the pursuer as soon as they are prepared." Accounts for the period, headed "Southern Machars

Group Practice Unaudited Accounts" (6/2 of process) were lodged by the defenders before 10 June 2015. These accounts are the subject of the Note of Objections and Answers. In the Note of Objections the pursuer refers to a "management charge of £174,935" and calls on the defenders to provide a full account of the charges levied by them under this head. In their Answers the defenders aver that it "was necessary for the partnership of the defenders to perform the obligations of the partnership in terms of the NHS contract" and that "it was considered inappropriate by the defenders and [the Health Board] for the [pursuer] to continue to work within the practice building following the dissolution of the partnership."

[11] As appears from another set of accounts in respect of the period 13 March 2014 to 30 June 2014 also lodged by the defenders (6/7 of process) the "partnership of the defenders" referred to by the defenders in their Answers to the Note of Objections was a partnership between only the two defenders and was styled the "Southern Machars Practice". In 6/7 of process there is an item for sundry fee income. If one deducts the sum of £2066 which relates to "insurance examinations, medicals and reports" from the total for sundry fee income, one arrives at a figure of £174,935. That has two components: reimbursement of costs - £114,935; and reimbursement of partner salary - £60,000.

[12] We shall come back to this when discussing the sheriff's decision but on the face of these sets of accounts (6/2 and 6/7 of process), over the period 12 March to 30 June 2014 a new partnership between the defenders (the Southern Machars Practice) had charged the dissolved partnership among the pursuer and the defenders (the Southern Machars Group Practice) with the costs (in the sense of outlays) of providing medical services together with "partnership salary". During the period the dissolved partnership received "Total NHS Income" of £210,038. As appears from the accounts 6/7 of process, the new partnership received no income directly from the Health Board.

The relevant findings-in-fact

[13] The sheriff recorded his findings-in-fact, in so far as relevant to the issue in the appeal as follows:

> "1. On or about 01 May 2013 the pursuer and the defenders formed a partnership at will which operated under the name The Southern Machars Group Practice which provided primary general medical services and operated a dispensing pharmacy within the south Machars area of Wigtownshire.
>
> 2. As a partner, during the continuance of the partnership, the pursuer was entitled to and did receive a one third share of partnership profits.
>
> 3. By February 2014 the partnership had ceased to function as a consequence of the irretrievable breakdown in the relationship between the pursuer and the two defenders.
>
> 4. The breakdown occurred because of the pursuer's unacceptable conduct. The pursuer was rude to and dismissive of patients. As a result of this attitude patients declined to consult the pursuer.
>
> …
>
> 9. On 20 February 2014 the defenders concluded the partnership could not continue. On 20 February 2014 the defenders required the pursuer to leave the partnership premises.
>
> 10. The partnership among the pursuer and the defenders was dissolved on 12 March 2014.
>
> 11. The partnership during its existence was contracted with Dumfries and Galloway Health Board to provide GP services within their area (the DGNHS contract).
>
> 12. Upon dissolution of the partnership the DGNHS contract still subsisted until the six months' notice period expired or other arrangements for provision of the services contractually due by the partnership could be made by the Health Board.
>
> 13. New arrangements were put in place by the Health Board with effect from 01 July 2014.
>
> 14. Throughout the period 13 March 2014 to 30 June 2014 the defenders carried out the services required of the partnership in terms of the DGNHS contract.

15. They carried out these services as partners of the dissolved firm, The Southern Machars Group Practice.

16. Throughout the period 13 March 2014 to 30 June 2014 the pursuer did not carry out any services in terms of the DGNHS contract.

17. At no time during the period did the pursuer attempt to carry out any services in terms of the DGNHS contract. …

22. The charges made by the defenders for their services, during the period 13 March to 30 June 2014 were reasonable in that they charged their services at a standard locum rate

…

24. The pursuer was entitled to receive £8322 as his share of profits from the dispensing pharmacy brought out in the accounts for the period 13 March 2014 to 30 June 2014 for the Southern Machars Group Practice.

25. The defenders, in the absence of the pursuer carrying out his share of the partnership business, reasonably incurred locum costs of £2980 in their management of the Southern Machars Group Practice in the period 13 March 2014 to 30 June 2014."

The sheriff's decision

[14] As appears from the sheriff's findings-in-fact, in the period from the dissolution of the former partnership on 12 March 2014 until new arrangements were put in place on 1 July 2014, the primary care services which the former partnership had contracted to provide under the DGNHS contract were actually provided by the defenders without any assistance from the pursuer.

[15] What is not the subject of a finding-in-fact (because the sheriff decided it was irrelevant and therefore could be ignored) but can be seen from the sheriff's note, and as we have foreshadowed above in our summary of the accounting, was that in their accounting the defenders had presented what had been done in the period between 13 March and 30 June as the sub-contracting by the dissolved partnership of the services to be performed

under the DGNHS contract to a new partnership between the two defenders (see sheriff's note paragraph 15). The sheriff decided that there was no legal basis for what the defenders' accounting purported to have been done. The authority conferred by section 38 of the 1890 Act on former partners for the purposes of winding-up did not go the distance of authorising the defenders, as partners of the dissolved firm, to enter into a new contractual relationship with a third party. Accordingly, in so far as the defenders were continuing to service the DGNHS contract the sheriff concluded that they were doing so as partners of the dissolved partnership, (note paragraph 22). Their management decisions in that respect were necessary and reasonable. The sheriff's conclusion on this is reflected in his findings-in-fact 12 to 15.

[16] At paragraph 30 of his note the sheriff records that the pursuer claimed one third of "the £60,000 management charge by the Southern Machars Practice (the new partnership) against the old partnership". This sum of £60,000 is what appears in the new partnership accounts as "reimbursement of partner salary". Viewed from the perspective of the dissolved partnership it is in effect the profit element in the payments made by the Dumfries and Galloway Health Board under the DGNHS contract after deduction of costs.

[17] The sheriff accepted the pursuer's submission that the introduction of the new partnership as a further party in the accounts should be ignored (note paragraph 28). However, he did not allow the pursuer a one third share in the £60,000. The pursuer had relied on the provision in section 24(1) of the 1890 Act that, in the absence of agreement to the contrary, all the partners are entitled to share equally in the profits of the business. The pursuer had contended that in that it had been the business of the former partnership that the defenders had been continuing until 30 June 2014 for the purpose of winding up, the pursuer was entitled to a one third share of profits generated in that period. Although he

does not quite say so explicitly, it would appear that, for the sheriff, entitlement to share in profits, as provided for by section 24 rule (1), was conditional on taking part in the management of the partnership business, as a partner is entitled to do by virtue of section 24 rule (5). Why that is so is not explained, although the terms of paragraphs 24 and 25 of the sheriff's note would suggest that he thought it important that the pursuer had played no part in what the defenders had done between 13 March and 30 June 2014. The sheriff summarises his conclusion at paragraph 27 of his note thus:

> "In summary on the primary issue of which provisions applied to the continuance of the old firm during its winding down I found the defenders acted in terms of s38 to the extent of maintaining the old firm's obligations under the DGNHS contract and that they were bound to account to the pursuer in term of the provisions of s42."

The SAC's decision

[18] The pursuer appealed to the SAC.

[19] For the SAC the issue was whether section 38, taken with section 24, or section 42(1) of the 1890 Act applied to the situation in the case. The cases of *Manley* v *Sartori* [1927] 1 Ch 157 and *Berry* v *Lamb* (1832) 10 S 792 which had been cited on behalf of the pursuer did not assist his position. While there was little law on the matter, as the facts found by the sheriff did not indicate to the SAC that the continuing provision of services under the DGNHS contract, to which the pursuer had not contributed, amounted to the completion of an "unfinished transaction" for the purposes of section 38, it followed that the sheriff had been correct in assessing the pursuer's entitlement to share profits by reference to section 42(1). The appeal was refused.

Submissions

Appellant

[20] On behalf of the pursuer and appellant Ms Davie confirmed that parties were agreed that the sum of £60,000 represented the profits to be attributed to the DGNHS contract during the relevant period. It was the position of the pursuer and appellant that he was entitled to a one third share of that sum. Accordingly, the appeal should be upheld, the decree of the sheriff quashed and, in substitution, decree pronounced for payment by the defenders to the pursuer of the sum of £35,949. Ms Davie adopted her written note of argument which she developed in her oral submissions.

[21] The decision at first instance was an unusual one. The sheriff had found that the defenders had been winding up the former firm after its dissolution by virtue of the authority conferred on them by section 38 but the net profit generated in respect of the services provided as part of that winding up was distributed in accordance with section 42(1). The pursuer had not presented his claim in terms of section 42(1) and neither, primarily, had the defenders presented their defence in terms of section 42(1); only at the end of the argument had it been suggested on behalf of the defenders that the subsection was relevant. In accepting that argument for the defenders the sheriff had effectively made the statutory election on behalf of the pursuer which the pursuer had not wished to make and had not made. This court should not endorse a process which amounted to sliding from section 38(1) into section 42(1).

[22] In terms of section 4(2) of the Partnership Act 1890 a partnership is regarded in Scots law as capable of owning property and of holding rights and assuming obligations. The dissolution of a partnership has the consequence that its affairs must be wound up and its assets distributed in accordance with section 44 of the Act. When a partnership comes to an end it is the right but also the duty of the former and surviving partners to realise the assets for the purpose of winding up the partnership affairs, including the payment of debts: *Re*

Bourne [1906] 2 Ch 427 at 431. Sections 32 to 44 of the Act fall under the heading "Dissolution of partnership and its consequences". They should be considered together: *Duncan* v *The MFV Marigold PD145* 2006 SLT 975 at para [28]. It is section 38 which confers the right on former partners to intromit with the assets of the former partnership. That is accordingly the starting point. The section has two functions: (1) to allow the former partners to wind up the partnership's affairs and (2) to allow the former partners to complete transactions begun but unfinished at the time of dissolution: *Dickson* v *National Bank of Scotland* 1916 SC 589 at 594. In respect of that second function it is the right and the duty of surviving former partners to complete all unfinished operations necessary to fulfil contracts of the firm which were still in force when the firm was dissolved: *Inland Revenue* v *Graham's Trs* 1971 SC (HL) 1 at 20. As at the date of the dissolution of the partnership the DGNHS contract had some time to run; it was a transaction begun but unfinished. The defenders had authority by virtue of section 38 to take steps to complete it and they did so. The pursuer had brought an action for count reckoning and payment on the basis that section 38 applied. He had not sought to apply section 42(1). It does not apply. This is not a case of an "outgoing partner" and "continuing partners" and there are no findings-in-fact to suggest that it is. It is irrelevant to the pursuer's claim to share in the profits of the completion of the DGNHS contract that the pursuer himself took no part in doing so.

[23] The SAC had erred in substituting its judgment that the continuing provision of services under the DGNHS contract did not amount to the completion of an "unfinished transaction" for the findings-in-fact of the sheriff which were clearly to the effect that it did. The DGNHS contract was the whole business of the former partnership (leaving aside the dispensing pharmacy). It had to be wound up and that is what was done over the relevant

period. There are no findings-in-fact to support an alternative explanation of what was going on in that period.

[24] The DGNHS contract continued to be fulfilled by the defenders as former partners of the dissolved partnership for a period of 15 weeks as part of the winding-up process. The pursuer is entitled to a distribution of his share of the profits generated during that period. Section 42(1) does not apply to these circumstances.

Respondent

[25] On behalf of the defenders and respondents Mr McIlvride QC adopted the written note of argument for the defenders and respondents. In developing that argument Mr McIlvride identified two issues as arising in the appeal: (1) whether the sheriff and the SAC had erred in proceeding on the basis that when the former firm was dissolved the pursuer was capable of being treated as an outgoing partner and the defenders as continuing partners; and (2) more fundamentally, whether persons in the position of these parties following dissolution can be said to have been winding up the former firm in such a way that the pursuer retained his entitlement to share profits on the contractual basis or whether the sheriff and the SAC were well founded in holding that parties' positions were to be determined by section 42(1).

[26] The submission for the defenders was that the sheriff and the SAC had been correct in their respective judgments that section 42 of the 1890 Act applied to the calculation of the pursuer's entitlement to post dissolution profits in the particular factual circumstances of the present case. These circumstances included the facts that (1) the dissolution of the partnership was precipitated by the pursuer's own unacceptable conduct and (2) the pursuer made no attempt to perform any services under the DGNHS contract. The sheriff and the SAC had not considered that the defenders had been involved in a winding-up. It

was a question of fact what the defenders had been doing. The sheriff found, as he was entitled to do on the evidence, that the pursuer ceased to be a partner of the firm on its dissolution and that the defenders had carried on the business of the firm, namely the provision of medical services equivalent to those provided for under the DGNHS contract, for the period following the dissolution on 12 March 2014 until 30 June 2014. That finding is patently a circumstance in which section 42 applies to the calculation of post dissolution profit and the sheriff was correct to decide that this was so: cf *Hugh Stevenson and Sons Ltd* v *Aktiengesellschaftfür Carton-Nagen-Industrie* [1918] AC 239 at 248, where Lord Dunedin distinguished between the respective positions of the partner who went on working in the business of the dissolved firm and the partner who did not. In *Manley* v *Sartori* [1927] 1 Ch 157 at 164 Romer J observed that profits, so far as earned by sources outside the partnership assets are not profits in which the executors of a deceased partner could be entitled to share. The sheriff had been correct to apply that analysis to the circumstances of the present case. The defenders had made considerable efforts to continue with the provision of medical services under the DGNHS contract, something the pursuer had made no attempt to do. The only real asset of the partnership to which the pursuer could lay claim was his interest in the DGNHS contract but, of course, this bundle of rights and obligations can only be created by the endeavour of the medical practitioners providing these services. In applying section 42 the sheriff was determining a matter of fact which ought not to be interfered with. While it was accepted that the sheriff had made no formal finding that the defenders had continued to carry on the business of the former partnership, his finding-in-fact 15 should be read as limited to a determination that there had been no valid sub-contract in favour of the new partnership. Moreover it was the sheriff's clear finding in fact that the sole reason for the dissolution of the partnership and the consequent litigation was the unreasonable

conduct of the pursuer. It was he who made the continuation of the partnership untenable and thus placed upon the defenders the considerable burden of having to perform the DGNHS contract by themselves.

[27] Section 38 is not applicable to the calculation of the pursuer's share of profits. Its purpose is to enable former partners to wind up the affairs of a dissolved firm (see *Hopper* v *Hopper* [2008] EWCA Civ 1417 (otherwise unreported) at paras 45 to 49). To fall within the terms of section 38 it must be shown that the survival of authority, a right or an obligation was necessary in order to wind up the affairs of the partnership and to complete transactions begun but unfinished at the time of the dissolution. Assuming that the DGNHS contract was a transaction begun but unfinished at the time of the dissolution or that services had to be provided to wind up the partnership, it remained for the pursuer to establish that a right to an equal share of the profits made through the provision of these services was necessary, if such was to survive dissolution. The pursuer did not do so or attempt to do so.

[28] In so far as there was a divergence between the sheriff and the SAC, the defenders adopted the reasoning of the SAC which supported its conclusion that the DGNHS contract was not a transaction which was begun but unfinished or necessary for the winding up of the partnership. That was a conclusion on a matter of law, not a matter of fact. Moreover, it is to be noted that the DGNHS contract was terminated and therefore finished upon dissolution. Thereafter the Health Board required that the "individual partners" provide services until the earlier of 30 September 2014 and the date of a new contract arrangement being established.

[29] There had been no error in law on the part of the SAC in holding that the sheriff had not erred. The court should adhere to the sheriff's interlocutor.

Decision

[30] This is a claim by one former partner of a dissolved partnership as against the two other former partners to share in the net income generated by the activities of the two other former partners in a period of about 14 weeks immediately following the dissolution of the partnership. In the course of submissions Mr McIlvride came to identify the issue as turning on a question of fact: whether the activities of the two former partners were for the purpose of winding up the former partnership or whether they were for their personal benefit. We rather think that Mr McIlvride is right about that, but in order to give us a context for scrutiny of the findings-in-fact by the sheriff we propose to consider more generally what the law has to say about the rights and obligations of the partners in a partnership with no partnership agreement. In such a case these rights and obligations fall to be determined by the terms of the 1890 Act.

[31] In Scots law, "a firm is a legal person distinct from the partners of whom it is composed": 1890 Act section 4(2). It follows that, in general, a partnership is regarded in Scots law as being capable of owning property and of holding rights and assuming obligations (cf *Duncan* v *The MFV Marigold PD145* at para [14]). All rights and interests in property originally brought into the partnership stock or acquired, whether by purchase or otherwise, on account of the firm, or for the purposes and in the course of the partnership business are partnership property and must be held and applied by the partners exclusively for the purposes of the partnership: section 20.

[32] Among the ways in which a partnership can acquire property, rights and obligations, is by entering into contracts. Some contracts will confer rights and impose obligations on a partnership for a future tract of time. A contract or the benefit arising from a contract to

which the firm is party is a part of the partnership property: cf *Don King Productions Inc* v *Warren* [2000] Ch 291. Thus, from the perspective of the balance sheet, where a contract confers a right which creates an obligation owed to the partnership, then that obligation owed to it is an asset of the partnership and thus part of its incorporeal property. Where a contract imposes an obligation on a partnership then that obligation becomes one of the partnership's liabilities.

[33] During the subsistence of a partnership each partner has an interest in the partnership property and, in so far as they might not be comprehended by that expression, in the other rights, obligations, assets and liabilities of the firm. The nature of that interest is determined in the absence of agreement by the terms of the Act. Every partner is liable jointly and severally with the other partners for all the debts and obligations of the firm: section 9 and, just as all partners are entitled to share equally in the capital of the firm, so are they entitled to share equally in the profits of the business carried out by the firm and bound to contribute equally towards the losses: section 24, rule (1). A partner cannot take a private profit from any transaction concerning the partnership, or from any use by him of the partnership property, name or business connection. He must account to the firm for any benefit derived by him without the consent of the other partners: section 29(1).

[34] During the subsistence of the partnership among the parties in the present case the firm was a party to the DGNHS contract. The sums payable to the partnership under the DGNHS contract were therefore part of the partnership property of the firm in which the pursuer had a one third share. He was entitled to a one third share of the profits of the business and therefore in so far as the DGNHS contract contributed to these profits (as it did) the pursuer was entitled to a one third share of that contribution.

[35] The partnership among the pursuer and the defenders was dissolved by notice on 12 March 2014. Dissolution brings a partnership to an end; but only to an extent; "for certain purposes a partnership continues notwithstanding dissolution": *Dickson* v *National Bank of Scotland* 1917 SC (HL) 50 at 52 (see also the discussion by Lord Hunter sitting in the Land Valuation Appeal Court in *Inland Revenue* v *Graham's Trs* 1971 SC (HL) 1 at 4). In the course of submissions before us this was likened to the ghost of the former firm continuing to manifest its presence until it is finally laid to rest by the completion of winding up and the payment of the surplus assets to the former partners. For example, section 38 provides that after dissolution every partner (in the sense of former partner) has authority, albeit limited authority, "to bind the firm ". Again by virtue of section 38, "notwithstanding the dissolution", the "other rights and obligations" of the partners continue "so far as may be necessary to wind up the affairs of the partnership". In terms of section 39, the dissolved partnership is taken to have, on the one hand, property, and, on the other hand, debts and liabilities. Section 29 which requires a partner to account to the firm for any benefit derived by him from any transaction concerning the partnership, applies also to transactions undertaken after the dissolution of a partnership: section 29(2) (and not only where the dissolution is by reason of the death of a partner, as was noticed by Lord Reed in *Duncan* at para [44] under reference to *Pathirana* v *Pathirana* [1967] 1 AC 233). This was also the position in the pre-Act Scots common law as can be seen from Bell's Commentaries (7th edition of 1870) II p527:

> "Partnership subsists after dissolution for the purpose of winding up the concern. The partnership is dissolved in so far as the power of contracting new debts is concerned; but continued to the effect of levying the debts, paying the engagements of the company, and calling on the partners to answer the demands."

[36] It is only with the completion of a winding up that matters are finally concluded. That should be a priority. Ms Davie emphasised the duty of former parties to proceed to a winding up as soon as was practicable after dissolution ("with as little delay as possible" according to Clark *On Partnership* II p682, cited by Lord Reed in *Duncan* v *The MFV Marigold PD145* at para [20]). As Romer LJ (the first of that distinguished judicial dynasty) stated in *Re Bourne* [1906] 2 Ch 427 at 431:

> "When a partner dies and the partnership comes to an end, it is not only the right, but the duty, of the surviving partner to realise the assets for the purpose of winding up the partnership affairs, including the payment of the partnership debts."

In the same case Vaughan Williams LJ described the obligation to proceed to a winding up once the partnership is dissolved in this way, at 430:

> "…there is, as between the surviving partner and the representatives of the deceased partner, an overriding duty to wind up the partnership assets and to do such acts as are necessary for that purpose, and if it is necessary for the winding up either to continue the business or borrow money or to sell assets, whether these assets are real or personal, the right and the duty are co-extensive."

The immediate necessity for and the comprehensive nature of a winding up also emerge from an authority cited by Mr McIlvride, *Hugh Stevenson and Sons Ltd* v *Aktiengesellschaftfür Carton-Nagen-Industrie* where Viscount Haldane stated at 246:

> "In the absence of a special agreement to the contrary ...the rule is that on a dissolution of partnership all the property of the partnership shall be converted into money by sale, and that the proceeds of the sale, after discharging all the partnership debts and liabilities, shall be divided among the partners according to their shares."

[37] Among the matters which the parties in the present case had to address on dissolution of the former partnership with a view to its winding up was the DGNHS contract. The sheriff's findings-in-fact disclose very little about the nature and terms of the DGNHS contract, albeit from what was said both by Ms Davie and by Mr McIlvride during submissions it would appear that the parties' representatives knew quite a bit about it and

the correspondence from the Health Board concerning the contract which had followed the dissolution of the partnership. We accordingly take from the sheriff's silence on the detail of the contract that the parties did not consider it to be of any importance. What does appear from the findings-in-fact is that for the period between dissolution of the partnership and its supersession by a new arrangement, the DGNHS contract was considered by the sheriff to continue in force and, although the pursuer did not participate in this, the obligations which it imposed on the dissolved firm were discharged by the defenders as "former partners of the dissolved firm" (finding-in-fact 15).

[38] Thus far, we have no difficulty with the sheriff's analysis. As we have already observed, the 1890 Act contemplates the possibility of a dissolved partnership having (or being treated as if it had) rights and obligations. While it will depend on the nature and terms of the contract, a contract to which a partnership is party is not necessarily brought to an end by the dissolution of the firm (see Bell's Commentaries II p526; *Alexander* v *Lowson's Trs* (1890) 17 R 571; *Inland Revenue* v *Graham's Trs*, Lord Fraser in the Lands Valuation Appeal Court at 11, and Lord Reid and Lord Guest in the House of Lords at 20 and 24 respectively). As is explained by Miller *Partnership* (2nd edit) at p515:

> "The firm may also at the date of dissolution be under a continuing obligation in terms of contracts entered into prior to dissolution the effect of which extends beyond the date of dissolution ...The contracts entered into by the firm are not as a general rule affected by the subsequent dissolution"

and at p520:

> "If it can be shown that the contract was entered into prior to dissolution then the firm and its partners are bound by it and any partner has authority to act on behalf of the firm in the implement of the unfinished contract"

In the passage at p520 of Miller the author is commenting on the effect of section 38 of the 1890 Act. That section was discussed by Lord Reid when *Inland Revenue* v *Graham's Trs* was on appeal to the House of Lords. He said this, at 21:

> "... it is clear that surviving partners have no right to bind the assets of the dissolved firm by making new bargains or contracts. Their right and duty is to wind up its affairs. In my view this must mean that the surviving partners have the right and duty to complete all unfinished operations necessary to fulfil contracts of the firm which were still in force when the firm was dissolved. Otherwise the position would be intolerable. ... Where there is a contract with a firm, the work cannot be done by the fictional person, the firm: it must be done by one or other of the partners. So in most cases it would be quite unreasonable to say that the surviving partners cannot complete work which was unfinished when the firm was dissolved. Each case must depend on intention, express or implied. ...In my opinion, section 38 does not make the surviving partners parties to the firm's contracts and so keep those contracts alive. That would involve a radical change in Scots law. But I see no difficulty in holding that this section does require unfinished operations to be completed under the conditions which would have applied if the contract had still existed."

By this stage in his speech Lord Reid had considered and rejected the contention that the particular agricultural lease which was under consideration had not been brought to an end by the dissolution of the firm which was the tenant. The above passage is therefore to be understood as Lord Reid expressing the opinion that section 38 confers authority on former partners to complete unfinished operations even under those contracts which have been terminated by dissolution. If, as may be the case, a contract has not been so terminated it may be that the section 38 authority will be all the more necessary in order to achieve an advantageous winding up. As Lord Upjohn put it in *Graham's Trs* at 27:

> "...this section makes it plain the ex-partners will remain entitled and bound to carry out the contracts made in the name of the partnership and must complete all those contracts and other matters which are *in medio* when the partnership was a going concern."

[39] The SAC questioned whether continuing with the DGNHS contract was an instance of completing a transaction "begun but unfinished at the time of the dissolution" as that expression is used in section 38 but, given the sheriff's findings-in-fact 11 to 15 and the

absence of any further findings about the terms of the DGNHS contract or any negotiations that there may have been with the Health Board, it appears to us impossible to come to any other conclusion about what happened: the obligations of what had been a contract between the dissolved firm and the Health Board were discharged by two of the former partners "as partners of the dissolved firm". The authority of partners to act for the firm which is conferred by section 5 of the Act came to an end on the dissolution of the firm. That is what makes section 38 necessary: to confer an authority to bind the firm after dissolution, albeit only for limited purposes, these being to wind up the affairs of the partnership and to complete transactions begun but unfinished at the time of the dissolution (cf *Dickson* v *National Bank of Scotland* 1916 SC 589 at 594). The SAC asserts that the DGNHS was not an unfinished transaction and that its continuing performance was not necessary to achieve a winding up. That rather has the look of the SAC superimposing its own (inconsistent) findings-of-fact on those made by the sheriff. Given the sheriff's finding-in-fact 12, what was the DGNHS contract as at 13 March 2014 if it was not a transaction which had been begun but was unfinished? Further, while no doubt parties were principally concerned with achieving continuity in the provision of primary health care in the area, the still subsisting DGNHS contract gave rise to rights and obligations and consequently assets and liabilities which had to be realised or discharged and taken into account in the process of winding up the dissolved firm. How else could the defenders carry out "the services required of the partnership in terms of the DGNHS contract" (finding-in-fact 14) other than by virtue of section 38?

[40] Regard can also be had to the way the defenders responded to the pursuer's demand for an accounting, in their pleadings and in the accounts prepared on their behalf. As we have already mentioned, the position taken by the defenders in their pleadings was that

they "provided medical services in accordance with the provisions of the contract until 30 June 2014 when new contractual arrangements were established" and that "it was necessary for the partnership of the defenders to perform the obligations of the partnership in terms of the NHS contract". Thus, it was the position of the defenders that the DGNHS contract subsisted until superseded by "new contractual arrangements" on 30 June 2014. As "[it] was considered inappropriate by the defender and [the Health Board] for the [pursuer] to continue to work within the practice building", it was the new partnership, in which only the defenders were partners, which provided the medical services required under the subsisting DGNHS contract but the new partnership did so on behalf of the dissolved partnership. Effectively the new partnership acted as a sub-contractor to the dissolved partnership. The accounts make matters even clearer: the winding up accounts of the dissolved partnership show as income received the payments to which the dissolved partnership is entitled to under the DGNHS contract and as expenditure management charges paid to the new partnership. The purported sub-contract was accordingly the mechanism by which the defenders diverted the whole income from the DGNHS contract (divided into two components characterised respectively as "reimbursement of costs" and "reimbursement of partner salary") to the new partnership. However, once the sheriff found the sub-contract to be invalid because the defenders did not have authority to enter into it, it and the consequential entry in the dissolved partnership's accounts fell to be ignored (sheriff's note para 28). In striking what the pursuer says is the profit generated by the dissolved partnership during what he would regard as its winding up period, he allows "reimbursement of costs" as a deduction from income received. He does not allow "reimbursement of partner salary". The pursuer claims that that component, quantified at £60,000, falls to be shared as part of the profits of the dissolved partnership.

[41] In our opinion, given the sheriff's findings-in-fact and the accounts when read and understood in the context of the applicable law, the pursuer's claim is unanswerable. Prior to dissolution of the partnership, the pursuer was entitled to share in the profits of the DGNHS contract in the sense that he was entitled to share in the profits to which that contract contributed. Why, it might be asked, if that contract continued to generate profit for the firm after dissolution, should the pursuer not continue to be entitled to the same share of that profit?

[42] One answer which the sheriff might give to that question is found, succinctly stated in paragraph 30.3.1 of his note: "I had found that the pursuer did nothing towards the profits of the old partnership and that any entitlement fell to be determined in accordance with s. 42." Before the SAC it was apparently argued that:

> "it would set a bad precedent if the pursuer, who had done nothing to contribute to the continuing performance of the Health Board contract, could obtain the same share of profit as he would have obtained if the partnership had continued with him as a partner."

A difficulty about that approach is that, in the absence of agreement to the contrary, the entitlement of a partner to share in profits is not conditional or otherwise dependent on that partner doing anything in particular towards generating these profits. The remedy of a partner or partners who consider that the inactivity of a co-partner has thrown the burden of the conduct of the business on him or them is to seek a dissolution: *Macredie's Trs* v *Lamond* (1886) 24 SLR 114, Miller p 565. It is to be borne in mind that each partner is entitled to an accounting from his fellow partners as to all things affecting the partnership: section 28, and that such an accounting includes an accounting for any benefit from any transaction concerning the partnership or from any use of the partnership property: section 29. As we have pointed out, the DGNHS contract was partnership property. Equally, at least on the

face of section 24 rule (6) of the 1890 Act, in the absence of agreement, no partner shall be entitled to remuneration for acting in the partnership business. That said, as Miller notes at p 564, there is English authority for payment to a partner of "compensation" or "some proper allowance in respect of the expense and trouble to which he was put in conducting the winding up of this business": *Meyer & Co* v *Faber (No 2)* [1923] 2 Ch 421 at 451, also *Re Aldridge* [1894] 2 Ch 97. Romer J also makes reference to surviving partners having been made "a proper allowance ...for their trouble" in *Manley* v *Sartori* at 162. The English position is discussed in Lindley & Banks *On Partnership* (20th edit) at paras 20-43 *et seq* under reference to, among other cases, *Popat* v *Shonchhatra* [1995] 1 WLR 908, David Neuberger QC sitting as a Deputy High Court Judge at 913H and *Emerson* v *Estate of Emerson* [2004] 1 BCLC 575. As can be seen from these authorities, in England a claim by a former partner for "compensation" may be allowed in respect of his expenditure of time and trouble, as well as outlays, in the course of a winding up. According to Chadwick LJ giving the judgment of the Court of Appeal in *Emerson* v *Estate of Emerson* at para [15] the underlying principle is that found in the speech of Lord Templeman in *Carver* v *Duncan* [1985] AC 1082 at 1120:

> "Trustees are entitled to be indemnified out of the capital and income of their trust fund against all obligations incurred by the trustees in the due performance of their duties and the due exercise of their powers."

As for Scotland, we note that "reasonable remuneration" was also allowed in the pre-Act case of *Berry* v *Lamb* (1832) 10 S 792, to which reference had been made before the SAC. In *Macredie's Trs* v *Lamond* a claim was made for "such allowances in their accounts with the firm as may be just, by way of compensation to them for [the] deceased's failure to perform his part under the contract, and for their being compelled to take full charge and management of the business without his assistance". The claim failed but it had been made in respect of a period prior to the dissolution of the partnership when one partner was

disabled by illness from attending to business. It does not follow from the decision in *Macredie's Trs* that a claim for compensation for time and trouble expended for the benefit of the dissolved partnership is necessarily not available in Scotland. Partnership property is held on trust and accordingly subject to fiduciary duties. To the extent that one or more of the former partners carry out work for the dissolved partnership, that is done by persons in the position of trustees in order to make proper use of trust property. There is at least scope for argument that, even in the absence of agreement, a fair settlement of accounts as between former partners who have been active in the winding up and the dissolved partnership (and therefore any former partner who has not been active) should reflect an element of compensation or indemnity for work done. However, this is not a matter which we need consider further. We heard no submissions in relation to such an approach. No claim for such compensation or allowance or indemnity was made to or allowed by the sheriff beyond the cost of a locum to assist the defenders, which cost the sheriff allowed as an outlay and which is not challenged. It is only the profit element in the defenders' charges, represented by the management charge, which is put in issue by the pursuer (and not reimbursement of costs). That claim, for a share of profit, in the opinion of the sheriff and the SAC, is closed off by the terms of section 42.

[43] A different result might of course have been produced if the sheriff, in applying section 42, had recognised that the DGNHS contract and therefore the profits produced by it were assets of the firm, but in our opinion, agreeing with the submission for the pursuer, on the facts found by the sheriff, this was not a case for applying section 42.

[44] The current edition of Lindley & Banks is the twentieth. In earlier editions the application of section 42 was discussed as an aspect of the more general question: if a person trades with property which does not belong to him, what are the rights of the owner against

him in respect of the profit he has made? That analysis has not been retained by the current author (Lindley & Banks para 25-24) but it is useful in providing a context for the nature of the problem that section 42 is intended to address. That it merits a particular provision in the 1890 Act may reflect the fact that the situation of trading with another person's property will commonly arise on dissolution of a partnership in that former partners will be likely to have control over what is the property of a dissolved partnership and will, for entirely good reasons, wish to continue trading in what effectively is a continuation of the business of the dissolved firm but is nevertheless a distinct (and new) concern. However, for a situation which section 42 is intended to address to arise it must be possible to distinguish between an "outgoing partner" and "continuing partners" and it is to be borne in mind that it is the profits made since the dissolution by the business carried out by the continuing partners in which the outgoing partner is entitled to share by virtue of the section. Section 42 has no application to profits of a dissolved firm which happen to be generated as part of an active process of winding up. We understood Mr McIlvride to accept that. Section 42 is designed to address the situation where a new concern has commenced business on its own account, albeit that the business is a continuation of the business of the former firm and is carried on by some or other of the former partners.

[45] The matter was explained by Etherton LJ when giving the opinion of the Court of Appeal in a case cited by Mr McIlvride and, as we understood it, commended by him to us, *Hopper* v *Hopper* at paras 45 to 49:

> "45 The meaning and operation of s. 42 must be seen in the context of the overall legal framework of dissolution of a partnership. ... The 1890 Act was not, and was never intended to be, a complete code of partnership law or a precise legislative enactment of existing case law and legal and equitable principles. On the other hand, it is clear that much of the Act, and in particular the statutory provisions relevant to this part of the appeal, broadly reflect the pre-existing law.

...

46 A partnership at will is dissolved as regards all the partners by the death of any partner: 1890 Act s. 33. Prior to that dissolution, every partner is an agent of the partnership and of the other partners for the purpose of the business of the partnership: 1890 Act s. 5. On dissolution of the partnership, the authority of each partner to bind the partnership, and the other rights and obligations of the partners, continue only so far as is necessary to wind up the affairs of the partnership and to complete transactions begun but unfinished at the time of dissolution: 1890 Act s. 38. Save to that extent the partnership contract is at an end. In the absence of agreement to the contrary by all the surviving partners and by the personal representatives of the deceased partner, nothing is to be done with regard to the business save with a view to winding it up and, for that purpose, realising the value of all the assets, by sale if necessary, and applying the assets in payment of the partnership's debts, and paying the surplus to the partners and the personal representatives of the deceased partner in accordance with the provisions of the 1890 Act s. 44.

47 When a partnership at will is dissolved by the death of a partner, the surviving partner or partners, and the personal representatives of the deceased partner, may all agree, solely for the purpose of the winding up, to continue the business of the former partnership in order best to maximise the value of its business and goodwill on sale or other realisation. If they do all so agree, their rights and obligations, including their shares of any profit from the continued trading, and the authority of each former partner to bind the others continue as before: 1890 Act s. 38.

...

48 Section 42 governs what happens in relation to post-dissolution profits if (1) the business of the former partnership is continued by one or more of the former partners, not for the purposes of winding up the former partnership, but for the personal benefit of those continuing to run the business, and (2) those persons do not include all the former partners and the personal representatives of the deceased partner, but (3) there are retained within the continuing business all or part of the shares of the assets of the former partnership to which those non-participants in the continuing business were entitled (in their personal capacity or as personal representatives) on dissolution of the former partnership. In summary, this is a familiar situation, well covered by the cases and equitable principles which applied both before and after enactment of the 1890 Act, where one person's property is employed in the business of another, who may or may not be in breach of trust in retaining that property, and the question arises what rights the owner of that property has in respect of profits of the business: see Lindley on Partnership (15th ed) pp. 719-723.

49 Against that background, the meaning and effect of s. 42 are clear. All such non-participant former partners are “outgoing partners”; and they and the estate of the deceased partner are entitled, in the absence of agreement to the contrary, to such share of the profits made since the dissolution as the Court may find to be

> attributable to the use of their shares of the partnership assets or, at their option, to five per cent per annum on the amount of their shares. ..."

[46] Now in the present case it may be said that the pursuer was excluded or excluded himself from active participation in the winding up over the period 13 March to 30 June 2014. Whatever the rights and wrongs about that may be (and the sheriff found the pursuer to be in the wrong) does not appear to us to matter. What was going on in that period could be said to be a continuation of the business of the dissolved firm but it was by the dissolved firm for the only purpose which was available to the dissolved firm, that is the purpose of winding up. A profit was made. As a former partner of the dissolved firm the pursuer was entitled to a share of the profit attributable to the dissolved firm. Section 42, which allows sharing in the profit of a concern which is distinct from the dissolved firm, has no application to the pursuer's claim.

[47] We shall accordingly allow the appeal. We shall recall the interlocutors appealed against and grant decree for payment by the defenders to the pursuer of the sum of £35,949 with interest thereon at the rate 8 per cent per annum from 2 February 2015 until payment. We shall reserve all questions of expenses.