Neutral Citation Number: [2016] EWHC 2418 (Ch)

Case No: HC-2015-004901

IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION

IN THE MATTER OF AN ARBITRATION
AND IN THE MATTER OF THE ARBITRATION ACT 1996

Rolls Building, Royal Courts of Justice
7 Rolls Buildings, Fetter Lane
London, EC4A 1NL

Date: 05/10/2016

Before :

MR JUSTICE NEWEY

- -

Between :

JEREMY HOSKING	**Claimant**
- and -	
MARATHON ASSET MANAGEMENT LLP	**Defendant**

- -
- -

Mr Pushpinder Saini QC, Mr John Machell QC, Miss Victoria Windle and Mr Paul Luckhurst (instructed by **Orrick, Herrington & Sutcliffe (Europe) LLP**) for the **Claimant**
Mr Neil Kitchener QC, Miss Jane McCafferty and Mr Gideon Cohen (instructed by **Herbert Smith Freehills LLP**) for the **Defendant**

Hearing date: 21 July 2016

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Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

....

Mr Justice Newey :

1. It is well-established that there are circumstances in which a fiduciary (in particular, an agent) who acts in breach of his fiduciary duties can lose his right to remuneration. The question raised by this appeal from an arbitration award is whether that principle is capable of applying to profit share of a partner in a partnership or a member of a limited liability partnership ("LLP").

The context

2. The defendant, Marathon Asset Management LLP ("Marathon"), carries on an investment management business originally set up in 1986 by the claimant, Mr Jeremy Hosking, and a Mr Neil Ostrer. Marathon took over the business in 2004, at which stage Marathon and its members entered into a deed dated 2 September 2004 ("the LLP Deed") to "set out the basis on which the LLP is to be organised and the rights and duties of the LLP and its Members" (to quote from a recital). Mr Hosking, Mr Ostrer and the two other original members were called the "Founding Members". The three Founding Members who are individuals were also designated "Class A Members", a term defined so as to encompass as well "any other person who is admitted to membership of the LLP as a Class A Member".

3. The LLP Deed provides for Class A Members to be either "Executive Members" or "Non-Executive Members". A Non-Executive Member is a Founder Member who no longer works in the business of Marathon by reason of death, incapacity, "retirement from executive duties" or a resolution of other Members. All other Class A Members are Executive Members and, as such, required to "diligently employ [themselves] in the business" of Marathon and, except as otherwise agreed, to devote all their time to that business.

4. Under the terms of the LLP Deed, profits falling to be allocated to Class A Members are to be shared amongst them equally, save that:

> "the Non-Executive Member(s) (or their personal representatives) shall … each be allocated 50 per cent. of the Income Profits for that Quarter as would have been allocated to the relevant Non-Executive Member(s) … had the relevant Non-Executive Member(s) been an Executive Member(s) during the relevant Quarter".

   In other words, a Non-Executive Member is to receive half as much as an Executive Member. The entitlement of an Executive Member is referred to informally within Marathon as "full rations" and that of a Non-Executive Member as "half rations".

5. On 5 April 2012, Mr Hosking gave notice of his intention to retire. His retirement took effect on 11 December 2012. He then became a Non-Executive Member of Marathon.

6. That same month, Marathon initiated arbitration proceedings against Mr Hosking. Issues as to liability were addressed during a hearing in 2014, following which the arbitrator, Mr David Owen QC ("the Arbitrator"), made an award dated 1 October 2014 ("the Liability Award"). While rejecting quite a number of allegations against

Mr Hosking, he found some to have been proved. More specifically, he held that Mr Hosking had breached contractual and fiduciary duties that he had owed to Marathon by discussing with four of its employees the possibility of starting a new business and producing a business plan outlining his thoughts. He also concluded that, as a result of Mr Hosking's breaches of duty, Marathon had lost a real or substantial chance of retaining three individuals referred to as "the Global Three", with the lost chance of retention being put at 5%.

7. Remedies were dealt with at a further hearing in 2015 and were the subject of an award dated 30 October 2015 ("the Remedies Award"). The Arbitrator concluded that Marathon was entitled to equitable compensation of some £1.38 million in respect of the lost chance of keeping the Global Three. He also, more importantly for present purposes, acceded to an argument that Mr Hosking should forfeit certain sums paid to him during the period of his breaches of duty. In that respect, he decided that Mr Hosking should return £10,389,957.50 to Marathon. This figure represented 50% of the "full rations" payments that Mr Hosking received in respect of the period between mid-July and mid-December 2012.

8. The Arbitrator took the view, as he said in paragraph 270(a) of the Remedies Award, that "50% of the relevant payments received by Executive Members was, in substance, remuneration for the performance of executive duties". In this connection, he said this in paragraph 260 of the Remedies Award:

> "a. It is correct that an Executive Member receives an allocation of Income Profits which is not described in the LLP Deed as remuneration for the performance of executive duties.
>
> b. However, one has to consider what, as a matter of substance, the allocation represents. If one asks oneself why, objectively, the Executive Member is receiving twice the allocation of profits that the retired Non-Executive Member receives, the answer is obvious. The Executive Member is carrying out, and is bound by, a range of duties, including fiduciary duties, and is correspondingly remunerated by an allocation of profit which is double the allocation which would be received by a Non-Executive Member who is not bound by the relevant duties. In short, the Executive Member receives an enhanced share of profit in return for undertaking the executive duties. The retired Non Executive Member no longer performs executive duties, and receives a lesser share, reflecting his past contribution to, and an ownership interest in, the business. No other reason was suggested for the difference in allocation of profit as between an Executive Member and a Non-Executive Member."

9. The Arbitrator considered whether forfeiture would be "proportionate and equitable" and decided that it would, noting, among other things, that "one is dealing with a series of serious breaches of fiduciary duty" (paragraph 265 of the Remedies Award).

He recognised that the amount sought to be forfeited was large, but observed that it had to be placed in the context of the scale of profits generated by the Marathon business (some £146 million in the year ending March 2012) (see paragraph 271 of the Remedies Award and paragraph 49 of the Liability Award). He further explained (in paragraph 271 of the Remedies Award):

> "Marathon accepts that forfeiture will not lead to Mr Hosking losing his entitlement to a half share of any relevant Income Profit by way of 'half-rations'. Therefore Mr Hosking will have the benefit of 'half-rations' equivalent to the amount forfeited in any event, reflecting his ownership interest. In so far as forfeiture increases profits available for distribution in the future, he will also receive the benefit of that distribution, by means of his ongoing 'half-rations' entitlement."

10. It was submitted to the Arbitrator on behalf of Mr Hosking "that forfeiture has no application to partnership profits, the distribution of which is always a matter of contractual bargain, and that the remedy which Marathon seeks is inconsistent with the provisions of the LLP Deed governing the partnership" (paragraph 244 of the Remedies Award). However, the Arbitrator stated in paragraph 260(g) of the Remedies Award that he had:

> "concluded that forfeiture of a 50% share of Income Profits, distinct from the 50% share received by way of 'half rations', is not inconsistent with, or excluded by, the terms and structure of the LLP Deed".

The forfeiture principle

11. The law relating to forfeiture of a fiduciary's remuneration is summarised in these terms in Snell's Equity, 33rd ed., at paragraph 7-062:

> "If a fiduciary acts dishonestly he will forfeit his right to fees paid or payable by the principal (as distinct from sums paid by a third party, such as a briber). He will also forfeit his right to such fees if he takes a secret profit from a third party which is directly related to performance of the duties in respect of which the fees were payable by the principal, even if the principal has benefited from the fiduciary's performance of those duties. However, a fiduciary's fees may not be forfeit if the betrayal of trust has not been in respect of the entire subject matter of the fiduciary relationship and where forfeiture would be disproportionate and inequitable.
>
> A fiduciary will also lose his or her right to fees payable by the principal if the fiduciary's breach of duty is so grave that there has effectively been no performance at all, on the basis of total failure of consideration."

12. The earliest forfeiture case to which I was referred was *Andrews v Ramsay & Co* [1903] 2 KB 635, which concerned an estate agent. Lord Alverstone CJ there said (at 638):

> "A principal is entitled to have an honest agent, and it is only the honest agent who is entitled to commission."

13. In contrast, estate agents who had failed to pass on an offer to a client were held not to have lost their right to commission in *Keppel v Wheeler* [1927] 1 KB 577. At 592, Atkin LJ said:

> "Now I am quite clear that if an agent in the course of his employment has been proved to be guilty of some breach of fiduciary duty, in practically every case he would forfeit any right to remuneration at all. That seems to me to be well established. On the other hand, there may well be breaches of duty which do not go to the whole contract, and which would not prevent the agent from recovering his remuneration; and as in this case it is found that the agents acted in good faith, and as the transaction was completed and the appellant has had the benefit of it, he must pay the commission".

14. The forfeiture principle was reaffirmed and explained by the Court of Appeal in *Imageview Management Ltd v Jack* [2009] EWCA Civ 63, [2009] Bus LR 1034. In that case, a footballer's agent had made a secret side deal with a club when negotiating for his client. He was held to have forfeited his commission. Jacob LJ (with whom Mummery and Dyson LJJ agreed) said (in paragraph 44):

> "I accept [counsel for the agent's] submission that there can be cases of harmless collaterality. And that there can be cases where there is just an honest breach of contract such as *Keppel's* case [1927] 1 KB 577. But this is simply not such a case. This is a case of a secret profit obtained because Mr Berry/Imageview was Mr Jack's agent. And there was a breach of a fiduciary duty because of a real conflict of interest. That in itself would be enough, but there is more: the profit was not only greater than the work done but was related to the very contract which was being negotiated for Mr Jack. Once a conflict of interest is shown, as Atkin LJ said in the last passage quoted, the right to remuneration goes".

Jacob LJ explained the policy behind the rule in paragraph 50:

> "The policy reason runs as follows. We are here concerned not with merely damages such as those for a tort or breach of contract but with what the remedy should be when the agent has betrayed the trust reposed in him – notions of equity and conscience are brought into play. Necessarily such a betrayal may not come to light. If all the agent has to pay if and when he is found out are damages the temptation to betray the trust reposed in him is all the greater. So the strict rule is there as a

> real deterrent to betrayal. As Scrutton LJ said in *Rhodes's* case 29 Com Cas 19, 28, 'The more that principle is enforced, the better for the honesty of commercial transactions'".

15. *Imageview* has been cited in, among other cases, *Bank of Ireland v Jaffery* [2012] EWHC 1377 (Ch) (where Vos J concluded that forfeiture would be disproportionate and inequitable) and *Avrahami v Biran* [2013] EWHC 1776 (Ch) (where I held that management fees had been forfeited).

16. Commission was also held to have been forfeited in *Stevens v Premium Real Estate Ltd* [2009] NZSC 15, [2009] 2 NZLR 384, which concerned estate agents. The judgment given by three judges in the Supreme Court of New Zealand (Blanchard, McGrath and Gault JJ) included this passage (at paragraph 90):

> "The remuneration is forfeited because it has not been earned by good faith performance in relation to a completed transaction. There is no inconsistency in awarding the principal both damages and the refund of the commission, as there would be, for instance, if a court were to order a defendant fiduciary both to pay damages and to account for profits made by the use of the principal's asset. Remuneration for services is not a profit of this kind. It is something to which an agent has no entitlement once he or she has committed a breach of fiduciary duty save in the circumstances described by Atkin LJ [in *Keppel v Wheeler*]".

The issue

17. Section 69 of the Arbitration Act 1996 provides for appeals from arbitration awards to be brought with the agreement of the other parties or the leave of the Court on points of law. In the present case, the question of law that was identified for determination and on which Mr Hosking sought and obtained permission to appeal was this:

> "Whether the share of profits of a partner of a partnership or a member of an LLP, paid out pursuant to and in accordance with a partnership or LLP deed, can be subject to the principle of forfeiture on the basis of the partner's/member's breach of fiduciary duties".

The parties' cases in brief outline

18. Mr Hosking's case is that the forfeiture principle has no application in relation to the share of profits of a partner or member of an LLP. Mr Pushpinder Saini QC, who appeared for Mr Hosking with Miss Victoria Windle and Mr Paul Luckhurst, pointed out that it cannot be assumed from the fact that a rule applies to one species of agent that it is also applicable to another: the obligations of a fiduciary and their incidents depend on the particular context. With partnerships and LLPs, there is (so it is said) a conceptual difference between profit share and remuneration. According to Mr Saini, "remuneration" refers to money payable in exchange for services as an expense prior to the division of profits and irrespective of the profitability of the firm, while the profit share of a partner or member reflects his status as a partner or member and his

ownership interest. Mr Saini submitted that a profit share does not lose its character as such and become remuneration merely because the partner or member is required to provide his services: the profit share remains payable to the partner or member as a partner or member, and in consequence of his interest in the partnership or LLP, and not as remuneration for his services, even if from a commercial point of view it also compensates the partner or member for his services. That view, it is argued, is supported by the case law and textbooks as well as the fact that there is no reference to forfeiture in the Partnership Act 1890, the Limited Liability Partnerships Act 2000 or the Limited Liability Partnership Regulations 2001. On the facts of the present case, moreover, no provision for forfeiture is to be found in the LLP Deed and, that being so, allowing forfeiture would (on Mr Hosking's case) be inconsistent with and distort the commercial bargain between the parties.

19. In contrast, it is Marathon's case that the Arbitrator was right to take the view that profit share can be forfeited. Mr Neil Kitchener QC, who appeared for Marathon with Mr Gideon Cohen, argued that any payment made to a partner in a partnership or a member of an LLP in return for services represents remuneration and is potentially susceptible to forfeiture. Mr Kitchener maintained that, as a matter of language, profit share payable for undertaking specific duties can appropriately be described as "remuneration" and that it would make no sense to exclude rewards from the forfeiture principle just because they happened to be conferred by way of profit share. To do so, Mr Kitchener said, would involve preferring form to substance, which would be inconsistent with the basis of the forfeiture principle. Further, the relevant legislation does not purport to define the rights and duties of partners or members of LLPs comprehensively and there is no authority that says either that partners and members of LLPs are to be treated differently in this respect from other fiduciaries or that it matters whether a payment for services is made by way of profit share. It is, on Marathon's case, consistent with principle that, where profit share of a partner or a member of an LLP can be identified as attributable to the provision of services, it should be liable to forfeiture, and that is said to chime with the "no profit" rule (as to which, see e.g. *Chan v Zacharia* (1984) 154 CLR 178, at 199); any potential for unfairness is removed by the requirement that forfeiture should not be disproportionate or inequitable. Finally, the fact that there may be no provision in the contractual documentation for forfeiture is, it is suggested, unimportant since the forfeiture rule overrides the ordinary operation of contractual entitlements to remuneration.

Materials

20. The parties sought support for their submissions in legislation and legal principles relating to partnerships and LLPs, in textbooks and in case law. I refer to some of these below.

Partnerships

21. As its long title indicates, the Partnership Act 1890 ("the 1890 Act") was designed to "declare and amend the Law of Partnership". It does not, however, represent a complete codification of partnership law (see Lindley & Banks on Partnership, 19th ed., at paragraph 1-05) and section 46 expressly provides for the "rules of equity and of common law applicable to partnership" to "continue in force except so far as they are inconsistent with the express provisions of this Act".

22. Section 24 of the 1890 Act contains rules by which the interests of partners in the partnership property and their rights and duties in relation to the partnership are to be determined, subject to "any agreement express or implied between the partners". The rules provide for partners to share equally in the capital and "profits" of the business (section 24(1)), for every partner to be able to take part in the management of the business (section 24(5)) and for no partner to be entitled to "remuneration" for acting in the partnership business (section 24(6)). A partner who derives a private profit must account for it to the "firm", a term which refers to all the partners (see sections 29 and 4 of the 1890 Act).

23. Mr Saini pointed out that the 1890 Act makes no reference to the possibility of forfeiture. Against that, the Act does not purport to contain all of partnership law and specifically preserves "rules of equity and of common law applicable to partnership".

24. Mr Saini also argued that section 24 of the 1890 Act distinguishes between "profits" and "remuneration". On the other hand, section 2(3) of the 1890 Act can be said to recognise that a share of profits can be appropriately termed "remuneration". Section 2(3)(b) states that a contract for the "remuneration" of a servant or agent of a person engaged in a business by a "share of the profits of the business" does not of itself make the servant or agent a partner in the business.

25. Partners are considered to owe fiduciary duties to each other. In *Helmore v Smith (1)* (1886) 35 Ch D 436, Bacon V-C said (at 444):

> "If fiduciary relation means anything I cannot conceive a stronger case of fiduciary relation than that which exists between partners. Their mutual confidence is the life blood of the concern. It is because they trust one another that they are partners in the first instance; it is because they continue to trust one another that the business goes on."

26. In *Cassels v Stewart* (1881) 6 App Cas 64, Lord Blackburn expressed the view (at 79) that "it is because [a partner] is an agent that the fiduciary character arises". The fact that a partner is an agent for the firm was also recognised in, for example, *Dunne v English* (1874) 18 Eq 524, where Jessel MR said of a partner (at 532):

> "The Defendant was not only in law the agent of the partnership to sell (being himself a partner, and every partner being an agent of the partnership), but he was in fact the agent who had been engaged in negotiating the sale."

LLPs

27. LLPs were introduced by the Limited Liability Partnerships Act 2000 ("the 2000 Act"). An LLP, unlike a partnership, has legal personality separate from its members (see section 1 of the 2000 Act). The rights and duties of the LLP and its members are governed by agreement or, in default, the provisions of the Limited Liability Partnerships Regulations 2001 (see section 5 of the 2000 Act). Regulation 7 of those Regulations contains provisions that closely correspond to the parts of the 1890 Act mentioned in paragraph 22 above. Thus, subject to the general law and the terms of any LLP agreement, the rights and duties of LLPs and their members are to be

determined by rules providing for members to share equally in the capital and "profits" of the LLP (regulation 7(1)), for every member to be able to take part in the management of the LLP (regulation 7(3)), for no member to be entitled to "remuneration" for acting in the business or management of the LLP (regulation 7(4)) and for a member who derives a private profit to account for it to the LLP (see regulation 7(10)).

28. "Every member of a limited liability partnership is the agent of the limited liability partnership" (section 6(1) of the 2000 Act). As was noted by Sales J in *F & C Alternative Investments (Holdings) Ltd v Barthelemy (No 2)* [2011] EWHC 1731 (Ch), [2012] Ch 613 (at paragraph 219), "there is nothing in the Act to qualify the usual fiduciary obligations which an agent owes his principal in relation to the transactions which the agent enters into on the principal's behalf".

29. When considering the content of the fiduciary obligations owed by, among others, the members of an LLP board in the *F & C* case, Sales J observed (at paragraph 223):

> "Fiduciary obligations may arise in a wide range of business relationships, where a substantial degree of control over the property or affairs of one person is given to another person. Very often, of course, a contract may lie at the heart of such a business relationship, and then a question arises about the way in which fiduciary obligations may be imposed alongside the obligations spelled out in the contract. In making their contract, the parties will have bargained for a distribution of risk and for the main standards of conduct to be applied between them. In commercial contexts, care has to be taken in identifying any fiduciary obligations which may arise that the court does not distort the bargain made by the parties: see the observation by Lord Neuberger of Abbotsbury writing extrajudicially in 'The Stuffing of Minerva's Owl? Taxonomy and Taxidermy in Equity' [2009] CLJ 537, 543 and *Vercoe v Rutland Fund Management Ltd* [2010] EWHC 424 (Ch) at [351]–[352]. The touchstone is to ask what obligations of a fiduciary character may reasonably be expected to apply in the particular context, where the contract between the parties will usually provide the major part of the contextual framework in which that question arises."

Sales J went on (at paragraph 225) to quote a passage from Lord Walker's judgment in *Hilton v Barker Booth & Eastwood* [2005] 1 WLR 567, in which the latter said (at paragraph 30) of obligations of a fiduciary type that:

> "they may have to be moulded and informed by the terms of the contractual relationship".

30. As Warren J pointed out in *Reinhard v Ondra LLP* [2015] EWHC 26 (Ch) (at paragraph 57, quoting Whittaker and Machell, "The Law of Limited Liability Partnership", 3rd ed., at 8–18):

> "the 'share' of a member [of an LLP] is the totality of the contractual or statutory rights and obligations of that member which attach to his membership".

Echoing Warren J, in *Flanagan v Liontrust Investment Partners LLP* [2015] EWHC 2171 (Ch), [2015] Bus LR 1172 Henderson J said (at paragraph 59):

> "Although it makes good sense in many contexts to talk of the 'share' or 'interest' of a member in an LLP, and these terms are used in various places in the relevant primary and secondary legislation, they are nowhere defined. I respectfully agree with the observations on this topic of Warren J in *Reinhard's* case [2015] EWHC 26 (Ch) at [55]-[57], where he said that the rights carried by such a 'share' can only be ascertained by reference to the agreements referred to in section 5(1) of [the Limited Liability Partnerships Act] 2000 and the default provisions in the [Limited Liability Partnerships] Regulations 2001."

31. The current (4th) edition of Whittaker and Machell, "The Law of Limited Liability Partnerships", states (at paragraph 11.33) that:

> "an LLP can have a member who, or a class of members that, is entitled to employment-like rights, such as a right to remuneration".

Textbooks on the forfeiture principle

32. The partnership textbooks to which I was taken do not refer to the possibility of forfeiture. By way of example, Lindley & Banks on Partnership states (at paragraph 21-08):

> "Just as partners have no inherent right to expel one of their number or to forfeit his share, they cannot properly exclude him from the enjoyment of his share of profits, unless this is expressly authorised by the partnership agreement."

33. It is also, however, fair to say that the partnership textbooks neither say that partnerships and LLPs are immune from the forfeiture principle nor endorse the distinction Mr Saini draws between profit share and remuneration. Further, Snell's Equity speaks simply of a "fiduciary" forfeiting fees without distinguishing between types of fiduciary.

Case law

34. In *Dunne v English* (1874) 18 Eq 524, a partner had made a secret profit from the sale of partnership property. The other partner sought and obtained relief "substantially in accordance with the first and second paragraphs of the prayer of the bill" (see 539), which had sought "a declaration … that the Plaintiff was entitled to share equally with the Defendant in the profits … and that the Defendant was bound to make over to the Plaintiff one half of the profits …" (see 527).

35. Mr Saini observed that there was no question of the defaulting partner not being permitted to retain the other half of the profits. The case, he suggested, implicitly proceeds on the assumption that the forfeiture rule does not apply to partnership profits. However, there does not appear to have been any claim or argument that the defaulting partner should not receive half of the profits.

36. In *Olson v Gullo* (1994) 17 OR (3d) 790, a decision of the Court of Appeal for Ontario, a Mr Olson and a Mr Gullo had formed a partnership to develop a tract of land. Mr Gullo nevertheless bought and sold part of the land for his own account at a substantial profit which he planned to pocket. The trial judge held that Mr Olson was entitled to recover the whole of the profit, but the Court of Appeal allowed an appeal. Morden ACJO, giving the judgment of the Court, said (at 796) that he had "concluded … that it was contrary to principle and authority … to deprive the defendants of their one-half share in the transaction in question". He explained (at 798):

> "We must, however, begin our consideration with the basic premise that the profit in question is the property of the partnership, not of all the partners except the defaulting partner. To exclude the wrongdoer would be to effect a forfeiture of his or her interest in this partnership property. The point may be understood by considering a starker form of wrongdoing – a case where a partner misappropriates partnership funds for his own benefit. In such a case I am not aware of any principle or decision to the effect that not only must the partner account to the partnership for the money but must also suffer a forfeiture of his or her interest in it. In fact, the case law of which I am aware is to the contrary."

37. Mr Saini noted that *Olson v Gullo* has been cited both in textbooks and by the Law Commission (see the 1983 Joint Consultation Paper on Partnership Law, at paragraph 14.7). Further, the Manitoba Court of Appeal followed *Olson v Gullo* in *MacDonald Estate v Martin* [1994] MJ No 398. The Court said (at paragraph 120):

> "Mr Martin [i.e. the defendant] has been rightly criticised for breach of fiduciary duty to Mr MacDonald and the estate …. But there was nothing the least bit unfair about an agreement between the two partners to invest on an equal basis in Westeel shares. In our opinion, that agreement should be honoured. Mr MacDonald never sought or expected anything more than equality on the Westeel venture. Under those circumstances we do not think that it is right to allocate the lion's share of the investment to Mr MacDonald by ignoring the agreement and exercising a discretionary power to do equity."

38. Mr Saini argued that, if the law does not deprive a partner who wrongfully makes a secret profit of any interest in that profit, there can be no legal basis for denying a defaulting partner an interest in profits which are unrelated to his wrongdoing. On the other hand, Mr Kitchener pointed out that (a) *Olson v Gullo* is not referred to in the textbooks on which Mr Saini relied in the context of any discussion about the applicability of the forfeiture principle and (b) the case did not involve any agreement

for profit share to be paid as remuneration for work that the defaulting partner was obliged to perform.

39. *Erikson v Carr* (1945) 46 SR (NSW) 9, a New South Wales case, is perhaps more obviously helpful to Mr Saini. There, an individual was alleged to have disentitled himself to commission as a result of a breach of duty. The Court thought it obvious that the legal rights of the parties would depend on the jury's conclusions as to, among other things, "whether it was partnership or agency" (see 15). Earlier in his judgment, Jordan CJ had observed that "if a partner in a subsisting partnership finds that his co-partner has made a secret profit for which he is accountable to the firm, this does not entitle him to rescind the partnership *ab initio*" but "to require the amount to be brought into the partnership account so that he may receive his proper share of it", while "[i]f a person, acting as agent under a subsisting contract of commission agency, accepts a secret commission in relation to an agency transaction, he must account for it to his principal" and "[o]rdinarily he also forfeits his right to commission" (see 14).

40. Mr Saini contended that *Erikson v Carr* shows the importance of the distinction between agency and partnership. Mr Kitchener, however, submitted that the case did no more than reflect a Court's assumptions in New South Wales in 1945 as to what remedies might be expected to be available as regards partnership and agency.

41. For his part, Mr Kitchener took me to *M Young Legal Associates Ltd v Zahid* [2006] EWCA Civ 613, [2006] 1 WLR 2562, where it was held that a person could be a partner even where the agreement was "not that he should be entitled to participate in [the firm's] profits but that he should be paid by the firm a specified sum, irrespective of profits, for work to be done by him on its behalf" (see paragraphs 1 and 38). Hughes LJ said (at paragraph 41):

> "the partners are free under the [1890] Act to arrange for the remuneration of themselves in any manner they choose, including by agreement that one or more shall receive specific sums, or that one or more receive nothing, in either case irrespective of profits".

Wilson LJ had cited (at paragraph 31) a passage from a book in which there was reference to a partner who "receives all or most of his remuneration in the form of a salary rather than a simple share of profits".

42. Mr Kitchener argued that, in the circumstances, the availability of forfeiture should not depend on the particular way in which the partnership in question chose to structure its affairs. He also relied on the case as illustrating that it can make sense to speak of profit share as remuneration. The Court was not, however, dealing with any issue as to forfeiture.

Conclusions

43. On balance, I agree with Mr Kitchener that profit share of a partner or LLP member can potentially be subject to forfeiture and, hence, that the question set out in paragraph 17 above is to be answered in the affirmative. My reasons include these:

i) The Arbitrator was, as it seems to me, right to take the view that the forfeiture principle can potentially apply to partners. While the principle has in the past been invoked mainly in relation to agents, the rationale for it (as seen in, for example, *Imageview Management Ltd v Jack*) extends more widely and so it is unsurprising that it has been taken to be applicable (e.g. by Snell's Equity – see paragraph 11 above) to other fiduciaries, too. In any event, a partner or LLP member *is* an agent (see paragraphs 26 and 28 above) and it is hard to see why the mere fact that someone is a partner or LLP member as well as an agent should preclude the operation of a principle which affects agents more generally. Supposing, therefore, that the arrangements relating to a partnership or LLP provided for a partner or LLP member to receive a set sum for undertaking particular services regardless of the profitability of the firm or LLP, it would, in my view, be susceptible to forfeiture. In fact, I did not understand Mr Saini to submit to the contrary;

ii) The distinction that Mr Saini draws between profit share and remuneration is not, in my view, well-founded. While it will often (typically, I suspect) be impossible to characterise all or any particular part of the profit share of a partner or LLP member as "remuneration", I do not see why that should always be the case. As a matter of language, it can sometimes be appropriate to speak of a person being remunerated by way of "profit share", as section 2(3)(b) of the 1890 Act and the textbook quoted in *M Young Legal Associates Ltd v Zahid* illustrate (see paragraphs 24 and 41 above). There is, moreover, no good reason to treat profit share differently from other forms of remuneration in the (probably unusual) cases where it can be identified as reward for undertaking specific duties. As Mr Kitchener said, it would make no sense for the law to be that forfeiture was available if a partner were entitled to an extra £10,000 for certain services but not if he were instead to be awarded extra points for the purpose of calculating how profits should be divided. Profit share may usually reflect the interest of the partner or member in the firm, but it is possible to envisage cases in which it rather represents compensation for certain services and, where that is so, profit share can fairly be viewed as remuneration and within the scope of the forfeiture principle. The law should here be concerned with substance rather than form;

iii) Neither the Acts and Regulations governing partnerships and LLPs nor cases such as *Dunne v English*, *Olson v Gullo*, *MacDonald Estate v Martin* and *Erikson v Carr* require me to arrive at conclusions different from those summarised in sub-paragraphs (i) and (ii) above. The legislation does not attempt to provide an exhaustive account of the relevant law and states that "rules of equity and of common law" are preserved (in the case of the 1890 Act) or that the default rules are "subject to the provisions of the general law" (in the case of the Limited Liability Partnerships Regulations). As for the cases, they did not specifically address the issue that now falls to be decided and the Commonwealth authorities are not in any event binding on me; and

iv) The fact that the contractual documentation relating to a partnership or LLP contains no provision for forfeiture cannot necessarily mean that there is no scope for it. While the forfeiture principle can doubtless be excluded by contract, it has been taken to apply where there is no reference to it in a

relevant contract. Take, for instance, the *Imageview* case. The defendant was held to be entitled to recover agency fees from the claimant even though they were payable on the face of the contract.

44. In the present case, the Arbitrator concluded that the sums he held to be forfeit were "in substance, remuneration for the performance of executive duties". If, as I have concluded, profit share is not inherently incapable of representing remuneration and being subject to the forfeiture principle, there can be no scope for Mr Hosking to challenge the Arbitrator's decision.

45. In the circumstances, I shall dismiss the appeal.