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Fiduciary Duties of Partners

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FIDUCIARY DUTIES OF PARTNERS

> 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 business goes on.[1]

In the United States the duties owed by partners traditionally have been defined by the courts. Many of these early common-law definitions were subsequently codified in the Uniform Partnership Act.[2] A partner at common law was considered to be a trustee, and under the Uniform Act he is regarded as a fiduciary.[3] The partner's fiduciary status embodies both a duty of care and a duty of loyalty to his copartners. The purpose of this Note is to explore the standards of care and loyalty imposed upon the partner by the courts and to contrast them with the duties of similar fiduciaries in the business association area.

I. Duty of Care

A. Development

Traditionally, the degree of care which a partner must exercise has been defined in time-honored language as being one of "reasonable-

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[1] Helmore v. Smith, 35 Ch. D. 436, 444 (1887) (Bacon, V.C.).

[2] The Uniform Partnership Act, first enacted in California in 1917, has gained widespread acceptance and has presently been adopted in forty states. See 7 Uniform Laws Ann. (Supp. 1961, at 7). The Uniform Partnership Act has made certain by codification some areas of partnership law; the remaining areas are still governed by the common law. See Uniform Partnership Act § 5. See generally Lewis, *The Uniform Partnership Act*, 24 Yale L.J. 617, 621-24 (1915).

The fiduciary duty probably arose with the development in the Middle Ages of the form of partnership called the *societas* or *compagnia*. In contrast to the *commenda*, which was the forerunner of the present limited partnership, the members of the *societas* were associated together with equal rights. Presumably, the enforcement of the purpose of the *societas*—to associate permanently "persons having confidence in each other to carry on business together"—led to the establishment of the fiduciary duty. See Mechem, Partnership xxi-xxiv (2d ed. 1920) [hereinafter cited as Mechem]; 1 Rowley, Partnership § 1.1, at 6 (2d ed. 1960) [hereinafter cited as Rowley].

[3] See Yeomans v. Lysfjord, 162 Cal. App. 2d 262, 327 P.2d 957 (2d Dist. 1958) (trustees); Lassiter v. Stainback, 119 N.C. 103, 105, 25 S.E. 726 (1896) (dictum) (same). See generally Scott, *The Fiduciary Principle*, 37 Calif. L. Rev. 539 (1949). Compare Conway, *The New York Fiduciary Concept in Incorporated Partnerships and Joint Ventures*, 30 Fordham L. Rev. 297 (1961). For the codification of the partner's fiduciary duty, see Uniform Partnership Act §§ 20, 21. See generally Bandy & Elkouri, *The Uniform Partnership Act*, 9 Okla. L. Rev. 377, 386 (1956).

In the preparation of this Note joint adventure decisions have been relied upon in some instances. The fiduciary duties of a partner are identical to those of a joint adventurer. See Whitsell v. Porter, 309 Ky. 247, 217 S.W.2d 311 (1949); A. Willmann & Associates v. Penseiro, 176 A.2d 739 (Me. 1962); McIver v. Norman, 187 Ore. 516, 205 P.2d 137 (1949); Crane, Partnership § 35, at 159 (2d ed. 1952) [hereinafter cited as Crane]: "A joint adventure is an association created by coness."[4] As early as 1798, a partner was required "to take the same care of the concerns of the partnership business as of his own."[5] However, this standard was not uniformly adopted and variations of the test appeared. Two of these variations were that a partner was required to exercise either that degree of care and diligence as men of common or average care and prudence would generally exercise[6] or that degree of reasonable care, skill, diligence, and economy as an ordinarily prudent businessman would use in similar transactions.[7]

Evidently, the "own business" and "prudent businessman" tests held the partner to a higher degree of care than did the "average care" test. In the first two tests the partner was held to the care of a prudent businessman, who was normally expected to devote full time to the business, while in the other he was held merely to the care of an ordinary and prudent man. The prudent businessman test is articulated in terms of fiduciary status, which suggests more conservative action.[8] It is apparent that all of these tests involved a determination of the "reasonableness" of the partner's conduct.

Additionally, a strict good faith standard had been recognized and applied in some jurisdictions.[9] Under the "good faith" test, an act which was not fraudulent or wanton and was executed by a partner in good faith would be deemed to satisfy the partner's requisite degree of care. Furthermore, when the "good faith" doctrine was applied, no mention was made of the partner's compliance with any of the standards of reasonableness.[10]

In some decisions there appears to be a blending of the "reasonable man" and "good faith" standards,[11] but a careful examination of the decisions will often disclose that either one or the other was dominant in the courts' reasoning. For example, the Iowa court in *Exchange Bank v. Gardner*,[12] in determining the liability of a partner for the alleged breach of his duty of care, stated that the partner was required "to act in good faith . . . and to exercise as high a degree of care and

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owners of a business venture, differing from partnership in that it has more limited scope and duration. The relations between the associates are goverened by the principles of the law of partnership, as to fiduciary duties."

[4] See Bohrer v. Drake, 33 Minn. 408, 23 N.W. 840 (1885); SCHUMACHER, PARTNERSHIP § 95 (2d ed. 1905).

[5] Jessup v. Cook, 6 N.J.L. 434, 438 (1798).

[6] Carlin v. Donegan, 15 Kan. 495, 500 (1875).

[7] Exchange Bank v. Gardner, 104 Iowa 176, 73 N.W. 591 (1897).

[8] Compare Boyd, *The Fiduciary Status of Directors, Officers, and Controlling Shareholders*, 1959 IOWA LEGAL INST. 3 (prudent director standard less stringent—full time not devoted to business).

[9] See, *e.g.*, Watt v. German Sav. Bank, 183 Iowa 346, 165 N.W. 897 (1917) (liable for losses resulting from willful disregard of duty); Northen v. Tatum, 164 Ala. 368, 375, 51 So. 17, 19 (1909) (averment of bad faith would cause loss to be borne by partner).

[10] See Houston v. Polk, 124 Ga. 103, 52 S.E. 83 (1905); Charlton v. Sloan, 76 Iowa 288, 41 N.W. 303 (1888) (fact that act was "unwise" did not require liability); Tilloston v. Paquet, 74 Ore. 539, 145 Pac. 268 (1914) (no liability for mistaken payment).

[11] See J. E. Crosbie, Inc. v. King, 192 Okla. 53, 133 P.2d 543 (1943).

[12] 104 Iowa 176, 73 N.W. 591 (1897).

skill as is generally exercised by businessmen in the management of such business."[13] The partner was in charge of the bulk of the firm's banking business. Without consulting his copartners he purchased for the firm notes of dubious quality on the strength of a single telegram; a "careful investigation" by him would have disclosed their true worth.[14] Certainly, a prudent person would have conducted a more extensive investigation to ascertain the value of a proposed investment, and the court so noted.[15] Even though the degree of care exercised was "not the highest," the court stressed the absence of bad faith and found him free from liability.[16] In a later decision the Iowa court seems to have abandoned the reasonable man doctrine in favor of a good faith test.[17]

The reasonableness tests subsequently fell into general disuse and the good faith doctrine became the accepted standard. Under this doctrine, absent any bad faith or willful misconduct, a partner has been found to be fulfilling adequately his fiduciary duty if his conduct results from a mistake or an honest error in judgment.[18] If the causation of the loss suffered by the firm can be traced to an act over which the partner had no control, the loss will be borne by the firm.[19] Furthermore, a partner is not required to guarantee to the partnership his own ability[20] in the absence of a clause in the partnership agreement providing for the exercise of a specific skill.[21]

An examination of the particular facts in a number of these cases reveals, however, that courts are excusing as "mistakes" what would be regarded as negligent conduct in other contexts. The amount of negligence which will be excused has not been definitely determined

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[13] *Id.* at 182, 73 N.W. at 592.

[14] *Id.* at 180-82, 73 N.W. at 592.

[15] *Ibid.*

[16] *Ibid.*

[17] Watt v. German Sav. Bank, 183 Iowa 346, 374, 165 N.W. 897, 905 (1917): "A partner is liable for losses . . . which result from willful disregard of duty on his part."

[18] See Houston v. Polk, 124 Ga. 103, 52 S.E. 83 (1905) (installation of wrong machinery); J. E. Crosbie, Inc. v. King, 192 Okla. 53, 133 P.2d 543 (1943).

[19] See Savery v. Thurston, 4 Ill. App. 55 (1879) (the Chicago fire). Damage to firm property caused by an act of God must be borne by all the partners. See United States v. Guerber, 124 Fed. 823 (S.D.N.Y. 1903) (storm at sea).

[20] See, *e.g.*, Houston v. Polk, 124 Ga. 103, 52 S.E. 83 (1905) (installation of improper waterwheel in electrical plant); Hurter v. Larrabee, 224 Mass. 218, 112 N.E. 613 (1916) (no individual liability for loss caused by faulty bookkeeping); Thomas v. Milfelt, 222 S.W.2d 359, 364 (Mo. Ct. App. 1949) (partner in charge of firm's books not liable for losses incurred).

Although a single partner may occupy a position of dominance in the firm, the requisite degree of care does not rise with the increase in his authority. See Gilroy v. White Eagle Oil Co., 104 F. Supp. 247 (N.D. Okla.), *aff'd*, 201 F.2d 113 (10th Cir. 1952) (no liability imposed on dominant party); Snell v. DeLand, 136 Ill. 533, 27 N.E. 183 (1891); J. E. Crosbie, Inc. v. King, 192 Okla. 53, 133 P.2d 543 (1943) (managing partner); MECHEM § 173.

[21] See Hurter v. Larrabee, 224 Mass. 218, 112 N.E. 613 (1916); Knudson v. George, 157 Wis. 520, 523, 147 N.W. 1003, 1004 (1914) (dictum) (joint adventure).

by the courts, but more recent decisions interpreting the duty of care indicate a trend toward a gross negligence standard.[22] For example, in *Thomas v. Milfelt*,[23] the partner who was in charge of the firm's bookkeeping advanced wages to one of the firm's employees. Whenever the employee received government checks, he endorsed them over to the firm to repay the advancements made to him. The partner could not determine the amount the firm owed to or was owed by the employee because he failed to keep accurate business and financial records.[24] The court based its decision of no liability upon the premise that the partner had not personally profited in the transaction and that the employee had testified that he was not paid more than he had coming.[25] In *Thomas* other losses were also excused because they were not the result of bad faith, fraud, or culpable negligence.[26] Certainly an average businessman would keep accurate business accounts or hire a qualified person to keep them for him. If he did not, it would seem that his action would be culpably negligent.

In *Kraemer v. Gallagher*,[27] an action was brought by one partner of a real estate partnership based upon his copartner's failure to engage an attorney when selling real estate for the firm. The copartner executed an agreement with the buyer's attorney which was disadvantageous to the partnership. The court decided the partner would not be allowed to complain because the defendant's custom to close titles without legal counsel was a long-standing practice, known to the plaintiff, and the risk was inherent.[28] With no more facts than these,

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[22] Gross negligence or a reckless disregard of a partner's obligations to the firm has been employed as the test by some courts. See Watt v. German Sav. Bank, 183 Iowa 346, 374, 165 N.W. 897, 907 (1917) (willful disregard); Hurter v. Larrabee, 224 Mass. 218, 112 N.E. 613 (1916) (reckless disregard); Tygart v. Wilson, 39 App. Div. 58, 68, 56 N.Y. Supp. 827, 833 (1899) (gross negligence). Other courts have defined the standard as being culpable or ordinary negligence. See Bohrer v. Drake, 33 Minn. 408, 23 N.W. 840 (1885) (ordinary negligence); Gordon v. Moore, 134 Pa. 486, 19 Atl. 753 (1890) (per curiam) (ordinary negligence); Binning v. Miller, 55 Wyo. 478, 506, 102 P.2d 64, 76 (1940) (dictum) (culpable negligence). However, in the application of the latter test the courts occasionally allowed conduct which would seem to have been more than ordinary negligence. In *Lyons v. Lyons*, 207 Pa. 7, 56 Atl. 54 (1903), the partnership's manager extended credit to a nearly bankrupt company which was managed by a man who had previously failed in the same business and therefore could not do business in his own name. Thereafter, he continued the identical business in the name of his wife. Although the court found the partner to be free from liability, it based its decision upon a lack of culpable negligence. From these facts it would seem that such actions would be culpably negligent since an ordinary, prudent businessman would have been aware of the financial instability of his large credit customers and would not have extended credit on such a risk. The court's decision can be supported by using a gross negligence standard rather than the culpable negligence standard, which seems to have been violated in that case.

[23] 222 S.W.2d 359, 364-65 (Mo. Ct. App. 1949).

[24] *Id.* at 364.

[25] Id. at 364-65.

[26] *Id.* at 365.

[27] 235 N.Y.S.2d 874 (App. Div. 1962).

[28] *Id.* at 876.

the result in *Kraemer* seems unquestionably correct. But the court went on to imply that since the partner desired the consummation of the sale and since the proceeds were immediately divided after the sale, this suit would be barred by those acts alone.[29] Certainly partners would normally desire the consummation of all partnership sales in order to profit therefrom. The fact that partners in a firm which sells only a few large items split the proceeds following a particular sale does not seem remarkable; there might be good reasons for doing so after every sale. Perhaps there may be found in the courts' reasoning the germ of a rational basis for excusing a certain amount of "negligent" activity.

This unarticulated rationale can be illustrated by an apparent inconsistency which has arisen. While excusing a certain amount of negligence, a partner has at all times been required to exercise his partnership duties to the best of his ability and judgment.[30] It would seem that a partner cannot be exercising his duties to the best of his ability when, at the same time, his actions are negligent. Therefore, it is probable that when the court suggests that a partner must exercise his duties to the best of his ability, it assumes that some negligence—or "mistake"—is likely to accompany a partner's actions in carrying out firm business. A certain propensity toward negligence is implicit in the concept of human ability, and, as between partners, it can be written off as a business risk because they have chosen to do business in this manner. However, for this "normal" negligence to be excusable, the act would have to be done in good faith.

B. *Comparison with Corporate Director*

The development of the partner's requisite degree of care has been the converse of the development of the care required by the courts to be exercised by a corporate director.[31] While the partner's duty of care appears to have changed from a reasonable man standard to a good faith-gross negligence rule,[32] the director's requisite care has progressed from a gross negligence rule to the present reasonable man standard.[33] Presently, a corporate director is liable for ordinary negligence, while a partner seems to escape liability for at least some of his equally culpable actions. In effect, the partnership standard is making the lack

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[29] *Ibid.*

[30] Hurter v. Larrabee, 224 Mass. 218, 112 N.E. 613 (1916); Degen v. Brooks, 77 N.D. 514, 43 N.W.2d 755 (1950) (counterclaim for time not devoted to partnership); Platt v. Henderson, 227 Ore. 212, 234, 361 P.2d 73, 83 (1961). In American Pac. Dairy Prods. v. Siciliano, 235 F.2d 74 (9th Cir. 1956), a partner agreed in the partnership agreement to exercise all his skill and energy for the best interests of the firm. The partner was held liable when he delegated the bulk of his duties.

[31] See generally Boyd, *supra* note 8, at 2-7.

[32] See *id.* at 2.

[33] HENN, CORPORATIONS § 235 (1961); LATTIN, CORPORATIONS § 10, at 242 (1959) [hereinafter cited as LATTIN]. However, a mistake which is in the exercise of honest business judgment will not subject a director to liability. "The standard is one of reasonable diligence, not the utmost amount of diligence." Casey v. Woodruff, 49 N.Y.S.2d 625, 642 (Sup. Ct. 1944).

of business acumen a sufficient defense for a partner's otherwise negligent conduct.

The gross negligence test for corporate directors is the old view; it has been adopted in only a few jurisdictions and has been criticized by most modern commentators.[34] If ordinary negligent conduct on the part of a director were permitted, it would appear tantamount to requiring that a director devote only passing attention to the affairs of the corporation. With the present wide separation of ownership from control in the large corporation, ownership interests have little voice in the management of corporate affairs.[35] Additionally, large corporations are approaching the status of quasi-public investment concerns in which the directors are dealing exclusively with other people's money.[36] These factors are among those which have led the courts to require more care from a director than was demanded when he was also a principal owner of the business.

It has been argued that in a close corporation where the directors are also the owners, a strict standard of care should not be enforced because it is an unnecessary restriction on private activity.[37] The close corporation would seem analogous to the partnership, for a partner also has an interest in both the ownership and the management of the business. A partner's duty of care remains at a lower level to protect his freedom, as an owner, to do with his property as he wishes.

II. The Duty of Loyalty

Although the partner and the corporate director are held to widely separated standards of care, the duty of loyalty owed in each position is very similar.[38] Thus, a partner's duty of loyalty is measured by a much stricter standard than is his duty of care. The duty of loyalty resulting from a partner's fiduciary position is such that the severity of a partner's breach will not be questioned. Rather, the question will be whether there has been any breach at all.[39] This stringent

[34] See 3 Fletcher, Corporations § 1034 (rev. perm. ed. 1947); Lattin § 10, at 243; Note, 82 U. Pa. L. Rev. 364, 367 (1934).

> If gross negligence be understood as meaning something nearly approaching fraud or bad faith, then the rule is not to be commended and is against the decided weight of authority. . . . [S]uch a rule is at the best misleading, and . . . "the plain and obvious rule is, that directors impliedly undertake to use as much diligence and care as the proper performance of the duties of their office requires." Fletcher, *op. cit. supra* at 554.

[35] See generally Berle & Means, The Modern Corporation and Private Property 84-90 (1947).

[36] See Note, 20 Iowa L. Rev. 808 (1935).

[37] See *ibid.*

[38] Compare Boyd, *supra* note 8, at 7-19; Scott, *The Trustee's Duty of Loyalty*, 49 Harv. L. Rev. 521 (1936).

[39] See Meinhard v. Salmon, 249 N.Y. 458, 164 N.E. 545 (1928) (joint adventure); Fouse v. Shelly, 64 W. Va. 425, 63 S.E. 208 (1908) (utmost good faith). In *Meinhard* Judge Cardozo stated:

> Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something more than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then

standard arises from the fundamental nature of a partnership. In a partnership each partner is the confidential agent of his copartners and vice versa.[40] Therefore, every partner has a right to information the others possess,[41] and no one may act at the expense of his copartners. Furthermore, a secret profit may not be made to the exclusion of copartners.[42]

Loyalty to copartners and to the partnership is required from all partners. However, if one partner is in a position to exert greater control over partnership affairs than can be exercised by his copartners, the court will require an even higher degree of loyalty from this partner.[43] Moreover, if the partnership relation results in opportunities for obtaining information not available to all partners, a stricter standard will be imposed on those who have a superior opportunity to acquire the information.[44]

When information is received by a single partner, he cannot mislead his copartners by furnishing them this information in a fraudulent manner. In addition, the partner's affirmative duty to disclose all matters material to partnership affairs forbids him from concealing material facts from his partners by complete silence.[45] Failure of a partner fully to disclose relevant information to his copartners vitiates any contract or settlement between them.[46]

> the standard of behavior. . . . Uncompromising rigidity has been the attitude of the courts of equity when petitioned to undermine the rule of undivided loyalty by the disintegrating erosion of particular exceptions. 249 N.Y. at 464, 164 N.E. at 546.

But see id. at 477, 164 N.E. at 550 (dissenting opinion) (distinguishes trustee from joint adventurer); Young v. Cooper, 30 Tenn. App. 55, 203 S.W.2d 376 (1947).

[40] See Linn v. Clark, 295 Ill. 22, 128 N.E. 824 (1920); Van Hooser v. Keenon, 271 S.W.2d 270 (Ky. Ct. App. 1954); Casey v. Grantham, 239 N.C. 121, 79 S.E.2d 735 (1954); 1 ROWLEY § 90, at 237-39.

[41] See Alexander v. Sims, 220 Ark. 643, 249 S.W.2d 832 (1952); Weidlich v. Weidlich, 147 Conn. 160, 157 A.2d 910 (1960); Poss v. Gottlieb, 118 Misc. 318, 193 N.Y. Supp. 418 (Sup. Ct. 1922).

[42] Stenian v. Tashjian, 178 Cal. 623, 174 Pac. 883 (1918). *But see* Maryland Cas. Co. v. City of Tacoma, 199 Wash. 72, 90 P.2d 226 (1939) (partner secretly agreed to share profits and losses with subcontractor).

[43] See Joseph v. Mangos, 192 Iowa 729, 185 N.W. 464 (1912); Bass v. Daetwyler, 305 S.W.2d 339 (Mo. Ct. App. 1957); Poss v. Gottlieb, 118 Misc. 318, 193 N.Y. Supp. 418 (Sup. Ct. 1922).

[44] See Arnold v. Maxwell, 223 Mass. 47, 111 N.E. 687 (1916); Seal v. Holcomb, 48 Tex. Civ. App. 330, 107 S.W. 916 (1908).

[45] See, *e.g.*, Poss v. Gottlieb, 118 Misc. 318, 193 N.Y. Supp. 418 (Sup. Ct. 1922); Stark v. Reingold, 18 N.J. 251, 113 A.2d 679 (1955); Salhinger v. Salhinger, 56 Wash. 134, 105 Pac. 236 (1909); CRANE § 67. Where each partner is aware that the other is carrying on a business similar to that of the partnership and each fails to make a claim on the other's personal business, neither partner is required to divulge to the other information obtained in the course of partnership business. Crawford v. Crawford, 163 Kan. 126, 181 P.2d 526 (1947).

[46] See William Goldstein Co. v. Joseph J. & Reynold H. Greenberg, Inc., 352 Pa. 259, 42 A.2d 551 (1945) (concealment vitiated contract between partners); Woldert v. Pulki, 221 S.W. 1112 (Tex Civ. App. 1920) (fraud vitiates voluntary settlement between partners).

The strength of the partner's duty to inform is shown in *Kelso v. Kelso*.[47] While one partner was in the military service, his copartner was left in charge of the firm's business. The partnership's books, after being in the hands of the copartner for this period, did not reflect the true worth of the complaining partner's share. Before the sale of his partnership share to a third person, he believed his copartner was honestly representing to him the firm's true value. Thereafter, the complaining partner sold his share for much less than its value, as determined by the copartner's subsequent sale of his share.[48] Although the partnership relation had been terminated for some time, an accounting was granted as if the partner had sold his share to his copartner.[49]

As a practical matter, the requisite degree of loyalty must be maintained at all times by every member of the firm. From the first exploratory discussions through formal association in partnership to final severance of the relationship, partners are required to exercise scrupulous loyalty and good faith.[50]

A. Partnership Opportunities

When a partner learns of or is offered any opportunity in his capacity as a member of a partnership, he cannot exercise this opportunity for his personal benefit without first offering it to the firm.[51] Therefore, as was stated in a recent declaratory judgment,[52] a partner will not be allowed to dissolve the firm in bad faith to obtain a partnership opportunity for himself but will, on the contrary, incur liability to his copartners for such action. In such cases a partner may not avail himself of even a portion of a partnership opportunity.[53] The firm will

[47] 40 Tenn. App. 681, 292 S.W.2d 483 (1955).

[48] *Id.* at 699-700, 292 S.W.2d at 491.

[49] *Ibid.*

[50] Boswell v. Gillett, 226 Ark. 935, 295 S.W.2d 758 (1958) (duty extends from time negotiations begin to the complete settlement of partnership affairs); Urzi v. Urzi, 140 Cal. App. 2d 589, 295 P.2d 539 (1st Dist. 1956) (duty extends after dissolution to termination); Bloom v. Lofgren, 64 Minn. 1, 65 N.W. 960 (1896) (duty extends to those negotiating to form a partnership).

[51] See Peterson v. Tharp, 299 F.2d 434 (5th Cir.), *cert. denied*, 83 Sup. Ct. 184 (1963) (by implication); Fortugno v. Hudson Manure Co., 51 N.J. Super. 482, 144 A.2d 207 (1958); Meinhard v. Salmon, 249 N.Y. 458, 164 N.E. 545 (1928) (joint adventure). If the sale of a partnership asset has been consumated, and the new owner and a partner then decide to become joint owners of the asset, there is no breach of the duty of loyalty. Linn v. Clark, 295 Ill. 22, 128 N.E. 824 (1920).

For an interesting but apparently minority view see Martin v. Carroll, 259 Ala. 197, 200, 66 So. 2d 69, 71 (1953) (constructive trust not imposed): "To constitute partnership property the land must have been acquired with partnership funds or on partnership credit and for partnership use."

[52] Page v. Page, 199 Cal. App. 2d 527, 18 Cal. Rptr. 897 (2d Dist. 1962).

[53] See Pratt v. Frazer, 95 Ark. 405, 129 S.W. 1088 (1910) (secret profit); Stenian v. Tashjian, 178 Cal. 623, 174 Pac. 883 (1918) (same); Goldman v. Cosgrove, 172 Wis. 462, 179 N.W. 673 (1920) (same). The doctrine has been extended to compel a partner to account for secret commissions on partnership transactions, even though he shared the commissions with an outsider who assisted him. See 1 ROWLEY § 21.1, at 532.

receive the entire benefit that the partner attempted to retain for himself even though the partner contributed value and a similar payment would have been made for identical services if rendered by a third person.[54] However, a partner will be permitted to take advantage of a partnership opportunity for himself—even if it is within the scope of the partnership's business—when his copartners have knowledge of and acquiesce to this action.[55] Similarily, if information is received by a partner in his capacity as a partner, such information may be utilized by the partner for his personal advantage and not disclosed to the firm if it concerns opportunities which are not within the scope of the partnership business.[56]

When the firm is presented with a business opportunity, a partner may take the opportunity for himself if the partnership does not have sufficient funds to take advantage of the opportunity or if the firm simply fails to take either affirmative or negative action.[57] Otherwise, a partner may avail himself of a partnership opportunity only when it has been completely abandoned by the firm.[58] Occasionally, a third party will refuse to deal with the partnership and will offer a partnership opportunity to a partner only in his individual capacity. A partner will not be allowed to accept such an offer from a third person while he is a member of the firm.[59]

A partner is not barred from engaging in additional enterprises in his own behalf as long as the venture is not within the scope of the partnership business and is done in good faith.[60] Moreover, he may be

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[54] Stenian v. Tashjian, *supra* note 53 (partner received commission from vendor on sale to partnership); Jordan v. Markham, 130 Iowa 546, 107 N.W. 613 (joint adventure) (same).

[55] See Levine v. Personnel Institute, 138 N.Y.S.2d 243 (Sup. Ct.), *aff'd*, 158 N.Y.S.2d 740 (App. Div. 1940). Where the complaining partner is aware that his copartner is the sole owner of a competing business when the partnership is formed, the copartner does not breach his fiduciary duty. Holmes v. Keet, 153 F.2d 132 (D.C. Cir. 1946).

[56] See Latta v. Kilbourn, 150 U.S. 524 (1893); More v. Burroughs, 111 Kan. 28, 205 Pac. 1029 (1922).

> [I]f a member of a partnership firm avails himself of information obtained by him in the course of the transaction of the partnership business, or by reason of his connection with the firm and . . . *he uses the information for purposes which are wholly without the scope of the partnership business, and not competing with it, the firm is not entitled to an account of such benefits.* Latta v. Kilbourn, *supra* at 549. (Emphasis by Court.)

[57] See Neilsen v. Holmes, 82 Cal. App. 2d 315, 325, 186 P.2d 197, 203 (4th Dist. 1947) (by implication); Shrader v. Downing, 79 Wash. 476, 140 Pac. 558 (1914) (by implication).

[58] See Williamson v. Monroe, 101 Fed. 322 (W.D. Ark. 1900) (partner dissolved firm, keeping partnership opportunity for self); Vetter v. Lentzinger, 31 Iowa 182 (1870) (partner procured patent after partnership's application denied).

[59] See Miller v. O'Boyle, 89 Fed. 140 (W.D. Pa. 1898) (proof of previous conspiracy not necessary); Ladas v. Psiharis, 241 Mich. 101, 105, 216 N.W. 458, 459 (1927) (dictum).

[60] See, *e.g.*, Latta v. Kilbourn, 150 U.S. 524, 549, (1893); Powell v. Powell, 181 Ore. 675, 704-05, 184 P.2d 373, 385-86 (1947); Shrader v. Downing, 79 Wash. 476, 140 Pac. 558 (1914).

a partner in more than one noncompeting firm if neither firm requires all of his time.[61] Neither will a partner be prohibited from doing business with the partnership as an individual or from standing in the position of a creditor to it.[62]

Partnership assets may be used only for the benefit of the firm. Opportunities may not be created for a partner's private gain by the unauthorized use of partnership funds, and a partner will not be allowed to retain benefits flowing from such use of the funds.[63] Moreover, partnership equipment may not be used for the private benefit of an individual partner.[64]

The renewal of partnership leases for the benefit of a single partner probably has caused the most litigation in the partnership opportunity area. Whenever a lease is obtained by a partnership, the expectancy of its renewal becomes a partnership asset which the duty of loyalty will compel all partners to protect. Therefore, when a partnership is leasing property, a partner may not secretly renew the lease in his own name to the exclusion of his copartners.[65] Even though the subsequent lease is to commence after the dissolution of the partnership, a single partner will not be allowed to renew it for his individual benefit.[66] Similar standards will be applied when a lease necessary to the firm is acquired in the first instance by an individual partner; the partner will be compelled to hold the lease for the benefit of the firm.[67]

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[61] See 1 ROWLEY § 21.1, at 542. Usually, however, a partner must devote his time in its entirety to the firm's business. See Platt v. Henderson, 227 Ore. 212, 234, 361 P.2d 73, 83 (1961) (dictum); MULDER & VOLZ, THE DRAFTING OF PARTNERSHIP AGREEMENTS 16 (rev. ed. 1955); *cf.* Dennis v. Gordon, 163 Cal. 427, 125 Pac. 1063 (1912).

[62] See Hargiss v. Royal Air Properties, Inc., 23 Cal. Rptr. 678 (4th Dist. 1962); Turner v. McDaniel, 194 Ore. 595, 243 P.2d 273 (1952). See generally 1 ROWLEY § 21.1(A)(4).

[63] See Bracht v. Connel, 313 Pa. 397, 170 Atl. 297 (1933); MECHEM § 185. Moreover, a partner will not be allowed to eliminate his copartner's right to share in a partnership contract and divert the profits to himself. See Nelson v. Abraham, 29 Cal. 2d 745, 177 P.2d 931 (1947); Abramson v. Davis, 100 N.J. Eq. 563, 135 Atl. 774 (1927) (per curiam).

[64] See Powell v. Powell, 181 Ore. 675, 698-99, 184 P.2d 373, 383 (1947); Waagen v. Gerde, 36 Wash. 2d 563, 219 P.2d 595 (1950).

[65] Mitchell v. Reed, 61 N.Y. 123 (1874); MacDonald v. Follett, 142 Tex. 616, 180 S.W.2d 334 (1944); Mullens v. Wolfe, 120 W. Va. 672, 200 S.E. 37 (1938).

[66] See Knapp v. Reed, 88 Neb. 754, 130 N.W. 430 (1911); Meinhard v. Salmon, 249 N.Y. 458, 164 N.E. 545 (1928) (joint adventure). *Contra,* Stewart v. Ulrich, 117 Wash. 109, 201 Pac. 16 (1921). When a partner has notified his copartner of his intent to dissolve the firm and the copartners have acknowledged same in writing, the partner may negotiate for renewal of the partnership lease for himself. See Thursby v. Kirby, 171 Misc. 310, 12 N.Y.S.2d 279 (Sup. Ct. 1939); Mitchell v. Reed, 61 N.Y. 123 (1874); Lacy v. Hall, 37 Pa. 360, 365 (1860) (dictum).

[67] See Deutschman v. Dwyer, 223 Mass. 261, 11 N.E. 877 (1916); Smith v. Brown, 294 Pa. 203, 143 Atl. 913 (1928) (dictum). See generally Note, *Disability of a Partner or Joint Adventurer to Take Renewal of Firm Lease,* 38 YALE L.J. 782 (1929).

The purchase of a reversionary interest in the leasehold has presented one of the few unsettled areas of partnership leases. If the high standard of loyalty is desired to be continued, the New York rule should be adopted. This rule interprets the partner's fiduciary duty as requiring such a sufficiently high degree of loyalty that it will not permit a partner to possess an asset in conflict with the interests of the partnership.[68] However, some jurisdictions have allowed partners to purchase the reversionary interest and thereby become the partnership's landlord.[69] This action has been permitted when a single partner has made complete disclosure of his intention to purchase the reversion. There can be no fraud involved in the transaction, and the firm must be allowed to fulfill its present lease. Courts adopting this principle have not considered the position of landlord so adverse to the interest of the partnership that the purchase would be prevented.

The classic case of *Meinhard v. Salmon*[70] demonstrates the very high degree of loyalty required from a partner. A lease for a hotel was obtained for the benefit of the firm. Shortly before the lease expired, one of the parties procured for his own benefit a new long-term lease which included the hotel and also much additional property. Buildings on the property were to be destroyed and a new real estate complex erected. Although, as the dissent points out,[71] the new lease involved an entirely new and different project, Judge Cardozo compelled the party participating in the new association to hold his share for the benefit of the parties in the original venture.

B. Transactions with Copartners and the Firm

Just as the partner is held to a high standard of loyalty when presented with a partnership opportunity, he is held to an equally strict standard in his transactions with his firm or his copartners. Nothing forbids partners from dealing with each other at arm's length, as ordinary businessmen, when negotiating a nonpartnership transaction.[72] However, when the transaction concerns any aspect of the partnership relation, the requisite degree of loyalty must be maintained. Whenever a partner has made a purchase of the partnership share of another, courts tend to view the transaction with suspicion. It is incumbent upon a purchasing partner to inform the selling partner fully of any information he possesses which would have an effect upon the value of the partnership share.[73] The purchaser may not, therefore,

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[68] See Boxill v. Boxill, 201 Misc. 386, 111 N.Y.S.2d 33 (Sup. Ct. 1952). *Contra*, Anderson v. Lemon, 8 N.Y. 236, 237 (1853) (dictum). This rule is not confined to New York courts. See Bakalis v. Bressler, 1 Ill. 2d 72, 115 N.E.2d 323 (1953).

[69] See Thanos v. Thanos, 313 Ill. 499, 145 N.E. 250 (1924); Sanek v. Hill Bldg. & Loan Ass'n, 138 N.J. Eq. 534, 49 A.2d 303, *aff'd*, 140 N.J. Eq. 108, 52 A.2d 852 (1947) (may purchase subject to existing lease); Lipinski v. Lipinski, 227 Minn. 511, 520, 35 N.W.2d 708, 713 (1949) (dictum) (same).

[70] 249 N.Y. 458, 164 N.E. 545 (1928).

[71] *Id.* at 472-80, 164 N.E. at 549-52 (Andrews, J., dissenting).

[72] See, *e.g.*, Emerzian v. Emerzian, 6 Cal. App. 2d 721, 44 P.2d 656 (4th Dist. 1935) (copartner signed note as accomodation maker); Jones v. Anheuser-Busch Brewing Ass'n, 189 S.W. 631 (Mo. App. 1916) (advancement to copartner).

[73] See, *e.g.*, Creswell v. Keith, 361 S.W.2d 542 (Ark. 1962); Malden Trust Co. v. Brooks, 276 Mass. 464, 177 N.E. 629 (1931); Penner v. De Nike, 288 Mich. 488, 285

conceal or fraudulently represent material facts to his copartner.[74] Similarly, if the purchase is from a representative of a deceased partner's estate, there cannot be arm's length negotiations. The partner making the purchase must voluntarily disclose all facts pertinent to the valuation of the interest being acquired.[75]

The very high standard by which a partner's conduct is measured when he purchases his copartner's share is demonstrated in *Inman v. Parr*.[76] Three partners owned an automobile agency of which one partner was the manager. The automobile manufacturer did not wish inactive participants to own its franchises. The managing partner told his copartners they would have to execute options to sell their shares to him or the firm would go out of business; the price offered by the buyer was allegedly one-third of the firm's net worth. The copartners, relying on their attorney's advice, entered into the option agreement.[77] However, after the option had been exercised, the partners discovered that the firm's net worth was more than ten times the amount represented by the purchaser. The court held that it was not necessary for the complaining partners to show that they relied on the purchaser to make a complete disclosure of the firm's financial condition. The fraud, by itself, was sufficient to grant money damages to one seller and to set aside the option agreement and quiet the other's title in the firm.[78]

Even though the sale of a partnership share is made under conditions making the relationship between the partners that of strangers, candor and good faith must be present. Therefore, if the sale is forced by a "strained" relationship between the partners, there is no lessening of the fiduciary duty between them.[79] There must be good faith in the negotiations whether the cause of the strained feelings stems from the partnership itself or from nonpartnership actions,[80] and when litigation arises between the partners the burden of proof will fall on the purchasing partner to show his full disclosure and good faith.[81]

N.W. 33 (1939). *But see* Elmore v. McConaghy, 92 Wash. 263, 266, 159 Pac. 108, 110 (1916): "[W]hen [the partners] . . . began to negotiate between themselves . . . they were then dealing with each other at arm's length."

[74] See Hansen v. Janitschek, 57 N.J. Super. 418, 154 A.2d 855, *rev'd on other grounds*, 31 N.J. 545, 156 A.2d 329 (1960); Nelson v. Matsch, 38 Utah 122, 110 Pac. 865 (1910).

[75] See Malden Trust Co. v. Brooks, 291 Mass. 273, 197 N.E. 100 (1935). The surviving partner is a trustee and owes his fiduciary duty to the cestui que trust, the representative of the deceased partner's estate. Mosher v. Lee, 32 Ariz. 560, 261 Pac. 35 (1927); Grigg v. Hanna, 283 Mich. 443, 278 N.W. 125 (1938).

[76] 311 S.W.2d 658 (Tex. Civ. App. 1958).

[77] *Id.* at 697-98.

[78] *Id.* at 702.

[79] See Johnson v. Peckham, 132 Tex. 148, 120 S.W.2d 786 (1938) (seller defrauded the buying partner); Lundquist v. Peterson, 134 Minn. 279, 158 N.W. 426 (1916) (buying partner defrauded the seller).

[80] See Karle v. Seder, 35 Wash. 2d 542, 214 P.2d 684 (1950).

[81] See Townes v. Townes, 270 Fed. 744 (5th Cir. 1921); Laux v. Freed, 53 Cal. 2d 512, 522, 2 Cal. Rptr. 265, 270, 348 P.2d 873, 878 (1960); Styles v. Shaver, 151 App. Div. 903, 136 N.Y. Supp. 347 (1912). *But cf. In re* Estate of Hewitt, 245 Iowa

When a partner sells his own property to the partnership, his fiduciary duty precludes him from failing to disclose that he is the true seller.[82] Property which is owned by a partner before the formation of the partnership is contemplated and which is subsequently sold to the firm is not required to have its cost to the seller or the personal profit to the seller disclosed.[83] However, if the seller does represent the cost of the property, he will incur liability if that representation was fraudulent.[84] Of course, if the partner is acting on behalf of the partnership when he purchases the property or is purchasing the property for the express purpose of selling it to the partnership, he is under an affirmative duty to reveal the true cost of the property and not to make a profit on its transfer to the firm.[85]

Whenever a partner sells firm property, not only must there be no misrepresentation to the firm, but there must be no concealment of the price the seller obtained for the property.[86]

C. *Purchase of Claims Against the Firm*

Courts have not permitted a partner in his position as a fiduciary to be tempted by the possibility of acting in a manner calculated to lower the value of the firm in the eyes of creditors in order to purchase firm obligations at depressed prices. Usually a partner may purchase claims against his firm, but they will be held for the benefit of the partnership. The purchasing partner will be entitled to pro rata contribution from his copartners for their share of the cost.[87] Gener-

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369, 62 N.W.2d 198 (1954) (fraud between partners must be shown by clear and convincing evidence).

Where the transfer has been made from the partnership to a third person and immediately thereafter a conveyance is made from the third person to a partner, it has been held that the purchasing partner must refute the presumption of fraud by clear and convincing evidence. Grossberg v. Haffenberg, 367 Ill. 284, 11 N.E.2d 359 (1937).

[82] See Bestor v. Lapsley, 106 Ala. 240, 257, 17 So. 389, 392 (1895):

> [T]he [selling partner] . . . may induce his associates into a purchase of particular property for the common benefit, concealing the fact that he is the real vendor . . . . [But] at the election of his betrayed associates the sale will be vacated, and the seller compelled to account for whatever loss the associates may have sustained.

[83] See Withroder v. Elmore, 106 Kan. 448, 188 Pac. 428 (1920) (joint adventure); Zogg v. Hedges, 126 W. Va. 523, 29 S.E.2d 871 (1944) (same); Densmore Oil Co. v. Densmore, 64 Pa. 43, 49-50 (1870) (dictum).

[84] See Moe v. Lowry, 69 Colo. 371, 194 Pac. 363 (1920) (joint adventure); Goldman v. Cosgrove, 172 Wis. 462, 179 N.W. 673 (1920).

[85] See Gates v. Megargel, 266 Fed. 811 (2d Cir.), *cert. denied*, 254 U.S. 639 (1920) (joint adventure) (cannot secretly profit from stock purchased for resale to firm); R. C. Gluck & Co. v. Tankel, 24 Misc. 2d 841, 199 N.Y.S.2d 12 (Sup. Ct.), *aff'd*, 12 App. Div. 2d 339, 211 N.Y.S.2d 602 (1961) (cannot make profit on resale of stamps); Densmore Oil Co. v. Densmore, 64 Pa. 43, 50 (1870) (dictum).

[86] See Karle v. Seder, 35 Wash. 2d 542, 214 P.2d 684 (1950) (misrepresentation of selling price). Although a partner agreed on a stipulated price for his share of a firm asset before its sale, he is entitled to his share of the proceeds of the sale if they are greater. Vogel v. Brewer, 176 F. Supp. 892 (E.D. Ark. 1959).

[87] See Nudelman v. Haimowitz, 314 Ill. App. 329, 41 N.E.2d 310, *aff'd*, 382 Ill.

ally, courts have held that the claim is enforceable by the partner against the firm only in the amount which he paid for it.[88]

III. REMEDIES

Even if the partner fails to maintain the proper degree of care, he may still escape liability. Knowledge by his copartners of his fraudulent or grossly negligent actions and their failure to act or object to them will bar the copartners from obtaining any redress from the offending partner.[89] When his copartner has failed to bring an action for such period of time that it would now be inequitable to force the erring partner to change his present position, his copartner's claim will be barred by laches.[90] However, even if a partner attempts to obtain a partnership opportunity for himself, he is not necessarily barred from personally enforcing partnership rights against a copartner who completes a similar breach.[91]

When a breach of a fiduciary duty is discovered, it usually is followed immediately by dissolution[92] and an accounting.[93] Upon the withholding by a partner of partnership property or of funds derived from the use of such property,[94] or the withholding of benefits to which the firm is entitled,[95] an exception is made and a partner is entitled to an accounting without the necessity for dissolution.

87, 46 N.E.2d 33 (1943); McLean v. Hargrove, 139 Tex. 236, 162 S.W.2d 954 (1942) (purchase at foreclosure sale). A partner has occasionally been allowed to purchase firm property for himself at a judicial sale. See Evans v. Carter, 176 S.W. 749 (Tex. Civ. App. 1915). Moreover, upon the sale of firm property by a receiver, a partner is allowed personally to acquire the firm property. James v. Wade, 200 Ark. 786, 141 S.W.2d 13 (1940).

88 See Miller v. Ferguson, 110 Va. 217, 65 S.E. 562 (1909); 1 ROWLEY § 21.1, at 540-41.

89 See Chalmers v. Chalmers, 81 Cal. 81, 22 Pac. 395 (1889) (per curiam) (awareness that debts owed firm could be barred by statute of limitations); Knipe v. Livingston, 209 Pa. 49, 57 Atl. 1130 (1904) (per curiam) (knowledge of lack of diligence in collections); Kraemer v. Gallagher, 235 N.Y.S.2d 874 (App. Div. 1962) (knowledge of closing real estate transactions without an attorney).

90 See, *e.g.*, Peden v. Peden, 350 S.W.2d 509 (Ark. 1961); Younis v. Greigo, 72 Ariz. 369, 236 P.2d 358 (1951); Marks v. Toney, 196 Miss. 572, 18 So. 2d 452 (1944).

91 See Lurie v. Pinanski, 215 Mass. 229, 102 N.E. 629 (1913). *Contra*, Coldren v. Clark, 93 Iowa 352, 363, 61 N.W. 1043, 1048 (1895).

92 UNIFORM PARTNERSHIP ACT § 32, provides in part:

> (1) On application by or for a partner the court shall decree a dissolution whenever:
>
> . . . .
>
> (c) A partner has been guilty of such conduct as tends to effect prejudicially the carrying on of the business,
>
> (d) A partner wilfully or persistently commits a breach of the partnership agreement, or otherwise so conducts himself in matters relating to the partnership business that it is not reasonably practicable to carry on the business in partnership with him.

93 See UNIFORM PARTNERSHIP ACT § 21.

94 See Weathers v. Roberts, 84 Okla. 98, 202 Pac. 775 (1921).

95 See Mervis v. Duke, 175 Md. 300, 2 A.2d 11 (1938) (stating general rule).

If a partner wishes to bring a suit against a copartner, an action at law will not lie until after an accounting and dissolution.[96] Therefore, he is confined to an equitable action if he wishes to obtain redress of the breach before dissolution. Of course, after dissolution the equitable action remains effective.

A. Equitable Remedies

Perhaps the most effective equitable remedy is the constructive trust. When a partner remains in possession of property which he obtained as a consequence of his breach, a trust will be imposed upon the partner, and he will hold the beneficial interest in the property for the partnership.[97] Before a constructive trust will be imposed, the property must be peculiarly suited for firm purposes.[98] In addition, there must be two conditions proved by convincing evidence: "a conflict of interest and . . . an unfair advantage taken of those deprived of participation."[99]

A court of equity may also enter an injunction restraining the breach, even though dissolution is not contemplated.[100] If the injunction is entered before dissolution, it will often alleviate the necessity for a subsequent dissolution since its effect will be to restrain a partner from violating either the rights of his copartners or the terms of the partnership agreement, both of which may result in dissolution.[101]

A money judgment may be obtained through an equitable action. When a partner has not maintained the required degree of care or loyalty and such breach has caused a loss to the partnership, the offending partner will be compelled to make good the entire loss.[102]

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[96] See Knapp v. First Nat'l Bank & Trust Co., 154 F.2d 395 (10th Cir. 1946); In Matter of Estate of Sternberg, 10 Ill. App. 2d 258, 134 N.E. 2d 663, *rev'd on other grounds*, 10 Ill. 2d 328, 140 N.E.2d 125 (1957); Friedland v. Friedland, 12 Misc. 2d 349, 175 N.Y.S.2d 264 (Sup. Ct. 1958). Only under exceptional circumstances can an action at law be brought by one partner against another. In Johnstone v. Morris, 210 Cal. 580, 584, 292 Pac. 970, 972 (1930), the court said: "It is also well settled that the mere fact a dissolution of the partnership has taken place before the action is brought does not change the rule that no action at law can be maintained between partners."

[97] See, *e.g.*, Betts v. Smither, 310 Ky. 402, 220 S.W.2d 989 (1949) (partner held partnership property in his name); Sorenson v. Nielson, 240 N.Y. Supp. 250 (Sup. Ct. 1930) (before dissolution partner obtained firm account for new associate); Wampler v. Harrington, 261 S.W.2d 883 (Tex. Civ. App. 1953) (acquired share of competing business).

[98] See De Santis v. Dixon, 72 Ariz. 345, 236 P.2d 38 (1951); *cf.* Clarke v. McAuliffe, 81 Wis. 104, 51 N.W. 83 (1892) (no breach in purchasing property unconnected with business).

[99] Homestake Mining Co. v. Mid-Continent Exploration Co., 282 F.2d 787, 800 (10th Cir. 1960). (Footnotes omitted.)

[100] Marble Co. v. Ripley, 77 U.S. (10 Wall.) 339 (1870); Mechem § 226.

[101] See *ibid.* Compare note 92 *supra* and accompanying text.

[102] See Thomas v. Milfelt, 222 S.W.2d 359 (Mo. Ct. App. 1949) (liable for losses caused by bad faith but not for poor judgment); Degen v. Brooks, 77 N.D. 514, 43 N.W.2d 755 (1950) (failure to work full time on partnership business). Whenever a partner seeks to recover in a court of equity, he must come into court with

If secret profits are made by one partner to the exclusion of his copartners, the wrongdoing partner will be permitted to keep only his share, and the remainder of the profit so made must be repaid to his copartners.[103]

B. Remedies at Law

Actions at law generally are used for redressing a breach of a partner's fiduciary duty only where there has been fraud or breach of an express agreement between the partners. After the final dissolution and accounting, a partner may maintain a tort action for fraud against the wrongdoer.[104] The erring partner will be liable for damages inflicted by his harmful conduct.

In order to bring an action at law for breach of partnership agreements, the partner must show that he sustained a personal loss from the breach of an independent transaction or an express covenant designed for his protection.[105] The loss must be specifically shown to be incurred by the partner rather than by the firm. Therefore, an action at law will not lie if the suit is for breach of the general provisions of the partnership agreement in which no special covenants are contained.[106]

IV. CONCLUSION

Although a partner's relationship to his firm and his fellow partners has been described as being that of a "fiduciary," an examination of similar relationships indicates that that characterization does not mean the same thing in all contexts, and the duties incident to those relationships vary accordingly.[107] Moreover, an examination of the

clean hands. See Boswell v. Gillett, 226 Ark. 935, 295 S.W.2d 758 (1956). *But cf.* Lurie v. Pinanski, 215 Mass. 229, 102 N.E. 629 (1913) (this does not mean "general depravity"—must be immediately related to equity sought).

103 See Van Hooser v. Keenon, 271 S.W.2d 270 (Ky. 1954); *In re* Kohn's Estate, 116 N.Y.S.2d 167 (Surr. Ct.), *aff'd*, 282 App. Div. 1045, 126 N.Y.S.2d 897 (1953). Compare Prince v. Harting, 177 Cal. App. 2d 720, 2 Cal. Rptr. 545 (1st Dist. 1960) (*semble*) (entire profit repaid).

An interesting distinction is drawn in Shulkin v. Shulkin, 301 Mass. 184, 16 N.E.2d 644 (1938), between a trustee and a partner. When a trustee profits from dealing with the trust property, the entire profit goes to the principal of the trust. Yet, when dealing with partners in a similar situation, the parties are put in the situation they would have been in if there had been no wrongdoing.

104 See Wright v. Lake, 178 Ark. 1184, 13 S.W.2d 826 (1929); Johnstone v. Morris, 210 Cal. 580, 292 Pac. 970 (1930); Reed v. Wood, 190 Okla. 169, 123 P.2d 275 (1942). Before an action at law will lie for conversion there must be an accounting and dissolution. See 17 MINN. L. REV. 225-27 (1932).

105 Parker v. Davis, 225 La. 359, 72 So. 2d 877 (1954); MECHEM § 214; see Ware v. Chatham, 56 S.W.2d 229 (Tex. Civ. App. 1932) (independent transaction).

106 See De Rigne v. Hart, 94 Cal. App. 209, 270 Pac. 1013 (3rd Dist. 1928); *cf.* Hirshfield v. Robins, 99 Pa. Super 217 (1930) (accounting, not assumpsit, was appropriate remedy).

107 Compare 3 SCOTT, TRUSTS §§ 227.2, 227.5 (2d ed. 1956) (Massachusetts "prudent man" rule for trust investments); Note, *Fiduciary Duties of Majority or Controlling Stockholders*, 44 IOWA L. REV. 734 (1959); part I.B. *supra* (duty of care for corporate director).

cases which discuss the fiduciary relationship shows variance within the partnership context itself. For these reasons it would appear desirable that at least some of the potentially troublesome areas of the partnership activities be considered when drafting the partnership agreement.

Since the partner's duty of care, as interpreted by the courts, allows many activities which may be detrimental to his copartners, a previous agreement defining permissible conduct is desirable. However, any attempt to articulate a general standard probably will not alleviate the situation, for it seems that the individual fact situation before the court is more likely to be the basis for disposing of the controversy than generalizations which have done nothing to increase predictability in the past. Moreover, the courts are apt to say that this type of clause merely restates the existing law.[108] Therefore, specific stipulations should be drafted which will be applicable to those situations for which the partners wish to change the mode of conduct usually required. For example, if a partner is bringing to the firm a specific skill which his copartners expect him to exercise, a proviso requiring this skill should be inserted.[109] Where specific methods of doing business are determined before the agreement is signed, such methods should be included so that the court will not excuse the failure to use them. Thus, if partnership decisions are to be made with or without advice of counsel, this should be specifically included in the agreement.[110]

On the other hand, courts probably will not be favorably disposed toward any stipulation which would have a tendency to relax the partner's duty of loyalty. However, it seems likely that clauses allowing partners to engage in a specifically designated activity—such as retention of a present interest in a competing business[111]—would be upheld if not unreasonable. Of course, clauses forbidding activity which might otherwise be permissible under common-law standards would be valid.[112]

Foresight in preparing the partnership agreement will not, of course, eliminate all sources of potential conflict. In the final analysis, whatever stipulations are included in the agreement, a partner should always remember that as a fiduciary he is in a position of trust and confidence and should prejudge his own actions accordingly.

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108 Compare 3 SCOTT, *op. cit. supra* note 107, § 227.14, at 1704 (courts tend to construe such clauses in trust agreements strictly).

109 See Knudson v. George, 157 Wis. 520, 147 N.W. 1003 (1914) (joint adventure).

110 See Kraemer v. Gallagher, 235 N.Y.S.2d 874 (App. Div. 1962) (excusing failure to employ counsel).

111 For an example of this type of stipulation, see 2 ROWLEY § 59.1, at 775:

> Neither partner shall, either alone or with any other person, either directly or indirectly, engage in any trade or business except upon the account and for the benefit of the partnership. (Provided, however, that the said......may continue the......business at......wherein he is now concerned or engaged).

See also MULDER & VOLZ, THE DRAFTING OF PARTNERSHIP AGREEMENTS 38 (rev. ed. 1955).

112 Compare 3 SCOTT, *op. cit. supra* note 107, § 227.14, at 1699 (trustee's power to invest may be restricted to areas narrower than usual).