THE PERSONAL, FIDUCIARY CHARACTER OF MEMBERS' INTER SE RELATIONS IN THE INCORPORATED PARTNERSHIP

A Historical and Comparative Analysis with Particular Reference to English, American, German, Scottish and South African Law

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"*Fundamentum est justitiae fides: id est, dictorum, conventorumque constantia, et veritas* "[1].

"Good faith is a legal norm for measuring the conduct of persons who stand in some form of a legal relationship to one another. It is synonymous with terms such as reasonableness, fairness and all three terms are often used in the case law in an interchangeable manner".[2]

"[T]he special character of the private company as a 'quasi-partnership company' has been recognized ....
'[T]he English courts have at last discovered [in *Ebrahami* v. *Westbourne Galleries*, [1973] A.C. 360 (H.L.(E.))] that the private company is a business organization *sui generis* and not merely a variety of a general conception of limited company'".[3]

"The moment of truth had arrived ....
.... The *Westbourne Galleries* case completes the discovery of the true character of the private company by the English courts ....
.... The essential characteristics of the private company in its true meaning is, as Lord Wilberforce put it, that it is an *association* founded on a *personal* [*good faith*] *relationship*".[4]

R E S U M E

La corporation, caractérisée par le fait que ses membres ne sont d'aucune manière responsables des dettes de la corporation et la société, caractérisée par des relations inter se de confiance mutuelle et de bonne foi, représentent deux types opposés.

Au cours des années pourtant une grande quantité de types hybrides se sont développés à partir de ces deux types opposés. Dans la société incorporée, représentant la dernière phase de ce développement, la société et la corporation se sont fusionnées.

Les droits américain et allemand reconnaissent la nature fiduciaire personnelle des relations inter se des associés d'une corporation lorsqu'il est question de faire exécuter des obligations fiduciaires. Il est étonnant de constater que le droit anglais des compagnies bien que reconnaissant cette nature fiduciaire dans une disposition statutaire portant sur la dissolution juste et équitable, ne la reconnaît cependant pas lorsqu'il s'agit de faire exécuter les obligations fiduciaires. Il serait souhaitable que le droit anglais reconnaisse les obligations fiduciaires entre les associés d'une corporation.

Corporation characterized by members' freedom from liability for corporate debts, and partnership, characterized by inter se relations of mutual confidence and good faith, are polar types.

Over the ages a host of hybrid types has evolved between those polar types. In the incorporated partnership - the final stage of that evolution - partnership and corporation coalesce.

American and German law recognize the personal fiduciary character of corporate partners' inter se relations for the purpose of enforcing fiduciary duties. Anomalously, English company law recognizes that character under the statutory just and equitable winding-up provision but not for the purpose of enforcing fiduciary duties. A case may therefore be made for recognizing fiduciary duties between corporate partners.

TABLE OF CONTENTS

ACKNOWLEDGEMENTS	(i)	- (ii)
QUOTATIONS	(iii)	
RÉSUMÉ	(iv)	
TABLE OF CONTENTS	(v)	- (xii)
PREFACE	(xiii)	- (xvii)
BIBLIOGRAPHY AND LIST OF SOURCES	(xviii)	- (1)
CHAPTER I:		
INTRODUCTION	1	- 6
1. *PURPOSE AND SCOPE*	1	- 3
2. *APPROACH*	4	- 6
3. *OUTLINE*	6	- 7
CHAPTER II:		
THE PARTNERSHIP IDEA	8	- 37
4. *PRELIMINARY*	8	- 10
5. *PARTNERSHIP AS A RELATION*	10	- 17
5.1. *INTRODUCTION*	10	- 10
5.2. *ROMAN LAW*	10	- 11
5.3. *SOUTH AFRICAN LAW*	11	- 12
5.4. *SCOTS LAW*	13	- 13
5.5. *ENGLISH LAW*	13	- 17
6. *THE CHARACTER OF THE INTER SE RELATION*	17	- 29
6.1. *INTRODUCTION*	17	- 18
6.2. *ROMAN LAW*	18	- 21
6.3. *ENGLISH LAW*	21	- 24
6.4. *SCOTS LAW*	24	- 26

6.5.	*SOUTH AFRICAN LAW*	26	- 29
7.	*THE CHARACTER OF THE RELATION AS AGAINST THE WORLD*	29	- 37
7.1.	*INTRODUCTION*	29	- 31
7.2.	*ROMAN AND CIVIL LAW*	31	- 33
7.3.	*SCOTS LAW*	33	- 35
7.4.	*ENGLISH LAW*	35	- 37
7.5.	*SOUTH AFRICAN LAW*	37	- 37
CHAPTER III:			
THE ENGLISH COMPANY LAW SYSTEM		38	- 41
8.	*THE BRITISH COMPANY REGIME*	38	- 41
8.1.	*SCOTLAND*	38	- 39
8.2.	*THE REPUBLIC OF SOUTH AFRICA*	39	- 41
CHAPTER IV:			
THE EVOLUTION OF THE INCORPORATED (PUBLIC) COMPANY IN THE BRITISH SYSTEM		42	- 63
9.	*PRELIMINARY*	42	- 43
10.	*THE EQUITABLE JOINT STOCK COMPANY*	43	- 47
11.	*THE INCORPORATED (JOINT STOCK) COMPANY*	47	- 60
11.1.	*PRELIMINARY*	47	- 47
11.2.	*REGULATION THROUGH REGISTRATION*	47	- 50
11.3.	*CONCESSION OF LIMITED LIABILITY AND FUSIQN OF THE EQUITABLE JOINT STOCK COMPANY WITH THE CHARTERED COMPANY*	50	- 52
11.4.	*BODY CORPORATE: CREATION AND EFFECT*	52	- 55

11.4.1.	*INTRODUCTION*	52	- 52
11.4.2.	*THIRD PARTY RELATIONS*	53	- 53
11.4.3.	*INTER SE RELATIONS*	53	- 55
11.5.	*THE NINETEENTH-CENTURY COMPANIES ACTS AND PARTNERSHIPS*	56	- 60
12.	*THE INCORPORATED COMPANY AND LEGISLATION SINCE 1856*	60	- 61
13.	*THE TERM "COMPANY" IN THE COMPANIES ACTS*	61	- 63

CHAPTER V:

THE PRIVATE (INCORPORATED) PARTNERSHIP AND THE PRIVATE (INCORPORATED) COMPANY IN THE BRITISH SYSTEM

14.	*PRELIMINARY*	64	- 64
15.	*THE EVOLUTION OF THE CONCEPT "PRIVATE COMPANY"*	64	- 65
15.1.	*THE PRIVATE COMPANY UP TO 1844*	65	- 65
15.2.	*THE PRIVATE COMPANY 1844 - 1900*	65	- 67
15.3.	*THE PRIVATE COMPANY 1900 UP TO THE COMPANIES ACT, 1980*	67	- 71
15.4.	*THE PRIVATE COMPANY AND THE COMPANIES ACT 1980*	71	- 72
16.	*PARTNERSHIP PROPER IN THE INCORPORATED PRIVATE COMPANY: THE INCORPORATED PARTNERSHIP*	72	- 76
17.	*JUDICIAL RECOGNITION OF THE INCORPORATED PARTNERSHIP*	76	- 79

CHAPTER VI:

THE PRIVATE (INCORPORATED) PARTNERSHIP AND THE PRIVATE (INCORPORATED) COMPANY IN THE CONTINENTAL AND AMERICAN SYSTEMS

18.	*GENERAL*	80	- 81

20.3.3.1.	*INTRODUCTION*	102	- 105
20.3.3.2.	*STATUTORY REJECTION OF JACKSON*	105	- 107
20.3.3.3.	*STATUTORY AUTHORITY FOR LIQUIDATION IN THE EVENT OF DEADLOCK AND DISSENSION*	107	- 111
20.3.3.4.	*LEGISLATIVE SILENCE WITH REGARD TO MEMBERS' INTER SE FIDUCIARY DUTIES*	111	- 113
20.3.4.	*JUDICIAL RECOGNITION OF THE CLOSE CORPORATION AS AN INCORPORATED PARTNERSHIP*	113	- 175
20.3.4.1.	*INTRODUCTION*	113	- 115
20.3.4.2.	*JUDICIAL TOLERANCE OF THE INCORPORATED PARTNERSHIP*	115	- 159
20.3.4.3.	*JUDICIAL RECOGNITION OF THE INCORPORATED PARTNERSHIP FOR WINDING-UP PURPOSES*	159	- 174
20.3.4.4.	*JUDICIAL RECOGNITION OF CLOSE CORPORATORS' INTER SE FIDUCIARY DUTIES*	174	- 175

CHAPTER VII:

JUDICIAL RECOGNITION OF THE INCORPORATED PARTNERSHIP AS THE QUASI-PARTNERSHIP COMPANY IN THE ENGLISH SYSTEM

21.1.	*INTRODUCTION*	176	- 181
21.2.	*THE QUASI-PARTNERSHIP COMPANY AND THE EXTREME REMEDY — CORPORATE DISSOLUTION*	181	- 219
21.2.1.	*INTRODUCTION*	181	- 182
21.2.2.	*THE STATUTORY JUST AND EQUITABLE WINDING-UP PROVISION*	182	- 186

21.2.3.	THE QUASI-PARTNERSHIP COMPANY CASE LAW	186	-	211
21.2.3.1.	SCOTLAND	187	-	192
21.2.3.1.1.	SYMINGTON	188	-	190
21.2.3.1.2.	THOMSON	190	-	192
21.2.3.2.	ENGLAND	192	-	202
21.2.3.2.1.	YENIDJE	193	-	196
21.2.3.2.2.	EBRAHIMI	196	-	202
21.2.3.3.	SOUTH AFRICA	202	-	211
21.2.3.3.1.	LAWRENCE	202	-	205
21.2.3.3.2.	MOOSA	205	-	211
21.2.4.	PROFILE OF THE INCORPORATED PARTNERSHIP	211	-	219
21.3.	THE INCORPORATED PARTNERSHIP AND THE MORE APPROPRIATE REMEDIES OF FIDUCIARY RESTRAINT	219	-	261
21.3.1.	INTRODUCTION	219	-	219
21.3.2.	THE CASE LAW	219	-	220
21.3.2.1.	SCOTLAND	220	-	228
21.3.2.1.1.	HARRIS	220	-	223
21.3.2.1.2.	SCOTTISH CO-OP WHOLESALE SOC.	223	-	228
21.3.2.2.	ENGLAND	228	-	246
21.3.2.2.1.	INTRODUCTION	228	-	231
21.3.2.2.2.	LEADENHALL	231	-	235
21.3.2.2.3.	PENNEL	235	-	240
21.3.2.2.4.	CLEMENS	240	-	246
21.3.2.3.	SOUTH AFRICA	246	-	261

21.3.2.3.1.	*INTRODUCTION*	246	-	249
21.3.2.3.2.	*SUPER SAFES*	249	-	251
21.3.2.3.3.	*BELLAIRS*	251	-	261

CHAPTER VIII

A COMPARATIVE ASSESSMENT OF THE PERSONAL CHARACTER OF THE INTER SE RELATIONS OF CORPORATE PARTNERS

22.1.	*INTRODUCTION*	262	-	264
22.2.	*THE CONTINENTAL APPROACH*	264	-	278
22.3.	*THE AMERICAN APPROACH*	278	-	288
22.4.	*THE ENGLISH PERSPECTIVE*	288	-	297

CHAPTER IX

SUMMATION AND CONCLUDING REMARKS

23.	*SUMMATION*	298	-	301
24.	*CONCLUDING REMARKS*	301	-	304

EXCURSUS I	**JURAL RELATIONS.**			
Part 1	*INTRODUCTION*	(i)	-	(ii)
Part 2	*THE VERTICAL OR NON-ASSOCIATIVE RELATION*	(ii)	-	(iv)
Part 3	*THE ASSOCIATIVE OR LATERAL RELATION*	(iv)	-	(vii)
Part 4	*SYMBIOSIS INVOLVING LATERAL AND VERTICAL RELATIONS*	(vii)	-	(viii)
Part 5	*CONFUSING LATERAL FOR VERTICAL RELATIONS*	(ix)	-	(xii)

EXCURSUS II	**INTUITUS PERSONAE**			
Part 1	*INTRODUCTION.*	(i)	-	(ii)

Part 3	*A HISTORICAL AND COMPARATIVE ASSESSMENT OF THE CONCEPT INTUITUS PERSONAE*	(ii)	-	(x)
ANNEXURE A				
Part 1	*NORTH CAROLINA CORPORATION ACT, 1955, § § 55-73(b)*	(i)	-	(i)
Part 2	*SOUTH CAROLINA CORPORATION CODE §§ 33-11-220*	(ii)	-	(iii)
Part 3	*DELAWARE GENERAL CORPORATION LAW, 1974, § 354*	(iv)	-	(iv)
Part 4	*PROPOSED STATUTORY CLOSE CORPORATION SUPPLEMENT, §§ 11(b)*	(v)	-	(vi)
Part 5	*CALIFORNIA CORPORATION CODE, 1975, §§ 300(b)*	(vii)	-	(vii)
ANNEXURE B				
Part 1	*COMPANIES ACT 1948 § 210*	(i)	-	(ii)
Part 2	*COMPANIES ACT 1980 § 75*	(iii)	-	(v)
Part 3	*R.S.A. COMPANIES ACT, 1973 § 252*	(vi)	-	(vii)
Part 4	*SOUTH CAROLINA CORPORATION CODE § 12-22.23*	(viii)	-	(viii)
Part 5	*PROPOSED STATUTORY CLOSE CORPORATION SUPPLEMENT, § 16*	(ix)	-	(xiii)
TABLE "A"	**PUBLIC AND PRIVATE LIMITED COMPANIES IN BRITAIN**	1	-	2
FOOTNOTES	1 to 1063	1	-	87

P R E F A C E

Partnership concepts have always permeated English company law thinking. The partnership notion of joint stock trading infiltrated the regulated company to turn it into the equitable joint stock company. In its turn, the lineal descendant of the equitable joint stock company, the present day incorporated company, is but a mutation of partnership. This is borne out by the very name "(incorporated) company". For there was a time, even in England, when *company* meant partnership as it still does on the Continent today.

In its original sense the word "company" referred to a French collective association of the Middle Ages consisting of several families combining to till the soil and to rear cattle together.[5] As the associates lived together and had their meals together they were called "companions". The word company was therefore to some extent indicative of a close and intimate relation which always has been and still is intimately associated with partnership.[6] In fact, as early as the thirteenth century the word *compahnia* was used in conjunction with the word *societas* (the Roman partnership) to distinguish it from the capital-based business organization of that time, the *commenda* (the forerunner of the *société en commandite* or limited partnership of today). Even in Britain partnership is still today sometimes referred to as a "company".[7] Otherwise than on the Continent, though, the term "company" is not frequently used in the sense of partnership any more. Nevertheless the term "incorporated company" today is also used to denote incorporated partnership in the British Isles. One commentator for instance, in discussing the effect which the statutory prohibition found in the earliest major company legislation in England had on large (*i.e.* public) partnerships, concludes:

> "There was thus introduced into the law beside the corporation and the partnership a *tertium quid*, an incorporated partnership. Henceforth the joint stock

company/ .....

company, by substituting the single liability of the unit for the several liability of the members, became a legal person distinct from the sum of the members, and was therefore entitled to rank as a corporation".[8]

Lindley, the original author of the standard English work on partnership, states in similar vein:

"They [incorporated companies] are not pure partnerships, for their members are recognized as an aggregate body; nor are they pure corporations, for their members are more or less liable to contribute to the debts of the collective whole. Incorporated companies are intermediate between the corporations known to the common law and ordinary partnerships, and partake of the nature of both; and the law relating to these companies depends as well on the principles which govern ordinary partnerships, as on those which are applicable to corporations strictly so called".[9]

Subsequently, a New South Wales court judicially underwrote these sentiments, saying:

"[I]t is necessary to remember that ... a company is a hybrid growth. It is a partnership which has been invested with the character of incorporation, and the rules which are applicable are partly referable to both characters".[10]

From its corporation ancestor the incorporated company inherited notions developed with regard to third parties. These notions are, in particular, those relating to limited liability. From its partnership ancestor the incorporated company inherited notions developed by equity with regard to the conduct of

associates/ .....

associates in their inter se relations. These notions are, in particular, those concerning the dissolution of a partnership where mutual co-operation is no longer possible and when inter se confidence has been destroyed.

Although there is ample proof that the English statutory company is in fact an incorporated partnership, it is the public partnership which has been the focal point of legislative attention in this regard. While English company legislation has developed around the outsize public partnership, the needs of the private partnership have been overlooked. In short, whereas the State conceded corporate personality to the public partnership in the middle of the nineteenth century, the private partnership is still struggling to attain that status.

The statutory recognition of the private (incorporated) company in 1907, which permitted associations of less than seven members to incorporate, provided an escape from this unsatisfactory situation for the private partnership. Henceforth, the members of a private partnership desiring corporate status could attain it by simply incorporating as a private company. Thus a further *tertium quid* — a further hybrid, this time the private incorporated partnership, the incorporated partnership proper — came into being.

Today the de facto existence of the incorporated partnership proper — herein later referred to as the incorporated partnership — is no longer a matter of debate. Thus for instance the incorporate partnership has been identified as a "partnership working in a corporate shell" and as an "enterprise which is economically a partnership though working in a protective company shell".[11] At the same time the need to create separate facilities for the incorporation of this type of enterprise has not gone unnoticed.[12]

The/ .....

The debate today concerns the character of the inter se relation of members of the incorporated partnership. The question, in a nutshell, is when and to what extent the appropriate principles of equity, developed over many centuries in respect of partners proper, should be applied to members of an incorporated partnership. These are the issues which will be canvassed in this dissertation.

It is customary for an author to indicate in his preface what elements in his thesis should be considered contributions to original knowledge. I believe that I have in this thesis demonstrated that the company type which the judiciary in the English system refers to as the "quasi-partnership" or "domestic company" is in fact the incorporated partnership as identified herein. I also believe that I have shown that under English, Scots and South African law, corporate partners stand in a personal fiduciary relation to one another, that the said character of the relation gives rise to inter se fiduciary duties; that the general recognition of this proposition by the judiciary is now imminent, and that such recognition has been long overdue. I have endeavoured to show that the personal fiduciary character of the said relation arises from the fact that the said relation has been concluded *intuitu personae* as opposed to *intuitu pecuniae*, both of which concepts I have borrowed from French jurisprudential writing. I also believe that in line with American jurisprudential writing I have managed to illustrate that, in the English system too, the existence of corporate status and the operation of inter se fiduciary duties are not mutually exclusive phenomena. All these, ideas as well as the concept of associative, lateral or horizontal, jural relations (as opposed to vertical jural relations) as developed in Excursus 1, I believe to be original. I trust that the said ideas will also qualify as and will prove to be contributions to knowledge.

In/ .....

In terms of the theses requirements of McGill University, the following historical statement of previous relevant work is included:

(i) *The Fiduciary Duty Concept and the Multi-National Enterprise - A Comparative Analysis:*

South African Chartered Accountant

("S.A.C.A.")	June	1976	Volume 12	no. 6,	203;
S.A.C.A.	July	1976	Volume 12	no. 7,	239;
S.A.C.A.	August	1976	Volume 12	no. 8,	276;
S.A.C.A.	September	1976	Volume 12	no. 9,	319;
S.A.C.A.	October	1976	Volume 12	no. 10,	345;
S.A.C.A.	November	1976	Volume 12	no. 11,	388;
S.A.C.A.	December	1976	Volume 12	no. 12,	433;
S.A.C.A.	February	1977	Volume 13	no. 2,	53;
S.A.C.A.	March	1977	Volume 13	no. 3,	87;
S.A.C.A.	June	1977	Volume 13	no. 6,	189;
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referred to by Rider, *Partnership Law and its Impact on "Domestic Companies"*, (*infra* n. 323) at 158 nn. 56 & 58;

(ii) *Close Corporations: Donahue v. Rodd Electrotype Co. and the Fiduciary Duty Obligation to offer equal participation in Redemption of Stock in the Close Corporation* - De Rebus Procuratoriis 1977 no. 113, 247 *referred to by* Cilliers, Benade & De Villiers, *Company Law*, (*infra* n. 198) at 529 n. 15;

(iii) *Legal Personality and Partnership - Quo Vadis?* Codicillus Volume XIX no. 1, 7 and no. 2, 18, Volume XX No. 1, 25, *referred to by* Hosten *et al.*, *Introduction to South African Law and Legal Theory* (*infra* n. 76) at 532 n. 155.

MONTREAL, 13th August, 1981.

D S RIBBENS

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§§16(b)(10)	486
§17	461

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	Footnote
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	Footnote
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	Footnote
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C

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D		
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1.	Statute	
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E		
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	An Act to repeal so much of an Act passed in the Sixth year of His late Majesty King George the First, as relates to the restraining several extravagant and unwarrantable Practicess	

	Footnote
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§2	221, 242
§25	219, 229
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§8	225
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§3	235
§4	239
§5	236
§7	232
§9	228
§10	232
§13(2)	229
§39	238
§61	231
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§37	276
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	Footnote
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§2	279
§§26(3)	282
§79	715
§§79(5)	702, 737
§121	276
Companies Act, 11 & 12 Geo. 6, c. 38 (1948)	178, 247, 714
§§1(1)	235, 280
§§2(1)(a)	236
§8	228
§§13(2)	219, 229, 827
§§20(1)	232
§§28(1)	277
§31	238
§127	283
§129	283
§210	480, 863
§§212(1)(d)	231
§§222(a)	716
§§222(c)	716
§§222(e)	716
§§222(f)	233, 697
§434	239
§§455(1)	249
Companies Act, c. 81 (1967)	179
§2	283
§120	239
Companies Act, c. 22 (1980)	180, 260, 312
§1	285
§§1(1)	287, 288
§§2(1)	290
§75	480
§85	289
§§87(2)	289
§§88(2)	286, 291
4th Schedule	286
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	Footnote
PARTNERSHIP	
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§§1(1)	61-63
§§1(2)	67
§4	167,171, 279
§§24(7)	1105
§28	69
§29	69, 108, 126
§30	69, 126
§§35(d)	118, 471
§§35(f)	471, 698, 701, 708
§46	68
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§3	297
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discussed in (1971) Sol. J. 202-203 and *noted in Ebrahimi, supra* by Lord Wilberforce at 378 and *by* Lord Cross at 387	878-883, 903, 913, 1052
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EUROPEAN LAW

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F		
	FRENCH LAW	
1.	Statute	
	Loi no. 66-537 of July 24, 1966	351
2.	Judicial Decisions	
	COUR DE CASSATION	
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G	GERMAN LAW	
1.	Statute	
	R.G. Bl. 477, April 20, 1892	324
2.	Judicial Decisions	
	R.G. 146	959
	R.G. 158	959
	R.G.D.R. 40	960
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R

ROMAN LAW

1. Imperial Code

Code 4.37.3	99, 100, 911
Digest 3.4.7.1	149
17.2.4.1	92
17.2.5	29
17.2.6	85
17.2.14	92
17.2.29.pr.	98
17.2.59	1094
17.2.63.	82, 990
17.2.65.pr	87
17.2.65.3	93
17.2.65.4	773
17.2.65.5	96, 108, 121, 128, 929, 994
18.1.35.1	85
50.17.202	41
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SCOTS LAW	
1. **Judicial Decisions**	
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SOUTH AFRICAN LAW

1. Pre-Union Statutes

COMPANY

Cape Joint Stock Companies Limited Liability Act, No. 23 of 1861 — 186

Joint Stock Companies Limited Liability Act No. 10 of 1864 — 189

De Akte van Maatschappijen met Beperkte Verantwoordelijkheid No. 5 of 1874 — 190

De Wet Over Beperkte Verantwoordelijkheid van Naamloze Vennootschappen, C. C Orange Free State, 1891 — 191

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Companies Amendment Ordinance, No. 24 of 1904 — 193

Companies Amendment Ordinance, No. 31 of 1909 — 194

PARTNERSHIP

Special Limited Partnership

Special Partnerships Limited Liability Act, 1861, No. 24 of 1861 (Cape) — 296

Special Partnerships Limited Liability Act, 1864, No. 1 of 1864 (Natal) — 296

2. Post-Union Statutes

COMPANY

Companies Act 1926, No. 46 of 1926 — 196
§§26(2) — 282

3. Republican

COMPANIES

The Companies Act, 1973, No. 61 of 1973, — 199, 703
§§1(1) — 250
§§20(1) — 278
§30 — 239
§§30(2) — 239
§31 — 239
§32 — 235, 281

	Footnote
§§49(1)(a)	236
§§65(1)	219, 229, 827
§§65(2)	232
§66	232
§92	231
§173	283
§§302(4)	283
§§344(e)	714
§§344(f)	716
§§344(h)	233, 704

STATUTORY COMMISSION REPORT

The Van Wijk - De Vries Report, R.P. 45/1970	284

OTHERS

Pre-Union Statute Law Revision Act, No. 36 of 1976	296

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N		
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1.	Judicial Decision	
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CHAPTER I

INTRODUCTION

1. *PURPOSE AND SCOPE*

The ultimate object of this dissertation is to establish to what extent it is permissible to apply notions of exemplary conduct developed in relation to partnership proper to members of an incorporated partnership in their dealings with one another. This in effect amounts to enquiring whether and why members of an incorporated partnership inter se stand in a fiduciary relation giving rise to reciprocal fiduciary duties of the highest order.

Essential to the attainment of the above-formulated object is the ascertainment of a more or less precise meaning of a number of concepts which are central to the main theme of this dissertation. Here satisfactory answers are for instance required to questions such as: what is a partnership proper? Why do partners inter se owe fiduciary duties? Are such duties in any way dependent on the fact that partners are usually also mutual agents? What obligations are imposed on partners in terms of such duties? In what respects does a partnership proper differ from an incorporated company? What is legal personality and what effect does it have on the inter se relations of members? Why are partnerships proper incorporated as private companies instead of, for instance, being converted into limited partnerships? Can a statutory private company be regarded as a partnership and under what circumstances? Is a fiduciary relation compatible with incorporation and can the former survive the latter?

Once the answers to these questions are obtained, a meaningful analysis of the English, Scottish and South African "just and equitable winding-up line" of cases — those cases in which the judiciary has recognized the incorporated partnership under the

name/ .....

name of the quasi-partnership company — can be undertaken. Here it will be observed that courts in various jurisdictions have not hesitated to give de jure recognition to the de facto existence of the incorporated partnership, albeit only in the narrow context of determining whether it is just and equitable that the particular company should be wound up. Here the endeavour will be to show that the true *ratio decidendi* of these decisions is that the courts, in decreeing a winding-up of the company when the inter se relations of its members have broken down, recognize the personal and fiduciary character of the inter se relations enjoyed by members of incorporated partnerships. It will further be shown that there is no reason why effect should be given to that particular character of the relation in question only in the context of the statutory just and equitable winding-up provision.

It seems obvious that if in fact the inter se relation of members of the incorporated partnership is a personal or fiduciary one, it should be recognized that, as in partnership proper, such a relation gives rise to inter se fiduciary duties between members of an incorporated partnership too. As a sequel it must follow that in less serious conflict situations — those for instance not involving a breakdown of relations between members — courts should apply the less drastic or extreme remedies of fiduciary restraint. These would include the setting aside of resolutions passed by members in breach of their inter se fiduciary duties, the rescission of contracts involving the purchase by one member of the shares of another without full disclosure of information relevant to the transaction, the accounting of profits in the case of the interception of a corporate opportunity by a member, etc. It will be shown that there are dicta in Scottish, South African and, to some degree English decisions supporting these conclusions. In order to delineate the scope of the enquiry about to be undertaken more closely, it is necessary to stress that this dissertation is not concerned with the fiduciary duties owed by corporators, *qua*

directors/ .....

directors, to their company. Such fiduciary duties differ from the fiduciary duties to be investigated in this dissertation in a number of ways. First, they are essentially one-way duties, that is they are non-reciprocal and are owed by the director to the company and not also by the company to the director. Second, as is shown in Excursus I hereto, they flow from vertical or non-associative relations (trust or agency for instance) as opposed to lateral or associative relations (partnership for instance). The significance of this distinction is that it seeks to distinguish between those situations where a corporator acts *qua* director, (*i.e.* in a representative capacity on behalf of the company) and those where he acts as member (*i.e.* as principal in his own right).

This dissertation is also not concerned with the question whether corporators, *qua* directors, do or do not owe fiduciary duties to their fellow corporators, *qua* members of the company. Likewise, the generally accepted notion that members of public-issue companies and even those of most private companies do not owe inter se fiduciary duties, will not be questioned.

This dissertation is concerned with the question whether members of an incorporated partnership, *qua* members, inter se stand in a lateral fiduciary relation to one another, and as such owe reciprocal fiduciary duties to one another. This dissertation further aims at establishing what the particular incidents of such relations are. In partnership proper the lateral fiduciary relation gives rise not only to reciprocal fiduciary duties of the highest order — duties which are not founded on agency — but also, if the relationship breaks down, to the very termination of the association itself. Here the crucial question is to what extent that relation and its characteristic incidents co-exist with corporate personality, that is, to what extent that relation remains operative in the incorporated partnership.

2. *APPROACH*

The approach adopted with regard to the relevant issues will be both comparatively and historically oriented. Here only some of the more salient aspects of the advantages of such an approach will be underscored.

It is widely acknowledged that there are those fields of law where there can be no progress without history.[13] How true this is of English company law is illustrated by Gower[14] who, after remarking that there are some branches of modern English law which cannot be properly understood without reference to their historical background, states:

> "[A]nd company law is certainly one of them: indeed of all branches of the law it is perhaps the one least readily understood except in relation to its historical development...."[15]

In fact, the neglect in English law up to the present of the incorporated partnership is to a major extent due to indifference to the historical background of the incorporated company and the factors which gave rise to it. For this reason the endeavour in this dissertation will be to trace the development not only of the incorporated company and partnership as such, but also of the basic association type from which they evolved, namely, partnership.

For the sake of perspective and the further advantages which comparative analysis brings[16], the development of particular legal institutions, traditions and rules in a particular legal system will be contrasted with the corresponding development in at least one other system. So for instance, the English partnership will be studied and compared with the Scots and South African partnership against the backdrop of the Roman *societas*. In this way a better understanding of certain problem areas will be obtained. The

question/.....

question whether partnership is a contract or a mere relation, is the one such issue. Roman lawyers regarded *societas* as a relation while Civilans treat it as a contract. English law again treats partnership as a relation. Comparative and historical analyses explain this phenomenon.[17] Another issue is whether partners should be permitted to exercise contractual rights without considering the legitimate interests of their co-partners. Roman law required *socii* to observe the utmost *bona fides* unto one another and consequently did not permit the unbridled exercise of contractual rights in the *societas*. English law following Roman law similarly requires partners to observe the highest good faith and does not permit contractual rights to be exercised unconscionably in the partnership. It is on this basis that the unconscionable exercise by members of an *incorporated* partnership of their statutory and contractual powers of expulsion has in English law been held to be wrongful, justifying the winding-up of the statutorily created incorporated partnership.[18] A further, and more difficult question, is why partners owe fiduciary duties and what the scope and purpose of such duties are. Here, in particular, comparative analysis is indispensable.

For similar reasons the private company[19] in the English system (for present purposes England, Scotland and South Africa) will be contrasted with the American close corporation[20] and with the Continental type namely the German G.m.b.H.[21] and the French S.à.r.l.[22] Here the focal point will be the character of the inter se relation of members. What is of particular interest in this regard is the remarkable progress that has been made by American courts in a relatively short period of time in recognizing the partnership-like nature of the inter se relation of members of a close corporation. Indeed in a number of decisions it has in fact been held that the members of a close corporation inter sese owe the same fiduciary duty as that owed

by partners proper inter sese![23] What is particularly remarkable in this regard is that, unlike the English company, the American business corporation has not developed from the (public) partnership concept and[24] a rigid concession theory fetters courts in their approach to corporation law. Thus the question must be posed why the English, with their more flexible company law approach fail to recognize the incorporated partnership for what it is, namely a partnership enjoying the statutory benefits of incorporation. To do so would, after all, require no great ingenuity for, as will be shown to be the case, the English incorporated company is in fact but a partnership endowed with corporate personality. What is more, the English have without wanting to admit it, already recognized the personal character of the incorporated partnership for the purposes of the more extreme remedy, that of winding-up. This raises the question why does English law not, like American, and for that matter, German law, recognize the personal character of the incorporated partnership for the less drastic remedies of fiduciary restraint. If valid reasons exist in the English system why members of the incorporated partnership cannot owe fiduciary duties in the same way as their counterparts in the American close corporations and to some extent in the German G.m.b.H., a comparative study should reveal what such reasons are.

3. *OUTLINE*

This thesis comprises nine chapters. Chapter II is titled "The Partnership Idea". It deals with three basic issues: partnership as an associative relation, the fiduciary character of the partnership relation inter se and the status of the partnership relation *vis-à-vis* third parties.

Chapter III sketches the broad outlines of the British Company regime with particular reference to its application in Scotland

and/.....

and the Republic of South Africa. Chapter IV traces the evolution of the incorporated public company in the British system. It also considers the meaning of the term "company" as used in the *Companies Act*. Chapter V again traces the evolution of the incorporated private company in the British system and the relation between that company type and partnership proper. Chapter VI considers the development and status of the incorporated partnership in the United States and on the Continent respectively. Here the endeavour is to establish to what extent partnership principles, and in particular partners' inter se obligations of good faith and confidence, are found in the American close corporation, the German G.m.b.H. and the French S.à.r.l. respectively. Against this background the case law in the English system dealing with the incorporated partnership is analysed in Chapter VII. Here the incorporated partnership has in the main been recognized as the quasi-partnership company for purposes of winding it up under the statutory just and equitable winding-up provision. Chapter VIII assesses the personal fiduciary character of the inter se relations of corporate partners on a comparative basis. Chapter IX contains a summation and conclusions.

Two cardinal issues, jural relations and *intuitus personae*, are dealt with in Excursus I and II respectively.

CHAPTER II

THE PARTNERSHIP IDEA

4. *PRELIMINARY*

Partnership is possibly one of the oldest commercial institutions known to man. Its history goes back to early Roman law days and perhaps even earlier. Over the ages the notion developed that partners are bound to display to one another the highest good faith and loyalty. It is not without significance that the classical consensual *societas* which was developed by the Roman chancellors from the rigid consortium of co-heirs[25] was an institution of the *jus gentium*, that is the law of nations as opposed to the *jus civile* or civil law which only applied to Roman citizens.

Commerce took the Roman *societas* to the far corners of the Roman Empire. Both because of its geographical dispersal and because of the universal application of its concepts developed over many centuries, the Roman law *societas* has had a powerful influence on the development of the Common Law partnership. "The English Law of Partnership" as Scrutton[26] observes, "is derived from three sources, the Common Law, the *Lex Mercatoria*, and the Roman Law."[27] Thus it is not surprising that Mr. Justice Story, who has made an elaborate and detailed study of the relation of the Common Law partnership to the Roman law *societas*, is able to find a great similarity between the two institutions.[28] Classical Roman law, for instance, classifies partnerships into universal partnerships, general partnerships and special partnerships or as they are now known, joint ventures.[29] The Common Law apparently still recognized a similar classification in the middle of the nineteenth century although the universal partnership was thought to be very rare.[30] Both Scrutton and Story agree, though, that the chief Common

Law/ .....

Law division at the time was between *private* and *public* companies or partnerships.[31] It is interesting to observe that the Civil Law follows somewhat similar division today by distinguishing between *sociétés de personnes* and *sociétés de capitaux*.[32] As will be observed in Ch. IV hereunder, the term "company" has in the English system acquired the connotation of a statutory or an incorporated company which, in turn, may either be a public or a private company, both of which concepts are now statutorily defined. At the same time, the concept private partnership is more usually rendered by the abbreviated term "partnership" or sometimes "partnership proper",[33] a term which will be used throughout this dissertation.

Partnership is in essence an associative or lateral relation.[34] As such it occupies a fundamental position in the hierarchy of associative relations.[35] The idea of partnership in its broadest sense is, not surprisingly, a basic theme which recurs in a variety of forms of business organization.[36] Despite opinion to the contrary, partnership is however not agency[37] — the former is an associative or lateral relation, the latter a non-associative or vertical relation. This distinction is of great importance especially when a partnership is treated as a legal person, that is a legal right-and-duty bearing unit[38], as in the incorporated partnership.

The Roman law *societas* was not viewed as a legal person. The notion of legal personality in partnership developed in Civil Law when, in the budding art of accountancy, partnership was treated as a separate entity distinct and apart from the partners who comprise it. This essentially Civil Law development has not found favour in England where the monopoly in the creating of corporations has been jealously treasured as a royal prerogative.[39] The failure of the English private partnership to

attain/ .....

attain legal personality has led to partnerships being incorporated as private companies and eventually to the evolution of the incorporated partnership.

The essentially Roman law notion that the partnership relation was one of the utmost good faith became in Common Law that partnership was a fiduciary relation giving rise to fiduciary duties of the highest order. Legal personality and inter se fiduciary relations are, however, not mutually exclusive as is shown by Scots Law.

5. *PARTNERSHIP AS A RELATION*

5.1. *INTRODUCTION*

In any legal analysis, the starting point must be the isolation of the specific legal relations involved.[40] This is particularly apposite to the law of associations in general and the law of partnership in particular. For in the final analysis the essence of a partnership in most legal systems is that it is an associative relation. This will become apparent from the brief survey about to be undertaken. Here various definitions of partnership will be considered with a view to providing a better appreciation of that concept throughout this dissertation, and in particular in Ch. VIII. A particular reason for establishing whether an associative relation constitutes a partnership, is to be able to determine whether the relation in question is such that the principles of equity, which have been developed in relation to partners over many centuries, are applicable to the persons who are associated in such relation.

5.2. *ROMAN LAW*

Either because Roman jurists did not feel the need for it, or as seems more probable, because they felt that they were unable

to/ .....

to formulate an abstract definition — *omnis definitio in jure civile periculosa est*[41] — there seems to have been no attempt to define *societas* in classical or later Roman Law.

In Roman law a *societas* was merely a *vinculum juris*, that is a (lateral) legal relation. *Societas* was a consensual contract which governed the obligations of the *socii*[42] in terms of which the *socii* mutually bound themselves to certain acts with a view to some common object.[43] As far as third parties were concerned, only the *socii* existed, not the *societas*. Owing to the undeveloped state of the Roman Law of agency, a contract made by a *socius* in the course of common business, subject to some qualifications, affected only the *socius* himself; he alone was liable to the third party and he alone had the sole right against such third party.[44]

That the Roman jurist saw *societas* simply as essentially an inter se relation cannot be stressed enough, particularly in view of the source from which the fiduciary obligation and duty in partnership is supposed to arise. "Since ... mutual agency of partners did not exist in Roman Law", Gladstone points out "the chief concern was with the relation of the partners inter se ...."[45]

5.3. *SOUTH AFRICAN LAW*

South African Partnership law, unlike that of Britain and other Commonwealth countries, is not codified and is found inter alia in the works of common law[46] authors such as the Roman-Dutch jurist Voet and the French jurist, Pothier.

These jurists, unlike their Roman predecessors, did not hesitate to define partnership. In doing so in true Civilian fashion[47] they described partnership in terms of a contract rather than

a relation. For instance, Pothier[48], who is known for the considerable authority he commands in Common Law jurisdictions as well, emphasizes the contractual element of partnership in the following definition:

> "*Le contrat de société est un contrat par lequel deux ou plusiers personnes mettent, ou s'obligent de mettre, en commun quelque chose, pour faire en commun un profit honnête, dont ils s'obligent réciproquement de se rendre compte* ".[49]

The element of good faith comes to the fore again when, on another occasion[50], he defines partnership in these terms:

> "*Societas est contractus de conferendis bona fide rebus aut operis, animo lucri quod honestum sit ac licitum in commune faciendi* ".[51]

Partnership is viewed in very similar vein by the Roman-Dutch author Voet[52] who defines it as follows:

> "*Societas est contractus juris gentium, bona fidei, consensu constans, semper re honesta, de lucri et damni communione*".[53]

The Roman-Dutch partnership, despite the prominence afforded to the contractual aspect thereof in the above definitions, is nevertheless still a relation. This appears clearly from the comment Morice[54] passes on the relation between the English and Roman-Dutch notion of partnership when he observes:

> "The Roman-Dutch definition of partnership (variously called *societeit, vennootschap, maatschappij* or *compagnieschap*) does not materially differ from the English, although it lays more stress on the contract than the relation between the parties produced by the contract".[55]

5.4./ .....

5.4. *SCOTS LAW*

The Roman and Civil Law influences on the development on the law of partnership in Scotland are undeniable.[56] After the Act of Union with England of 1707 the Common Law began to influence the development of partnership in Scotland.[57] Noticeable in the writings of the earlier authors on partnership is the Continental usage of "company and partnership" as synonomous terms. Although the passing of the *Partnership Act*, 1890[58] did much to foster the assimilation of English and Scots partnership law, important areas of divergence remain,[59] the most important of which, as will be observed in para 7.3. hereunder, concerns the status of partnership as a legal entity.

In keeping with the Civil Law tradition, partnership is defined by Erskine, a Scottish jurist of the eighteenth century as a "[C]onsensual contract ... by which the several partners agree concerning the communication of loss or gain arising from the subject of the contract".[60]

In 1890, however, the British Parliament reframed the definition of partnership in Scots Law when it introduced a new statutory definition of partnership for the whole of the United Kingdom including Scotland in *Partnership Act*, 1890,[61] § 1(1).

5.5. *ENGLISH LAW*

The *Partnership Act*, 1890,[62] §§ 1(1), in true Common Law tradition defines partnership as a relation rather than a contract. This statute begins as follows:

> "Partnership is the relation which subsists between persons carrying on business in common with a view to

profit/.....

profit ".[63]

This statutory definition caused the eclipse of the term *quasi-partnership* in the sense in which it had been understood and used up to then, namely as connoting a relation between partners and a third party.[64] However, as will presently be observed, the said statutory definition does not at the same time pretend to be exhaustive: *Partnership Act*, 1890 *§§* 1 (2) clearly provides that certain specified associative relations, which would otherwise have fallen within the ambit of the statutory definition, are nevetheless not partnerships under the *Partnership Act*, 1890. To the extent that such other relations comply with the common law definition of partnership, they will be common law partnerships.

With regard to the relation between the said associative relation *viz.* partnership on the one hand, and the contract giving rise to it on the other, *Lindley* correctly maintains that, although partnership is often called a contract, it is not the contract itself but the resulting relation.[65] "The statutory definition", *Lindley* further points out, "does not state from what the relation arises, but that an agreement, *express* or *implied*, is the source of the relation was clearly established before the Act and may be inferred from its provisions".[66] As will be observed, the fact that the relation may flow from an implied agreement is of immense significance for the incorporated partnership or, as the judiciary prefers to call it, the quasi-partnership company.

Whatever the source of the said associative relation may be, it is clear that partnership, as defined above by the English legislature in *Partnership Act*, 1890, *§§* 1(1), is an extremely wide concept, capable of embracing almost all associative relations from the corporation at the pinnacle of the hierarchy to the lowest order of associative relations, with the possible

exception/ .....

exception of the passive group holding. The correctness of this interpretation is borne out by the very language the legislature goes on to use in *Partnership Act*, 1890, §§ 1 (2). In order to ensure that the statutory provisions of the *Partnership Act*, 1890, would not apply to the whole spectrum of such further relations, the legislature found it necessary to qualify the above-quoted statutory definition of partnership. Thus a rider to *Partnership Act*, 1890, §§ 1 (1) provides:

> "But the relation between members of any company or association which is -
>
> (a) Registered as a company under the Companies Act 1862 or any other Act of Parliament for the time being in force and relating to the registration of joint stock companies; or
>
> (b) Formed or incorporated by or in pursuance of any other Act of Parliament or letters patent, or Royal Charter; or
>
> (c) A company engaged in working mines within and subject to the jurisdiction of the Stannaries:
>
> is *not* a *partnership within the meaning of this Act* ".[67]

It is clear from the italicized words that what the legislature has done here is merely to say that the relation among the members of any of the mentioned associations, be they companies, corporations or anything else, *will not constitute a partnership within the meaning of the Partnership Act*, 1890, and will consequently not be governed by its provisions, that is, it will not be a statutory partnership. The reasons for this provision are obvious. Partnerships are best regulated in a statute dealing exclusively with partnerships. Likewise, other

lateral/ .....

lateral relations which are not partnerships are best regulated by specialized legislation tailored to the needs of that particular form of business organization.

At the same time, the legislature does not state that the inter se relation of the members of incorporated companies or corporations cannot constitute a partnership at common law as opposed to a statutory partnership under the *Partnership Act*, 1890. Here it must be borne in mind that the statute in question is not a code and that pre-statute decisions may still be authoritative in proper circumstances. In fact the said statute specifically provides that "[t]he rules of equity and of common law applicable to partnership shall continue in force except so far as they are inconsistent with the express provisions of this Act".[68] Thus although the legislature has enacted specific provisions with regard to the duty of partners not to compete with the firm, to render accounts etc. and the accountability of partners for private profits, it has never been doubted that the rules of equity with regard to partners' fiduciary duties developed prior to the enactment of *Partnership Act*, 1890, remain authoritative.[69]

The pre-statute common law definitions of partnership are obviously in like fashion authoritative with regard to those associative relations which do not fall within the statutory definition of *Partnership Act*, 1890, § 1 and which are consequently not governed by the said statute. Of these earlier definitions two are apposite in the present context. According to Rutherforth partnership exists, "[w]hen two or more persons join money, or goods, or labour, or all of these together and agree to give each other a common claim upon such *joint stock* ...."[70] And in 1890 Pollock, the author of the *Partnership Act*, 1890, defined partnership as "the *relation* which subsists between persons who have agreed to share the profits of a business carried on by all or any of them on behalf of all

of/ .....

of them".[71] Pollock formulated this definition in order to meet the objection that a person cannot be a partner unless he has a direct and principal interest in the business, that is unless the business is conducted on his behalf.

In terms of these definitions the relation between members of a statutory company could in fact qualify as partnership proper at common law. Such a relation would, it is submitted, so qualify if the company concerned is an incorporated partnership, that is if it is concluded *intuitu [delectu] personae* — for which see Excursus II.

6. *THE CHARACTER OF THE INTER SE RELATION*

6.1. *INTRODUCTION*

The character of the inter se relation of partners is central to the theme of this dissertation. Its significance is explained by the willingness of twentieth-century courts to turn to "principles of equity developed in relation to partnerships"[72] in order to resolve conflicts between members of *incorporated* companies.

The tradition whereby the inter se conduct of partners is characterized by the most scrupulous good faith has stood the test of time. Conceived in Roman law two millennia ago it has since spread and been adopted in most legal systems. Thus it is today widely acknowledged that the essence of the associative relation, partnership, is mutual confidence, and, inseparable therefrom, good faith. A Civilian authority confesses to that in these terms:

> "Each partner contributes not only a share of the capital necessary but also his reputation, his abilities and individual experience. The association is based essentially on mutual confidence ".[73]

And/ .....

And the Common Law agrees. "The foundation-stone of the partnership edifice", echoes Underhill, referring to the Common Law partnership, "is mutual confidence".[74] Here Underhill is, of course, referring to partnership proper, not the outsize or gigantic partnership or, as Story calls it, the public company. Indeed, the fundamental distinction between these two categories of partnership hinges on this very concept of mutual confidence and good faith. So for instance, partnership proper is described by *Lindley*[75] as consisting "of a few individuals known to each other" who are "bound together by the ties of friendship and mutual confidence" and are consequently "not at liberty without the consent of all to retire from the firm and substitute other persons in their places". In contra-distinction thereto, the now outlawed unincorporated public company — for which see Ch.IV para.11 hereunder — "consisted of a large number of individuals not necessarily nor indeed usually acquainted with each other at all so that it was a matter of comparative indifference whether changes amongst them were effected or not".[76]

To what is this distinctive feature of partnership proper traceable? On proper analysis it will be found to be traceable to *intuitus personae* or, as it is known in Common Law, *delectus personae* — for which see Excursus II — a concept which, according to Bell is "inseparable from the nature of a contract of such exuberant trust".[77]

6.2. ROMAN LAW

A *socius*, in Roman law was a companion, comrade, fellow or ally. Consequently one should see the Roman *societas* rather as a personal relation involving co-operation between companions as opposed to an impersonal arms' length relation in which the personal element is over-shadowed by factors such as weight of numbers (*i.e.* a large body of members) or amassed capital.[78]

A/ .....

A *societas* was created *intuitu personae*, that is between specific *socii* and no one else, and therefore the *socii* were supposed to have confidence in each other,[79] so much so that the *societas* lasted only as long as those particular *socii* were members of it. Death or retirement of any of the *socii* automatically terminated the *societas*.[80]

What is more, *societas* was as a consensual contract a *bonae fidei negotium*, with the result that "both parties were bound to do not merely what they promised to do ... but ... also ... to do whatever is involved in the requirements of bona fides".[81] Moreover, because it developed from the ancient consortium of co-heirs (the pre-classical *ercto non cito*), *societas* right from the outset involved a certain *fraternitas* — *societas jus quodam modo fraternitas in se habeat* —[82] which corroborated the idea of *bona fides* in partnership.[83] Thus Daube, with reference to this *jus fraternitas*, deprecates overreaching between *socii* in these terms:

> "*Socii* no doubt are not merely 'hostile' parties like buyer and vendor, each being bent on getting the utmost out of the other: they are 'friends' [brothers], as against third parties".[84]

The underlying concept of fairness which pervaded *societas* made it possible for prospective *socii* to agree that their respective shares in the to-be-concluded *societas* could be determined by one of them.[85] Because such a determination, if unfair, could and would be adjusted to conform with what fairness required, a stipulation to that effect was, unlike a comparable stipulation between buyer and vendor, with regard to the purchase price of the *res vendita*, not void for vagueness.[86] At the same time the institution by a *socius* of the *actio pro socio* (action on the firm) normally terminated the *societas*[87] because, as

Buckland/ .....

Buckland puts it, "litigation and fraternity do not go well together."[88] This idea of brotherly fairness naturally dictated that the *beneficium competentiae* be available to a *socius* if his fellow *socius* obtained a judgment against him.[89] In terms of the "benefit of competence" the liability of the *socius* debtor was held to be limited to the value of his property.[90] Some of the dictates of this brotherly fairness have since fallen by the way-side, others have survived to this day.[91]

Because of these notions of confidence, good faith and fairness, no overreaching by one *socius* of another would be suffered. This approach was strictly observed with regard to the voluntary termination of a *societas*. Thus, although any *socius* could at any time, by giving notice to that effect, dissolve a *societas* which was not contracted for a specific period[92], and thus terminable at will, no *socius* could ever do so, if his purpose was to serve his own selfish interest thereby. Renunciation had to be in good faith and not at an unseasonable time, that is, *bona fide et tempestive*.[93] Renunciation was not *bona fide* when a *socius* renounced in order to appropriate to himself alone the profit the *socii* had proposed to make when they entered into *societas*.[94] Renunciation would be *intempestiva* if made at a time when things no longer remained in *statu quo*, and when it was in the interest of the *societas* to wait for a more favourable time to complete the business of the *societas*.[95] And in order to judge whether a renunciation was made *intempestiva*, it was necessary to consider the common interest of the *societas* and not the private interests of an individual *socius*: *semper enim non id, quod privatim interest unius ex socius, servari solet, sed quod societati expedit.*[96] Where the contractual power of renunciation was exercised *mala fide* or *intempestiva*, the renunciation was regarded as void and the miscreant *socius* was compelled to account for his ill-gotten gain.[97] The notions of confidence, good faith and

fairness/ .....

fairness, were obviously also concerned with the inter se relations of members *stante societate*. So for instance each *socius* was to receive his rightful[98] share of profits earned in the normal course of the affairs of an on-going *societas*. This is only to be expected: *"cum in societatis contractibus fides exuberet ...."*,[99] that is since absolute good faith was expected to govern partnership in all its facets.

Story is entirely correct when, summing it all up, he concludes that the Roman law expressed the *obligation of good faith* in exceedingly strong language.[100] What should be noted though, is that the idea of an *obligation* of *good faith* had not yet been recognized as a *fiduciary duty*. This refinement was to take place centuries later in English law And in this context it should always be remembered that the Roman idea of confidence, good faith, fairness and loyalty in partnership developed in the absence of the concept (mutual) agency in partnership law. This latter concept was only developed many centuries later during the Middle Ages.[101]

6.3. *ENGLISH LAW*

Most of the notions developed in Roman law regarding the personal character of the inter se relation of partnership are found in English law, where they have been given new thrust and impetus and courts have developed them to their logical conclusion. Thus the principle of good faith is acknowledged by *Lindley* to be the basis of the law of partnership insofar as it relates to the rights and obligations of partners inter se.[102] Good faith gives rise to fairness. *Lindley* therefore refers to the "obligation to perfect fairness"[103] which subsists between partners and Underhill to the "obligation of each partner to observe the utmost fairness and good faith to his fellows".[104]

Thus/ ....

Thus if a partner should stand to be accused that he has sought to benefit himself at the expense of the partnership he "will be required to show, not only that he has the law on his side, but that his conduct will bear to be tried by the highest standard of honour".[105] Likewise, no agreement will be permitted to stand whereby a partner enjoying superior knowledge about the state of the partnership business sells, without proper disclosure, his interest in the partnership to a less informed co-partner.[106] On similar grounds the utmost good faith will be required to be observed when a power of expulsion is exercised.[107] *Lindley* explains the obligation of partners not to benefit themselves at the expense of their co-partners in these terms:

> "Good faith requires that a partner shall not obtain a private advantage at the expense of the firm. He is bound in all transactions affecting the partnership, to do his best for the common body and to share with his co-partners any benefit which he may have been able to obtain from other people and in which the firm is in honour and conscience entitled to participate: *Semper enim non id, quod privatim interest unius ex sociis, servari solet, sed quod societati expedit*".[108]

A clear application of these equitable principles is found in *Blisset* v. *Daniel*[109], a case which was followed in and has particular significance for the House of Lords decision in *Ebrahimi*.[110] In the latter matter an incorporated partnership was wound up because the House of Lords held that the expulsion of a member from his position as director by his fellow associates acting under a statutory and contractual power to that effect was "unlawful", that is, *mala fide* and *intempestiva*.

In/ .....

In the former matter a partner was expelled from an unincorporated partnership proper by his fellow associates, acting under a contractual power enabling a majority of partners to expel any one of their number. The court referred *inter alia* to Institutes 3.26.4. and set the expulsion aside as being a fraud on the expelled partner. The reference to *fraud* in *Blisset* was a significant advance. In the particular context it implied the existence of an inter se *fiduciary relationship*.[111] Equity was now a stone's throw away from imputing inter se fiduciary *duties* to partners, duties, in other words, which flow from lateral fiduciary relations. Thus in one instance the existence of an inter se fiduciary relation in partnership was specifically related to the good faith which partners are required to owe one another.[112] In this particular instance James, L.J., held that it was clear that "in partnership matters there must be the utmost good faith and that there is to that extent a fiduciary relation between the parties".[113]

In another instance the existence of an inter se fiduciary relation in partnership was related to mutual confidence which must necessarily subsist between partners.[114] In that particular matter Bacon, V.C., said:

> "If a fiduciary relationship 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".[115]

In this way the Roman notion of *fraternitas* and *(bona) fides* flowered in English law into the idea of a *fiduciary relation*

which/ .....

which in turn gives rise to a *fiduciary duty* obliging partners to be fair and loyal to one another in their inter se dealings. Although there was a time when courts sought to relate partners' inter se fiduciary duties to the concept of mutual agency — partnership being imagined to be but a variety of agency — those sentiments appeared to have waned. In fact none of the major English text writers today attempts to explain partners *inter se* fiduciary duties in terms of agency at all.[116)]

A further incident of the inter se fiduciary relation subsisting between partners is that an irretrievable breakdown of confidence provides a just cause for judicial dissolution. Thus, although the general rule is that a court will not ordinarily enter into partnership squabbles, it will order the dissolution of a partnership if the conduct complained of is, in the words of *Lindley*, "of such a nature as to destroy the mutual confidence which must subsist between partners if they are to continue to carry on their business together ".[117)] The test is whether it "is impossible for the partners to place that confidence in each other which each has a right to expect, and that such impossibility has not been caused by the person seeking to take advantage of it ".[118)] As will be observed in Ch.VII hereunder, it is these latter notions developed by equity in relation to partnership proper which have been employed by the judiciary under the statutory just and equitable provision to wind-up solvent incorporated partnerships when confidence between members has broken down.

6.4. SCOTS LAW

The Scots Law relating to the character of the inter se relation between partners is a curious combination of Roman law and Common Law. At the same time the notion that Scots partnership

is/ .....

is a legal *persona* has brought the question of agency to the fore and raised suggestions that the concepts of good faith in Scots partnership law are in some way tied up with agency.[119]

Bell and Clark, two of the older Scottish authorities on partnership, with obvious reference to the Roman idea of *"fides exuberet"*, describe partnership as a contract of "exuberant trust".[120] This term is explained by Clark in these words:

> "[A]nd therefore the law expects and requires that the conduct of partners shall be characterized by the most scrupulous good faith that they shall zealously act and co-operate for the common good, and that they shall not place their individual interests before those of the company".[121]

Miller, again, does not favour the use of the term *uberrima fides* (or exuberant trust) in the context of partnership[122] unless that term is "loosely used as equivalent to fiduciary duty".[123] Instead Miller prefers to describe the purport of the obligations of good faith which arise from the partnership relation as being "that the conduct of partners to one another will bear to be tried by the highest standard of honour".[124] This approach cannot be faulted.

At the same time Miller sees the operation of such obligations of good faith as partners may inter se owe one another as being limited to those transactions where partners might act as agents[125] of the partnership, viewed as a legal *persona*. This approach is incorrect. It obviously implies than when in their inter se relations partners deal with one another as principals (as for instance when one buys out the other's partnership interest) no obligation of faith arises by virtue of their being partners. Not only does this view conflict with all the authorities, but the statutory provisions on which Miller seeks to

rely/ .....

rely, do not support him.[126] It is true that in the old Scottish case *Cassels* v. *Stewart*[127], on which Miller relies, Lord Blackburn ascribed the fiduciary character of partnership to agency. But that judgment is not only not founded on any authority, it is also unconvincing.[128] That the obligation of the utmost good faith operates independently of notions of agency was later clearly underlined in *Harris*.[129]

6.5. SOUTH AFRICAN LAW

The South African law relating to the character of the inter se relation between partners is essentially Roman-Dutch. It has at the same time also been heavily influenced by the Common Law with regard to terminology and case law precedent. This hybrid character of South African Law with regard to the character of the inter se relation of partners is illustrated by the following two quotations which date back to the early part of this century. Morice, an early author in this field, described this position as follows:

> "Roman-Dutch law agrees with the English equity doctrine as to the fiduciary position in which partners stand to one another. A partner must deal with his co-partner *uberrimâ fide* ...."[130]

And in the Transvaal Supreme Court Sir John Wessels, J., was more explicit when in *Wegner* v. *Surgeson*[131] he said:

> "A partnership is usually expressed nowadays to be a contract *uberrimae fidei*. I do not know that we have any equivalent expression in the civil law, but in one of the *leges* of the Digest (17.2. lex 63)... *Societas jus quodammodo fraternitatis in se habeat*; in other words, the relationship between partners is very much the same as that between

brothers/ .....

brothers, which is equivalent to saying that partnership is a contract *uberrimae fidei*. During the continuance of the partnership one partner cannot overreach the other partner, nor can he dissolve the partnership with such intention and yet retain the benefits that flow from his act ".[132)]

South African law neatly distinguishes between a number of important consequences which arise from, what one authority terms, the duty of good faith.[133)] all of which can be explained in terms of the principles already recognized in Roman law One important consequence of this fiduciary duty is that a contract entered into in breach thereof is null and void not only *inter partes*[134)] but also *vis-à-vis* third parties.[135)] Another consequence exhibits itself in the duty of an errant partner to account inter se, that is to his co-partners. This duty flows from the requirement that a partner may not place his own interests above those of the partnership, or as it is stated in Digest 17.2.65.5, *semper enim, non id, quod privatim interest unius ex socius, servari solet, sed quod societati expedit*. One text refers to this as a [negative] "duty of non-preference".[136)] Seen from the point of view of the obligee partnership, as opposed to that of the obligor partner, this duty may more properly be termed a positive duty of loyalty obliging a disloyal partner to account to his fellow partners. For it is generally accepted that fair play requires that any benefit received by a partner in breach of this duty be communicated to the partnership.[137)] This principle is illustrated by the decision of the Transvaal Supreme Court in *Goldberg* v. *Trimble and Bennet*.[138)] Here the court held the defendants liable to account to the plaintiff for a one-third share of the profits accruing to the former as a result of the purchase by them of certain immovable property which the partnership had endeavoured to acquire. The purchase by the defendants was held by the court to be in conflict with the

interests/ .....

interests of the partnership which existed between the plaintiff and the defendants and, as such, incompatible with the fiduciary relationship which existed between the parties as partners.

A final consequence of the inter se fiduciary relation in partnership is that a serious breach of the duty of good faith will entitle the aggrieved partner to claim dissolution of the partnership.[139] This principle was followed in *Doucet*.[140] It was also applied in *Armstrong* v. *Wallwork*[141] and in *Salter* v. *Haskins*.[142] In *Salter* a partner was held to be entitled to wind up a partnership on the ground that his co-partner had committed adultery with his wife. In *Armstrong* the court ordered the winding-up of a partnership on the ground that mutual co-operation and trust were no longer possible between the partners. Here Searle, J., quoted from *Lindley* to the effect that the court was satisfied that, owing to quarrelling, bickering and loss of confidence, the partners could no longer carry on business and said:

> "There is no substantial difference between the English law and our law on the point. *Pothier* ... mentions *justa causa*, and one of the *justae causae* would be where the mutual co-operation is no longer possible, and when confidence had been destroyed".[143]

The parallel between English and South African Law in this regard is close indeed. None of the South African text writers or commentators, for instance, suggests that the fiduciary duties in partnership are in any way founded on the notion of (mutual) agency which is usually present in partnership. What is equally significant is that South African courts follow English courts in applying principles enunciated in *Lindley* to wind up solvent *incorporated* partnerships. A case in point

is *Lawrence*[144] in which, in addition, the *ratio* of *Salter* was adopted. This matter will be considered in further detail in Ch.VII hereunder.

7. *THE CHARACTER OF THE RELATION AS AGAINST THE WORLD*

7.1. *INTRODUCTION*

Three issues are relevant here. The first concerns the basic question of the nature of legal personality. The second relates to the effect of the recognition of legal personality on both the associative or lateral relations and the non-associative or vertical relations in partnership from the point of view of its implication for the fiduciary duties owed by partners. The third issue concerns the extent to which legal personality status has been attained by partnership in the legal system under consideration.

A natural tendency exists from both a commercial and a legal point of view to treat an association of persons in its dealing with third parties as an entity, that is as a corporate or legal *person*. The seminal concept *person* is, as Kocourek shows, but a conceptual point of reference by which the law makes a convenient adjustment of human interests.[145] Consequently a corporate, legal or moral person is a person who enjoys no human existence and therefore only exists in the contemplation of the law. The phrase "right-and-duty-bearing unit" which Maitland coined[146], is preferable to the more usual "corporate [legal or moral] person".[147] If partnership proper and corporation (or to use the common English term [incorporated] company) are polar concepts, as one commentator correctly suggests[148], it is because the law recognizes corporation as a corporate person enjoying corporate personality while partnership has traditionally been viewed as not enjoying that status.

The/ ....

The most important incident of an association's being viewed as a legal person is simply that such an association is viewed as a unit, both with regard to claims the associates have *qua* associates against third parties and *vice versa*.[149] In the case of partnership for instance, recognition would affect the partners in their vertical or non-associative relations with one another but not in their associative or lateral relations. With regard to the former set of relations a moral right-and-duty-bearing unit will be substituted as principal for the individual partners *qua* partners. Consequently the non-reciprocal fiduciary duties owed by whosoever acts on behalf of the partnership will be owed to the partnership as right-and-duty-bearing unit. On the lateral or associative level, recognition of right-and-duty-bearing unit status will not replace the inter se relation of partners. The continued association of the individual partners is necessary merely in order that the partnership may exist as a moral right-and-duty-bearing unit. And, as in the case of a partnership which is not viewed as a legal person, all decisions regarding the affairs of the partnership must still be taken by the partners, *qua* partners. Without such decision-making on the part of the partners, it will not be possible for the right-and-duty-bearing unit which exists by virtue of the association of such partners to function as a principal.

Legal personality and inter se fiduciary relations are however not mutually exclusive or incompatible concepts. The recognition of a partnership as a legal person, in other words, does not, as a matter of principle, destroy or disturb the considerations upon which the inter se fiduciary relations between partners are founded. Therefore those fiduciary relations will continue to exist and to operate despite the partnership's being regarded as a right-and-duty-bearing unit. Consequently, partners of a partnership enjoying legal personality status

should/ .....

should continue to owe inter se fiduciary duties arising from the considerations previously discussed. Thus a member of such a partnership will not be able to dissolve the partnership in bad faith or at an unseasonable time, must act loyally to the partnership, and may therefore not compete with the partnership or intercept opportunities which are in the line of business of the partnership and are such that the partnership has a preferred interest therein, etc.

Because of its bearing on the development of the private company, it is necessary to determine to what extent, if any, partnership has been recognized as a legal *persona* in England, Scotland and South Africa. Here again Roman law, and now too, Civil Law provides the necessary frame of reference, revealing at the same time that there is no magic about the concept legal personality and that it is nothing but a convenient commercial and legal device.

7.2. *ROMAN AND CIVIL LAW*

That the Roman *societas* was not a legal person is widely acknowledged. Sohm paints the following vivid picture:

> "Legally speaking, the *societas*, as such, can neither act nor hold property, it cannot buy the food for the dinner, nor acquire the ownership of it nor become liable for its price. All that can only be done by the *socius*. A *societas* is merely a legal relationship as between the *socii* themselves, and has no existence for anybody else."150)

The status of the *societas* as perceived by the authors of the *Corpus Juris Civilis* in the fifth century is described by Maitland in these terms:

"[T]he/ .....

> "[T]he *universitas* [corporation] is a person; the *societas* is only another name, a collective name, for the *socii*. Since then jurisprudence had kept or endeavoured to keep the two in very different boxes, in spite of the efforts of Natural Law to break down the partition ".[151]

Owing largely to the sobering influences of the law merchant, this partition, at least as far as the large or public partnership is concerned, appears to have broken down on the Continent some centuries later.[152] The role of the developing art of bookkeeping in this revolutionary process deserves mention.[153] Here Italian ingenuity played a pioneering role as it did in many other situations. This process of translating the financial activities of the firm into figures and recording them was facilitated by the change from Roman to Arabic numerals in Italy in the sixteenth century.[154] However, the importance of the double-entry system of keeping books lay, as Cooke correctly points out, not in its arithmetic, but in its metaphysics.[155] Once the financial position of both the partnership and the partners became to be recordable, it was soon realized that the accounts of the firm were in fact separate from the accounts of the individual partners constituting the partnership. As a result, the said accounts were kept separate from those kept for the individual partners. Once accepted, this notion that the firm was separate and apart from the partners, gained momentum and snowballed with the introduction of the balance sheet in about 1608.[156]

Following in the footsteps of financial realities, legal recognition of the separate and distinct character of the firm as a *persona ficta*, that is as a right-and-duty-bearing unit, came into European practice in the sixteenth and early seventeenth century.[157] Maitland sums up this development in the following passage:

> "[T]he *universitas* [corporation] was lowered to the rank

of/ .....

> of the *societas*, or (but this was the same process) the *societas* was raised to the rank of the *universitas*. Both alike exhibited a certain unity in plurality; both alike might be called 'moral persons' but in the one case as in the other, this personality was to be thought of as a mere labour-saving device, like stenography or the mathematician's symbols".[158]

Today this recognition is reflected in most Continental commercial codes. Across the channel in the British Isles with the exception of Scotland, a different attitude however prevails. A discussion of the complex reasons for this divergence between Civil Law and Common Law falls beyond the scope of this dissertation.

7.3. *SCOTS LAW*

It is fundamental to the Scots law of partnership that the firm is a legal *persona* distinct from the individuals who comprise it.[159] This rule, which dates from the seventeenth century, is clearly the result of Scotland's links with the Civil Law Continent. However, although Scots law undoubtedly recognizes the separate *persona* of partnership, that notion is not taken to its full logical conclusion.[160]

Thus the obligations of the partnership are correctly regarded as the proper obligations of the partnership viewed as a separate person and not as the joint and several obligations of the partners. Yet, despite the fact that the right-and-duty-bearing unit, the partnership, is liable in the first instance, the individual partners are, unlike the members of a corporation, accessorily liable for the debts of the firm. In the words of Lord President Cooper:

"Partners/ .....

> "Partners are of course, liable jointly and severally in a question with a firm creditor for the obligations of the firm, but the theory of Scots law views them as being liable only *subsidiarie*, the partners being in substance guarantors or cautioners of the firm's obligations, and each being entitled on payment of a firm debt for relief *pro rata* from the others".[161]

In line with this principle, creditors rank for the full amount of their claims in the first instance against the partnership itself upon sequestration.[162]

As the bearer of rights, too, partnership is viewed by the Scots as a unit or entity. And because rights vest in the separate *persona* and not in the individual partners, the doctrine of *confusio* does not operate to extinguish such right or, consequently, to preclude litigation between two firms with common partners.[163] Yet — possibly because of English influence after 1707 — partnership property is viewed as being "held by means of trustees and not directly like a corporation".[164] Clark, the principal writer on Scottish partnership law in the nineteenth century, gives the following explanation:

> "As ... a partnership or unincorporated company is only a *quasi* person, and not a proper person like an individual or a corporation, it should seem that it cannot hold property directly .... Whatever therefore ... becomes the property of the company, must be taken as held in trust for the uses and purposes of the company ".[165]

At the same time, perpetual succession is, as Smith puts it, "not imputed"[166] although a degree of continuity is accepted for the sake of business convenience and tax liability. When the *Partnership Act*, 1890[167] was enacted it recognized this

state/ .....

state of affairs, for §§ 4(2) thereof provides:

> "In Scotland a *firm* is a *legal person* distinct from the partners of whom it is composed but an individual partner may be charged on a decree of diligence directed against the *firm*, and on payment of the debts is entitled to relief *pro rata* from the firm and its other members ".

Perhaps because partnership is in practice not treated as a complete legal person, the private, incorporated statutory company has a definite role to play in Scotland. Many private partnerships are therefore incorporated as statutory companies. In fact one such company — *Symingtons' Quarries, Limited* — can lay claim to the honour of being the first statutory company which was recognized by the judiciary in the English system as an incorporated partnership. That this discovery should have been made in Scotland must to some extent be attributed to the close resemblance between partnerships and companies in that jurisdiction. This matter will be considered in Ch.VII hereunder.

7.4. *ENGLISH LAW*

A peculiar feature of the English law of partnership, which distinguishes it from the law of Civil Law countries and of Scotland, is the persistency with which the firm, as distinguished from its individual partners, has been ignored both at law and in equity.[168] Unlike an (incorporated) company a partnership in England is, therefore, not a person separate and distinct from its members. In the words of *Lindley:*

> "The rights and liabilities of a partnership are the rights and liabilities of the partners and are enforceable by and against them individually: *Si quid societati debetur singulis debetur et quod debet societas singuli debent* ".[169]

As/ .....

As early as 1855, the Mercantile Law Amendment Commission, after full enquiry, recommended the introduction into the law of England and Ireland of the "Scots principle" of legal personality in partnership, a principle which, the commissioners minuted, "is a very convenient and useful one".[170] To this day this recommendation has not yet been implemented. *Partnership Act*, 1890,[171] *§§* 4(1) today still provides:

> "Persons who have entered into partnership with one another are for the purposes of this Act called collectively a firm, and the name under which their business is carried on is called the firm name."

Lindley squarely acknowledges that the non-recognition of the firm is a defect in English partnership law. "It is to be regretted," the lament echoes, "that the Partnership Act did not go further than it did in the direction of assimilating English law to Scots law in this respect".[172] Today rules of court do, however, alleviate the position of members of an unincorporated partnership to some extent as far as litigation is concerned. Legal proceedings by or against partnerships, instead of having to be brought in the names of the individual partners as previously, may now be brought in the name of the firm.[173]

This refusal of Common Law to recognize partnership as a legal entity, is deeply rooted in English history. Here the royal prerogative with regard to the creation of corporations played a prominent role. Cooke explains:

> "A business could not be separated from its owners in the Italian manner unless it had unequivocal corporate form. So, for the unincorporated business, other devices had to be brought into play".[174]

One/ ....

One such device turned out to be the trust, that "most specifically English of all our legal institutes".[175] By marrying the trust (which in essence is a vertical relation) to the large, unincorporated partnership (which in essence is an associative relation) the British overcame the disabilities which resulted from the failure of the law to recognize the public partnership as a right-and-duty-bearing unit. This development will be traced in Ch.IV hereunder.

Another such device turned out to be the statutory private company. This company type was recognized by the legislature in 1907 for the first time. It soon became the vehicle through which partnership proper sought to attain legal personality. In this way the incorporated partnership came into being. These matters will be considered in Chs. V. and VI hereunder.

7.5. SOUTH AFRICAN LAW

As in English law, partnership is not recognized as a legal person or entity in South African law but is seen as a mere association of persons".[176] Here the predominant influence of English law in the Cape after 1806, especially on mercantile practice, played a definite role. As in English law, legal proceedings by or against a partnership may now, both in the Supreme Court and in the Magistrate's Court, be instituted in the name of the partnership instead of the individual partners. And as in England, partnership proper here too seeks expression in the statutory private company.

CHAPTER III

THE ENGLISH COMPANY LAW SYSTEM

8. *THE BRITISH COMPANY REGIME*

English company law is found throughout the former British Empire. Canada, the West Indies, Africa, New Zealand, Australia and the Far East, all came under the sway of that "magna carta of co-operative enterprise", the *Companies Act*, 1862[177], and subsequent British Companies Legislation at some stage and to some extent. This explains why the statutory just and equitable winding-up provision is found in the company statutes of all those jurisdictions and also why the concept "quasi-partnership company" has found its way there. For present purposes, only the introduction of the British statutory regime in the hybrid systems of Scotland and South Africa will be considered. This regime has evolved over more than one and a half centuries and some of the salient features of that evolution will be highlighted in Ch.IV hereunder. Suffice it to note here that the current English statute is the *Companies Act*, 1948[178] as supplemented by the *Companies Act*, 1967[179], and the *Companies Act*, 1980[180] respectively.

8.1. *SCOTLAND*

Despite the constitutional situation, the *Joint Stock Companies Act*, 1844[181], did not apply to joint stock companies in Scotland.[182] Only with the enactment of the *Joint Stock Companies Act*, 1856[183], were Scots concerns for the first time brought in under the sway of the British statutory regime

concerning/.....

concerning incorporated companies. Ever since, British Company legislation has consistently been applied to Scots companies. Although the Scots judiciary, which, according to Gower[184], was distinctly more liberal than its English counterpart, has influenced the course of company development in the English system, the English influence has also left its mark on the Scots tradition. For a long time Scotland had shared with the Continent the custom of using a single word, namely, "company"[185] to refer to both statutory companies and common law partnerships. After the introduction of the *Joint Stock Companies Act*, 1856, that began to change. "Company" then, as in England, began to acquire the exclusive meaning of an "incorporated company registered in terms of an enabling companies act". Today one searches in vain for authority that a "partnership" is still referred to as a "company" in Scotland.

Although Scots company law gradually became anglicized in this fashion, it still retained sufficient vitality of its own to play a distinctive role in the evolution of the incorporated partnership, as will be seen in Ch.VII hereunder.

8.2. *THE REPUBLIC OF SOUTH AFRICA*

The present-day Republic of South Africa, consisting of the four provinces of the Cape, Transvaal, Orange Free State and Natal, which became the Union of South Africa in 1910, has for one hundred and twenty years now followed the British statutory model closely.

The first company legislation in this region was enacted in 1861, in that area where the British influence was established the longest, namely the colony of the Cape of

Good Hope. That statute was the *Cape Joint Stock Companies Limited Liability Act*, 1861.[186] It was virtually a *verbatim* re-enactment of the *English Joint Stock Companies Act*, 1844,[187] and of the *Limited Liability Act*, 1855[188], which had at the time already been repealed in Britain. This essentially British statute soon served as a model in the neighbouring British colony of Natal, and some while later, in the Boer Republic of the Transvaal.

As early as 1864, Natal re-enacted the 1861 Cape Act as the *Joint Stock Companies Limited Liability Act*, 1864.[189] The Transvaal Republic did not do so until 1874 when it enacted the Act as *De Akte van Maatschappijen met Beperkte Verantwoordelijkheid*, 1874.[190]

The other Boer Republic, the Republic of the Orange Free State, lagged behind, and adopted this model only in 1891 when it enacted *De Wet over Beperkte Verantwoordelijkheid van Naamloze Venootschappen*, 1891.[191] In the following year it enacted *De Wet voor Liquideeren van Naamloze Venootschappen*, 1892.[192] The title of the next Companies Act in the region was the *Companies Amendment Ordinance*, 1904[193], which reflected the defeat of the burghers by the British in the war of 1899-1902, as did the title of the *Companies Act*, 1909.[194] This Transvaal Act closely followed the *English Companies (Consolidation) Act*, 1908[195], of only the previous year.

The goldmining industry which sprang up on the Witwatersrand caused an influx of foreign capital and the centre of commercial activity moved from the Cape to the Reef. After the establishment of the Union in 1910, the Transvaal *Companies Act*, 1909, served as model for the first South African Companies Act, namely the *Companies Act*, 1926.[196] Although the South African legislature has from time to time gone its own way, introducing

local/ .....

local innovations, it is generally accepted that South African Company law is basically English-orientated.[197] In the Republic of South Africa, as in Britain, the *Companies Acts* are not regarded as codes in the Continental sense.

In view of this background it is not strange to find that English decisions on company law have considerable persuasive authority in South African courts.[198] Even though it has been said that the *R.S.A. Companies Act*, 1973[199], which on January 1, 1974 repealed and replaced the *Companies Act*, 1926, "effectively cut the umbilical cord between English and South African company legislation"[200], the authority of English decisions in the field of company law is unlikely to abate. English company law has, since Britain's entry into the European Common Market, had to move closer towards European company law. The abolition, in the 1980 English company legislation, of the statutory definition of private company which has served the British company system since 1908, followed by proposals for a statutory incorporated partnership, is possibly the most dramatic step towards closer harmonization with Continental company law. As yet the South African legislature has not followed. There is, however, every reason to believe that it will sooner or later do so.

CHAPTER IV

THE EVOLUTION OF THE INCORPORATED (PUBLIC) COMPANY IN THE BRITISH SYSTEM

9. *PRELIMINARY*

To evaluate the concept "company" in the English system satisfactorily, it is necessary to turn back the clock two centuries and more. Seventeenth-century England knew two types of business organization, namely the common law partnership and the statutory, or chartered, corporation created by special Act of Parliament or by charter of the Crown. Neither the corporation nor the partnership, however, was entirely suited to the needs of the time.

The corporation proved unsatisfactory because of the expense, time and difficulty involved in obtaining a charter or having a private bill promoted in Parliament. The partnership failed because of certain of its basic features. The two main obstacles in the latter regard were the principle of *delectus personae* — for which see Excursus II hereto — and the inherent lack of corporate personality.

In the absence of legal personality, the associative relation partnership naturally lacked the capacity to litigate. Whenever the partnership was involved in litigation, all the partners had to be joined as co-plaintiffs, or co-defendants, as the case might be. More serious, however, was the firm's lack of contractual capacity and capacity to acquire, hold and transfer property. Because the partnership was not a legal entity and lacked the aforesaid capacity, all legal transactions which it wished to conclude had to be transacted by all the partners acting as agents for each other as principals. By

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that time mutual agency had already long established itself as one of the natural incidents of partnership. Because the partners, and not the non-existent legal *persona*, would thus be bound as principals, each and every partner would incur full liability for the obligations of the partnership.

The principle of *delectus personae*, on the other hand, barred the admission of new partners, either by succession or by alienation, and thus fettered the free transferability of shares. This, in turn, seriously hampered the marketability of stock and the ability of entrepreneurs to raise capital.

10. THE EQUITABLE JOINT STOCK COMPANY

To overcome the abovementioned drawbacks, the seventeenth-century businessmen created by contractual arrangement the "equitable joint stock company",[201] or as it is also called, the "deed of settlement company".[202]

True, the *Bubble Act*[203] made corporateness, with its particular attribute of transferable shares, the exclusive preserve of a grant of incorporation or a recognized prescriptive right to be a corporation. But, as Du Bois points out:

> "Between the corporation and the partnership there arises the equitable joint stock association which, without any formal act of incorporation ... arrogates to itself all the outward symbols of the juristic person from common seal to transferable shares. One is not justified, however, in regarding this hybrid of the times as something new or even *sui generis*, for the eighteenth century specialist be he financier or solicitor, saw it only as a partnership".[204]

In form the equitable joint stock company was nothing but an

outsize/ .....

outsize partnership.[205] In substance, however, it differed from the ordinary partnership in at least two important respects. First and foremost, it was, unlike partnership proper, not concluded *intuitu personae* but *intuitu pecuniae* (for which see Excursus II) and it was intended to be no more than a mere vehicle for the aggregation of capital. The impersonal capital-orientated character of this type of association is starkly portrayed by an observer of the time, who, stressing the part-time nature of the investor's involvement, says:

> "Each individual member having his own separate pursuit or profession which engrosses the chief part of his time and attention; and therefore are [joint stock companies] besides their direct public usefulness, suitable to the convenience of private persons as absorbing their spare and superfluous capital".[206]

Then again, because the concepts of mutual agency and *delectus personae* were no longer suited to the requirements of this type of business organization, they were shed. Thus instead of all the partners being agents of the association, only those who were specifically appointed as such, would now be able to bind it.[207]

And with the exclusion of *delectus personae* and the obvious lack of mutual confidence and trust between members, the idea of inter se fiduciary relations vanished. "[I]n the eyes of the law," says Gower as he describes the equitable joint stock company, "it was merely a partnership ... often swollen to a size which destroyed any possibility of the mutual confidence between members which was supposed to be at the root of partnership law ...."[208]

In/ .....

In accordance with its partnership origin, the equitable joint stock company was, unlike the chartered corporation, not created by governmental grant, but originated simply in contract. Its constitution was consequently determined entirely by its members. However, because it was not created under the specific authority of the state, it obviously lacked corporate personality. As such it could not, in its own name, contract or litigate, or acquire, hold or convey property. At the same time its members were obviously liable in full for all obligations incurred on its behalf.

Some of the difficulties inherent in this situation were more easily overcome than others. The lack of capacity to contract, and litigate and to acquire hold and convey property was overcome by resorting to the trust device, *i.e.* by vesting the property and the control and management of the association in trustees.[209] By marrying the vertical, proprietary, trust relation to the associative and consensual, partnership relation, a perfect balance was achieved. On the one hand, the property and undertaking of the association were vested in trustees in whom legal title vested, the beneficial title being in the company. Flexibility was nevertheless maintained. Smith explains:

> "What binds the members to each other is the contract and the trust is merely the device which experience has shown to be the most suitable for the convenient administration of the common property".[210]

The hallmark of the modern public issue company, namely separation of ownership and control, soon revealed itself as a necessary corollary of the trust device which so admirably

substituted/ .....

substituted for corporate personality in the equitable joint stock company. Remarks Cooke:

> "Here was a legal entity independent of the persons deriving benefit from it, for whose benefit it had been brought into existence but who were separated completely from its management and owners".[211]

For most practical purposes the equitable joint stock company was a quasi-corporation.[212] "In truth and in deed", Maitland recalls, as he sings the praise of the unincorporated equitable joint stock company, "we made corporations without troubling King or Parliament, though perhaps we said that we were doing nothing of the kind".[213]

However, because the corporate status thus established was achieved without the sanction of the state, it was only to be expected that the true corporate principle, that members are not liable for corporate debts, did not apply to the members of these companies. Since public and legislative opinion in England was traditionally hostile to the idea of limited liability, the attainment of limited liability was not achieved immediately or very easily. And attempts to limit the liability of members to the capital contributed by them, did not generally find favour with the English courts. England, unlike the Continent, required that the privilege of limited liability be bestowed by Parliament. This did not come about without great effort.

Moreover, when the English Parliament finally repealed the then defunct *Bubble Act* in 1825[214], it irrevocably entrenched a deep-rooted suspicion of freedom from liability. For in the second part of the repealing Act, the age-old precept[215] that

corporateness and freedom from liability are synonomous, was abrogated. Henceforth the extent to which members of a corporation would be individually liable for the debts of a corporation, would be in the discretion of the Crown authorities. This explains why members of a joint stock company incorporated under the Joint *Stock Companies Act*, 1844,[216] continued to be liable in full for the company's debts.

11. *THE INCORPORATED (JOINT STOCK) COMPANY*

11.1. *PRELIMINARY*

So popular had the unincorporated equitable joint stock company in fact become, that the state was compelled to intervene. But instead of outlawing it outright, Parliament sought to regulate that creature of Chancery by legalizing it. However, although corporate status was conceded, limited liability was, in keeping with the British approach, not granted immediately. And when limited liability was finally granted, it was not granted in full. Thus although the state gracefully "capitulated", as Maitland[217] puts it, it was with extreme reluctance that the state gave way: another eleven years elapsed before limited liability would be granted in some form.

11.2. *REGULATION THROUGH REGISTRATION*

The full title of the first major British effort in this sphere, is *An Act for the Registration, Incorporation and Regulation of Joint Stock Companies*.[218] It leaves one in no doubt about the legislature's primary aim. This was to regulate the flotation of unincorporated equitable joint stock companies so as to be able to combat fraudulent issues of shares to the public. How this was to be achieved becomes apparent from the very preamble of the Act. Here the legislature referred to the expediency of making provision for the due registration of joint stock

companies/ .....

companies, investing such companies with the qualities and incidents of corporations (but "subject to some modifications", which happened to concern the question of members' liability), and preventing the establishment of companies which were not registered in terms of the *Joint Stock Companies Act*, 1844.

In pursuance of the said aim, the first substantive provision of the *Joint Stock Companies Act*, 1844, § 4, provided: "That before proceeding to make public, whether by way of Prospectus, Handbill or Advertisement, any Intention or proposal to form a company ... it shall be the duty of the Promoters ... to make to the Office ... for the registration of Joint Stock Companies ... Returns of the following Particulars ...."

As foreshadowed in the marginal note to this provision, the return of the prescribed particulars resulted in provisional registration only; this in turn was both a prerequisite for and a prelude to a public issue of shares. Provisional registration did not, however, confer corporate status. Attributes of corporateness would, in terms of *The Companies Act*, 1844, § 25, follow only upon the grant of a "Certificate of Complete Registration", which in turn required that the "Deed of Settlement" constituting the company be filed with and registered by the Registrar of Joint Stock Companies in London.

More important, however, although the *Joint Stock Companies Act*, 1844, specifically referred to the company and all present and future shareholders as being "incorporated", it is nevertheless clear that such "incorporation" did not limit the personal liability of members. Members in effect continued to be liable as ordinary common law partners. The relevant portion of the statutory provision in this regard read:

"On/ .....

> "On the complete Registration of any Company ... such Company and the then shareholders therein, and all the succeeding shareholders, whilst Shareholders shall be and are hereby incorporated ... but so as not in anywise to restrict the liability of any of the Shareholders ... but every such Shareholder shall ... be and continue to be liable as he would have been if the said Company had not been incorporated ...."[219)]

Yet, despite this drawback of unlimited liability, progress had undoubtedly been made. "The wedge", Maitland remarks, "was in"[220)]. For a grant of corporateness was now no longer a matter of royal prerogative, but since it required no more than the registration of documents in a central office in London, it was reduced to a mere formality.

This privilege was, however, open to a particular class of partnership only, namely the gigantic or public partnership when it appealed to the public for funds; the said privilege was not at the same time available to the private partnership. Thus the *Joint Stock Companies Act*, 1844, was the first enactment to differentiate between the said two types of partnership. To that end the legislature defined, "Joint Stock Company" as "every Partnership whereof the Capital is divided or agreed to be divided into Shares, and so as to be transferable without the express Consent of all the Co-partners; and also ... Every Partnership, which at its Formation, or by subsequent Admission ... shall consist of more than Twenty-five Members ...."[221)]

In terms of this definition an incorporated (joint stock) company is in essence therefore a public partnership. Partnership proper or the private partnership was clearly not intended to be embraced by the term "Joint Stock Company".

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The reference to freely transferable shares and to a minimum membership of twenty five are of particular significance in this context. It implies absence of *delectus personae* and consequently, of the personal character of the inter se relation of members. "The English legislation gave recognition to the fact," Gower correctly points out, "that the partnership form is not intrinsically suited to large joint-stock enterprise, for partnership principles presuppose mutual trust and confidence among the members which is impossible if their number is unduly large".[222] The *Joint Stock Companies Act*, 1844, laid the foundation of modern English company legislation. "There have been alterations and additions to the building since", as Cooke puts it: "parts have been pulled down and rebuilt; vast new extensions have appeared; the internal services have been modernized. [T]he general plan of the building remains the same".[223]

The edifice so created was that of the public-issue company. More than half a century would pass before the private incorporated company would be accommodated, almost in an annex as it were. Before that could happen, though, the fusion between the equitable joint stock company created and nourished by the Chancery, and the chartered company, recognized by the common law courts, had to be consummated.

11.3. CONCESSION OF LIMITED LIABILITY AND FUSION OF THE EQUITABLE JOINT STOCK COMPANY WITH THE CHARTERED COMPANY

The struggle for limited liability had in the meantime been waged unabated. Finally, in 1855, the *Limited Liability Act*, 1855[224] was passed. That statute provided that the liability of a member of an incorporated company stood to be limited to the amount unpaid (if any) on his shares and only arose after

execution/ .....

execution against the assets of the company had proved insufficient.[225]

Within a year the said Act was repealed and consolidated in a revised form with the *Act for the Incorporation and Regulation of Joint Stock Companies and other Associations*, 1856.[226] The *Joint Stock Companies Act*, 1856, in the words of Cooke, clothed the joint stock company in modern garb. "[T]he general purpose of the Act", Cooke elaborates, "may be described as the fulfilment of the expressed purpose of the Companies Act of 1844, which was to invest joint stock companies 'with qualities and incidents of corporations'. Where the Act of 1844 failed to fuse the equitable company with the common law company, the Act of 1856 succeeded".[227] Instead of both provisional and final registration, the Act now provided for a single registration only. And the old "Deed of Settlement" was replaced by the memorandum and articles of association which are still in use today. More important, both corporateness and its attributes were spelt out in explicit terms in the Act. Thus the *Joint Stock Companies Act*, 1856, provided for the registration by the Registrar of Companies of the memorandum of association of a company (whether accompanied by articles of association or not[228]), and the certification by him that the company was incorporated. Upon conclusion of these simple formalities a statutory right-and-duty-bearing unit, a body corporate, as it is referred to by the legislature, came into being. The provision in question, *Joint Stock Companies Act*, 1856, § 13, read:

> "[T]he subscribers of the memorandum of association, together with such other persons as may from time to time become shareholders in the company, shall thereupon be/ .....

> be a *body corporate*, by the name prescribed in ... having a perpetual succession and a common seal, with power to hold lands, but with such pecuniary liability on behalf of shareholders as is hereinafter mentioned ...".[229]

The incorporated company had arrived.

11.4. BODY CORPORATE: CREATION AND EFFECT

11.4.1. INTRODUCTION

Joint Stock Companies Act, 1856, § 13 formed the backbone of the English incorporated company at the time. In amended form it still does so today. It is found in all company statutes based on the British model and the corresponding sections in present day statutes are in virtually indentical terms.

While it is difficult to envisage the legislature using Maitland's term, "right-and-duty-bearing unit", it must not be overlooked that there was possibly a time when the term "body corporate"[230] would have been equally meaningless and lacking in appeal. Generally though, and in particular before 1825, corporate status came to imply complete limited liability: with regard to relations between third parties, and the body corporate, the body corporate alone incurred liability and not its members as well. This the legislature clearly accepted subject to minor qualifications in the above provision. What is of extreme significance though, is that the legislature did not express itself at all about the implications which the fact of the corporateness of the (body of) members had upon their inter se relations. Here, in the absence of a provision to the contrary, the common law position must be taken to prevail.

11.4.2./ .....

11.4.2. THIRD PARTY RELATIONS

As far as relations with third parties were concerned, the members of a limited liability company, which was thus incorporated, might, despite the interposition of the body corporate between them and third parties, nevertheless incur statutory liability *vis-à-vis* the said third parties in two distinct situations.

The first instance occurred if the company were wound up because of its inability to pay its debts. Here existing shareholders were in terms of the *Joint Stock Companies Act*, 1856, liable to contribute to the assets of the company to an amount sufficient to pay its debts and the winding-up expenses. The contribution was, however, limited to the unpaid amount, if any, on the shares in question.[231)]

The second, as will be seen hereunder, arose upon non-observance of the statutory requirements concerning minimum membership. The said requirements were essentially aimed at withholding the privileges of incorporation from partnerships proper. Later, though, with the statutory recognition of the private company, this sanction was partially lifted.

11.4.3. INTER SE RELATIONS

Although the inter se lateral relation of members of the public partnership was anthropomorphized into a body corporate as regards relations with third parties, at least one of its essential partnership features appears to have survived incorporation. That feature is the consensual character of the relation between members which was specifically retained by the legislature in the *Joint Stock Companies Act*, 1856, and subsequent enactments.

Thus/ .....

Thus *the Joint Stock Companies Act*, 1856 specifically provided that when registered, the memorandum and articles of association of the company would bind the company and the shareholders therein to the same extent as if each shareholder had subscribed his name and affixed his seal thereto or otherwise duly executed the same.[232] This all-important provision is also found in all company statutes based on the British model and the wording of the present day provisions differs only in minor respects. The effect of a provision in these terms is that members stand in a contractual relation not only to the right-and-duty-bearing unit but also to one another inter se. The result is a most flexible company constitution which the about-to-be associates are, as in partnership, at liberty to shape to their will.

Amongst other things, the associates are at liberty to will that their inter se relation shall be a fiduciary one, that is one of mutual confidence and trust. Obviously when the associates are large in number — as they would necessarily have been in the case of the companies incorporated under the early *Companies Acts*— inter se mutual confidence and trust would be a fiction. And while intimacy of numbers and close inter se relations of mutual confidence and trust go together, the statutory regime of the nineteenth century did not provide for the incorporation of private partnerships. Thus the belief, that members of an incorporated company do not inter se stand in a fiduciary relation, grew up. With the statutory recognition of the incorporated private company the basic premise obviously changed but by that time the tradition, that members cannot inter se be fiduciaries, had already entrenched itself.

Suffice it, however, to point out that the existence of the body corporate created in terms of *Joint Stock Companies Act*,

1856/ .....

1856, § 13, did not at the time prevent the corporate members — the members of the statutorily created right-and-duty-bearing unit — from standing in an inter se relationship and as such being fiduciaries. Nor do the present day successors of that provision do so today. This is clearly recognized in the following passage from a speech by Lord Wilberforce in a recent case where his Lordship held:

> "The words [just and equitable[233)]] are a recognition of the fact that a limited company is more than a mere legal entity, with a personality in law of its own: that there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals with rights, expectations and obligations inter se which are not necessarily submerged in the company structure [which is] defined by the Companies Act and by the articles of association by which the shareholders agree to be bound".[234)].

Here his Lordship was of course dealing with an incorporated partnership. Whether those salient partnership proper characteristics, good faith and mutual confidence and trust, apply in any particular situation to corporate members so that their inter se relation becomes a fiduciary one, depends on a number of factors. One such factor is the intention of the associates, that is whether they came together *intuitu personae* or *intuitu pecuniae* (for which see Excursus II). A closely related factor obviously is number, that is the size of the body of corporators. In this latter respect the nineteenth-century legislation contained rather specific requirements which affected partnership proper in a most specific way and made it rather unlikely for a statutory company to be an incorporated partnership.

11.5./ ....

11.5. THE NINETEENTH-CENTURY COMPANIES ACTS AND PARTNERSHIPS

In the nineteenth century the privilege of incorporation by registration was open only to associations having at least seven members — thus excluding the majority of partnerships proper. This is apparent from the first substantive provision namely *Joint Stock Companies Act*, 1856, § 3 which read:

> "Seven or more persons, associated for any lawful purpose may, by, subscribing their names to a memorandum of association, and otherwise complying with the requirements of this Act in respect of registration, form themselves into an incorporated company, with or without limited liability".[235]

This position prevailed for close on one hundred and thirty-four years. In fact the requirement that a public company had to have at least seven members was only in 1980 relaxed and the minimum membership requirement reduced to two.

In essence the incorporated company is a partnership, albeit of the public-issue type. This made it necessary for the legislature to compel[236] incorporated companies to be distinguishable from the unincorporated ones by having a "red flag warning"[237], *Limited* affixed at the end of their names.

In keeping with the basic nature of the incorporated company as a partnership of some type, the liability of its members as "incorporated" partners lay dormant, only to be awoken when they acted contrary to the statutory scheme. The relevant provisions in this regard read as follows:

> "If any company registered under this Act carries on business when the number of shareholders is less than 7,

for/ .....

for a period of 6 months after the number has been so reduced, then every person who is a shareholder in such company during the time that it so carries on business after such period of 6 months shall be *severally liable* for the payment of the whole debts of the company, contracted during such time, and may be sued for the same without the joinder in action or suit of any other shareholder".[238)]

The obvious effect of this provision was that the members of the body corporate would be at pains to ensure that there would be at least seven of them at all times to avoid their becoming personally liable for corporate debts. From the above provisions it is apparent that the object of the legislature was to place the benefits of incorporation effectively beyond the reach of the truly private partnership.

At the other end of the scale, another provision endeavoured to ensure that partnerships of more than twenty members entered the corporation fold. Here the measure was a prohibition couched in the following terms:

"Not more than 20 persons shall, after the 3rd November 1856, carry on in partnership, any trade or business having gain for its object, unless they are registered as a company under this Act or are authorized so to carry on business by some private Act of Parliament or by royal charter or letters patent;...and if any persons carry on business in partnership contrary to this provision, every person so acting shall be severally liable for the payment of the debts of the partnership, and may be sued for the same without the joinder in action or suit of any other members of the partnership".[239)]

The/ .....

The object of this provision, in the words of James, L.J., was:

> "[T]o prevent the mischief arising from large trading undertakings being carried on by large fluctuating bodies, so that persons dealing with them did not know with whom they were contracting, and so might be put to great difficulty and expense, which was a public mischief to be repressed".[240]

In this regard the prohibition was singularly successful, for, as Carr[241] observes, it "drove" the unincorporated equitable joint stock companies, *(i.e.* the public-issue partnerships of the time), "within the compass" of the *Companies Act*. The coercive factor here was the penal, several liability of the illegal partners while the benefits of incorporation served as persuasion. Thus was created a statutory regime which affected partnership at both ends of the scale and which turned on the number of persons linked together in a particular associative relation.

Between these perhaps arbitrarily[242] selected cut-off points — and possibly to mitigate the harshness and cushion the inequity of the said statutory regime — a neutral, no man's land served as a buffer zone. Here the lateral relation consisted of not fewer than seven and not more than twenty associates who, at their choice, could elect either to be registered as an incorporated company or to carry on as a common law partnership. Outside this zone there was Hobson's choice. If for instance, on the one hand, the associative relation comprised twenty-one or more associates, they were compelled to register as an incorporated company in order to avoid being visited with the punitive, several liability attaching to illegal partners.

If/ .....

If, on the other hand, the lateral relation comprised six or fewer associates, the single option available to the laterally associated persons was even less attractive. Such a relation was a partnership — pure, simple and proper — and limited liability was not open to it, that is until the statutory recognition of the private company. Only with the introduction of the latter-mentioned company type, did it become possible to invest partnership proper with corporate status by clothing it in the formal statutory garb in which the incorporated private company appears.

Therefore, although the *Joint Stock Companies Act*, 1856, like its predecessor the *Joint Stock Companies Act*, 1844, was aimed primarily at regulating company promotions, *i.e.* the raising of capital from the public[243] by public-issue partnerships, it had a significant effect on the law concerning private partnerships as well. At the one end of the spectrum it caused the eclipse of the formerly common, unincorporated equitable joint stock company, with its large body of impersonal members, by legalizing it out of existence. Owing to the coercion and persuasion approach of the *Joint Stock Companies Act*, 1856, this species of partnership disappeared from the scene in the English system.[244]

At the other end of the spectrum there was the private partnership, destitute and out in the cold. Corporate personality, with its main advantage, *viz.* freedom from liability for members, was not yet to be within the reach of six or fewer partners. This state of affairs gave rise to renewed efforts to obtain the benefits of limited liability in other ways. One of these was a fresh interest in the Continental *société en commandite* which, though it did not prove to be a panacea for all the ills of partnership, gave rise to the recognition of the English limited partnership. Another was the employment of symbolic or nominee subscribers and members. This ultimately

led/ .....

led to the statutory recognition of the English private company, which in turn gave birth to the incorporated partnership. That was still some way off, though. The next important event was the first great consolidation, *The Companies Act*, 1862.

12. *THE INCORPORATED COMPANY AND LEGISLATION SINCE 1856*

In the year 1862 the English Parliament passed its first major consolidation Act, which merged the *Joint Stock Companies Act*, 1856, with a considerable number of other Acts under the short title *The Companies Act*, 1862.[245] This Act marks the coming of age of the incorporated equitable joint stock company. For the first time the joint stock company is statutorily referred to by the name by which it would henceforth be known, namely "company" and not "joint stock company" as in the past.

The next important consolidating Act was the *Companies (Consolidation) Act*, 1908.[246] It dealt with two diametrically opposed issues. It both introduced the prospectus requirements to be complied with by public-issue companies and also statutorily recognized the private company. This was the thin edge of the wedge which would eventually threaten to split the "unity of the English company concept". Henceforth an (incorporated) company would be either a public company or a private company. In this system the public company up to the year 1980 constituted the residual class: a company was a public company, unless it fell within the statutory definition of a private company. Thus the English private company was but a slightly varied form of the general institution of the incorporated company so that one may rightly talk of the unity of the company concept in the English system. These matters will be considered in further detail in Ch.V hereunder. In the private company, partnership proper found a staunch ally in its quest to attain the benefits of corporate personality.

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In the *Companies Act*, 1948,[247] — a statute founded on the notions of a past era but intended to provide the basic statutory framework for English Company Law in the second half of the twentieth century — the unity of the English Company was preserved. However, the statutory scheme no longer accorded with reality as the basic company type intended to be served by the Act, the public company, had long been dwarfed by the populous statutory private company.

The *Companies Act*, 1980[248] did not bring the statutory scheme into line with reality. It was passed primarily with the object of implementing the E.E.C. Second Directive, which is concerned with "public limited liability companies". As will be seen in Ch.V hereunder, the *Companies Act*, 1980, adopts an entirely new system of classification of companies as "public" and "private", the latter being excluded from the requirements of the Second Directive and from the corresponding provisions of the Act. Before proceeding to deal with these matters it is necessary first to take stock of the term "company" as used in the Companies Acts.

13. *THE TERM "COMPANY" IN THE COMPANIES ACTS*

The *Companies Act*, 1948,[249] §§ 455(1) provides that for purposes of that Act, the expression "company" means "a company formed and registered under this Act or an existing company." *R.S.A. Companies Act*, 1973,[250] §§1(1) is to the same effect.

It has been suggested that this statutory "definition" can hardly qualify as a definition of a company.[251] True, that statutory attempt is conceivably as much a definition of a company as the suggestion that "a rose is a rose" is a definition of a rose. But that is not, however, to underestimate the formidability of the task of defining the concept

company/ .....

company. For it is generally accepted that a company (like a corporation) can assume such a variety of forms that it is not susceptible to definition at all.[252]

What is significant, though, is that all the definitions which have been attempted in that regard define company in essence as some form of partnership. This is not surprising, for if the definitions of *partnership proper*, which have previously been considered, are compared to those of *company*, which are now to be listed, a striking resemblance will be evident. Lindley, for instance, defines a company as "an association of many persons who contribute money, or money's worth to a common stock and employ it in some trade or business, and who share the profit or loss (as the case may be) arising therefrom".[253] The following attempt by Buckley, J., in a decision handed down just prior to the statutory recognition of the private company, focuses on numerical size and absence of *delectus personae:* "The word company has no strictly technical meaning. It involves, ... two ideas — namely, first, that the association is of persons so numerous as not to be aptly described as a firm; and, secondly, that the consent of all the other members is not required to the transfer of a member's interest".[254] So does Halsbury, although he tends to lay particular emphasis on the distinction between incorporated, and unincorporated companies when he defines a company in these terms: "The word 'company' imports an association of a number of individuals formed for some common purpose. Such an association may be incorporated (that is, a body corporate with perpetual succession and a common seal) or it may be unincorporated. An incorporated company is a legal person separate and distinct from the individual members of the company, whereas an unincorporated company has no such separate existence and it is not in law distinguishable from its members".[255] A South African authority neatly brings all these definitions together in three terse lines: "A company can be adequately described

in/ ....

in general terms as an association of persons for the common object of the acquisition of gain ...."[256] What is particularly striking of this last definition is that it is equally applicable to partnership.

In essence a company is but a lateral or associative relation,[257] or, as it is more usually referred to, a partnership. An (incorporated) company is nothing more than a partnership which has statutorily been invested with corporate personality: *i.e.* recognized as a right-and-duty-bearing unit. In principle such a partnership may be either a public partnership or a private partnership. In the nineteenth century, companies of the former type were common while companies of the latter type were exceedingly rare. That was so because partnership proper presupposes mutual confidence and trust, which in turn presuppose a close intimate circle, that is, a small number of partners, usually not more than three, four or five members. Until a way could be found around the statutory requirement that an incorporated company had to have at least seven members it was unlikely that any partnerships proper would have been incorporated during the nineteenth century. That only became possible with the advent of the private company. That development will now be considered.

CHAPTER V

THE PRIVATE (INCORPORATED) PARTNERSHIP AND THE PRIVATE (INCORPORATED) COMPANY IN THE BRITISH SYSTEM

14. PRELIMINARY

In the private (incorporated) company, partnership proper found a means by which to attain the corporate status which it lacked and to which it aspired. Thus it is not surprising that in all but two of the decisions in which the incorporated partnership surfaced, the companies in question were statutory private companies (for which see para 15.3 hereunder). In the two instances where the companies concerned were not statutory private companies,[258] those companies had been incorporated prior to the statutory recognition of the private company. And there, in order to circumvent the statutory minimum membership requirement of seven, the nominee or symbolic shareholder device was used to bring membership up to the requisite statutory level of seven.[259]

Although it may safely be said that since 1907— the year in which the private company was statutorily recognized— all incorporated partnerships have been private companies, the converse does not hold, that is, not all private companies have been incorporated partnerships. In order to see why this is so, it is necessary to trace the history of the private (incorporated) company. And because the term *private company* has never had a single fixed meaning and has with time changed to express changing concepts, that enquiry will take place against the background of the evolution of the concept "private company".

15. THE EVOLUTION OF THE CONCEPT "PRIVATE COMPANY"

At least four more or less distinct periods can be distinguished

in/ .....

in the recent evolution of the term private company. These are respectively the period up to the *Companies Acts* of the mid-nineteenth century; the subsequent period up to 1900; the period from 1900 to the coming into operation of *Companies Act*, 1980[260], and the period from then onwards.

15.1 THE PRIVATE COMPANY UP TO 1844

There was a time when the term "private company" was used to identify the equitable joint stock company. This was in eighteenth-century England when the term "corporation" was consistently applied only to bodies incorporated by state authority through either royal charter or Act of Parliament.[261] The term "company" was then employed rather indiscriminately to connote both the incorporated and the unincorporated joint stock company. But to avoid confusion, the term "public company" was applied to a joint stock company created under state authority and the term "private company" to the association not based on royal or parliamentary authority[262], *i.e.* the equitable joint stock company. The term is obviously no longer used in this sense.

15.2. THE PRIVATE COMPANY 1844 - 1900

After the legislation of the mid-eighteenth century the term "private company" came to be employed to denote a company which was not of the public-issue type. When Sir Francis Palmer published his *Private Companies and Syndicates*[263] in 1877, the term appears to have already come into general use. The essence of the type denoted by the term "private company" was, as Cooke puts it, "absence of dealings in capital with the general public, either in subscription to the joint stock fund, or in sales and purchases of shares ...."[264] An early reference by the judiciary to the private company of the type in question, is found in *In re British Seamless Paper Box Company*.[265] Here Cotton, L.J., said:

"It/ .....

> "[I]t is an established fact that when the company was formed it was intended to be a private company, that is, it was intended to carry it on without calling in the public, or issuing any shares except to the then existing shareholders".[266]

Gradually it became evident that not all of the seven subscribers and shareholders need be interested in the concern. Some— even the majority— might be mere nominees for one or more principal shareholders. Thus the practice arose whereby it became possible even for the individual trader to incorporate his business by employing six symbolic subscribers who would each hold one share as nominee for the real owner(s) of the business.

In 1896 this practice was sanctioned by the House of Lords in the landmark decision *Salomon v. A. Salomon And Co. Ltd.*[267] Here it was held that, although the *Companies Act* required a minimum of seven members before a company could be incorporated, the legislature was not concerned with the extent or degree of the interest which might be held by each of the seven members. It was further held that the legislature was not concerned with the proportion of interest or influence possessed by one of the majority of the shareholders over the others or with what motive a person became a shareholder. Lord Halsbury, L.C., in his speech drew a clear distinction between the relations of shareholders *vis-à-vis* third parties and the relations of shareholders inter se. In refusing to lift the corporate veil for purposes of enabling creditors to claim against the company members he said:

> "If they are shareholders, they are shareholders for all purposes ... if six of them were the cestuis que trust of the seventh, whatever might be their

rights inter se, the statute would have made them shareholders to all intents and purposes with their respective rights and liabilities, and, dealing with them in their relation to the company, the only relations which I believe the law would sanction would be that they were corporators of the corporate body".[268]

This judgment is significant not only because, as is generally accepted, it braces the corporate entity principle[269] in the English system, but also because of its impact on the incorporated partnership. If shareholders can at one and the same time be corporators *vis-à-vis* the world but nevertheless inter se stand in the vertical relation of trustee and cestui que trust they should, *à fortiori*, inter se be able to stand in a lateral fiduciary relation.

15.3. THE PRIVATE COMPANY 1900 UP TO THE COMPANIES ACT, 1980

The first record of the legislature's treating the private company as a class apart is found in the *Companies Act*, 1900 §§2(3) and §§6(7).[270] Although that Act introduced a number of a new formalities which were aimed at curbing prospectus frauds, it singled out a particular type of company for purposes of exempting it from those formalities. In the marginal note that company was referred to as a "private company" and in the text itself merely as a "company which does not issue any invitation to the public". The task of statutorily defining and recognizing the private company as a distinct type was not undertaken at that stage. Such a step was not to be mooted before the publication in 1906 of a report by the Loreburn Committee.[271]

The *Loreburn Report* identified the private company in these terms:

"A/ ....

> "A large and increasing proportion of the companies under the Acts were classed in common parlance as *private companies. The number of members of these companies generally does not exceed twenty, and very commonly is not above seven.* The regulations of such companies usually restrict more or less the right to transfer shares. The capital for working such companies is subscribed privately, but they cease to be private companies when they appeal to the public to subscribe for their shares ....[272]

It is significant that the private company so identified fell either into the buffer zone of the statutory regime created by the founding *Companies Acts* (*i.e.* between seven and twenty members, where incorporation was permissible but not compulsory), or into the category of partnership proper, an association which generally has fewer than seven members. Prior to the acceptance of the nominee device, incorporation was thought to be impossible to achieve in this latter situation.

In view of the ease with which the minimum membership requirement was circumvented by incorporators who merely had to resort to the nominee device approved by *Salomon*, the Loreburn Committee concluded that there was no need to change the law by reducing the minimum membership requirement to fewer than seven to accommodate private companies.[273] The Loreburn Committee did, however, feel that it was necessary to distinguish the private company from the public company and that to that end recommended:

> "If any distinction is made in the law applicable to public and private companies, it will be necessary

to/ ....

to define a private company and for this purpose we think that the definition be a company consisting of not more than thirty members and by its regulations restricting the right of transfer of shares, and prohibiting

(a) the increase of the number of its members to more than thirty, and

(b) any invitation to the public to subscribe for any shares, debentures or debenture stock of the company".[274]

This conception of the private company as the antithesis of the public-issue was accepted in principle by the legislature and found its way, with minor amendments, into the statute book in 1907.[275] However, instead of restricting membership to a mere thirty, as was mooted in the *Loreburn Report*, the legislature liberally permitted a private company to have as many as fifty members. Thus a private company came to be defined as

"a company which by its articles -

(a) restricts the right to transfer its shares; and

(b) limits the number of its members to fifty ...; and

(c) prohibits any invitation to the public to subscribe for any shares or debentures of the company".[276]

This definition is found in *Companies Act*, 1948,[277] §§28(1) and *R.S.A. Companies Act*[278] 1973, §§20(1). All companies

which did not qualify as private companies in terms of this statutory definition, subsequently came to be referred to as public companies.

Although the statutory private company so created was in essence but a slightly varied form of the general incorporated company, the legislature afforded it a special statutory status. Despite recommendations to the contrary in the *Loreburn Report*, the legislature afforded the private company two particular privileges. First, the minimum membership requirement was relaxed in the case of private companies so that, instead of seven subscribers and subsequent members, as in the case of a public company, two would suffice.[279] This provision is found in *Companies Act*, (1948), § 1(1)[280] and *R.S.A. Company Act*, 1973, § 32.[281] Second, private companies were exempted from the statutory provisions requiring that a company's balance sheet be made public.[282] Subsequently private companies were exempted from the requirement of furnishing certain further particulars to the Registrar of Companies.[283] For a number of reasons it has also always been cheaper and easier to incorporate a company as a private company rather than a public company.

By virtue of the various advantages enjoyed by a private company over a public company, the former type has virtually swamped the latter. This is apparent from statistics furnished in the annual reports on companies published by the British Board of Trade. Table "A" hereto sets out, in comparative table, figures taken from the said reports showing the number of public and private companies in Britain[284] registered at 31st December for roughly each of the decades since 1911 up to 1968 and for every year since then up to 1979. Out of a total of 50 000 limited companies incorporated at the year ended 1911, 18 600 (or 37,2 per cent) were public and 31 400

(or/ ....

(or 62,8 per cent) were private. In a short period of five years private companies, after starting from the bottom line, were almost twice as numerous as public companies. In 1979, private companies numbered 768 534 (or 97,87 per cent of all companies), and public companies a mere 17 154 (or 2,19 per cent of all companies).

Lack of further statistical information giving a more detailed breakdown, makes it impossible to attribute the immense popularity enjoyed by the private company to any one of the grounds of distinction between private and public companies listed above. What must be accepted, though, is that the reduction of the minimum membership from seven to two, as a result of which it has become possible for partnerships proper to incorporate freely, has played some role in the popularization of the private incorporated company. What is also evident is that the company type around which the English Companies Acts have been built over the years, namely the public-issue company, has long ceased to be the typical company type. The typical English company has in effect become the statutory, private incorporated company.

15.4. THE PRIVATE COMPANY AND THE COMPANIES ACT 1980

The *Companies Act*, 1980, s 1[285] introduces an entirely new classification of companies as "public" and "private" companies. Not only does the Act repeal the time-honoured statutory definition of private company discussed above, but a converse approach to the one followed up to now is adopted.[286] Whereas previously the undefined "public company" was the residual company type, the new "private company" is now installed in that position. Accordingly, public company is now defined and every company which is not a public company as defined, is deemed to be a private company.[287] In terms of the said definition a public company is a company which is limited (whether by shares or guarantee), with a memorandum which states that the company is to be a public company; such company must further have complied with the statutory provisions relative to the registration or re-registration of a company

as/ .....

as a public company.[288] These provisions in essence lay down certain minimum requirements relating to a public company's issued and paid up share capital[289]. For the first time public companies are, like private companies, permitted to be incorporated with two instead of seven members.[290] At the same time the repeal of *Companies Act, 1948, § 28* by *Companies Act*, 1980, *§§ 88(2)*[291] has abolished the upper limit of fifty on the number of members a private company may have, consequently permitting it, too, to have unlimited membership now.

The object of the new system of classification and definition is to permit English companies to be excluded from the E.E.C. Second Directive[292] relating to public limited companies and from the corresponding provisions in the *Companies Act*, 1980. It is more than likely that the ratio between the number of private companies and the number of public companies in existence will swing further in favour of the former type. But that in itself is of little significance from the point of view of the incorporated partnership. For none of the public companies of the previous era which can be classified as private companies under the new classification is likely to be an incorporated partnership. The relevance of this new classification for the incorporated partnership, however, is that the term "private company" with which the incorporated partnership has been associated for more than seventy years, will henceforth in Britain no longer signify the type of company referred to as a private company in the decisions discussed in Ch.VII hereunder.

16. PARTNERSHIP PROPER AND THE INCORPORATED PRIVATE COMPANY: THE INCORPORATED PARTNERSHIP.

During the eighteenth and part of the nineteenth century, the partnership form served the corporate purpose. But by the beginning of the twentieth century the wheel had turned full circle[293] and in the twentieth century partnership and company

changed/ .....

changed roles, the latter now serving the former. During the century and a half preceding the *Companies Acts* of the mid-nineteenth century, the partnership form was, as one commentator describes it, "pressed into the service of joint stock enterprise; a norm designed to enable a small number of associated entrepreneurs to carry on a business in common had acquired the uncongenial function of regulating the mutual relationships of hundreds or even thousands of owners of joint stock".[294] But as the same commentator goes on to explain, by the beginning of the present century, "company law which since 1844, and especially since the conferment of the privilege of limited liability in 1855 ... had been the legal form of joint stock undertakings, had come to annex the functions of the law of partnership".[295]

The reason why these roles were reversed and the incorporated company came to serve partnership proper is essentially that partnership proper lacks legal personality while the incorporated company enjoys it. The Continental *société en commandite*, or the limited partnership, as it is known in English, was statutorily recognized too late in England to be of any significance.[296] Moreover, because the limited partnership itself also lacked legal personality (and still does today),[297] it could not as a general rule[298] be a viable alternative to partnership proper nor assist in the attainment of corporate status. Another drawback of this form of business association is that only limited or special partners (*commanditaires*) enjoy freedom from liability for partnership debts, whereas general partners (*commandités*) are liable in full. Moreover, there must at all times be at least one general partner and a limited partner forfeits the immunity to liability he otherwise enjoys if he participates in the management of the partnership.

The company type which began to assert itself at the turn of the present century proved to be able to fill that void. That

company/ ....

company type is the private incorporated company. Not only did the private incorporate company enjoy corporate status, but, once the law permitted (even a majority of) members of a company to be mere nominees not having any beneficial interest in the shares they hold, the incorporated company could, even when the statutory requirement called for seven members, accommodate even the smallest private partnership of two. Obviously when the private company was statutorily recognized in 1907 and the minimum membership requirement statutorily relaxed to two, it was only natural that more partnerships proper would avail themselves of the opportunity of being incorporated as a statutory private company.

Thus it is not surprising that a renowned English lawyer exclaimed during the first decade after the statutory recognition of the private company: "Certain it is that private companies, or *incorporated partnerships* as they may be called, constitute more than a third nowadays of the whole number of companies registered".[299] The use of this term at this early stage is enlightened. Years later, a New Zealand court described a statutory private company which was being wound up on partnership principles as an incorporated partnership.[300] More recently, a statutory private company was in similar circumstances called an incorporated partnership by counsel in an appeal before the House of Lords.[301] But the term which the judiciary favoured for the statutory private company, which is in essence a partnership proper being carried on through the instrumentality[302] or machinery[303] of a limited liability company, is a "quasi-partnership company".[304] Frequently, though, a company of that character has been referred to as an incorporated partnership by commentators and others. The report of the Jenkins Committee for instance contains the following minute: "[I]n fact many companies are intended to be nothing more than partnerships *incorporated* to obtain limited liability and tax and other advantages .... It has been suggested that ... a new form of corporate body, described as

an/ ....

an *incorporated partnership* should be statutorily instituted."[305] That suggestion was recently reiterated.[306] The fact that the private company was previously exempt from the requirement compelling a company to make its financial statements public and the prohibition against loans to directors has in England been justified on the basis that "a private company is really just an incorporated partnership".[307] And a South African authority described a small private company as being, "the modern equivalent of the old partnership with the advantages of incorporation and limited liability".[308]

So popular did the statutory private company become both in Britain and South Africa - and in fact wherever it gained entry — that it has, in a sense, superseded the partnership proper in all spheres except in certain professions. In the words of one commentator:

> "Today one meets partnerships in Great Britain normally only amongst doctors, chemists, solicitors, accountants and similar members of a business, or other profession. All other enterprises, even if of small size, are promoted in the form of a private company, an institution which enjoys immense popularity ...."[309]

Naturally, when a partnership proper is incorporated — whatever the reasons prompting such a move may be — such a partnership then becomes an incorporated partnership. The commentator referred to ascribes the popularity of the private company to the fact that it enables the incorporators primarily to separate their business assets from their private assets and thus to keep the business creditors away from their personal savings.[310] Another authority agrees:

> "The obvious reasons [for the immense growth of private

companies/ .....

> companies] are the advantages which necessarily flow from corporate personality, separation of the property, rights and liabilities of the company from those of its members, limited liability, facilitation of legal proceedings and perpetual succession".[311]

Obviously a large percentage of private companies must be incorporated partnerships. Yet in the absence of more specific and detailed statistical data it is not possible to quantify such percentage with any precision. At the same time it is obvious that the terms "private company" and "incorporated partnership" are not synonymous. An incorporated partnership is essentially a partnership proper in the guise of a limited liability, that is an incorporated company. The hallmark of partnership proper is the character of the inter se relation of its members. That relation is, as has been seen previously, a personal relation steeped in mutual good faith and confidence. Such a relation is not possible in an association where membership is unlimited or even large. The mere fact that a statutory private company has since 1907 been permitted to have as many as fifty — and since the coming into operation of the *Companies Act*, 1980,[312] any number of — members, makes it possible that there will be private companies in which the inter se relation is an impersonal, arm's length one. Such companies will obviously not be incorporated partnerships.

17. *JUDICIAL RECOGNITION OF THE INCORPORATED PARTNERSHIP*

The judicial recognition which the incorporated partnership has to date enjoyed in the British system, is disappointing. This is particularly so if the lineage of the English incorporated company and the role which the Courts of Chancery have played in the evolution of that legal figure, are taken into account. After all the British incorporated company is in essence but an incorporated partnership albeit in the

mould/ .....

mould of a public-issue partnership. The fate of the incorporated partnership in this regard must be attributed to the British tradition of regarding the statutory company — whether it be a public company or a private company — as a single type. The unfortunate outcome of this approach has been the refusal, up to now, of the legislature to recognize that the truly private company, that is the incorporated partnership proper, and the public-issue company are just as much polar types as partnership proper and corporation, and therefore do not deserve to be in the same statute.

Despite this negative statutory environment, the judiciary in the British system has nevertheless, albeit on a somewhat selected basis and in a somewhat muted fashion, been recognizing the incorporated partnership proper for many years in a long line of decisions commencing with *Symington*[313] and culminating in the landmark decision of *Ebrahimi*.[314] That latter decision has still to be fully appreciated in all its facets. Yet there is reason for optimism for, as a commentator, referring to *Ebrahimi*, points out:

> "The essential characteristic of the private company in its true meaning is, as Lord Wilberforce put it, that it is an *association founded* on a *personal relationship*. Translated into Continental legal terminology, the private company in its true sense is a *Personalgesellschaft* in the form of a *Kapitalgesellschaft*".[315]

By "private company" the commentator of course means "incorporated partnership" or, as it is referred to in the terminology of the judiciary, quasi-partnership company. And by *Personalgesellschaft* the commentator generally means *Personengesellschaft* or *société de personnes*, that is, an association which is established *intuitu personae* as opposed to a *Kapital-*

gesellschaft/ ...

gesellschaft or *société de capitaux*, which is, an association which is established *intuitu pecuniae*. As will be seen in CH.VI hereunder, the personal, fiduciary character of the inter se relation of members of an incorporated company is recognized both in Germany and in the United States if the company in question happens to be a *Personengesellschaft*, in the former jurisdiction, and a close corporation, in the latter. This contrasts sharply with the English experience to date.

In the English system, regrettably, the recognition of the personal character of the incorporated partnership, or to be more precise, the fiduciary nature of the inter se relation of its members, as will be observed in Ch.VII hereunder, has up to now been limited almost exclusively to winding-up situations. If what matters is substance and not form and if in fact an incorporated partnership is but a partnership proper which is being carried on in the guise of a private limited company, English company law has up to now been inconsistent in the extreme. Such inconsistency is manifested by its willingness to recognize the personal, fiduciary character of the inter se relation found in the incorporated partnership for some purposes but not also for other, more appropriate and plausible, purposes. Up to date the judiciary in the British system has, barring some exceptions, recognized the said character only under the just and equitable winding-up provision, that is for purposes of imposing the extreme remedy, winding-up, and not also for purposes of imposing other lesser equitable remedies developed in relation to partnership proper. Where one associate commits a minor impropriety *vis-à-vis* a co-associate, contrary to the dictates of good conscience and mutual confidence which are necessarily implicit in the inter se fiduciary relation

subsisting/ .....

subsisting between such associates, such lesser remedies might often be more appropriate than winding-up. This discrepancy in English company law, and the reasons for it, are shown up by contrasting the English experience in this regard to the American and European experience. It is for this purpose that the Continental and American developments in this field will be considered next.

CHAPTER VI

THE PRIVATE (INCORPORATED) PARTNERSHIP AND THE PRIVATE (INCORPORATED) COMPANY IN THE CONTINENTAL AND AMERICAN SYSTEMS

18. GENERAL

The English private company belongs to a family which is exemplified on the Continent by the German G.m.b.H., and the French S.à.r.l. and in North America by the close corporation.[316] These companies are representative of the private company type since the company law systems in question represent the major company law systems in the world.[317] By comparing how the inter se relation between members of these company types are viewed in the different jurisdictions, it is possible to evaluate what the English system has achieved or failed to achieve in this regard.

Such a comparison promises to be fruitful as the company law systems in question have much in common. The company laws of the two basic systems, the Civil Law of the Continent and the Common Law of the English-speaking world, diverged only during the eighteenth and nineteenth centuries.[318] Of the systems concerned, English company law and American corporation law are possibly the closest. Not only do they share a common culture and language but they are, in the words of an English authority, "based on the same principles of law and equity derived from a common heritage".[319] And as the same authority goes on to point out, these basic principles have not been "submerged or destroyed by differing statutes; on the contrary, neither Britain nor any of the states [in the U.S.A.] has codified the whole of its corporation law. All the statutes presuppose basic principles which for the most part have never been embodied in

statutory/ .....

statutory form".[320]

Thus it is not strange to find English and American courts resorting to principles of equity developed in relation to partnership proper, to resolve internal conflicts in incorporated partnerships. But, as will be seen hereunder, the British and American experience in this particular regard dovetail rather than coincide, complement rather than mirror one another. This verifies the statement that "if there are sufficient basic similarities to make a comparison possible, there are, equally, sufficient differences to make it fruitful".[321] Very much the same applies to a comparison between the private company types found in the Continental and the Anglo-American systems. For while the Continental private company has obviously developed in a different cultural and sociological environment and also along different lines, there are sufficient basic similarities to warrant comparison with the Anglo-American private company type. Both types are centred on partnership proper and in both systems partnership proper shares a common ancestor in the Roman law *societas*. This explains why the age old tradition that partners are bound to exhibit the utmost good faith to one another in their inter se dealings, finds application in the incorporated partnership in all the jurisdictions concerned to a greater or lesser degree. But what is remarkable, is that these norms of exemplary behaviour which have been developing in partnership since Roman law days, find their greatest application in the American version of the incorporated partnership today.

19. *THE CONTINENTAL PRIVATE COMPANY*

19.1. *INTRODUCTION*

It is an acknowledged fact that the Continental private company

generally/ .....

generally bears a greater degree of similarity to a partnership than to a public-issue corporation.[322] Thus it is only to be expected that courts in certain Civil Law jurisdictions would "have been prepared to fully recognize the essential nature of the enterprise as an incorporated partnership and strike down a resolution of the majority on the basis of bad faith".[323] The Continental private company type is modelled on the *Gesellschaft mit beschränkter Haftung*, or G.m.b.H. which was created by the German legislature in 1892.[324] Unlike the English private company which resulted from a long historical evolution, and which was known in practice long before it was statutorily recognized, the German G.m.b.H. came into the world, "without historical antecedent and exclusively by virtue of legislative fiat".[325] But, as will be seen hereunder, that did not prevent the *Gesellschaft mit beschränkter Haftung* from being modelled on partnership. It is for this reason that the G.m.b.H. is regarded as the outstanding German contribution in the field of company law[326] and that it has been copied by legislatures all over Europe with such modifications[327] as local circumstances may require. Austria was first to do so in 1906, then followed France in 1925, Belgium in 1935, Switzerland in 1937, Italy in 1942 and finally the Netherlands in 1971.[328] France played an important role in this movement. She modelled her private company, the *société à responsabilité limitée* (S.à.r.l. for short), as its name indicates, on the German G.m.b.H. which she found in Alsace and Lorraine when those provinces were reacquired from Germany after the First World War. In fact, as one source points out, the introduction of the *société à responsabilité limitée* by an Act of 7th March 1925, "was prompted by the need to settle the fate of the numerous S.à.r.l. set up in these provinces under German law".[329] In turn France passed that model on to the Benelux countries, Italy and Spain.[330]

As/ .....

As has been quite rightly observed, the name, G.m.b.H., or, S.à.r.l, itself is undistinguishing: "limited liability is equally characteristic"[331] of other, non-private companies. The terminology found in Belgium — *sociétés de personnes à responsabilité limitée des associés* or limited liability company of the personal or partnership type — is closer to the mark. Closer still is the Dutch, *besloten vennootschap met beperkte aansprakelijkheid*, or closed partnership — compare the American term "close corporation" — with limited liability, that is intimate partnership with corporate status, or incorporated partnership proper.

19.2. PARTNERSHIP AND THE G.m.b.H. or S.à.r.l.

The object of the legislature introducing the G.m.b.H. in 1892 was, "[t]o create a type of company midway between a *partnership* characterised by the *intuitus personae*, and a joint stock company, operated on a purely capitalist [*intuitu pecuniae*] principle".[332] Judging by the popularity of the G.m.b.H. not only in Germany but elsewhere, it seems as if the legislature has been notably successful in that endeavour.

In Germany a leading campaigner[333] in the movement which ultimately led to the introduction of the G.m.b.H., had in fact recommended that the G.m.b.H. should be modelled on partnership. Although the legislature did not adopt this recommendation in its entirety, it is not without significance that the German courts often apply the partnership norms of the Civil and Commercial Codes when the G.m.b.H. statute is silent.[334] Of particular interest in this context is the willingness of the judiciary to hold members of a G.m.b.H. in apt circumstances liable to inter se fiduciary obligations when the particular company is

a/ .....

a *Personengesellschaft*.

In France, too, the S.à.r.l. was designed to be a type of partnership and not "a narrow version" of the joint stock company.[335] "As it emerged in 1925", the same source states, "the S.à.r.l. did, in fact, rather resemble a partnership with the result that a few authorities class it as such although doctrine for the most part regards it as unique or hybrid".[336] This is not suprising, for the new company type was, after all, "intended primarily to enable firms to be established by a small number of persons wishing to form a permanent partnership, while avoiding liability".[337]

19.3. SEPARATE PRIVATE COMPANY REGIME

To achieve the aim of creating a company type halfway between a partnership and a corporation or A.G., the German legislature wisely decided not to lock the G.m.b.H. and A.G. into one statute and accordingly created a special regime for the G.m.b.H.. In France and in other jurisdictions, the legislature adopted a similar course. In fact, until 1971 when the Netherlands introduced the *besloten vennootschap*,[338] she alone, of the jurisdictions mentioned above, had not yet introduced separate regimes for public and private companies. The basic premise from which this Continental movement proceeds thus is, as a text writer correctly points out, the recognition of the diversity of the company concept.[339] As a result of the recognition of a separate regime for both the capital-orientated joint stock type — the German *Aktiengesellschaft* or A.G., the French *sociétés anonymes* or S.A. and the Dutch *naamloze vennootschap* or N.V. — and the intimate, more personal private type of institution, the latter has been permitted to develop a special, *intuitus personae*, character of its own, as a result of which the personal aspects of the inter se relation of members have

come to the fore.

19.4. SPECIAL PERSONAL CHARACTER OF THE G.m.b.H. & S.à.r.l.

Continental law readily appreciates the disparity between certain basic polar concepts. One such concept is partnership characterized by *intuitus personae* (or *delectus personae*) and the personal relations of mutual trust and good faith to which it gives rise. Another such concept is the capital-orientated A.G. or S.A. characterized by *intuitus pecuniae* and the resultant impersonal relations. This awareness is mirrored in the dichotomy between *Personengesellschaft* and *Kapitalgesellschaft* or *sociétés de personnes* (or *sociétés par intérêts*) and *Sociétés de capitaux* (or *sociétés par actions*).

By *Personengesellschaft* is understood in German law, "a union of several persons in a company of which membership is based upon the person and on the individual members".[340] It would therefore be fair to say that a *Personengesellschaft* is created *intuitu personae*. This is clearly the position in French law where the concept *société de personnes* is, for instance, described in the following terms: "*Les sociétés de personnes offrent ce caractère commun d'être dominées par le contrat qui les crée. La personne morale n'est pas dégagée de la loi du contrat: elle reste marquée par son origine. Or, dans ce contrat, la considération de la personne joue un rôle essentiel: le contrat est conclu intuitu personae*".[341] The hallmark of the *société de personnes* therefore is that the personal characteristics of the associates are mutually important.[342]

Ever'since the introduction of the G.m.b.H. it has been keenly debated whether it is a mere *Kapitalgesellschaft*, like an A.G.,

or/ .....

or a *Personengesellschaft*, like a partnership. Both in strict law and in theory the G.m.b.H. is regarded as a *Kapitalgesellschaft*.[343] This undoubtedly follows from the enabling legislative provisions governing the incorporation of the G.m.b.H.. Members of a G.m.b.H. nevertheless enjoy a great measure of contractual freedom. In fact, the statutory scheme applies only to the extent that it has not been modified by agreement between members, such modification being introduced by way of contrary clauses in the articles of association. In this regard the G.m.b.H. is remarkably similar to the English (incorporated) company whether of the public or private type.

Although a G.m.b.H. is not a partnership proper, its founders enjoy virtually the same contractual freedom as the founders of a partnership in the true sense do. On the other hand, a G.m.b.H. shares certain traits with an A.G. Like the A.G. it is a statutorily created corporate person whose members enjoy full freedom from liability for its debts. Compared with the A.G. the G.m.b.H. is, the question of contractual freedom apart, not only incorporated and administered with a minimum of formality and publicity, but is in fact in many respects more like a partnership. Where, for instance, an A.G. must be registered with a minimum of five members, the G.m.b.H. requires only two. And, unlike the A.G., the G.m.b.H., like a partnership, need not make its financial statements public. Moreover, although there are no legal provisions, mandatory or otherwise, either requiring *intuitus personae* or prohibiting the issue of freely transferable securities (as has been seen in para. 15.4 above, this is in fact also now the position in Britain because of the repeal of *Companies Act*, 1948, § 28), it has never been doubted that in practice, a G.m.b.H. is concluded *intuitu personae*, and, that the shares in it cannot be represented by transferable securities.[344] An authorative source sums it all up in these words:

"In/ .....

> "In practice, however, the G.m.b.H. very often loses its capitalist aspect and bears more resemblance to a partnership. The freedom allowed to the members in organising the company enables them to make their relations conform down to the smallest detail to those existing in partnership. There would consequently be scarcely any de facto situation for which a G.m.b.H. and partnership would not be equally suitable ...." 345)

Thus despite a G.m.b.H. de jure being a *Kapitalgesellschaft*, it may turn out de facto to be a *Personengesellschaft*.[346] A G.m.b.H. of such hybrid character is often referred to as a *Personalgesellschaft*[347] as in the following epigram:

> "*Sie [such a G.m.b.H.] ist typisch eine kleine, intime Kapitalgesellschaft. Daraus ergibt sich, dass sie vielfach - mehr oder minder - eine Hinneigung zu einer Personalgesellschaft aufweist*".[348]

One authority has in this context in fact suggested that, in line with the American [*sic*] usage, namely *incorporated partnership*, the term *"inkorporierten Personengesellschaft"* should be used.[349]

The S.á.r.l. is treated in a very similar fashion in France to the G.m.b.H. Generally the S.á.r.l. is classed as a *société de personnes* because, it seems, a S.á.r.l. is concluded *intuitu personae*. In the words of an authorative text:

> *"Le contrat est conclu intuitu personae. Les associés se connaissent et, bien qu'il n'y ait entre eux aucune solidarité, prennent en considération la personne qui entre dans la société".*[350]

At the same time it is always acknowledged that the S.á.r.l.

shares/ .....

shares several features with the *société de capitaux* and that, since the 1966 legislation the scale has been tipped somewhat towards the latter type. The same source explains:

> "*Les sociétés à responsabilité limitée méritent d'être classées aujourd'hui dans la catégorie des sociétés de capitaux, mais ne sont pas totalement dégagées des sociétés de personnes parmi lesquelles elles avaient leur place jusqu'à la loi de 1966*".[351]

It is thus correct to say that the S.à.r.l. too is a hybrid type — an incorporated partnership of some sort.

On the Continent, recognition of the personal partnership character of the private company proper, that is the incorporated partnership, would therefore appear to some extent to be attributable to the recognition of the dichotomy between *Personengesellschaft* (or *sociétés de personnes*) and *Kapitalgesellschaft* (or *sociétés de capitaux*) and, resulting from this dichotomy, the diversity of the company concept. In terms of this latter conception, the private company proper is, as an English commentator aptly remarks, "a form of business organization sui generis, a legal person in form and a partnership in essence economically a hybrid between a company and a partnership."[352] The relevance of the said dichotomy and of the diversified company concept for the operation of inter se fiduciary duties, will be considered in further detail hereunder.

20. THE AMERICAN CLOSE CORPORATION

20.1. INTRODUCTION

The American experience in the field of corporation law stands in stark contrast to the English experience in company law in many relevant respects. The first obvious contrast is found in basic terminology. In the United States the terms "corporation" and "incorporated" are used whereas the terms "company" and "limited" are used in the English system. This different usage dates back to a differentiation of structure which emerged in the eighteenth century.[353] Cooke explains:

> "In America business was never troubled with the difference between corporate and unincorporate form after the Revolution. It moved rapidly towards corporations on the one hand and partnerships on the other. In England the main trend of development was towards an intermediate form — not corporation, not partnership, but company [that is incorporated partnership] acting under a deed".[354]

And what is particularly significant in this regard is, as Gower remarks, that, "although America was earlier in her recognition of the distinctive roles of partnerships and corporations, she never drew the distinction between them with the same clarity as England has done since 1844".[355] The very close bloodties between the English [incorporated] company and partnership necessitates the discrete distinction which English law endeavours to draw between the said two concepts. In view of the ancestry of the American corporation, American law does not find it necessary to concern itself with this distinction to the extent that English law does.

This divergence between British company law and American corporation law is deeply rooted in history and is to some extent attributable to the indifferent approach adopted in North

America/ .....

America to the infamous *Bubble Act*.[356] In the New World the *Bubble Act*, despite its being extended to the colonies in 1741,[357] "seems wisely to have been ignored".[358] As a result the unincorporated equitable joint stock company "though not unknown, was correspondingly less important".[359] According to Cooke the corporation was already a familiar figure in American economic life, particularly in New England by the end of the eighteenth century. Cooke gives the following account:

> "One effect of the American Revolution was to upset the English tradition that incorporation was to be granted only after inquiry into the merits of petitions for it. The American system, based on equality of treatment, rejected the partiality of the English method. The Crown and the Crown's prerogative of granting charters had been overthrown; equal privileges for all meant equality of rights to incorporation. Again, the avenue to a charter from the State legislature was broader and smoother than the tortuous and difficult approach to a Bill in the English Parliament. Hence the unincorporated joint stock company had no real reason to remain unincorporated ...."[360]

Thus it is not surprising that incorporation by registration under a general act became possible in North America more than three decades before it did in Britain.[361] However, as Gower points out, "the model which the [American] legislative draftsmen had in mind was the statutory or chartered corporation rather than the unincorporated company or partnership".[362] Because of this "modern American corporation law owes less to partnership and contractual principles than does the British"[363] company. The result is that the American corporation is

"less/ ....

"less flexible than the English model".[364] It must be borne in mind, however, that in those states where general incorporation only became possible at a later stage in history, the limited partnership, as will be observed in para. 20.3 hereunder, made its presence felt.

Although America admitted general incorporation long before Britain did, she was much slower in recognizing the private business corporation, that is, the close corporation. In fact it was not until after the Second World War that the close corporation shed its orphan image.[365] And what is remarkable is that the close corporation, despite both its late start and its lack of partnership ancestry, soon surpassed the English private company[366] to lead the field in being recognized as bearing inter se fiduciary duties akin to those found in partnership proper. What is interesting to observe is that the close corporation in this regard displays a trend similar to the one developing in the German G.m.b.H. despite the gulf that separates the two legal systems.

20.2. *THE NOTION OF THE CORPORATE PARTNERSHIP AND THE INCORPORATED PARTNERSHIP*

20.2.1. *INTRODUCTION*

The reasons why the private business corporation, that is the *close* corporation, turned up so late in North America are certainly manifold and complex. Part of the explanation, however, must be sought in the prevalence of the limited partnership in the New World. Unlike Britain where this form of business association never established a foothold, the limited partnership established itself in America in the early part of the previous century. In fact, in many states limited partnership

acts/ .....

acts preceded by several decades the general incorporation acts[367] with the result that the limited partnership out of necessity substituted for the corporation. "The impetus for adoption here", as one authority explains, "was the desire to avoid the doctrine of partnership liability to third persons, based on profit sharing ...."[368] In very much the same way the concept of the limited partnership would later inspire the notion of the *close* corporation or private business corporation. Prior to courts and legislatures in some states permitting corporators to import partnership proper principles into a corporation, turning the latter effectively into an incorporated partnership, the limited partnership again had a useful role to play. It now substituted for the corporation in those cases where both the protection of corporate status and the intimacy and flexibility of the partnership form were required.

20.2.2. *THE STATUTORY INTRODUCTION OF THE CORPORATE (OR LIMITED) PARTNERSHIP*

The first limited partnership act to be adopted in an Anglo-American jurisdiction was adopted by the New York legislature in 1822.[369] The New York statute was modelled on the French *société en commandite*[370] which settled in Louisiana with the French. In fact, fourteen years prior to the efforts of the New York legislature, the Louisiana legislature made provision for the *société en commandite* in the Louisiana Civil Code of 1808, calling it in English the "corporate partnership".[371] Today all states (except Louisiana) as well as the District of Columbia and the Virgin Islands, have enacted, in one form or another, the provisions formulated in the 1916 version of the Uniform Limited Partnership Act,[372] which, in turn, are largely based on the earlier New York legislation.[373] It is evident that the limited partnership is taken seriously in the United States as the question whether limited partners

owe/ .....

owe inter se fiduciary duties has come up for judicial decision there while the issue does not appear to have been raised outside that country. In the New York Court of Appeal Mr. Justice Scott,[374] in dealing with this issue, pointed out that *delectus personae* does not usually apply to special or limited partners in that the consent of the general partners is not usually required in respect of a sale by a limited partner of his interest in the partnership and held:

> "Indeed throughout the whole act [the Uniform Limited Partnership Act] ... the special partner, so far as concerns his relations to his general partners, is treated as a mere contributor of capital [i.e. as having joined the association *intuitu pecuniae*] with none of the rights or liabilities belonging to general partners .... The element of mutual trust and confidence, which is the keynote in the relation between general partners, is wholly and conspicuously lacking".[375]

At the same time the symbiotic union between limited partnership and corporation (as in the German G.m.b.H. & Co.[376]) is also found and recognized here.[377]

In North America the limited partnership has, true to its original English name on that continent, namely, "corporate partnership", inspired the idea of a form of business organization between the polar types, partnership and corporation. In that fashion the limited partnership has made a real contribution to the evolution of the idea of the incorporated partnership.

20.2.3. *THE STATUTORY INTRODUCTION OF THE (LIMITED) PARTNERSHIP ASSOCIATION*

Four states, namely Ohio, New Jersey, Michigan and Pennsylvania, have/ ....

have statutorily created what is called the "limited partnership association" in the first two states, and the "partnership association" in the last two.[378] Pennsylvania adopted the partnership association as early as 1874. Michigan followed suit in 1877, New Jersey in 1880 and Ohio in 1881.[379] In 1966 Pennsylvania repealed the enabling statute save insofar as it applies to associations solely of professional persons not authorized by law to practice as a corporation.[380] At that time it appeared that New Jersey was the only state using this form of business organization to any significant extent.[381]

What is significant is that the partnership association is regarded as having "more of the attributes of a corporation than does the general or limited partnership", although it is nevertheless recognized "as a form related to partnerships".[382] It is distinguished from the limited partnership in that all the partners, and not only some of them, are immune from liability for the debts of the association.[383] At the same time the association is generally regarded as a right-and-duty-bearing unit and not as a mere aggregate of individuals as is the case in the ordinary partnership.

When a New Jersey court was faced with the issue whether a member of such an association could be considered an employee within the coverage of the Workmen's Compensation Act, it held that such a company is "a hybrid creature" and that "it might be called a *quasi*-corporation."[384] In truth these associations are in fact incorporated partnerships. One commentator has aptly suggested that the said statutes in these four states dealing with the partnership association might be called "special statutes for close corporations".[385]

20.2.4. *THE CONCEPTION OF THE INCORPORATED PARTNERSHIP AND OBSTACLES IN ITS WAY*

It is against this background of the corporate partnership that

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another commentator suggested that the Uniform Partnership Act should be re-enacted but "with limited liability language added" or conversely, that the Uniform Limited Partnership Act should "be re-enacted, but with limited liability applicable to all partners".[386] What entrepreneurs want in effect is "the best of both worlds — the limited liability of the corporation and the intimacy of the partnership".[387] In order to achieve this goal, entrepreneurs either conduct a partnership through the instrumentality of a corporation,[388] or, in terms of a shareholders' agreement, set up management and financial arrangements "separate from and often in conflict with that contemplated by the corporation law",[389] whereby the affairs of a corporation are conducted.

In view of the strict concession theory approach adopted in America, it is not surprising that such arrangements have been struck down by courts in many states. In terms of the concession theory — also called the fiat theory[390] or franchise theory — the fact that a corporation is created by state or sovereign grant is emphasized, such emphasis often giving rise to a "rather strict construction of corporation statutes by the courts which insist that the corporate form adhere rather strictly to the statutory norms".[391] After the concession theory was received in English law from canon law in the fifteenth century[392], it emigrated to North America with the early colonists. Here it fell on fertile soil and flourished. In the words of Maitland: "Nowhere has the concession theory been proclaimed more loudly, more frequently, more absolutely than in America".[393] A clear application of the concession theory approach is found in *Benintendi*, a famous New York case in which corporate bylaws requiring unanimity were struck down. Here Mr Justice Desmond said: "The state, granting to

individuals/ .....

individuals the privilege of limiting their individual liabilities for business debts by forming themselves into an entity separate from the persons who own it, demands in turn that the entity take a prescribed form and conduct itself procedurally, according to fixed rules".[394]

20.2.5. *JUDICIAL INTOLERANCE OF THE PARTNERSHIP CORPORATION*

Given, on the one hand, the desire of corporators both for limited liability, for freedom of consensual arrangement and a flexible association, and on the other hand, rigid statutory rules prescribing incorporation, a head-on collision was inevitable. Such showdown is highlighted in the early New Jersey decision of *Jackson* v. *Hooper* .[395] Here an attempt by stockholders to contractually arrange their affairs inter se as if they were partners, was struck down by the court.

This case is a typical case of a partnership being conducted through the instrumentality of the corporation. *J* and *H* employed two corporations, one English, one Illinoisian, as mere agencies for carrying on various businesses undertaken by them. In terms of a shareholders' agreement they undertook that as long as they were associated in business they would conduct such business by mutual assent. It was also agreed that their ownership interest and control in management would be equal. Except for nominal shares, which were held by three other persons to qualify them as directors, *J* and *H* owned all the shares in the two corporations in equal shares. Profits were withdrawn by *J* and *H* in equal amounts. Although the two corporations were employed as agencies for implementing the policy agreed to by *H* and *J* from time to time, there were times when these corporations were by-passed and *J* and *H* transacted business in their

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own names. Disagreement arose and *J* found himself outvoted and excluded from participation in the business which was turned over to *H* who allegedly, through mismanagement, waste and unnecessary disposition of assets, was running the business down. *J* instituted proceedings for the dissolution of the partnership, an accounting of its affairs and an injunction to restrain the defendants from withdrawing assets from the business and excluding him therefrom. Although *J* was successful in the court *a quo*, the Prerogative Court of New Jersey reversed that ruling and held:

> "The law never contemplated that persons engaged in business as partners may incorporate, with intent to obtain the advantages and immunities of a corporate form and then, Proteus-like, become at will a co-partnership or a corporation, as the exigencies or purposes of their joint enterprise may from time to time require. The policy of the law is to the contrary. If the parties have the rights of partners they have the duties and liabilities imposed by law and are responsible in solido to all creditors.
>
> If they adopt the corporate form, with the corporate shield extended over them to protect them against personal liability, they cease to be partners and have only the rights, duties and obligations of stockholders. They cannot be partners inter se and a corporation as to the rest of the world ".[396]

The above passage has since been quoted in other courts, particularly in those of New York. Thus, for instance, the New York Court of Appeals relying on the above passage in *Weisman* v. *Awnair Corp. of America*[397] held in 1957:

"[W]hen/ .....

> "[W]hen individuals do determine to conduct business through a corporation, as is here alleged, they are not at one and the same time joint venturers and stockholders, fiduciaries and non-fiduciaries, personally liable and not personally liable ...
> Inasmuch as it is not possible for individuals to carry on a joint venture through the instrumentality of a corporation, no confidential or fiduciary relationship can be said to exist between the parties and the equitable relief of an accounting is not available to plaintiffs".[398]

In terms of these decisions it would therefore appear that, prima facie, limitation of personal liability and the continuance of a fiduciary relationship are legally incompatible.[399] But such a proposition has not been generally acclaimed[400] and has since fallen into disfavour. This is largely due to the recognition of the incorporated partnership under the general name of close corporation.

20.3. RECOGNITION OF THE CLOSE CORPORATION

20.3.1. INTRODUCTION

In the same way as the term "private company" is generally used to indicate the opposite of a public-issue company in the English system, the term "close corporation" is often used in the American system to indicate the opposite of the public-issue or held corporation.[401] No unanimity exists as to what a close corporation is, however.

20.3.2. THE CLOSE CORPORATION STATUTORILY AND JUDICIALLY DEFINED

Sometimes the term "close corporation" is statutorily defined, at

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other times, judicially. One commentator is of the opinion that although the statement " a close corporation is like a spiral staircase, hard to describe but recognizable when you see one", is true, it is not appropriate to the statutory de-definition.[402] Unfortunately this is not entirely correct as even some of the statutory "definitions" are no more than mere synonyms.[403]

20.3.2.1. STATUTORY DEFINITIONS

In some states — like for instance Delaware, Pennsylvania and Kansas — a close corporation is statutorily defined as a corporation whose charter provides that its stock shall be held by not more than a specified number of persons; that its stock shall be subject to restrictions on transfer and that the corporation shall make no offering of its stock which would constitute a *public offering* as defined in the United States Securities Act of 1933.[404] The Illinois statute again requires that in order for a corporation to qualify as a close corporation, the transfer of shares of its stock must be subjected to one or more of enumerated permissible restrictions.[405] In this sense a close corporation is clearly but the opposite of a public-issue corporation or a corporation whose securities are traded over the counter. The Maryland statute in "a classic non-definition 'defines'"[406] a close corporation as a corporation whose charter states that the corporation is a close corporation.[407] The Californian statute again rolls these elements into one, defining a close corporation as a corporation whose articles both limit the number of shareholders to a specific number not exceeding ten, and state that "[t]his corporation is a close corporation".[408] In the proposed *Statutory Close Corporation Supplement* to the *Model Business Corporation Act*[409]

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a very similar approach is adopted: A statutory close corporation is defined as a corporation whose articles of incorporation contain a statement that the corporation is a statutory close corporation.[410] Any corporation organized under the General Business Corporation Act and having less than 50 shareholders may become a statutory close corporation by amending its articles of incorporation to include the statement referred to immediately above.[411]

20.3.2.2. JUDICIAL DEFINITIONS

The judicial definitions of the close corporation are particularly significant. They tend to focus on the incorporated partnership concept. Just as in England not all private companies are viewed as incorporated partnerships, so in the United States not all close corporations are treated as incorporated partnerships. The term "close corporation" is, however, reserved by some scholars to refer to the incorporated partnership concept of close corporations.[412] This lead is followed by the judiciary in many states. "The term close corporation", O'Neal acknowledges, "is sometimes used to designate an incorporated enterprise in which the participants consider themselves partners inter sese and have tried by shareholders' agreement or otherwise to obtain for the enterprise one or more partnership advantages or attributes."[413] In this sense the close corporation has been referred to as a "chartered partnership"[414] an "incorporated partnership"[415] and "a corporation de jure and a partnership de facto".[416] Possibly the most comprehensive definition of the term "close corporation" in this sense is found in the recent decision of the Massachusetts Supreme Judicial Court.[417] Here Tauro, C.J., after reviewing

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a number of earlier judicial definitions, came to the conclusion that both integration of management and control and paucity of shareholders (and the corollary thereof, namely absence of a market for the shares of the company), are all elements of the definition of a close corporation. "We deem a close corporation to be typified", Mr. Justice Tauro said, delivering the judgment of the court" by (1) a small number of stockholders; (2) no ready market for the corporate stock; and (3) substantial majority stockholder participation in the management, direction and operation of the corporation."[418] As will be seen in Ch.VII hereunder, this definition bears remarkable resemblance to what Lord Wilberforce in the slightly earlier House of Lords' decision in *Ebrahimi*[419] described as typical elements which justify the superimposition of equitable considerations of a *personal character* arising between one individual and another in a small private company. Such considerations, even though they are not contained in the company's articles of association, Lord Wilberforce was prepared to concede, nevertheless make it unjust or inequitable to insist on legal rights, or to exercise those rights in a particular way.[420]

What stands out in a comparison of the Massachusetts' and House of Lords' decisions, is that although Lord Wilberforce was at pains to hold out that he was not referring to a particular company type — as he was in fact doing — Mr. Justice Tauro, laboured under no illusions in that regard. "As thus defined," the Massachusetts judge stressed, "the close corporation bears striking resemblance to a partnership. Commentators and courts have noted that the close corporation is often little more than an 'incorporated' or 'chartered' partnership".[421] This is so, because, as Mr. Justice Tauro acknowledged "[t]he stockholders 'clothe' their partnership 'with benefits peculiar to a corporation, limited liability, perpetuity and the like'".[422]

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It is under these circumstances that the learned judge went on to hold that "[m]any close corporations are 'really partnerships, between two or three people who contribute their capital, skills, experience and labour'".[423] It is this type of close corporation with which this thesis is concerned and which will be subjected to further scrutiny hereunder.

Here it should be noted, though, that when the individual partners who incorporate their partnership are themselves corporations, the resultant association is usually referred to as a "joint venture corporation".[424] The shareholders of such a venture are described by a leading commentator in these terms, "they consider themselves joint venturers (in other words, 'partners' engaged in an undertaking of limited scope), just as shareholders in a close corporation often think of themselves as partners...."[425] And again, [m]ost of the problems of close corporations ... are equally the problems of joint venture corporations."[426] Some courts, in line with *Jackson*,[427] have in effect held that joint venture and corporation are mutually exclusive business forms, that is, a joint venture agreement does not survive incorporation with the result that participants in an enterprise cannot at one and the same time be both joint venturers and stockholders.[428]

20.3.3. STATUTORY RECOGNITION OF THE CLOSE CORPORATION

20.3.3.1. INTRODUCTION

It is difficult to assess whether the idea of a private business corporation in American law owes more to the English private company than to the Continental type. On balance it would appear that the English institution played the predominating role in this regard.

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In 1929, in what was possibly the first appeal for the statutory recognition of the American close corporation, an early commentator noted, "we have drawn many a lesson from the English law ... Its system of private companies deserves at least a hearing".[429] Particularly significant is the fact that "[t]he first sign in the United States of a consciousness of a theoretical difference [between the public-issue corporation and the close corporation] comes", as the said commentator put it, "from an unexpected quarter — the Treasury Department".[430] And it is in this endeavour to class small corporations with partnerships for income tax purposes that the parallel with the Continental development arises. For, as the said commentator went on to acknowledge, "[t]his has its historical counterpart. One of the chief reasons for introducing the G.m.b.H. in Austria was the severity of the ordinary corporation taxes, and in Germany the former was favoured in taxation from 1892 to 1902".[431] How remarkable the vision of that pioneer commentator was, is evident from the following lines recorded more than a half a century ago:

> "The temptation to prophesy grows by example: will this proposal be looked upon some day as the starting point of a change in our corporation laws? That some such change should come sooner or later seems desirable ... If we are to avoid burdening the private company with regulations necessary only for the large, we must sever the small and the large. Equally so if we are to regulate the large with a proper consideration of the interests involved".[432]

Today close corporations are realities of life.[433] In fact, although the statistical data that are available do not distinguish between public-issue and close corporations, it is generally accepted that in America, as in Britain and on

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the Continent, the number of public-issue corporations which are in existence is minute compared to the number of close corporations in existence. In America, however, unlike Europe, the question whether to enact completely separate close corporation statutory provisions or whether to include close corporation statutory provisions within the general corporation statute, remains unresolved. The main obstacle to what is sometimes referred to as *integrated*[434] close corporation statutes — special separate statutes or a separate division of the business corporation act to deal with close corporations and their specific needs — is mainly one of definition: the difficulty of distinguishing the close corporation from the public-issue corporation.[435] This was in fact the fate that befell the "Close Corporation Law" which another commentator[436] mooted for New York as early as 1943.

Since those early days considerable progress has been made in the field of close corporation legislation, particularly after World War II, and more particularly after the pioneering legislation of the three Southern States, North Carolina in 1955, South Carolina in 1962,[437] and Florida in 1963. Before proceeding to consider the more relevant provisions of these pioneering close corporation statutes, it is desirable to identify the two main objectives to be achieved by close corporation statutes. The primary aim of the pioneering close corporation legislation was to blunt the cutting edge of the concession theory — that villain of the close corporation piece. In the words of one commentator: "[t]he preeminent purpose of close corporation legislation is to free planning from senseless legal obstacles ... [T]he price for limited liability and the corporate entity privilege is not a planning straightjacket".[438] The first step in this direction was to statutorily overrule *Benintendi*[439]; the second was to legalize partnership-like agreements such as those struck down in *Jackson*.[440] In both

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these respects close corporation legislation has been successful. This last-mentioned type of provision will be considered in para. 20.3.3.2 hereunder. The third step was the introduction of measures to permit deadlock and other conflict situations to be resolved by means of dissolution, as in partnerships. This idea too has had to overcome the bias of the concession-theory approach and is making headway only slowly. This development will be considered in para. 20.3.3.3. hereunder. Another primary object of close corporation legislation is to minimize unfairness and unconscionable conduct in the close corporation.[441] But, as the same commentator laments, "[t]o date, close corporation legislation has missed the boat on this point".[442]

20.3.3.2. STATUTORY REJECTION OF JACKSON

The first attempt to rescue from rude invalidation by uncomprehending courts, contractual arrangements between close corporators whereby they invest their corporation with benefits peculiar to partnership came from the North Carolina legislature.[443] The hub of the cardinal provision in question is that, in a corporation whose shares are not generally traded in the markets, a written agreement assented to by all shareholders (whether embodied in the charter or bylaws or in a written side agreement) and relating to any phase of the corporation's affairs, shall not be invalid as between the parties thereto, "on the ground that it is an attempt by the parties thereto to treat the corporation as if it were a partnership or to arrange their relationships in a manner that would be appropriate only between partners ...."[444] This provision has been correctly described as the rejection of the "philosophy, exemplified by ... *Jackson* that there is something reprehensible about adopting a corporate form for an incorporated partnership and yet retaining a quasi-partner relationship among the co-owners of the close corporation".[445]

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It is also, quite rightly, regarded as the "basic philosophy provision relating to close corporations that are virtually incorporated partnerships".[446] Enacted in 1955, the said statutory provision took effect in 1957. It may be described as an unintegrated, close corporation statute. In 1962 South Carolina enacted an abbreviated version of this provision.[447]

An almost identical provision[448] was contained in the first separate, integrated close corporation statute[449] which was enacted by Florida in 1963, but which has since been repealed.[450] A provision on the same lines is still found today in what could possibly be described as the leading integrated close corporation statute, namely the General Corporation Law of Delaware[451] which first saw the light in 1967.

In 1975 the Californian legislature, when it enacted its unintegrated close corporation provisions, introduced a similar provision.[452] One commentator sees in this provision the "substantive heart"[453] of the special provisions relating to close corporations and refers to shareholder management which is permitted by this provision as "the logical outcome of the incorporated partnership concept".[454] Other commentators draw attention to the significance of this provision by emphasizing the importance in the close corporation of the shareholders' agreement and by recalling that "shareholders in a close corporation not uncommonly want to be shareholders to the outside world but partners among themselves".[455] The Californian legislature went further than any of the other state legislatures in its efforts to ensure the enforcement of these incorporated partnership arrangements. It specifically provided that the failure of a close corporation to observe corporate formalities relating to meetings of directors or shareholders in connection with the management of its affairs,

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pursuant to an agreement authorised by § 300(b), shall not be considered a factor tending to establish that the shareholders have personal liability for corporate obligations.[456]

Both these concepts are found in the *Proposed Statutory Close Corporation Supplement*[457] which may be described as an integrated statute, in a more polished form. For example the provision validating arrangements whereby shareholders arrange their inter se affairs as those of partners, expressly mentions written agreements which regulate the exercise of corporate powers and the management of the business and affairs of the corporation, and written agreements which regulate the relations among the shareholders of the corporation.[458] More important, a further provision[459] expressly validates all such agreements in positive terms as opposed to the negative language employed in the earlier statutory provisions referred to above.[460] Should the court wish to pierce the corporate veil merely because the close corporation in question happens to be an incorporated partnership, there is language to prevent it doing so in equally clear terms:

> "The failure of a statutory close corporation to observe usual corporate formalities or requirements relating to the exercise of its corporate powers or the management of its business and affairs shall not be grounds for imposing personal liability on the shareholders for obligations of the corporation".[461]

Thus the legacy of *Jackson* is buried statutorily.

20.3.3.3. STATUTORY AUTHORITY FOR LIQUIDATION IN THE EVENT OF DEADLOCK AND DISSENSION

As a general rule American courts are loathe to resort to the "drastic"/.....

"drastic" remedy of pronouncing a forfeiture of a corporate charter.[462] In the words of a feted commentator: "[D]estruction of the legislative creature [the right-and-duty-bearing unit] is not easy. Historically the courts have been reluctant to destroy it except under conditions expressly spelled out by the legislature as warranting such action; and even under such conditions the courts are wont to speak of dissolution as a 'drastic' remedy and to seek almost any other available alternative before resorting to it".[463] The same commentator convincingly argues that this dogma, this "sacred cow of corporate existence",[464] is misplaced in the arena of close corporations, that is right-and-duty-bearing units, typically organized by individuals seeking the benefits of incorporation while regarding themselves as partners.[465] In this regard the commentator finds the partnership analogy obviously apt,[466] and concludes: "a simple and flexible remedy for deadlock or stalemate must be provided, and the untouchability of the sacred cow must not be permitted to impede its exercise".[467] What is required, the commentator stresses, "is faith in the sensitivity of the Chancellor's foot, and to permit him, with due dignity, and in a proper case, to apply the boot to the sacred cow of corporate existence".[468]

This, basically was, the policy followed by the South Carolina legislature in 1962, guided as it was by a desire to permit shareholders in a close corporation to act inter se virtually as if they were partners.[469] It is therefore not surprising that in terms of the *South Carolina Business Corporation Act*,[470] courts are empowered to decree the dissolution of, and to liquidate the assets and business of, a corporation in an action brought by a shareholder on grounds which have clearly been inspired by partnership precepts.[471] One such ground is division between shareholders with respect to the management of the corporation resulting in irreparable injury to the

corporation/ .....

corporation or inability to conduct the business and affairs of the corporation to the advantage of the shareholders generally.[472] A related ground is a corresponding division between directors coupled with the further inability of the shareholders to terminate such division.[473] Another ground is such division among shareholders as results in their failure to elect successors to retiring directors for a period which includes at least two consecutive annual meetings.[474] Other grounds include the misapplication or waste of corporate assets,[475] and conduct by directors or controllers of a corporation which is illegal or fraudulent or dishonest, or which is oppressive or unfairly prejudicial either to the corporation or to any shareholder.[476] What is extremely significant is that the legislature has found it necessary to provide that a dissolution based on any of the above grounds shall not be denied solely because it is found that the business of the corporation has been or could be conducted at a profit.[477]

Equally significant are the provisions of *South Carolina Business Corporation Act*, §§12.23[478] which invest the court with a discretion to grant relief other than dissolution. This provision has been modelled[479] on the *Companies Act*, 1948,[480] § 210. It provides that in any action filed by a shareholder to dissolve the corporation on the grounds discussed above, the court may make such order or grant such relief, other than dissolution, as in its discretion it deems appropriate. This relief may include, but is not limited to, an order: cancelling or altering any provision contained in the articles of incorporation or in the bylaws of the corporation; cancelling, altering or enjoining any resolution or other act of the corporation; directing or prohibiting any act of the corporation or of shareholders, directors, officers or other persons party to the action or providing for the purchase, at their fair value, of shares of any shareholder, either by the corporation or by other

shareholders/ .....

shareholders.[481] The court is specifically empowered to grant such relief as an alternative to a decree of dissolution or whenever the circumstances of the case are such that relief, but not dissolution, would be appropriate.[482]

In the *Proposed Statutory Close Corporation Supplement*,[483] § 16 the dissolution provisions and the alternative remedy provisions found in the *South Carolina Business Corporation Act*,[484] as discussed above,[485] are neatly re-arranged and combined in a single, coherent provision. Not only is the range of relief which the court may grant spelled out in much greater detail than in existing legislation, but the drastic remedy, dissolution, is held out to be appropriate only as a last resort, *i.e.* becomes available only after all other relief ordered by the court has failed to resolve the dispute.[486] In line with this approach, relief is not tied to either a dissolution suit or the establishment of grounds for dissolution, as it is in existing legislation.

A further provision that deserves mention, is *Proposed Statutory Close Corporation Supplement*,[487] § 15. This provision, is not novel and is found in existing state legislation.[488] It is intended to afford members of a statutory close corporation, if they so elect, essentially such powers of dissolution as partners enjoy. In essence it provides that the articles of association of a statutory close corporation may grant any shareholder an option to have the corporation dissolved at will or upon the occurrence of any specified event or contingency.

In the light of the legislative provisions and the proposals discussed above, it is clear that the previously popular notion that there is something sacrosanct about a corporation is on the wane. In appropriate circumstances a corporation will

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be dissolved almost in the same fashion and almost as easily as a partnership. That would particularly be so if the close corporation happens to be an incorporated partnership.[489]

20.3.3.4. LEGISLATIVE SILENCE WITH REGARD TO MEMBERS' INTER SE FIDUCIARY DUTIES

By de facto definition the close corporation involves, as one commentator correctly observes, few participants who are associated "on a fairly intimate personal basis and in a relatively closely-knit relationship".[490] From this it follows that the "highly personal and closely-knit relationship" which constitutes the associative relation which is statutorily recognized as a right-and-duty-bearing unit, "makes a stringent fiduciary principle more appropriate as a basis for defining the legal concepts to control that relationship".[491] This must be so because such an associative relation is essentially concluded *intuitu personae*, as other observers point out, and is consequently "like partnerships... based on personal relationships that give rise to expectations that legislatures and the courts should protect, though they seldom have done so in the past".[492] It must be acknowledged though, that courts have here, as will be observed in para. 20.3.4.4. hereunder, been less remiss than state legislatures.

This omission on the part of the legislature has not gone unnoticed. Twenty years ago a commentator, dealing with the fiduciary duty concept in incorporated partnerships and joint ventures, suggested that the early Close Corporation Statutes did not go far enough with regard to validating partner-like arrangements between members of a close corporation.[493] This commentator came to the conclusion that it would be better to provide that no provision of the Business Corporation Law shall be deemed to preclude a court from finding that stock-

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holders have agreed, expressly or by implication, to treat each other as though they were partners or joint adventurers.[494] That suggestion itself does not go far enough. What is required is a provision stating, in express terms, that members of a close corporation, just as partners in an unincorporated partnership proper, are to be held to inter se fiduciary duties of the highest order both in regard to the operation of the business and to their dealings among themselves. This has in fact been mooted recently by an acknowledged expert in the close corporation field.[495] A provision of that nature would be sound and in accord with reality and should be supported as such. Not surprisingly, courts have on occasion held close corporators to strict partner-like fiduciary duties despite the absence of any express agreement between such corporators to that effect.

It is therefore obviously disappointing that the otherwise enlightened *Proposed Statutory Close Corporation Supplement*[496] does not contain any positive proposals in this regard. It is true that the said proposals do provide, as has been seen above,[497] for incorporated partnership arrangements between members of a statutory close corporation. Such arrangements may obviously provide that the parties thereto shall be bound by partners' inter se fiduciary duties. However, in order to attain validity and be enforceable, such agreements must not only be unanimous but must at the same time be in writing. In this way the onus to establish written, unanimous agreement is effectively passed back to the corporate partner who wishes to enforce an inter se fiduciary obligation against a fellow corporate partner. Might it not be better to provide instead that, in the absence of an agreement to

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the contrary, all close corporators shall be deemed to be subject to partners' inter se fiduciary obligations? This, in effect, is the approach that has been adopted by many courts up to now, a practice which is realistic and may be expected to continue even in the absence of a change of heart by the legislature.

20.3.4. JUDICIAL RECOGNITION OF THE CLOSE CORPORATION AS AN INCORPORATED PARTNERSHIP

20.3.4.1. INTRODUCTION

It is fitting to commence a discussion of the topic under consideration with the following passage from one of the earlier commentaries in the field:

> "Corporation law confirms the eternal triangle of statute, common law and custom ... In a no-man's land unoccupied by the legislature, the 'incorporated partnership' ... is a reality. Not the legislature, but the judges (who must deal with lawyers) and the lawyers (who must deal with clients) have quickened into life a type of business organization needed to meet the exigencies of the market place".[498]

The business-organization type which the observer refers to, which was shaped by and honed to the needs of the market place and was recognized by the judiciary, is a species of close corporation which is appropriately referred to as the incorporated partnership. What will be found to be particularly significant in this recognition by the judiciary of the incorporated partnership, is the liberal resort to partnership proper concepts. This is not surprising for, in partnership proper business practice found a more or less ideal vehicle,

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suitably invested it with corporate status and aptly christened it, *chartered*[499] or *incorporated partnership*. And as the more commonly used name for this corporation type indicates, namely *"close* corporation", the focus here, just as in a partnership proper, is on the inter se relations of the associates, that is, the (close) corporators or the "partners". Such relations must necessarily be close, intimate and personal and therefore give rise to fiduciary obligations of the highest order. Two recent judicial pronouncements bear this out. For example a Massachusetts court in 1975 observed that many close corporations are really partnerships between two or three persons who contribute their capital, skills, experience and labour.[500] That court consequently came to the conclusion that the relationship among the stockholders in a close corporation must, just as in partnership, be one of trust, confidence and absolute loyalty if the enterprise is to succeed.[501] At about the same time a New Jersey court came to a remarkably similar conclusion. In that instance the court held that to denominate the principals in a close corporation as partners or co-adventurers (*i.e.* joint venturers) not only provides an accurate functional description of the corporation, but also appropriately recognizes the mutual rights and obligations which should characterize the relationship of the associates.[502]

In both these instances the court clearly intended to convey not only that close corporators are fiduciaries inter se, but also that corporate status and inter se fiduciary obligations are not mutually exclusive or incompatible in the close corporation. This amounts to a rejection of the rationale of *Jackson*.[503] The unfounded premise on which that opinion is based, namely that shareholders cannot be partners inter sese and a corporation to the rest of the world, has never been accepted by courts in a large number

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of states. At the same time it is evident too that both the authority and sphere of influence of that opinion is waning.

20.3.4.2. JUDICIAL TOLERANCE OF THE INCORPORATED PARTNERSHIP

Long before courts were faced with the issue whether inter se partners' fiduciary obligations and corporate status were compatible concepts, they were confronted with the question whether a partnership relation could, as such, survive incorporation. And although some courts have taken up the view that the corporate form necessarily supersedes any prior, or other, inter se relation, the majority of courts have come to an opposite conclusion. Under the latter view a partnership or joint venture agreement survives incorporation where the corporation is intended to serve as a mere medium or instrumentality of the joint venture or partnership. What is particularly significant in the light of all those opinions, is that the courts were concerned only with the inter se relations of the corporators and not with the relations of the right-and-duty-bearing unit *vis-à-vis* third parties at all. This usually appears from observations by the courts that the interests of creditors or other third parties were not in issue and were not affected.

The idea that a lateral relation may be conducted through the medium or instrumentality or medium of another legal figure such as trust or corporation is not novel. There are, for instance, decisions concerning business trusts in which the lateral partnership relation has been recognized and to which effect has been given.[504] On the other hand, there are older decisions concerning corporations where, by disregarding the corporate entity, an underlying partnership relation was found to subsist between the corporators.[505] What the courts effectively did in these latter instances was to "look through the form to get at the real intent of the association of individuals or corporations forming the organisation, and, if rights of third

parties/ .....

parties had not intervened, ... give effect to the real purpose of the organisation in order to promote square dealing and effectuate justice."[506] What was at issue in all these inquiries was the real inter se relation between the corporators and not the relations between the corporation and outsiders. The corporate veil was invariably pierced, but only when the corporation was but an "instrumentality, adjunct or alter ego",[507] of one or more of the corporators. As early as 1915 the California Court of Appeal[508] applied the instrumentality test when it referred to the familiar principle that equity will look through form to substance in order to effect justice between the individual corporators. In the result the court found that the corporations in question were "but the mere *instrumentalities* through which the associates acted".[509] This approach was adopted in order to test whether one stockholder, as an associate, had acted bona fide in acquiring the interests of his co-associate in the venture.

The alter ego theory led to partnership principles being applied to corporators in various states, notably New York,[510] Illinois[511] and Virginia.[512] In terms of this approach, if for instance a corporation is "but an incorporated partnership ... a court of equity will disregard the legal fiction that a corporation is a separate entity, where justice [so] requires".[513] But while this form of veil piercing has been adopted in situations where corporators have incorporated their pre-existing partnership, or where intending corporators have entered into an agreement to form a corporation to carry on a business, courts have refused to apply this rule to a corporation organized and existing and operating as a distinct entity prior to the conclusion of a partner-like arrangement between the stockholders.[514]

Therefore/ ....

Therefore, it is evident that the alter ego theory came to be applied to a limited range of situations only. It served as justification for piercing the corporate veil if one stockholder had acted unconscionably in respect of a co-stockholder but only to revive, as it were, for the sole purpose of achieving justice between the aggrieved corporator and the miscreant corporator, a *pre-incorporation* partnership or joint venture agreement which had on incorporation been metamorphozed into a corporate relation. Yet this must be seen as a major advance. For, once it was accepted that a pre-incorporation partnership or joint venture agreement might subsequent to incorporation be revived for specific purposes, the law was well on the road towards recognizing that a pre-incorporation partnership or joint venture agreement might survive incorporation and that a partnership or joint venture agreement might even co-exist with a corporation, the latter serving as medium for the former. In terms of this latter approach, joint venture or partnership and corporation do not contradict one another but co-exist. No veil piercing is resorted to and the corporate entity is consequently not disregarded when the later inter se partnership relation between the stockholders is recognized and given effect to. Both the partnership, or joint venture, and corporation are recognized but each from a different point of view, the former with regard to inter se relations, the latter with regard to relations with outsider, third parties.

A clear application of this approach is found in the early Missouri decision of *Denny* v. *Guyton*.[515] In this matter the Missouri Supreme Court sustained a joint venture agreement between corporators when it tested the acquisition by one corporator of the stock interests of another fellow stockholder against the dictates of the utmost good faith.

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the particular joint venture supplied large numbers of horses and mules from all over the country to the British government and its allies during World War I, and was, out of necessity, conducted through various corporations in which the five joint venturers were the sole stockholders and controllers. The court held that the joint venture agreement in question was neither illegal nor self-contradictory because it was conducted through these corporations.[516] The court proceeded from the premise that, in carrying on its activities, it was lawful for a partnership or joint venture to cause corporations to be formed for the operation of its business and said that any agreement among partners or joint venturers to adopt such a course would not be against public policy unless plainly in contravention of some provision of the Constitution, some positive statute, or some well-established rule of law announced by the judicial decisions of the state or nation.[517] The court found that there was "no suggestion of an agreement or intention of the joint adventurers to mask their identity as such by ownership of the stock of these corporations, or to conduct them 'independent of statutory control', ignore them as corporate entities, or control them in any unlawful manner".[518] Because of these circumstances the court came to the conclusion[519] that the rationale of *Jackson*[520] was inapplicable. What is particularly significant is that the joint venture agreement in the instant case was treated as surviving incorporation despite the fact that it was neither reduced to writing, nor in fact an express agreement. In this regard the court stressed that "a joint adventure may be established without any specific formal agreement to enter into a joint enterprise; it may be implied or proven by facts and circumstances showing such enterprise was in fact entered into."[521]

In some jurisdictions, courts have placed greater emphasis

than/ .....

than the Missouri court has on the fact that both the corporation served as *medium* or *instrumentality* of the joint venture and that the joint venture survives incorporation. What is important, however, is that over the years a considerable body of case-law has been developed in this area of law in an ever expanding number of jurisdictions. These decisions accept the theory that because the corporators intended the corporation to be a mere instrumentality of the joint venture or partnership, their pre-incorporation joint venture or partnership agreement, which provides for the use of a corporation as medium for the venture, survives incorporation. Some of the more important opinions in this line will now be noted. This approach is adopted in Michigan. In 1933 the Supreme Court of Michigan[522] handed down an opinion in which it was held that the joint venture in question survived incorporation. On the grounds of fraudulent non-disclosure, this court allowed stockholders to recover from their co-stockholder, as joint venturer, the money invested by them by way of subscription for stock in a joint venture with him. The court held that the corporation was "merely a medium for carrying out the joint venture, and that the plaintiffs were not interested in purchasing stock in a corporation, but desired only to acquire the property together by the use of this convenient medium, each person taking a unit".[523]

This approach was also adopted in California, although some of the earlier opinions still reveal traces of corporate veil piercing. In 1943 the California District Court of Appeals[524] for instance stated that as a general rule an incorporator may not proceed in disregard of the corporate entity but acknowledged that there were exceptions. The court then held:

"If a corporation or formal partnership is a mere agency

for/ .....

> for the purpose of convenience in carrying out a joint venture agreement, and independent and innocent third parties, such as creditors or stockholders are not injured thereby ... justice would seem to demand that in determining the rights of the parties they be placed in the position each occupied under the original agreement".[525]

The court went on to find that the only real persons having an actual interest in the business, regardless of whether it was of a corporate nature, or arising from a partnership or co-adventure, were two individual joint venturers, and upheld an order founded on equitable principles. In a more recent matter[526] no reference is found to corporate veil piercing or to the corporate entity being disregarded. At the same time the concept of the joint venture surviving the corporation which serves as medium for its operations was clearly emphasized. Here the court held that in cases concerning the enforcement of pre-incorporation joint venture or partnership agreements, a joint adventurer or partner may be treated as an equitable owner of the assets contributed to the corporation, even though there was a corporate entity. This finding was predicated on the fact that the venture survived the corporation which served as its instrumentality.[527]

In the State of New York a very similar trend is to be observed. What is more, a few years ago the United States Court of Appeals for the Second Circuit has, in a landmark decision not only confirmed that a joint venture agreement survives incorporation, where the corporation is intended as mere instrumentality, but has at the same time rejected *Jackson*.[528] In a much earlier matter though, namely *Modlin et al.* v. *Licht et al.*[529], which dates back more than half a century, the earlier approach in which veil piercing is prominent, is clearly visible. Here the plaintiffs and *L* concluded a joint venture agreement concerning

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a real estate speculation. A corporation was organized to take title to the property purchased and the corporate stock was divided among the venturers. *L* induced the other venturers to sell to him 210 of the 600 lots, for which no money consideration passed. Subsequently *L* acquired the plaintiff's stock without revealing to them his negotiations with third parties for the sale of the entire tract of 600 lots. At the same time *L* caused the plaintiffs to believe that the real estate market was quiet and that there were no prospects of selling for at least a year. Under these circumstances Mr. Justice Scudder of the Appellate Division of the New York Supreme Court ruled that "[t]he parties were essentially joint adventurers, and, as such, owed the duty of utmost good faith to each other ".[530] The reasoning of the court, which is clearly predicated on veil piercing, appears from the following passage:

> "Where, as in this case, the defendants' conduct was not honest, equity will look behind the corporate form and consider the parties in their real relation to each other .... In violation of their obligation to act in good faith, they [the defendants] conspired to purchase the plaintiff's interest in the enterprise in the form of corporate stock while secretly negotiating for the sale of the corporate assets, at the same time representing to the plaintiffs that their stock was worth less than its true value because of a stagnated real estate market. These acts constitute such fraudulent conduct as to warrant a court of equity in granting relief".[531]

Twenty seven years later, hints of veil piercing and alter ego theory still lingered on in *Macklem*.[532] That opinion, however, at the same time served notice of the demise of *Weisman*.[533] Ten years later, in 1965, in *Arditi* v. *Dubitzky*[534]

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the more modern approach is clearly discernable. Now the unfounded theory that partnership, or joint venture, and corporation are mutually exclusive forms of business,[535] is explicitly rejected. Now there is no longer any need to resort to veil piercing. Here the plaintiff and the defendant concluded a joint venture agreement for the development of a high-rise apartment project. The defendant, who was a Connecticut builder and land developer, provided the land for the project. He further undertook not only to assist the plaintiff, a New York commodity dealer, to obtain suitable finance for the project, but also to devote all his time to the project. During the negotiations which culminated in the joint venture agreement the defendant is said to have represented himself as skilled and experienced in such ventures. These representations were alleged to have been knowingly false. Long after the conclusion of the joint venture agreement a corporation was formed to carry out the venture. The plaintiff and defendant between them held all the stock of the corporation. The suit instituted by the plaintiff for an accounting and damages was dismissed by the District Court. Such dismissal was based on the contention that any contractual obligations which a joint venture might have created prior to incorporation became merged into the corporation organized to serve the venture. The Court of Appeals, reversed. It held in part that the complaint for breach of the joint venture agreement stated a good cause of action under laws of New York and New Jersey, despite incorporation after entering into the joint venture. This ruling was predicated on the finding that the parties *intended* the corporation to be merely an instrumentality of the joint venture. The court reasoned as follows:

> "The rule of Jackson v. Hooper has come under heavy attack and has been rejected by many jurisdictions .... There is little logical reason why individuals cannot be 'partners

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inter sese and a corporation as to the rest of the world', so long as the rights of third parties such as creditors are not involved .... The courts of New York and New Jersey have come to recognize this trend, at least to the extent of permitting suit upon joint venture obligations if it is apparent that ... the corporation should be only a means of carrying out the joint venture — a conduit of title as in Macklem, or a way of organizing different branches of a wide-reaching joint enterprise, as in Fortugno".[536]

A similar approach is adopted in Maryland, as is evidenced by *De Boy* v. *Harris et al*.[537] Here an oral, pre-incorporation agreement concluded between three persons was sustained by the Maryland Court of Appeals. The said agreement was described as a joint venture agreement and was entered into for the purpose of acquiring sites for, and the construction of industrial and warehouse facilities to be leased, sold or otherwise dealt with. The said agreement further provided for the sharing of profits in fixed proportions and the formation of a corporation to "be an instrument or tool of the joint venturers." The plaintiff complained that, in wilful disregard of his rights under the said joint venture agreement, the defendants, both as directors and stockholders of the said corporation, caused the stock of the corporation to be increased and offered to all stockholders in proportion to their existing holdings. The plaintiff alleged that the sole purpose of the proposed rights issue was to "water down" his interest in the venture because such a large number of shares was offered that he would not be able to take up his rights and maintain his agreed proportionate percentage in the corporation. In the result plaintiff instituted action for damages sustained by him as a result of the alleged breach of contract. The Maryland Court of Appeals

overruled/.....

overruled the defendants' demurrer, and, finding that the plaintiff had stated a cause of action for an equitable accounting, ordered the case be transferred to the equity court for an accounting. In doing so Justice Collins, who delivered the opinion on behalf of the court, observed that the question whether an agreement such as the instant one, survives after incorporation had not previously been decided in Maryland. After referring to *Jackson*[538] and after reviewing the recent case-law developments, Justice Collins held:

> "As the allegations in the declaration before us are that the corporation was to be used merely as a medium to carry out the purposes of the agreement, we are of the opinion that under the allegations herein the corporation did not wipe out the agreement".[539]

It would appear that a new approach, in line with the trend discussed above, might be in the offing too in New Jersey, birthplace of *Jackson*.[540] This would seem to follow from the decision of the Intermediate Appeal Court of New Jersey, in *Fortugno* v. *Hudson Manure Co.*,[541] a matter in which the court was prepared to recognize a number of corporations as mere "mechanical devices"[542] for running a long-established, family, partnership enterprise. In doing so the court, however, resorted to the earlier technique of disregarding the corporate entity. This was actually unavoidable as the proceedings came before court by way of action for dissolution of the family partnership because of dissension between its members and the desire of some of them to go their own way. Because of the character of these proceedings, a more detailed discussion thereof will follow in para. 20.3.4.3. hereunder. The significance of this decision, however, is that it represents the acceptance by a New Jersey court of the principle that partnership and corporation are not mutually exclusive

forms/ .....

forms of business and that they can co-exist in one enterprise. In the instant case, too, the partnership agreement was not a formal one; in fact it was concluded orally between the widow and seven children of the founding father of the business shortly after his death, each being allocated a one-eighth interest in the business.[543]

It is also now accepted in Wisconsin, that a joint venture agreement survives incorporation if the corporation serves as medium or instrumentality through which the operations of the venture are conducted and if the rights of third parties are not in issue. Thus, in 1969 the Wisconsin Supreme Court in *Jolin et al.* v. *Oster et al.*,[544] after referring to the relevant case law and after reviewing some of the opinions in question, summed up the position as follows:

> "[A]lthough the early cases adopted the view that incorporation spelled the end of the joint venture, the later cases consistently have taken the view that where the intention of the parties is clearly expressed to use a corporation as a means of conducting the joint-venture business, the courts will give effect to their expressed intention, so long as the rights of innocent third persons are not prejudiced. We think this is the better rule and we adopt it".[545]

In the instant case the parties, *O* and *J*, had expressed their intention in this regard in a written agreement which recorded *inter alia*, that they would form a corporation for the purpose of carrying on a joint venture between them. What is particularly significant is that the parties further recorded that "they were aware [that] the 'close corporation vehicle' being used by them and the nature of the business required that

many/ .....

many rules of association of a partnership must necessarily prevail in the actual operation of the business".[546] In these circumstances the complaint alleged the existence of a joint venture between *O* and *J* and a breach by *O* of his fiduciary obligations thereunder. The Circuit Court upheld the denial by *O* of the existence of a joint venture. The Supreme Court reversed and remanded the matter back on trial on the issues of fiduciary relationship, breach thereof and damages.

Massachusetts boasts a long tradition in this field, dating back to the end of the previous century. The first reference to a corporation in effect being a partnership is found in *Anchor Electric Co. v. Hawks*.[547] Here certain corporations had sold their assets to a new corporation in exchange for all the stock in the latter and by agreement were entitled to share the profits generated by the latter. The court referred to these circumstances and said:

> "Although the parties provided for the establishment of a corporation, their arrangement was in the nature of a copartnership".[548]

Two decades later the first reference to "instrumentality" in this context appeared in *Arnold* v. *Maxwell*.[549] Here, *A*, an experienced business man, was persuaded by *M*, a trade-mark and patent solicitor, who had access to a chemical patent, to join him in a venture to acquire the said patent and enter upon its manufacture. It was agreed between *A* and *M* that they would share equally all aspects of the business into which they were about to enter *i.e.* ownership, profits and expenses, and that as soon as it became expedient, *M* would organize a corporation to take over the said business. It was further agreed that *M* would handle the legal side of the enterprise and that *A* would take charge of managing the

business/ .....

business, both parties working without remuneration. It was subsequently established that shortly after the enterprise began to develop, *M* conceived the idea of gaining control of the corporation and the business. He ultimately achieved this aim. *A* instituted a suit against *M*, alleging that fiduciary relations existed between them and that *M* had breached the duties flowing from these relations. The court noted that the agreement between *A* and *M* was referred to as an "equality agreement", remarked that it undoubtedly created a partnership between *A* and *M* and held:

> "It is immaterial as between themselves whether they conducted the business under a firm name, or adopted the instrumentality and name of a corporation".[550]

The court went on to find that the corporation records, as between the parties, stood on the same footing as partnership books and held the defendant chargeable in a partnership accounting on the basis of the agreement of equality.[551] The same reasoning was adopted in *Silversmith* v. *Sydeman*[552] in which a corporator was held liable to account in terms of partnership norms. Plaintiff and defendant, who together owned all the capital stock of a furniture corporation, resolved to discontinue the business of the corporation and to liquidate its affairs. Plaintiff, who initially assisted defendant in the liquidation of corporation, left the completion of that task to defendant on leaving permanently for another city. Defendant, who was treasurer and general manager of the corporation, withheld interest charges on money loaned to the corporation by him and for discounting a note of the corporation in the absence of an agreement to that effect. Plaintiff instituted an action for an accounting. The Supreme Judicial Court of Massachusetts upheld a decree awarding the plaintiff one-third of the said charges. It reasoned as follows:

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> "[T]he plaintiff and the defendant were acting as partners in the conduct of the company's business and in the liquidation of its property even though they had adopted a corporate form as the instrumentality by which they should associate in the furtherance of their joint venture".[553]

The court confirmed the Master's finding that a fiduciary relationship existed between the parties from the time they first became associated in the furniture company and said:

> "The parties occupied a position substantially similar to partners and upon the facts ... the defendant was not entitled to receive any compensation for the work done by him in winding up the affairs of the furniture company. No special circumstances are disclosed that make the case an exception to the general rule that a partner is not entitled to compensation for settling the business of the firm".[554]

A similar approach was adopted in *Mendelsohn* v. *Leather Manuf. Corp.*[555] Here the court referred to the joint venture formed by three parties with a view to producing a leather substitute and said: "That the parties later saw fit to carry out their purposes through the medium of a corporation did not change the essential nature of the relationship ... While the enterprise continues, joint venturers, like partners, owe to one another the utmost good faith and loyalty".[556]

Judicial recognition of the survival of a joint venture, if it is being conducted through the medium or instrumentality of a corporation, dates back to 1942 in Wyoming. In that year the Supreme Court of Wyoming, in the matter of *Dutch Maiden*

Bakeries/ .....

Bakeries Inc. v. *Schleicher et ux.*,[557] described the association before it as a "joint business venture in the nature of a co-partnership though the business was to be carried on through the medium of a corporation".[558] The particular association consisted of two venturers, *S*, the defendant, an experienced baker and, *O*, a corporation engaged in the flour-milling and bakery business. In terms of an oral, joint venture agreement, it was agreed that both *S* and *O* would contribute bakeries to the venture and that a corporation, Dutch Maid Bakeries, would be organized to take over such bakeries and to conduct the venture. *O* took 51% and *S* 49% of the stock of the corporation upon it being incorporated. Mr. Justice Kimball said:

> "Dutch Maid was the instrumentality to take over the bakeries and to carry on the business with defendant as manager. It could hardly be said that the parties to the venture were dealing at arm's length. There was a fiduciary relation in the nature of a joint adventure .... That relation did not terminate when the business was put in the hands of Dutch Maid, the instrumentality chosen to carry on the venture ...."[559]

In view of these circumstances the court refused, *O*, who had acted unconscionably, such relief as *O* would otherwise have been entitled to. A very similar approach was adopted in Florida in 1953. In *Donahue et al.* v. *Davis et al.*,[560] the Supreme Court of Florida held that "[t]he fact that joint adventurers may determine to carry out the purpose of the agreement through the medium of a corporation does not change the essential nature of the relationship".[561] In the instant case the complaint was that the defendants had committed material misrepresentations when they had induced the plaintiffs to join them in a joint venture which had as

object/ .....

object the acquisition of a particular tract of real estate for resale at a profit. It was agreed by the venturers that for purposes of acquiring the said land, a corporation would be incorporated by them to hold title for their benefit. It was further agreed that each venturer would contribute one-fourth of the purchase price for the property and receive one-fourth of its capital stock. In breach of this joint venture agreement, the first defendant, *D*, not only paid nothing for his stock but, by selling the land to the venture at a price in excess of that paid by him(and without disclosing such fact to the plaintiffs, his co-venturers), also made a substantial secret profit at the expense of the plaintiffs. In breach of the said agreement, *O* did not pay in full for his stock. The Supreme Court of Florida overruled exceptions filed by *D* and *O* and decreed relief in accordance with the recommendations of the special master, namely that equity should restore the parties by reallocating the stock to each party in the ratio that his actual contribution bore to the actual purchase price of the property. In the result it was decreed that *D* had, as trustee for the plaintiffs, acquired all fifteen shares which had been issued to him in the stock of the corporation and that six of the fifteen shares similarly issued to *O* had likewise been acquired by *O* as trustee for the plaintiffs.

In arriving at this result the court relied on a much quoted passage from a judgment by Mr. Justice Cardozo in *Meinhard*[562] in order to hold that joint adventurers, like co-partners, owe to one another, so long as the relationship continues, the duty of the finest and highest loyalty.

More recently courts in some states, without treating the corporation before them as a mere medium for or instrumentality of an underlying joint venture or partnership relation, have applied provisions of pre-incorporation, joint venture or

partnership/ .....

partnership agreements, to corporators in matters relating to their inter se relations. This marks a clear advance in the judicial evolution of the incorporated partnership. A case in point is the Illinois matter, *Moss* v. *Waytz*.[563] Here three partners, the plaintiff and two Waytz brothers (Sol and Max), signed a pre-incorporation contract to convert their partnership in a medicine and pharmaceutical business into a corporation. The said partners, all three of whom were registered pharmacists, became the sole stockholders and directors of the said corporation. The pre-incorporation agreement which, *inter alia*, provided for unanimity among directors, was at all relevant times after the incorporation of the corporation, faithfully adhered to in all respects including the vote requirements. This was despite the corporate records containing no formal adoption of the said contract and despite provisions in the by-laws of the corporation providing for majority vote as opposed to unanimity in decision making. When, in terms of the said agreement, *S* retired as stockholder (but not as director), a third Waytz brother, *B*, who was also a registered pharmacist, acquired a shareholding in the corporation. Some two years later resolutions were proposed whereby the salaries of the three Waytz brothers were to be increased by 50%. These resolutions were carried and implemented despite the plaintiff's opposition thereto. Both the Illinois Circuit Court and the Appellate Court of Illinois held that the pre-incorporation contract was binding and that the resolutions were ineffective because such resolutions were not passed in accordance with the requirements of the preincorporation agreement, *i.e.* unanimously. That the said pre-incorporation agreement was not formally adopted, and the fact that the by-laws provided for rule by a majority vote and that *B* was not a party to the pre-incorporation contract, were all held to be of no consequence. The court observed that until the meeting in question, the contract unanimity rule, and not the majority by-law requirement, was honoured in the administration of the corporation. In the result the court found that having adhered to the unanimity rule, there could

be/ .....

be no departure from it except by the unanimous vote of the original partners, the plaintiff, *M* and *S*.[564] This opinion constitutes authority for the proposition that where a pre-incorporation, partnership practice is adopted by the corporators in their inter se dealings, despite corporate norms to the contrary, such partnership practice will bind the corporators in their inter se relations.

Another case in point is the Kansas matter, *Campbell* v. *Campbell et al.*[565] Here two brothers, Max, the plaintiff, and Ralph, the defendant, embarked upon a joint venture for the manufacture and sale of a flexible metal hose coupling and fitting which they invented and patented jointly. It was understood that each would share equally in the venture. True to the partnership character of the relation, *M* was primarily engaged in production, while *R* devoted his attention to sales and promotion, and the operation was named M&R Development Company. The trade name "Hydro-Flex" was also used and this name was incorporated in the name of the corporation, which *M* and *R* subsequently organized as joint venturers when their business expanded and additional finance became necessary. Upon incorporation the most valuable asset of the joint venture, the patent, was assigned to the corporation. The corporation, in turn, issued 127 shares of stock to each of the two venturers, *R* and *M* and a further number to third parties who put up finance. After incorporation of their venture, *M* and *R* continued to receive equal salaries and bonuses and to perform the same duties and responsibilities in carrying on the business as before. Some time after incorporation, *R*, with the intention of gaining control of the corporation, secretly, that is behind the back of *M*, started buying up stock which had been issued to outsiders. *M*, upon discovering this, confronted *R* and demanded one-half of the stock which the latter had purchased. *R* not only refused to sell this stock to *M*,

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but, by voting his stock, both removed *M* as director and officer of the corporation, and increased his own salary. *M* instituted action, alleged that a joint venture agreement had continued after incorporation and averring that a confidential or fiduciary relationship therefore existed at all times relevant to the action, claimed equitable relief. The District Court of Kansas rendered judgment generally for the plaintiff and against the defendant who appealed. The Supreme Court of Kansas, however, upheld this judgment on the basis that there was ample evidence to support the trial court's finding "that at the time pertinent hereto the plaintiff and the defendant had an agreement that they would share equally in the fruits of the patent which was represented by the stock in the corporation".[566] What the court in effect was suggesting here, although it did not say so, was that Hydro-Flex Corporation, Inc. was an incorporated partnership. This is borne out by excerpts the court earlier quoted, with approval, from the opinion of the trial court. In one such passage the trial court had accepted evidence showing "the existence of an agreement and an understanding that the two brothers, Ralph and Max, would continue with a partnership-like arrangement between them after the incorporation and that they would continue to participate and control the affairs of the corporation on an equal basis".[567] In a further passage the trial court had found that "when these two brothers incorporated their business, it was only for the purpose of expanding and raising capital and that they had no intention of converting it into something that would be thereafter on an arms' length basis or an every-man-for-himself relationship".[568] The facts of this case, the judicial findings and the relief granted, call for comparison with those in *Ebrahimi*.[569]

The approach observed in the last two opinions was recently adopted by the United States Court of Appeals for the Fifth Circuit.

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This was in a Texas matter[570] where the Federal Court ruled that the definition of joint venture accepted in Texas[571] does not necessarily imply that the formation of a corporation to carry out the purposes of a joint venture would cause the venture to cease.[572] This reasoning is sound and is not without significance for other jurisdictions.

The decisions considered up to now may be broadly classed in three categories. Common to all three categories is the willingness of courts to apply partnership precepts and principles to corporators in their inter se dealings. In the first category are found those early cases in which, because equity had so demanded, courts had brushed aside the corporate veil to discover that the persons behind the corporate structure are but partners. These decisions may be seen as representing the first phase in the judicial evolution of the incorporated partnership. In the second category are found those cases in which courts upheld the survival of pre-incorporation joint venture or partnership agreements based on the proved or presumed intention of the corporators and which envisage the use of the corporation as mere medium for or instrumentality of the seminal joint venture or partnership. These decisions may be regarded as representing the second stage in the judicial evolution of the incorporated partnership. In the third category are found those cases in which courts have ceased to regard it necessary to typify the corporation involved as a mere medium for or instrumentality of a partnership which survives incorporation.

In the fourth category, now to be considered, courts regard small intimate, close corporations for what they in fact are, namely incorporated partnerships. This is the final stage in the judicial evolution of the incorporated partnership. Now courts begin to distinguish consciously between the public-issue corporation, with a large body of widely dispersed

stockholders/.....

stockholders, and the close corporation with a small intimate circle of stockholders, who are related to or acquainted with one another and who therefore mutually repose confidence and faith in one another. In some of these cases courts still refer to partnership precepts in order to impose fiduciary duties on close corporators; in others, courts treat close corporators as fiduciaries *per se*.

An early case in this line is the Minnesota decision, *Fewell v. Tappan et al.*[573] Here there was no pre-existing partnership and no pre-incorporation joint venture or partnership agreement either. Plaintiff and defendant had been long-time friends and business associates, the latter, as the former's lawyer, incorporated a bakery for the former many years before the suit. At the time, though, defendant did not acquire any financial interest in the corporation. Some years later defendant and plaintiff became equal owners of the bakery stock, each owning a half interest and each drawing an equal salary. Still later the plaintiff and defendant entered into a written stockholder agreement in terms of which they agreed upon complete equality between themselves with regard to remuneration, board representation and voting. The said agreement also provided that no stock would be issued or sold without the consent of both parties. Because it was necessary that there be at least three stockholders in order to function as a corporation, one qualifying share was issued to *L*, plaintiff's son-in-law. And, in order to maintain complete balance between the corporators, another one share was issued to *E*, the defendant's son. The plaintiff regarded the defendant as his "partner"; the latter had promised the former to protect the former's interests as his own. Subsequently defendant convinced plaintiff that, in view of the supposed precarious financial position of the bakery, creditors were likely to bring pressure to bear to enforce their claims and

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that insolvency proceedings were imminent. To avoid this disaster, defendant advised plaintiff that they should avail themselves of the opportunity to sell to an undisclosed third party who was willing to buy their stock at $20 000 in cash provided they both agreed. Under these circumstances plaintiff, who was seriously ill, parted with his stock to the representative of an undisclosed principal, who subsequently turned out to be the defendant's son, *E*. It was also later established that defendant not only knew that the bakery was never threatened with legal proceedings likely to cause receivership or other harmful consequences, but also that the shares were worth far in excess of the amount of the $20 000 which plaintiff received. In the ensuing suit instituted by plaintiff for damages, it was established that prior to the transaction, *E* had taken steps to prevent plaintiff from discovering the true state of affairs. The court alluded to plaintiff's referring to defendant as a partner, and, finding that the basis for plaintiff's characterization of their relationship as partners justified in view of the stockholder agreement, held:

> "As to each other, they were in a situation similar in effect to that of ordinary co-partners. The [stockholder] agreement ... fortifies and clinches that view. Not only did they so consider themselves then, but they solemnly pledged equal rights and privileges to each other in respect of the indefinite future. There was a complete balance of rights and interests between them. ... Everything considered, we think that these men by virtue of their contract and their manner of operating under it, stood in the relationship of co-partners". 574)

The court thereupon observed that the relationship between partners is essentially one of mutual trust and confidence and that the law imposes upon partners the highest standard of integrity and good faith in their dealings inter se.

Applying/ ....

Applying the law to the facts before it, the court found that fair dealing in the acquisition of plaintiff's stock was conspicuously absent and ruled in favour of plaintiff. Although the court did not consciously draw a distinction between a public-issue corporation and a close corporation, it is safe to say that it had the latter in mind.

In the United States Court of Appeals for the District of Columbia matter, *Helms, N.O.* v. *Duckworth et al.*,[575] this distinction appears to have moved to the fore for the first time. Here *E*, who had been engaged in business as a roofing and sheet metal contractor for almost half a century, and *D*, a roofing contractor employee, decided to become business associates. To that end the prospective associates entered into a written agreement providing *inter alia* for the formation of a new corporation with 1500 shares of $10 par value stock in which *E* was to hold 51%, and *D* 49% of the stock. The said corporation was to carry on the business established by *E*. While *D* was to pay for his shares in cash, *E* was to pay for his by transfer of business assets. Although cast in corporate form, the association clearly displayed essentially partnership features. The said agreement further provided for the execution of a trust agreement in terms of which both *D* and *E* would place their stock in trust and they agreed that on death (or, sooner, by mutual consent) the stock of the associate concerned would be sold to the survivor or continuing member "'the purchase price of the stock [to such other stockholder] ... [being] the par value of $10 per share *unless modified by the parties by subsequent agreement*'".[576] At the same time a formal survival-purchase agreement was executed, *E* then being seventy years of age and *D* only thirty seven. At the time of the conclusion of the survivor-purchase agreement the real, net worth of the corporation was reflected by a figure of $10 per share. Eight years later when *E* passed

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away, neither party had proposed a change in the purchase price in accordance with the trust survivor-purchase agreement. The last financial statements of the corporation then reflected the stock to be worth $80 per share. When *D* tendered the administratrix in the deceased estate his cheque for the deceased's stock at $10 per share, the latter instituted suit contending that the survivor purchase agreement should be cancelled if *D* was not prepared to pay the true value of the stock as at decendent's death, *i.e.* $80 per share. The said administratrix urged that *D* had fraudulently induced the deceased *E* to execute the survivor-purchase agreement by representing that he, *D*, would consent to a periodic re-determination of the stock purchase price. It was further contended that the said misrepresentation violated the confidential relationship existing between the parties, and, that in any event it was so grossly inadequate as to warrant a rescission of the agreement. *D*, on the other hand, stood on the letter of the contracts and maintained that in the absence of any mutually agreed change in the buy-out price, he was entitled to the shares at the stipulated price of $10 per share. In this fashion the focus was centered on the inter se relations of *D* and *E* and therefore indirectly, on the character of the corporation in which they were associated.

In the United States Court of Appeals, these issues were immediately grasped by Mr. Justice Burger who straight away directed himself at the stockholder and the ancillary survivor-purchase contracts. These agreements he described as being "typical ... agreements made between partners of small businesses or stockholders of closely held corporations where the major stockholders are also the managers in the enterprise".[577] Because of the partnership-like character of the inter se relation between *D* and *E*, the court did not find it necessary to determine whether *D* had fraudulently induced *E* to execute the

survivor-/ .....

survivor-purchase agreement by means of misrepresentation or otherwise. "In an intimate business venture such as this," Mr. Justice Burger explained, "stockholders of a close corporation occupy a position similar to that of joint adventurers and partners".[578] The learned judge went on to hold that "the holders of closely held stock in a corporation such as shown here bear a fiduciary duty to deal fairly, honestly, and openly with their fellow stockholders and to make disclosure of all essential information".[579] In this regard the court drew a clear distinction between public-issue corporations and close corporations. For, as Mr. Justice Burger pointed out, although courts have held that stockholders do not inter se bear such duties in the former type of corporation, such a view "ignores the practical realities of the organization and functioning of a small 'two man' corporation organized to carry on a small business enterprise in which the stockholders, directors and managers are the same persons".[580] Equally significant are the court's comments concerning a more appropriate name for the last-mentioned corporation type. "Indeed, 'chartered partnership' or 'incorporated partnership'" the court readily acknowledged, "is a more descriptive and accurate designation of the relationship than 'close corporation'".[581] In this way the United States Court of Appeals has clearly recognized the existence of the incorporated partnership. The court singled out the absence of a division between stockholder-owners and the director-managers[582] of the incorporated partnership as its distinguishing characteristic but left the challenge of defining the concept of incorporated partnership more precisely, to future courts. The task was taken up by the Massachusetts court almost two decades later.

In Massachusetts the first hesitant steps in this direction were taken in *Samia et al.* v. *Central Oil Co. Of Worcester.*[583] This case concerns the inter se relations of the members of a family corporation. The said corporation conducted an oil business

previously/ .....

previously carried on by two members of a family in partnership the assets of which partnership business were exchanged for stock in the said corporation. Here the court observed that the corporation in question was a "small family corporation" and not a "large publicly owned organization".[584] This, the court felt, imposed fiduciary obligations on the three brothers who had deprived their three sisters, who at all times had at least an indirect beneficial interest in the said family corporation, of the stock in the said corporation which the latter had inherited from a fourth brother.[585] A few years later this opinion was cited by the Supreme Judicial Court of Massachusetts in *Wilson* v. *Jennings*,[586] in support of a finding that three stockholders "on an informal and somewhat ambiguous basis ... had entered into what was essentially a joint venture in corporate form to exploit [an] ... invention".[587] The association between the said associates came about as a result of an agreement between two patentees *W*, and *M*, and an entrepreneur, *J*, to organize a corporation to promote the patent belonging to *W* and *M*. It was agreed that one third of the stock was to be held by each of the associates and that such three-way equal division would be permanent. For his third share, *J* was obligated to do the financing, to be the general manager of the corporation and to operate it on behalf of its stockholders. *W* and *M* earned their two-third share by assigning their patent to the corporation. It was mutually understood that *W* and *M*, who were resident in California, would be kept informed by *J* what was happening on the East Coast and *vice versa*. In essence, therefore, the association was a partnership in corporate apparel. Not surprisingly, the court concluded that the relationship was to be one of trust and confidence and that consequently an inter se fiduciary relationship subsisted between the corporators.[588] In this regard the court clearly distinguished between the fiduciary relation between any corporator as director, and the corporation (the

vertical/ .....

vertical fiduciary relation) and the inter se fiduciary relation between the corporators as such (the horizontal or lateral fiduciary relation). The court did not, however, specifically distinguish between close corporations and public-issue corporations.

In *Donahue*[589] the Supreme Judicial Court of Massachusetts took care to distinguish between the "close corporation" or "incorporated partnership",[590] on the one hand, and "other corporations", on the other,[591] and also to emphasize that it limited the applicability of its holding to the former type.[592] Here the court was faced with a suit brought by a minority stockholder when the corporation repurchased its shares from a majority stockholder, *R*, without also repurchasing its shares from the plaintiff. The plaintiff characterized the said corporate purchase of stock as an unlawful distribution of corporate assets to the controlling stockholders in breach of their fiduciary duty to minority stockholders to enjoy an equal opportunity. Very little is known about the history of the corporation apart from the fact that *R* took employment with it many years previously and worked himself up to a position where he controlled the corporation (then renamed after him) and acquired 80% of its stock. *D*, a technician who was employed by the corporation at about the same time as *R*, also advanced himself in the corporation. Although *D* started off as a mere "finisher" of electroplates, he ultimately achieved the position of plant superintendent and corporate vice president. *D*, at the instance of *R*, who hoped to interest *D* in the business, acquired a 20% stake in the corporation. Prior to the corporate purchase of stock from *R*, *R* had by way of gift distributed the majority of his shares equally among his two sons and his daughter, leaving himself 81 shares, which the corporation purchased from him upon his retirement. When the suit was instituted, *D* was already deceased, and his shares were owned by his wife, the plaintiff, and his son.

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The fact that the court emphasized the distinction between close corporations and other corporations, to some extent compelled it to formulate a more comprehensive judicial definition of the concept "close corporation" than the previous endeavours in that regard. In so doing, the court came to combine the aspect of "integration of ownership and management" alluded to by some courts with the aspect of paucity of stockholders and the aspect of absence of a ready market for the corporate stock, mentioned by others, into a coherent single concept to achieve a satisfactory, formal definition of "close corporation." At the same time, the aspect of mutual confidence and trust, that corner stone of partnership which in turn is a natural incident of *delectus personae*, was also recognized as a feature of the incorporated partnership. Chief Justice Tauro, writing on behalf of the court, said:

> "Just as in a partnership, the relationship among the stockholders must be one of trust, confidence and absolute loyalty if the enterprise is to succeed .... All participants rely on the fidelity and abilities of those stockholders who hold office. Disloyalty and self-seeking conduct on the part of any stockholder will engender bickering, corporate stale-mates, and, perhaps efforts to achieve dissolution".[593]

The court stressed that in this respect close corporations, with substantial assets and with more numerous stockholders, are no different from small close corporations. This statement is not entirely correct: while the extent of the financial operations of a corporation does not have a bearing on the inter se relations of its members the number of its members does have a bearing on the personal character of their inter se relation. It is significant that the court regarded the aspect of inter se mutual confidence and good faith in the close corporation as important enough to be referred to again in two further respects. In one context the court stated that "because of the trust and confidence reposed in them" by other stockholders, close

corporators/ .....

corporators participating in management, are held accountable to "a standard of fiduciary duty more exacting than the traditional good faith and inherent fairness".[594] In another context the court held that "[b]ecause of the fundamental resemblance of the close corporation to the partnership [and because of] the [consequential] trust and confidence which are essential to this scale and manner of enterprise and the inherent danger to minority interests in the close corporation ... stockholders in the close corporation owe one another substantially the same fiduciary duty *in the operation of the enterprise* that partners owe to one another".[595] In this regard the court referred to *Meinhard*[596] and spoke of "[t]he more rigorous duty of partners and participants in a joint adventure ... extended to stockholders in a close corporation",[597] and of "the standard of duty owed by partners to one another as the 'utmost good faith and loyalty'".[598] Against this background the court drew a clear distinction between the close corporation and the public-issue corporation. In the words of Chief Justice Tauro: "[w]e contrast this strict good faith standard with the somewhat less stringent standard of fiduciary duty to which directors and stockholders of all corporations must adhere in the discharge of their corporate responsibilities".[599]

On the facts of the instant case, the court held that the defendant corporation was a close corporation. In doing so the court applied the formal definition formulated by it. In this regard the court noted that members of two families, the Rodds and the Donahues were the sole owners of the corporation's stock, that there were only six stockholders in all, that no market seemed to exist for the shares which, consequently, were never traded, that the parties concerned all worked for the corporation and that the Rodds had retained the paramount management positions.[600] The court further found that the

purchase/ .....

purchase by the corporation of the shares held in its stock by the head of the Rodd clan, amounted to a distribution of a portion of the corporate assets to that person without an equal opportunity being offered to the plaintiff stockholder. The court also found that the said transaction constituted a breach of the fiduciary duty owed by the Rodds as controlling stockholders to the minority, the plaintiff and her son, and granted equitable relief. It is clear that on the evidence before the court, the instant corporation was a close corporation in terms of the definition propounded by Mr. Justice Tauro. Whether the particular close corporation was also truly an incorporated partnership, is another matter. While it is possible that a partnership in corporate form came about when *R* and *D* respectively acquired 80% and 20% of the corporation's stock and operated the corporation as a partnership in corporate form, it is not clear what the specific character was of the inter se relationship between successors in title of *D* and *R*, *i.e.* whether they were at arm's length or whether their inter se relationship was one of mutual confidence and trust. Within a matter of months another Massachusetts court was faced again with the issue of a close corporation, which in that case clearly turned out to be an incorporated partnership proper at all relevant times.

In the Massachusetts Court of Appeals matter *Cain et al.* v. *Cain et al.*,[601] the central figures were two brothers *J* and *P* and their incorporated partnership named Airport Express, Inc., a corporation engaged in the trucking business at the Boston Airport. *P* had some time prior to entering into partnership with *J*, acquired Airport Express, Inc. as an existing corporation because of its Interstate Commerce Commission certificate to carry goods. Subsequently *J* was employed by Airport Express, Inc. and some time later *P* agreed to admit his brother *J* as a

partner/ .....

partner in the business. To that end a document entitled "articles of co-partnership" was executed. The agreement *inter alia*, recorded that the said brothers had formed a co-partnership for the purpose of engaging in the transportation business in the name of Airport Express, Inc.. It further provided that each partner would receive a weekly salary of $350, that all profits and losses would be shared equally between the two partners, that both partners would work equal hours, that *P* would supervise loading and unloading of freight and other duties that pertained to freight services and that *J* would be in charge of the office and records, dispatch of drivers and of any other duties that pertained to the office. Pursuant to that agreement *P* transferred fifty shares of the corporation's stock to *J*. This turned *J* into an equal shareholder with *P* in the corporation, the said two partners being the said corporation's sole stockholders. *J* was also appointed as director, treasurer and clerk of the corporation; *P* continued to serve both as director and president. The only other directors were the wives of the two partners.

While *J* was still a director, officer and stockholder of the said corporation, he started a sole proprietorship. The sole proprietorship took over the account of *N*, a freight forwarder, which accounted for a substantial part of the business of the incorporated partnership with which he was still thus associated. The sole proprietorship also enticed employees away from the incorporated partnership.

The Massachusetts Court of Appeals found that the plaintiff corporation was an "obvious example" of a close corporation, as defined by Mr. Justice Tauro, and, quoting a passage from the latter's opinion, said:

> "'[T]he enterprise remains one in which ownership is limited to the original parties ... in which ownership

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and management are in the same hands, and in which the owners are quite dependent on one another for the success of the enterprise'".[602]

The court noted that the said opinion was built on and found support in such cases as *Wilson*[603] and *Samia*.[604] The court further observed that close corporations were in these latter cases "assimilated to partnerships or joint ventures in measuring the fiduciary duty owed to the corporation by a stockholder, officer and director of the corporation",[605] and stated that it found the "strict duty of loyalty to all stockholders in close corporations", as propounded by Mr. Justice Tauro, particularly applicable to the circumstances in the instant case.[606] Against this background Mr. Justice Goodman, who wrote the opinion in the Court of Appeals, acknowledged that the court looked to partnership law to assess the duty owed by *J* to the plaintiff close corporation and whether *J* breached such duty in organizing his private business, hiring former employees of the plaintiff corporation and taking business away from the latter. He held:

"Such competition is a clear violation of the fiduciary duty owned by one partner to another. '[T]he general rule [is] that a partner will not be permitted to obtain for himself profits arising from carrying on a separate business of the same nature as that of the firm, ... but must account to his co-partners for the benefits derived therefrom'".[607]

Thus it is clear that the Massachusetts Court of Appeals imposed on members of an incorporated partnership, *qua* stockholders, as opposed to directors and officers of such corporation, inter

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se fiduciary duties developed in relation to partners. This was again stressed by the court. In pointing out that J had also breached the fidicuary duty he owed the corporation *qua* director, the court held:

> "Indeed, John's acquisition of Novo's [the client's] business formerly enjoyed by Airport [the incorporated partnership], whether viewed as the appropriation of a corporate opportunity or direct competition with Airport ... is, in the circumstances of this case — *quite apart from his position of stockholder in a close corporation* — violation of John's duty as an officer and director 'reasonably to protect the interests of the corporation'".[608]

As explained in Excursus I, the inter se fiduciary relation subsisting between close corporators, should be viewed as an associative, lateral or horizontal, fiduciary relation. Similarly the fiduciary relation subsisting between a director and his corporation should be regarded as a vertical fiduciary relation. The two should not be confused. Of equal significance is the particular distinction drawn by the court in this latter regard between close corporations and other corporations. Mr. Justice Goodman explained:

> "The competition in this case is quite different from the type of activity in which an officer or director of a corporation may be expected to engage as 'a natural concession to commercial practice' ... where the office or directorship is not in a close corporation and is not a full-time job".[609]

The court emphasized in this regard that one of the duties of

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J to the incorporated partnership was, as a salesman, to promote for it the very business *J* had appropriated for himself.[610)]

In the most recent Massachusetts decision in this field, *Wilkes v. Springside Nursing Home, Inc. et al.*[611)] the close corporation concerned was undoubtedly once again a true, incorporated partnership. The close corporation in question was organized by four individuals to run a nursing home which they proposed to operate in partnership with one another. Here the initiative was started when plaintiff, *W*, a roofing and siding contractor and successful real estate dealer, acquired an option to purchase a lot with a hospital building thereon. *R*, an acquaintance of *W*, on learning about the option, interested *Q* and also *P*, an acquaintance of both *W* and *R*, to join *W* in the investment. As it turned out, the four agreed that they would all participate jointly in the purchase as a real estate investment that offered sound profit prospects both on resale or rental. It was subsequently decided to operate the proposition as a nursing home. The four of them were alerted to the fact that in terms of their proposals they were partners, and would as such, be liable for all debts of the enterprise. On taking legal advice and after thorough deliberation the four partners decided to organize a corporation in which to vest their partnership property.

In essence therefore the corporation was an incorporated partnership and its stockholders were corporate partners. Each of the four partners invested an equal amount in the business and acquired an equal number of shares in the corporation. Moreover, at the time of incorporation it was understood by all of the partners that each would be a director

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of the corporation and that each would participate actively in the management and decision making involved in operating the corporation. At the same time it was also understood and intended by all the partners that, provided corporate resources permitted, each would receive money from the corporation in equal amounts as long as each assumed an active and ongoing responsibility for shouldering a portion of the burdens necessary to operate the business. The partnership character of the undertaking is also apparent from the arrangement whereby each associate was responsible, presumably in accordance with each particular individual's specialized skills and aptitude, for supervising a particular aspect of the business of running a nursing home. Pursuant to their partnership arrangement each of the partners was appointed as director in terms of the articles of organization of the corporation, and, apart from *P*, all of them served as corporate officers as well. The nature of the corporation as an incorporated partnership does not appear to have changed when *P*, after a long illness, sold his shares to *C*. The last-mentioned was known to *R*, *Q* and *W* because of his dealings with the corporation as its banker. Although *C* was assigned no specific area of responsibility in the operation of the nursing home, he served as financial adviser to the corporation and participated in business discussions and decisions as director. *C* received a weekly stipend from the corporation equal to that received by *W*, *R* and *Q*. All profits were returned to the partners by way of salaries and the corporation never declared or paid any dividends.

Not surprisingly, all the parties in the proceedings before court were agreed that the corporation was at all relevant times a close corporation in terms of the above definition of Chief Justice Tauro. It is significant that because of this particular nature of the defendant corporation, the

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court acknowledged that it did not consider it vital to its approach to the case, whether the claim was governed by partnership law or the law applicable to business corporations.[612] In all these circumstances it therefore appears that it would have been more appropriate to characterize the defendant corporation as an incorporated partnership and not just as a close corporation, as the court saw fit to refer to it.

The instant proceedings were the direct result of the bad blood arising between *Q* and *W* after many years of harmonious co-operation in running the business together. The resultant animosity culminated in *W* being forced out of active participation in the management and operation of the corporation and being "severed from the payroll." This all came about because *W* had insisted on *Q* paying more for a property (*Q* had acquired from the corporation) than *Q* had bargained for. The court came to the "inescapable conclusion" that the action of the majority stockholders here was a "designed 'freeze out' for which no legitimate business purpose has been suggested".[613] To the court it seemed that the true aim of the other partners was to pressure *W* into selling his shares to the corporation at an unrealistic price. It consequently found that *Q*, *R*, and *C*, as majority stockholders, breached their fiduciary duty to *W*, as minority stockholder, and remanded the matter back for further proceedings concerning the issue of damages.[614] The nature of the relief applied for and awarded in the instant case stands in stark contrast to the relief applied for and awarded in very similar circumstances in *Ebrahimi*,[615] which will be considered hereunder. In *Ebrahimi*, however, the House of Lords was loathe to concede that relief was influenced by the character of the company concerned.

Promising signs with regard to the recognition of the incor-

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porated partnership are noticeable elsewhere in the United States. In some States, though, the emphasis is still placed on the dichotomy, "close corporation" and "public-issue corporations," instead of clearly recognizing the "incorporated partnership" concept. One such State is Illinois. In this regard for instance, Mr. Justice Underwood referred to "a definite, albeit inarticulate, trend toward eventual judicial treatment of the close corporation as *sui generis*"[616] in 1965 in the Illinois Supreme Court matter, *Galler* v. *Galler*.[617] And, as the learned judge went on to record, the Illinois court "has recognized, albeit *sub silentio*, the significant conceptual differences between the close corporation and its public issue counterpart ...."[618] But as is apparent from the following passage in the judgment of Mr. Justice Underwood, the traditional approach adopted in Illinois is subject to some limitations: "[w]here, as ... here, no complaining minority interests appears, no fraud or apparent injury to the public or creditors is present, and no clearly prohibitory statutory language is violated, we can see no valid reason for precluding the parties from reaching any arrangements concerning the management of the corporation which are agreeable to all".[619] In this light the following declaration, in which the dilemma of the judiciary is neatly highlighted, does not surprise:

> "Perhaps as has been vociferously advanced, a separate comprehensive statutory scheme governing the close corporation would serve best here. ... At any rate, however, the courts can no longer fail to expressly distinguish between the close and public-issue corporation when confronted with problems relating to either. What we do here is to illuminate this problem — before the bench, corporate bar, and the legislature, in the context of a particular fact situation. To do less would be to shirk our responsibility, to do more would, perhaps be

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to invade the province of the legislative branch ".[620]

In the case at bar, the court, however, had no hesitation in ruling that it was dealing with a "so-called close corporation".[621] The corporation concerned was organized more than forty years previously to incorporate the wholesale drug business which two Galler brothers had been operating in equal partnership for a number of years prior thereto. After incorporation the brothers, *I* and *B*, continued, as before, to be equal associates, each owning 50% of the corporation's 220 shares of stock. Some twenty years prior to the instant litigation each of the brothers undertook to sell to *R*, an employee of the corporation 6 of the shares he owned. Prior to the death of *B*, an agreement was concluded for the financial protection of the immediate families of *I* and *B* in order to ensure that they would have equal control of the corporation after the death of either brother. After the death of *B*, *I* acquired the 12 shares from *R* and refused to honour the agreement previously concluded. The Illinois Appellate Court found that the said agreement violated public policy and was therefore void in its entirety. The Illinois Supreme Court reversed, essentially on the ground that the instant corporation was a close corporation, and held the agreement to be operative as long as one of the two principal stockholders survived.

Mr. Justice Underwood who delivered the opinion on behalf of the court, clearly distinguished between public-issue and close corporations in this regard, recognizing that shareholder agreements similar to the instant one are often essential for the protection of those financially interested in the close corporation. Here the absence of a ready market in which the stockholder can "liquidate" his investment if

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relations should sour, necessitates protection in the form of a shareholder agreement. In the words of Mr. Justice Underwood:

> "While the shareholder of a public-issue corporation may readily sell his shares on the open market should management fail to use, in his opinion, sound business judgment, his counterpart of the close corporation often has a large total of his entire capital invested in the business and has no ready market for his shares should he desire to sell. He feels, understandably, that he is more than a mere investor and that his voice should be heard concerning all corporate activity. Without a shareholder agreement, specifically enforceable by the courts, insuring him a modicum of control, a large minority shareholder might find himself at the mercy of an oppressive or unknowledgeable majority".[622]

At the same time, close corporators are often, as the court observed, both stockholders and directors or officers of their close corporations. With substantial shareholding interests abiding in each member of the board of directors, it is often quite impossible to secure, as in the large public-issue corporation, independent board judgment free from personal motivations concerning corporate policy. For these and other reasons the court found that often the only sound basis for protection is afforded by a comprehensive, detailed shareholder agreement securing the rights and obligations of close corporators.[623] For purposes of its opinion the court stated that a close corporation was a corporation in which the stock was held in a few hands, or in a few families, and wherein it was not at all, or only rarely dealt in by buying or selling.[624] The court obviously was not asked to consider whether the particular close corporation was an incorporated partnership

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at the time, that is after the death of *B*. Clearly, during the lifetime of the two partners, *I* and *B*, the corporation was an incorporated partnership. Whether the instant corporation retained that character after the death of *B* depends on whether the heirs of *B* entered into a new partnership with *I*. The record is unfortunately silent on this question.

In other states, courts have come out in recognition of the close corporation as an incorporated partnership. Indiana has taken the lead in this field. The opportunity to do so presented itself in *Hartung* v. *Architects Hartung/Odle/Burke, Inc. et al.*[625] Here the plaintiff-appellee corporation was organized to continue the professional practice previously carried on as a sole proprietorship by an architect, *H*, the defendant-appellant. *O* and *B*, professional architects and former employees of *H*, joined with *H* as incorporators. Each served as an officer, a director, and an equal shareholder in the new corporation. Apart from the fact that the former employees, *O* and *B*, became equal partners, albeit in an incorporated partnership, with *H*, incorporation of the firm did not bring about major changes in the operations of the proprietorship. Prior to incorporation *H*, as sole proprietor, acted as "contact" or "front" man, that is, the link between the firm and its clients. Upon incorporation, *H*, who was elected president, continued to act as the "front" man and the clients of the proprietorship were assigned to the corporation. In a like fashion the offices rented by the proprietorship on a monthly tenancy were also assigned and became the corporate offices.

Within four months after incorporation, discord set in and *H* resigned both as president and director. Before resigning *H* renewed the lease of the corporate offices in his

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own name and had enticed corporate clients back to him. *O* and *B*, individually and as officers of the incorporated partnership filed suit against *H* for breaches of fiduciary duty both as stockholder and as director and officer. The Indiana Circuit Court entered judgment for the plaintiffs and *H* appealed, unsuccessfully.

In the Indiana Court of Appeals Mr. Justice Robertson had no difficulty in disposing of the contention advanced by *H* that the evidence was insufficient to establish the existence of a fiduciary duty on the part of *H*. In this regard the learned judge noted that the corporation in question was "an 'incorporated partnership' comprised of professional people"[626] of which *H* was a director, an officer, and one of only three shareholders and held that a fiduciary duty attached to *H* in each capacity.[627] After noting that a director has long been held to be a fiduciary, Mr. Justice Robertson held: "In addition, the shareholders in a close corporation, also referred to as an 'incorporated partnership', stand in a fiduciary relationship to each other ".[628] This fiduciary relationship will clearly be an associative, lateral, or horizontal fiduciary relation, as opposed to the vertical fiduciary relation subsisting between a director and a corporation. The argument, which *H* raised, that a fiduciary duty should not arise in an incorporated partnership of professional architects, was rejected outright by Mr. Justice Robertson who explained: "The critical factor giving rise to such a duty should not be the nature of the work product of the corporation, rather it should be the relationship expected by the principals to exist between themselves and the corporation and each other".[629] The learned judge also observed that the nature of the said fiduciary duty was basically the same regardless of the capacity in which it arises, (a

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statement which will be analyzed hereunder) and that, in essence, the purport of the said duty was that the fiduciary must deal fairly, honestly and openly with his corporation and fellow stockholders.[630] More recently this sound opinion was reaffirmed by the Indiana Court of Appeals in *Cressy* v. *Shannon Continental Corporation et al.*[631]

In *Cressy*[632] the Indiana Court of Appeals once again recognized a close corporation for what it really is, namely an incorporated partnership. Here *C*, a realtor, located an old office building suitable, if remodelled, to be turned into a profitable rental location. After negotiating with the owners with a view to purchasing it, and having architectural drawings and renderings prepared to demonstrate his ideas, *C*, in an effort to implement these ideas, approached several prospects including *R* whom he knew socially. Agreement was reached between *C* and *R* whereby they would be "fifty-fifty partners" in owning the building and would form a corporation to carry out their purpose. In pursuit of their plan *R* contracted to buy the building and made a down payment of which one half represented reimbursement for the contributions of *C* in putting the transaction together. Shortly thereafter the defendant corporation was incorporated by *C* and *R* and the property vested in it. *C* and *R* each subscribed to, and received, 425 shares in the common stock of the said corporation leaving 150 shares unissued. Subsequently 30 of these shares were issued to the parents of *R*, for advancing funds when the corporation was in need thereof, and 120 to three individuals in connection with professional services rendered by them for the corporation. Among these was *F*, the treasurer and accountant of the corporation. At a later stage *C*, without notifying *R*, acquired all of the 75 shares held by *F* in the corporation. When

transfer/.....

transfer of the said 75 shares into the name of *C* was refused, litigation commenced. The trial court determined that the mutual intent of the two shareholders *C* and *R* had been one of equal partnership and fashioned equitable relief. The order was that the articles of incorporation be amended to provide for a second class, non-voting stock and that the 30 shares held by the parents of *R* and the 75 shares assigned by *F* to *C*, be non-voting shares of such class. *C* appealed, challenging the ability of the court to recognize an "incorporated partnership" and to grant relief in the form provided by the order. The Indiana Court of Appeals found that while the trial court had the power to enter an order against *C* and *R*, requiring them to exercise their voting rights consistent with their obligations or had the power to order the sale of an "equalizing" number of shares, it exceeded its powers when it declared the articles amended.[633]

Mr. Justice Garrard, who spoke on behalf of the Court of Appeals, was at pains, though, to stress that the trial court had not erred "in finding an 'incorporated partnership'".[634] Dealing with the latter concept, the learned judge said:

> "The imposition of such duties as the term 'incorporated partnership' implies is a recognition that this form of business enterprise is a hybrid. While parties incorporate to obtain the benefits of limited liability, perpetual existence of business entity or tax consideration accruing to the corporate form, they often expect to act and to be treated as partners in their dealings among themselves".[635]

At the same time Mr. Justice Garrard took care to point out that the court did "not suggest that such a relationship arises *a fortiori*/....

fortiori in a corporation involving few shareholders". For as the learned judge correctly observed, "such parties may well intend to do business with the world and among themselves strictly in accord with the norms of general corporation law".[636] Yet, as Mr. Justice Garrard acknowledged, "[w]hen this intention is manifest and no harm results to outsiders thereby, there appears little reason to frustrate the parties' actual intent by strict adherence to the traditional norms of corporate law".[637] Mr. Justice Gerrard referred to Mr. Justice Burger's observations in *Helms*[638] that close corporators bear towards each other that same relation of trust and confidence which prevails between partners. The learned judge also referred to the Indiana court previously in *Hartung*[639], recognizing the "principle of 'incorporated partnership'" and the principle that, independent of possible status as officers or directors, close corporators owe to each other a fiduciary duty to deal fairly, honestly and openly.[640] Against this background, the Court of Appeals confirmed the trial court's finding that *C* and *R* intended equal ownership and control of the business and held:

> "The 'partnership' expectation of equality of shareholdings carried with it the duty on the part of each principal to disclose to the other the availability of outstanding shares for sale and to afford the opportunity to share in the purchase of such stock".[641]

In the result the Indiana Court of Appeals concluded that the trial court was justified in determining that *C* and *R* had each breached such fiduciary duty.

The incorporated partnership has at last arrived. Traces of earlier theories are sometimes still evident. Yet the judicial recognition of the incorporated partnership in its own right is today indisputable. This is clearly borne out by the body of case law reviewed above.

20.3.4.3. *JUDICIAL RECOGNITION OF THE INCORPORATED PARTNERSHIP FOR WINDING-UP PURPOSES*

Despite the traditional conception that "[t]he dissolution of corporations, like their creation, is primarily and fundamentally a matter of legislative and not of judicial cognizance",[642] the judiciary has gradually taken the responsibility upon itself of dissolving solvent corporations where equity has demanded it. Partnership principles have also played a role here, more particularly once the idea of the close corporation had become established. Yet compared with the large volume of decisions in which courts have applied partnership principles to achieve justice, other than by dissolution of the corporation, the decisions in which courts have to that end resorted to dissolution by applying partnership principles, are but few and far between.

At the beginning of the present century, courts began to question the traditional concepts in this field. The suggestion that a new approach could be in the offing might perhaps be inferred from the following passage found in a judgment handed down in 1916:

> "Is there, then, anything sacrosanct about a corporation as a form of association? We think not. It is only another means of associating men together under the forms of law for the achievement of a certain purpose, and when the purpose has manifestly failed, the compulsion to remain associated may as well be relaxed".[643]

Yet, the general consensus at the time seems to have been that the traditional rule survived and the few contrary cases were regarded merely as exceptions, proving a general rule.[644]

Reference/ .....

Reference to partnership in this context began to show up as early as the second and third decade after the turn of the previous century. A case in point is the Michigan decision, *Flemming v. Heffner & Flemming*.[645] Here the defendant corporation was organized for the purpose of dealing in real estate. One-half of the shares were held by the plaintiff, and the other by Heffner and his wife, who held one share, possibly as a nominee. Mr. Heffner served as president, his wife as vice-president, and the plaintiff as secretary treasurer. The plaintiff, in his bill of complaint, alleged that the Heffners at a board meeting, the validity of which the plaintiff questioned because of his absence therefrom, removed him as secretary-treasurer and substituted Mrs. Heffner in his place. The plaintiff further alleged that the purpose of the said substitution was to enable the Heffners to control the corporate funds which, under the by-laws, could be withdrawn from deposit only upon order of the president and the secretary-treasurer and that his ousting was in furtherance of a scheme to "freeze" him out of the corporation and to force him to sell his stock therein at an unconscionably low price. The prayer which was, *inter alia*, for the appointment of a receiver, was granted. The defendants appealed.

Mr. Justice North, who wrote the opinion on behalf of the appeal court, acknowledged that the general rule undoubtedly was that courts of equity did not have power to wind up a corporation in the absence of statutory authority. The learned judge, however, conceded that the said rule was subject to a number of qualifications and pointed out that when it turned out that the purpose for which a corporation was formed could not be attained, it was the duty of the "company" to wind up its affairs.[646] Mr. Justice North further acknowledged that

"when/ .....

"when dissension among those in charge of a corporation got too bad, it was necessarily impossible for the corporation to attain the objects for which it had been formed and failure was inevitable".[647] Against this background the Michigan Court of Appeal affirmed the appointment of the receiver and held:

> "There are many authorities which uphold the power of a court of chancery to dissolve a corporation because of dissensions of so serious a character as under the circumstances will inevitably defeat the purpose for which it was created. Especially is such the holding in cases where there are only a few stockholders, so that the corporation for practical purposes, as between those interested, is much like a partnership".[648]

Prior to the recognition of the close corporation as such, corporations had been wound up by courts of equity when such corporations had served as mere instrumentality or medium of a partnership and justice could be obtained only by winding up the corporation. A case in point is the early United States Court of Appeals matter for the Fifth Circuit, *La Varre* v. *Hall*.[649] Here two newspaper men conceived the idea of acquiring a group of newspapers in the Southeast and, to that end, entered into a partnership agreement on an equal basis. Each partner was to contribute such skill and experience as he had, but because neither possessed sufficient means to finance the project, outside capital was obtained. Pursuant to this arrangement the said partnership acquired the entire capital stock of a number of newspaper publishing companies. *L*, however, in breach of the partnership agreement, appropriated the said stock for himself and *H* successfully petitioned for a decree dissolving the partnership and compressing the

capital/ .....

capital stock of the newspaper corporations in question with his interest. *L* appealed, contending that the partnership agreement sought to be enforced was against public policy. The argument advanced on behalf of *L* in this regard was that *H* and *L*, as co-partners, were attempting to do business in corporate form for their own convenience, and that they were treating the corporate powers and functions as mere incidents. This argument found no favour with the United States Circuit Court of Appeals and was rejected by it in one terse line: "This contention requires no discussion as it is entirely without merit".[650]

More recently a somewhat similar result was achieved by the New Jersey court in *Fortungo*.[651] Here the court was asked to wind up five corporations which were set up as mere mechanical devices for running the family partnership enterprise. The basic dispute concerned the distribution of partnership assets. The central issue was whether the five corporations, which were operated and controlled by the family partnership as the instrumentality of its operations, were assets of the partnership or were owned by the individual partners. If the said corporations were assets of the partnership, the further question was whether such assets were to be distributed equally among the partners by means of a distribution of shares of capital stock or whether the said assets of each individual corporation were to be treated as partnership property and (a) liquidated and the proceeds distributed, or (b) divided in their then form and distributed equally? One of the partners, *A*, claimed the corporations were assets of the partnership and that he was entitled upon dissolution of the partnership to his proportionate share in cash, rather than to be forced to exchange his position as an equal partner for that of a minority shareholder in the

family/ .....

family-controlled corporations whose shares would have no value on the open-market. *A* in essence contended that he was entitled to an *effective* dissolution — one that would permit him to get out of the family partnership completely and forever. The other partners (relying on the partnership agreement between them) contended that the shares of stock in the corporations should be distributed, *i.e.* that the businesses of the corporations were not the businesses of the family partnership but of the corporations themselves, viewed as separate entities.

The Superior Court of New Jersey, Appellate Division, came to the "inescapable conclusion" that all the corporations constituted a single whole with the partnership and were treated as a single enterprise by the partners and said:

> "It is therefore not unfair to the remaining partners to treat them as truly partners upon dissolution. Only the partners are involved in this litigation, there are no creditors or other third parties. In such cases we may ignore the corporate entity in order to do that which is just ...."[652]

The court stated that its sense of fair play would be offended if it left *A* at the mercy of the other partners in this regard and that the assets of the partnership, including those of all the corporations, should be liquidated, and the proceeds distributed in cash.[653]

The impact of the recognition of the close corporation in this field is particularly noticeable in New York decisions. An early example is *In re Pivot Punch and Die Corp.*[654] This was a proceeding for the dissolution of what the court referred to as a "domestic", New York corporation. The undertaking was started many years previously by the petitioner, one Kopczynski.

Subsequently/ .....

Subsequently one of the respondents, a Mr. King, joined the corporation, obtaining a 50% stock interest in it, thus becoming an equal stockholder with the petitioner. Although the corporation initially prospered and relations were cordial, management and policy disputes between the two equal stockholders crept in. As such disputes became acute, prosperity declined. The deadlock which arose between the stockholders made it impossible to elect a board of directors and further disputes resulted in the petitioner being discharged by arbitrators from his corporate office and the said arbitrators taking office in his stead. Therefore a situation prevailed where the petitioner had no voice in the management of the corporation and received no income from it while his co-shareholder was receiving a substantial return for his services to the corporation. The petitioner under these circumstances petitioned for the dissolution of the corporation under the General Corporation Law. The respondent, although conceding that there was a deadlock of the two equal stockholders, resisted on the ground that there was no deadlock between the directors.

Mr. Justice Jasen of the New York Supreme Court rejected the respondent's contention in this regard, pointing out that General Corporation Law, § 103 specifically provided for dissolution in cases of deadlock between stockholders, in addition to deadlock between directors. The learned judge went on to hold that the petitioner had further established, as he was required to do by statute, that the dissolution would be beneficial to the stockholders and that the dissolution would not be injurious to the public. With regard to the former requirement, Mr. Justice Jasen observed that in determining what was beneficial to stockholders, the court

had/ .....

had to take into consideration the *type* of corporation before it and said:

> "We have here what is generally referred to as a close corporation, 'one that has been organized by an individual or a group of individuals seeking the recognized advantages of corporations .... but regarding themselves basically as partners'".[655]

Close corporation in this sense clearly means "incorporated partnership".[656] Mr. Justice Jansen stressed this in the following lines:

> "It must be conceded by all concerned that in effect, the Pivot Punch and Die Corporation is a close corporation and, being a close corporation, it is simply a partnership consisting of Mr. Kopczynski and Mr. King, clothed with the benefits peculiar to a corporation, limited liability perpetuity and the like. It would be mere prolixity to substantiate such a conclusion by quoting decisions in this and other states. The United States Government ... has acknowledged the kinship of a close corporation vis-a-vis a partnership by permitting, in a situation such as before this Court, the stockholders to file and pay income taxes as though they were in fact partners. Obviously, the United States has concluded that a close corporation is in effect a partnership".[657]

The court noted that it was trite law that a partnership might be dissolved at any point or by any partner or by the court where a partner's conduct is harmful. What was, however, of greater significance in the mind of the court in finding

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that the petitioner had adequately alleged benefit to stockholders in terms of the statutory requirements, was the character of the inter se relation of the members of an incorporated partnership. In the words of Mr. Justice Jasen:

> "In addition to the technical rules surrounding a partnership and perhaps from a purely moral point of view, more important, there exists between partners the highest degree of fidelity, loyalty, trust, faith and confidence. *When these characteristics in a partnership cease, then the true partnership ceases*, and when *these characteristics cease between owners* of equal, or verily, substantially equal, shares *in a close corporation*, the *close corporation ceases* to be beneficial to the deadlock stockholders".[658]

Similar sentiments, it will be recalled, had previously been expressed in an English court in a matter concerning partnership proper.[659]

A few years later a similar situation came before the New York Court of Appeals in the matter of *Kruger et al.* v. *Gerth et al.*[660] Here minority stockholders brought action against the corporation and two of its three directors to compel the said directors to dissolve the corporation and to enjoin, as a waste, the payment of certain bonuses to a director and employees of the corporation. On the available facts it is not clear whether the instant corporation was an incorporated partnership or just a mere close corporation. The dissenting judgment of Field, J., however, appears to indicate that the corporation might have been of the former type. A, the principal defendant-respondent, held 53% of the

common/ ....

common stock, his brother 1% and the petitioners-appellants the remaining 46%, which they had acquired under the will of a deceased testator. The directors of the corporation were *A*, and his brother, and prior to his death, the deceased testator who had been employed by the corporation and had at all times prior to his illness received a salary equal to that received by *A*. The complaint was that *A* was taking for himself a bonus and a salary in such amounts as reduced the net corporate profit below the amount necessary to provide dividends to pay plaintiffs on their common stock.

The New York Appellate Division held that the dissolution of the corporation was not justified only because the amount of bonuses received by *A* so reduced the net profit of the corporation as to leave an insufficient amount to provide a fair return to minority stockholders. The minority stockholders appealed to the Court of Appeals, where a majority of 4 to 3 affirmed the refusal of the dissolution order. For present purposes the separate dissenting opinions of Desmond, C.J., and Field, J., in which Burke, J., concurred, are of significance.

Desmond, C.J., approached the issues from the point of view of the corporation being a "two-man corporation." The main issue in his view was not that the salary and bonus paid to *G* were exorbitant, but that the corporation was being kept alive solely to pay that salary and bonus. In this context the learned judge referred to the "modern and just rule" whereby a court of equity would wind up the affairs even of a solvent, going corporation, if liquidation is not only the way of preventing loss to stockholders but also serves a beneficial purpose to all stockholders.[661] Against this

background/ .....

background the learned judge distinguished between small, two-man corporations on the one hand, and large corporations, on the other

"Such small corporations," Desmond, C.J., said, "being really partnerships between two or three people who contribute their capital, skills, experience and labour should be treated by a court of equity as partnerships in many respects".[662] On the other hand, as the learned judge observed, "[a] large corporation or one that has some prospect of becoming large is really an institution separate and distinct from its owners serving a separate purpose in ... society by providing employment, accumulating capital for proper purposes ...."[663] However, the crucial distinction between the two types of corporations in the view of Desmond, C.J., was the grounds upon which winding-up would be justified in the one case, but not the other. In his own words:

> "Even if such a large or growing corporation is temporarily operating at a loss there may be quite reasonable expectations that its position will improve. Not so with the two-man corporation which owns no valuable trade secrets, market advantages or growth probabilities but simply continues to exist as the form in which two individuals pool their efforts. When one of those two dies and everything indicates that the corporation can never do more than pay a salary to the survivor, the reason for corporate existence is gone...."[664]

For these reasons the learned judge felt that it was just that the instant corporation should be wound up. Fuld, J., concurred but for different reasons. "The enterprise before us," he said, "is a 'close corporation' in the strictest sense, that is one in which, regardless of the distribution of the shareholdings, 'management and ownership are substantially identical'".[665]

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In this regard, Fuld, J., distinguished between the close corporation and the "larger or less closely held enterprise". In the case of the first, where, in the words of Fuld, J., "the relationship between the shareholders is very much akin to that which exists between partners or joint venturers", it seemed to him almost self-evident that the fiduciary obligation of the majority to the minority extended considerably beyond the reach of the second type.[666] Although the judge acknowledged that each case had to be determined upon its own facts, he felt that despite *Weisman*,[667] there "is no inherent reason why a court of equity cannot treat the participants in a genuine close corporation, insofar as their relationship inter se is concerned, as they regarded themselves — as partners or joint venturers".[668] On this construction such participants became, in the view of the learned judge, "not only entitled to the benefits of the relationship but equally subject to its burdens, including the power of a court of equity to dissolve the venture ...."[669] Summing it all up, Fuld, J., concluded:

> "Thus, it is my opinion, particularly in view of the increasing trend to legislative and judicial recognition of the distinctive character of the genuine close corporation, [*i.e.* an incorporated partnership], that the analogy of the relationship between the participants themselves — wholly apart from that of their corporate creature to the world at large — to an informal joint venture with the shares of the corporation as its asset is apposite and useful".[670]

Further evidence of the trend referred to by the learned judge, is found in two subsequent New York decisions namely *Mtr. of*

Surchin/.....

Surchin v. *Approved Business Machines Co., Inc.*[671] and Mtr. of *Weis et al.* v. *Gordon Weis, Inc.*[672]

In *Surchin*,[673] Mr. Justice Levy decreed that a solvent "closed corporation" be wound up on the grounds of serious internal dissension between two shareholders and that such dissolution would be beneficial, both individually and otherwise, to the two factions in which the shareholders had come to be divided. In this matter no account of the history of the corporation or of the composition of its members was given. However, that did not deter the learned judge from quoting at length from *Pivot Punch*[674] and stating:

> "Now I am quite convinced that, if we are to follow Mr. Justice Jasen's and the learned academicians' viewpoint that a close corporation, such as the one now before me, is quite like a partnership, the present partnership-corporation should be dissolved, because the partners have shown that they have no confidence in, and indeed that they mistrust, each other, whatever their protestations may be".[675]

Mr. Justice Levy made it quite clear, however, that even under the ambit of the Business Corporation Law, he saw no solution to the controversy between the shareholders other than to direct a dissolution by judicial decree. He held:

> "I cannot believe that I would not be authorized by this statute to direct a dissolution of a close corporation, when one of the two active shareholders, who is an active director and active officer of the corporation, issues threats of personal violence, listens in surreptitiously on his associate's telephonic talks, seizes and cuts telephone wires, acts in the presence of employees so as

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to demean his associate as an employer in the corporation, takes trips at corporate expense without advance mutual consent, leaves the shop inadequately manned, and engages in other activities as if he were the sole owner of the business. And I would say that dissolution would be in order even if money were being made quite fully and readily by the corporation under such conditions — which is not the case here".[676]

The learned judge specifically noted that although the benefit to shareholders of a dissolution was of paramount importance, it was equally clear that, in terms of a recent legislative amendment, dissolution was not to be denied merely because the corporate business had been or could be conducted at a profit. Against this background Mr. Justice Levy found that there was unquestionably serious deadlock between both shareholder and directors and decreed a final order of dissolution.

In *Weis*[677] the Supreme Court of New York, Appellate Division, by a majority of 4 to 1, upheld an order granting an application for the dissolution of a close corporation. The corporation in question operated as a service corporation in the advertising field. Since its incorporation some 6 years earlier it had prospered to a reasonable extent and was at the time of the proceedings still earning some profits. The services for the clients were performed by the two parties to the proceedings, who were equal shareholders and enjoyed equal representation on the board of directors. There was a third shareholder, who owned 10 shares, but apparently enjoyed no voting rights. His position appears to have been regarded as purely nominal. No particulars were furnished concerning the purpose and circumstances of his stock ownership.

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It was common cause that the principal shareholders were not getting on and were not working together. No significant corporate action was possible by reason of the inability of the board of directors to function because there was either deadlock or by purposeful absence of a quorum the board could not function. This situation brought about a consequent decrease in profits and loss of personnel.

The respondent alleged that for some time prior to the proceedings the petitioner had been trying to push him out of the business and that various methods had been adopted to this end. First, the respondent alleged, there had been an attempt to acquire his interest at a price he regarded as grossly inadequate. This, he maintained, was followed up by sundry illegal measures designed to coerce him into acceptance. Finally, when the petitioner was thwarted in these efforts, the proceedings before court were instituted.

Mr. Justice Steuer, who delivered the majority opinion, saw the issues simply as those peculiar to a close corporation. In a passage describing the advance made by the close corporation in recent times, particularly in the legislative field, he said:

> "In the instance of the close corporation, both the legislature and the courts have come closer to treating the situation as it exists in fact rather than in theory. The enactment of section 1111(b)(3), providing that in cases of deadlock among directors and shareholders dissolution should not 'be denied merely because it is found that the corporate business has been or could be conducted at a profit', reflects that change. The earlier thinking stressed the distinction between the corporation as an entity and the shareholders, and as long as the

former/ .....

former could continue to function profitably the relationship between the shareholders was of no moment ...."[678]

In an obvious reference to the recognition by the judiciary of the incorporated partnership Mr. Justice Steuer observed that it was "being increasingly realized that the relationship between the stockholders in a close corporation vis-a-vis each other in practice closely approximates the relationship between partners ...."[679] This therefore justified the conclusion that "when a point is reached where the shareholders who are actively conducting the business of the corporation cannot agree, it becomes in the best interests of those shareholders to order a dissolution".[680]

Mr. Justice Steuer found that the respondent's claim that the application was brought *mala fide*, because dissolution was allegedly sought to "squeeze" the respondent "out of the business for an inadequate consideration", to be of no consequence. "While his [the respondent's] averments do show", the learned judge noted, "that the petitioner had embarked on a course of conduct which did have that end in view, the institution of this proceeding precludes it".[681] In explaining this statement more fully the learned judge said the following:

"Whatever respondent's share of the business is, he will get it. Instead of forcing respondent to accept an inadequate consideration for his share of the business, petitioner now applies to the court to make the distribution".[682]

The myth that corporate existence is sacrosanct, has been exploded.

20.3.4.4. *JUDICIAL RECOGNITION OF CLOSE CORPORATORS' INTER SE FIDUCIARY DUTIES*

True to the general name, "close corporation," which properly used identifies the incorporated partnership, the character of the inter se relation of its members is close,[683] that is, is steeped in mutual confidence and trust. As Oleck puts it, "[t]he identity of the other stockholders is important to each; the incorporators have confidence in one another which they may not have in an outsider."[684] In a nutshell, *delectus personae*[685] pervades the relation subsisting inter se the close corporators. This explains why one commentator could exclaim, "[c]lose-corporation law . . . is witnessing the not very surprising development of the notion that shareholders of such a corporation are fiduciaries *inter sese*."[686] This is borne out amply by the many opinions reviewed above.

Of the many instances encountered, two are particularly apposite in the present context. In *Donahue*,[687] for instance, the reason why Mr. Justice Tauro found that close corporators owed one another substantially the same fiduciary duty in the operation of the enterprise that partners owe to one another, was that mutual trust and confidence were essential to this scale and manner of enterprise.[688] Earlier the learned judge had held that the relationship among the stockholders must be one of trust, confidence and absolute loyalty if the enterprise was to succeed.[689] And in *Pivot Punch*,[690] Mr. Justice Jasen found that just as a true partnership ceases to exist when the highest degree of fidelity, loyalty, trust, faith and confidence which pervade the inter se relation of partners, cease, so an incorporated partnership ceases in effect, when such characteristics cease.[691] In both instances the judiciary was referring to

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lateral fiduciary relations as opposed to vertical, fiduciary relations. In fact, it will be recalled that in all of the many opinions which were considered, the basic relation was a lateral or associative relation and not a vertical relation.

Against the above background it is now possible to evaluate the judicial experience encountered in the English system in this sphere.

CHAPTER VII

JUDICIAL RECOGNITION OF THE INCORPORATED PARTNERSHIP AS THE QUASI-PARTNERSHIP COMPANY IN THE ENGLISH SYSTEM

21.1. INTRODUCTION

The English private company happily exists in an environment far more hospitable to the survival and operation of partnership principles than is the case with, for instance, its American counterpart, the close corporation. The English incorporated company has after all evolved from the equitable joint stock company or public-issue incorporated partnership, which, true to its partnership nature, was based, not on a statutory charter, but as in partnership on the contract between the associates. In fact, it enjoyed a constitution as supple and flexible as is found in partnership and in many other respects resembled partnership despite its achieving corporate status. It is not surprising, therefore, that the English incorporated company has been referred to as a quasi-corporation,[692] or as a hybrid, a partnership, invested with the character of incorporation, so that it is governed by rules that derive from both the law of corporations and the law of partnership.[693]

In the case of the English company one would, therefore, expect the judiciary to have been willing to recognize the operation of partnership-like inter se fiduciary duties between members of statutory private companies at least as readily as the American judiciary has, if not more so. Yet the contrary seems to be true. For until about five years ago, and apart from two earlier Scottish matters — *Harris*,[694] and *Scottish Co-op. Wholesale Soc.*[695] — the only instances in which partnership

principles/ .....

principles have been applied to members of incorporated companies in their inter se relations are those in which courts, in terms of the statutory just and equitable winding-up provision, have wound up solvent companies that have come to be identified as quasi-partnership companies.

It is interesting to observe, as the House of Lords did in *Ebrahimi*,[696] that the same words, "just and equitable", are found in both *Companies Act*, 1948,[697] §§ 222(f), and *Partnership Act*, 1890,[698] §§ 35(f). Lord Wilberforce in fact referred to this similarity as a significant signpost, of which the "importance" was that it "provide[d] a bridge between cases under section 222(f) of the Act of 1948 and the principles of equity developed in relation to partnership".[699] Whereas in a different context the similarity between these statutory provisions may certainly be of historical significance its importance from a practical, company law, point of view should be kept in perspective. Caution should be observed not to regard the above statutory provisions as the sole "bridge" between principles of equity developed in relation to partnership proper and company law. In particular caution should be observed not to fall into the trap of mistaking this statutory provision for some magical *fons et origo* of justice for shareholders. This is the illusion under which the Court appears to have laboured in *Clemens*,[700] a matter in which the Court was asked to avoid a resolution passed in disregard of the rights of a minority member and not to wind up the company. Despite this the Court nevertheless found it necessary to base its ruling on the just and equitable provision in apparent deference to the sentiments expressed by Lord Wilberforce.

The application of principles of equity developed in relation

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to partners in their inter se relations, to members of an incorporated partnership in their inter se relations, does not depend on the existence of a statutory just and equitable winding-up provision either in partnership law or in company law. The importation of partnership precepts into company law is justified by considerations other than the mere use of similar words in a partnership statute and a company statute respectively. One such consideration that may be of significance is, for instance, the character of the company concerned as determined by the nature of the inter se relation of its members. This may, for instance, establish that the company in question is a partnership in corporate guise. Another, closely related, consideration in the English system is the close kinship between companies and partnerships, and consequently also of company law and partnership law. This kinship naturally results in the mutual exchange, between the two systems and institutions, of concepts and precepts as may be required. A case in point is the statutory just and equitable winding-up provision. However, what should be borne in mind in this regard is that *Partnership Act*, 1890,[701] §§ 35(f), was modelled on an earlier company law provision, to wit *Companies Act*, 1862,[702] §§ 79(5). The latter provision, in turn was, inspired by partnership precepts! In fact, although a similar statutory provision is not found in South African partnership law, South African courts have not hesitated to apply partnership precepts in winding-up solvent, quasi-partnership companies in applications brought under the statutory just and equitable winding-up provisions of the *R.S.A. Companies Act*, 1973,[703] or its predecessors. More important, however, South African courts have on three occasions within the last five years referred to partnership principles in judging the propriety of conduct of members of statutory companies,

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in their inter se relations. In none of these matters was the relief sought the winding up of the company, and in none did the court find it at all necessary to appeal to *R.S.A. Companies Act*, 1973, [704] §§ 334(h), to justify its resorting to partnership precepts. Needless to say, the companies in question were incorporated partnerships. Scottish experience in this regard is very similar. In fact, the first courts in the English system to apply partnership precepts to members of incorporated companies in their inter se relations, with regard to both winding-up and non-winding-up situations, happened to be Scottish courts. In none of these decisions, however, was it sought to justify the resort to partnership proper principles in terms of the statutory just and equitable winding-up provision. This was not necessary. Here the close likeness in Scotland between companies and partnerships has always served as a far more direct link between the principles of equity developed in relation to partnership proper and company law than has the ostensible similarity between the statutory just and equitable winding-up provisions found, respectively, in the two relevant statutes.

In principle the position in England in this regard should be the same, and to some extent it is. In all decisions relevant to the present discussion in which solvent companies have been wound up in terms of the just and equitable winding-up provision, the character of the company, as determined by the inter se relation of members — that is, whether it is in fact an incorporated partnership — has assumed far greater significance than the ostensible similarity between the statutory winding-up provisions referred to above. This explains the repeated use, by the judiciary and commentators alike, of the term "quasi-partnership" in this context.

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"The term *quasi* partnership" an old Scottish authority acknowledges, "has always been held to form a very strong presumption for the existence of an actual partnership".[705] In this light it is clear that the use of the term "quasi-partnership company" in the present context is intended to convey that although a particular association may be de jure an incorporated company, it is de facto a partnership; in short, that the company concerned is an incorporated partnership. This will be found to be the case in the decisions to be considered. This, it is submitted, is the real reason why courts have resorted to the partnership principles in decreeing the winding-up of solvent companies.

That Lord Wilberforce saw fit to caution against the injudicious use of the term "quasi-partnership company" in this context is of little moment, as will be observed hereunder. Of greater moment is his Lordship's identifying the characteristic features of an incorporated partnership in his endeavour to enumerate some of the considerations that in his view make it just and equitable to subject the exercise of legal rights to equitable considerations. This epitomizes the extreme irony of the English approach in this sphere. English company law has turned its back on its rich, readily accessible partnership heritage. Yet principles of equity developed in relation to partnership are consciously invoked in company law. When invoked, however, these principles of partnership law are applied not to ensure the continued existence of the company but instead to bring about its dissolution and the winding-up of its affairs. This appears to be anomalous in the extreme. A quasi-partnership company is permitted to pass away in accordance with partnership rites—the resulting extinction of its very soul, the statutorily created right-and-duty-bearing unit, that is the

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body corporate, notwithstanding. Yet a quasi-partnership company is apparently, because of the very fact of incorporation — that is, the statutorily creation of the right-and-duty-bearing unit — not permitted to live according to partnership norms even if such norms touch upon the inter se relations only of its members. This makes nonsense of the concept of incorporation.

Against this background it is now proposed to consider the more representative English, Scottish and South African decisions concerning the winding-up, under the statutory just and equitable winding-up, provision of solvent quasi-partnership companies. This will be followed by a discussion of the small number of decisions in which partnership norms have been applied to members of incorporated partnerships in situations not concerning winding-up. Here, as in the discussion of the corresponding American decisions, the general approach will be to establish in each case the nature of the aberrant conduct, whether unconscionable or otherwise wrongful; the particular character of the company concerned as determined by the nature of the inter se relations of its members; and the true *ratio decidendi* of the decision. In each case the pertinent enquiry will be whether the winding-up or other order which was decreed, was in any way related to the character of the company concerned.

21.2. *THE QUASI-PARTNERSHIP COMPANY AND THE EXTREME REMEDY — CORPORATE DISSOLUTION*

21.2.1. *INTRODUCTION*

Before considering the relevant case-law it is

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necessary to discuss briefly the history and ambit of the statutory just and equitable winding-up provision. This paragraph will conclude with a general profile of the incorporated partnership viewed as a quasi-partnership company.

21.2.2. *THE STATUTORY JUST AND EQUITABLE WINDING-UP PROVISION*

The statutory just and equitable winding-up provision did not appear in the *Joint Stock Companies Act*, 1844,[706] but made its debut four years later in *An Act to amend the Acts for facilitating the winding-up of the Affairs of Joint Stock Companies unable to meet their Pecuniary Engagements, and also to facilitate the Dissolution and winding-up of Joint Stock Companies and other Partnerships*, 1848,[707] §§ 5(8). The reference in the title to "other partnerships" is particularly significant. It emphasized the close affinity between partnerships and companies and paved the way for a similar provision in the *Partnership Act*, 1890,[708] §§ 35(f). It is interesting to observe that although the Court of Chancery had worked out recognized grounds for dissolution of a partnership, the words "just and equitable" had not been used before in any context.[709]

The 1848 enactment is generally regarded as the first statutory provision enabling members, *qua* members, to petition the court for the dissolution of a solvent incorporated company.[710] However, because six of the preceding grounds for dissolution in that provision were all related to insolvency and the eighth ground itself was worded "[o]r if any other Matter or Thing shall be shown which in the Opinion of the Court shall render it just and equitable that the company should be dissolved", the latter provision appeared

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to be an obvious candidate for the application of the *ejusdem generis* construction.[711] Within a year of its being enacted the provision was in fact interpreted in that fashion. In 1849 Lord Cottenham remarked that "this clause [§§5(8)] was no doubt thus worded in order to include all cases not before mentioned," and added: "of course, it cannot mean that it should be interpreted otherwise than in reference to matters *ejusdem generis* as those in previous clauses".[712]

In the *Joint Stock Companies Act*, 1856,[713] the just and equitable provision was dropped in favour of a provision empowering winding-up if three-fourths of the subscribed capital had been lost.[714] This regime was short-lived, for within a decade and a half the legislature restored the just and equitable ground, albeit in a different setting and wording. Thus of the five grounds in *Companies Act*, 1862,[715] § 79, only one related to insolvency.[716] Moreover, the fifth ground, the just and equitable provision, read: "[w]henever the Court is of the opinion that it is just and equitable that the company should be wound up." This rendered the link with the preceding grounds more tenuous and the application of the *ejusdem generis* rule more difficult. Yet habit, like tradition, sometimes dies hard. In 1867 Lord Cairns in *Re Suburban Hotel Company*[717] still loyally maintained that the wording of the just and equitable provision was exactly the same in the 1862 as in the 1848 statute and duly proceeded to apply the *ejusdem generis* rule. Although still regarded as well established in 1877,[718] the authority of the *ejusdem generis* rule gradually slipped into decline and was ultimately rejected in 1905 in Scotland in *Symington*[719] and in 1916 in England in *Yenidje*.[720] That rejection was subsequently blessed both by the Privy Council in *Loch* v. *John Blackwood Ltd.*[721] and by the

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House of Lords in *Ebrahimi*.[722] In the latter matter Lord Cross of Chelsea, after alluding to the "unfortunate influence" the *ejusdem generis* interpretation had for many years in the previous century had on the just and equitable winding-up provision, concluded:

> "In the present century ... petitions brought under it have generally related to disputes between rival shareholders or groups of shareholders in *private companies;* and in many cases the parties to the dispute have stood to one another in a *relationship analogous to that of partners in an unincorporated business*".[723]

Once the statutory just and equitable winding-up provision had shaken off the shackles of its association with the insolvency grounds - grounds that relate not to relations inter se but to relations with third parties — the operation of this provision was bound to be extended by the judiciary into new spheres. Here the obvious arena for expansion was the area already explored and charted by the law of partnership, to wit the sphere of members' inter se relations, or as it has been dubbed in this context by a Canadian commentator, the area of "intra-corporate conduct".[724] As has been observed in para. 5.2 above, partnership law had as early as Roman times focused on the inter se relations of members. Thus it is not surprising that company law, in its search for standards of intra-corporate conduct, should turn to and draw upon the "principles of equity developed in relation to partnerships "[725] over many centuries. In the English system such resort to partnership precepts is, moreover, further justified by the close affinity between incorporated partnerships and partnerships proper.

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All the quasi-partnership company decisions are concerned with aberrant conduct in the intra-corporate sphere. In *Loch*[726] the Privy Council shed some light on the approach a court should adopt in a consideration of the justice and equity of pronouncing an order for winding-up in terms of the statutory provision in question. "Such a consideration", Lord Shaw of Dunferline said delivering the judgment on behalf of the Privy Council, "in their Lordships' view, ought to proceed upon a sound induction of all the facts of the case, and should not exclude, but should include circumstances which bear upon the problem of continuing or stopping courses of conduct which substantially impair those rights and protections to which shareholders, both under statute and contract are entitled".[727] More recently the House of Lords was called upon to comment upon the operation of the said statutory provision in the sphere of members' inter se relations. It was urged upon the Law Lords that, assuming a petitioner is a shareholder and not a creditor, the words "just and equitable" must be confined to such circumstances as affect him in his capacity as shareholder. Their Lordships did not agree and held that there was no reason for preventing a petitioner "from relying upon any circumstances of justice or equity which affect him in his relations with the company, or, in a case such as the present, with other shareholders".[728]

In an earlier decision it was observed that the words "just and equitable" were of the widest significance, that they did not limit the jurisdiction of the court in any way and that it was always a question of fact, each case depending upon its own circumstances.[729] Yet, it has also been held that although the *ejusdem generis* rule had been abandoned, so that a wider view prevailed with regard to the ambit of the discretion

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entrusted to the court, such discretion must at all times be judicially exercised. In the words of Lord President Cooper Clyde: "It is not enough for the Court in exercising it to have, in the familiar phrase of a decree-arbitral, 'God and a good conscience' before its eyes; grounds must be given which can be examined and justified".[730] Because partnership norms have stood the test of time in the field of inter se relations they have proved to offer invaluable guidelines in this regard. It is not surprising, therefore, that courts have almost invariably turned to partnership precepts for guidance when faced with issues concerning aberrant intra-corporate conduct in petitions for the winding-up of solvent quasi-partnership companies. In all these matters the character and history of the company concerned, as mirrored in the inter se relations of its members, will be found to have played a prominent role. It is therefore only natural that courts should refer to such companies as quasi-partnership companies.

21.2.3. *THE QUASI-PARTNERSHIP COMPANY CASE LAW*

The body of case law in which winding-up on the statutory just and equitable ground has been granted with resort to partnership principles represents, as Lord Wilberforce after reviewing it correctly observed, "a sound and rational development of the law which should be endorsed".[731] His Lordship did of course state that he viewed the words "just and equitable" as the foundation of this whole development, and although one may disagree with his Lordship's emphasis in that regard one must agree with him that "if there is any respect in which some of the cases may be open to criticism, it is that the courts may sometimes have been too timorous in giving them full force".[732]

This line of cases stretches back to the turn of the century,

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when the incorporated partnership was first recognized by a Scots court in an application for the winding-up of an incorporated company under the statutory just and equitable winding-up provision. The Scottish decision was soon followed by courts in other jurisdictions where partnership did not enjoy legal personality. The time was ripe for this development. It was the period shortly after the highest court in England had confirmed the legality of the nominee device whereby the benefits of incorporation were placed within easy reach of partners proper, the *ejusdem generis* interpretation of the statutory just and equitable provision was in the process of being finally rejected, and the statutory private company was about to be born.

The major decisions mirroring the evolution in Scotland, England and South Africa of the incorporated partnership, under the flag of the quasi-partnership company, will now be considered. It will be observed that in virtually all these decisions a partnership relation of some kind underpins the formal company structure.

21.2.3.1. *SCOTLAND*

That the Scottish courts should have been the first in the English system to recognize the incorporated partnership is no coincidence. Scotland at the time still used the word "company" to refer both to an incorporated company and to a partnership. Scotland, moreover, had for many centuries recognized partnership proper as a distinct *persona* enjoying all the important incidents of legal personality. The differences between private companies, or partnerships proper, and statutorily incorporated companies were therefore insignificant at the time as they still are today. It is not surprising, then, that a Scottish court in 1905 handed down a decision

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in which a statutorily incorporated company was wound up in terms of the statutory just and equitable winding-up provision as if it were a private company, *i.e.* a partnership proper. That was in *Symington et al.* v. *Symingtons' Quarries, Ltd.*,[733] a matter that will now be considered. Of the other Scottish decisions in this field, only *Thomson* v. *Drysdale*[734] is relevant for present purposes.

21.2.3.1.1. *SYMINGTON*

Symingtons' Quarries, Ltd. was incorporated in 1899 some years before the statutory recognition of the private company. It was incorporated in terms of an agreement to continue a partnership carried on between two brothers, *H* and *D*. Its members were to be three brothers, *H*, *D* and *J*, and, to ensure compliance with the statutory requirements in force at the time, four nominee shareholders. The agreement was that apart from a small holding to *J* "to enable him to hold balance for voting", one-half of the company's shares would be issued to each of *D* and *H*, or their respective nominees. It was also agreed that all three brothers would be directors and that *H* would in addition be managing director. Some time after incorporation of the company the brothers quarrelled, *H* turned *"imperator"*[735] and usurped control. With the aid of the nominee shareholders *H* executed a *"coup d' état"*[736] that involved the passing of resolutions whereby the number of directors was reduced to one and appointed himself sole director. *J* and *D* successfully petitioned for a winding up order in terms of *Companies Act*, 1862,[737] *§§* 79(5). The court was unanimous in granting the order but each of the three Law Lords differed in their reasoning. The Lord President saw it simply as a matter of failure of *substratum* in that "the only company to which under the agreement the *private partnership* was bound

to/ .....

to make over the assets ... has been put out of possible existence by the *coup d' état.*[738] Lord Kinnear, on the other hand, appeared to rely on partnership principles treating the issue as one of deadlock, which could be relieved only by a winding-up order.[739] Of the three judgments Lord McLaren's was the best reasoned.

Lord McLaren clearly based his judgment on a very particular partnership ground: the impossibility of carrying on business. In this regard his Lordship referred to the practice of the court to decree a dissolution where there is a "small number of *partners* equally, or nearly equally divided, so that it is impossible that the business of the *Company* can be carried on ".[740] That Lord McLaren intended to refer to partnership proper in this regard and at the same time to distinguish between public-issue and private statutory companies is evident from his Lordship's further explanation that "[t]hat is a rule that would very seldom be applicable to a company under the Companies Act, — never certainly where the company appeals to the public for subscriptions to its shares ...."[741] Particularly significant in this regard is his Lordship's classification of the instant company as a partnership company. In the words of Lord McLaren: "But then this is not a company that is formed by appeal to the public. It is what, for want of a better name, I may call a domestic company. The only real *partners* are the three brothers ...."[742] Against this background Lord McLaren held:

> "[A]ll the reasons that apply to the dissolution of *private companies* [*i.e.* partnerships proper] on the grounds of *incompatibility* between the views or methods of the *partners* would be applicable in terms to the division amongst the shareholders of this Company ... this is a

case in which it would be just and equitable that this company should be wound up, and these *partners* allowed to take out their money and trade separately if they please".[743]

If Symingtons' Quarries Ltd had been anything but an incorporated partnership, a winding up order would clearly not have been granted on the facts before court.

21.2.3.1.2. *THOMSON*

Here the company concerned, R.T. Motor Services, Ltd., was once again clearly an incorporated partnership. It was incorporated as a private company by *T*, the petitioner and owner of a touring-agent business, and *D*, the respondent and owner of a garage and several touring buses. The object of this association was, as Lord President Clyde put it, "that these two businesses could be advantageously carried on in connection with each other under the protection of limited liability".[744] If the venture had not been incorporated it would undoubtedly have been a partnership proper. In keeping with the partnership character of the venture its issued share capital of £2 was contributed equally by *T* and by *D*, who were its sole directors as well. Subsequently a further 500 shares of £1 each were issued to *D* in payment of additional buses brought into the business by him. Although the preponderant voting power was thus vested in *D* the venture retained its partnership character. In the words of Lord President Clyde: "While the form of company administration was followed, the business was really being conducted rather as a kind of partnership between the two shareholders than as a limited company concern ...."[745]

Although the business prospered, *T* and *D* fell out and *D*, relying

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on his overwhelming voting power, usurped the whole of the powers of the company and practically possessed himself of everything it owned. Under these circumstances a winding-up order was granted to *T*. Although each of the four Law Lords handed down a separate opinion, they all founded the winding-up order upon the abuse by *D* of the overwhelming voting power he enjoyed as shareholder. Despite the corporate form, therefore, the partnership principle of unanimity seemed to be applicable, implying that the company was in fact an incorporated partnership. In some of the opinions this notion is more obvious than in others.

Both Lord President Clyde and Lord Cullen relied heavily on the fact that confidence had broken down. While the former referred to *Loch*[746] and *Baird*[747] and held that the use by *D* of his overwhelmingly preponderant voting power made the instant matter *a fortiori* of those cases, the latter more explicitly referred to partnership principles. "I think", Lord Cullen said in a clear reference to partnership, "he [*D*] has acted ..., to a degree which makes it impossible to expect that the petitioner should any longer have the necessary confidence in him as *co-adventurer* ".[748]

Although Lord Skerrington stressed that a court should not allow itself to be made an instrument for relieving a petitioner from the natural and lawful consequences of his contracts, his Lordship nevertheless felt that *D*, in view of his overwhelming voting advantage, could not ignore the interests of *T*. In these circumstances Lord Skerrington held that the abuse by *D* of his "position as a shareholder possessing a preponderating voting power" justified the remedy of winding-up.[749]

Lord Sands' opinion in this regard is equally explicit, although

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his Lordship did not trouble to refer to partnership by name. "I do not think", Lord Sands said clearly, acknowledging that the venture was concluded *intuitu personae* and not *intuitu pecuniae*, "that one can regard this case as if the measure of the petitioner's interest was 1 share against 1501".[750] This distinction received further emphasis when Lord Sands continued:

> "The history of the company is peculiar, and shows that the measure of his [*T's*] interest is of a different character; and therefore, while one might hesitate to order the winding-up of a company at the will of a person holding a negligible number of shares, I do not think that that condition applies here".[751]

From the history of R.T. Motor Services Ltd, it is clear that the company was an incorporated partnership. From Lord Sands' opinion, in particular, it is obvious that if the said company had been anything but an incorporated partnership the extreme winding-up remedy would not have been granted. None of the Law Lords, however, ventured to refer to the incorporated partnership by the name which was then already current in England, namely quasi-partnership company.[752]

21.2.3.2. *ENGLAND*

Although England, unlike Scotland, has never recognized partnership proper as a legal person in any sense, it did not take the English judiciary long, in winding up solvent companies in terms of the just and equitable winding-up provisions, to adopt an approach similar to the one adopted by Lord McLaren. The first English decision in this line is *In re Yenidje*

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Tobacco Co., Ltd.[753] It was in England too, that the name quasi-partnership company first came to be associated with the incorporated partnership in this context.

21.2.3.2.1. *YENIDJE*

From the history of the instant company, Yenidje Tobacco, Ltd. it is clear that the venture was an incorporated partnership. It was incorporated as a statutory private company by two tobacco merchants, *W* and *R*, for the purpose of amalgamating their separate trading interests. *W* and *R* were the only shareholders of the company and were intended to enjoy equal voting rights at all times. In keeping with the partnership nature of the venture the articles of association of the company provided that *W* and *R* were to be directors for as long as they lived and that there was to be no casting vote during that time. Not surprisingly, Warrington, L.J., repeatedly referred to *W* and *R* as "partners".[754]

Soon after incorporation of the "partnership" the "partners" fell out, *R* charging *W* with fraud in obtaining his consent to the amalgamation of the business. Because of continuous quarrelling thereafter, relations between *W* and *R* broke down completely, the two partners refusing to speak to one another; so that all communications between them had to be conducted through the secretary. Despite this, the company flourished and continued to make considerable profits. Under these circumstances a winding-up order was granted at the instance of *W* in terms of the statutory just and equitable winding-up provision and this order was upheld on appeal.

Although no explicit reference was made to Yenidje Tobacco Co., Ltd. being an incorporated partnership, partnership terminology was

freely/...

freely used by the court. Lord Cozens-Hardy, M.R., with whom Lord Pickford, L.J., concurred, and Lord Warrington, L.J., time and again referred to "private" or ordinary partnerships. This in the context clearly implied the existence of a *tertium quid*, an incorporated partnership proper. It is not strange therefore, that partnership precepts were extensively used in both judgments to justify the winding-up of the incorporated company.[755]

Lord Cozens-Hardy, M.R., in the opening lines of his speech identified the issues correctly. "I think it is right to consider", his Lordship said, "what is the precise position of a private company such as this and in what respects it can be fairly called a partnership in the guise of a private company".[756] It is for this reason that his Lordship posed the question of what the position would have been if the association had been a "private partnership, an ordinary partnership between two people having an equal share".[757] And, having established that in that event dissolution would have been decreed because of its being impossible for the partners to place the confidence in each other that each has a right to expect, Lord Cozens-Hardy held:

> "[B]ut this is not a partnership strictly, it is not a case in which it can be dissolved by action. But ought not precisely the same principles to apply to a case like this where in substance it is a partnership in the form or the guise of a private company? It is a private company, and there is no way to put an end to the state of things which now exists except by means of a compulsory order".[758]

Although his Lordship went on to find that the instant case was a classic example of deadlock, it is clear that he did

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not found the winding-up order on that ground. This was made clear by Lord Cozens-Hardy himself when he said, "but, whether it exists or not, I think that the circumstances are such that we ought to apply if necessary, the analogy of the partnership law and to say that this company is now in a state which could not have been contemplated by the parties when the company was formed and which ought to be terminated as soon as possible".[759] The state referred to by Lord Cozens-Hardy was the breakdown of mutual confidence. "It is contrary to the good faith and essence of the agreement between the parties", his Lordship stressed, "that the state of things ... should be allowed to continue".[760] The essence of the agreement referred to was of course the personal *intuitus personae* character of the inter se relation between *W* and *R*.

Lord Warrington, L.J., on the other hand, saw the matter as one of deadlock between partners. His Lordship said:

> "In substance ... these two people are really *partners*. It is true they are carrying on the business by means of the *machinery* of a limited company, but in *substance* they are *partners;* the litigation in *substance* is an action for dissolution of the *partnership*, and I think we should be unduly bound by matters of form if we treated either the relations between them as other than that of *partners* or the litigation as other than an action brought by one for the dissolution of the *partnership* against the other ..."[761]

Lord Warrington did not, however, lose sight of the fact that the venture was an incorporated partnership, for he acknowledged that, because "there is this [right-and-duty-bearing] entity called a company ... the machinery for winding-up had to be resorted to"[762] to obtain, as his Lordship put it, "what is equivalent to a dissolution of the partnership".[763] On this foundation a large body of case law has been built in juris-

dictions/ .....

dictions throughout the British Commonwealth. The term "quasi-partnership company" was however, introduced neither by Lord Cozens-Hardy nor by Lord Warrington. It was mooted in the next English decision, *Davis and Collet, Ltd.*[764] and has enjoyed popularity ever since, notwithstanding Lord Wilberforce's cautioning in *Ebrahimi* v. *Westbourne Galleries Ltd. et al,*[765] against the incorrect use of the term in question, namely quasi-partnership company.

21.2.3.2.2. *EBRAHIMI*

The issues involved in this matter were stated succinctly by counsel for the appellant, *E*, when in the opening lines of his address he said,"[t]his appeal raises for the first time in this House the question of an incorporated partnership: does one apply the partnership rule or the strict company rule of majority".[766]

The instant company, Westbourne Galleries, Ltd., was undoubtedly an incorporated partnership. It was incorporated to continue the partnership business which two dealers in Persian rugs, *E* and *N*, had started many years previously. *E* and *N* were the first and only directors of the company until *G*, the son of *N*, was appointed shortly after incorporation. At the same time *E* and *N*,who each held 500 shares in the company and were its sole shareholders, each transferred 100 shares to *G*. The business prospered and all profits were distributed in the form of directors' remuneration and not as dividends to shareholders.

Relations between *E*, on the one hand, and *G* and *N*, on the other, soured and the latter passed a resolution removing *E* as director, thereby effectively depriving him of any income from the

company/ .....

company. The said resolution was passed in accordance with all statutory requirements and the provisions of the company's articles of association and was therefore perfectly lawful. *E* petitioned for an order that *N* and *G* should purchase his shares or sell their shares to him on such terms as the court should think fit, alternatively for an order under the statutory just and equitable winding-up provision. The court granted a winding-up order. It was held that *N* and *G* had done *E* a wrong. For by excluding *E* from participation in the business, on which they had embarked on the basis that all should participate in its management, *N* and *G* had committed an abuse of power and a breach of the good faith which partners owed inter se. The Court of Appeal allowed an appeal by the respondents. Its point of departure was that the instant company was a quasi-partnership company. Nevertheless, it held that the exercise by a majority of their statutory and contractual powers of expulsion did not constitute a ground for winding up a company under the statutory just and equitable winding-up provision unless the petitioner could satisfy one of two requirements. One was to show that such power had not been exercised bona fide in the interests of the company. The other, alternative, requirement was to show that the grounds for exercising the power were such that no reasonable man could think that the removal was in the interests of the company. *E* successfully appealed to the House of Lords.

The partnership character of Westbourne Galleries, Ltd. did not escape Lord Wilberforce, who delivered the majority speech in the House of Lords in which Lord Pearson and Viscount Dilhorne concurred. Lord Wilberforce stated that it was clear that a potential basis for a winding-up order under the just and equitable clause existed and found:

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> "The appellant after a long association in partnership, during which he had an equal share in the management, joined in the formation of the company. The inference must be indisputable that he, and Mr Nazar, did so on the basis that the character of the association would, as a matter of *personal relation* and *good faith*, remain the same".[767]

What Lord Wilberforce is referring to here is obviously the inter se relation of mutual confidence and trust between *E* and *N* as partners. This clearly implies that the association was concluded *intuitu personae* and, therefore, was an incorporated partnership.

Although Lord Wilberforce stated that "[a] company, however small, however domestic, is a company not a partnership or even a quasi-partnership ...",[768] his Lordship did not hesitate to formulate the cardinal issue as being whether *E* had "established a case which, if he had remained in partnership with a term providing for expulsion, would have justified an order for dissolution?"[769] What further role partnership principles played in the majority judgment, that a winding-up was justified, soon became apparent. As point of departure Lord Wilberforce observed that a director who found himself either removed from office or not re-elected in terms of the contractual provisions contained in a company's articles of association would normally have to accept that situation unless he could prove fraud or mala fides. Yet, as Lord Wilberforce went on to point out, such a director might nevertheless find solace in the just and equitable provision "if he can point to, and prove, some special *underlying obligation* of his fellow member(s) in *good faith*, or *confidence*, that so long as the business continues he shall be entitled to management participation, an obligation so basic that, if

broken/.....

broken, the conclusion must be that the association must be dissolved".[770] Of even greater significance than the proposition itself is the justification Lord Wilberforce proffered in support of it. "And the principles on which he may do so", his Lordship acknowledged, "are those worked out by the courts in partnership cases where there has been exclusion from management ... even where under the partnership agreement there is power of expulsion ...."[771] Not surprisingly, the finding to which Lord Wilberforce ultimately came was that the respondents, *G* and *N*, were not entitled, in justice and equity, to make use of their legal powers of expulsion, and that in accordance with the principles of such cases as *Blisset*[772] the only just and equitable course was to dissolve the association. This conclusion again was clearly inspired by the precepts of partnership proper. Therefore his Lordship, in arriving at this ruling, found it necessary to quote the following passage from the judgment of Plowman, J., in the court *a quo*,[773]: "'... while no doubt the petitioner was lawfully removed, in the sense that he ceased in law to be a director, it does not follow that in removing him the respondents did not do him a wrong. In my judgment, they did do him a wrong, in the sense that it was an abuse of power and a breach of the good faith which partners owe to each other to exclude one of them from all participation in the business upon which they embarked on the basis that all should participate in its management.'"[774]

What is once again significant in this regard is that Lord Wilberforce relied heavily on the fact that *N* made it quite clear that he regarded *E* not as a partner but as a mere employee. "But", his Lordship stressed, "there was no possible doubt as to Mr. Ebrahimi's status throughout, so that Mr

Nazar's/.....

Nazar's refusal to recognize it amounted, in effect, to a repudiation of the [partnership] relationship".[775] In the final analysis, what stands out in the speech of Lord Wilberforce is that his Lordship found it necessary to refer on four occasions[776] to principles of equity developed in relation to partnership, and on four further occasions[777] to a personal interge relation involving mutual confidence. "One may ask", one commentator opined "why he [Lord Wilberforce] considers the most closely analogous situation in the field of partnerships to be so important having regard to his suggestion elsewhere that the concept of a quasi-partnership may be 'confusing' ...."[778] The answer to that question is obvious if regard is had to what Lord Wilberforce in actual fact said in this regard, namely that "[t]o refer, as so many of the cases do, to 'quasi-partnerships' or 'in substance partnerships' may be convenient but may also be confusing".[779] Moreover, to explain himself more fully his Lordship went on to say: "[i]t may be convenient because it is the law of partnership which has developed the conceptions of probity, good faith and mutual confidence, and the remedies where these are absent which become relevant once such factors [the elements of an incorporated partnership] as I have mentioned are found to exist...."[780] And finally: "[b]ut the expressions may be confusing if they obscure, or deny, the fact that the parties (possibly former partners) are now co-members in a company, who have accepted, in law, new obligations".[781] Those words of caution were directed at the use of that term in a situation in which the claims of third parties were in issue. That was clearly not the situation in the instant matter. "There is no suggestion", counsel for *E* had emphasized in his address to the House, "that the Companies Act does not apply, but the whole of the obligations of everybody in the company is

suffused/.....

suffused by the obligations of that [partnership] rule [of good faith]".[782] And again: "[i]f one starts with uberrimae fidei, natural justice is not far away".[783] On closer analysis it is clear that Lord Wilberforce did accept those submissions, gave effect to them and treated Westbourne Galleries, Ltd. as an incorporated partnership. What is important in this context is that the *ratio decidendi* of a decision is found not in what a court says it does, but in what it in fact does.[784] What is indisputable in the instant case is that the winding-up order was granted by Lord Wilberforce because of the particular character of the inter se relation of members and therefore of the company itself: in short, because the said relation was a personal, *intuitus personae* relation and, therefore, because the company was in fact an incorporated partnership.

The minority judgment delivered by Lord Cross of Chelsea was also based on the fact that Westbourne Galleries, Ltd. was an incorporated partnership. (Lord Salmon concurred in this minority opinion and also in the majority opinion of Lord Wilberforce.) "People do not become partners", his Lordship said, stressing the *intuitus personae* concept, "unless they have confidence in one another and it is of the essence of the relationship that mutual confidence is maintained".[785] Consequently "[i]f neither has any longer confidence in the other so that they cannot work together in the way originally contemplated then the relationship should be ended — unless, indeed, the party who wishes to end it, has been solely responsible for the situation which has arisen".[786] Against this background Lord Cross recognized Westbourne Galleries, Ltd. as an incorporated partnership and said:

"All that happened was that without one being more to

blame/.....

blame than the other the two could no longer work together in harmony. Had no company been formed Ebrahimi could have had the partnership wound up and though Nazar and his son were entitled in law to oust him from his directorship and deprive him of his income, they could only do so subject to Ebrahimi's right to obtain equitable relief in the form of a winding-up order ...."[787)]

In essence the corporate partners ceased to have confidence in one another and that justified the winding-up of the incorporated partnership Westbourne Galleries, Ltd.

21.2.3.3. SOUTH AFRICA

In this jurisdiction, too, with its hybrid system of Roman-Dutch law and brush of English law the practice of applying principles of equity developed in relation to partnership proper to incorporated companies has taken root. While the influences of *Yenidje*[788)] and of *Ebrahimi*[789)] are not unknown, however, decisions such as *Lawrence* v. *Lawrich Motors (Pty.) Ltd.*[790)] and *Moosa N.O.* v. *Mavjee Bhawan (Pty.) Ltd. et al.*,[791)] reflect the particular local approach. Here the focus is on the lateral inter se relation between members and, more particularly, the agreement from which it arises.

21.2.3.3.1. LAWRENCE

In this matter the respondent company, Lawrich Motors (Pty.) Ltd., is clearly an example of an incorporated partnership. The association came about after *L* had repeatedly requested *R*, the second respondent, to become his employee. When *R*

was/.....

was not agreeable to that, it was agreed that a new company would be formed in which *L* and *R* were to have equal shares. *R* was to run the company and *L* to finance it. The lease of the company's premises was originally secured by *L*, but *R* and *L* later became joint lessees. *L* and *R* were the company's sole shareholders and directors. The company's articles provided for unanimity between shareholders and between the directors in all the normal decisions of the company. Murray, J., viewed the company in the following light:

> "[E]ven in the absence of some specific agreement to that effect between the parties when forming the respondent company, they came together on the basis, substantially, of a partnership between them in the form of a limited liability company. No one else was invited to join as a shareholder ... It was not contemplated that any third party should be introduced to manage the company's affairs ...."[792)]

The learned judge considered it was irrelevant that *L* might have left the actual management of the business in the hands of *R*. "The applicant", Murray, J., held referring to *L*,"as chairman, as a director, and as a shareholder holding half the issued capital had the full right to interfere in such management even if in fact he did not exercise the same, and could insist on the necessity of his concurrence in every action of the company".[793)] The significance of this is that participation in management is not in South Africa treated as a prerequisite to incorporated partnership status.

What gave rise to the application for winding-up at the instance of *L* was two acts of adultery committed by

R/ .....

R with the wife of *L*. This resulted in *L* warning *R* not to set foot on the premises of the company again and threatening that unless the latter left town he would be shot. It was common cause that if Lawrich Motors (Pty) Ltd. were a "partnership in its ordinary sense" the commission of adultery by one partner with the wife of the other partner would justify the latter claiming an immediate dissolution of the partnership.[794] *R*, however, contended that Lawrich Motors (Pty.) Ltd. was an incorporated company, and not an unincorporated partnership, and that in any event its business was entirely solvent and it should not be placed in liquidation. In opposing the application *R* relied on the decision in *Loch*[795]. Thus it was submitted that to warrant a winding-up order, the lack of confidence must be grounded on the directors' conduct not in regard to their private life or affairs but in regard to the company's business, and that there must be a wrong to the company, not merely to a shareholder as in the present case. It was also submitted that, in any event, the misconduct of *R*, if any, related only to his private life. It was further contended that, apart from the fact that *L* himself was a man of questionable morals, no deadlock existed inasmuch as another manager could be appointed or either of the parties could buy the other out, without necessarily involving the dissolution of the company.

From the judgment it is clear that what mattered, in the view of the court, was solely the lateral associative relation between *R* and *L*, and not the vertical relation between *R* and the company. "It is not a question", Murray, J., exposing the very crux of the matter emphasized, "of the applicant's own moral standards in comparison with that of Richards but the fact that Richards' misconduct was committed with the applicant's wife which is important in determining whether there was *such a tension or resentment between the partners, caused by the adultery, as*

would/.....

would render continued co-operation impossible".[796] The contention that winding-up could be avoided by the appointment of a third party, as manager, or by either *R* or *L* buying the other out, similarly did not find favour. "Assuming the basis of the parties' original association to be as indicated", Murray, J., held, "viz. substantially a partnership, the impossibility of a continuation thereof can only be properly met by winding up the company in the guise whereof they were partners ".[797]

The main question, as viewed by Murray, J., was therefore whether the conduct of *R* had been such as to render future co-operation between himself and *L* impossible. This focused the enquiry on the state of the lateral inter se relation between them. For as Murray, J., was at pains to stress, it was not the general character or conduct of *R* that was at issue, but the misconduct on the part of *R* with the wife of *L*, his co-director and co-shareholder, who stood to him "in the relation substantially as a partner ".[798] In these circumstances Murray, J., was prepared to grant a winding-up order not only because it became impossible that any harmony could be expected to prevail between *R* and *L* but, in particular, because "a wrong had been done to applicant which prevented him from reposing the necessary confidence in Richards ...."[799] This conclusion was without question predicated on the principles of equity developed in relation to partnership proper.[800] Had Lawrich Motors (Pty.) Ltd. been anything but an incorporated partnership, a winding-up order would clearly not have been granted.

21.2.3.3.2. *MOOSA*

Here the respondent company, Mavjee Bhawan (Pty.) Ltd., was

once/ .....

once again an incorporated (family) partnership, albeit in the mould of the classical consortium of co-heirs or *ercto non cito*.[801] The instant company was a private company operating essentially as a property holding and letting company. It had five shareholders, four of whom were the heirs of the founding father of the business. The fifth shareholder was the son and nominee of the second respondent, *M*, who was the largest shareholder in the company.

At all relevant times *M* was the sole director and chairman of the company. With the consent of the other heirs he assumed the management of the company after the founder's death and had retained it ever since. As it turned out, *M* abused the confidence reposed in him by the other heirs. When confidence broke down, one of the heirs and shareholders brought an application for the company to be wound up in terms of the statutory just and equitable winding-up provision. One of the major complaints levelled against *M* was that he had been conducting the affairs of the company mainly for his and his son's benefit and not for the benefit of the shareholders' as a whole.

Trollip, J., before whom the matter served on the return day of a provisional order, immediately identified the company as a solvent company and "obviously" of the kind "which is in the nature of the partnership".[802] The learned judge noted that the applicant had relied on "two distinct principles" which he found "useful as guides ... for the exercise" of a court's discretion in terms of the statutory just and equitable winding-up provision.[803]

The first of these principles operates to justify a winding-up when there is "'justifiable lack of confidence in the conduct

and/ .....

and management of the company's affairs ... grounded on conduct of the directors, not in regard to their private life or affairs, but in regard to the company's business'".[804] The underlying relationship is obviously a vertical one: a relation between the director and the company as a statutory right and duty-bearing unit. This explains why the aberrant conduct of the director is relevant only if it relates to the company's business. "[T]hat lack of confidence is not justifiable", Trollip, J., emphasized, "if it springs merely from 'dissatisfaction at being outvoted on the business affairs, or on what is called the domestic policy of the company', but is justifiable if in addition there is a lack of probity in *the directors' conduct of those affairs*".[805]

The second of the said two principles, in the words of Trollip, J.,:

> "[I]s founded on the analogy of partnership and is strictly confined to those small domestic companies, in which, because of some *arrangement, express, tacit* or *implied*, there exists between the members in regard to the company's affairs a *particular relationship of confidence and trust* similar to that *existing between partners in regard to the partnership business*. Usually that relationship is such that it requires the members to act reasonably and honestly towards one another and with friendly co-operation in running the company's affairs".[806]

In the nature of things, the underlying relationship in such companies will be a lateral, associative relation steeped in mutual confidence and good faith. As in partnership, that character constitutes the very essence of the relationship.

This/ .....

This was acknowledged by Trollip, J., when he held:

> "If by conduct which is either wrongful or not as contemplated by the arrangement, one or more of the members destroys that relationship, the other member or members are entitled to claim that it is just and equitable that the company should be wound up, in the same way as, if they were partners, they could claim dissolution of the partnership ".[807]

Why this second principle (sometimes incorrectly categorized as the "deadlock" principle) operates only in respect of incorporated partnerships, and not public-issue companies or private companies common, was soon explained: the answer lies in the personal character of the said relation. "'It is the destruction of that personal relationship'", Trollip, J., said, echoing McPherson, "'and not the absence of some compulsive means of terminating the deadlock, which provides the criterion for the intervention of the Court ....'"[808] Thus a winding-up order in terms of this principle is dependent not on "proof of deadlock" but on "proof that the relations between the parties have deteriorated to a point where all hope of future co-operation between them is precluded ...."[809] It is for this reason that the existence of a preponderating or casting vote, by which deadlock can be prevented, is in this context irrelevant in an incorporated partnership but not in a public-issue company or private company common. This explains why, in the case of the latter types, the existence of an effective means of solving the deadlock is fatal to the success of an application for winding-up, whereas in the case of the former type it is irrelevant. This in turn explains why the second of the said principles, whereby a winding-up order is justified by irretrievable breakdown of confidence, is operative only in the context of the incorporated partnership.

Although/ .....

Although the said two principles are distinct they may, according to Trollip, J., be used either alternatively or, as in the instant matter, conjointly.[810] On the facts Trollip, J., found that in terms of the first principle the lack of probity displayed by *M* in managing the company's affairs justified a winding-up order. In this context two matters stood out. The first was the exercise by *M* of the company's borrowing and lending powers for the sole benefit of himself and his son.[811] The second related to his fraudulent conduct[812] with regard to the company's major asset, the immovable property. Such conduct, Trollip, J., held, "justifiably ended the confidence ... in his [*M*'s] management of the company's affairs, furnishing good cause for a winding-up order ...."[813]

Moreover, the second principle was found by Trollip, J., to be applicable as well, either additionally or alternatively. The instant lateral or associative inter se relation, however, appears to have been of the type found in the typical consortium of coheirs. In the instant matter the lateral inter se relation arose after the death of the testator and founding father of the business, from whom the present shareholders, his sons and daughters, had inherited their shares in the company. The consortium apparently came about when *M*, as the largest of the shareholders, with their consent as coheirs assumed control of the company.[814] "[B]y *arrangement, explicit* or *implicit*", as that event was described by Trollip, J., "a *personal relationship* of *trust* and *confidence between all the members was created*, in which it was contemplated that he [*M*] would, *vis-à-vis* the others, manage the company reasonably, fairly and honestly and that, whenever necessary, for example at meetings, they would

cordially/ .....

cordially co-operate in running the company's affairs".[815] But as the learned judge, pointing to a number of incidents, went on to find, "that fundamental personal relationship ... has been irreparably destroyed, thereby providing a good cause for winding-up".[816] The first of the incidents identified by Trollip in this regard was "interminable litigation" between *M* and his sister — a fellow-shareholder — stretching over a decade and a half, which had "engendered acute enmity and animosity between them in regard to the company's affairs ".[817] The second was brother and sister being seriously at loggerheads resulting in the former refusing the latter information about her shareholding and her entitlement in a rights issue. The third was the misbehaviour of *M* at a particular meeting of shareholders which caused Trollip, J., to remark that "it is now futile for them to meet together in general meetings"[818] and to conclude that "[a]ll their trust and confidence in him [*M*] had ended, and there is no hope of their co-operating with him in the company's affairs in the future which, although it was not contemplated she would directly participate in as director, it was contemplated, and on occasions urged in letters by second respondent [*M*], she should participate in as a shareholder ".[819] The last straw, in the view of Trollip, J., was the inability of the brother and sister to settle their differences about a "simple company" amicably despite suggestions from the bench and efforts of their counsel in that regard.[820] Again it is clear that had the respondent company been a public-issue company or a private company common, the winding-up order would not have been granted; for it is particularly noteworthy that Trollip, J., took care to distinguish between a "public company", on the one hand, and between "domestic or 'partnership' companies"[821] on the

other/ .....

other. The winding-up order was granted in the instant matter only because the company fell into the latter category.

21.2.4. *PROFILE OF THE INCORPORATED PARTNERSHIP*

A feature common to all the companies featured in the above review of cases is the partnership proper characteristics displayed by each of the companies so encountered. And because it seems certain that a winding-up order would not have been granted in any of these decisions had the said partnership features not been present, it is correct to treat these companies as a type or class apart.

The obvious term to denote this company type appears to be *incorporated partnership*: a partnership, in other words, which has been incorporated in terms of an enabling *Companies Act* to attain corporate status and its attendant benefits. To date the term "incorporated partnership" has not, however, achieved the recognition in the English system that is due to it. In the English system the term first used in this context is "domestic company".[822] Coined before the introduction of the statutory private company, the term was obviously intended to denote that the company in question was more in the nature of a partnership than of a public-issue company. As such the term "domestic company" was neither accurate nor, for that matter, particularly descriptive. In fact, the first company to be thus referred to, namely Symingtons' Quarries, Ltd., was an incorporated family partnership — a partnership incorporated by two brothers who sought to obtain the benefits of incorporation. Another, somewhat similar, term that is sometimes used in this context is "family company".[823]

But/ .....

But the term which came to be the most consistently used in this field is "quasi-partnership company ".[824] Prior to the introduction of a partnership statute in England in 1890, the term "quasi-partnership company" was employed in partnership law to denote persons who were held liable *vis-à-vis* third parties as partners although in law they were inter se not partners at all.[825] After the rejection of the *ejusdem generis* interpretation of the statutory just and equitable winding-up provision, the term "quasi-partnership" came to be used in the completely opposite context. It then served to refer to the inter se relations of members of incorporated partnerships in proceedings in which the rights and claims of third parties were not at issue or affected.[826] In that the inter se relations in all these situations were of a personal character, suffused with mutual confidence and good faith, they resembled the inter se relations of partners proper. Not surprisingly, a company of this nature came to be referred to as a "quasi-partnership company" or as being "in substance a partnership ". Clearly the functionally more correct and descriptive term for this type of company is "incorporated partnership". Compared to the term "quasi-partnership company" the term "incorporated partnership" is even less likely to give rise to confusion. It accurately conveys the idea of a partnership in the guise of a limited liability company. The basic status, namely that of corporateness in terms of *Companies Act*, 1948,[827] *ss* 13(2), is conveyed by the first word in the term "incorporated partnership". At the same time the notion of being partners inter se within the corporate framework is permitted and recognized by the last word in that term. Although this term has not yet found favour with the judiciary in the English system,

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it was used once by a New Zealand court[828] many years ago. Recently that very term was employed by counsel in the House of Lords.[829] Since then it has also cropped up in legal writing.[830] What is encouraging is that the term "incorporated partnership" has been mentioned as the name for a new form of statutory private company.[831] What is being proposed in this regard is the creation of a "new form of incorporated business organization drawing on partnership law as regards internal regulation ...."[832] This makes particularly good sense: partnership law has, after all, focused on inter se relations all along.

Practical problems are bound to be encountered. "It is easy to recognize a partnership company", counsel in *Ebrahimi* correctly submitted, "when one sees it, but difficult to formulate a test".[833] This problem is, however, not peculiar to company law. "Probably no legal term", a renowned American authority once remarked in a different context, "can be defined with perfect accuracy so as to include all that is intended to be included and to exclude everything else...."[834] At best one can endeavour "to give such a description of a legal concept that others will know in a general way what one is talking about".[835] This is particularly true of associations in general and incorporated partnerships in particular. Lawyers confronted with the task of formulating a definition for partnership have for many centuries grappled with this very problem. It has also been observed how both the legislature and lawyers have struggled to define the concept "company".[836] If, therefore, it is extremely difficult — perhaps even impossible — to define concepts such as partnership and incorporated company, it is *a fortiori* as difficult or impossible, if not more so, to define a concept such as incorporated partnership. The former concepts have, after all, been known for a fairly long time; the latter

is/ .....

is of more recent origin. How difficult it is to define this latter concept is clearly mirrored in the various hesitant, but nevertheless commendable, attempts by the judiciary to describe this type of association. Needless to say, this has always happened in the context of the statutory just and equitable winding-up provision. The first, very tentative, endeavour in this regard is of course found in the judgment of Lord McLaren in the Scottish matter, *Symington*.[837] Years later an Australian judge took this concept a step further when he stressed the character of the inter se relation of members of such a company. This was in the matter of *Wondoflex Textiles Pty. Ltd.*[838] Here Mr. Justice Smith referred to the "rule" whereby "a private company which is in substance a partnership"[839] might be wound up under the statutory just and equitable winding-up provision. The learned judge agreed with Lord McLaren that this "rule" could ordinarily have no application where the company's capital had been obtained by public subscription but hastened to add that the *mere fact* that the company was a private company did not necessarily render that "principle" applicable.[840] Against the background of this clear distinction between the public-issue company, on the one hand, and the private company common, on the other, it is easy to recognize a third type: a hybrid between corporation and partnership — the incorporated partnership. Mr. Justice Smith identified it in these terms:

> "But this principle [of applying partnership law by analogy] will, ... ordinarily be applicable where the members of the company are a *relatively small number of persons who have become associated as members in pursuance of an agreement or arrangement involving the creation of a personal relationship between them*, and where, in addition, there are restrictions upon the

transfer/ .....

transfer of shares which, as in the case of a partnership, prevent a member from extricating his interest upon just terms without a winding-up ...."[841]

The learned judge concluded this description of the incorporated partnership by noting that, for the partnership analogy to apply, it was in his opinion not essential that there should be any agreement or understanding that all the associates should be entitled to participate in the conduct of the company's business.[842] It is interesting to observe that this latter approach was in fact adopted in both the South African decisions reviewed above. There again the focus was very much on the lateral inter se relation.

More recently the incorporated partnership concept twice came up for consideration in England. "I doubt", Mr. Justice Brightman correctly acknowledged in the first of the two matters, *Leadenhall*,[843] "if it is possible to devise a precise test for determining whether a company is a quasi-partnership for the purposes of a petition under section 222(f)."[844] The learned judge then said:

"There does not seem to be any exact pattern into which the decided cases will fit. In general terms — and it seems to me that a test can only be expressed in general terms — I think that a company can *properly be described as a quasi-partnership if the members intend to participate in the business of the company in just the same way as they would have done had they been partners under articles of partnership similar to the articles of the company* (so far as appropriate to a partnership) so that the *existence* of the *company* is *mere form (as between the partners) and not substance.* Whether this intention

so/ .....

so exists is a question of fact to be deduced from all the circumstances ".[845]

The judge went on to say that although equality of interests was a factor to be considered, it was not by itself decisive. It was similarly stated that although withdrawal of profits as remuneration, rather than by way of dividend, was a factor to be taken into account, that factor too, was not *per se* decisive. Mr. Justice Brightman did, however, at the same time feel that "equal participation in the day's work" was not only an important but perhaps even a decisive factor.[846] Nevertheless, he conceded that there might well be other relevant factors in particular cases. Against this background the House of Lords was called upon to decide whether in effect Westbourne Galleries Ltd was an incorporated partnership and what the test in that regard should be. Counsel for the appellant, clearly following Brightman, J., correctly submitted that the nub was whether a particular company was really a "working partnership in the guise of the company".[847] The stand of the House of Lords, as expressed by Lord Wilberforce, appears to be a compromise between the respective formulations of Mr. Justice Smith and Mr. Justice Brightman.

Lord Wilberforce, like Mr. Justice Smith, did not under-estimate the formidability of this task. "It would be impossible, and wholly undesirable", his Lordship acknowledged, "to define the circumstances in which these considerations may arise".[848] Considerations in this context referred to "considerations ... of a *personal character* arising between one individual and another, which may make it unjust, or inequitable, to insist on legal rights, or to exercise them in a particular way",[849] that is, to principles of equity developed in relation to

partnership/.....

partnership proper, as Lord Wilberforce repeatedly referred to them. Like Mr. Justice Smith, Lord Wilberforce did not think that the fact that a company was a small one, or a statutory private company, was enough. For as Lord Wilberforce proceeded to emphasize, there were very many of those small, statutory private companies where the "association was a *purely commercial* one" of which it could be safely said that the "basis of association" was adequately and exhaustively laid down in the formal constitution. In effect his Lordship appears here to have distinguished between associations concluded *intuitu pecuniae* and associations concluded *intuitu personae*, that is between associations based on an impersonal, arm's length, lateral inter se relation, and associations based on a close, intimate and personal, lateral relation of mutual confidence and trust. That this is in fact the case is borne out by Lord Wilberforce himself, for as his Lordship explained:

> "The superimposition of equitable considerations [*in casu*, the principles of equity developed in relation to partnership] requires something more which typically may include one, or probably more, of the following elements:
>
> (i) an *association formed* or *continued* on the basis of a *personal relationship*, involving *mutual confidence* — this element will often be found where a pre-existing partnership has been converted into a limited company;
>
> (ii) an agreement, or understanding, that all or some (for there may be 'sleeping' members), of the shareholders shall participate in the conduct of the business;
>
> (iii) restriction upon the transfer of the members' interest in the company — so that if *confidence* is lost

or/ .....

or one member is removed from management, he cannot take out his stake and go elsewhere".[850]

Whether Lord Wilberforce is prepared to acknowledge so or not, he has in listing the above typical elements — a shortlist which did not pretend to be exhaustive[851] — in fact identified the profile of an incorporated partnership. (And, as has been pointed out previously, what is legally relevant is not what a court *says* it does, but what it in fact *does*.) The so-called typical elements are in fact but the characteristic features of the incorporated partnership.

These features were identified twenty-two years previously, albeit in a slightly different presentation — by Mr. Justice Smith in the Australian matter, *Wondoflex*.[852] In the Massachusetts matter, *Donahue*[853] two years later, Mr. Justice Tauro, independently of Lord Wilberforce, found the close corporation (in the sense of an incorporated partnership) to be typified by essentially the same characteristic features as those listed by Lord Wilberforce in the House of Lords. When Schmitthoff exclaimed that the English courts had at last discovered that the private company (in the sense of an incorporated partnership) was a business organization *sui generis* and not merely a variety of a general conception of a limited company, and that the discovery of the true character of the private company (in the sense of the incorporated partnership) had been completed,[854] he undoubtedly had the lines from the speech of Lord Wilberforce, quoted above, in mind.

21.3./ .....

21.3. *THE INCORPORATED PARTNERSHIP AND THE MORE APPROPRIATE REMEDIES OF FIDUCIARY RESTRAINT*

21.3.1. *INTRODUCTION*

In this paragraph the enquiry will be to establish to what extent the separate company type recognized by the judiciary under the just and equitable winding-up provision, as the quasi-partnership company, *i.e.*, the incorporated partnership, is also recognized as such where the nature of the aberrant conduct does not warrant the extreme remedy, winding-up. In particular, the enquiry will be to establish whether principles of equity, developed in relation to partnership proper, have had a parallel influence in this sphere and have inspired the imposition of fiduciary duties on members of the incorporated partnership. Here, as before, the approach will be to establish the character of the company in question and the nature of the inter se relation of its members.

21.3.2. *THE CASE LAW*

The decisions about to be considered are, unlike the statutory just and equitable winding-up line of cases, few in number, not united under a single banner, such as the statutory just and equitable winding-up provision and therefore not recognized as a coherent body of case law. These decisions do, however, cover a broad spectrum of situations and complement the just and equitable line of decisions. It will be found that all the cases in question are predicated on the existence of the incorporated partnership being a separate type. In some of these decisions the less drastic and, in given circumstances, more appropriate, remedies of fiduciary restraint and reparation have in fact been recognized as realistic alternatives to the

extreme/ .....

extreme and final remedy of corporate dissolution. As such, these decisions also "represent", in the phrase of Lord Wilberforce, "a sound and rational development of the law which should be endorsed".[854a)]

21.3.2.1. *SCOTLAND*

Principles of equity, developed in relation to partnership proper, have been applied in Scotland to members of an incorporated partnership for purposes not of winding-up the statutorily created right-and-duty-bearing unit, but of maintaining it. But this has to date occurred on only two occasions. These were respectively in *Harris* v. *A. Harris Ltd. et al.*[855)] and in *Scottish Co-operative Wholesale Society Ltd.* v. *Meyer*.[856)] The former concerns the abuse of superior voting power, the latter the unconscionable withholding of business opportunities from an association with the object of "starving" an associate into surrender.

21.3.2.1.1. *HARRIS*

Here the respondent company was clearly an incorporated partnership of some sort. It was incorporated as a private company with the aim of taking over a family partnership business doing business as cigar importers, cigarette manufacturers and tobacconists. The business was run by a father *A* and his three sons, *E*, *J* and *W*. In terms of the company's articles of association, membership was restricted to the founding father *A* and members of his family. The right to hold office as director was further restricted to *A*, *E*, *J* and *W*. After the death of *A*, two of his shareholders' sons, *E* and *W*, against the wishes of the third, *J*, persuaded other members of the family to have their shares transferred and registered in the names of

E/ .....

E and *W*. With their superior voting power thus acquired, the said two brothers appointed themselves life-long managing directors of the company and passed a resolution which had the effect of substantially increasing what they themselves (*E* and *W*) were to receive from the company as remuneration in one form or another.[857] Because of this increased charge against the profits of the company, no dividends could be paid to other shareholders. In the result, *J*, claiming that the said resolution was invalid and that it was passed from an oblique motive in fraud of his interests and not in the bona fide interest of the company, brought an action to have it set aside.

The action failed. Two of the three judges were of the opinion that majority rule, which applied to public-issue and other companies, was applicable. The third, Lord Murray thought that the relevant question here was not whether *J* had established that *E* and *W* "were guilty of fraud, in the common law sense". Instead his Lordship adopted "as the true test, a higher standard of conduct", namely whether *E* and *W* were or were not "in breach of a fiduciary duty to the Company and its constituent shareholders".[858] Lord Murray too, however, dismissed the action in the absence of satisfactory proof that such fiduciary duty had been breached.

Lord Murray treated the instant company as an incorporated partnership and clearly referring to principles of equity developed, in relation to partnership, both in Roman and English Law, and to the lateral relation between *E*, *W* and *J*, said:

"Now, it cannot be disputed that the defenders, not

merely/ .....

merely as directors or managers, but also as shareholders, were here under a fiduciary duty to the Company at large, and therefore to their fellow shareholders as a body. This is elementary in contracts of partnership. *'In societatis contractibus fides [bona] exuberet'*; act in the utmost good faith. 'For a majority of partners to say: We do not care what another partner may say, we, being the majority, will do what we please, is ... what this Court [of Equity] will not allow'.... And what is true of partners in a contract of copartnery is equally true of directors of or shareholders in an incorporated company".[859]

A clear distinction between vertical and lateral fiduciary relations is evident in the above passage. As shareholders *E*, *W* and *J* stood in a lateral fiduciary relation giving rise to mutual confidence and good faith. Because of such mutual inter se confidence and good faith, it was not permissible for *E* and *W*, in exercising their rights as shareholders, to act unscrupulously *vis-à-vis J* or for that matter, the right-and-duty-bearing unit spawned from their lateral, inter se relation. As managers and directors *E* and *W* owed fiduciary duties to the right-and-duty-bearing unit arising from the vertical fiduciary relation that existed in that regard. If *E* and *W* had, in exercising their voting rights as shareholders, acted unconscionably, they would have breached their fiduciary duty in that regard *vis-à-vis* their fellow shareholder *J*. On the other hand, if *E* and *W*, acting as directors, had benefited themselves at the expense of the company, they would have been in breach of their vertical fiduciary duties. While Lord Murray did in effect refer to these last-mentioned duties as well, it is clear that he was looking primarily at the first-mentioned.

Against/ .....

Against this background, Lord Murray rejected the contention advanced on behalf of *E* and *W*, namely that to warrant judicial intervention, actual fraud would have to be established. Instead his Lordship adopted the stricter test "whether the conduct ... evidences such a breach of duty as warrants the intervention of a Court of Equity".[860] This test, as has been observed above, turned out to be the test developed in regard to partners proper. However, on the facts, Lord Murray found that *J* had failed to establish that *W* and *E* had breached their fiduciary duties, and dismissed the action.

While it is not possible to judge whether Lord Murray was correct on the facts, his approach on the law cannot be faulted and it must be regretted that it has not been followed or even cited in subsequent decisions.

21.3.2.1.2. SCOTTISH CO-OP WHOLESALE SOC.

In this matter the company concerned, the Scottish Textile and Manufacturing Co., Ltd. ("*S.T.M.*") was undoubtedly an incorporated partnership. It was incorporated shortly after the Second World War as a private company by the respondents, *M* and *L* as well as *S*, the appellant company, with a view to manufacturing rayon cloth in Scotland. The partnership nature of the undertaking is clear from the circumstances which brought the three parties together in a limited liability private company. *S* owned a weaving mill in Scotland but had no experience in the manufacture of rayon cloth. *M* and *L*, former German nationals, had such experience and, in addition, extensive connexions in the particular field on the Continent. *M* and *L* not only provided the necessary formulae, knowledge and experience to manufacture the rayon cloth but also obtained

the/ .....

the necessary licences for the purchase of the raw material and the manufacture of the end product, the rayon cloth, which at the time was controlled. As far as the actual operation of the undertaking was concerned, *L* and *M* obtained the necessary supply of yarn. *S* paid for it, processed and wove it into a cloth at his own mill and then sold the end product to *S.T.M.* which, in turn, marketed it. *L* and *M*, on the one hand, and *S*, on the other, were not equal partners in *S.T.M.* The board of *S.T.M.* consisted of *M* and *L* and three nominees of *S*. *M* and *L* held 3900 shares in the share capital of *S.T.M.* and *S* the remaining 4000. In legal terms, *S.T.M.* was a subsidiary of *S*. The venture prospered but prosperity bred discord. Hostility, on the part of *S* and its board of nominees, towards *M* and *L* set in when, in 1951, *S* proposed to increase its holding in *S.T.M.* by acquiring some or all of the shares held by *M* and *L* at par instead of at current values, as *M* and *L* required. In the heat of the moment the board of nominees of *S* threatened to liquidate *S.T.M.*, or to increase its capital to £25000, the object clearly being to intimidate *M* and *L* into surrender. On obtaining an auditor's valuation which set the value of the share at least £6 a piece, *S* dropped its proposal of acquiring the shares held by *L* and *M*. Instead *S*, through its nominee directors, directed its efforts towards converting *S.T.M.* into a subsidiary branch of itself. This *S* set out to achieve by so conducting the affairs of *S.T.M.* as "to squeeze out"[861] *M* and *L* and by "starving them into surrender",[862] so as to induce and compel them to part with their shares at a low price. When governmental control over rayon production was withdrawn, the reason for the production of rayon at the mill of *S* under the licence of *S.T.M.*, fell away. This therefore made *S.T.M.* redundant from the point of view of *S*. As a result of the purpose for which *S.T.M.* was incorporated falling

away/ .....

away, the nominee directors of *S* adopted a policy of passive support of *S* by inactivity and by allowing the trading activities of *S.T.M.* to decline or to disappear. Within three months *S* established a new converting department for the finishing and dyeing of rayon fabrics at its own mill, and refused to accept orders from *S.T.M.* Within another six months the latter was informed that rayon cloth would in future be manufactured for it on a commission basis and at fixed, prohibitive prices whereby its business was brought to a virtual standstill. Another month later the appointment of *L* and *M* as directors was terminated and they were informed shortly thereafter that no business would be done for *S.T.M.* at the mill of *S* on any basis. Thus the shares of *L* and *M* in *S.T.M.* were rendered virtually worthless. In effect *S* had terminated the partnership between itself and *L* and *M*. The conduct of *S* clearly amounted to *mala fide* and *intempestiva* renunciation of the partnership between itself and *L* and *M*. In terms of the Roman and Civil law principles discussed above, *L* and *M* would have been entitled to claim *inter alia* an accounting of profits from *S* if they had been ordinary partners. The fact that *S.T.M.* was an incorporated partnership should of course in principle not have affected the rights of *L* and *M* in that regard.

It was common cause that *S.T.M.* could be wound up under the statutory just and equitable winding-up provision. However, possibly because of the fact that *S* had caused the business of *S.T.M.* to run down completely, *L* and *M* did not institute proceedings in terms of that provision. It is unlikely that they would have recovered anything in that fashion. Instead *L* and *M* wisely opted to commence proceedings under the alternative statutory remedy provided by *Companies Act*,

1948/ .....

1948,[863] §210. The relief claimed was that *S* be ordered to purchase the shares held by *L* and *M* in *S.T.M.* at £6, Os. 11d. because *S* had conducted the affairs of *S.T.M.* in a manner which was oppressive to *M* and *L*. In these proceedings the focus was on the relation between *S* and *S.T.M.* and not on the relation between *S*, *M* and *L*. The court was not asked to treat *S.T.M.* as an incorporated partnership and did not find it necessary to do so. This is to be regretted for it is possible that the court would have done so. Lord President Cooper in fact said that the particular statutory provision "warrants the Court in looking at the business realities of a situation and does not confine them to a narrow legalistic view ".[864] As it turned out, his Lordship saw the matter only from the point of view of a holding company and subsidiary company relationship. "The truth is that ", the Lord President said "whenever a subsidiary is formed as in this case with an independent minority of shareholders, the parent company must, if it is engaged in the same class of business, accept as a result of having formed such a subsidiary an obligation so to conduct what are in a sense its own affairs as to deal fairly with its subsidiary ".[865]

S was ordered to buy the said shares at £3 15s a share, but appealed to the House of Lords. All the Law Lords were agreed that the conduct of *S* was oppressive within the meaning of the statutory provision in question and dismissed the appeal.

Lord Keith identified himself with the observations of Lord President Cooper concerning *S.T.M.* being a subsidiary of *S* but at the same time focused attention on the lateral inter se relation between *S*, *M* and *L*. In essence

his/ .....

his Lordship treated *S.T.M.* as an incorporated partnership. The significance of this is that in deciding whether the conduct of *S* had been oppressive it was now possible to have regard to partnership precepts. Lord Keith's point of departure was that if *S* could be regarded as an organization independent of *S.T.M.*, no legal objection could be taken to the actions and policy of *S*. This, as was pointed out in the Court *a quo*, was however not the situation. In the words of Lord Keith:

> "In law, the society and the company were, it is true, separate legal entities. But they were in the relation of parent and subsidiary companies, the company [*S.T.M.*] being formed to run a business for the society[*S*] which the society could not at the outset have done for itself unless it could have persuaded the respondents [*L* and *M*] to become servants of the society. This the respondents were not prepared to do. The company through the knowledge, the experience, the connexions, the business ability and the energies of the respondents, had built up a valuable goodwill in which the society shared and which there is no reason to think would not have been maintained, if not increased, with the co-operation of the society".[866]

The above reasoning led Lord Keith to the following conclusion:

> "The company [*S.T.M.*] was in substance, though not in law, a partnership consisting of the society[*S*] and the respondents [*L* and *M*]. Whatever may be the other different legal consequences following on one or other of these forms of combination one result, in my opinion,

follows/....

follows in the present case from the method adopted, which is common to partners, that there should be the utmost good faith between the constituent members. In partnership the position is clear .... 'A partner cannot without the consent of his co-partners, lawfully carry on for his own benefit, either openly or secretly any business in rivalry with the firm to which he belongs'".[867]

In these circumstances, and particularly in the light of the said partnership principle, Lord Keith held that he had no doubt that the conduct of *S* was oppressive.

21.3.2.2. ENGLAND

21.3.2.2.1 INTRODUCTION

The English contribution to the recognition of the operation of inter se fiduciary duties in the incorporated partnership beyond the ambit of the statutory just and equitable winding-up provision, has been disappointing. The following observation made by an English judge at the turn of the century has played a significant role in this regard:

> "It was strenously urged that, though incorporation affected the relations of the shareholders to the external world, the company thereby becoming a distinct entity, the position of the shareholders inter se was not affected, and was the same as that of partners or shareholders in an unincorporated company. I am unable to adopt that view".[868]

In urging that shareholders inter se were in the same position

as/ .....

as partners inter se, counsel in this particular context clearly *intended to convey* merely that the shareholders in question, inter se stood in a fiduciary relation similar to the one found in partnership and that they consequently owed similar inter se fiduciary duties to each other. As it turned out, counsel unfortunately did not distinguish between lateral and vertical fiduciary relations in this particular context.[869] This naturally gave rise to confusion. So for instance, there is no indication whether the directors, who had bought shares from the company's shareholders (at the invitation of last-mentioned) and who were being sued for breach of fiduciary duty for not disclosing that negotiations were pending at the time and that these negotiations may have enhanced the value of the shares, were shareholders of the company as well. In a nutshell, counsel did not *actually submit* that the said purchasers, *qua shareholders*, breached lateral inter se fiduciary duties. Not surprisingly the finding of the court was that the purchasing *directors* were under no obligation to disclose to their vendor shareholders the negotiations which ultimately proved to be abortive. Whether Swinfen Eady, J., was correct in pronouncing that the directors in question did not breach their fiduciary duties, is a matter which falls beyond the scope of this thesis and need not be considered further. However, what is clear is that this decision is not authority for the proposition that shareholders in an incorporated partnership do not owe inter se fiduciary duties or that one shareholder in an incorporated partnership may, with impunity, overreach a fellow shareholder in buying his shares.[870]

During the last decade a more positive attitude towards the recognition of inter se fiduciary duties in the incorporated

partnership/....

partnership, appears to have set in. "There are many small companies " Lord Donovan acknowledged in 1971, "which are conducted in practice as though they were little more than partnerships, particularly family companies running a family business ...."[871] What is more, Lord Wilberforce, it will be recalled, shortly thereafter held that there is room in company law for recognition of the fact that behind the body corporate, or amongst it, there are individuals, with rights, expectations and obligations inter se, which are not necessarily submerged in the company structure.[872] In 1971 Brightman, J., in an unreported matter, *In re Leadenhall General Hardware Stores Ltd*,[873] found that members of a quasi-partnership company owed inter se fiduciary duties and that a breach of such duties justified liquidation! This matter came before court by way of petition for the winding-up of the company in question under the statutory just and equitable winding-up provision. In 1974 the term quasi-partnership company cropped up twice in English courts in matters not concerned with the winding-up of solvent companies. In the first matter, that of *Bentley-Stevens* v. *Jones*,[874] an injunction to restrain shareholders from removing a director from his office as such, was unsuccessfully sought. One of the grounds upon which the motion was based was that the company was a quasi-partnership company, and that, on the principles enunciated by the House of Lords in the previous year, the court should restrain the first and the second defendants as "two of the three partners in the quasi-partnership, from expelling the third partner ...."[875] Plowman, J., was however, not prepared to apply those principles to the instant matter and refused the injunctions. In the same year in the unreported matter, *Pennel et al.* v. *Venida Investments Ltd., et al.*[876] Templeman, J., was prepared, however, to grant injunctions to restrain shareholders and directors from implementing a rights

issue/ .....

issue proposed by a quasi-partnership company. The order was based on passages from the speech of Lord Wilberforce regarding the just and equitable winding-up provision despite the fact that no petition had in the instant matter been presented in terms of the statutory just and equitable winding-up provision. In 1976 Foster, J., in *Clemens* v. *Clemens Bros. Ltd. et al.*[877] under very similar circumstances set aside a resolution on exactly the same grounds, but did not refer to the company in question as a quasi-partnership company. The proper ratio *decidendi* of both the latter matters is, it is submitted, that in each case the company was an incorporated partnership and that its members owed inter se fiduciary duties.

21.3.2.2.2. *LEADENHALL*

The judgment of Brightman, J., in this matter sheds light on the connection between the ratio of those decisions in which winding-up orders have been granted in terms of the statutory just and equitable winding-up provision and the two decisions in which that provision has been successfully relied upon, although no petition for winding-up had been presented. The orders in both these matters, it is submitted, are based on the principle that members of an incorporated partnership inter se owe one another a duty of good faith, and loyalty and are as such fiduciaries. In the instant matter, a petition in terms of the statutory just and equitable winding-up provision was brought for the liquidation of the company by one of its three shareholders, *G*. It was alleged that the company was in substance and in management a partnership between *G* and two brothers, *V* and *L*, in that the three contributed to its assets and shareholding and had since participated in its profits in equal shares. *G*, and the two

brothers/ .....

brothers, *L* and *V* were the sole shareholders and directors of the company in question which carried on business as a general hardware dealers in Leadenhall market. The company was incorporated by *G*, *L* and *V* to avail themselves of the opportunity which arose when the hardware department which *G* had managed for more than 36 years in Leadenhall market, closed down. The brothers whose family had suitable premises next door, but who themselves had no previous experience at all in the hardware business, wished to engage in the particular business, and, making the said premises available for that purpose, persuaded *G* to come in as manager. All three participants put up exactly the same amount of capital by way of equal loan accounts and shareholding. *G* agreed to conduct the day to day running of the business and he was the only full-time working director. *V* took no appreciable part in the day to day running of the business. *L* lent a hand when not otherwise engaged, mainly over week-ends and during holidays and luncheon hours. *L* also performed secretarial duties.

The petition further alleged that *G* had been removed from the board by *L* and *V* at an extraordinary general meeting of the company and that there was a situation of total mistrust between *V* and *L*, on the one hand, and *G* on the other hand, in consequence whereof it was just and equitable that the company should be wound up as a quasi-partnership company. This situation came about because of clear indications that *G* was taking large sums of money from the till for gambling purposes. That *G* had actually embezzled company funds, could however not be proved in a court of law.

G/ .....

G disputed the propriety but not the validity of the resolution whereby he was removed as director. The crucial issue, as seen by the court, was whether the instant company was or was not a quasi-partnership company. Brightman, J., quite correctly proceeded from the premise that a direct correlation existed between the character of members' inter se relations, the remedy available to an aggrieved member and the type of company concerned. To this end Brightman, J., drew a clear distinction between incorporated partnerships and other, ordinary companies. The learned judge dealt with the latter type first and said that in the case of "an ordinary company which is not a quasi-partnership", it might well be that a resolution removing a director from office could be called in question if the majority so resolving were not acting with a bona fide regard for the interests of the company. The learned judge stated that in such a case it might well be that the complainant could obtain a declaration that the resolution was void, or an injunction to prevent the resolution being acted upon. "But", Brightman, J., quite rightly concluded, "if the Company is not a quasi-partnership, such absence of good faith will not justify a compulsory winding-up order...."[878] Brightman, J., then turned to the incorporated partnership type, and held:

> "If however, the Company is a quasi-partnership, the same facts would not only found proceedings for such a declaration or injunction but they would also found a petition for a winding-up order on the ground that liquidation is just and equitable".[879]

The reason for the distinction suggested to, and accepted by, the learned judge is the following:

> "In the case of a *quasi-partnership company*, as in the

> case of a *partnership proper*, the *members owe a duty of good faith towards each other* .... A breach of that duty justifies liquidation at the instance of the injured party just as it would justify a dissolution in the case of a partnership ".[880]

On the facts, however, Brightman, J., found that the instant company was "not a quasi-partnership, so that the principles of partnership law ought not to be applied"[881] in the context of the instant winding-up petition. The determining factor in the mind of the learned judge was that of the three participants, *G* was the only full-time working director. At the same time the learned judge was of the opinion that, apart from the pursuit of profit, the arrangement between the participants did not have any of the normal characteristics of a partnership. "I do not see", Brightman, J., emphasized, "that this particular company had any special characteristics which require me to apply partnership principles to this petition".[882] The learned judge consequently concluded that in the absence of a "quasi-partnership situation," the petitioner's remedies, if he had been wronged, lay elsewhere than in liquidation.[883]

Brightman, J., clearly erred, in regard to the finding that the instant company was not a quasi-partnership company. Participation, (equal or unequal) in management, is not a *sine qua non* either in a partnership proper or in an incorporated partnership. Moreover, apart from the fact that the object of the association was the pursuit of profit, equality of interests prevailed between the participants *G*, *L* and *V*, who in true partnership fashion pooled their particular skills and resources with a view to utilizing a particular opportunity.

G, it will be recalled, provided not only the managerial know-how necessary to run a hardware store, but also such goodwill as was attached to his name, having served in a similar capacity in the particular market for many years. *V* and *L*, on the other hand, made the premises available without which it would not have been possible for the associates to realize the opportunity which had come their way.

Taking everything into consideration, it is clear that had *G*, *V* and *L* not incorporated their venture they would have been partners proper. The fact that Brightman, J., overlooked this elementary truth, does not detract from the merit of his judgment. The particular contribution of this decision is the recognition of the fact that members of incorporated partnerships inter se owe fiduciary duties analogous to those owed by partners.

21.3.2.2.3. *PENNEL*

In this matter the term quasi-partnership company was used throughout the case both by counsel and the judge in referring to the company concerned, Nationwide Homes Ltd. ("N.H.").[884] N.H. was clearly an incorporated partnership. It was incorporated by two property developers *P* and *S* with the objects of a property and development company. *N.H.* required funds to purchase sites and for general development purposes. *M*, who, through his connexions in the financial world had access to sources of finance, was prepared to procure loan funds for *N.H.* but only on condition that he be given a controlling shareholding in the venture. To this end an oral agreement was concluded whereby *M* would hold 51 per cent of the share capital of *N.H.* (through a company *V*), and *P* and *S* the remaining 49 per cent (through *P.S.* a nominee company of *P*).

Templeman, J., found that the oral agreement gave rise to a "quasi-partnership arrangement" between *V* and *P.S.*, in terms of which *V* was to be the "financial partner" solely responsible for the financial affairs of *N.H.*, and *P.S.* was to be the "development partner" in charge of the real estate and building operations.[885] In accordance with the said agreement 51 shares were issued and allotted by *N.H.* to *V* and a further 49 shares to *P.S.* In addition to *P* and *S*, the board of *N.H.* consisted of three representatives of *V*. In law *N.H.* was a subsidiary company (not unlike *S.T.M.* in *Scottish Co-op.* — for which see para. 21.3.2.1.2. above); in substance, however, it was an incorporated partnership.

The partnership character of *N.H.* did not escape the attention of Templeman, J. when the instant proceedings came before him. Friction had developed between *P* and *M* against the background of the financial conditions which prevailed at the time. *N.H.* was facing bankruptcy and *V.*, because of a crisis in the money market, found it difficult to obtain loans to keep *N.H.* afloat. Under these circumstances *M* convened a board meeting of *N.H.* for the purposes of convening an extraordinary general meeting of *N.H.*. The object of the meeting was to increase *N.H.*'s share capital to £200,000 to be followed by a nine-for-one rights issue. The fact that both *S* and *P* were given such short notice of the directors' meeting that they were unable to attend it and oppose the passage of the said proposals gave rise to suspicion regarding the motives of *M*. Moreover the said notice had in clear terms indicated that it was assumed that *P.S.* would not wish to invest the substantial amount of money required (£44,000) in *N.H.* in its present state and that *M* anticipated that his group would thus obtain

a/ ....

a 90 per cent interest in *N.H.* It was common cause that neither *P* nor *S* nor *P.S.* would have been able to raise the funds necessary to follow their rights and that *M* was aware of their predicament. It was averred that *M* was in fact bargaining on the *P.S.* faction being unable to take up its rights as substantial fiscal advantages would, by way of group relief in respect of the tax losses suffered by *N.H.*, accrue to the group of companies of which *V* was part, and which was controlled by *M.*[886] *S*, *P* and *S.P.* issued a writ seeking injunctions restraining the shareholders of *N.H.* at the proposed general meeting and the directors at any board meeting from voting for the increase in capital and ensuing rights issue.

The plaintiffs asserted that *N.H.* was a quasi-partnership company. They averred that it was a term of the partnership or quasi-partnership agreement that unless both factions consented to a change, the share capital would be held constantly in the ratio of 51:49, and also that there would be no increase of the share capital without the consent of either faction. Reliance was placed on many passages from the speech of Lord Wilberforce in the House of Lords decision considered above, and it was submitted that the situation was one where the exercise of legal rights should be subjected to equitable considerations. The defendants argued that *N.H.* was commercially insolvent and that an injection of capital was necessary for its survival. It was common cause that outsiders were not prepared to advance funds because of the financial state of *N.H.* It was submitted that *V* was not doing anything to prevent *P.S.* from taking up its rights if the latter chose to do so and that it was not the fault of *V* if *P.S.* lacked the financial resources to take

up/ .....

up its rights. It was admitted that *V* did have the funds necessary to rescue *N.H.* but it was urged that it would be unfair to require *V* to do so without the support of *S.P.*. Templeman, J., granted the injunctions in a judgment which is strongly reminiscent of the judgment handed down by Lord Wilberforce in the House of Lords during the previous year. Although there was probably no pre-existing partnership between *P* and *M*, the learned judge found that *N.H.* was a quasi-partnership company and that the relationship between the *V* and *S.P.* factions was one based on mutual confidence and trust.[887] This, in the final analysis, appears to be the *ratio decidendi* although the learned judge went to great lengths to couch his decision in formulae previously used by Lord Wilberforce in regard to the just and equitable winding-up matter that served before him. Thus, for instance, Templeman, J., referred to the existence of an *express contract* which resulted from the arrangement between the two factions, to the effect that their respective share-holdings would always be in a constant ratio of 51:49 unless both agreed otherwise.[888] In addition the learned judge was prepared to infer that there must have been an *understanding* between the factions that there would be no increase in share capital without the consent of the plaintiffs.[889] It is against this background that the learned judge was prepared to grant injunctions to restrain breaches of both the express contract on the one hand, and, the understanding, on the other hand, that there would be no increase in share capital without the plaintiffs' consent. Templeman, J., clearly using the language used by Lord Wilberforce in regard to the statutory just and equitable winding-up provision, reasoned that any such breach would be *"inequitable*, on the basis that the present was an occasion when the *exercise* of *legal*

rights/ .....

rights should be subjected to *equitable considerations*, because of this *fundamental understanding* upon which the association between the two factions had come into existence and was based".[890]

Irrespective of the language used and the resort to the just and equitable phraseology, the injunctions were granted because of the fact that *N.H.* was recognized as an incorporated partnership. This is borne out by the repeated references to the terms"quasi-partnership"company and"quasi-partnership arrangement". This in turn explains the references to the (inter se) relation of mutual trust and confidence and to "development partner" and "financial partner". These concepts provide a more plausible basis than the one mooted by Templeman, J., for the inference that the share capital of *N.H.* could not be increased without the consent of the plaintiffs. Because the associates were "partners", the particular method of funding adopted by *V* was unconscionable *vis-à-vis* *S.P.* and, therefore, to *S* and *P*. In making funds available to *N.H.*, *V* as financial partner was at liberty to adopt one of two courses. It could provide the requisite funds by way of loan or by injection of equity share capital in terms of a rights issue. A loan would, as Templeman, J., observed, normally have been more advantageous to *V* in that it would have provided *V* with entitlement to regular interests payments and, in any liquidation, would have given *V* priority to any contributories. At the same time a loan, unlike an injection of fresh equity capital by way of rights issue, would not have prejudiced *S.P.* at all. An injection of share capital as proposed by

M, on the other hand, would have benefited the group of which *V* was a member because of the inability of *S.P.* to follow its rights. This, the learned judge found, was the predominant purpose in the mind of *M* in choosing a rights issue and not a straight loan. In proceeding in this fashion, *M* was acting in disregard of the interests of *S* and *P* and therefore in breach of the obligation of good faith, *i.e.* fiduciary duty, owed to them. This, it is submitted, is the true basis of the decision although Templeman, J., did not express himself in these particular terms.

21.3.2.2.4. *CLEMENS*

The decision of Foster, J., in this matter complements the decision of Templeman, J., considered above. Both matters concern share issues. Both came before court by way of proceedings under the statutory just and equitable winding-up provision, although in neither was the relief which was sought winding-up.

In the instant matter, the plaintiff, *P*, held 45 per cent of the shares in a family company,[891] the remaining 55 percent being held by her aunt *M*. *P* sought an order setting aside resolutions which had already been passed (but not implemented) as opposed to the resolutions in the previous matter which had merely been proposed when the injunctions were granted. And where the share issue in that matter concerned a rights issue, the share issue in the instant matter did not. In the judgment of Foster J., the intention had been to water down the plaintiff's stake in the company to less than twenty-five percent. The new shares

were/ .....

were to be issued to a trust for the benefit of the non-shareholding directors and employees of the company. There was no suggestion that the company required an injection of capital, in fact the company itself proposed to advance £16,575.00 to the employee's trust. The evidence was that the directors were overpaid and that the argument that the directors should be given shares as incentives was somewhat unreal. Foster, J., moreover came to the conclusion that the proposal was not in the best financial interests of the company, involving, as it did, the depletion of the company's capital at a time of grave economic crisis in the construction industry.

Possibly in deference to the caution sounded by Lord Wilberforce, Foster, J., unlike Templeman, J., did not once refer to the company concerned as a quasi-partnership company. Yet Foster, J., again unlike Templeman, J., immediately identified the vital issue as being whether *M* as shareholder owed *R* a fiduciary duty in voting for the resolutions in question. "The directors", the learned judge observed, effectively distinguishing between vertical fiduciary relations and lateral fiduciary relations, "have a fiduciary duty, but is there any, or any similar restraint, on shareholders exercising their powers as members at general meetings?".[892] In Scotland the answer to that question had been furnished many years previously by Lord Murray when he found that the Roman Law adage, *in societatis contractibus fides exuberet*, applied to members of an incorporated partnership. The relief sought in that matter, as in the present was the setting aside of a shareholders' resolution. In England too Brightman, J., in 1971 and Lord Wilberforce in

1970/ .....

1970 had referred to and relied upon similar notions in matters in which winding-up orders were sought in terms of the statutory just and equitable winding-up provision. Brightman, J., it will be recalled, in fact found that in the case of an incorporated partnership, as in the case of a partnership proper members owed a duty of good faith to each other, that is a fiduciary duty inter se. Lord Wilberforce it is true, did not formulate the principle in such explicit terms, but his Lordship nevertheless repeatedly referred to principles of equity developed in relation to partnership. The principles which his Lordship had in mind were, *inter alia*, that a partner may not, in exercising his contractual rights, act in disregard of the interests of his fellow associates. This particular facet of equity — it could be appropriately styled the duty of loyalty — had been recognized in Roman law already. It was received in English Law, and applied in *Blisset*[893] to set aside a resolution expelling a partner from an unincorporated partnership. Here Page-Wood, V.C., held that partners must exercise their contractual powers "with good faith, and not against the truth and honour of the contract "[894] and that such powers exist "not for the benefit of any particular parties holding two-thirds of the shares, but for the benefit of the whole society and partnership, it being considered to be an advantage to all that there should be this particular power ".[895]

The principle in question was conceived long before the recognition of the incorporated partnership and long before the statutory just and equitable winding-up provision was placed on the statute book for the first time in England. Yet there is no reason why the said principle should not also be applied

to/ .....

to incorporated partnerships. There is also not any reason why, in petitions brought under the statutory just and equitable winding-up provision, reliance should not be placed on this principle. In fact in *Ebrahimi*[896] it actually happened that this principle was applied to an incorporated partnership in a matter that came before court by way of the statutory just and equitable winding-up provision. Here, it will be recalled, Lord Wilberforce, after referring to *Blisset* and after saying that the test was "whether it is equitable to allow one (or two) to make use of his legal rights to the prejudice of his associate(s)",[897] held that the petitioner's co-shareholders "were not entitled, in justice and equity, to make use of their legal powers of expulsion ...."[898] These words were uttered in the context of the statutory just and equitable winding-up provision. But Lord Wilberforce did not suggest that the said principle, or any of the other principles of equity developed in relation to partnership proper, applied to incorporated partnerships only by virtue of the said statutory provision. Unfortunately both Templeman, J., in the matter just considered, and Foster, J., in the instant matter, mistakenly proceeded from the premise that Lord Wilberforce had in fact said just that.

Foster, J., however,did not err in identifying the crucial issue in the instant matter. Therefore the learned judge correctly posed the question whether *M* as shareholder holding 55 percent of the shares, when voting for the resolutions, honestly believed that those resolutions would be for the benefit of the plaintiff.[899] But like Templeman, J., before him, Foster, J., in seeking the answer to the above question, unfortunately

found/ .....

found it necessary to invoke the cant phrase "just and equitable" which, for obvious reasons, played such a prominent role in the speech of Lord Wilberforce.[900] To this end the learned judge cited a passage from that speech which explained the meaning of the phrase in question in order to justify the conclusion that *M* was not entitled to exercise her majority vote in whatever way she pleased, and, not surprisingly, professed to the difficulty of finding a principle.[901]

Foster, J., emphasized this point and said:

> "[I]t would be unwise to try to produce a principle, since the circumstances of each case are infinitely varied. It would not ... assist to say more than that in my judgment. Miss Clemens [*M*] is not entitled as of right to exercise her votes as an ordinary shareholder in any way she pleases. To use the phrase of Lord Wilberforce, that right is 'subject ... to equitable considerations ... which make it unjust ... to exercise [i]t in a particular way ....'"[902]

The difficulty suggested by Foster, J., is self-induced and illusionary. It is the result of the invocation of the "just and equitable" provision in the particular context. At the same time, the principle in issue is obvious. Members of an incorporated partnership, as Brightman, J., in *Leddenhall*[903] correctly observed, inter se owe a duty of good faith towards one another. The norm against which the question posed by Foster, J., is to be tested, is therefore a fiduciary norm. That norm is neither static nor uniform and is, like moral conceptions, fashioned by the generally accepted notions and the social conscience of the particular

community/ ...

community and era.[904] It does not matter that the circumstances of each case are infinitely varied. For in every particular case it is a question of fact whether there has, or has not, been a deflection from the norm. In essence this question is not more difficult to answer than the question whether a fiduciary who stands in a vertical relation, like the director for instance mentioned by Foster, J., has or has not breached his fiduciary duty.

As it turned out Foster, J., arrived at the same conclusion which he would have reached, had he applied the fiduciary test. This conclusion was that a court of equity would not allow *M* to use her legal right to vote in the way that she has. What proved to be decisive in this particular context was that although *M* was pursuing a legitimate purpose in voting in the way she did, she nevertheless acted in disregard of the rights of her fellow shareholder *R*.[905] Such a disregard by one shareholder of the interests of a fellow shareholder will be legally relevant if there is a duty on the shareholder in question to consider and have regard to the interests of his fellow shareholder. Such a duty will be a fiduciary duty and it will flow from a fiduciary relation which in turn will imply that the company in question is an incorporated partnership.

It is true that Foster, J., did not once refer to the company in question as an incorporated partnership or a quasi-partnership company, or state that *M* and *R* were in substance partners. Yet those circumstances appear to offer the soundest basis for subjecting the exercise of legal rights to equitable con-

siderations/ .....

considerations.[906]

21.3.2.3. SOUTH AFRICA

21.3.2.3.1. INTRODUCTION

In this jurisdiction the basically English approach that members of a company cannot and do not inter se owe fiduciary duties, appears to have been in vogue for a long time. As recently as 1968, a South African court, for instance, accepted the correctness of *Percival*[907] and followed it. This was in the matter of *Meskin N.O.* v. *Anglo-American Corporation of S.A. Ltd.*[908] Here the crucial issue was whether a confidential or fiduciary relationship existed between the real plaintiff, *T*, and the two defendants, *A* and *X* and whether a fiduciary duty rested upon *A* and *X* to disclose essential information to *T* about a company *U* which was engaged in mining and exporting a mineral called ilmenite. *T* at the time was a shareholder of *U* but apparently not a director of that company. *X* was a director of *U* but apparently not a shareholder of that company. *X* was both an employee and nominee of *A*, the most influential mining house in the country. The pleadings did not allege whether *A* was the other shareholder of *U*, although it is very likely that *A* was. *U* apparently had no other shareholders and might in fact have been an incorporated partnership having *T* and *A* as members.

It was common cause that *X* had invited *T* to subscribe for further shares in the unissued share capital of *U* and that *A* had simultaneously offered to buy *T*'s existing and future holding in *U* at a price in excess of that which *T* had paid for it. Under these circumstances *T* accepted *X*'s offer and subscribed for further shares in *U* but declined *A*'s offer and did not

sell/ .....

sell any of its shares to the latter. As it turned out the shares were worthless. Unbeknown to *T*, *U* was contractually obliged to sell the major portion of its total anticipated production of ilmenite overseas at a price below both cost and the ruling world price. Not surprisingly *U* failed and went into liquidation, as did *T*. In these circumstances *T*'s liquidator instituted action against *A* and *X* for loss suffered, alleging that by concealing the existence of the contract, of which they were aware at all relevant times, they had breached their duty with regard to *T*. The defence that the summons disclosed no cause of action was successfully raised by *A* and *X* by way of exception. The central issue was whether the relationship between the parties was such as to give rise to a duty to disclose. Jansen, J., who delivered the judgment in the Appeal Court, noted that no fiduciary relationship had been alleged, save, possibly one constituted by the fact that *X* was a director of *U*, the company in which *T* held shares. "The only authority quoted in this regard" Jansen, J.A. remarked, "is from the English law (such as *Percival* ...), which seems to be against the acceptance of such a relationship between shareholder and director ...."[909] The learned judge held that there seemed, likewise, no reason in South African law to accept a fiduciary relationship between director and shareholder and allowed the exceptions.[910] This is correct. There is no direct relation between a director and the shareholders of his company. There is a direct relation between a director and his company but that relationship is a vertical relation which imposes a fiduciary relation on the director in favour of his company only and not also in favour of its shareholders.

The crucial question which was never raised in this matter,

was/ .....

was whether, *A* stood in a fiduciary relationship to *T* on the lateral level. Unfortunately there is no record of either of these aspects. In order to establish whether a duty to disclose might have arisen on other grounds, Jansen, J., in a scholarly judgment adopted a comparative approach and referred to Roman, Roman-Dutch, English and American law. If *U* were an incorporated partnership and *A* a member thereof, a lateral fiduciary relation would have existed between *A* and *T*. That relation in turn would have given rise to *A* owing *T* a fiduciary duty similar to the one owed between partners inter se. Such a conclusion was drawn in Scotland by Lord Murray many years previously when he adopted the Roman Law adage *in societatis contractibus fides exuberet.*[911] Similar conclusions have also been drawn by American courts on numerous occasions[912] and by an English court on at least one occasion.[913] It is clear however, that Jansen, J., did not lay down that *A, qua* member of an incorporated partnership did not owe a fiduciary duty to *T, qua* co-member thereof. This issue was not argued or considered at all. The question whether members of an incorporated partnership inter se stood in a fiduciary relationship, and as such owed fiduciary duties, was therefore left open for decision in South African law.

In three recent decisions this question was either argued or raised by the court *mero motu*. In *Super Safes (Pty.) Ltd. et al.* v. *Voulgarides et al.*[914] for instance, a matter in which the validity of a restraint of trade clause was in issue, the question of partnership norms was raised in passing by the Witwatersrand Local Division of the South African Supreme Court. In possibly the most exciting development in this field in the English system so far, namely *Bellairs* v. *Hodnett et al.*,[915] the operation of inter se fiduciary duties

between/ .....

between members of an incorporated partnership was accepted without qualification. Here the company was unquestionably an incorporated partnership and treated as such. In addition the corporate partners had made no secret of their intent with regard to the character of their inter se relation. One of the stipulations of the shareholders' agreement concluded by the two associates was that there would be *uberrimae fidei*. Here action was instituted for an accounting of profits and arose because of one partner usurping opportunities which fell in the line of business of the incorporated partnership. Not surprisingly the Appellate Division of the South African Supreme court applied partnership principles to determine whether an accounting should be ordered. Very recently the Witwatersrand Local Division has once again identified a company as an incorporated partnership. This was in the matter of *Bauermeister* v. *C.C. Bauermeister et al.*[916] Here Nicholas, J., tersely referred to two associates as "carrying on business in partnership in the form of a private company ...."[917] This observation was, however, made merely in passing and did not seem to influence the relief which was sought.

21.3.2.3.2. *SUPER SAFES*

In this matter the applicant, *S*, a company carrying on business as a manufacturer and seller of safes, unsuccessfully endeavoured to enforce a restraint of trade clause against *V* and *T*, two of its shareholders who respectively held 35 percent and 10 percent of its issued share capital. The remaining 55 percent of the shares was held by *G*.

An associative relationship between *V*, *T* and *G* came about when

G/ ...

G acquired 80 percent of the company's share capital from its previous owner. At the time *V* and *T* managed and controlled the business for the previous owner who took no active part in running it. Between themselves *V* and *T* possessed knowledge of and had built up a connection with the customers of the company and also had the technical know-how and ability required to manufacture the safes and other articles manufactured by the company. *G* did not possess any of this knowledge or ability. Because he realized that *V* and *T* had an important contribution to make, and in order to retain their loyalty and fidelity to the undertaking, *G* gave *T* a 10 percent equity stake in the company and brought *V*'s up to 35 percent. *V* was appointed director and both he and *T* signed a restraint of trade clause which was clearly unenforceable. It would appear as if *G*, *V* and *T* might have been in partnership, albeit in corporate form. The company's affairs were administered by the three associates who drew salaries agreed upon between themselves. Subsequently relations soured, *V* resigned as director and as employee as did *T*, whereupon they started a business in competition with *S*. In the litigation which ensued Nicholas, J. indicated that the restraint in question seemed unjustified. At that late stage counsel for *S* for the first time submitted that on the facts before court the situation was not dissimilar to a partnership where the parties were engaged in a joint venture for their joint profit to the extent of the shares acquired by each of them. Nicholas, J., found this submission attractive and said:

> "Where it can be shown that the shareholders are *de facto* carrying on a partnership by means of the machinery of a limited liability company, it may well be that the reasonableness of the restraint as between the shareholders and between them and the company will fall to be dealt with as if the restraint were one agreed upon between partners ".[918]

What/ .....

What Nicholas, J., in effect said, was that if *S* were an incorporated partnership and *V*, *T* and *G* were therefore in substance partners their inter se relation would have been a fiduciary relation requiring them to be loyal to one another and to the company. In the light of the (fiduciary) duty of loyalty, the restraint might, depending on its further terms, not be unreasonable and therefore justifiable. On the other hand, the same restraint would have been unreasonable had the parties not stood in a personal fiduciary relation of confidence but an impersonal *intuitus pecuniae* one instead. However, because the applicant did not endeavour to make out that case on affidavit and because there was insufficient information before court to show that that was the situation, the restraint was found to be one against mere competition and as such, not justified.[919] Although Nicholas, J., was therefore not prepared to make a positive finding in that regard, his judgment augurs well for the future.

21.3.2.3.3. *BELLAIRS*

In this matter the central issue was whether *B*, as a member of an incorporated partnership, was liable to account to *H*, his fellow member in the incorporated partnership, in regard to profits made by *B* in "usurping" two "corporate opportunities".

In the court *a quo*[920] Botha, J., referred to the well-known New York decision *Meinhard*[921] in order to determine the scope of the fiduciary duty owed by *B*. It would therefore be useful to consider the facts of the instant decision against the backdrop of that, earlier, New York case. Meinhard concerned a joint venture between *M* and *S* and the liability of *S* to account to *M* in regard to usurping a partnership opportunity. Here the New York Court of Appeals, by a majority of four to

three/ .....

three, affirmed a judgment ordering *S* to account to *M* although the opportunity in question in fact arose after the termination of the (time-wise) limited venture.

Like *M* and *S*, *B* and *H* were joint venturers involved in property development. However, unlike *M* and *S* who employed the vehicle of a joint venture *simpliciter*, *B* and *H* carried on their joint venture through the "machinery"[922] of an incorporated company, Northcliff Townships (Pty.) Ltd. ("N.T."). In the New York matter the property involved was central city property in the heart of New York. The venture entailed the leasing of a hotel block by *M* and *S* for a period of twenty years. In the instant matter the property concerned was undeveloped land on the Transvaal Highveld north-west of Johannesburg. Initially the venture between *B* and *H* was limited to the development of one single township, Northcliff Ext. no. 15 ("*N.15*"). By subsequent agreement between *B* and *H* the scope of their venture was expanded to include the development of a further township, Northcliff Ext. no. 19 ("*N.19*"). The scope of both ventures in question was therefore particularly limited. While this fact did not deter the New York Court of Appeals from holding *S* liable to account, it did inhibit the South African Appellate Division from holding *B* liable to account. In both matters an account of profits was claimed. Yet the opportunities which were allegedly usurped were quite dissimilar. In the New York matter the opportunity was the renewal by *S* for himself of the venturer's existing lease when the original term expired. In the instant matter the opportunity was the acquisition by *B* for himself of two further tracts of undeveloped land suitable for township development. The one tract was 30 miles away from the company's operations at *N.19* and was identified by the court

as/ .....

as the Uhlenhorst proposition *('U.I.')*; the other immediately contiguous to it, and was identified as the Northcliff Ext. 20 proposition *("N.20")*. Both these two opportunities therefore fell beyond the limited scope of the incorporated joint venture.

The status of *B* and *H* as joint venturers was never contradicted in either the Witwatersrand Local Division or the Appellate Division. This was despite the venture's corporate exterior and despite the fact that neither *B* nor *H* had originally incorporated the company, *N.T.*. *B*, an experienced property developer, in fact acquired *N.T.* as a going concern because it owned *N.15*. The object was to develop the property into a township. Subsequently *B* and *H* fortuitously met on the property when *B* learnt that *H* wished to buy it for township development purposes. Later *B* decided to form a syndicate to develop the property, and invited *H* to acquire from him a third equity stake as well as a third of his loan account, which *H* did. It was also agreed that finance, when not otherwise obtainable, would be provided by the venturers in the same ratio as their shareholding. *B* and *H* were the company's only shareholders and directors. *B* apparently acted as *de facto* managing director. In keeping with the fiduciary character of their inter se relation, *B* and *H*, as shareholders, agreed to the following stipulation:

> "CONTRACT TO BE UBERRIMAE FIDEI.
> The parties hereto shall exhibit the utmost good faith in all their dealings with one another and with the company ".[923]

This provision clearly related to the lateral, inter se relation between *B* and *H* as shareholders. In the instant matter

therefore/ .....

therefore a personal relation of confidence and trust arose between *B* and *H* by explicit, written agreement as opposed to the implicit understanding as in, for instance, *Moosa*.[924]

Both in the court *a quo* and in the Appellate Division, *B*, in resisting the claims for an account of profits, did not challenge the partnership status of the company. In fact reliance was placed on particular features of this status to defeat the claim. Thus counsel argued that on the analogy of a partnership, or joint venture entered into for the purpose of one transaction only, *B* and *H* were, in substance, partners in a joint venture which originally consisted of the exploitation of *N.15* only; that the scope of the joint venture was enlarged by express agreement to include *N.19* and that it could only have been enlarged further by a further agreement. Counsel for *B* further contended that the fact that *N.T.* was, in terms of the object clause of its memorandum, empowered to acquire further properties, was irrelevant and that because both *N.20* and *U* fell beyond the scope of the business of the joint venture, *B* was at complete liberty to acquire both for his own account as he did.

Botha J., before whom the matter served in the first instance did not agree. The learned judge said that the analogy was, in his view, not a true one, and held:

> "The analogy of a partnership may often be resorted to in considering the affairs of a two-man company such as we have here, ... and, indeed, I shall myself make use of the analogy at a later stage, when discussing the legal principles applicable to fiduciary relationships. But the analogy cannot be used in such a way as to ignore, blur or obliterate the fact of the existence of the

company/ .....

company as a separate legal entity, distinct from the 'partners' who carry on their joint venture through, or by means of the company. It is the scope of the business of the company which falls to be considered, not the scope of the business of the shareholders and directors".[925]

The learned judge was of course wrong in both respects. In regard to the incorporated partnership, courts have often disregarded the formal company constitution in favour of the real agreement between the parties or even their settled cause of conduct even when the last-mentioned had not been cast in the mould of a formal contract.[926] And, as has been observed earlier, inter se lateral fiduciary relations and corporate status are not mutually exclusive concepts. It is for this very reason that principles of equity developed in relation to partnership proper are often invoked to determine the propriety of inter se conduct in the incorporated partnership.

As it turned out the learned judge found it necessary to refer, *inter alia*, to *Meinhard*[927] and to *Goldberg* v. *Trimble et al.*[928] concerning respectively a joint venture and partnership in order to determine the scope of the fiduciary duty owed by *B*. Botha, J., quoted extensively from the last-mentioned case, and, in applying the principles enunciated therein by Chief Justice Innes, to the facts of the instant matter, held that the acquisition by *B* of *N.20*

"was an acquisition of a property intimately connected with the business of the company, and which it was *potentially detrimental to its interests* to hold for himself, and that the acquisition and development of it

was/ .....

was a matter directly concerning the company".[929]

Botha, J., further quoted extensively from the judgment of Mr. Justice Cardozo in the New York matter in question. The learned judge conceded that the last-mentioned matter concerned two joint venturers, *simpliciter* but held the fiduciary relationship between a managing director and his company, to which he had expressly bound himself to exhibit the utmost good faith, could hardly be less exacting.[930] (Unfortunately the learned judge did not endeavour to indicate in which capacity *B* had acted in breach of his fiduciary duty, that is as member, or as director or both. The recent approach adopted by American courts in this regard, of distinguishing clearly between breaches of fiduciary duty *qua* shareholder and *qua* director, is preferred.[931]) On these grounds Botha, J., found that *B* had acted in breach of his fiduciary duty towards *N.T.* when he acquired *N.20* for himself and that he was consequently liable to account to *N.T.* for the profits which resulted from that proposition. At the same time the learned judge felt that different circumstances prevailed with regard to *U* and rejected that claim. Both *B* and *H* appealed.

In the Appellate Division it was common cause that *N.T.* was an incorporated partnership. Counsel for *B* conceded that *B* and *H* were in substance partners and *N.T.* a mere vehicle for their venture.[932] As in the court *a quo*, it was agreed that the propositions in question fell beyond the limited scope of the venture. Here the argument succeeded. The Full Bench, rejected in no uncertain terms, the finding of Botha, J., that the partnership analogy was not appropriate

and/ .....

and found in effect that fiduciary relations and corporate status are not mutually exclusive concepts:

> "We think that the analogy of a partnership to the relationship of Bellairs and Hodnett and the company is an apposite and true one. *That they chose the form of a company to give effect to and carry out that relationship does not affect the existence, nature or extent of any fiduciary duty resting upon Bellairs* that is relevant to the present dispute. Since principles of equity underlie a fiduciary duty we think that the substance of their relationship and not the form in which it was cast must be looked at in order to ascertain its existence, nature and extent. Hence, the fact that the company was a separate, legal persona is not of great importance in considering the present problem".[933]

The key to the approach of the Full Bench to the instant problem is found in the above passage, for, as the court went on to explain:

> "[I]f Bellairs did not at the time owe his co-shareholder and co-partner and fiduciary duty of the kind contended for, he did not owe it to the company either. We shall return to this aspect again in due course. Suffice it to say here that we think that the rejection by the Court *a quo* of the analogy of partnership and the reliance placed on the company being a separate legal *persona* was not warranted in the light of the present inquiry".[934]

While the lateral, fiduciary relation which came about between

B/ .....

B and *T* as joint venturers, would not have been affected by the fact that the association was an incorporated one, the same cannot be said of the vertical relation. The non-reciprocal, one way fiduciary duty which arises from this latter relation will, upon incorporation, no longer be owed to the individuals to which it was owed prior to incorporation but will instead be owed to *N.T.*, the statutory right-and-duty-bearing unit. In all probability the court was here referring only to the lateral relation between *B* and *H*. This is clear from the references to co-shareholder and to co-partner. It is not unnatural, in some instance though, to extend this reciprocal, mutual fiduciary duty which arises from the lateral or associative, fiduciary relation and which is owed inter se members, to the right-and-duty-bearing unit itself. That would be in order where the body corporate is only the individual corporators (as in the present case) and where their interests are collectively at stake (as in the case of the interception of the corporate opportunity). It is in this light that the Full Bench's reference to the fiduciary duty to the company must be understood.

It is significant that the Full Bench found it necessary to appeal to analogy. The court not only repeatedly described *B* and *H* as joint venturers, but also insisted on determining the scope of their venture independently of the object clause in the company's memorandum! Thus, for instance the Full Bench observed that it was plain from the judgment of the court *a quo* that in determining the *scope* of the company's business it was largely influenced by the fact that the company was a separate legal *persona* distinct from the only two directors and shareholders, *H* and *B*, and held:

"We are, however, of the opinion that in a case such as

the/ .....

> the present the business of a company although a separate *persona*, does not transcend the contemplation of the persons embarking on a joint venture and employing the company as the means of achieving their object. It follows that in the present case the emphasis must fall, initially, on the contemplation of Bellairs and Hodnett at the time Hodnett became a member of the company ".[935]

After referring to the relationship between *B* and *H* respectively as "a joint venture limited to the development of *N.15*," as a "joint venture" and as a "venture" which originally embraced no more than *N.15*,[936] the Full Bench said:

> "On the evidence as a whole it seems clear that Hodnett and Bellairs embarked upon a limited joint venture — the developing of N.15. By subsequent agreement that was enlarged to include N.19 — but to that extent it remained a limited venture. Mere 'loose talk' could not enlarge its ambit. It follows that the scope of the business of the Company, the machinery employed, did not transcend this limited scope."[937]

Thus, as in *Fortugno*,[938] the company was but a vehicle of the joint venture. Yet partnership-like fiduciary duties were applied not *per se* but merely by analogy.

As it turned out, the finding that the scope of the joint venture was limited to the acquisition of *N.15* and *N.19*, was used to absolve *B* from fiduciary liability. "As the scope of the company business did not include the acquisition of further property in Northcliff," the Full Bench reasoned, "no fiduciary duty existed making it incumbent upon Bellairs to pass on to

the/ .....

the Company any opportunity of obtaining further ground in Northcliff".[939] Support for this conclusion was gleaned from the speech of Lord MacNaghten in the Privy Council decision of *Trimble*.[940] Here his Lordship proceeded from the clearly doubtful premise that the purchase of the properties (which were owned by the company in which the partnership acquired shares for resale) was not within the scope of the partnership. As was previously, correctly observed by Mason, J., in the Transvaal Supreme Court, it seemed impossible to hold that the shares of the company were within the scope of the partnership business, but that the stands owned by that company had nothing to do with the partnership.[941] To hold otherwise is clearly to put form before substance, an approach which the Full Bench had previously, itself, categorically rejected. It is therefore strange to see that very approach slipping in through the back door. It is submitted that the Full Bench erred in preferring the Privy Council decision to that of the Transvaal Supreme Court in this regard. The Full Bench nevertheless identified itself with *dicta* from the speech of Lord MacNaghten in the Privy Council. Thus the Full Bench held that the purchase of the properties, as opposed to the shares, was not within the scope of the partnership, that the subject matter of the said purchase was not part of the business of the partnership and was neither an undertaking in rivalry with the partnership, nor indeed connected with it in any proper sense . Itopined that the same applied in the instant matter.[942] "Bellairs' duty to disclose the utmost good faith....," the Full Bench concluded, "related to the operations of the Company within the scope of its business and did not extend to transactions beyond that scope ".[943] For these reasons the Appellate Division concluded that it could not be found that

B/ .....

B had committed a breach of fiduciary duty either in respect of *N.20* or *U1*.

It is clear that if the Appellate Division followed the approach adopted both in *Goldberg*[944] and in *Mevnhard*,[945] *B* would have been held in breach of his fiduciary duties in respect of the acquisition of *N.20* and perhaps of *U*, as well. But whether the court was or was not correct in applying particular partnership precepts in preference to others, one fact is clear. That is that principles of equity developed in relation to partnership proper were applied to members of an incorporated partnership in their inter se relation. More important perhaps, the operation of inter se fiduciary duties between members of an incorporated partnership was accepted as a fact by the Appellate Division of the South African Supreme Court.

CHAPTER VIII

A COMPARATIVE ASSESSMENT OF THE PERSONAL CHARACTER OF THE INTER SE RELATIONS OF CORPORATE PARTNERS

22.1. INTRODUCTION

The personal character of the inter se relation of members of the incorporated partnership is recognized in many jurisdictions to a greater or lesser degree. In some legal systems the said relation is recognized as a fiduciary one from which fiduciary duties arise. This is the situation in a large number of jurisdictions in the United States. To a lesser extent this is also the situation in German law. In other jurisdictions the said relation is not generally seen as a fiduciary one although some recognition is given to its special, personal character. In France, for instance, the personal nature of the inter se relationship of members of an incorporated partnership is, according to Drury, described by the term, *intuitus personae*.[946)]

In the English system again, members of a so-called quasi-partnership company have often been referred to as being "in substance partners" and principles of equity developed in relation to partnership proper have been applied to such members in their inter se relations as if they were partners. The said approach has, however, in the main been adopted for purposes of only the extreme remedy, winding-up, and not generally for the less extreme remedies and in most instances the more appropriate remedies of fiduciary restraint as well. And it is only on the very rare occasion that English courts have ventured to identify the inter se relations of members of an incorporated partnership as a personal relation, involving mutual confidence, or to find that such members owed inter se duties of good faith. And apart from the recent pronouncement in that regard by the South

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African Appellate Division in *Bellaire*[947] no court in the English system has yet found in express terms that members of an incorporated partnership inter se stand in a fiduciary relation and as such owe fiduciary duties. In view of the sterling tradition of the English Chancery, in the field of fiduciary relations, this extraordinary state of affairs requires explanation.

It is in the English courts of Chancery that the vertical relation between trustee (*fiduciarius* in Roman law [from which the word "fiduciary" is derived]) and *cestui que trust* (*fideicommissarius* in Roman law) achieved its finest hour. Today the trust is recognized as a (vertical) fiduciary relation in English law.[948] It is the genius of the English courts of Chancery which has honed the Roman idea of *bona fides* and *fraternitas*, which was supposed to prevail between *socii*, into that formidable remedial device, the fiduciary duty. Today, in English law, partnership is recognized as a (lateral) fiduciary relation *par excellence* giving rise to fiduciary duties of the highest order.

Then again the field of company law has traditionally been the preserve of the Chancery. It has already been observed how the genius of Chancery recognized the equitable joint stock company which developed from the two equitable relations falling within its jurisdiction, namely the (vertical) trust and the (lateral) partnership relation. In the nature of things these companies were public-issue companies and being capital oriented, the lateral relation was created *intuitu pecuniae*. Here too the genius of the Chancery was at work, developing the office of company director on the analogue of the (vertical) trust and agency relation. Today the relation between a

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director and his company is regarded as a *sui generis*, (vertical) fiduciary relation giving rise to non-reciprocal fiduciary duties. Although these duties were originally based on the analogy of the fiduciary duties of trustees and agents, they are today regarded as being *sui generis*.

And it is the same genius of Chancery which recognized the incorporated partnership as the quasi-partnership company in petitions based on the just and equitable provision. The equitable relief which Courts of Equity have been prepared to grant in these instances, has in all instances been premised on the personal character of the lateral inter se relations of members. Naturally such inter se relations are concluded *intuitu personae* and give rise to mutual confidence and good faith. Yet courts have been loathe to label those relations as fiduciary relations. The reticence of the judiciary to recognize the said relations as fiduciary relations and to acknowledge that, by virtue of the said character thereof, members of an incorporated partnership inter se owe fiduciary duties, is attributable to a particular tradition of the British company system. This tradition is the notion of the unity of the company concept whereby the statutory private and the statutory public company are conceived to be a single company type.

22.2. *THE CONTINENTAL APPROACH*

The fiduciary duty doctrine, as applied in German law, does not appear to display the same vitality and dynamism which the Chancery Courts have injected into that doctrine in the English system.(949) The distinction between the two systems was described two decades ago by a German commentator in these terms:

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> "The American fiduciary duty doctrine demonstrates to the continental jurist one of the most exciting examples of the social function of the common or 'judge-made' law. It may be compared with the German 'Interessen-jurisprudenz.' But, although this school of legal thought has found some recognition, the fact remains that German corporate law allows at present only partial application of the fiduciary idea".[950]

That German law should lag behind in this regard, is to some extent surprising. In terms of B.G.B., § 242, *"[d]er Schuldner ist verpflichtet, die Leistung so zu bewirken, wie Treu und Glauben mit Rüksicht auf die VerKehrsitte es erfordern"*, that is, the debtor is obliged to perform in such manner, as good faith with regard to custom requires. This principle finds application in all spheres of law including mercantile law in general and *Gesellschaftsrecht*, in particular.[951] Moreover, apart from the notion of *Treu und Glauben*, or loyalty and faith, German law also knows the notion of *Treuepflicht* or fiduciary duty.

With regard to the operation of the concept of *Treu und Glauben* and *Treuepflicht* in the field of *Gesellschaftsrecht*, German law draws a clear distinction between a *Kapitalgesellschaft* and a *Personengesellschaft*. While the general principle *Treu und Glauben* will apply to members of a *Kapitalgesellschaft* in their inter se relations, the particular principle, *Treue-pflicht*, however, will normally not. Therefore, in an A.G. an abuse of power by members will not be tolerated and a resolution which dishonours the notion of equality between shareholders runs the risk of being rescinded.[952] This is so because of the operation of B.G.B., § 242 and not because members inter se owe *Treuepflichten*.[953]

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In a *Personengesellschaft* the position is quite different. Here, apart from the operation of *Treu und Glauben*, members inter se owe *Treuepflichten*. According to Hueck a *Treuepflicht* arises *"wo ein echtes Gemeinschaftsverhältnis Personen miteinander verbindet "*, that is, if a *true associative relation* binds *persons* to one another.[954] This appears once again to relate the existence of inter se fiduciary duties to the notion of *intuitus personae*. In view of the hybrid nature of the G.m.b.H., it is not surprising that divergent opinions are held with regard to the question whether members of a G.m.b.H. inter se owe fiduciary duties. Those commentators who view a G.m.b.H. merely as a *Kapitalgesellschaft* naturally maintain that its members do not inter se owe *Treuepflichten*.[955] Then again those commentators who recognize a G.m.b.H. as a *Personengesellschaft*, have no difficulty in opining that its members do inter se owe *Treuepflichten*. Today the latter commentators outnumber the former. As in American law recognition of the said fiduciary duties is of fairly recent origin and appears to be gaining momentum.

Eichler, for instance suggested, as early as 1950, that a *Treuepflicht* would exist between the members of a G.m.b.H. if there was the necessary *"persönlichen Gebundenheit"*[956] (literally "personal bond") between such members. *"Immerhin bietet die G.m.b.H"*, Eichler reasoned, *"bei einem entsprechenden persönlichen Zuschnitt der Gesellschaftsbeziehungen Ansätze für ein Vertrauensverhältenis der Teilhaber"*.[957] (After all, the corresponding personal character of the associative relation found in the G.m.b.H. provides a natural foundation for a fiduciary relation between its partner-like associates.) A similar view was subsequently adopted by Baumbach and Hueck[958] although they doubted the existence of a similar duty in the A.G.. These authors feel that this *Treuepflicht* which

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obtained inter se members of a G.m.b.H., exceeded the general principle of *Treu und Glauben*. In terms of this fiduciary duty, members of a G.m.b.H. are, according to Baumbach and Hueck, obliged to support and protect the interests of the company but in each case the scope of such duty depends on the particular facts. In cases of severe breaches of this duty, the aberrant member may even be expelled. (Expulsion of the offender seems more sensible than the English approach of winding-up the company under the just and equitable winding-up provision!) Baumbach and Hueck seem to deduce the existence of this *Treuepflicht* from the hybrid character of the G.m.b.H. as a *tertium quid* between the A.G. (or public-issue company) on the one hand, and the O.H.G. (or partnership) on the other. The point of departure in the approach of these jurists appears to be that if members of an A.G. owe fiduciary duties,[959] then members of a G.m.b.H., *a fortiori* owe such duties, *"da die Beziehungen der Gfter zur GmbH wesentlich enger sind als die der Aktionäre zur AG,* "[960] that is, because the relation between the *associates* in a G.m.b.H. is *substantially* and *essentially closer* than the relation between the *shareholders* in an A.G. The correct view, according to these authors, is that a special *Treuepflicht* does not exist in an A.G. if that statement is supposed to mean more than the obvious implication that the relationship between shareholders of an A.G. in the exercise of their rights and duties, is governed by the basic norm of *Treu und Glauben*. On the other hand, the authors point out:

> *"Dagegen besteht für die Mitglieder einer Personengesellschaft, die zu einer wirklichen Gemeinschaft zusammengeschlossen sind, eine echte Treuepflicht .... Die GmbH steht zwischen AG und Personengesellschaft, sie kann sich je nach ihrer Ausgestaltung der Personenges*

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stark nähern".[961]

In a nutshell members of a *Personengesellschaft* who have bound themselves in a true association owe real fiduciary duties with the result that a G.m.b.H. may in practice approximate an extremely intimate and close, personal relation.

Kühn also explains the operation of members' inter se *Treuepflichten* in terms of a particularly close and intimate relation, which in turn, obviously implies *intuitus personae*. *"Die Treupflicht"* Kühn observes, referring to the existence of fiduciary duties between associates, *"setzt ein besonders enges Verhältnis der Gesellschaftsmitglieder voraus".*[962] This may be deduced, he argues from a general duty of an associate (*Gesellschafter*) to further the common associative purpose. On this basis Kühn concludes that the associative *Treupflicht* is found first and foremost in *Personalgesellschaften*[963] a term Kühn and later commentators use in preference to the term *Personengesellschaften*, employed by Baumbach and Hueck, for instance. Like others, Kühn sees the G.m.b.H. as a *tertium quid* between an A.G. and an O.H.G.. Kühn however, typifies this dichotomy as being between a *Kapitalgesellschaft*, on the one hand, and a *Personalgesellschaft*, (instead of a *Personengesellschaft*) on the other.[964] The only apparent reason for this shift in emphasis is to stress the personal character of the inter se relation in the corporate (*i.e. Kapitalgesellschaft*) context. This paved the way for terms such as *"personalistischen* G.m.b.H." used by Kühn, *"personalistische Kapitalgesellschaft,"* used by Immenga, and *"inkorporierten Personengesellschaft,"* or incorporated partnership, suggested by Immenga. Kühn identifies a number of consequences arising from G.m.b.H. enjoying this status. The first is the imposition on the associates of a particular *Treupflicht*. Another is the

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right to exclude a member who does not honour his duties, or to resign from the association. A third relates to the right of associates to information and inspection of the company's books[965] as in a partnership.

Kühn, like many other commentators draws a clear distinction between the general principle of *Treu und Glauben* and the particular *Treupflicht* which is peculiar to *Gesellschaftsrecht* The statutory imposed *Treu und Glauben* norm is described by him as a general legal principle which finds expression and operates in all legal spheres by virtue of the basic principle of justice. As such it also finds application in *Gesellschaftsrecht* in which respect the distinction between *Kapital-* and *Personalgesellschaften*, according to Kühn, plays no role.[966] The special *Treupflicht*, on the other hand, is quite different. It is regarded by Kühn as a more sophisticated development of the basic *Treu und Glauben* which imposes a special fiduciary duty [of loyalty and confidence] on the members of the association.[967] This fiduciary duty, as has been pointed out above, presupposes an especially intimate and close relationship between the members of the association. Not surprisingly therefore, this special *Treupflicht* is rejected in the case of the *Kapitalgesellschaft* of which the A.G. is the prototype. But, as Kühn observes because of the [personal] character of the G.m.b.H., the *Treupflicht* is generally accepted in the case of such company type and especially so in the more recent case law.[968]

In recent times a number of commentators have endeavoured to explain the operation of *Treuepflichten* in the G.m.b.H. in rational terms. One such commentator is Wiedemann whose point

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of departure is the disadvantageous position in which a *G.m.b.H.-Gesellschafter*, that is associate as opposed to shareholder, *(Aktionäre)*, finds himself as opposed to the position in which a *Personengesellschafter* finds himself.[969] Wiedemann argues that the first-mentioned is not only subject to the principle of majority rule but at the same time also unable to influence both the imposition and extent of the operation of that principle. A *G.m.b.H.-Gesellschafter*, the argument continues, is at the mercy of his fellow associates because he is prohibited by the rules of capital maintenance from withdrawing his investment in the association. Not only is there no ready market for his shares, but when such an associate manages to find a purchaser for his shares his fellow associates still have to approve of the prospective purchaser. In a sense these fellow associates are, Wiedemann suggests, therefore the ultimate purchasers. In the result, "*[d]er Kapitalabzug kann somit nicht, wie in der Personengesellschaft, als Druckmittel benutzt werden, um den eigenen Interessen mehr Gehör zu verschaffen*",[970] that is unlike in a partnership, the possibility that one partner might wish to withdraw his capital, would not serve as a deterrent to protect a minority shareholder's interest in a G.m.b.H..

Wiedemann laments that the German legislature failed in 1892 to safeguard the interests of the *G.m.b.H.-Gesellschafter* on the lines of the far-reaching measures which existed in the *Personengesellschaft* for the protection of minorities and that all legislative attempts to remedy the situation have been unsuccessful. According to Wiedemann, however, this void has been filled by jurisprudential developments which, although they were hesitant at first, became increasingly purpose-oriented and concerned with the plight of minorities. Initially solutions were sought, Wiedemann observes, on the analogy of corporate law *(Aktienrecht)* from which the remedy of extraordinary enquiry *(Sonderprüfung)* was borrowed. However, since

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the Second World War the pursuit has turned to the factually closer and more appropriate *Personengesellschaftsrecht*, or law of personal associations, from which the (lateral) associative *(gesellschaftliche) Treuepflicht* was taken over.[971] According to Wiedemann the German judiciary has, however, succeeded only sporadically in its aim of protecting aggrieved *Gesellschafter*.[972] Although Wiedemann finds it necessary to refer to the more advanced American experience in the field of close corporations, *Wilkes*[973] is the only American decision which is discussed by him.

Immenga, in a treatise appropriately titled the *Die personalistische Kapitalgesellschaft*, compares the German G.m.b.H. to the American close corporation. Unfortunately the question of inter se fiduciary duties is treated as a minor issue only. With regard to the close corporation, Immenga notes that American law recognizes the existence of a *Treupflicht* between members *(Gesellschafter)*. In associations of this type, he observes, disputes may usually be solved by recourse to *"Treubindungen"*, or fiduciary obligations.[974] After referring to two earlier decisions, Immenga suggests that at the time, American law had not yet reached the stage of treating members of a close corporation in the same way as members of a partnership *(Personenhandelsgesellschaft)* with regard to their *"Treuepflichten"*.[975] However, referring to the dissenting judgment of Mr. Justice Field in *Kruger*[976], Immenga mooted that close corporation law was clearly moving closer towards partnership law in that regard. It is probable that had Immenga been aware of all the American decisions in this field, he would have attributed a more prominent role to partnership fiduciary duties in the American close corporation.

However, Immenga attributes the development of

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associative fiduciary duties (*Gesellschaftsrechtliche Treuepflichten*) in American law to the trust.[977] This is both an over-simplification and an incorrect account of the development of fiduciary duties in the close corporation. It is true that in corporate law, in general, the (vertical) equitable relation trust, inspired the development of fiduciary duties between directors and their corporations, the former serving the latter in a vertical fiduciary relation. It is also true, as Immenga notes, that, in American law, these fiduciary duties were later extended to controlling shareholders when the last-mentioned either usurped the functions of the board of directors, or, were in a position to do so.[978] But this was essentially a development which took place in corporations which did not purport to be close corporations and would probably have been classed as *Kapitalgesellschaften* and not as *Personengesellschaften* or as *Personalgesellschaften* in German law. For this reason the American development referred to by Immenga is neither really relevant in the particular context nor in fact appropriate in view of the scope of the enquiry undertaken by him. Moreover, apart from being concerned with *Kapitalgesellschaften*, the said American development concerned disputes which relate to the affairs of the corporation itself and therefore, as Immenga correctly concedes to the (vertical) relation between the corporation and its servants, as opposed to the inter se relations of its members. On the other hand, as has been observed in para.20 above, the legal figure which played the prominent role in the development of the close corporation was the partnership, not the trust. It was the associative relation, partnership, which inspired both the American incorporated partnership and the character of the inter se relation of its members. It will also be recalled that the fiduciary duties which American courts had imposed

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in that regard were imposed on close corporators *qua* members and not qua directors or servants. In all the instances referred to, close corporators were acting as principals in their own right and not as servants or agents of the corporation.

With regard to German law, Immenga opines that the outlines of the *Treupflicht* resting on majority associates (*Gesellschafter*) have not yet been defined as clearly as in American law.[979] He does however state that the development seems to point towards a general principle of *Treupflichten* on the part of the *Gesellschafter* in the *personalistische* G.m.b.H.[980] The difficulty, according to Immenga, is formulating the criteria of the fiduciary principle in concrete terms. Such difficulty, he feels, is occasioned by the impossibility of determining the limits of a fiduciary obligation (*Treubindung*) if one proceeds from the isolated case as starting point. The basic question, as seen by Immenga is whether fiduciary obligations (*Treubindungen*) exist inter se the associates. Whether associates in this context have a claim against one another depends as Immenga correctly observes, on the existence of an inter se relation.[981]

Immenga, after a review of the relevant case law, concludes that it has become possible, in the case of a G.m.b.H., to speak of a general recognition of a *Treupflicht* on the part of the *Gesellschafter* towards the *Gesellschaft*. This is despite there being, in his view, no community relationship (*Gemeinschaftsverhältenis*) between the *Gesellschafter*, as in the case of the partnership (O.H.G.), to give rise to the existence of a fiduciary duty towards one another.[982] What Immenga appears to have overlooked in this regard is that the act of affording the lateral, associative relation corporate

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status, that is, is recognizing it as a right-and-duty-bearing unit, does not *per se* destroy inter se personal or fiduciary relations and obligations. Immenga does, however, conclude that *Gesellschafter* are subject to genuine, broad fiduciary duties which extend beyond the basic *Treu und Glauben*. Immenga, citing case law explains: *"denn die Beziehungen des Gesellschafters zur G m b H seien nicht rein kapitalistisch, sondern auch persönlicher Art".*[983] This is so because the relations between the *Gesellschafter* and the G.m.b.H. are not purely of a capital nature without also displaying some personal characteristics. And, quoting further decisions, Immenga speaks of a *Treupflicht* on the part of *G.m.b.H.-Gesellschafter*, or G.m.b.H.-associates, which is greater and stronger than the duty owed by *Aktionäre* or shareholders, in A.G., *"da die Beziehungen zur Gesellschaft in der Regel enger seien"*,[984] that is because, as a rule, the relationship in a [personal] association is *closer*.

In order to explain this phenomenon Immenga analyses the operation of fiduciary obligations between associates in great depth.[985] With regard to the G.m.b.H. he establishes that the source of the *Treupflicht* between *"Gesellschafter"* is the intimate and close personal relation between them, a relation which, he reiterates, is *"nicht rein kapitalistisch, sondern auch persönlicher Art"*,[986] Immenga demonstrates that the judiciary attributed the operation of the inter se fiduciary duty in the G.m.b.H. to the existence of a *"stark eingreifende"*, *i.e.* extremely deeprooted legal relationships between the associates. This very character of the relation explains, he suggests why it can be dissolved on serious grounds only. Relations which bring about a mutual *Interessenverflechtung* or interdependence of interests and

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which presuppose mutual co-operation on a personal level as well as a sound understanding and undisturbed mutual confidence, Immenga reasons require support at all times. He points out that even the slightest disturbance of such a relationship has significant legal implications. All this, he submits, can be explained only by the fact that a legally relevant relation exists between the associates. Immenga feels that the term coined by the judiciary, namely, *"gesellschaftlichen verbundenheit"*, *i.e.* lateral or associative relationship, should be understood in a similar sense.[987] Moreover, Immenga notes, the courts accept that a breach of fiduciary duty *(Treupflichtverletzungen)* by an associate justifies his being expelled. This, Immenga submits, must mean that a mutual fiduciary duty exists between the *Gesellschafter*. Immenga finds further support for the existence of a fiduciary relation between the *Gesellschafter* in the fact that apart from the statutory grounds on which a G.m.b.H. could be wound up, a further ground has been created by the judiciary. In terms of the said judicial ground a G.m.b.H. may be wound up because of serious disagreement between the *Gesellschafter*. Immenga correctly reasons that this too presupposes a legally relavant relationship *(rechtlich erhebliche Verbundenheit)* between the *Gesellschafter*, for, as he explains, such a relation is necessary in order that legal consequences can be attached to such upheavals. Therefore, Immenga concludes, a proper understanding of the principles relating to the solving of problems in the G.m.b.H., is unthinkable if there is no relation between the *Gesellschafter*, of which the law can take cognizance *(rechtliche Beziehungen)*. A contrary view, Immenga feels would belie the possibility, expressly allowed for by the legislature, namely of employing the G.m.b.H. as

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an *"inkorporierte Personalgesellschaft"* that is as an incorporated partnership.[988] These conclusions are correct and meaningful not only for German company law but for company law in other legal systems as well, and particularly company law in the English system.

In French company law too a particular awareness of the personal character of a S.à.r.l. is detectable. This is mirrored by the fact that the French distinguish not only between *sociétés de capitaux* and *sociétés de personnes* but also between *sociétés* which have been concluded *intuitu pecuniae* and those which have been concluded *intuitu personae*. And the S.a.r.l. falls in both the second mentioned categories. What is disappointing though is that French law has not yet fully developed the consequences of the personal character of the inter se relation between the *associés* of a S.à.r.l.. Despite the personal character of the said relation being explicitly recognized in French law the relation is nevertheless not treated as a fiduciary relation.

In French law the concept *intuitus personae* connotes, as it did in Roman law, that the personal qualities of *associés* are mutually important and that the inter se relation is steeped in confidence. Drury spells it out in the following terms:

> "The idea is that the personal qualities of each of the participants are of the utmost importance to the others. They repose a mutual confidence in each other. Consequently the free right of a member to transfer his share in the enterprise to whoever he chooses is inconsistent with the concept of the société being formed out of a contract concluded *intuitus personae*".[989]

This principle operates in all *societés de personnes* and therefore also in the S.à.r.l.. The said principle does, however, obviously not operate in a *societés de capitaux*

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Intuitus personae, however, is not the only concept taken over by French law from the Roman law. French law has also taken over from it the tradition of *jus fraternitas*[990] of which Roblot gives the following account:

> "*[L]es associés doivent se présenter au contrat non comme des adversaires discutant leurs intérêts, mais comme des collaborateurs animés d'un esprit de fraternité*".[991]

This principle, according to Roblot, applies to all *sociétés*[992] that is both *de capitaux* and *de personnes*. Moreover, according to Roblot "*une obligation renforcée de bonne foi en vue de l'oeuvre*" exists inter se *associés* of all *sociétés*. This explains why discord between *associés* is a cause for dissolution if co-operation is thereby rendered impossible, or if the activity of the société is thereby hampered. This approach is however, not restricted to *sociétés de personnes*, and has apparently also found application in the case of the S.A. Possibly because of the *intuitus personae* character of the S.à.r.l., and because the scope of *jus fraternitas* is greater in the S.à.r.l. than it is in the case of the S.A., the application of the principle in question has been more frequent in the case of the S.à.r.l.[993] A further consequence which flows from the said obligation of good faith is that a resolution will be treated as an abuse of power (*d'abus du droit*), and therefore as a nullity, if it is passed by associates "*contrairement à l'intérêt social, dans l'intérêt personnel exclusif des associés concernés*". This principle is clearly derived from the Roman law notion found in the adage "*semper enim, non id quod privatim interest unius ex socii,*

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servari solet, sed quod societati expedit".[994] In French law this principle finds application both in the S.A. and in the S.à.r.l.[995] Unlike German, American and English law, French law does, however, not appear to have developed the said notions of good faith and confidence into fiduciary duties and attendant remedies. The reasons for this state of affairs fall beyond the scope of the present enquiry.

22.3. *THE AMERICAN APPROACH*

The Continental terminology *société de capitaux* or *Kapitalgesellschaft* and *société de personnes* or *Personengesellschaft* is not used in American law. In broad terms the distinction embodied in that dichotomy is in American law rendered by the dichotomy public-issue corporation and close corporation. And although American law in this regard is, unlike Continental law, not based on the diversity of the corporation concept, it has nevertheless succeeded in assuming the lead in recognizing the personal inter se relation between members of an incorporated partnership as a fiduciary relation. While the reasons for this situation are certainly complex, two factors may be singled out. The first pertains to the general attitude to partnership in American law. The second is the role played by academic commentators and the judiciary in developing the close corporation.

It has already been observed how the idea of the partnership has inspired the recognition by the judiciary of the incorporated or chartered partnership. What possibly facilitated this development and added impetus to it, is "the effort" as it was described by Lattin as he referred to a trend in American litigation, "of the complaining party to qualify as a partner with the defendant party, and thus obtain the

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benefits that partnership status bestows in such matters as holding the other to a fiduciary standard of behavior, obtaining an accounting and other equitable relief from the other, forcing the dissolution of an enterprise ... *etc*". [996] Kessler concurs."[I]f recognized standards of fiduciary obligation on the part of one participant vis-à-vis another are desired," Kessler succinctly puts it, "the organization may simply be characterized as a partnership[:] this automatically brings to the organization a large body of case law on the rights and duties of the participants inter se".[997] In an incorporated partnership such an approach would be both legitimate and appropriate. Here, as in partnership proper, the lateral inter se relation is a fiduciary one. The identity of the other corporators, as one authority puts it mutually important and they repose confidence in one another.[998] In the words of another, *delectus personae*,[999] prevails.

The flexible approach adopted by the American judiciary with regard to the concept, partnership, must have played a significant role in the corporate sphere. It will be recalled that a Federal court recently observed that the Texas definition of partnership for instance was sufficiently flexible and embracing to include the concept corporation. It is also known that American courts have for many years been putting the partnership test to use to a dual end. The one purpose has been to ascertain whether, in a given situation, a particular relation was a partnership relation inter se. The other purpose has been to determine whether a given relation was a partnership relation *vis-à-vis* third persons.[1000] Not suprisingly in close corporation matters where third parties were not involved and the issues concerned only

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members in their inter se relations and the character of their inter se relation American courts have been prepared to treat the close corporation as an incorporated partnership. This explains the repeated references in the case law to statements that third parties were not interested and their rights not affected. The spade-work necessary for this judicial development was undertaken by academic and other commentators. One early commentator in this field is Winer. As early as in 1943, for instance, he clearly distinguished between the impersonal arm's length, *intuitus pecuniae*, character of the inter se relation in public-issue corporations and the personal, intimate *intuitus personae* character of the inter se relation in close corporations. Winer had the following to say with regard to the lateral inter se relation:

> "It is in the relationship of the stockholders to one another that corporate concepts are least fitting. For one of 400,000 stockholders to owe personal duties to another whom he has never met, simply because both own securities in one company, is, by today's standards, stretching a point. For three stockholders, seeing one another daily, planning their business together hourly, not to owe fiduciary obligations, is so incongruous that it clearly appears not to be the law. General statements that stockholders are trustees for one another only when they misuse majority control, when they usurp the functions of the board, or only in questions of management do not apply to close corporations".[1001]

With regard to members' inter se relations, the partnership norm, the principles of equity, as Lord Wilberforce put it, developed in relation to partnership, is clearly more appropriate than the corporate norm. It is for this reason that Winer referred to *Meinhard*,[1002] as the *locus classicus*

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in American law in the field of partners' fiduciary duties. Prophetically Winer suggested that if in that matter *M* and *S* had been stockholders in the close corporation and not mere co-adventurers, the result would have been the same. In other words, they would inter se have owed fiduciary duties but the position would not have been the same if either of them had been one of 400 000 stockholders.[1003] It is significant that courts have since, on numerous occasions, relied on passages from the opinion of Mr. Justice Cardozo in the said New York matter in order to hold corporate partners liable to fiduciary duties. Many other commentators have also since taken up the cause. One such commentator is Conway who, in 1957, for instance, effectively demolished the argument that inter se fiduciary relations (and thus duties) and corporate status are mutually exclusive concepts.[1004] "It is difficult to perceive", Conway states,[1005] "how a relationship of trust and confidence between stockholders can have any relevancy whatsoever on the question of their liability to corporate claimants, except when such close relationship is accompanied by something entirely separate from and not germane to, the fiduciary concept, namely, the disregard by the stockholders themselves of corporate formalities and amenities". However, as the learned scholar goes on to emphasize, the central issue in conflicts of this nature always has been and is the inter se relations of members, and not liability to third parties. Said he "the fiduciary concept pertains solely to the relation of the stockholders *inter sese*. The presence or absence of personal liability of the stockholders depends upon other factors having nothing to do with that relationship".[1006] Conway also argues that the result in *Meinhard*[1007] would not have been any different had the joint venturers there seen fit to incorporate their venture.

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"The courts," he concludes "should have no hesitancy in declaring the confidential relationship where it is found in fact to exist, even though the parties happen to be stockholders and to grant the [equitable] relief requested ...."[1008] American law has been blessed in that these "scholarly effusions," as Chayes described them, "have borne an increasing fruit of judicial decision ...."[1009] In the result close-corporation law has been "witnessing the not very surprising development of the notion that shareholders of such a corporation are fiduciaries *inter sese*".[1010]

As in German law, the fiduciary duties which apply to close corporators in their inter se dealings are however, of a much higher standard and intensity then those owed by controlling shareholders in public-issue corporations.[1011] "We contrast this strict good faith standard" Mr. Justice Tauro affirmed in *Donahue*, referring to the more rigorous duty of corporate partners, "with the somewhat less stringent standard of fiduciary duty to which directors and stockholders of all corporations must adhere in the discharge of their corporate responsibilities".[1012]

What distinguishes American law in this regard from German law and English law is both the frequency with which the operation of inter se fiduciary duties between corporate partners has been recognized and the range of cases involved. In America this spectrum ranges from, on the one extreme, the dealings between prospective corporate partners which precede incorporation, to, on the other extreme, transactions whereby one corporate partner buys out the interest of his fellow corporate partner in their incorporated partnerships. It includes all forms of unconscionable and disloyal conduct which affect the mutual interests of the corporate

partners/ ....

partners in the right-and-duty-bearing unit, which is the incorporated partnership, such as, for instance, the interception or diversion of corporate opportunities.

The operation of inter se fiduciary duties has been recognized by American courts in matters where one corporate partner has withheld material information from, or has otherwise defrauded, his future fellow corporate partner in the negotiations preceding association. One such matter is *Latimer*.[1013] Here a corporate partner who had defrauded a fellow corporate partner was held to have breached his fiduciary duty *vis-à-vis* the latter. The Supreme Court of Michigan ordered the errant fiduciary to refund the money the aggrieved partner had invested in the venture, against surrender by the latter of the relevant certificates of stock. Another matter of this kind is *Donahue* v. *Davis*.[1014] Here the Supreme Court of Florida ruled that a corporate partner, who had breached his fiduciary duty by overstating the value of his contribution to the venture, was holding the shares he had received in excess of his true contribution in trust for his defrauded fellow corporate partners. Another example in this regard is *Helms*[1015]. Here one corporate partner had breached his fiduciary duty *vis-à-vis* his fellow corporate partner by not disclosing his fixed intent never to agree to an upward adjustment of the price at which the survivor was entitled to purchase the shares of the first dying in terms of a provision in a survivor-purchase agreement. The said provision envisaged that such adjustments would be made at periodic intervals by mutual consent. The United States Court of Appeals for the District of Columbia held that the said breach of fiduciary duty warranted a cancellation of the survivor-purchase agreement. And in *Wilson*,[1016] the Supreme Judicial Court of Massachusetts held that a corporate partner's failure to disclose his secret employment agreement with the corporation to a fellow corporate partner constituted a breach of the

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fiduciary duty owed to the latter in consequence of which the said agreement was void.

American courts have enforced inter se fiduciary duties in order to maintain equality between corporate partners with regard to their shareholding in the corporation. Thus, for instance, the Supreme Judicial Court of Massachusetts in *Arnold*,[1017] held a corporate partner liable, as in a partnership accounting, to account to his corporate co-partner for the value of certain stock (together with dividends and the value of treasury stock which accrued thereon) which the latter had secretly acquired in their incorporated partnership in breach of an agreement of equality. In *Campbell*[1018] too the corporate partners had also agreed to equal shareholding and control. When one corporate partner secretly acquired shares which gave him a majority holding, the Supreme Court of Kansas decreed that the aggrieved corporate partner was owner of one-half of the stock purchased by the other corporate partner in breach of his fiduciary duty in that regard. And in *Cressy*,[1019] two corporate partners had each secretly acquired further shares in their close corporation although it was originally intended that equal ownership and control of the business would prevail. The Indiana Court of Appeals described the fiduciary duty which it found both corporate partners had breached, in the following terms:

> "The 'partnership' expectation of equality of shareholdings carried with it the duty on the part of each principal to disclose to the other the availability of outstanding shares for sale and to afford the opportunity to share in the purchase of such stock".[1020]

The said court further found that although the court *a quo*

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might have entered an order against both corporate partners requiring them to exercise their voting rights consistent with their obligations, or might have ordered the sale of an 'equalising' number of shares, it exceeded its power as a court of equity when it declared the articles to be amended by declaring certain shares to be non-voting shares.[1021)]

American courts have also enforced inter se fiduciary duties between corporate partners in order to maintain equality between them in yet another sense. When, for instance, one corporate partner buys out the interest of his corporate co-partner in the incorporated partnership, courts have on a number of occasions insisted that such corporate partners transact on equal footing as buyer and seller. This presupposes that the party with superior knowledge concerning the financial affairs of the incorporated partnership, and therefore the value of the shares, is bound in terms of a fiduciary obligation to make a proper disclosure to the less informed party. Failure to do so and the withholding of material information constitute a breach of the inter se fiduciary duty and entitle the corporate partner who has been overreached because he has sold his shares to rescind such sale. This conclusion was reached by the Supreme Court of Missouri in *Denny*,[1022)] the New York Supreme Court in *Modlin*,[1023)] the Minnesota Supreme Court in *Fewell*,[1024)] and the Supreme Judicial Court of Massachusetts in *Sher* v. *Sandler*.[1025)] In *Wise Realty*[1026)] the Californian Court of Appeal and in *Mendelsohn*[1027)] the Supreme Judicial Court of Massachusetts came to a similar conclusion as to the law but found that, on the facts, the particular duty had not been breached.

The pursuit of the ideal of equality between corporate partners

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by the enforcement of inter se fiduciary duties explains the Supreme Judicial Court of Massachusetts decision in *Donahue*.[1028] Here Chief Justice Tauro held that the rule of equal opportunity in stock purchases by close corporations envisaged equal access for all members to the benefits which accrued from what was in effect a distribution of corporate assets The learned judge found that the stockholder whose stock had been purchased received a relative advantage over his fellow stockholders inconsistent with his strict fiduciary duty. That advantage was to turn corporate funds to personal use. The court found that the participating corporate partner, by denying the non-participating corporate partners the opportunity of equal participation, had breached his strict fiduciary duty to the latter. The relief which the court deemed appropriate was that the *status quo* be restored or that the stock of the aggrieved corporate partner be purchased by the corporation on terms equal to those on which the errant corporate partner's stock had been purchased.

Similar concepts seem to underlie the decision in *De Boy*.[1029] Here it was found that corporate partners had breached their lateral fiduciary duty *vis-à-vis* a fellow corporate partner by voting and implementing a further issue of stock because such issue was designed to "water down" the latter's proportionate interest in the incorporated partnership. The Court of Appeals of Maryland found that the other stockholders, by offering such a large number of shares that the plaintiff could not maintain his proportionate stake, intended to destroy his interest in the venture. It ordered that plaintiff's claim for loss, suffered by him as a result thereof, be transferred to the equity court for an accounting. American

courts/ .....

courts have also enforced lateral fiduciary duties between corporate partners to compel a disloyal partner to account to the incorporated partnership for the profits accruing from the corporate opportunity usurped by him. Recent cases such as the Massachusetts decision, *Cain*[1030], and the Indiana case, *Hartung*[1031], clearly distinguish between (lateral) fiduciary duties owed by corporate partners *qua* stockholders inter se and (vertical) fiduciary duties owed by corporate partners, *qua* directors, in favour of the corporation itself. In the older decisions like for instance the Massachusetts matters *Samia*[1032] and *Wilson* and the dissenting judgment of Circuit Judge Hays in the United States Court of Appeals matter *Burg* v. *Horn*[1033], the court did not draw this distinction and it is difficult to determine in which particular capacity the breach of fiduciary duty was committed.

A breach of fiduciary duty also underlies the decision in *Wilkes*.[1034] Here it was held that corporate partners breached their fiduciary duty to their fellow corporate partner by severing him from the payroll of the corporation and by refusing to re-elect him as salaried officer and director. The Supreme Judicial Court of Massachusetts came to the conclusion that, in the absence of a showing of misconduct on the part of the plaintiff corporate partner, there was no legitimate purpose for the said expulsion. It also found that the motive appeared to be to pressure the said stockholder into selling his shares to the corporation at a price below their value. However, instead of granting a winding-up order, as an English court would have done, the Massachusetts court found that plaintiff was entitled to damages, in lieu of the salary he would have received, had he continued as a director and officer subsequent to his dismissal. Alternatively the court might have re-instated the deposed director where further co-operation was still possible between the corporate partners.

Breach of fiduciary duty has been said to justify the intervention of a court of equity to grant corporate dissolution in at least one matter, *Kruger*.[1035] Cessation of the characteristic highest fidelity, loyalty trust and confidence which corporate partners are expected to display to one another, has similarly been held to justify a winding-up. A case in point is *Pivot Punch*.[1036]

22.4. THE ENGLISH PERSPECTIVE

The Continental dichotomy, *Kapitalgesellschaft* or *société de capitaux* and *Personengesellschaft* or *société de personnes* is, as Schmitthoff puts it, "unknown in English law and hardly comprehensible to the English lawyer as an abstract proposition".[1037] The English expressions which, according to a European authority,[1038] are roughly equivalent to the Continental terminology in question, are "partnership" and "company" respectively. "Company" in this context obviously means public-issue "corporation" or "incorporated company". The use of the word "company" and not "corporation" in this context, is significant. Such usage is indicative of the partnership ancestry of the association type, which, in the English system, is equivalent to the Continental *société de capitaux* or *Kapitalgesellschaft*. It also provides a clue to the reticence displayed by the courts in the English system in applying partnership concepts as freely in company law as, for instance, partnership concepts are applied in American corporation law. In the English system, the unincorporated partnership and the incorporated company are as types statutorily and therefore also judicially, kept apart and treated as incompatible types for the very reason that they derive from a common ancestor. It is for this reason that Lord Wilberforce ruled that a(n) incorporated) company is a company, and not a partnership, implying in effect that the two types cannot

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ever coincide.[1039] And while the unincorporated partnership is typified as giving rise to inter se fiduciary relations of the highest order, but lacking corporate personality, the incorporated company is characterized as enjoying corporate personality but lacking inter se fiduciary relations. The notion that these characteristics are mutually exclusive is, however, patently fallacious. As has been seen above, the concession of corporate personality essentially affects external relations only (*i.e.* those between outsiders and company members as a right-and-duty-bearing unit). It generally does not affect internal relations as well (*i.e.* inter se relations between those members composing that right-and-duty-bearing unit). The concession of legal personality certainly does not affect such fiduciary relations as would exist inter se associates who carry on their association in unincorporated fashion.

Fiduciary relations of the highest order are present in a partnership proper, but lacking in the incorporated company, not because the latter enjoys corporate personality and the former lacks it, but because the former is concluded *intuitu personae* and the latter is generally concluded *intuitus pecuniae* and not *intuitus personae*. This has unfortunately not always been realized in the English system where corporate personality and inter se personal, fiduciary relations have, until recently, been treated as mutually exclusive concepts. A step in the right direction was taken by Lord Wilberforce when he ruled in the House of Lords that there is room in company law for recognition of the fact that behind the company (in the sense of a body corporate *i.e.* a statutorily created right-and-duty-bearing unit) there are individuals with personal rights, expectations and obligations inter se

which/ .....

which are not necessarily submerged in the formal company structure.[1040] In effect his Lordship acknowledged that the corporate personality of a company does not prevent company members from enjoying personal inter se relations This admission constitutes an important discovery. The existence of a personal inter se relation between associates is, as demonstrated by Immenga, a *sine qua non* if inter se fiduciary duties are to arise. This appears to have been realized in a number of recent decisions in the English system and augurs well for the future. Obstacles, however, still remain.

Unlike Continental law English company law is not based on the diversity of the company concept. This has had a particularly unfortunate effect on the incorporated partnership. Because the incorporated public-issue company necessarily enjoys corporate personality it has always been believed that its members are, for that reason, incapable of bearing inter se fiduciary duties. The true reason why the members of such a company do not bear inter se fiduciary duties is that they do not stand in a fiduciary relation to one another. That the said members do not stand in a fiduciary relation to one another is not due to the fact that the lateral relation is statutorily recognized as a right-and-duty-bearing unit but to the fact that such lateral relation has been concluded *intuitus pecuniae* and not *intuitus personae*. However, because of the "unity", as Schmitthoff[1041] terms it, "of the company concept" in the English system and because of the common denominator, corporate personality, members of a private (incorporated) company have, like the members of a public-issue company, been regarded as being incapable of bearing inter se fiduciary duties. In truth, the presence or absence of inter se personal or fiduciary relations between members of

a private company is likewise in no way affected by the notion of corporate personality. The existence of such fiduciary duties hinges essentially upon the concept of *intuitus* or *delectus personae*. If the particular company has been formed *intuitu personae*, inter fiduciary relations will exist. If not, then clearly a personal character giving rise to inter se fiduciary duties will be absent, unless it is reintroduced by a stipulation to that effect in a shareholders' agreement or otherwise. That this is so has been borne out by the American experience in the close corporation field.

Unlike the American judiciary the English judiciary has not had to cope with what an American commentator termed those "villains of the close-corporation piece", [1042] the concession theory and its offspring, rigorous corporate norms and standard structural arrangements imposed by enabling corporation acts. These hurdles have, however, not deterred the American judiciary from discovering the incorporated partnership and recognizing the operation of inter se fiduciary duties between its members. In view of the flexibility of the English company structure and the partnership ancestry of the incorporated company, it is ironical that the judiciary in the English system should have conceded the lead in recognizing the operation of inter se fiduciary duties in the incorporated partnership to the judiciary in the American system. The judiciary in the English system, after all, was first to recognize the principle in question in that it wound up solvent incorporated companies as if such companies were in fact partnerships. It is not clear why the application of the said principle has for so long been restricted to winding-up situations and has not matched developments in the American system.

It is true that the statutory definition of partnership is more restrictive in England than it is in the United States. The English *Partnership Act*, 1890,[1043] specifically provides that the relation between the members of an incorporated company shall not be a partnership for the purposes of the said act whereas the American *Uniform Partnership Act*[1044] contains no provision in that vein. The difference in the statutory definition of partnership in the two systems does, however, not account for the fact that the English judiciary, in applying partnership precepts to members of incorporated private companies in their inter se relations, has adopted a more conservative approach than the American judiciary has, with regard to the application of partnership precepts to close corporators. The exclusion in the statutory definition of the said relation has, after all, not deterred the English judiciary from treating the relation between the members of incorporated private companies as a partnership relation or from applying principles of equity developed in relation to partnership proper, in order to wind up such incorporated private companies under the statutory just and equitable winding-up provision. In effect these English courts appear to have ignored the statutory definition of partnership and to have relied on the common law concept of partnership. This is understandable. The issue in these matters was not whether the relation between such company members was or was not a partnership relation *vis-à-vis* the world at large. The issue was simply whether such members were partners inter se and then for the restricted purpose only of applying principles of equity developed in relation to partnership proper to such members in their inter se relations. It is for this reason that the said incorporated companies have been called quasi-partnership companies, that is companies which for certain purposes are treated as if their members were partners. It is significant in this regard that third parties were not

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involved and their rights also not affected in any of the quasi-partnership cases with the exception of *K/9 Meat Supplies*.[1045] It is because of the very involvement of third party rights there that the court correctly refused to apply partnership concepts. However, as long as third parties are not involved, there is no reason why the said principles of equity should not be applied by the judiciary in the English system to members of private companies in their inter se relations also in situations other than winding-up.

It is true that academic writing advocating recognition of inter se fiduciary duties in quasi-partnership companies by the judiciary has, until very recently,[1046] been non-existent in the English system, whereas it has played a major role in that regard in the United States. This silence in academic writing does, however, not explain the lack of development in the English system in the particular field, it merely mirrors it. Explanations for this phenomenon must be sought elsewhere, possibly in the close relationship between company law and partnership law in the English system and the notion of the unity of the English incorporated company.

The American achievement in this field dwarfs the English achievement in all respects but one. American commentators like Winer, Kessler and Conway, to name but three, have explored the rationale for the existence of the incorporated partnership and the operation of inter se fiduciary duties between corporate partners in great depth. American courts have backed this learning up with a vast body of case law. As has been observed above, this case law, in the main, deals with the normal situation where, *stante societate*, the appropriate remedy is the enforcement of inter se fiduciary

duties between corporate partners with a view to maintaining the integrity of the incorporated partnership. As of late, the granting of the extraordinary remedy of corporate dissolution has, in extreme cases, become a recognized extension of the ordinary remedies of fiduciary restraint. It is in this field that the English performance surpasses the American. In the English system the main body of case law dealing with the incorporated partnership is concerned with the extreme situation where the extraordinary, "sledge-hammer" remedy which entails the winding-up of the company under the statutory just and equitable provision is justified. The ordinary fiduciary remedies, which are more appropriate in the great majority of cases, have, barring an early Scottish case, not found application in the incorporated partnership until very recently. It is noteworthy that the English judiciary has in two of the three decisions in question endeavoured to explain the relief which was granted by it as but an extension of the statutory "just and equitable [winding-up] provision". This is putting the cart before the horse and reveals a lack of appreciation of the principles involved on the part of the English courts.

In the English system the principles of equity developed in respect of partnership proper have been resorted to in order to wind up solvent companies in a wide range of situations. These include the irretrievable breakdown of mutual confidence and good faith between corporate partners, as in *Yenidje*[1047] and in *Lawrence*[1048], abuse of majority voting powers as in *Thomson*,[1049] the usurpation of control of the incorporated partnership, as in *Symington*,[1050] the unconscionable exercise of statutory or contractual powers, as in *Ebrahimi*[1051] and *Leadenhall*[1052] *etc.*. To some extent

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all the abovementioned cases are instances of a single broad principle, namely that the disintegration of the foundation of mutual confidence and good faith which underpins the incorporated partnership, makes it just and equitable that the statutorily created right-and-duty-bearing unit, be dissolved. *Ebrahimi*[1053] must in fact be seen in this light. Had mutual confidence between the corporate partners not irretrievably broken down in that matter, rescission of the offending resolution would have been more appropriate than dissolution of the body corporate.

The decisions in the English system in which principles of equity developed in relation to partnership proper have been resorted to in order to bring about justice between the corporate partners other than by dissolution of the body corporate, are but few in number. As such they stand in sharp contrast to the vast body of American case law dealing with corresponding issues and principles and the body of case law in the English system applying those very principles to justify corporate dissolution. In Scotland these principles were resorted to in *Harris*[1054] in order to test the propriety of shareholders voting in a particular way, and in *Scottish Co-op.*,[1055] in order to determine whether in siphoning off partnership opportunities to themselves and starving the incorporated partnership to death, corporate partners were acting oppressively *vis-à-vis* their fellow corporate partners. In South Africa those principles were employed in *Bellairs*[1056] to determine whether a corporate partner was liable to account for profits arising from corporate opportunities usurped by him, and, as in *Super Safes*[1057] are likely to influence the question whether a restraint of trade clause is reasonable between corporate partners. In England again, those

principles/ .....

principles are likely to assist a corporate partner in enjoining the implementation of a proposed rights issue, as in *Pennel*,[1058] or in having the resolutions authorising a further issue of shares, set aside, as in *Clemens*,[1059] when the issuing of further shares is in disregard of the legitimate interests of a fellow corporate partner. This may be the case because a particular corporate partner has not been invited to participate in the rights issue. This would also be the case where a corporate partner, is, to the knowledge of those proposing the rights issue, unable to participate, but it is possible to acquire the required further capital in a different manner. However, there is no reason why the application of the said principles of equity should be restricted to the narrow range of situations enumerated above. The courts should here heed the criticism voiced by Lord Wilberforce that they have been "too timorous" in the past in applying, in effect, principles of equity developed in relation to partnership proper.[1060]

The decisions in the quasi-partnership company line of cases make it clear that principles of equity developed in relation to partnership proper are the appropriate standard for determining whether conduct of one corporate partner *vis-à-vis* a fellow corporate partner constitutes such a serious encroachment of their inter se relation as to warrant the most extreme relief, namely dissolution of the statutorily created right-and-duty-bearing unit. As such these decisions underline the extreme importance which the judiciary attaches to the personal, fiduciary character of the inter se relation between members of the incorporated partnership. Such a high premium is in fact placed upon the personal character of the relation in question that the very corporate existence is subordinated to the personal character of the said relation. When, because of the less serious nature of an encroachment of that relation

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ordinary fiduciary relief would be more appropriate than the extreme relief, corporate dissolution, those very principles of equity developed in relation to partnership proper should, *a fortiori*, be the appropriate norm determining the propriety of the conduct in question.

The time for the general acceptance of this conclusion in the English system has arrived. The current proposals[1061] for the statutory introduction of yet a further *tertium quid*, an incorporated partnership proper which is to exist separate and apart from the incorporated company, are ringing in a new era. In a sense history is repeating itself. For as Cooke has aptly observed in an earlier context:

> "This, indeed, has been the usual course of company legislation; it follows the growth of the company. It does not invent a new form".[1062]

These proposals, if implemented, would destroy the conceptual fetter which has for so long impeded English legal thought in this regard. This shackle is the notion of the unity of the English incorporated company. The creation by the legislature of a separate statutory regime for the incorporated partnership should encourage a greater willingness on the part of the judiciary to apply principles of equity developed in relation to partners proper to the corporate partners. The fear voiced by Lord Wilberforce that principles of company law and partnership law might be confused for one another, and that principles of partnership law might swamp company law and undermine its independent existence, will then have been put to rest.

CHAPTER IX

SUMMATION AND CONCLUDING REMARKS

23. *SUMMATION*

1. Corporate status and inter se lateral relations are not mutually exclusive concepts. Corporate status concerns the relations of laterally related persons, *i.e.* associates, who, viewed as a right-and-duty-bearing unit, face the world at large. Inter se relations concern the relations of laterally related persons when they face one another only and not the world at large.

2. Inter se relations may be strictly business-like, impersonal arms' length relations, or may, conversely, be intimate, close personal relations. A relationship of the former type is properly denoted as an *intuitus pecuniae* relationship. Because the inter se lateral relation in such event is not a fiduciary relation, it does not give rise to inter se fiduciary duties. A relationship of the latter type is properly denoted as an *intuitus personae* relationship. Because the inter se lateral relation in such event is a fiduciary one, it gives rise to inter se fiduciary duties. Relations of the former type are found in a corporation or public-issue company while relations of the latter type are found in partnership proper.

3. An incorporated partnership combines characteristics of both types. *Vis-à-vis* the world at large, the laterally related associates are a body corporate or right-and-duty-bearing unit. Inter se, such associates are associated

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in a close, personal, fiduciary relation. Such association exists because the associates repose confidence in, and trust, one another. Such an association continues to exist only because the associates continue to repose confidence in, and trust, one another.

4. The incorporated partnership is found in all legal systems dealt with above. In the American system it co-exists with the close corporation. It is found in German law as a variation of the G.m.b.H. and in French law, as a variation of the S.à.r.l. to the extent that the *associés* have associated *intuitu personae*. And in the English system, the incorporated partnership finds expression in the statutory, private company.

5. In all these legal systems the inter se relation of corporate partners is, at the lowest, recognized as a personal relation. In American and German law, it is further commonly accepted that the close or intimate, personal relation must necessarily also be a fiduciary relation, which gives rise to inter se fiduciary duties. Here the fiduciary norm governs the inter se relations of the corporate partners in all spheres. In the English system the judiciary has not been consistent in this regard. Here the close and intimate personal character of the inter se relations of corporate partners is freely recognized under the statutory just and equitable winding-up provision for the purpose of winding-up the statutorily created right-and-duty-bearing unit. Yet when the enforcement of inter se fiduciary duties between corporate partners is called for, these same courts are generally loathe to give recognition to that very character of the said relation which they eagerly recognize for decreeing the extreme remedy, winding-up.

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6. The basic partnership character of the English incorporated company in general and the precedent established in the quasi-partnership line of cases under the statutory just and equitable winding-up provision in particular, afford the judiciary in the English system far greater justification than, for instance, the American judiciary has ever enjoyed for recognizing and enforcing inter se fiduciary duties between corporate partners.

7. In line with a universal trend, the general recognition of inter se fiduciary duties operating between corporate partners is inevitable in the English system. This is more likely to happen sooner than later. A trend in this direction is already noticeable in the case law developments of the last decade. Britain's entry into the European Common Market and its efforts to harmonize its laws with that of its European partners, will certainly encourage this trend. This is borne out by the recent Green Paper, *A New Form of Incorporation for Small Firms*[1063] published early this year in the wake of the statutory abolition in Britain of the traditional English concept of the statutory private company. It proposes the statutory recognition of the incorporated partnership. Scots law and South African law in particular, with their Continental leanings, should not experience any discomfort in this regard. At the same time it is only to be hoped that the judiciary in the English system will in future seek guidance from the time - and experience - tested American precedents, which cover a wide range of situations. Basically the principles in this particular field are compatible in all legal systems, particularly in so far as they concern the inter se relations of corporate partners. In all the legal systems in question, the incorporated partnership is but a twentieth-century version of a common prototype, the Roman *societas*. And it is essentially

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the basic notion of *fides* which developed in that context which is shared in and treasured by all civilized legal systems.

24. *CONCLUDING REMARKS*

1. The incorporated partnership is, as a type, *sui generis*. It is neither a corporation pure and simple, nor a partnership proper, pure and simple. It is at one and the same time both a corporation and a partnership which have coalesced into a single new type, the incorporated partnership. With regard to the world at large the corporate partners are a right-and-duty-bearing unit. Inter se they are fiduciaries.

2. The status of a corporate partner is *sui generis*. Its development in this regard parallels the development of the office of company director. Originally the company director was seen as but a corporate agent or trustee. Today both the office of director and the fiduciary duties emanating from that office are regarded as *sui generis* so that less and less reliance is being placed on the notions of agency and trust in that regard.

3. Corporate partners are fiduciaries because they are corporate partners, that is, because their inter se relation has been concluded *intuitu personae* and is therefore steeped in mutual good faith and confidence and not because of any other fact. It is not correct (as suggested by some courts and commentators) that members of an incorporated company are fiduciaries because, a court discovers, having pierced the corporate veil, that the corporators are in fact partners. Veil piercing is essentially resorted to in order to lay bare, by by-passing the existence of the right-and-duty-

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bearing unit, the relation between corporators and third parties. Inter se, corporators stand in a fiduciary relation and it is not necessary to resort to veil piercing to give effect to the fiduciary incidents of such relation.

It is true that the definition of corporation (or incorporated company) and partnership proper, respectively, could be couched in such wide terms that, *ex definitio*, a corporation is a partnership, and *vice versa*. But such wide definitions are not likely to be particularly meaningful. Moreover, the fact that *ex definitio* a corporation may also be a partnership, does not necessarily imply that such corporation will be governed by partnership law as well. The truth of the matter is, that because an incorporated partnership is incorporated in terms of an enabling statute, it will be governed by the provisions of such statute and no longer by the statute (or, in South Africa, the common law) relating to partnership proper. That is however, not to say, that corporate partners may not inter se be fiduciaries *as if* they were partners proper.

As in partnership proper, corporate partners will be inter se fiduciaries if their inter se relation has been concluded *intuitu personae* and is therefore steeped in mutual good faith and confidence. Whether this is so or not will inevitably be a question of fact to be determined in the light of all the circumstances of each particular case. The requisite intention here might, but need not, stand revealed in an express provision in that regard in a shareholders' agreement to the effect either that the relation between the corporators shall be *uberrima fidei* or that the inter se relation between the corporators shall be such *as if* they were partners.

To say that partnership survives incorporation does not,

however/ .....

however, imply that partnership and corporation co-exist, separate side by side in symbiosis, as it were. In the incorporated partnership corporation and partnership, as symbionts, become one if in fact the undertaking of the corporation is co-extensive with that of the partnership. It is for this reason that courts correctly treat corporate partners not as partners but *as if* they *were* partners and apply the principles of equity developed in relation to partnership proper by analogy. It is possible that the fiduciary duties owed by corporate partners will ultimately be determined without reference to the analogous duties owed by partners proper. Yet it is more than likely that the principles of equity developed over very many centuries in relation to partners proper will, because of the extensive judicial experience pent up in those principles, for a long time to come continue to serve as the norm, governing the inter se relations of corporate partners. The norm in question is a flexible norm. Its dictates are determined by the conceptions and notions of justice, fairness and propriety of the particular society and a particular age which cares to apply them.

4. The fiduciary norm has served partnership proper well. There is no reason why it should not do the same for the incorporated partnership. The fact that company members are not treated as fiduciaries in the English system explains the elaborate, but largely inadequate, statutory provisions, which are found in Annexure B pts. 1 to 3 and which are aimed at combatting oppressive conduct. The fact that partners proper are treated as fiduciaries explains why it has never been necessary to introduce a similar statutory provision in partnership law. What is called for is not more statutory regulation but less. The danger is well expressed by the

adage/ .....

adage *expressio unius est exclusio alterius*. The basic and statutory provision should be that corporate partners are fiduciaries inter se. Provisions on the lines of those found in Annexure B pt.5 could be supplemental to that basic tenet. Equity will take care of the rest.

EXCURSUS I

JURAL RELATIONS

Part 1 INTRODUCTION

The importance of the jural or legal relation is, because of its conceptual nature, not always readily appreciated.[1064] Yet, as Kocourek emphasizes, "no legal phenomenon can exist without dealing with one or more jural relations".[1065] In fact "[t]he idea of a jural relation is as fundamental for legal phenomena as is the idea of gravitation for physical phenomena".[1066] Pound concurs. In his view the idea of a legal relation, is, as a legal concept, at least as important as the idea of the will and of the legal transaction.[1067] These views are particularly apposite in the context of the law of corporations or companies. Here the popular view appears to be that corporate status contradicts the existence of inter se legal relations between corporators.

A classification of legal relations which is particularly meaningful in the sphere of associations and corporations is one which distinguishes between associative and non-associative relations. This distinction hinges on the relative positions of the interests of the parties that are linked together by the particular relation. The interests of such

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1064. Kocourek *Jural Relations*, *supra* n.40, iii.

1065. *Id.*, at v.

1066. *Id.*, at iii.

1067. 1 *Jurisprudence*, *supra* n.17, at 210.

parties may either be equal and on par, or unequal and the one party's subjugated to that of the other. From this point of view it is convenient to refer to an associative relation as a lateral relation and to a non-associative relation as a vertical relation. It will be found that this classification is indicative of the nature and object of the fiduciary duty owed by the parties to a particular relation if such relation happens to be a fiduciary relation in addition.

Part 2 *THE VERTICAL OR NON-ASSOCIATIVE RELATION*

Trust, agency[1068] and directorship are prime examples of this type of relation. While agency is of a contractual nature, trust is proprietary, the former involving the power to alter legal relations between the principal and third parties, the latter merely the holding of property. A consequent difference is that while the principal has a direct right of control over the conduct of the agent, the *cestui que trust* has only an indirect right to hold the trustee to the terms of the trust. Directorship, on the other hand, involves some aspects of both agency and trust, perhaps more of the former than the latter. Today, however, it is regarded as an office *sui generis*. With regard to the subject matter of the relation, the interests

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1068. Both these concepts developed from the same idea which found expression in the Latin *ad opus* "on behalf", which in old French became *al oes, ues* and in English mouths *use*, the latter being the forerunner of the present day trust. See Scott, *On Trusts, supra* n.834, at 74 and Maitland, *Equity* (reprinted ed. 1969) 24. The link between agency and the Roman Law *mandatum* appears to be tenuous except for the latter's influence upon the fiduciary nature of the relation between principal and agent. In the equitable joint stock company trust and agency blended together to give birth to the office of director.

of the one party, the *cestui que trust*, principal or company, are preferred to the interest of the other, the trustee, agent or director, respectively. This disparity of interests has a number of important consequences.

First, in terms of this relation the party with the non-preferred interests, *viz.* the trustee, agent or director — the fiduciary in other words — must, within the scope of the relation, subjugate his interest to those of the party with the preferred interests, *viz.* the *cestui que trust*, principal or company — the beneficiary, in other words.[1069]

Second - this necessarily results from the first - the fiduciary duty which flows from such a relation is not a mutual one owed reciprocally by the parties thereto. It is a one-way duty owed only by the fiduciary to the beneficiary. Thus the agent owes a fiduciary duty to the principal, the trustee to the *cestui que trust* and the director to the company, and not *vice versa*.

Third, perhaps an equally important result, the incompatibility of the disparate and unequal interests of the parties to the relation, the fiduciary and the beneficiary, rules out any coalescence of those interests. The very act of uniting the disparate interests with which the relation is concerned, would extinguish, and thus terminate, the relation just as the union of the interests of debtor and creditor would appear to extinguish the relation between debtor and

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1069. Weinrib, *The Fiduciary Obligation*, (1975) 25 U. Toronto L.J. 1, 15 and 17, refers to the fiduciary duty flowing from this relation as "a device for controlling and purifying the exercise of a discretion" by the fiduciary.

creditor. The implication of this for the law of associations is obvious: a vertical relation which cannot be incorporated as a right-and-duty-bearing unit or as a body corporate.

Part 3. THE ASSOCIATIVE OR LATERAL RELATION

3.1. GENERAL

The various types of associative relations which exist, may be grouped together in what one commentator calls a graduated hierarchy.[1070] Before considering these it would be helpful to isolate and identify the characteristic which is common to all of them.

The distinctive feature of the associative or lateral relation is that the interests of the persons linked together in association with one another are neither subjugated nor preferred but equal and on par.[1071] This parity of interests has a number of consequences. The first and foremost feature of this relation is that the fiduciary duty emanating from it is a mutual, two-direction, one flowing inter se the persons related to each other in the association.[1072]

1070. Drake, *Partnership Entity And Tenancy In Partnership, The Struggle For A Definition, supra* n.41, at 611.

1071. From a qualitative but not quantitative point of view. Thus one associate may quantitatively hold more shares in the association than another but that does not detract from the fact that from a qualitative point of view, they are equals. This feature is absent from the vertical relation.

1072. When Weinrib, *The Fiduciary Obligation, supra* n.1069, at 15, 17, 18, 20 and 21 refers to a fiduciary duty as a "device to protect the integrity of commercial organizations" or as a "device for the maintenance of business structures", he appears to have this type of duty in mind.

Second, this parity of interests brings about a compatibility, a natural inclination towards the union of the qualitatively equal interests by the incorporation thereof as a corporate person. And in the graduated hierarchy of associative relations, the association enjoying corporate personality, represents the ultimate evolution.

3.2. THE HIERARCHY OF ASSOCIATIVE RELATIONS

The lowest order in this hierarchy is occupied by the least complicated associative relation, namely group tenure. It consists, for instance, of *A* and *B* who are associated together in holding property. The fundamental characteristic is the passive right of group tenure.[1073]

A higher order in this hierarchy is occupied by partnership. It consists, for instance, of *A* and *B* who are associated together for the purpose of gain. Since approximately the Middle Ages, active group or associative activity has been characteristic of this relation.[1074] At the same time the lateral and vertical relations began to link up in symbiotic union — for which see pt. 4 hereunder. Above this order of unincorporated partnership classes towers the partnership classes enjoying corporate personality. At this level the lateral or associative relation between say *A*, *B* and *C*, is, unlike the associative relations found at lower

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1073. Drake, *Partnership Entity And Tenancy In Partnership, The Struggle For A Definition, supra* n. 41, at 611-2. As an example of this relation Drake cites *condominium* of Roman law and joint tenancy of Common Law. The consortium of co-heirs, the *ercto non cito* of the *ius civilis* — for which see n.25 above — appears to be another example.

1074. *Ibid.*.

orders, telescoped as it were, into a right-and-duty-bearing unit, a *persona ficta*, say *X*. Here the fundamental characteristic is *legal* or *corporate personality*.

Of all the theories which seek to explain corporate personality, Ihering's expansible symbol — or, as Maitland[1075] happily dubs it, *bracket* — theory is the most successful in highlighting the connexion between jural relations and the concept body corporate or right-and-duty-bearing unit. The essence of Ihering's bracket theory is that only human beings, say *A*, *B*, *C*, etc., can be bearers of interests and rights, that is, be the subject of jural relations. *X*, the *persona ficta* of the corporation is but a legal device or formula -- "a mere labour saving device like stenography or the mathematician's symbols"[1076] — to enable complex jural relations to be more readily understood.[1077] It involves the putting of a bracket around the individual associates in order to treat them as a body corporate, that is a legal unit. *X*, in other words, represents the aggregation of *A*, *B*, *C*, etc . as a unit entity, as in *X* = (*A* + *B* + *C*, etc.). Maitland once said, as he referred to this theory:

> "In America where law schools flourish, where Supreme Courts are many and the need for theory is more urgent than it is in England, highly interesting attempts have been made to dispel the Fiction or rather open the Bracket and find therein nothing but contract-bound men".[1078]

1075. *Political Theories*, *supra* n.151, at xxiv.

1076. *Ibid.*

1077. Paton, *A Textbook Of Jurisprudence*, (4th ed. 1972), para 90.

1078. *Political Theories*, *supra* n.151, at xxiv.

In truth, the bracket exists from the point of view only of the associates being a right-and-duty-bearing unit. Inter se it does not exist; in that regard the associates stand in a direct, lateral or associative, relation to one another.

Part 4 *SYMBIOSIS INVOLVING LATERAL AND VERTICAL RELATIONS*

With the development of the non-associative vertical relations, *viz.* agency and trust in the Middle Ages new horizons opened up for expansion in a different dimension on this level: associative and non-associative relations could be joined in symbiotic union.

Agency was resorted to for purposes of conducting active group or associative activity both in partnership proper and in the outsize partnership, the burgeoning equitable joint stock company. Thus, for instance, the laterally associated *A* and *B* were, for purposes of their association, both principals and agents. Gradually this became the rule so that in the absence of agreement to the contrary, every partner had a right to represent and bind the partnership, so much so that mutual agency has become one of the characteristic features of partnership proper today. The proprietary trust device was again invoked in connection with passive group holding tenure. Owing mainly to *delectus personae* and the limitation it placed on the number of members an association may have, joint tenure was no serious problem in partnership proper. Not so with the large partnership stripped of *delectus personae*. Here the virtually unlimited number of members an association may have, made the introduction of a small number of trustees, say T_1, T_2, and T_n, in whom the realty and, later the business of the association could be vested, a practical expediency. Expediency turned into

necessity when the Common Law insisted that an unincorporated group of persons could not own property as a group. Invariably these trustees were managing partners of the company. In due course these trustees became known as the directors of the company. This symbiosis between a lateral or associative relation and a vertical or non-associative relation found expression in a variety of forms, one of the most interesting of which is the business trust or the Massachusetts trust, found in the United States. This "association" is distinguishable from partnership in two main respects. First, in that as regards the world at large, the associative or lateral relation between *A, B, C, etc.*, the *cestuis que trust*, is treated as having almost completely withered away, leaving virtually only the vertical relation between, on the one hand, T_1, and T_2, *etc.* the trustees, and *A, B, C, etc.*, the *cestuis que trust* on the other hand, intact. Inter se the *cestuis que trust* do of course still stand in a lateral or associative relation. Second, in that *A, B, C, etc.*, the *cestuis que trust*, are free from all personal liability while the trustees are liable in their place but then only to the extent of the trust fund. This prompted Gower to observe that this almost corporate-like refinement which was attained by the Massachusetts trust but which England never succeeded in achieving, represents the "final evolution of the unincorporated company".[1079] Concludes Maitland: "So now-a-days the American trust (in the sense in which economists and journalists use that term) is almost always if not quite always a corporation".[1080]

1079. Gower, *British and American Corporation Law*, *supra* n.24, at 1373.

1080. *Collected Papers*, *supra* n.39, at 395.

Part 5. CONFUSING LATERAL FOR VERTICAL RELATIONS

It is sometimes said that partnership is but agency. That this cannot be so is revealed by the distinction between lateral and vertical relations. It is true that partnership and agency can link in symbiosis and that mutual agency has since the Middle Ages become a characteristic of partnership This does not, however, make partnership a vertical relation or equate it with agency. This point is often overlooked.

In the Scottish decision *Morrison* v. *Service*,[1081] for instance the eminent Clark, Sheriff Principal of Lanarkshire, as he then was, said:

> "One of the strongest tests of the partnership relation is the existence of mutual agency, by which any one of the alleged partners has the power of binding his fellows of the concern with third parties. This is indeed aptly expressed in the civil law by the brocard, *contractus societatis non secus ac contractus mandati* ...."[1082]

The appeal to the so-called Civil Law brocard is misplaced and appears to have been inspired by Story who misquoted Pothier[1083] in this particular instance. "Pothier", Story suggested, "considers partnership as but a species of mandate saying: *Contractus societatis non secus ac contractus mandati*".[1084] From this passage it may seem that partnership is simply a *vertical* or non-associative relation like

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1081. *Supra* n. 705, at 1158.

1082. *Id.*, at 1160.

1083. *Pandectae* 17, 2, Intr..

1084. *Partnership, supra* n.28.

the one which subsists between principal and agent. This it is not and it becomes clear that this is not what Pothier said or implied in the particular text when Pothier's original work is consulted. What Pothier in fact said was *"Contractus Societas, non secus ac contractus mandati, ex eorum est numero contractuum qui nudo consensu perficiuntur. Quapropter Titulo Mandati subjicitur hic Titulus PRO SOCIO"*, that is, that the contract of partnership does not differ from the contract of mandate, in the sense that both of them are among those contracts which are concluded by mere consent and that it is, therefore, convenient to discuss partnership after mandate. In fact, if Pothier, *Traité du Contrat de Société*,[1085] Ch. I, § 3 is consulted, it is clear that Pothier himself distinguished clearly between partnership and mandate on the basis of equal and preferred interests. "[I]t is essential in this contract", Pothier said, "that the partnership should be contracted for the *common interest* of the parties. When, in an agreement, the *private interest* of one of the parties only is regarded, it is not a Contract of Partnership, but a contract of mandate ...." Fortunately there are courts which have treated the relationship between agency and partnership in its proper perspective. A case in point is the American decision *Meehan* v. *Valentine*.[1086] Here Mr. Justice Gray after citing and discussing the above-quoted lines from Story held:

> "[A]s has been pointed out in later English cases, the reference to agency as a test of partnership was unfortunate and inconclusive, inasmuch as *agency results*

1085. *Supra* n.48.

1086. 145 U.S. 619 (Cir. 1892).

> *from partnership rather than partnership from agency* ... Such a test seems to give a synonym, rather than a definition; another name for the conclusion, rather than a statement of the premises from which the conclusion is to be drawn. To say that a person is liable as a partner, who stands in the relation of principal to those by whom the business is actually carried on, adds nothing by way of precision, for the *very idea of partnership* includes *the relation of principal and agent*".[1087]

What is important in all these instances is to determine in what particular capacity the person concerned has acted. The crucial issue is whether the partner, or corporate partner, in question acted as principal in his own right or whether he acted as agent on behalf of the unincorporated partnership or director on behalf of the incorporated partnership. If the partner or corporate partner, as the case may be, acted as agent or director, the question is whether he has, as such, breached his non-reciprocal fiduciary duty. This duty arises from the vertical relation in that regard and is owed to the (unincorporated) partners *qua* principals, or, as the case may be, the incorporated partnership, *qua* principal. If, on the other hand, the partner or corporate partner, as the case may be, acted as principal in his own right, the question is whether he has, as such, breached the reciprocal fiduciary duty owed inter se the partners, or as the case may be, corporate partners, which arises from their inter se lateral, fiduciary relation. The notion that partnership is but a species of agency is unfounded. Equally unfounded is the related notion that partners proper and corporate partners owe fiduciary

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1087. *Id.*, at 622. (Italics added.)

duties only when they act as agents *qua* the partnership. Partners proper and corporate partners, in truth, owe fiduciary duties because they stand in a personal, fiduciary lateral relation to one another. The said lateral relation is a personal, fiduciary relation because it is concluded *intuitu personae*.

EXCURSUS II

INTUITUS PERSONAE

Part 1 INTRODUCTION

Associative relations may be classified into two types. They are either close, intimate personal relations, or arm's length impersonal relations. Relations of the first type are of a fiduciary character and give rise to inter se fiduciary duties. Relations of the second type are not of a fiduciary character and therefore do not give rise to fiduciary duties. The term *intuitus personae* is associated with the first type while the term *intuitus pecuniae* associated with the second type of associative relation.

As the term indicates, the concept *intuitus personae* is of Roman origin. In the twentieth century the concept has received the most attention in French law. Valleur, for instance explains the concept in the following terms:

> *"'Intuitus personae'—littéralement 'contemplation considération de la personne—cette expression indique d'après le Vocabulaire Juridique, que la considération de la personne avec laquelle on a contracté a déterminé le consentement du ou des contractants".*[1088]

The prime example of a contract of this type cited by the author is the *société de personnes*.

Jeandel, another French jurist, highlights the role of *intuitus personae* in the *société de personnes*. He explains the connection between these two concepts in the following terms:

> *"Les sociétés du premier groupe [sociétés de personnes] sont appelées sociétés de personnes parce que, dit-on, elles reposent sur l'intuitus personae, c'est-à-dire sur la considération de la personne".*[1089]

1088. *L'Intuitus Personae dans les contrats* (1938), para. 1.

1089. *L'Intuitus Personae dans les Sociétés Commerciales, supra* n. 32, at 5.

In French law the converse of a *société de personnes* is a *société de capitaux* or a capital-orientated association. Unlike a *société de personnes*, a *société de capitaux* is not concluded *intuitu personae*. It is concluded *intuitu pecuniae*. In the words of Jeandel:

> "*Les sociétés du deuxième groupe sont appellées au contraire sociétés de capitaux, parce qu'elles reposent sur l'intuitus pecuniae, c'est-à-dire sur la considération de l'apport fait en société*".[1090]

In this sense the dichotomy *intuitus personae* and *intuitus pecuniae* parallels the dichotomy personal, close, confidential inter se relations and impersonal, arm's length, capital oriented inter se relations. The former is characteristic of partnership proper, the latter of corporation.

Today the concept *intuitus personae* is not only still in use in Civil Law jurisdictions on the Continent, but it is also known in Common Law and hybrid jurisdictions by the name of *delectus personae*. (Strangely enough one searches in vain for either of these terms in South African law.) And while the term, *intuitus personae*, or its equivalent, *delectus personae*, is not used as freely in this context in English or American law as it is used, say in French law, the notions of mutual confidence and trust, which are implicit in these notions, have been developed to their fullest in the latter jurisdictions. Here an inter se associative relation which has been concluded *intuitu personae* is treated not only as a personal, confidential relation but also as a fiduciary relation.

1090. *Id.*, at 6.

Part 2 *A HISTORICAL AND COMPARATIVE ASSESSMENT OF THE CONCEPT INTUITUS PERSONAE*

Van Warmelo gives the following account of *intuitus personae* in Roman law:

> "The *societas* was created *intuitu personae, i.e.* between specific partners and no others. The partners were supposed to have *confidence in each other* and the partnership lasted as long as those parties are members of it. If one were to die or resile, the partnership was brought to an end".[1091]

It is significant that Van Warmelo does not explicitly state that if the mutual confidence resulting from *intuitus personae*, broke down, the *societas* could be terminated by a *socius*. Yet it is more than likely that a breakdown of mutual confidence was a ground for dissolving a *societas* even in classical Roman law. In the following passage Cicero makes it clear how highly mutual confidence was rated in *societas:*

> *"In rebus minoribus socium fallere turpissimum est; neque injuria; propterea quod auxilium sibi se putat adjunxisse, qui cum altero rem communicavit. Ad cujus igitur fidem confugiet, cum per ejus fidem laeditur, cui se commiserit? Atque ea sunt animadvertenda peccata maxime, quae difficillime praecaventur. Tecti esse ad alienos possumus; intimi multa apertiora videant necesse est. Socium vero cavere qui possumus? Quem etiam si metuimus, jus officii laedimus. Recte igitur majores eum, qui socium fefellisset, in virorum bonorum numero*

1091. *An Introduction to the Principles of Roman Law*, *supra* n.79, at para. 496. (Italics added.)

non putarunt haberi oportere".[1092]

The reason why even the most minor act of deceit between *socii* was viewed as an extreme depravity was, as Cicero explains, because of the inter se mutual confidence and trust between the *socii*. In whom could a partner then repose confidence, Cicero asks, if one's fellow partner to whom one had entrusted one's faith, shocked one's confidence? To mistrust one's partner, Cicero correctly observes, is to be in breach of one's duty to him. It is for this reason that the ancients, according to Cicero, viewed an unfaithful partner as someone who should be ostracized. Whatever the position might have been in classical Roman law, it is clear that in the modern law a breakdown of confidence affords a just ground for terminating the personal relation which is partnership.[1093] In Roman Law it was not possible to exclude the operation of that principle by stipulation. Thus, for instance, it was not possible, even at the commencement of the partnership, to stipulate that the heir of any of the partners who happened to die during the continuance of the partnership would become a partner in the place of the deceased.[1094] Why this was so is explained by Pothier in the following passage:

1092. *Pro Roscio Amer.* c.40. *cited by*, *Pufendorf*, *op.cit.*, 5,8.4. by Collyer, *On Partnership* (1832), 95 and by Story, *Partnership*, *supra* n.28, at § 172.

1093. In *Fortune*, *supra* n.800, at 348, for instance, it was held with reference to a number of Civil Law authorities that ~~any~~ misconduct on the part of one partner ~~which~~ irretrievably shatters the mutual confidence, which is supposed to exist inter se partners justifies dissolution of the partnership.

1094. Digest 17, 2, 59 *noted by* Pothier, *Traité du Contrat de Société*, *supra* n.48, at para. 145.

> "[P]artnership being a right which is *founded upon the friendship of the parties for each other and upon the reciprocal confidence which each has in the fidelity and good qualities of the other*, it was contrary to its nature that it could be contracted with an uncertain and unknown person and consequently with the heirs of the contracting parties ".[1095]

What is particularly significant in the above passage is the connection between mutual confidence and *intuitus personae*. In Pothier's opinion, however, the rule was no longer to be applied as rigidly in the modern law of his time as it was applied in Roman law for instance. This is apparent from the following passage:

> "[I]n our law, although the partnership regularly terminates by the death of one of the partners, and his heir does not succeed him in the future rights of the partnership, nevertheless, a stipulation that he shall succeed is binding".[1096]

Once it was settled that a stipulation that an heir of a partner would succeed him was enforceable, the law was well advanced on the road towards permitting partners to dispense with the requirement that new partners were only to be admitted with the concurrence of all existing partners. This development ultimately resulted in the evolution of the impersonal, capital-oriented *société de capitaux*, *Kapitalgesellschaft* or the public-issue corporation. The necessity for

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1095. *Traité du Contrat de Société*, *supra* n.48, at para. 145. [Present author's emphasis.]

such a provision obviously arose from the need for some partnerships to acquire substantial working capital to fund their operations and normally such necessity would stand in direct proportion to such need.

This was patently the case in the large or gigantic partnership with its freely transferable interests. Such an association would not be concluded *intuitu personae*. It would be concluded *intuitu pecuniae*. In that event mutual confidence and good faith will obviously no longer mark the inter se relation of members. But the fact that it thus became possible to introduce the principle of freely transferable shares into the gigantic partnership, did not at the same time imply either the extinction of the concept *intuitus personae* or the deterioration of the personal character of the inter se relation in the private partnership or partnership proper.

Thus, for instance, the concept *intuitus personae* is still found today in French law, where it is seen as the foundation of the personal character of the partnership relation. Ripert, discusses this character as follows:

> *"Le droit de l'associé est dominé par le contrat qui l'a créé. Or ce contrat a été conclu intuitu personae De son origine le droit tient un caractère personnel. Les associés s'accordent une confiance réciproque; ils ne sauraient admettre que l'un d'eux sorte du contrat et y fasse entrer un tiers à sa place. C'est dire que la part est en principe incessible, ou plutôt qu'elle n'est cessible qu'avec le consentement de tous. La société, comme tout contrat conclu en considération de la personne, prend fin lorsque l'un des contractants*

disparaît ou perd l'exercise de ses droits. Par là, encore, s'accuse le caractère personnel du droit".[1097]

The concept *intuitus personae* is also found in German law today and in most other Civil law jurisdictions on the Continent.[1098] The idea underlying the concept *delectus personae* apparently became familiar in the United States, through Story. Here, though, it is referred to as *delectus personae*, which according to Story, is essential "to the constitution of the partnership".[1099] Today the principle is enshrined in U.P.A.*§§* 18(g) which provides that "[s]ubject to any agreement between the partners ... no person can become a member of a partnership without the consent of all the partners". As is observed by Crane and Bromberg, the principle thus codified usually goes by the Latin label *delectus personae*. These authors view this notion as "representing one's right to be particular who his partners are" and describes it as "an abstract characteristic of the partnership relation which may be watered down in practice".[1100]

It is, however, the American judiciary which has developed the notions of mutual confidence and trust which necessarily

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1097. *Traité Élémentaire de Droit Commercial supra* n.32, at para. 742.

1098. See Zweigert, *The Private Limited Company, supra* n.7, at paras. 5, 6, 18 and 48.

1099. *Partnership, supra* n.28, at § 5. Story notes that the Common Law, like Pothier and Scots law but unlike Roman law, treats a stipulation to admit the heir of a partner into partnership as valid and obligatory.

1100. *On Partnership, supra* n.367,5c, at 43-44. These authors further point out that the requisite consent may be given or waived by conduct or given in advance by agreement.

accompany *intuitus personae* almost to perfection. The *locus classicus* in this regard is the following passage in which Mr. Justice Cardozo, in almost Ciceronian terms, described the personal character of the inter se relation between partners:

> "Joint adventurers, like co-partners, owe to one another, while the enterprise continues, the duty of the finest loyalty. 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 stricter than the morals of the market place. Not honestly alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the disintegrating erosion of particular exceptions".[1101]

Observe the explicit reference to "arm's length" relations and the implicit reference to close, personal, *intuitus personae* relations. That the principles of equity developed in Roman law with regard to *societas* played a role in the development of similar notions in American law, through Story, is evidenced by the following passage from an opinion of Mr. Justice McFaddin:

> "In Story on 'Partnership', the author traces the duties of partners *inter se* from the Roman Republic to the present time.... The necessity of entire good faith,

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1101. *Meinhard* v. *Salmon* 249 N.Y. at 464, 164 N.E. at 546, 62 A.L.R. at 4-5 (1928). In *Hodnett, supra* n. 920 at 119 Botha, J., cited this passage making special mention of the fact that it was couched in "beautifully arresting language".

and of the absence of fraud on the part of partners towards each other, is inculcated by Cicero in terms of deep import and sound morality. Good faith not only requires, that every partner should not make any false representations to his partners, but also that he should abstain from all concealments, which may be injurious to the partnership business".[1102]

The *rationale* of this notion is that a partnership is concluded *intuitu personae* and that the partners consequently repose confidence and trust in one another. In Scotland, too, the term *delectus personae*, rather than *intuitus personae*, is used. An early Scottish commentator, Erskine, highlighted the notion *fraternitas*, *i.e.* close, intimate relations in the concept *delectus personae* as follows:

"As partners are, from a *delectus personae*, or the reciprocal choice they make of each other, united in a kind of brotherhood, no partner could by the Roman Law transfer his interest or share in the society to a third person, without the consent of the company".[1103]

It will be recalled that Bell, another Scots jurist, described *delectus personae* as being inseparable from the fiduciary character of partnership.[1104]

1102. *Alexander* v. *Sims*, 249 S.W. 2d 832, 836 (Ark. 1952). Here it was held that a partner, selling his partnership interest to a co-partner, is obliged to observe the utmost good faith.

1103. 3 *Institute* 3:22 *cited by* Miller, *Partnership*, *supra* n.56, at 17. The reference to brotherhood is clearly inspired by the Roman notion of *jus fraternitas* — see n.82 above — and is indicative of a fiduciary obligation. Observe too the use of the word "company" in the sense of "partnership".

1104. *Supra* n.77.

While the term *delectus personae* is not in common use in England, the concept is, however, not unknown. Regarded as one of the fundamental principles of partnership law, it is expressly recognized by the *Partnership Act*, 1890,[1105] §§24(7) which requires that no person may be introduced as a partner without the consent of all existing partners. Again the operation of this principle may be excluded by agreement, whether express or implied, between the partners. The rule, according to *Lindley*, appears to flow from the presumed intention of the partners, which usually is that the partnership should exist between themselves and themselves alone. *Lindley* explains the underlying *rationale* in these terms:

> "The mutual confidence reposed by each in the other is one of the main elements in the contract, and it is obvious that persons may be willing enough to trust one another, yet be unwilling to place the same trust in anyone else".[1105]

An English Vice Chancellor neatly summed it all up when with obvious reference to *delectus personae* in partnership, he stated that partners' mutual confidence is the very life blood of the partnership; that it is because the partners trust one another that they are partners at all and that it is only because they continue to have confidence in one another that the partnership carries on.[1106]

1105. *Supra* n.62.

1106. Bacon, V.C., in *Helmore*, *supra* n.114.

ANNEXURE A

Part 1

NORTH CAROLINA BUSINESS CORPORATION ACT, 1955, §§55-73(b)

Except in cases where the shares of the corporation are at the time or subsequently become generally traded in the markets maintained by securities dealers or brokers, *no written agreement* to which all of the shareholders have actually assented, whether embodied in the charter or bylaws or in any side agreement in writing and signed by all the parties thereto, and which relates to any phase of the affairs of the corporation, whether to the management of its business or division of its profits or otherwise, *shall be invalid as between the parties thereto, on the ground that it is an attempt by the parties thereto to treat the corporation as if it were a partnership or to arrange their relationships in a manner that would be appropriate only between partners....* A transferee of shares covered by such agreement who acquires them with knowledge thereof is bound by its provisions." (Italics added.)

ANNEXURE A

Part 2

SOUTH CAROLINA CORPORATION CODE

§§ 33-11-220

AGREEMENTS AMONG SHAREHOLDERS RESPECTING MANAGEMENT OF CORPORATION AND RELATIONS OF SHAREHOLDERS.

(a) No agreement among shareholders respecting the management and affairs of their corporation or the relations of shareholders among themselves shall be deemed invalid solely because the agreement purports to treat the affairs of the corporation as if it were a partnership and the shareholders as if they were partners.

(b) No written agreement, whether contained in the articles of incorporation or bylaws or in a written side agreement, and which relates to any phase of the affairs of the corporation, shall be deemed invalid solely because the agreement limits or restricts the powers or discretion of the directors of the corporation, if the following conditions are satisfied:

(1) The agreement is set forth, or its existence is clearly referred to, in the articles of incorporation;

(2) The agreement has been authorized by all shareholders of the corporation, whether or not entitled to vote to elect directors;

(3) The term of the agreement does not exceed ten years from the date thereof. Any such agreement shall be renewable at any time within one year before the expiration of such ten-year period by agreement of all

of/.....

of the shareholders bound thereby at the date of renewal.

(c) An agreement authorized by subsection (b) shall be valid only so long as the shares of the corporation are not traded on any national securities exchange or regularly traded in any over-the-counter market maintained by one or more brokers or dealers in securities.

(c-1) The text of any agreement authorized by subsection (b) shall be set forth in full, or a clear reference shall be made to the agreement, upon the face or back of each certificate for shares issued by the corporation.

(d) A transferee of shares in a corporation whose shareholders have entered into an agreement authorized by subsection (b) shall be bound by such agreement if he takes the shares with actual notice thereof. A transferee shall be deemed to have actual notice of any such agreement if the text of the agreement, with any amendments, is set forth in the articles of incorporation.

(e) The effect of an agreement authorized by subsection (b) shall be to relieve the director or directors of, and to impose upon the shareholders consenting to the agreement, the liability for managerial acts or omissions that is imposed by law upon directors to the extent that and so long as the discretion or powers of the directors in their management of corporate affairs is controlled by any such provision.

ANNEXURE A

Part 3

DELAWARE GENERAL CORPORATION LAW, 1974, § 354

OPERATING CORPORATION AS PARTNERSHIP

No written agreement among stockholders of a close corporation, nor any provision of the certificate of incorporation or of the by-laws of the corporation, which agreement or provision relates to any phase of the affairs of such corporation, including but not limited to the management of its business or declaration and payment of dividends or other division of profits or the election of directors or officers or the employment of stockholders by the corporation or the arbitration of disputes, *shall be invalid on the ground that it is an attempt by the parties to the agreement or by the stockholders of the corporation to treat the corporation as if it were a partnership or to arrange relations among the stockholders or between the stockholder and the corporation in a manner that would be appropriate only among partners.* (Italics added.)

ANNEXURE A

Part 4

PROPOSED STATUTORY CLOSE CORPORATION SUPPLEMENT, §§11(b)

SECTION 11. [AGREEMENTS AMONG SHAREHOLDERS]

(a) The shareholders of a statutory close corporation may by unanimous action enter into one or more written agreements to regulate the exercise of the corporate powers and the management of the business and affairs of the corporation or the relations among the shareholders of the corporation.

(b) *Except as otherwise provided in this Act any agreement authorized by this Section shall be valid and enforceable according to its terms* notwithstanding the elimination of a board of directors, any restriction on the discretion or powers of the board of directors or any proxy or weighted voting rights given to directors and *notwithstanding that the effect of the agreement is to treat the corporation as if it were a partnership or that the arrangement of the relations among the shareholders or between the shareholders and the corporation would otherwise be appropriate only among partners.*

(c) If the corporation has a board of directors, the effect of an agreement authorized by this Section restricting the discretionary powers of the directors shall be to relieve the directors of, and to impose upon the person or persons in whom such discretion or powers are vested, the liability for acts or omissions imposed by law upon directors to the extent that the discretion or powers of the directors are controlled by the agreement.

(d) An election not to have a board of directors in an agree-

ment/ .....

ment authorized by this Section shall not be valid unless the articles of incorporation contain a statement to that effect in accordance with Section 10.

(e) An election granting one or more shareholders the right to have the corporation dissolved at will or upon the occurrence of any specified event or contingency shall not be valid unless a statement of this right is included in the articles of incorporation in accordance with Section 15.

(f) A shareholder agreement authorized by this Section shall not be amended except by the unanimous written consent of the shareholders — unless otherwise provided in the agreement.

(g) Any action permitted by this Section to be taken by shareholders may be taken by the subscribers to shares of the corporation if no shares have been issued at the time of the agreement authorized by the Section.

(h) This Section shall not prohibit any other agreement among two or more shareholders authorized by law. (Italics added.)

ANNEXURE A

Part 5

CALIFORNIA CORPORATION CODE,
1975, §§300(b)

[N]o shareholders' agreement, which relates to any phase of the affairs of a close corporation, including but not limited to management of its business, division of its profits or distribution of its assets on liquidation, shall be invalid as between the parties thereto on the ground that it so relates to the conduct of the affairs of the corporation as to interfere with the discretion of the board or that it is an attempt to treat the corporation as if it were a partnership or to arrange their relationships in a manner that would be appropriate only between partners.

ANNEXURE B

Part 1

COMPANIES ACT 1948 § 210 (U.K.)

MINORITIES

ALTERNATIVE REMEDY TO WINDING UP IN CASES OF OPPRESSION

(1) Any member of a company who complains that the affairs of the company are being conducted in a manner oppressive to some part of the members (including himself) or, in a case falling within subsection (3) of section one hundred and sixty-nine of this Act, the Board of Trade, may make an application to the court by petition for an order under this section.

(2) If on any such petition the court is of opinion —

(a) that the company's affairs are being conducted as aforesaid; and

(b) that to wind up the company would unfairly prejudice that part of the members, but otherwise the facts would justify the making of a winding-up order on the ground that it was just and equitable that the company should be wound up;

the court may, with a view to bringing to an end the matters complained of, make such order as it thinks fit, whether for regulating the conduct of the company's affairs in future, or for the purchase of the shares of any members of the company by other members of the company or by the company and, in the case of a purchase by the company, for the reduction accordingly of the company's capital, or otherwise.

(3) Where an order under this section makes any alteration

in/ .....

in or addition to any company's memorandum or articles, then, notwithstanding anything in any other provision of this Act but subject to the provisions of the order, the company concerned shall not have power without the leave of the court to make any further alteration in or addition to the memorandum or articles inconsistent with the provisions of the order; but, subject to the foregoing provisions of this subsection, the alterations or additions made by the order shall be of the same effect as if duly made by resolution of the company and the provisions of this Act shall apply to the memorandum or articles as so altered or added to accordingly.

(4) An office copy of any order under this section altering or adding to, or giving leave to alter or add to, a company's memorandum or articles shall, within fourteen days after the making thereof, be delivered by the company to the registrar of companies for registration; and if a company makes default in complying with this subsection, the company and every officer of the company who is in default shall be liable to a default fine.

(5) In relation to a petition under this section, section three hundred and sixty-five of this Act shall apply as it applies in relation to a winding-up petition.

ANNEXURE B

Part 2

COMPANIES ACT 1980

§ 75 (U.K.)

POWER OF COURT TO GRANT RELIEF AGAINST COMPANY WHERE MEMBERS UNFAIRLY PREJUDICED.

(1) Any member of a company may apply to the court by petition for an order under this section on the ground that the affairs of the company are being or have been conducted in a manner which is unfairly prejudicial to the interests of some part of the members (including at least himself) or that any actual or proposed act or omission of the company (including an act or omission on its behalf) is or would be so prejudicial.

(2) If in the case of any company —

(a) the Secretary of State has received a report under section 168 of the 1948 Act (inspectors' reports) or exercised his powers under Part III of the 1967 Act or section 36(2) to (6) of the Insurance Companies Act 1974 (inspection of company's books and papers); and

(b) it appears to him that the affairs of the company are being or have been conducted in a manner which is unfairly prejudicial to the interests of some part of the members or that any actual or proposed act or omission of the company (including an act or omission on its behalf) is or would be so prejudicial,

he may himself (in addition to or instead of presenting a petition for the winding-up of the company under section 35(1)

of the 1967 Act) apply to the court by petition for an order under this section.

(3) If the court is satisfied that a petition under this section is well founded it may make such order as it thinks fit for giving relief in respect of the matters complained of.

(4) Without prejudice to the generality of subsection (3) above, an order under this section may —

(a) regulate the conduct of the company's affairs in the future;

(b) require the company to refrain from doing or continuing an act complained of by the petitioner or to do an act which the petitioner has complained it has omitted to do;

(c) authorise civil proceedings to be brought in the name and on behalf of the company by such person or persons and on such terms as the court may direct;

(d) provide for the purchase of the shares of any members of the company by other members or by the company itself and, in the case of a purchase by the company itself, the reduction of the company's capital accordingly.

(5) Where an order under this section requires the company not to make any, or any specified, alteration in the memorandum or articles then, notwithstanding anything in the Companies Acts, the company shall not have power without the leave of the court to make any such alteration in breach of that requirement.

(6) Any alteration in the memorandum or articles of the company made by virtue of an order under this section shall be of the same effect as if duly made by resolution of the company and the provision of the Companies Acts shall apply to the

memorandum or articles as so altered accordingly.

(7) An office copy of any order under this section altering, or giving leave to alter, a company's memorandum or articles shall, within 14 days from the making of the order or such longer period as the court may allow, be delivered by the company to the registrar of companies for registration; and if a company makes default in complying with this subsection, the company and every officer of the company who is in default shall be liable on summary conviction to a fine not exceeding one-fifth of the statutory maximum or, on conviction after continued contravention, a default fine not exceeding one-fiftieth of the statutory maximum for every day until that copy is delivered.

(8) In relation to a petition under this section 365 of the 1948 Act (general rules for winding up) shall apply as it applies in relation to a winding-up petition.

(9) This section shall apply to a person who is not a member of a company but to whom shares in the company have been transferred or transmitted by operation of law as it applies to a member of the company, and references to a member or members shall be construed accordingly.

(10) In subsections (2) to (9) above "company" means any body corporate which is liable to be wound up under the 1948 Act.

(11) Section 210 of the 1948 Act and section 35(2) of the 1967 Act (which are superseded by this section) shall cease to have effect except in relation to proceedings on a petition presented before the appointed day.

ANNEXURE B

Part 3

R.S.A. COMPANIES ACT, 1973
§ 252

RELIEF FROM OPPRESSION

252. MEMBER'S REMEDY IN CASE OF OPPRESSIVE OR UNFAIRLY PREJUDICIAL CONDUCT.

(1) Any member of a company who complains that any particular act or omission of a company is unfairly prejudicial, unjust or inequitable, or that the affairs of the company are being conducted in a manner unfairly prejudicial, unjust or inequitable to him or to some part of the members of the company, may, subject to the provisions of subs. (2), make an application to the Court for an order under this section.

(2) Where the act complained of relates to —

(a) any alteration of the memorandum of the company under 55 or 56;

(b) any reduction of the capital of the company under 83;

(c) any variation of rights in respect of shares of a company under § 102; or

(d) a conversion of a private company into a public company or of a public company into a private company under § 22,

an application to the Court under subs. (1) shall be made within six weeks after the date of the passing of the relevant

special resolution required in connection with the particular act concerned.

(3) If on any such application it appears to the Court that the particular act or omission is unfairly prejudicial, unjust or inequitable, or that the company's affairs are being conducted as aforesaid and if the Court considers it just and equitable, the Court may, with a view to bringing to an end the matters complained of, make such order as it thinks fit, whether for regulating the future conduct of the company's affairs or for the purchase of the shares of any members of the company by other members thereof or by the company and, in the case of a purchase by the company, for the reduction accordingly of the company's capital, or otherwise.

(4) Where an order under this section makes any alteration or addition to the memorandum or articles of a company —

(a) the alteration or addition shall, subject to the provisions of paragraph (b), have effect as if it had been duly made by special resolution of the company; and

(b) the company shall, notwithstanding anything contained in this Act, have no power, save as otherwise provided in the order, to make any alteration in or addition to its memorandum or articles which is inconsistent with the order, except with the leave of the Court.

(5) (a) A copy of any order made under this section which alters or adds to or grants leave to alter or add to the memorandum or articles of a company shall, within one month after the making thereof, be lodged by the company in the form prescribed with the Registrar for registration.

(b) Any company which fails to comply with the provisions of paragraph (a), shall be guilty of an offence.

ANNEXURE B

Part 4

SOUTH CAROLINA CORPORATION CODE

§ 12-22.23.

DISCRETION TO COURT TO GRANT RELIEF OTHER THAN DISSOLUTION.—

(a) In any action filed by a shareholder to dissolve the corporation on the grounds enumerated in 12-22.15, the court may make such order or grant such relief, other than dissolution, as in its discretion it deems appropriate, including, without limitation, an order

(1) Cancelling or altering any provision contained in the articles of incorporation, or any amendment thereof, or in the bylaws of the corporation;

(2) Cancelling, altering, or enjoining any resolution or other act of the corporation;

(3) Directing or prohibiting any act of the corporation or of shareholders, directors, officers or other persons party to the action; or

(4) Providing for the purchase at their fair value of shares of any shareholder, either by the corporation or by other shareholders.

(b) Such relief may be granted as an alternative to a decree of dissolution, or may be granted whenever the circumstances of the case are such that relief, but not dissolution, would be appropriate.

ANNEXURE B

Part 5

PROPOSED STATUTORY CLOSE CORPORATION SUPPLEMENT, § 16

SECTION 16 [POWER OF COURT TO GRANT RELIEF IN CERTAIN CIRCUMSTANCES.]

(a) Any shareholder of record, the beneficial owner of shares held by a nominee, or the holder of voting trust certificates of a statutory close corporation may file a petition in the [ ] Court for relief on the grounds that - -

(1) The directors or those in control of the corporation have or will have acted in a manner that is illegal, oppressive, fraudulent or unfairly prejudicial to the petitioner, whether in his capacity as a shareholder, director or officer of the corporation; or

(2) The directors or those in control of the corporation are so divided respecting the management of the corporation's affairs that the votes required for action cannot be obtained and the shareholders are unable to break the deadlock, with the consequence either that the corporation is suffering or will suffer irreparable injury or that the business and affairs of the corporation can no longer be conducted to the advantage of the shareholders generally; or

(3) Conditions exist that would be grounds for involuntary dissolution of the corporation.

(b) The jurisdiction of the Court shall be plenary and exclusive. If the Court finds that one or more of the conditions specified in subsection (a) exist, it shall grant such relief

as in its discretion it deems appropriate, including, without limitation, orders granting one or more of the following types of relief:

(1) Cancelling, altering or enjoining any resolution or other act of the corporation;

(2) Directing or prohibiting any act of the corporation or of shareholders, directors, officers or other persons party to the action;

(3) Cancelling or altering any provision contained in the articles of incorporation or by-laws of the corporation;

(4) Removing from office any director or officer, or ordering that a person be appointed a director or officer;

(5) Requiring an accounting with respect to any matters in dispute;

(6) Appointing a custodian to manage the business and affairs of the corporation;

(7) Appointing a provisional director who shall have all the rights, powers and duties of a duly elected director and serve for the term and under the conditions established by the Court;

(8) Ordering the payment of dividends;

(9) If the Court finds that the relief specified in paragraphs (1) through (8) is or would be inadequate or inappropriate, ordering that the corporation be liquidated and dissolved unless either the corporation or one or more of the remaining shareholders has purchased all of the shares of another shareholder at their fair value by a designated date,

with the fair value and terms of the purchase to be determined as provided by subsection (d). In the event the share purchase is not consummated and the corporation is dissolved and liquidated, any shareholder whose shares were to be purchased shall have the same rights and priorities in the assets of the corporation as would have been the case had no purchase been ordered by the Court.

(10) Ordering liquidation and dissolution, but only if grounds exist for ordering involuntary dissolution if the corporation were not a statutory close corporation, or if all other relief ordered by the Court has failed to resolve the matters in dispute.

In determining whether to enter a judgment under paragraphs (9) or (10), the Court shall take into consideration the financial condition of the corporation but shall not refuse to order liquidation solely on the grounds that the corporation has earned surplus or current operating profits.

(11) Awarding damages to any aggrieved party in addition to or in lieu of any other relief granted.

(c) If the Court determines that any party to a proceeding brought under this Section has acted arbitrarily, vexatiously, or otherwise not in good faith, it may award reasonable expenses, including attorneys' fees and the costs of any appraisers or other experts, to one or more of the other parties.

(d) If the Court orders relief pursuant to subsection (b) (9), the Court shall --

(1) Proceed to determine the fair value of the shares to be purchased, considering the going concern value of the corporation, any agreement among some or all of the shareholders

fixing a price or specifying a formula for determining the value of the corporation's shares for any purpose, the recommendations of any appraisers appointed by the Court, any legal constraints on the ability of the corporation to acquire the shares to be purchased and other relevant evidence.

(2) Enter a decree specifying the identity of the purchaser and the terms of the purchase found to be proper under the circumstances, including such provisions as are deemed proper concerning payment of the purchase price in two or more installments, payment of interest on the installments, subordination of the obligation to the rights of other creditors of the corporation, security for the deferred purchase price, and a covenant not to compete or other restrictions on the selling shareholder.

(3) Order that the selling shareholder shall, concurrently with the payment of the purchase price, or in the event of an installment purchase, concurrently with the payment of the initial payment called for in the order, make delivery of all his shares and from that date have no rights or claims against the corporation or its directors, officers or shareholders by reason of his having been a shareholder, director or officer of the corporation, except the right to receive the unpaid balance of the amount awarded him under this Section and any amounts due under any agreement with the corporation or the remaining shareholders that are not terminated by the Court's orders.

(4) Order that if the purchase is not completed in accordance with the Court's decree, the corporation shall be liquidated.

(e) Except as otherwise provided in subsections (f), and (g), the rights of a shareholder to file a proceeding under this

Section are in addition to and not in lieu of any other rights or remedies the shareholder may have.

(f) No shareholder shall be eligible to file an action under this Section until he shall have exhausted any non-judicial remedy for resolution of the issues in dispute to which the shareholder has agreed in writing.

(g) If a shareholder has the right to dissent from any proposed action and to receive the fair value of his shares under any provision of this Act or the [General] Business Corporation Act, any action under this Section brought in respect of the proposed action shall be filed prior to the time limitation for a dissenting shareholder to file with the corporation notice of intention to dissent and to demand fair compensation specified in Section [ ] of the [General] Business Corporation Act.

TABLE "A"

PUBLIC AND PRIVATE LIMITED COMPANIES IN BRITAIN

YEAR	PUBLIC COMPANIES	PRIVATE COMPANIES	TOTAL
1911	18,600 37,2%	31,400 62,8%	50,000
1921	12,700 16,9%	62,300 83,1%	75,00
1931	16,831 15,39%	92,499 84,61%	109,330
1938	15,872 10,52%	134,882 89,48%	150,754
1946	15,428 7,52%	189,575 92,48%	205,003
1956	14,195 4,89%	276,068 95,11%	290,263
1966	15,144 2,85%	516,091 97,15%	531,235
1967	16,583 2,91%	553,237 97,09%	569,820
1968	16,657 3,01%	536,625 96,99%	553,282
1969	16,672 3,01%	536,127 96,99%	552,799
1970	16,639 2,97%	542,858 97,03%	559,497
1971	16,679 2,89%	560,549 97,11%	577,228
1972	16,707 2,77%	587,228 97,23%	603,935
1973	16,695 2,62%	620,953 97,38%	637,648

YEAR	PUBLIC COMPANIES	PRIVATE COMPANIES	TOTAL
1974	16,658 2,5%	641,201 97,5%	657,859
1975	16,695 2,4%	653,235 97,6%	669,930
1976	16,716 2,41%	674,181 97,59%	690,897
1977	16,819 2,38%	689,179 97,62%	705,998
1978	16,954 2,28%	727,487 97,72%	744,441
1979	17,154 2,19%	768,534 97,81%	785,688

FOOTNOTES

1. Cicero, *de Offic. Lib. 1. cap. 7.*

2. Prins, *The Protection Of The Minority Shareholders In A Limited Company At English, South African and Dutch Law* (1972, Leiden), 37.

3. Schmitthoff, *New Concepts in Company Law*, (1973) J. Bus. L. 312, 314.

4. Schmitthoff, "How the English discovered the Private Company" in (Zonderland ed.), *Quo Vadis Ius Societatum? Liber Amicorum P. Sanders* (1972), 188, 191 and 193.

5. Wessels, *History of The Roman-Dutch Law* (1908), 656 suggests that the word company was developed in France from the Latin *cum* and *panis* meaning "with bread", which became *cumpanio, comphania, compagnie* and ultimately *company*.

6. *Id.*.

7. Gower, *Modern Company Law*, *infra* n.14, at 3 and n.5. Thus for instance the partnership proper which is referred to in *Ebrahimi*, *infra* n.765, at 373, was styled the "Oriental Carpet Company": *Re Westbourne Galleries Limited*, [1970] 3 All E.R. 374, 375.

8. Carr, *The General Principles Of The Law Of Corporations* (1905), 109.

9. *Lindley On Partnership* (Scammell and Banks ed. 1979) [hereinafter cited as *Lindley*], 24 and n.99 referring to *Re International Life Assurance Soc.* (1870), L.R. 5 Ch. App. 424, 431 and 732. That companies and partnerships have much in common is witnessed by the fact that the first four editions of this work which appeared between 1860 and 1878 were titled *A Treatise On The Law of Partnership Including Its Application To Companies.* That work was in 1888 divided into *Lindley On Companies Considered As A Branch Of The Law of Partnership* and *Lindley On Partnership*.

10. *Australian Coal & Shale Employees' Fed'n et al.* v. *Smith et al.* (1937), 38 S.R. (N.S.W.) 48, 53 *per* Jordan, C.J..

11. Morse and Tedd, *Partnership Companies*, (1971) J. Bus. L. 261, 262 and 261.

12. Sandars, *Small Businesses — Suggestions for Simplified Forms of Incorporation*, (1979) J. Bus. L. 14, 14 and 19. In February 1981 a Green Paper - for which see n.831 hereunder - was published in Britain inviting consideration of the case for introducing into the laws of the United Kingdom new forms of corporate entity, the incorporated partnership.

13. Cardozo, *The Nature Of The Judicial Process* (1921), 54-55 *citing* Mr. Justice Holmes in *N.Y. Trust Co.* v. *Eisner*, 256, U.S. 345, 349 (1921): "Upon these points, 'a page of history is worth a volume of logic'". Corroboration for these sentiments is found in the age old adage *"sine historia jurisprudentia caeca est"*.

14. *The Principles of Modern Company Law* (4th ed. 1979), hereinafter cited as *Modern Company Law*.

15. Gower, *Modern Company Law*, *supra* n.14, at 22.

16. For which see David & Brierley, *Major Legal Systems in the World Today* (1968), para. 8.

17. In Roman law the central point was not the will or the agreement into which it flowers, but the relation between persons. In the dogmatic theory by which the Civilian theorists sought to unify the precepts of Roman Law so as to be able to expound them as a logically coherent system, the central point became the will [by analogy to the will of God which is believed to pervade the universe] and the legal transaction, the agreement, for instance, which results from the meeting of two wills. 1 Pound, *Jurisprudence* (1959), 210.

18. As in *Ebrahimi*, *infra* n.765. Here the House of Lords relied on the earlier English decision of *Blisset* [*infra* n.109] in which, in turn, reliance was placed on Institutes 3.25.4. [*infra* n.97] to set aside a notice of expulsion in a partnership proper.

19. For which see Ch.V.

20. For which see Ch.VI para 20.3. hereunder.

21. For which see Ch.VI para. 19 hereunder.

22. For which see Ch.VI para. 19 hereunder.

23. For which see Ch.VI para. 20.3.4 hereunder.

24. Gower, *Some Contrasts Between British And American Corporation Law*, (1956) 69 Harv. L. Rev. 1369 [herein later cited as *British and American Corporation Law*], 1371 - 1372. See too Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises* (2d ed. 1970), § 1, at 4 n.6.

25. For the pre-classical consortium of co-heirs, or *ercto non cito*, see Daube, *Societas* As Consensual Contract, (1938) 6 Camb. L.J. 381; 2 De Zulueta, *The Institutes Of Gaius* (1953), para. 148-54b; Lee, *The Elements Of Roman Law*

(3rd ed. 1952), para. 498 and Van Oven, *Leerboek Van Romeinsch Privaatrecht* (3rd ed. 1948), para. 166. The ancient consortium of co-heirs has relevance even today as a number of the decisions to be considered in Ch.VII hereunder concern family partnerships involving the same basic idea and principles which are found in the ancient *ercto non cito*.

26. *The Influence Of The Roman Law on the Law of England* (1885).

27. *Id.*, at 159.

28. The first edition of Story's *Commentaries On The Law Of Partnership As A Branch Of Commercial And Maritime Jurisprudence* appeared in 1841. In this thesis the sixth edition by Gray, which appeared in 1868 will be used and will be cited as Story, *Partnership*. See too Hahlo & Kahn, *The Union Of South Africa: The Development of its Laws and Constitution* (1960) [herein later cited as Hahlo, *The Union Of South Africa*], 699 who refers to "the basic affinity of the concept of partnership in the two systems".

29. Digest 17. 2. 5. *cited by Story, Partnership, supra* n.28, at para. 73.

30. Story, *Partnership, supra* n.28 at para. 72. See too Scrutton *loc. cit.*

31. Scrutton, *loc. cit.*, Story, *Partnership, supra* n.28, at para. 76 where a private partnership is described as a partnership composed of two or more partners for some merely private undertaking, trade or business and a public company as a partnership where a large number of persons are concerned and the stock is divided into a large number of shares, the object of the undertaking often embracing public as well as private interests and benefits. Companies, as Story points out, are in turn subdivided into unincorporated companies or associations and into incorporated companies, fraternities or guilds and corporations existing under a royal or statutory charter which enjoy special statutory or chartered privileges, powers and rights.

32. Ripert, *Traité Élémentaire De Droit Commercial* (Roblot ed. 1974), at para. 692; Jeandel, *L'Intuitus Personae dans les Sociétés Commerciales* (1932), 5. A major point of distinction between a *société de personnes* and *société de capitaux* is that the former is concluded *intuitu personae* and the latter *intuitu pecuniae*. See Jeandel, *op. cit.*, 5 to 7 Ripert, *op. cit.*, 742 and Bourcart, *De l'intuitus personae dans les sociétés*, (1927) 9 - 10 Journal Des Sociétés Civiles Et Commerciales 513, 515, 518 and 519.

These terms indicate whether an association is an impersonal arm's length, capital orientated one or a close and personal one. See further Excursus II.

33. As in *Leadenhall, infra* n. 873, at 7c. See too Lee, *An Introduction To Roman-Dutch Law* (5th ed. 1953), 311.

34. For the meaning of this concept see Excursus I, Pt.3.

35. For which see Excursus I, Pt. 3.2..

36. See Kessler, *With Limited Liability For All: Why Not A Partnership Corporation?*, (1967) 36 Ford. L. Rev. 235, 260 and n.31 above.

37. See Excursus I, Pt. 5.

38. For which see para. 7 hereunder.

39. "[T]he personality of the corporation ... " says Maitland, *The Collected Papers* (Fisher ed. 1911), 310 referring to the fiction theory which originated in Italy but captured the English legal imagination, "is the gift of the Prince. It is not for you and me to feign and to force our fictions upon our *neighbours - solus princeps fingit quod in rei veritate non est*".

40. Kocourek, *Jural Relations* (2d ed. 1928), 77. See also Excursus I Part I and nn.1064, 1065 and 1066.

41. Digest 50.17.202. *noted by* Drake, *Partnership Entity And Tenancy In Partnership: The Struggle For A Definition*, (1917) 15 Mich. L. Rev. 609, 614.

42. Stein, *The Mutual Agency of Partners in The Civil Law*, 33 Tul. L. Rev. 595. Van Oven, *Leerboek van Romeinsch Privaatrecht, supra* n.25, at para. 165 at 280 - 281 shows that the word *societas* did not refer to the partnership agreement like *emptio-vendito* and *locatio-conductio* respectively refers to the agreement of purchase-sale and letting-hiring. *Societas* he states was a relation not a transaction: what is today referred to as the partnership agreement, was rendered in Roman law by the terms *societatem coire* or *inire*.

43. Sohm, *The Institutes: A Textbook Of The History And System Of Roman Private Law* (3rd ed. 1907) [herein later cited as *The Institutes*], para. 38 at 202.

44. Stein, *loc. cit.*.

45. *Theory And Operation Of Partnership Under The Latin American*

Codes, (1941) 16 Tul. L. Rev. 27, 30. "[V]ery little was said", Gladstone stresses, "about the relationship with third parties, the most prominent topic in the English law of partnership."

46. Here, like in Scotland, the system is essentially a hybrid one. The first European settlement was established by the *V.O.C.* in 1652. Up to 1806 Roman-Dutch Law, the native law of the Dutch settlers, was in force at the Cape whence it trekked with them as they penetrated the interior. After the Cape fell into English hands for a second time in 1806, English law was superimposed on the Roman-Dutch law. Today Roman-Dutch law has regained most of the territory it lost to Common Law in the private law sphere. However, it is in commercial law and, in particular, in company law, that the English influence is still predominant.

47. See Pound, *Jurisprudence*, *supra* n.17, at 210.

48. Pothier, *Traité du Contrat de Société*, para. 1 *noted by Lindley*, *supra* n.9, at 15.

49. Partnership is a contract by which two or more persons put or oblige themselves to put something in common in order to make therefrom in common a lawful profit to which they reciprocally bind themselves to render each other an account. (Tudor's translation.)

50. Pothier, *Pandectae*, 17.2.1.1, *noted by Lindley*, *ibid.*.

51. Partnership is a contract which is steeped in good faith for the contribution of assets or labour with a view to pursuing joint profit in an endeavour which is honest and lawful. [Present Author's translation.]

52. *Comm. ad Pandectae*, 17.2.1.

53. Partnership is a contract recognized by the *jus gentium*, it is characterized by good faith and is based upon consent involving an endeavour aimed at joint profit or loss.

54. *English and Roman-Dutch Law* (2d ed. 1905).

55. *Id.*, at 190. See too Hahlo, *The Union Of South Africa*, *supra* n.28, at 699.

56. Clark, *A Treatise On The Law Of Partnership And Joint Stock Companies* (1886) [herein later cited as *Partnership*], 2 shows that for a century or two prior to 1707 the law of Scotland presented a somewhat foreign appearance and exhibited a much closer resemblance to Continental than

English jurisprudence. "To this the law of partnership formed no exception", Clark adds when he points out that the early traces of partnership, "point unmistakeably to a system adopting the principles of the Roman *Societas*, as these have been modified and extended by the Dutch, and more particularly the French mercantile usages". See too Smith, *Scotland, the Development of its Laws and Constitution* (1962) [herein later cited as Scotland], 3, and Miller, *The Law Of Partnership In Scotland* (1973) [herein later cited as *Partnership*], 1.

57. Du Bois, *The English Business Company after the Bubble Act 1720-1800* (1938), 225 - 226.

58. *Infra* n. 62.

59. Miller, *Partnership, supra* n.56, at 1.

60. 2 Erskine, *Institutes Of The Law Of Scotland* (Nicolson ed. 1781), 3.18.

61. *Infra* n.62.

62. 53 & 54 Vict. c. 39 (1890).

63. *Id.*. (Italics added.) See too the similar provisions in Canadian jurisdictions, such as, for instance, the *Partnership Act*, R.S.O. 1970, c. 399, § 2 and R.S.O. 1980, c.370 §2.

64. *Lindley, supra* n.9, at 5; Miller *Partnership, supra* n.56, at 63 (and 60 - 62 for the development of the concept "quasi-partnership"). Today the term "quasi-partnership" lives on in the composite term "quasi-partnership company", a term coined by the judiciary to identify the incorporated partnership for winding it up under the just and equitable winding-up provision by resorting to principles of equity developed in relation to partnership proper.

65. *Lindley, supra* n.9, at 14.

66. *Id.*. (italics added) *referring to Davis v. Davis* ,[1894] 1 Ch.393.

67. *Partnership Act*, 1890, *supra* n.62 §§ 1(2). (Italics added.) The reference to Stannaries jurisdiction in §§ (1) 2 (c) is an anachronism. In early times Stannaries courts enjoyed special jurisdiction over the tinners (*Stannum* being the Latin for an alloy of silver and lead) of Cornwall and Devon. See Miller *Partnership supra* n.56, at 14.

68. *Partnership Act*, 1890. § 46. See too Miller, *Partnership, supra* n.56, at 2.

69. The statutory provisions in question are found in *Partnership Act*, 1890, § 28, § 29 and § 30. For the existence and

operation of the said rules of equity, see *Lindley supra* n.9 at 430 - 441; Underhill, *Principles Of The Law Of Partnership, infra* n.74, at 77 - 88 and para. 6.3 hereunder.

70. 1 *Institutes Of Natural Law*, (1754), Ch.13 § 9, *cited by Lindley, supra* n.9, at 15 and n.47.

71. Pollock, *On The Law Of Partnership* (Gower ed. 1952), 6, repeating Pollock, *The Law Of Partnership* (3rd ed. 1890), and *noted by Lindley, supra* n.9, at 15 and n.42.

72. *Per* Lord Wilberforce in *Ebrahimi, infra* n.765, at 375.

73. Zweigert & Goldman, *Report On The Possibility Of Harmonising Member States' Legislation On Private Limited Companies (Or Similar Bodies)* (1969) [herein later cited as Zweigert, *Private Limited Companies*], para. 47.

74. *Principles Of The Law Of Partnership* (Ivamy ed. 1971), 82.

75. *Supra* n.9, at 23 - 24.

76. *Id.*

77. 2 *Commentaries On The Law Of Scotland* (7th ed. 1870), Bk.7 § 5 at 508.

78. Van Oven, *Leerboek Van Romeinsch Privaatrecht, supra* n.25, para. 165 at 280.

79. Van Warmelo, *An Introduction to the Principles of Roman Law* (1976), para. 497.

80. See Excursus II, pt. 2.

81. Sohm, *The Institutes, supra* n.43, para. 82.

82. Digest 17.2.63.1. *quoted in, Wegner, infra* n.131, at 579.

83. Buckland, *Roman Law And Common Law A Comparison In Outline* (Lawson ed. 1965) [herein later cited as *Roman Law*], 304.

84. *Societas* As Consensual Contract, *supra* n.25, at 391.

85. Digest 17.2.6, 18. I. 35. I.

86. See Buckland, *Roman Law, supra* n.83, at 304.

87. Digest 17.2.65 pr.

88. Buckland, *Roman Law, supra* n.83, at 304.

89. See Morice, *English And Roman Dutch Law, supra* n.54, at 202.

90. Schulz, *Classical Roman Law* (1951), paras. 793 and 794.

91. According to Holdsworth, *The Early History Of Commercial Societies*, (1916) 28 Jurid, Rev. 305, 308, the inter se relations of partners down to the seventeenth century maintained the connotation of brotherhood: "The association is a 'comphania', the members are 'companions', and have *inter se* the *beneficum competentiae*". Earlier this century the idea that partners are brothers has been accepted by a South African court. See *Wegner*, *infra* n.131.

92. *Dissociamur renuntiatione:* Digest 17.2.4.1, *discussed by* Pothier *Traité du Contrat de Société*, *supra* n.48, para. 149. On the other hand where a *societas* was contracted for a fixed term any *socius* could before the expiration of that fixed term upon just cause, withdraw from the *societas* thus terminating it even in the face of an express clause to the contrary! Just cause in this regard would include conduct by a fellow *socius* which was so harmful or wrongful that it was not to the advantage of the aggrieved partner to endure it further, or as Ulpian puts it *ita injuriosus et damnosus socius sit ut non expediat eum pati*. Digest 17.2.14 *cited by*, *Pothier Traité du Contrat de Société*, *supra* n.48, para. 152 and *followed in*, *Armstrong*, *infra* n.141, at 980.

93. Pothier, *Traité du Contrat de Société*, *supra* n.48, para. 150. See too Bell, *Commentaries On The Law Of Scotland*, *supra* n.77, at 523. Pothier here quotes the Digest 17.2.65.3. example of a partner who on learning that he has been instituted as an heir of another, renounces a universal partnership in order not to share the inheritance with his partners. Pothier extends this principle to a partner who renounces an ad hoc partnership in order to acquire for himself the very opportunity — as for instance the purchase of a commodity at a bargain price with a view of a profitable resale — for which the partnership was concluded.

94. *Ibid.*.

95. Pothier, *Traité du Contrat de Société*, *supra* n.48, at para. 151.

96. Digest 17.2.65.5., *cited by* Pothier, *Traité du Contrat de Société*, *supra* n.48, at para. 151, *by Lindley*, *supra* n.9, at 432 and n.17 and *by* Story, *supra* n.28, on cover page. Pothier, *op. cit.*, para. 59 further argues that a partner

ought not to prefer his private interest to that of the partnership, nor to take away from it an advantageous bargain by making such a bargain on his own private account. Here Pothier argues that if a bargain which a partner made on his own private account was advantageous and belonged to the species of business which was the object of the partnership, and it would have been in the interest of the partnership to have acquired such bargain on its own account, then that partner can be compelled to hand over what he acquired to the partnership. Implicit in this text is the hint of an obligation of loyalty imposing on a miscreant partner a duty to account for opportunities falling in the same line of business as that of the partnership if the interests of the partnership so required. See too Story, *On Partnership, supra* n.28, at para. 177. What is important to observe is that this duty to account is not based on a vertical agency relationship. Pothier, *op. cit.*, paras. 66 to 72 deals with agency in partnership but does not then endeavour to link the duty to account to the vertical agency relation.

97. Institutes 3. 25. 4. *Veluti si totorum bonorum socius cum ab aliquo haeres esset relictus, in hoc renuntiaverit societati ut ob veniens aliquod lucrum solus habeat,* as *cited in Blisset, infra* n.109 at 523. See too Pothier, *Traité du Contrat de Société, supra* n.48, para. 150 at 110.

98. In the absence of an agreement to the contrary, this meant in equal shares. Digest 17.2.29 pr.; Institutes 3.25.1. Hahlo, *The Union of South Africa, supra* n.28, at 703.

99. Code 4.37.3. *cited by* Story, *Partnership, supra* n.28, para. 172 n.2; Lindley, supra n.9, at 430; *Parr, infra* n.132 at 211 and *Harris, infra* n.855 at 204.

100. *Partnership, supra* n.28, para. 171 *citing* Code 4.37.3 and Cicero, *Pro Roscio Amerino,* for which see Excursus II pt.2, n.1092.

101. Stein, *The Mutual Agency Of Partners In The Civil Law, supra* n.42, *passim.*

102. *Supra* n.9, at 431. Thus it is not surprising that Ch.16 of *Lindley* is titled *The General Duty of Partners To Observe Good Faith* and the first sub-title of that chapter is headed *High standard of honour requisite Among Partners.* And to cap it all the very opening lines of the chapter in question announce: "*In societatis contractibus fides exuberet*". The expression *uberrima fides,* which seems to be derived from this last mentioned adage, is however

more commonly used in England. See for instance *Green* v. *Howell*, [1910] 1 Ch.495, 504, where Cozens-Hardy, M.R., said "[P]artnership is a contract in which *uberrima fides* is required."

103. *Supra* n. 9, at 430.

104. *Principles Of The Law Of Partnership*, *supra* n.74, at 82.

105. *Lindley*, *supra* n.9, at 430 *citing Blisset*, *infra* n.109.

106. *Lindley*, *supra* n.9, at 430 *citing Maddeford* v. *Austwick*, 1 Sim. 89; *Law* v. *Law*, [1905] 1 Ch.140.

107. *Lindley*, *supra* n.9, at 430 and n.8 citing *Blisset*, *infra* n.109.

108. *Supra* n.9, at 432 citing Digest 17.2.65.5. for which see n.96 above. This principle, as interpreted by the English judiciary on numerous occasions, is today enshrined in *Partnership Act*, 1890, § 29. In *Green*, *supra* n.102, at 504 Cozens-Hardy, M.R., held that a contractual power of expulsion may not be used otherwise than in good faith and that an expulsion would not be justified if the essential motive was to get an undue advantage over the expelled partner by purchasing his interest on unfavourable terms. Compare text to nn.93 to 94 above.

109. (1853), 10 Hare 493 *applied* in *Ebrahimi*, *infra* n.765.

110. *Infra* n. 765.

111. See *Nocton* v. *Lord Ashburton*, [1914] A.C. 932, 963-4 where Lord Dunedin said "the word 'fraud' in the older cases in Chancery is often used where the thing so characterized is a wrongful breach of *duty*, without a consideration of whether there is such a *mens rea* as would found an action for deceit .... All the cases are based upon the existence of a *fiduciary relationship*, and subsequently the *breach* of *duty* arising." (Italics added.) Viscount Haldane, L.C. held a similar view. "In Chancery", his Lordship said at 953, "the term 'fraud' thus came to be used to describe what fell short of deceit, but imported breach of a *duty* [by persons standing in a *fiduciary relation*] to which equity had attached its sanction ...." (Italics added.)

112. *Dean* v. *Macdowell* (1878), 8 Ch.D. 345.

113. *Id.*, at 350. In the same matter Cotton L.J., at 354 referred to the "fiduciary relation which partners owe to one another."

114. *Helmore* v. *Smith* (no.1) (1886), 35 Ch.D. 436.

115. *Id.*, at 444 *noted in* Randelman, *The Fiduciary Responsibilities of a Surviving Partner Acting as Executor of the Deceased Partner's Estate*, (1980) 33 Vand. L. Rev. 175, 179.

116. *Lindley, supra* n.9, at 431, for instance, does refer to agency in this context but only to show that the obligation to good faith does not impose a fiduciary character upon the agency which exists between partners!

117. *Supra* n.9, at 625 and n.99. Instances of such conduct cited by *Lindley, supra* n.9, at 625 nn.3, 4 and 5 include *inter alia*, keeping of erroneous accounts, refusal to meet on matters of business, continued quarrelling and such a state of animosity as precludes all reasonable hope of reconciliation and friendly co-operation.

118. *Lindley, supra* n.9, at 625 - 626. Compare the provisions of *Partnership Act*, 1890, §§35(d).

119. "It is this quality of mutual agency ...", Miller, *Partnership, supra* n.56, at 158 suggests, referring to Story, *Partnership, supra* n.28, at 1 and to Clark, *Partnership, supra* n.50, "which is productive of most of the legal specialities of the relations of partners among themselves". See too Miller, *Partnership, supra* n.56, at 175 - 76 of this issue of his work under the heading *Theoretical grounds for a distinction between the rule as applying in partnership and that applying in agency.*

120. Clark, *Partnership, supra* n.56, at 182 and 2 Bell, *Commentaries On The Law of Scotland, supra* n. 77, at 508, *noted by* Miller, *Partnership, supra* n. 56, at 161 and nn. 19 and 20.

121. *Partnership, supra* n.56 at 182. The reference to Digest 17.2.65.5: *Semper enim, non id, quod privatim interest unius ex sociis, servari solet, sed quod societati expedit*, is unmistakeable. Clark, *Partnership, supra* n.56, at 183 goes on to point out that one of the consequences of the exuberant trust "which is inseparable from the contract of partnership", is that whenever a partner purchases, even with his own money, and in his own name, something which is in the company's line of trade, or would be a beneficial acquisition for it, he will be bound to communicate it to the company.

122. Miller, *Partnership, supra* n.56, at 161, 162, and 165.

123. Miller, *Partnership, supra* n.56, at 164.

124. Miller, *Partnership, supra* n.56, at 189, citing *Lindley supra* n.9, at 430. In Miller's views the terms "fiduciary duty" and "duty to exhibit *uberrima fides*" are but figures of speech and not legal terms of art. *Ibid.*, and at 182.

125. Miller, *Partnership, supra* n.56, at 165 *et seq.*. Miller, *op. cit.*, 167 referring to *Pender* v. *Henderson* (1864), 2 M.1428, 1440 acknowledges, that "[t]he true basis of the general rule [that a partner must account for a secret profit] is that where a partner has secured a clandestine personal benefit in transacting the business of his firm he has been guilty of 'a breach of faith with his co-partners'".

126. "The two sections" Miller, *Partnership, supra* n.56, at 165 opines, referring respectively to *Partnership Act*, 1890, § 29 and § 30, "place the partner in a fiduciary position analogous to that occupied by an agent in regard to his principal, and as in the case of agency the emphasis in the prohibition is upon the secret nature of the profit". As the headnotes to the said sections indicate, the statutory provisions in question respectively deal with a partner's accountability for "private" profits and his duty not to compete with the firm. But as has been observed earlier — n.96 above — the obligation to account developed independently of agency as did the obligation of loyalty. Both are founded on the principle that partners must subjugate their private interests to the collective interests of the firm. As far as *Partnership Act*, 1890, § 29 and § 30 are concerned, there is nothing to suggest that a partner, who, by agreement is not to have any representative powers, is exempt from the operation of the statutory duties in question.

127. (1881), 8 R. (H.L.) 1 *referred to by* Miller, *Partnership, supra* n.56, at 167 and 180-1, Stewart, Cassels and Reid were equal partners in terms of an agreement which, *inter alia*, provided that on the death, insolvency or retirement of any partner, the remaining partners should have the option of buying his interest at the book value thereof. The partnership agreement also provided not only that no partner had the power to assign his share or interest in the partnership to any person but also that an assignment contrary to that stipulation would be null and void. Reid secretly entered into an agreement with his nephew, Stewart, whereby the latter acquired from him his entire interest in the partnership at a particular date. Reid thereafter continued ostensibly as partner till his death some seven years later during which time the business and the prosperity of the "company" greatly increased. When this clandestine agreement came to light, Cassels instituted action against Stewart to compel him to communicate the benefit which he had obtained by his secret agreement with his uncle Reid. The action was dismissed. In the words of Lord Blackburn (at 7): "[I]f a partner being an agent (for I think it is because he is an agent that the fiduciary character arises) makes a profit out of the

concerns of his principal, and as acting for him, he must communicate it to his principal; he cannot make a profit out of his principal's business for himself. [A] partner is an agent, and the principle applying to him is a branch of that general rule which applies to agents. [T]hat is of necessity confined to those cases where it is part of the business of the company or firm that is carried on ... it is quite impossible to say that the purchase of a partner's beneficial interest in the partner's share in the partnership was one of those things in which the business of the company was carried on, and in which, therefore, Mr Stewart may be considered as in the nature of an agent for that class of dealings for Mr Cassels." *Contra* English authorities referred to in n.106 *supra* and American authorities found in para. 20.3.4.2 below.

128. Tried to the test of the highest standard of honour or the most scrupulous good faith, the conduct of both Stewart, and Reid, the plaintiff's co-partners, falls short. The clandestine assignment of Reid's beneficial interest in the partnership to Stewart frustrated the plaintiff's contractual right to acquire Reid's interest in the partnership on the latter's death or earlier retirement. Upon the principle stated in Digest 17.2.65.5. and Institutes 3.25.4, the secret sale by Reid of his interest to Stewart should have been declared void and both Stewart and Cassels should have been given the opportunity of acquiring Reid's said interest as provided for in terms of the partnership agreement.

129. *Infra* n.855 , at 204.

130. Morice, *English And Roman-Dutch Law*, *supra* n.54, at 207. A more recent text, Bamford, *On The Law Of Partnership And Voluntary Associations In South Africa* (2d ed. 1971) [herein later cited as *Partnership*], 28, is in similar vein. "Partners" the author maintains, "stand in a fiduciary relation to one another and are obliged to observe *uberrimae fides*, the highest degree of good faith. This duty embraces ...."

131. 1910 T.S. 571.

132. *Id.*, at 574. As Hahlo, *The Union Of South Africa*, *supra* n.28, at 704 correctly points out, the fraternal *beneficium competentiae* has quietly disappeared from modern law largely because of the view of Groenewegen *De Leg. Abr., ad Inst.* 4.6.38 (who opposed the reception of that defence) being preferred to that of Voet 17.2.20 (who supported it). But the general notion of brotherly fairness has survived: "The latitude excused in dealings between strangers is not permitted to them [partners].

No overreaching of the one by the other will be sanctioned". *Per* Buchanan, J., in *Parr* v. *Crosbie* (1886), 5 E.D.C. 197, 211. The concept of absolute good faith was nevertheless not overlooked by the same judge who had earlier remarked: "Each partner is required to act to the other with the utmost good faith — *uberrimae fides*, as it is termed. In the language of the Civil Law: *"In societatis contractibus fides exuberet ...."* These later sentiments were confirmed in *Olifants Tin "B" Syndicate* v. *De Jager*, 1912 T.P.D. 305, 314 *(affd.* 1912 A.D.) where De Villiers, J.P., said: "It is a general principle of our law that the contract of partnership is based on the utmost good faith. All the cases flow from that one great principle".

133. *Partnership, supra* n.130, at 28.

134. *Partnership, supra* n.130, at 29 where on the authority of *Hargreaves* v. *Anderson*, 1915 A.D. 137 and *Naturman* v. *Preskovsky & Fluxman*, 1935 W.L.D. 36 reference is made to the prohibition against a partner buying partnership property without the consent of his co-partners. The interests of a partner as buyer of partnership property are inimical to those of the partnership (see text to n.84 above). It is for that reason that such a transaction is void as a matter of policy, just as a notice of termination is, if given *mala fide* or *intempestiva*. This fiduciary duty must obviously flow from a lateral or associative relation and is not in any way related to a vertical relation like agency.

135. *Partnership, supra* n.130, at 28 where reference is made to *Hutton* v. *Steinweis* 1905 T.S. 43 and *Doucet* v. *Piaggio* 1905 T.H. 267. In the former case a contract was set aside between a partner, *X*, and a third party. The reason why the contract was set aside, was because *X* had instructed the third party to keep, *Y*, the partner of, *X*, under surveilance on suspicion that, *Y*, was committing fraud against, *X*. This constituted a breach of his fiduciary duty *vis-à-vis*, Y. Here obviously the fiduciary duty in question was once again not related to a vertical relation like agency and could only have flowed from the lateral or associative relation between *X* and *Y* as partners.

136. Bamford, *Partnership, supra* n.130, at 29.

137. Bamford, *Partnership, supra* n.130, at 29 *citing* Pothier, *Traité de Contrat de Société*, [*supra* n.48, at] para. 121 and 122. Pothier, *op. cit.*, para. 59, which Bamford omits to refer to, appears to be even more in point.

138. 1905 T.S. 255 *reversed on appeal* to the Privy Council in *Trimble and Bennet* v. *Goldberg, 1906 T.S. 1002* ,[1906] A.C. 494. For the reasons set out in n.941 hereunder the decision of the Transvaal Provincial Division is preferred to

that of the Privy Council. See too n. 929.

139. Bamford, *Partnership, supra* n.130, at 29.

140. *Supra* n.135.

141. 1913 C.P.D. 978.

142. 1914 T.P.D. 264 *followed in Lawrence infra* n.790.

143. *Armstrong, supra* n.141, at 980. For the passage quoted from *Lindley* see n.117 above.

144. *Infra* n.790.

145. *Jural Relations, supra* n.40, at 57. The word, *person* has in turn experienced many shifts of meaning. Originally it was used to denote a mask worn in a Greek play. Then it became the character portrayed by the mask and eventually the *role* itself played by such character.

146. *Collected Papers, supra* n.39, at 307 - 308 where Maitland states that "the organised group, whether called a corporation or not, will be treated as a person: that is [a] right-and-duty-bearing unit".

147. "[T]he terms [corporate, legal, moral] *person* and [corporate, legal] *personality*", 4 Pound, *Jurisprudence* (1959), 261 remarks, "have been used so long that we can hardly hope to persuade lawyers and law teachers to give them up. The most we can do perhaps, is to get rid of the natural-law metaphysical and psychological ideas of [corporate, legal] *personality* which have attached to the *legal conception* of a *legal unit* and realize that we are speaking of a *legal conception* and nothing more". (Italics added.)

148. Kessler, *With Limited Liability for All: Why Not A Partnership Corporation?, supra* n.36, at 242.

149. Digest 3.4.7.1: *cited by Lindley, supra* n.9, at 21 - 22: *Si quid universitati debetur, singulis non debetur, nec quod debet universitas singuli debent.* Compare text to n.169 and to n. 215 hereunder.

150. *The Institutes, supra* n.43, at para. 38. Lee, *The Elements Of Roman Law* (4th ed. 1956), para. 512, contends that while a *societas* was not generally a juristic person, certain large partnerships which were formed to undertake public works or to form revenues, *viz.* the so-called *societates publicanorum* and *vectigalium*, were or might have been juristic persons.

151. Introduction to Gierke, *Political Theories Of the Middle*

Ages (Maitland trans., 1938) [herein later cited as Maitland, *Political Theories*], xxii.

152. For an account of this evolution see Drake, *Partnership Entity And Tenancy In Partnership: The Struggle For A Definition*, *supra* n.41, at 611 - 613. Thus for instance Scaccia, a sixteenth century writer on the law merchant, could say:
Aliud est corpus unius societatis, et aliud est quilibet socius ipsius societatis — that is, the *corpus* of a partnership is one thing, but any member of the same partnership is another.

153. See Cooke, *Corporation Trust And Company, An Essay in Legal History* (1950) [herein later cited as *Corporation Trust And Company*], 46 and 185.

154. Cooke, *Corporation Trust And Company*, *supra* n.153, at 46.

155. *Corporation Trust And Company*, *supra* n.153, at 185. Here Cooke likens the creation, in financial terms, of a capital fund (which can be reflected as a favourable or adverse balance of a sum total of debits and credits, owing to or being owed by the proprietor of the business) to the creation in legal terms of a *persona ficta* — a right-and-duty-bearing unit, a labour-saving device, or a clearing house system, in other words.

156. Cooke, *Corporation Trust And Company*, *supra* n.153, at 48 and n.4.

157. Cooke, *Corporation Trust And Company*, *supra* n.153, at 48.

158. *Political Theories*, *supra* n.151, at xxiv. Maitland's reference to "mathematician's symbols" is to Ihering's symbolist — or as it is happily dubbed by Maitland, "bracket" — theory in terms of which a right-and-duty-bearing unit may be represented as X where $X = (A+B+C$ etc.)

159. *Per* Lord President Cooper in *Mair* v. *Wood*, [1948] Sess. Cas. 83, 86.

160. "The separate personality of a Scottish partnership", Smith, *Scotland*, *supra* n.56, at 276 correctly reflects, "is clearly recognized, but the exact nature of that *persona* is less easy to determine". Smith, *op. cit.*, at 277 goes on to classify Scottish partnership as a *"quasi-persona* or a *quasi-corporation*". Miller, *Partnership*, *supra* n.56, at 16, agrees that the entity (which the author also refers to as a quasi-persona) is different in its legal consequences from the juristic *persona* of an incorporated association.

161. *Mair*, *supra* n.159, at 86.

162. Smith, *Scotland, supra* n.56, at 276.

163. *Ibid.*.

164. *Ibid.*.

165. *Partnership, supra* n.56, at 168. "Heritable property", Clark, *loc. cit.*, continues, "is held in the names of one or more of the partners, or in those of third persons as trustees chosen for that purpose, moveables or personality appear to be held by all the parties jointly or *pro indiviso* as trustees for the concern".

166. *Scotland, supra* n.56, at 277.

167. *Supra* n.62.

168. *Lindley, supra* n.9, at 5.

169. *Supra* n.9, at 22. Compare n.149 above.

170. Mercantile Law Amendment Commission: Second Report, 1855, 18 *discussed by* Lindley, *On Partnership* (6th ed. 1893), 775. For the conflict between the mercantile and legal view of the firm in England see *Lindley, supra* n.9, at 29 - 31.

171. *Supra* n.62.

172. *Lindley, supra* n.9, at 5.

173. Rules of the Supreme Court, Order 81 § 1, for which see *Lindley, supra* n.9, at 980 *et seq.*.

174. *Corporation Trust And Company, supra* n.153, at 185.

175. Maitland, *Collected Papers, supra* n.39, at 317.

176. Bamford, *Partnership, supra* n.130, at 22; Hosten *et al.*, *Introduction to South African Law and Legal Theory* (1979), 532 and n.155; Hahlo, The *Union of South Africa, supra* n.29, at 702. For a recent application of this principle see *Strydom* v. *Protea. Eiendomsagente*, 1979 (2) S.A.L.R. 206, (T.P.D.) 210.

177. *Infra* n.245.

178. 11 & 12 Geo. 6, c.38 (1948).

179. C.81 (1967).

180. C.22 (1980).

181. *Infra* n.218.

182. For the early history of Scots public companies see Brown, *The Genesis of Company Law In England And Scotland*, (1901) 13 Jurid. Rev. 185; Christie, *Joint Stock Enterprise In Scotland Before the Companies Acts*, (1909/10), 21 Jurid. Rev. 128.

183. *Infra* n.226.

184. *Modern Company Law*, *supra* n.14, at 41 & n.11.

185. This word in Dutch is *"societeit"*, in French *"société"* and in German *"Gesellschaft"*. Depending on the context in which that term is used, it may refer to a partnership, to a company or to both. See "Introduction" to (Frommel & Thompson ed.), *Company Law in Europe* (1975), para. 49. See too Christie, *Joint Stock Enterprise In Scotland Before the Companies Acts*, *supra* n.182, at 129.

186. No. 23 of 1861.

187. *Infra* n.218.

188. *Infra* n.224.

189. No. 10 of 1864. Remarks a commentator in *The Law of Limited Liability Joint Stock Companies*, (1888) 5 Cape L.J. 231, 236 "our sister Colony is as far behind the times as we are in regard to this subject".

190. No. 5 of 1874.

191. C. C Orange Free State (1891).

192. No. 2 of 1892.

193. No. 24 of 1904.

194. No. 31 of 1909.

195. 8 Edw. 7, c.69 (1908) which, Schmitthoff, *How the English discovered the Private Company*, *supra* n.4, at 183, describes as "[o]ne of the great landmarks in the history of English company legislation".

196. No. 46 of 1926.

197. Suzman, *The South African Companies Acts* (1953), intr. 14, Pyemont, *Company Law of South Africa* (6th ed. 1953), intr. LXI. One such innovation is the procedure of judicial management as alternative to winding-up.

198. Cilliers, Benade & De Villiers, *Company Law* (3rd ed. 1977), 11.

199. No. 61 of 1973.

200. Hahlo, *South African Company Law Through the Cases* (3rd ed. 1977), 10-11. Thus for instance the *R.S.A. Companies Act*, 1973, no longer provides for the incorporation of unlimited companies, prohibits the issue of partly-paid shares and provides for a statutory derivative action which is not found in English legislation.

201. Cooke, *Corporation Trust And Company*, *supra* n.153, at 85-7, 96-101, 124-5, 128-31, 142.

202. "The deed of settlement", says Formoy, *The Historical Foundations of Modern Company Law* (1923), 40-41, "was in effect a deed of partnership. It consisted in a mutual covenant between a few of the shareholders acting as trustees for the purpose, and the other shareholders whose names appeared in the schedule, to carry out the provisions contained in the deed. These provisions contained the regulations of the partnership in the same way as the regulations of a company [incorporated under a Companies Act] are now contained in its articles and memorandum of association. Upon points which are not contained in it, the general law of partnership prevailed, and, as regards third parties, the shareholders stood on the same footing as an ordinary partnership ...."

203. 6 Geo. 1, c.18 (1719).

204. *The English Business Company after the Bubble Act 1720-1800*, *supra* n.57, at 40.

205. "Indeed it may be said", echoes *Lindley*, *supra* n.9, at 24, "that the law of unincorporated [equitable joint stock] companies was composed of little else than the law of partnership modified and adapted to the wants of a large and fluctuating number of members".

206. Corbett, *An Enquiry into the Causes and Modes of the Wealth of Individuals or The Principles of Trade and Speculation Explained* (1841), 99. With the introduction of the vertical, proprietary, trust relation, this divorce between ownership and control was accentuated.

207. Compare Lattin, *The Law Of Corporations* (2d ed. 1971), 51 where he describes the comparable situation in the joint stock company as it exists in the U.S.A. today, in these terms: "Through the use of transferable shares, *delectus*

personarum is surrendered and, through representative control the inherent right of partners to community of control is lost".

208. *The English Private Company*, (1953) 18 Law & Contemp. Prob. 535 at 535.

209. Du Bois, *The English Business Company After the Bubble Act, 1702 - 1800*, *supra* n.57, at 27. "Our way of escape", Maitland, *Collected Papers*, *supra* n.39, at 281 says, "was the trust. Vest the lands, vest the goods in some man or men. The demand for personality is satisfied. The lands, the goods, have an owner: an owner to defend them and recover them: an owner behind whom a Court of Common Law will never look. All else is mere equity".

210. *The Law of Associations* (1911), 19.

211. *Corporation Trust And Company*, *supra* n.153, at 185 - 186. Needless to say, there was no fiduciary relation between members on the lateral or associative plane. On the vertical plane, though, a fiduciary relation would exist between the agents or trustees in favour of the company members.

212. This term was used in *In re European Ass. Soc.* (1875), 1 Ch.D. 307, at 320.

213. *Collected Papers*, *supra* n.39, at 283. All this had been accomplished, Maitland stresses, "without troubling the State to concede or deny the mysterious boon of personality".

214. 6 Geo. 4, c.91 (1825).

215. See n.149 above. Cooke, *Corporation Trust And Company*, *supra* n.153, at 105 speaks of the "traditional rule that a grant of incorporation was necessarily accompanied by limited liability".

216. *Infra* n.218.

217. *Collected Papers*, *supra* n.39, at 389 and 393. Cooke, *Corporation Trust And Company*, *supra* n.153, at 186 gives the following account of this struggle: "[T]he hostility of the common law courts did not inhibit the growth of the joint stock company. All through the eighteenth-century the unincorporated joint stock company continued to flourish under the protection of the Chancery, covered by the mantle of the trust. The ingenuity of the Chancery lawyers defeated the common law at every point ...."

218. 7 & 8 Vict., c.110 (1844) [hereinafter cited as the *Joint Stock Companies Act*, 1844].

219. *Joint Stock Companies Act, 1844*, *supra* n.218, § 25. Compare in this regard the present-day provisions of *Companies Act*, 1948, *supra* n.178, §§ 13(2) and of *R.S.A. Companies Act 1973*, *supra* n.199, §§ 65(1). See too n.229 hereunder.

220. *Collected Papers*, *supra* n.39, at 392. "The enemy", Maitland exclaims at 389, "was within the citadel".

221. *Joint Stock Companies Act*, 1844, *supra* n.218, § 25.

222. *British And American Corporation Law*, *supra* n.24, at 1372.

223. *Corporation Trust And Company*, *supra* n.153, at 138.

224. 18 & 19 Vict., c.133 (1855).

225. *Id*, § 8.

226. 19 & 20 Vict., c.47 (1856) [hereinlater cited as the *Joint Stock Companies Act*, 1856]. This time joint stock companies established in Scotland were not excluded.

227. Cooke, *Corporation Trust And Company*, *supra* n.153, at 158. Gower, *The English Private Company*, *supra* n.208, at 537 noted that, the 1856 Act swept away most of the safeguards which the 1855 Act had provided — minimum issued paid-up share capital, approval of a company's auditors by the Board of Trade, personal liability of directors, in the event of their paying dividends knowing the company to be insolvent — and retained only the one pillar on which the 1844 Act had been built, namely the principle of publicity.

228. In terms of *Joint Stock Companies Act*, 1856, § 9 the memorandum of association could be accompanied by or have endorsed thereon, articles of association signed by the subscribers and prescribing regulations for the company; if no such regulations were prescribed or insofar as they did not extend to modify the regulations contained in table "B" to that Act, such regulations, so far as they were applicable, would be deemed to be the regulations of the company. Thus corporators were at liberty to frame their own constitution, which obviously brought about the desired flexibility so lacking in the American corporation. This arrangement has survived to this day, except that table "B" has become table "A" and the term "regulation" has been replaced by the term "articles of association". For the present day provisions, see *Companies Act*, 1948, *supra* n.178, § 8 and *R.S.A. Companies Act*, 1973, *supra* n.199, § 59.

229. Compare this provision with its predecessor *Joint Stock Company Act*, 1844, *supra* n.218, § 25 and its successors, *Companies Act*, *supra* n.178, 1948, §§13(2) and the *R.S.A. Companies Act*, 1973, *supra* n.199, §§65(1). The relevant provisions of the said § 25 provide that "[t]he subscribers of the memorandum, together with such other persons as may from time to time become members of the company, shall be a *body corporate* by the name contained in the memorandum, capable forthwith of exercising all the functions of an *incorporated company*, and having *perpetual succession* and a common seal, but with such *liability* on the part of the members to contribute to the assets of the company in the event of its being wound up as is mentioned. (Italics added.) The relevant provisions of the said §§65(1) read, "[t]he subscribers of the memorandum together with such other persons as may from time to time become members of the company, shall be a *body corporate* with the name stated in the memorandum, capable of exercising all the functions of an *incorporated company*, and having *perpetual succession*, but with such *liability* (if any) on the part of the members to contribute to the assets of the company in the event of its being would up as provided by this Act". (Italics added.)

230. Carr, *The General Principles Of The Law Of Corporations*, *supra* n.8, at 150 shows that the words like corporate body, *corpus*, *corps*, *corps politique*, *etc.*, date from the Middle Ages when it was convenient fashion to draw an analogy between the corporation and the human body. "This 'crude anthropomorphism'", Carr says, using Maitland's turn of phrase, "though never very precise or valuable, was sometimes elaborate and striking".

231. *Joint Stock Companies Act 1856*, *supra* n.226, § 61. *Companies Act*, 1948, *supra* n.178, §§ 212(1)(d) contains a similar provision today. Since *R.S.A. Companies Act*, 1973, § 92, prohibits the issue of shares as partly paid-up after December 31, 1973, liability of a member to contribute in the aforesaid fashion has now become largely academic in the Republic of South Africa.

232. *Joint Stock Companies Act*, 1856, *supra* n.226, § 7 and § 10 *Companies Act*, 1948, *supra* n.178, §§ 20(1) provides:

> "Subject to the provisions of this Act, the memorandum and articles shall, when registered, bind the company and the members thereof to the same extent as if they respectively had been signed and sealed by each member, and contained covenants on the part of each member to observe all the provisions of the memorandum and of the articles".

In similar vein *R.S.A. Companies Act*, 1973, *supra*, n.199,

§§ 65(2) provides:

> "The memorandum and articles shall bind the company and the members thereof to the same extent as if they respectively had been signed by each member, to observe all the provisions of the memorandum and articles of association...."

233. *Companies Act*, 1948, *supra* n.178, §§ 222(f); *R.S.A. Companies Act*, 1973, *supra* n.199, § 344(h). For these provisions see Ch.VII para. 21.2.2 below.

234. *Ebrahimi*, *infra* n. 765, at 379 B-C. See too text to n.268 below.

235. Compare *Companies Act*, 1948, *supra* n.178, §§ 1(1) which provides:

> "Any seven or more persons, or, where the company to be formed will be a private company, any two or more persons, associated for any lawful purpose may, by subscribing their names to a memorandum of association and otherwise complying with the requirements of this Act in respect of registration, form an incorporated company, with or without limited liability".

The provisions of *R.S.A. Companies Act*, 1973, *supra* n.199, § 32 are largely similar except that a company can no longer be incorporated as an unlimited company. In addition the existence of one-man private companies (a concept which has as yet not been accepted by the English legislature), is also now expressly recognized.

236. *Joint Stock Companies Act*, 1856, *supra* n.226, § 5. This is still the position today. See *Joint Stock Companies Act*, 1948, *supra* n.178, §§ 2(1)(a); *R.S.A. Companies Act*, 1973, *supra* n.199, §§ 49(1)(a).

237. Gower, *The English Private Company*, *supra* n.208, at 537 and n.14a. "The arbitrary exclusion of freedom from liability despite incorporation," Gower observes, "which had prevailed in the preceding 12 years [1844-1855] made this necessary and accounts for the fact that English Companies are still distinguished by 'Ltd.' instead of the more logical 'Inc.' used in the United States".

238. *Joint Stock Companies Act*, 1856 *supra* n.226, § 39. The provisions of *Companies Act*, 1948, *supra* n.178, § 31 are almost identical but for the reference to two members in the case of a private company. In *R.S.A. Companies Act*, 1973, *supra* n.199, § 66, the reference to the two members of a private company had to be dropped in view of the statutory recognition of one-man companies. (The South African provision further differs from the English in that the former permits membership of a wholly-owned subsidiary to fall below seven with impunity whereas the

latter does not.)

239. *Joint Stock Companies Act*, 1856, *supra* n.226, § 4. For the corresponding provisions today see *Companies Act*, 1948, *supra* n.178, § 434 and *R.S.A. Companies Act*, 1973, *supra* n.199, § 30 and § 31. In both instances the civil sanction of being held *liable severally* for the debts of the partnership has been substituted by a criminal sanction. Moreover, certain organised professions are now exempted from complying with the membership ceiling of twenty: *Companies Act*, 1967, *supra* n.179, § 120 and *R.S.A. Companies Act*, 1973, *supra* n.199, §§ 30(2).

240. *Smith* v. *Anderson* (1880), 15 Ch.D. 247, 273, *cited by* Scmitthoff *et al. Palmer's Company Law* (22nd ed. 1976), para. 85 - 14.

241. *The General Principles Of The Law Of Corporations*, *supra* n.8, at 109.

242. The figure twenty appears to be a compromise between the figure twenty-five found in the definition of "Joint Stock Company" in the *Joint Stock Companies Act*, 1844, *supra* n.218, § 2 and the figure fifteen, mooted by Bellenden Kerr. The boom in company promotions of 1836 moved the latter as Commissioner of the Board of Trade, to propose a system of registration for partnership and joint stock companies in his *Report on the Law of Partnership, Parliamentary Papers*, 44 (1837 - 38). Kerr recommended not only that the sale of shares in unregistered companies should be prohibited, but also that all partnerships having more than fifteen members should be illegal, unless they were constituted by a registered deed of settlement.

243. "Registration" as Gower, *The English Private Company supra* n.208, at 537 points out, "was thought of primarily as a method of enabling the entrepreneur to obtain capital from the public".

244. It is not unlikely that if the development of the public partnership had not been arrested in this fashion by the English legislature, the public partnership would have attained limited liability as it has in North America. "If the State had not given way", Maitland *Collected Papers*, *supra* n.39, at 392 referring to the legalization of the unincorporated equitable joint stock company observes "we should have had in England joint-stock companies, unincorporated, but contracting with limited liability".

A case in point is the North America business or Massachusetts trust which, because of its members' freedom from liability, may be viewed as the ultimate stage in the development of the unincorporated joint stock company.

245. 25 & 26 Vict., c.89 (1862).

246. 8 Edw. 7, c.69 (1908) [herein later sometimes referred to as the *Companies Act*, 1908].

247. *Supra* n.178.

248. *Supra* n.180. The Act received Royal Assent on 1st May 1980, but its provisions remain in suspense until brought into effect by commencement orders which will declare appointed days for the commencement of the various provisions.

249. *Supra* n.178.

250. *Supra* n.199.

251. Cilliers, *et al*, *Company Law*, *supra* n.198 at 2.

252. *Id.*, citing Nekam, *The Personality Conception of the Legal Entity* (1938), 110 and 113 where Nekam concludes that to define corporation correctly is an impossible task because that word stands for no single well-ascertained concept: its meaning varies according to the exactness or vagueness of the definition which may be attempted in each particular instance.

253. *A Treatise On The Law Of Companies Considered As A Branch Of The Law Of Partnership* (5th ed. 1889), 1. Here Lindley goes on to reason that a company which is neither incorporated nor privileged by the Crown or the Legislature is substantially a partnership; that although the transferability of the shares of such a company considerably modifies the application to it of the ordinary law of partnership, such a company, like a partnership proper, but unlike an incorporated company, does not enjoy corporate status.

254. *Re Stanley, Tennant* v. *Stanley*, [1906] 1 Ch.131, 134. "Firm" in this context obviously refers to "partnership proper".

255. *Laws of England* (4th ed. 1974) Volume 7 para. 1.

256. Cilliers, *et al.*, *Company Law*, *supra* n.198, at 2 relying on Gower, *Modern Company Law*, *supra* n.14, at 9 - 11.

257. Compare the sentiments expressed by Mr. Justice Bijur in *Farmers' Loan & Trust Co.* v. *Pierson*, 222 N.Y.S. 532 (1927) to the effect that "... a corporation is more merely a method than a thing and that the law in dealing with a corporation ... may treat it as a name for a useful and usual collection of *jural relations*...." (Italics added.) *cited by* 1 OLeck, *Modern Corporation Law* (1958), § 2 at 6 & n.23, *and by* Cilliers, *et al.*, *Company Law*, *supra* n.198, at 2 & n.1.

258. *Symington, infra* n. 733 and *Loch, infra* n. 721.

259. *Symington, infra* n. 733 at 122; *Loch, infra* n. 721, at 786.

260. *Supra* n. 180.

261. "'The Corporation'", says Du Bois, *The English Business Company after the Bubble Act 1720-1800, supra* n.57, at 87, and 138n.1 "'is the creature of the State'". Today of course the term corporation is in England used singularly to denote a body created by statute for a particular social or public economic purpose.

262. Du Bois, *The English Business Company after the Bubble Act 1720-1800 supra* n.57, at 87 and 138 n.14. It is possible that this dichotomy came from the Romans who distinguished between public law *universitates* and private law *universitates*.

263. Schmitthoff, *et al., Palmer's Company Law*, supra n. 240, para. 4-01 & n.2.

264. *Corporation Trust And Company, supra* n.153, at 181.

265. (1881), 17 Ch.D. 467.

266. *Id.*, at 479.

267., [1897] A.C. 22, (H.L.(E)).

268. *Id.*, at 30.

269. "[I]t [*Salomon*] established", remarks Gower, *The English Private Company, supra* n.208, at 539, "the 'corporate entity' principle in a particular rigorous form and largely stultified all efforts by the courts to 'lift the veil' so much so that *lifting the veil*, that popular subject of academic discussion in the United States, is almost totally ignored in the English literature...." Gower goes on to say that where the corporate veil has been lifted it is usually as a result of express statutory enactment "for normally it is only the legislature which can forge a sledge-hammer capable of cracking open the corporate shell.'" Only of late is this legacy being re-evaluated. See Schmitthoff, *Salomon in the Shadow*, (1976) J. Bus. L. 305 and Powles, *The "See-Through" Corporate Veil*, (1977) 40 M.L. Rev. 339.

270. 63 & 64 Vict., c.48 (1900).

271. Cd. No. 3052 (1906), hereinafter sometimes referred to as

the *Loreburn Report* (Italics added.)

272. *Id.*, at para. 45.

273. *Loreburn Report, supra* n.271, para. 48. As it turned out the legislature ignored this particular recommendation.

274. *Loreburn Report, supra* n.271, para. 49.

275. 7 Edw. 7, c.50 consolidated in the following year in the *Companies Consolidated Act*, 1908, 8 Edw. 7, c.69.

276. 7 Edw. 7, c.50, § 37 (1907), which became 8 Edw. 7, c.69, § 121 (1908).

277. *Supra* n.178.

278. *Supra* n.199.

279. *Companies Act*, 1908, *supra* n.246, § 2.

280. *Supra* n.178.

281. *Supra* n.199.

282. *Companies Act*, 1908, *supra* n.246, §§ 26(3). See too *S.A. Companies Act*, 1926, *supra* n.196, §§ 26(6).

283. *Companies Act*, 1948, *supra* n.178, § 127 and § 129. But see *Companies Act*, 1967, *supra* n.179, § 2. See too *R.S.A. Companies Act*, 1973, *supra* n.199, § 173 and §§ 302 (4) in terms of which only public companies are enjoined to lodge copies of their financial statements.

284. No comparative statics are available about the situation in the Republic of South Africa. It was reported though, in the *Van Wyk De Vries Report* R.P. 45/1970, that at the time (1969) private companies represented more than 90% of the total of all limited companies in the Republic of South Africa.

285. *Supra* n.180.

286. *Companies Act*, 1980, *supra* n.180, §§ 88(2) read together with Sch.4 of that Act.

287. *Companies Act*, 1980, *supra* n.180, §§ 1(1) *discussed by* Morgan and Morse, *Transitional Provisions of the Companies Act 1980*, (1980) J. Bus. L. 242, 243.

288. *Id.*.

289. *Companies Act*, 1980, *supra* n.180, § 85 and §§ 87(2).

290. *Companies Act*, 1980, *supra* n.180, §§ 2(1).

291. *Supra* n.180.

292. 77/91/E.E.C.: O.J. 1977 L.26/1.

293. Gower, *The English Private Company*, *supra* n.208, at 539.

294. Renner, *The Institutions Of Private Law* (Kahn-Freund ed. 1949), 221-222.

295. *Id.*.

296. "[L]imited partnerships, "Gower, *The English Private Company supra* n.208, at 541 proffers, "did not take root in English business life; the need for them had passed". The *Limited Partnership Act*, 1907, 7 Edw. 7, c.24 has not lived up to the high expectations cherished for it at the time. According to estimate figures obtained from the Board of Trade, only a small number is registered annually and the total number of these associations in existence as at September 1979 was no more than between 600 and 700. It is possible that many of these are dormant as the Act is silent on deregistration. Possibly because of the British influence in the mercantile field after 1806 in South Africa, the experience there is very similar despite the Roman-Dutch *kommànditêre vennootskap* which developed from the French, *société en commandité*. Recently both the *Special Partnerships' Limited Liability Act*, 1861, No.24 of 1861 (Cape) and the *Special Partnerships Limited Liability Act*, 1865, No.1 of 1865 (Natal) were repealed in terms of *Pre-Union Statute Law Revision Act*, No.36 of 1976. At the time of such repeal there were only 70 such special limited partnerships in the Cape and 126 in Natal. At the same time the common law *kommànditêre vennootskap* is not very common either. This is surprising in view of the fact that *Eaton & Louw* v. *Arcade Properties (Pty.) Ltd.* 1961 (4) S.A.L.R. 234 (T) 240 held that the doctrine of the undisclosed principal does not operate in respect of the *kommànditêre vennootskap*.

297. See *Limited Partnership Act*, 1907, *supra* n.296, § 3 read together with *Partnership Act*, 1890, *supra* n.62 § 4. In South Africa a *kommànditêre vennootskap*, like an ordinary partnership, lacks legal personality.

298. Tax considerations have, for instance, in certain jurisdictions made the limited partnership an attractive vehicle for investment. One such jurisdiction is Germany. To avoid the double taxation to which companies are otherwise liable in Germany, and to afford the participants the immunity from liability which flows from corporateness, the German private company, the G.m.b.H., is combined with a limited partnership,

or *Kommanditgesellschaft*. The object of this symbotic union, called a "G.m.b.H. & Co," is the attainment of the best of both worlds. While, as a limited partnership, the G.m.b.H. & Co., enjoys non-corporate status from a tax point of view, the corporate status of the G.m.b.H. as the essential general partner, shields the special partners from claims by third parties. Zweigert, *Private Limited Companies, supra* n.73 para.7, depicts this union as being *de jure* a (limited) partnership and *de facto*, that is from the economic point of view, a limited liability company. Compare text to n.376 *infra*.

299. Topham, *Palmer's Company Law* (10th ed. 1916), 367. (Italics added.)

300. In *Tench , infra* n.828.

301. In *Ebrahimi, infra* n.765.

302. See text to n. 550 *infra*.

303. See text to nn. 761, 918, 922 and 937 *infra*.

304. See n.824 *infra*.

305. Cmnd. No. 1749 paras. 71-72 (1962).

306. Sandars, *Small Businesses - Suggestions for Simplified Forms of Incorporation, supra* n.12, *passim*. See too n.831 *infra*.

307. Gower, *The English Private Company, supra* n.208, at 541.

308. Hahlo, *South African Company Law Through the Cases*, (3rd ed. 1977), 11.

309. Schmitthoff, *How the English discovered the Private Company, supra* n.4, at 184. In the Republic of South Africa a similar situation prevails. That partnership proper is still the preferred vehicle in the enumerated professions is due solely to the rules of their governing bodies prohibiting incorporation. More recently however, some of such bodies have relaxed their opposition to incorporation and permit their members to form incorporated (private) companies in which members' liability for company debts are not limited.

310. Schmitthoff, *How the English discovered the Private Company, supra* n.4, at 184.

311. Gower, *The English Private Company, supra* n.208, at 543.

312. *Supra* n.180.

313. *Infra* n.733.

314. *Infra* n.765.

315. *How the English discovered the Private Company, supra* n.4, at 193 (italics added).

316. Frommel & Thompson, *Company Law in Europe* (1975), "Introduction para. 69; De Vries & Juenger, *Limited Liability Contract: The G m b H*, (1964) 64 Colum.L. Rev. 866, 867; McFadyean, *The American Close Corporation And Its British Equivalent*, (1958) 14 Bus. Law. 215; Schneider, *The American Close Corporation And Its German Equivalent*, (1958) 14 Bus. Law. 228; O'Neal, *The American Equivalent of the Private Company*, (1956) 3 Bus. L. Rev. 304.

317. See 1 Levy, *Private Corporations and their Control* (1950), 221-222. The sphere of influence of German company law includes Austria, Hungary, Switzerland, Poland, the Scandinavian countries, Turkey and Japan. Owing largely to the *Code de Commerce* 1807, and the *Companies Act*, 1867 the French model has been followed in the Netherlands, Belgium, Italy, Spain, Portugal, Rumania, Yugoslavia, Mexico and the South American countries.

318. Hahlo, *Company Law Through the Cases* (2d ed. 1969), 7.

319. Gower, *British and American Corporation Law, supra* n.24, at 137(

320. *Ibid.*.

321. *Ibid.*.

322. See para. 19.2 hereunder and following note.

323. Rider, *Partnership Law And Its Impact On "Domestic Companies"*, (1979) 38 Camb. L.J. 148, 153.

324. *Gesetz betreffend die Gesellschaften mit beschränkter Haftung*, R.G. Bl. 477, was enacted on April 20, 1892.

325. De Vries & Juenger, *Limited Liability Contract: The G.m.b.H., supra* n.316, at 869. Conard "Company Laws of the European Communities from an American Viewpoint" in (Schmitthoff ed.), *The Harmonisation of European Company Law* (1973), 55 is in similar vein: "Whereas most forms of business organisation were first created by the ingenuity of merchants and their lawyers, and belatedly recognized by legislation, the limited liability [private] company is an origination which sprang from the forehead of the German legislature in 1892, and gradually spread nearly everywhere else except to the English-speaking countries". Hahlo & Trebilcock, *Hahlo's Casebook On Company Law* (2d ed. 1977), 5 submit however that the English statutory

private company which was introduced by the *Companies Act*, 1907, was modelled on the German G.m.b.H..

326. See David & Brierley, *Major Legal Systems in the World Today* (2d ed. 1978), para. 5.

327. At present, however, in line with the trend towards the Harmonization of legislation in force in Council of Europe member states, serious consideration is being given to the possibility of also harmonizing the legislation governing private limited companies in the various member states by cutting back unnecessary diversity where feasible. See in general Zweigert, *Private Limited Companies*, *supra* n.73, *passim*.

328. Zweigert, *Private Limited Companies*, *supra* n.73, at paras. 10, 11, 17, 22 and 29.

329. *Id.*, at para. 11.

330. Drury, *Legal Structures Of Small Businesses In France And England Compared*, (1978) 27 Int. & Comp. L.Q. 510, 511.

331. Conard, *Company Laws of the European Communities from an American Viewpoint; supra* n.325, at 55 and 214 & n.92.

332. Zweigert, *Private Limited Companies*, *supra* n.73, at para. 5.

333. This campaigner was a certain Oechelhäuser who is reputed to have had a profound knowledge of the evolution of the private company idea in England. Wooldridge & Sharma, *The Private Company in German Law*, (1975) 4 Anglo-Am. L. Rev. 40, 40 and n.7.

334. Wooldridge & Sharma, *The Private Company in German Law*, *supra* n.333, at 41 and n.5.

335. Zweigert, *Private Limited Companies*, *supra* n.73, para. 12. (Footnote omitted.)

336. *Id.*, referring in part to 2 Gain & Delaisi, *Les sociétés à responsibilité limitée* (8th ed. 1954), 5: *Sociétés analogues aux sociétés des personnes*.

337. *Id.*, at para. 12 and n.12.

338. In terms of *Burgerlijk Wetboek* § 175 *et seq.*, discussed *inter alia* by Maeijer, *Vennootschapsrecht in beweging:*

leerboek/ .....

leerboek naamloze en besloten vennootschap (3rd ed. 1978), 259 where it is shown that the members of the b.v. are referred to as partners ("vennoten") and not shareholders (" aandeelhouers"). According to Zweigert, *Private Limited Companies*, *supra* n.73, at para. 40, Netherlands doctrine recognized a company as having the character not of a joint stock company, but of a partnership, even prior to the introduction of the b.v.. See too Welch, *The English Private Company - A Crisis of Classification*, (1974) J. Bus.L. 277, 280.

339. Schmitthoff, *How the English discovered the Private Company*, *supra* n.4, at 187. Schmitthoff, *New Concepts in Company Law*, *supra* n.3, at 313 further shows that the G.m.b.H. is further distinguished from the A.G. in that the shares in the G.m.b.H. are called *Geschäftsanteile*, not *Aktien* as in the A.G. and its managers *Geschäftsführer* and not *Direktören* as in the A.G.. Similarily the members of a G.m.b.H. are referred to as *Gesellschafter* (partners) and not *Aktionäre* (shareholders).

340. See Creifelds, *Rechtswörterbuch* (5th ed. 1978), 852. Typical characteristics of the *Personengesellschaft*, are *inter alia*, personal liability of members for the debts of the associates and personal involvement by the associates in the conduct of its business. Creifelds, *op. cit.*, 626 describes a *Kapitalgesellschaft*, on the other hand, in these terms:

> "[A] *Kapitalgesellschaft* is — in contrast to the *Personengesellschaft* — a company where the membership is based solely on the capital co-operation [*i.e. intuitus pecuniae*] and not on personal co-operation [*i.e. intuitus personae*] of the members of the company".

Typical characteristics of this type include freely transferable shares (both actively and passively); members' freedom from liability for company debts and lack of identity between ownership and control, which again is usually found in partnership proper and therefore too in the *Personengesellschaft*. As a corporate person, again, a *Kapitalgesellschaft* enjoys corporate personality.

341. Ripert, *Traité Élémentaire De Droit Commercial*, (*supra* n.32), para. 716.

342. Drury, *Legal Structures Of Small Businesses In France And England Compared*, *supra* n.330, at 515. It is because of the mutual importance of the personal characteristics of associates that their interests in the enterprise *(intérêts)*

are/ ....

are not freely transferable. On the other hand the personality of the individual members is, in the *sociétés de capitaux* typified by the S.A., irrelevant and therefore shares *(actions)* in such entities may usually be transferred freely.

343. Zweigert, *Private Limited Companies, supra* n.73,at para. 6 and n.3 *citing* Gessler, *Probleme der G.m.b.H.-Rechtsform, G.m.b.H.-Rdsch.* (G.m.b.H.-Rundschau) (1966), 102, 103, Limbach, *Theorie und Wirklichkeit der G.m.b.H.* (1966), 22.

344. Zweigert, *Private Limited Companies, supra* n.73,at para. 6.

345. Zweigert, *Private Limited Companies, supra* n.73,at para. 7. Usually the only practical difference influencing the choice between the two institutions in Germany is found in the different systems of taxation applicable to them.

346. Creifelds, *Rechtswörterbuch, supra* n.340,at 626 points out that a G.m.b.H. can be established in such a way that it resembles a *Personengesellschaft*. See too 1, Wiedemann, *Gesellschaftsrecht* (1980), 412 *et. seq.* where the evolution of the *Treuepflicht*, or fiduciary duty, in the G.m.b.H. is explained in terms of the G.m.b.H. being a *Personengesellschaft*.

347. Immenga, *Die personalistische Kapitalgesellschaft* (1970), at 17 and 18 shows that the term,*personalistische*, or, *personenbezogene Kapitalgesellschaft*, developed as a result of tax concessions granted to *Kapitalgesellschaften* in which the personal element predominated. The term *personalistiche Kapitalgesellschaft* was apparently used as early already as 1915 by one Fränkel. Kühn, *Die Minderheitsrechte in der G m b H und ihre Reform, zugleich ein Beitrag zum Wesen der G m b H* (1964), 29 employs the concepts *Personalgesellschaft* (as opposed to *Personengesellschaft*) and *Kapitalgesellschaft* as polar concepts between which the G.m.b.H. takes up a middle position. At the same time Kühn uses the term *personengesellshaftliche*, in the sense of "personal element" indicating that it is a determinative factor in classifying a particular G.m.b.H..

348. Schmitthoff,*How the English Discovered the Private Company, supra* n.4, at 184, *quoting* Gierke, *Handelsrecht und Schiffahrtsrecht* (8th ed. 1958), 407. ("It is typically a small intimate *Kapitalgesellschaft*. From that it follows that it often more or less portrays a tendency towards being a *Personalgesellschaft*".)

349. *Immenga, Die personalistische Kapitalgesellschaft, supra* n.347, at 17 where reference is made to Hornstein, Judicial *Tolerance Of The Incorporated Partnership, infra* n. 498.

350/ .....

350. Ripert, *Traité Élémentaire De Droit Commercial, supra* n. 32 at para. 716. See too *Legal Structures Of Small Businesses in France And England Compared, supra* n. 330, at 515.

351. Ripert, *Traité Élémentaire De Droit Commercial, supra* n. 32 at para. 919. See too the same authority para. 716 and Amos & Walton, *Introduction to French Law* (Lawson ed. 1967), 351. The legislation referred to is *Loi* no, 66 - 537 of July 24, 1966.

352. *New Concepts in Company Law, supra* n.3, at 313.

353. Cooke, *Corporation, Trust And Company, supra* n.153, at 94.

354. *Ibid.*.

355. *British and American Corporation Law, supra* n.24, at 1372.

356. *Supra.* n.203.

357. 14 Geo. 2, c. 37 (1741). See Gower, *British And American Corporation Law, supra* n.24, at 1372 and n.12.

358. Gower, *British and American Corporation Law, supra* n.24, at 1372.

359. *Ibid.* Because the equitable joint stock company was not harnessed into serving the corporate form it has survived to this day to co-exist with the corporation. See generally *Notes: The Joint Stock Company And The Problems Of The Close Corporation,* (1964) 50 Ia.L.Rev. 118, 121, *et seq.*. As the author points out (at 120 n.19) the giant American Express Company was until the mid-sixties still an un-incorporated joint stock company!

360. Cooke, *Corporation, Trust And Company, supra* n.153, at 93.

361. *Ibid.* Gower, *British And American Corporation Law, supra* n.24 at 1372.

362. Gower, *British and American Corporation Law, supra* n.24, at 1372.

363. *Ibid.*.

364. *Ibid.*.

365. Chayes, *Madame Wagner And The Close Corporation,* (1960) 73 Harv. L. Rev. 1532. See too O'Neal, *Close Corporation:*

Existing/ .....

Existing Legislation and Recommended Reform, (1978) 33 Bus. Law. 873.

366. Iacobucci & Johnston, "The Private or Closely-held Corporation" in 2 (Ziegel ed.) *Studies In Canadian Company Law: Corporation and Securities Law in the 'Seventies* (1973) 77.

367. Crane and Bromberg, *On Partnership* (1968), § 26 at 144.

368. *Ibid.* and n.24 where reference is made to *Waugh* v. *Carver* H.Bl. 235 (1793).

369. N.Y. Laws, 45th. Sess., c.244 (April 17, 1822). See O'Neal, *An Appraisal of the Louisiana Law of Partnership*, (1949) 9 La. L. Rev. 306, 488; Bergstedt, *Partnership In Commendam - Louisiana's Limited Partnership*, (1961) 35 Tul. L. Rev. 815, 817 and "Comments" *The Limited Partnership*, (1936) 45 Yale L.R. 895—896.

370. *Ibid.*.

371. *Ibid.*. Bergstedt, *op.cit.*, 817 n.13 shows that the term "corporate partnership" was replaced in the Code of 1825 by the term "partnership in commendam" which is still used today.

372. Lynn, Goldberg and Abrahams, *Real Estate Limited Partnerships* (1977), 2.

373. Bergstedt, *Partnership in Commendam - Louisiana's Limited Partnership*, *supra* n.371, at 817 and n.18.

374. In *Skolny* v. *Richter*, 139 App. Div. 534, 541, 124 N.Y.S. 152, 157 (1910).

375. *Id.*, 139 App. Div. at 541, 124 N.Y.S. at 157 (1910).

376. See n.298 above.

377. As in *Frigidaire Sales Corp.* v. *Union Properties Inc.*, 88Wash.2d 400, 562 P.2d 244 (1977) *noted in*, (1978) 53 Wn. L. Rev. 775.

378. Schwartz, *The Limited Partnership Association - An Alternative to The Corporation For The Small Business With "Control" Problems?* (1965) 20 Rutgers L. Rev. 29, 29; Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises*, *supra*, n.24 at §41.

379. "Notes" *The Joint Stock Company And The Problems Of The*

Close/ .....

Close Corporation, supra n. 359, 126.

380. Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises, supra* n.24, § 41.

381. "Notes" *The Joint Stock Company And The Problems Of The Close Corporation, supra.* n.359, at 126 n. 59.

382. Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises, supra* n.24, § 41.

383. "Notes" *The Joint Stock Company And The Problems Of The Close Corporation, supra* n.359, at 127.

384. *Carle* v. *Carle Tool & Engineering Co.* 36 N.J. Super. 36, 40, 114 A. 2d 738, 740 (1955). In arriving at this conclusion the court after analysing the New Jersey statute said: "[T]he statute plainly indicates that an association formed thereunder attains corporateness: it becomes an entity separate and apart from its members.... It takes on practically every substantial attribute of a corporation. As an artificial being it is endowed with the capacity of suing and being sued, of acquiring, holding and conveying property in that character; the members do not act as individuals or as partners but through and in the name of the corporate body; disposal of members' interest or his death or insolvency does not bring about dissolution".

385. Latty, *The Close Corporation And The New North Carolina Business Corporation Act*, (1956) 34 N.C. L. Rev. 432, 456.

386. Kessler, *With Limited Liability for All: Why Not A Partnership Corporation? supra* n.36, at 259.

387. Carnahan, *Relief to Oppressed Minorities in Close Corporations: Partnership Precepts and Related Considerations*, 1974, Ariz. St. L.J. 409, 412. In the words of Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises, supra* n.24, § 258: "The associate or associates of a close corporation often desire to carry on the business with the external attributes of the corporate form (primarily limited liability), certain tax consequences (minimizing double taxation), and the internal attributes of the individual proprietorship of partnership, *i.e.*, informality of organization and operation, flexibility of financing and distribution of profits, active participation in management, *delectus personae*, and easy dissolution, termination, and liquidation of the business".

388/ .....

388. Kessler, *With Limited Liability for All: Why Not a Partnership Corporation? supra* n.36,at 247 n.73.

389. *Ibid.*.See too, Notes "*Joint Venture Corporations: Drafting The Corporate Papers*, (1964) 78 Harv. L. Rev. 393, 397.

390. "Until and unless the State has cried 'Fiat' over a corporation,"Carr *The General Principles Of The Law Of Corporations*, *supra* n.8,at 164, states, "that corporation - according to the Concession-theory — does not, and cannot exist".

391. Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises, supra*, n.24, § 78 at 108.

392. 4 Pound, *Jurisprudence* (1959), 215.

393. Maitland, *Political Theories, supra* n.151 at 31.

394. *Benintendi* v. *Kenton Hotel*, 294 N.Y. 112, 118;60 N.E. 2d 829,831 (1945).In the early Indiana decision of *Ohio Ins. Co.* v. *Nunnemacher*, 15 Ind. 294, 295 (1860),Mr. Justice Perkins said: "A corporation is a creature existing, not by contract; but, in this country, is created or authorized by statute; and its rights, and even modes of action, may be, and generally are, defined and marked out by statute; and when they are, they can not be changed, even by the contracts of the corporators ", *quoted by* Gower, *British And American Corporation Law, supra* n.24,at 1372. For an earlier pronouncement in this vein see *Head & Amory* v. *Providence Ins. Co.*, 6 U.S. (2 Cranch), 127, 169 (1804), where Mr. Chief Justice Marshall said: "The act of incorporation is to ... [corporators] an enabling act; it gives them all the power they possess; it enables them to contract, and when it prescribes to them a mode of contracting, they must observe that mode ...." *quoted in*, *The Joint Stock Company And The Problems Of The Close Corporation, supra* n.379.

395. 76 N.J. Eq. 592, 75 Atl.568 (Ct. Err & App 1910) reversing 76 N.J.Eq. 185, 74 Atl. 130 (Ch. 1909).

396. 76 N.J. Eq. at 599, 75 Atl. at 571. The court further held that upon grounds of public policy the plaintiff's submissions could not be tolerated as it would render "nugatory and void the authority of the Legislature — a co-ordinate branch of the government — established by the Constitution in respect to the creation, super-

vision/ .....

vision, and winding up of corporations".

397. 3N.Y. 2d 444, 144 N.E. 2d 415, 165 N.Y.S. 2d. 745 (1957).

398. 3 N.Y.2d at 449-50, 144 N.E.2d at 418, 165 N.Y.S. 2d. at 750. Though it was stressed that a joint venture may not be carried on by individuals *through* a corporate form, it was acknowledged that corporations may be parties to a joint venture. See too *Joint Venture Corporations : Drafting The Corporate Papers, supra* n.389, at 397.

399. See too O'Neal & Payne, *Close Corporations* (2d ed. 1979), [herein later cited as O'Neal, *Close Corporations*] § 5.05 and n.3; *Ballantine On Corporations* (Revised ed. 1946), § 183 at 423 and n.96.

400. Conway, *The New York Fiduciary Concept In Incorporated Partnerships And Joint Ventures*, (1961) 30 Fordham L. Rev. 297, at 309, for instance eloquently reasons that this is not the case and concludes "such a postulate is a mere *ipse dixit*, a generalized assumption without reason or precedent to support it ... no policy of the law exists which would preclude legal recognition of the dual incidents of limitation of liability and a fiduciary relationship". Latty, *The Close Corporation And The New North Carolina Business Corporation Act, supra* n.385, at 437, dismisses the pronouncement in *Jackson* as having a "certain verbal plausibility and superficial attractiveness ... but nothing more". See too O'Neal, *Close Corporations, supra* n.399, § 5.05 and n.5.

401. O'Neal, *Close Corporations, supra* n.399, § 1.02.

402. Kessler, *With Limited Liability For All: Why Not A Partnership Corporation?, supra* n.36, at 255. For problems encountered in defining the term "close corporation" see *Corporations - Definition of the Close Corporation*, (1963) 16 Vand. L. Rev. 1267, 1268 and n.6 See too n.435 hereunder.

403. *Cf.* Kessler *ibid.* and compare text to n.251 *supra*.

404. Del. Code Ann. Tit. 8, § 342 (1974); Pa. Stat. Ann. Tit. 15 §§ 1371 - 72 *cited by* O'Neal, *Close Corporations, supra* n.399 at § 1.02 and nn. 13 & 14.

405. Ill. Rev. Stats. c.32, §§ 1203(a), *cited by* O'Neal, *loc. cit.*.

406/ .....

406. O'Neal, *Close Corporations: Existing Legislation and Recommended Reform,* (1978) Bus. Law. 873, 877.

407. Ann. Code Md. Tit. 4 §§4-101, (201) (a) , *cited by* O'Neal, *Close Corporation Legislation and Recommended Reform, supra* n.406, at 873, 877 and n.22.

408. Cal. Corp. Code §158(a), Cal. A.B. 376(1975), *noted by* O'Neal & Magill, *California's New Close Corporation Legislation,* (1976) 23 U.C.L.A. L.Rev. 1155, 1156 & n.7; Jordan, *The Close Corporation Provisions Of The New California General Corporation Law,* (1976) 23 U.C.L.A. L. Rev. 1094, 1096 & n.9; Bradley, *A Comparative Assessment of the California Close Corporation Provisions and a Proposal for Protecting Individual Participants,* (1977) 19 Corp. Prac. Comm. 281, 285 & n.8.

409. The *Model Business Corporation Act,* was initiated and conceived by the Committee on Corporate Laws of the Corporation, Banking and Business Law Section of the American Bar Association. It was modelled in large part on the *Illinois Business Corporation Act,* 1933. Since it was first published in 1950, it has been adopted in substantially its present form by more than half of all the states and followed by many more. (Sebring and others, *Model Business Corporation Act Annotated* (2d ed. 1973), ix and Cary, *Cases and Materials On Corporations* (4th ed. 1969), 11.) As such the *Model Business Corporation Act* has replaced the earlier *Uniform Business Corporation Act* which was promulgated and approved by the National Conference of Commissioners on Uniform State Laws and the American Bar Association in 1928. Although subsequently redesignated a Model Act, it was withdrawn from active promulgation in 1957. (Knepper, *Liability Of Corporate Officers And Directors* (2d ed. 1973), para. 1.01.)

410. *Proposed Statutory Close Corporation Supplement To The Model Business Corporation Act,* §§3(a). The draft referred to is the seventh draft dated March 1 1981 and will hereinlater be cited as the *Proposed Statutory Close Corporation Supplement.* Gratitude is expressed to Professor Harry J. Haynsworth of the Faculty of Law, University of South Carolina, for making this draft and other papers available to the author. See also Haynsworth, *The Need for a Unified Small Business Legal Structure,* (1978) 33 Bus. Law. 849.

411. *Proposed Statutory Close Corporation Supplement,* §§ 3(b)

412/.....

412. Carnahan, *Relief to Oppressed Minorities in Close Corporations: Partnership Precepts and Related Considerations*, *supra* n.387, at 411 and n.15.

413. *Close Corporations*, *supra* n.399, § 1.02.

414. *Ripin* v. *United States Woven Label Co.*, 205 N.Y. 442, 447, 98 N.E. 855, 856 (1912) *cited by* O'Neal, *Close Corporations*, *supra* n.399, § 1.02 at 3 and 5 and n.9.

415. Per Shearn, J., dissenting judgment in *Cuppy* v. *Ward*, 187 App. Div. 625, 639, 176 N.Y.S. 233, 243 (1st Dept. 1919) *cited by* O'Neal, *Close Corporations*, *supra* n.399, § 1.02 at 2 and 6 and n.10.

416. Luna, *Protection of Minority Interests through Stockholders' Agreements: A Commentary on Section 9 of the New York Stock Corporation Law*, (1953) 28 Philippine L.J. 506, 535 *cited by* O'Neal, *Close Corporations*, *supra* n.399, § 1.02 at 3 and 6 and n.11.

417. *Donahue* v. *Rodd Electrotype Co. of New England, Inc.*, 367 Mass. 578, 328 N.E. 2d 505 (1975) *noted by* Ribbens, *Close Corporations*, (1977) De Rebus Procuratoriis 247, *in* (1975) 89 Harv. L. Rev. 423 *and in* (1976) 61 Cornell L. Rev. 986.

418. *Donahue*, *supra* n.417, 367 Mass. at 586, 328 N.E. 2d at 511-12.

419. *Infra* n. 765.

420. *Id.*, at 379.

421. *Donahue*, *supra* n.417, 367 Mass. at 586, 328 N.E.2d at 512, *citing Ripin*, *supra* n.414.

422. *Donahue*, *supra* n.417, 367 Mass. at 587, 328 N.E.2d at 512, *citing in the Matter of Surchin* v. *Approved Bus. Mach. Co. Inc.*, 55 Misc. 2d 888, 889, 286 N.Y.S. 2d 580, 581 (Sup. Ct. 1967).

423. *Donahue*, *supra* n.417, 367 Mass. at 587, 328 N.E.2d at 512, *citing Kruger* v. *Gerth* 16 N.Y. 2d 802, 805, 263 N.Y.S 2d. 1,3,210 N.E. 2d 355, 356 (1965).

424. Broden & Scanlan, *The Legal Status Of Joint Venture Corporations*, (1958) 11 Vand. L. Rev. 673, 674-676; O'Neal, *Close Corporations*, *supra* n.397, § 1.06a; Notes: *Joint Venture Corporations: Drafting The Corporate Papers*, *supra* n.389 at 424. "The joint venture corporation differs from a two-man corporation", the latter note observes, "primarily in that its shareholders are themselves corporations whose stock may be widely owned and traded".

425. O'Neal, Close Corporations, *supra* n.399, § 1.06a.

426. *Ibid.*.

427. *Supra* n.395.

428. For a collection of these authorities see O'Neal, *Close Corporations, supra* n.399, § 106 b. and nn. 5 and 6; Notes: *Joint Venture Corporations: Drafting The Corporate Papers, supra* n. 389, at 397-398.

429. Weiner, *Legislative Recognition Of The Close Corporation,* (1929) 27 Mich. L. Rev. 273, 284.

430. Weiner, *Legislative Recognition Of The Close Corporation, supra* n.429, at 283. For the present day tax advantages enjoyed by a close corporation see Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises,* n.24 § 262 at 520 and n.3; *Donahue supra* n.417, 367 Mass. at 586 n.12, 328 N.E. 2d at 512 n.12. Painter *Corporate and Tax Aspects of Closely Held Corporations* (1971), 24-39.

431. Weiner, *Legislative Recognition Of The Close Corporation supra* n.430 at 283 and n.25. See too Immenga, *Die personalistische Kapitalgesellschaft, supra* n.347, at 17.

432. Weiner, *Legislative Recognition Of The Close Corporation supra* n.429, at 283-84.

433. For the extensive literature which has developed on close corporations see Soderquist, *Reconciling Shareholders' Rights and Corporate Responsibility: Close and Small Public Corporations,* (1980) 33 Vand. L. R. 1387, 1389 n.9.

434. O'Neal, *Close Corporations: Existing Legislation and Recommended Reform,* (1978) *supra* n.406, at 875 and nn.9, 10, 11 and 12. Delaware, Maryland, Pennsylvania and Kansas have all enacted this type of statute. New Jersey, Michigan and California have, on the other hand, enacted "unintegrated" close corporation statutes, *i.e.* statutes in which the provisions designed to meet the needs of closely held corporations are not set forth in a separate statute or in a separate chapter of the general Business Corporation Act, but are scattered throughout the latter. O'Neal, *op. cit.*, at 878.

435. Conway, *The New York Fiduciary Concept In Incorporated Partnerships And Joint Ventures, supra* n.400, at 304 and nn. 29 and 30. See too O'Neal, *Close Corporations, supra* n.399, § 1.13a and n.9 and O'Neal & Magill, *California's New Close Corporation Legislation, supra* n.408, at 1155 and n.2 and 1156 and n.4.

436. Winer, *Proposing A New York "Close Corporation Law",* (1943) 28 Cornell L.Q. 313. See too n.435 above.

437. O'Neal, *Close Corporations: Existing Legislation and Recommended Reform, supra* n.406, at 873 and 874.

438. Bradley, *A Comparative Assessment of the California Close Corporation Provisions and a Proposal for Protecting Individual Participants*, *supra* n.408, at 282. Noteworthy is the commentator's reference to "hobbling the close corporation by a set of rigidified prescriptions pertaining to how a corporation ought to be set up and operated" and to a "pervasive principle of freedom of contractual planning so that the participants may adopt whatever arrangements they decide are useful and conducive to the success of their venture".

439. *Supra* n. 394. In 1948 the New York legislature legalized high voting requirements and high quorum requirements for shareholder and director action in terms of *N.Y. Stock* Corp. L. *§* 9. See O'Neal, *Close Corporations: Existing Legislation and Recommended Reform*, *supra* n. 406 at 874; Conway, *The New York Fiduciary Concept In Incorporated Partnerships And Joint Ventures*, *supra* n. 400, at 305; O'Neal, *Close Corporations*, *supra* n. 399, *§* 4.14 nn. 5 and 6; Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises*, *supra* n.24, *§* 266 nn. 6, 7 and 8. As the latter authority correctly shows greater-than-normal shareholder quorum/voting requirements enable minority shareholders to veto action at shareholder level; like direct veto provisions they are inconsistent with majority rule and often enhance the probability of deadlock and other paralysis at the shareholder level.

440. *Supra* n. 395.

441. Bradley, *A Comparative Assessment of the California Close Corporation Provisions and a Proposal for Protecting Individual Participants*, *supra* n. 408, at 283.

442. *Ibid.*.

443. N.C. Sess. Laws. 1955 c.1371; N.C. Gen. Stat. *§§* 55-1 to 55-175 *discussed by* Latty, *The Close Corporation And The New North Carolina Business Corporation Act*, *supra* n.385, at 438 and n.19, *by* Bradley, *Toward a More Perfect Close Corporation — The Need for More and Improved Legislation*, (1966) 54 Geo. L.J. 1145, 1150, *and by* O'Neal, *Close Corporations*, *supra* n. 399, *§* 1.14a.

444. N.C. Gen. Stat. *§§* 55-73(b) (1955). It is interesting to observe that *§§* 55-73(a) further provides that a written agreement signed by two or more shareholders to vote their shares as a unit for the election of directors shall be enforceable inter se. The act further declares that a shareholders' agreement shall not be invalid between the parties

thereto because it interferes with the board of directors. Shareholders to such an agreement are, however, saddled with such liability as would otherwise be vested in directors. See O'Neal, *Close Corporations, supra* n.399, §§ 1.14a. For the text of §§55-73(b). See Annexure A, pt.1.

445. Latty, *The Close Corporation And The New North Carolina Business Corporation Act, supra* n.385 at 438.

446. *Ibid.*.

447. S.C. Code Ann. § 12-16.2.(a). Pt.2 of Annexure A sets out the current South Carolina provisions which are found in S.C. Code Ann.§§ 33-11-220(a) and §§311-11-220(b).

448. Fla. Stats. Ann.§§608.70 - 608.77 at§§ 608.75(2). Cary, *Cases And Materials On Corporations, supra* n.409, at 429 describes the latter provision as the pioneering one, Although North Carolina was first to enact a provision upholding shareholders' agreements of the type in question, Florida was first to enact a complete and separate close corporation statute. The Florida provisions validating incorporated partnerships arrangements were couched in positive, not the negative terms used in other similar State provisions. See too (1964) 77 Harv. L. Rev. 1551.

449. O'Neal, *Close Corporations, supra* n.399. at§ 1.14(b).

450. *Ibid.*. and nn. 1.5 and 2.5.

451. Del. Code Ann. Tit.§ 354 (1974) for which see Annexure A, pt.3.

452. Cal. Corp. Code, *supra* n.408,§§ 300(b) for which see Annexure A, pt.5.

453. Bradley, *A Comparative Assessment of the California Close Corporation Provisions and a Proposal for Protecting Individual Participants, supra* n.408, at 286. Bradley sees the drafting model in §§300(b) as tracing back to the pioneer effort of the North Carolina legislature.

454. Bradley, *A Comparative Assessment of the California Close Corporation Provisions and a Proposal for Protecting Individual Participants, supra* n.408, at 290.

455. O'Neal & Magill, *California's New Close Corporation Legislation, supra* n.408, at 1161. These commentators trace §§300(b) back to the Delaware Code of 1974.

456. Cal. Corp. Code, *supra* n.408, §§300(e). Bradley, *A Comparative Assessment of the California Close Corporation Provisions and a Proposal for Protecting Individual Participants, supra* n.408, at 292 expresses the fervent hope that this provision "will convince the courts that limited liability is compatible with a corporate governance structure that varies from the ancient rites of the corporation".

457. *Supra* n.410.

458. *Id.*, §§11(a) for which see pt.4 of Annexure A hereto.

459. *Id.*, §§11(b) for which see pt.4 of Annexure A hereto.

460. For criticism of the negative approach, see Bradley, *A Comparative Assessment of the California Close Corporation Provisions and a Proposal for Protecting Individual Participants, supra* n.408, at 288.

461. *Proposed Statutory Close Corporation Supplement, supra* n.410, §17.

462. 19 Am. Jur. 2d, § 1632 (1965).

463. Israels, *The Sacred Cow Of Corporate Existence — Problems Of Deadlock And Dissolution,* (1952) 19 U. Chi. L. Rev. 778 at 778.

464. *Ibid.*. Chayes, *Madame Wagner And The Close Corporation, supra* n.365, at 1545 refers to the said "sacred cow" as a "kind of judicial solicitude for the lives of fictional persons, creatures of the law ...." This approach is correct. There is in fact nothing sacrosanct about a corporation.

465. Israels, *The Sacred Cow Of Corporate Existence — Problems Of Deadlock And Dissolution, supra* n.463, at 778.

466. *Id.*, at 790 and 791. Both Chayes, *Madame Wagner And The Close Corporation, supra* n.365, at 1546 and Oleck, *Modern Corporation Law, supra* n.257, § 203 at 529, however point out that the partnership analogy should not be stretched too far.

467. Israels, *The Sacred Cow Of Corporate Existence — Problems Of Deadlock And Dissolution, supra* n.463, at 793. "Too precise definition, too onerous requirements as to who may seek relief, and too much rigidity of available remedy," Israels maintains, "will do social harm".

468. Israels, *The Sacred Cow of Corporate Existence — Problems Of Deadlock And Dissolution, supra* n.463 at 793.

469. Folk, *The Model Act and the South Carolina Corporation Law*, (1963) 15 S.C.L.R. 275, 281, *noted by* O'Neal, *Close Corporations*, *supra* n.399, § 1.14(a) and n.11.

470. S.C. Code Ann.§§12-11.1-12.31.2 (1962).

471. In terms of the *Uniform Partnership Act*,§ 32 (1914) a court may decree a dissolution of a partnership on a number of grounds. One such ground is the wilful or persistent breach of the partnership agreement or such other conduct by one partner that it is not reasonably practicable to carry on business in partnership with him. (Compare n.92 above and *Partnership Act*, 1890, *supra* n.62,§§ 35(d).) Another ground is such misconduct by a partner as tends to affect prejudicially the carrying on of the business of the partnerships. Yet another is such other circumstances as render a dissolution equitable. (Compare *Partnership Act*, 1890, *supra* n.62, §§35(f).)

472. *South Carolina Business Corporation Act*, *supra* n.470, §§ 12-22.15.(a)(3).

473. *Id.*, §§ 12-22.15(a)(1).

474. *Id.*, §§ 12-22.15(a)(2).

475. *Id.*, §§ 12-22.15(a)(5).

476. *Id.*, §§ 12-22.15(a)(4).

477. *Id.*, §§ 12-22.15.(f).

478. *Supra* n.470. The provisions of § 12.22.23 are set out in Pt.4 of Annexure B hereto.

479. O'Neal, *Close Corporations*, *supra* n.399, § 1.14(a), at 59.

480. *Supra* n.178. The provisions of § 210 are set out in Pt.1 of Annexure B. These provisions have been superseded by *Companies Act*, 1980, *supra* n.180, § 75 for which see Annexure B, pt.3.

481. *South Carolina Business Corporation Act*, *supra* n.470, §§ 12.23(a).

482. *Id.*, at §§ 12.23(b).

483. *Supra* n.410. The provisions of the proposed § 16 are set out in Pt.5 of Annexure B, hereto.

484. The current South Carolina provisions are found in S.C. Code Ann. § 33-21-150 (1976).

485. For other similar state legislative provisions see Cal. Corp. Code, *supra* n. 408, § 1800; Mich. Comp. Laws Ann. § 450. 1825 (1978); Minn. Stat. Ann. § 301.49(3); N.J. Stat. Ann. § 14A: 12-7 Ann. Supp. (Unpublished materials prepared by Professor H. Haynsworth.)

486. *Proposed Statutory Close Corporation Supplement, supra* n.410, §§ 16(b)(10).

487. *Supra* n.410.

488. *Delaware General Corporation Law, supra* n.404, § 355; N.Y. Bus. Corp. Law §§ 1002(a); N.J. Rev. Stats. § 14A: 12-5; Pa. Stats. Ann. Tit 15, § 1386; S.C. Code Ann. § 12-22.14. See too O'Neal, *Close Corporations, supra* n.399, at § 907.

489. *Cf.* Jordan, *The Close Corporation Provisions Of The New General California General Corporation Law, supra* n.408, at 1146.

490. Bradley, *A Comparative Assessment of the California Close Corporation Provisions and a Proposal for Protecting Individual Participants, supra* n.408, at 283.

491. *Ibid.*.

492. O'Neal & Magill, *California's New Close Corporation Legislation, supra* n.408, at 1167 referring to *Ebrahimi infra* n. 765.

493. Conway, *The New York Fiduciary Duty Concept In Incorporated Partnerships And Joint Ventures, supra* n.400, at 324.

494. *Ibid.*.

495. O'Neal, *Close Corporations, supra* n.399, § 1.14(c), at 75.

496. *Supra* n.410.

497. *Supra* nn. 444, 447, 448, 451, 452, 458 and Annexure A.

498. Hornstein, *Judicial Tolerance Of The Incorporated Partnership*, (1953) 18 Law & Contemp. Prob. 435 at 435.

499. Cary, *Corporations, supra* n. 448, at 20.

500. *Donahue, supra* n.417, and n.423 above.

501. *Ibid.*.

502. *68th Street Apts., Inc.* v. *Lauricella*, 142 N.J. Super.

546, at 560, 362 A2d 78 at 86 (1976) *noted by* O'Neal, *Close Corporations*, *supra* n.399, § 1.02 and n.12.

503. *Supra* n.395. See Note: *Corporations: Does A Joint Venture Agreement to Use the Corporation as a Medium Survive Incorporation?*, (1956) 44 Calif.L.Rev. 590; *Contra* Note: *Incorporation Terminates Obligations Between Joint Venturers*, (1955) 55 Colum.L.Rev. 419.

504. *Williams et al.* v. *Inhabitants Of Milton*, 215 Mass. 1 at 6, 102 N.E. 355 at 356 (1913): "Where persons associate themselves together to carry on business for their mutual profit, they are none the less partners because ... their shares in the partnership are represented by certificates which are transferable and transmissible, and because ... as a matter of convenience (if not of necessity ...) the legal title to the partnership property is taken in the name of a third person." See too *Howe* v. *Chmielinski*, 237 Mass. 532, 130 N.E. 56 (1921), where in fact it was held that the inter se fiduciary relationship of the partners survived the union between trust and partnership.

505. As in *Beardsley* v. *Beardsley* 138 U.S. 262, 11 S.Ct. 318, 321, 34 L.Ed. 928. (1891). In this matter the United States Supreme Court held that the relationship between two stockholders in a railroad corporation was that of joint owners of the undertaking.

506. *Wabash Ry. Co.* v. *American Refrigerator Transit Co.*, 7 F.2d.335,344 (8th. Cir. 1925), *cert. denied*, 270 U.S. 643 (1926). It is significant that in justifying this approach the court had remarked that "there is no particular divinity surrounding the term 'corporation'".

507. *Cf. Oleck, Modern Corporation Law*, *supra* n.257, § 10, at 42-53.

508. In *Wise Realty Co. et al.* v. *Ashby et al.*, 169 Cal. 176, 146 P. 534 (1915).

509. *Id.*, 169 Cal. at 185, 146 P. at 538. (Italics added.) Earlier the court (at 181) had observed that the operations were carried out "through the *instrumentality* of the corporations, the equitable ownership of the stock in ... which ... was in the three associates, the corporations themselves being but convenient *mediums* for the transaction of their business". (Italics added.)

510. As in *Brady* v. *Erlanger*, 165 App. Div. 29, 149 N.Y.S. 929. (1914), *followed in*, *Macklem* v. *Marine Park Homes, Inc.* 191 N.Y.S. 2d 374 (1955). In the former matter an accounting

as in partnership was ordered. Here Scott, J. (at 930) said: "The true state of affairs ... was that the defendant organized the Theatre Corporation to take over his interest in the joint enterprise, and as a *medium* through which he could, with a minimum of risk to himself, carry on the theatre as a business enterprise. ... As between the original parties, it is quite clear that plaintiff and defendant remained co-joint adventurers to the end; the corporation acting as *alter ego* for the defendant". (Italics added.) In the latter matter the court held that the corporation in question was formed subsequent to the commencement of the joint venture, merely as a *conduit* of title and that there was never any intention on the part of the associates to carry on their venture as stockholders in a corporation. The court found that it was very likely that if a third party were involved, the corporate veil would be pierced. The court further found that the facts brought the situation within *Brady* and was consequently not controlled by *Boag, infra* n.535.

511. As in *Urnest* v. *Forged Tooth Gear Company*, 102 Ill. App. 2d 178, 243 N.E. 2d 596 (1968). Here the Illinois court found that the corporate form was used simply as a device to minimize tax, that the corporation was consequently merely the *alter ego* of one of its shareholders, and accordingly that the legal fiction of its distinct corporate existence could be disregarded. And because no interests of creditors or third parties were involved, the court held that it was permissible to disregard the corporate entity in order to adjudicate what was in reality only a dispute between individual members.

512. As in *Kaufman* v. *Catzen et al.*, 130 S.E. 292 (W. Va. App. 1925).

513. *Cuppy* v. *Ward*, 187 App. Div. 625 at 627, 176 N.Y.S. 233 at 236 (1919).

514. *Ibid.*. In principle it should, however, not matter whether the joint venture agreement or arrangement precedes or succeeds incorporation. In fact, none of the statutory provisions set out in Annexure "A" endeavours to draw a distinction between pre-and post-incorporation agreements. It is possible that the distinction drawn by the judiciary between pre-incorporation and post-incorporation agreements is tied up with the fact that the corporate veil is being pierced.

515. 327 Mo. 1030, 40 S.W. 2d 562 (1931).

516. *Id.*, 327 Mo. at 1052, 40 S.W. 2d at 570.

517. *Ibid.*.

518. *Denny, supra* n.515, 327 Mo. at 1053, 40 S.W. 2d at 570.

519. *Ibid.*

520. *Supra* n.395.

521. *Denny, supra* n.515, 327 Mo. at 1055-56, 40 S.W. 2d at 571.

522. In *Latimer et al.* v. *Piper*, 261 Mich. 123, 246 N.W. 65 (1933).

523. *Id.*, 26 Mich. at 125, 246 N.W. at 67. In *Hathaway* v. *Porter Royalty Pool Inc.*, 296 Mich. 90, 733, 295 N.W. 571 (1941), a Michigan court held that the character of an oil royalty pool organized as a joint venture was not changed by its later incorporation because the corporate form was used merely as a convenient medium to carry out the intention of the parties.

524. In *Elsbach* v. *Mulligan*, 58 Cal. App. 2d 354, 136 P.2d 651 (1943).

525. *Id.*, 136 P.2d at 659.

526. In *MacMorris Sales Corporation* v. *Kozak*, 263 Cal. App. 2d 430, 69 Cal. Rptr. 719 (1968).

527. *Id.* 69 Cal. Rptr. at 723.

528. *Supra* n.395. The citation of the decision of the United States Court of Appeals for the second circuit is found in n.534 hereunder.

529. 224 App. Div. 614, 231 N.Y.S. 265 (1928).

530. *Id.* 224 App. Div. at 615, 231 N.Y.S. at 266.

531. *Ibid.*

532. *Supra* n.510.

533. *Supra* n.396. *Macklem, supra* n.510, it will be recalled, distinguished *Boag, infra* n.535, preferring to follow *Brady, supra* n.510 instead.

534. 354 F.2d 483 (2d Cir. 1965).

535. *Jackson, supra* n.395, *Heisman supra* n.396 and *Manacher* v. *Central Coal Co. Inc.*, 284 App. Div. 380, 131 N.Y.S. 2d 671 (1st Dep't 1954). In the latter matter three brothers pursuant to an agreement to maintain equality between themselves in a joint enterprise organized a corporation, subsidiaries and affiliates and allocated shares of stock and management equally among themselves. One brother

assigned his stake to a nominee company which adopted the joint venture agreement but subsequently disposed of the stock to the second brother who thereupon held a 66 2/3% interest in the venture. The third brother unsuccessfully sought a declaratory order that the business was a joint venture and that the stock acquisition by the second brother breached this relationship. The court applied *Jackson, supra* n.395, and held that the joint venture terminated upon incorporation. Courts adopting this view argue that associates should have decided which form of business they desired, and the law governing the enterprise will depend on that choice. Thus in *Boag* v. *Thompson*, 208 App. Div. 132, 203 N.Y.S. 395, 398 (1924), the court held: "He cannot be a stockholder and seek relief as a co-partner or as a joint venturer, for surely he is either one or the other".

536. *Arditi, supra* n.534, at 486-87. (Citations omitted.) The court *inter alia* referred to Conway, *The New York Fiduciary Duty Concept In Incorporated Partnerships And Joint Venturers, supra* n.400; Notes: *Joint Venture Corporations: Drafting The Corporate Papers, supra* n.389; Note: *Corporations: Does A Joint Venture Agreement To Use the Corporation As A Medium Survive Incorporation?, supra* n.503, and *De Boy, infra* n.537. The court went on to observe that the plaintiff was entitled to attempt to show at trial that the intention of the parties to the present suit was, to set up a corporation only as a means of carrying out their joint venture, and held: "If Arditi can show that such an agreement was entered into, and that Arditi and Dubitzky intended the corporation to be merely an instrumentality of the joint venture, the requirements of Fortugno and Macklem would appear to have been met. Nor is there any allegation tending to show that the parties intended their personal joint venture agreement to be merged into and carried on by a corporation".

537. 207 Md.212, 113 A.2d 903 (1955).

538. *Supra* n.395.

539. *De Boy, supra* n.537, 207 Md., at 220, 113 A.2d at 907.

540. *Supra* n.395.

541. 51 N.J. Super. 482, 144 A2d, 207 (App. Div. 1958).

542. *Id.*, 144 A.2d at 218.

543. *Id.*, 144 A.2d at 211. Compare in this regard the *consortium* of co-heirs, the so called ancient *ercto non cito*, of Roman law, which was, however, not a consensual association.

544. 44 Wis. 2d 623, 172 N.W. 2d 12 (1969).

545. *Id.*, 172 N.W. 2d at 17.

546. *Id.*, 172 N.W. 2d at 13-14.

547. 171 Mass. 101, 50 N.E. 509, 41 L.R.A. 189 (1898).

548. *Id.*, 171 Mass. at 108, 50 N.E. at 511. 41 L.R.A. 193 *cited in Dutch Maid, infra* n. 557.

549. 223 Mass. 47, 111 N.E. 687 (1916).

550. *Id.*, 111 N.E. at 688-89.

551. *Ibid.* and at 111 N.E. at 690.

552. 305 Mass. 65, 25 N.E. 2d 215 (1940).

553. *Id.*, 305 Mass. at 68, 25 N.E. 2d at 217.

554. *Id.*, 25 N.E. 2d at 220.

555. 326 Mass. 226, 93 N.E. 2d 537.

556. *Id.*, 326 Mass. at 233, 93 N.E. 2d at 541 *citing, Arnold, supra* n.549 *and Meinhard, infra* n.1101.

557. 131 P.2d 630 Wyo.(1942).

558. *Id.*, at 634. The court here referred to the Massachusetts matter *AnchorElectric, supra* n.547.

559. *Dutch Maid, supra* n.557, at 634. Here the court relied on *Arnold, supra* n.549, *Silversmith, supra* n.552 and *Modlin, supra* n.529.

560. 68 So. 2d 163 (Fla. 1953).

561. *Id.*, at 171. As authority for this proposition, the Florida Court cited the earlier Massachusetts case, *Mendelsohn, supra* n.555.

562. *Infra* n.1101.

563. 4 Ill. App. 2d 206, 124 N.E. 2d 91 (1955).

564. *Id.*, 124 N.E. 2d at 93.

565. 198 Kan. 181, 422 P.2d 932 (1967).

566. *Id.*, 422 P.2d at 941.

567. *Id.*, 422 P.2d at 937.

568. *Ibid.*.

569. *Infra* n. 765.

570. *Colonial Refrigerated Transportation Inc., et al.* v. *George P. Mitchell et al.*, 403 F.2d 541(5th Cir. 1968).

571. Defined by the Texas Court of Civil Appeals in *Griffin* v. *Reilly*, Tex. Civ. App., 275 S.W. 242, 246 (1925) as "a special combination of two or more persons, where, in some specific venture a profit is jointly sought, without any actual partnership or corporate designation".

572. *Colonial Refrigerated Transportation, supra* n.570, at 548-49.

573. 223 Minn. 483, 27 N.W. 2d 648 (1947).

574. *Id.*, at 487 and 493-94.

575. 249 F.2d 482 (D.C. Cir. 1957).

576. *Id.*, at 484 (Italics added.)

577. *Id.*, at 484-85.

578. *Id.*, at 486.

579. *Id.*, at 487.

580. *Id.*, at 486.

581. *Ibid.*

582. *Ibid.* "[T]he former [the stockholder-owners]," Mr. Justice Burger went on to explain, "either personally manage and direct the business or so dominate the directors as to render the latter agents."

583. 339 Mass. 101, 158 N.E. 2d 469 (1959).

584. *Id.*, 339 Mass. at 112, 158 N.E. at 476.

585. *Ibid.*.

586. 344 Mass. 608, 184 N.E. 2d 642 (1962).

587. *Id.*, 344 Mass. at 614, 184 N.E. 2d 646.

588. *Id.*, 344 Mass. at 615, 184 N.E. 2d at 646 where the court referred to *Sher, infra* n.1025, and to *Mendelsohn, supra* n.555.

589. *Supra* n.417.

590. *Id.*, 367 Mass. at 591, 328 N.E. 2d at 514.

591. *Id.*, 367 Mass. 585, 328 N.E. 2d at 511.

592. *Ibid.*.

593. *Id.*, 367 Mass. at 587, 328 N.E. 2d at 512.

594. *Id.*, 367 Mass. at 595, 328 N.E. 2d at 516.

595. *Id.*, 367 Mass. at 593, 328 N.E. 2d at 515. (Footnotes omitted and italics added.)

596. *Infra* n. 1101.

597. *Donahue, supra* n.417, 367 Mass. at 594, 328 N.E. 2d at 516.

598. *Id.*, 367 Mass. at 593, 328 N.E. 2d at 515.

599. *Id.*, 367 Mass. at 593-94, 328 N.E. 2d at 515-16.

600. *Id.*, 367 Mass. at 601, 328 N.E. 2d at 519.

601. Mass. App., 334 N.E. 2d 650 (1975).

602. *Id.*, at 654.

603. *Supra* n.586.

604. *Supra* n.583.

605. Mass. App. 334 N.E. 2d at 654-655.

606. Mass. App. 334 N.E. 2d 650 at 655.

607. *Ibid., citing Holmes* v. *Darling*, 213 Mass. 303, 306, 100 N.E. 611, 612 (1913); *Shulkin* v. *Shulkin*, 301 Mass. 184, 192-193, 16 N.E. 2d 644 (1938).

608. Mass. App. 334 N.E. 2d at 655. (Italics added.)

609. *Id.*, at 656.

610. *Ibid.*.

611. 370 Mass. 842, 353 N.E. 2d 657 (1976).

612. *Id.*, 370 Mass. at 848, 353 N.E. 2d at 661.

613. *Id.*, 370 Mass. at 852, 353 Mass. N.E. 2d at 664.

614. *Id.*, 370 Mass. at 843, 353 Mass. N.E. 2d at 664.

615. *Infra*. n. 765.

616. *Infra*. n.617, at 203 N.E. 2d 584.

617. 32 Ill. 2d 16, 203 N.E. 2d 577 (1965).

618. *Id.*, 203 N.E. 2d 585.

619. *Ibid.*.

620. *Ibid.*.

621. *Id.*, 203 N.E. 2d at 583.

622. *Id.*, 203 N.E. 2d at 583-84.

623. *Id.*, 203 N.E. 2d at 584.

624. *Id.*, 203 N.E. 2d at 583.

625. 301 N.E. 2d 240 (Ind. App. 1973).

626. *Id.*, at 243.

627. *Ibid.*.

628. *Ibid.*, *citing Helms*, *supra* n.575 Conway, *The New York Fiduciary Concept In Incorporated Partnerships And Joint Ventures*, *supra* n.400, *and* Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises*, *supra* n.24, at § 268.

629. *Hartung*, *supra* n.625, at 243.

630. *Ibid.*.

631. 378 N.E. 2d 941 (Ind. App. 1978).

632. *Ibid.*.

633. *Id.*, at 946. The court pointed out that unless the legislature had made specific grant of power to courts allowing such amendments, that power does not exist. Compare however, *Proposed Statutory Close Corporation Supplement*, *supra* n.410 §§ 16(b)(3)for which see Annexure B pt.5.

634. *Id.*, at 946.

635. *Id.*, at 945.

636. *Id.*, at 945 and n.6. The onus in this regard should, however, as has been suggested above — see p.112-113 — statutorily be placed on the corporators to show that they did not intend inter se to be fiduciaries.

637. *Id.*, at 945 *quoting* Conway, *The New York Fiduciary Concept In Incorporated Partnerships And Joint Ventures*, *supra* n.400, *and* Hornstein, *Judicial Tolerance Of The Incorporated Partnership*, *supra* n.498.

638. *Supra* n.575.

639. *Supra* n.625.

640. *Cressy*, *supra* n. 631, at 945.

641. *Ibid.*.

642. *Russel Box Co.* v. *Commissioner Of Corporations & Taxation*, 325 Mass. 536 at 539, 91 N.E. 2d 750 at 752 (1950) *cited in Rizzuto* v. *Onset Cafe Inc. et al.*, 330 Mass. 595 at 597, 116 N.E. 2d 249 at 251 (1953).

643. *Riley* v. *Callahan Min. Co.*, 28 Idaho 525, 545, 155 Pac. 665 (1916), *cited by* Tingle, *The Stockholder's Remedy of Corporate Dissolution* (1959), 40 and n.91.

644. Hornstein, *A Remedy For Corporate Abuse — Judicial Power To Wind Up A Corporation At The Suit Of A Minority*, (1940) 40 Colum. L. Rev. 220 at 220 and n.6.

645. 263 Mich. 561, 248 N.W. 900 (1933).

646. *Id.*, 263 Mich. at 567, 248 N.W. at 902, *citing Miner* v. *Belle Isle Ice Co.*, 93 Mich. 97, 112, 17 L.R.A. 412.

647. *Id.*, 263 Mich. at 567, 248 N.W. at 902 *citing Nashville Pocket Co.* v. *Neville*, 144 Tenn. 698, 235 S.W. 64.

648. *Id.*, 263 Mich. at 568, 248 N.W. at 902, *citing* 14a C.J. pp. 1123, 1124; *Green* v. *National Advertising & Amusement Co.*, 137 Minn. 65, 162 N.W. 1056, L.R.A. 1917 E, 784; *State, ex rel. Conlan*, v. *Oudin, etc., Manfg. Co.*, 48 Wash. 196, 93 Pac. 219; *Nelson* v. *United Elevator Co.*, 115 Kan. 567, 223 Pac. 814.

649. 42 F. 2d 65 (5th. Cir. 1930).

650. *Id.*, at 67.

651. *Supra* n.541.

652. *Id.*, at 219. Earlier the court had pointed out that the general rule was that a corporate entity may not be disregarded and said: "But the principle is not without its exceptions. In refusing to go behind the corporate form the trial judge laid stress on the lack of any allegation of fraud in the setting up of the corporations. However, a court of equity is always concerned with substance, and not merely form ".

653. *Fortugno, supra* n.541, at 219. Earlier, (at 217) the court drew the following distinction and said:

> "A partnership may, of course, be created for the prime purpose of buying and selling shares of stock. In such a situation a partnership goes no further than the stock itself; the partners are not entitled to be considered the equivalent of owners of the corporations in which the stock is held. But the partnership in this case was not engaged in the buying and selling of corporate shares; it conducted a manure business in all of its out-branches. [T]he partnership did not obtain the corporate shares that it did simply as an investment, but acquired them naturally in the course of the evolution and expansion of its prime business. The partnership's stock ownership was not for the purpose of participating in corporate affairs in the normal manner, but was resorted to in order simply to make each corporation an instrumentality or department of the integrated family enterprise ".

654. 15 Misc. 2d 713, 182 N.Y.S. 2d 459 (1959).

655. *Id.*, 182 N.Y.S.2d at 462 *citing* New York State Law Review Commission and New York Leg. Doc. No. 65K, 389 *et seq.* (1948).

656. Prunty, *Business Association*, (1959) 34 N.Y.U. L. Rev. 1425, 1433-34.

657. *Pivot Punch, supra* n.654, at 462-63, *citing, Technical Amendments Act*, (1958) 26 U.S.CA.§§1371 *et seq.*

658. *Pivot Punch, supra* n.654, at 463. (Italics added.)

659. Compare the sentiments expressed by Bacon, V.-C., in *Helmore, supra* n.114 (see n.115).

660. 16 N.Y. 2d 802, 210 N.E. 2d 355 (1965).

661. *Id.*, 210 N.E. 2d at 356 *citing* Hornstein, *A Remedy For Corporate Abuse, supra* n.644 *and Leibert* v. *Clapp*, 13 N.Y. 2d 313, 247 N.Y.S. 2d 102, 196 N.E. 2d 540.

662. *Id.*, 210 N.E. 2d at 356.

663. *Ibid.*.

664. *Ibid.*.

665. *Id.*, 210 N.E. 2d at 357.

666. *Ibid.*.

667. *Supra* n. 397.

668. *Kruger, supra* n.660, at 357 *referring to De Boy, supra* n.537, and *La Varre, supra* n.649.

669. *Kruger, supra* n.660, at 357.

670. *Ibid., citing* Conway, *The New York Fiduciary Concept In Incorporated Partnerships And Joint Ventures, supra* n.400.

671. 286 N.Y.S. 2d 580 (1967).

672. 301 N.Y.S. 2d 839 (1969).

673. *Supra* n.671.

674. *Supra* n.654.

675. *Surchin, supra* n.671, at 584.

676. *Id.*, at 584.

677. *Supra* n.672.

678. *Id.*, at 842.

679. *Ibid.*.

680. *Ibid.*.

681. *Weis, supra* n.672, at 841.

682. *Ibid.*.

683. *Cf.* Oleck, *Modern Corporation Law, supra* n.257 § 188, at 465.

684. *Id.*, § 188, at 464.

685. Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises, supra* n.24, § 257, at 507.

686. Chayes, *Madame Wagner And The Close Corporation, supra* n. 365, at 1543.

687. *Supra* n.417.

688. *Id.*, 367 Mass. at 592, 328 N.E. 2d at 515.

689. *Id.*, 367 Mass. at 587, 328 N.E. 2d at 512.

690. *Supra* n.654.

691. *Id.*, at 463.

692. As *In re European Ass. Soc., supra* n.212.

693. As in *Australian Coal, supra* n.10.

694. *Infra* n.855.

695. *Infra* n.856.

696. *Infra* n.765.

697. *Supra* n.178.

698. *Supra* n.62.

699. *Ebrahimi, infra* n.765, at 375. "The same words 'just and equitable'", Lord Wilberforce observed "appear in the Partnership Act, 1890, section 25 [*sic*], as a ground for dissolution of a partnership and no doubt the considerations which they reflect formed part of the common law of partnership before its codification".

700. *Infra* n.877.

701. *Supra* n.62.

702. *Supra* n.245.

703. *Supra* n.199.

704. *Ibid.*

705. *Morrison* v. *Service* (1879), 6R.1158, 1160. See too text to n. 64 above.

706. *Supra* n.218.

707. 11 & 12 Vict., c.45 (1848).

708. *Supra* n. 62.

709. Mr. Justice Aickin, *Foreword* to Callaway, *Winding Up On The Just And Equitable Ground* (1978), X. As the learned judge points out, the relevant grounds for dissolution were stated by Lindley, *A Treatise On The Law of Partnership Including its Application to Companies* (1st ed. 1860), 180 in a passage which remained the same in all subsequent editions until the passing of the *Partnership Act*, 1890. In those earlier editions, Lindley himself summarized these grounds in three particular categories as examples of the general principle involved. These categories are:
(a) the hopeless state of the partnership business;
(b) the confirmed lunacy of one of the partners, and
(c) misconduct on the part of one or more of the members of the firm, and the *destruction of mutual confidence.*
Conspicuous in its absence is the phrase "just and equitable."

710. Callaway, *Winding Up On The Joint And Equitable Ground* (1978), 2, Huberman, "Winding-up of Business Corporations" in 2 (Ziegel ed.), *Studies In Canadian Company Law: Corporation and Securities Law in the Seventies* (1973), 273, 280. As the former points out, prior to the said enactment, proceedings could only be brought by creditors in the Court of Bankruptcy; thereafter members could bring such proceedings in the Court of Chancery.

711. Callaway, *Winding Up On The Just And Equitable Ground, supra* n.710, at 3. McPherson, *Winding Up on the "Just and Equitable" Ground,* (1964) 27 Modern L. Rev. 282 at 282. The essence of this rule of interpretation — also rendered by the maxim *noscitur a sociis, i.e.* "birds of a feather ...." — is that general words are limited in their meaning because of their association with particular words if they all belong to some one *genus.* Thus the just and equitable ground would, because of its association with the preceding grounds, also be confined to insolvency.

712. *Re Agriculturist Cattle Insurance Co., ex p. Spackman* (1849), 1 Mac. & G. 170, 174 *noted by* McPherson, *Winding Up On The Just And Equitable Ground,* 282 and n.2 *and by* Callaway, *Winding Up On The Just And Equitable Ground, supra* n.710, at 3 and n.18.

713. *Supra* n.226.

714. Callaway, *Winding Up On The Just And Equitable Ground* *supra* n.710, at 2. Although a corresponding provision today no longer appears in the *Companies Act*, 1948, *supra* n.178, it is still found in *R.S.A. Companies Act*, 1973, *supra* n.199, §§344(e).

715. *Supra* n.245.

716. The said ground was the inability of the company to pay its debts (compare *Companies Act*, 1948, *supra* n.178, § 222(e) and *R.S.A. Companies Act*, 1973, *supra* n.199. § 344(f)); the others were respectively, the passing of a special resolution that the company be wound up (compare *Companies Act*, 1948, §§222(a) and *R.S.A. Companies Act*, 1973, §§344(a)); the company not commencing business within a year from incorporation or suspending its business for a whole year (compare *Companies Act*, 1948, §§222(c) and *R.S.A. Companies Act*, 1973, §§344(c)) and the number of members being reduced to below seven (compare Companies Act, 1948, §§222(d) and *R.S.A. Companies Act*, 1973, §§344(d) and see n.238 above.)

717. (1867), L.R.2 Ch. App. 737, 740.

718. Callaway, *Winding Up On the Just And Equitable Ground*, *supra* n.710, at 3 and n.24 *citing Re The New Gas Co.* (Ltd.) (1877), 36 L.T. (N.S.) 364, 366.

719. *Infra* n.733, at 129-130.

720. *Infra* n.753, at 431-432.

721. [1924] A.C. 783, 788-794 (Barbados).

722. *Infra* n.765, at 382-383.

723. *Ibid.*, (Italics added.) For the position in South Africa, see *Redler*, *infra* n.788, at 463; *Moosa*, *infra* n.791, at 148 E-G. and *Emphy et al.* v. *Pacer Properties (Pty) Ltd.* 1979 (3) S.A.L.R. 363 (D.& C.L.D.) 365 H.

724. Huberman, *Winding-up of Business Corporations*, *supra* n.710, at 281.

725. *Ebrahimi*, *infra* n.765, at 375.

726. *Supra* n.721, at 788.

727. *Ibid.*. See too the remarks of Lord President Clyde in *Baird* v. *Lees*, [1924] Sess. Cas. 83, 92.

728. *Ebrahimi, infra* n.765, at 375 *Per* Lord Wilberforce. In the same breath his Lordship had rejected another restrictive interpretation, the tendency of creating categories or headings under which cases must be brought if the just and equitable provision is to apply. Lord Wilberforce rejected this as wrong. "Illustrations may be used", his Lordship said, "but general words should remain general and not be reduced to the sum of particular instances".

729. *In re Blériot Mfg. Aircraft Co. Ltd.* (1916), 32 T.L.R. 253, 255. See too *In re Straw Products Pty. Ltd.*, [1942] V.L.R. 222, 223 affng. 139 for which see n.798 *infra*.

730. *Baird, supra* n.727, at 90.

731. *Ebrahimi, infra* n.765, at 379.

732. *Ibid.*.

733. [1905] 8F. Sess. Cas. 121.

734. [1925] Sess. Cas. 311.

735. *Symington, supra* n.733, at 128 *Per* Lord President.

736. *Ibid.*.

737. *Supra* n.245.

738. *Symington, supra* n.733, at 129. (Italics added.)

739. *Id.*, at 131.

740. *Id.*, at 130. (Italics added.)

741. *Ibid.*. Why this reasoning is not applicable in the case of a public-issue company is obvious: "because if the directors are equally divided, or if there is such a division as makes it difficult to carry on the company's affairs, the remedy of the shareholders is to turn them out and to elect a harmonious board of directors".

742. *Symington, supra* n.733, at 130. (Italics added.)

743. *Ibid.*.

744. *Thomson, supra* n.734, at 312.

745. *Id.*, at 313.

746. *Supra* n.721.

747. *Supra* n.727.

748. *Thomson, supra* n.734, at 316. (Italics added.)

749. *Ibid.*.

750. *Id.*, at 317.

751. *Ibid.*.

752. That term has been used only once in a Scottish decision, namely *Lewis* v. *Haas*, (1970) S.L.T. 67. The term "domestic concern" cropped up again in *Elder et al.* v. *Elder & Watson Limited*, [1952] Sess. Cas. 49, 56.

753. [1916] 2 Ch. 426.

754. *Id.*, at 433 *et. seq.*.

755. *Id.*, at 430 and 434. Here Lord Cozens-Hardy, M.R., had quoted at length from the then current edition of Lindley, *On Partnership*. (See 14th ed. 1979, 625) where "refusal to meet on matters of business, continued quarrelling, and such a state of animosity as precludes all reasonable hope of reconciliation and friendly co-operation..." are given as sufficient grounds for winding-up a partnership proper. The preceding passage in Lindley was subsequently quoted *in extenso* by counsel for the applicant in *In re Davis And Collett, Ltd.*, [1935] 1 Ch. 693, 697, a case in which an incorporated company was wound up as if it were an incorporated partnership when one shareholder, by irregular means, removed his co-shareholder from his office as director.

756. *Yenidje, supra* n.753, at 429.

757. *Id.*, at 430.

758. *Id.*, at 432.

759. *Ibid.*.

760. *Id.*, at 433.

761. *Id.*, at 434.

762. *Ibid.*.

763. *Ibid.*.

764. *Supra* n.755.

765. [1973] A.C. 360 (H.L.(E.)), *reversing sub nom. Re Westbourne Galleries*, [1971] Ch. 799, *reversing*, [1970] 3 All E.R. 374.

766. *Id.*, at 363.

767. *Ebrahimi, supra* n.765 at 380. (Italics added.)

768. *Ibid.*.

769. *Ibid.*.

770. *Ibid.*. (Italics added.)

771. Lord Wilberforce (at 380) referred to *Constable* v. *Harris*, (1824) Tur. & Rus. 496, 525; *Blisset, supra* n.109, and Lindley, *On Partnership* (13th ed. 1971), 331 and 595.

772. *Supra* n.109. Chesterman, *The "Just And Equitable" Winding Up Of Small Private Companies*, (1973) 36 Modern L. Rev. 129, 145 missed the point when he criticized Lord Wilberforce's relying on *Blisset* in this context. Chesterman formulated it thus: "[H]owever, the remedy was not dissolution, but a declaration that the expulsion, having been carried out 'against the truth and honour' of the partnership agreement, was void. Page-Wood V.-C. explained this concept in these words.
'It must be plain that you can neither exercise a power of this description by dissolving the partnership [!] ....'"
Page-Wood, V.-C., did not suggest — as Chesterman's exclamation seems to imply — that dissolution was an inappropriate *judicial remedy* in the particular context. What Chesterman overlooked was that Page-Wood V.-C., had here quoted Institutes 3.25.4 for which see n.97 above and n.773 below. Neither the said Roman law texts, nor *Blisset*, however, debar a court from finding that the all essential inter se relation of mutual confidence, upon which partnership is based has irretrievably broken down and consequently declaring that the partnership should be dissolved. This is clearly illustrated by *Yendije, supra* n.753, and *Lawrence, infra* n.790. What Chesterman did achieve was to highlight the anomaly that English courts do recognize the operation of partnership precepts in company law but then essentially for purposes only of declaring the right-and-duty-bearing unit to be terminated. Subsequently Chesterman, *Small Businesses* (1977), 71 seems to have undergone a change of heart: "This harnessing of a partnership analogy illustrates

also that in appropriate contexts within small business ... loose aspects of fiduciary duties imposed by company law may have to be bolstered up by the stricter fiduciary duties imposed by partnership law".

773. [1970] 3 All E.R. 374, 384. Plowman, J., cited no authority for this proposition in partnership law and it is possible that he may have had the same English decisions in mind which Lord Wilberforce relied upon. A more basic proposition is found, however, in Digest 17.2.65.4 *noted and discussed by* Pothier *Traité du Contrat de Société*, supra n.48, at para. 150, *by* Story, supra n.28, at para. 176 and in Institutes 3.25.4 *cited in Blisset, supra* n.109, at 523. Although the issues raised in the said texts are not entirely *in pari materia* with those raised in *Ebrahimi*, they are nevertheless sufficiently analogous to be relevant in the present context. The issues in the said texts revolved around a partnership at will being renounced by one partner with the object of appropriating for himself profits about to accrue to the partnership. All the said authorities are agreed that although the partner who renounced had an absolute right to renounce, he was nevertheless under a duty to renounce in good faith and that such duty was breached when that absolute right was exercised, contrary to the dictates of good conscience or good faith, or at an inopportune time. A *mala fide* or an *intempestiva* exercise of such an absolute right is viewed as being void and as resulting in an accounting of profits. Clearly the same should apply with regard to the expulsion of one partner from participation in the management of a partnership irrespective of whether or not such partnership is unincorporated or incorporated. Similarly, when such a breach of duty is so serious that it causes the inter se relation of mutual confidence between members to break down, dissolution might, in proper circumstances, be the appropriate remedy. The fact that such a situation was not discussed by the said authorities should be seen in that light that the notion of mutual agency in partnership is of fairly recent origin and was not known to them.

774. *Ebrahimi, supra* n.765, at 380-81.

775. *Id.*, at 381.

776. *Id.*, at 375C; 377C; 379H and 380B.

777. *Id.*, at 379D; 379F; 380E and 380G.

778. Chesterman, *The "Just and Equitable" Winding Up Of Small Private Companies*, supra n.772, at 146.

779. *Ebrahimi, supra* n.765, at 379.

780. *Ibid.*. His Lordship did go on to conclude"...: the words 'just and equitable' sum these up in the law of partnership itself ". That conclusion, however, should not be taken literally. His Lordship was here obviously endeavouring to justify his pre-occupation with the words "just and equitable ". If any term could be said to sum up the concept in question, it would be the term *"intuitus personae"* rather than the term "just and equitable". See Drury, *Legal Structures Of Small Businesses In France And England Compared, supra* n.330, at 524 and 525.

781. *Ebrahimi, supra* n.765 at 380. A case in point is *In re K/9 Meat Supplies (Guildford) Ltd.* , [1966] 1 W.L.R. 1112. Here the trustee of a bankrupt shareholder and director had contended that the company concerned was a quasi-partnership and that, since *Partnership Act*, 1890, *supra* n.62, §33 provided for dissolution on the bankruptcy of one of the partners, a winding-up order was warranted under the just and equitable winding-up provision. Pennycuick, J., did not agree and held that since the "partnership" had been transformed into a company and since the articles gave no automatic right to a winding-up on bankruptcy, bankruptcy of a member did not constitute a ground for winding-up of itself. In *Ebrahimi supra* n.765, at 377, Lord Wilberforce underwrote the reasoning of Pennycuick, J., in this regard.

782. *Ebrahimi, supra* n.765, at 364.

783. *Ibid.*.

784. "[W]e should take only the decision, "Dias & Hughes, *Jurisprudence* (1957), 73 & n. 5 relying on Oliphant, *A Return To Stare Decisis*, (1928) 14 Am. Bar. Ass. J., suggests, "and disregard what the judge had said in giving his decision". See too Lloyd, *The Idea of Law* (1964), 214 and 279: "[W]hat really matters is not words but actions, not what the court *says*, but what it *does*.", and *Collett v. Priest* (1931), A.D. 290, 302 where De Villiers, C.J., said: "[W]hatever the reasons for a decision may be, it is the principle to be extracted from the case, the *ratio decidendi*, which is binding, and *not necessarily the reasons given for it*". (Italics added.)

785. *Ebrahimi, supra* n.765, at 383-84 referring to *Yenidje supra* n.753. Compare the sentiments of ~~Bacon, V-C.,~~ in *Helmore supra* n.114.

786. *Ibid.*. It is thus clear that Lord Cross saw *Yenidje supra* n.753, not as a case of deadlock, but rather as a case of breakdown of confidence.

787. *Id.*, at 386-87.

788. *Supra* n.753, cited for the first time in *Redler* v. *Collier And The Cereal Mfg. Co., Ltd.*, 1923 C.P.D. 458 at 463.

789. *Supra* n.765 cited for the first time in *Emphy*, *supra* n.723, at 365 and 367 - 368.

790. 1948(2) S.A.L.R. 1029 (W.L.D.).

791. 1967(3) S.A.L.R. 131 (T.P.D.).

792. *Lawrence*, *supra* 790, at 1033.

793. *Ibid.*. *Contra* Brightman, J., in Leadenhall, *infra* n.873, at 10 and 11. But see *Ebrahimi*, *supra* n.765, at 379.

794. *Lawrence*, *supra* n.790, at 1030, where reference was made to *Salter*, *supra* n.142, at 264.

795. *Supra* n.721.

796. *Lawrence*, *supra* n.790, at 1030-31. (Italics added.)

797. *Lawrence*, *supra* n.790, at 1033.

798. *Lawrence*, *supra* n.790, at 1034. Here the learned judge explicitly rejected the argument, based on *Loch*, *supra* n.721, at 788, that to justify winding-up the misconduct must be in relation to the company's business. Compare the remarks of Mr. Justice Lowe in *In re Straw Products (Pty.) Ltd.*, [1942] V.L.R. 139, 141 where the latter held that if the aberrant conduct was such that it *furnished just ground for the destruction of confidence*, it would under the statutory provision be just and equitable to grant a winding-up order.

799. *Lawrence*, *supra* n.790, at 1034.

800. Apart from referring to *Salter*, *supra* n.142, Murray, J., observed (at 1032-1033) that a dissolution of partnership would *inter alia* be warranted when it was "impossible for the partners to place that confidence in each other which each has a right to expect...." Here Murray, J., relied on a passage in Lindley as reported in *Yenidje*, *supra* n.753 and *Davis*, *supra* n.755 (for which today see *Lindley*, *supra* n.9 , at 625-26). The said passage in

Lindley was again cited with approval by Broome, J.P., in *Marshall* v. *Marshall (Pty.) Ltd. et al.* 1954 (3) S.A.L.R. 571(N) 579 and was referred to by Léon, J., in *Emphy, supra* n.723, at 366. Here Leon, J., further referred to the Roman-Dutch authority, Kersteman, *Hollandsch Rechtsgeleert Woorden-Boek, s.v. societeit* and to *Fortune* v. *Versluis*, 1962 (1) S.A.L.R. 343 (A.), 349 for the proposition that a partnership could be wound up at the instance of a partner "*omdat zijn mede compagnon zo knibbelziek, injurieus en schadelijk is, dat het ondienstig is hem langer te lyden of verdragen*". [*i.e.* because his fellow associate is so quarrelsome, troublesome and harmful that it is impracticable to put up with or suffer him longer.]

801. For which see n.25 above and compare *Loch*, supra n.721, a matter in which the coheirs of the founder of an engineering business established a consortium for the first time after his death. As in the instant matter, that consortium was carried on through an incorporated company. Upon incorporation, the trustee in the deceased estate became managing director of the company. He was not a shareholder in his own right but merely a nominee for his wife, one of the four equal heirs in the estate and shareholders in the company. As in the present matter, the managing director and trustee abused the confidence reposed in him by the other shareholders. In that matter the only relevant fiduciary relation was the vertical fiduciary relation between the said managing director as trustee, and the company. In the instant matter, because *M* was also a shareholder (and member of the consortium of coheirs), he stood in a lateral fiduciary relation to the other shareholders (and consortium members) as well.

802. *Moosa, supra* n.791, at 137.

803. *Ibid.. citing* McPherson, *Winding Up On the "Just and Equitable" Ground, supra* n.711. In this context Trollip, J., at 136 observed that the statutory just and equitable ground, unlike the preceding statutory grounds found in the same provision, postulated not facts, but only a broad conclusion of law, justice and equity as a ground for winding up.

804. *Moosa, supra* n.788, at 137. The passage cited, is from *Loch, supra* n.721, at 788, a matter in which there was no associative or lateral relation between the aggrieved shareholders and the wrongdoer who was merely a nominee for his wife.

805. *Ibid.*.

806. *Moosa, supra* n.791, at 137 (Italics added.) Trollip, J., acknowledged that the principle involved was derived from *Yenidje, supra* n.753.

807. *Moosa, supra* n.791, at 137-38.

808. *Id.*, at 138 *citing* McPherson, *Winding Up on the "Just and Equitable" Ground, supra* n.711, at 296.

809. *Ibid.*. This approach, as Trollip, J., correctly pointed out, was adopted in *Marshall* v. *Marshall (Pty.) Ltd. et al.* 1954(3) S.A.L.R. 571(N.) and in *Ronaasen et al.* v. *Ronaasen & Morgan (Pty.) Ltd.*, 1935 C.P.D. 562.

810. *Moosa, supra* n.791, at 137.

811. *Id.*, at 142-43. At the instance of *M* the company borrowed money from him and his son at 8% and lent it back to them interest free.

812. Apparently *M* embarked upon an underhand scheme which was aimed at securing the said property for his and his son's personal benefit. *Moosa, supra* n.791, at 146.

813. *Moosa, supra* n.791, at 147. It is interesting to observe that with regard to both above situations *M* had possibly breached the fiduciary duty he owed the company *qua* director which would *inter alia* have entitled the latter to avoid those transactions and claim either loss suffered by it or profit made by the miscreant director.

814. *Moosa, supra* n.791, at 133 and 147.

815. *Moosa, supra* n.791, at 147 (Italics added.)

816. *Moosa, supra* n. 791, at 148.

817. *Moosa, supra* n. 791, at 147.

818. *Ibid.*.

819. *Ibid.*.

820. *Moosa, supra,* n.791 at 148. "No clearer demonstration" Trollip, J., emphasized, "of that breakdown in trust and confidence between them could have been afforded...."

821. *Moosa, supra* n.791, at 148.

822. *Symington, supra* n.733, at 130. See too n.821 above and *Emphy, supra* n.723.

823. *Loch supra* n.721, at 786. The company in question, John Blackwood Ltd., was in fact an incorporated consortium of co-heirs of the founder, the late John Blackwood. See too *Elder* v. *Elder & Watson,* [1951] Sess. Cas. 49, 56.

824. First mooted by counsel in *Davis, supra* n.755, at 695, this term gradually achieved popularity and was used inter alia in *Re Expanded Plugs, Ltd.,*[1966]1 All E.R. 877 Ch.D. ; *Re K/9 Meat Supplies, supra* n.781; *Re Fildes Bros. Ltd.* ,[1970]1 All E.R. 923 (Ch.D.); *Westbourne Galleries supra* n.765 (both court *a quo* and Appeal Court); *Leadenhall, infra* n.873 ; *Pennel infra* n.876 ; *Bentley-Stevens, infra* n.874 and *Re A & B.C. Chewing Gum Ltd.,* [1975]1 All E.R. 1017 (C.A.). In Scotland that term has been used in *Lewis, supra* n.752. The term does not appear to have been used in South African courts yet. It has however, been used in a host of Canadian, Australian, African and Commonwealth decisions.

825. *Lindley, supra* n.9, at 5; Miller, *Partnership, supra* n.56, at 63 and n.51.

826. In the only exception where third party rights were affected *K/9 Meat Supplies, supra* n.781, the court refused to apply partnership principles and thus to recognize the quasi-partnership concept.

827. *Supra* n.178. Compare *R.S.A. Companies Act,* 1973, *supra* n.199, *§§*65(1).

828. In *Tench* v. *Tench Bros Ltd.,* [1930] N.Z.L.R. 403, 414. The company "was really what has been termed an incorporated partnership in which, on the petitioner's allegation, he lost his status as partner and was reduced to a servant or was dismissed".

829. In *Ebrahimi, supra* n.765, at 363 for which see n.766 above.

830. Rider, *Partnership Law And Its Impact On "Domestic Companies," supra* n.323, at 153; Sandars, *Small Business-Suggestions for Simplified Forms Of Incorporation, supra* n.12, *passim.*

831. *A New Form of Incorporation for Small Firms,* Cmnd. No. 8171 (1981), *passim* and §§4.4 and Annex. A, para. 8, at 30.

832. *Small is Beautiful?*, (1981) 2 Bus. L. Rev. 97.

833. *Ebrahimi, supra* n.765, at 364. Compare text to n.402 above.

834. 1 Scott, *On Trusts* (3rd ed 1967), para. 2.3.

835. *Ibid.*.

836. See para. 13 above.

837. *Supra* n.733. For this endeavour see n.742 above.

838. [1951] V.L.R. 458, *noted in Ebrahimi, supra* n.765. at 378.

839. *Id.*, at 465.

840. *Ibid.*. Compare Lord Wilberforce's parallel thoughts in *Ebrahimi, supra* n.765.

841. *Ibid.*. (Italics added.)

842. *Ibid.*.

843. *Infra* n.873.

844. *Id.*, at 10.

845. *Ibid.*.

846. *Ibid.*. *Contra* Smith, J., in *Wondoflex, supra* n.838, at 465; Trollip, J., in *Moosa, supra* n.791, *passim* and Lord Wilberforce in *Ebrahimi, supra* n.765, at 379.

847. *Ebrahimi, supra* n.765, at 364.

848. *Id.*, at 379.

849. *Ibid.*. (Italics added.)

850. *Ibid.*.

851. *Ibid.*. "It is these, and analogous, factors ...." Lord Wilberforce said, "which may bring into play the just and equitable clause". One such analogous factor is, for instance, an understanding or agreement to draw profits in the form of directors' salaries rather than by the fiscally extravagent method of paying dividends

on share capital. (See *Ebrahimi*, at 381 and *Leadenhall*, *infra* n.873 at 10.) Another is the existence in a company's articles of association (or in a shareholders' agreement) of a clause requiring unanimity as for instance in *Lawrence*, *supra* n.790 and in *A & B.C. Chewing Gum*, *supra* n.824. All these "factors" are in fact typical elements in the make-up of a partnership proper.

852. *Supra* n.838. For the said definition see n.841 above.

853. *Supra* n.417. For the said definition see n.418 above.

854. *How the English discovered the Private Company*, *supra* n.4, at 191.

854a. *Ebrahimi*, *supra* n.765, at 379.

855. [1936] Sess. Cas. 183.

856. [1958] 3 All E.R. 66 (H.L. Scot.); 1958 Sess. Cas. (H.L.) 40.

857. This was achieved in three ways. First, approximately a third of all profits accruing to the company from libraries installed on its premises, were passed on to *E* and *W*. Secondly, *W* and *E*, each became entitled to entertainment expenses of half of their salaries. Thirdly, by *ex post facto* halving, in the company's books, the salary earned by the late *A*, *E* and *W ex post facto* increased the commissions to which they were entitled in previous years.

858. *Harris*, *supra* n.855, at 202. Lord Murray cited, *inter alia*, *Nocton*, *supra* n.111 and went on to show how in Chancery, the term "fraud" had come to import breach of a fiduciary duty.

859. *Harris*, *supra* n.855, at 205.

860. *Id.*, at 209.

861. *Per* Lord President Cooper in *Meyer et al.* v. *Scottish Co-operative Wholesale Society Ltd.* [1954] Sess. Cas. 381, 389.

862. *Id.*, at 390.

863. *Supra* n.178. For the provision in question see Annexure B pt.1.

864. *Meyer, supra* n.861 at 391.

865. *Ibid.*

866. *Scottish Co-op Wholesale Soc., supra* n.856, at 84.

867. *Ibid. citing* Lindley, *On Partnership* (11th ed. 1962), 401.

868. *Per* Swinfen Eady J. in *Percival* v. *Wright*, [1902] 2 Ch. 421, 426. For a recent critical analysis of this case see Rider, *Percival v. Wright* — Per Incuriam, (1977) 40 Modern L. Rev. 471.

869. From the following passage, (at 424) it is apparent that counsel only had a vertical fiduciary relation in mind:

"No doubt at law it [the undertaking] belongs to the company, but in equity it belongs to the shareholders, and the directors as trustees for sale of the undertaking cannot purchase the interest of a beneficiary without giving him full information. In this respect the shareholders inter se are in the same position as partners, or shareholders in an unincorporated company. If managing partners employ an agent to sell their business, he cannot purchase the share of a sleeping partner without disclosing the fact of his employment. Incorporation cannot affect this broad equitable principle. It does not alter the rights of the shareholders inter se, though it affects their relations to the external world".

For the effect of incorporation on vertical and lateral relations see para. 7.1. above.

870. For partnership decisions dealing with this principle, see Excursus II. For American decisions upholding this principle in the context of the incorporated partnership context see *Denny, supra* n.515; *Modlin, supra* n.529; *Mendelson, supra* n.555 and *Fewell, supra* n.573.

871. *Bushell* v. *Faith*, [1970]1 All E.R. 53, 58 (H.L.(E.)).

872. *Ebrahimi, supra* n.765, at 379.

873. February 4, 1971, *discussed in* (1971) Sol. J. and *noted in Ebrahimi, supra* n.765, by Lord Wilberforce at 378 and *by* Lord Cross at 387. I am deeply indebted to the late W.J. Sandars of Linklaters Paines, London, who, at my request, was kind enough to procure a copy of this unreported decision, specifically for the purpose of this thesis.

874. [1974]1 W.L.R. 638.

875. *Id.*, at 640.

876. July 25, 1974 *discussed by* Burridge, *Wrongful Rights Issues*, (1981) 44 Modern L. Rev. 40, *and by* Burridge, *Minority Shareholders: A Further Ray of Hope?* (1981), 2 Co. Law. 107.

877. [1976] 2 All E.R. 268. Ch.D. *discussed by* Prentice, *Restraints On The Exercise Of Majority Shareholder Power*, (1976) 92 L.Q. Rev. 502; Ribbens, *The Fiduciary Duty Concept And The Multi-national Entrp.*, (Pt. 9), 1977 12 no.35.S.Afr. Chrt. Acc. 87, 89-90 n.269; Joffe, *Majority Rule Undermined?*, (1977) 40 Modern L.R. 71 and Rider, *Partnership Law And Its Impact On "Domestic Companies"*, *supra* n.323 at 152-53.

878. *Leadenhall*, *supra* n.873 at 7.

879. *Ibid.*.

880. *Ibid.*. (Italics added.) Compare Tingle, *The Stockholders Remedy of Corporate Dissolution*, *supra* n.643, at 36.

881. *Id.*, at 10.

882. *Id.*, at 11.

883. *Ibid.*.

884. Burridge, *Wrongful Rights Issues*, *supra* n.876, at 42.

885. *Id.*, at 42-43.

886. *Id.*, at 44.

887. *Id.*, at 48.

888. *Id.*, at 49. Compare *Ebrahimi*, *supra* n.765, at 380 E, where Lord Wilberforce held that the just and equitable provision nevertheless comes to the assistance of a petitioner "if he can point to and prove some special underlying obligation of his fellow members ... an obligation so basic ...."

889. *Id.*, at 49. Compare *Ebrahimi*, *supra* n.765 at 380 G, where Lord Wilberforce referred to an indisputable inference that the character of the particular association would, "as a matter of personal relation and good faith remain the same". Templeman, J., similarly reasoned

that *S* and *P* would "only have agreed to change from a position of total control to that of a vulnerable minority on the basis that the ratio of 51:49 would remain constant and not be prejudiced by any subsequent manoeuvres of the majority ". Burridge, *loc. cit.*

890. Burridge, *Wrongful Rights Issues*, *supra* n.876, at 49. (Italics added.)

891. The company was incorporated in 1913 by two brothers, (one of whom was the father of *M* and the grandfather of *R*) who carried on business together in partnership as building contractors and shopfitters. The father of *R*, and brother of *M*, had, until his death some seven years before the case conducted the business. After his death there has not been a male member of the Clemens family in the business. Shortly after her father's death *R* resigned as director. *M* however, stayed on as non-executive director.

892. *Clemens*, *supra* n.877, at 280.

893. *Supra* n.109.

894. *Id.*, at 522.

895. *Id.*, at 523 *citing* Institutes 3.26.4. [*sic*]

896. *Supra* n.765.

897. *Id.*, at 380 B-C. See too 379D.

898. *Id.*, at 381 C.

899. *Clemens*, *supra* n.877, at 281. Here the learned judge referred to *Allen* v. *Gold Reefs of West Africa Ltd.* [1900] Ch. 656, 671 for the proposition that majority shareholders [in a public-issue company] must exercise their majority powers, not only in the manner required by law, but also bona fide for the benefit of the company as a whole and that such powers must not be exceeded. *A Fortiori* the members of incorporated partnerships must exercise their powers in that fashion. Foster, J., also, quoting from *Greenhalgh* v. *Arderne Cinemas Ltd.*, [1950] 2 All E.R. 1120, 1126, explained that the phrase "'the company as a whole'" means the "'corporators as a general body'" not "'the company as a commercial entity as distinct from the corporators,'" that is not the right-and-duty bearing unit. The test therefore is "'whether

what is proposed is, in the honest opinion of those who have voted in its favour, for that person's [any individual hypothetical member] benefit'".

900. *Ebrahimi, supra* n.765, at 379: "The 'just and equitable' provision does not ... entitle one party to disregard the obligation he assumes by entering a company, nor the court to dispense him from it. It does, as equity always does, enable the court to subject the exercise of legal rights to equitable considerations; considerations, that is, of a personal character arising between one individual and another, which may make it unjust, or inequitable, to insist on legal rights, or to exercise them in a particular way ".

901. *Clemens, supra* n.877, at 282. "[O]bviously" Foster, J., continued "expressions such as 'bona fide for the benefit of the company as a whole', 'fraud on a minority' and 'oppressive' do not assist in formulating a principle."

902. *Clemens, supra* n.877, at 282.

903. *Supra* n.873 at 7.

904. *See Meskin, infra* n.908, at 800, *Per* Jansen, J., *citing* van den Heever, *Aquilian Damages in S.A. Law* (1944), 45-46. The learned judge and author were, of course, dealing with the standard of the reasonable man the *bonus paterfamilias*. And while the two standards are quite different both in scope and object they share common basic features. The test of the reasonable man is reason: has a person on whom a duty of care rests acted unreasonably or not? The test of the fiduciary (loyal man) is conscience: has the person on whom a fiduciary duty rests, acted unconscionably (disloyally) or not? As such, both tests involve the determination whether there has been a deflection from a norm or ideal standard of conduct of some sort. *See too* Prins, *The Protection Of The Minority Shareholders In A Limited Company At English. South African and Dutch Law, supra* n.4, at 37.

905. *Clemens, supra* n.877 at 282. "But I cannot escape the conclusion", the learned judge observed, conceding that *M* genuinely desired the other directors to have shares and a trust for employees to be established "that the resolutions have been framed so as to put into the hands of Miss Clemens [*M*] and her fellow directors complete control of the company and to deprive the plaintiff [*B*] of her existing rights as a shareholder with more than 25 percent of the votes and greatly reduce her [pre-emption]

rights ..." The said resolutions, Foster, J., explained "are specifically and carefully designed to ensure not only that the plaintiff can never get control of the company but to deprive her of what has been called her negative control".

906. Ribbens, *loc. cit.*. *Cf.* Rider, *Partnership Law And Its Impact On "Domestic Companies"*, *supra* n.323, at 153 and 166 and Prentice, *Restraints On The Exercise Of Majority Shareholder Power*, *supra* n.877, at 506, referring to *Donahue*, *supra* n.417. In the particular context a reference to *De Boy*, *supra* n.537, would have been more appropriate.

907. *Supra* n.868.

908. 1968(4) S.A.L.R. 793 (W.L.D.) 807.

909. *Ibid.*.

910. *Ibid.*.

911. In *Harris*, *supra* n.855, at 204. As it turned out Jansen, J., in vain turned to the duty of disclosure which Roman law and Roman-Dutch law respectively imposed on a seller and referred to Cicero, *De Officiis*, 3.12, De Groot, *De Jure Belli ac Pacis*, 2.12.9 and Pufendorf, *De Jure Naturae et Gentium* (1688), 5,3,2. But, because no contractual relationship existed between *T* and *A*, as the former had not accepted the latter's offer to purchase, the conclusions drawn by these authorities in this regard were of no avail. If *U* were an incorporated partnership and *A* a member thereof, Jansen, J., might, apart from Code 4.37.3., and the many authorities in which that principle has been adopted, appropriately have referred to Cicero, *Pro Roscio Amer.* 40 for which see Excursus II & n.1092 and which have been cited by Pufendorf, *op. cit.*, 5.8.4. and by Story, *Partnership*, *supra* n.28, § 172.

912. See para. 20.3.4.3 above, in general, and the decisions referred to in footnotes 515, 529, 555 and 573 in particular dealing with the purchase by one member, of an incorporated partnership, of the shares of a fellow member. As it turned out Jansen, J., (at 804-806) referred to Prosser, *Handbook Of The Law Of Torts*, (3rd ed. 1964), 710 *et. seq.*, to the *Restatement of the Law of Contracts*, 472 and to the *Restatement of the Law of Torts*, 551.

913. *Leadenhall*, *supra* n.873, at 7. As it turned out Jansen, J., (at 796 and 805) referred to Spencer Bower, *Law relating to Actionable Non-disclosure* (1915), paras. 184, 223, 629; Spencer Bower, *Law of Actionable Misrepresentation* (2d ed. 1927), para. 91 and Salmond and Williams, *Contract* (1954 ed.), 278.

914. 1975(2) S.A.L.R. 783 (W.L.D.).

915. 1978(1) S.A.L.R. 1109 (A.).

916. 1981(1) S.A.L.R. 274 (W.L.D.).

917. *Id.*, at 276. Very little information is given on the company in question apart from the fact that it operated in the field of drilling and prospecting for minerals. It had only two shareholders *B* and *V* who each held respectively 75 and 73 shares. *B* had always been engaged in drilling operations. *V*, on the other hand, had worked on the mines for many years where he had acquired considerable experience in the same field. *B* had frequently requested *V* to go into business jointly with him. Eventually *V* left the mines and joined *B* and the company. *Prima facie* it would appear that the company was an incorporated partnership.

918. *Super Safes, supra* n.914 at 786. The reference to "by means of the machinery of a limited liability company" is reminiscent of the words of Lord Warrington in *Yenidje, supra* n.753, at 434 for which see n. 761 above. It also reminds of the phrase often used in American decisions namely "partnership carried on through the instrumentality of a corporation". It is not without significance that similar phraseology was used shortly thereafter in *Bellairs supra* n.915 at 1132E-F.

919. *Ibid.*. This ruling should be compared with the ruling of Mr. Justice Kimball in *Dutch Maid, supra* n.557. There the restraint was not unreasonable and thus was justified However, because the applicant acted unconscionably and did not come to court with clean hands, that application too was refused.

920. Unreported judgment delivered in the Supreme Court of South Africa, Witwatersrand Local Division on 27th November 1974 in case no. 8025/1971 *sub. nom. Hodnett et al.* v. *Bellairs*.

921. *Infra* n.1101.

922. *Bellairs, supra* n.915, at 1132F.

923. *Id.*, at 1121.

924. *Supra* n.791, at 147 for which see n. 815 above.

925. *Hodnett, supra* n.920, at 65.

926. *Lewis, supra* n.752, at 68 and the English authorities cited there.

927. *Infra* n.1101.

928. 1905 T.S., 255 reversed on appeal *sub nom. Trimble et al.* v. *Goldberg*, 1906 T.S. 1002 (P.C.). Here *G*, *T* and *B* entered into a partnership arrangement with a view to buying for purposes of resale, certain properties and shares in a company owning a number of further properties most of which adjoined the firstmentioned properties. *T* and *B*, without the knowledge of *G* purchased from the company half of the properties which adjoined the firstmentioned properties and resold them at a profit. The Transvaal Supreme Court ruled that *T* and *B* were liable to account to *G* for the profits realized on the sale of the said properties in that their acquisition was in conflict with the interests of the partnership and incompatible with the fiduciary relationship existing between partners. The Privy Council reversed, holding that the purchase of the *particular* properties did not fall within the scope of the partnership business and had not been shown to have been in rivalry with or injurious to it.

929. *Hodnett, supra* n.920, at 106 where Botha, J., cited the following passage from the judgment of Innes, C.J., "'If a partner in breach of his duty acquires property *intimately connected with the business of the partnership*, and *which it is detrimental to its interests that he should hold for himself*, he ought to be held to have acquired it for the partnership *even though it may not fall directly within the scope of the firm's business*'". (Botha, J.'s, emphasis.) See *Goldberg supra* n.926, at 267-268. Innes C.J. here referred to two old English authorities *Featherstonhaugh* v. *Fenwick*, 17 Ves.298 and *Russel* v. *Austwick*, 1 Sim. 52. The reference to "detrimental to its [the partnerships] interests" reminds one of Digest 17.2, 65,5. (for which see n. 96 above) and of Pothier, *Traité du Contrat de Societe*, *supra* n.48, para 59 where this problem is discussed with clear insight. According to Pothier, when a partner usurps an opportunity which "was advantageous and belonged to the species of business which was the object of the partnership, and it would have been for the *interest of the partnership*" to have acquired such opportunity for itself, such errant partner can be compelled by his co-partners to account "for he *ought not prefer his private interests to that of the partnership*, nor to take away from it an advantageous bargain by making it on his own private account". (Tudors translation.)

930. *Hodnett*, *supra* n.920, at 119-128.

931. Compare *Hartung*, *supra* n.625 and *Cressy*, *supra* n.631.

932. The following submissions are contained in paras. 46 and 47 of the written heads of argument filed on behalf of *B*, *viz.*:"*Scope of Joint Venture — Fiduciary Duty*. 46. It is submitted that the facts demonstrate that Bellairs and Hodnett entered into a joint venture or limited partnership such as discussed in Pothier on partnership chapter 11 section 2, and *Bester* v. *van Niekerk* 1960(2) S.A. 779 (A.D.) at 784. The fact that they used their company as a vehicle for their venture cannot effect the substance of their relationship in a case in which the disputes are in substance disputes between the two of them. It is respectfully submitted that the Court a quo in refusing to lift the veil has allowed light to be blotted out. 47. Furthermore it is submitted that the Court a quo has, by declining to have regard to the true substratum, misdirected itself by speaking of the "germ of further acquisitions" and by, in effect, placing the onus on Bellairs to show that there was an express agreement limiting the venture's business simply because in form, a company and not a partnership was used. It was for Hodnett to show that the venture extended to N.20 and Unlenhorst, not for Bellairs to prove the opposite. A company, like a partnership, may decide to extend its business. There is no intrinsic reason why a two-man company with a limited business should be found to be more subject to such an extension than a partnership ".

933. *Bellairs*, *supra* n.915, at 1130.

934. *Ibid.*

935. *Id.*, at 1131.

936. *Id.*, at 1131, 132D and 132E.

937. *Id.*, at 1132E-F.

938. *Supra* n. 541.

939. *Bellairs*, *supra* n.920, at 1132.

940. *Supra* n.928, at 1006. In *Hodnett*, *supra* n.920, at 106 Botha, J., correctly found that the conclusion arrived at by the Transvaal Court is to be preferred to that of the Privy Council. In the Appellate Division counsel for *H* submitted that the Privy Council did not appear to dissent from the statement of principles to be applied, but apparently considered that the facts did not disclose

a real conflict of interests. The Full Bench appears to have adopted this approach, thus leaving the Transvaal court decision intact.

941. *Goldberg, supra* n.928 at 273.

942. *Bellairs, supra* n.915, at 1132.

943. *Ibid.*.

944. *Supra* n.928.

945. *Infra* n.1101.

946. *Legal Structures of Small Businesses In France and England Compared, supra* n.330, at 524. For the meaning of this concept see Excursus II.

947. *Supra* n.915.

948. "A trust", Maudsley, *Hanbury's Modern Equity* (9th ed. 1969), 85 states, "is a relationship recognised by equity which arises when property is vested in (a person) or persons called the trustees, which those trustees are obliged to hold for the benefit of other persons called *cestuis que trust* or beneficiaries".

949. Naude, *Die Regsposisie Van Die Maatskappydirekteur* (1970), [hereinafter cited as "Maatskappy Direkteur"] 222.

950. Eckert, *Shareholder And Management: A Comparative View On Some Corporate Problems In The United States And Germany*, (1960) 46 Ia. L. Rev.12, 70 *noted by* Naude, *loc. cit.*, who correctly points out that Mestmäcker, *Verwaltung, Konzerngewalt und Rechte der Aktionäre* (1958),209 in fact goes so far as to declare that there is no institution in German Law which, as far as the question in particular of liability is concerned, can be compared with the consequences of fiduciary relations and fiduciary duties.

951. Weber, *Treu und Glauben* (1961), 101; Naude, *Maatskappy Direkteur, supra* n.949, at 218.

952. Würdinger, *Aktien - und Konzernrecht* (2d ed. 1966), 49-50, Naude, *Maatskappy Direkteur, supra* n.949, at 219.

953. Weber, *Treu und Glauben, supra* n.951, at 103, 104-105; Naude, *Maatskappy Direkteur, supra* n.949, at 219 & n.3 and the authorities cited there.

954. *Der Treuegedanke im modernen Privatrecht* (1947), 18 *cited by* Naude, *Maatskappy Direkteur, supra* n.949, at 218. [Present author's emphasis.]

955. See for instance, *Jura Europae, Gesellschaftsrecht* (1966), para. 10.00.14. cited by Naude, *op. cit.*.

956. *Die Rechtslehre vom Vertrauen* (1950), 66.

957. *Ibid.*.

958. *G.m.b.H.- Gesetz* (13th ed. 1970).

959. *Id.*, at 69 referring to R.G. *146*, 76 and 394 and to R.G. *158*, 248.

960. *Id.*, at 69 referring to R.G.D.R. *40*, 2177.

961. *Id.*, at 69.

962. Kühn, *Die Minderheitsrechte in der G.m.b.H. und ihre Reform, supra* n.347, at 32.

963. *Ibid.*.

964. *Id.*, at 29.

965. *Id.*, at 29-30.

966. *Id.*, at 32.

967. *Id.*, at 32 and the authorities cited in n.122.

968. *Id.*, at 32 and the authorities cited in n.123.

969. Wiedemann, *Gesellschaftsrecht, supra* n.346, at 413.

970. *Ibid.*.

971. *Ibid.*.

972. *Ibid.*. Wiedemann mentions a breakthrough being achieved in the landmark I.T.T. decision, B.G.H.Z. 65, S. 15ff.

973. *Supra* n.611.

974. *Die personalistische Kapitalgesellschaft, supra* n.347, at 185.

975. *Id.*, at 186 and nn.191 and 192 referring to *Helms, supra* n.575 and *Samia, supra* n 583.

976. *Supra* n.669.

977. *Die personalistische Kapitalgesellschaft, supra* n.347, at 261.

978. *Ibid.* Immenga submitted that the fiduciary obligations imposed in American law on majority shareholders exercising their voting rights at shareholders' meetings in dealing with the company's affairs, were based on the concept of trust. "The majority" he explained, "is considered to be the trustee administering third party assets". For the development of these fiduciary duties see n. 1011 below.

979. *Id.*, at 262.

980. *Id.*, at 261.

981. *Id.*, at 261.

982. *Id.*, at 263-264.

983. *Id.*, at 264. These very words are cited at 271 and n.512 where reference is made to B.G.H.Z. 9, 157, 163.

984. *Id.*, at 264 and n.478, citing B.G.H.Z. 14, 25/38.

985. *Id.*, at 270-275.

986. *Id.*, at 271.

987. *Id.*, at 273.

988. *Ibid.*

989. Drury, *Legal Structures Of Small Businesses In France And England Compared, supra* n. 330, at 524-525.

990. Digest 17.2.63. Compare, n.84 above.

991. *Traité Élémentaire De Droit Commercial, supra* n. 32, at para.721.

992. *Ibid.*.

993. As in judgment of April 27, 1971, Cour de cassation, Cass. comm., [1971] Bulletin des arrêts de la Cour de cassation 4 no 116, 111.

994. Digest 17.2.65.5 for which see nn. 96, 108, 121 and 128 above.

995. As in judgment of October 11 1967, Cour de cassation, Cass. comm., [1968] Dalloz 136.

996. Lattin, Jennings & Buxbaum, *Corporations Cases And Materials*,)4th ed 1968) at 12-13.

997. Kessler, *With Limited Liability For All: Why Not A Partnership Corporation?*, *supra* n.36, at 260 referring to *Meinhard*, *infra* n. 1101.

998. O'Leck, *Modern Corporation Law*, *supra* n.257,§ 188 at 464.

999. Henn, *Handbook Of The Law Of Corporations And Other Business Enterprises*, *supra* n.24,§ 257 at 507.

1000. O'Neal, *An Appraisal of the Louisiana Law of Partnership*, *supra* n. 369, 367.

1001. Winer, *Proposing A New York "Close Corporation Law,"* supra n. 436 , at 321 (Footnotes omitted.)

1002. *Infra* n.1101.

1003. Winer, *Proposing A New York "Close Corporation Law,"* *supra* n.436 at 322. In order to remove any doubt as to the operation of fiduciary duties inter se close corporators, Winer opined that a statute clearly creating fiduciary obligations, was desirable. See too Berle *Developments In the Pattern Of Corporate Joint Enterprise*, (1959) 14 Bus Law. 309, 312.

1004. *The New York Fiduciary Concept In Incorporated Partnerships And Joint Ventures*, *supra* n.400, at 311.

1005. *Ibid.*.

1006. *Ibid.*.

1007. *Infra* n.1101.

1008. *The New York Fiduciary Duty Concept In Incorporated Partnerships And Joint Ventures*, *supra* n.400, at 313.

1009. *Madame Wagner And The Close Corporation*, *supra* n.365, at 1532.

1010. *Id.*, at 1543.

1011. Henn, *Handbook Of The Law Of Corporations And Other*

Business Enterprises, supra n.24, § 268 and § 240. In public-issue corporations the imposition of fiduciary duties on controlling stockholders in favour of non-controlling stockholders results from taking one of two routes. In terms of the older approach - appropriately termed the indirect approach - account is taken of the relationship between the dominant stockholders and the directors. If the dominant stockholders dominate the corporation through their influence over the board of directors, then such stockholders are burdened with directors' (vertical) fiduciary duties *vis-à-vis* non-controlling stockholders. In effect, agency principles are used to extend the fiduciary obligations of directors to controlling stockholders. In terms of a more recent approach — the "direct" approach — account is taken of the (lateral) relation between the majority and minority shareholders. Because the majority's position of superiority and influence compels the minority to rely upon principles of good faith and fair dealing, equity establishes a (lateral) fiduciary relation between the majority and minority stockholders. *Notes: The Fiduciary Relation of the Dominant Shareholder to Minority Shareholders*, (1958) 9 Hastings L.J. 306; *Fiduciary Duties of Majority or Controlling Stockholders*, (1958) 44 Ia. L. Rev. 734, 742.

1012. *Supra* n.417, 367 Mass., at 594 & n.20; 328 N.E. 2d, at 516 & n.20.

1013. *Supra* n.522, at 68.

1014. *Supra* n.560, at 171.

1015. *Supra* n.575, at 487.

1016. *Supra* n.586, 344 Mass., at 615-616, 184 N.E. 2d, at 646, 647.

1017. *Supra* n.549, at 690.

1018. *Supra* n.565, at 937 and 941.

1019. *Supra* n.631.

1020. *Id.*, at 945.

1021. *Id.*, at 946.

1022. *Supra* n.515, 327 Mo., at 1092-1093, 40 S.W. 2d, at 590 citing *Meinhard, infra* n.1101.

1023. *Supra* n.529, at 266.

1024. *Supra* n.573, at 494.

1025. 325 Mass. 348 at 353-354, 90 N.E. 2d 537 at 539.

1026. *Supra* n.514, at 184.

1027. *Supra* n.555, 326 Mass. at 233, 93 N.E. 2d at 541.

1028. *Supra* n.417, 367 Mass. at 600 and 603, 328 N.E. 2d 505 at 519 and 520. See too *Kruger, supra* n.660.

1029. *Supra* n.537, 207 Md. at 217 and 224, 113 A. 2d 903 at 906 and 909. See too *Wilson, supra* n.586, 344 Mass. at 617, 184 N.E. 2d at 645.

1030. *Supra* n.601, at 655.

1031. *Supra* n.625, at 243.

1032. *Supra* n.583, 339 Mass. at 123, 158 N.E. 2d at 482.

1033. 380 F.2d 897, 903 (1967). (2d Cir. 1967).

1034. *Supra* n.611, 370 Mass. 842, at 852 and 854, 353 N.E. 2d 657, at 664.

1035. *Supra* n.660, at 356.

1036. *Supra* n.654, at 463.

1037. *How the English discovered the Private Company, supra* n.4, at 185.

1038. "Introduction" to (Frommel & Thompson ed.) *Company Law in Europe* (1975), para. 54.

1039. *Ebrahimi, supra* n.765, at 380.

1040. *Cf. Ebrahimi, supra* n.765, at 379.

1041. *How the English discovered the Private Company, supra* n.4, at 187.

1042. Chayes, *Madame Wagner And The Close Corporation, supra* n.365, at 1532.

1043. *Supra* n.62.

1044. For the history of this Act which today is law in the greater part of the United States see Crane and Bromberg, *On Partnership*, *supra* n.367, § 2, at 13 and 16. According to 47 C.J., § 36 (1929) the *Uniform Partnership Act* is partially based on the English *Partnership Act*, 1890.

1045. *Supra* n.781.

1046. Reference to the little academic writing that exists in this field is found in Rider, *Partnership Law And Its Impact on "Domestic Companies"*, *supra* n.323, at 158 n.56.

1047. *Supra* n.753.

1048. *Supra* n.790.

1049. *Supra* n.734.

1050. *Supra* n.733.

1051. *Supra* n.765.

1052. *Supra* n.873.

1053. *Supra* n.765.

1054. *Supra* n.855.

1055. *Supra* n.856.

1056. *Supra* n.915.

1057. *Supra* n.914.

1058. *Supra* n.876.

1059. *Supra* n.877.

1060. *Ebrahimi*, *supra* n.765, 379. Lord Wilberforce did of course here refer to the words "just and equitable". But as his Lordship himself explained, the "conceptions of probity, good faith and mutual confidence, and the remedies where these are absent" developed in the law of partnership, are summed up in the words "just and equitable". Foster, J., in *Clemens*, *supra* n.877,

heeded this admonition but unfortunately took the reference to "just and equitable" too literally.

1061. *A New Form of Incorporation for Small Firms, supra* n. 831, Annex A., at 24-36. These proposals are "in effect for an incorporated partnership with legal personality, the members of which might enjoy a measure of limited liability". *Id.*, §§4.1, at 16. For the question of limited liability compare nn. 149 and 215 above.

1062. Cooke, *Corporation Trust and Company, supra* n. 153, at 182.

1063. *Supra* n. 831. In the words of Gower, *Whither Company Law?* (1981) 15 U.B.C. L. Rev. 385, 386:

> "[T]he United Kingdom, having joined the European Economic Community (E.E.C.) has begun to move away from the Anglo-American group. As a result of the harmonization programme embodied in the flood of Company Law Directives, which have emerged from or are in the pipe-line, we are becoming in- increasingly influenced by the Franco-German system of our civil law partners".

These developments bring into perspective the following statement made by that great Scottish jurist, T.B. Smith, in an address delivered in May 1961:

> "To some extent Scots law has been able to bring English law into closer touch with Civilian ideas.... I should like to think, however, that Scottish law and Scottish lawyers might even yet have a role to play in mediating more actively between countries of the Civil law and countries of the Anglo-American Common law. [I]f Britain were to join Europe...then that part of Britain which is traditionally European and Civilian - Scotland - might help to promote also a juridical rapprochement between the somewhat insular South Britons and their fellow Europeans".

Smith, *Studies Critical and Comparative* (1962), 44.