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Can a Partner also be an Employee or Worker of the Partnership

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The Employee Question Raised

In her judgment in *Clyde & Co LLP v Bates van Winklehof*,[1] Lady Hale asked the following question:

> …is it indeed the law…that a partner can never be an employee of the partnership?.. Suffice it to say that Mr John Machell QC…. mounted a serious challenge to the rule against dual status. Ellis v Joseph Ellis [one of the cases always quoted to give a negative answer] was decided before section 82 of the Law of Property Act 1925 made it clear that a person could contract with himself and others. There are some contracts which a partner may make with the members of a partnership, such as lending them money or granting them a lease or a tenancy. So why should it be legally impossible to be employed… by the partnership?

Why indeed? It is my purpose in this short paper to attempt to provide an answer first to that question, and then to consider, if the answer to that question is in the negative, the consequential issue as to whether a partner may nevertheless be a worker with limited protection rights under the Employment Rights Act 1996.

Lady Hale's judgment was agreed to by Lords Neuberger and Wilson. Lord Clarke went further: in his opinion "there was much to be said for the view" that dual status (of partner and employee) was possible.[2] Only Lord Carnwarth, who, as chair of the Law Commission, presented the Law Commissions' Report on Partnership Law Reform in 2003, rejected the idea.[3]

Context in which the Question Arose

But first it is very important to remember the context in which Lady Hale posed this question. It certainly came from left field. The actual dispute and decision in the

[1] [2014] UKSC 32 at [29]; [2014] 1 WLR 2047.
[2] ibid at [52].
[3] ibid at [59].

case was whether a member of an LLP could be a "worker" within section 230 of the Employment Rights Act 1996 and so entitled to protection in the event of whistleblowing. Such protection is given not only to employees but also to workers (a person who by contract undertakes to do or perform personally any work or services for another party who is neither a client or customer of the business carried on by the individual). Given that by definition a member of an LLP is not a partner within the meaning of the Partnership Act 1890 and that an LLP unlike an English partnership has legal personality,[4] why should that involve questions as to whether partners could also be employees? Despite its name, an LLP is sui generis and not a form of partnership, as the editor of Lindley constantly points out.[5]

The answer is the peculiarly drafted section 4(4) of the LLP Act 2000 which provides that a member of an LLP shall not be regarded *for any purpose* as employed by the LLP unless if he and the other members were partners in a partnership he would be regarded for that purpose as employed by the partnership. If, as has been the traditional view, partnership and employment are mutually exclusive there can only be one answer to that – a member could never be an employee on the hypothesis that he was also a partner. The Court of Appeal in *Clyde* recognised this absurdity (adopting the traditional mutually exclusive position)[6] and suggested a different (purposive) interpretation (asking the question not simply on hypothesis that X was a partner but whether if it was a *partnership w*ould X be a partner or employee).

But that alternative construction was rejected by Lady Hale. In her view, on the rather tenuous basis that Scottish partnerships do have legal personality and that the LLP Act applies equally in Scotland, it was unnecessary to give the section any strained construction.[7] Whatever the position would be if the LLP were a partnership, then for Lady Hale the position is the same in an LLP.

It followed that in order to make sense of the section as Lady Hale read it, literally, she then had to pose the question before us. Only if partnership and employment are not mutually exclusive, will section 4(4) then make sense. She didn't have to answer her own question, however, as she decided that section 4(4) had no application to the "worker" question for LLPs on the basis that the words "employed by" in section 4(4) did not include the question as to whether a member of an LLP could be a worker.[8] She disagreed with Lord Clarke's view to the contrary. Immediately perhaps one can smell a rat here. If a centuries old doctrine is to be overturned to

[4] So that the "employer" would be the LLP and not the other members, which is not the case with an English partnership.
[5] R C I'Anson Banks, *Lindley & Banks on Partnership* (20th edn, Sweet & Maxwell 2017).
[6] *Clyde & Co LLP v Bates Van Winklehof* [2012] EWCA Civ 1207 at [42]; [2013] 1 All ER 844, approving that test as applied by Rimer LJ in *Tiffin v Lester Aldridge LLP* [2012] 1 WLR 1887; [2012] ICR 647 CA.
[7] [2014] UKSC 32 at [21]; [2014] 1 WLR 2047.
[8] This was on the basis of Parliament not wishing to exclude by implication the concept of a worker from LLPs (see below as to whether it follows that a partner may be a worker) and the fact that the extended definition of employment in s 230(5) of the Employment Rights Act 1996 (to cover workers) could not be read into section 4(4): [2014] UKSC [23]-[27]; [2014] 1 WLR 2047.

make sense of a badly drafted statute applicable to a different entity one should surely question cause and effect.

This paper is not concerned with the issues as to whether a member of an LLP can be either an employee or a worker. The latter was answered in the positive in the case by the Supreme Court by simply applying the wording of the definition to the facts without considering whether it was compatible with the particular LLP ethos,[9] and seems to have been accepted without question since, leading to some interesting consequences.[10] LLPs simply are not partnerships. They are hybrids involving some partnership concepts but many corporate ones as well. There are examples of judges treating them the same as partnerships and others where they are regarded as being separate.[11]

As stated above, I am concerned first as to consider whether the concepts of partnership and employment can co-exist and then to consider the "worker" issue on the same point. It is also very important to note that that question is not whether a partner can be an employee of the partnership (as posed by Lady Hale) but, as Lord Carnwath pointed out, whether a partner can be employed by the partners – given that there is no legal personality. [12] It is a common misconception that under English law a partnership exists as a legal entity whereas it is of course actually simply a relationship.[13]

I also make no comment on the position as to the dual capacity situation in Scotland which appears to be uncertain according to the two Law Commissions' joint 2000 Consultation Paper on partnership law. Except to say that Lady Hale's reference to the fact that the legal personality afforded to Scottish partnerships might be a factor in the debate, at best muddies the waters. That form of legal personality is not really understood by English lawyers (being an aspect of the civil law – see the tax case of *Major v Brodie*[14]) and surely should have no undue effect on English law. Suffice it to say that in the event the Law Commissions of England and Scotland finally recommended in 2003 that the two concepts of partnership and employment should be mutually exclusive on both sides of the border. No-one appears to have argued to the contrary, until now.

The Current Position on Employment – Incompatibility of Dual Status

Current acceptance of the traditional dichotomy between being a partner and being an employee is widespread. Everyone, with the exception it seems of John Machell QC, has until now regarded the position as being clear. Text books (including the

[9] This approach is germane to the partner/worker issue discussed below.
[10] See *Wilsons Solicitors LLP v Roberts* [2018] EWCA Civ 52; [2018] 1 BCLC 306.
[11] See *Palmer's LLP Law* (3rd edition) Sweet and Maxwell 2017 at paras A1-04 et seq.
[12] [2014] UKSC at [59].
[13] Under s 1 of the Partnership Act 1890.
[14] [1998] STC 491; 70 TC 576.

very authoritative *Lindley* but not Mr Machell's book on LLPs[15]), the two Law Commissions, and a series of cases, all point the same way. Two differently constituted CAs, *Clyde & Co*[16] in 2012 and in *Tiffin v Lester Aldridge*[17] also in the same year, regarded it as being well established, citing two more CA cases, *Ellis v Joseph Ellis & Co* (in 1905)[18] and *Cowell v Quilter Goodison Co Ltd* (in 1989).[19] The reasoning in all these cases is simple. It is that partnership is sui generis and outside employment law altogether. The very concept of the partnership relationship itself leaves no room for the employer/employee relationship as between the partners.

Until now, disputes have instead concerned whether an individual is either an employee or a partner – hence the various cases on the status of salaried partners, following the seminal judgment of Megarry J in *Stekel v* Ellice,[20] where Mr Stekel was seeking the rights of a partner rather than those of an employee. It clearly never occurred to anyone that he could be both. In more recent times, fixed share partners have been designed to make the holders partners and not employees, largely for tax purposes, which in turn has led to counter moves by HMRC (see e.g. *M Young Legal Associates v Zahid*[21] and The Income (Trading and Other Income) Act 2005 ss 863A, 863B which is intended to prevent LLP employees from claiming self-employed status). In other words, it is usually better to be a partner than an employee, especially but by no means exclusively for tax, although as the Clyde & Co case demonstrates there might now be advantages in the employment status (notwithstanding any tax consequences if that is the result). What the tax position would be for a person who is both a partner and an employee is a matter for speculation. It is interesting to note that HMRC, in its anti-avoidance legislation, requires genuine participation in risk, rights to capital and involvement in management for a fixed share member of an LLP to be regarded as self-employed. The sections are couched in terms of LLPs, since members of LLPs are taxed in the same way as partners. An LLP is also tax transparent so that the members are taxed as self-employed individuals, another example of the unfortunate misconception about the relationship between partnerships and LLPs.

But now we must in turn ask two questions: first, why are the partnership relationship and employment said to be incompatible. Partnership is above all a relationship, as section 1 of the Act makes clear; it is not in England a legal entity. Then, second, assuming that the established position is correct, do the factors identified by Lady Hale and Lord Clarke, i.e. section 82 of the Law of Property Act 1925, and leases

[15] John Whittaker and John Machell, *The Law of Limited Liability Partnerships* (4th edn, Bloomsbury Press 2016)
[16] [2012] EWCA Civ 1207; [2013] 1 All ER 844.
[17] [2012] 1 WLR 1887; [2012] ICR 647
[18] [1905] 1 KB 324 CA.
[19] [1989] IRLR 392 CA.
[20] [1973] 1WLR 191.
[21] [2006] 1 WLR 2562.

and loans between one partner and the partners as a body, render that position suddenly open to challenge?

Reasons for Incompatibility of Partnership and Employment

The employment lawyers state that the definition as to what is and what is not an employment contract is not easy to ascertain but that the basic ideas are to be found in the judgment of MacKenna J in *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance*.[22] The question revolves around the concept of control, taking into account opportunities of profit or loss, investment in facilities, permanency of relationship. For Elias LJ in the CA in *Clyde & Co*, employment presupposes a hierarchical relationship whereby the worker is to some extent subordinate to the employer.[23] Lady Hale rejected any idea relating to subordination in relation to a "worker" but did not pursue that as regards employment.[24]

So, what is it about the partnership relationship which makes it incompatible with employment? I think that there are at least three factors. First is the very nature of the relationship itself. Although it is clearly contractual, it is also subject both to equitable principles, and to the Partnership Act 1890, as Lord Millett made clear in *Hurst v Bryk*[25] in denying the application of repudiation to a partnership contract. On the same point, Neuberger J (as he then was) himself said in *Mullins v Laughton*: "The relationship is contractual, but it is subject to equitable principles and the provisions of the Partnership Act."[26]

Partnership is in fact a very complex relationship, which generates a number of unique interfaces between contract and equity which was simply never considered by the majority of the Supreme Court.

The Act itself imposes three fiduciary duties by sections 28 to 30 of the Act. These are the duties of uberimae fidei, the no conflict/no profit rule and no competition. The limitations on the no conflict rule which differ from those for companies, is an example of the contract/equity interface. Others can be found in what can be classed as partnership property, repudiation, and expulsion clauses among others. In addition, there is the overriding fundamental duty of good faith – or mutual confidence. This has recently been described as the most fundamental obligation which the law imposes on a partner in *Campbell v Campbell*,[27] and in the Canadian case of *Dockrill v Coopers v Lybrand*, Chipman JA said: "In short, the relation of partnership is one of the closest relationships known to the law…"[28]

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[22] [1968] 2 QB 497.
[23] [2012] EWCA Civ 1207 at [64]; [2013] 1 All ER 844.
[24] [2014] UKSC 32 at [39]; [2013] 1 WLR 2047.
[25] [2002] 1 AC 185 HL.
[26] [2003] Ch 250.
[27] [2018] EWCA Civ 80; [2018] 2 All ER 567.
[28] (1994) III DLR (4th) 62

The involvement of equity, being the consequence of partners acting as being mutually reliant, not least because of the unlimited liability which follows, is not easy to reconcile with employment. Employment gives rise to a number of rights (many more than those of a worker) which are in turn difficult to reconcile with this equitable relationship between the potential employers and employees. Partnership presupposes mutuality, and it is always very important to remember that the employers would not be some legal entity such as a company or an LLP, but the other partners, who have each entered that special type of relationship. If X and Y truly are partners with all that that implies, how can X also be an employee of Y? There is no third-party employer.

Of course, in large modern firms there is undoubtedly some element of hierarchy in fact as in Clyde & Co. In *Cowell v Quilter Goodison Co Ltd*,[29] Lord Donaldson MR, pre-LLP, specifically rejected an argument that the nature of firms had changed and had become more akin to a body corporate so as to allow for an employment situation. That might however be relevant as to whether a partner can be a worker. But perhaps it might be said that if X is both a partner and an employee then the equitable concepts could somehow be bolted on to the employment relationship, although that would require a characterisation as to whether X was acting as a partner or as an employee in any particular case. Legal certainty, so fundamental to businesses, would undoubtedly suffer.

But there is a second aspect of the partnership relationship which mitigates against a partner who fulfils all the requirements for being a partner also being an employee. Partnership is the relationship between persons carrying on a business in common. The important words are "in common". There is one business which is carried on for the partners' mutual benefit which also of course, reflects the fiduciary nature of the relationship. It is in effect a specialised form of a joint venture and agency – as Elias LJ put it in *Clyde*:

> …each partner is agent for the other and is bound by the acts of the other and each partner is both severally and jointly liable for the liabilities of the partners. There is lacking the relationship of service and control which is inherent in the concept of employee. The partnership concept is the antithesis of subordination.[30]

In what sense can an employee partner be held vicariously liable for the acts of the employer partners? Again, at the risk of repeating myself, the possibility of employment in a partnership founders on the lack of legal personality. Elias LJ again:

> A partnership under the 1890 Act is not a separate legal entity: hence the partners are all in a contractual relationship with each other in a joint venture

[29] [1989] IRLR 392.
[30] [2012] EWCA Civ 1207 at [65]; [2013] 1 All ER 844.

> and this is inconsistent with a hierarchical relationship of employer and employee.[31]

The contractual relationship in a company or an LLP is very different. How can a joint-venturer in any form of a joint venture also be an employee in connection with that joint venture?

The original decision on the mutual exclusion of partnership and employment was the Court of Appeal case of *Ellis v Joseph Ellis* in 1905.[32] In that case Lord Collins MR also distinguished there between co-adventurers and employees. But he also dealt with another difficulty in equating the two: remuneration.

> "It seems to me that, when one comes to analyse an arrangement of this kind, namely one by which a partner himself works and receives sums which are called wages, it really does not create the relation of employers and employed, but it is, in truth, a model of adjusting the amount which must be taken to have been contributed to the partnership assets by a partner who has made what is really a contribution in kind, and does not affect his relation to the other partners."[33]

A partner is simply not paid wages in the employment, or indeed taxation, senses of that word.

Finally, turning to a third aspect of the relationship, finance, a partner's interest in partnership assets and any other financial entitlement to partnership income or property is not recoverable by a simple action. With regard to assets, whilst the Australian courts have investigated the nature of a partner's interest in some depth, the position in England was set out very clearly by Nourse LJ in *Popat v Schonchhatra* as follows:

> While each partner has a proprietary interest in each and every asset he has no entitlement to any specific asset, and, in consequence no right, without the consent of the other partners …. to require the whole or even a share of any particular asset to be vested in him ….. As part of the process [of dissolution], each partner is presumptively entitled to payment of what is due to him in respect of capital before division of the ultimate residue…. It is only at that stage that a partner can accurately be said to be entitled to a share of anything….[34]

More generally, all partnership financial affairs can only be settled (other than in exceptional cases) by the taking of an account, and no action will be allowed to permit one partner to recover from another partner a sum which is referable to a partnership asset save though an action for account. These considerations mitigate

[31] [2012] EWCA Civ 1207 at [57]; [2013] 1 All ER 844.
[32] [1905] 1 KB 324.
[33] ibid at [328].
[34] [1997] 1 WLR 1367 at 1372.

against any rights under a co-existing employment contract unless an entirely new exception is made.

In summary therefore, the very nature of the partnership relationship as equitable contracting co-venturers in a joint business would seem to preclude a co-existing employment relationship between them. So, let us turn to the three matters expressly mentioned by Lady Hale as reasons for considering changing the law in order to provide for dual capacity of partner and employee or, as indeed would follow, an employer.

Questions of Capacity

The first of the reasons given by Lady Hale for questioning the traditional dichotomy between partnership status and employment was that the original case where that dichotomy was promulgated, *Ellis v Joseph Ellis & Co*, was decided in 1905, before section 82 of the Law of Property Act 1925 was enacted. Section 82 provides:

> 82 Covenants and agreements entered into by a person with himself and another or others.
> (1) Any covenant, whether express or implied, or agreement entered into by a person with himself and one or more other persons shall be construed and be capable of being enforced in like manner as if the covenant or agreement had been entered into with the other person or persons alone.

The effect of this is that any contract made between one partner with all the partners, including himself, will be construed as one between that partner on the one hand and the remaining partners on the other. This clearly alters the prior law that any such contract would be void on the basis that persons cannot contract with themselves. So, goes the argument, there is no longer any restriction based on capacity on a partner also being an employee, as he or she would not now be their own employer. The employment contract would be construed as one between the employee/partner on one side and the employer/partners on the other.

This is clearly true, but was the capacity restriction the only reason for the decision in *Ellis*? Lord Carnwath in *Clyde & Co* thought not (although he does seem to flirt with the capacity issue as well):

> Furthermore, the reasoning of the Court of Appeal in *Ellis v Joseph Ellis* does not turn simply on the lack of capacity to contract. As Lord Collins MR said, the particular arrangements made in that case in relation to payment for work did not affect the workers' relation to the other partners, which was of 'co-adventurers and not employees'.[35]

[35] [2014] UKSC 32 at [59]; [2014] 1 WLR 2047.

In other words, the stumbling block is not solely the issue of capacity, but the incompatibility of the two relationships.

But there are other statements in the cases which suggest that the capacity issue was one of the main reasons why partnership and employment were regarded as incompatible. These almost certainly caused Lady Hale and the others to raise section 82 in order to question the traditional view. For example, in the CA in *Clyde & Co*, Elias LJ gave as one of his reasons why a partner cannot be an employee:

> Since the partnership is not a separate legal entity, the parties are in a relationship with each other and accordingly each partner has to be employed, inter alia, by himself. He would be both workman and employer which is a legal impossibility.[36]

Section 82 would seem to solve that issue, as the partner would not be both employer and employee; his other partners would be his employers. The reason for all these probably inaccurate statements is that section 82 was clearly never argued in any of them. Unlike the Supreme Court, the Court of Appeal in *Clyde* did not have the benefit of John Machell QC's argument.

However, once again, Elias LJ did not base his decision in *Clyde* on the capacity issue alone – he also referred to the incompatibility of the employment relationship with the partnership ethos. So viewed, the effect of section 82 is, at best, to remove the capacity issue from the equation (including the lack of legal personality as a capacity issue) but it leaves the fundamental reasoning of incompatibility untouched (where the lack of legal personality is relevant - see e.g. per Lord Donaldson MR in *Cowell v Quilter Goodison* Ltd).[37]

There is also another technical issue associated with using section 82 in the partnership context. If there is an employment contract between a partner and his fellow partners and there is a breach of that contract then he can sue the other members in breach, presumably not as a partner but as an employee. But there is a possibility that if the breach is committed by a partner acting as an agent of the partners within section 5 of the Partnership Act 1890, that agent may also be acting as the employee/partner's agent, in which case no recovery would be possible. Of course, the employer partners would have to show that the agent really was acting on behalf of the employee partner as well.

But the partnership cases are very keen to stress the width of the mutual agency concept. In the Canadian case of *Dockrill v Coopers & Lybrand*,[38] a partner in dispute was held to be entitled to see legal advice prepared for the other partners on that basis.

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[36] [2012] EWCA Civ 1207 at [63]; [2013] 1 All ER 844.
[37] [1989] IRLR 392.
[38] (1994) III DLR (4th) 62.

One possible scenario is where the partners alter the business model for good commercial reasons for the benefit of all the partners, but this has a consequence of giving rise say to an action for constructive dismissal by the employee/partner. This agency dilemma is based on the speeches of the HL in *Bonsor v Musician's Union*,[39](1956) concerning an unincorporated trades union.

Following on from section 82, Lady Hale then raised two specific examples of where a partner was apparently able to occupy two capacities. The first was as the landlord of a lease where the partners were the tenants so that the lease became partnership property. Mr Machel's authority for that was the case of *Rye v Rye*,[40] and paragraph 10.45 of Lindley (19th edition). Lord Carnwath regarded those authorities as inconclusive – certainly the paragraph in Lindley refers to the question of whether a partner who is the tenant of premises and allows his co-partners to occupy them is in breach of a covenant. That is a totally different question.

In *Rye v Rye*, the issue was whether two partners could grant themselves an oral lease of premises they owned. This raised the potential effects of section 72(3) and (4) of the LPA 1925.

> Subs (3) provides that "a person may convey land to or vest land in himself.
>
> Subs (4) provides that: "Two or more persons…may convey…any property vested in them to any one or more of themselves in like manner as they could have conveyed such property to a third party…

Four members of the House of Lords held that in any event for technical reasons (the meaning of "conveyance") section 72 did not apply to an oral tenancy. Three members, Viscount Simonds, Lord Reid and Lord Denning also decided that section 72(3) and (4) did not in any event allow A to grant a lease solely of his own property to himself: so that, as in the case itself, A and B equally could not grant themselves a lease over their joint property. None of their Lordships referred to section 82, however, and it does seem that under that section one partner may grant a lease to the other partners – but not to himself, as the contract would be between him and the other partners? But then the lease would have to be excluded from the general run of partnership property, so what would happen on a dissolution? Would the partner/lessor not be entitled to a share of the proceeds if the lease was then assigned for value? Of course, *Rye v Rye* could easily be distinguished, so that section 72 would allow the partner/lessor to also be a partner/lessee with a beneficial interest in the lease if the lessor(s) and lessees were not identical. It would be a strange beneficial interest, however, as he would have rights against himself; a proposition which did not appeal to a majority of the HL in *Rye*. Alternatively, the other partners could own the lease as co-owners outside the partnership, as was held in the

[39] [1956] AC 104 HL.
[40] [1962] AC 496 HL.

Victorian cases under section 20(3) of the PA 1890.[41] The position is further complicated by the fact that the land will be subject to the Trusts of Land and Appointment of Trustees Act 1996 and thus the court's discretion under the Act.

It is true, therefore, that the position as regards leases is far from clear. But assuming that it is possible for a partner to have the dual capacity of landlord and partner/tenant and partner, does that assist the argument in relation to employment? There seems to be a world of difference between a lease and a contract of employment. A lease is not just a contract, it is an estate in land, and it is perfectly possible to have more than one estate in land. As Neuberger J, as he then was, said in *Mullins v Laughton*: "Unlike a lease, where there is an interest in land which is effectively detached from the contract which created it…".[42]

At best the landlord/tenant example simply confirms that dual capacity is possible, but it is so far removed from any aspect of a contract of employment as to be irrelevant to the central issue of compatibility of the latter.

Finally, as another example of partnership dual capacity, Lady Hale referred to a partner lending money to the firm, so as to be at once both a borrower and lender. I think that here the answer is rather more straightforward, and was set out quite clearly by the Court of Appeal in *Green v Hertzog* as long ago as 1954.[43] In that case one partner brought a common law action against two other partners following the winding up of the business, to recover the full amount of money lent by her to the partnership, as she would not recover the full amount from her share of the net assets in the winding up. Lord Goddard CJ gave the only judgment, with which the other members of the Court agreed. Accepting that a partner could lend money to a partnership of which she was a member, and that the sums involved were loans and not advances of capital, the action was held to be misconceived.

> There is no common law claim here for money lent: it is a loan by one partner to the partnership…and section 44(2) of the Partnership Act 1890 shows how that money is to be reclaimed and dealt with. There must be a taking of accounts, and, if it be shown that there is enough money in the partnership accounts to repay the plaintiff the money that she has advanced, or some of it, after the creditors of the partnership have been paid, she will get that money in priority to the others.[44]

In other words, the lending partner is not a creditor in the general sense of that word; any sums recoverable are as a partner – there is no real dual capacity at all. That does leave open the question as to whether any security taken by the lending partner would alter the position, but that would then possibly involve issues of insolvency law and fraudulent preferences etc.

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[41] See e.g. *Davis v Davis* [1894] 1 Ch 393.
[42] [2003] 4 All ER 94.
[43] [1954] 1 WLR 1309 CA.
[44] ibid at [p1312].

But even if there is some element of dual capacity involved in a loan situation, that again, involving property rights, is a far cry from an employment relationship. It is course worth remembering that in all these situations the issue is not between a partner and a partnership, but between a partner and the partners – a problem which of course does not arise with LLPs.

If a Partner can be an Employee – How Will it Work?

If, contrary to my arguments above, the Supreme Court does subsequently allow for the dual capacity of partner and employee, probably, given their predilection for overruling the Court of Appeal, because they identify with the complainant, as they clearly did in *Clyde*, how would it work? I think that there would be serious issues to resolve. The following are a few which occur to me, but undoubtedly there would be many more.

The first question is how the employee relationship would be determined. Lord Clarke in *Clyde* clearly thought that the relationship could arise simply from the terms of the partnership itself [52] and that the complainant in that case would have been an employee if the LLP had been a partnership. In *Clyde*, Ms Bates van Winklehof was an "equity member" of the LLP. That entitled her to a fixed share of the profits and such profit sharing units as the management board might determine. She also had a vote in the election of the "senior partner" and the members of the management board. All equity members agreed to carry on the business for the best advantage of the LLP and to devote their full time and attention to the business. They also agreed to be just and faithful to the LLP in all transactions relating to the business and in relation to the property and other assets of the LLP.

It is not clear to me which parts of that relate to employment. Indeed, it seems to be structured so that HMRC would not regard her as an employee for tax purposes. But the Supreme Court made no attempt to reconcile the concept of "worker" with the relationship between the members of the LLP from the LLP agreement. There is also the problem that in many partnerships the existence of the partnership itself and therefore of its terms are to be implied from conduct. Surely complying with one's obligations as a partner, with all that that connotes, cannot in themselves amount to employment without more?

The alternative of course is that the relationship could arise under a separate contract with the partners, validated by section 82 of the Law of Property Act and permissible under the freedom of contract regime established by section 19 of the Partnership Act. As I have already mentioned, that freedom is curbed in some cases by the involvement of equity. The cases on salaried and fixed share partners have, of course, had to examine such contracts on the either/or basis, and I suppose it is possible that they could be construed as creating both a partnership and an employment if that became legally possible. Such a conclusion could arise either by design or by accident. Ingenuity and litigation will be at a premium. If there is more than one partner/employee, each will then be both an employee and employer of

each other. It would be possible therefore for all the partners to be employees and employers – a tangled web indeed.

The second problem which would follow from dual capacity would be to distinguish between the legal consequences of each. This would require a characterisation of every dispute – the form and availability of litigation, the remedies in financial disputes, and the potential clash between partnership obligations *inter se* and employer/employee obligations, and, in particular, the overarching duty of good faith (not necessarily present in an LLP but clearly imposed by the LLP agreement in *Clyde*) are some of the issues which would come into question. To take one example: would the actions of partner A who was also an employee allow the other partners to bring a dissolution petition under section 35 of the Partnership Act on either the prejudicial conduct or just and equitable grounds? Would they have in addition to justify his dismissal as an employee? There are also the other grounds for dissolution to consider. It is worth noting that in many of the salaried partner cases, the plaintiff was seeking to dissolve the alleged partnership.

Then there is the problem of taxation. Insofar as income tax is concerned, it is perfectly possible for a taxpayer to have both employment and self-employment income, each charged according to the relevant rules under the Income Tax (Earnings and Pensions) Act 2003 and the Income Tax (Trading and Other Income) Act 2005. But I am not aware of any situation where that has arisen when the income from the same source, i.e. the profits of the partnership business, is paid to the same person. It would require agreement as to how much of the income received was as an employee and how much as a partner. New forms would have to be invented – more work for the accountants. With regard to Capital Gains Tax, it is more likely that that would be on the partnership basis, since the partner is unlikely to own partnership assets, given the definition of such property, in the capacity of an employee. Of course he could alternatively own an asset as an employee which is used in the business but is not partnership property.

So, the answer to the question posed by Lady Hale awaits another case. But even if it is answered by that Court in such a case in the negative (and in populist times that may not be very likely), the subsequent question which then arises is whether nonetheless a partner may instead be a worker, and so entitled to the more limited protection which that status brings.

Can a Partner also be a Worker?

As stated above, the definition of a "worker" which gives rise to certain limited employee protective rights, is set out in section 230 of the Employment Rights Act 1996:

> A person who by contract undertakes to do or perform personally any work or services to another party who is neither a client or customer of the business carried on by the individual.

In *Clyde & Co*, it was accepted that Ms Bates van Winklehof clearly fell within the express words of the section,[45] which was enough for the Supreme Court to decide the issue.[46] Lady Hale rejected any additional concept of subordination, as suggested by the Court of Appeal, in the definition of a worker as being a "mystery ingredient,"[47] although observing that it might sometimes be an aid to distinguishing workers from other self-employed persons, but it was not a freestanding and universal characteristic of being a worker.[48] Lady Hale considered a number of cases which had sought to decide whether a particular individual was a worker within the section. These she distilled into two suggested tests. The first was the integration test, i.e. whether the individual markets his services as an independent person or has been recruited to work for his principal as part of the principal's operations.[49] The second test, the dominant purpose test, concentrated on whether the contract involved a dependent work relationship or was one between two independent business undertakings.[50]

In the event, however, Lady Hale agreed with the approach of Maurice Kay LJ in *Hospital Medical Group Ltd v Westwood*,[51] that neither of these was a test of general application. In that case a doctor was considered to be a worker in relation to his work for a medical group, although he was also a general practitioner, and had another post with another clinic. He had a high degree of autonomy, but could still be a worker within the meaning of the Act. There was, agreed Lady Hale, no substitute for applying the words of the statute to the facts of the individual, which was what she proceeded to do. Nevertheless, Lady Hale seemed to refer back to the two tests, marketing and integration, by concluding on the facts of the case that Ms Bates van Winklehof could not market her services to anyone other than the LLP, and was an integral part of their business.[52]

It might well be arguable in relation to those two criteria that any partner or member who has signed a restrictive covenant is in the same position as to marketing, and that any partner or member is also *de facto* an integral part of the LLP or partnership business, so that all are potential "workers". But in the case of LLPs that bird has

[45] [2014] UKSC 32 at [40]; [2014] 1 WLR 2047.
[46] Since the decision in *Clyde*, the Supreme Court has considered the meaning of "perform personally" and "client or customer" in the definition of a worker in *Pimlico Plumbers Ltd* v *Smith* [2018] UKSC 29. It is unlikely that either of these will be of significance in relation to a partner vis a vis the partnership.
[47] Ibid at [39]. In the CA, Elias LJ considered that simply applying the express wording of the section (which he thought might well make Ms Van Winklehof a worker) was not enough. It required a subtler analysis involving some element of subordination: [2012] EWCA Civ 1207 at [69]-[71].; [2013] 1 All ER 844.
[48] Ibid.
[49] See *Byrne Bros (Formwork) Ltd v Baird* [2002] ICR 667 at [17(4)]; *Cotswold Developments Construction ltd v Williams* [2006] IRLR 18 at [53].
[50] See per Elias J in *James v Redcats (Brands) Ltd* [2007] ICR 1006 at [50] *and Mirror Group Newspapers Ltd v Gunning* [1986] ICR 145 at [59].
[51] [2012] EWA Civ 1005, [2013] ICR 415.
[52] [2014] UKSC 32 at [40]; [2014] 1 WLR 2047.

flown, and it is now accepted that a member of an LLP can be a worker.[53] However, can the same be said of a partner?

What if Ms Bates van Winklehof had been a Partner?

What would the position have been if Clyde & Co had been a partnership and not an LLP? Ms Van Winklehof was subject to the firm's members' agreement, which corresponds to a partnership agreement. In fact, many of its terms were those commonly found in partnership agreements. As an "equity member" of the LLP, she had a right to share in profits (as determined by the management group) and to vote in the election of the senior partner (sic) and the management group. She was also to devote her full time and attention to the business and above all to be "just and faithful to the LLP in all transactions relating to the business [of the LLP] and in relation to the property and other assets of the LLP." None of the justices of the Supreme Court addressed the question as to whether the detailed provisions of that agreement were incompatible with the status of being a "worker". There was certainly no subtle analysis of the kind undertaken by the Court of Appeal. The face value of the section was deemed a sufficient criterion.

If the same approach is applied to partnerships as it was to LLPs, i.e. that it is simply a question of applying the wording of the section to the particular facts, it would seem that being involved in management and sharing profits and being bound by the duty of good faith will equally not prevent a partner from being a worker. In fact, it is hard to see on that analysis why the senior partner or indeed any of the other members in the case could not be workers. They were all bound to provide services for the LLP and were an integral part of the business. But of course, the managers would not be as subordinate as Ms Bates van Winklehof, so would that then be used as a criterion? The position is far from being as clear cut as it is perceived to be.

There is, however, one essential legal distinction between an LLP and a partnership. In *Clyde & Co*, the business of which Ms Bates van Winklehof was an integral part, was that of the LLP, a separate legal person. Under English law at least that is not true of a partnership. One of the basic tenets of a partnership is that the partners are carrying on a business in *common*.[54] If it had been a partnership, it would have been Ms Bates van Winklehof's own business of which she was an integral part. There cannot be a partnership if there is no joint business – it is a specialised form of a joint venture.[55] As stated earlier, the partnership concepts of mutuality, partnership property and financial arrangements are predicated on that basic precept, not to

[53] It was so accepted before the CA in *Wilsons Solicitors LLP v Roberts* [2018] EWCA Civ 5; [2018] 1 BCLC 306, and is listed as a class of "worker" on the Government's website at www.gov.uk/employment-status/worker.
[54] Under s 1 of the Partnership Act 1890.
[55] See e.g. *Thames Cruises Ltd v George Wheeler Launches Ltd* [2003] EWHC 3093 (Ch); *Marshall v Marshall* [1999] 1 QdR 173 CA.

mention the fiduciary duties applicable to partners, which do not necessarily apply to members of an LLP.[56]

On the other hand, the wording of section 230 takes no account of any of the above factors. Whereas the concept of employment is less precise, the statutory definition of a worker is clear. If that is applied on its face value, since partners are, under the partnership contract, usually obliged to undertake to perform services on behalf of the other partners, who are neither customers nor clients of the partnership, then, without some element of subordination or hierarchy, that definition potentially applies to all partners. They are thus all potential workers, and nothing in the partnership ethos or legal mechanics can alter that fact without some gloss or "mystery element" being put on the definition. If, and when, the question arises, it will be for the court to decide which approach to take – to apply the wording of the statute *per se* or to apply the statute purposively in context. The issue will not be whether a partner can also legally have a dual capacity[57] but whether the two capacities of worker and partner are incompatible. Given the tenor of the judgments in *Clyde* it seems very unlikely that if Ms Van Winklehof had been a partner the result would have been any different.

If a Partner is a Worker – it's Partnership but not as we Know it?[58]

Should the courts decide that a partner can be a worker; early indications are that rights attached to that status that will survive existing partnership law. In *Wilsons Solicitors LLP v Roberts*,[59] the Court of Appeal upheld the judgment of the Employment Appeal Tribunal allowing a solicitor in an LLP to apply to recover compensation under the whistleblowing legislation despite the intervening lawful termination of his membership. The applicant had purported to accept a repudiatory breach of the agreement by the other members, but that doctrine has no place in LLP law.[60] It was held that although this made his subsequent expulsion lawful, it did not break the chain of causation between earlier pre-termination detrimental treatment and post termination losses giving rise to compensation as a worker. Since the position would have been exactly the same had it been a partnership[61] it would presumably produce the same result once it was conceded that the partner is a worker, as it was in the case. Thus, the right to compensation survived the application of partnership law.

Of course, there may be rather sharper conflicts between workers' rights and partnership law – whistleblowing and the good faith principle is an obvious example.

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[56] See *Alternative Investments (Holdings) Ltd v Barthelmy* [2011] EWHC 1731 (Ch).
[57] See the discussion earlier in relation to employment.
[58] With apologies to Captain Kirk and Star Trek.
[59] [2018] EWCA Civ 52.
[60] *Flanagan v Lion Trust Investment Partners LLP* [2015] EWHC 2171 (Ch); [2016] 1 BCLC 177
[61] *Hurst v Bryk* [2002] 1 AC 185 HL; *Mullins v Laughton* [2003] 4 All ER 94; *Goldstein v Bishop* [2013] EWHC 881 (Ch); [2014] Ch 131, affirmed on different grounds [2014] EWCA Civ 10.

It is interesting to note, therefore, exactly what these rights can amount to.[62] They include protection from unfair deduction of "wages" (really – a partner does not receive those[63]), a right to the minimum wage if part time (the same point can be made); the right to holiday pay (pay?), a right to rest breaks, a right to limit working to 48 hours per week unless opted out of, protection from discrimination (partners are already so protected under the Equality Act 2010), protection for whistleblowing and various rights to sick pay, maternity and paternity pay, adoption pay and shard parenting pay.

It is obvious from that list that most of these rights which relate to wages and pay are difficult to equate with the legal characteristics of financial rewards to which partners are entitled under partnership law. Discrimination is also already covered, and the 48-hour rule can be negotiated away, although informal partnerships are unlikely to do so.[64] But, as evidenced by the cases, whistleblowing remains as a clearly operative right, and it is surely in that context that the courts will one day have to decide the issue. At that point it will then have to decide how to apply the clear and succinct definition of a worker to the partnership involved. I do not see how the court could avoid applying the section to all partners on the wording of the section alone, unless it returns to the subordination issue and its mystery character.

[62] See the details at www.gov.uk/employment-status/worker and links therefrom.
[63] See (n 33) above.
[64] If it is included in a partnership agreement then it does tend to suggest a concession that the partner is a worker.