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DOI: https://dx.doi.org/10.18820/24150517/JJS42.v2.4

ISSN 0258-252X (Print)
ISSN 2415-0517 (Online)

Journal for Juridical Science
2017 42(2):104-119

Clarifying the distinction between partners and their creditors: The first reformative partnership legislation

Abstract

This contribution reflects on the United Kingdom's *Act to Amend the Law of Partnership* some 150 years after its promulgation. The statute was introduced to reform the common law rule that a person who shares in the profits of a partnership is considered a partner and, as such, liable for partnership debts, which had become firmly enshrined in English jurisprudence. After a range of parliamentary initiatives during the 19th century to alleviate the effect of the common law rule, the *Act* was passed in 1865. The statute provided that a person, who advanced money to, and shared in the profits of an undertaking, would not be deemed a partner, provided that this was in terms of a written contract. It went further to declare such a lender a deferred creditor, should the undertaking go bankrupt. In a preceding decision, *Cox v Hickman*, the House of Lords is considered to have established, in effect, that receipt of a share of the profits is not conclusive proof of a partnership. From disparaging decisions handed down after the promulgation of the *Act*, it soon appeared that the judicature was more reform minded than the legislature, placing the emphasis on the parties' intention and the real substance of the agreement rather than on form alone. When the *Act* was repealed by the *Partnership Act* of 1890, it was not only substantially re-enacted, but its provisions were made even stricter, notably the proviso regarding the existence of a not only written, but now also signed contract in sec. 2(3)(d). Although the law commissions of England, Wales and Scotland proposed in 2003 that the sec. 2(3)(d) proviso be repealed as a relic of the past, it elicited no legislative response. Fortunately, this is one confusion that the South African law of partnership was spared. Despite some early support for English decisions, the current approach is that a partnership is not formed, unless the participants' contributions are subjected to the risks of the venture. Where capital is advanced on the basis that the full amount plus interest must be returned at a later stage, irrespective of the fortunes of the business, the agreement is one of loan and not partnership.

1. Introduction

The history of partnership law spans more than four millennia.[1] Few branches of the law contain as many

1 See for example, Bromberg & Ribstein 1988:13; Szlechter 1947:113-122; Henning 2015:1-3.

historical survivals as the law of partnership, with the struggle between ancient concepts and modern business practices being particularly apparent. This is highlighted by the tendency to attach more importance to what partnership law is at present than to the matter of its growth. A case in point is the first reformative partnership legislation in the United Kingdom, the *Act to Amend the Law of Partnership*,[2] which was passed over 150 years ago. It was intended to clarify the distinction between partners and partnership creditors.[3] Commonly, it was named after Sir William Bovill,[4] who was instrumental in promoting the *Act*.

In essence, the *Act* stipulated that a person who advanced money to, and shared in the profits of a trade or undertaking would not be deemed a partner of the entrepreneur, provided that the contract was in writing. With its historical context having been obscured by time, it should be viewed against the background of the rigorous common law rule that a person who shares in the profits of the partnership is considered a partner and, as such, liable for the debts of the partnership, as well as reformative judgements.

This contribution focuses on the historical background to the *Act*, its provisions and consequences.[5]

2. Historical background

2.1 The common law rule

The association of loan with partnership can be traced back to constructs designed to circumvent the medieval usury prohibition. With the revival of trade, considerable thought went into the development of constructs whereby compensation could be paid for the use of money without violating the prohibition. For instance, it was argued that a partner could be insured by the other partner against the risk of the loss of his capital and that there was no reason why the partnership agreement and the insurance contract, each one legal in itself, should be illegal when entered into by the same persons.[6] This construct received support from the civilian legal systems and in the common law.[7] Next, it was maintained that, if a partner could be insured against the loss of his capital, he could also be assured of a certain profit.[8] This construct consisted of a combination of a partnership contract, an insurance contract, and a purchase contract. Although this construct was eventually legally considered as a valid partnership, an essential element in partnership, participation in risk, had been contracted away. It

2 *Act to Amend the Law of Partnership* 28 and 29 Vict c 86.
3 See for example, Morse 2010:10.
4 26 May 1814 to 1 November 1873. For further information, see http://en.wikipedia.org/wiki/William_Bovill (accessed on 1 February 2017).
5 See in particular, Henning 2007:33.
6 Berman 1983:334-336; Endemann 1874:369; Holdsworth 1938:103.
7 Endemann 1874:369-370; Holdsworth 1938:103.
8 Heaton 1948:201; Ashley 1931:441.

was, in effect, nothing more than an agreement with all the implications of a modern loan transaction.[9]

The concept that the person advancing money to a business for a share of the profit should be considered a partner and not a mere creditor had become firmly enshrined in English jurisprudence. In *Grace v Smith*,[10] for instance, it was accepted that every person who had a share of the profits of a trade ought also to bear his share of the loss. This decision appears to have been based on *Bloxham and Fourdrinier v Pell and Brooke*,[11] where a contract that was invalid as a contract of loan on the ground of usury was nevertheless upheld as a contract of partnership. This approach was approved and applied in *Waugh v Carver*,[12] the leading authority on the subject at the time, and in numerous subsequent decisions.[13]

The resulting common law rule, namely that any person who shared in the profits of the partnership was considered a partner and, as such, liable for any debts of the partnership,[14] was characterised as arbitrary, unjust and the cause of great confusion.[15] In his seminal work of 1841 on the law of partnership, Story emphasised that it is far from being universally true that a mere participation in profits constitutes a person a partner, but that the common law already settled it to the contrary.[16] Consequently, numerous parliamentary reform initiatives were launched during the 19th century, all without effect, until 1865.

The Commission on the Mercantile Laws and on the Law of Partnership of 1854 serves as an example of the difference of opinion on the issue. This commission was appointed to explore the question of limited and unlimited liability of partners. Despite the commissioners' experience and competence, the body failed to reach unanimity. Men of great experience and talent arrived at diametrically opposite conclusions. Eventually, a bare majority of five commissioners signed a report opposing the proposal that a person should be able to lend money to a partnership at an interest rate varying with the profits, without incurring partnership liability. The common law rule was, therefore, confirmed. Contrary to this report was the immediate and unanimous passing by the House of Commons of a resolution to the effect that the law of partnership ought to be amended by introducing the concept of limited liability for profit-sharing moneylenders. In the subsequent session of parliament, the *Partnership Amendment Bill* was introduced to allow profit-sharing loans to partnerships, without the

9 Decock 2012:11: "The result of the threefold contract was not very different from a money deposit or a loan for consumption." See in particular, Henning 2015:44-47.

10 *Grace v Smith* (1775) 2 Wm Bl 997, 96 ER 587.

11 *Bloxham and Fourdrinier v Pell and Brooke* (1775) 2 Wm Bl 999.

12 *Waugh v Carver* (1793) 2 Hy Bl 235, 126 ER 525.

13 See Henning 2015:48-49.

14 *Canada Deposit Insurance Corporation v Canadian Commercial Bank* [1992] 3 SCR 558; Banks 2010:94.

15 Banks 2010:95.

16 Story 1841:53-54.

lender incurring the liability of a partner. It progressed to a second reading in the House of Commons, but was not proceeded with any further.[17]

Sharp differences of opinion on the issue also appeared in 1856 during the second reading of the next *Partnership Amendment Bill* in the House of Commons aimed at the reform of the common law rule. On the one hand, the opinion was expressed that the *Bill* may be regarded as the natural corollary and complement of the repeal of the usury laws.[18] On the other, it was argued that the *Bill* would spread a great delusion among the public. It would enable any man to give an air of prosperity to a bad concern by obtaining a loan from another party, who, by collusion with the first, could secretly withdraw his capital as soon as he saw that things were going wrong. Yet, in the commercial world, the concern would retain the false credit to which it was no longer entitled.[19]

2.2 House of Lords

In 1860, the question before the House of Lords in *Cox v Hickman*[20] was whether the creditors, who were being paid out of profits, were liable to subsequent creditors as partners. The company of B Smith & Son fell into financial difficulty and was unable to pay its creditors. The Smiths consequently entered into an agreement with some of its creditors, assigning the company to them as trustees for all of the creditors, for a term of 21 years. During that period, the trustees were to carry on the business of the company and "pay the net income, after answering all expenses; which net income was always to be deemed the property of the two Smiths, among [all] the creditors of the Smiths". In other words, the creditors "were to be paid their debts out of the profits of their debtors' business".[21] The repayment was to be only to the extent of the debts. Once all the debts were paid, the trustees were to hold the estate in trust for the Smiths. The company's financial afflictions continued under the new management, and the enterprise again reached a point where it was unable to pay its debts. Since the common law rule at the time stated that a person who shared in the profits was liable as a partner, the question was not whether those creditors, who were being paid out of profits, were to be ranked equally with subsequent creditors, but whether the former group were to be themselves liable as partners to subsequent creditors. In deciding that they were not so liable, the House of Lords is considered by later decisions to have established, in effect and among other things, that receipt of a share of the profits is not conclusive proof of a partnership.[22]

17 Henning & Wandrag 1997:150.

18 See http://hansard.millbanksystems.com/commons/1856/feb/08/partnership-amendment-bill (accessed on 1 February 2017).

19 See http://hansard.millbanksystems.com/commons/1856/feb/08/partnership-amendment-bill (accessed on 1 February 2017).

20 *Cox v Hickman* (1860) 8 HLC 268, 11 ER 431.

21 *Canada Deposit Insurance Corporation v Canadian Commercial Bank* fn. 14; Banks 2010:96.

22 *Canada Deposit Insurance Corporation v Canadian Commercial Bank* fn. 14.

Notably, the judges in the courts below were not unanimous on the issue. The Court of Common Pleas decided that the creditors, by their execution of the deed of arrangement, had become the partners of those who conducted the business of the company. The judges in the Court of Exchequer Chamber were equally divided, so the judgement of the Court of Common Pleas was affirmed.[23]

Of the five law lords presiding in *Cox v Hickman*, three handed down judgements, while the remaining two each concurred with a different judgement. The *ratio decidendi* is not abundantly clear. The Lord Chancellor (Lord Campbell) was of the opinion that, even in terms of *Waugh v Carver*, a participation of profits was not made out on the facts to constitute a partnership. Lord Brougham concurred. In the most detailed decision, Lord Cranworth stated the following:

> It is often said that the test, or one of the tests, whether a person not ostensibly a partner, is nevertheless, in contemplation of law, a partner, is, whether he is entitled to participate in the profits. This, no doubt, is, in general, a sufficiently accurate test; for a right to participate in profits affords cogent, often conclusive evidence, that the trade in which the profits have been made, was carried on in part for or on behalf of the person setting up such a claim. But the real ground of the liability is, that the trade has been carried on by persons acting on his behalf. When that is the case, he is liable to the trade obligations, and entitled to its profits, or to a share of them. It is not strictly correct to say that his right to share in the profits makes him liable to the debts of the trade. The correct mode of stating the proposition is to say that the same thing which entitles him to the one makes him liable to the other, namely, the fact that the trade has been carried on on his behalf, *i.e.*, that he stood in the relation of principal towards the persons acting ostensibly as the traders, by whom the liabilities have been incurred, and under whose management the profits have been made.[24]

This statement has often been relied on for a finding that mutual agency is one of the essentials of partnership.[25] However, Lord Cranworth earlier also emphasised that:

> … partners may stipulate among themselves that one or some of them only shall enter into particular contracts, or into any contracts, or that as to certain of their contracts none shall be liable except those by whom they are actually made.[26]

Lord Wensleydale, in turn, stated that, if two or more agreed that they should carry on a trade and share its profits, each was a principal and each an agent for the other, and each was bound by the other's contract

23 The judges concerned were called, and Lord Chief Baron Pollock, Mr Justice Wightman, Mr Justice Williams, Mr Justice Crompton, Mr Baron Channell and Mr Justice Blackburn attended.

24 *Cox v Hickman* fn. 19.

25 De Wet & Yeats 1964:561.

26 *Cox v Hickman* fn. 19.

in carrying on the trade, as much as a single principal would be by the act of an agent, who was to give the whole of the profits to his employer. Therefore, it becomes a test of the liability of one for the contract of another that he is to receive the whole or a part of the profits arising from that contract by virtue of the agreement made at the time of the employment. Lord Chelmsford concurred.

Interestingly, the House of Lords professed to overrule no previous authority.[27]

Immediately after the decision, there was a difference of opinion in *Killshaw v Jukes*[28] as to the effect of *Cox v Hickman*. In *Bullen v Sharp*,[29] Judge Blackburn stated that it was a question for the legislature to decide whether the effect of *Cox v Hickman* was more or less expedient than *Waugh* v *Carver*. In view of all this uncertainty, it is conceivable that the promoters of the *Act to Amend the Law of Partnership* deemed it appropriate at the time to continue with the introduction of legislation alleviating the effect of the common law rule in the circumstances specified, so as to allay any remaining doubts.[30]

3. The Act to Amend the Law of Partnership

After a significant number of parliamentary initiatives were launched during the 19th century to reform the common law rule, the *Act to Amend the Law of Partnership* was passed, and received royal assent on 5 July 1865 with the intention to give statutory relief from partnership liability to investors. In brief, it stipulated that sharing of profits will, in the circumstances provided for, not be conclusive evidence of partnership, and that lenders in consideration of a share of the profits will be deferred creditors.

Sec. 1 of the *Act* provided as follows:

> The advance of money by way of loan to a person engaged or about to engage in any trade or undertaking *upon a contract in writing* with such person that the lender shall receive a rate of interest varying with the profits, or shall receive a share of the profits arising from carrying on such trade or undertaking, shall not, of itself, constitute the lender a partner with the person or the persons carrying on such trade or undertaking, or render him responsible as such.[31]

Secs 2 to 4 dealt with related matters. Sec. 5 then stipulated that, in the event of the bankruptcy of the trader, the lender would be a deferred creditor, rendering him unable to recover any portion of his principal sum or interest or share of the profits until the claims of all the other creditors have been satisfied.

27 Banks 2010:95.
28 *Killshaw v Jukes* (1863) 3 B 7 S 847.
29 *Bullen v Sharp* (1865-66) LR 1 CP 86 Ex Chamber.
30 Lindley 1881:43; Miller 1973:61-62.
31 Emphasis added.

The phrase "of itself" in sec. 1 shows that the legislature had the reform of the common law rule foremost in mind, while the limiting proviso "upon a contract in writing" most probably was the result of the difference of opinion in the legislature, referred to above, concerning the merits and demerits of the common law rule. The "contract in writing" referred to a signed contract that showed, on the face of it, that the transaction was not one of partnership, but of loan.[32]

Critical decisions handed down, *inter alia*, by the Privy Council[33] and the Master of the Rolls,[34] surmised that the promoters of the *Act* failed to fully appreciate the effect of *Cox v Hickman* at the time.[35] On the other hand, the view was expressed that the *Act* was framed on the basis "of the law being as it was declared to be in *Cox* v. *Hickman*".[36] Some commentaries indicate that, as *Cox v Hickman* did not entirely allay the doubts entertained as to the precise position under common law, this legislation was passed specifically to deal with those particular cases.[37] Notably, various aspects of this legislation are sometimes still being considered in contemporary jurisprudence.[38]

The fact that the House of Lords professed that no previous authority was overruled, encouraged the Master of the Rolls to infer that the common law rule never existed:

> I do not know why those words, 'of itself', were put into the Act, unless it was supposed by the framer … that sharing profits would otherwise have created a partnership of itself. If you take that meaning, then it is an alteration of the law; but *Cox* v. *Hickman* decided that that was not so, and never had been so, for of course *Cox* v. *Hickman* did not lay down any new law—the Lords say so in their speeches—and, consequently, it was not true that at any time sharing profits constituted a lender a partner …

He continued:

> That being so, what is the effect of the Act? The Act is this, that the advance of money must be 'by way of loan'. Now what does that mean? It is not the 'advance of money', but 'the advance of money by way of loan'. I take it to mean this, that the person advancing

32 *Pooley v Driver* (1877) LR 5 Ch D 458; *Syers v Syers* (1876) 1 App Cas 174 HL.
33 *Mollwo March & Co v Court of Wards* (1871-73) LR 4 PC 419; 17 ER 495.
34 *Pooley v Driver* (1877) LR 5 ChD.
35 See also Pollock 1882:83.
36 *In re Fort Ex parte Schofield* [1897] 2 QB 495 CA. See also *Holme v Hammond* (1871-72) LR 7 Ex 218 Ex Ct; *Davis v Davis* [1894] 1 Ch 393; *Leggett v Hyde* (1874) 58 NT 272, 17 Am Rep 244; Morse 2015:58.
37 Lindley 1881:43; Miller 1973:61-62; Morse 2015:57.
38 See *Re LB Holliday & Co Ltd* [1986] 2 All E.R. 367; *The Owners of Cargo Lately Laden on Board the Ship Aramis v Aramis Maritime Corpora*tion 1988 WL 1608973; *Canada Deposit Insurance Corporation v Canadian Commercial Bank* fn. 11; *Sukloff v A H Rushforth & Co* [1964] SCR 459; *Stonehaven Country Club Centre de villégiature & spa, l.p.* 2011 QCCA 718; *Installations Doorcorp inc./Doorcorp Installations Inc* 2012 QCCA 702.

> must be a real lender; that the advance must not only profess to be by way of loan, but must be a real loan; and [that] consequently you come back to the question whether the persons who enter into the contract of association are really in the position of creditor and debtor, or in the position of partners, or in the only third position which I think could be suggested, that of master and servant. But the Act does not decide that for you. You must decide that without the Act; and when you have decided that the relation is that of creditor and debtor, then all the Act does is this: it says that the creditor may take a share of the profits, but, as I understand the law … if you have once decided that the parties are in the position of creditor and debtor you do not want the Act at all, because the inference of partnership derived from the mere taking a share of profits, not being irrebuttable, is rebutted by your having come to the conclusion that they are in the position of debtor and creditor …[39]

Later decisions accepted that, although the law lords avowed not to overrule any previous authority, *Waugh v Carver* and other similar cases had, in fact, been overruled and that the common law rule was set aside in *Cox* v *Hickman*, which, in effect, established that receipt of profits was only *prima facie* evidence of a partnership.[40] It is clear that the *Act* made no advance on this interpretation given to the judgements in *Cox v Hickman* in later decisions. In this event, it seems that the judicature was more reform minded than the legislature, by placing the emphasis on the parties' intention and the real substance of the agreement rather than on the form alone.[41]

This was confirmed in *Badeley v Consolidated Bank*,[42] where the plaintiff had advanced money to a contractor to enable him to carry out his contract to build a railway. The deed provided that the plaintiff should receive 10 per cent interest and 10 per cent of the profits of the contract, and the contractor assigned to him all his machinery and plant by way of security. It was held that these provisions were consistent with an intention to secure a loan, and insufficient as evidence of partnership. Although the *Act* endeavoured to enable persons to lend money to traders and receive a rate of interest varying with profits, or a share of profits in lieu of interest, without becoming responsible as partners, the lender, who advanced money for a share of profits, could be discontent with being a passive creditor. Under the supposition that the *Act* enabled him to assume the position of a partner in everything but liability, he entered into an agreement whereby his advance was completely embarked in the capital of the business, and he received in return most of the usual rights

39 *Pooley v Driver* (1877) fn. 32.

40 See also *Mollwo March & Co v Court of Wards* (1871-73) LR 4 PC 419; 17 ER 495; *Pooley v Driver* (1877) fn. 29; *In re Fort Ex parte Schofield* fn. 31; *Badeley* v *Consolidated Bank (*1888) LR 38 ChD 238 CA; *Adam* v *Newbigging (*1888) LR 13 App Cas 308 HL, 13 AC 316.

41 For example, *Badeley v Consolidated Bank* fn. 40; *Re Young, ex parte Jones* [1896] 2 QB 484; *Davis v Davis* fn. 36. See also Milman & Flanagan 1983:12-14; Morse 2015:40-41.

42 *Badeley v Consolidated Bank* fn. 39.

and powers of a partner as between himself and the nominal borrower. Then, if the business failed, he found that he was precisely in the position he wanted to avoid. The *Act* declared that a person could lend money and take a share of profits without being a partner; this, however, did not enable a person to enter into what was substantially a partnership, and then limit his liability by calling it a loan.[43]

Initially, it was presumed that this legislation had introduced something in the nature of a limited partnership. In *Syers v Syers*,[44] it was held that it did not. It protected the creditor if he was not involved in the running of the business. If he in truth was, he became fully liable as a partner, notwithstanding that he was described as a contributor under the *Act*. In addition, the *Act* made *bona fide* creditors deferred creditors in bankruptcy. It did not constitute a limited partnership, for it did not enable a person to become a partner without incurring unlimited liability.[45]

4. Consequences

It would appear that everyone was very appreciative of the reform-minded judicature. Notably, when the *Act* was repealed by the *Partnership Act* of 1890,[46] it was not only substantially re-enacted by secs 2 and 3 of the *Partnership Act*, but its provisions were made even stricter. For instance, the proviso was emphasised and the contract not only had to be in writing, but also signed by the parties.

Sec. 2(3)(d) provides presently that the advance of money by way of a loan to a person engaged or about to engage in any business, on a contract stating that the lender shall receive a rate of interest varying with the profits, or shall receive a share of the profits arising from the carrying on of the business, does not of itself make the lender a partner of the person carrying on the business, or liable as such. Importantly, this arrangement is made subject to the express proviso that the contract must be in writing, and must also be signed by, or on behalf of all the parties.

Sec. 3, following on sec. 5 of the 1865 *Act*, in brief provides that, in the event of the bankruptcy or insolvency of the borrower (the "person engaged or about to engage in any business"), the lender is not entitled to recover anything in respect of his loan until all other claims of the borrower's creditors have been satisfied.[47]

At first glance, the effect of the proviso to sec. 2(3)(d) seems to be that a lender receiving a rate of interest varying with the profits of the business in terms of a contract *not* in writing or *not* signed by, or on behalf of all the contracting parties is *not* entitled to the benefit of paragraph (d), and that the advance of money under such circumstances would, therefore, of itself

43 Pollock 1880:726.
44 *Syers v Syers* (1876) 1 App Cas 174, HL.
45 Gower 1979:50.
46 *Partnership Act* 53 and 54 Vict c 39.
47 For further discussion, see *Sukloff v A H Rushforth & Co* [1964] SCR 459.

make the lender a partner *or* liable as such.[48] Indeed, in *Re Fort, ex parte Scofield*,[49] the Queen's Bench took this very view and decided that, if the benefit of sec. 2(3)(d) is "desired by the lender, then under the proviso the contract must be in writing". It follows that, if this approach is taken, it may be argued that a person who never was a partner, but only a creditor, and with regard to whom the only evidence is participation in profits, is to be deemed a partner in the absence of a written and signed contract.[50] This, it has been submitted, cannot be a correct interpretation.[51] Later, the courts treated sec. 2(3)(d) as simply re-enacting what was regarded as the original test in *Cox v Hickman*, namely that the sharing of profits, although it constitutes strong evidence of a partnership in some cases, does not raise the irrefutable presumption of a partnership.[52] Eventually, it was firmly established by the House of Lords in *Gosling v Gaskel*[53] that a person, who did not hold himself out as a partner, was not liable to third parties for the acts of persons whose profit he shared, unless they were really partners *inter se*, or they were his agents.

It appears that hardly any attention was given to the fact that the phrase "of itself" was retained in sec. 2(3)(d) of the *Partnership Act* and that the proviso relating to the contract in writing was not only retained, but also strengthened, in the same section. Small wonder that modern commentators refer to the interpretation of the phrase "of itself" in sec. 2(3)(d) as "problematical".[54]

Sec. 3 provides that a person, who has lent money to a business "upon such a contract as is mentioned" in sec. 2(3)(d), is postponed to all the other creditors of the business. Such a lender will only be able to recover his debt if the partnership is dissolved after all the other partnership creditors have been paid in full. Notably, sec. 3 applies to any contract of loan providing for a return of net profits whether oral or in writing, while the proviso to sec. 2(3)(d), referring to a contract in writing, relates only to those wishing to take advantage of sec. 2(3)(d) to avoid being partners.[55]

Morse[56] concludes that, presently, sec. 2(3)(d) confers few benefits, whereas sec. 3 remains a burden to be reckoned with.

In 1997, the Law Commission of England and Wales as well as the Scottish Law Commission undertook a joint review of partnership law. Their comprehensive joint consultation paper of 2000 questioned the usefulness of the proviso to sec. 2(3)(d), and proposed that it should be repealed, as

48 Banks 2010:97.
49 *Re Fort, ex parte Scofield* [1897] 2 QB 495:501.
50 Ivamy 1986:8-9; Miller 1973:87-88; Blackett-Ord 1997:32-33.
51 Ivamy 1986:9.
52 *Davis v Davis* [1894] 1 Ch 393; Morse 2015:56-58.
53 *Gosling v Gaskel* (1897) AC 575 HL. See Banks 2010:96.
54 See for example, Morse 2010:57-58.
55 *Re Fort, Ex p Schofie*ld [1897] 2 QB 495. See also *Re Gieve, ex p Shaw* [1899] WN 41, CA.
56 Morse 2015:66.

it appeared to be a relic of earlier times.[57] Their joint final report of 2003 supported the repeal of the proviso to sec. 2(3)(d) and recommended that the wording of the subsection should be amended to reflect *Cox v Hickman*. The Law Commissions also recommended the repeal of sec. 3 as being at variance with modern insolvency rescue procedures.[58] Unfortunately, these recommendations elicited no legislative response.[59]

The *Partnership Act* has not only been in force in England, Wales and Scotland since 1891, but it has also served as an example for the partnership legislation of the majority of Commonwealth jurisdictions. Provisions similar to secs 2 and 3 of the *Partnership Act* appear in over 30 other partnership acts and ordinances, with dates of implementation ranging from 1891 to 1997.[60] Notably, it has also influenced American partnership legislation, such as sec. 7(4) of the *Uniform Partnership Act* of 1914. Sec. 202(c)(3) of the American *Revised Uniform Partnership Act* of 1997 still provides that a person, who receives a share of the profits of a business, is presumed to be a partner in the business, unless the profits were received in payment of, for instance, debts by instalments, or rent, or for the sale of goodwill of a business or other property by instalments, or for services as an independent contractor, or for wages or other compensation to an employee.[61]

5. South African perspective

The validity of the construct of joint partnership and insurance agreements, where a partner was insured against the loss of his capital by the other partner, was expressly approved by a significant number of institutional Roman-Dutch commentators, including De Groot and Van der Linden, who mostly remarked that this was not a *societas leonina*, as all the participants shared in the profit.[62] Thus, De Groot stated that there were really two contracts joined in one – one of partnership, whereby the profits, if any, would be equally divided, and another of assurance, whereby one of the partners secured the capital of his fellow partner. De Groot added that this method was not at all unreasonable if, when the capital of the one was secured, the assurer received more out of the profit than he would otherwise be entitled to. According to Van der Linden, in his commentary on Pothier's treatise on partnership, there is nothing untoward in joining

57 Law Commission of England and Wales and the Scottish Law Commission 2003:par. 5.40.

58 Law Commission of England and Wales and the Scottish Law Commission 2003:paras. 4.53 and 5; Draft Bill cl 1(7) and Schedule 1.

59 See http://www.bis.gov.uk/policies/business-law/company-and-partnership-law/partnership-and-llp-law (accessed on 1 February 2017).

60 Henning 2015:51-52.

61 Bromberg & Ribstein 2002:563-564.

62 *Hollandsche Consultatien* 1645-1685:3.303.4; De Groot 1670:1.12.24.3; Voet 1956:17.2.8, 17.2.27; Vinnius 1642:3.25.2; Vinnius 1653:1.54; Huber 1742:4.24.2; Van Leeuwen 1780:4.24.21; Lybrechts 1758:89; Wassenaer 1661:2.17.9; Van den Berg 1694:1.74, 2.90, 3.75, 3.76.

a contract of insurance with a partnership contract. In this instance, both share in the profit, while one of the partners insures the other against the loss of his capital.[63]

One of the most famous theologians from the Low Countries, Lessius,[64] who, it has been contended, influenced the commercial legislation of Antwerp, supported this and similar constructs. He defended it on the basis of theological, moral, legal and economic policy arguments as a just means for providing guaranteed commercial credit with a fixed annual dividend. In this manner, savings could be invested in a productive way, without the investor running the risk of condemnation for usury.[65]

Some warned that this construct would be permissible only where the partner not participating in loss contributed labour and nothing else,[66] while others[67] expressed their disapproval of the construct.

Bearing in mind that a number of institutional writers on, and other reputable sources of the *ius commune* were in support of the construct where a partner was insured against the loss of his capital by the other partner, it should be clear how fortunate Roman-Dutch law and, therefore, South African law were to avoid the confusion that befell English common law.[68] Although there is some evidence of early judicial support for English decisions,[69] the current approach is that a partnership will, in principle, not be formed unless the participants' contributions to the enterprise are subjected to the risks of the venture. Where capital is advanced to a business on the basis that the full amount plus interest must be returned at a later stage, irrespective of the fortunes of the business, the agreement is one of loan and not partnership.[70]

However, the fact that a party is entitled to the return of the full amount of the principal sum contributed by him is not always conclusive. If a partner contributes the use of capital to the business, he remains entitled to the return of the full amount, and only the interest on it will be subjected to the risks of the business. Where both capital and services are contributed,

63 Van der Linden 1802:1.19. Van der Linden (1806:4.1.11) limits this view to instances where one partner contributes only his labour and nothing else.
64 1554-1623.
65 See in particular, Decock 2012:30-31.
66 Van der Keessel 1967:2.12.10, 2.12.19, 3.21.5; Van der Keessel 1860:250.
67 Van Bynkershoek 1744:2.1.6; Felicius 1666:chs 18, 19; Pothier 1854:par. 22: "It is very clear that the three pretended contracts comprised in the agreement are only feigned in order to disguise a loan at interest, and that, in truth I had no intention of entering into a partnership with the merchant, but only of getting from him interest on the sum which I lent. And even if, by a misconception, I should have persuaded myself that I really had the intention of entering into three successive contracts with him, this would be an illusion produced by my cupidity, in order to disguise for myself the vice of usury in the loan at interest to which the whole of the agreement resolves itself."
68 See in particular, Henning 2015:44-45.
69 Compare De Wet & Yeats 1964:561.
70 Henning 2016:219

the agreement is not necessarily a loan merely because the capital plus interest is to be repaid in full, as a partner may also lend money to the firm. Authorities emphasise that, in such instances, all other surrounding facts must be considered to ascertain the true nature of the agreement.[71]

6. In conclusion

The law commissions of England, Wales and Scotland proposed that sec. 3 and the proviso to sec. 2(3)(d) of the *Partnership Act* should be repealed as relics of the past and that the wording of the latter should be amended to reflect the effect of *Cox v Hickman.* It elicited no legislative response, although sec. 2, in particular, has served its purpose of clarifying doubts with ancient origins.[72] In consequence, these sections still reflect the particular approach of the 1865 *Act*. It may conceivably encourage a view that, in this way, the legacy of the 1865 *Act* is allowed to linger on long past its expiry date, albeit in a different guise as part of the *Partnership Act.* Fortunately, this was one confusion that the South African law of partnership was spared.

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71 See Henning 2016:220 and authorities referred to.
72 See in particular, Morse 2015:64-65.

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