Employment status and incomplete partnership negotiations

By Alex Leonhardt
3PB Barristers

1. In ***Christopher Watson v Wallwork Nelson Johnson & Anor [2024] EAT 105*** the EAT grappled with the issues around an ET making a finding that a "traditional" partnership (a partnership per the Partnerships Act 1890 (**'PA 1890'**), rather than an LLP) existed in circumstances where there had been protracted and "shambolic" negotiations over terms.

2. It also touched upon issues of fundamental law, relating to the possibility of worker status where such a partnership is found to exist, although those matters were not directly brought before it.

Facts

3. Mr Watson was an accountant who had a decade's experience with the Respondent when it promoted him to the role of associate in April 2019.

4. He received an increase in salary, the Respondent ceased making payments to its pension scheme on his behalf, and he was issued with a P45. The Respondent stopped making employer's NI contributions, and stopped making deductions for income tax and national insurance through PAYE.

5. At this point there was no written agreement on remuneration, holiday or notice. Nor had Mr Watson been able to review information on the partnership's income and liabilities, or made any capital contribution.

6. Negotiations on terms continued for some time, and Mr Watson expressed frustration at the fact that he was still being treated, as he saw it, as an employee: in January 2020 there was still no partnership agreement.

7. Of note for the appeal to the EAT, and a point the parties had agreed upon from the outset, was that Mr Watson would not bear liabilities for the debts and obligations of the partnership.

8. In February and March 2020, the Claimant further requested a confirmed partnership agreement. In the absence of this, he suggested that payroll records back to April 2019 be adjusted to show, in effect, that he was an employee throughout that period.

9. The Respondent suggested, in turn, that he return to his previous (employed) position and a Partnership Agreement be agreed to cover a period of self-employment. This was not accepted by the Claimant, who asserted the continued effectiveness of his contract employment from May 2018.

10. During April 2020 the partnership decided to reduce drawings as a result of the Covid pandemic. The Claimant characterised this as a salary reduction (in light of his position that he was an employee). In turn, the Respondent characterised the Claimant's continued assertions of employment as being a breach of the Claimant's fiduciary duties as a partner. Both were asserting, in effect, the right to terminate the agreement with the other.

11. The Respondent terminated the partnership agreement (or, as the Claimant saw it, terminated his contract of employment) on 12 June 2020, and the Claimant presented his claims (including for Unfair Dismissal) to the Tribunal.

The Decision of the Employment Tribunal

12. The ET, at first instance, determined the Claimant to have been a partner at the relevant time (ie. the bringing of his claim). Both sides had agreed that partnership precluded an employment relationship. The Claimant was therefore unable to bring his claims for unfair dismissal or breach of contract.

13. In determining whether the Claimant was an employee or partner, the Tribunal had engaged in a multi-factorial assessment. It placed particular weight on the arrangements for paying the Claimant and for paying tax, in light of the particular nature of the business and the expertise of both Claimant and Respondent in these areas.

14. The Tribunal accepted that no full agreement had been made between the parties, but that there was sufficient agreement on the essential terms that the Claimant had been engaged

as a partner (and therefore not an employee). It found that as a result of that engagement, the Claimant was in fact liable for the debts and obligations of the partnerships as per s.8 of the PA 1890 in the absence of an explicit agreement otherwise. This exposure to risk was a factor which the Tribunal took as indicative of the Claimant not working under a contract of employment at the time.

15. The Tribunal did find, however, that the Claimant was a worker under s.230(3)(b) of the ERA 1996: he had undertaken to perform work personally, and the partnership was not in any sense a client or customer of his. The law is, surprisingly, not settled on whether a partner in a traditional partnership (as opposed to an LLP) can be a worker: the practitioner text ***Lindley & Banks*** explicitly describes the proposition as having "not, as yet, been tested", and the decision of the Supreme Court in the leading case of ***Bates van Winkelhof v Clyde & Co LLP*** explicitly drew a distinction between LLPs and traditional partnerships and did not decide the question in relation to the latter. Neither side took on this issue at first instance or at the EAT.

The Grounds of Appeal to the EAT and Arguments

16. Permission to appeal was given for the Claimant to appeal on five grounds, although not all will be addressed in this note.

17. Of particular interest are the grounds:

    a. That the ET erred in law in finding there had been an agreement between the parties, within the meaning of the Partnership Act 1890; and
    b. The finding that the Claimant had, in fact, been exposed to financial risk as a partner was contrary to the ET's finding that he was a worker.

18. The Claimant argued that the ET relied too heavily on an agreement to pay, which is not determinative of partnership status (per s.2 of the PA 1890). The parties had agreed at the outset that the Claimant was not to be liable for the partnership's debts, and this was a material term that needed to be agreed before there could be a contract for partnership. Other conditions which the Claimant had orally stated as being necessary before he agreed to becoming a partner had not been satisfied.

19. The finding of the Claimant was exposed to financial risk was said to amount to an error of substitution, and went against the weight of the evidence.

The EAT's Decision

20. At paragraphs 38-49, Eady P carried out a thorough review of the relevant law of determining employment status in the context of a partnership or potential partnership, that any practitioner would find useful to bookmark for future reference (as the author has).

21. She noted that the ET had, permissibly, placed weight upon the label the parties had themselves used at the time, without treating this as determinative. It was a matter of fact, upon which the ET was best placed to answer, whether the Claimant's purported conditions for agreeing to partnership remained constant, such that he could not be said to be a partner without those conditions being satisfied.

22. She did, however, express herself as "initially troubled" by the fact that the agreement which the ET found the parties had entered into did *not* include their common intention to exclude the Claimant from liability (s.9 of the PA 1890 instead applying, as the default).

23. The curious result is that, had the parties agreed on such an exclusion it is possible this may – as part of the multi-factorial assessment – swing the needle back in favour of the relationship being that of employment: the *absence* of an agreement labelled as a partnership agreement may, in this case, have been what resulted in a partnership.

24. Ultimately, however, she did not consider this an error of law: it was open to the Tribunal to find that the absence of agreement on this point was not fatal to an agreement of partnership, and that the position was therefore governed by s.9 of the PA 1890. More broadly, the ET was "satisfied that the agreement between the parties was […] sufficiently certain as to mean that a legally binding partnership existed between them". The President, in language that does not appear a ringing endorsement of the Tribunal's decision, stated she "cannot say the ET was not entitled to reach the conclusion that it did".

25. On the other ground summarised above, the key issue was not properly before the EAT in the judgment: neither side had sought to upset the assumption of the ET, following the practitioner text, that a partner may well be a worker even if they cannot be an employee. So long as that position remained tenable in law, it was a matter of fact for the Tribunal to determine and the ET "was entitled to see the facts of this case as tipping the balance in favour of the claimant being a worker for section 230 purposes notwithstanding its conclusion that those facts did not (on its assessment) allow for a finding of employee status".

Conclusions

26. As many practitioners will have experienced, the nature of small partnerships all too often gives rise to disputes on the precise nature of agreements, not always fully set out or formally executed.

27. This judgment may be useful for those wishing a Tribunal to be "brave" in inferring an agreement – particularly of partnership – in the absence of a fully executed agreement setting out all relevant matters.

28. It is, further, a clear statement that there is no case law indicating that a partner cannot also be a worker (although, the matter not being before it, the EAT did not provide *positive* authority to that effect).

As noted above, the judgment also serves as a clear statement of the relevant principles in determining the existence of an employment relationship against the background of a potential partnership.

8 July 2024

Alex Leonhardt

Barrister
3PB Barristers

020 7853 8055
Alex.leonhardt@3pb.co.uk

3pb.co.uk