IN THE HIGH COURT OF NEW ZEALAND
NAPIER REGISTRY

CIV-2010-441-000833
[2012] NZHC 204

UNDER	the Arbitration Act 1996
BETWEEN	MATTHEW BRUCE LAWSON AND BLAIR ROBINSON Appellants
AND	MICHAEL JOHN WENLEY, ALAN JAMES DAVIES, LAWRENCE WILLIAM WILLIS AND RICHARD IAN CROSS Respondents

Hearing: 22 November 2011

Counsel: J O Upton QC for Appellants
M J Wenley for Respondents

Judgment: 22 February 2012

JUDGMENT OF THE HON JUSTICE KÓS

Introduction

[1] A law partnership fragments. Three of the seven partners resign in the course of three months. By law, each resignation dissolves the partnership. By agreement, the remaining partners reconstitute in partnership immediately. At the third resignation they promote a staff member; the reconstituted partnership includes him also. By agreement also, retiring partners are entitled to payment of their capital, advances and an agreed proportion of work in progress. But a clause in the partnership agreement restricts the total payable in any year to 5 per cent of the net income of the continuing partnership. There is no express provision for interest should this cap delay the payout. With three leaving, there will be a delay.

[2] Two of the retiring partners contend that the admission of the new partner means the cap can no longer apply. And if, notwithstanding, it still does apply, then they should receive interest. An arbitrator disagrees. By leave, they appeal to the High Court.

Facts

[3] The firm of Willis Toomey Robinson (WTR) has existed in one form or another for almost 125 years. It is based in the city of Napier. The firm is the product of the merger, nearly 30 years ago, of two predecessor firms: Robinson Toomey & Partners and Lusk Willis & Co.

[4] As from 1 October 2001 (following the retirement of Tim Twist) the partnership comprised seven men: Russell Robinson, Michael Wenley, Alan Davies, Lawrence Willis, Richard Cross, Matthew Lawson and Blair Robinson (Russell's son). On 31 December 2008, two partners retired: Russell Robinson and the appellant Matthew Lawson. Mr Lawson had been a partner for over 12 years at that point. Three months later, on 31 March 2009, the second appellant, Blair Robinson also retired. Mr Robinson Jr had been a partner for exactly 10 years.

[5] On 1 April 2009 two things happened:

(a) the appellants formed a new partnership, called Lawson Robinson; and

(b) the remaining partners of WTR, the respondents, formed a new partnership. This included a new partner, previously an employee of the firm, Kevin Callinicos.

[6] The changing partnership of WTR can be tabulated thus:

01/10/01-31/12/08	01/01/09-31/03/09	01/04/09-
Robinson Sr* Wenley Davies Willis Cross Lawson* Robinson Jr	Wenley Davies Willis Cross Robinson Jr*	Wenley Davies Willis Cross Callinicos**
*= retires at end of period		**=new partner

[7] The essence of the dispute between the parties, which I will enlarge on later, is that despite the termination of the WTR partnership on 31 December 2008, and then again on 31 March 2009, neither Messrs Lawson nor Robinson Jr has been paid sums provided for in the partnership agreement by way of retirement entitlements. The partnership agreement provides that retiring partners are entitled to:

(a) repayment of capital as at date of retirement; plus

(b) the amounts credited to a partner's current account as at date of retirement; plus

(c) (if the partner had served 10 years) that partner's share of 60 per cent of the work in progress of the partnership at the date of retirement.

[8] It is common ground that Mr Lawson is owed the following:

Capital	$50,000
Current account	$ 9,239
Work in progress	$34,852
	$94,091

Likewise, that Mr Robinson Jr is entitled to:

Capital	$50,000.00
Current account	$ (5,060.41)
Work in progress	$40,937.85
	$85,877.44

[9] Payment of these amounts has been deferred under the clause that caps payment. The same clause gives priority to payment to partners retiring by reason of advanced age or death. That has meant that Mr Robinson Sr is to be paid out first. The key questions are whether Messrs Lawson and Robinson Jr are entitled to receive these amounts now, despite the cap, and (if not) whether they are entitled to interest pending payment.

Partnership agreement

[10] The partnership agreement was entered in August 1999. It provides, relevantly, as follows:

> 3 THE partnership shall continue until terminated in manner hereafter provided. The death, retirement or bankruptcy of any Partner shall not determine the partnership as to the other Partners.
>
> ...
>
> 9 THE interest of any Partner in the partnership business shall cease and determine and his share or interest in the assets of the partnership shall be payable to him as hereafter provided in the event of:
>
> (a) The death or permanent disability (including permanent illness or sickness) of the Partner;
>
> (b) The voluntary retirement of the Partner by the Partner giving to the other Partners three (3) months' notice of his retirement from the practice;
>
> (c) The bankruptcy of the Partner;
>
> (d) The Partner involved attaining the age of sixty five (65) years subject to continuation at the option of the Partner reaching such age up to a time no later than his 70th birthday;

(e) The expulsion of the Partner from the partnership.

...

12 ...

(b) On the death or retirement of a Partner full and complete accounts of the partnership business shall be taken as at the date of death or retirement of the Partner as the case may be.

(c) The share of the deceased or the retired Partner shall be calculated as follows and the retired Partner or the administrators of the estate of the deceased Partner shall be entitled to the sum of the following:

(i) Repayment of the capital of that Partner in the capital of the partnership as at the date of death or retirement fund or alternatively if the capital of that Partner shall be in debit then that debit will be reimbursed by that Partner or deducted from any moneys that would otherwise be payable to him hereunder.

(ii) The amount (if any) lying to the credit of that Partner in his current account as at the date of death or retirement or alternatively by deducting from the share the amount by which the current account of the Partner is in debit if such be the case.

(iii) The Partner's share in the proceeds of the policies of the life of that Partner referred to in sub-paragraph 14(a) hereafter set out or in any policies in substitution or in addition thereto.

(iv) That Partner's share of the moneys comprising any retirement fund which is the property of the firm.

13 UPON the death or retirement of a partner after ten (10) years' service as a partner, they (or their executors as the case may be) shall also be entitled to and shall be paid by the then remaining Partners that Partner's share of sixty per cent (60%) of the work in progress of the partnership as at the date of death or retirement and it is hereby agreed that such payment shall be deemed to be payment of income.

...

15 PAYMENTS to any Partner, Partners or his or their administrator/s pursuant to clauses 12 and 13 hereof shall be limited to a total amount in any one year not exceeding five

> (5) per cent of the nett income of the partnership in that year and the payments to the Partner, Partners or estates involved shall be spread accordingly. If the amounts payable in any year are payable to more retiring or deceased Partners' estates than one (1) then the sums involved are to paid first to the Partner (or his representative) whose retirement is due to death or to age or to ill-health in priority to any Partner who has ceased to be a Partner for any other reason PROVIDED HOWEVER that the provisions of this clause shall not apply to the proceeds of any insurance policies paid pursuant to clause 14 hereof.
>
> ...
>
> 18 ALL disputes which may arise between the Partners or between one of them and the personal representative of the other or between their respective personal representatives touching or concerning the partnership or any matter incidental to it shall be referred to a single arbitrator; to be nominated in case the Partners or their representatives cannot agree by the President for the time being of the Hawke's Bay District Law Society. The arbitrator shall have full power to dissolve the partnership if he thinks fit AND this clause shall be deemed a *"a submission"* within the meaning of the Arbitration Act 1996. The prime consideration to be applied by the arbitrator should be fairness to all concerned as opposed to the purely legal position which, of course, must be a factor to be taken into account.

[11] It may be noted that the agreement provides no restraint of trade on retiring partners.

The award

[12] Three issues were referred to the arbitrator, the Hon B J Paterson QC. The third need no longer concern us. The two primary issues were these:

(a) Whether by virtue of the entering of the respondents into partnership with Mr Callinicos on 1 April 2009, the respondents are required to make immediate payment to the appellants of their entitlements due upon their respective retirements from partnership with the respondents?

(b) Whether the appellants are entitled to interest at the rate of 5 per cent per annum on their entitlements from the dates of their respective retirements pursuant to s 45(1) of the Partnership Act 1908 (the Act)?

[13] On the first issue, the learned arbitrator held that until 31 December 2008 there had been a partnership in which all parties to the arbitration were partners, together with Mr Robinson Sr. That partnership came to an end on 31 December 2008 when Messrs Lawson and Robinson Sr retired. A new partnership comprising Mr Robinson Jr and the four respondents came into existence on 1 January 2009. That partnership then terminated with the retirement of Mr Robinson Jr on 31 March 2009. Subsequently another partnership came into existence on 1 April 2009 when the respondents reconstituted their partnership, admitting Mr Callinicos in the process. It was agreed by the parties that that analysis by the arbitrator is correct.

[14] The arbitrator then noted the background to clause 15, being an identical provision in an earlier 1992 partnership agreement. Its contextual rationale was this: in 1987 three partners had retired together to form a new firm. This "mass exodus" had caused financial hardship to the remaining partners. The arbitrator held that the "plain and ordinary meaning" of the words in clause 15 should be departed from. He interpreted the words "net income of the partnership" as "the net income of the successive partnership or partnerships to the partnership which is dissolved". The arbitrator noted this would cause possible hardship for the appellants. But he was satisfied that a reasonable person would not consider the meaning of the term only applied while the remaining partners were the only partners in the firm. In other words, the admission of Mr Callinicos into the partnership on 1 April 2009 did not displace the cap in clause 15.

[15] On the second issue, interest, the learned arbitrator held that s 45 of the Act did not apply. That was because there had in fact been a "final settlement of accounts". There was no dispute that "complete accounts of the partnership business" had been taken at the dates of retirement - in accordance with clause 12(b) of the partnership agreement. Accordingly s 45(1) did not apply. Alternatively, that provision could not apply because the partnership agreement was an "agreement to the contrary". It followed that interest was not payable. The consequence of the

award was that the appellants would have to wait for their money, without payment of interest, until Mr Robinson Sr had been fully paid out.

[16] The arbitrator did consider clause 18 of the partnership agreement. That has been set out already at [10] above. He thought the provision ambiguous. That was because it suggested fairness as a primary consideration, but then required the legal position also to be taken into account. The arbitrator said:

> If I were to consider applying the provision in this arbitration, it would be applied to the claimants' interest claim. The evidence suggests that the claimants may be out of their money for some time without payment of interest. It is obvious that the relationships between the claimants and respondents are not cordial. Equity and justice may suggest that it will be appropriate for the respondents to suggest an arrangement either to accelerate the payments due and/or pay interest on them after a reasonable period of time.
>
> The difficulty is that the parties entered into an agreement and for a particular reason agreed to cap payments to outgoing partners. They did so under an agreement which did not require interest to be paid on the amounts pending payment. The legal position is that there is no obligation to pay interest or to accelerate the payments. In the circumstances, I do not see that I can award interest under this provision.

Issues

[17] On 24 June 2011 Allan J gave leave to appeal on the following questions of law:[1]

> (a) Whether the arbitrator's interpretation of the provisions of cl 15 of the Partnership Agreement is correct.
>
> (b) Whether the arbitrator erred in his interpretation of what was required for there to be a "final settlement of accounts" for the purposes of s 45 of the Partnership Act 1908.
>
> (c) Whether the arbitrator erred in his interpretation of the Partnership Agreement and/or the Partnership Act 1908 in finding that there was no requirement to pay interest on the amounts due pending payment.
>
> (d) Whether the arbitrator erred in his interpretation of the Partnership Agreement and/or the Partnership Act 1908 in finding that the provisions of the Partnership Agreement contained an "agreement to the contrary" which negated the obligation to pay interest in accordance with s 45 of the Partnership Act 1908 on the sums due by the respondents to the applicants.

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1 *Lawson v Wenley* HC Napier CIV-2010-441-833, 24 June 2011.

(e) Whether the arbitrator erred in law by failing to give effect to the concluding words of cl 18 of the Partnership Agreement.

[18] It is convenient to consider questions (a) and (e) together first, under the heading "payment cap", and then issues (b) – (d) and (e) (again) under the heading "interest".

Issue One: Payment cap

Submissions

[19] Mr John Upton QC, for the appellants, submitted that cl 15 addresses two things. First, the rate of payment of the sums owing under cl 12 and 13 (i.e. to a maximum of 5 per cent per annum of net income per annum). Secondly, priority of payment to partners retiring because of advanced age. He submits that "the partnership" referred to in cl 15 is the new partnership. In relation to Mr Lawson, that was the partnership formed on 1 January 2009, following his retirement and that of Mr Robinson Sr. In relation to Mr Robinson Jr, it was the "further partnership coming into existence as from 1 April 2009 with the admission of Kevin Callinicos". But, he says, cl 15 does not contemplate a partnership including someone not liable to the retiring partners. That, he says, is its plain and ordinary meaning. Mr Upton's essential submission was this:

> While cl 15 of the deed contemplates payment over time by the new partnership comprising the remaining partners, as soon as they enter into another partnership with a third party and transfer their partnership assets to that other partnership, then the debts of the former partnership (in the absence of agreement with the outgoing partners to transfer to the debts to the other partnership), are payable before the assets are applied to the new partnership.

[20] Mr Upton's argument was that the approach taken by the arbitrator (to treat "the partnership" in cl 15 as whatever succeeding partnership continued from time to time) was an improper departure from the plain and ordinary meaning for which he contends. The arbitrator's approach conferred the benefit of cl 15 "on successive partnerships" (including strangers). And it treated the partnership as if "in a form of perpetual existence". It meant the appellants had agreed to payment of moneys due to them to be determined by people with whom they have no partnership

relationship, have no contractual relationship, and may not even know the existence of in the future. The appellants would have no control over the net profit of the new partnership. And nor will those of the respondents who themselves retire in the future.

[21] Mr Upton submitted that the arbitrator's approach also meant the respondents would get to have their cake and eat it. They were able to sell assets to incoming partners, and apply the proceeds for their own purposes, and still have the benefit of time payment to the appellants.

[22] As to cl 18, Mr Upton submitted that its effect is to mandate fairness as the "prime consideration" to be applied by the arbitrator. The "ordinary meaning" of cl 15, limiting the deferral of the obligation to liable partners continuing in partnership, without admission of new partners, would in fact achieve fairness. Clause 18 would reinforce that approach. Fairness would also mitigate the effect of cl 15 where the continuing partners have a benefit of capital paid in by new partners, but do not pay out the old.

[23] Mr Michael Wenley appeared on his own behalf and that of the other three respondents. He submitted the arbitrator's interpretation of cl 15 was correct. The words "net income of the partnership in that year" means "net income of the successive partnership or partnerships to the partnership which is dissolved". The intent of the clause was that if the firm continued in operation, the cap in cl 15 would apply to the income of the ongoing firm.

[24] Mr Wenley submitted that cl 15 was not intended to apply only while the remaining partners were the only partners in the firm, but would include a partnership comprising also third parties. Mr Wenley acknowledged that Mr Callinicos bears no liability to the appellants. However, to the extent, that he generates part of the net income of the partnership, his part is taken into account, and the net income (and cap) is enlarged accordingly. That was said to be logical, because the whole net income of the continuing firm (in whatever form it took) should be considered when regulating the payment stream from the liable continuing partners to the retiring partners.

[25] As to cl 18, Mr Wenley submits that it should not be allowed to strip away the protection and benefits of cl 15 provided, and which all parties intended by adopting the partnership agreement. He submits, correctly, that the benefit of cl 15 is not to successive partnerships, but rather to those continuing partners who are obliged to the retiring partners. Incoming partners, in accordance with the partnership agreement, contribute by instalment to the working capital of the firm. The payment in of capital by one new partner would not off-set the burden of paying out three retiring partners.

Analysis

[26] It is necessary to start with four preliminary observations.

[27] First, the parties were in agreement at least that "the partnership" referred to in cl 15 – the one whose net income caps the flow of funds to the retiring partners – had to be the *new* partnership. What they disagreed upon was what happened if the continuing parties took in a new partner. An alternative construction – that the relevant "partnership" for the purposes of cl 15 is the partnership *before* dissolution – was canvassed at the hearing. Principally at the prompting of the Court. But neither party expressed enthusiasm for it. I accept that construction is not available. The limit applies "in any one year" – i.e. post dissolution – and is calculated by reference to "the net income of the partnership *in that year*". So it must be the post-dissolution partnership, and therefore the new WTR partnership, whose income is measured in cl 15.

[28] Secondly, the consequence of the first point, on which the parties agree, is that the production of the net income is in the control of the remaining, non-retired (or "continuing") partners. There is a theoretical prospect of financial manipulation. That would be so whether or not a new partner was admitted. But (in practice) good faith, and (in law) the continuation of fiduciary obligations despite the termination of partnership, effectively preclude that. As to the latter point, see s 41 of the Partnership Act 1908, *Thompson's Trustee in Bankruptcy v Heaton,*[2] *Perens v*

[2] *Thompson's Trustee in Bankruptcy v Heaton* [1974] 1 WLR 605 (Ch).

Johnson,[3] *Chan v Zacharia,*[4] and *Hogar Estates Limited in Trust v Shebron Holdings Limited.*[5]

[29] Thirdly, it is the persons who were in partnership with Mr Lawson on 31 December 2008 and have not retired with him who must account Mr Lawson's share of capital, current advances and work in progress. Likewise those in partnership with Mr Robinson Jr on 31 March 2009. The appellant Mr Robinson Jr is liable to Mr Lawson in the former case. The reverse does not apply. This was a point rather glossed over by the appellants. But it is Mr Robinson Jr and the other non-retiring partners as at 31 December 2008, rather than the current partnership, who are liable to Mr Lawson. And it is the continuing partners, not including the new partner Mr Callinicos, who are liable to Mr Robinson Jr. The pleadings confirm that, correctly: no claim is made against Mr Callinicos.

[30] Fourthly, it is quite incorrect to say that cl 15 confers a benefit on the new partnership, including new partners. As I have just said, the liability remains that of the partners who have not retired. All that cl 15 does is to limit the rate at which the liability is discharged. It does so by reference to the generation of net income by the new partnership. That is a computational aid, but it does not transfer the liability, and the benefit of the cap, to new partners.

[31] The starting position in analysing the entitlement of retiring partners to be part of the assets of the partnership from which they have retired must be the Act, in particular s 42, 46 and 47:

> **42 Rights of partners as to application of partnership property**
>
> On the dissolution of a partnership every partner is entitled as against the other partners in the firm, and all persons claiming through them in respect of their interests as partners, to have the property of the partnership applied in payment of the debts and liabilities of the firm, and to have the surplus assets after such payment applied in payment of what may be due to the partners respectively after deducting what may be due from them as partners of the firm; and for that purpose any partner or his representatives may, on the termination of the partnership, apply to the Court to wind up the business and affairs of the firm.

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[3] *Perens v Johnson* (1857) 3 SM.&G. 419.

[4] *Chan v Zacharia* (1984) 154 CLR 178.

[5] *Hogar Estates Limited & Trust v Shebron Holdings Limited* (1979) 101 DLR (3d) 509 (Ont HC).

> **46 Retiring or deceased partner's share to be a debt**
>
> Subject to any agreement between the partners, the amount due from surviving or continuing partners to an outgoing partner or the representatives of a deceased partner, in respect of the outgoing or deceased partner's share, is a debt accruing at the date of the dissolution or death.
>
> **47 Distribution of assets on final settlement of accounts**
>
> In settling accounts between the partners after a dissolution of partnership the following rules shall, subject to any agreement, be observed:
>
> (a) Losses, including losses and deficiencies of capital, shall be paid first out of profits, next out of capital, and lastly, if necessary, by the partners individually in the proportion in which they were entitled to share profits:
>
> (b) The assets of the firm, including the sums (if any) contributed by the partners to make up losses or deficiencies of capital, shall be applied in the following manner and order:
>
> (i) In paying the debts and liabilities of the firm to persons who are not partners therein:
>
> (ii) In paying to each partner rateably what is due from the firm to him for advances as distinguished from capital:
>
> (iii) In paying to each partner rateably what is due from the firm to him in respect of capital:
>
> (iv) The ultimate residue, if any, shall be divided among the partners in the proportion in which profits are divisible.

[32] The latter two provisions are explicitly made subject to agreement. Section 42 must likewise take effect subject to agreement otherwise.

[33] In the present case the partnership agreement does affect the statutory position. First, clause 3 has the effect of automatically reconstituting the non-retiring partners in a new partnership. Not as the old partnership, but as a new one: [6]

> In law, the retirement of a partner, or the admission of a new partner, constitutes the dissolution of the old partnership and the formation of a new one. Here upon the happening of such events there was no overt signs of dissolution; the partnerships financial structure and arrangements were such that none was required but that does not alter the underlying legal significance of any retirement or new admission: ... nor, in my opinion, is it possible to avoid those legal propositions by the terms in the partnership agreement: no doubt it is competent for partners to agree in advance that in

[6] *Hadlee v Commissioner of Inland Revenue* [1989] 2 NZLR 447 at 455 per Eichelbaum CJ, affirmed on appeal: [1991] 3 NZLR 517 (CA), and [1993] 2 NZLR 385 (PC).

> the event of a retirement remaining partners will continue to practice in partnership but that does not overcome the consequence that the partnership practicing the day after the retirement is a different one from that in business the previous day.

[34] Secondly, as between the members of the prior partnership, the agreement provides that retiring partners are to be paid out in accordance with cls 9 and 12 to 15. No distribution in the sense contemplated by ss 42 and 47 (which apply in the case of a general dissolution unregulated by agreement) is to occur. As Webb & Molloy state:[7]

> Where, by agreement, one or more members of the firm are to continue the business upon terms that paying off the share of the outgoing or deceased partner or partners, ascertained upon a certain agreed basis, there should be no need to have a final accounting distribution. The agreement is, in effect, substituted for it.

The remaining assets are retained by the non-retiring partners who continue in a new partnership. In the absence, however, of a restraint of trade clause, not all the goodwill of the partnership will necessarily pass to the continuing partners. Those retiring partners who wish to do so may compete. With immediate effect. Subject to that qualification, the continuing partners bring the former partnership assets into the new partnership. They may admit new partners in accordance with the agreement. And they may require such capital contributions to any new partner as they see fit to cover his or her share of that new, revitalised venture. The retiring partner is entitled to the payments provided for in cls 12 and 13. Those obliged to meet that entitlement are the former partners, who thereafter continue in partnership in accordance with cl 3.

[35] Thirdly, the implied effect of cl 15 is that those payments are payable within a reasonable time of the taking of full and complete accounts under cl 12(b). That itself must occur within a reasonable time of the retirement. I say a "reasonable time" in each case, because no specific time is specified. There is nothing unusual about that omission.

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7 Webb & Molloy *Principles of the Law of Partnership* (6 ed, Butterworths, Wellington, 1996) at 306.

[36] Against that background, I turn to consider the merits of the competing contentions.

[37] The partnership agreement is plainly drafted with the intent that the partners continuing the partnership as WTR (and to whom the business and other assets of the former partnership is transferred in accordance with cl 3, subject to paying the retirement entitlements of the retiring partners) would not be unduly impacted by the payment of those entitlements. The 5 per cent limit of net income is obviously harsher when more than one partner has retired. On the other hand, the cap is all the more essential in that circumstance. And particularly so where the retiring partners are setting up in competition with WTR, so that there will be a falling-off of business. The evidence is that the cl 15 cap was the product of difficulties faced in 1987 when three partners left in one fell swoop to form another firm. So the context in which the cap was devised is in many ways similar to the situation that has given rise to the present dispute.

[38] As already noted, the parties are agreed that the "partnership" whose net income is referred to in cl 15 must be the new (or "continuing") partnership. The disagreement is over the effect of that partnership including a new partner, Mr Callinicos. But for Mr Callinicos' entry into the new partnership, there would be no argument under this heading. Had Mr Callinicos *not* been taken into the new partnership, there could be no doubt that cl 15 would limit the payment of the appellants' entitlements to 5 per cent of the net income of the continuing WTR partnership. The only argument would be about interest.

[39] So what difference does the entry of Mr Callinicos to the new partnership make?

[40] In the context described, it makes little sense to infer that the application of cl 15 is confined to a continuing WTR partnership comprised exclusively of the non-retiring partners, so that the admission of Mr Callinicos would have the effect of displacing the cap in cl 15.

[41] First of all, cl 15 simply does not say so.

[42] Secondly, the appellants' argument is mispremised on the proposition that the arbitrator's construction of cl 15 somehow confers a benefit on the new partnership (i.e. including the new partner), yet with the appellants unable to enforce the *quid pro quo* payment obligation against that entity. I have already demonstrated the falsity of that proposition. The payment obligations remain those of the former partners of the retiring partner. In the case of Mr Lawson (who was first out), that includes his co-appellant Mr Robinson Jr. It is those persons who have to reach into their pockets and find the money to pay the appellants. Mr Robinson Jr's obligations are not waived or cancelled because he has himself left the partnership. And nor are they altered by the fact that Mr Callinicos has joined the successor partnership. Save, that is, in one respect, which I explain in the next paragraph. But Mr Callinicos shares none of his partners' obligations to the retired partners, and the partnership he has joined makes no payment to them.

[43] Thirdly, the 5 per cent cap is referenced to the net income of the succeeding partnership for computational ease. Admission of a new partner can realistically be expected to *add* to the net income (i.e. income less expenses, before drawings and tax) of the continuing partnership. That is all the more so when the new partner was formerly an employed solicitor, whose salary was an expense. There would be little point in any case in admitting a new partner whose effect was to reduce net income, by generating more expense than income. So the admission of a new partner should benefit the retired partners, by increasing in dollar terms the amount that the continuing partners must pay to the retiring partners year by year. To that extent the entry of a new partner does affect the continuing partners' obligations to those who have retired. The admission of further partners is not inimical to the purpose of the clause, and it is beneficial to the interests of the retiring partners. There is no need therefore to read the clause down in the way suggested by the appellants.

[44] Fourthly, there is no need to address the application of the clause in the situation where, unlike here, there is a general dissolution. Nor where there is a second mass exodus of partners (so that the 5 per cent limit is not very much at all). In the former circumstance the cap would not apply at all. In the latter circumstance, its operation may potentially be affected by the implication of a term. But there is no

need in this case, where all the non-retiring partners[8] are continuing in partnership and operating the business of WTR, augmented by a new partner, to resort to implication.

[45] I am not persuaded by the appellants' submission that the absence of privity with the new partnership is fatal to "the partnership" including new partners. There is no need for such privity. The appellants are owed contractual and fiduciary duties[9] by the respondents, the continuing or non-retiring partners. Those duties continue notwithstanding the formation of a new partnership. Mr Robinson Jr's obligations to Mr Lawson to meet his retirement entitlements continue regardless of the fact that he has himself left the WTR partnership. The false premise in the appellants' argument is that it is necessary for the appellants to enjoy a contractual relationship with the new partnership. Mr Upton had sought to submit that the retired partners are: "left unable to enforce or recover the debt from parties with whom they had no relationship". But that misses the point; the relevant liabilities are of the continuing partners to the retiring partner. It is simply the *rate* at which those obligations are to be discharged that is regulated by the activities of the successive partnerships. The identities of those liable, and those continuing the WTR practice, may differ. Privity is not required.

[46] Nor does the construction given to the clause by the arbitrator have the effect of "giving partnerships a form of perpetual existence", as Mr Upton submitted. It does no such thing. The clause merely regulates the rate at which the obligations of the non-retiring and continuing partners are to be discharged, by reference to the activity of the new partnership. The participation in that partnership of a new partner does not displace the logic of the provision. There is nothing unusual about the discharge rate of an extended obligation being indexed to an independent reference point.

[47] Against that background I conclude that the arbitrator was correct to hold that "the partnership" in cl 15 means: "the net income of the successive partnership or partnerships to the partnership which has dissolved".

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8 Apart, in the case of those liable for Mr Lawson's entitlements, from his now current partner, Mr Robinson Jr.

9 See at [28].

[48] The arbitrator considered this was not the plain and ordinary meaning of the clause. To the extent he was of that view, I do respectfully disagree. The "partnership" referred to in cl 15 as a matter of construction must be the partnership continuing the "partnership business" of WTR in accordance with cls 2,[10] 3 and 5[11] of the partnership agreement. When one appreciates that the point of the provision is calculation of rate of payment, rather than any ascription of liability, there is no impediment to that including newly admitted partners from time to time. And indeed there is every reason economically and practically to do so, as it can be expected to enlarge the payments to retired partners.

[49] Had I not been of the view that this was the plain and ordinary meaning of cl 15, I would have reached the same conclusion under cl 18.

[50] A clause in the form of cl 18 is relatively unusual in New Zealand.[12] Such provisions are sometimes referred to as *ex aequo et bono* or "amiable compositeur" clauses, although they vary widely in form. The editors of *Williams & Kawharu on Arbitration* say that "the common law has traditionally been suspicious of clauses permitting decisions according to equity or justice rather than law; civil law much less so".[13] Such clauses are not uncommon in cross-border contracts.

[51] The Arbitration Act 1996, sch 1, art 28(3) makes it clear that an arbitrator is not free to decide a dispute according to considerations of general fairness and justice unless the party has expressly authorised the tribunal to do so. It is clear that cl 18 is exactly such authority. Article 28(3) was considered by Baragwanath J in *A's Co Ltd v Dagger.*[14] It is unnecessary for me to retraverse the discussion of the principles underlying the exercise of *ex aequo et bono* jurisdiction outlined by Baragwanath J in that judgment. Particularly as I received no submissions on underlying principle from counsel.

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[10] Partnership to continue to conduct the partnership business in Napier.
[11] Firm name to be Willis Toomey Robinson.
[12] *Williams & Kawharu on Arbitration* (Lexis Nexis, Wellington, 2011) at 346.
[13] Ibid, 347.
[14] *A's Co Ltd v Dagger* HC Auckland, M1482-SD00, 7 March 2003.

[52] It is clear that in the present case the arbitrator found the clause difficult. I have set out already what he had to say about it.[15] With great respect to the arbitrator, the clause may not be as difficult as it might first appear. The clause is clear enough that the primary consideration to be applied by the arbitrator is fairness to all concerned. The "purely legal position" remains a factor to be taken into account. But the clause authorises the arbitrator to dispense with the purely legal position if another outcome is fairer to all parties. As Baragwanath J's judgment makes clear, this modified jurisdiction has been familiar to civilian lawyers since the 13th century. Although the *Dagger* case concerned procedural rather than substantive aspects of the application of such a clause, I agree with Baragwanath J that art 28(3) and a clause such as cl 18:[16]

> … must result in modification of the strict language of the written contract to the extent of any inconsistency with a fair and equitable result.

[53] In the present case, however, I conclude that the fair application of the contract is consistent with its ordinary construction according to law. The appellants' case is mispremised on the assumption that the re-entry of the continuing partners into a new partnership including a third party confers a benefit on strangers to the 1999 partnership agreement. It does not. It is mispremised, also, on the proposition that the arbitrator's construction of cl 15 in effect creates partnerships of perpetual succession. Again, it does not.

[54] A broad equitable approach to the application of the contract in the present case will take into account the origins of the clause, the way in which it has been applied in the past, and the respective economic interests of the various factions. Had Mr Callinicos not been admitted to the succeeding partnership after Mr Robinson Jr retired, there would have been no argument under this heading. But the entry of a new partner to the continuing partnership is, from the outlook of fairness, immaterial to the obligations of the previous partners. Rather it has the mutually beneficial result of expanding the cap under cl 15 by including the new partner's contribution to net income in the computation of the capped amount payable annually by those who are continuing partners. There is simply nothing

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[15] At [16].
[16] At [146].

unfair in holding the appellants to a bargain which would have applied, somewhat less beneficially, had the continuing partnership not incorporated Mr Callinicos when it reformed on 1 April 2009. What would be unfair would be to treat that beneficial development as giving rise to a greater benefit still: the displacement of the agreed cap.

[55] In saying this I recognise that Mr Callinicos will have introduced additional working capital to the new partnership. How much is unclear, but the evidence shows that it is being injected on a staggered basis over 5 or 6 years. As was the case when the appellants joined the WTR partnership. The amount payable would appear to be nothing like the amount the continuing partners owe to the appellants. But the issue was insufficiently explored in evidence for me to be able to make any meaningful assessment either way. There is insufficient evidence of consequent unfairness to engage cl 18 on this basis.

Conclusion

[56] The effect of cl 15 of the agreement is to displace the usual requirement for settlement of amounts in accordance with s 47, following dissolution. The respondents remain liable to the appellants to meet their cl 12 and 13 entitlements, but subject to the cap in cl 15. I am satisfied therefore that the arbitrator's interpretation of cl 15 was correct. Clause 18 does not compel a different outcome.

Issue Two: Interest

[57] Of central significance to the argument in relation to interest was s 45 of the Act:

> **45 Right of outgoing partner to share profits made after dissolution**
>
> (1) Where any member of a firm dies or otherwise ceases to be a partner, and the surviving or continuing partners carry on the business of the firm with its capital or assets without any final settlement of accounts as between the firm and the outgoing partner or his estate, then, in the absence of any agreement to the contrary, the outgoing partner or his estate is entitled, at the option of himself or his representative, to such share of the profits made since the

> dissolution as the Court may find to be attributable to the use of his share of the partnership assets, or to interest at the rate of 5 percent per annum on the amount of his share of the partnership assets.
>
> (2) Provided that where by the partnership contract an option is given to surviving or continuing partners to purchase the interest of a deceased or outgoing partner, and that option is duly exercised, the estate of the deceased partner or the outgoing partner, or his estate, as the case may be, is not entitled to any further or other share of profits; but if any partner assuming to act in exercise of the option does not in all material respects comply with the terms thereof he is liable to account under the foregoing provisions of this section.

[58] The arbitrator held:

> Neither counsel concentrated on the meaning of "final settlement of accounts". It is difficult to see that there was not a final settlement of accounts in this case. The amounts due to the claimants were fixed by accounts prepared at the respective dates of dissolution. There is no dispute that "complete accounts of the partnership business" were taken at the date of retirement, and in accordance with cl 12(b) of the partnership agreement. Section 47 of the Act sets out the mechanism for determining those accounts in the absence of any agreement. Because of the final settlement of accounts, s 45(1) does not apply.

Submissions

[59] For the appellants Mr Upton submits that a "final settlement of accounts" for the purposes of ss 45 and 47 does not occur until the accounts are actually paid. As Mr Upton put it, "preparation of accounts may be a step on the way, but it does not in itself constitute a settlement, let alone a final settlement". In the absence of a final settlement of accounts, s 45(1) would require in this case – on the basis there is no agreement to the contrary – either payments to the appellants of a share of the profits (reflecting the profits made from the use of their share of the partnership assets not paid to them) or simple interest at the rate of 5 per cent per annum on their share of the retained partnership assets. The appellants' pleadings before the arbitrator were equivocal as to which option they chose. But it is clear from the submissions made to me that their claim is to interest.

[60] For the respondents, Mr Wenley submitted that "final settlement of accounts" for the purposes of s 45 is the definition of final entitlements – the debt due in accordance with s 46 – but does not mean payment of that debt. Mr Wenley's core

argument was that s 45 was in any event inapplicable, because cl 9 of the partnership agreement had the effect of being an automatic accruer clause, so that upon retirement the retiring partners ceased to have any share or interest in the assets of the partnership. Instead that share was converted to a debt owed to the retiring partner by the continuing partners. This was, for the purposes of s 45(1), an "agreement to the contrary", and there was no basis on which the appellants could contend that they were entitled to a profit share beyond the date of partnership. The effect of cl 9 was that the rights of the retiring partners converted to a debt. The debt was not immediately payable, despite accounts being finally settled, because the agreement provides for payment in instalments limited to 5 per cent of the successor partnership income in each year.

Analysis

[61] Clause 9 (which I have set out already at [10]) is, as Mr Wenley submits, an automatic accruer clause. The operation of such a clause is described by the editor of *Lindley & Banks on Partnership* in these terms:[17]

> There are, in essence, two ways in which continuing or surviving partners can acquire an outgoing partners share, i.e. pursuant to an option or a so-called "automatic accruer". By the latter expression is meant a provision which states that the share of an outgoing partner will automatically vest in the remaining partners on the date that he ceases to be a member of the partnership, whether by reason of his death or otherwise. In either case the agreement will, of course, establish the financial entitlement of the outgoing partner in respect of his share, whether expressed in terms of an option price or the sum payable on or consideration of the accruer.

[62] Such accruer clauses are commonplace in professional services partnerships. The effect of such a clause is that there is no need to undertake a general dissolution, in accordance with ss 42 and 47 of the Act. The entitlement of the retiring partner is not to distribution of assets, but as against his former partners to payment of the debt represented by the entitlements expressed here by cls 12 to 13.

[63] Sections 45 to 47 are in each case subject to a partnership agreement to the contrary. Neither ss 45 nor 47 are applicable in the present situation where the automatic accruer in cl 9 applies and the appellants' entitlements are fixed by

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[17] *Lindley & Banks on Partnership* (19 ed, Sweet & Maxwell, UK, 2010) at 10-151.

agreement. That position is supported by authority. The editor of *Lindley & Banks on Partnership*, after discussing the House of Lords' decision in *Vyse v Foster,*[18] says:[19]

> It follows that any provision for the automatic accruer for the outgoing partner's share will necessarily exclude his rights under s 42(1).

The reference to s 42(1) in the United Kingdom legislation is, of course, s 45(1) of ours.

[64] It follows that ss 45 and 47 are in the present case simply inapplicable. The partnership agreement contemplates its own process of payment.

[65] Furthermore, in my view the arbitrator was entirely right to say that the expression "final settlement of accounts" contemplates the resolution of what is owing, rather than the discharge of debt itself. The expression "settled accounts" is one of long mercantile usage. It simply means accounts that have been agreed by debtor and creditor.[20] Such accounts are conclusive, and may be raised as a defence to an action to account further. But they do not connote discharge of the debt itself.

[66] In the partnership context, such a construction is confirmed by the decision of the Court of Appeal in *Holdgate v Holdgate.*[21] That decision recognised that the final settlement of accounts is a necessary pre-requisite to the establishment of a creditor/debtor relationship between former partners in the absence of an automatic accruer provision.[22] Subject to agreement, of course, the debt itself will accrue for purposes of limitation from the date of dissolution, in accordance with s 46.[23]

[67] In this case the payments due under cls 12 and 13 are debts. The debts accrue at the date of dissolution. The rate of payment, however, is modified by cl 15. The

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18 *Vyse v Foster* (1872) 8 LR Ch Appellant 309 (CA) affirmed in (1874) 7 LR HL 318; followed in *Hordern v Hordern* [1910] AC 465 (PC).
19 *Lindley & Banks on Partnership* (19 ed) at 25–38.
20 *Darthez Bros v Lee* (1836) 2 Y & C Ex 5; *Newen v Wetten* (1862) 31 Beav 315; *Phillips-Higgins v Harper* [1954] 1 QB 411 (CA).
21 *Holdgate v Holdgate* [2002] 3 NZLR 609 (CA).
22 See [37], [40] and [41] of the decision.
23 See at [31] above.

continuing partners are entitled to defer payment of the debt in accordance with that clause.

[68] A debt does not in and of itself carry interest. At common law, interest will be payable where there is express agreement to pay interest, where such agreement can be implied from contract or the parties course of dealing, or in certain circumstances by way of damages for breach of contract. These instances apart, debts do not carry interest at common law.[24] Neither equity[25] nor statute alters that outcome in this case. The Courts possess a discretion to award interest on debts under s 87 of the Judicature Act 1908. Period and rate are discretionary, as is the making of the award itself. Similarly under the Arbitration Act 1996, s 12(1)(b).

[69] In the present case the parties elected to provide for deferral of payment under cl 15. Preference was given to payment to those who retired by reason of advanced age, ill health or death. They will not compete with the existing partnership. Others who are free to compete with it may have to wait. Clause 15 is carefully drafted. It contemplates deferral of payment and priorities between partners in different circumstances. It is self-evident that some may have to wait. Yet it is silent as to interest. As a matter of history, the partnership has not paid interest to previous retiring partners.

[70] In these circumstances there is no sound basis to imply an obligation to pay interest, either as a matter of pure contract law, or in accordance with cl 18's broader authority. I therefore decline to do so. At the suggested 5 per cent simple interest rate, Mr Lawson is out of pocket by some $4,700 per annum, and Mr Robinson Jr some $4,300. While this may be felt to be unjust, that is the bargain that they made. In the meantime they are free to exercise their right to compete with the continuing partners of WTR. That is a right that they are exercising.

[71] I turn now to cl 18. The contract provides priority to the payment of partners who are retiring because of advanced age or ill health, or to the estates of those who have died. Such partners will not compete with the continuing partnership. Those

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[24] *President of India v La Pintada Compagnia Navigacion SA* [1985] AC 104 (HL) at 115–116 per Lord Brandon.

[25] There being no breach of equitable obligation in not making payment earlier than cl 15 requires.

who are younger, and who can compete, may in accordance with the clause be required to wait to be paid out. Although there is a cost to them of being out of their money, that is at least balanced by the fact that in the absence of a restraint of trade clause they are free to compete, and to divert the goodwill of the previous partnership as far as they can to themselves. As noted, historically interest has not been paid. The potential (and at best partial) offset of Mr Callinicos' staggered working capital contributions was insufficiently explored in evidence before the arbitrator for me to conclude that it provides any basis to engage cl 18.[26]

[72] The consequence is the application of cl 18 in this case would not alter the ordinary legal construction of the contract.

Conclusion

[73] I am satisfied therefore that the arbitrator did not misdirect himself on the issue of interest.

Disposition

[74] The appeal is dismissed.

[75] Costs in this Court are to lie where they fall.

Stephen Kós J

Solicitors:
Lawson Robinson, Napier for Appellants
Willis Toomey Robinson, Napier for Respondents

[26] See [55] above.