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DePaul Business and Commercial Law Journal

Volume 12
Issue 3 *Spring 2014*

Article 2

Self-Help in the Break-Up of Informal Partnerships

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Recommended Citation

Val Ricks, *Self-Help in the Break-Up of Informal Partnerships*, 12 DePaul Bus. & Com. L.J. 259 (2014)
Available at: https://via.library.depaul.edu/bclj/vol12/iss3/2

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Self-Help in the Break-Up of Informal Partnerships

*Val Ricks**

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I. THE SELF-HELP PROBLEM IN INFORMAL PARTNERSHIPS

A. *The Scenario*

Jerry, Nick, and Lorenzo Monteleone formed a partnership to own and operate the Monte Auto Body Shop.[1] The brothers had no written partnership agreement.[2] But they had agreed to split profits and losses, and contribute capital and labor, equally.[3] Each would receive weekly compensation.[4] Because the three had no other agreements, to that extent their arrangement was governed by the default provisions of the partnership code.[5] Because the brothers did not have any

* Professor of Law, South Texas College of Law. Thanks to Robert W. Hillman and Gary Rosin for comments and conversations prior to publication.

1. Monteleone v. Monteleone, 497 N.E.2d 1221, 1223 (Ill. App. Ct. 1986).
2. *Id.*
3. *Id.* at 1225.
4. *Id.*
5. That would be the result under the Texas Business Organizations Code. *See* TEX. BUS. ORGS. CODE ANN. § 152.002(a) (2013) ("To the extent that the partnership agreement does not

agreement regarding the length of time their partnership would last, and they undertook an activity of indefinite duration (as opposed to a specific task), their partnership was at will.[6]

Several years after the partnership formed, Nick and Lorenzo came to believe that Jerry had wronged them and the partnership. Jerry took too much money in his weekly draw,[7] misappropriating partnership funds.[8] Jerry also failed to contribute equally, demanded that his son be made a partner in the business, required (over Nick and Lorenzo's decision otherwise)[9] that a certain employee be discharged, and refused to return certain "partnership books and records."[10]

Nick and Lorenzo might have consulted a lawyer. They could have sued Jerry. But this would have been the first time that the three engaged the legal system. They were, after all, a partnership by default. Rather than obtain the help of others, Nick and Lorenzo engaged in self-help. They excluded Jerry from the premises. Nick and Lorenzo continued to operate the business.[11]

So Jerry sued, alleging that Nick and Lorenzo had wrongfully excluded him, thus "effecting a dissolution of the partnership."[12] Jerry asked for a ruling that the partnership had dissolved, a wind-up of its

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otherwise provide, this chapter and the other partnership provisions govern the relationship of the partners and between the partners and the partnership."); *see, e.g.*, ALAN R. BROMBERG & LARRY E. RIBSTEIN, BROMBERG & RIBSTEIN ON PARTNERSHIP § 7.02(c)(3) (2010).

6. *See* Bendalin v. Youngblood & Assocs., 381 S.W.3d 719, 740 (Tex. App. 2012); *Monteleone*, 497 N.E.2d at 1225; *see also* Jordon v. Bowman Apple Prods. Co., 728 F. Supp. 409, 416 (W.D. Va. 1990); Chandler Med. Bldg. Partners v. Chandler Dental Grp., 855 P.2d 787, 793–94 (Ariz. Ct. App. 1993); Page v. Page, 359 P.2d 41, 42–44 (Cal. 1961); Fischer v. Fischer, 197 S.W.3d 98, 104–05 (Ky. 2006); Miami Subs Corp. v. Murray Family Trust, 703 A.2d 1366, 1370–71 (N.H. 1997); Girard Bank v. Haley, 332 A.2d 443, 447 (Pa. 1975); Canter's Pharmacy, Inc. v. Elizabeth Assocs., 578 A.2d 1326, 1329–30 (Pa. Super. Ct. 1990).

7. *Monteleone*, 497 N.E.2d at 1225.

8. *Id.* at 1223.

9. In a partnership, "[e]ach partner has equal rights in the management and conduct of the business." TEX. BUS. ORGS. CODE ANN. § 152.203(a) (2013). "A difference arising in a matter in the ordinary course of the partnership business may be decided by a majority-in-interest of the partners." *Id.* § 152.209(a). Under the Revised Uniform Partnership Act, such a "difference . . . may be decided by a majority of the partners." R.U.P.A § 401(j) (1997). In this case, as in most informal partnerships, the difference between the TBOC and RUPA does not matter, because the partners have agreed to split profits equally. An equal split of profits is also the default rule under the TBOC. *See* TEX. BUS. ORGS. CODE ANN. § 152.202(c) (2013). An equal split of profits among the partners renders application of "majority-in-interest" and the per capita rule of RUPA identical. *See id.* § 151.001(4) (specifying that "majority-in-interest" is determined by stake in profits, absent agreement otherwise). If the default rule for profits is equality, then each partner has an interest equal to their per capita standing.

10. *Monteleone*, 497 N.E.2d at 1223.

11. *Id.*

12. *Id.*

business, and damages.[13] Nick and Lorenzo counterclaimed, of course.[14] Jerry was the wrongdoer, they asserted; Jerry's claim must have seemed like sheer chutzpah.

B. *The Law: An Introduction*

Nevertheless, a certain view of the law suggests that Jerry was right. The common law does not provide partners a right to expel one of their own.[15] For statutory authority in this Article, I intend to reference the Texas General Partnership Law,[16] a statute largely inspired by the Revised Uniform Partnership Act.[17] I prefer to work with the law of a certain place, as opposed to a uniform code. Texas is a large state, and this statute governs many informal partnerships. Moreover, Texas courts have dealt with the self-help fact pattern numerous times, and, if Texas' helpful case law is to remain relevant, the statutes currently in force there should remain supportive. The Texas General Partnership Law, just like the various versions of the Uniform Part-

13. *Id.*

14. *Id.*

15. *See, e.g.*, Ehrlich v. Howe, 848 F. Supp. 482, 490 (S.D.N.Y. 1994) (applying New York law); Cadwalader, Wickersham & Taft v. Beasley, 728 So. 2d 253, 256 (Fla. Dist. Ct. App. 1998); Dawson v. White & Case, 672 N.E.2d 589, 592 (N.Y. 1996); Dillard v. Wholesale, 286 S.W.2d 675, 677 (Tex. App. 1956) ("at law a partner may not expel another partner"); *see also, e.g.*, Rowley v. Fuhrman, 982 P.2d 940, 944 (Idaho 1999) (joint venture); Allan W. Vestal, *Law Partner Expulsions*, 55 WASH. & LEE L. REV. 1083, 1111, 1110 n.205 (1998) (listing numerous authorities). In *Gregan v. Kelly*, 355 S.W.3d 223 (Tex. App. 2011), the court extolled at length that partnerships were at will, citing *Bohatch v. Butler & Binion*, 977 S.W.2d 543 (Tex. 1998). But *Bohatch* merely meant that no ground for expulsion is required when the partnership agreement already provides for expulsion. *Bohatch*, 977 S.W.2d at 545–47. The partnership agreement in *Bohatch* "contemplate[d] expulsion of a partner and prescribe[d] procedures to be followed." *Id.* at 546. The agreement clearly provided a right to expel. *Gregan* was also a suit alleging breach of a partnership agreement and partnership fiduciary duties. 355 S.W.2d at 227, 230–31. Whether the plaintiff there was a partner or merely an employee was not clearly settled in the trial court, and the plaintiff failed to cause the issue to be submitted to the jury, which merely held that the relationship was at will. *Id.* at 231. In rejecting the plaintiff's claims of fiduciary duty breach, the court purported to analyze both at-will employment and at-will partnership law. *Id.* at 230–31. If a partnership's at-will status equated to employment at will, then it might be possible to expel a partner without anything about expulsion mentioned in the partnership agreement. In affirming as a matter of partnership law the plaintiff's dismissal from a law partnership whose partnership agreement lacked an expulsion provision, the *Gregan* court appears to suggest that no expulsion agreement is necessary. *Id.* But *Bohatch* held no such thing, and in this *Gregan* is contrary to *Dillard* and perhaps section 152.501 of the TBOC.

16. TEX. BUS. ORGS. CODE ANN. § 1.008(f) (2013) authorizes this designation to Chapters 151, 152, and 154 of the TBOC.

17. 19 ELIZABETH S. MILLER & ROBERT A. RAGAZZO, TEXAS PRACTICE SERIES, BUSINESS ORGANIZATIONS § 6:1 (3d ed. 2011); *compare* TEX. BUS. ORGS. CODE ANN. § 152.501 *with* R.U.P.A. § 601 (1997). While Texas uses the word "withdraw" where the RUPA employs "dissociate," the concepts operate similarly, the statutes employ a similar logic, and the substantive grounds for either are in all cases relevant to this article more or less identical.

nership Act, provides the means for partners to part ways.[18] Read somewhat narrowly, the statute appears to favor Jerry.

This might seem odd. If Jerry is harming the business, locking Jerry out of the premises appears necessary to protect the business. The law should favor preservation and enhancement of productive enterprise—in this case, a profitable body shop. If locking out a destructive partner is the only way to prevent harm to the business, and the other partners are the only ones capable of doing so (or perhaps the only ones able to do so in the required time frame), then the law should support them.

While some courts, including the *Monteleone* court,[19] have granted protection to self-helpers such as Nick and Lorenzo,[20] these scenarios are more complex than they first appear. Self-help's complexity arises in informal partnerships in part because the parties themselves do not bother to fit their actions intentionally into available legal categories. The self-help problem is similar to the issue of whether a partnership formed by default. Cases addressing whether a partnership formed on facts showing no formal partnership creation are legion.[21] A partnership can form even when the parties intended their relationship to be something else.[22] In these cases, courts sort out hard-to-categorize

18. TEX. BUS. ORGS. CODE ANN. § 152.501(b) (2013).

19. Monteleone v. Monteleone, 497 N.E.2d 1221, 1223 (Ill. App. Ct. 1986).

20. *See* Ohlendorf v. Feinstein, 636 S.W.2d 687, 689 (Mo. Ct. App. 1982) ("There is no doubt that Ohlendorf wrongfully breached the partnership agreement causing a dissolution of the partnership."); Schnitzer v. Josephthal, 202 N.Y.S. 77 (N.Y. Sup. Ct. 1923); M.R. Champion, Inc. v. Mizell, 904 S.W.2d 617 (Tex. 1995) (per curiam); *see also* Stiles v. Bradley, 117 N.Y.S. 637 (N.Y. App. Div. 1909) (holding, pre-UPA, that a law partner who was to devote all time to the practice breached the agreement by becoming a justice of the peace, thereby making himself too busy to fulfill his partnership obligations and justifying his partner in declaring their partnership for a term to be at an otherwise premature end); Drashner v. Sorensen, 63 N.W.2d 255, 252–53 (S.D. 1954) ("[T]he insistent and continuing demands of the plaintiff . . . rendered it reasonably impracticable to carry on the business in partnership with him. . . . [T]he evidence supports the finding that plaintiff caused the dissolution wrongfully."). Some commentators have also supported this approach. *See* J. WILLIAM CALLISON & MAUREEN A. SULLIVAN, PARTNERSHIP LAW AND PRACTICE: GENERAL AND LIMITED PARTNERSHIPS § 16:14 (2013) ("[T]he better approach permits courts to exercise their equitable powers and hold that partner misconduct which gives rise to a dissolution decree also permits application of UPA § 38(2) sanctions" available only when a partner wrongfully causes dissolution.).

21. *See, e.g.*, BROMBERG & RIESTEIN, *supra* note 5, §§ 2.05–2.09, 2.14 (indeed, most of chapter 2); MILLER & RAGAZZO, *supra* note 17, §§ 6:6–6:8.

22. *E.g.*, Vohland v. Sweet, 433 N.E.2d 860 (Ind. Ct. App. 1982) (affirming a finding as a partnership what both parties appeared to treat as employment with commissions); Lupien v. Malsbenden, 477 A.2d 746 (Me. 1984) (affirming a finding of a partnership when both parties apparently believed that their relationship was a creditor-borrower relationship). Conversely, a partnership does not result merely because people refer to each other as partners. *See, e.g.*, Beecher v. Bush, 7 N.W. 785, 785 (Mich. 1881) ("If they agree upon an arrangement which is a partnership in fact, it is of no importance that they call it something else, or that they even

facts that the parties did not plan in advance with partnership law in mind. In both kinds of cases—partnership beginnings and partnership endings—later analysis must fit the facts into available legal categories. There is not always a close fit, and the potential for inconsistency across several such cases is greater because the parties' conduct may be characterized in several ways. This is a common problem in partnership law.[23]

The Texas General Partnership Law offers a cafeteria of categories under which lawyers may argue informal partnership self-help facts. These categories fit within a broader structure of partnership termination rules. "A partnership is an entity distinct from its partners."[24] So, though a partner may leave the partnership—an event known as "withdrawal"[25]—"[a] partnership continues after an event of withdrawal."[26] The continuing partnership may continue its business, notwithstanding a withdrawal, unless "an event requiring a winding up" occurs.[27] "Winding up" is liquidation of the partnership's business and termination of the partnership.[28] "In winding up the partnership business, the property of the partnership . . . shall be applied to discharge its obligations to creditors," and "surplus shall be applied to pay in cash the net amount distributable to partners . . . ."[29] Events requiring a wind-up are specifically defined; however, a mere withdrawal is not one of them.[30]

In the self-help cases we are considering, the partners have parted ways. The association of Nick, Lorenzo, and Jerry, for business purposes, is no more. Perhaps a withdrawal occurred at some point in this fact scenario. Withdrawal under the code purports to be a technical, defined term.[31] While it includes actions Jerry might take—expressing his will to withdraw and filing bankruptcy[32]—it also includes

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expressly declare that they are not to be partners. The law must declare what is the legal import of their agreements, and names go for nothing when the substance of the arrangement shows them to be inapplicable."); City of Corpus Christi v. Bayfront Assocs., 814 S.W.2d 98, 109 n.4 (Tex. App. 1991) ("[A] duck which is called a horse does not become a horse; a duck is a duck.").

23. *See, e.g.*, ROBERT W. HILLMAN, DONALD J. WEIDNER & ALLAN G. DONN, THE REVISED UNIFORM PARTNERSHIP ACT 403–05 (2013-2014 ed. 2013) (noting a variety of ways in which partners may express, by words or by actions, a will to withdraw, and the variety of ways in which courts can, and have, responded).

24. TEX. BUS. ORGS. CODE ANN. § 152.056 (2013).

25. *See id.* § 152.501.

26. *Id.* § 152.502.

27. *Id.* § 152.701.

28. *Id.* §§ 152.701, 152.706.

29. TEX. BUS. ORGS. CODE ANN. § 152.706(a)–(b).

30. *See id.* §§ 11.051, 11.057.

31. *Id.* § 152.501(b).

32. *Id.* § 152.501(b)(1), 152.501(b)(6)(A).

actions others might take with respect to Jerry: his "expulsion as provided by the partnership agreement,"[33] his "expulsion by judicial decree" for wrongful conduct,[34] someone else's filing an involuntary bankruptcy against Jerry,[35] or Jerry's death.[36] It may also occur by operation of law.[37]

When informal partners engage in self-help, it is often not clear whether withdrawal occurred, or, if it did, what kind of withdrawal occurred. In fact, courts have handled self-help cases in just about every way imaginable. Perhaps no withdrawal occurred—none was intended.[38] Cases so concluding are discussed in Part II.A.1. But why didn't the conduct of the excluding partners (Nick and Lorenzo) express their will to disassociate or withdraw? It is hard to argue that Nick and Lorenzo meant to continue with Jerry in the association we call partnership. Part II.A.2 discusses cases ruling that the excluding conduct withdrew *the excluding partners*, not the excluded one.

Still other cases suggest that the excluding conduct is an expulsion. If the partnership agreement did not provide for expulsion, then this expulsion is a breach of the partnership agreement. Cases so concluding—and awarding damages for the breach—are discussed in Part II.A.3. Finally, some cases focus on the conduct of the excluded partner—on Jerry's conduct. Noting the wrongfulness of the conduct, these courts conclude that Jerry's conduct itself causes a withdrawal. These cases are discussed in Part II.B. Less directly supported by statutory language, these cases are best rationalized as grounded in contract.

Such variety! What to do? Analyzing these cases closely, I reach two conclusions. First, all of these cases are based on reasonable readings of the partnership code. This is not obvious, particularly in the cases focusing on the conduct of the excluded partner. However, as discussed in Part II, the code is flexible enough to support each result.

Second, the reason the cases reach different results is that, notwithstanding the strong similarities between the cases, they ultimately have different facts. Most importantly, their partnership agreements, and the kind of breach that occurred, differ. Of course, in an informal partnership, the explicit partnership agreement is minimal. The agreements in these cases are largely inferred by the courts based on

33. *Id.* § 152.501(b)(3).
34. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(5).
35. *Id.* § 152.501(b)(6)(A).
36. *Id.* § 152.501(b)(7)(A).
37. *Id.* § 152.501(b)(2).
38. *See infra*, Part II.A.1.

the partnership's business and the way the partners have acted in the past. These are intensely factual decisions, and they depend, to some extent, on assumptions that businesspeople, lawyers, and judges bring to the situation. But, in the end, the facts differ.

Because the variety of decisions in this area largely reflects factual differences, this Article concludes that there is no need to reform the code. These cases call not for reform, but merely for rationalization.[39] Part III concludes by summarizing the available options and suggesting, roughly, when courts should select each.

II. LEGAL RESPONSES TO SELF-HELP

A. *Code Options*

1. No Withdrawal

Perhaps the consequence of self-help behavior is that nothing happens: it has no legal effect. This seems counter-intuitive. Self-help activity seems always to break the "association of two or more persons to carry on a business for profit as owners."[40] This is the current language of the partnership code that, at one time, was thought to define the concept of partnership.[41] The current code also calls a partnership an entity distinct from its partners, however.[42] Is it possible that conduct breaking the partnership association could also leave the partnership intact?

Read narrowly, the code's provisions describing withdrawal—primarily section 152.501(b)[43]—include only conduct well within the meaning of the language of that section.[44] "'Event of withdrawal' or 'withdrawal' means an event specified by Section 152.501(b)."[45] The use of the word "means" suggests that the code wants 501(b) to exhaust the code's possibilities for withdrawal.[46] What that actually en-

39. Forty years ago, Robert W. Hillman briefly addressed self-help in partnership break-ups in a longer article on partnership misconduct as a ground for expulsion. Robert W. Hillman, *Misconduct as a Basis for Excluding or Expelling a Partner: Effecting Commercial Divorce and Securing Custody of the Business*, 78 Nw U. L. REV. 527, 539–44 (1983). On the basis of only a few cases and brief policy analysis but with keen insight into the Uniform Partnership Act, Hillman presciently announced: "The issue is best resolved by focusing on the objectives of the dissolving partners and permitting a limited use of self-help." *Id.* at 543. Analyzing in detail the terms of a later partnership code, surveying the policy landscape, and, with the help of several cases that have now addressed the issue, I reach the same conclusion.

40. TEX. BUS. ORGS. CODE ANN. § 152.051(b).

41. *See, e.g.*, U.P.A. § 6 (1914).

42. TEX. BUS. ORGS. CODE ANN. § 152.056.

43. *Id.* § 152.501(b).

44. *Id.* § 152.501(b) ("An event of withdrawal of a partner occurs on: . . .").

45. *Id.* § 152.001(1).

46. *Id.*

tails for partnership law is not as clear, as discussed in Part II.B.2.[47] However, a court thinking narrowly within the language of the code, and not prompted by the facts of a case to take a second look, may well stop with what the code makes most obvious.

The legal result may be that, unless the conduct of the self-helpers seems to fall within the language of 501(b), it has no effect at all. An example might be *Deere v. Ingram*.[48] Deere was a medical doctor and Ingram a psychologist.[49] The two agreed orally to work together in a new pain clinic.[50] Ingram could not operate the clinic without a medical doctor.[51] The two agreed to split revenues and, on that basis, worked together for over a year.[52] Then, Ingram prepared a written agreement in which he claimed that he owned the clinic and that Deere was a mere employee.[53] Deere in response "left the premises . . . and never returned."[54] Deere appears to have seen Ingram's actions as a breach,[55] and his self-help solution was to walk away.[56] However, there was also evidence that Ingram told Deere to go,[57] also a form of self-help.

The break-up in *Deere v. Ingram* looks suspiciously like voluntary withdrawal. The nearest code language indicates that withdrawal occurs on "receipt by the partnership of notice of the partner's express will to withdraw as a partner."[58] The code retains the suggestion that a partnership is formed by "an association of two or more persons to carry on a business for profit as owners."[59] When a person walks out and never returns, especially if such action is done in response to an

47. *See infra* Part II.B.2.

48. Deere v. Ingram, 198 S.W.3d 96 (Tex. App. 2006), *rev'd on other grounds*, 288 S.W.3d 886 (Tex. 2009).

49. *Id.* at 99.

50. *Id.*

51. *Id.*

52. *Id.*

53. *Deere*, 198 S.W.3d at 99.

54. *Id.* at 101.

55. *See* Appellants' Brief, *Deere*, 198 S.W.3d 95 (No. 05-05-00063-CV), 2005 WL 1658591 at *4–5.

56. Deere's brief shows a more understandable statement of facts: Ingram's personal finances were poor; he kept asking for a larger share of the revenue and finally asked Deere to sign an agreement stating Deere was Ingram's employee; Deere refused to sign, and Ingram said it appeared they could not get along and handed Deere a check for what Ingram supposedly thought was Deere's balance; and the next week when Deere was to come see a patient, Ingram called and "told him not to come because he had hired a new physician." *Id.* These facts come from the record. If they are correct, the understanding that Deere did not express the will to withdraw is more understandable and supportive of the jury's verdict for Deere.

57. *Id.*

58. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(1) (2013).

59. *Id.* § 152.051(b).

associate's order, has their association not ended? Is the person who left still carrying on a business? For profit? Do we require an affirmative statement? Does substance count for nothing?

Deere sued Ingram three years later, and a jury awarded him revenues from the business for the period after he walked out.[60] That holding is possible only if Deere's leaving was not a withdrawal.[61]

The court held that it was not: "This evidence alone does not affirmatively establish that Deere abandoned the partnership."[62] The court cited what it believed was evidence that Deere had not abandoned the partnership, but that evidence was extraordinarily slight. The court noted that "Deere testified [in court] that he had no desire to withdraw from the partnership and that he did not abandon the partnership."[63] Also, the court explained that "Deere never stated that he was backing out on their oral agreement."[64] This is all the court said. So, as reasoned by this opinion, you can leave the business and never return, but if you later sue and testify that you had no desire to withdraw, you are still a partner.[65]

Faced with Jerry's disloyal acts and wanting to preserve the business, Nick and Lorenzo changed the locks. It is possible that a court, as in *Deere*, would conclude that this was not an event of withdrawal as defined in the statute. After all, Jerry never expressed a will to withdraw. In fact, Jerry still wanted the partnership business.[66] He even wanted his son to participate in it.[67] Under *Deere*, Jerry did not withdraw. Nick and Lorenzo could also say in court that they had no desire to withdraw and did not abandon the partnership; on the contrary, they were protecting it. They never stated that they were backing out of their oral agreement. Instead, by protecting the business, they were acting to shore up the oral agreement.

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60. Deere v. Ingram, 198 S.W.3d 96, 99 (Tex. App. 2006).

61. Deere would have had no interest in the revenues, otherwise. Instead, he would have had an interest in the business as of the day he withdrew, which would need to be redeemed. At the time *Deere* took place, that right was set forth in Texas Revised Partnership Act Art. 6132b-7.01 (1999); now it appears in TEX. BUS. ORGS. CODE ANN. § 152.601 (2013). In the case of the pain clinic, it is likely that the goodwill of the alleged partnership in *Deere* would not have belonged to Deere for long after the break-up. *See* Salinas v. Rafati, 948 S.W.2d 286 (Tex. 1997) (holding that earning capacity of professionals is nearly always personal to them and therefore not a partnership asset). Deere himself claimed that the clinic was successful partly on the basis of his own reputation, while he was there. Appellants' Brief, *supra* note 55, at *4.

62. *Deere*, 198 S.W.3d at 101.

63. *Id.*

64. *Id.*

65. See a similar holding in *In re Woskob*, 305 F.3d 177, 182–84 (3d Cir. 2002).

66. Monteleone v. Monteleone, 497 N.E.2d 1221, 1223 (Ill. App. Ct. 1986).

67. *Id.*

One could argue that a more closely relevant subsection of the statute might be the general expulsion provision, which holds that a withdrawal occurs on "the partner's expulsion as provided by the partnership agreement."[68] Were Nick and Lorenzo's actions not an expulsion? The *Deere* court dealt with this possibility, too. Ingram claimed to have expelled Deere,[69] and Deere's brief to the court reported that Ingram had told Deere not to come to the office anymore.[70] But this was not enough for the court: "The statute reads: 'the partner's expulsion *as provided in the partnership agreement.*' There is no evidence in the record that the parties orally or in writing agreed that a specified event would lead to a partner's expulsion. Accordingly, Ingram's reliance on this event of withdrawal is misplaced."[71] If we read the statute to require a kind of formal act of agreement, as this passage seems to require, then Nick and Lorenzo's act of locking Jerry out is not a withdrawal by expulsion. Nick, Lorenzo, and Jerry had no more formality in their partnership agreement than did Ingram and Deere. If the court is looking for a specific provision, it will not find one. So Jerry would remain a partner.

If *Deere* were the sum of the law, what should Nick and Lorenzo do? Jerry is causing problems. They do not want to withdraw from the partnership because they want to continue running the business. Jerry is not about to withdraw; he, too, wants the business.[72] So what options would Nick and Lorenzo have?

Their options are limited. They should consult a lawyer instead of changing the locks. The Texas General Partnership Law purports to offer a way to preserve the business. The following withdrawal provision seems to be the only one helpful:

> (b) An event of withdrawal of a partner occurs on: . . . (5) the partner's expulsion by judicial decree, on application by the partnership or another partner, if the judicial decree determines that the partner:
>
> (A) engaged in wrongful conduct that adversely and materially affected the partnership business;
>
> (B) wilfully [sic] or persistently committed a material breach of: (i) the partnership agreement; or (ii) a duty owed to the partnership or the other partners under Sections 152.204–152.206; or

68. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(3) (2013).

69. *Deere*, 198 S.W.3d at 101.

70. *See* Appellants' Brief, *supra* note 55.

71. *Deere*, 198 S.W.3d at 101–02 (quoting Tex. Rev. Civ. Stat. Ann. art. 6132b-6.01(b)(3) (Vernon Supp. 2005) (citations omitted).

72. *See Monteleone*, 497 N.E.2d at 1223 ("Jerry filed a motion requesting that the court order a judicial sale of partnership assets prior to the court's decision on the issues of the parties' interests in the business . . . .").

> (C) engaged in conduct relating to the partnership that made it not reasonably practicable to carry on the business in partnership with that partner[.][73]

This section was obviously placed in the code to deal with a partner such as Jerry. A partner who misappropriates partnership funds, hides and refuses to return books and records, and does not abide by management decisions of the partnership engages in wrongful conduct that materially affects the partnership business. Such conduct is a breach of the partner's duties under sections 152.204–152.206, which describe the duty of loyalty.[74] Even refusal to abide by management decisions may be disloyal.[75] And carrying on a business in partnership with one who engages in such conduct may not be reasonable.[76]

No method exists to calculate with certainty how long it will take to obtain a decree of expulsion, but Nick and Lorenzo's counsel should seek an immediate temporary restraining order and a temporary injunction. Depending on how long it takes their lawyer to draft a complaint, they could have a ruling on a temporary restraining order a day or so after they contact their lawyer. In the meantime, they can remain at the partnership premises to watch what Jerry does there, if anything, or they can hire someone to do so. If Jerry tries to enter, however, it would be difficult to stop him. He is still a partner. As a partner, Jerry is a manager of the business and has a right to enter.[77] Once the injunction is in place and Jerry is notified, the concern for the business would likely abate.

2. Withdrawal

Most courts do not read the code so narrowly, and many cases present facts that speak more strongly. Most courts do not require an

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73. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(5).

74. *See id.* §§ 152.204 –.206. Refusal to return books also violates other duties to the partnership and the other partners. *See id.* § 152.212.

75. Though all partners, as owners, have residual management authority, *id.* § 152.303(a), differences among the partners on management issues "may be decided by a majority-in-interest of the partners" or in some other manner specified by the partnership agreement. *Id.* § 152.209(a); *see id.* § 152.002(a). Loyalty, at a minimum, requires that the partners not act adversely to the interests of the partnership. *See id.* § 152.205(2)–(3). Once the partnership's interests are determined by its management authority, acting contrary to management's decision appears to be acting adversely to the partnership. In a partnership of three or more, the code's default rules generally determine who is the partnership's ultimate managing authority. In a partnership of two, this is far more difficult. *See, e.g.*, Covalt v. High, 675 P.2d 999 (N.M. Ct. App. 1983) (suggesting that equal partners remain independent managers with power to set partnership management goals, despite disagreement); Nat'l Biscuit Co. v. Stroud, 106 S.E.2d 692 (N.C. 1959) (same).

76. *See, e.g.*, Brennan v. Lehn, 2006 WL 2949111, at *12–14 (Conn. Super. Ct. 2006).

77. *See, e.g.*, TEX. BUS. ORGS. CODE ANN. § 152.203(a)–(b) (2013).

express statement of withdrawal; rather, conduct may give notice of express will to withdraw. These courts are likely to find that Nick and Lorenzo's actions had a legal effect. Such a court might hold that Nick and Lorenzo had themselves withdrawn.

"An event of withdrawal of a partner occurs on . . . receipt by the partnership of notice of the partner's express will to withdraw as a partner . . . ."[78] Did this happen to Nick and Lorenzo? The first act by a partner expressing what looks like a will to withdraw was Nick and Lorenzo's exclusion of Jerry from the shop. Did this give Jerry notice of Nick and Lorenzo's express will to withdraw from the partnership? A partnership is created by "an association of two or more persons to carry on a business for profit as owners."[79] When Nick and Lorenzo made clear that they no longer intended to associate with Jerry in this business as co-owners, by excluding Jerry from the premises, they appeared to withdraw.[80]

In *Rhue v. Dawson*,[81] Rhue and Dawson agreed to be partners in the development, operation, and sale of a shopping center.[82] The partnership agreement was oral at first,[83] but Dawson produced a written agreement a few days later.[84] Rhue did not read the document but instead asked Dawson questions about it, which Dawson answered; Rhue then signed.[85] Dawson had slipped in an onerous term, however. When Rhue discovered the term two months later, he sent Dawson a letter claiming he would not be bound by it.[86] Dawson responded by locking Rhue out of partnership offices. The court called this an "ouster,"[87] a non-statutory term. But the court was clear on the effect: Dawson had "dissolved" the partnership, the rough

78. Id. § 152.501(b)(1).

79. *Id.* § 152.051(b). The provision says such an association "creates a partnership," a phrase that does not exclude a partnership being created in some other way. *Id.* Because the phrase is no longer considered by the code to be definitional, the removal of a partner no longer results in the partnership ceasing, or dissolving, as the UPA put it. Rather, the partnership, which "is an entity distinct from its partners," *id.* § 152.056, continues with a slightly different set of partners. *See, e.g.*, Robert W. Hillman, *RUPA and Former Partners: Cutting the Gordian Knot with Continuing Partnership Entities*, 58 LAW & CONTEMP. PROBS. 7 (1995). Moreover, the partnership as an entity might possibly continue when one of two partners withdraws. *See infra* note 93–94 and accompanying text.

80. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 5, § 7.02(c)(4) & n.39 ("by ejecting a partner and carrying on the business separately").

81. Rhue v. Dawson, 841 P.2d 215 (Ariz. Ct. App. 1992).

82. *Id.* at 218, 222–23.

83. *Id.* at 222.

84. *Id.* at 219.

85. *Id.*

86. *Rhue*, 841 P.2d at 219.

87. *Id.* at 222 n.10 & 223.

equivalent under the Uniform Partnership Act (UPA) of an event of withdrawal—withdrawal by Dawson, that is. Nick and Lorenzo appear to have "ousted" Jerry in a similar manner. At the very least, they manifested their will no longer to associate with Jerry in the business.[88]

The consequence of Nick and Lorenzo's withdrawal by express will from an at-will partnership may be that the partnership continues. This counter-intuitive result flows from the rule that "[a] partnership is an entity distinct from its partners"[89] and the related rule that "[a] partnership continues after an event of withdrawal."[90] No event requiring a wind-up under the statute has occurred.[91] Whether a partnership continues when only one partner is left is the subject of some dispute,[92] and it also seems plausible that a court would rely on the traditional definition of partnership ("an association of two or more") to say that the partnership ended.[93]

Either way, Nick and Lorenzo did not want to be held as having withdrawn. If the partnership as an entity continues after Nick and Lorenzo withdraw, then it is in the hands of Jerry, who is the sole

88. For similar cases, see *Infusaid Corp. v. Intermedics Infusaid, Inc.*, 739 F.2d 661 (1st Cir. 1984); *Schoenborn v. Schoenborn*, 402 N.W.2d 212, 214 (Minn. Ct. App. 1987) (reporting the trial court's decision). In *Dawson v. White & Case*, 672 N.E.2d 589 (N.Y. 1996), the partners in a law partnership, on discovering their partnership agreement lacked an expulsion term, intentionally withdrew from the firm (called a "dissolution" under the applicable partnership law). *Id.* at 592. That was the only way they could think of to rid themselves of the partner with whom they no longer wished to associate.

89. TEX. BUS. ORGS. CODE ANN. § 152.056 (2013).

90. *Id.* § 152.202.

91. *See id.* §§ 11.051, 11.057, 152.701.

92. *See* Robert W. Hillman & Donald J. Weidner, *Partners Without Partners: The Legal Status of Single Person Partnerships*, 17 FORDHAM J. CORP. & FIN. L. 449 (2012) (arguing both sides). In *In re Leal*, 360 B.R. 231 (Bankr. S.D. Tex. 2007) (Texas law), a bankruptcy judge opined that, "[b]ecause a partnership requires two or more partners, [one partner's] letter expressing his will to withdraw from the partnership was effectively a request for a winding up of the partnership." *Id.* at 240. Moreover, the court said that winding up was required because the remaining partner did not have a majority-in-interest. *Id.* at 240 n.7.

93. TEX. BUS. ORGS. CODE ANN. § 152.051 (entitled "Partnership Defined" and asserting that "an association of two or more persons to carry on a business for profit as owners creates a partnership"). Note that the actual language of the statute says "creates," which conflicts with the section's heading, which says "defined." *Id.* The language of the section preserves partnership as a residual category but does not purport to limit the concept. Hillman cites numerous unreported California cases in support of the idea that the partnership dissolves. *See* Hillman & Weidner, *supra* note 92, at 455 n.12. However, California has a real definition of partnership, *see* CAL. CORP. CODE § 16101(9) (West 2012). Hillman also cites an Idaho case, but the Idaho case concludes that the joint venture at issue dissolved; the court reasoned that the joint venture was not a partnership, which would have been governed by Idaho's partnership code, which, like Texas's, is modeled on the Revised Uniform Partnership Act and declares a partnership an entity. Hillman & Weidner, *supra* note 92, at 453 n.12 (citing Costa v. Borges, 179 P.3d 316, 319–20 (Idaho 2008)).

remaining partner. Nick and Lorenzo sought to exclude Jerry for the sake of the business. Leaving Jerry the business would accomplish the opposite of their goal. Imposing that legal result on their conduct would be contrary to their understanding and intent.

If the partnership terminates when Nick and Lorenzo withdraw, leaving only one partner, then perhaps the partnership must wind-up. In fact, partners in the position of Nick and Lorenzo could cause that to happen regardless of whether a partnership continues as an entity separate from its partners. Often, a partner expressing the will to withdraw will request a winding up, and in that case,

> an event requiring winding up of the partnership . . . occurs on the 60th day after the date on which the partnership receives notice of a request for winding up the partnership from a partner, . . . unless a majority-in-interest of the partners deny the request for winding up or agree to continue the partnership.[94]

Nick, Lorenzo, and Jerry were by default equal partners, so Nick and Lorenzo could have required Jerry to wind up. They, not Jerry, are the majority-in-interest.[95] Jerry would have no power to stop the winding up.

But Nick and Lorenzo did not want a winding up. They wanted the business to continue, and they wanted to run it. Several unfortunate consequences would occur if locking Jerry out were held to constitute Nick and Lorenzo's express withdrawal. First, as noted, because Nick and Lorenzo would no longer be partners, Jerry would be the sole remaining partner; therefore, Jerry would be in control of the business for the moment.[96] Even if the partnership will be wound up, "[a] partnership continues after an event of withdrawal"[97] "until the winding up of its business is completed, at which time the partnership is terminated."[98] "After the occurrence of an event requiring a winding up . . . , the partnership business may be wound up by . . . the partners who have not withdrawn . . . ."[99] During this time, Jerry, the remaining partner, would be in control of the business and its assets.

Second, because withdrawing from the business would put Jerry in control, locking Jerry out would constitute conversion of the partner-

94. TEX. BUS. ORGS. CODE ANN. § 11.057(d).

95. Majority-in-interest "means partners who own more than 50 percent of the current percentage or other interest in the profits of the partnership." *Id.* § 151.001(4). Because Nick, Lorenzo, and Jerry had agreed to split profits equally, *Monteleone v. Monteleone*, 497 N.E.2d 1221, 1225 (Ill. App. Ct. 1986), any two were a majority-in-interest. *See* TEX. BUS. ORGS. CODE ANN. § 152.002(a).

96. *E.g.*, TEX. BUS. ORGS. CODE ANN. § 152.704.

97. *Id.* § 152.502.

98. *Id.* § 152.701(a).

99. *Id.* § 152.702(a)(1).

ship assets. In *In re Leal*,[100] Leal, one of two partners in an auto glass business, gave express notice of withdrawal from the general partnership.[101] Leal later obtained a judgment against his partner for prior conversion of partnership assets.[102] Leal's partner had been disloyal,[103] similarly to how Nick and Lorenzo alleged that Jerry was disloyal. After expressly withdrawing, Leal changed the locks on the doors.[104] Perhaps Leal was afraid that his partner would convert more partnership property. Nevertheless, the court held that "Leal's conduct was clearly wrongful. Once he withdrew from the partnership, Leal did not have any right to control" its business.[105] The court held Leal liable for conversion of partnership assets and for disloyalty as a former agent of the partnership with lingering fiduciary duties.[106] A court could hold that Nick and Lorenzo stand in the same position as Leal.

Finally, if Nick and Lorenzo were held to have expressly withdrawn, then at a wind-up, when partnership assets are sold,[107] they would have to bid against Jerry for the business. They might lose the bidding. If the winding-up process and resulting litigation cause unbearable expense, the business might even be liquidated to pay creditors. Nick and Lorenzo believed that, because they had done nothing wrong but only acted to protect the business, they should be able to continue and should not have to buy the business from Jerry. Obviously, a finding that Nick and Lorenzo had withdrawn is not an optimal solution for them, and it is certainly not what they understood would happen; it was not their intent. But it is an option for a court on the facts of some self-help cases.

3. Expulsion

Obviously, Nick and Lorenzo were not trying to withdraw. They were more likely trying to expel Jerry in order to protect the partnership. Why not argue that locking Jerry out was his expulsion from the partnership? The Texas Supreme Court, in *Bohatch v. Butler & Bin-*

100. *In re Leal*, 360 B.R. 231 (Bankr. S.D. Tex. 2007). *In re Leal* was decided under the prior partnership law, but the substance of the provisions has not changed with regard to the issues discussed here. *Id.* at 235 n.1.

101. *Id.* at 240.

102. *Id.* at 237.

103. *Id.*

104. *In re Leal*, 360 B.R. at 240.

105. *Id.*

106. *Id.* at 240–41.

107. TEX. BUS. ORGS. CODE ANN. §§ 11.052, 152.703(a).

ion,[108] famously claimed that partners at will "have no duty to remain partners."[109] "A partnership exists solely because the partners choose to place personal confidence and trust in one another."[110] If that trust is broken, the partnership is unlikely to remain a partnership.

It is possible to see Nick and Lorenzo's actions as an expulsion. "An event of withdrawal of a partner occurs on . . . the partner's expulsion as provided by the partnership agreement[.]"[111] The code clearly considers an expulsion possible. While the *Rhue* decision opted not to find an expulsion in favor of the non-statutory "ouster" (constituting withdrawal by express will of the ousting party),[112] other courts have found expulsion in self-help scenarios.

The clause in the code, however, contains the proviso "as provided by the partnership agreement." In *Bohatch*, the partnership agreement "contemplate[d] expulsion of a partner and prescribe[d] procedures."[113] But if the partnership agreement has no provision for expulsion, then expulsion is a breach of the expelled partner's rights. All the partners are, in a sense, "owners" of the partnership.[114] Each is also a manager.[115] Each has a right to "use or possess partnership property" for partnership purposes.[116] One can easily understand why, without a provision in the partnership agreement, locking a partner out would violate the partner's rights.

In *Young v. Qualls*,[117] Young financed a real estate development in which Young and Qualls agreed to be partners.[118] Young bought the property in the name of an LLC he owned.[119] Qualls was to supervise the clearing and development of the property and sell lots.[120] The two agreed to split profits after expenses were repaid with interest.[121] No

108. Bohatch v. Butler & Binion, 977 S.W.2d 543 (Tex. 1998).

109. *Id.* at 544.

110. *Id.* at 546.

111. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(3).

112. Rhue v. Dawson, 841 P.2d 215, 222 n.10 (Ariz. Ct. App. 1992) ("Rhue was ousted rather than expelled from the partnership. Expulsion of a partner can occur only if the partnership agreement provides for such expulsion and the expulsion occurs according to the provisions of the agreement. A.R.S. § 29-231(A)(4). In locking Rhue out of the partnership offices, Dawson was not acting in accordance with the provisions of any agreement between Rhue and Dawson. The partnership was, by that act, dissolved, and Rhue was ousted from the partnership.").

113. *Bohatch*, 977 S.W.2d at 550 (Hecht, J, concurring).

114. TEX. BUS. ORGS. CODE ANN. § 152.501(b).

115. *Id.* § 152.203(a).

116. *Id.* § 152.203(b).

117. Young v. Qualls, 279 S.W.3d 670 (Tex. App. 2005).

118. *Id.* at 672.

119. *Id.*

120. *Id.* at 672, 674 n.3.

121. *Id.* at 672.

sales occurred, however. After many months, and without consulting Qualls, Young had the electricity turned off and telephone disconnected and asked Qualls to leave the property.[122] The jury found Young had breached the partnership agreement.[123] The court of appeals agreed, finding Young's "expulsion" of Qualls to be a violation of Qualls's rights.[124]

A relatively ancient Texas case reflects the same position. In *Ball v. Britton*,[125] Ball and Britton agreed that Britton would furnish money so that Ball could buy machinery and erect buildings that would serve as an ice works, after which Ball would operate the business and the two would split the profits.[126] Ball supervised construction of the ice works, opened the business in May 1879, and operated it successfully for five months, making $3,000 net profits.[127] The business appeared to be a success, and Ball anticipated the ice works clearing $5,000 profit each year thereafter.[128] However, on September 20, 1879, Britton excluded Ball from the premises "by threats to take his life, by calling him a pauper, a liar and a thief and ordering one John P. Toliver to knock his brains out if he attempted to superintend the business."[129] When Ball sued, Britton claimed that Britton had merely withdrawn from the partnership,[130] but the court held otherwise:

> [T]hat is not the state of facts which the petition sets forth. The defendant did not withdraw from the firm. He expelled the plaintiff out of it; and he not only retained all that he had put into it, but he kept all that had been contributed by the plaintiff, except a certain portion of the profits.[131]

After finding that Britton had no right to expel Ball, the court held that Ball could properly claim the value of his work and suggested that punitive damages were also appropriate.[132] "The defendant appears to have taken the law into his own hands, and to have closed the partnership in a manner entirely too summary to be sanctioned by a court of justice."[133] If the court saw the facts that way, a court could hold that Nick and Lorenzo had treated Jerry as Britton treated Ball.

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122. *Young*, 279 S.W.3d at 672.
123. *Id.* at 673.
124. *Id.* at 673–75.
125. Ball v. Britton, 58 Tex. 57 (Tex. 1882).
126. *Id.* at 57.
127. *Id.* at 57–58.
128. *Id.* at 58.
129. *Id.*
130. *Ball*, 58 Tex. at 60–62.
131. *Id.* at 62.
132. *Id.* at 62–63.
133. *Id.* at 63.

Even large law firms get this wrong, sometimes. In *Cadwalader, Wickersham & Taft v. Beasley*,[134] Cadwalader, Wickersham & Taft ("Cadwalader"), a large law partnership, sent a notice to partners in its Palm Beach, Florida office that the firm intended to close the office.[135] Beasley, a Palm Beach partner, hired Professor Robert Hillman to send Cadwalader an opinion that Cadwalader had no authority to expel Beasley.[136] Cadwalader, it seems, did not have a partnership agreement clause providing for expulsion of partners. Cadwalader sent a notice repenting, but then it offered Beasley a Hobson's choice between relocation to New York or D.C. or voluntary withdrawal from the partnership.[137] Beasley complained that this was equivalent to expulsion.[138] A court eventually agreed.[139] Leaving for New York or D.C. "would have severely diminished his rainmaking abilities. Under these circumstances, . . . his rejecting the offer as impractical was not tantamount to a voluntary withdrawal."[140] The legal upshot, said the court, was that the firm "anticipatorily expelled Beasley."[141]

The story continues, however. After turning down this "choice," Beasley sued the firm for breach of fiduciary duty, and, in response, Cadwalader sent a letter purporting to expel Beasley.[142] The court held that this was expulsion even if the false choice was not.[143] The court allowed Beasley to recover for "wrongful expulsion"[144] and breach of fiduciary duties.[145] Beasley was able to recover punitive damages for the firm's "conscious[ ] disregard[ ]" of his rights.[146] *Young*, *Ball*, and *Beasley* are not the only cases in this line.[147]

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134. Cadwalader, Wickersham & Taft v. Beasley, 728 So. 2d 253 (Fla. Dist. Ct. App. 1998). A wonderful discussion of *Cadwalader* appears in Allan W. Vestal, *"Assume a Rather Large Boat . . .": The Mess We Have Made of Partnership Law*, 54 WASH. & LEE L. REV. 487 (1997) and Donald J. Weidner, Cadwalader, *RUPA and Fiduciary Duty*, 54 WASH. & LEE. L. REV. 877 (1997).

135. *Cadwalader*, 728 So. 2d at 255.

136. *Id.*

137. *Id.*

138. *Id.*

139. *See id.* at 256.

140. *Cadwalader*, 728 So. 2d at 256.

141. *Id.*

142. *Id.* at 255–56.

143. *Id.* at 256.

144. *Id.* at 255, 257.

145. *Cadwalader*, 728 So. 2d at 258–59.

146. *Id.* at 259.

147. *See, e.g.*, Norber v. Marcotte, 134 S.W.3d 651 (Mo. Ct. App. 2004) (affirming an award of punitive damages for, *inter alia*, locking out a partner and misappropriating funds).

Did Nick and Lorenzo expel Jerry in conscious disregard of his rights? It is clear that they had no more an express provision in their partnership agreement authorizing expulsion than did Young and Qualls, Britton and Ball, or Cadwalader. If they had no right to expel, they risked offending Jerry's rights by locking him out of the auto body shop, just as Young offended Qualls's, Britton offended Ball's, and Cadwalader offended Beasley's. The jury would be welcome to make such a finding on these facts.

Nick and Lorenzo would not only be paying damages for offending Jerry's rights as a partner. The Texas General Partnership Law also requires that Jerry, as a withdrawn partner, be bought out. "The partnership interest of a withdrawn partner automatically is redeemed by the partnership as of the date of withdrawal . . . ."[148] The redemption price for Jerry's interest is "the fair value of the interest on the date of withdrawal."[149] A contrasting section suggests that "fair value" includes goodwill, i.e., that "fair value" is going concern value: A partner who wrongfully withdraws is entitled only to "the lesser of . . . fair value [or] . . . the amount that the withdrawn partner would have received if an event requiring a winding up of partnership business had occurred at the time of the partner's withdrawal."[150] Fair value versus liquidation value—the contrast shows that fair value normally would include the value of a going business. That is what Nick and Lorenzo would owe Jerry if their locking him out were construed as an expulsion in violation of Jerry's rights, as per *Cadwalader.*

B. *A Contractual Solution:* Monteleone[151]

1. *Monteleone* and the Code: Might the Answer Be No?

In contrast to other courts' focus on Nick and Lorenzo's changing of the locks, the *Monteleone* decision focused instead on the offending conduct of Jerry—the reason the locks were changed. As with the other cases mentioned in this Article, *Monteleone* was decided under an older statute, the Uniform Partnership Act (1914),[152] but the case's reasoning is just as consistent or inconsistent with that statute as it would be with the current Texas General Partnership Law.

148. TEX. BUS. ORGS. CODE ANN. § 152.601 (2013).

149. *Id.* § 152.602(a).

150. *Id.* § 152.602(b).

151. Monteleone v. Monteleone, 497 N.E.2d 1221 (Ill. App. Ct. 1986).

152. *Id.* at 1224.

Briefly put, the *Monteleone* court declared that Jerry's conduct constituted a wrongful withdrawal from the partnership.[153] The court's reasoning appears in the following passage:

> [I]nnocent partners have the right to continue partnership business where another partner has wrongfully terminated the partnership. . . .
>
> . . . .
>
> A partner's conduct is considered "wrongful" when it is taken in derogation of the duties imposed either explicitly by the partnership agreement or implicitly by virtue of the nature of the partnership itself. The Uniform Partnership Act empowers a court to order partnership dissolution whenever, for example, a "partner has been guilty of such conduct as tends to affect prejudicially the carrying on of the business, [or whenever a] partner wilfully [sic] or persistently commits a breach of the partnership or agreement . . . ."
>
> . . . .
>
> In our opinion these allegations [of Jerry's conduct] . . . were sufficient to state a claim that Jerry's behavior was in contravention of the partnership agreement or a breach of Jerry's fiduciary duties, and would amount to "wrongful termination" of the partnership.[154]

This passage seems inconsistent with the 1914 UPA in several ways, two of which are relevant here.[155] First, in the UPA, breach of the partnership agreement or breach of fiduciary duties is not itself a withdrawal or dissolution of the partnership within the statute.[156] The structure of the UPA's dissolution and termination provisions strongly suggests that, in a partnership at will—meaning without "a definite

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153. *Id.* at 1224–25.

154. *Id.* (citing, *inter alia*, Uniform Partnership Act § 32 (1914), as enacted in Illinois law at the time) (citations omitted).

155. In addition to the two sections discussed here, the court also applies section 38(2) and (3) as a remedy in an at-will partnership, something the statute almost surely did not contemplate. Section 38(2) was to apply only to a partnership for a definite term or particular undertaking, which is why it authorizes the remaining partners to continue the business only "during the agreed term." *See* U.P.A. § 38(2)(b) (1914). The *Monteleone* court finessed this issue by claiming that "the term originally agreed upon by the partners" was "at will." 497 N.E.2d at 1225.

156. *See, e.g.*, U.P.A. § 31 (1914) (Causes of Dissolution). The UPA uses the term *dissolution* to describe the end of the partnership, which is described as "an association of two or more persons to carry on as co-owners a business for profit." U.P.A. § 6(1) (1914). The partnership is thought of primarily as an aggregate or group of partners. When the partners are no longer associated together in that fashion, then the association that is the partnership is at an end. The business may go on under a different partnership (for instance, an association of the remaining partners), or may be wound up, depending on other circumstances. *See, e.g.*, U.P.A. §§ 37–38 (1914). The code treats winding up as a separate issue. Our code now reaches similar results through a different logic. The primary difference is that the partnership is treated as an entity. *See* TEX. BUS. ORGS. CODE ANN. § 152.056 (2013). A partner may withdraw from the partnership, but the entity remains and continues to own the business. *See id.* §§ 152.501, 152.502. The business may go on, or the entity and business may be wound up and terminated, depending on circumstances other than the withdrawal of a partner. *See id.* § 152.701.

term or particular undertaking specified in the [partnership] agreement"[157]—since no cause for dissolution is necessary, no cause for dissolution is relevant other than the will of the withdrawing partner. The sufficiency of a partner's expressed will to dissolve renders irrelevant the partners' reasons for dissolution; the law cares only that the partner wants to dissolve, not why.[158] The at-will nature of the partnership suggests that no legally recognized dissolution for cause exists.

The same is true under the current Texas General Partnership Law. In a partnership at will, any expressed will to withdraw received by the partnership functions as a withdrawal,[159] and such a withdrawal is not wrongful under the statute.[160] This implies, as under the UPA, that the reasons for an expression of withdrawal are irrelevant. Under the facts in *Monteleone*, it was clear (and the court itself admitted)[161] that the partnership was at will. Therefore, the only issue under the code was whether Jerry had expressed the will to dissolve. Of course, he had not. Rather, he had complained that Nick and Lorenzo had wrongfully excluded him, "thereby effecting a dissolution."[162] Jerry asked for the right to continue the business as the remaining owner. At no time until he sued did he express the will to disassociate; nor had Nick and Lorenzo, except to exclude Jerry, and the code suggests their reasons for doing so were technically irrelevant. Thus, no dissolution, disassociation, or withdrawal occurred.

Second, and conversely, the *Monteleone* court suggested that the section providing for dissolution by decree of court supports its analysis. To justify concluding that Jerry had wrongfully dissolved the partnership, the court cited the dissolution by judicial decree provision, UPA section 32, which provides that, on the proper showing, "the court shall decree a dissolution."[163] The court's argument is a bit of a stretch. If the law meant for the conduct of a partner to cause dissolution, why must the court enter a decree? Is the result in *Monteleone* a "Dissolution by Decree of Court," as section 32's heading proclaims, or dissolution by egregious conduct, as the *Monteleone* court's reason-

157. U.P.A. § 31(1)(a) (1914) (defining an at-will partnership as a partnership without "definite term or particular undertaking specified in the [partnership] agreement").

158. *See, e.g., id.* §§ 31, 32, 38. Under section 31, dissolution is caused "[w]ithout violation of the agreement between the partners" by the expression of a partner's will to dissolve. Premise: a partner may withdraw without any wrongdoing merely by expressing the will to disassociate, without any cause at all; conclusion: having a cause to disassociate adds nothing—the law is not concerned with cause for disassociation in an at-will partnership.

159. TEX. BUS. ORGS. CODE ANN. § 152.501(b).

160. *See id.* § 152.503.

161. Monteleone v. Monteleone, 497 N.E.2d 1221, 1225 (Ill. App. Ct. 1986).

162. *Id.* at 1223.

163. U.P.A. § 32 (1914).

ing suggests? If egregious conduct alone causes disassociation, one would need to file for a decree only when there was a dispute about whether such conduct had occurred, and the "decree of dissolution" would be a mere finding of fact, not a judicial order decreeing dissolution. What the court did is not a natural reading of section 32.

The Texas General Partnership Law may seem equally opposed to *Monteleone* for the same reason. In the Texas provision, egregious conduct that under the UPA warranted a judicial decree of dissolution even more clearly requires a judicial decree: "An event of withdrawal of a partner occurs on: . . . (5) the partner's expulsion by judicial degree, on application by the partnership or another partner, if the judicial decree determines that the partner [committed the egregious conduct]."[164] Thus, the expulsion, which is the event of withdrawal, occurs by judicial decree, not by a partner's conduct. And the decree is conditioned on both a petition by a proper party and a proper finding. It would be difficult to cite this section alone in support of a holding that a partner's misconduct had caused the partner's withdrawal long before the decree occurred.

As noted, Texas law also purports to take control of the definition of "wrongful": "A partner's withdrawal is wrongful only if: (1) the withdrawal breaches an express provision of the partnership agreement; (2) . . . [the partnership] has a period of duration, is for a particular undertaking," or is required to wind up on the occurrence of a certain event, and one of these occurs; or "(3) the partner is expelled by judicial decree under Section 152.501(b)(5)."[165] Of course, none of these happened in *Monteleone*. There was no express partnership agreement, the partnership was at will, and there had been no decree. So, under the Texas General Partnership Law's provisions, Jerry might not have withdrawn, and even if he had, the withdrawal was not wrongful. The Revised Uniform Partnership Act (RUPA) largely agrees.[166]

On the other hand, Texas case law includes a version of *Monteleone*, reasoned with equal obscurity: *M.R. Champion, Inc. v. Mizell.*[167] The case is pre-Texas General Partnership Law, but, given the incongruities between these cases and any partnership code, that should not be

164. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(5).

165. *Id.* § 152.503(b).

166. The Revised Uniform Partnership Act agrees with this result, as a matter of default terms. *See, e.g.*, R.U.P.A. 22 §§ 601, 801 (2001); HILLMAN, WEIDNER & DONN, *supra* note 23, at 429 ("Assuming the partnership agreement does not provide for expulsion by action of the partnership, the aggrieved partner's options are limited to seeing judicial expulsion under Section 601(5) or petitioning for a decree of dissolution under Section 801(5).").

167. M.R. Champion, Inc. v. Mizell, 904 S.W.2d 617 (Tex. 1995) (per curiam).

a strike against or for the case. In *M.R. Champion*, Mizell and Champion formed a partnership to provide services to Northwestern Resources Co. for one year, beginning in January 1986.[168] Near the end of 1986, Champion negotiated a second year for the partnership in the name of his own company.[169] However, in January 1987, Northwestern banned Mizell from its property.[170] Champion continued to perform, using equipment leased from Mizell.[171] In December 1987, Champion negotiated an additional three-year contract, again in the name of his own company.[172] One month later, he told Mizell the partnership was at an end.[173]

Mizell sued Champion for the profits of the additional three years.[174] In defense, Champion claimed that the partnership terminated in January of 1987 when Northwestern banned Mizell from its property.[175] Mizell claimed that the partnership continued until Champion terminated it in January 1988.[176] The jury "found that after Mizell was barred from Northwestern's premises in January 1987, he breached the partnership agreement and conducted himself in such a way that it was not reasonably practicable to carry on the partnership business."[177] Therefore, the trial court found that the partnership was terminated in January 1987, a finding—and interpretation of partnership law—that the Texas Supreme Court affirmed in a per curiam opinion.[178]

Squaring this case with the Texas General Partnership Law, at least superficially, is a difficult task.[179] The only event that occurred in January 1987 is that Mizell was banned from Northwestern's property. This was neither the expression of a partner's will to withdraw nor a judicial decree of withdrawal. This event did fit into one legally relevant category: conduct such that "it was not reasonably practicable to carry on [the] partnership business."[180] This language appears in the code only in the justification for a judicial decree of expulsion, how-

168. *Id.* at 617.
169. *Id.*
170. *Id.*
171. *Id.*
172. *M.R. Champion*, 904 S.W.2d at 617.
173. *Id.* at 617–18.
174. *Id.* at 618.
175. *Id.*
176. *Id.*
177. *M.R. Champion*, 904 S.W.2d at 618.
178. *Id.* at 618–19.
179. But not impossible. It is in fact the task undertaken in Section III.B of this paper.
180. *M.R. Champion*, 904 S.W.2d at 618.

ever.[181] The code does not make such conduct on its own an event of withdrawal. The code alone, read this way, does not appear to justify the court's decision in this case.

The court also held that Mizell had "breached the partnership agreement."[182] The statute names this as cause for a judicial expulsion.[183] It is easy to see why Mizell's conduct satisfied this category. If a partner makes himself so odious to the partnership's only client—whom the partnership was formed to serve—that the client bans the partner from the client's property, the conduct is clearly contrary to the partners' understanding of acceptable behavior in the conduct of the business. Indeed, such behavior is contrary to the conduct of any business for profit. Yet the judicial expulsion provision of the code seems to give little support to the court's declaration that Mizell's conduct was itself a withdrawal.

2. The Case for Informal Partnerships and Self-Help

Counter-arguments in favor of the *Monteleone/M.R. Champion* type of opinion exist, however. These arguments are more substantive. They are also equally logical. Moreover, they do not appear to be opposed by the code. In several ways, the code supports them, though perhaps not obviously.

First, regarding wrongfulness: expulsion by judicial decree for misconduct is wrongful withdrawal,[184] presumably because the misconduct itself is wrongful; it is not the judge's actions the statute declares wrongful. Yet if conduct that supports a judicial expulsion warrants a declaration of wrongfulness, then it was wrongful conduct even before the judicial decree.[185]

Moreover, if such conduct warrants judicial expulsion at the time of the decree, presumably it warrants a finding of withdrawal; that is, in fact, what the statute declares it warrants. And if it warrants a finding of withdrawal, then cannot it also be, or cause, a withdrawal? To say that the withdrawal comes only on the court's decree prohibits the court from doing justice from the time of the wrong done, as if commission of a tort depended on a decree that the conduct was wrongful. If that were true, damages should flow only from the date of the de-

181. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(5)(C) (2013).

182. *M.R. Champion*, 904 S.W.2d at 618.

183. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(5)(B).

184. *Id.* § 152.503(b)(3).

185. The Revised Uniform Partnership Act likewise uses the word "wrongful" inconsistently. *See* HILLMAN, WEIDNER & DONN, *supra* note 23, at 425–26 ("Unfortunately, R.U.P.A. is not entirely consistent in its use of the term wrongful. . . . By sometimes using 'wrongful' very precisely and at other times using it more loosely, R.U.P.A. is likely to cause much confusion.").

cree. The partnership code itself does not understand that to happen when withdrawal is wrongful.[186] And cases decreeing the equivalent of withdrawal under older statutes took account of this conundrum by decreeing withdrawal to have occurred not on the date of the decree but on the date of the misconduct.[187]

Nor does the code make itself the exclusive arbiter of withdrawal events. While section 152.001 provides that "'[e]vent of withdrawal" or "withdrawal" means an event specified by Section 152.501(b),'"[188] and 152.501(a) proclaims that "[a] person ceases to be a partner on the occurrence of an event of withdrawal,"[189] nothing in the statute claims these to be the only or exclusive means of ceasing to be a partner.[190] Moreover, the statute invites the parties to expand withdrawal events by contract, and invites courts to recognize such provisions. Section 152.501(b)(2) includes "an event specified in the partnership agreement as causing the partner's withdrawal."[191] And the general expulsion provision of 152.501(b)(3) allows expulsion "as provided by the partnership agreement."[192] The limits on contractual modifications of the default partnership withdrawal provisions prohibit a contract to "vary the power to withdraw as a partner under section 152.501(b)(1), (7), or (8),"[193] but a partner's power to withdraw under those sections is not varied by the contractual addition of other withdrawal methods. The same section limits the power to "vary the right to expel a partner by a court in an event specified by section 152.501(b)(5),"[194] but the right of a court to expel is not varied when a court in addition declares that the partner herself withdrew by com-

186. TEX. BUS. ORGS. CODE ANN. § 152.503(c) (specifying that "a wrongfully withdrawing partner is liable to the partnership and to the other partners for damages caused by the withdrawal," with no mention of the decree as a limiting date).

187. *See* Vangel v. Vangel, 254 P.2d 919, 926 (Cal. Ct. App. 1953) ("In some cases where the breach is serious and unequivocal the dissolution may be decreed as of the date of the breach." (dicta)); HILLMAN, WEIDNER & DONN, *supra* note 23, at 416–17 ("Nothing in R.U.P.A. reveals an intent to change prior case law, which suggests flexibility to fix a date of separate to suit the circumstances of a given case. Accordingly, the effective date of disassociation by judicial expulsion may be the date of conduct or circumstances giving rise to the decree . . . ."); *see also* Fisher v. Fisher, 212 N.E.2d 222, 224 (Mass. 1965) (holding the partner guilty of misconduct and a victim of wrongful ouster but undeserving of any profits from the partnership after the date of the ouster and declaring the partnership dissolved on the date of the ouster, "nunc pro tunc").

188. TEX. BUS. ORGS. CODE ANN. § 152.001(1) (emphasis added).

189. *Id.* § 152.501(a) ("A person ceases to be a partner on the occurrence of an event of withdrawal.")

190. *Cf., e.g.*, HILLMAN, WEIDNER & DONN, *supra* note 23, at 420 ("[Section 601] itself does not specify that the list of dissociation events is exclusive.").

191. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(2).

192. *Id.* § 152.501(b)(3).

193. *Id.* § 152.002(b)(5).

194. *Id.* § 152.002(b)(6).

mitting misconduct that would itself warrant expulsion by the court. In other words, the code does not prevent contractual additions to any of the sections relevant to withdrawal in these cases. The events specified in section 152.501 are thus not the only possible means of withdrawal.

Courts should therefore be open to arguments based on contract or agreement. Partnership is a contractual relationship. While it is common to refer to the provisions of the partnership code that control partnerships in the absence of agreement as default provisions, the code actually makes the partnership agreement the first source for rules governing partnership: "To the extent that the partnership agreement does not otherwise provide, this chapter and the other partnership provisions govern the relationship of the partners and between the partners and the partnership."[195] So, technically, only if the partners' agreement does not solve the issue do the provisions of the code become defaults. Analysis of partnership begins in contract.

While "partnership" is a default category that can be applied even to persons not intending to be partners,[196] the acts that persons must do to become partners are all contractual in nature. A partnership can form only between persons who have some kind of contract, even if very informal.[197] At a minimum, they must agree to associate to carry on as co-owners a business for profit.[198] "Factors indicating that persons have created a partnership" are all contractually obtained: "receipt or right to receive a share of profits," "participation or right to participate in control of the business," "agreement to share or sharing" of losses or liabilities, and "agreement to contribute or contributing money or property to the business."[199] The one qualification necessary to be a partner is "capacity apart from" the partnership code, meaning, presumably, contractual capacity.[200] And most of the provisions in the Texas General Partnership Law are default provisions; except in a few named instances, "a partnership agreement governs the relations of the partners and between the partners and the partnership."[201]

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195. *Id.* § 152.002(a).

196. TEX. BUS. ORGS. CODE ANN. § 152.051(b).

197. City of Corpus Christi v. Bayfront Assocs., 814 S.W.2d 98, 107 (Tex. App. 1991) ("This relationship must be based on an agreement, either expressed or implied.").

198. *Id.*

199. TEX. BUS. ORGS. CODE ANN. § 152.052(a). Of course, it is possible that such rights are given by gift or devise, but that would be the rare exception.

200. *Id.* § 152.053. *Cf. id.* § 3.004(a) (declaring capacity to contract the sole qualification for organizing a filing entity).

201. *Id.* § 152.002(a).

The legal result of formation of a partnership contract is that, unless displaced by the partnership code, contract law also applies. The Texas General Partnership Law is quite clear that "principles of law and equity . . . supplement" the law "unless otherwise provided."[202] It would be remarkable if contract law did not apply. And principles of equity have always played a role in partnership break-up law.[203]

If partnership is a contract, then partners may establish the terms of that contract by manifesting their intentions, expressly or by implication.[204] The terms of that contract must necessarily be examined in a broad-minded way. The Texas General Partnership Law is intended to govern partnerships, but partnerships are an extraordinarily broad category of business relationships. On the continua of resources, sophistication, and size of business, for instance, on one end reside giant law firms, construction companies, and investment vehicles served by legions of lawyers, bankers, accountants, and other advisors. On the other end of those continua are backhoe contractors, plumbers, and landscapers, many of whom fall into the partnership category by default. If this latter group has an explicit partnership agreement, it is oral,[205] and it may be nothing more explicit than an agreement to split profits.[206] They might never have profits, but if they agree to split them, contribute roughly equally to the business, and by their conduct obviously share control, they are likely to be found partners.[207] This kind of informal partnership is just as much a partnership as the large

202. *Id.* § 152.003.

203. *See, e.g.*, Sanders v. Kirkland & Co., 510 So. 2d 138, 140–41 (Ala. 1987) ("The law of Alabama has historically and consistently treated any claim of 'wrongful exclusion' from a partnership as being a purely equitable claim."); Cagnolatti v. Guinn, 189 Cal. Rptr. 151, 155 (Cal. App. 1983) (naming a partner following dissolution by expulsion the equivalent of a trust beneficiary); Gherman v. Colburn, 140 Cal. Rptr. 330, 342 (Cal. Ct. App. 1977); Owen v. Wilden Hosp., 62 N.W.2d 186 (Iowa 1954) (equity action for accounting and dissolution for alleged wrongful expulsion); Schoenborn v. Schoenborn, 402 N.W.2d 212, 214–15 (Minn. Ct. App. 1987); Herman v. Pepper, 166 A. 587, 588 (Pa. 1933) ("The exclusion of one partner by another from the management of the partnership business or possession of the partnership property is undoubtedly ground for dissolution by a court of equity.").

204. "[A] partnership agreement governs the relations of the partners and between the partners and the partnership." TEX. BUS. ORGS. CODE ANN. § 152.002(a) (2013). *See, e.g.*, Bailey & Williams v. Westfall, 727 S.W.2d 86, 90 (Tex. App. 1987) ("Where there is a partnership agreement, . . . the rights of a withdrawing partner are governed by that agreement, not by statute."); Dobson v. Dobson, 594 S.W.2d 177, 180 (Tex. App. 1980) ("[The partnership agreement] governs the rights of the partners; only where it is silent do the provisions of the [statute] come into play.").

205. Oral partnership agreements are common. *See, e.g.*, Johnson v. Graze Out Cattle Co., 2012 WL 2923329 (Tex. App. 2012); Malone v. Patel, 397 S.W.3d 658, 674–75 (Tex. App. 2012) (finding evidence to support a finding of partnership in an oral agreement and opining that "[t]he law recognizes oral agreements"); Sewing v. Bowman, 371 S.W.3d 321 (Tex. App. 2012).

206. TEX. BUS. ORGS. CODE ANN. § 152.052(a)(1) (2013).

207. *See id.* § 152.052(a).

law firm that intentionally chooses the business form. Identical code provisions, however, potentially have wildly different economic and moral effects on such partnerships and on the incentives of people who form them.

The *Beasley* case,[208] on the one hand, and *Monteleone*[209] and *M.R. Champion*[210] on the other, provide good examples. When Cadwalader, Wickersham & Taft, the large law firm, discovers that it lacks an expulsion provision in its partnership agreement and therefore has violated partner Beasley's rights,[211] most of us are apt to laugh. If the wisdom of the high-falootin' Manhattan firm is not enough to plan for dissatisfaction with a small Florida office, the firm has no one to blame but itself. Society rightly places the moral responsibility for planning for withdrawals on the central management of the large law firm, which has resources and the know-how to draft a nuanced agreement of all partners in advance. Moreover, the sums at issue in an expulsion from this successful practice justify even a CW&T lawyer's time to draft the required provisions.

But when two fellows team up to buy a bulldozer and push earth for people around the county,[212] no one expects them to plan for their eventual dissatisfaction with each other.[213] Few small, close businesspeople decide to start a business as co-owners and share management decisions day-to-day while at the same time holding in their heads a plan for the termination of their relationship. Not only does no one blame the partners for not calling a lawyer to organize their business, the damages from a wrongful expulsion multiplied by the probability of an explosive break-up were probably far less than the fee they would have had to pay the lawyer to draft the clause. They and their neighbors might laugh at them for paying a lawyer for such things, and they would probably be right to do so. In that case, writing such a contract would be inefficient. Given the hopefulness of the parties in their undertaking, planning for its demise often seems immoral to them, though they may and often do each have well-defined expectations regarding the conditions on which they are to do business.

These are types or paradigms that I am describing, but they make obvious that when we talk of the agreement of the partners, and their relationship, we are talking about different problems depending on

208. Cadwalader, Wickersham & Taft v. Beasley, 728 So. 2d 253 (Fla. Dist. Ct. App. 1998).

209. Monteleone v. Monteleone, 497 N.E.2d 1221, 1223 (Ill. App. Ct. 1986).

210. M.R. Champion, Inc. v. Mizell, 904 S.W.2d 617 (Tex. 1995) (per curiam).

211. *Cadwalader*, 728 So. 2d at 255–56.

212. Nolen v. Burnett, No. CA91-151, 1992 WL 16080 (Ark. Ct. App. 1992).

213. The parties appeared not to have done so. *Id.* *2–4 (reporting the partners' very informal negotiations).

the kind of partnership at issue. How the law governs such relationships might differ. For instance, when the law chooses a default rule, often it is best to choose the rule that the parties would have chosen had they negotiated it, or at least something close to it, if that can be determined.[214] In this way, the law lowers transaction costs: It is cheaper to form a business when the form itself already contains the rule we would expect to govern us.[215]

Sometimes, the law chooses an intentionally inefficient rule: a default rule which is not the rule the parties would have chosen had they had time to negotiate.[216] The rule penalizes parties who do not bargain away from it, so some call this kind of rule a "penalty default."[217] We might choose this rule if we have no idea what the parties would choose, we wish to encourage them to choose something, and we think that a desirable enough number of them will take notice and contract around the default. If all the relevant parties are sophisticated and have the means to negotiate around the penalty, then such a rule might result in better law—economically, morally, and prudentially—because it will be chosen by the parties.

What must be avoided, however, is the imposition of a penalty default rule on parties who are unlikely to know that they should negotiate away from it, or lack the means or incentive to negotiate away from it, or reasonably believe that the law does not seek to penalize them if they fail to negotiate. A penalty default in such a case is uneconomical, immoral, and unjust.

With regard to the self-help problem, the kind of partnership at issue is almost always the small, informal kind. Those who have the sophistication, means, and reason to get a lawyer involved early often do. The three fellows at the Monte Auto Body Shop either lacked the sophistication or the means to do so, or perhaps the costs of it would

214. This is a kind of majoritarian default rule but is tailored to the parties' views. *See, e.g.*, Russell Korobkin, *The Status Quo Bias and Contract Default Rules*, 83 CORNELL L. REV. 608, 613–17 (1998) (providing a lucid description of the foundational literature); *see also* Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87, 91 (1989). A "tailored default" rule, which "attempts to provide a contract's parties with precisely 'what they would have contracted for,'" on the one hand, differs from an "untailored default," which "provides the parties to all contracts with a single, off-the-rack standard that in some sense represents what the majority of contracting parties would want." Ayres & Robert, *supra* note 214, at 91.

215. *See* Korobkin, *supra* note 214, at 615; Ayres & Gertner, *supra* note 214, at 93 ("The 'would have wanted' approach to gap filling is a natural out-growth of the transaction cost explanation of contractual incompleteness.").

216. *See, e.g.*, Ayres & Gertner, *supra* note 214, at 94–95 (developing one theory for when the law should choose a penalty default rule).

217. *Id.* at 91.

have outweighed the benefits. Perhaps adding the lawyer's expenses to their bottom line would change its color from black to red. Perhaps they have acted quite reasonably, in context, and believed the law would back them up. The rule that applies to their conduct probably should in fact back them up. It should not be a penalty default. Rather, it should reflect their reasonable expectations.

Courts should be on the lookout to protect the reasonable expectations of the partners developed within their relationship. When courts adjudicate disputes between partners in small, informal partnerships as to their rights against each other—in other words, issues about the meaning of their relationship—the reasonable expectations of the partners in context is a better guide to their agreement, a more moral guide as to the proper result, and a more economically sensible rule for small, informal partnerships in the future—than any other rule. The reasonable expectations of the partners is, in fact, the partnership agreement, as much as the written partnership agreement of CW&T was theirs.

It must and should be so. These small, informal partnerships have very little in the way of explicit agreement. They may have agreed only to split profits, though that explicit agreement may have been a key component of a court's conclusion that they have become partners. But no one would claim that the entire agreement of the partners in an ongoing business is captured in the single phrase "to split profits." Running a business is a complicated endeavor. Looking at what the partners have done, and how they have done it over the time the business operated, will reveal a great deal more about what they have actually agreed, and what they reasonably expect for the future. This understanding, which shapes the partners' thinking and conduct, should shape the rules that bind the partners when their relationship unravels.

In fact, a careful look at all of this conduct is how courts determine in the first instance that an informal, default partnership exists.[218] The analysis is typically factored, contextual, closely tailored to the parties' understanding, and based on a broad factual analysis.[219] The law would be oddly incongruous if it looked at all of this conduct to determine that a partnership exists and then ignored it all and applied only

218. *See, e.g.*, Ingram v. Deere, 288 S.W.3d 886, 893–904 (Tex. 2009); BROMBERG & RIBSTEIN, *supra* note 5, ch. 2.

219. That Bromberg and Ribstein take an entire chapter to detail partnership formation is a testament to the complexity and particularity of the analysis. *See* BROMBERG & RIBSTEIN, *supra* note 5, ch. 2. The chapter contains broad sections on the context of the determination, *id.* § 2.02; the requisite intent, *id.* § 2.05; and the factors that must be examined, *id.* §§ 2.06–2.09. The authors include a section on formalities, also. *Id.* § 2.13.

explicit code-determined default rules in determining how the same partnership should cease.

When such partnerships come to an end, firmly established case law sometimes looks to this same pattern of conduct to determine the legal parameters of partnership termination. A long line of cases address whether a partnership is at will or for a definite term or particular undertaking.[220] The line between the two is not clear,[221] and only an examination of the facts showing the partners' understanding will allow a court to say. Occasionally, a court might even allow that informal understanding to conflict with the formal partnership agreement.[222] Courts have not been hesitant to look.

Looking to this informal understanding might also, just as well, suggest what counts as withdrawal from a partnership[223] or when the partners have a right to expel one of their members.[224] Sticking to the partners' agreement, even such an informal one as this, will encourage others (including the parties in dispute) to begin business in the future on the strength of their own reasonable expectations. If when small businesses begin to fall apart nothing that the parties reasonably expected to happen happens, then the next time around some will just not start the business. At the margins, the costs of beginning some businesses will be too high, and they will never begin. We will all be the poorer for it.

In the self-help context, then, the rules that apply to informal partnerships should not penalize the parties' reasonable understanding.

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220. *See supra* note 6; *see also, e.g.*, BROMBERG & RIBSTEIN, *supra* note 5, § 7.02(c)(3).

221. HILLMAN, WEIDNER & DONN, *supra* note 23, at 428–29 ("A substantial body of case law has developed under the U.P.A. concerning implied agreements that establish terms or undertakings. . . . [T]he U.P.A. decisions will be relevant in determining whether a term or undertaking should be inferred for a R.U.P.A. partnership.").

222. In *Bendalin v. Youngblood & Assocs.*, 381 S.W.3d 719 (Tex. App. 2012), a written partnership agreement appeared to require a written withdrawal notice. A partner expressed his intent to withdraw orally, and the court held this effective notwithstanding the agreement's requiring of a writing. 381 S.W.3d at 736. The statute's "provisions do not state that oral notice is ineffective if the notice is not received in writing where required," the court reasoned. *Id.* at 737. "To hold otherwise would require this Court to overlook the practical implications of a partner's actual departure from a partnership." *Id.*

223. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 5, § 7.02(c)(4) ("Sometimes it is unclear whether a partner acted with intent to dissolve . . . .").

224. An expulsion provision can be a part of an oral partnership agreement. *See* Frank v. R.A. Pickens & Son Co., 572 S.W.2d 133 (Ark. 1978); Hogan v. Morton, No. 03A01-9206-CH-00214, 1993 WL 64220, at *6 (Tenn. Ct. App. 1993) (finding that a question of fact existed regarding whether a partner could be expelled from a law firm partnership pursuant to agreement based on prior practices); *see also* Lawlis v. Kightlinger & Gray, 562 N.E.2d 435, 439 n.1 (Ind. Ct. App. 1990) (allowing parol evidence of the partners' agreement because "this partnership [agreement] is not integrated").

Rather, they should reach the most efficient result, the one that confirms the reasonable assumptions of the partners.

Again, the code allows this flexibility. In the Texas General Partnership Law, the relevant default statutory provisions of partnership law are equivalent to default contractual terms only after we look first to the partners to discern their agreement.[225] So a court may determine—as the *Monteleone* and *M.R. Champion* courts did—the terms of the partnership agreement or the nature of the partnership, based on the parties' understanding and conduct, standard usage, and finally statutory default rules. This rationale supports what those courts did.

The code itself mentions the possibility of contractual withdrawal terms when it refers, as noted above,[226] to "an event specified in the partnership agreement as causing the partner's withdrawal."[227] On first glance, the word "specified" seems to require a measure of formality, and one might think that partners in informal partnerships could never reach it. But the law that governs informal business relationships is not and should not be so biased against informal business relationships.[228] Though the word "specified" seems to suggest the thing is expressed, some ways of violating an informal relationship are so obvious that they specify themselves. For example, in *M.R. Champion*, the informal promise violated was to remain able to serve our partnership's only business client, a promise violated when partner Mizell was permanently banned from that client's property.[229] In *Monteleone,* the partnership relationship (and explicit oral promises) required that each partner take an equal weekly draw, a term Jerry violated.[230] The partnership relationship was also based on a governance structure of three equal votes, a structure that would be upset by Jerry's bringing his son in as a partner.[231] Jerry's combined misconduct would break the implicit trust required in such a small business.

One could readily imagine circumstances other than *M.R. Champion* and *Monteleone* that would qualify. The paradigmatic example might be the maniacally destructive partner. Suppose a law partnership has three partners (A, B, and C) and three offices (1, 2, and 3).

225. TEX. BUS. ORGS. CODE ANN. § 152.002(a) (2013).

226. *See supra* notes 189–95 and accompanying text.

227. TEX. BUS. ORGS. CODE ANN. § 152.501(b)(2).

228. Hillman addressed a similar concern when he reasoned that failure of informal partners to agree on an expulsion provision should also not be held against them. Hillman, *supra* note 39, at 543. He reasoned, "The absence of an expulsion agreement . . . may represent nothing more than a failure of the partners to consider the possibility of such an arrangement." *Id.*

229. M.R. Champion, Inc. v. Mizell, 904 S.W.2d 617, 618 (Tex. 1995) (per curiam).

230. Monteleone v. Monteleone, 497 N.E.2d 1221, 1225 (Ill. App. Ct. 1986).

231. *Id.*

One night, office 3 burns to the ground. Partner C calls in the next morning claiming he is traumatized and will not be at work. On security recordings recovered later that day at 4:30 pm, partners A and B see partner C spreading gasoline throughout office 3 and lighting a match. They immediately change the locks to offices 1 and 2 and employ guards to secure those offices. Have they offended partner C's rights? Surely an implied promise in their agreement and relationship is that none of them will actively destroy the business. The law does not need this promise to be more expressly specified. In these circumstances, self-help appears to be the only reasonable response. In other words, if one looks at the actual circumstances of these partnerships, one sees that the partners' understanding was specific enough that every partner knew that, if he acted in a certain way, the partnership was largely pointless to continue, that it was going to end.

One could easily walk this understanding of the partners' informal contract through the technicalities of contract law, and one Texas court has done just that. Under general contract law, it is possible to breach a contract so severely that the other party to the contract is released from its obligations. "It is a fundamental principle of contract law that when one party to a contract commits a material breach of that contract, the other party is discharged or excused from further performance."[232] Texas law contains an intriguing case in which *M.R. Champion* was rationalized by counsel in just such fashion.[233] In *Harris v. Archer*, one partner contended that another had materially breached a partnership agreement.[234] The partner argued that "the material breach effected a dissolution of the partnership and that he thereafter owed no duty to offer his former partners a business opportunity which arose after the partnership terminated. He relies on *M.R. Champion, Inc.*"[235]

The *Harris* court rejected a reading of *M.R. Champion* grounding the case solely on the general contract law of material breach, however. The court explained,

> In *Champion*, the jury found that Mizell, a partner, breached the partnership agreement and also conducted himself in a way that it

232. Mustang Pipeline Co. v. Driver Pipeline Co., 134 S.W.3d 195, 196 (Tex. 2004) (per curiam); *see* BFI Waste Sys. of N. Am., Inc. v. N. Alamo Water Supply Corp., 251 S.W.3d 30, 30–31 (Tex. 2007) (per curiam) (quoting *Mustang Pipeline*, 134 S.W.3d at 195, 196); Henry v. Masson, 333 S.W.3d 825, 840 (Tex. App. 2010) (in the context of a settlement agreement between partners winding down a partnership, quoting *BFI Waste Systems*, 251 S.W.3d 30–31 (quoting *Mustang Pipeline*, 134 S.W.3d at 196)).

233. Harris v. Archer, 134 S.W.3d 411 (Tex. App. 2004).

234. *Id.* at 430.

235. *Id.* at 446.

> was not reasonably practicable to carry on partnership business. Based on such jury finding, the trial court found that Mizell's conduct effected a termination of the partnership. *Champion* does not hold that a material breach of a partnership agreement, without more, effects a dissolution of the partnership.[236]

In support, the *Harris* court cited the withdrawal statute then in force in Texas.[237]

What is the "more" that *M.R. Champion & Harris* requires? The logical reading of these cases is that the court doubted whether a finding of withdrawal ("dissolution" under the older code) is the proper remedy for every material breach of a partnership agreement. After all, releasing one from contractual obligations is not the same remedy as declaring that withdrawal from a partnership occurred.[238] However, when the material breach is exactly the conduct warranting a decree of judicial expulsion under the statute and makes carrying on the partnership business impracticable, withdrawal is, in fact, the effect of material breach. This is the something "more" that *Harris* appears to require.[239]

The result is a finding that the partners' agreement as to their partnership has been breached in a way that justifies withdrawal as a remedy. As noted, this agreement is mostly tacit. It is agreement, as *Monteleone* says, "implicitly by virtue of the nature of the partnership itself."[240] An earlier California court reasoned, "In some cases where the breach is serious and unequivocal . . . [,] the misconduct really dissolves the partnership."[241] This is the kind of material breach warranting a finding of withdrawal, or its equivalent, whether we say it is based on contract or the contractual basis of the parties' understandings. In fact, keeping the offending partner in the partnership contract

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236. *Id.*

237. *Id.*

238. *See also* Fisher v. Fisher, 212 N.E.2d 222, 224 (Mass. 1965) ("There is no provision in the agreement or in the Uniform Partnership Act that a breach is equivalent to withdrawal from the partnership, and we will not imply one.")

239. The *Fisher* case is not inconsistent in its result. Though the *Fisher* court held that "ousting" the partner guilty of misconduct was "wrongful action," the court also held that the partnership was dissolved as of the date of the ouster and that the ousted partner was not entitled to profits from the partnership after that date. *Id.* at 224. The court grounded this move on "[e]quity and the furtherance of justice." *Id.*

240. Monteleone v. Monteleone, 497 N.E.2d 1221, 1224 (Ill. App. Ct. 1986) (*citing* Hillman, *supra* note 39, at 538–39); *see also* Vangel v. Vangel, 254 P.2d 919, 924–25 (Cal. Ct. App. 1953) (holding that no legally recognized harm occurred when two partners took a check that a third partner had given into possession of a bank, cashed it, and distributed the proceeds to themselves and the third partner after depositing needed sums in the partnership account and reasoning that the partners accurately assessed the partnerships needs even though they misapplied the proceeds).

241. *Vangel*, 254 P.2d at 926.

at that point would be unconscionable.[242] Either way, in the case of Jerry, Nick, and Lorenzo Monteleone, the court is justified in holding that Jerry has taken himself out of the partnership by his conduct, or at least given Nick and Lorenzo the right to declare that Jerry is no longer a partner, should they elect.

This is why courts granting a judicial decree of withdrawal sometimes date the time of the withdrawal to the partner's misconduct.[243] There is merely procedural, not substantive, difference between (i) granting judicial withdrawal and dating the time of the withdrawal to the date of the misconduct, on the one hand, and (ii) a court's declaring that the partner guilty of serious misconduct withdrew on the date of the misconduct. On substance, these are identical. Because the true ground for both is contractual and the relevant contractual event is the partner's misconduct, the proper rationalization of these cases is that withdrawal occurred by the misconduct on the date of the misconduct.

This misconduct is wrongful, morally if not legally. It may or may not be a "wrongful withdrawal," given that section 152.503 defines "wrongful" such that the label is inappropriate before a decree exists.[244] Perhaps none of the specific consequences of "wrongful withdrawal" as defined in the statute must occur.[245] But it may be withdrawal nonetheless, and presumably other contract remedies, including contractual damages, would be an appropriate remedy for it. On the other hand, it is also possible to follow the understanding of the partners in the informal partnership more fully. If the court understands that *Monteleone* and *M.R. Champion* best fit the partners' understanding of the nature of their partnership—that they have agreed in their informal way that conduct such as Jerry's and Mizell's would be wrongful, then they may be held to the conclusion that the kind of withdrawal committed by Jerry and Mizell is wrongful.

In that case, the partners have created grounds for the court to hold that wrongful withdrawal occurred on the date of the wrongful conduct. They have done this because it is what they most reasonably expected, and because holding in line with the reasonable expecta-

242. Unconscionability as grounds for relief from a contract, and the court's discretion regarding relief for unconscionability, are addressed in the Restatement (Second) of Contracts § 208 (1981) ("[A] court may refuse to enforce the contract, or may enforce the remainder of the contract without the unconscionable term, or may so limit the application of any unconscionable term as to avoid any unconscionable result.").

243. *See supra* note 187.

244. TEX. BUS. ORGS. CODE ANN. § 152.503(b)(3) (2013).

245. *See id.* §§ 152.602(b), 152.603, 152.604.

tions of the parties will be the most efficient, most moral, and most just resolution of their dispute.

III. WHAT TO DO

All of the four methods described in Section II for characterizing self-help conduct in the break-up of an informal partnership are justified by the law, either by clear statutory provision or, given a proper factual showing, by those provisions supplemented by the law of contract and equitable principles. Because these methods are all legally available to a court confronting a self-help fact pattern, the court has the means to reach a moral, efficient, and just result.

If the informal agreement of the partners and the conduct of an offending partner warrant a finding that the partnership agreement has been materially breached and that it is not reasonably practicable to carry on the partnership business as a result of the offending conduct, then the court may find the breaching party has withdrawn from the partnership as of the date of the wrongful conduct. If the breach of the partnership agreement, even an informal agreement, is egregious enough that the impracticability of continuing as a partnership is obvious, then support for the reasonable expectations of the partners strongly suggests this result. This principle best explains the outcome in *Monteleone*[246] and *M.R. Champion*.[247]

On the other hand, if the offending conduct is not egregious enough to amount to material breach, or the carrying on of the partnership remains reasonably practicable, the court might find that the partners who engaged in self-help conduct withdrew from the partnership, or not, depending on whether the meaning of their conduct, in context, expressed a will to withdraw. These principles explain *Ingram v. Deere*,[248] *Rhue v. Dawson*,[249] *In re Leal*,[250] *Young v. Qualls*,[251] Ball v. Britton,[252] and *Cadwalader, Wickersham & Taft v. Beasley*.[253] Depending on whether self-help conduct that excluded a partner expressed a will to withdraw, the court might also find that exclusion of a partner breached the excluded partner's rights as an owner and

246. *Monteleone*, 497 N.E.2d at 1223.

247. M.R. Champion, Inc. v. Mizell, 904 S.W.2d 617 (Tex. 1995) (per curiam).

248. Ingram v. Deere, 198 S.W.3d 96 (Tex. App. 2006), *rev'd on other grounds* 288 S.W.3d 886 (Tex. 2009).

249. Rhue v. Dawson, 841 P.2d 215 (Ariz. Ct. App. 1992).

250. In re Leal, 360 B.R. 231 (Bankr. S.D. Tex. 2007).

251. Young v. Qualls, 279 S.W.3d 670 (Tex. App. 2005).

252. Ball v. Britton, 58 Tex. 57 (Tex. 1882).

253. Cadwalader, Wickersham & Taft v. Beasley, 728 So. 2d 253 (Fla. Dist. Ct. App. 1998).

manager of the firm, as the courts held in *Leal*,[254] *Young*,[255] Ball,[256] and *Cadwalader, Wickersham & Taft*.[257] These rules harmonize the self-help cases. At root, the reasonable expectations of the parties in context should be respected.

The default rules governing businesses need not provide more clarity for better planning. Those who plan ahead can contract for whatever clarity they wish. In the cases, the parties themselves have not specified a legal category into which their conduct should fit. Following their reasonable expectations, inasmuch as they can be discerned, allows the parties' contracts to bear fruit while prohibiting the parties from taking advantage of each other. The lack of clarity is a cost they should bear. They have opened themselves up to the risk of a court's interpreting their conduct in various ways. As Hillman noted, partners engaging in self-help must be "prepared to assume the risk that their assessment of the wrongfulness of the conduct of the offensive partner may not withstand judicial review."[258] The partners have failed to specify explicitly any rule for interpreting their conduct and therefore made a difficult factual determination (including perhaps, a trial) all but necessary. The difficulty and expense of settling the legal meaning of self-help conduct will surely deter the partners from entering into another relationship without better planning or at least strongly urge them to contact a lawyer next time, before they change the locks. The difficulty of the determination is penalty enough, without a default rule also penalizing them, as it surely would penalize some if it were more specific. The law should encourage even people who do not know (or know how to manipulate) the law to use their time productively, even if that encouragement can only be given post hoc.

254. 360 B.R. at 240.
255. 279 S.W.3d at 673-75.
256. 58 Tex. at 62-63.
257. 728 So. 2d at 255.
258. Hillman, *supra* note 39, at 543.