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GROUNDBREAKING HIGH COURT DECISION BRINGS RELIEF TO LLPS

The High Court has today, for the first time, decided that the doctrine of repudiatory breach does not apply to LLP agreements*. The decision in *Flanagan v Liontrust Investment Partners LLP*, in which Macfarlanes LLP and Serle Court Chambers acted for Liontrust, will be welcomed by LLPs across the City and beyond. Had the Petitioner been successful in arguing that the LLP Agreement had been repudiated and the default rules in the LLP Regulations applied instead, he would have been entitled to a windfall. Rather than receiving an annual fixed profit share and having no share in the equity (as the LLP Agreement allowed for), he would have been entitled to an equal share of the equity.

Although it is now well established that the doctrine of discharge for repudiatory breach does not apply to ordinary partnerships, one of the favourite tactics of claimants in LLP disputes has been to allege that the LLP (and sometimes the other members) have committed repudiatory breaches of the LLP Agreement. That argument is advanced either to enable the claimant to assert that he or she can walk away without serving a period of notice or (more adventurously) to assert that he or she remains a member of the LLP but on terms that his or her rights are governed by the LLP default rules rather than the LLP agreement. This latter argument is advanced where the allegedly wronged member has a low profit share and would gain a financial advantage by moving to an equal share under the default rules. Until now, no claimant has actually taken this argument to a hearing and there has been no authority on the application of the repudiation doctrine to LLPs. The decision in *Flanagan v Liontrust Investment Partners LLP* [2015] EWHC 2171 (Ch) has finally answered the question: it does not, at least not in an LLP with more than two members.

The claimant (Mr Flanagan) asserted that Liontrust Investment Partners LLP (the LLP) had committed repudiatory breaches of the contract between them, which he had accepted, such that the LLP Agreement had been terminated (at least so far as he and the LLP were concerned), and he was a member subject to the default rules contained in the LLP Regulations 2001. Thus, he argued, rather than merely being entitled to receive his £125,000 annual fixed profit share and no share in the equity, he was entitled to an equal equity share in the LLP, and the LLP had lost its contractual entitlement to remove him from membership. He sought a compulsory buyout of his share pursuant to section 994 of the Companies Act 2006, and indicated that he thought his share might be worth £8m.

Henderson J considered the matter in detail and reached the conclusion that the repudiation doctrine was impliedly excluded by the LLP legislation. He noted in particular the practical difficulties that would ensue if, as suggested by the claimant, the rights and obligations of one member (or group of members) were subject to the default rules and others remained subject to the LLP Agreement: "*it is all but self-evident that the co-existence of two different contractual regimes governing the same LLP is likely to lead to results which are legally incoherent and could only be resolved by further agreement between all the members*". He held that the statutory scheme should, if reasonably possible, be construed in a way which avoids this possibility, and went on to find that the statutory scheme does implicitly exclude the common law doctrine, at least where there are more than two members.

The judge said that he was fortified in his decision by the fact that it would be *"offensive to common sense, and contrary to the reasonable commercial expectations of the parties, if the effect of the doctrine were to permit Mr Flanagan to share in the profits of the LLP on a basis of notional equality with the other members, when the LLP Agreement itself gave him only a fixed allocation of income profits and no entitlement to any capital profits".*

Lawyers acting for claimants in LLP disputes may be disappointed by the decision in Flanagan, but it is difficult to argue with Henderson J's conclusion that the application of the default rules to some but not all the members would be offensive to common sense and the expectations of the parties.

** the Judge left open the possibility that the doctrine of repudiatory breach may apply to LLPs with only two members.*

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