1963

MARY HELEN ELLIOTT and CANADA PERMANENT TORONTO GENERAL TRUST COMPANY, Executors of the last will and testament of George Andrew Elliott, deceased, (*Applicants*) ..APPELLANTS;

*Mar. 26
May 1

AND

JAMES L. WEDLAKE (*Respondent*) ....RESPONDENT.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Contracts—Partnership agreement—Annual payments by one partner in reduction of capital account of other partner—Essentials of an agreement for sale lacking—Dissolution of partnership—Distribution of Assets—The Partnerships Act, R.S.O. 1960, c. 288, s. 44.

The respondent and E who carried on business together, in partnership, as hardware merchants, entered into an agreement which terminated that partnership and was intended to form a limited partnership for the continued operation of their business. It was provided in the agreement that E would contribute $90,000 to the capital of the partnership, that the respondent would pay interest on this amount, or on such capital of E as remained in the partnership from time to time, and that the respondent would also make annual payments towards the purchase of E's share. It was further provided that in the event of E's death his personal representatives would continue the partnership. E died in 1955 and the partnership was continued by his executors (the appellants) and the respondent until 1961, when an agreement was made between the respondent and the appellants for the dissolution of the partnership and liquidation of the partnership assets by the respondent. After satisfying all outstanding liabilities, there remained on hand the sum of $36,608.99.

The appellants applied to the Court for a judgment declaring their rights in connection with this sum and also the liability of the respondent to the appellants. Their contention was that, under the terms of the agreement, the respondent had agreed to purchase from E his interest in the partnership for $90,000 of which $53,000 still remained unpaid. They claimed, therefore, that they were entitled to all the moneys realized from the partnership assets and also a personal judgment against the respondent for the amount of the difference between that amount and $53,000. Judgment on the motion was given in favour of the appellants but, on appeal, this decision was reversed. An appeal was then brought to this Court.

Held: The appeal should be dismissed.

The partnership agreement lacked the essential ingredients of an agreement for sale. The essential purpose of the agreement was to provide for a partnership, for the terms governing the partnership relation and the operation of the partnership. It provided for the gradual reduction by the respondent of the capital account to E's credit during the continuance of the partnership. There was no outright covenant by the respondent, without any reservation or limitation, to buy E's capital interest. The respondent did no more than to undertake, while the partnership lasted, to make limited annual payments in reduction of E's capital account.

*PRESENT: Cartwright, Fauteux, Abbott, Martland and Judson JJ.

1963

ELLIOTT AND CANADA PERMANENT TORONTO GENERAL TRUST CO. v. WEDLAKE

The agreement was completely silent as to the distribution of assets on dissolution and, that being so, the statutory rules governed. The appellants were entitled to no more than a proportionate interest in the distribution of assets and the proportions were to be determined in accordance with the respective capital interests of the appellants and the respondent as of the date of the dissolution of the partnership.

APPEAL from a judgment of the Court of Appeal for Ontario, reversing a judgment of Smily J. upon an application for a declaration of the rights of the parties under an agreement of partnership. Appeal dismissed.

Honourable R. L. Kellock, Q.C., for the applicants, appellants.

G. D. Finlayson, for the respondent.

The judgment of the Court was delivered by

MARTLAND J.:—The respondent and George Andrew Elliott carried on business together, in partnership, as hardware merchants, at the City of Brantford, under the terms of a partnership agreement dated October 1, 1937, until June 30, 1954. That partnership was terminated on the latter date by an agreement between them dated June 21, 1954 (hereinafter referred to as "the agreement"), the relevant portions of which provided as follows:

WHEREAS the Parties hereto have been carrying on business as hardware merchants at the City of Brantford under the name of Elliott Wedlake under the terms of an agreement of partnership dated October 1st, 1937,

AND WHEREAS the Parties hereto have agreed to terminate and dissolve the said partnership and to enter into a Limited Partnership under the provisions of the Limited Partnership Act, R.S.O. Chap. 208 on the terms and conditions hereinafter set out,

AND WHEREAS it is the intention of the parties hereto that the Party of the Second Part shall purchase the interest of the Party of the First Part in the said Limited Partnership in accordance with the terms hereinafter set forth in this agreement,

NOW THIS AGREEMENT WITNESSETH that the Parties hereto covenant and agree with each other as follows:

1. The general partnership heretofore carried on by the Parties hereto at the City of Brantford under the name of Elliott Wedlake shall be terminated on June 30th, 1954.

2. The Party of the Second Part on or before said date will pay to the Party of the First Part the sum of Twelve Thousand and Forty three Dollars and Thirteen Cents ($12,043.13), less any drawings of the Party of the First Part since the 31st of May, 1954, being the amount to the credit of the capital account of the Party of the First Part in said business in excess of $90,000 and for the amount of the value of good will and por-

tion of depreciation on fixed assets of said business agreed upon by the Parties, less drawings on account by the Party of the First Part during 1954, . . .

* * *

4. The Party of the First Part is to contribute the sum of $90,000 to the capital of the partnership as a limited partner under the provisions of the Limited Partnership Act, R.S.O. Chap. 208, and a new limited partnership to be known as Elliott Wedlake is to be formed as of the date July 1st, 1954 under the terms and conditions herein set out.

5. The limited partnership shall continue from year to year during the lifetime of the Party of the First Part, and continue thereafter subject to the conditions hereinafter contained.

6. Interest at 5% is to be paid to the Party of the First Part on said sum of $90,000 or on such capital of the Party of the First Part as may remain in the partnership from time to time, payable quarterly or as may be required, and the Party of the Second Part is also to pay the sum of Two Thousand Dollars ($2,000) on account of the purchase of the share of the Party of the First Part each year during the remainder of the lifetime of the Party of the First Part, such payments to be made on the 31st day of January in each year commencing January 31st, 1955.

7. In the event of the death of the Party of the First Part during the continuance of the partnership, the personal representatives of the Party of the First Part shall continue the partnership as limited partners on the same terms and conditions as are herein contained excepting that the Party of the Second Part shall be entitled to increase the annual payment on account of the purchase of the share of the Party of the First Part to any amount desired by him on giving the personal representatives of the Party of the First Part two (2) months' notice in writing of the amount intended to be paid by him.

8. The lease of the premises 193 Colborne Street made by the Party of the First Part to Elliott Wedlake dated the 22nd day of November, 1949, is assigned to the Limited Partnership and the Party of the First Part consents thereto and is to be amended as follows:

The Lessee is to pay one half the total municipal taxes chargeable against the said premises and the land therewith and one half of all local improvements for the remainder of the term reserved by said lease, including the whole of the year 1954.

The Party of the Second Part is to pay two per cent (2%) per annum on $90,000 or on such amount as the Party of the First Part may have invested in said partnership as of the 1st day of February in each year from time to time in addition to the interest at five per cent (5%) per annum provided by the Limited Partnership Act, such additional interest to be charged by the Party of the Second Part as rent for accounting purposes, the intention being that the Party of the First Part shall receive seven per cent (7%) on capital invested in said partnership.

9. It is agreed between the Parties hereto that the Party of the First Part shall not be entitled to any profits arising from the operation of the said business with the exception of the payments herein set forth of interest at 5% on the invested capital of the Party of the First Part and 2% increase of rent calculated on invested capital of the Party of the First Part.

Although the agreement contemplated a limited partnership, with Elliott as a limited partner, it is conceded by counsel for both parties that this was not accomplished, as

1963

ELLIOTT AND CANADA PERMANENT TORONTO GENERAL TRUST CO. v. WEDLAKE

Martland J.

there was no contribution of an actual cash payment by Elliott to the common stock, as required by s. 2 of *The Limited Partnerships Act,* R.S.O. 1950, c. 208. However, it is also similarly conceded that this does not in any way affect the outcome of these proceedings, since all creditors of the partnership were paid off in full.

Elliott died on August 6, 1955, and the appellants are the executors of his last will and testament. The partnership was continued by the appellants and the respondent, as provided for in clause 7 of the agreement. The respondent made payments to the appellants in accordance with the agreement, including payments pursuant to clauses 6 and 7 of the agreement. As a result of the payments made by the respondent pursuant to those two clauses, both before and after Elliott's death, Elliott's contribution to the capital of the partnership, which had been defined in the agreement at $90,000, had been reduced, as of January 31, 1961, to $58,000. Subsequent to that date and prior to the time these proceedings were commenced, a further $5,000 payment was made by the respondent, reducing this amount to $53,000.

Losses occurred in the operation of the partnership business. These were absorbed by the respondent, whose capital interest in the partnership was correspondingly reduced from time to time in the amount of the losses. Thus, whereas as of June 11, 1959, the respondent's capital interest was $60,292.24, this had been reduced by January 31, 1961, to $39,208.78.

On May 25, 1961, an agreement was made between the respondent and the appellants for the dissolution of the partnership and for liquidation of the partnership assets by the respondent. After satisfying all outstanding liabilities, there remained on hand the sum of $36,608.99.

The appellants applied to the Court on November 22, 1961, for a judgment declaring their rights in connection with this sum and also the liability of the respondent to the appellants. Their contention was that, under the terms of the agreement, the respondent had agreed to purchase from Elliott his interest in the partnership for $90,000, of which $53,000 still remained unpaid. They claimed, therefore, that they were entitled to all the moneys realized from the partnership assets and also a personal judgment against the respondent for the amount of the difference between that amount and $53,000.

The respondent's contention was that the proceeds of the realization of the partnership assets should be divided between the appellants and himself in proportion to the standings of their respective capital accounts as of the date of dissolution.

Judgment on the motion was given in favour of the appellants but, on appeal, the Court of Appeal unanimously reversed this decision and held in favour of the respondent. From that judgment the present appeal is brought.

Before this Court it was submitted, on behalf of the appellants, that the effect of clauses 6 and 7 of the agreement, coupled with the third recital clause, was to constitute a binding agreement by the respondent with Elliott to purchase the latter's interest in the partnership for $90,000, of which there still remained owing a sum of $53,000.

With respect to the effect of clauses 6 and 7 of the agreement, Kelly J.A., who delivered the judgment of the Court of Appeal, held as follows:

> Considered by themselves, clauses 6 and 7, in my opinion, lack the essential ingredients of an agreement for sale; there is no mutual undertaking to buy on the one hand and to sell on the other; there is no purchase price stated or capable of being determined by any means specified in the agreement; there is no obligation on the part of Wedlake to pay anything beyond the sum of $2,000 a year during the lifetime of Elliott. In my view, unless the operative parts of the agreement can be bolstered up by the words of the third recital, the agreement fails completely to be an effective agreement of sale of which the Elliott executors can enforce performance.

He then went on to consider whether this result was altered by the wording of the third recital clause and, after referring to various authorities dealing with the effect of a recital clause upon the interpretation of an agreement, he concluded as follows:

> Clauses 6 and 7 are not ambiguous in the sense that they are capable of alternative constructions to choose between which the Court may be assisted by reference to the recitals. Clauses 6 and 7 are vague in the sense that by themselves they do not support a construction which would lead to establish an enforceable contract of purchase or sale. Resort to the recitals may not be had to clear up the vagueness and to incorporate words which it would be necessary to insert in order that those clauses expressed the agreement of sale and purchase sought to be found in them by the Elliott executors.

I have reached the same conclusion as the Court of Appeal, for the following reasons. I agree entirely that clauses 6 and 7 do not spell out the essential ingredients of

1963

ELLIOTT AND CANADA PERMANENT TORONTO GENERAL TRUST CO. v. WEDLAKE

Martland J.

an agreement for sale whereby the respondent undertook, without reservation, to purchase Elliott's interest in the partnership for $90,000. The essential purpose of the agreement was to provide for a partnership, for the terms governing the partnership relation and the operation of the partnership. The effect of clauses 6 and 7, even when read in conjunction with the recital clause, which, it must be remembered, referred only to "the intention" of the parties that the respondent should purchase Elliott's interest "in accordance with the terms hereinafter set forth in this agreement", was to make provision for the gradual reduction by the respondent of the capital account to Elliott's credit during the continuance of the partnership. There is no outright covenant by the respondent, without any reservation or limitation, to buy Elliott's capital interest. The respondent did no more than to undertake, while the partnership lasted, to make limited annual payments in reduction of Elliott's capital account.

The appellants are seeking to claim a preference on dissolution for the full return of Elliott's capital and I find nothing in the agreement which so provides. It is completely silent as to the distribution of assets on dissolution and, that being so, the statutory rules must govern and the division should be made in the manner directed by the Court of Appeal.

The appellants also submitted that, even if there were no firm agreement by the respondent to purchase Elliott's interest, that the appellants had a lien on the partnership assets to the extent of the appellants' interest at the date of dissolution. This argument was based upon the proposition that under the terms of the agreement the respondent was obligated to assume all losses incurred by the partnership; that as the proceeds of realization of the partnership assets were insufficient to pay off the remaining portion of the appellants' capital interest, there had obviously been a capital loss and, consequently, for the amount of this loss the respondent was responsible to the appellants out of what otherwise would have been his share of the proceeds of the sale of the partnership assets.

I do not find anything in the agreement to justify this contention. The agreement does not, in terms, even obligate the respondent to assume operating losses. Clause 9 provided merely that Elliott should not be entitled to any

profits from the operation of the business other than the 5 per cent per annum on his invested capital and the rent in respect of the business premises calculated at 2 per cent on his invested capital. It may be implied from this provision that the respondent agreed to assume operating losses and this, in fact, he did. His own capital interest was reduced from time to time by the amount of the operating losses sustained by the business and, in consequence, the extent of his proportionate participation in the distribution of the partnership assets on dissolution was reduced. There is, however, no covenant on his part that, upon a dissolution of the partnership, the apellants should be entitled to be fully reimbursed for all moneys invested in the partnership by Elliott in priority to any participation therein by himself.

The appellants relied upon a statement of the law found in Lindley on Partnership, 12 ed., p. 383, reading as follows:

> In other words, each partner may be said to have an equitable lien on the partnership property for the purpose of having it applied in discharge of the debts of the firm; and to have a similar lien on the surplus assets for the purpose of having them applied in payment of what may be due to the partners respectively, after deducting what may be due from them, as partners, to the firm.

This proposition does not assist the appellants. The debts of the partnership were all paid off. There were no outstanding advances by Elliott to the partnership. There is no evidence that he made any such advances. What he did was to make a contribution to the capital of the partnership. There were no debts owing by the partnership to the appellants or by the respondent to the partnership. That being so, in the absence of any provision in the agreement to the contrary (and there is none), the appellants are entitled to no more than a proportionate interest in the distribution of the partnership assets, the proportions to be determined in accordance with the respective capital interests of the appellants and the respondent as of the date of the dissolution of the partnership.

In my opinion, therefore, the appeal should be dismissed with costs.

Appeal dismissed with costs.

Solicitors for the applicants, appellants: Read & Innes, Brantford.

Solicitors for the respondents: McCarthy & McCarthy, Toronto.