PLAYING WORD GAMES WITH PROFESSOR MONTROSE

From the nature of their work, lawyers acquire considerable dexterity in the manipulation of words, the discernment of fine shades of meaning and the revelation, or creation, of nice distinctions. Sometimes, the opportunity to display this semantic virtuosity seems to have an almost mesmeric effect on the lawyer, drawing him irresistibly along a tortuous route to conclusions which may lack both consistency and commonsense. It is as though a sheer delight in the display of vocabular skills, and some perverse pleasure in the anomalous, causes him to ignore the possibility of any alternative approach, lest it be too obvious and too pedestrian to need the sophistication of his skills.

An excellent example of this intellectual sleight-of-the-hand is to be found in Professor J. L. Montrose's article "Liability of Principal for Acts Exceeding Actual and Apparent Authority".[1] By the use of an unlikely example and much verbal manipulation, Professor Montrose appears to reveal a loophole in Section 5 of the Partnership Act 1890 (U.K.). Having regard to the fact that the only situation in which this loophole would be available is one which is most unlikely to arise in practice, one might have thought that this particular part of Professor Montrose's very valuable discussion of apparent authority would have remained hidden from those whose researches into the law of partnership were confined to a reading of the general texts. Not so. Such is the fascination which complex verbal analysis has for lawyers, that this rather unimportant and peripheral part of Professor Montrose's article is treated as warranting a specific reference (without dissent) in *Bowstead on Agency,*[2] Stoljar, *The Law of Agency,*[3] Powell, *The Law of Agency*[4] *Fridman's Law of Agency,*[5] *Chitty on Contract,*[6] and Higgins, *The Law of Partnership in Australia and New Zealand.*[7] Indeed, both Stoljar and Higgins do not merely refer to Professor Montrose's point; they embrace it with enthusiasm. Higgins goes so far as to assert that "Professor Montrose shows quite conclusively that there is a 'loophole'."[8] It is the belief that this comparatively wide-spread acknowledgement of the alleged loophole is entirely ill-founded which provides the writer with his excuse for joining in Professor Montrose's word game.

Section 8 of the Partnership Act 1908 is the New Zealand equivalent of the English section discussed by Professor Montrose. For

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1. (1939) 17 Can. B.R. 693.
2. 13th Ed., p. 258.
3. p. 57.
4. 2nd Ed., p. 76.
5. 2nd Ed., p. 257.
6. 23rd Ed., Vol. II, p. 69.
7. pp. 93-94.
8. *op. cit.,* p. 94.

convenience the problem will be discussed in terms of the New Zealand legislation. This makes no difference to the outcome.

Section 8 defines the apparent authority (or, as *Fridman*[9] would have it, the implied authority) of one partner to bind his firm. The relevant portion of the section reads:

> and the acts of every partner who does any act for carrying on in the usual way business of the kind carried on by the firm of which he is a member bind the firm and his partners, unless the partner so acting has in fact no authority to act for the firm in the particular matter, and the person with whom he is dealing either knows that he has no authority or does not know or believe him to be a partner.

Professor Montrose was concerned with the last qualification in this section: "and the person with whom he is dealing . . . does not know or believe him to be a partner." (This qualification will be referred to as "the proviso"). In order to confine discussion to the way in which the proviso operates it is assumed in each example given in this article that in entering into the unauthorised transaction in question, the active partner was doing "an act for carrying on in the usual way business of the kind usually carried on by the firm".

Notwithstanding dicta to the contrary in *Watteau* v. *Fenwick*,[10] the proviso makes it quite clear that a firm cannot be bound by an unauthorised transaction entered into by one of its members, unless the other party to the transaction either knew or believed the person with whom he was dealing to be a partner. Thus, if the other party believed he was dealing with a sole trader, then the firm would not be bound by an unauthorised transaction entered into by one of its members. Professor Montrose says that in this respect the draftsman of the English equivalent of our Section 8 made a deliberate attempt to preclude the law of partnership from developing anything akin to the controversial doctrine which was later to be introduced into the general law of agency by the decision in *Watteau* v. *Fenwick*.[11] He

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9. *op. cit.*, p. 94.
10. [1893] 1 Q.B. 346.
11. In that case, the defendants had bought a hotel business from one Humble. After the transfer, Humble continued on as manager of the business. His name appeared over the door of the premises and to all appearances he was still the owner of the business. Contrary to his instructions from the defendants, Humble bought from the plaintiff certain goods which were to be used in the business. The plaintiff believed Humble to be the owner of the business and did not believe himself to be giving credit to any other person. Subsequently, upon discovering that the defendants were the real owners of the business, the plaintiff sued them for the price of the goods. The Court held that the defendants were liable for all acts of their agent which were within the authority usually conferred upon an agent of his particular character, although he had never been held out by the defendants as their agent. It was no defence to show that the plaintiff did not believe that Humble was acting on behalf of someone else.

gives two examples to show that this attempt was only partially successful and then goes on to give a third which reveals the alleged loophole with which this article is concerned.

Where the firm consists of two partners only, the attempt to exclude the doctrine in *Watteau* v. *Fenwick* is successful. In Montrose's first example, Wholesaler and Retailer X are partners in a hotel business. Wholesaler is the dormant partner while Retailer X is the active partner. The business is run in the name of Retailer X and he appears to be the sole proprietor of it. The partnership agreement provides that all goods, other than bottled ales and mineral waters, will be bought from Wholesaler. Contrary to the terms of the agreement, Retailer X buys whisky on credit from Plaintiff. Plaintiff later discovers that Wholesaler is a partner in the hotel business and sues the firm for the price of the whisky. As Montrose says, the firm cannot be liable to Plaintiff because, in the express words of the Act, "the partner acting has in fact no authority to act for the firm in the particular matter and the person with whom he is dealing does not know or believe him to be a partner". This is the direct reverse of the decision made in *Watteau* v. *Fenwick* in respect of a principal and agent who were not partners, but master and servant.

Professor Montrose's second example demonstrates that in the case of a firm consisting of more than two partners, a dormant partner can be liable for the unauthorised acts of another member of the firm, even though the dormant partner was not known or believed to be a partner in the business. Wholesaler, Retailer X and Retailer Y are all partners in a hotel business. They agree that all goods, other than bottled ales and mineral waters, will be bought from Wholesaler. Wholesaler is a dormant partner while Retailer X and Retailer Y are active partners. The business is run in the names of Retailer X and Retailer Y, who appear to be the only partners in the firm. Retailer X buys some whisky on credit from Plaintiff. Plaintiff knows that Retailer Y is a partner in the business, but, it is only after the sale has been made, that he learns that Wholesaler is also a member of the firm.

In order to be consistent with the result in the first example, one would argue that since Plaintiff believed himself to be giving credit to Retailer X and Retailer Y only, it is not fair that he should later be able to hold Wholesaler liable for a transaction which Wholesaler had expressly forbidden his partners to make. As Plaintiff was not induced to give credit by the belief that he would have recourse against Wholesaler, he cannot claim that Wholesaler's invocation of the restriction imposed by the partnership agreement unfairly deprives him of a right which he believed himself to have against Wholesaler.

However, notwithstanding the force of this argument, the words of the section compel its rejection in this second example. Retailer X had done an act "for carrying on in the usual way business of the kind carried on by the firm". Accordingly, by virtue of Section 8, the

act binds the firm, including Wholesaler, even though it was done without authority. Wholesaler cannot rely on the proviso, because, although Plaintiff did not know Wholesaler was a member of the firm, it cannot be said that Plaintiff "did not know or believe Retailer X to be a partner". Plaintiff knew that Retailer X was a partner of Retailer Y and this is enough to preclude the proviso. It is sufficient that Plaintiff knows that the person with whom he is dealing is a member of a partnership. The section does not require him to know the identity of the other partners or their number. As Montrose points out, to absolve Wholesaler from liability would involve treating the section as though it included the additional words which are emphasised in the following passage:

> unless the person with whom he is dealing does not know or believe him to be a partner *of the partner whom that person is seeking to make liable.*

The rules of statutory interpretation will not, of course, permit words to be "read in" to a section in this way.

Montrose's third example is the same as his second, with one variation. Retailer X and Retailer Y act together in the purchase of the whisky. Plaintiff knows they are partners as between themselves but does not know that there is any other member in the firm. Montrose says that in this example there will be no liability on Wholesaler because the proviso requires Plaintiff to know that the firm includes some person in addition to the persons with whom he actually makes the contract.

This is the "loophole" which has been so readily accepted by Higgins and other text writers. Yet, there is a manifest anomaly in making Wholesaler liable in example two but not liable in example three. It is absurd that Wholesaler should be fixed with liability if Retailer Y waits out on the street while Retailer X goes into Plaintiff's premises in order to make the unauthorised purchase, when, by contrast, Wholesaler is exempted from liability if Retailer Y chances to accompany Retailer X when the whisky is bought from Plaintiff. Thus, one would have thought that any judge or academic writer would give the same answer to both examples unless the words of the section were so clear that they absolutely compelled him not to do so, and left no room for any alternative construction. It is surprising, therefore, to see that Montrose really offers only the very briefest justification for his interpretation, and neither he, nor the other writers who accept it, make any attempt to find an alternative interpretation which would enable example three to be resolved consistently with example two.

Because Montrose's argument in support of his own interpretation of Section 8 is expressed in such elliptical fashion, it may be worthwhile to expand the argument into a series of propositions.

1. This whole problem arises because the section is poorly drafted. It is essentially an exercise in statutory interpretation.

2. Section 4 of the Acts Interpretation Act 1924 provides than in any Act of Parliament "words importing the singular number include the plural number and words importing the plural number include the singular number".

3. Therefore, in applying Section 8 of the Partnership Act to a situation where two partners act jointly on behalf of the firm, it is legitimate to substitute the plural for the singular where it is necessary to do so in order to make the words appropriate to the situation which is being considered.

4. Adopting this approach, and leaving out words which have no bearing on the third example, Section 8 will read as follows:

> The acts of the partners (A) . . . bind their partners (B) . . . unless . . . the person with whom they are dealing . . . does not know or believe them to be partners (C).

5. The word "partners" is used three times in the section and it is clear that this word does not refer to the same partnership or the same set of partners on each occasion. Thus, it is quite clear that Partners (A) denotes a different partnership from Partners (B). Partners (A) denotes the partners who are in fact acting in this particular transaction (i.e. Retailer X and Retailer Y) but Partners (B) obviously refers to some wider group (i.e. a group which includes someone in addition to Retailer X and Retailer Y), whom the Plaintiff wishes to make liable for the acts of Retailer X and Retailer Y. If this were not so, then the section would be saying the acts of Retailer X and Retailer Y are binding upon Retailer X and Retailer Y. This would be absurd because it is obviously the purpose of the section to make liable some persons in addition to the partners who actually entered into the transaction in question.

6. Having demonstrated by reference to Partners (A) and Partners (B) that the word "partners" is used in at least two different senses (i.e. to denote two different partnerships or sets of partners), it now becomes necessary to determine the sense in which the word "partners" is used in Partners (C). Does it mean the partnership between the acting partners only (as it does in Partners (A)), or does it mean the partnership between the two actors and some other person or persons (as it does in Partners (B))? This is the essential question.

7. In determining the sense in which the word "partners" in Partners (C) is used, it is necessary to look again at the purpose or object of Section 8. The purpose or object of the section is to make some person or persons other than the actor or actors liable for the latter's transactions. The question then becomes: in deciding whether Plaintiff is to have recourse against some person other than the partners who actually negotiated the contract, is it more appropriate or significant for Plaintiff to know:

(a) What the relationship is between the actors and the other people whom the Plaintiff seeks to make liable? or

(b) What the relationship is between the two actors themselves?

Putting the question another way, is it more logical for the dormant partners to be liable:

(a) Because the Plaintiff believed the actors to be acting on behalf of some persons other than themselves? or

(b) Because the Plaintiff believed one actor to be the partner of the other actor (although he did not believe that any other person was a member of the firm)?

8. Answer (a) seems the correct one to both of the questions asked in the preceding paragraph. Plaintiff cannot make the dormant partners liable unless, at the time when he made the contract with the acting partners, he knew that there were also some dormant partners in the firm. It is of the essence of this liability that he should believe the actors to be acting on behalf of some persons in addition to themselves, i.e. he must believe himself to be giving credit to a firm which includes some persons in addition to the acting partners. He must believe them to be acting as both agents and principals, and not just as principals only.

9. Higgins says that the word "partners" in Partners (C) "cannot mean partners *inter se* because to apply that interpretation to the version in the singular would be absurd."[12] That is to say, in the first and second examples where the transaction is entered into by one partner acting on his own, then Partner (A) means the actor, Partner (B) means some person in addition to the actor and Partner (C) must also signify some person in addition to the actor. In Montrose's first two examples, where there is only one actor, Partner (C) must, by necessary implication, be read as "a partner of some other person" because obviously the actor cannot be a partner of himself. Thus,

> The acts of the actor bind the dormant partners unless the person with whom he is dealing does not know or believe him to be a partner (of some other person).

As Partner (C) (in the singular) denotes the relationship between the actor and some other person, then it is clearly inconsistent in example three to regard Partners (C) (in the plural) as referring to the relationship between the actors themselves, rather than the relationship between the actors and some other person. Accordingly, where Section 8 is applied to a case where two partners act jointly, it should read:

> The acts of the actors bind the dormant partners unless the person with whom they are dealing does not know or believe them to be partners (of some other person).

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12. *op. cit.*, p. 94.

10. If the above interpretation is not correct, then the escape clause which Section 8 deliberately provides can never be used where the transaction is entered into by two partners jointly.

There can be little room for disagreement with the first five propositions in the foregoing argument but proposition 6 is open to criticism. In his article, Montrose appears to regard Partners (C) as referring to the same group as is designated by Partners (B). However, if one looks back to example two, it becomes clear that Partners (C) is not coextensive with Partners (B). In the second example, Partners (B) (i.e. the group which is to be made liable) includes Retailer X, Retailer Y *and Wholesaler*. On the other hand, Partners (C) (i.e. the persons whom Plaintiff knows to be members of the firm) comprises only Retailer X and Retailer Y. Partners (B) refers to three persons but Partners (C) describes only two people. Thus, while proposition 6 shows that the word "partners" does not refer to the same set of partners on each occasion on which it is used in Section 8, it does not establish that Partners (C) must necessarily refer to people other than the actors. It will be submitted later that rather than equating Partners (C) with Partners (B), it may be more appropriate to regard Partners (C) as closer in meaning to Partners (A).

Propositions 7 and 8 of the argument are not mentioned by either Montrose or Higgins but they seem to be crucial steps in the reasoning. It is proposed to return to these two propositions after demonstrating that neither of the reasons advanced by Montrose and Higgins is sufficient to establish their interpretation of the section. The two reasons put forward by these writers are embodied in propositions 9 and 10.

Higgins' argument, as expanded in proposition 9, is based on the indisputable premise that in Section 8 the word Partner (C) should mean the same thing no matter how many active partners there might be. He says, again correctly, that in Montrose's first two examples, where there is only one actor, it is necessary to treat Partner (C) as referring to a relationship between the actor and some other person. Consistency requires that, in example three, where there are two active partners, Partners (C) should also be regarded as referring to a relationship between the actors and some other persons. However, Montrose and Higgins can achieve this consistency of interpretation only by sacrificing consistency of result. Thus, they both concede that it is anomalous that the result in example two should (on their own interpretation) differ from the result in example three.

In the second example it is clear that Wholesaler is liable on the unauthorised contract. Yet Plaintiff knew nothing of Wholesaler at the time when the contract was formed. Wholesaler is liable not because he was known to be a partner of Retailer X but because some other person (Retailer Y) was believed to be Retailer X's partner. If, in the second example, it is sufficient that Plaintiff knows of the partnership between Retailer X and Retailer Y, why is the Plaintiff's

knowledge of the same partnership not sufficient to fix Wholesaler with liability in example three? Why does Montrose's third example require Plaintiff to know of the relationship between Wholesaler and Retailers X and Y, when he is not required to know of it in example three?

In view of these difficulties, one can only repeat that it is surprising that Montrose and Higgins did not make some more apparent effort to find an interpretation which not only gives the same meaning to the word Partners (C) in each example but also ensures that the results which it produces in all three examples are consistent and in accordance with commonsense. An interpretation which has both of these virtues is suggested below.

Proposition 10 reproduces Montrose's contention that if his interpretation is not correct then the proviso will never operate in cases where two partners act jointly. This contention is quite correct but it does not prove that Montrose's interpretation is correct. It begs the question by assuming that the proviso ought to operate in at least some cases where two partners act jointly. There is no general presumption that a proviso must provide an escape route in every situation or even in every group of situations to which the section might otherwise apply. Indeed, Montrose himself, accepts that the proviso does not operate in example two. Why then does he believe that it must, as a matter of logical necessity, apply in example three? Even if the proviso does not apply to either example two or example three, it will not be rendered inoperative. It will still operate in respect of example one. Whether or not the proviso ought to apply to any given situation or group of situations in addition to the basic situation described in example one, must depend upon the purpose or object of Section 8. This brings the discussion back to propositions 7 and 8. A consideration of these propositions will show that it is by no means inconsistent with the object of Section 8 to say that the proviso does not operate in cases where there are two active partners.

Neither Montrose nor Higgins discuss propositions 7 and 8, which deal with the purpose or object of Section 8. To support Montrose's interpretation, it is argued in these propositions that the purpose of the section is to make some persons other than the actors liable. For this purpose, it is not important for Plaintiff to know the relationship between the actors themselves. It is, however, important for him to know of the relationship between the actors and some of the persons whom it is sought to make liable on the unauthorised contract made by the actors.

It is notoriously difficult to discern the object of a statutory provision. Either there is no readily apparent object or else there is a proliferation of possible objects, from which each of the opposing parties may choose the one best calculated to support his own cause. The object which propositions 7 and 8 suggest for Section 8 of the Partnership Act is one which is quite tenable in the abstract. Neverthe-

less, an acceptance of this object causes example three to be resolved inconsistently with example two. This makes it desirable to see if the section might have some other object.

An alternative object becomes apparent when it is realised that Montrose's phrase "Partners (B)" is a contraction of the words actually used in the section. He omits the words which are emphasised in the following extract from the section:

> the acts of every partner . . . bind *the firm and* his partners . . .

Montrose is probably correct to treat the words "the firm" as mere surplusage. Since the firm is not a separate entity, anything which binds the firm necessarily binds the partners.[13] The Act seems to treat phrases such as "bind the firm" and phrases such as "bind the partners" as more or less interchangeable. Sections 8 and 9 use both phrases. On the other hand, Sections 10, 11, 13, 14, 18 and 19 talk only of "the firm", without adding "and the partners". Finally, Section 16 talks of liability in terms of the partners, without mentioning the firm. There appears to be no real significance in the fact that sometimes both phrases are used while in other cases only one of them is used.

In any case, it is no longer necessary to say that the purpose of the section is to define the circumstances in which some persons other than the actors will be liable on unauthorised transactions. As an alternative, it is possible to ascribe to the section the object of defining the circumstances in which a firm will be liable for the unauthorised acts of some of its members. Since the object of the section is to make the firm liable, the essential thing which the Plaintiff must know is that he is giving credit to a firm, rather than to an individual. On this basis, it is possible to modify Montrose's formulation in the following way:

> the acts of a member of a firm (i.e. Partner (A)) . . . bind the firm (i.e. Partners (B)) . . . unless . . . the person with whom he is dealing . . . does not know or believe him to be a member of a firm (i.e. Partner (C)).

Not only does the new formulation share with Montrose's interpretation the virtue of enabling the same meaning to be given to Partners (C) in every factual situation, but it also has the additional virtue of producing a consistent result in every case. Thus, under the new formulation, Wholesaler is liable on the unauthorised contract in example three, just as he is in example two. The reason that Wholesaler cannot invoke the proviso in order to escape liability in example three is that Plaintiff knows that he is giving credit to a firm. He knows this because he realises that the persons with whom he is dealing (i.e. Retailer X and Retailer Y) are partners as between themselves.

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13. See e.g. *Bishop* v. *Chung Bros.* (1907) 4 C.L.R. 1262, a decision relating to the criminal liability created by Section 13.

It cannot be suggested that the new formulation enables all examples to be resolved in a way that is satisfactory to all. For example, those who are opposed to the decision in *Watteau* v. *Fenwick* may find the new formulation even more objectionable than Montrose's, in that Wholesaler is now liable in example three as well as in example two, even though in neither case was Plaintiff induced to give credit to the active partner or partners by the expectation that he would have recourse against Wholesaler. It may well be doubted whether this was the intention of either Parliament or the draftsman. The fact remains that, as Montrose conclusively demonstrates, Wholesaler is liable in example two even though Plaintiff did not know of him. It is submitted that, however unjust this result may be, the wording of the section leaves the Court no option but to recognise it. Since the Court is committed to this result, in example two, it is likely that it would seek to resolve example three in a way which was consistent with the earlier example. It is most unlikely that the Court would feel that it was free in example three to mitigate the injustice which the very words used by Parliament cause in example two. In this situation the desire for consistency, which need be nothing less noble than a desire not to make a mockery of the section, must prevail over the desire to do justice in the individual case. To attempt to do individual justice would be to repudiate the theory that the Courts must assume that Parliament means what it says.

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