



# Partnership agreements: A primer

## Corporate Update

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So you and your partners want to run a business together, and have decided to enter into a partnership - what next? The first step is the preparation of a partnership agreement. Partnership agreements allow you and your partners to agree in advance how you will handle different issues that may arise in starting and running your business and manage your relationship. In a separate article, we explored the different types of partnership. In this installment, we review partnership agreements and discuss key items that are typically addressed in these agreements.

In most Canadian jurisdictions, a partnership can be formed without a written agreement between the partners. However, this is not recommended, especially when forming a limited partnership or a limited liability partnership, as a written agreement among the partners will ensure that all partners are on the same page. Similar to the articles, bylaws, and shareholder agreements of corporations, partnership agreements are the governing documents of most partnerships, and deal with important matters such as the rights, responsibilities and liabilities of each partner, the management of the partnership and its business, contributions of the partners, distribution of profits, handling of disputes, and dissolution and winding-up of the partnership.

## 1. Partnership laws apply by default

The partnership laws of the province or territory in which the partnership is formed will apply to the partnership. Partnership laws contain standard provisions that may not be suitable to every partnership. Partnership agreements allow partnerships to modify certain aspects of those standard provisions to ensure that the structure works for

you and your specific situation. To the extent that a partnership agreement does not address such provisions, the applicable partnership law will apply by default.

In respect of limited partnership agreements, it is important that the partnership agreement does not endanger the limited liability status of limited partners, i.e., by providing for participation in the management and control of the partnership. The partnership agreement should clearly allocate those responsibilities to the general partner or general partners.

## 2. Written vs oral agreements

General partnerships may be formed without a written agreement in most Canadian jurisdictions (in Quebec, a written agreement is required), as long as the partners are in agreement to carry on business in common with a view to profit. However, without a written agreement, the rights and obligations of the partners may be unclear and subject to debate and disagreement when things go wrong.

In the case of a limited partnership, the partners are required to file a certificate or a declaration with the corporate registry which contains certain details about the partnership, including the name of the general partner, the term of the partnership, and the amount of contribution of limited partners. However, there are several other matters that need to be agreed upon between the general partner and the limited partners in order to ensure that the business of the partnership is run smoothly and the rights and the investment of limited partners are protected. A written agreement, as opposed to an oral agreement, is proof of what the partners agreed upon, and is strongly recommended so that the rights and obligations of all of the partners are clear.

## 3. Privacy

Partnership agreements are not required to be filed with the corporate registry in any jurisdiction and accordingly the contents of the agreements (to the extent they are not disclosed in the declaration of partnership) are private. However, in certain jurisdictions, including Alberta, a partnership formed outside of the jurisdiction will be required to file a copy of the partnership agreement with the corporate registry if the partnership wishes to extra-provincially register in the jurisdiction. Copies of such agreements may be obtained by any person.

## 4. Key provisions of partnership agreements

Partnership agreements typically address the following questions, among others:

- *Management of the business:* Who will manage the day-to-day business of the partnership? By law, each partner can act on behalf of the partnership, and any action taken by a partner is binding on all other partners. Therefore, it is critical to clearly define the role of each partner. In a general partnership, the partners may agree that one partner is the managing partner. In a limited partnership, the general partner is responsible for management of the business, although the limited partners may participate in certain fundamental decisions outside of the ordinary course of business, such as the purchase or sale of significant partnership assets, borrowing or lending significant amounts of money, issuance of equity in the partnership, or the winding up or dissolution of the partnership. In limited partnership agreements, the authority and powers of the general partner are described in detail. Such agreements may also contain a limited power of attorney granted by the limited partners to the general partner.
- *Decision making:* How will the partnership make crucial decisions? While the general partner in a limited partnership and a managing partner, if appointed by a general partnership, will generally make day-to-day business decisions, the partners still need to make fundamental decisions such as entering into a new business, taking on significant amount of debt, lending money to someone or dissolving the partnership. It is important to decide how these matters should be approved - by simple majority (i.e., more than 50%), super majority (a 66% or 75% majority) or unanimous approval (100% approval). Partnership agreements may also contain provisions on how meetings of the partnership will be conducted.
- *Capital contributions:* What contributions will each of the partners be expected to make (including initial contributions and subsequent contributions), and what form will those contributions take (e.g., cash, other assets)? What are the consequences if a partner fails to make contributions as required by the agreement?
- *Allocations of profits and losses:* How are profits and losses to be allocated amongst the partners? The default

position under partnership laws is that all partners share equally in the profits and must contribute equally to the losses, however the partnership agreement may provide for special allocation ratios.

- *New partners*: How can new partners be admitted (if new partners are permitted)? Partnership agreements typically provide that new partners must agree to be bound by the partnership agreement. Requirements for new partners to contribute capital, and how the calculation of profit and loss may be affected by the introduction of new partners, should be addressed in the agreement.
- *Expulsion of partners*: Can partners be expelled in certain situations? Partnership agreements should address if and when a partner can be expelled or forcibly removed. This can occur if the partner commits a default under the partnership agreement, refuses to make his or her contributions, acts in a way that damages the partnership's business, discloses the partnership's confidential information, etc.
- *Reporting / financial statements*: Is the partnership required to provide financial statements on a quarterly or annual basis to the partners? Must the financial statements be audited? For limited partnerships that are publicly traded, requirements for audited financial statements and their disclosure are dictated by applicable securities laws.
- *Disputes*: How are disputes amongst the partners to be handled? Can a partner sue the partnership or other partners in court, or are they required to address the matter by way of mediation or arbitration?
- *Non-competition and non-solicitation*: Should outgoing partners be prohibited from participating in businesses that compete with the business of the partnership, or from hiring personnel of the partnership for a competing business?
- *Restrictions on assignment of partnership interest*: What are the procedures if a partner wishes to sell his or her partnership interest to a third party? Will the other partners have a right of first refusal to purchase such interests?
- *Dissolution and winding up*: Are there any special circumstances under which the partnership should automatically dissolve (e.g., loss of a regulatory approval, insolvency or bankruptcy of a certain partner, sale of a certain asset)? Under what circumstances should a partner be entitled to terminate the partnership (e.g., change of control, breach of the agreement)? What are the procedures for payment of the liabilities of the partnership and distribution of the remaining assets of the partnership amongst the partners?
- *Fees and costs of the partnership*: How will the various fees and costs of the partnership be allocated amongst the partners?

## Conclusion

Prior to entering into a partnership, you should discuss with your potential partners and agree on important issues relating to the management of the business of the partnership. A well-drafted partnership agreement, prepared with the advice of legal counsel, will serve as a guideline for you and your partners as you launch and navigate your business going forward, and will allow you to focus on your business rather than resolving partnership issues.

This article provides only general information about legal issues and developments, and is not intended to provide specific legal advice. Please see our [disclaimer](#) for more details.

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