Contracting Out of Partnership

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Can parties contract out of the general partnership form of business organization, even if their conduct would otherwise establish a partnership? Although a recent judicial decision suggests that they can, treating contractual disclaimers of partnership as dispositive is inconsistent with modern statutes. More importantly, permitting parties to contract out of partnership imposes substantial costs by undermining the protections of fiduciary duty, creating uncertainty about the operating rules for the business, and threatening to deny the rights of third parties. These costs outweigh the benefits of promoting freedom of contract and providing certainty on the partnership formation question, particularly because such benefits can largely be captured within existing partnership and LLC law.

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I. INTRODUCTION

"Mere words will not blind us to realities. Statements that no partnership is intended are not conclusive. If as a whole a contract contemplates an association of two or more persons to carry on as co-owners a business for profit, a partnership there is."[1]

"In other words, a duck which is called a horse does not become a horse; a duck is a duck."[2]

The general partnership serves as the "default" or "residual" form of co-owned, for-profit business organization in this country.[3] If two or more persons associate to carry on as co-owners a business for profit, and if they choose not to organize as a corporation, limited liability company, or other entity that requires a state filing for its creation, a general partnership has been formed.[4] This state of affairs existed under the 1914 Uniform Partnership Act, and it has been carried forward in the uniform partnership statutes that are prevalent today.[5]

In determining whether two or more persons have associated to carry on as co-owners a business for profit—i.e., in determining whether a general partnership has been formed—the parties' conduct is of paramount importance.[6] By contrast, the parties' subjective intent to be characterized (or not characterized) as partners is of little relevance.[7] Indeed, modern

1. Martin v. Peyton, 158 N.E. 77, 78 (N.Y. 1927).
2. City of Corpus Christi v. Bayfront Assocs., Ltd., 814 S.W.2d 98, 109 n.4 (Tex. App. 1991).
3. *See infra* notes 20–24 and accompanying text.
4. *See infra* notes 20–24 and accompanying text.
5. *See* UNIF. P'SHIP ACT § 6 (UNIF. L. COMM'N 1914); REV. UNIF. P'SHIP ACT § 202(a)–(b) (UNIF. L. COMM'N 1997) [hereinafter RUPA]; REV. UNIF. P'SHIP ACT § 202(a)–(b) (UNIF. L. COMM'N 1997) (amended 2013) [hereinafter RUPA (2013)].
6. *See infra* notes 25–32 and accompanying text.
7. *See infra* notes 28–32 and accompanying text.

partnership statutes state that "the association of two or more persons to carry on as co-owners a business for profit forms a partnership, *whether or not the persons intend to form a partnership*."[8] If the parties' actions demonstrate that they have, in fact, associated as co-owners in a for-profit business, a partnership is formed, even if the parties expressly deny that they are partners.[9] Stated differently, denying that a conduct-based partnership is a partnership is just as ineffective as denying that a duck is a duck.

Or so it seemed. In the 2020 decision of *Energy Transfer Partners, L.P. v. Enterprise Products Partners, L.P.*,[10] the Supreme Court of Texas effectively concluded that, as between themselves, parties could avoid a partnership characterization by simply agreeing not to be partners, even if their conduct would otherwise meet the statutory definition.[11] Moreover, because the court relied primarily on general freedom of contract concepts, its holding could easily be replicated in other jurisdictions.[12] As a consequence, the issue raised by the *Enterprise* court—whether disclaimers of partnership should be dispositive in disputes between the parties themselves—is far more than a Texas issue. It is a critical matter of national partnership law that has the potential to upend well-accepted doctrinal and policy principles.

This Article argues that allowing parties to contract out of partnership is inconsistent with modern statutes. More importantly, the Article concludes that the costs of permitting parties to contract out of partnership outweigh the benefits, particularly when much of the benefit of allowing dispositive disclaimers of partnership can be captured without the need to alter established principles of partnership formation.

Part II of this Article presents an overview of partnership formation and its totality-of the-circumstances focus on the parties' conduct rather than subjective intent. Part III provides more detail on the *Enterprise* decision and its uneasy fit with the uniform partnership statutes that are prevalent today. Part IV examines the costs and benefits of allowing parties to contract out of partnership. With respect to costs, permitting parties to enter into dispositive disclaimers of partnership undermines the protections of fiduciary duty and creates uncertainty about the operating rules for the business. In addition, although the *Enterprise* court purported to limit its holding to disputes between the alleged partners themselves, the decision nevertheless threatens the rights of third persons who did not agree to any disclaimer. With respect to benefits, allowing parties to contract out of partnership promotes freedom of contract and brings more certainty to the partnership formation inquiry.

Part V weighs the costs and benefits of permitting parties to contract out of partnership. It argues that the benefits of freedom of contract and certainty on partnership formation mainly boil down to the parties' desire to control their fiduciary duty exposure—a desire that can largely be accommodated within the existing general partnership setting. That desire can also be accommodated to an even greater degree beyond the general partnership setting, if the parties so choose, by forming a limited liability company in a

8. RUPA § 202(a) (emphasis added); *accord* RUPA (2013) § 202(a).

9. *See infra* notes 25–32 and accompanying text. As mentioned, this assumes that the parties have not otherwise chosen to form an entity that requires a state filing for its creation. *See supra* text accompanying note 4; *infra* notes 20–24 and accompanying text.

10. 593 S.W.3d 732 (Tex. 2020).

11. *See infra* Part III(A).

12. *See infra* notes 73–78 and accompanying text.

jurisdiction that permits the elimination of fiduciary duties. Under either option, what the parties really want can be accomplished without having to incur the substantial costs of permitting dispositive disclaimers of partnership.

II. PARTNERSHIP FORMATION: AN OVERVIEW

The law governing general partnerships is largely derived from statute. The National Conference of Commissioners on Uniform State Laws (NCCUSL)[13] promulgated the Uniform Partnership Act (UPA) in 1914.[14] With the exception of Louisiana, UPA was adopted in every state.[15] In 1997, NCCUSL concluded a process of revising UPA, and the final act became known as the Revised Uniform Partnership Act (RUPA).[16] From 2009–2013, NCCUSL worked to harmonize, to the extent possible, all of the uniform acts that addressed unincorporated business organizations. That effort resulted in the promulgation of an amended version of RUPA (RUPA (2013)).[17] As of this writing, thirty-five states have adopted RUPA, and four states (and the District of Columbia) have adopted RUPA (2013).[18] Thus, some version of RUPA governs partnerships in most of the jurisdictions in this country.[19]

The general partnership is unique among business organizations with two or more owners because its formation does not require a public filing with the state.[20] RUPA § 202(a) indicates that "the association of two or more persons to carry on as co-owners a business for profit forms a partnership, whether or not the persons intend to form a partnership."[21] Partnership, therefore, has a legal definition (provided by statute), and a partnership is formed when the parties' actions meet this definition. Although other business organizations, such as corporations and limited liability companies, could also be described as co-owned businesses for profit,[22] such "filing entities" are explicitly excluded from the partnership definition.[23] Thus, the general partnership has been characterized as the "default" or "residual" form of co-owned, for-profit business organization.[24] If such a business does not organize as a filing entity, it is a general partnership and will be governed

13. NCCUSL is also known as the Uniform Law Commission. *About Us*, UNIF. L. COMM'N, https://www.uniformlaws.org/aboutulc/overview [https://perma.cc/AA3R-V3K2].

14. *See* JONATHAN R. MACEY & DOUGLAS K. MOLL, THE LAW OF BUSINESS ORGANIZATIONS 33 (14th ed. 2020).

15. *See id.*

16. *See id.*

17. *See id.*

18. *See id.*

19. Because of the prevalence of RUPA and RUPA (2013), this Article will primarily cite and discuss those statutes rather than UPA.

20. *See* CHRISTINE HURT, D. GORDON SMITH, ALAN R. BROMBERG & LARRY E. RIBSTEIN, BROMBERG & RIBSTEIN ON PARTNERSHIP § 2.01[A], at 2-5 (2d ed. 2019) [hereinafter BROMBERG & RIBSTEIN] ("Unlike a corporation or other limited liability entity, a general partnership may be formed without a public filing.").

21. RUPA § 202(a); *accord* RUPA (2013) § 202(a); *see also* RUPA § 101(6) (defining a "partnership" as "an association of two or more persons to carry on as co-owners a business for profit formed under Section 202, predecessor law, or comparable law of another jurisdiction"); RUPA (2013) § 102(11) (substantially the same).

22. This assumes, of course, that the corporation or LLC has more than one owner.

23. *See* RUPA § 202(b) ("An association formed under a statute other than this [Act], a predecessor statute, or a comparable statute of another jurisdiction is not a partnership under this [Act]."); *accord* RUPA (2013) § 202(b).

24. *See infra* text accompanying note 175.

by the jurisdiction's general partnership statute.

Traditionally, the most important factors in determining whether the legal definition of partnership has been met—i.e., in determining whether parties have "associate[ed] . . . to carry on as co-owners a business for profit"—are the sharing of profits and control. As explained by the comment to RUPA (2013) § 202(a):

> Consistent with the common law and UPA (1914), under this act "co-ownership" is a key concept. Ownership involves the power of ultimate control (albeit a power that can be substantially diminished by agreement) and a right to share in the profits of the co-owned business. To state that partners are co-owners of a business is to state that: (i) they share in the profits (if any) of the enterprise; and (ii) *ab initio* at least, they collectively have the power of ultimate control.[25]

Other factors that courts have found relevant to the partnership determination include sharing losses of the business, contributing money or property to the business, and any other evidence that is typically associated with ownership.[26] Partnership formation is considered to be a totality-of-the-circumstances inquiry; thus, if a court concludes that sufficient evidence exists of these factual predicates, the legal definition of partnership is met.[27]

Significantly, so long as the parties' conduct falls within the statutory definition, a general partnership is created, even if the partners do not realize that they are forming such an enterprise, and even if they specifically disclaim that they are partners.[28] Put differently, while it is often stated that the intent of the parties is critical to the question of whether a partnership has been formed, the intent that matters is the intent to do the things that meet the legal definition of partnership—not the parties' subjective intent to be characterized (or not characterized) as "partners."[29] As one court explained:

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25. RUPA (2013) § 202(a) cmt.; *see, e.g.*, Westside Wrecker Serv., Inc. v. Skafi, 361 S.W.3d 153, 166 (Tex. App. 2011) ("Shared rights to profits and to control the business are generally considered the most important factors in establishing the existence of a partnership."); *see also* BROMBERG & RIBSTEIN, *supra* note 20, § 2.06[A], at 2-69 ("Profit sharing is probably the most important element in the case law and has been singled out for a special statutory presumption. Control is also important . . . .").

26. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 20, § 2.14[A], at 2-175 (listing profit sharing, control sharing, loss sharing, contribution, and co-ownership of property as relevant factors in the determination of partnership); *see also* ALAN DONN, ROBERT W. HILLMAN & DONALD J. WEIDNER, THE REVISED UNIFORM PARTNERSHIP ACT § 202, at 133 (2019–2020 ed.) ("The essential factors found in a 'pure' partnership are those that indicate co-ownership of a business, including the voluntary sharing of contributions, profits, losses, authority and control, not necessarily equally, with representations to others persuasive but not required." (footnotes omitted)).

27. *See, e.g.*, Ingram v. Deere, 288 S.W.3d 886, 903–04 (Tex. 2009) (stating that "[w]hether a partnership exists must be determined by an examination of the totality of the circumstances," and observing that "[m]any states apply this totality-of-the-circumstances test"); *see also* Eggleston v. Eggleston, 47 S.E.2d 243, 247 (N.C. 1948) ("Partnership is a legal concept, but the determination of the existence or not of a partnership . . . involves inferences drawn from an analysis of all the circumstances attendant on its creation and operation." (internal quotations omitted)).

28. *See, e.g.*, MACEY & MOLL, *supra* note 14, at 34; *infra* notes 29–31 and accompanying text.

29. *See, e.g.*, Hilco Prop. Servs., Inc. v. United States, 929 F. Supp. 526, 536–37 (D.N.H. 1996) ("The conduct of the parties and the circumstances surrounding their relationship and transactions control the factual question of whether a partnership existed . . . . And although the question of intent is a crucial part of the calculus, the only necessary intent . . . is an intent to do those things which constitute a partnership." (internal quotation

> The statutory language is devoid of any requirement that the individuals have the subjective intent to create a partnership. Stated more plainly, the statute does not require partners to be aware of their status as "partners" in order to have a legal partnership. . . . Thus, one analyzes whether the parties acted as partners, not whether they subjectively intended to create, or not to create, a partnership.[30]

The comment to RUPA (2013) § 202(a) expresses similar sentiments:

> [RUPA] added, "whether or not the persons intend to form a partnership" to the UPA (1914) formulation, thereby codifying a rule uniformly applied by courts: Subjective intent to create the legal relationship of "partnership" is irrelevant. What matters is the intent *vel non* to establish the business relationship that the law labels a "partnership." Thus, a disclaimer of partnership status is ineffective to the extent the parties' intended arrangements meet the criteria stated in this subsection.[31]

As these authorities reveal, the legal definition of partnership cannot be circumvented by the parties' agreement that a partnership has not been formed or, similarly, that they are not to be characterized as partners. So long as the parties' actions fall within the statutory definition (based on a totality-of-the-circumstances inquiry), a partnership has been formed and the parties are partners, regardless of their subjective desires.[32]

III. THE ENTERPRISE DECISION

A. Summary

ETP and Enterprise were competitors that were among the ten largest energy companies in the United States.[33] In March of 2011, the companies agreed to explore the viability of a project that would convert a natural gas pipeline into one that could transport oil and would extend the pipeline from the Dallas, Texas area to Cushing, Oklahoma.[34] The so-called "Double E" project would result in a pipeline that could transport oil from Cushing to the Texas Gulf Coast. Such a project "would require a massive investment from

omitted)); *infra* notes 30–31 and accompanying text.

30. Byker v. Mannes, 641 N.W.2d 210, 215–16 (Mich. 2002).

31. RUPA (2013) § 202 cmt.; *see* RUPA § 202 cmt. 1 ("The addition of the phrase, 'whether or not the persons intend to form a partnership,' merely codifies the universal judicial construction of UPA Section 6(1) that a partnership is created by the association of persons whose intent is to carry on as co-owners a business for profit, regardless of their subjective intention to be 'partners.' Indeed, they may inadvertently create a partnership despite their expressed subjective intention not to do so.").

32. This is not to say that the parties' subjective intent is irrelevant. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 20, § 2.14, at 2-174 (noting that "[t]he elements of partnership can be broken down into two general categories: subjective partnership intent and the objective indicia of partnership"). Given the statutory language "whether or not the persons intend to form a partnership" and the interpretive comments, however, the parties' subjective intent should be of minimal relevance, particularly when their actions contravene that intent. *See supra* notes 28–31 and accompanying text; *infra* note 160 and accompanying text (stating that "in a close case where the evidence for and against the existence of a partnership is mixed, such evidence [of the parties' subjective intent to avoid partnership] might tip the scales").

33. *See* Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P., 593 S.W.3d 732, 734 (Tex. 2020).

34. *See id.*

the parties and committed customers willing to pay a sufficient tariff to justify the investment."[35]

The parties signed three written agreements in March and April of 2011—a Confidentiality Agreement, a Letter Agreement (with an attached "Non-Binding Term Sheet"), and a Reimbursement Agreement.[36] According to the court, in these three written agreements, the parties "reiterated their intent that neither party be bound to proceed until each company's board of directors had approved the execution of a formal contract."[37] The language of the Letter Agreement is representative:

> Neither this letter nor the JV Term Sheet create any binding or enforceable obligations between the Parties and, except for the Confidentiality Agreement . . . , no binding or enforceable obligations shall exist between the Parties with respect to the Transaction unless and until the Parties have received their respective board approvals and definitive agreements memorializing the terms and conditions of the Transaction have been negotiated, executed and delivered by both of the Parties. Unless and until such definitive agreements are executed and delivered by both of the Parties, either [Enterprise] or ETP, for any reason, may depart from or terminate the negotiations with respect to the Transaction at any time without any liability or obligation to the other, whether arising in contract, tort, strict liability or otherwise.[38]

New interstate pipelines are subject to a Federal Energy Regulatory Commission rule that "requires an 'open season' of 30 to 45 days in which shippers are asked to commit to daily barrel volumes and tariffs."[39] For the Double E pipeline project to be viable, ETP and Enterprise needed shipping commitments of at least 250,000 barrels a day for ten years at a tariff of $3.00 per barrel.[40] The initial open season was unsuccessful, and it was extended twice. On August 12, 2011, the last day of the second extended open season, Chesapeake Energy Corporation committed to shipping 100,000 barrels daily. ETP was hopeful that Chesapeake's commitment would attract other shippers, but by that point, Enterprise had begun preparing to exit the project.[41]

After ending its relationship with ETP orally on August 15, 2011, and in writing a few days later, Enterprise moved forward with another party, Enbridge, on a project that would use a different pipeline to move oil from Cushing to the Texas Gulf Coast.[42] They eventually obtained an anchor shipper commitment from Chesapeake, which resulted in the securing of many additional commitments during their open season. Their new pipeline, named "Wrangler," opened in June 2012, and it was a financial success.[43]

ETP sued Enterprise. Despite the disclaimers in the parties' written agreements, ETP argued at trial that the parties' conduct had formed a partnership to "market and pursue" a

35. *Id.*
36. *See id.* at 734–35.
37. *Id.* at 734.
38. *Enterprise*, 593 S.W.3d at 735.
39. *Id.* at 736.
40. *See id.*
41. *See id.*
42. *See id.*
43. *See Enterprise*, 593 S.W.3d. at 736.

pipeline. It further argued that Enterprise, as a partner, had breached its duty of loyalty by pursuing the Wrangler project with Enbridge. The jury agreed that a partnership had been formed and a judgment was ultimately entered against Enterprise for a total of $535,794,777.40 plus prejudgment interest.[44]

The Dallas Court of Appeals reversed and rendered judgment for Enterprise. The court concluded that the Texas Business Organizations Code (TBOC) allowed parties to contract for conditions precedent to partnership formation, and that two conditions precedent—board approvals and definitive agreements—had not been met.[45] Moreover, it concluded that ETP had the burden "either to obtain a jury finding that the conditions were waived or to prove waiver conclusively, which it failed to do."[46]

The Supreme Court of Texas affirmed the judgment of the court of appeals. It framed the issue as "whether Texas law permits parties to conclusively agree that, as between themselves, no partnership will exist unless certain conditions are satisfied."[47] The court began its analysis by citing two Texas statutory provisions that address partnership formation. The first, TBOC § 152.051(b), is analogous to RUPA § 202(a). It states, in relevant part, that "an association of two or more persons to carry on a business for profit as owners creates a partnership, regardless of whether . . . the persons intend to create a partnership."[48] The second provision, TBOC § 152.052(a), does not have an analog in RUPA. It provides the following:

> (a) Factors indicating that persons have created a partnership include the persons':
>
> (1) receipt or right to receive a share of profits of the business;
>
> (2) expression of an intent to be partners in the business;
>
> (3) participation or right to participate in control of the business;
>
> (4) agreement to share or sharing:
>
> (A) losses of the business; or
>
> (B) liability for claims by third parties against the business; and
>
> (5) agreement to contribute or contributing money or property to the business.[49]

The court also cited a third provision, TBOC § 152.003, which is analogous to RUPA § 104. It provides that "[t]he principles of law and equity and the other partnership provisions supplement this chapter unless otherwise provided by this chapter or the other partnership provisions."[50]

ETP argued that the TBOC's totality-of-the-circumstances test in § 152.052(a)

44. *See id.*

45. *See id.*

46. *Id.* at 736–37.

47. *Id.* at 734. In two other places, the court suggested that the holding was limited to disputes between the alleged partners themselves. *See infra* text accompanying notes 128–30. Whether the holding can be limited in that manner is discussed in Part IV(A)(3).

48. TEX. BUS. ORGS. CODE § 152.051(b); *see Enterprise*, 593 S.W.3d at 737; RUPA § 202(a).

49. TEX. BUS. ORGS. CODE § 152.052(a); *see Enterprise*, 593 S.W.3d at 737.

50. TEX. BUS. ORGS. CODE § 152.003; *see Enterprise*, 593 S.W.3d at 737; RUPA § 104.

controlled partnership formation to the exclusion of the common law.[51] More importantly, it argued that a condition precedent to partnership formation is simply one factor to be weighed—"expression of an intent to be partners in the business"—along with the others in § 152.052(a).[52] In response, Enterprise emphasized freedom of contract and argued that "if parties cannot by contract protect themselves from the creation of an unwanted partnership, detrimental economic consequences to the State and constant litigation will ensue."[53] The court sided with Enterprise:

> We maintain our view expressed a decade ago in *Ingram* [*v. Deere*, 288 S.W.3d 886, 898 (Tex. 2009),] that the Legislature did not "intend[] to spring surprise or accidental partnerships" on parties. Section 152.003 expressly authorizes supplementation of the partnership-formation rules of Chapter 152 with "principles of law and equity" . . . and perhaps no principle of law is as deeply engrained in Texas jurisprudence as freedom of contract. We hold that parties can contract for conditions precedent to preclude the unintentional formation of a partnership under Chapter 152 and that, as a matter of law, they did so here.[54]

The court acknowledged that performance of a condition precedent could be waived, but it concluded that evidence of traditional partnership factors, such as the sharing of profits and control, were not relevant to the waiver inquiry:

> [W]here waiver of a condition precedent to partnership formation is at issue, only evidence directly tied to the condition precedent is relevant. Evidence that would be probative of expression of intent under § 152.05[2](a)—such as "the parties' statements that they are partners, one party holding the other party out as a partner on the business's letterhead or name plate, or in a signed partnership agreement"—is not relevant. *Nor is evidence that would be probative of any of the other § 152.052(a) factors*. Otherwise, a party in ETP's position could claim waiver in virtually every case.
>
> ETP has not pointed to any evidence that Enterprise specifically disavowed the Letter Agreement's requirement of definitive, board-of-directors-approved agreements or that Enterprise intentionally acted inconsistently with that requirement[55] . . . The only record evidence that ETP points to—the parties held themselves out as partners and worked closely together on

51. *See Enterprise*, 593 S.W.3d at 740.

52. *See id.*; *see also infra* note 59 (discussing TBOC § 152.052(a) and its factor-balancing inquiry).

53. *Enterprise*, 593 S.W.3d at 740.

54. *Id.* The court's citation to *Ingram* regarding surprise or accidental partnerships is misleading. *See infra* note 177.

55. It is difficult to reconcile (a) the court's acknowledgment that waiver can be shown by Enterprise intentionally acting inconsistently with the requirement of definitive, board-approved agreements, and (b) the court's statement that evidence of the § 152.052(a) factors is not relevant to the question of "waiver of a condition precedent to partnership formation." How would Enterprise "intentionally act[] inconsistently" with the requirement of definitive, board-approved agreements before partnership formation? Presumably it would require evidence that Enterprise was acting like a partner—i.e., sharing profits, losses, and control—even without definitive, board-approved agreements. According to the court, however, that evidence is not relevant.

> the Double E project—is not relevant to the issue of waiver of definitive, board-approved agreements.
>
> We hold that parties can conclusively negate the formation of a partnership under Chapter 152 of the TBOC through contractual conditions precedent. ETP and Enterprise did so as a matter of law here, and there is no evidence that Enterprise waived the conditions. The judgment of the court of appeals is affirmed.[56]

B. Implications

1. Partnership Formation as a "Default Test"

As mentioned, partnership has a legal definition—"the association of two or more persons to carry on as co-owners a business for profit."[57] That legal definition implicates factual predicates (such as the sharing of profits) which determine whether the definition has been met. So long as there is sufficient evidence of these factual predicates, a partnership has been formed, regardless of the subjective intent of the parties. Put differently, so long as the parties' actions fall within the statutory definition (based on a totality-of-the-circumstances inquiry), the formation of a partnership is a mandatory conclusion.[58]

The holding of the *Enterprise* court dramatically changes the analysis. Instead of a legal definition that, if met, gives rise to a mandatory conclusion of partnership formation, partnership is now a legal definition that, if met, gives rise to a default conclusion of partnership formation—a conclusion that can be circumvented by the parties' agreement.[59] Indeed, in two places, the court phrased the issue as whether the parties could use conditions precedent to "override" the statutory "default test" for partnership formation.[60] More importantly, by explicitly stating that evidence of the § 152.052(a) factors—the factual predicates of partnership formation—is "not relevant" to waiving "a condition precedent to partnership formation,"[61] the court allows parties to use a condition precedent to block a partnership conclusion, even if they are otherwise fully acting as partners (by,

56. *Enterprise*, 593 S.W.3d at 741–42 (emphasis added).

57. *See supra* note 21 and accompanying text.

58. *See supra* notes 20–32 and accompanying text.

59. To be fair, the non-uniform § 152.052(a) of the TBOC does include "expression of intent to be partners in the business" as one of five "[f]actors indicating that persons have created a partnership." The inclusion of that factor is peculiar, however, particularly because § 152.051(b) of the TBOC makes clear that a partnership can be formed "regardless of whether . . . the persons intend to create a partnership." The *Enterprise* holding, in effect, elevates that one factor to dispositive status when the parties express their intent not to be partners. Such an outcome is inconsistent with the factor-balancing inquiry of § 152.052(a) as well as the language of § 152.051(b). Moreover, it seems to violate the court's earlier precedent. *See* Ingram v. Deere, 288 S.W.3d 886, 903–04 (Tex. 2009) (stating that "[w]hether a partnership exists must be determined by an examination of the totality of the circumstances"); *id.* at 898 ("Even conclusive evidence of only one factor normally will be insufficient to establish the existence of a partnership."); *see also infra* note 177 (discussing *Ingram*).

60. *Enterprise*, 593 S.W.3d at 738 ("Can persons override the default test for partnership formation in Chapter 152 by agreeing not to be partners until conditions precedent are satisfied?"); *see id.* at 739 ("We have never squarely addressed whether parties' freedom to contract for conditions precedent to partnership formation can override the statutory default test, in which intent is a mere factor.").

61. *See supra* text accompanying notes 55–56.

for example, sharing profits, losses, and control).

Although the *Enterprise* court focused on the use of conditions precedent to override a partnership conclusion, it is critical to note that the court's logic would seem to extend to absolute disclaimers of partnership. After all, a conditional disclaimer with a condition that is difficult, if not practically impossible, to satisfy ("we are not partners *until* the year 9999") is no different in effect from an absolute disclaimer of partnership ("we are not partners"). Similarly, a conditional disclaimer with a condition whose satisfaction remains within the control of one or both parties ("we are not partners *unless and until* our boards approve a definitive written partnership agreement") can be intentionally manipulated to have the same effect as an absolute disclaimer. In addition, if a conditional disclaimer of partnership ("we are not partners *until*") can override a partnership conclusion, it would not make sense as a matter of logic to prevent an absolute disclaimer from doing so.[62] Finally, the court's emphasis on freedom of contract, reference to partnership formation as a "default test," and statement that acting as partners is "not relevant" to the issue of waiver all suggest that the court would have reached the same outcome if the parties had simply agreed, as an absolute matter, that they were not partners.[63] At bottom, the *Enterprise* court seemingly determined that, as between themselves,[64] parties can circumvent a partnership conclusion, even while fully acting as partners, so long as they have disclaimed partnership status.[65]

2. The Legality of Partnership Disclaimers

Before the passage of RUPA, some cases suggested in an *Enterprise*-like manner that a disclaimer of partnership was dispositive in disputes between the alleged partners themselves ("*inter se*" disputes). In *Kingsley Clothing Manufacturing Co. v. Jacobs*,[66] for

62. An absolute disclaimer of partnership ("we are not partners") is a stronger form of disclaimer than a conditional disclaimer of partnership ("we are not partners *until*"). If a weaker disclaimer can override a partnership finding, it would be puzzling to conclude that a stronger disclaimer cannot.

63. *Enterprise*, 593 S.W.3d at 738–42; *see supra* text accompanying notes 54, 60–61.

64. *See supra* note 47 and accompanying text.

65. To be sure, conditions precedent do have a role in the partnership formation inquiry, but only at the level of the factual predicates. The ultimate question is whether the legal definition of partnership has been met—i.e., have the parties associated to carry on as co-owners a business for profit? As mentioned, to answer this question, a court examines various factors, such as whether the parties have agreed to share profits. *See supra* text accompanying notes 25–27. An agreement to share profits can be demonstrated by (a) a written or oral agreement to share profits, or (b) the actual sharing of profits. A condition precedent operates on option (a) by making it clear that the parties *have not agreed* to share profits until a later time or subsequent event. So long as there is no evidence of option (b)—the actual sharing of profits—there is no evidence of an agreement to share profits until the condition occurs.

In light of this discussion, it is tempting to read the *Enterprise* decision more narrowly. Perhaps the court simply concluded that there was insufficient evidence of the factual predicates of the partnership definition. The condition precedent made it clear that the parties had not agreed to share profits, control, or losses until a later time (i.e., the time of board approval), and there was no evidence of the *actual* sharing of profits, control, or losses. (Indeed, in its waiver discussion, the court referred to the "only" record evidence pointed to by ETP: "the parties held themselves out as partners and worked closely together." *Enterprise*, 593 S.W.3d at 742.) The problem with this interpretation is that the court did not acknowledge that evidence of *actual* sharing would have made a difference; in fact, the court explicitly said the opposite by indicating that evidence of the § 152.052(a) factors "is not relevant" when a "condition precedent to partnership formation is at issue." *Id.* at 741–42.

66. 26 A.2d 315 (Pa. 1942).

example, the Supreme Court of Pennsylvania stated that "[a]s between the parties themselves partnership is a matter of intention, and where they expressly declare that they are not partners this settles the question, for, whatever their obligations may be as to third persons, the law permits them to agree upon their legal status and relationship *inter se*."[67] *Kingsley* and similar cases did not represent a mainstream position;[68] moreover, the passage of RUPA further undermined them. Indeed, RUPA § 202(a) does not suggest that the formation inquiry changes depending upon whether the plaintiff is an alleged partner or a third party. It simply states, with no distinction in context, that "the association of two or more persons to carry on as co-owners a business for profit forms a partnership, *whether or not the persons intend to form a partnership*."[69] Similarly, the comment notes—again with no distinction in context—that parties "may inadvertently create a partnership *despite their expressed subjective intention not to do so*."[70] The comment to RUPA (2013) § 202(a)

67. *Id.* at 317.

68. *See, e.g.*, Rosenberger v. Herbst, 232 A.2d 634, 636 & n.2 (Pa. Super. Ct. 1967) (quoting the *Kingsley* language that disclaimers "settle[] the question" in *inter se* disputes, but then noting that "[t]his is not the rule in most jurisdictions"); *see also* Arnold v. Erkmann, 934 S.W.2d 621, 630 (Mo. Ct. App. 1996) (involving a disclaimer of partnership in an *inter se* dispute, citing a UPA-based definition of partnership, and noting that a disclaimer "is not dispositive of the determination of the existence of a partnership if an intent to enter into a partnership can be found in other provisions of the agreement"); Rubenstein v. Small, 75 N.Y.S.2d 483, 485 (App. Div. 1947) (involving a disclaimer of partnership in a pre-RUPA *inter se* dispute, and stating the following: "The court is not bound by the disclaimer of partnership, joint venture or agency between the parties in determining their true relationship. . . . The transaction must be judged by its real character rather than by the form and color which the parties have seen fit to give it." (citation omitted) (internal quotation omitted)); BROMBERG & RIBSTEIN, *supra* note 20, § 2.04[C], at 2-54 ("The courts have been somewhat more willing to give effect to the parties' characterization of their agreement as a non-partnership in cases involving rights and duties between the purported partners. Nevertheless, even in cases wholly among the purported partners, the courts have held that the characterization of a partnership or non-partnership was not controlling where the facts indicated a contrary intent." (footnote omitted)); SCOTT ROWLEY, DAVID SIVE & REED ROWLEY, ROWLEY ON PARTNERSHIP § 7.6(C), at 167–68 (2d ed. 1960) ("In determining the existence of a partnership it is well-settled that the true contract and intention of the parties is looked to at least as between themselves, in order to establish the existence of such relation. This has led to a general statement that, as between the immediate parties, a partnership is formed and exists only by their intention to form such a relationship, but the law looks to the substance and not the form. It is not what the parties call their relation that determines but what they actually agree upon in their contract. It is the intent to do those things which constitute a partnership that should usually determine whether or not that relation exists between the parties." (footnotes omitted)); *id.* § 7.0(C), at 127 (stating that "the intention of the parties is the real test," but cautioning that "intention, as sometimes used, does not necessarily refer to the conscious working of the mind, but to a legal intention which the law deduces from the acts of the parties, and, if they intend to do a thing which in law constitutes a partnership, they are partners, though their purpose was to avoid the creation of such a relation" (footnotes omitted)); *cf.* San Joaquin Light & Power Corp. v. Costaloupes, 274 P. 84, 88 (Cal. Dist. Ct. App. 1929) (involving a disclaimer of partnership in a pre-RUPA third-party dispute, and stating the following: "We may concede . . . that the contract expressly declares that the parties thereto are not partners. However, this does not establish the fact that the parties did not intend to create a partnership *between themselves* or as to a third person. The parties did intend to create exactly the relationship as shown by the contract, but did not intend that relationship to be called that of partners. Their intention in this respect is immaterial." (emphasis added)).

69. RUPA § 202(a) (emphasis added); *accord* RUPA (2013) § 202(a).

70. *Id.* § 202(a) cmt. (emphasis added); *see also* DONN, HILLMAN & WEIDNER, *supra* note 26, § 202, at 134–35 ("As [RUPA § 202] Official Comment 1 indicates, the drafters did not intend to change the law by adding to the statute the words 'whether or not the persons intend to form a partnership.' These words are merely intended to put into the statute what is clear upon an examination of the case law: that the intent of the parties to be classified as partners *or to avoid partnership classification* is not determinative. Rather, the question is whether or not the

states even more directly that "a disclaimer of partnership status is ineffective to the extent the parties' intended arrangements meet the criteria stated in this subsection."[71] Thus, as a doctrinal matter, a conclusion that disclaimers are dispositive in *inter se* disputes is questionable, particularly in RUPA jurisdictions.[72]

The *Enterprise* decision is especially notable, therefore, because it reached a *Kingsley*-like conclusion[73] in a RUPA jurisdiction and explicitly observed that partner-like conduct was irrelevant to the issue of waiving the disclaimer.[74] Moreover, the *Enterprise* rationale is easily portable, as the court emphasized freedom of contract and determined that such freedom could "override" the partnership formation inquiry.[75] As authority for incorporating freedom of contract, the court cited TBOC § 152.003, which states, in relevant part, that "[t]he principles of law and equity . . . supplement this chapter."[76] RUPA, which is followed by the vast majority of jurisdictions in this country,[77] has substantially the same partnership definition as the Texas statute, and RUPA also makes clear that "the principles of law and equity supplement this [Act]."[78] Given these

partners have intended to enter into a relationship, however it is denominated, the essence of which is partnership." (emphasis added) (footnote omitted)).

71. RUPA (2013) § 202(a) cmt.

72. One partnership treatise cites *Kingsley* along with four other pre-RUPA cases for the proposition that "if the parties agree that they shall not be treated as partners, the courts generally have held that no partnership existed in actions between the parties." J. WILLIAM CALLISON & MAUREEN A. SULLIVAN, PARTNERSHIP LAW AND PRACTICE: GENERAL AND LIMITED PARTNERSHIPS § 5:7, at 153 (2019–2020 ed.). That treatise, however, acknowledges that the text of RUPA § 202(a) and its comment "might change the result in these cases." *Id.* at 153 n.26; *see also id.* § 5:1, at 67 n.1 ("Although the Comment to RUPA § [202](a) states that 'no substantive change in the law is intended,' since UPA § 6(1) has always been understood as an operative rule and since courts have always considered persons meeting the definition to be partners regardless of their subjective intention, *it is probable that application of* RUPA § [202](a) *would change the rule stated in several cases*; that persons who would otherwise be 'partners' can agree that they will not be partners as to one another." (emphasis added)); J. William Callison, *Blind Men and Elephants: Fiduciary Duties Under the Revised Uniform Partnership Act, Uniform Limited Liability Company Act, and Beyond*, 1 J. SMALL & EMERGING BUS. L. 109, 154 & n.254 (1997) (citing *Kingsley* and stating the following: "Under the UPA, one method for partners to opt out of partnership fiduciary duties has been for them to agree that they are not partners as to one another. *Section 202(a) of RUPA forecloses this approach* by stating that an 'association of two or more persons to carry on as co-owners a business for profit forms a partnership, whether or not the persons intend to form a partnership.'" (emphasis added)).

73. One might argue that this is a misstatement of the *Enterprise* court's holding, as the court only focused on a particular type of agreement—a conditional disclaimer of partnership—and not on more absolute disclaimers that simply deny that the parties are partners. As mentioned, while it is technically correct to assert that the court's holding was limited to conditional disclaimers, the logic of the opinion is not so easily constrained. *See supra* text accompanying notes 62–65.

74. *See supra* text accompanying notes 55–56, 61.

75. *See supra* text accompanying note 54; *supra* note 60 and accompanying text.

76. TEX. BUS. ORGS. CODE § 152.003 (2006); *see* Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P., 593 S.W.3d 732, 740 (Tex. 2020) ("Section 152.003 expressly authorizes supplementation of the partnership-formation rules of Chapter 152 with 'principles of law and equity', and perhaps no principle of law is as deeply engrained in Texas jurisprudence as freedom of contract.").

77. *See supra* notes 18–19 and accompanying text.

78. *Compare* RUPA § 202(a) (stating that "the association of two or more persons to carry on as co-owners a business for profit forms a partnership, whether or not the persons intend to form a partnership"), *and id.* § 104 (stating that "the principles of law and equity supplement this [Act]"), *with* TEX. BUS. ORGS. CODE § 152.051(b) (stating that "an association of two or more persons to carry on a business for profit as owners creates a partnership, regardless of whether . . . the persons intend to create a partnership"), *and id.* § 152.003 (stating that "[t]he principles of law and equity . . . supplement this chapter").

similarities, the holding of the *Enterprise* court could easily be replicated in other jurisdictions. The role of freedom of contract in the partnership formation inquiry, therefore, is not simply a Texas issue—it is a significant issue of national partnership law. Thus, it is important to consider not only the uneasy doctrinal fit between the *Enterprise* holding and RUPA/RUPA (2013) § 202(a), but also the substantial normative question—should disclaimers of partnership be dispositive in *inter se* disputes?

IV. CONTRACTING OUT OF PARTNERSHIP: COSTS AND BENEFITS

Parties can always opt out of the general partnership by choosing a filing entity for their business. The question here is more focused: even without choosing a filing entity, should parties be able to conclusively disclaim general partnership status by agreement, even though they are carrying on as co-owners a business for profit? On the one hand, allowing such an outcome would undermine the protections of fiduciary duty, create uncertainty about the operating rules for the business, and threaten to deny the rights of third parties who did not agree to the disclaimer. On the other hand, such an outcome would promote freedom of contract and would result in a more predictable conclusion on the partnership formation question. Each of these costs and benefits will be discussed in turn.

A. Costs of Allowing Parties to Contract Out of Partnership

1. Undermining Mandatory Fiduciary Duties

It is impossible to start a co-owned business in this country without confronting the existence of fiduciary duties. The structure of every co-owned business organization involves duties that are owed by managers to the organization itself and its owners.[79] Understanding why fiduciary duties are ubiquitous in the business organization setting is not difficult. Co-owned businesses involve persons who are willing to come together and pool their money, talent, services, and property, and that pooling is very unlikely to occur unless there is a substantial degree of trust among the participants. In general, this is the province of fiduciary duty—relationships that involve significant trust and confidence between the parties.[80] Fiduciary duties in the business organization setting help constrain those with managerial control from abusing that trust—i.e., from exercising their control in ways that take unfair advantage of the business or the owners.[81]

79. *See, e.g.*, RUPA § 404 (general partnership); RUPA (2013) § 409 (general partnership); UNIF. LTD. P'SHIP ACT § 408 (UNIF. L. COMM'N 2001) (limited partnership); UNIF. LTD. P'SHIP ACT § 409 (UNIF. L. COMM'N 2001) (amended 2013) (limited partnership); REV. UNIF. LTD. LIAB. CO. ACT § 409 (UNIF. L. COMM'N 2006) (limited liability company); UNIF. LTD. LIAB. CO. ACT § 409 (UNIF. L. COMM'N 2006) (amended 2013) (limited liability company); MODEL BUS. CORP. ACT §§ 8.30, 8.42 (AM. BAR ASS'N., amended 2016) (corporation).

80. *See, e.g.*, DAN B. DOBBS, PAUL T. HAYDEN & ELLEN M. BUBLICK, THE LAW OF TORTS § 697, at 749 (2d ed. 2011) (describing a fiduciary as a person "who appear[s] to accept, expressly or impliedly, an obligation to act in a position of trust or confidence for the benefit of another or who [has] accepted a status or relationship understood to entail such an obligation, generating the beneficiary's justifiable expectations of loyalty").

81. *See, e.g.*, Tamar Frankel, *Fiduciary Law*, 71 CALIF. L. REV. 795, 807 (1983) (observing that "all fiduciary relations give rise to the problem of abuse of power" and that "the purpose of fiduciary law should be to solve this problem"); *id.* at 809 ("[W]hile the fiduciary must be entrusted with power in order to perform his function, his possession of the power creates a risk that he will misuse it and injure the entrustor.").

Compared to other business structures that provide limited liability, the general partnership form requires even more trust among the participants. In a general partnership, the owners (known as "partners") are personally liable for the partnership's debts if the partnership itself has insufficient assets to satisfy its obligations.[82] Partners are also agents of the partnership who can create both tort and contract liability for the business.[83] Thus, if a partner's conduct creates a partnership obligation, that obligation has the potential to put the personal assets of fellow partners at risk. When limited liability is absent, in other words, trust between the owners is even more important, as owner conduct (and misconduct) can affect not only the partnership's assets but also the personal assets of the partners. Fiduciary duties help reinforce this trust by encouraging partners (via the threat of legal action) to consider the interests of the business and their fellow partners when making decisions.[84]

Given the importance of trust to the general partnership structure, it is perhaps unsurprising that RUPA explicitly provides for the fiduciary duties of care and loyalty in general partnerships.[85] Although the duties can be substantially modified by a partnership agreement, RUPA § 103 prevents the agreement from eliminating the duties entirely.[86] By allowing modifications but not eliminations, RUPA "ensure[s] a fundamental core of fiduciary responsibility"[87] and "rejects the notion that a contract can completely transform an inherently fiduciary relationship into a merely arm's length association."[88]

In combination, the partnership definition under RUPA § 202[89] and the "mandatory minima" of fiduciary duty in RUPA § 103[90] tell a pretty clear story—when two or more persons associate to carry on as co-owners a business for profit without forming a filing entity, a partnership relationship characterized by trust has been established that carries with it "a fundamental core of fiduciary responsibility."[91] Indeed, the inability to use contract to eliminate the fiduciary character of the partnership relationship indicates that RUPA and adopting state legislatures do not permit a non-filing association of co-owners

82. *See* RUPA §§ 306(a), 307(c)–(d); RUPA (2013) §§ 306(a), 307(c)–(d).

83. *See* RUPA §§ 301, 305; RUPA (2013) §§ 301, 305.

84. *Cf.* Cont'l Ins. Co. v. Rutledge & Co., 750 A.2d 1219, 1237 (Del. Ch. 2000) (stating that a general partner's duty of loyalty prevents it from "us[ing] its position as general partner, and its ability to control the terms of transactions, to invest . . . partnership funds for its own gain, as opposed to investing for the benefit of the . . . partnership"); Meehan v. Shaughnessy, 535 N.E.2d 1255, 1263 (Mass. 1989) ("As a fiduciary, a partner must consider his or her partners' welfare, and refrain from acting for purely private gain.").

85. *See* RUPA § 404(a)–(c); RUPA (2013) § 409(a)–(c). Under RUPA (2013), the duty of care is no longer considered a "fiduciary" duty. *See* RUPA (2013) § 409 cmt. ("This act no longer refers to the duty of care as a fiduciary duty, because: the duty of care applies in many non-fiduciary situations; and (ii) breach of the duty of care is remediable in damages while breach of a fiduciary duty gives rise also to equitable remedies, including disgorgement, constructive trust, and rescission . . . . However, the label change is merely semantics; no change in the law is intended.").

86. *See* RUPA § 103(b)(3)–(4); RUPA (2013) § 105(c)(5), (d).

87. RUPA § 103 cmt. 4.

88. RUPA (2013) § 105 cmt.; *see also id.* at (d)(2) (stating that "the partnership agreement may not transform the relationship inter se partners and the partnership into an entirely arm's length arrangement").

89. *See supra* note 21 and accompanying text.

90. Donald J. Weidner, *RUPA and Fiduciary Duty: The Texture of Relationship*, 58 LAW & CONTEMP. PROBS. 82, 89–90 (1995) (stating, under the heading "RUPA's Mandatory Minima," that "RUPA rejects the position of more extreme contractarians by continuing the language of fiduciary obligation and by providing a mandatory minimum of fiduciary obligation"); *supra* notes 86–88 and accompanying text.

91. *See supra* note 87 and accompanying text.

in a profit-seeking business without that fiduciary core.

If parties can use contractual disclaimers to deny partnership status while fully acting as partners, it completely circumvents this principle. Without forming a filing entity, parties *can* associate as co-owners in a profit-seeking business without any fiduciary obligations. Any court reaching this result would seem to have directly undermined the policy choice made by the state's legislature when RUPA was adopted. That alone should give one pause when considering the wisdom of permitting such disclaimers to be conclusive, but the problem goes further than merely circumventing a legislative policy choice. There is great danger to permitting the effective elimination of fiduciary duties via conclusive disclaimers of partnership because many parties are unlikely to understand the full extent of what they are giving up by relinquishing such duties.[92] In addition, there is reason to doubt that parties can accurately foresee the form and likelihood of future misconduct by their fellow partners.[93] Circumventing the legislative policy choice to maintain a fiduciary core, therefore, is not only bad for its own sake, but it also leaves partners vulnerable to abuse.

a. Fiduciary Duty Modifications and Information

Because of the importance of fiduciary duties, it should go without saying that we want parties to fully understand what they are giving up when they agree to modify such duties. The ideal rule for modifications, therefore, would nudge the party desiring the change to convey the most information in the most intelligible manner to the other parties about the need for the fiduciary modification.

When fiduciary duties are limited (as opposed to eliminated), the limitation itself conveys information about the problem or conflict that the party foresees. For example, in a real estate partnership, a prominent developer may not wish to join the venture if he has to turn over all of his development opportunities to the partnership.[94] An agreement authorizing the partner to retain certain development opportunities for his own account would likely be permitted as a type or category of activity that does not violate the duty of loyalty.[95] More importantly, courts will require that limitation to be stated clearly and with particularity in a partnership agreement.[96] That requirement will help ensure that the other

92. *See infra* Part IV(A)(1)(a).

93. *See infra* Part IV(A)(1)(b).

94. *Cf.* Leo E. Strine, Jr. & J. Travis Laster, *The Siren Song of Unlimited Contractual Freedom*, *in* RESEARCH HANDBOOK ON PARTNERSHIPS, LLCS AND ALTERNATIVE FORMS OF BUSINESS ORGANIZATIONS 11, 15 (Robert W. Hillman & Mark J. Loewenstein eds., 2014) (describing the desire of managers in alternative entities to limit the risks posed by the analogous corporate opportunity doctrine: "A sponsor operating in a particular industry, such as the energy arena, wishes to raise capital from investors for a particular project, such as exploiting a natural gas field. . . . The sponsor does not want the entity to have a claim to all future opportunities in the natural gas industry that might come to the sponsor's attention.").

95. *See infra* text accompanying notes 189–194; *cf.* RUPA § 103 cmt. 4 ("A provision in a real estate partnership agreement authorizing a partner who is a real estate agent to retain commissions on partnership property bought and sold by that partner would be an example of a 'type or category' of activity that is not manifestly unreasonable and thus should be enforceable under the Act."); *id.* ("Likewise, a provision authorizing that partner to buy or sell real property for his own account without prior disclosure to the other partners or without first offering it to the partnership would be enforceable as a valid category of partnership activity.").

96. *See, e.g.*, RUPA (2013) § 105 cmt. (citing cases for the proposition that "displacement of fiduciary duties is effective only to the extent that the displacement is stated clearly and with particularity"); *see also* RUPA § 103 cmt. 4 ("The [exculpatory] agreement may be drafted in terms of types or categories of activities or

parties are aware of the particular problem that the developer foresees, and they can decide if they are comfortable proceeding with such a limitation.

When fiduciary duties are eliminated, however, no information is provided on the particular problem that the party envisions. A blanket statement in a partnership agreement that the partners "do not owe the partnership or each other a fiduciary duty of loyalty" generally indicates that the proposing party does not believe that the benefits of the fiduciary duty of loyalty exceed its costs, but no detail is provided. The specific problem that the party foresees remains hidden.

From an information-forcing standpoint, therefore, there is logic to authorizing limitations while prohibiting eliminations. Limitations convey specific information about foreseeable conflicts that parties without legal backgrounds can understand—e.g., competition is permitted, business opportunities do not have to be turned over, etc. Eliminations convey no information about the problem envisioned by the proposer, and they require parties to have a legal understanding of what "no fiduciary duty of loyalty" means. Of course, if sophisticated enough,[97] parties can always ask questions in an effort to learn more about the basis for an elimination provision, and if sufficient resources exist, access to lawyers can help explain what such eliminations mean. Nevertheless, given that potential partners may vary widely in sophistication and resources, a rule that provides the best chance for information to be shared in an intelligible manner is preferable.[98] Thus, RUPA's policy choice to allow limitations but prohibit eliminations is sensible, as it helps to ensure that the parties understand what they are relinquishing when they alter fiduciary duties.[99] Circumventing this policy choice by allowing parties to act as partners while

transactions, but it should be reasonably specific.").

97. If one believed that only sophisticated parties will enter into disclaimers of partnership (and that line-drawing problems relating to the concept of sophistication could be solved), the concern that parties will not fully understand the rights they are relinquishing is lessened. Because the sophistication of potential partners can vary widely, however, it seems reasonable to assume that many disputes will involve a "non-partnership agreement" that was proposed by a more sophisticated party to a less sophisticated party who did not fully understand the agreement's legal significance. *Cf.* Mohsen Manesh, *Creatures of Contract: A Half-Truth About LLCs*, 42 DEL. J. CORP. L. 391, 433 (2018) (suggesting that, in publicly traded limited partnerships, the governing agreement denying fiduciary duties is drafted by a sophisticated, controlling party and offered to unsophisticated investors who are unlikely to understand its terms). Further, because partnership disclaimers can likely be oral or implied, *see infra* notes 121–122 and accompanying text, even ventures with only unsophisticated parties may find themselves in disputes involving such disclaimers.

For a further discussion of whether an *Enterprise*-like holding should be limited to sophisticated parties, see *infra* note **Error! Bookmark not defined.**.

98. *Cf.* Rutheford B. Campbell, Jr., *Bumping Along the Bottom: Abandoned Principles and Failed Fiduciary Standards in Uniform Partnership and LLC Statutes*, 96 KY. L.J. 163, 189 (2008) ("To maximize the efficiencies created by such a broad [duty of loyalty] opt out right, however, it is essential that the opt out be coupled with provisions that provide strong incentives for full information sharing among the parties at the point of the opt out."); *id.* ("The provisions described above—requiring that the opt out be in specific terms and be included in the partnership or LLC operating agreement . . . become even more important because of the broad and generous loyalty opt out rights.").

99. *Cf.* RESTATEMENT (THIRD) OF AGENCY § 8.06 cmt. b (2006) (stating that "a broadly sweeping release of an agent's fiduciary duty may not reflect an adequately informed judgment on the part of the principal," but noting that "[i]n contrast, when a principal consents to specific transactions or to specified types of conduct by the agent, the principal has a focused opportunity to assess risks that are more readily identifiable."); *id.* ("Likewise, when a principal consents after-the-fact to action taken by an agent that would otherwise breach the agent's fiduciary duty to the principal, the principal has the opportunity to assess what the agent has done with a

conclusively disclaiming partnership—and, therefore, the fiduciary duties that accompany partnership—will result in parties making critically important decisions on a less informed basis.[100]

b. Fiduciary Duty Modifications and Cognitive Biases

Fiduciary duties, particularly the duty of loyalty, function as a backstop against opportunistic conduct.[101] It is hard to argue that partners should have the option to eliminate the backstop unless we believe that they can correctly anticipate the form and likelihood of future misconduct by their fellow partners. After all, if the parties themselves cannot appropriately understand the risks of eliminating the duty of loyalty, it is easier to

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degree of specificity not available before the agent takes action.").

Professor Booth has similarly observed:

> A statute that allows for total waiver would likely undercut serious bargaining between the parties. Again, the primary concern is the duty of loyalty. A statute that requires specification of the types of conflicts to be exempted places the burden on the party who expects to be faced with such conflicts to raise the issue in advance and, in effect, to disclose the likely conflict to the other partners. More importantly, a statute allowing for total waiver . . . would allow the more informed party simply to insist on a total waiver without specifying the nature of the conflict expected.
>
> . . . .
>
> Again, the question arises: Why not allow total waiver? The answer is that total waiver is too easy. . . . If total waiver is allowed, it is unlikely that genuine bargaining will arise. Partial waiver, no matter how closely it approaches total waiver, requires the person with information as to likely conflicts to disclose those conflicts and to seek advance approval from the other partners. Total waiver in the absence of specification allows a partner who expects a conflict simply to demand a total waiver.

Richard A. Booth, *Fiduciary Duty, Contract, and Waiver in Partnerships and Limited Liability Companies*, 1 J. SMALL & EMERGING BUS. L. 55, 61, 64 (1997) (footnote omitted).

100. Fiduciary duties are not the only legal protection that parties give up by disclaiming partnership. RUPA also provides, for example, management and information rights to partners. *See* RUPA §§ 401, 403; RUPA (2013) §§ 401, 408. An agreement that conclusively disclaims partnership status eliminates all of these rights without explicitly signaling that it is doing so. Once again, parties would have to understand partnership law to know what they are relinquishing. By contrast, if parties acting as partners are not able to disclaim partnership status, they will still maintain the ability to contractually alter these rights. *See* RUPA § 103; RUPA (2013) § 105. Contractual alterations, however, will need to specifically address the right, which conveys more information and draws more attention to the issue than a blanket disclaimer of partnership. The additional information and attention will hopefully result in more informed decisions by the parties.

Delaware allows for the elimination of fiduciary duties in the general partnership. *See* DEL. CODE ANN. tit. 6, § 15-103(b), (f) (2013). When the legislature has already decided that a general partnership can exist with no fiduciary core, allowing parties to indirectly eliminate fiduciary duties by conclusively disclaiming partnership seems less problematic. That said, even Delaware requires fiduciary duty alterations to be stated clearly and with particularity, *see, e.g.*, Paige Cap. Mgmt., LLC v. Lerner Master Fund, LLC, No. Civ. A. 5502-CS, 2011 WL 3505355, at *31 (Del. Ch. Aug. 8, 2011), presumably because Delaware wants parties to understand, as much as possible, what they are giving up. A statement in a partnership agreement that the partners "do not owe the partnership or each other any fiduciary duties, including the duties of care and loyalty" draws attention to the issue of eliminating duties in a way that a general disclaimer of partnership does not. The same can be said for contractual alterations of other rights, such as management or information. Even in a jurisdiction like Delaware, therefore, one might argue that a disclaimer of partnership is more problematic than a contractual alteration of rights because the disclaimer conveys less information and calls less attention to the particular rights at issue.

101. *See supra* notes 81, 84 and accompanying text.

justify a paternalistic refusal to allow elimination.

An inability to appreciate the risks of eliminating the duty of loyalty is certainly present with unsophisticated parties, as they are less likely to understand their legal rights in the first place. Due to various cognitive limitations, even sophisticated parties with an awareness of what the duty of loyalty means are unlikely to accurately assess the risks of elimination:

> Given the limits of cognition, the core duty-of-loyalty rules should not be subject to a general waiver.
>
> To begin with, because of bounded rationality the beneficiaries could not possibly identify all the varying circumstances to which a general waiver of the duty of loyalty would apply. Furthermore, the beneficiaries would likely be unduly optimistic about the extent to which the manager would deal fairly despite the lack of fiduciary restraints. The availability and representativeness heuristics would enhance such undue optimism: Beneficiaries would tend to give undue weight to their good relationship with the manager at the time of contract formation, because that relationship is vivid, concrete, and instantiated, as compared with the possibility that the manager would exploit the bargain at some point in the future, which is abstract, general, and pallid, and would tend to overestimate the extent to which the present relationship with the manager is a reliable index of the future relationship. Similarly, faulty telescopic faculties would lead the beneficiaries to give undue weight to the present benefits of the relationship as compared to the future costs of the waiver. Finally, beneficiaries would tend to underestimate the risks that the waiver entailed. Thus, a general waiver of the duty of loyalty would inevitably permit unanticipated opportunistic behavior on the part of managers.[102]

102. Melvin Aron Eisenberg, *The Limits of Cognition and the Limits of Contract*, 47 STAN. L. REV. 211, 249 (1995); *see also* RESTATEMENT (THIRD) OF AGENCY § 8.06 cmt. b (2006) (stating that "an agreement that contains general or broad language purporting to release an agent in advance from the agent's general fiduciary obligation to the principal is not likely to be enforceable" because "a broadly sweeping release of an agent's fiduciary duty may not reflect an adequately informed judgment on the part of the principal," and observing that, "if effective, the release would expose the principal to the risk that the agent will exploit the agent's position in ways not foreseeable by the principal at the time the principal agreed to the release"); J. Dennis Hynes, *Fiduciary Duties and RUPA: An Inquiry into Freedom of Contract*, 58 LAW & CONTEMP. PROBS. 29, 37 n.38 (1995) ("Persons who enter into a relationship of trust and confidence, in which a contractual override of fiduciary duties originally seems acceptable, may later find that one of their numbers has abused that trust and confidence in a manner that was not and probably could not have been anticipated." (quoting letter from Melvin A. Eisenberg)); *id.* ("[A]n opportunistic partner could often find ways to exploit a contractual provision that eliminated a fiduciary duty even though the provision seemed fair at the time of the contract. It is almost impossible to deal adequately with this potential for ex post opportunism by ex ante contracting." (quoting letter from Melvin A. Eisenberg)).

Two distinguished Delaware jurists make similar arguments:

> Another argument often made in favor of alternative entity statutes is that they allow for the elimination of fiduciary duties and the establishment of a purely contractual relationship between entity managers and investors. As judges who have seen our fair share of alternative entity disputes, we do not immediately grasp why this would be seen as a compelling advantage. . . .
>
> . . . .
>
> The corporate experience makes us skeptical that the drafters of the governing instruments of

Limitations on the duty of loyalty, however, are less likely to suffer from the same cognitive defects. Because the limitation must be stated clearly and with particularity,[103] the conflict addressed by the limitation is present and concrete, rather than simply a distant possibility:

> On the other hand, managers might not as easily exploit an agreement to govern a specific self-dealing issue. Informed consent to a specific conflict-of-interest transaction, for example, may not suffer from defective cognition, because the consent would relate to a specific present event rather than to an unknowable future. An agreement that a specific type of business venture will not be deemed a [business] opportunity may also fall into this category.[104]

Once again, the policy choice made by RUPA and adopting state legislatures to allow fiduciary duty limitations but not eliminations is sensible, as it recognizes the limits of human foresight and the dangers of permitting general waivers. Allowing parties to act as partners while conclusively disclaiming partnership undermines this policy choice and leaves partners vulnerable to opportunistic conduct. Left unchecked, such vulnerability threatens to discourage prospective venturers from engaging in entrepreneurial activity with others.[105]

> alternative entities are likely to have greater success in attempting to provide contractually for all reasonably conceivable circumstances. It takes only a moderate degree of self-awareness and modesty to recognize that the human mind cannot foresee every potential situation that could arise after contracting. All contracts necessarily will be incomplete. But assuming that drafters could anticipate all future states of the world, a fully complete contract still would be beyond the parties' power. After all, contracting is costly. Trying to identify, negotiate, and draft language to address every eventuality would take so much time and require such a large investment of resources that the deal itself would never happen. . . . Sadly, the normative ideal of rational parties contracting efficiently to allocate risks is just that—an ideal.

Strine & Laster, *supra* note 94, at 9–10, 12–13; *see also* BROMBERG & RIBSTEIN, *supra* note 20, § 6.07[H], at 6-119 ("Some commentators have argued that the partners' ability to agree to alterations in fiduciary duty should be limited. Commentators' objections to free contracting in partnerships and other unincorporated firms include partners' inability to foresee the risks of fiduciary duty waivers or rationally to evaluate those risks, disparities in bargaining position, and the need to preserve 'norms' of good behavior among partners.'" (footnote omitted)); William J. Carney, *The Theory of the Firm: Investor Coordination Costs, Control Premiums and Capital Structure*, 65 WASH. U. L.Q. 1, 59–60 (1987) ("Investors in closely held enterprises are likely to be subject to conditions of bounded rationality, under which they either fail to perceive the complete set of problems that may occur later, or underestimate the probability of their occurrence.").

103. *See supra* note 96 and accompanying text.

104. Eisenberg, *supra* note 102, at 249; *see also* RESTATEMENT (THIRD) OF AGENCY § 8.06 cmt. b (AM. L. INST. 2006) ("In contrast [to an agreement that contains general or broad language purporting to release an agent in advance from the agent's general fiduciary obligation to the principal], when a principal consents to specific transactions or to specified types of conduct by the agent, the principal has a focused opportunity to assess risks that are more readily identifiable."); *id.* ("Likewise, when a principal consents after-the-fact to action taken by an agent that would otherwise breach the agent's fiduciary duty to the principal, the principal has the opportunity to assess what the agent has done with a degree of specificity not available before the agent takes action.").

105. *See, e.g.*, Anupam Chander, *Minorities, Shareholder and Otherwise*, 113 YALE L.J. 119, 159 (2003) ("Protections against expropriation—and, equally important, protections regarding the fair division of potential gains—help lead capitalists to part with control over their capital.").

2. Creating Uncertainty About the Operating Rules for the Business

Modern business organization statutes provide rules that govern various aspects of the business, including formation, governance, financial rights, liability, transferring ownership interests, dissociation, and dissolution.[106] Most of these provisions are default rules that the parties can change by agreement. If they do not, the statute itself provides the "rules of the road" for how the business will operate.[107] This helps the parties understand what their rights are in particular situations, and it makes it easier for courts to resolve disputes in the event that the parties cannot.

The general partnership fits this pattern. Almost all of RUPA's provisions are default rules[108] that were drafted with the small, informal partnership in mind.[109] A default rule that is unsuitable for a particular business, of course, can always be changed by agreement. Thus, like other business organization statutes, RUPA provides the baseline rules for the operation of the partnership,[110] but almost all of the rules can be displaced by the parties' agreement.

If parties can contract out of general partnership status—even while fully acting as partners—the baseline rules provided by RUPA will not be applicable. The parties' agreement will need to provide the operating rules for the business. While the law of agency can provide guidance on certain matters, such as the liability of a principal for contracts entered into by an agent,[111] agency principles do not address a host of co-owner issues, including, among others, voting rights, access to books and records, and the sharing of profits and losses. Without a comprehensive agreement between the parties, disputes will be difficult to resolve, as the parties themselves may be uncertain about their rights with respect to a particular issue. Moreover, a court will have no statutory guidance to fall back on.

Are parties likely to disclaim partnership status without providing a comprehensive agreement to cover their affairs? This is a difficult question to answer, but some general statements can be made. To begin with, the Reporter for RUPA has noted that "individuals rarely 'bargain' as equals for partnership agreements that completely define their

106. *See, e.g.*, UNIF. LTD. LIAB. CO. ACT (2013) §§ 201, 304, 407, 501–02, 601–03, 701–02 (LLCs); UNIF. LTD. P'SHIP ACT §§ 201, 303, 404, 406, 503, 601–05, 701–02, 801–02 (last amended 2013) (limited partnerships).

107. *See, e.g.*, UNIF. LTD. LIAB. CO. ACT § 105 (UNIF. L. COMM'N 2006) (last amended 2013); UNIF. LTD. P'SHIP ACT § 105 (UNIF. L. COMM'N 2001) (last amended 2013); *see also* UNIF. LTD. LIAB. CO. ACT § 105(b) (UNIF. L. COMM'N 2006) (last amended 2013) ("To the extent the operating agreement does not provide for a matter described in subsection (a), this [act] governs the matter."); UNIF. LTD. P'SHIP ACT § 105(b) (UNIF. L. COMM'N 2001) (last amended 2013) ("To the extent the partnership agreement does not provide for a matter described in subsection (a), this [act] governs the matter.").

108. *See* RUPA § 103(a); RUPA (2013) § 105; *see also* Weidner, *supra* note 90, at 83 ("Because almost all of RUPA's rules governing the relations among partners are default rules rather than mandatory rules, partners are free to agree to virtually any relationship they wish.").

109. *See* Weidner, *supra* note 90, at 83–84 (stating that "[t]he basic mission of RUPA is to serve small partnerships" which "often are created quite informally"); *id.* at 83 ("Large partnerships can fend for themselves more easily by drafting partnership agreements that suit their special needs.").

110. *See, e.g.*, RUPA §§ 202, 306, 401, 502–03, 601–03, 801, 807 (addressing formation, governance, financial rights, liability, transferring ownership interests, dissociation, and dissolution); RUPA (2013) §§ 202, 306, 401, 502–03, 601–03, 801, 806 (same).

111. *See, e.g.*, RESTATEMENT (THIRD) OF AGENCY §§ 6.01–6.03 (AM. L. INST. 2006). This assumes that at least one of the parties would be legally characterized as the agent of the other.

relationship," and he has opined that "[t]he law should assume that the completely defined partnership relationship is the exception rather than the norm."[112] That said, when the parties are sophisticated, there is presumably a better chance of a more detailed arrangement, particularly because such parties will typically have better access to lawyers and more resources to devote to drafting a thorough agreement. Even for a sophisticated party, however, preparing a comprehensive and effective agreement can be difficult.[113] With less sophisticated parties, it is reasonable to assume that there is a greater likelihood of incomplete agreements, especially if there are fewer resources available to retain competent counsel. These less sophisticated parties may have learned that a disclaimer of partnership can evade the fiduciary duty aspects of partnership law, but they may not realize that the same disclaimer creates the need for an agreement that provides all of the baseline rules for the parties' relationship.

Under RUPA, incomplete agreements can occur when parties displace default rules with contractual provisions that do a poor job of providing clear guidance, whether because of ambiguity, incoherence, or otherwise. This problem of displacing a default rule with an inadequate replacement provision is one that courts currently grapple with.[114] If parties are permitted to contract around partnership status, however, an additional type of incomplete agreement is possible—one where the parties completely fail to address a particular *inter se* issue (e.g., management, financial, or information rights), and where there is no default rule to fill the gap.[115] Allowing the parties to contract around partnership status, therefore, increases the likelihood that courts will confront incomplete partnership agreements in one form or another.

Courts will still need to resolve disputes, of course, even when incomplete "non-partnership agreements" are present. Contract interpretation principles might be used, but there would need to be enough content in the parties' agreement to allow for meaningful interpretation.[116] Alternatively, a court might invoke equity and attempt to do what it thinks is fair in the circumstances.[117] The point is not that such disputes will go unresolved; to the

112. Weidner, *supra* note 90, at 82.

113. *See, e.g.*, Kahn v. Portnoy, Civ. A. No. 3515-CC, 2008 WL 5197164, at *1 (Del. Ch. Dec. 11, 2008) (involving the LLC agreement of a "publicly traded Delaware LLC" that was "one of the largest operators of truck stops in the United States," describing portions of the agreement as "poor drafting," and noting that when parties "have broad discretion to design the company as they see fit in an . . . agreement," there is "the risk—for both the parties and this Court—that the resulting . . . agreement will be incomplete, unclear, or even incoherent"); *cf.* Strine & Laster, *supra* note 94, at 12–13 (observing that "[a]ll contracts necessarily will be incomplete" and that "a fully complete contract [is] beyond the parties' power").

114. *Cf.* Acela Invs. LLC v. DiFalco, No. CV 2018-0558-AGB, 2019 WL 2158063, at *24 (Del. Ch. May 17, 2019) (stating that "[u]nfortunately, as this case shows . . . freedom [of contract] allows parties to adopt contractual arrangements that do not work"); *supra* note 113 (citing *Portnoy* for the proposition that the parties' agreement may be "incomplete, unclear, or even incoherent").

115. *See, e.g.*, RUPA §§ 401 (management and financial rights), 403 (information rights); RUPA (2013) §§ 401 (management and financial rights), 408 (information rights).

116. *Cf.* Omri Ben-Shahar, *"Agreeing to Disagree": Filling Gaps in Deliberately Incomplete Contracts*, 2004 WIS. L. REV. 389, 393 (stating that "[s]ome seemingly unresolved aspects [of indefinite contracts] could be overcome by courts through liberal interpretation of meaning or by reference to context (e.g., prior oral agreements, course of performance)," but also noting that "other unresolved aspects cannot because the parties simply failed to reach agreement or to manifest any type of inferable assent over these matters").

117. *See, e.g.*, Hillman v. Hillman, 910 A.2d 262, 276–77 (Del. Ch. 2006) (describing "equity as the ultimate default" and relying in part on equity to determine the amount that should be received by an expelled partner).

contrary, they will be resolved, but in a less principled and uniform manner than if a set of organizational default rules were available.[118] The general partnership's traditional role as the residual form of co-owned, for-profit business organization provides a uniform set of gap-fillers (not to mention decades of case law) that result in more consistent outcomes when the parties have not spoken.[119] Conclusive disclaimers of partnership eliminate those gap-fillers, and when coupled with the inevitable incomplete agreements between the parties, consistent outcomes are less likely.[120]

This problem of uncertainty about the operating rules for the business is magnified when one considers that a disclaimer of partnership can generally be written, oral, or implied.[121] Thus, during a dispute involving *inter se* rights or duties, even parties who are familiar with general partnerships and who intend to be governed by RUPA's default rules run the risk that a co-owner will argue that the parties orally or impliedly disclaimed partnership status. As one commentator observed:

> Even if a factfinder would eventually see through the unscrupulous co-owner's lies, the co-owners would . . . not "know whether they are in a partnership until a jury tells them." If agreements not to be partners are dispositive, co-owners of informal businesses could always reach a jury

118. *See* Joseph K. Leahy, *An LLC is the Key: The False Dichotomy Between Inadvertent Partnerships and the Freedom of Contract*, 52 TEX. TECH L. REV. 243, 283 (2020) (discussing parties "contract[ing] around partnership as a matter of law," noting that "[w]hen disputes arose (as they inevitably would), courts would be forced to fashion rules out of whole cloth for businesses governed neither by [statutory] rules for partnerships nor its rules for filing entities; alternatively, courts might imply extensive governing agreements between the parties," and concluding that "[t]his ad hoc rule-making would undermine uniformity in business organization law and create uncertainty for informal businesses who opt out of partnership law without creating a system of rules to govern their businesses").

119. *See supra* text accompanying notes 20–24, 107–108.

120. *See supra* note 118 and accompanying text.

Perhaps this problem is less significant than it appears. One might argue that parties who co-own a business will not want to operate the company as a purely contractual venture for very long. After all, a non-partnership agreement might only control *inter se* disputes; if a third party sues, partnership rules may apply, including the rule that partners are personally liable for the debts of the business. *See* RUPA § 306(a); RUPA (2013) § 306(a); *infra* Part IV(A)(3) (discussing the rights of third parties). As a result, co-owners who ultimately decide to go into business together will be incentivized to quickly form a filing entity that provides limited liability. That formation will reintroduce statutory default rules, *see supra* notes 106–107 and accompanying text, and will minimize the amount of time when gap-fillers are unavailable.

While these behaviors are possible, it should be noted that Enterprise and ETP worked together under their contractual non-partnership agreements for approximately five months, which is not an insignificant amount of time. *See* Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P., 593 S.W.3d 732, 734–36 (Tex. 2020). Moreover, it is by no means certain that a disclaimer of partnership will only control *inter se* disputes. *See infra* Part IV(A)(3). If such a disclaimer also governs third-party disputes, the partnership rule of personal liability for business debts will not apply, and the co-owners will have less reason to transition their business into a filing entity.

121. *See* RUPA § 101(7) (defining "partnership agreement" as "the agreement, whether written, oral, or implied, among the partners concerning the partnership, including amendments to the partnership agreement"); RUPA (2013) § 102(12) (substantially the same). An agreement disclaiming partnership may not fall within the "partnership agreement" definition. It is not "among . . . partners," and it arguably does not "concern[] the partnership." *See* Leahy, *supra* note 118, at 282 n.233. Nevertheless, "[a]s a general matter, contracts can be oral or implied unless the Statute of Frauds requires that they be in writing." *Id.* at 282. As a result, an agreement disclaiming partnership—even if it does not constitute a "partnership agreement"—can likely be oral or implied in most instances, as it would not typically fall within the statute of frauds.

> with after-the-fact claims that they had orally or implicitly agreed not to be partners because the burden of proof of establishing the existence of a partnership is on the proponent of partnership, and courts generally do not make credibility determinations on summary judgment. This would leave honest owners of informal co-owned businesses . . . uncertain about the rules governing their businesses.
>
> . . . .
>
> Under current law, agreements not to be partners are not binding if a factfinder concludes that the parties otherwise satisfied the definition of partnership . . . . The [*Enterprise*] decision would completely upend this law and leave business co-owners who have no written partnership agreement without any certainty that their business relationships are in fact partnerships. . . . [E]very informal business in which the owners believe they are partners would be advised to immediately sign a written agreement declaring that they are partners to ward off future claims by disgruntled co-owners that they had orally agreed otherwise.
>
> Partners who did not promptly adopt such an agreement would be left deeply uncertain about the rules that govern their business. If a court were to conclude that they were never partners, then that would only begin the inquiry about the rules that govern the business. The court could conclude that the parties were merely contracting at arms' length. Or, the court could find that the parties orally or implicitly agreed to other rules to govern their co-owned business; if so, the court would then have to decide the content of these supposed oral or implied rules. This is precisely the type of ad hoc decision making that the partnership statute is designed to avoid.[122]

In short, allowing conclusive disclaimers of partnership will lead to uncertainty about the operating rules for the parties' business relationship.[123] This uncertainty can present itself when the parties agree to disclaim partnership status without providing comprehensive rules for their association, but it can also result from disputes between the parties over whether a disclaimer was entered into at all.

3. Denying the Rights of Third Parties

Partnership law provides third parties with a number of rights, including the right to sue partners for partnership obligations and the right to rely upon a partner's statutory apparent authority.[124] RUPA § 103 explicitly states that a partnership agreement cannot restrict the rights of third parties,[125] which indicates that RUPA and adopting state

122. Leahy, *supra* note 118, at 284–86 (footnotes omitted).

123. *See generally* Anthony D'Amato, *Legal Uncertainty*, 71 CALIF. L. REV. 1, 5–7 (1983) (observing that uncertainty in the law "may deter activity that the state wants to encourage" and "leav[es] persons unsure of their entitlements while affording unfettered discretion to official decisionmakers").

124. *See, e.g.*, RUPA §§ 301, 306(a); RUPA (2013) §§ 301, 306(a). *See generally* RUPA §§ 301–308 (addressing "relations of partners to persons dealing with partnership"); RUPA (2013) §§ 301–308 (same).

125. *See* RUPA § 103(b)(10) (stating that a partnership agreement may not "restrict rights of third parties under this [Act]"); RUPA (2013) § 105(c)(17) (stating that a partnership agreement may not "restrict the rights

legislatures do not permit agreements between co-owners in a non-filing, profit-seeking business to alter third-party rights. If parties can conclusively disclaim partnership status even while fully acting as partners, it completely circumvents this principle, as parties can effectively deny the rights of third persons while associating as co-owners in a non-filing, profit-seeking business. Any court reaching this result would seem to have directly undermined the policy choice made by the state's legislature when RUPA was adopted. Moreover, such a result violates a basic principle of contract law, as an agreement between parties typically cannot take away the rights of non-parties.[126] Contracts require assent, and it would be highly unusual for an outside third party to have assented to a non-partnership agreement between the venturers.[127]

The *Enterprise* court seemed to recognize the problems of allowing a disclaimer of partnership to affect third-party rights. The first sentence of the opinion described the issue in the case as "whether Texas law permits parties to conclusively agree that, *as between themselves*, no partnership will exist unless certain conditions are satisfied."[128] The court later noted that "[a]n agreement not to be partners unless certain conditions are met will ordinarily be conclusive on the issue of partnership formation *as between the parties*,"[129] and it stated in a footnote that "[s]uch an agreement would not, of course, bind third parties, and we do not consider its effect on them."[130] The court's intention, it appears, was to hold that a disclaimer of partnership was binding on the alleged partners themselves, but would have no effect on third parties. The consequence of this rationale is that the partnership formation test can differ depending on the identity of the plaintiff. In a third-party's suit alleging partnership formation, the inquiry will be governed solely by whether the alleged partners' conduct meets the legal definition of partnership in RUPA § 202. In an *inter se* suit alleging partnership formation, however, the inquiry into conduct is irrelevant if the parties agreed to disclaim partnership status.

The problem with the court's effort to impose a conduct-based formation test for third-party disputes and an agreement-based formation test for *inter se* disputes is that RUPA seems to forbid such an approach. RUPA § 308(e)—a provision with a Texas analog that neither the court nor the parties cited or mentioned in any way—states that, with the exception of a partnership-by-estoppel claim,[131] "persons who are not partners as to each

under this [act] of a person other than a partner").

126. *See, e.g.*, IMG Worldwide, Inc. v. Westchester Fire Ins. Co., No. 1:11 CV 1594, 2015 WL 5093428, at *5 n.10 (N.D. Ohio Aug. 28, 2015) ("A contract between two parties cannot be held to negatively alter the rights of a non-party to the contract."); *cf.* EEOC v. Waffle House, Inc., 534 U.S. 279, 294 (2002) ("It goes without saying that a contract cannot bind a nonparty.").

127. *See, e.g.*, Mohsen Manesh, *Creatures of Contract: A Half-Truth About LLCs*, 42 DEL. J. CORP. L. 391, 409–10 (2018) (stating that "one only becomes a party to a contract if she objectively manifests her assent to the contract's terms," and observing that "[a]bsent such assent, one is not bound to the contract").

128. Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P., 593 S.W.3d 732, 734 (Tex. 2020) (emphasis added).

129. *Id.* at 741 (emphasis added).

130. *Id.* at 741 n.34.

131. A "partnership in fact" is a business that has met the legal definition of partnership in RUPA § 202 (or RUPA (2013) § 202). A partner in such a business is a "partner in fact." A "partnership by estoppel" is not an actual partnership at all. It is a theory of liability that is based on a representation of partner status to a third party who then enters into a transaction in reliance on the representation. *See* RUPA § 308(a)–(b); RUPA (2013) § 308(a)–(b); BROMBERG & RIBSTEIN, *supra* note 20, § 2.11[A], at 2-136.1 ("Liability under U.P.A. § 16 and R.U.P.A. § 308 is based on how the relationship is represented to third parties rather than on the existence of a

other are not liable as partners to other persons."[132] The implication is that if parties can use a disclaimer to conclusively avoid a finding of partnership as to each other, that same disclaimer will also prevent a partnership finding as to a third party.[133] While the *Enterprise* court does not appear to have intended this result, its holding and its failure to comment on the application of RUPA § 308(e) leaves room for future litigants to push for this extension to the third-party setting. Such an extension would compound the problems associated with the holding, as a partnership disclaimer would allow parties to fully act as partners while sidestepping the statutory obligations owed to third-party outsiders who deal with partners. Is there any way to avoid this undesirable result?[134] An examination of the history of RUPA § 308(e) is helpful in exploring this question.

a. The Doctrine of Partnership as to Third Persons

Under English partnership law in the late 18th century, the sharing of profits was

true partnership."); *id.* at 2-137 (stating that "liability is based on (1) a holding out of a person as a partner, (2) by or with the consent of the one held out, and (3) reasonable reliance by the plaintiff"). Put simply, if X (not a partner in fact) consents to being held out by Y and Z (partners in fact) as a partner of Y and Z, and if a third party enters into a transaction in reliance on that holding out, the person(s) being held out (X) and the persons doing the holding out (Y and Z) are liable to the third party as if they were all partners in fact. *See id.* ("U.P.A. § 16 and R.U.P.A. § 308 provide for liability both of the one held out as partner . . . and of those doing the holding out . . . ."). Estoppel liability (which RUPA and RUPA (2013) call "purported partner" liability) "is the exclusive basis for imposing liability as a partner on persons who are not partners in fact." RUPA § 308 cmt.

132. RUPA § 308(e); *accord* RUPA (2013) § 308(e); *see* TEX. BUS. ORGS. CODE ANN. § 152.053(b) (West 2006).

133. Once again, RUPA § 308(e) and RUPA (2013) § 308(e) carve out a partnership-by-estoppel theory of liability. *See supra* note 131 and accompanying text. Thus, these statutory provisions are only addressing partnership-in-fact liability—i.e., if persons are not partners in fact as to each other, they cannot be partners in fact as to third parties. *See supra* note 131 (discussing partners in fact).

134. One might argue that this result is not undesirable. Perhaps a third party should never be able to impose partnership liability on a person unless the third party entered into a transaction in reliance on a representation of partner status. In other words, perhaps a third party should only be able to impose partnership liability via an estoppel theory. *See* RUPA § 308; RUPA (2013) § 308; *supra* note 131 (discussing partnership by estoppel).

A full consideration of this issue is beyond the scope of this Article. Nevertheless, it should be mentioned that current law does not limit a third party to an estoppel theory of recovery. Under RUPA § 306(a), "all partners are liable jointly and severally for all obligations of the partnership," regardless of whether a third party even knows that he is dealing with a partnership. *See also* RUPA (2013) § 306(a) (substantially the same). In addition, limiting a third party to an estoppel theory would deny a recovery to many tort victims, as such victims would not be able to establish that they entered into a transaction in reliance on a representation of partner status. *See* RUPA § 308(a) (stating that a person represented as a partner is liable "to a person to whom the representation is made, if that person, relying on the representation, enters into a transaction with the actual or purported partnership"); RUPA (2013) § 308(a) (same); *see also* BROMBERG & RIBSTEIN, *supra* note 20, § 2.11[D], at 2-148 ("In tort cases there will rarely be liability under a partnership by estoppel theory because the victim did not rely."). Finally, allowing a third party who did not know that he was dealing with a partnership to recover from persons whom he did not know were partners is analogous to the liability of an undisclosed principal under agency law. A third party dealing with an agent for an undisclosed principal is permitted to recover from the principal, even though the third party did not rely on (or even know of) the principal's existence when entering into the transaction. *See* RESTATEMENT (THIRD) OF AGENCY §§ 1.04(2)(b), 6.03, 7.03 (AM. L. INST. 2006); *cf.* RUPA § 301 (stating that "[e]ach partner is an agent of the partnership for the purpose of its business"). Simply put, specific reliance is not always the primary concern of the law. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 20, § 2.01[C], at 2-9 ("A partnership between X and Y may have the outward-looking consequence of imposing personal liability on Y for third-party debts incurred by X. The result in the case ought to depend on the policies relating to vicarious liability.").

considered to be conclusive evidence of partnership formation in lawsuits brought by third parties.[135] In *Waugh v. Carver*,[136] two ship agents who operated separate and distinct businesses "enter[ed] into an agreement to share, in certain proportions, the profits of their respective commissions, and the discount on tradesmen's bills employed by them in repairing the ships consigned to them."[137] Their agreement also provided that "neither shall be answerable for the acts or losses of the other, but each for his own."[138] Lord Chief Justice Eyre's opinion suggested that, as between the ship agents themselves, a partnership was not established:

> [I]t is plain upon the construction of the agreement, if it be construed only between the Carvers and Giesler [the ship agents], that they were not nor ever meant to be partners. They meant each house to carry on trade without risk of each other, and to be at their own loss. Though there was a certain degree of control at one house, it was without an idea that either was to be involved in the consequences of the failure of the other, and without understanding themselves responsible for any circumstances that might happen to the loss of either.[139]

Because the ship agents shared a portion of each other's profits, however, the court concluded that the agents were liable as partners "to all persons with whom either contracts as such agent":

> [U]pon the authority of *Grace v. Smith* . . . he who takes a moiety of all the profits indefinitely, shall, by operation of law, be made liable to losses, if losses arise, upon the principle that by taking a part of the profits, he takes from the creditors a part of that fund which is the proper security to them for the payment of their debts. That was the foundation of the decision in *Grace v. Smith*, and I think it stands upon the fair ground of reason.[140]

The *Waugh* decision gave rise to the so-called doctrine of "partners as to third persons"—a doctrine that created partnership liability to third parties based solely on profit sharing, even if a partnership would not be found in a dispute between the alleged partners themselves.[141] Although this doctrine was heavily criticized,[142] it influenced a number of American courts,[143] and it remained the law of England for almost a century.[144]

135. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 20, § 2.01[C], at 2-10; *id.* § 2.06[B][3], at 2-72 to 2-73.

136. 126 Eng. Rep. 525 (1793).

137. *Id.* at 525; *see also* ROWLEY, SIVE & ROWLEY, *supra* note 68, § 7.0(B), at 107 (discussing *Waugh*).

138. *Waugh*, 126 Eng. Rep. at 525.

139. *Id.* at 532.

140. *Id.* at 525, 532.

141. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 20, § 2.06[B][3], at 2-73.

142. *See, e.g.*, ROWLEY, SIVE & ROWLEY, *supra* note 68, § 7.0(B), at 109 n.11.

143. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 20, § 2.06[B][3], at 2-73; ROWLEY, SIVE & ROWLEY, *supra* note 68, § 7.0(C), at 118, 122.

144. *Waugh* and its accompanying partners-as-to-third-persons doctrine was effectively overruled in England by *Cox v. Hickman*, 11 Eng. Rep. 431, 431 (1860). The *Cox* court backed off the notion that a person's participation in profits conclusively established the person's partnership liability to third parties:

> [I]t was argued that as they would be interested in the profits, therefore they would be partners. But this is a fallacy. It is often said that the test, or one of the tests, whether a person not ostensibly a partner, is nevertheless, in contemplation of law, a partner, is, whether he is

In the United States, the passage of UPA effectively abolished the doctrine of partners as to third persons.[145] UPA § 7(4) (followed by RUPA § 202(c)(3) and RUPA (2013) § 202(c)(3)) provided that profit sharing was only prima facie (rather than conclusive) evidence of partnership.[146] The provision also specified certain "low-participation profit-sharing relationships" that did not give rise to an inference of partnership, including "leasing of property, employment for wages, and extension of credit."[147] More importantly, UPA § 7(1) (followed by RUPA § 308(e) and RUPA (2013) § 308(e)) stated that, with the exception of partnership-by-estoppel situations, "persons who are not partners as to each other are not partners as to third persons."[148] This provision was designed to repudiate the doctrine of partners as to third persons and to make it clear that a uniform test was to govern the partnership formation question.[149] If a partnership in fact did not exist between the partners themselves, there was no partnership at all—regardless of who was asserting the claim:

> U.P.A. Section 7 contained the rules to determine the existence of a partnership, the first of which was: "Except as provided by section 16 [dealing with partnership by estoppel] persons who are not partners as to each other are not partners as to third persons." Section 202, which is the successor to U.P.A. Section 7, no longer contains this rule concerning partnerships as to third persons. Rather, the rule is located in Section 308(e): "Except as otherwise provided in subsections (a) and (b) [dealing with partnership by estoppel, which RUPA calls "purported partner" liability], persons who are not partners as to each other are not liable as partners to other persons."
>
> The rule in Section 308(e) is a critical concept in the definition of partnership. It is a repudiation of the doctrine of "partnership as to third persons." Under that doctrine, courts found that partnerships existed in

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> entitled to participate in the profits. This, no doubt, is, in general, a sufficiently accurate test; for a right to participate in profits affords cogent, often conclusive evidence, that the trade in which the profits have been made, was carried on in part for or on behalf of the person setting up such a claim. But the real ground of the liability is, that the trade has been carried on by persons acting on his behalf. When that is the case, he is liable to the trade obligations, and entitled to its profits, or to a share of them. It is not strictly correct to say that his right to share in the profits makes him liable to the debts of the trade.

Id. at 446–47; *see also* ROWLEY, SIVE & ROWLEY, *supra* note 68, § 7.0(B), at 112 ("[T]he rule of the test of sharing profits . . . was the well-established rule of English law for almost a century, when it was practically overruled in 1860 in the case of *Cox v. Hickman*.").

145. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 20, § 2.06[B][3], at 2-73. Even before UPA was promulgated, a number of American courts had rejected the doctrine. *See, e.g.*, ROWLEY, SIVE & ROWLEY, *supra* note 68, § 7.0(C), at 122 ("While some of the American courts followed . . . the doctrine of Waugh v. Carver, many of them soon broke away from it . . . after the rule was changed in England by Cox v. Hickman.").

146. *See* UPA (1914) § 7(4); RUPA § 202(c)(3) & cmt. 3 (substantially the same as UPA § 7(4), but "[t]he sharing of profits is recast as a rebuttable presumption of partnership . . . rather than as prima facie evidence thereof"); RUPA (2013) § 202(c)(3) & cmt. (substantially the same).

147. BROMBERG & RIBSTEIN, *supra* note 20, § 2.06[B][3], at 2-73.

148. UPA § 7(1); *see* RUPA § 308(e) (substantially the same); RUPA (2013) § 308(e) (substantially the same); *see also supra* note 131 (discussing partnership by estoppel).

149. *See infra* note 150 and accompanying text.

> order to spread liability for losses to third parties in cases in which no partnership would have been found if the issue had been rights and liabilities among the alleged partners. The suppression of the doctrine of partnership as to third persons is intended to apply a uniform test to determine the existence of a partnership: either there is a partnership or there is not. Thus, apart from the purported partner rules, those who are not partners as among themselves are not liable as partners to third parties.[150]

150. DONN, HILLMAN & WEIDNER, *supra* note 26, § 202, at 167 (footnote omitted); *see* Roethke v. Sanger, 68 S.W.3d 352, 360 (Ky. 2001) ("The latter [Kentucky] statute is a verbatim adoption of section 7 of the UPA and represents a repudiation of the ancient doctrine of 'partnership as to third persons' under which courts formerly implied the existence of partnerships in order to spread liability for losses to third parties in cases where no partnership would otherwise be found."); Martin v. Peyton, 158 N.E. 77, 78 (N.Y. 1927) ("Much ancient learning as to partnership is obsolete. Today only those who are partners between themselves may be charged for partnership debts by others."); *see also* RUPA § 308 cmt. ("Subsection (e) is derived from UPA Section 7(1). It means that only those persons who are partners as among themselves are liable as partners to third parties for the obligations of the partnership, except for liabilities incurred by purported partners under Sections 308(a) and (b).").

In Texas, commentators also recognized that UPA would repudiate the doctrine of partners as to third persons:

> Moreover, adoption of the act would eliminate the vague "partners as to third persons" doctrine that has found some support in the Texas cases. Under this doctrine the courts apply a less strict test and require less evidence to establish a partnership as to a third person, even in the absence of the elements of partnership by estoppel, than to show the existence of a partnership as among the partners. In Texas the doctrine manifests itself in a tendency on the part of the courts to give more weight to the "actual intention," including expressions of intent, of the alleged partners when the question involves rights and obligations among themselves, than they do when the dispute is between the alleged partner and a third person. One objection to the doctrine is its vagueness and uncertainty. In addition there is no valid reason for imposing liability to a third person on someone associated with the owner of a business in some such capacity as lender or landlord, where there are no elements of estoppel present,z if there are missing from their relationship certain attributes essential to their being held partners inter se. The act eliminates these objections by declaring that except in the case of partnership by estoppel, "persons who are not partners as to each other are not partners as to third persons."

Byron D. Sher & Alan R. Bromberg, *Texas Partnership Law in the 20th Century—Why Texas Should Adopt the Uniform Partnership Act*, 12 SW. L.J. 263, 267–68 (1958) (footnotes omitted). Interestingly, by giving more weight to the subjective intent of the partners in *inter se* disputes, the *Enterprise* court returns Texas partnership law (at least in part) to the position that was eliminated when UPA was adopted.

Despite the fact that UPA § 7(1) and RUPA/RUPA (2013) § 308(e) were intended to make clear that a uniform test governs the partnership formation question, Delaware purports to apply a different standard of proof in an *inter se* dispute. *See, e.g.*, Ramone v. Lang, No. Civ. A. 1592-N, 2006 WL 905347, at *12 (Del. Ch. Apr. 3, 2006) ("It is important to note that [w]here the suit is between the parties as partners, stricter proof is required of the existence of a partnership than where the action is by a third person against either actual partners or persons sought to be charged as partners." (internal quotation omitted)); DONN, HILLMAN & WEIDNER, *supra* note 26, § 308, at 293 ("Neither R.U.P.A. nor its predecessor is explicit that a uniform test is to be applied. It is thus perhaps not surprising that there has been slippage in the case law. Delaware is one influential R.U.P.A. jurisdiction that continues to state that different standards apply if no third-party claimant is involved." (footnote omitted)).

In contrast to Delaware, the Supreme Court of Nebraska has observed:

> We have said that where the plaintiff is alleging a partnership with the defendant, which the defendant denies, the plaintiff must establish the existence of the partnership by clear and convincing evidence. In contrast, where a third party to the alleged partnership has brought the action, the third party need only prove the existence of a partnership by a preponderance of the evidence. Thus, we have required more convincing evidence to prove the existence of a

b. Limiting the Effect of RUPA § 308(e)

If RUPA/RUPA (2013) § 308(e) was designed to impose "a uniform test to determine the existence of a partnership,"[151] decisions like *Enterprise* are problematic.[152] Under such decisions, when disclaimers of partnership are present in *inter se* disputes, the formation inquiry is based solely on the parties' subjective intent to avoid partnership. Yet when such disclaimers are present in third-party disputes, the formation inquiry is based on a holistic review of the parties' conduct. Given the different approaches, those who are not partners as among themselves may very well be liable as partners to third parties.

To ensure that a disclaimer of partnership does not affect the rights of non-party third persons, it is clear that § 308(e) has to be narrowly construed or ignored. Perhaps it could be argued that the sole function of the statutory provision was to eliminate the doctrine of partners as to third persons.[153] In other words, one might argue that the provision's sole purpose was to convey that the sharing of profits does not conclusively establish a partnership as to third parties, and the section has no application beyond that purpose.[154] Of course, RUPA/RUPA (2013) § 202(c)(3) already indicates, in a much more direct manner, that the sharing of profits does not conclusively establish a partnership.[155] Determining that § 308(e) does nothing more than convey the same principle seems odd.

As an alternative construction, perhaps § 308(e) should be understood as simply applying to conduct-based analyses when the parties have not disclaimed partnership status by agreement. Put differently, assuming that the legal definition of partnership is now a

> partnership where the alleged partners are the only litigants than where the controversy is between a third party and the partners.
>
> . . . .
>
> We have never explained, nor is there any reasoning to support, the confusing myriad of standards we have applied to what is, effectively, the same legal issue. Thus, we believe that the tenuous distinction between actions by alleged partners inter sese and actions by a third party against the alleged partnership should be abolished. . . .
>
> Generally, in both law and equity, proof . . . of alleged contracts between the parties need only be shown by a preponderance of the evidence. We see no reason to hold out a special standard for partnership relations that favors the party denying the relationship over the party asserting that the partnership exists. . . . By eliminating any common-law distinctions as to the burden of proof between actions alleging a partnership inter sese and actions by third parties, we bring greater predictability and consistency to partnership determinations.

In re KeyTronics, 744 N.W.2d 425, 438–39 (Neb. 2008) (footnotes omitted).

151. *See supra* text accompanying note 150.

152. *Cf.* BROMBERG & RIBSTEIN, *supra* note 20, § 2.01[C], at 2-10 to 2-11 ("The attempt in the U.P.A. and R.U.P.A. to eliminate distinctions between third-party cases and cases between the purported partners except those based on estoppel has the advantage of bringing predictability to the partnership determination. However, this idea appears to be inconsistent with the cases that have said that the parties' intent to be treated as partners, as distinguished from their intent to engage in a relationship that contains the prerequisites of partnership, is controlling only in actions among the partners." (footnote omitted)).

153. *See supra* Part IV(A)(3)(a).

154. *See supra* Part IV(A)(3)(a).

155. *See supra* notes 146–147 and accompanying text.

"default test,"[156] perhaps the application of § 308(e) can be limited to when that conduct-based default definition has not been displaced by a non-partnership agreement. When the default definition is applicable, § 308(e) ensures that the same conduct will be relevant to the partnership formation inquiry in the same way, regardless of whether a third-party or an *inter se* dispute is involved. Understood in this manner, there is a "uniform test to determine the existence of a partnership,"[157] but only when that test is applicable by default due to the absence of a partnership disclaimer.

As mentioned, a narrow interpretation of § 308(e) is necessary to ensure that parties cannot use a partnership disclaimer to deny the rights of third persons, such as the right to sue partners for partnership obligations and the right to rely upon a partner's statutory apparent authority.[158] It is by no means certain that a court will accept such an interpretation, which creates the risk that an *Enterprise*-like holding will also affect the rights of non-parties to the disclaimer.[159] No strained interpretation is necessary, however, if disclaimers of partnership are not considered dispositive in *inter se* disputes. Such disclaimers would be evidence of the parties' subjective intent to avoid partnership but would have no binding effect.[160] Partnership would remain a legal definition that, if met by the parties' conduct, would give rise to a mandatory conclusion of partnership formation. Consistent with RUPA/RUPA (2013) § 202(a), a partnership could be found "whether or not the persons intend to form a partnership,"[161] and under § 308(e), there would be one uniform conduct-based test to determine the existence of a partnership. In fact, the ability to easily harmonize § 202(a) and § 308(e) when rejecting dispositive partnership disclaimers suggests that such a rejection is consistent with the intent of the drafters of RUPA.

156. *See supra* Part III(B)(1).

157. *See supra* text accompanying note 150.

158. *See supra* notes 124–126 and accompanying text. Even if a court were willing to narrowly construe § 308(e) in a manner that limited the dispositive effect of partnership disclaimers to *inter se* disputes, allowing such disclaimers raises, as previously discussed, significant concerns related to the existence of fiduciary duties and the presence of operating rules for the business. *See supra* Part IV(A)(1)–(2).

159. The point here is not that third parties will definitively be unable to find a legal theory to overcome the loss of partnership rights. For example, with respect to partner liability for partnership obligations, perhaps a third party could establish that venturers with a non-partnership agreement should each be viewed as an agent of the other, such that all of the venturers are responsible for the business-related actions of each of them. *Cf.* RESTATEMENT (THIRD) OF AGENCY §§ 1.04(2)(b)–(c), 6.02–6.03, 7.03 (AM. L. INST. 2006) (discussing the liability of unidentified and undisclosed principals for an agent's actions). The point is simply that (a) creative lawyering will be necessary (with no assurance of success) to overcome the loss of rights that partnership law now guarantees to third parties, and (b) those third-party rights were lost because of a non-partnership agreement to which the third parties did not assent.

160. Given the "whether or not the persons intend to form a partnership" language of RUPA § 202(a), *see supra* text accompanying notes 28–32, evidence of the parties' subjective intent to avoid partnership should not be particularly compelling. Nevertheless, in a close case where the evidence for and against the existence of a partnership is mixed, such evidence might tip the scales. *See supra* note 32.

161. RUPA § 202(a); *accord* RUPA (2013) § 202(a); *see supra* text accompanying notes 28–32.

V. BENEFITS OF ALLOWING PARTIES TO CONTRACT OUT OF PARTNERSHIP

A. Promoting Freedom of Contract

Modern society has long valued freedom of contract.[162] As a general matter, letting parties structure their affairs as they see fit, free from governmental interference, is viewed as a social good.[163] Courts routinely cite freedom of contract as an important public policy,[164] and even some statutes in the business organizations area tout the importance of enforcing the parties' agreement.[165] The *Enterprise* court itself relied heavily upon the policy of freedom of contract in its analysis:

> [I]f there is one thing which more than another public policy requires it is that men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts when entered into freely and voluntarily shall be held sacred and shall be enforced by Courts of justice. Therefore, you have this paramount public policy to consider—that you are not lightly to interfere with this freedom of contract.[166]

Providing parties with the discretion to contract out of partnership status, even while fully acting as partners, would certainly promote freedom of contract. A non-partnership agreement would control over the statutory definition of partnership and would allow the parties to fully act as partners while avoiding *inter se* (and perhaps third-party) partnership consequences. This result could be reached without the necessity of forming a filing entity, and the venture would not be subject to any business organization statute.

The law restricts freedom of contract in a number of contexts, however, particularly

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162. *See, e.g.*, Samuel Williston, *Freedom of Contract*, VI CORNELL L.Q. 365, 366 (1921) (stating that "Adam Smith, Ricardo, Bentham, and John Stuart Mill successively insisted upon freedom of bargaining as the fundamental and indispensable requisite of progress; and imposed their theories on the educated thought of their times"); *see also* JOSEPH M. PERILLO, CALAMARI AND PERILLO ON CONTRACTS § 1.3, at 4–5 (5th ed. 2003) (observing that "[t]he law of contracts permeates every aspect of our society" and noting that "the parties' power to contract as they please for lawful purposes remains a basic principle of our legal system"); David P. Weber, *Restricting the Freedom of Contract: A Fundamental Prohibition*, 16 YALE HUM. RIGHTS & DEV. L.J. 51, 52 (2013) (noting the "prevalence of contract in modern society" and stating that "[t]he right to contract is one of those fundamental rights in our society that is frequently lauded").

163. *See, e.g.*, E. ALLAN FARNSWORTH, CONTRACTS § 1.7, at 20 (3d ed. 1999) ("From a utilitarian point of view, freedom to contract maximizes the welfare of the parties and therefore the good of society as a whole. From a libertarian point of view, it accords to individuals a sphere of influence in which they can act freely."); DAVID SCHULTZ, THE ENCYCLOPEDIA OF AMERICAN LAW 284 (2002) ("This freedom of contract principle rests on the idea that it is in the public interest to allow individuals to structure their affairs through binding agreements free from government interference.").

164. *See, e.g.*, Bombardier Aerospace Corp. v. SPEP Aircraft Holdings, LLC, 572 S.W.3d 213, 230 (Tex. 2019).

165. *See, e.g.*, DEL. CODE ANN. tit. 6, § 15-103(d) (2013) ("It is the policy of this chapter to give maximum effect to the principle of freedom of contract and to the enforceability of partnership agreements."). *See generally* Daniel S. Kleinberger & Douglas K. Moll, *The Limited Effect of "Maximum Effect,"* BUS. L. TODAY (Aug. 13, 2020), https://businesslawtoday.org/2020/08/limited-effect-maximum-effect/ [https://perma.cc/6UNC-56SJ] (discussing the limited practical significance of the "maximum effect" language in the LLC setting).

166. *See* Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P., 593 S.W.3d 732, 738 (Tex. 2020) (quoting Wood Motor Co. v. Nebel, 238 S.W.2d 181, 185 (Tex. 1951)); *see also id.* at 739 (stating that "[w]e have never squarely addressed whether parties' freedom to contract for conditions precedent to partnership formation can override the statutory default test").

when private parties seek to alter legal definitions. For example, if the circumstances surrounding a particular worker fall within the legal definition of "employee," contractual efforts to characterize the worker as an "independent contractor" are ineffective, even when the dispute is between the parties to the contract themselves.[167] Similarly, in the business organizations setting, if the legal definition of "agency" is established, contractual denials of an agency relationship do not change the result.[168] This is true even when the dispute is

167. *See, e.g.*, Hopkins v. Cornerstone Am., 545 F.3d 338, 341–42, 346 (5th Cir. 2008) (concluding that former "Sales Leaders" of Cornerstone, who agreed to be independent contractors of Cornerstone but who later sued claiming that they were employees, were in fact employees who were entitled to overtime wages under the Fair Labor Standards Act). As the Fifth Circuit explained:

> Specifically, Cornerstone notes that the Sales Leaders contractually agreed to be, and actually believed themselves to be, independent contractors. While this may be accurate, '[s]ubjective beliefs cannot transmogrify objective economic realities. A person's subjective opinion that he is a businessman rather than an employee does not change his status.' Furthermore, 'facile labels . . . are only relevant to the extent that they mirror economic reality.'

Id. at 356 (quoting Brock v. Mr. W Fireworks, Inc., 814 F.2d 1042, 1044, 1049 (5th Cir. 1987)); *cf.* Blea v. Fields, 120 P.3d 430, 436 (N.M. 2005) ("How an employment contract defines the status of an individual, while relevant and material, does not answer whether an individual is a public employee or an independent contractor. We must also consider the extent to which the employer has, in the broadest sense, the right to control the individual."); Newspapers, Inc. v. Love, 380 S.W.2d 582, 590 (Tex. 1964) ("It has been definitely established that a form of written agreement will not prevent the existence of a master-servant relationship when such contract is a mere sham or a cloak designed to conceal the true legal relationship between the parties."); Space City Oil Co. v. McGilvray, 519 S.W.2d 257, 259 (Tex. Civ. App. 1975) (stating that "the written contract is important, but the test [for employee versus independent contractor] remains right of control which may be shown by actual control exercised in derogation of a written contract").

One might object to this example on the grounds that the employer-employee relationship is generally characterized by unequal bargaining power, which explains the restrictions on freedom of contract. Parties to a non-partnership agreement may or may not have the same bargaining power disparities. The point here, however, is more modest: freedom of contract does not always prevail when countervailing policies are at stake, and such countervailing policies exist in the partnership context. *See supra* Part IV(A) (discussing the costs of allowing parties to contract out of partnership).

168. *See, e.g.*, RESTATEMENT (THIRD) OF AGENCY § 1.02 cmt. a (AM. L. INST. 2006) ("Whether a relationship is one of agency is a legal conclusion made after an assessment of the facts of the relationship and the application of the law of agency to those facts. Although agency is a consensual relationship, how the parties to any given relationship label it is not dispositive. Nor does party characterization or nonlegal usage control whether an agent has an agency relationship with a particular person as principal."); *id.* cmt. b ("The parties' agreement may negatively characterize the relationship as not one of agency, or as one not intended by the parties to create a relationship of agency or employment. Although such statements are relevant to determining whether the parties consent to a relationship of agency, their presence in an agreement is not determinative and does not preclude the relevance of other indicia of consent."); *id.* cmt. c ("Whether an actor has a relationship of agency with a particular principal, with one possible principal as opposed to another, with multiple principals, or is a coagent or a subagent, or is not an agent at all, is resolvable only by applying the legal definition of agency to the facts of the relationship. . . . How the parties characterized the relationship is not dispositive, nor is popular usage."); RESTATEMENT (SECOND) OF AGENCY § 1 cmt. b (AM. L. INST. 1958) ("Agency is a legal concept which depends upon the existence of required factual elements . . . . The relation which the law calls agency does not depend upon the intent of the parties to create it, nor their belief that they have done so. To constitute the relation, there must be an agreement, but not necessarily a contract, between the parties; if the agreement results in the factual relation between them to which are attached the legal consequences of agency, an agency exists although the parties did not call it agency and did not intend the legal consequences of the relation to follow."); *infra* note 169.

between the agent and the principal who agreed to the denial,[169] and even though agency, like partnership, imposes fiduciary duties and other obligations on the parties.[170] Other examples in the business organizations setting, such as the inability to eliminate the implied covenant of good faith and fair dealing,[171] underscore that freedom of contract—even between the parties to the contract—is not absolute.[172]

B. Providing Certainty on the Partnership Formation Question

As mentioned, partnership formation is considered to be a totality-of-the-circumstances inquiry into the parties' conduct. If a court concludes that sufficient evidence exists of the factual predicates of partnership (e.g., sharing of profits and control), the legal definition of partnership is satisfied.[173]

The problem with a totality-of-the-circumstances inquiry is that a court's conclusion as to whether a partnership exists can be difficult to predict, especially when the evidence is mixed. Dean William Draper Lewis, the principal drafter of the 1914 UPA,[174] was aware of this uncertainty generated by the partnership definition, but he viewed it as a necessary consequence of the partnership serving as the residual form of co-owned, for-profit business organization:

> . . . [I]t will always be possible to give a number of real or supposititious cases in which men will differ as to whether the facts show co-ownership of a given business. The uncertainty lies in the fundamental characteristic which distinguishes partnerships from every other business association. All other business associations are statutory in origin. They are formed by the happening of an event designated in a statute as necessary to their formation. In corporations this act may be the issuing of a charter by the proper officer of the state; in limited partnerships, the filing by the associates of a specified document in a public office. On the other hand, an infinite number of combinations of circumstances may result in co-ownership of a business. Partnership is the residuum, including all forms of co-ownership, of a business except those business associations organized under a specific

169. *See, e.g.*, RESTATEMENT (THIRD) OF AGENCY § 1.02 cmt. (AM. L. INST. 2006) (Reporter's Notes) (citing cases for the proposition that "[a]s between the parties to an agreement, an assertion or negation of agency is not determinative"); *supra* note 168.

170. *See, e.g.*, RESTATEMENT (THIRD) OF AGENCY §§ 8.01–8.15 (AM. L. INST. 2006) (addressing the agent's duties to the principal, including the "fiduciary duty to act loyally for the principal's benefit," and the principal's duties to the agent).

171. *See, e.g.*, DEL. CODE ANN. tit. 6, § 15-103(b) (2013) (stating that a "partnership agreement may not . . . [e]liminate the implied contractual covenant of good faith and fair dealing").

172. As another example, in the commercial law area, § 9-109 of the Uniform Commercial Code states that Article 9 applies to "a transaction, regardless of its form, that creates a security interest in personal property or fixtures by contract." U.C.C. § 9-109 (AM. L. INST. & UNIF. L. COMM'N 2001). The Official Comment notes that "[w]hen a security interest is created, this Article applies regardless of the form of the transaction or the name that parties have given to it." *Id.* cmt. 2. In addition, "the subjective intention of the parties with respect to the legal characterization of their transaction is irrelevant to whether this Article applies." *Id.*

173. *See supra* notes 24–27 and accompanying text.

174. *See* BROMBERG & RIBSTEIN, *supra* note 20, § 1.02[B], at 1-17 (noting that William Draper Lewis, Dean of the University of Pennsylvania Law School, took over the drafting of the Uniform Partnership Act, changed it radically from the approach of his predecessor, and completed it in 1914).

statute.

> If a partnership act were to declare that a partnership was not formed until the formal requirements of the statute were complied with, it would not be a statute regulating common law partnerships, but one abolishing common law partnership and establishing a new form of statutory association. If no formal act can be specifically designated as a necessary prerequisite to the formation of a common law partnership, it follows that it is not always easy to determine whether the acts proved indicate co-ownership of a business.[175]

Despite the fact that uncertainty as to partnership formation was knowingly incorporated into UPA (and followed in RUPA),[176] some have asserted that it is problematic for parties to not know whether they are partners—and whether they are subject to the duties and obligations of partners—until a court or jury tells them as much.[177]

175. William Draper Lewis, *The Uniform Partnership Act*, 24 YALE L.J. 617, 622 (1915); *see also* Leahy, *supra* note 118, at 270 n.168 (observing that "it is impossible for businesspeople to obtain perfect certainty about formation of a partnership").

176. UPA's totality-of-the-circumstances inquiry into partnership formation was followed by RUPA and RUPA (2013). *See* UPA §§ 6–7; RUPA § 202; RUPA (2013) § 202; *see also* RUPA § 202 cmt. 1 (noting that "Section 202 combines UPA Sections 6 and 7," but observing that "[n]o substantive change in the law is intended").

This notion of uncertainty as to partnership formation should not be overstated. Parties can protect themselves from a partnership finding by not acting like partners. Avoiding the sharing of profits, for example, is almost certain to defeat a partnership claim. If profits are to be shared, designing the relationship to fit within one of the "low-participation profit-sharing relationships" of RUPA § 202(c)(3) would help to rebut any inference of partnership. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 20, § 2.07[D], at 2-106 ("Once one of the relationships specified in [UPA § 7(4) or RUPA § 202(c)(3)] is shown, the proponent of partnership must present evidence of partnership other than profit sharing in order to survive a motion for directed verdict or similar motion."); *supra* note 147 and accompanying text.

177. *See, e.g.*, Brief of Respondent at 2, Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P., 593 S.W.3d 732 (Tex. 2020) (No. 17-0862) [hereinafter Enterprise Respondent Brief] (asserting that the inability to enter into a dispositive disclaimer of partnership "would result in a legal limbo, where parties cannot know whether they are partners until a jury decides").

The *Enterprise* court effectively made this same argument by citing an earlier decision of the Supreme Court of Texas where the court "expressed skepticism that the Legislature 'intended to spring surprise or accidental partnerships on independent business persons.'" Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P., 593 S.W.3d 732, 738 (Tex. 2020) (quoting Ingram v. Deere, 288 S.W.3d 886, 898 (Tex. 2009)); *see also id.* at 740 ("We maintain our view expressed a decade ago in *Ingram* that the Legislature did not 'intend[] to spring surprise or accidental partnerships' on parties." (quoting *Ingram*, 288 S.W.3d at 898)).

The language from the earlier *Ingram* decision, however, was used only to suggest that a partnership conclusion should not be reached unless sufficient evidence exists of the factors that are relevant to the partnership definition. *See Ingram*, 288 S.W.3d at 898 ("Even conclusive evidence of only one factor normally will be insufficient to establish the existence of a partnership. To hold otherwise would create a probability that some business owners would be legally required to share profits with individuals or be held liable for the actions of individuals who were neither treated as nor intended to be partners. *The Legislature does not indicate that it intended to spring surprise or accidental partnerships on independent business persons, if, for example, an employee is paid out of business profits with no other indicia of a de facto partnership* under [the Texas Revised Partnership Act]." (emphasis added) (citations omitted) (footnote omitted)). To use the *Ingram* language as support for the proposition that parties should be able to definitively contract out of partnership is a far cry from how it was actually used by the *Ingram* court.

In addition, the case law in Texas and elsewhere is replete with decisions involving courts that imposed

This uncertainty arguably makes parties reluctant to collaborate on business ventures. Moreover, if collaboration occurs, the uncertainty may produce substantial litigation costs if a party contends that it has partnership-related rights.

If disclaimers of partnership are dispositive, parties would have the ability to conclusively block a general partnership finding.[178] The parties would not owe the duties and obligations of partners, and they would avoid the possibility of an expensive dispute over whether a partnership was formed. Nevertheless, unless the dispositive nature of the disclaimer was extended, via RUPA § 308(e), to claims brought by third parties,[179] these benefits of greater certainty would be limited to *inter se* disputes. Even in that context, certainty on the formation question would be offset by any uncertainty about the operating rules for the business, which may produce its own substantial litigation costs.[180]

VI. WEIGHING THE COSTS AND BENEFITS

A. Within the General Partnership

In weighing the costs and benefits of permitting dispositive disclaimers of partnership, it is important to focus on what the parties are actually seeking. With respect to the benefit of promoting freedom of contract, for example, the general partnership form of business is designed to promote contractual flexibility, even without *Enterprise*-like decisions. RUPA expressly provides that "relations among the partners and between the partners and the partnership are governed by the partnership agreement," and "[t]o the extent the partnership agreement does not otherwise provide, this [Act] governs relations among the partners and between the partners and the partnership."[181] Given this contractual freedom, what do parties gain from having the ability to disclaim partnership status in *inter se* disputes? If

"surprise or accidental partnerships" upon parties who did not seek to form such ventures. *See, e.g.*, Howard Gault & Son, Inc. v. First Nat'l Bank of Hereford, 541 S.W.2d 235, 236–37 (Tex. Civ. App. 1976) (noting that the written agreements stated that "the parties are not engaged in the transaction as partners but as landlord and tenant," but nevertheless concluding that "their farming operation was a partnership"); *see also* Lupien v. Malsbenden, 477 A.2d 746, 748–49 (Me. 1984) (concluding that a partnership was formed, even though the parties "may well have viewed their relationship to be that of creditor-borrower, rather than a partnership"). Such "surprise or accidental partnerships" are a necessary consequence of the partnership serving as the default or residual form of co-owned, for-profit business organization. *Cf. Lupien*, 477 A.2d at 748 (stating that "[i]f the arrangement between the parties otherwise qualifies as a partnership, it is of no matter that the parties did not expressly agree to form a partnership or did not even intend to form one"); Beecher v. Bush, 7 N.W. 785, 785 (Mich. 1881) ("It is nevertheless possible for parties to intend no partnership and yet to form one. If they agree upon an agreement which is a partnership in fact, it is of no importance that they call it something else; or that they even 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."); *Gault*, 541 S.W.2d at 237 ("The statement in one of the agreements that the farming operation was not a partnership is not conclusive on the question of partnership. It is the intent to do the things that constitute a partnership that determines that the relationship exists between the parties, and if they intend to do a thing which in law constitutes a partnership, they are partners whether their expressed purpose was to create or avoid the relationship.").

178. While it is true that dispositive disclaimers of partnership would provide certainty on the partnership formation question, parties can also avoid a partnership finding by not acting like partners. *See supra* note 176.

179. As discussed, such an extension would have its own problems. *See supra* Part IV(A)(3).

180. *See supra* Part IV(A)(2).

181. RUPA § 103; *see* RUPA (2013) § 105 (substantially the same).

dispositive disclaimers are permitted, the parties will still need a detailed agreement to specify how their contractual venture will operate.[182] If dispositive disclaimers are prohibited, the parties may be held to be partners, but they can still employ a detailed agreement to specify how their partnership venture will operate. In either case, freedom of contract is promoted because the parties retain the ability to structure their business as they see fit. What then turns on the ability to avoid the partnership characterization?

The answer is that partnership statutes typically carve out some mandatory rules that the parties' agreement cannot alter.[183] Unquestionably, the most important of these rules in the *inter se* setting is the inability to eliminate the fiduciary duty of loyalty (and, to a lesser extent, the inability to eliminate the fiduciary duty of care).[184] Indeed, for most parties, it is likely that entering into a disclaimer of partnership is primarily (if not exclusively) an effort to avoid the fiduciary duties that would otherwise be owed if a partnership were formed.[185] Thus, the freedom of contract provided by definitive non-partnership agreements is, at bottom, the freedom to eliminate fiduciary duties by agreement. Similarly, the desire for certainty on the partnership formation question derives largely from the desire to confirm the absence of partner fiduciary duties.

As mentioned, given that RUPA prohibits the elimination of fiduciary duties, allowing parties who are acting as partners to use a disclaimer to avoid such duties seems like an impermissible circumvention of the statute.[186] In addition, there are good policy reasons supporting the inability to eliminate fiduciary duties, including the lack of information provided by eliminations and cognitive biases that make it difficult to foresee future risks.[187] Safeguarding partners from abuse by other partners is clearly the goal behind such prohibitions, and freedom of contract has never been absolute when other important interests are at stake.

Perhaps most importantly, although it is true that partner fiduciary duties cannot be eliminated, the duties can be substantially limited. Even without recognizing dispositive disclaimers of partnership, in other words, parties retain substantial control over their fiduciary duty exposure.[188] With respect to the duty of loyalty, RUPA prohibits elimination of the duty, but it permits the partnership agreement to "identify specific types or categories of activities that do not violate the duty of loyalty, if not manifestly unreasonable."[189] In addition, RUPA allows "all of the partners or a number or percentage specified in the partnership agreement [to] authorize or ratify, after full disclosure of all material facts, a

182. *See supra* Part IV(A)(2).

183. *See, e.g.*, RUPA § 103(b); RUPA (2013) § 105(c); *see also* RUPA § 103 cmt. 1 ("Only the rights and duties listed in Section 103(b) . . . are mandatory and cannot be waived or varied by agreement beyond what is authorized. Those are the only exceptions to the general principle that the provisions of RUPA with respect to the rights of the partners *inter se* are merely default rules subject to modification by the partners.").

184. *See* RUPA § 103(b)(3)–(4); RUPA (2013) § 105(c)(5), (d).

185. *See, e.g.*, Leahy, *supra* note 118, at 267 (noting the suggestion of Enterprise that "the entire point of avoiding partnership was to avoid owing each other [Enterprise and ETP] fiduciary duties").

186. *See supra* text accompanying notes 89–92.

187. *See supra* Part IV(A)(1)(a)–(b).

188. *See, e.g.*, BROMBERG & RIBSTEIN, *supra* note 20, § 6.07[H], at 6-119 ("As with respect to other rights and duties among the partners, the partners may agree to alter the standard form fiduciary duties to suit their particular relationship.").

189. RUPA § 103(b)(3)(i); *see* RUPA (2013) § 105(d)(3).

specific act or transaction that otherwise would violate the duty of loyalty."[190] This language provides partners with significant flexibility to authorize foreseeable conduct that would otherwise raise duty of loyalty issues:

> RUPA attempts to provide a standard that partners can rely upon in drafting exculpatory agreements. It is not necessary that the agreement be restricted to a particular transaction. That would require bargaining over every transaction or opportunity, which would be excessively burdensome. The agreement may be drafted in terms of types or categories of activities or transactions, but it should be reasonably specific.
>
> A provision in a real estate partnership agreement authorizing a partner who is a real estate agent to retain commissions on partnership property bought and sold by that partner would be an example of a "type or category" of activity that is not manifestly unreasonable and thus should be enforceable under the Act. Likewise, a provision authorizing that partner to buy or sell real property for his own account without prior disclosure to the other partners or without first offering it to the partnership would be enforceable as a valid category of partnership activity.
>
> Ultimately, the courts must decide the outer limits of validity of such agreements, and context may be significant. It is intended that the risk of judicial refusal to enforce manifestly unreasonable exculpatory clauses will discourage sharp practices while accommodating the legitimate needs of the parties in structuring their relationship.
>
> . . . .
>
> Subsection (b)(3)(ii) is intended to clarify the right of partners, recognized under general law, to consent to a known past or anticipated violation of duty and to waive their legal remedies for redress of that violation. This is intended to cover situations where the conduct in question is not specifically authorized by the partnership agreement. It can also be used to validate conduct that might otherwise not satisfy the "manifestly unreasonable" standard.[191]

190. RUPA § 103(b)(3)(ii); *see* RUPA (2013) § 105(d)(1)(A).

191. RUPA § 103 cmts. 4, 5.

With respect to the duty of care, RUPA indicates that the duty may not be "unreasonably reduce[d]" by the partnership agreement. RUPA § 103(b)(4); *see* RUPA (2013) § 105(c)(5), (d)(3)(C). While an elimination of the duty of care would presumably violate this provision, modifications are permitted:

> Under subsection (b)(4), the partners' duty of care may not be unreasonably reduced below the statutory standard set forth in Section 404(d), that is, to refrain from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law.
>
> For example, partnership agreements frequently contain provisions releasing a partner from liability for actions taken in good faith and in the honest belief that the actions are in the best interests of the partnership and indemnifying the partner against any liability incurred in connection with the business of the partnership if the partner acts in a good faith belief that he has authority to act. Many partnership agreements reach this same result by listing various activities and stating that the performance of these activities is deemed not to constitute gross negligence or willful misconduct. These types of provisions are intended to come within the

Courts have upheld a variety of provisions in partnership agreements that modify the duty of loyalty, including provisions permitting competition with the partnership,[192] authorizing self-dealing or other benefits from partnership transactions,[193] and allowing for certain partnership opportunities to be taken by individual partners.[194]

Within the general partnership form, therefore, parties have the ability to use a partnership agreement to significantly control the reach of fiduciary duties. Freedom of contract, although not absolute, is respected under modern partnership law. In addition, to the extent certainty on the question of partnership formation is desired because it resolves the issue of partner fiduciary duties, a careful delineation of what will be considered permissible conduct is likely to be enforced. While a dispositive non-partnership agreement may reduce litigation costs by allowing for the likelihood of summary judgment on a partnership-based breach of fiduciary duty claim,[195] it is already possible to obtain

> modifications authorized by subsection (b)(4). On the other hand, absolving partners of intentional misconduct is probably unreasonable. As with contractual standards of loyalty, determining the outer limit in reducing the standard of care is left to the courts.
>
> The standard may, of course, be increased by agreement to one of ordinary care or an even higher standard of care.

RUPA § 103 cmt. 6.

192. *See, e.g.*, Whalen v. Connelly, 545 N.W.2d 284, 291–92 (Iowa 1996); Singer v. Singer, 634 P.2d 766, 768, 772 (Okla. App. 1981); *see also* Alloy v. Wills Family Tr., 944 A.2d 1234, 1253–57 (Md. Ct. Spec. App. 2008) (assuming that a provision in the partnership agreement was specific enough to permit competition, but affirming a judgment for breach of fiduciary duty based on a failure to disclose the competing transactions: "In this case, even if we were to assume that the Trust waived certain competition aspects of the duty of loyalty . . . it did not thereby waive its right to be notified of such Partnership opportunities and conflicts."); BROMBERG & RIBSTEIN, *supra* note 20, § 6.07[E], at 6-111 ("As with respect to partnership opportunities, the scope of permissible competition may be determined by the parties' expectations at the outset of the relationship or by the partnership agreement."); *id.* § 6.07[H][2], at 6-123 to 6-124 ("Courts have held that partners may be permitted to benefit from transactions outside or competing with the partnership by provisions in the partnership agreement.").

A Delaware court similarly observed:

> I think it a correct legal conclusion that where a partnership, by virtue of an unambiguous clause in its partnership agreement which authorizes competition with the partnership, is on notice that the partners intend to compete directly with the partnership, it hardly can be said to have a legitimate 'expectancy' to be informed of—let alone participate 100% in—relevant investments.

Kahn v. Icahn, No. Civ. A. 15916, 1998 WL 832629, at *3 (Del. Ch. Nov. 12, 1998).

193. *See, e.g.*, Carella v. Scholet, 773 N.Y.S.2d 763, 765 (App. Div. 2004); Marmac Inv. Co. v. Wolpe, 759 A.2d 620, 624–27 (D.C. 2000); *see also* BROMBERG & RIBSTEIN, *supra* note 20, § 6.07[H], at 6-125 ("The parties' agreement may authorize not only benefit from the dealings outside the partnership but also self-dealing or benefit from partnership transactions.").

194. *See, e.g.*, Dremco, Inc. v. South Chapel Hill Gardens, Inc., 654 N.E.2d 501, 539–40 (Ill. App. Ct. 1995); Fronk v. Fowler, 883 N.E.2d 972, 976–77 (Mass. App. Ct. 2008); Cowin v. Ross, 406 N.Y.S.2d 841, 841–42 (App. Div. 1978); *see also* BROMBERG & RIBSTEIN, *supra* note 20, § 6.07[D], at 6-104 ("It is important to note that the partnership opportunity doctrine can be (and very commonly is) waived by agreement in investment partnerships such as those dealing with real estate, oil and gas, securities, futures contracts, and agriculture.").

195. This assumes that the non-partnership agreement is in writing. If the purported agreement is oral or implied, obtaining summary judgment may be difficult. *See supra* notes 121–122 and accompanying text. Moreover, even with a dispositive non-partnership agreement, there may still be considerable litigation costs, as an aggrieved plaintiff may simply focus on other claims (e.g., breach of contract, including breach of the implied covenant of good faith and fair dealing).

summary judgment on the basis that the partnership agreement permitted the challenged conduct.[196]

On balance, the costs of allowing parties to contract out of partnership outweigh the benefits. Permitting dispositive disclaimers of partnership allows those acting as partners to circumvent the prohibition on eliminating fiduciary duties, which will leave many business co-owners vulnerable to abusive conduct by their fellow venturers.[197] Moreover, if a disclaimer is dispositive, the parties' contract will need to provide all of the rules for the operation of the business. Given the challenges of drafting complete contracts, it is likely that courts will confront disputes that are difficult to resolve due to a lack of contractual and statutory guidance.[198] Finally, in light of RUPA § 308(e), it will be difficult for courts to confine the effect of dispositive disclaimers to *inter se* disputes.[199] While permitting dispositive disclaimers does promote freedom of contract and provide increased certainty on the partnership formation question,[200] those benefits are largely tied to the parties' desire to control their fiduciary duty exposure—a desire that existing partnership law can accommodate.[201] Further, any increased certainty brought about by dispositive disclaimers will be offset, at least to some extent, by increased uncertainty generated by parties (a) who will draft incomplete agreements to govern their relationship, and (b) who will claim the existence of an oral or implied disclaimer of partnership well after the commencement of their co-owned, for-profit business.[202]

B. Beyond the General Partnership

Parties seeking freedom of contract and certainty on the partnership formation question have another option beyond the confines of the general partnership setting. By forming a limited liability company (LLC) in a jurisdiction such as Delaware that explicitly permits the elimination of fiduciary duties, the parties can ensure a business arrangement with the contractual flexibility and arm's length relationship that they desire.[203]

196. *See, e.g.*, Dremco, Inc. v. South Chapel Hill Gardens, Inc., 654 N.E.2d 501, 536, 539–40, 543 (Ill. App. Ct. 1995) (affirming a summary judgment on a partnership opportunity claim based in large part on an "agreement [that] memorialized . . . the partners' right to independently pursue other opportunities"); Cowin v. Ross, 406 N.Y.S.2d 841, 841–42 (App. Div. 1978) (granting summary judgment on a partnership opportunity claim based on the language of the limited partnership agreement that permitted some of the partners to pursue a new development); *see also* Kahn v. Icahn, No. Civ. A. 15916, 1998 WL 832629, at *3 (Del. Ch. Nov. 12, 1998) (granting a motion to dismiss on plaintiffs' breach of fiduciary duty claim based on a provision in the partnership agreement that permitted the general partner to "compete, directly or indirectly with the business of the Partnership").

197. *See supra* text accompanying notes 89–93.

198. *See supra* Part IV(A)(2).

199. *See supra* Part IV(A)(3).

200. *See supra* Part V(A).

201. *See supra* text accompanying notes 183–196.

202. *See supra* Part IV(A)(2).

203. *See, e.g.*, Leahy, *supra* note 118, at 257 ("If Enterprise and ETP wished to avoid a partnership and the resulting fiduciary duties, then these companies should have formed a Delaware LLC (or perhaps even a Texas LLC) and agreed that it was the exclusive vehicle to govern their potential business relationship."); *id.* at 257–58 ("If Enterprise and ETP wished to avoid forming a partnership with relative certainty, they should have taken two simple steps at (or near) the outset of their negotiations: (1) form a filing entity, such as an LLC, and (2) designate that entity as the sole vehicle for their (possible) joint venture. If ETP and Enterprise had done so, they could have easily avoided partnership and the resulting fiduciary duties."); *id.* at 269 ("In fact, sophisticated parties can easily

RUPA makes clear that "[a]n association formed under a statute other than this [Act], a predecessor statute, or a comparable statute of another jurisdiction is not a partnership under this [Act]."[204] By forming a Delaware LLC at the inception of a prospective business relationship, therefore, the parties can negotiate terms between themselves and commence business without having to worry about the possibility of forming a general partnership.[205] The Delaware Limited Liability Company Act (DLLCA) provides significant deference to freedom of contract, as it states that "[i]t is the policy of this chapter to give the maximum effect to the principle of freedom of contract and to the enforceability of limited liability company agreements."[206] Perhaps most importantly, DLLCA indicates that fiduciary duties "may be expanded or restricted *or eliminated* by the provisions in the limited liability company agreement."[207]

Of course, forming an LLC requires a filing with the state,[208] and there is a fee associated with that filing. The fee, however, is relatively minor; in Delaware, it is only $90.[209] An LLC will also typically have a detailed operating agreement that covers how the business will be run, and one would expect attorney's fees involved with the drafting of that agreement.[210] A dispositive disclaimer of partnership, however, will also give rise

avoid forming unwanted partnerships and design their relationships as they see fit by forming an LLC instead of attempting simply to disclaim partnership.").

204. RUPA § 202(b); *accord* RUPA (2013) § 202(b); *see* text accompanying notes 22–24.

205. *See, e.g.*, Leahy, *supra* note 118, at 261–62 ("If two parties that are exploring a joint venture form an LLC to govern their nascent business relationship, their relationship will by definition never ripen into a partnership. Even if a factfinder later concludes that the parties were co-owners of a for-profit business, the applicable partnership statute (be it in Texas or elsewhere) precludes a finding of partnership absent unusual circumstances that sophisticated parties can easily avoid."); *id.* at 263–64 (describing cases "where courts have held that a partnership exists between the owners of a filing entity in addition to the filing entity itself," but concluding that "[w]hen parties form an LLC at the outset of their business negotiations and specify in the LLC's governing documents that any business arising out of their negotiations will be governed solely by their LLC, courts in Texas (and elsewhere) will respect their decision to govern their business as an LLC rather than a partnership" (footnote omitted)).

206. DEL. CODE ANN. tit. 6, § 18-1101(b) (2013); *see also* Leahy, *supra* note 118, at 268 ("If Enterprise and ETP had agreed to form a Delaware LLC to govern their potential joint venture, they would have enjoyed near-total freedom to define the terms of their potential joint venture.").

207. DEL. CODE ANN. tit. 6, § 18-1101(c) (2013) (emphasis added); *see also* Leahy, *supra* note 118, at 265 (stating that "[t]here is no doubt that members of a Delaware LLC can entirely eliminate *any and all* fiduciary duties owed by managers and/or managing members of the LLC").

208. *See, e.g.*, DEL. CODE ANN. tit. 6, § 18-201 (2013).

209. *See* DEL. DEP'T OF STATE, DIVISION OF CORPORATIONS FEE SCHEDULE (Aug. 1, 2020), https://corpfiles.delaware.gov/Augustfee2020.pdf [https://perma.cc/67PA-VWCV]; *see also* Leahy, *supra* note 118, at 260 (describing the formation of a Delaware LLC, noting its low filing fee, and stating that the "potential owners and managers" need not be publicly disclosed).

A Delaware LLC does not have to file an annual report, but it does have to pay a yearly tax of $300. *See* Delaware Division of Corporations, *Annual Report and Tax Instructions*, https://corp.delaware.gov/paytaxes/ [https://perma.cc/VC3H-8GAN]. If an LLC formed in Delaware is going to transact business in another state, it will have to register as a foreign LLC, which will incur another fee. *See, e.g.*, Leahy, *supra* note 118, at 260 (noting that if a Delaware LLC were to transact business in Texas, it would need to register and pay a $750 fee).

210. The state filing for purposes of forming the LLC, *see* text accompanying note 208, requires very minimal information and a lawyer's assistance is not required. *See, e.g.*, DEL. CODE tit. 6, § 18-201(a) (2013) (requiring the certificate of formation to include only the name of the LLC, the address of its registered office, and the name and address of its registered agent). Nevertheless, if a lawyer is used to draft the filing, a modest additional amount of attorney's fees will be incurred.

to the need for a detailed agreement that provides the rules for the operation of the business.[211] As a result, any formation fee differential between (1) a co-owned business organized contractually via a dispositive non-partnership agreement, and (2) a co-owned business organized as an LLC, is not likely to be meaningful. If differences (in cost or otherwise) are meaningful to particular parties, however, they can always forego an LLC and work with the tools provided in the general partnership setting—including significant freedom of contract and the ability to limit fiduciary duties—to structure their relationship as they desire.

The fact that parties can use an LLC to obtain the benefits of promoting freedom of contract and achieving certainty on the partnership formation question is significant. It reveals that purported business needs can be accommodated without altering the general partnership's status as the residual form of co-owned, for-profit business organization in all circumstances[212]—including when the parties act as partners but seek to disclaim partnership status. The general partnership can continue to serve that residual role while protecting partners from difficult-to-foresee exploitation and providing default operating rules for courts to resolve disputes.[213] Further, there is no need to strain to interpret (or completely ignore) statutory language that (a) indicates that the parties' subjective intent to avoid partnership is of little relevance, and (b) links the formation inquiry in the *inter se* and third-party settings.[214] While one might question the merits of a business organization statute (such as DLLCA) that provides relatively few default rules and the ability to eliminate fiduciary duties,[215] the point here is that there is no reason to extend that state of affairs to the general partnership setting, as parties have a viable choice.[216] They can

211. *See supra* Part IV(A)(2).

212. *See supra* notes 22–24 and accompanying text.

213. *See supra* Part IV(A)(1)–(2) (discussing fiduciary duties and default rules in the general partnership setting).

214. *See supra* Parts III(B)(2), IV(A)(3) (discussing the legality of partnership disclaimers and the effect of RUPA § 308(e)).

215. *See* Daniel S. Kleinberger, *Don't Dabble in Delaware*, BUS. L. TODAY (July 2017), https://businesslawtoday.org/2017/Iont-dabble-in-delaware/ [https://perma.cc/PLG2-XGCT] (noting that DLLCA "has only a skeletal set of default rules, unlike the [Uniform LLC Act] and the LLC statutes of most nonuniform states," and also observing that DLLCA "stand[s] out by authorizing an operating agreement to eliminate all fiduciary duties"); *supra* note 207 and accompanying text. This Article has, of course, questioned the merits of a statute that provides relatively few default rules and the ability to eliminate fiduciary duties. *See supra* Part IV(A)(1)–(2).

216. Indeed, while it is true that freedom of contract can be promoted by minimizing the number of mandatory rules associated with a particular business form, freedom of contract can also be promoted by offering entrepreneurs a menu of organizational choices, each with its own distinct set of mandatory rules, and allowing owners to select the form that best suits their needs. This latter approach has the advantage of providing choice while eliminating (via the mandatory rules) the need for parties to negotiate almost every term of their arrangement. A legislature may very well prefer the transaction-cost savings offered by this approach. *Cf.* John Armour, Henry Hansmann & Reinier Kraakman, *What is Corporate Law?*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 22 (2d ed. 2009) ("When used in conjunction with a choice of corporate *forms*, [mandatory rules] can perform an enabling function similar to that served by default rules."); *id.* ("More particularly, mandatory rules can facilitate freedom of contract by helping corporate actors . . . signal the terms they offer . . . . The law accomplishes this by creating corporate forms that are to some degree inflexible (i.e., are subject to mandatory rules), but then permitting choice among different corporate forms."); *id.* at 23 ("Thus, paradoxically, greater rigidity within any particular form may actually enhance overall freedom of contract in structuring private enterprise, so long as there is a sufficiently broad range of alternative forms to

establish an LLC that promotes freedom of contract and permits the elimination of fiduciary duties, or they can form a general partnership that respects freedom of contract and provides substantial flexibility to modify (but not eliminate) such duties.[217]

VII. CONCLUSION

"And although the question of intent is a crucial part of the calculus, the only necessary intent . . . is an intent to do those things which constitute a partnership."[218]

"[O]ne analyzes whether the parties acted as partners, not whether they subjectively intended to create, or not to create, a partnership."[219]

For over one hundred years, partnership statutes in this country have made clear that a partnership is formed when two or more persons associate to carry on as co-owners a

choose from.").

217. Even if the costs of dispositive disclaimers of partnership generally outweigh the benefits, one might argue that sophisticated parties should be able to arrange their affairs as they see fit. *Cf.* Energy Transfer Partners, L.P. v. Enter. Prods. Partners, L.P., 593 S.W.3d 732, 738 (Tex. 2020) ("Texas courts regularly enforce conditions precedent to contract formation and reject legal claims that are artfully pleaded to skirt unambiguous contract language, *especially when that language is the result of arm's-length negotiations between sophisticated business entities*." (emphasis added)). Although permitting dispositive disclaimers would provide less information about potential conflicts and would subject the parties to the dangers of cognitive limitations, *see supra* Part IV(A)(1), sophisticated parties would presumably have the resources to mitigate these risks (e.g., insurance) or to simply absorb them if they came to pass. With sophisticated parties, in other words, there might be less of a concern with the cost of undermining the protections of fiduciary duty and a correspondingly greater emphasis on the benefit of promoting freedom of contract.

While this position is undoubtedly more defensible than permitting dispositive disclaimers when an unsophisticated party is involved, such a position still raises concerns. First, and as mentioned, even sophisticated parties will have difficulty preparing a fully comprehensive agreement, which means that courts will need to resolve disputes without a set of organizational default rules to fall back on. *See supra* notes 113, 116–20 and accompanying text. Although the parties might be comfortable with this risk, the judiciary's interest in resolving disputes consistently, efficiently, and without unnecessary difficulty is not well-served. Second, if dispositive disclaimers of partnership also govern third-party disputes, the fact that sophisticated persons entered into a disclaimer does not alleviate the problem of taking away the rights of non-parties. *See supra* Part IV(A)(3).

Third, and most importantly, permitting dispositive disclaimers of partnership between sophisticated parties would create new difficulties relating to the need to define "sophisticated." Would sophisticated status be recognized based on financial data such as assets or income? Experience with hedging or insuring against risk? Knowledge of partnership law and the scope of fiduciary duties? A history of disclaiming partnership in other co-owned ventures? There are also definitional issues within each metric—e.g., what amount of assets or income would be sufficient? Would these metrics be established by statute, or would courts have to resolve particular disputes over whether the parties were sophisticated enough? Finally, there is simply no need to wrestle with such inquiries when sophisticated parties already have a choice—they can establish an LLC that permits the elimination of fiduciary duties, or they can work within the general partnership structure to limit their fiduciary duty exposure. *See supra* Part VI. In short, while limiting dispositive disclaimers of partnership to sophisticated parties is preferable to a more general application, such an approach still poses a number of challenges.

218. Hilco Prop. Servs., Inc. v. United States, 929 F. Supp. 526, 537 (D.N.H. 1996) (internal quotation omitted).

219. Byker v. Mannes, 641 N.W.2d 210, 216 (Mich. 2002).

business for profit—regardless of whether the persons intend to form a partnership.[220] By allowing parties to contract out of partnership, even while fully acting as partners, decisions like *Enterprise* flout this statutory language and threaten to upend national partnership law. More importantly, permitting parties to contract out of partnership imposes substantial costs by undermining the protections of fiduciary duty, creating uncertainty about the operating rules for the business, and threatening to deny the rights of third parties. These costs outweigh the benefits of promoting freedom of contract and providing certainty on the partnership formation question, particularly because such benefits can largely be captured within existing partnership and LLC law.[221]

Ducks are not horses; ducks are ducks. Partnership law has long recognized this simple truism and should continue to prohibit parties from contracting out of partnership. Denying that a conduct-based partnership is a partnership, in other words, should remain just as ineffective as denying that a duck is a duck.

220. *See* UNIF. P'SHIP ACT § 6(1) (UNIF. L. COMM'N 1914); RUPA § 202(a) & cmt. 1; RUPA (2013) § 202(a) & cmt.

221. *See supra* Parts IV–VI.