

**EMPLOYMENT APPEAL TRIBUNAL**  
58 VICTORIA EMBANKMENT, LONDON EC4Y 0DS

At the Tribunal  
On 25 November 2008  
Judgment handed down on 21 April 2009

**Before**

**HIS HONOUR JUDGE BIRTLES**

**MR T MOTTURE**

**MR D WELCH**

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MR M KOVATS

APPELLANT

1) TFO MANAGEMENT LLP  
2) THE FAMILY GROUP OF COMPANIES

RESPONDENTS

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Transcript of Proceedings

JUDGMENT

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## APPEARANCES

For the Appellant

MR OLIVER HYAMS  
(of Counsel)  
Instructed by:  
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For the Respondent

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## **SUMMARY**

### **JURISDICTIONAL POINTS: Worker, employee or neither**

Can a partner in a limited liability partnership be an employee? The EAT decided that on the facts of the case the Appellant was a partner in a limited liability partnership and not an employee. Appeal dismissed.

## **HIS HONOUR JUDGE BIRTLES**

### **Introduction**

1. This is an appeal from the reserved judgment of an Employment Tribunal sitting at London Central on 19-20 May and 3 June 2008. The Employment Tribunal decided:

**“(1)On the preliminary issue with employment that the Claimant was not an employee of the First Respondent or the Second Respondent.**

**(2)The Claimant’s claims for unfair dismissal and in respect of the Respondents’ failure to provide written reasons for dismissal are struck out and dismissed as the Tribunal has no jurisdiction to consider them.”**

Mr Kovats who was the Claimant before the Employment Tribunal appeals against that judgment. The Appellant is represented by Mr Oliver Hyams of counsel and the Respondents by Mr Shaen Catherwood of counsel. We are grateful to both counsel for their written and oral submissions.

### **The material facts**

2. The Tribunal made the following relevant findings of fact which are contained in paragraph 3 of its judgment:

**“3.1 On 22 September 2004, the Claimant signed a deed of accession, agreeing to be bound by a members’ agreement for the First Respondent, which is a limited liability partnership. That Members’ Agreement was drafted and agreed on 13 May 2004. In other words, there was an intention that the Claimant become a member or partner of the First Respondent. The other members were the chief executive officer and founder of the partnership and the Family Group of Companies, Mr A Al Omran; Ms D A Jawad, and TFO Limited, the English subsidiary company. On 21 September 2004, the Claimant signed a document or letter containing additional terms and conditions of his membership of the First Respondent. It was said that in addition to the duties and obligations set out in clause 12 of the members’ agreement, he was to be authorised to manage the office of the limited liability partnership in the absence of the chief executive, and in addition to serving as a member of the LLP, his role was to perform the LLP’s advisory function in the capacity as the chief investment officer for the Family Group of Companies, in which capacity he would report directly to the chief executive and oversee all investment activities of the Family Group of Companies’ clients etc. He was given a number of specific tasks in the investment advice business of the First Respondent. In accordance with the members’ agreement, he was entitled to a fixed membership distribution of £80,000 per annum, which was intended to be a draw-down against the future profits of the business. This was a new start-up business, the start-up capital being provided either by Mr Al Omran personally or by the Family Group of Companies. The members agreement which the Claimant signed up to had a clause 12.3.1 that, subject to agreed holiday arrangements and sick leave, each member would devote his whole time and attention**

to the business during normal business hours and at any other time when it was necessary to do so to enable him to perform his duties to the LLP or any of its clients. The Claimant was entitled by the side letter to 25 days holiday per annum, which he took, and to paid sickness absence, which had to be certificated after two days. There was no notice provision within the side letter, but the membership agreement provided that he could be given six months notice at a meeting which made a general decision requiring him to retire. The Claimant chose at his own request to be paid gross and be responsible for his own income tax and national insurance. As far as we are aware, he did fill in tax returns and he paid class 4 national insurance. In a further letter he was granted the option to acquire 300,000 shares, which shares would vest in three years' time. In other words, they were of no value to the Claimant until he had been in the business for three years.

- 3.2 The Claimant was head-hunted by Mr Al Omran from HSBC, taking a cut in remuneration from about £180,000 per annum to join the First Respondent as chief investment officer. The business of the First Respondent is to provide investment advice to high net worth individuals, and the only client of the partnership was TFO Bahrain. The company structure is a somewhat complex one, but TFO Management LLP, the First Respondent, had as its members when the Claimant joined the membership, Mr Al Omran with six of the 11 shares, the Claimant with one share, Ms D Abdul-Jawad with one share and TFO Limited incorporated in the UK with three shares. TFO Limited was a wholly owned dormant company of the Family Office Company (or TFO Bahrain), which was incorporated in Bahrain. The Claimant was head-hunted because the First Respondent was looking for someone to run the London office and to manage a recruitment team, both in London and Bahrain. The First Respondent was an investment adviser to TFO Bahrain. As the CIO, the Claimant did not start work until 1 November 2004, and that is when he started to take his draw down, paid gross in 12 monthly instalments per annum. Later, in July 2005, the Claimant asked for his remuneration to be paid into two different bank accounts as a way of regulating his tax liability.
- 3.3 For the first 14 months, from January 2005 to March 2006, the Claimant was the only person working in the London office. He was establishing in the firm's presence in London, setting out the premises and IT systems and ensuring the First Respondent was compliant with its regulatory obligations. He was authorised to sign documents on behalf of the First Respondent, including the agreement to provide advisory services to TFO Bahrain, but also bank mandates, quarterly returns for accounting purposes, etc. In March 2006 he hired a deputy CIO, Mr Ven Chidambaram, who was hired as an employee and never became a member of the partnership. So far as the Bahrain team was concerned, the Claimant was sometimes involved in hiring people and sometimes not. It had been anticipated that he would spend at least one week per month in Bahrain as he was responsible for running the investment team there. In March 2006, the Claimant signed a revised membership agreement, which included provisions for profit-sharing and the ownership of assets. It appears to be the case that the Claimant was entitled to 1/11<sup>th</sup> of any profits the company made and if the partnership had been sold he would have [been] entitled [to a 1/11<sup>th</sup> share of the sale proceeds. The profit share is set out at clause 10.5 of the new agreement. There was a new clause, 12.1.9, under the duties and obligations of members, which was that the members were obliged to carry out such duties as may be agreed with the chief executive from time to time. It is also noted that by clause 19.1.5, a member could be expelled from the membership if guilty of any conduct likely to have a serious adverse effect upon the business. However, so far as retirement from the membership was concerned, then this could be done by clause 20.1.2 by a general decision requiring the member to retire on six months notice.
- 3.4 Difficulties arose with the running of the team in Bahrain. In a nutshell, the Claimant did not expect to or want to be in a hands-on role running the Bahrain team and he did not wish to travel frequently to Bahrain. He expected there to be a London based team. However, the expectation of Mr Al Omran was that the Claimant would exercise control over the Bahrain team, although this was perhaps a little unrealistic given the Claimant was based mainly in London. We find that this meant that in practice Mr Al Omran and later Mr Shafi had to step in and take decisions over the Claimant's head, that he might have been expected to take if he had had more of a hands-on day-to-day role in running the Bahrain team. Performance issues also arose and we have seen a detailed exchange of emails between the Claimant and Mr Al Omran in the early part of 2007, and indeed between the Claimant and Mr Shafi when Mr Shafi joined as chief operating officer in March 2007. It is not necessary for us to go into the detail of these performance issues for the purposes of our

determination of whether the Claimant was an employee or not. Mr Shafi found that the investment team in Bahrain seemed to lack leadership, direction and enthusiasm, and there was not much activity or energy in the London office either. Mr Shafi was tasked by Mr Al Omran to deal with these issues and to sort the matter out. Thus, we find that although the intention of the parties had been that the Claimant would run the London office and indeed the Bahrain team with a substantial amount of autonomy; gradually, over a period of time, Mr Al Omran and then Mr Shafi took on more and more direct responsibility for this work, as the Claimant appeared reluctant and unwilling to carry out his full duties. The trip to China is a good example of the Claimant's reluctance to perform his role. It was a very important trip, designed to build up business and to take place in April 2007. The Claimant was very reluctant to go on this trip, and made excuses such that he would have to travel over Easter and that he had a pre-booked holiday in Cuba. In the end, however, he did attend. However the dye was cast so far as his future was concerned, and a decision was taken on the China trip by Mr Al Omran and Mr Shafi that they would hold a membership meeting at which the Claimant would be required to retire from the partnership. Mr Al Omran felt that the London operation was not presenting good value for the group and they believed that the Claimant was not the right person to perform the CIO role. In fact, he had been offered by Mr Shafi an alternative role as strategist, with no cut in his draw down or change in his terms and conditions, but he had rejected that proposal. There were also some concerns about the Claimant's behaviour, both in his workplace in London and also on the China trip.

- 3.5 The members meeting was convened for 20 April 2007. The Claimant received very little notice of this meeting. In fact, the first notice that he received that was sent on 17 April was that there will be a general meeting of the members three days later to discuss the future operations and the role of the LLP and its members, and whether Mr Shafi should be admitted to the membership of the LLP. The first time that the Claimant's his continued membership of the LLP was referred to as a matter to be considered at the meeting was by letter dated 19 April, when the Claimant was notified that one of the matters that would be discussed would be whether he should be required to retire from the membership. At the meeting, the resolutions were voted upon, and the Claimant was required to retire. He abstained from the voting. He was required to work out his six month notice period, and he was informed that his terms of engagement would continue to be governed by the partnership document and the side letter. On 3 May 2007, the Claimant wrote to Mr Shafi saying that he had been informed of his dismissal, as he described it. This is the first time in his relationship with the Respondent that he had hinted that he might be regarding himself as an employee. On 14 May, the Claimant wrote to TFO's chairman, Mr Bill Morrison, referring to his contract of employment and that his status regarding his shares and options need to be clarified and what sort of compensation package he was being offered. Mr Al Omran responded by saying that he was not an employee of the LLP and that his status as a member of the LLP would be akin to partnership not employment. There then followed further correspondence between the parties; over the Claimant's status with the LLP.'

### **The Employment Tribunal Judgment**

3. Having set out what it said were the relevant material facts the Employment Tribunal set out the relevant law at paragraphs 4-6 of its judgment. It then reached its conclusions in

paragraphs 7-8. The Employment Tribunal said this:

“7 Having regard to our findings of relevant fact, and applying the appropriate law, and taking into account the parties’ submissions, the Tribunal has reached the following conclusions:

7.1 We have been asked to consider the various elements in the case law that distinguish a relationship; of employer/employee from that of employer and independent contractor. Undoubtedly having regard to those elements, there are many features of the relationship between the First Respondent and the Claimant that are similar to an employment relationship, such as mutuality of obligation, an element of control (which started off as being relatively relaxed, but increased as time went on and performance issues began to emerge), holidays and sick pay, the requirement to work personally for the partnership, etc.

7.2 However, we conclude that this is not the correct way to look at the relationship in the context of this case, where a partnership is being alleged. Section 4(4) of the Limited Liability Partnership Act is the starting point. That is that a member of an LLP, such as the Claimant, shall not be regarded for any purpose as employed the LLP unless, if he and the other members were partners of the partnership, he would be regarded for that purpose as employed by the partnership. The “any purpose” and “that purpose” must be regarded in this case as a reference to the Claimant’s work as chief investment officer, and we have to ask ourselves whether if this was a partnership in the normal sense, presumably under the auspices of the Partnership Act 1890, the Claimant’s role as CIO would be regarded as employment. We also have to ask ourselves whether the Claimant’s role as CIO is incompatible with the partnership agreement. We conclude that it is not and that the original agreement at clause 12.3.1 provides that members shall devote their whole time and attention to the business during normal working business hours etc, and in the revised agreement which the Claimant signed and worked to for more than a year, that by clause 12.1.9, he was obliged to carry out such duties as might be agreed with the chief executive from time to time. The letter of agreement or side letter that he signed was an agreement with the chief executive as to his duties as chief investment officer. In any normal partnership, we believe, all partners will generally have a role to play in furthering the business of the partnership. In this partnership, the Claimant’s role, because of his expertise, was to find investment opportunities for the partnership’s clients, in this case TFO Bahrain, and he was to carry out this role under the general direction of Mr Al Omran, the chief executive officer.

7.3 The parties themselves intended this to be a partnership. The Claimant came into the partnership giving up a substantial remuneration with HSBC and taking a 100% pay cut. He must have been expecting to take his share of the profit and enjoy the share options when they vested, benefits that were not given to employees. The Claimant never at any time suggested that he was an employee until he was voted out of the partnership and had taken legal advice. He signed up to two agreements and a side letter which are wholly compatible with his being a partner.

7.4 So far as the performance of the role is concerned, the Claimant had considerable autonomy in the London office and over the Bahrain investment team, and would have continued to have such control if he had performed to the standard expected of him by Mr Al Omran and later Mr Shafi. He also signed important documentation as a partner which bound the partnership, such as the investment agreement with TFO Bahrain. Other factors are that he had no direct contractual relationship with the Second Respondent, and he was a partner with the First Respondent. Importantly, if the partnership had been sold he would have been entitled to a share of the proceeds. Unlike an employee, he could and did opt to have his draw down paid gross, and account for income tax on it himself. He paid class 4 national insurance, consistent with section 13 of

the Limited Liability Partnership Act 2000 and consistent with his status as a partner rather than an employee.

- 7.5 The Claimant maintains that the arrangement was a sham. We do not agree. The relationship between the Claimant and the First Respondent persisted for over two years, and if the Claimant thought it was a sham, he would have no doubt raised this matter much earlier in the relationship and would have alleged that he was an employee and would not have signed the revised membership agreement in March 2006. Both parties genuinely considered and rightly considered that this was a true partnership arrangement. They acted at all times consistently with the partnership agreement, both in terms of the performance of the Claimant's duties and his relationship with his partners and the partnership, and also in the manner of the termination of his relationship with the partnership. Although the Claimant did not make any direct capital contribution into the business and therefore did not sustain the direct financial risk that Mr Al Omran had, nevertheless he lost out financially quite considerably when he left HSBC with a substantial cut in pay to join the First Respondent, and his share options never materialised, and indeed so long as the partnership made no profit then his loss of earnings would continue. To that extent he took a share in the loss and provided sweat equity, as Mr Al Omran characterised it. He was in a very real sense a manager of the business, and the success of the business depended to a large extent on his input.
8. Therefore the Tribunal's unanimous conclusion is that the Claimant was not an employee of either the First or the Second Respondent, and therefore the Tribunal has no jurisdiction to hear and determine his case of unfair dismissal and for compensation for failure to provide written reasons for dismissal."

### The Agreements

4. The Employment Tribunal referred in its judgment to two agreements. The Members' Agreement relating to TFO Management LLP is dated 13 May 2004: EAT bundle pages 49-79. The letter of accession signed by the Appellant dated 22 September 2004 is at EAT bundle page 84.

5. The relevant parts of the Members' Agreement seem to us to be as follows:

(a) Preamble

**"THIS MEMBERS' AGREEMENT** is dated 13 May **2004** and is made **BETWEEN:**

- (1) The persons whose names are set out in Schedule 1 ("Members"); and
- (2) TFO Management LLP, a limited liability partnership incorporated in England and Wales under the Limited Liability Partnership Act 2000 with registered number OC 307894, and having its registered office at 19 York Road, Maidenhead, Berkshire, SL6 1SQ. (the "LLP")."

- (b) **“10. Profit-sharing and ownership of assets**
- 10.1 The shares of the Members in the Net Profits and in any losses shall be allocated in accordance with the respective allocations of Units as set out in Schedule as at the relevant date.
- 10.2 The Members shall share in the Net Capital Profits of the LLP. Any profits or losses of a capital nature occurring to the LLP in accordance with their respective allocations of Units as set out in Schedule 1 as at the relevant date of the distribution.
- 10.3 The Members may, by a unanimous decision, agree to allocate a fixed distribution per annum to one or more of the Members.
- 10.4 The Members acknowledge and agree that their beneficial interest in the assets of the LLP (excluding the Current Accounts and the Regulatory Capital) shall be determined by reference to each Member’s share of the Units in issue from time to time.
- (c) **“12 Duties and obligations of Members**
- 12.1 Each Member shall at all times:
- 12.1.1 act diligently in carrying out the Business;
- 12.1.2 act with the utmost good faith in all transactions in relation to the LLP and the other Members;
- 12.1.3 provide full details on request to the Chief Executive of all transactions carried out by him or at his direction for the account or in the name of the LLP, and provide all information regarding the Business in his knowledge or possession for the Chief Executive requests from time to time;
- ...
- 12.3.1 (subject to agreed holiday arrangements and sick leave) each Member shall devote his whole time and attention to the Business during normal business hours and at any other time when it is necessary to do so to enable him to perform his duties to the LLP or any of its clients;”
- (d) **“13 Accounts**
- 13.8 Each Member may draw on account of its share of the Net Profits to such extent as the Majority of the other Members may from time to time decide, having regard to the cash resources available after the special distributions referred to in clause 14.1. If at any time there is a debit balance on the Credit Account of any of the Members it shall if so required by a Majority of the other Members repay the amount of such deficiency.”
- (e) **“14 Taxation**
- 14.1 Each Member shall be entitled to special distributions on account of its share of the Net Profits sufficient to discharge:
- 14.1.1. such Member’s personal liability to pay any tax on its income or capital gains to the extent that such liability does not exceed what it would have been if its only source of income or capital gains were its share of the Net Profit; and
- 14.1.2 such Member’s personal liability to pay its net National Insurance contributions in respect of such Net Profits.”

(f) **“17 Nature of Partnership**

17.1 Otherwise known as Members of the LLP and as set out in this Deed, nothing in this Deed shall create a partnership or establish a relationship of principal and agent or any other fiduciary relationship between or among any of the parties (including any person who has executed a Deed of Accession).

17.2 Each Member shall punctually pay and discharge its separate debts (including without limitation any liability to tax on its separate income or capital gains) and engagements, whether present or future, and shall at all times indemnify the other Members and each of them and their respective employees, agents and officers and the capital and effects of the LLP against the said debts and engagements and all actions, proceedings, costs, claims and demands in respect thereof.”

(g) **“19 Retirement and death**

19.1 A Member will cease to be a Member and become a Former Member upon:

19.1.1 his death; or

19.1.2 (if earlier) Six months elapsing from the date of a General Decision requiring him to retire.”

6. The letter dated 21 September 2004 says this:

**“Dear Michka**

**TFO Management LLP (“TFO”**

**Thank you for your interest in becoming a member of TFO. I am pleased to inform you that the current members of TFO have decided to offer you membership in TFO.**

**Your fixed membership distribution will be £80,000 per annum. You will also be granted an option to acquire 300,000 shares as follows: (i) 150,000 shares at no cost and (ii) 150,000 shares at par value of US\$1.00 (all shares will vest in accordance with Attachment 1, the Share Ownership Plan Chart). The above option will be effective as of the date that you assume your full-time Chief Investment Officer duties, and will be subject to the terms and conditions of The Family Office Share Scheme.**

**Should you accept this offer, you will be required to sign a Deed of Accession to the Members’ Agreement relating to TFO and a side agreement which sets out further terms of our arrangement. This offer of membership will remain open until 30 September 2004.**

**If you agree to become a member of TFO, please sign the enclosed copy of this letter and complete and sign Attachment 2, the Fitness and Propriety Questionnaire, and return one signed copy of this letter and the completed and signed questionnaire to me. I will then arrange for the Deed of Accession, the Members’ Agreement relating to TFO and the side agreement setting out the additional terms of membership (“Documents”) to be sent to you for your perusal and signature.**

**By countersigning this letter, you agree to keep secret and confidential the information contained in the Documents, even if you do not sign the Deed of Accession.**

**I look forward to hearing from you and working with you.**

**Yours sincerely  
Abdul Monsin Omran Al Omran  
Chief Executive”**

7. The letter signed by the Appellant on 22 September 2004 (although dated 21 September 2004) concerning additional terms and conditions of membership in TFO Management LLP is at EAT bundle pages 80-83. It says this:

“Dear Michka

**Additional Terms and Conditions of Membership in TFO Management LLP**

The purpose of this letter is to set out the additional terms and conditions of your membership of TFO Management LLP.

Unless the context requires otherwise, all capitalized expressions used in this letter have the meaning as described to such expressions in the Members’ Agreement relating to TFO Management LLP, dated 13 May 2004 (the “Members’ Agreement”).

1. *General Authority*

In addition to the duties and obligations set out in clause 12 of the Members’ Agreement, you shall be authorized to manage the office of the LLP in the absence of the Chief Executive. In this capacity you could act and sign on behalf of the LLP with respect to daily office administrative matters, provided that when the aggregate of total expenses incurred, but not approved, has reached US\$5,000 then you must obtain the approval of the Chief Executive for any further expenses.

2. *Specific Duties and Responsibilities*

The purpose of the LLP is to act as an advisor to The Family Group of Companies, its employees and its clients. In addition to serving as a Member of the LLP, your role will be to perform the LLP’s advisory function in the capacity as the Chief Investment Officer for the Family Group of Companies. In this capacity you will report directly to the Chief Executive and oversee all investment activities of the Family Office Group of Companies’ clients, including trust and family assets, and ensure that their investment transactions, policies, and procedures meet short and long term objectives and requirements as described in both portfolio-wide and individual account investment policy statements as well as other documents relating to investment goals and objectives. The primary objectives of the Chief Investment Officer are to identify suitable investment markets and vehicles for clients, manage and optimize portfolio assets and provide appropriate asset allocation programs for all clients.

As the Chief Investment Officer you shall:

- (a) establish and update investment policies, including buy and sell disciplines, asset allocation programs, return goals and benchmarks, and risk control parameters for the portfolio as a whole as well as for individual accounts;
- (b) develop and implement firm-wide asset allocation models and model portfolios and manage all investment related staff of the Family Office Group of Companies, including product specialists;
- (c) actively work with the Family Office Group of Companies’ Investment Committee, outside advisors, and investment managers to implement Investment Committee directives, and prepare and present analyses and make recommendations on investment activities to the Investment Committee on a regular basis.
- (d) oversee the management of client investments, including the approval of client risk tolerance level, setting of client customized benchmark and asset allocation, due diligence on potential new managers, manager and security selection, new manager review, manager termination, asset

monitoring, due diligence, performance review and rebalancing for the portfolio as a whole as well as for individual accounts, and provide investment support to the Family Office Group of Companies' relationship managers;

- (e) establish and manage performance measures to ensure that all portfolios perform within standards indicated by the respective client's investment policy statement or per Investment Committee instructions and to ensure that all client accounts achieve the pre-agreed, targeted rate of return and
- (f) develop and coordinate the investment managers' selection process, including the due diligence process, and monitoring the global financial markets (including assessing, developing and researching new investment management styles, including hedge funds and other alternative investments) and providing regular reports to the Chief Executive.

3. *Representation and warranty*

You represent and warrant that you are not bound by or subject to any court order, agreement, covenant, arrangement, regulatory code or undertaking or have any other interest or obligation which in any way restricts or prohibits you from becoming a Member of the LLP or from performing your role, duties and obligations in accordance with this letter and the Members' Agreement.

4. *Membership distribution*

- (a) Your fixed distribution will be £80,000 per annum. This distribution will accrue daily and is payable in equal monthly instalments in arrears on or about the 25<sup>th</sup> date of each calendar month.
- (b) The Chief Executive will review your distribution annually in February, the first such review to take place in February 2005. There is no obligation on the Members to increase your distribution.

5. *Holidays*

- (a) Your annual paid holiday entitlement is 25 working days. In your first year as a Member of the LLP, your holiday entitlement will be calculated on a pro rata basis rounded (to the nearest half day) for each completed month during the year.
- (b) Holiday dates must be agreed in advance with the Chief Executive. You will be entitled to English public holidays in addition to your annual holiday entitlement.
- (c) On retirement from the LLP, your holiday entitlement will be calculated on a pro rata basis and you will be entitled to payment in lieu of any unused entitlement. Should you be expelled from the LLP in accordance with clause 18 of the Members' Agreement, the LLP reserves the right to insist that you forfeit your entitlement to any distribution you may be entitled to as a result of unused holidays. In the event that you have exceeded your annual holiday entitlement at the date of the termination of your memberships in the LLP, the LLP reserves the right to deduct from any distribution due to you on the termination of your membership in the LLP, payment of such amount as is necessary to take into account any unearned holiday.

6. *Absence from work*

- (a) If you are absent from work for any reason you should notify the Chief Executive as soon as possible.
- (b) For any absence due to sickness for longer than two business days, you must be covered by a doctor's certificate.

- (c) The LLP reserves the right to request that you attend a medical examination with a doctor and/or occupational health advisor nominated by the LLP. In these circumstances, you agree that the LLP will be entitled to receive a copy of this report.

7. *Medical examination*

The LLP requires that you pass a medical examination performed by a doctor nominated by the LLP prior to your start date. You consent to disclosing to the appointed doctor all known illnesses which may affect your ability to serve as a Member of the LLP.

8. *Medical insurance*

- (a) You will be entitled to participate in the private medical insurance scheme that the LLP maintains for the benefit of Members, subject to the terms and conditions of the relevant policy in force from time to time.
- (b) The LLP reserves the right to withdraw or amend the relevant policy, including the level of benefits. The LLP is not liable to provide any benefits or any compensation in lieu thereof, in circumstances where the policy provider refuses to provide benefits, for whatever reason.

9. *Restrictive covenants*

You undertake with the LLP that after termination of your membership in the LLP, you will not, without the prior written consent of the Chief Executive (such consent shall not be unreasonably withheld), whether by yourself, through agents or otherwise and whether on your own or on behalf of any other person, company or other organisation, directly or indirectly for a period of 36 months:

- (a) solicit business from, endeavour to entice away or otherwise have any business dealings with any client and/or any prospective client (that has been targeted during the 12 months previous to the termination of your membership in the LLP) of the Family Office Group of Companies; or
- (b) solicit or entice away from, or endeavour to solicit or entice away, any employee to cease working for the Family Office Group of Companies, whether or not any such employee would commit any breach of their contract of employment; or
- (c) engage in any business or be associated with any person, firm or company engaged in any trade or business using the name(s) "Family Office" or incorporating the words "Family Office".

While the restrictions in this paragraph 9 are considered by the parties to be reasonable in all the circumstances, it is agreed that if any such restrictions (by themselves or taken together) are adjudged to go beyond what is reasonable in all the circumstances for the protection of legitimate interests of the Family Office Group of Companies, but would be adjudged reasonable if part or parts of the wording is deleted, the relevant restriction(s) shall apply with such deletion(s) as may be necessary to make it or them valid and effective.

10. *Choice of laws*

This letter shall be governed by and construed in accordance with the laws of England and Wales.

To acknowledge acceptance of the terms and conditions set forth in this letter, please sign the enclosed copy and return it to me.

Yours sincerely  
Abdul Mohsin Omran Al Omran  
Chief Executive

I agree with, and accept, the terms and conditions of this letter.  
[signature, Michka Kovats]  
22 Sept 2004"

8. Finally, there is the Deed of Accession dated 22 September 2004 whereby the Appellant accedes to the Members' Agreement: EAT bundle page 88.

9. The revised and restated Members' Agreement dated 15 March 2006 is at EAT bundle pages 95-125. As the Employment Tribunal notes at paragraph 3.3 of its decision (set out above) this included provisions for profit-sharing and the ownership of assets. They are contained at paragraph 10: EAT bundle pages 107-108. They say this:

- “10 Profit-sharing and ownership of assets**
- 10.1 The Chief Executive may agree to allocate a Priority Fixed Distribution per annum to one or more of the Members and such agreement shall be evidenced in writing, except that any Member shall be entitled to waive his right to receive a Priority Fixed Distribution by written notice to the Chief Executive.**
- 10.2 After the Priority Fixed Distribution has been allocated, each Member will also be allocated such amount of any remaining Net Profits as are necessary to cover any reasonable expenses of that Member in relation to which the Member which would have been able to obtain reimbursement under clause 14 but which have not otherwise been reimbursed by the LLP in accordance with clause 14.1.**
- 10.3 Of the remaining profits, there shall next be allocated to the Members:**
- (i) such amount of Net Profits as shall in the reasonable opinion of the Chief Executive (such opinion to be made in good faith) be required to be retained in the LLP as working capital to meet anticipated, current or foreseen liabilities and expenditure of the LLP and is sufficient to cover other contingencies in accordance with general principles of prudent management, which amount of Net Profits shall be treated in accordance with Clause 8.5 and shall be credited to the Members' contribution Account; and**
  - (ii) such amount of Net Profits as is necessary to meet the Member's corporation tax liability in respect of profits allocated to it under this clause 10.3 and such amount shall be credited to the Member's current Account.**
- 10.4 The remaining Net Profits shall be allocated by the Chief Executive between the Members at the absolute discretion, such discretion to be exercised reasonably and in good faith.**
- 10.5 The Members shall share in the Net Profits of the LLP and any profits or losses of a capital nature accruing to the LLP in accordance with their respective allocations of Units as set out in 0 as at the relevant date of the distribution.**
- 10.6 The Members acknowledge and agree that their beneficial interest in the assets of the LLP (excluding the Current Accounts and the Contribution Accounts) shall otherwise be determined by reference to each Member's share of the Units in issue from time to time.”**

## **The Notice of Appeal**

10. The Notice of Appeal is at EAT bundle pages 10-11. This is amplified in Mr Hyams' two skeleton arguments. There is a Respondents' answer at EAT bundle pages 12-15. It is supplemented by Mr Catherwood's skeleton argument.

11. The appeal is in fact only pursued against the First Respondent as the Second Respondent has no legal personality in the United Kingdom.

12. As far as we are aware this appeal raises two questions which are novel. The first question is whether or not a member of a limited liability partnership under the **Limited Liability Partnerships Act 2000** is capable of being an employee? The second question is: if such a person can be an employee then on the facts of this case did the Employment Tribunal make an error of law?

## **Limited Liability Partnerships Act 2000**

13. Section 1 provides as follows:

### **“1 Limited liability partnerships**

(1) There shall be a new form of legal entity to be known as a limited liability partnership.

(2) A limited liability partnership is a body corporate (with legal personality separate from that of its members) which is formed by being incorporated under this Act; and-

- (a) in the following provisions of this Act (except in the phrase “oversea limited liability partnership”), and
- (b) in any other enactment (except where provision is made to the contrary or the context otherwise requires),

references to a limited liability partnership has unlimited capacity.

(3) A limited liability partnership has unlimited capacity.

(4) The members of a limited liability partnership have such liability to contribute to its assets in the event of its being wound up as is provided for by virtue of this Act.

(5) Accordingly, except as far as otherwise provided by this Act or any other enactment, the law relating to partnerships does not apply to a limited liability partnership.

(6) The Schedule (which makes provision about the names and registered offices of limited liability partnerships) has effect.

#### **4 Members**

(1) On the incorporation of a limited liability partnership its members are the persons who subscribed their names to the incorporation document (other than any who have died or been dissolved).

(2) Any other person may become a member of a limited liability partnership by and in accordance with an agreement with the existing members.

(3) A person may cease to be a member of a limited liability partnership (as well as by death or dissolution) in accordance with an agreement with the other members or, in the absence of agreement with the other members as to cessation of membership, by giving reasonable notice to the other members.

(4) A member of a limited liability partnership shall not be regarded for any purpose as employed by the limited liability partnership unless, if he and the other members were partners in a partnership, he would be regarded for that purpose as employed by the partnership.”

14. We particularly note Section 1(5) and Section 4(4).

#### **The grounds of appeal**

15. We take each ground of appeal in turn.

#### **Grounds 1 and 2: the correct legal test**

16. In our judgment the Employment Tribunal was correct to take as its starting point Section 4(4) of the **Limited Liability Partnerships Act 2000** as set out above.

17. We agree with Whittaker and Matchell: *The Law of Liability Partnerships* at paragraph 8.27 (2nd Edition 2004):

“if the LLP was a partnership, and a person was held out as a partner for the purposes of s.14 of the (Partnership Act 1890) but was actually an employee of the partnership rather than a partner, the same criteria which determined his status as between employee and partner will apply to determine whether or not he is an employee of the LLP.”

18. Parliament has thus expressly provided that the legal test which determines whether a person is a partner or an employee of a partnership also determines whether a member of an LLP is employed by the LLP. We agree with the following submissions by Mr Catherwood:

- (1). The partnership test applies for determining whether the person is an employee for any purpose including whether or not for the purposes of the **Employment Rights Act 1996**;
- (2) The question of whether a person can be both a member of an LLP and its employee is not relevant to the facts of this case. The question for the Employment Tribunal was whether, having regard to Section 4(4) Mr Kovats was an employee. The fact (if it is a fact) that, if he was an employee, he might remain a member of the LLP does not affect that determination;
- (3) The application of this test does not ask the standard common law tests applicable to determine whether the person is an employee or self-employed. In our judgment the test of determining employment status in a LLP is additional to the standard common law tests. Thus in the context of partnership the Tribunal is required to decide into which of two legal categories a person falls: partnership or employment. If the Tribunal decides that the person is not a partner, it does not follow that he is necessarily an employee: the usual common law tests will still need to be applied, as the person may in fact be self-employed: Lindley and Banks on Partnership paragraph 5-70 (18th edition 2007);
- (4) The Tribunal were correct to first consider whether Mr Kovats was a partner in the partnership. Having found that he was a partner in the partnership (in accordance with

Section 4(4) of the 2000 Act) the Tribunal correctly considered the common law tests and decided that they would not have conferred employment status on him.

19. In our judgment the Employment Tribunal were correct in concluding as follows:

- (i) **“Section 4(4) of the Limited Liability Partnership Act is the starting point. That is that a member of an LLP, such as the Claimant, shall not be regarded for any purpose as employed by the LLP unless, if he and the other members were partners in the partnership, he would be regarded for that purpose as employed by the partnership.”**
- (ii) **“The “any purpose” and “that purpose” must be regarded in this case as a reference to the Claimant’s work as chief investment officer, and we have to ask ourselves whether if this was a partnership in the normal sense, presumably under the auspices of the Partnership Act 1890, the Claimant’s role as CIO would be regarded as employment.”** Judgment paragraph 7.2.

20. In our judgment this is a correct statement of the law

### **Ground 1: the wrong test**

21. Ground 1 in full is: The Tribunal applied the wrong test by asking itself an irrelevant question in the form of whether the Appellant’s role as Chief Investment Officer was “incompatible with the partnership agreement”.

22. In our judgment the Tribunal did not err by asking itself this question. At paragraph 7.2 of its judgment the Tribunal considered two matters. First, whether Mr Kovats’ role as Chief Investment Officer went beyond, or was otherwise inconsistent with, the duties which all members carried out or might be required to carry out pursuant to the terms of the Members’ Agreement. Second, whether Mr Kovats’ role as Chief Investment Officer went beyond, or was otherwise inconsistent with, the duties generally undertaken by partners in a partnership.

23. Both considerations were relevant to the question of whether or not Mr Kovats was an employee. Had the Employment Tribunal answered either question in the affirmative that

might have pointed against his being a partner. In the event the Tribunal found as a fact that his role was not inconsistent with either the Members' Agreements or the general duties of partners. The Tribunal was entitled to take that fact into account in reaching its conclusion.

**Ground 2: Misconstruction of s.4(4)**

24. The full ground of appeal argues that the Tribunal misconstrued s.4(4) of the 2000 Act. For the reasons we have just given we reject this.

**Ground 3: The £80,000 per year draw-down**

25. The full ground of appeal is that the Tribunal wrongly concluded (in paragraph 3.1 of its Reasons) that the Claimant's fixed membership distribution of £80,000 per year "was intended to be a draw-down against the future profits of the business".

26. This is a finding of fact. There was material before the Employment Tribunal which entitled it to make that finding of fact, namely:

- (i) but for the fixed distribution, Mr Kovats would have enjoyed a 1/11<sup>th</sup> net profit – share (original agreement Clause 10.1 EAT bundle page 60 and revised agreement paragraph 10.5 EAT bundle page 107). The LLP was a start-up which was not expected to make substantial profits at first. In an agreed note of evidence Mr Omar Shafi said:

**"A 1/11<sup>th</sup> share of profits would not be enough to live on. (His) current account was credited with a certain amount, £80,000."**

(ii) In the same agreed note of evidence Mr Al Omran said:

**“All partners agree on a fixed distribution to start, to be adjusted as the business grows. It is treated as a draw-down, not as a salary.”**

(iii) In our judgment the Employment Tribunal was therefore entitled to characterize the payment as a draw-down against future profits. From the LLP’s point of view, Mr Kovats was drawing sums in excess of his 1/11<sup>th</sup> profit entitlement in the expectation that such payments would be justified by later profits. Once the profits rose sufficiently, Mr Kovats would receive an increased draw-down (or indeed could be taken off the fixed distribution altogether).

**Ground 4: 1/11<sup>th</sup> of profits**

27. The full ground is that: the Tribunal wrongly concluded (in paragraph 3.3 of its Reasons) that the Appellant “was entitle (d) to 1/11<sup>th</sup> of any profits the company made”.

28. As long as he received a fixed distribution Mr Kovats was not entitled to a 1/11<sup>th</sup> share of net profits of the LLP. However, for the reasons set out above he was entitled to a discretionary distribution of surplus profit, and a distribution of profits “of a capital nature”. Furthermore, Mr Kovats was entitled to a 1/11<sup>th</sup> share of the proceeds upon any winding-up or sale. This is a clear pointer towards partnership. In **Stekel v Ellice** [1973] 1 WLR 191 Megarry J. considered that under a partnership agreement a salaried partner on a fixed salary, not dependent on profits, could still be a true partner at least if he was entitled to a share in the profits on a winding-up: *ibid.* at 199H.

29. Even if the Employment Tribunal did make an error of fact on this point it was a minor one. It does not impugn the other conclusions made by the Tribunal and does not affect the result of the case.

**Ground 5: Entitlement to “a share of the proceeds” of sale**

30. The full ground is: the Tribunal took into account an irrelevant factor when it took into account what it saw as a fact (recorded by it in paragraphs 3.3 and 7.4 of its Reasons) that “if the partnership had been sold “the Appellant” would have been entitled to a share of the proceeds”.

31. At paragraph 7.4 of its judgment the Employment Tribunal correctly state that an entitlement to share in the proceeds is an important indication of partnership: **Stekel**.

32. Mr Hyams objects that there was no evidence that the LLP might have been sold. In answer to this Mr Catherwood points to the following matters:

- (i) in the agreed note of evidence Mr Al Omran gave evidence that “If the LLP should be sold all the partners would benefit. If sold for \$100 million all benefit.” This was evidence that Mr Al Omran did indeed contemplate a future sale;
- (ii) there is no evidence that it was ever suggested to Mr Al Omran in cross-examination that a sale was improbable;
- (iii) there was no evidence that a sale was improbable. As with any business, a future sale would depend on how the business prospered. What mattered was Mr Kovats’ rights upon a sale. The Tribunal is not required to speculate as to the likelihood of the sale. It was not suggested to the Tribunal by Mr Kovats’ representative that it should so speculate.

33. Mr Hyams also suggests that Mr Al Omran could defeat Mr Kovats' right to share in the proceeds of a sale of the business by giving 6 months' notice. In our judgment this is fallacious. Mr Al Omran was bound to exercise his power to retire Mr Kovats in good faith and not for an ulterior motive: Whittaker and Machell: *The Law of Limited Liability Partnerships* paragraph 11.25 (2<sup>nd</sup> Edition 2004). The authority relied on for this proposition is drawn from company law: **Allen v Gold Reefs of West Africa Ltd** [1900] 1 Ch 656 (CA) at 671 and partnership law: **Blisset v Daniel** [1853]10 Hare 493 at 522. We agree.

#### **Ground 6: Perversity**

34. The full ground of appeal is: The Tribunal's conclusion that the Appellant was not an employee was contrary to the weight of the evidence, or otherwise simply wrong: the only proper conclusion on the facts before the Tribunal was that the Appellant was an employee.

35. Mr Hyams sets out his submissions at paragraphs 39-43 of his second skeleton argument. However elegantly expressed they amount to an allegation of perversity. The test of perversity is well-known: **Yeboah v Crofton** [2002] IRLR 634 at paragraphs 92-95 per Mummery P (as he then was).

36. In reaching its conclusions the Employment Tribunal made a series of findings of fact. The majority of these have not been challenged, namely:

- (i) the parties themselves intended this to be a partnership;
- (ii) Mr Kovats never at any time suggested that he was an employee until he was voted out of the partnership and had taken legal advice;
- (iii) he signed two membership agreements and a side letter as a partner;
- (iv) he had considerable autonomy in the London office and over the Bahrain team;

- (v) he signed important documentation as a partner which bound the LLP;
- (vi) he opted to have his draw-down paid gross and to account for income tax himself;
- (vii) he paid Class 4 National Insurance contributions;
- (viii) the arrangement was not a sham: had Mr Kovats thought it was, he would have said so at the relevant time;
- (ix) both parties genuinely considered that this was a true partnership arrangement;
- (x) the parties at all times acted consistently with the partnership agreement;
- (xi) although Mr Kovats made no direct capital contribution into the business, his salary reduced significantly when he left HSBC and the loss would continue while the LLP made no profits. To that extent he sustained a loss and provided sweat-equity: agreed notes of evidence page 48 B, second paragraph;
- (xii) he was in a very real sense a manager of the business and the success of the business depended to a large extent on his input.

37. Mr Kovats accepted a draw-down representing half of his current salary at HSBC. His share options would not vest for three years, and financial returns from the LLP were speculative and would not be forthcoming in the short term. The Employment Tribunal correctly concluded from this and the other factors that Mr Kovats was a partner, i.e. that he was carrying on business in common with his fellow members with a view to profit. He was not an employee.

38. It seems to us in the light of these facts that the Appellant cannot succeed in a perversity challenge to the Employment Tribunal's judgment.

## **Hansard**

39. During the course of the appeal we were referred to Hansard concerning the passage of what is now Section 4(4) of the **Limited Liability Partnerships Act 2000**. We asked for further written submissions on this aspect of the appeal which we subsequently received. Both counsel have referred us to **Pepper v Hart** [1993] AC 593. We have carefully read the further material submitted to us by counsel. We do not find that Section 4(4) is so ambiguous or obscure or leads to absurdity that we need to rely upon clear statements by the relevant Minister. Indeed, we do not find the comments made by the relevant Minister to be particularly clear themselves.

40. In the circumstances we do not find the additional material helpful and we do not therefore invoke **Pepper v Hart**.

## **Conclusion**

41. For these reasons the appeal is dismissed.