

Interpreting an expulsion clause in an LLP: commercial approach rejects unanimous decision in THJ Systems v Sheridan

The recent case of *THJ Systems and another v Sheridan and another* [2023] EWHC 927 (Ch) offers valuable insights in respect of the decision to remove a defaulting member from a limited liability partnership (an “LLP”). The court's decision to adopt a commercial approach in interpreting an expulsion clause, ensuring that a member cannot vote on his / her own expulsion, is worth highlighting. This clarification serves as a necessary safeguard against an unreasonable and absurd interpretation of the expulsion clause. By prioritising real-world corporate considerations, the court demonstrated business common sense. Additionally, the case provides clarity on the meaning of serious and persistent breaches of an LLP agreement.

The case involved an LLP formed between two members, S and THJ, for the purpose of exploiting certain software. S was granted an end user license to use the software for training and mentoring purposes. The LLP agreement specified that S must (i) display a specific copyright notice on material related to the software and (ii) advertise and promote the software.

THJ and the LLP alleged that (i) S and his company infringed copyright by, amongst other matters, displaying images of the software during presentations and (ii) S was in breach of his obligations under the LLP agreement by failing to comply with the advertising requirements applicable to him under such agreement.

As a result, S was expelled from the LLP based on the expulsion clause, which allowed expulsion for serious or persistent breaches of the LLP agreement upon written notice. However, S was not granted the right to vote on his own expulsion, as THJ and the LLP argued that unanimous consent was not required for expulsion.

While the court dismissed the passing off and breach of copyright claims, it found that S had indeed committed a “serious and persistent” breach of the LLP agreement by failing to meet the advertising requirements.

In clarifying the meaning of a “serious” breach under an LLP agreement, the court confirmed that a serious breach is more than trivial but less than repudiatory, being a matter which has a serious effect on the benefit that the innocent party would have derived from the contract's performance in accordance with its terms. For a breach to be considered “persistent”, it must be repeated, non-trivial, and collectively amount to a serious impact. The court emphasised that assessing whether a breach is serious and/or persistent requires consideration of all of the relevant circumstances, such as the nature of the contract, the provision breached, the breach itself, and its consequences. Having determined

that the breach of the advertisement requirements constituted a serious breach, justifying S's expulsion, the court turned to the procedural validity of the expulsion.

The court rejected the argument that the expulsion clause allowed S to vote on his own expulsion. Instead, it concluded that the references in the LLP agreement giving the LLP the power to expel a member under specific circumstances should be interpreted as "*the LLP (acting for this purpose by the Members other than the Member concerned)*", i.e. the LLP acting by a majority of its members other than S (being in this case THJ alone). THJ rightfully stated that construing "*the clause as requiring a member to vote for his or her own expulsion would be absurd and would render the clause ineffective*".

Additionally, the court highlighted that expulsion of a member is not part of the day-to-day business of the LLP but nor was it a matter requiring the unanimous approval of the members under the LLP agreement. Considering the duty of utmost good faith imposed on the members under the LLP agreement, akin to traditional partnership principles encompassing standards of fairness and honour, the court reached the conclusion that THJ did not breach this duty. THJ raised legitimate concerns regarding S's breaches and provided reasonable opportunities for S to address the allegations before resorting to litigation. Ultimately, the court upheld the validity of the notice of expulsion.

In its ruling, the court demonstrated a keen and practical consideration of commercial sensibilities, ensuring an efficient and logical decision-making process within the context of partnership relations and business operations.

Authors: [Hugh Naylor](#) and [Rita Doureradjam](#)

Contacts: [Simon Norris](#) and [Hugh Naylor](#)