

## "Subject to Contract" Documents Defeat English Law Claim of Partnership at Will

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*In Valencia v. Llupar, [2012] EWCA Civ 396, the Court of Appeal for England and Wales rejected an argument that a partnership at will or in fact had been created between the parties, since the defendant's solicitors had marked correspondence regarding the proposed partnership agreement as "subject to contract". As a result, the defendant had to repay to claimant £80,000 he had invested in the proposed venture on the grounds of unjust enrichment, plus interest and costs.*

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The defendant, Natalia Valencia, was the owner and manager of two restaurants in North London, "Natalie's Café" in Manor Park, which also had living accommodations above, and the "Tropical Taste" in Walthamstow. The claimant, Norberto Llupar, made four payments to the defendant by cheque totaling £80,000. The core dispute concerned the basis on which those payments were made and received.

According to the claimant, the defendant induced him to make the payments by representing that her restaurant businesses were doing very well, taking in between £700 to £1,000 a day, and that, in return for his investment, he would have a 40% share and be provided with living accommodations above Natalie's Café. He soon discovered, while the defendant was away in the Philippines, that the takings there were nothing like what he had been led to believe and were as little as £300 a day on many occasions. It also turned out that the accommodations were unavailable for his occupation.

The defendant's solicitors sent a letter to the claimant headed "Partnership Agreement-subject to contract." The solicitors said that they had been instructed by the defendant "in regard to a Partnership Agreement" with him, that they intended to prepare a draft agreement for his approval and that it was important that he should appoint his own independent legal representative to advise him. They asked him to remit half of the estimated legal costs of £500 plus VAT that they understood he had agreed to pay. The defendant, however, made no payment towards legal costs and no partnership agreement was ever tendered for his consent.

At about that time the claimant began to work at Tropical Taste, and continued to do so while the defendant was away. During that period he wrote a letter to the defendant asking for written confirmation of payment to record the details "of the agreement we have reached in relation to the four following payments totalling £80,000" made by him. The dates and amounts of the payments were listed. The letter concluded as follows:

"I think you will agree that as the contract has not yet been finalized. I will require some form of proof that you have received these payments and I would appreciate if you could sign below to confirm."

The defendant signed that letter on her return from the Philippines. This was the only document signed by both parties.

The defendant's solicitors sent a further letter to the claimant which, like their previous letter, was headed "Partnership Agreement-subject to contract". It recorded their view that it would be appropriate for him to appoint independent legal advisers to represent him in negotiating a partnership agreement.

Thereafter the claimant stopped working at Tropical Taste. He demanded the immediate repayment of his money and stated his intention to terminate the business relationship. As noted, no partnership agreement or other formal document had ever been drawn up and signed by the parties.

The claimant sought restitution of his £80,000 on the basis that (a) it was paid by him to the defendant in circumstances in which no partnership at will existed; (b) the defendant's representations inducing him to enter into a partnership and to make the payments were untrue; and (c) there was a failure of consideration.

The defendant's response was that the claimant was not entitled to the return of the £80,000 or to any remedy against her other than the winding up of a partnership. She had been looking for a new business partner with money to invest in her businesses, and the claimant agreed to pay and in fact paid £80,000 in order to develop them and contribute to future profitability. He worked at Tropical Taste, doing manager duties pursuant to a legally binding arrangement with her. They were, she said, partners at will, as evidenced by his participation in the running of the business and the fact that he took £300 per week from the takings for five weeks. He then left the business and repudiated the agreement. The defendant further denied that she had made any misrepresentations to the claimant.

The claimant began proceedings for repayment of the £80,000 with interest for total failure of consideration, or for damages for misrepresentation, or for breach of contract. The defendant counterclaimed for an account of his receipts from the business and for damages for breach of contract.

After a trial with an acute conflict in evidence, Judge Cowell ordered the defendant to repay to the claimant the sum of £80,000, together with interest and costs. He also made an order that the defendant's beneficial interest in a property stand charged, by way of an interim charging order, with the sum of £124,480.

On appeal, Lord Justice Mummery, with whom Lady Justice Black and Dame Janet Smith agreed, readily acknowledged that it is legally possible for a partnership to come into existence before a formal written agreement is executed, or without any formal legal document ever being executed. However, in this case the contemporaneous correspondence could not have been clearer on the key point: the parties did not intend the legal relationship of partnership to exist between them unless and until they had entered into a formal written partnership agreement. What was key were the references in the two letters from the

defendant's solicitors to "Partnership Agreement-subject to contract". The first letter was written soon after the payments were made and on the date when the claimant began to work at Tropical Taste. The second solicitors' letter was sent while he was still working there. The in-between letter signed by both parties referred to a contract not yet and never finalized, as contemplated, in the form of a written agreement. To Lord Justice Mummery, those three letters pointed to only one conclusion, namely, that the parties had no intention of entering into the legal relationship of partnership without having first executed a formal written agreement. He concluded that the parties by their conduct had not converted their "subject to contract" stance regarding a partnership into an unconditional and binding agreement, or into an actual partnership giving rise to partnership rights and obligations.

It then followed that, since the matter expressly made "subject to contract" did not proceed to a formal binding agreement, transfers of money in anticipation of such a contract should be returned to the person who has made them. The case fell within the general principles of the law of unjust enrichment:

"...Thus a claimant who pays money to the defendant on a 'subject to contract' basis and who then decides that he does not wish to go through with the purchase is entitled to recover from the defendant the sum so paid..."

In short, the use of "subject to contract" in English practice precludes either party from being legally bound pending negotiation and execution of a formal agreement. Until that occurs, each side is free to withdraw from the proposed transaction without incurring legal liability for breach of contract. When moneys are exchanged, care must always be taken to document properly and fully the parties' intent as to their relationship, and regarding application of the transferred funds, to avoid what for the defendant Ms. Valencia turned out to be a rude awakening.

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If you have questions, please contact the Pillsbury attorney with whom you regularly work or the author:

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