When is the Syndicate Manager a Fiduciary?

(Some thoughts and an update.)

In a typical station Syndicate Agreement the syndicate manager acts as agent for the owners in numerous capacities. As noted in Lindsay-Field v. Friendly, 36 Cal. App. 4th 1728, 1731 (1995):

> The syndicate agreement sets forth the relationship of the members of the **syndicate manager** as principal and **agent,** and the rights, duties and authority of the manager. The manger has possession of the horse and reasonable authority and discretion concerning ordinary care and supervision.

As it is universally recognized that "agency is a fiduciary relationship," Restatement of Agency, Second, Section 1; McAlister v. Whitford, Ky., 365 S.W.2d 317 (1962),this is recognized in the horse industry:

> It is clear that syndicate managers are the agents and, thus, the fiduciaries of the owners to an extent consistent with their contractual undertakings; they also have the same duties as all agents. E.g., Miller, The Sale of Horse and Horse Interests; A Transactional Approach, 78 KY. LJ517, 561 (1990).

The problem arises, of course, out of the fact that syndicate managers usually are in the same business as owners of stallion shares. Syndicate managers directly complete with fractional interest owners in many ways, as, for example, when the syndicate manager sells his/her breeding rights (or his/her own nominations from his/her own fractional interests) on the market, in competition with the fractional interest owners who want to sell their seasons. It is in this context (the sale of seasons) that most of the industry is familiar with the case of Kefalas v. Bonnie Brae Farms, Inc., 630 F.Supp 6 (E.D. Ky. 1985). That case ended the open and much discussed issue determining (as an SEC ruling had before it) that the standard thoroughbred syndicate agreement did not create a "security" under federal and state securities laws. Under the standard agreement, since the fractional interest owners compete with each other (either by breeding to their own mares or selling their nominations on the market), and the syndicate manager does not have the responsibility to sell annual nominations for the owners, there was neither "vertical" or "horizontal" commonality as required by standard securities law analysis. Attendees at seminars were regularly cautioned not to provide for "pooling" of excess breeding rights, for securities law purposes – as well as to avoid being classified as a partnership for other purposes. The fact is, however, that Kefalas did not dispense with all issues, and this is emphasized by the case of Sheets v. Dziabis, 738 F.Supp. 307 (N.D. Ind. 1990), where Kefalas is distinguished because the plaintiff in the Sheets case "was induced to buy the syndicate shares by promises that he could sell this breeding rights" through the syndicate manager -- irrespective of what the syndicate agreement said.

Apart from the sale of seasons, however, the syndicate manager is very much in charge. The interesting case of Savin v. Ranier, 898 F.2d 304 (2d Cir. 1990) holds that the Kentucky-based owner of a fractional interest in a New York-based thoroughbred stallion was held not to be subject to Connecticut's long arm statute, where the original owner of the stallion (who still owned some fractional interests) lived, because the "syndicate manager in New York would have all authority and discretion with respect to managing the syndicate and with respect to the keeping, care, maintenance, management, breeding and supervision of the stallion." As early as the well known tax case of

Guggenheim v. Commissioner of Internal Revenue, 46 T.C. 559 (1966) 630, the fiduciary obligation of the syndicate manager was recognized, for this very reason. The Internal Revenue Service had argued that since the original owner of the stallion remained in control as the syndicate manager, the sale of fractional interests should not be treated like the sale of other property interests. The court noted, however, that after the sale "he could not disregard the interest of the purchasers," and so the sale was like the sale of any minority interest in property.

Though not expressed in any of these cases, it is clear from them that there is lurking here the simple fact that when an owner puts on the hat of an agent, he/she becomes a different person with different duties– a trustee for other people. The typical syndicate agreement does not (though perhaps it should) mention even the fact that the syndicate manager will sell his/her own seasons and yearlings in competition with fractional interests owners, but at least in that enterprise pretty much everyone understands that the agent will be looking out for him/herself.