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NATIONAL TUTORIAL 2024

PARTNERSHIPS

MODEL ANSWER

This is an Outline Answer, covering the points raised in a very broad problem. This Outline Answer is intended to be read alongside the Detailed Notes provided to Delegates.

You have been instructed to prepare a note of the key points you will need to address and your reasoning. The specific focus of your notes should be what structure might already exist, and how the family business might be structured differently to accord with the children's interests and wishes.

The key points to bring to a meeting are in ***bold italics***, with some explanation below as to why they are important.

Partnership between Bruce and the in-laws

Although this isn't the current agreement in place, it is worth considering what the position is here.

Bruce thinks that there was a written agreement, but it has never been found. It could be assumed that there was no agreement in place.

If there was no written agreement in place, then the Partnership Act 1890 would govern the partnership. The Act also provides a default position if a written agreement is silent on a particular point – so it is an important piece of legislation.

The Partnership Act 1890 will apply subject to any agreement between the partners to the contrary – this agreement between the partners could be by a written express agreement or through implied consent which could be evidenced through a "course of dealing". Things like the signing of annual accounts are useful to show a particular "course of dealing" – the accounts for the partnership are important documents.

There are default provisions within the Partnership Act 1890 which govern the dissolution of a partnership. We know that Bruce's in-laws are both deceased. The death of a partner will trigger a dissolution pursuant to section 33 Partnership Act 1890.

Therefore, we can assume that on his in-laws deaths, that partnership was dissolved. We have no details from Bruce as to what happened on the death of his in-laws. Some key points to discuss in relation to this partnership could be:

1 ***Was the partnership wound up?***

2 ***What happened to the assets?***

3 ***Does Bruce know what the partnership assets were?***

Current agreement

There is currently a partnership in relation to Home Farm which involves Bruce, Holly, Lucy and Stuart.

There is no written partnership agreement. This partnership does not have anything to do with the running of the wider Estate.

4 ***As there is no written agreement, the Partnership Act 1890 will kick in to provide default provisions.***

5 ***Bruce and Holly need to be aware that if they retire from the current partnership, this would dissolve the partnership, as per section 26 Partnership Act 1890.***

The legal title to Home Farm is in Bruce and Holly's name. At the meeting, to assist with considering how best to the structure the business going forward, you would need to find out some further details in relation to the current partnership's assets.

6 ***Is Home Farm currently a partnership asset?***

A good place to start with, is to ask the partners. Another place to look to see if the land has been treated as a partnership asset is the partnership accounts – you would see if the land has been included on the balance sheet. This may not always provide an accurate picture and so it is important to also speak to the accountants and partners to see what their intentions are.

It is important to distinguish between whether the land is in or out of the partnership as this will impact several things including the tax position and how the land can be dealt with.

If the land is held within the partnership, then the beneficial ownership of the land will change. Bruce and Holly would still be the legal owners of the land, but they would be holding the land on trust for the benefit of the partnership.

The land would become a partnership asset and Bruce and Holly (as landowning partners) would no longer own the land directly, but instead they would own the interest in the capital of the partnership. Importantly, unless it had been agreed otherwise, Lucy and Stuart would also own an interest in the capital of the partnership which would include the land, even though they do not own the legal title.

This could cause some issues when considering the future restructuring of the business. If the land is currently held within the partnership, as a partnership asset, Bruce and Holly cannot just remove the land and bequeath it in their Wills to the children. They would only have an interest in the capital of the land, not the land itself.

If it is important that a partner has the ability to recover the land itself, then this is something that expressly needs to be provided for in an agreement – although consideration would need to be given to the impact the removal of the land would have on the partnership business.

It is quite common in farming families that the more senior members of the family own the legal title to land and so it is important to consider in these instances how that land will be held.

It is also important to remember that a partnership agreement will take precedent over a partners Will, so it is very important when drafting these agreements that the succession planning of the clients are dovetailed with any partnership agreement that is entered into.

If the land is not within the partnership, then we would need to consider what agreement is currently in place that governs the occupation of the partnership at the farm. Is there a tenancy agreement? Is there a licence? In practice, you can include a licence for the partnership to occupy non-partnership land within the written partnership agreement itself and can be quite a simple option to go with if the partnership is a simple family situation. However, there may be a reason why the partners would like the occupation to be more formal and set out in a tenancy agreement.

7 ***What has been agreed between the current partners in relation to capital / profit shares.***

At the previous meeting it was clear that Lucy and Stuart were not on board with Bruce and Holly's retirement plans and were not impressed with the idea of sharing the profits/management etc. relating to Home Farm given that they have put their own money into the holding. As well as asking Bruce and Holly, it would be a good idea to have a look at the accounts to see how these injections of money/capital into the partnership from Stuart and Lucy have been dealt with.

As Bruce and Holly's agent it would be prudent to point out that Stuart in particular (as he will not be in line to inherit part of the Estate personally) may consider any right he has to make a claim in relation to Home Farm, given that he has been working on the holding and putting his personal finances into it. He may be able to assert some sort of estoppel claim, so at this meeting you would need to discuss with Bruce and Holly what arrangements there are currently in relation to how the capital is held and profits are split and what has been discussed with Stuart and Lucy about their future in relation to Home Farm.

As there is no written agreement, unless it can be shown through a course of dealings that the capital and profits are dealt with in a particular way, then the Partnership Act 1890 would provide the default provision that the partners are entitled to share equally in these. They also need to contribute equally towards any losses (section 24).

Potential future agreement

Bruce and Holly will need to consider what would be the best way to balance the children's interests and wishes.

8 ***Split the Estate?***

Holly and Bruce may want to consider splitting the running of the Estate. They may wish to continue the partnership with Lucy and Stuart in relation to Home Farm and then have a separate agreement in place which governs the business relating to the rest of the Estate.

They would need to take advice on the tax implications of this and whether there would be any potential issues in doing so.

Karl would rather that all agricultural enterprises on the Estate were removed. It is unlikely that this will be practical or in the best interest of the Estate. Bruce and Holly may want to consider that the current partnership in relation to Home Farm, could have the other tenanted agricultural land introduced into it, so as to keep all the agricultural interests being run by one partnership.

Bruce and Holly would also need to consider whether they would like to formally retire from the partnership, or whether it would be better for them to continue as partners.

9 ***How is the land going to be dealt with?***

If the land relating to Home Farm is not currently a partnership asset, they would need to get advice as to whether this should change. The tax treatment of the land will differ depending on whether it is a partnership asset or not. In terms of IHT, if the land is held in the partnership, then APR of 100% is available – although this will only relieve the agricultural value of the land asset.

Business Relief has the scope of relieving the full market value of the land. If the land is a partnership asset, then it would be an interest in a business and could qualify for 100% relief. If it was held outside of the partnership, this relief would only be available at 50%.

10 ***Get succession planning advice***

Holly and Bruce will need to make sure that they get advice on the most tax efficient way to distribute the Estate on their death and this will then influence the structure of the business in the meantime.

There are also other points to consider in relation to any new agreement which would govern the partnership relating to the rest of the Estate and if Bruce and Holly decide to continue the partnership with Lucy and Stuart in relation to the agricultural land, it would also be prudent to put a written partnership agreement in place for this. This would provide a good opportunity for the partners to agree any new terms and formalise the arrangement.

11 ***Should the agreement be for a fixed or indefinite term?***

12 ***What are the partnership assets? How is the capital to be divided between the partners?***

13 ***How is the land to be dealt with – will it be a partnership asset? If so, what proportion of the land capital will each partner own?***

14 ***If it is not, what occupation rights are the partnership going to have in relation to the land?***

15 ***What is happening with the tenanted land?***

The tenanted land will either need be surrendered, or will carry on being tenanted, provided that there is not unity of title and possession.

16 ***How are the profits/losses to be divided between the partners? How much should the partners be entitled to draw on account of profits?***

17 ***Bank accounts – how many signatories are required, are there to be any limits on expenditure?***

18 ***Frequency of partnership meetings. What voting procedures should there be? Is there anything that requires the consent of all the partners.***

19 ***What is to take place on the death/retirement of a partner? Notice periods, options to purchase and outgoing partners share, nominated successor partners?***

20 ***In what circumstances would a partner be expelled?***

21 ***How would any dispute be resolved?***

There are lots of things for Bruce and Holly to consider, but before any drafting of the documents required to restructure the business, it would be a good idea to sit down with a tax advisor and have a think about succession planning.

Grace Awan and Hannah Drew
September 2024

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