Detail counts

Julie Butler and Libby James explain the importance of ensuring farming partnership agreements are drafted accurately and reviewed regularly.

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The current pressure to transfer assets among farming families due to the proposed inheritance tax (IHT) relief restrictions for agricultural property relief (APR) and business property relief (BPR) is weighing heavily, not just on tax advisers but also on farming families (see 'Meticulous forward planning', *Taxation*, 23 January 2025). Making the correct decision is extremely difficult when facing a fixed deadline with huge amounts of uncertainty, not only regarding the future legislation and industry outlook, but also with regard to life expectancy and each family member's hopes and plans moving forward.

As mentioned, farmers are seriously considering making lifetime transfers as a result of the IHT relief cuts from April 2026. With the announcement just before Christmas of the increase to £2.5m of the 100% allowance for APR and BPR combined, some could argue that the intense pressure of the necessity for lifetime transfers has been reduced in some cases. Instead, the need to identify non-partnership property increases because the relief on that will be only 50% BPR, whereas partnership property will achieve 100% BPR thus, it can be argued, making the role of the partnership agreement even greater. Farmers need to plan ahead in a tax-efficient way with strong and excellent tax advice. However, they could be transferring assets in a way that they wouldn't otherwise do. The role of farming businesses in sustaining livelihoods and contributing billions to the UK economy is undeniable, while ensuring UK food production. Agriculture uses about 70% of the UK's land, and home-grown produce is the largest source of the UK's food. Note though that the legal framework surrounding farming can be complex, especially as it is so inter-generational and all families and farmland are different.

Complications arise when there is a potential divorce. Unlike many other industries, farming is deeply personal.

Key points

- A court may set aside a transaction if it finds a person was tricked into transferring assets.
- Importance of a well-drafted partnership agreement and a clear record of how assets are owned is highlighted by the *Merryman* case.
- Proprietary estoppel cases involve a claim that a promise has been made about inheritance that someone has relied on to their detriment.
- There should be a meeting with all partners to agree and sign the partnership accounts.

Family ties, generational promises and lifestyle sacrifices blur the line between business, emotion and tradition. The presumption is that the person on the legal title is the owner of the land but if, for example, someone is persuaded to sign something they can't read, or the document is written in a language they can't understand, it could result in the title being transferred to someone else without full comprehension and control.

The *Merryman* case

If evidence can be provided that a person was tricked into transferring assets and it wasn't the free exercise of their will, the court may set aside that transaction. However, this is not something the court will do without strong justification and convincing evidence is needed. Below we explore the case of *Julie Annette Merryman v Alex Raymond Merryman v Elizabeth Lawson, Katie Ann Merryman, Scott Merryman, Robert Paul Merryman* [2024] EWFC 58, which concerns farming partnership assets and proprietary estoppel.

The importance of a well-drafted partnership agreement and a clear record of how assets are owned is highlighted by this divorce case, in which four adult children in a farming family 'intervened'. Issues included confusing records, contradictions in the partnership agreement and a lack of documentation in certain areas relating to the farming property assets.

Such problems sadly are concerns that arise in a large number of farming partnerships, where there can be a lack of attention to detail and future worries. While there has been some recent improvement in this respect with making tax digital (MTD) for VAT, addressing the concerns over the proposed APR and BPR reductions and non-stop 'nagging' from the tax and farming press, there is still some way to go.

Intervention by the children

The case in question concerned the six equal members of the partnership – Alex Merryman, his wife Julie, and Alex's children Elizabeth, Katie, Scott and Robert. All six worked on the farm, with the children having devoted their working lives to the development of the farm business with little payment from the time they each left agricultural college or university. That last sentence could come as a great surprise to anyone not brought up in farming, but is commonplace in farming family businesses.

None of the partners took a salary, with the business funding their day-to-day needs and 'modest drawings' shown in the 2022 accounts. Alex and Julie's marriage broke down in 2021 and Julie brought financial remedy proceedings against her husband. It was at this point that Alex's four adult children (Julie's stepchildren) intervened, asserting that they were each entitled to a one-sixth share in four properties, by virtue of them being partnership property, or alternatively on the grounds of proprietary estoppel. Proprietary estoppel is a legal principle that can give someone rights to property if they were promised a share, relied on that promise and would be unfairly harmed if the promise wasn't honoured.

The question has to be asked, what could have happened to protect the children before the proprietary estoppel claim was paid? The family could have sorted the role of the children (and parents) in legal terms before with a stronger partnership agreement. Looking at the problem from the outside and by those who weren't involved in farming, this may seem obvious. However, farmers do not often think in these terms, especially when their business partners are close family members.

Where a marriage involving a farming partnership breaks down, disputes about who owns what can become especially complicated – particularly when third parties such as adult children claim a stake in the farm. As mentioned, this case shows how early clarification of ownership and ground rules for the running of the business is something that can be very difficult in an inter-generational business. As they say, the lack of formal agreements is 'OK until they are not OK'.

Unsigned accounts

Alex agreed with the claim made by his children (the intervenors). By contrast, Julie's pleaded case was that the intervenors had no interest in any of the properties – an obvious approach, given the more Alex lost to his children, the less she could claim in the divorce.

The four properties in question were two farms, a student buy-to-let and a further residential property. All the children were party to an agricultural charge against the farming properties for borrowings. However, while all the properties were included in the partnership accounts, which in part gave clarity, none of the annual accounts had actually been signed by all the farming partners. Again, this is not that unusual in farming arrangements but acts as a reminder to all accountants and legal advisers of farming families that this should not be the case and to ensure everything is in place.

It is important that all parties to a farming business keep clear financial records, for example where a family member has contributed to property improvements or to payments towards a mortgage or other borrowing, always assuming they would get a share of that property because they may have built an extension, or improved land. However, that must be recorded and clearly agreed.

Another example of the need to keep clear records is where money may be transferred to someone else. It's useful to have the correct reference in the farm records of the business. Not every judge is the same, but in general a court, and indeed legal advisers, are likely to put greater weight on contemporaneous documentation rather than oral testimony.

What is and is not partnership property

Two of the properties (Border View Farm and Dunston Farm) were integral to the farming business. The third (Heavygate Road) was a student buy-to-let and the fourth (Smugglers) was bought by Alex in 2021 as a home for Julie following their separation before the divorce. All four properties were included in the partnership accounts. The issues for the court were:

- if any of the four properties were partnership assets; and
- if any were not partnership assets, the question was whether Alex and/or Julie were prevented from relying on their rights to those non-partnership properties by proprietary estoppel.

Proprietary estoppel cases are increasingly common in farming and involve a claim that a promise has been made about inheritance that someone has relied on to their detriment, often by working for little money and forgoing other opportunities. By the time the case came to court, the four children had collectively established an estimated 77 years' work in the farming business. The farming business only had one bank account, with all transactions relating to the farm and the properties going through that account.

In the ruling, Judge Baddeley said: 'I find that the intervenors each relied on these promises when committing their working lives to the farm. Their evidence on this issue was compelling. They each said in their own way that they would have been foolish to put in all that effort for a share in the farm income alone. In my judgment, the evidence of the intervenors' reliance on those assurances is overwhelming.'

The judge was disappointed that the partnership agreement signed by all six partners in 2020 didn't clarify which property belonged to the partnership. But such lack of clarity is not that unusual. Had the agreement been clearer (and ideally accounts signed), the need for expensive and stressful litigation could probably have been avoided. Since this was not the case, the judge had to look at the other facts and try to decide what a reasonable person – knowing what everyone knew at the time – would think the document meant.

The judge found there was a common understanding that Border View Farm and Dunston Farm were partnership property. The intervenors had all worked hard on the farm, receiving no pay after they finished school, and it would not make much sense for them to do that unless they were meant to be part-owners. However, the judge found that Heavygate Road and Smugglers were not part of the partnership. Those properties had nothing to do with the farm and, even though they were included in the partnership accounts, the judge did not see that as definitive. As such, it was ruled that each intervenor was entitled to one-sixth share of the two farms but had no ownership interest in the other two properties.

This is an interesting point as there is much debate about whether a partnership asset should be in the partnership accounts. The answer is yes, as it belongs to the partnership, but this case shows the need to question and to have guidance and corroboration in the partnership agreement for anything that is not clearcut. Where the legal understanding and even the tax returns do not dovetail with the accounts, this renders them almost meaningless and unreliable evidence if later required in court.

> "In an ideal world there should be a meeting with all partners to agree and sign the partnership accounts."

Need for a strong farm partnership agreement

The *Merryman* case reinforces the need for clear drafting of the farm partnership agreement. In this instance, it wasn't just that the drafting hadn't been done well. There were clearly things that anyone who had taken the time to read it through would realise were mistakes, perhaps resulting from using a template where some options had not been struck through.

The judge concluded: 'The case was complicated by a poorly drafted and inconsistent partnership agreement. The partnership deed should have clearly defined the partnership property. Had it done so, the need for this expensive and stressful litigation could probably have been avoided.'

This is a strong statement for all those drafting partnership agreements to remember the quality of drafting that is needed, and to check the partnership agreement reflects what is happening on the ground and in the accounts regularly. In an ideal world there should be a meeting with all partners to agree and sign the partnership accounts. It is often good practice and can be helpful and protectionary for accountants to attach the partnership agreement with the accounts, reconciling the freehold property and highlighting key points to be considered. ●

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