OWNERSHIP ARGUMENTS

Julie Butler considers whether inclusion of an error in the accounts changes legal ownership

The issue in the *Ham v Bell and Ors* [2016] EWHC 1791(Ch) case concerned a partnership between husband and wife, and their son, and centred on whether the land being farmed was an asset of the partnership. There was a written partnership agreement but it did not specifically deal with the question of whether the land being farmed was a partnership asset. It was 'quiet' on the subject of land ownership.

The son argued that the land was an asset of the partnership because it was shown as such in the accounts for the first few years of the partnership, which had not been signed by the partners. Later accounts, which were signed by all the parties, including the son, did not show that the land was a partnership asset.

After examining the evidence, which included the accounts, it was held by the Court that the land was not an asset of the partnership. Part of the reasoning to say it was not a partnership asset was because the parties had not agreed that it should be, the parents having made it clear to their son that they did not wish the land to be an asset of the partnership. So often the importance of the detail of accounts is not fully understood by the partners.

In *Ham v Bell,* the Court held that the fact that the farm appeared in the relevant accounts as an asset of the partnership had been due to error. It was decided that on the balance of the evidence there had not been an agreement nor understanding that the farm had become an asset of the partnership. In reality, the facts must be 'drilled down' to understand the true position regarding farm ownership.

The case shows the accountancy profession needs the help of the legal profession in both the correct identification of asset ownership and the drafting of a comprehensive legal agreement to support this understanding. The judge found as a fact in this case that the partners had not signed the accounts of the new partnership in which the land was shown as a partnership asset. Those accounts were not therefore evidence of the parties having agreed that the land was to be an asset of the partnership.

ROLE OF THE ACCOUNTANT

This highlights the importance for the signature to the partnership accounts to be both explained to clients and the important part that the signature as approval to the accounts plays. Such a case does highlight the impact on everyday decisions facing the accountancy profession such as accounts approved by email.

Having considered the evidence, the judge concluded that the son had been aware of what the accounts contained, and that these accounts were evidence that it had been agreed that the land was not to be a partnership asset. The importance was the intention of the partners as to ownership.

NO MORE THAN EVIDENCE

The judge pointed out that the accounts were no more than evidence and would be disregarded if they did not reflect what the parties had agreed, adding on the role of accountants in this case of *Ham v Bell* that 'the accounts of a partnership may provide evidence as to whether there was an express agreement to make land a partnership asset. If one partner says there was such an express agreement and the other denies

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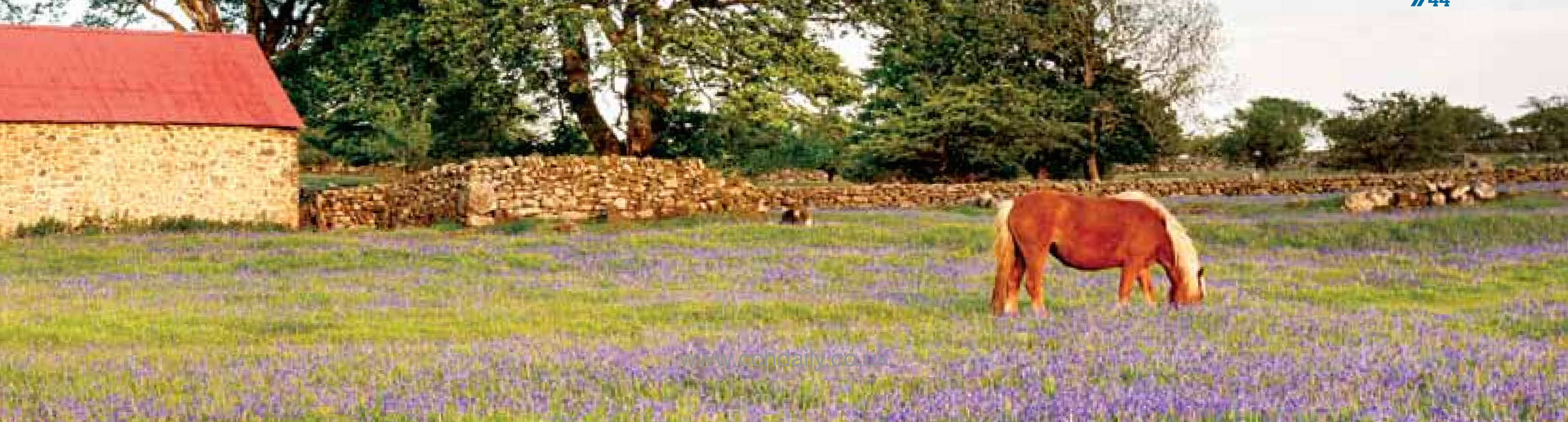

HIGH COURT RULING – HAM V BELL

Ham v Bell & Ors [2016] EWHC 1791(Ch) (John Ronald Ham v Jeremy Bevan Bell, Keith Harden Turner and Lorna Jean Ham)
On appeal from Ham v Ham & Anor [2013] EWCA Civ 1301

Farming partnership dispute over farm of 900 acres, of which 350 acres were rented, and 550 owned. Case revolved around partnership arrangements, involving signing off of partnership accounts and tax returns, and historic cost of farm in the balance sheet

Judge: His Honour Judge McCahill QC

Where: High Court of Justice, Chancery Division, Bristol District Registry

When: 11 April 2016

Decision: Judge 'concluded that the farm and milk quota were not assets of the new partnership and that John [Ham] always knew that'.

it, the accounts may help the court to decide whose recollection is more reliable.

'That was the submission of Mr Jourdan [defendant's QC] who went on to contend that farmers and other business people do not always look carefully at accounts or appreciate what the entries in them mean and mistakes can be made.'

It is quite a worry if the accounts are the final deciding factor as to the ownership of partnership assets and the accountant who prepares the accounts must put protection in place.

A practical approach is for accounts to be supported by a 'letter of representation' to be signed by the partners about what is included in the balance sheet which is further understanding and verification. Likewise a full documented explanation of the accounts to the partners is very important.

ACCOUNTING ISSUES

It is essential to remember the importance of the accounting treatment of freehold property/ partnership assets. Such treatment is not an accounting exercise nor an accounts exam. It is real understanding and might be used as evidence. Any changes to disclosure should be taken into account on the balance sheet.

The facts of the *Ham v Bell* case were that in 1997 the son was brought into the partnership and the land was shown as being a partnership asset in the accounts for the new partnership, but this was later corrected. The question before the Court was what could be inferred from the accounts. The issues were described by the judgment as follows: 'Accordingly, the central issue… to decide has been broken down into sub-issues, although there is a dispute over whether one aspect of the third sub-issue arises on the pleadings.'

The sub-issues focused on whether the inclusion in the accounts for the years ending 28 February 1998 to 2003 of figures representing the historic cost of the farm mean that it was an asset of the new partnership or was simply an accounting error that was put right in the accounts for the years ending 29 February 2004 (a leap year) and subsequently.

ACCOUNTS AND OWNERSHIP

Many would argue that the accounts treatment should not be able to change legal ownership, however those charged with preparation thereof must realise the consequences, with such high agricultural values of the incorrect treatment of the freehold property. The farming, accountancy, tax and legal professions must work as a team with regard to ensuring correct understanding.

The importance of the accounts treatment is very influential. Are those tasked with preparing the accounts aware of this responsibility?

TAX PLANNING

Many farmers and some accountants do not understand the difference between 'jointly owned property' and 'partnership property'. They also need to be aware of the key tax point that partnership property achieves 100% business property relief (BPR) for inheritance tax and

non-partnership property only achieves 50%.

To consider the tax position in more detail, it can be important, for tax reasons, to identify and distinguish between the land and other assets being used in a partnership.

If the farmland is partnership property or is owned by an individual partner who permits the partnership to use them, the value of land which is a partnership property should be reflected in the value of the business itself, or a share in it, which may qualify for the inheritance tax (IHT) business property relief (BPR) at the rate of 100% (see s104(1)(a) and s105(1)(a) Inheritance Tax Act 1984 (IHTA 1984).

Land which is used by the partnership but owned by an individual partner, rather than being a partnership asset, will only qualify for the relief at the rate of 50% (see s105(1)(d) and s104(b) IHTA 1984). In the case of capital gains tax (CGT) entrepreneurs' relief, if the land is part of the partnership property then any gain realised when it is disposed of as part of the partnership business will qualify for entrepreneurs' relief in its entirety without the reductions that may be applied when there is an 'associated disposal' of land held outside the partnership.

The question of whether, for example, land is a partnership asset will depend upon what the partners have agreed and that it is in the form of a partnership agreement. Alternatively, the accounts may provide evidence. In practice less than a quarter of farming partnerships have partnership agreements so the accounts have huge responsibility placed upon them and those tasked with this role.

NOT A PARTNERSHIP ASSET

All those involved must realise that making a substantial asset, like land, partnership property for tax planning purposes, will have important legal consequences. A worse case could be that the former owner of the land may possibly find out that on a dissolution of the partnership he may have to pay a substantial sum to buy back his own land. Such protection depends on what the partnership agreement says. Regarding land ownership in these situations, the deceptively simple default provisions of the Partnership Act 1890 may apply if the partnership agreement does not provide, and as partnership property it is held jointly as joint tenants, so the property can pass back to the remaining partners.

With so much unregistered farmland in the UK there is large scope for future confusion

THE WILLS

Another aspect of having a formal partnership agreement is that, if prepared by legal advisers, the Court would consider the terms of the will. In *Ham v Bell* the Court took account of the parents' wills and noted that they had disposed of their interests in the farmland in their wills; bequests which would have been ineffective if the land had been a partnership asset. This was considered evidence that the land was not intended to be a partnership asset.

The solicitor drafting the partnership agreement must be mindful of the detail of the partnership accounts, wills and general understanding of what the accounts show. Partnership property can be held as beneficial tenants in common.

With so much unregistered farmland in the UK there is large scope for future confusion. There also has to be client responsibility. The farming community must understand the importance of farmland ownership and the individuals in the partnership must take time to understand the legal and tax consequences of how the farm is owned.

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