LAW&TAX

Law and Tax for Professional Partnerships

Peter White

Law & Tax Series

Law and Tax
for
Professional Partnerships

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Preface

This new book deals with what the partners of a professional practice really need to know about the legal, financial and tax implications of their professional firm. It examines these aspects of professional partnerships from the time of creation, through changes in the partnership by admission or retirement, to the ultimate dissolution. Important matters, such as salaried partners, the partnership income and the provision of capital, are also considered. Even the topic of insolvency is dealt with, although only briefly since it is a subject which rarely needs to be contemplated in relation to the professions.

The book is designed not just for firms of lawyers and accountants, but for all the professions, including surveyors, architects, tax practitioners and estate agents. Most professionals carry on business through partnerships and their professional rules prohibit any other type of business medium through which to carry on their professional business. But professions do not necessarily have to be carried on by individuals. Some professions, such as architects, estate agents, insurance brokers and stock-brokers are permitted to carry on business through a limited company, and others, such as surveyors and, for some work, accountants, may carry on professional business through an unlimited company. All professions can use service companies.

This book, therefore, covers the legal and tax implications of companies in relation to the professional firm, including whether to use a company instead of a firm, or as a service company, or, indeed, as a partner. Similarly, limited partnerships may be a possibility for some professions, and the implications are considered in Chapter 12.

The value of this book as a guide to professional practices is considerably enhanced by the partnership precedent in Appendix 1. It is a modern tax-efficient agreement and can be used as a model for all professional partnerships. It is taken from Potter & Monroe's *Tax Planning* and is printed here with the permission of the editors, A R Thornhill and R Venables, and of the authors A R Thornhill, R Venables, A G Wilson and W G S Massey, and of the publishers, Sweet & Maxwell, to all of whom the author is grateful. A measure of the importance of this agreement is that it is used (with minor adjustments) as the standard precedent for partnership agreements for the Solicitors' Final Examination.

Budget 1984

This book was held back in publication in order to take into account the effect of the Budget on 13 March 1984.

Alterations have been made throughout the book to bring it up to date for the tax year 1984/85, but is has not been possible to wait for the publication of the Finance Bill, let alone the Finance Act 1984.

A brief summary of those Budget proposals which affect this book is set out below.

Income tax

The income tax rates for 1984/85 will be:

Taxable Income	*Rate*
The first £15,400	30%
to £18,200	40%
to £23,100	45%
to £30,600	50%
to £38,100	55%
remainder	60%

The investment income surcharge has been abolished.

Personal reliefs

For the tax year 1984/85, the major personal reliefs will be:

Relief	*Amount*
Single person's	£2,005
Married man's	£3,155
Wife's earned—up to	£2,005
Age (single)	£2,490
Age (married)	£3,955
Single parent family	£1,150
Widow's bereavement	£1,150

Life assurance relief

Relief for existing policies remains at 15%, but for policies taken out or enhanced after 13 March 1984 the relief is abolished.

Retirement annuity relief

Is unchanged for 1984/85.

Stock relief

Is abolished for any period of account which begins on or after 13 March 1984. There will be no clawback of relief previously given, however.

Capital allowances

First year allowances on plant and machinery are to be phased out. For expenditure incurred after 13 March 1984 but before 1 April 1985, the relief is reduced to 75%: for expenditure incurred from 1 April 1985 to before 1 April 1986, the relief is reduced to 50%. Thereafter no first year allowances will be given, but the 25% writing down allowance will continue to be available.

Corporation tax

The rate of corporation tax is to be reduced over four years, as follows:

Financial year	*Rate*
1983	50%
1984	45%
1985	40%
1986	35%

The small companies rate for the financial years 1983–86 is 30% and the threshold remains unchanged at £100,000 with marginal rates to £500,000, and the marginal percentage 55%.

Capital gains tax

The annual exemption is increased to £5,600 for 1984/85. The limit for retirement relief is increased from £50,000 to £100,000, and for those between age 60 and 65 the relief is proportionately increased. A consultative document has been issued about further changes in retirement relief.

The self-employed will be able to benefit from private residence exemption when in 'job-related' accommodation in the same way as the employed, for disposals on or after 6 April 1983.

Capital transfer tax

The rates effective from 13 March 1984 are:

Chargeable transfers £	*Higher rate* %	*Lifetime rate* %
0— 64,000	nil	nil
64,000— 85,000	30	15
85,000—116,000	35	17½
116,000—148,000	40	20
148,000—185,000	45	22½
185,000—232,000	50	25
232,000—285,000	55	27½
285,000 and over	60	30

Otherwise, exemptions and reliefs remain the same.

Peter White
March 1984

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Chapter 1

Forming a partnership

1.01 Why have a partnership?

Whenever two or more persons are about to start in business together, they will consider whether they should do so through the medium of a company, limited or unlimited, or as partners. Even the sole businessman will consider whether, if he is in due course to take others into business with him, he should start out as a sole trader instead of through a company, so that when those others join him, they will either become his partners or co-directors as well as, perhaps, shareholders.

This book is about professional partnerships and most professionals have no choice. Solicitors, barristers, doctors, dentists, actuaries and others are not allowed to carry on their professions through the medium of a company, limited or unlimited. Some professions, such as stockbrokers, estate agents and architects, allow the use of limited companies and accountants may carry on some non-audit work through the medium of an unlimited company. Most professions can however use companies as service companies. The point is that the main advantage of a limited company—limited liability—is not usually available to professionals, in respect of their professional work. The whole topic of companies and partnerships is dealt with comprehensively in Chapter 13.

It is, however, worth bearing in mind the tax advantages of having a partnership and these are as follows.

The assessment rules

The preceding year basis of assessment can give up to 21 months' postponement of tax liability on profits, and the cessation rules can eliminate liability on more than a whole accounting year's profits. The tax planning implications are considered in Chapter 2.

Spouses

A salary paid to a spouse is deductible only to the extent that it is reasonable: *Copeman* v *Flood* (1941) 24 TC 53. In non-professional partnerships, or where the spouse is professionally qualified, it can be better to take a spouse into partnership because both will then be taxed on their own partnership share, and if both are actively engaged, each share will be treated as earned income.

When business is being commenced, however, it is often sensible to employ a spouse, paying a reasonable salary, to keep profits down in the first year, thus minimising the first three tax years' assessments. The spouse can then be admitted to partnership, with a continuation election under TA 1970, s 154(2).