

Chapter 8

PARTNERSHIPS

1 Introduction

A partnership is a single trading entity, but for taxation purposes each individual partner is effectively treated as trading in his own right and is assessed on his or her share of the adjusted trading profit of the partnership. It is essential to understand therefore that it is not the partnership itself that is assessed upon its adjusted trading profit, but it is each individual partner who will be assessed on his or her share of that adjusted trading profit.

2 Trading income

- (a) The partnership's tax adjusted profits or loss for an accounting period is computed in the same way as for a sole trader.
- (b) Partners' salaries and interest on capital debited on the statement of profit or loss are not deductible as expenses as these are simply an allocation of trading profit by the owners of the business.

3 Allocation of the trading profit or trading loss

- (a) The trading income or trading loss is divided between the partners according to their profit sharing arrangements in force during the accounting period.
- (b) Partners may firstly be entitled to salaries and interest on capital. The balance of any trading profit (or loss) will then be allocated in the profit sharing ratio (PSR).

4 A change in the profit sharing agreement

If the profit sharing agreement is changed during a period of account, the profit must be time apportioned before allocation under the different agreements.

EXAMPLE 1

Doug and Rob are in partnership. The trading income for the year ended 30 September 2017 was £18,000.

Up to 30 June 2017 profits were shared between Doug and Rob 3:2, after paying salaries of £3,000 and £2,000 per annum.

From 1 July 2017 profits were shared 2:1 after paying salaries of £6,000 and £4,000 per annum.

Show the allocation of trading profits for the Accounting Period ended 30 September 2017.

5 Partnership capital allowances

- (a) Capital allowances are deducted as normal in calculating the tax adjusted trading profit.
- (b) If assets are used privately by the partners, then as for a sole trader only the business proportion is included in the capital allowances computation.

6 Commencement and cessation

- (a) The rules for commencement and cessation when a partner joins the partnership or leaves the partnership are the same as for a sole trader.
- (b) The profit is allocated between the partners for accounting periods and then the assessment rules are applied.
- (c) Each partner is effectively taxed as a sole trader on his/her share of the adjusted trading profit
- (d) Continuing partners will be assessed using CYB
- (e) When a new partner joins a partnership, they are treated as commencing a new trade and hence the opening years rules apply
- (f) When an old partner leaves a partnership they are treated as ceasing a trade and hence the closing years rules apply
- (g) Each partner has their own overlap profit available for relief.

7 A change in the membership of a partnership

- (a) As long as there is at least one partner common to the business before and after the change, the partnership continues.
- (b) The commencement or cessation rules apply ONLY to the individuals joining or leaving the partnership.

EXAMPLE 2

Ann and Beryl have been in partnership since 1 July 2015 making up their accounts to 30 June each year. On 1 July 2017 Clair joins the partnership.

The partnership's trading profit is as follows:

	£
Year ended 30 June 2016	12,000
Year ended 30 June 2017	14,000
Year ended 30 June 2018	24,000

Profits are shared equally.

Show the amounts assessed on the individual partners for all relevant tax years of assessment.

8 Partnership losses

- (a) Losses are allocated between partners in the same way as profits.
- (b) Loss relief claims available are the same as for sole traders and each partner may choose their own preferred use of their loss
- (c) Partners continuing in a partnership will be able to claim to carry forward their loss, or to set off against total income of current and / or preceding tax years and thereafter extend against chargeable gains.
- (d) A partner joining the partnership may also choose to claim under opening years loss relief, for losses in the first four tax years of his membership of the partnership.
This relief is not available to existing partners.
- (e) A partner leaving a partnership may also choose to claim under terminal loss relief.
This relief is not available to partners remaining in the partnership.

EXAMPLE 3

John, James and Paul are in partnership making up their accounts to 5 April. During 2018/19 Paul left the partnership and George joined in his place.

For the year ended 5 April 2019 the partnership made a trading loss.

State the loss relief claims that will be available to the partners.

Students may now attempt Practice Question 18