# PARTNERSHIPS

A partnership is an association of 2 or more persons who share the ownership of a business that is operating for profit.

The common types of partnerships in farming are;

* Husband / Wife partnerships, where all business profits and losses are shared between them.
* Equity partnerships; where a number of people with similar objectives join forces as partners, to invest in a venture that none have the resources or skills to do alone.

No legal formalities are required to form a partnership; (the structure is governed by the Partnership Act 1908) but a documented partnership agreement (or deed) should be drawn up. This will ensure that the partners have considered all points before entering into the partnership.

Any agreement should cover the following points:

* The nature of the business (goals and objectives).
* Who will contribute what in terms of capital, labour, skills, etc.?
* Who is responsible for management decisions, and how they will be made.
* How any profits will be distributed? (Particularly if not 50/50 basis).
* Who will keep what records? (Records are important for the division of profits, and for maintaining an inventory of assets and their ownership).
* Who is responsible for what, in terms of business operations?
* What will happen on dissolution of the partnership? (If one partner wishes to leave).

Many partnerships fail and break up. Goals and attitudes may change over time; misunderstandings or jealousies can occur.

A well researched proposal with clear objectives, together with a documented partnership agreement and a policy of regular management meetings, is essential for the success of any partnership.

The basic characteristics of a partnership are;

* A sharing of business profits and losses.
* Shared control of capital and property, with possible shared ownership.
* Shared management of the business.

The exact sharing arrangements for the above characteristics are flexible, and should be outlined in the partnership agreement. Profits are generally shared in proportion to the assets contributed by each partner, but can be shared on any basis agreeable to the partners.

A partnership can be terminated in a number of ways. The agreement may specify a termination date. If not, a partnership will terminate on the death of a partner, incapacitation of a partner, bankruptcy, or by agreement.

Termination upon the death of a partner can be prevented by provisions in the written agreement allowing the deceased partners share to pass to the legal heirs.

On dissolution of the partnership there are several ways that the capital can be repaid to the partners.

* The assets sold off and the partnerships debts paid from the proceeds.
* One or more partners may continue with the business buying the others out.
* The business may be sold to another party as a “going concern”.

A partnership is a close relationship, both legal and personal, between two or more persons. There must be complete understanding and trust between the partners if the business is going to succeed. Compatibility is very important; as personal conflicts often lead to the termination of partnerships. Each partner must believe that the partnership will be more advantageous than operating alone. Finding like-minded people with similar goals and objectives, is the challenge in setting up a successful partnership.

**Advantages**

* Ease of formation. A partnership is easy to form and can be very flexible.

It can be suitable in situations where a spouse or children wish to enter the business. (i.e. may contribute only labour initially, but can be modified to allow for increasing contributions of management and capital).

* Works very well for married couples whose assets are often joint anyway.
* The pooling of capital, management skills, and other resources allows a larger business, which can lead to efficiencies of size and economies of scale, allowing greater profitability. It may also increase the amount of credit available, allowing further expansion.
* Growth possibilities. Partnerships allow businesses to grow by bringing in more expertise and capital.
* Access to accounts and financial records by partners at any time, unless otherwise agreed.

# Disadvantages

* A partner cannot be held responsible for the personal debts of the other partners, but can be held personally and individually responsible for any lawsuits and financial obligations arising from the operation of the partnership.

If the partnership does not have sufficient assets to cover legal financial obligations, creditors can bring suit against all partners individually to collect any money due, i.e. a partner’s personal assets can be claimed by a creditor to pay debts owing.

* It is very important for all partners to ensure that they are very familiar with the day to day financial affairs of the business.; one partner may be able to incur debt on behalf of the partnership without the other partner’s knowledge. E.g. If partners have sole signing authority at their bank, one partner may legitimately be permitted by the bank to increase the seasonal overdraft facility without the other partner’s signature.
* If a partnership is formed to give more tax effective results when one partner owns or has contributed significantly more than the other, specialist legal advice should be taken first. (Unless separate steps are taken to adjust the ownership under the PRA 1976 as between married or de facto couples, all partnership assets are ‘relationship property’ under the Act.)
* If partners are not also spouses, the impact of the PRA can be huge, as a partner’s interest in the partnership may be ‘relationship property’. This could lead to the partnership needing to be wound up to allow the partner who is separating to access his / her assets for a property division.
* Conflict can arise between partners on management issues.
* Before a partner can transfer his/her stake in the partnership to someone else, there must be total agreement between partners. This may be difficult to obtain. It may be necessary to dissolve the partnership and then form a new one.
* More difficult to exit the business than as a sole trader; the partnership would usually need to be wound up and a new structure created.

# Taxation

The income tax paid by each partner is based on their respective share of the partnership income.

In a 50/50 partnership, each partner would declare half of the partnership income, depreciation, capital gain, etc. This is then included with any other income the partner may have, and is taxed at individual tax rates.

An advantage of this is the spread of income to a number of individuals, e.g. a farm owned by a married couple. If they trade as a partnership as opposed to a sole trader, less tax may be incurred as the income is split between the two partners, taking advantage of lower tax rates.