IN SIDER

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the municipality finances her expenditures with taxes instead of with debts. Hence, public political parties, which generally represent landlords rather than tenants, are against higher debts, as opposed to more left-wing parties.

If not only the municipality but also adjacent bodies or the central Government had to settle the liabilities of the municipality, according to Eichenberger/Stadelmann real estate prices would not only decline locally, but also supralocally due to high indebtedness. As people are much more mobile and flexible as in the past, and are even willing to move abroad, an excessive debt policy can pull downwards the real estate prices of the entire country. In general, this means „the higher the debts, the lower the property prices."

If this is right, property prices would have to be relatively low in the USA, Japan, Spain, France or also Germany, as opposed to those in Switzerland, Luxembourg and the Scandinavian countries.

Amongst other issues, we will discuss these correlations in our next Real Estate practice group meeting, which will take place on 19 April 2013 in Lisbon.

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TRUST & ESTATE PLANNING (TEP)

The use of family limited partnerships in the context of UK tax and estate planning

By Camilla Wallace

For over a century in the UK, the trust has been the favoured structure for holding family wealth. However, the UK Government's extension of inheritance tax (IHT) in 2006 to virtually all new and some existing trusts saw many wealthy families look for alternatives. Two of those alternatives are family partnerships and family investment companies.

There are three different forms of family partnership: general partnerships, limited partnerships and limited liability partnerships. This article will focus on family general partnerships (FGPs) and family limited partnership (FLPs). Generally, limited liability partnerships are less popular as they are subject to UK company law and have annual filings to make with the UK's Registrar of Companies which means the names of the underlying owners are publically available. They are also subject to a double layer of taxation (at company and shareholder level) which again has made them less popular in UK estate planning.

What are FGPs and FLPs?

FGPs and FLPs are defined in s.1 of the Partnership Act 1890 as "the relation which subsists between persons carrying on a business in common with a view of profit." In the context of estate planning, a partnership is used to manage family wealth with the partners comprising junior family members (the ultimate beneficiaries) or nominees appointed on their behalf if they are under 18. The assets will generally be contributed to the partnership by senior family members although they should not be partners themselves if the structure is to be effective from an IHT perspective. Partners in a FGP have unlimited liability for their debts, whereas a FLP has the attraction of limited liability.

A FLP has a more complex structure than a FGP as it splits control and economic benefits between a "general partner" and up to 19 "limited partners". The general partner (usually a company controlled by senior family members) has unlimited liability for the partnership's debts and obligations and is responsible for managing the partnership business. The role is one of control and is akin to a trustee in a trust structure. The limited partners have limited liability up to the amount of their contributions but no management powers. These persons are generally junior family members, similar to beneficiaries of a trust.

Either way, all partners sign a partnership deed, the partnership's governing document, which sets out how capital, income and gains are to be shared amongst the partners and under what circumstances the partners can receive withdrawals of capital.

Key features

The essential features, advantages and drawbacks of FGPs and FLPs are as follows.

Tax: The main driving force behind these structures is tax. Most UK trusts are now subject to an IHT charge every ten years and when capital leaves the trust. In addition, when creating a UK trust, a settlor faces an immediate charge to IHT at 20% of the value of the assets settled if these exceed his available nil-rate band (currently a maximum of £325,000). By contrast, there is no IHT charge when creating a FGP or FLP (provided the donor survives seven years) and no on-going IHT charges during the subsistence of the partnership. A partnership also has advantages from a UK income tax perspective as the most flexible form of UK trust is subject to income tax at 50%. A partnership however, is tax transparent, meaning that the partners are assessed on the income of the partnership as if they owned it directly, in accordance with their shares. As such, income is taxed at the partners' marginal rates of income tax with the benefit of personal allowances. In many cases, unless the partner is a top rate tax payer, this will produce an income tax saving. Note, however, that income of minor partners will be taxed at their parent's rate if their contribution to the partnership came from a parent.

Business: The partners must be carrying out a business in order for a partnership to exist. Merely holding investments will not suffice unless they are being actively managed. Holding residential property is acceptable provided the property is let and managed. In many instances, the requirement for some form of business activity presents a practical difficulty for families unless their assets or intentions are of a commercial nature.

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Asset protection: Partnerships provide a similar level of asset protection to a trust by allowing senior family members to pass wealth down to younger generations without relinquishing complete control. This can be done by senior family members acting as, or being the controlling force behind, the general partner (in a FLP) and/or writing appropriate protections into the partnership deed regarding capital withdrawals and the age at which these can be made.

Regulation: FLPs usually have to be regulated by the UK's Financial Services Authority (FSA) as a "collective investment scheme". In practice this means that the general partner delegates his management and operational functions to a FSA-authorised professional. This delegation makes FLPs expensive to run; they would usually need assets in excess of £10m to make them cost effective. FGPs do not generally have this layer of regulation and make a cheaper alternative, but they do not have the same level of control for senior family members.

Confidentiality: FGPs and FLPs do not have to file annual accounts with the UK's Registrar of Companies meaning that the identity of partners can be kept confidential.

Comment

The FLP is generally the more popular choice of alternative wealth management vehicle in the UK but they are still relatively rare because of the expense involved and because the trust is still the traditional "tried and tested" family estate planning structure. However, where significant wealth is at stake, the merit of a FLP should be weighed up against those of a trust, as the particular circumstances of the family may make it worthwhile. Particularly so if the family are concerned with short-term tax savings: it is possible to set up a FLP at no tax cost and with no limitation on the amount that can be put in, whereas a trust holding investments will invariably have an upfront IHT cost.

However, some words of warning to end on. FLPs may be subject to the UK's new taxation regime for "non-natural persons" holding UK residential property (for personal use) worth more than £2m as at 1 April 2012. This consists of an annual charge, a 28% rate of capital gains tax and 15% rate of stamp duty land tax. In addition, the Government hinted in its annual Autumn Statement on 5 December 2012 that it would be looking closely at tax avoidance involving partnerships. However, until that time, they remain viable alternatives to trusts for UK tax and estate planning purposes.

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