Neutral Citation Number: [2022] EWHC 2689 (Ch)

Case No: BL-2020-MAN-000005

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURT IN MANCHESTER
BUSINESS LIST (ChD)

Manchester Civil Justice Centre,
1 Bridge Street West,
Manchester,
M60 9DJ

Date: 29/09/2022

Before:

HIS HONOUR JUDGE HALLIWELL

- -

Between:

JULIE ANN MORTON
(AS EXECUTRIX TO THE ESTATE OF JENNIFER RUTH MORTON DECEASED)

Claimant

- and -

(1) SIMON NIGEL MORTON
(2) ALISON MARY MORTON

Defendants

- -
- -

MR GILES MAYNARD-CONNOR KC (instructed by **Aaron and Partners LLP**) for the **Claimant**
MR JONATHAN EDWARDS (instructed by **Quinn Barrow Solicitors**) for the **Defendants**

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Approved Judgment

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HIS HONOUR JUDGE HALLIWELL :

1. On 27 January, I gave judgment on Ms Julie Morton's claim for declaratory and related relief in relation to the ownership of the family partnership assets at Reddish Hall Farm, Lymm, Cheshire and Fairoak Grange, Ecclesall, Staffordshire. My judgment is at [2022] EWHC 163 (Ch). The partners were the late Jennifer Ruth Morton and the defendants, Mr Simon Morton and his wife Mrs Alison Morton. Julie Morton sues as Jennifer's executrix.

2. On 26 April, I made an order declaring that the partnership dissolved on 8 May 2015. As remedies fashioned from the law of proprietary estoppel, I made an award enlarging Simon's share in the assets of the partnership. I set aside the contract for the purchase of Jennifer's share in the assets of the partnership under an option in the partnership deed dated 19 December 2012 ("the Partnership Deed") and extended time for Simon and Alison to exercise the option so as to expire three months after the court has determined the purchase price. I also made directions providing for the determination of the purchase price on the footing that the purchase price was to be based on the formula prescribed by the Partnership Deed but adjusted so as to take into account Simon's enlarged share and Jennifer's correspondingly reduced share in the partnership assets.

3. By clause 19 of the Partnership Deed, the purchase price is "the amount standing to the credit of the Outgoing Partner on the date of the Determining Event [as defined] after there shall have been a revaluation at that date of the partnership's then assets". In the present case, the Determining Event is the expiry, on 8 May 2015, of Jennifer's written dissolution notice.

4. Directions were made permitting the parties to jointly instruct Ms Sally Longworth of Longworth Forensic Accounting Limited as their expert to prepare a balance sheet for the partnership as at 8 May 2015, separately recording the capital in the current account for each partner. The order contained directions for the parties to provide the expert with a schedule setting out balance sheet adjustments - denoted as the Accounting Issues - and for the expert to provide the parties with a final balance sheet and report.

5. Ms Longworth filed a report dated 29 July with a balance sheet recording the net partnership assets of £5,974,558. After accounting for Simon Morton's liability on a Barclays loan in the sum of £1,632,568 and trade creditors of £30,939, Ms Longworth's assessment was that Jennifer was entitled, on capital account, to the sum of £2,116,492, Simon was entitled to £2,178,149 and Alison Morton was entitled to £16,410.

6. The present hearing was listed under the court's directions dated 26 April with a view to determining the Accounting Issues, as defined, and determining the purchase price in the event that the option is exercised. It was also listed with a view to resolving the extent to which, having elected to claim interest under *section 42* of the *Partnership Act 1890*, Julie Morton is entitled to do so. I am also asked to give directions for the winding up of the partnership and other matters arising in the event that the option is not exercised. It will ultimately be necessary for me to resolve the issue of costs.

7. I shall deal first with the outstanding Accounting Issues. The matter came before me at a PTR earlier this month on 1 September when Mr Giles Maynard-Connor KC appeared on behalf of Julie Morton and Mr Jonathan Edwards, appeared on behalf of Simon and Alison Morton, as indeed both counsel have done throughout these proceedings. At the PTR, Mr Maynard-Connor confirmed that Julie Morton was willing to agree Ms Longworth's report. At that stage, Quinn Barrow, the solicitors for Simon and Julie Morton, were awaiting Ms Longworth's replies to a series of questions in relation to her report. In anticipation, Mr Edwards undertook on their behalf to identify which parts of the report were agreed or not agreed by 16 September. As it happens, Ms Longworth's detailed response was on 4 September and, by letter dated 16 September, Quinn Barrow identified the remaining matters in issue and these were canvassed with Aaron and Partners on behalf of Julie Morton.

8. When the present hearing commenced on Monday, Mr Maynard-Connor was able to confirm that there should be a reduction of £17,147 in respect of Jennifer's capital account to reflect Ms Longworth's conclusion in paragraph 16 of her letter of 4 September. On this basis, the overall amount to which Jennifer is notionally entitled on capital account must be reduced from £2,116,492 to £2,099,345, subject to further adjustment.

9. Mr Maynard-Connor also conceded that an additional sum of £19,283 should be deducted from Jennifer's capital account on the basis that Ms Longworth was unaware, when preparing and filing her account, that this related to Pheasant Lodge. She was led into error because the relevant entry was for "Reddish Hall Farm Cottage" and she did not appreciate this was another name for Pheasant Lodge. Once the sum of £19,283 is deducted from £2,099,345, this leaves £2,080,062.

10. Quinn Barrow's schedule of adjustments dated 10 June 2022 included a list of post dissolution expenses in respect of Jennifer or her estate amounting to some £38,711.23. At the beginning of the hearing, Mr Maynard-Connor conceded that £14,855.04 should be deducted from Jennifer's capital account made up of six items applied for her benefit, including continued drawings at a rate of £600 per month until Jennifer's death, a taxi fare on 1 October 2015 and bills in respect of window cleaning and her personal tax liability.

11. I heard evidence from Julie, Alison and Simon Morton. I also heard expert evidence from Ms Longworth. Mr Maynard-Connor was critical of Simon Morton's evidence. At this stage, I am satisfied that I can generally rely on the evidence of each of the witnesses, including Simon, save for his evidence on one aspect to which I shall refer later. The outcome of the remaining issues essentially turns on the contemporaneous records in the light of Ms Longworth's expert evidence, subject to some discrete questions to which I shall refer later.

12. In the light of Alison Morton's evidence, the parties reached agreement during the hearing, that some £26,783.04 should be deducted in respect of the post dissolution expenses incurred on behalf of Jennifer or her estate, for the most part, to Pheasant Lodge. They did so on a pragmatic basis, welcomed by this court, so as to reduce to £2,053,278.96, the amounts to be credited or treated as credited to Jennifer's capital account.

13. However, by the time counsel made their closing submissions, there remained two matters in issue in relation to the treatment of Jennifer's capital account, namely the mortgage payments in respect of Fairoak Grange and some account entries in respect of the children's loan account.

14. I shall first turn to the mortgage payments. Ms Longworth dealt with the mortgage payments at paragraph 3.29 to 3.44 of her report. Having observed that the purchase price for Fairoak Grange was £2,070,960 part funded from a loan of £1,700,000 from Barclays Bank for which Simon assumed responsibility, she noted that, as at 8 May 2015, the bank borrowing had been reduced by some £66,921 to £1,632,568. Since this was funded by the partnership and accounted for in the partners' profit sharing ratio, she concluded that the repayment of capital should be treated as drawings for the benefit of Simon. However, contrary to Julie's submissions, she concluded that since the partnership had utilised the land to generate a profit without being required to pay rent, the interest payments should be treated as a cost of the business and apportioned in the profit sharing ratios.

15. Mr Maynard-Connor does not challenge Ms Longworth's conclusions in relation to the payments of interest and, in my judgment, he was correct not to do so. The interest payments reflect the value of the loan that was acquired to purchase the land at market value. Since the land was introduced to the partnership and, as such, utilised as a partnership asset rent-free, the partners could reasonably be expected to meet payments of interest.

16. However, I am also satisfied that Ms Longworth was correct in her treatment of the repayment of capital. It was always understood that Simon, not Jennifer, would be credited with the value of the land funded from the Barclays Bank loan. He assumed liability on the mortgage and it was expressly provided in clause 15.3 of the Partnership Deed that, as such, his secured borrowing would be deducted from his share, not her share, and when any dissolution account was required, it would not be treated as a partnership liability for the purpose of determining any partner's partnership share on dissolution. This was consistent with clause 15.1.2 which provided that "the Partnership Freeholds [as defined would] insofar as…reflected in their respective partnership shares be credited or appropriated to [the partners] in the proportions in which they own such Partnership Freeholds beneficially and on any dissolution such beneficial interests [would] be appropriated to their respective partnership shares". To the extent Simon suggested otherwise, I do not accept his evidence. It is inherently unlikely that partners had any contrary intention.

17. In these circumstances, there was, and is, no room to treat the capital repayments as a partnership liability for which Jennifer was responsible. In his submissions on behalf of Simon and Alison, Mr Edwards submitted that the treatment of mortgage payments as rent was "the lynchpin" of my reasons for rejecting Simon's submissions that other land was partnership property because it had been funded from the profits of the business. However, this is an overstatement. My conclusion was based simply on the principle that, without more, mortgage payments do not create interests in property under a trust. In the absence of contractual provision or admissible evidence that the payments might somehow have been made with the intention that they would give rise to a trust, they did not operate to do so. In the absence of such evidence, it could easily be inferred that the payments could be treated as rent. The purchase of Fairoak Grange was different since Simon agreed to assume responsibility for the repayment

of the mortgage and the 2012 mortgage deed expressly provided for such repayments to be deducted from his share. As I understand his argument, Mr Edwards submitted that clause 15.3 only applies to the partnership liabilities on dissolution and not to payments made prior to dissolution. However, in my judgment, the preliminary part of clause 15.3 is plainly apt to comprehend payments prior to dissolution and thus applies to the account taken upon dissolution.

18. I shall now turn to the entries in respect of the so-called children's loan account. In the partnership accounts for the year ending on 31 March 2013, an item of £24,000, denoted "children's loan account", was written off under the heading "Long Term Liabilities" from the entries in the previous year's accounts. It appears this was an accumulated amount in respect of intended gifts to the children or grandchildren within the annual IHT gift exemption. In paragraph 3.48 of her report, Ms Longworth made an adjustment writing back the balance to Jennifer and Simon respectively in the sums of £16,500 and £7,500.

19. There is no evidence that Jennifer or Simon ever made such a gift to the children or grandchildren. Indeed, when cross-examined on the issue, Simon confirmed that no money was paid and he had no recollection of a loan. However, in his submissions on Simon's behalf, Mr Edwards submitted that the liability should not have been written off since the burden of proof was on Julie to show that the creditors - presumably Simon's children, Victoria and Ben - ever released Jennifer or Simon from liability under the loans.

20. Notwithstanding the ingenious way in which this part of Simon's case was presented, it is without evidential foundation.

21. Firstly, whilst the accounts are least indicative of an intention to make gifts to the children, there is no evidence that any such gifts were ever made. A unilateral intention to make a gift does not qualify as a gift. No money ever changed hands and there is no evidence that anything was ever done to transfer the gift to the children, whether in the sense envisaged by Turner J in *Milroy v Lord* [1862] EWHC (Ch) 78, or so as to render it unconscionable for Jennifer or Simon to retract and thus engage the principle in *Pennington v Waine* [2002] 1 WLR 2075. If the bare entries in the partnership accounts are consistent only with such an intention - and it is not obvious that they are - this would not suffice for such a purpose.

22. Secondly, there is no evidence that the children ever entered into a contract with Jennifer or Simon to lend the money back. If they ever knew of the intention to make such a loan, there is no evidence that they entered into a contract with Jennifer or Simon in relation to the application of the loan monies, if any. Indeed, it is inherently unlikely that they ever did so. I am thus satisfied that Ms Longworth was correct in her treatment of this part of the accounts.

23. This takes me to the issue between the parties about Jennifer's claim for an account under the provisions of *section 42* of the *Partnership Act 1890*. The heading to *section 42* of the *Partnership Act 1890* is as follows: "Right of outgoing partner in certain cases to share profits made after dissolution". The heading would not have been subject to debate in Parliament; it would have been incorporated for ease of reference only. However, it can be taken into consideration, as part of the overall context, when construing the Act itself.

24. *Section 42(1)* provides:

> "Where any member of a firm has died or otherwise ceased to be a partner, and the surviving or continuing partners carry on the business of the firm with its capital or assets without any final settlement of accounts as between the firm and the outgoing partner or his estate, then, in the absence of any agreement to the contrary, the outgoing partner or his estate is entitled at the option of himself or his representatives to such share of the profits made since the dissolution as the court may find to be attributable to the use of his share of the partnership assets, or to interest at the rate of five percent per annum on the amount of his share of the partnership assets."

Section 42(2) provides as follows:

> "Provided that where by the partnership contract an option is given to surviving or continuing partners to purchase the interest of a deceased or outgoing partner, and that option is duly exercised, the estate of the deceased partner, or the outgoing partner or his estate, as the case may be, is not entitled to any further or other share of profits; but if any partner assuming to act in exercise of the option does not in all material respects comply with the terms thereof, he is liable to account under the foregoing provisions of this section."

25. The Act thus confers a statutory right on the outgoing partner, at her election, to a share of the profits or interest at five percent per annum on the amount of her share of the partnership assets. However, the statutory right only applies in the absence of agreement to the contrary. Moreover, where the partnership contract contains an option to purchase, the outgoing partner is not entitled to any further or other share of the profits if the option is duly exercised unless the partner who exercises the option does not in all material respects comply with the terms of the option itself.

26. At one point in the argument, it was suggested that the statutory proviso in *section 42(2)* only applies if the outgoing partner elects to take a share of the profits as distinct from interest on the amount of her share of the partnership assets. In my judgment, that suggestion is unsound. Whilst it is true that *section 42(2)* refers in terms to the outgoing partner's right to a share of profits only, there can be no statutory right of election if the outgoing partner's right to a share of profits is itself barred by *section 42(2).* Had it been intended otherwise, the *Act* could reasonably have been expected to provide for this in clear and unambiguous terms given that the outgoing partner can have no meaningful election if and once her right to a share of profits has been statutorily excluded. Moreover, there could be no obvious reason to exclude the outgoing partner's share of profits but not her alternative right to interest in the event a contractual option is exercised. No doubt, the process of quantifying the outgoing partner's share of profits would potentially be more complex and time consuming than the calculation of interest but it is difficult to see why this would justify excluding altogether the right to a share of profit but not the right to statutory interest.

27. For the sake of completeness, I was referred to *Paragraph 25-41* of *Lindley & Banks on Partnership (20th edition)* in which the editor takes a different view, albeit on the basis that the statutory right to interest would generally be excluded by necessary implication where a contractual option is exercisable, for example where the Partnership Deed expressly provides for the payment by instalment without interest. However, this view is apparently based on a narrow interpretation of the reference, in *section 42(2),* to "further or other share of profits" and does not take into consideration the full ambit of the statutory mechanism in *section 42(1)* and *(2).*

28. In the present case, the Partnership Deed did originally provide for the payment by instalment, subject to specific provision for interest. Of course, the contractual scheme was modified when I gave judgment but, regardless of whether a contrary agreement can be discerned, I am satisfied that the proviso in *section 42(2)* is applicable to a statutory claim for interest where there is a contractual option.

29. In the present case, the option in the Partnership Deed was exercisable within six months of the Determining Event, itself defined so as to include the expiry of a written notice of dissolution. The option, in clause 17, provided for the purchase of the interest of the Outgoing Partner in the profits, capital and assets of the partnership immediately prior to the Determining Event at a price calculable under clause 19.

30. By clause 18, it was provided that "when exercising the option…the option holder or holders shall indicate whether or not he or they wish to pay the price referred to in clause 19 by instalments. If such an indication is given at the time the option holder shall be entitled to pay for the interest of the Outgoing Partner by five equal instalments, the first instalment to be paid one year from the date of dissolution with interest on the outstanding balance from time to time or a late payment of an instalment at the base lending rate from time to time of Barclays Bank Plc".

31. By clause 19, it was provided that "the price payable under clauses 17 and 18 above shall be the amount standing to the credit of the Outgoing Partner on the date of the Determining Event after there shall have been a revaluation at that date of the partnership's then assets."

32. In the present case, the dissolution notice operated to dissolve the partnership on 8 May 2015. Simon and Alison then exercised their option to purchase Jennifer's share in the partnership by notice dated 26 October 2015. At this stage, they entered into a binding contract for the purchase of Jennifer's interest in the profits, capital and assets of the partnership. This can be seen from my judgment at [143]. To the extent necessary, the court would provide by implication the machinery necessary to give effect to the parties' contractual obligations, *Sudbrook v Eggleton* [1983] 1 AC 444. Once the price payable under clause 19 has been determined, a term would no doubt be implied for completion to take place within a reasonable period of time.

33. In the exercise of my equitable jurisdiction, I made an order setting aside the contract under Simon and Alison's notice dated 26 October 2015 and extending time for the service of another option notice under the Partnership Deed.

34. On behalf of Simon and Alison, Mr Edwards submits that, in the event his clients duly exercise the extended option, Julie will be precluded from claiming an account of interest under the provisions of the statutory proviso in *section 42(2).* He also submits

that she is precluded from claiming an account because the option provisions in the partnership agreement amount to an agreement to the contrary for the purpose of *section 42(1),* at least in a case where the option is exercised.

35. Notwithstanding the skill with which Mr Edwards' submissions on this issue were presented, I am satisfied that Julie is entitled to a statutory account of interest. When I gave judgment, I did not disallow Julie's right to a statutory account of profits or interest under *section 42* in the exercise of my equitable jurisdiction. Mr Edwards is thus driven to rely on the statutory limitations in *section 42* itself.

36. I shall deal with Mr Edwards' submissions in relation to the effect of *section 42(2)* first. The short answer to this part of his case is that, once I set aside the contract under Simon and Alison's initial contractual option notice and extended time for them to serve a new notice, their rights to serve such a notice were based on the judicial award itself rather than a partnership contract. The judicial remedy was awarded under the doctrine of proprietary estoppel. It was based on principles separate and distinct from the law of contract. (See *Thorner v Major* [2009] UKHL 18 approving at paragraphs 56 to 57 and 101 the observations of Hoffmann J in *Walton v Walton* [1994] CA Transcript No 479).

37. Mr Edwards did not submit that Julie is precluded from relying on her statutory right to an account by virtue of the service of the initial contractual option notice. No doubt, any such argument would be founded on the proposition that, through the service of the initial contractual option notice, the contractual option in clause 17.3 was "duly exercised" so as to engage the proviso in *section 42(2).* However, in my judgment *section 42(2)* is apt to comprehend only an extant contract under the option notice. In the present case, this has been set aside. Moreover, the statutory proviso is subject to the qualification or condition that "if any partner assuming to act in exercise of the option does not in all material respects comply with the terms [of the option], he is liable to account…" Had this been a live issue, it is difficult to see how, following their unexplained delay - upwards of five years prior to trial - in taking any meaningful steps to complete the option, Simon and Alison could be shown to have complied with it in all material respects.

38. Mr Edwards' submissions in relation to *section 42(1)* are based on the proposition that the contractual provisions of the Partnership Deed, including the option mechanism, amount or are capable of amounting to an agreement contrary to the statutory right to an account. He submits that, if the option is exercised and the transaction proceeds to completion, the amount payable is the amount fixed by contract only. Whilst the new option has been awarded by estoppel, Mr Edwards submits that it is based on the option provisions in the Partnership Deed itself. In the event the new option is exercised, it will thus be governed by the provisions of the Partnership Deed and qualifies as "agreement to the contrary" within the meaning of *section 42(1).* These submissions are certainly susceptible of argument and they were skilfully developed before me. However, I was not persuaded. In substance, the material option rights are now a function of the judicial remedy, based on proprietary estoppel, together with the court order of 26 April 2022. Subject to my judgment, the Partnership Deed continues to apply to the parties' post dissolution rights. This includes the option provisions. However, there is nothing in the Partnership Deed itself to contradict the statutory right to an account in the event Simon and Alison exercise the rights accorded to them by my judgment under the law of proprietary estoppel.

39. I have thus reached the conclusion that Julie is entitled to statutory interest under *Section 42(1).* However, in my judgment, her right to statutory interest is limited to the share of partnership assets from which, or in respect of which, Simon and Alison have carried on the business. Following the service of the dissolution notice, Jennifer remained in possession and occupation of Pheasant Lodge and, once she ceased to reside there, it remained in her possession or is to be treated as such until her death. On this basis, I am satisfied that the value of Jennifer's interest in Pheasant Lodge should be taken out of account at least until the date of her death.

40. Mr Edwards has not yet intimated on behalf of his clients any claim to remuneration for services. He may wish to take instructions on whether or not they wish to make such a claim. The foundations for such a claim are set out in *Lindley (supra)* at *paragraph 24-35*. I appreciate that, following the hearing, counsel will wish to take instructions and discuss between them the price payable in the event that the option is exercised. This can be embodied in a court order. The option will then be exercisable for a period of three months from the date of the order. In all likelihood, the order will be drawn up tomorrow, 30 September, and take effect from that date. Unfortunately, in the absence of agreement to the contrary, it will thus be timed to expire on Friday 30 December during the Christmas vacation. Counsel may wish to reflect on whether they wish to modify the date.

41. Everyone will be aware of the dramatic market movement this week in relation to interest rates. Simon and Alison will thus wish to reflect carefully on whether to exercise the option. Regardless of whether they do so, Julie will be entitled to statutory interest under *section 42*. I do not currently envisage making an order requiring them to make a payment until asked to do so. If they decide not to exercise the option, it is likely that the properties will have to be sold and the monies to which Julie is entitled can be taken out of the proceeds of sale. In any event, the net proceeds will at least *prima facie* be applied in the statutory order set out in *section 44* of the *Partnership Act*.

42. I was asked to give guidance as to how the properties should be marketed and disposed of. As I mentioned before, I would envisage the parties will jointly instruct an estate agent or estate agents with local knowledge and agricultural expertise to advise on the best way forward with a view to maximising the sale price that can be achieved. It is conceivable he or she will recommend that the properties are divided into separate parcels or lots and marketed for sale on that basis.

43. Mr Edwards indicated during his submissions that his clients would prefer an *in specie* distribution in anticipation that at least one farmhouse could be disposed of to his clients. With that in mind, he referred me to clause 8.2 of the Partnership Deed which provides for the net profits and losses of a capital nature arising in respect of the partnership freeholds, including Reddish Hall Farmhouse, to be divided between the partners in the proportions they own the partnership freeholds in question beneficially.

44. Since Simon owned Reddish Hall Farmhouse when the parties entered into partnership, he will be entitled to the capital profits from this part of the estate. As I mentioned in argument, this may have been intended to accommodate the issue identified by the editor of *Lindley* at *Paragraph 17-04* in relation to capital assets entered at their written down book value when introduced to partnership. However,

Reddish Hall Farmhouse is a partnership asset and will be treated as such when the properties are marketed, notwithstanding that the value or enhanced value is likely to be credited to Simon.

45. It will thus be for the estate agent to give professional advice on how it is best dealt with. He may decide to market it in separate lots, in which case the parties will be at liberty to submit an offer or bid. Alternatively, they may wish to make an offer or bid for one or other of the farms but that all depends on the guidance that the valuer estate agent gives.

(Hearing continues)

(This Judgment has been approved by the Judge.)