



**THE SOCIAL SECURITY COMMISSIONERS**

Commissioner's Case no: CIS/5481/1997

SOCIAL SECURITY ACTS 1992 - 1998

**APPEAL FROM A DECISION OF A SOCIAL SECURITY APPEAL  
TRIBUNAL**

**ON A QUESTION OF LAW**

**DECISION OF THE SOCIAL SECURITY  
COMMISSIONER**

*Mr Commissioner David Williams*

Claimant:

Benefit: income support

Tribunal:

Tribunal case ref:

Tribunal hearing:

## DECISION OF THE SOCIAL SECURITY COMMISSIONER

1 I allow the claimant's appeal against the majority decision of the Sheffield social security appeal tribunal, brought by leave of the chairman. The decision of the tribunal was that the claimant is not entitled to income support from 9.8.96. For the reasons given below, the decision was erroneous in law. I therefore set it aside. I refer the case to a freshly constituted tribunal to determine the appeal in accordance with this decision.

2 While it is for the President of the Appeal Service (or the chairman to whom responsibility is delegated) to decide, in my view it will be of considerable assistance if the new tribunal were constituted with a financially qualified panel member under regulation 36(3) of the Social Security and Child Support (Decisions and Appeals) Regulations 1999. Income support is a "relevant benefit" for the purposes of that provision: section 8(3) of the 1998 Act.

3 The President may appoint a financially qualified panel member if, in his opinion, the appeal;

"may require consideration .... of issues which are, in the opinion of the President, difficult and which relate to ...profit and loss accounts, revenue accounts or balance sheets relating to any enterprise".

While the specific issue on which this appeal is decided is that of the nature of the assets of a partnership being dissolved, the case must on full hearing also relate to the profit and loss accounts and balance sheet of that partnership in order to determine the financial effects of the points considered in this decision. This is because, as an income support case about the means of a self-employed person, it involves issues about the income and capital of the claimant. For the reason set out in particular at paragraphs 14 and 15, this may require a view to be taken of accounting practice. If so, such an issue will be difficult for a non-expert as it would require expert evidence for proper decision. That is why I refer the case to a tribunal rather than deciding it myself. It is one of the kinds of case where the expertise of a financially qualified panel member should prove to be of considerable assistance in future appeals because it will enable a tribunal to take an expert decision.

### *The tribunal decision under appeal*

4 The reason why the majority of tribunal refused income support to the claimant was that his capital was over £8,000. This was because it took the view that the claimant's capital included the proceeds of sale of his share of assets of a partnership business. The dissenting member disagreed, taking the view that the proceeds of sale should be left out of account as business assets under Schedule 10 paragraph 6 to the Income Support (General) Regulations 1987.

5 Both parties agreed that the decision of the majority of the tribunal should be set aside as wrong in law, but they did not agree why. As I indicated in a direction on 14 June 1999, I agree with their conclusions, although not with all their reasons. One reason for setting aside the decision is that the tribunal failed to determine the terms of the partnership deed of which the claimant was a party. Until the matter came before the tribunal, both the claimant and the Department staff had talked in terms of a "company". The tribunal found that the business was a partnership but failed to establish the terms on which the partnership was run. The first explicit mention of a partnership deed was in the grounds of appeal. But if a deed existed, then its terms would be central to the claimant's argument. As a result, regrettably, this is yet another case where central questions in the appeal may depend on the interpretation and application of key documents that do not form part of the appeal papers. If there was a deed, the tribunal should have seen it. This is because without the deed, or without establishing that there was no deed, the tribunal was unable to determine some of the questions before it. In attempting to do so, it erred in law, and the decision must be set aside.

#### *Importance of the partnership deed*

6 In the first submission to the Commissioner, the adjudication officer referred to the belated production of a copy of what was said to be part of the partnership deed as "evidence". The officer argued that as the "evidence" was not produced to the tribunal, it could not be said to have erred in not considering it. Instead, there could be a review for mistake as to a material fact. That approach is fundamentally wrong. A partnership is governed by the terms of the partnership deed or agreement together with the terms of the Partnership Act 1890. For most purposes, the terms of the deed or agreement prevail over the terms of the Act: *Moss v Elphick* [1910] 1 KB 846. The validity and operation of a deed necessarily involves questions of law. An error about the terms of the deed is therefore an error of law. Producing the deed is not a matter of producing new evidence. It is a matter of producing the necessary legal documents to decide the case. Because of the status of a deed of partnership in determining questions such as those in this case, the deed is, so far as relevant, "the law". It follows that an officer or tribunal that tries to take decisions about the application of deeds or contracts, such as this deed of partnership, without seeing the proper documents will probably be wrong in law in any decision taken. Interpretation of a deed or written contract is always a question of law.

7 But there is a further problem here. I asked the claimant to produce a copy of the deed. What he produced is an unsigned and unexecuted draft. As a result, I am not sure there was a deed, thought the unexecuted deed might represent the terms of a contract. If there is a deed, it is the original deed, or at least a properly certified copy of the original, duly signed and executed by the parties, that must be produced. The current document is not a proper copy of a deed. The tribunal, however, did not consider this because it did not consider the terms of the partnership.

### *Partnership or company?*

8 The analysis of the issue in this case is also not helped by a confusion about whether the business was a partnership or a company. It was a partnership. Discussion about “the assets of the company” is a completely wrong view of English partnership law. Unlike a company, a partnership has no separate legal personality in English (and Welsh) law: *Income Tax Commissioners v Gibbs [1942] AC 402*. (I emphasise, as did the House of Lords in that case, that the Scottish law of partnership is different. No part of this decision should be taken as referring to the position in Scotland.) At any one time the assets and liabilities of the partnership are, subject to the partnership deed or agreement and the Partnership Act 1980, the joint and several assets and liabilities of the partners.

9 While there is no doubt that there was a partnership, there is a further uncertainty over who the partners of the partnership are. The draft deed identifies the claimant, but not his wife, as partner, but there are several other references, including a references in a letter from the accountants, to four partners. There is a finding of fact by the tribunal that the wife is also a partner, but its basis is not clear. The new tribunal will need to sort that question out. Some additional information about the partnership is now in the case papers, but more may be needed.

### *The questions in issue*

10 The tribunal found that the claimant, his wife, and two others ran a partnership (SC). It ceased trading on 31 July 1996 because of debts. The claimant, with honesty, admitted that it was to avoid bankruptcy. The claimant claimed income support with effect from 2 August 1996. Both the claimant and his wife had been working in SC, but drawing very little money. The partners sold “the business” of SC to a third party, for a sum received in instalments. I call it “the business” because there is no consistent description in the papers of exactly what was sold, and the adjudication officer is reported as deciding that the business was sold (adjudication officer’s submission, paragraph 5.6). It cannot have been “the business” that was sold because the purchaser did not become a partner in, or sole trader of SC. There may have been a written document setting out what was sold and on what terms. If it is relevant, the new tribunal should ensure it has any such document before it. Part of the proceeds of sale of “the business” had been received on 2 August 1996. The adjudication officer took the view on 8 August 1996 that the total assets of the claimant and his wife included their shares of the proceeds of sale and were in excess of £8,000. The calculation was redone on 28 August 1996, and the same conclusion was reached. Income support was paid for the few days before 8 August 1996, but not after.

11 The appeal raises the following linked questions about the assets of SC at and after the time it ceased trading:

11.1 Were there any assets of the partnership when it ceased trading? This is a question of fact, depending in part on the profit and loss accounts and balance sheet of the partnership, which I leave for the new tribunal to consider. For present purposes, I assume that there are such assets.

11.2 What rights did the claimant and his wife have over those assets after trade had ceased but before there was a distribution to the partners on or after dissolution? That is a matter of law, which I note below, and which is relevant to the third question.

11.3 Were those rights to be counted as "capital" of the claimant and his wife for income support purposes, or were they exempted as business assets under paragraph 6 of Schedule 10, or otherwise? If they were to be exempted, for how long should that exemption apply? That is considered below.

11.4 If the rights were to be taken into account, what was the value of those rights at any time relevant to this claim? That again is a question of fact, which I also leave to the new tribunal.

*Schedule 10, paragraph 6: business assets*

12 Regulation 46(1) of the Income Support (General) Regulations 1987 provides that the capital of a claimant shall be the whole of his capital. Regulation 46(2) provides that any capital specified in Schedule 10 shall be disregarded under regulation 46(1). Schedule 10 paragraph 6(1) provides:

"The assets of any business owned in whole or in part by the claimant and for the purposes of which he is engaged as a self-employed earner or, if he has ceased to be so engaged, for such period as may be reasonable in the circumstances to allow for the disposal of any such asset."

There is an identically worded exemption in Schedule 8, paragraph 11(1) to the Jobseeker's Allowance Regulations 1996 and in Schedule 3 paragraph 6 to the Family Credit (General) Regulations 1987.

13 The structure of the relevant provisions in the Income Support (General) Regulations 1987 adopts a distinction between business income and business capital. It defines the relationship in part in regulation 38. This has specific but rather unsystematic provisions about capital expenditure, capital, capital assets, business assets, existing assets, and specific kinds of assets. None of these terms are defined, and there are no relevant provisions in the exclusions from earnings listed in Schedule 8. The wording of regulation 38 uses what I might

term income tax language and concepts in a number of places. The general approach taken is similar to that for income tax. This distinguishes between income and capital receipts. If the asset sold generates an income receipt, then the income should go to the profit and loss account. Only if the receipt of proceeds of sale relate to the sale of a capital asset does Schedule 10 paragraph 6 apply.

### *Income or capital?*

14 The distinction between income and capital in an individual case is a question of fact. The key principle was recently restated by Lord Nolan, giving the decision of the Privy Council in *CIR v Wattie* [1998] Simon's Tax Cases 1167:

It is well settled that in considering whether a particular item of receipt or expenditure is of a capital or revenue nature the approach to be adopted should be that described by Dixon J in *Hallstroms Pty Ltd v Federal Comr of Taxation* (1946) 72 CLR 634 at 648, where he said that the answer to the question -

“depends on what the expenditure is calculated to effect from a practical and business point of view rather than upon the juristic classification of the legal rights, if any, secured, employed, or exhausted in the process.”

That approach was adopted by their Lordships' Board in *BP Australia Ltd v Comr of Taxation of the Commonwealth of Australia* [1966] AC 224 and has been followed in many other cases of high authority ... it is familiar law that within the context of the same business, similar principles will apply to payments and to receipts. This appears from the general discussion of the earlier cases by Lord Macmillan in *Van Den Burghs Ltd v Clark (Inspector of Taxes)* [1935] AC 431 at 438 - 441...

15 The approach of the courts to this issue is to look to the accounting evidence. In *Gallagher v Jones* [1993] Simons Tax Cases 537 at 555, the Master of the Rolls, after an extensive review of the caselaw, summarised the approach to be taken as:

Subject to any express or implied statutory rule, of which there is none here, the ordinary way to ascertain the profits or losses of a business is to apply accepted principles of commercial accountancy. That is the very purpose for which such principles are formulated. As has often been pointed out, such principles are not static: they may be modified, refined and elaborated over time as circumstances change and accounting insights sharpen. But so long as such principles remain current and generally accepted they provide the surest answer to the question which the legislation requires to be answered.

The judgment of Sir Thomas Bingham was agreed to by Nolan LJ (as he then was). Concurring, Sir Christopher Slade emphasised:

In conclusion, I would stress that the reason why the courts rightly attach so much importance to accepted principles of commercial accounting in this context is, of course, that these principles will normally afford the surest means of ascertaining the *true* profits or losses of a trader, as the case may be.

The approach shows why the introduction of financially qualified panel members to tribunals should prove of significant value in cases such as this.

16 In this case it is a question of fact whether the sale of “the business” should be regarded as partly relevant to earnings or as wholly relevant to the capital base of a business. I say that because no attempt has so far been made properly to identify the assets. Under partnership law, the general rule is that assets must be sold on dissolution: *Featherstonhaugh v Fenwick* (1810) 17 Ves 298. Where goodwill exists, it must be sold as any other asset: *Hill v Fearis* [1905] 1 Ch 466. It is clear from this approach that “asset” effectively means anything which can be sold. That is not the same distinction as the distinction, relevant here, between sales of assets that give rise to earnings and sales that give rise to capital receipts. So far, it has been assumed that all the assets were capital. But if what was sold was in effect all the assets of an on-going business, with its name, customer contacts and contracts, knowhow and goodwill, then it may be that some of the “assets” sold were not capital assets but stock in trade, work in hand, or other revenue items relevant to earnings. That is another question of fact that the new tribunal must consider.

*To which assets does paragraph 6 apply?*

17 Schedule 10, paragraph 6, applies only to the capital assets “of any business owned... by the claimant”. This language presents a second difficulty because it introduces the concept that the assets belong to the business, and the business belongs to the claimant. That fits well with an incorporated business but, at least in England and Wales, does not describe the position of a partner. This is because, unless other arrangements are made, the assets belong directly to the partners along with all their other assets. Further, all the assets (in the widest sense of everything salable) of an active partner are at risk if a partnership business fails, not just the assets of the “business”. In the widest sense therefore, all the assets of a partner actively involved in a business could be regarded as business assets, including his home. That was rejected as an approach by the Commissioner in R(SB) 4/85, and I also reject it here.

18 The tribunal found that the sale of assets was a sale of fixed assets. That term appears to have come from the claimant, but it is not clear what this was describing, as there was no further detail of the assets or of how SC’s accountant viewed the sale. The tribunal then considered whether the proceeds of sale of those assets were within paragraph 6. The conclusion of the majority was:

“the majority of the tribunal do not consider that the balance in the bank account as at the date of claim to income support does fall within paragraph 6. In our view

paragraph 6 was written to allow for fixed assets of a business to be disposed of and to allow the claimant reasonable time to do this. We consider that such items as fixed plant and machinery would come within paragraph 6, because a claimant would need a reasonable time to sell these items and a disregard would be appropriate under this paragraph.”

The minority view was that:

“... paragraph 6 applied in this case and that the monies in the bank account could be said to be an asset of the previous partnership and it was reasonable to allow a reasonable period for debts to be paid, etc which would constitute the disposal of the monies in the account.”

19 The claimant's view on appeal is that the majority is wrong and that: “routinely business assets must always include financial assets until such time as all creditors have been paid off. The accounts of any company show assets as plant, machinery, stock and any moneys held in the bank” (document 60). This and other comments of the claimant refer to “the company” which, as I have noted, is both wrong in law and somewhat confusing when considering partnership assets. But the claimant also relies on standard accounting practice, which must be taken into account for the reasons I have also noted. The adjudication officer argued for the view of the majority:

“It is my submission that from the date of the sale of the assets, the disregard in paragraph 6 of Schedule 10 could not have had any application as the assets had already been disposed of. That disregard cannot apply to the proceeds of sale of the assets of a business, only to the assets themselves.” (Document 64).

The officer further argues that the proceeds of sale are capital of the claimant from receipt, and that liabilities cannot be deducted from them.

20 I consider that the minority view of the meaning of “assets” is the view which most accords with both the legislation and the business context in which it must operate. The exclusion in paragraph 6 applies to all capital assets of the business of whatever nature. What is capital must be decided on standard accounting principles. The proceeds of sale are as much “assets” of the business as the previous assets sold. The test whether those proceeds are capital is one of fact: if the assets sold were capital, then so are the proceeds of sale. The majority is wrong in confining paragraph 6 to fixed plant and machinery and similar assets (or, indeed, unfixed plant and machinery such as a van). There is no basis for such a restriction in the undefined terms of paragraph 6, or in the context of those terms in the Income Support (General) Regulations 1987.

#### *A reasonable period for disposal*

21 The effect of the conclusion in paragraph 20 on the period allowed for disposal becomes clearer if we ignore for the moment the existence of the partnership. If a single trader ceases business, paragraph 6 allows a reasonable time to dispose of the assets. It must first be decided when the duty to dispose starts. Once that is decided, what is reasonable must be decided, if necessary from time to time, as assets are realised. If those assets include, for example, a

freehold interest in a property for which there is little market interest, it may take some time to dispose of it. A freehold interest is typically disposed of by a contract in exchange for the contractual right to receive the sale price on completion. If the period between contract and completion is reasonable, then those contractual rights will be protected under paragraph 6 from being taken into account until completion. On completion, the cash in the bank becomes the business assets. It must now be considered what is a reasonable time to dispose of the cash assets. This is also a question of fact, but it may be that a tribunal decides that there is no need for any delay at all, and that it is reasonable to assume that the individual can dispose of the cash in the bank to himself or herself immediately on receipt.

22 Applying that approach to this case, SC sold "the business" to a purchaser in exchange for an immediate sum of money and a later instalment. The assets of the business after that sale were the cash together with the right to receive further cash at a later date. It has first to be considered whether, on accepted accounting practice, the assets were income or capital or some of both. Only the capital assets are relevant for present purposes. Next, it must be decided from what time the duty to dispose of the capital assets arises. It has then to be considered, both for the cash attributable to the capital assets and the right to receive the later sum, what was the reasonable time for the disposal of those assets. It may be that it was reasonable to wait for the second instalment to be paid before reconsidering whether it should be disposed of (and that seems to be the implicit assumption in this case). It is also necessary to consider the reasonableness of disposing of the cash proceeds of sale from the partnership to the partners.

*When does the duty to dispose of the assets start?*

23 There appears to be a further confusion in this case about when the partnership stopped trading, and when it was dissolved. The partnership did not cease to exist when it stopped trading. It ceased to exist when it was dissolved. Even then section 38 maintains certain rights and obligations until the affairs of the partnership are wound up. Those events may have all been at the same time, but that is also a question to be determined. For the purposes of paragraph 6 of Schedule 10, if the events are separated, the assets of SC remained business assets after SC stopped trading at least until it is dissolved. But paragraph 6 does not take that into account expressly.

24 Instead of operating until the business is dissolved, paragraph 6 applies two other time limits sequentially. First, the assets remain excluded while the claimant remains "engaged as a self-employed earner". That may of course be at the same time as the partnership stops trading, or it may be when the partnership is dissolved, or it may be some other time. It is a question of fact (unless it is determined by court order, deed or contract). The second time limit starts when the claimant "has ceased to be so engaged" and lasts for "such period as may be

reasonable in the circumstances.” That is also a question of fact. These questions are also for the new tribunal. If the questions whether the claimant has ceased to be involved in the partnership proves one of difficulty, the tribunal should consider the decision of the Court of Appeal in *Knight v Chief Adjudication Officer* (1997, to be reported as R(IS) 14/98). In that case the Court emphasised that for a partner to be within this provision there had to be involvement in the business in some practical sense, but indicated that the involvement need not be substantial.

### *Realising the assets of a partnership*

25 When a partnership is dissolved, the position with regard to the partnership assets is defined first by the partnership deed or agreement and then by the Partnership Act 1890. The partners - and least of all a partner acting individually - cannot just “take the cash and run”. They must dissolve the partnership. The terms on which they dissolve that partnership, and their rights to receive the resulting assets, depends first on the terms of the partnership deed, if there is one, and in the absence of such a deed or agreement on the terms of the Partnership Act 1890. If the Act applies, then consideration must be given in particular to sections 39 and the following sections of the Act. Note must also be made of the provision in section 38 allowing the rights of all partners to continue after the dissolution of the partnership for certain purposes. Those rights and obligations are relevant in this case in deciding on the reasonableness of the time taken to dispose of an asset. It is clearly not reasonable to expect one of the partners to dispose of an asset such as proceeds of sale if the other partners could demand its later return to satisfy creditors. It is also to be remembered that in the event of a dispute about winding up a partnership, it is for the court to decide the matter.

26 In assessing a reasonable time for disposal of the assets, the tribunal must take account of the need to deal with the obligations on the partners in dissolving the partnership and winding up its affairs. This will depend in part on the obligations imposed on the partners in dissolving the partnership in accordance with the deed and the 1980 Act. In the last resort, it may depend on a court order. In my view, paragraph 6 is couched in the most general terms. It deliberately creates a discretion in a set of rules where such approaches are usually avoided. That discretion can be used by the tribunal in this case to reach its own best judgment on how to deal with a complicated situation. There is bound to be a period while creditors and debtors are determined. But in some cases partners may take a long time winding up the partnership because their conduct is unreasonable to each other, or perhaps because accountants have taken an excessive time sorting the position out. Alternatively, they may be acting reasonably (if slowly) and the delay may be the fault of third parties who are themselves taking a considerable time, or a court order may prove unavoidable because of a legal difficulty. These are all factors that the new tribunal must consider in reaching its decision as to what is a reasonable time for

disposing of capital assets. It may also be that what is a "reasonable" time is something that changes if circumstances change. It is only after the reasonable time has expired that accounts can be taken of the claimant's share of any remaining assets of the business under regulation 46 without regard to the exemption.

*Directions for rehearing*

27 I therefore allow the appeal and direct the new tribunal to reconsider the appeal. It will be for the new tribunal to decide for itself on the facts how, and for how long, to apply the exemption for business assets.

28 The claimant should produce the original or a proper copy of the partnership deed and, if there is one, the original or a copy of the agreement for the sale of "the business", to the Secretary of State and the new tribunal.

29 The Secretary of State should prepare a new submission to the tribunal to take account of the partnership deed (if there is one) and the evidence offered by the claimant during this appeal. It will be of assistance to the tribunal if the Secretary of State can also indicate for how long this claim for income support stands, and whether any other questions require determination in deciding on any entitlement to income support during the relevant period.

David Williams  
Commissioner

24 November 1999

CIRCULATION NOTE

(Hogg)

*Income support - capital - exclusion of business assets - Income Support (General) Regulations 1987 Schedule 10 paragraph 6.*

In this case I suggest that the tribunal to which I refer the case for rehearing should include a financially qualified panel member. I comment more generally on the value of such members in appropriate cases, and emphasise that questions of the division of "income" and "capital" for IS and similar purposes are matters of fact to be decided on accounting practice (see paragraph 14).

The decision deals with what assets count as "business assets" to be excluded from capital under Schedule 10 paragraph 6 for IS (and similarly jobseeker's allowance and FC/WFTC) purposes. I disagree with the majority of the tribunal and adjudication officer in holding that the proceeds of sale of a business asset are also assets of the business. But I also disagree with the claimant's view that all his assets and their proceeds, in a broad business sense, should be excluded under paragraph 6. This is because some "assets" in the business sense of the term are income assets not capital assets, and proceeds of sale should therefore go to the profit and loss account and not be regarded as capital. I agree with R(SB) 4/85 that "business assets" does not include private assets even though they may be at risk if a business fails.

Aside from identifying the assets, the time when the duty to dispose of them arises must also be determined. I also caution the new tribunal that in considering what is a reasonable time for disposal under paragraph 6 it must take account of the obligations on partners to sort out the partnership debts before distributing the assets. Further, as the assets change so the reasonableness of realising them must be reconsidered. And it may be that what is reasonable for any asset needs to be reconsidered if circumstances change.

I also comment on the importance in cases such as this of producing the original deeds or documents, and not just guessing about their contents. That is the ground on which I overturn the tribunal decision.

DW

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