[2022] EWHC 1967 (Ch)

IN THE HIGH COURT OF JUSTICE **Claim No. BL-2018-001656**
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
BUSINESS LIST (ChD)
B E T W E E N :

Date: 28 July 2022

Before :

James Pickering QC
(sitting as a Deputy High Court Judge)

- -

Between :

PETER JOHN TRIBE	**Claimant**
and	
ELBORNE MITCHELL LLP	**Defendant**

- -
- -

James Mather (instructed by **CM Murray LLP)** for the **Claimant**
George Bompas QC and Sarah Harman (instructed by **Elborne Mitchell LLP)** for the **Defendant**

Hearing date: 29, 30 March 2022

- -

APPROVED JUDGMENT

James Pickering QC (sitting as a Deputy High Court Judge):

PART I: INTRODUCTION

1. The Claimant, Peter Tribe, is a retired solicitor. The Defendant, Elborne Mitchell LLP, is a boutique city law firm ("**the LLP**"). For over 25 years, Mr Tribe practised from the LLP and its predecessor business.

2. In 2016, Mr Tribe retired from the LLP in acrimonious circumstances. In 2018, Mr Tribe issued a claim against the LLP seeking payment of sums said to be due to him from the LLP. Two elements of the claim have already been determined – one in Mr Tribe's favour, the other in the LLP's favour. It is the trial of the third and final element of the claim – which effectively seeks the determination of a single issue relating to the relevant partners' accounts for a particular year – which is the matter now before me.

PART II: THE BACKGROUND TO THE DISPUTE

Mr Tribe

3. Mr Tribe qualified as a solicitor in 1987. In 1990, he became a salaried partner in the unincorporated partnership of Elborne Mitchell – in other words, the immediate predecessor to the defendant LLP. In 1997, Mr Tribe became an equity partner.

The LLP

4. On 25 November 2010, the LLP was incorporated as a limited liability partnership. All five equity partners within the old unincorporated partnership (including Mr Tribe) became members of the new LLP.

5. On 1 September 2011, the business of the old unincorporated partnership was transferred to the new LLP. Also on that date, the above five members (including Mr Tribe) entered into a Members' Agreement ("**the Members' Agreement**") in order to regulate the terms on which the LLP was to be organised and carry on its business.

6. The Members' Agreement contained all the usual terms including various provisions relating to accounting. In particular, clause 10 provided for the preparation of two distinct forms of accounts as follows:

(1) By clause 10.4, the LLP was to prepare **Statutory Accounts** as at the last day of each financial accounting period. "Statutory Accounts" were elsewhere defined as "the accounts of the LLP for any financial accounting period prepared in accordance with the requirements of the Companies Act".

(2) By clause 10.10, it was provided that "in addition to the Statutory Accounts" the equity partners "shall cause **Partners' Accounts** to be prepared" in respect of each financial accounting period. "Partners' Accounts" were elsewhere defined as "the accounts of the LLP prepared from time to time for the information of the Partners including… but not limited to a profit and loss account showing details of Distributable Profits, capital accounts, current accounts and tax reserves." "Distributable Profits" were elsewhere defined as:

> "…such revenue or capital profits of the LLP as are shown in the Partners' Accounts and which are to be shared between the Partners in respect of any financial accounting period and which may be the same or more or less than the revenue or capital profits of the LLP as set out in the Statutory Accounts…"

Fixed Share Partner "F"

7. On 2 September 2013, the LLP took on a fixed share partner (referred to throughout these proceedings simply as "F") under the terms of a "Fixed Share Partner – Members' Agreement" ("**the FSP Agreement**").

8. Under clause 4 of the FSP Agreement, F was entitled to a proportion of any fees billed and collected by the LLP from work introduced by him. Under clause 5.1, he was entitled (subject to review) to a monthly draw of £4,000 which "shall be a loan against fixed share profit"; while clause 5.2 provided that "If your account is overdrawn, you shall refund the amount overdrawn immediately or as the Senior Partner may decide".

9. In short, therefore, the monthly draw was only a payment on account such that, in the event of his profit share under clause 4 being less than the amount drawn under clause 5, he would be liable to repay any outstanding balance on demand.

10. Unfortunately, F's practice was not a success. By way of example, by June 2015, his total profit share entitlement under clause 4 had reached little more than £12,000. Over the same period, however, under clause 5 he had drawn just under £105,000. As a result, by the above date F owed the LLP just over £93,000 and rising.

<u>Mr Tribe's resignation from the LLP</u>

11. In October 2015, Mr Tribe gave notice of retirement from the LLP. Pursuant to clause 20 of the Members' Agreement, this was to take effect from 30 April 2016.

<u>Discussions regarding F</u>

12. In January 2016, there were discussions amongst some of the equity partners regarding the position of F. On 14 January 2016, Mr Tribe emailed saying that he would like the partners "to have a chat" about F before his retirement took effect in April. He further stated that "the yearly cost to the partnership has been considerable" and that "whilst there has been renewed hope that the [redacted] claim now has secured funding and sufficient merit, we do need to know where this is all going". On the same day, the senior equity partner, Tim Brentnall, replied saying that he agreed and that he did not feel that the future was "rosy" with F.

13. Some two weeks later on 28 January 2016, Mr Brentnall sent a further email to the equity partners asking for views as to the way forward with F. The options, according to Mr Brentnall, ranged:

> "…from asking for his net lent drawings back (he won't be able to pay) to reducing the same going forward or simply not paying anything going forward (although I suspect that won't work either)."

14. On 23 February 2016, emails were exchanged between Mr Brentnall and F with a view to arranging a lunch to discuss the way forward. In a private email exchange of the same day, Mr Brentnall also emailed fellow equity partner, Tim Goodger, asking if he could attend the lunch in his place stating:

> "We've got to structure something sensible. I don't think we're looking for a complete break-off in relations…"

15. On the following day, 24 February 2016, a further exchange took place between Mr Brentnall and Mr Goodger in which consideration was being given as whether there should be a variation of the basis on which F was receiving drawings. In particular, Mr Brentnall stated:

> "…in the current year I have suggested we simply give him the £4k a month, but then he will have to scrabble around in May and start paying some tax on that… Where we go after May I'm not sure.
>
> The best solution would be if [F] could find one or two paying clients and actually earn some money!!"

16. On 28 April 2016, it came to Mr Brentnall's attention that another of F's matters with just under £50,000 of work in progress would have to be written off. Later that day, he emailed F stating that this was "disappointing" before adding:

> "I'm afraid I think the time has come to re-evaluate what is a feasible monthly draw in light of the fact that, as you know, the deficit on your current account is already very substantial. Let's schedule another coffee soon."

17. Later that same day, Mr Brentnall emailed the LLP's Director of Finance, Andrew Greenleaf, asking him to suspend F's drawings for May "and any further drawings until further notice."

30 April 2016

18. On 30 April 2016, the LLP's financial accounting year (as defined in the Members' Agreement) came to an end.

19. It was also, of course, the date on which Mr Tribe's retirement from the LLP took effect. This being the case, it was also on this date that clause 23 of the Members' Agreement took effect which provided that when an equity partner ceased to be a member of the LLP, he or she would be paid (in 8 instalments) the balance of his or her capital account together with any credit in his or her current account, in each case adjusted to take account of Distributable Profits. As explained above, the references to an equity partner's capital account and current account, and also to Distributable Profits, were all references to figures appearing in the relevant Partners' Accounts (as opposed to, for example, the Statutory Accounts).

20. It is also worth noting that, as at this date, F was overdrawn with respect to the LLP in the sum of £128,554.80.

Events after 30 April 2016

21. On 1 May 2016, the LLP's new financial accounting period began. Shortly after, there were discussions with F as to a potential new project. On 10 May 2016, Mr Brentnall, who as stated above had recently suspended F's drawings, emailed F stating:

> "On reflection I think the best way of dealing with this, if you agree F, is for the £4k to be reinstated on 20/5 but pro tem to be treated as sched d earnings and not as a further loan."

22. In that same email, Mr Brentnall continued with reference to the new potential project:

> "If however matters progress well at the end of next week, or generally on other fronts, which looks like it will allow for a certain degree of repayment, then of course that would be a tax neutral event because we have already paid tax. I suggest that we then have a more comprehensive review at the end of the month when hopefully we can assess more clearly realistic timelines/prospects etc…"

23. On about 20 May 2016, it transpired that the potential new project raised by F was not going to come to anything after all. Nevertheless, on 2 June 2016, F sent an email to Mr Brentnall saying that he believed that "the quickest way for the firm to be repaid the money it has advanced to me, is for me to continue working for the firm full-time on the projects on my list, and to continue to seek to bring in other business" – an email which Mr Brentnall merely forwarded to others for information but without any further comment.

24. On 4 July 2016, Mr Greenleaf raised with some of the remaining equity partners (apparently for the first time) the possibility of creating a provision against F's overdrawn current account for the purposes of the Statutory Accounts for the year ended 30 April 2016. On the following day, 5 July 2016, Mr Brentnall replied stating "I think we are possibly approaching the end of the road with" F.

25. On 6 July 2016, F emailed Mr Brentnall informing him that an important project – known as Project L – had fallen through. On the same day, Mr Brentnall forwarded the same to Mr Greenleaf simply stating: "End of the road, I think?"

26. As stated above, in May 2016 F had been paid £4,000 (albeit as Schedule D income as opposed to as a loan). He was also paid £4,000 for each of June and July. On 30 August 2016, another equity partner, Katharine Payne, emailed F informing him that the LLP would pay him a further £2,000 (again as Schedule D income) for August but that there

would be no further such payments "until we can see that there is a reasonable business case for doing so".

27. On 29 September 2016, Mr Greenleaf emailed the LLP's accountants and auditors, Crowe Clark Whitehill ("**CCW**"), who were in the process of preparing the Statutory Accounts for the year ended 30 April 2016. In that email, he proposed a provision of £128,553.80 (in other words, the full amount owed by F to the LLP as at 30 April 2016) against F's current account – and therefore also against the profits earned by the LLP over that period.

28. On 14 October 2016, the audit clearance meeting with CCW took place. On 17 October 2016, draft audited accounts (i.e., a draft of the Statutory Accounts for the LLP for the year ended 30 April 2016) were sent to the continuing equity partners. Shortly after, on 21 October 2016, a draft was also sent to Mr Tribe. As per Mr Greenleaf's earlier proposal, the above draft accounts made full provision for the sum of £128,553.80 owed by F to the LLP as a result of which the profit for the LLP was shown as £2,124,693.

<u>F's resignation</u>

29. On 28 October 2016, F resigned as a fixed share partner.

<u>The Distributable Profits resolution</u>

30. On 31 October 2016, a meeting of the members of the LLP took place comprising the four continuing equity partners. At that meeting, it was resolved that (in accordance with clause 13.1of the Members' Agreement) the amount of the Distributable Profits for the year ended 30 April 2016 to be divided amongst themselves and Mr Tribe was to be £2,124,693 – in other words, the same sum as appeared as profit for the LLP in the Statutory Accounts for the same period (and which therefore was some £128,553.80 less than it would have been but for the full provision made for F's debt).

<u>The approval of the Statutory Accounts by the continuing equity partners</u>

31. On 8 November 2016, the Statutory Accounts for the year ended 30 April 2016 were approved by the continuing equity partners and signed on their behalf by Mr Brentnall. As explained above, the above accounts made full provision for the sum of £128,553.80 owed by F to the LLP.

Further steps taken in relation to F

32. On 24 November 2016, the LLP (by way of a letter from Mr Brentnall) made formal demand for the repayment of the sum owing (which then stood at £152,336.25). This was the first time that any such demand had been made.

33. In 2017, further correspondence followed but in early May 2017, following a letter from Mr Brentnall threatening to serve a statutory demand and a subsequent telephone call in which F told Mr Brentnall that "if we wanted to make him bankrupt we could", Mr Brentnall reported back to the continuing equity partners concluding:

> "Not sure it's really worth spending much more time or effort on [F]."

The approval of the Partners' Accounts for the year ended 30 April 2016

34. On 18 April 2018, the continuing equity partners approved the Partners' Accounts for the year ended 30 April 2016. As per the Members' Agreement, the Partners' Accounts were required to set out the capital and current accounts for each partner adjusted to take account of Distributable Profits. As explained above, back on 31 October 2016 it had been resolved that the Distributable Profits for the year ended 30 April 2016 would be a sum which made full provision for F's debt in the sum of £128,554.80 – and accordingly, the Partners' Accounts for the above period also therefore effectively made full provision for the same. The effect of this, of course, was to reduce the sum which otherwise would have been due to Mr Tribe (and indeed to all of the equity partners) in respect of the above period.

35. In any event, in June 2018, Mr Tribe (through an advisor) wrote to the LLP questioning the treatment of F's debt in the various accounts. Correspondence then followed in

which the LLP maintained that the making of full provision for F's debt had been appropriate – something which Mr Tribe continued to dispute.

PART III: THE PROCEDURAL BACKGROUND

36. On 20 July 2018, Mr Tribe issued the present claim seeking payment of sums said to be due to him following his retirement from the LLP.

37. As mentioned above, the claim involved several different elements. On 24 June 2019, the first of these – Mr Tribe's claim for sums due to him under his capital and current accounts - was determined in his favour at which time he obtained summary judgment against the LLP from Deputy Master Hansen in the sum of £93,465 plus interest and costs.

38. Various further hearings followed including on 18 May 2021 when Deputy Master Raeburn directed that there should be a trial pursuant to Mr Tribe's claim for an account (as set out in paragraph 18 of his Particulars of Claim) on the following issue:

> "Whether the LLP profits figure for the purposes of the partners' accounts for the 2015/2016 year should take account of a provision against the debt of £128,554 due from [F] to the LLP at the year end date."

39. In May 2021 the second aspect of the claim – involving allegations that the decisions dealing with the discretionary allocation of profit shares among the partners for the years ended 30 April 2015 and 30 April 2016 were defective – was tried. In due course, Mr Tribe's claim in respect of that element was dismissed with Mr Tribe being ordered to pay indemnity costs. In short, therefore, while Mr Tribe was successful on the first element of the claim, it was the LLP which was successful on the second element.

40. In any event, following the above trial, the only element of the claim still outstanding became that as had been directed by Deputy Master Raeburn on 18 May 2021 (as set out in paragraph 38 above) – which is, of course, the matter now before me.

PART IV: THE EVIDENCE

The evidence of fact

41. I heard evidence of fact from Mr Tribe (on behalf of himself) and Ms Payne (on behalf of the LLP).

42. The primary issue of fact before me related to the circumstances of F and the debt which he owed the LLP. As to this, I had the benefit of a comprehensive bundle of contemporaneous emails and other correspondence. Both witnesses offered their perspective on the relevant events but, while I have no doubt that both Mr Tribe and Ms Payne gave their evidence honestly and did their best to assist the court, neither was able to add materially to the contemporaneous documentation which largely spoke for itself. This being the case, I say nothing more about the evidence of fact.

The expert evidence

43. As for expert evidence, I heard from Rosie Barnes (on behalf of Mr Tribe) and Paul Smethurst (on behalf of the LLP). Both are chartered accountants and the issue they had been asked to address was the appropriate accounting treatment of F's debt in the various financial statements for the year ended 30 April 2016. Both experts, I say without hesitation, gave their evidence clearly and impressively.

44. The uncontroversial starting point for both experts was that the key principle for present purposes was that set out in Financial Reporting Standards ("**FRS**") 102 which (at section 11) states:

> "At the end of each reporting period, an entity shall assess whether there is objective evidence of impairment of any financial assets that are measured at cost or amortised cost. If there is objective evidence of impairment, the entity shall recognise an impairment loss in profit or loss immediately…"

45. It was further uncontroversial that although the assessment of impairment is to be made at the end of the relevant reporting period, under FRS 102 (at section 32) matters occurring between the end of the reporting period and the date on which the accounts

are authorised for issue can be relevant in the assessment of impairment but only to the extent that such matters provide evidence of impairment as at the end of the relevant reporting period (as opposed to at a later date).

46. In short, therefore, if, for example, the relevant reporting period ends on 30 April, that is the date on which the impairment of the relevant asset has to be assessed. If on, say, 30 May something happens which shines a light on extent of the impairment as at 30 April, then that matter may be relevant (and will be classed as an adjusting post balance sheet event). If, on the other hand, something happens on 30 May which suggests an impairment of the asset but only as at that later date, it will not be relevant (and will be classed as a non-adjusting post balance sheet event).

47. While (perhaps unsurprisingly) both experts agreed on the relevant principles to be applied, they disagreed on the application of those principles to the present case. In short, Mr Smethurst was of the opinion that making full provision for F's debt was entirely appropriate. Ms Barnes, on the other hand, was of the opinion that 100% provision was too high and that it ought to have been subject to a provision of 50%. The difference between the two experts, so it seems to me, was their interpretation of the importance of the circumstances relating to F and the debt he owed to the LLP from time to time – something which I address in the following section.

PART V: THE STATUTORY ACCOUNTS

48. The starting point, so it seems to me, is the appropriate treatment of F's debt in the Statutory Accounts (in other words, the audited accounts of the LLP which it was required to prepare in accordance with the Companies Act and then file at Companies House).

49. In a nutshell, the issues are these: As at 30 April 2016 (and taking into account any adjusting post balance sheet events), was there objective evidence of impairment of F's debt? And, if so, to what extent should it be recognised?

50. As indicated in the previous section, both experts acknowledged that as at 30 April 2016 there was indeed objective evidence of impairment of F's debt. The difference

between them was that while Mr Smethurst was of the view that (as at that date) a 100% provision was appropriate, Ms Barnes was of the view that (as at that date) only a 50% provision was appropriate.

51. It was uncontroversial that there were two routes by which F's debt could be recovered by the LLP. The first (and preferred) route was that F would (to paraphrase Mr Brentnall) find some paying clients and earn some money to extinguish or at least reduce his debt. The second route (which for obvious reasons was less palatable but nevertheless something which the LLP was prepared to do as a last resort) was to seek to recover the debt from F's own assets, whether by way of enforcement proceedings or otherwise.

52. This being the case, the above issues can be further refined as follows: to what extent was there objective evidence that as at 30 April 2016 the debt owed by F to the LLP would not be recovered, whether by him generating fee income or from his own resources.

53. Having considered the evidence, it seems to me that as at 30 April 2016 (and taking into account adjusting post-balance sheet events) the position was as follows:

(1) There was undoubtedly objective evidence of impairment – in other words, there were objective grounds to justify the view that the debt, which prima facie was worth £128,554, was not in fact worth that sum.

(2) That objective evidence, however, did not justify a 100% provision. As at that date, the LLP still had *some* confidence that F would be able to generate fee income; and nor had the possibility of recovering the debt by way of enforcement been totally ruled out.

(3) Taking a relatively broad-brush approach, the appropriate provision to be made – as at 30 April 2016 – was 50%.

54. In reaching this view, I take into account in particular the following matters:

(1) As stated above, as at 30 April 2016 it is clear that the LLP still had some confidence that F would be able to generate fee income. On 23 February 2016 Mr Brentnall was suggesting to Mr Goodger that, going forward, "we've got to structure something sensible" before adding "I don't think we are looking for a complete break-off in relations." Further, on the following day, there were discussions as to the extent to which, from May 2016 onwards, F would be paid. Even on 28 April 2016 – just two days before the key date - when the "disappointing" news as to another write off was received, rather than terminating the arrangement with F there and then, the message to F was simply that the time had come "to re-evaluate what is a feasible monthly draw" before concluding "let's schedule another coffee soon". In short, therefore, while the LPP understandably had very serious concerns, as at 30 April 2016 the LLP had not entirely discounted the possibility of F generating fee income to extinguish or at least reduce his debt.

(2) The events post-30 April 2016, in my judgment, only reinforce the above view that, as at 30 April 2016, the LLP had not entirely discounted the possibility of F generating fee income. On 10 May 2016, Mr Brentnall emailed F about one of his projects and the possibility that "it will allow for a certain degree of repayment". Further, as stated above, the LLP continued to pay F (albeit on a different basis) until August 2016 – something which it would not have done if it had considered that there was no prospect of repayment. These matters, in my judgment, are all adjusting post-balance sheet events which helpfully confirm the position as at 30 April 2016.

(3) Other events, however, are, in my judgment, clearly non-adjusting post balance sheet events. Following various glimmers of hope in May and June 2016, on 6 July 2016 F emailed Mr Brentnall to inform him of the death of Project L prompting the latter to send an email stating "End of the road, I think?" Indeed, as stated above, at the end of August 2016 F was informed that he would receive a final payment of £2,000 but that no further payments would be made unless and until there was a reasonable business case for doing so. By this time, therefore, the LLP had pretty much given up on F being able to recover any fees. Importantly, however, the final straws which broke the camel's back and pushed the LLP to this position all took place after the key date. In short, therefore, while such events no doubt justified the stance which the LLP then took, they do not alter the position as at 30 April 2016.

(4) As for the alternative route of recovery from F's own assets, it is certainly correct that pre-30 April 2016 Mr Brentnall at least had serious doubts as to the feasibility of this as early as January 2016. It also seems, however, that this was not fully explored or discussed until after F's resignation from the LLP in October 2016. Indeed, as the stated above, formal demand from F was only first made in November 2016 and it was not until May 2017 that, following the telephone call in which F said that the LLP could make him bankrupt if it wanted that Mr Brentnall finally concluded that that it was not really "worth spending much more time or effort on" F.

55. As stated above, therefore, it seems to me that as at 30 April 2016, while there was undoubtedly objective evidence of impairment of F's debt, that evidence – although significant - does not justify a 100% provision. It is correct that in her report Ms Barnes does not explain how she reached the figure of 50%. Somewhat necessarily, however, the approach has to be slightly broad-brush and impressionistic and, doing the best I can, I conclude that 50% is indeed the appropriate provision which ought to have been made for F's debt in the Statutory Accounts.

PART VI: THE PARTNERS' ACCOUNTS

56. Importantly, however, the story does not end there. As will be recalled, the direction made by Deputy Master Raeburn was (with underlining added):

> "Whether the LLP profits figure for the purposes of the partners' accounts for the 2015/2016 year should take account of a provision against the debt of £128,554 due from [F] to the LLP at the year end date."

57. This was, of course, the appropriate direction to make – Mr Tribe's ultimate complaint (as set out in paragraph 18 of the Particulars of Claim) was the sum which had been allocated to him in the Partners' Accounts. While it was the Statutory Accounts which set out the position of the LLP as a whole, it was the Partners' Accounts which set out the positions of the individual partners – including of course as to the amounts due to each partner under the relevant capital and current accounts.

58. Indeed, the accounting structure for the LLP (as set out in the Members' Agreement) was effectively this: Statutory Accounts had to be prepared which would show the position of the LLP as a whole (clause 10.4). In addition, Partners' Accounts had to be prepared (clause 10.10) which would show the Distributable Profits and, based on those Distributable Profits, the capital and current accounts in respect of each partner (clause 1). In short, therefore, while the making of 100% provision first appeared in the draft (and then final) Statutory Accounts for the LLP, it was not this provision that Mr Tribe was challenging – what he was challenging (as set out in paragraph 18 of his Particulars of Claim and as directed by Deputy Master Raeburn) was the corresponding 100% provision which appeared in the Distributable Profits and, therefore, in the Partners' Accounts.

59. Counsel for Mr Tribe accepted that this was the correct approach but submitted that in effect it made no difference – the principles which apply to the Partners' Accounts must be the same as those which apply to the Statutory Accounts. Accordingly, so he submitted, if I were to find that full provision should not have been made for F's debt in the Statutory Accounts, it ought to follow that I should also find that full provision should not have been made for the same in the Partners' Accounts.

60. While there is some force in the above argument, the position for the Statutory Accounts and the Partners' Accounts, as counsel for the LLP pointed out, may in fact be different. Indeed, as stated above, in the Members' Agreement, the term "Distributable Profits" was defined (with underlining added) as:

> "…such revenue or capital profits of the LLP as are shown in the Partners' Accounts and which are to be shared between the Partners in respect of any financial accounting period <u>and which may be the same or more or less than the revenue or capital profits of the LLP as set out in the Statutory Accounts</u>…"

61. In short, therefore, while the figure for the profits appearing in the Partners' Accounts could be the same as the figure set out in the Statutory Accounts, it was expressly contemplated that it could be different.

62. The reason for this, of course, is that the two sets of accounts serve different purposes. The purpose of the Statutory Accounts is to show the financial position of the LLP at a particular date and over a particular period of time. They simply set out a factual position. So, for example, the value of any asset appearing in the balance sheet of the Statutory Accounts is designed to show to any person reading those accounts what, as a matter of fact, was the value of that asset at a particular date. Similarly, the profit figure appearing in the profit and loss account of the Statutory Accounts is designed to show to any person reading those accounts what, as a matter of fact, was the profit earned by the LLP over the relevant financial period.

63. By contrast, the Partners' Accounts are designed to show the position as between the relevant partners. Importantly, these accounts have to take into account the Distributable Profits. The process of determining the Distributable Profits starts with a factual exercise of determining the actual profit made over the relevant period – which will necessarily be the same figure as appears in the Statutory Accounts – but there then follows a <u>discretionary</u> process (the mechanics of which are set out in clauses 12 and 13 of, and the Third Schedule to, the Members' Agreement). So while that discretion may be exercised in such a way that the Distributable Profits will be the same as the profits shown in the Statutory Accounts, that discretion may also be exercised in such a way that the Distributable Profits will be (for example) less – hence the reference in the definition of Distributable Profits to profits "which may be the same or more or less than the revenue or capital profits of the LLP as set out in the Statutory Accounts."

64. In short, therefore, while the profit figure in the Statutory Accounts is a question of fact which has to be settled on well-established accountancy principles (as considered in this case by the respective experts), the profit figure in the Partners' Accounts involves an element of discretion where commercial considerations may be taken into account.

65. The position may be demonstrated by an example. One can imagine a scenario where the LLP has just a single client and over the course of the financial year it bills £1 million. As at the financial year end on 30 April, those fees have not yet been paid but there is no reason to suspect that they will not be paid. On 30 May, however, some unexpected and unforeseeable catastrophe befalls the client and it becomes immediately clear that the LLP will not receive a penny of its debt. On 30 June, the LLP then prepares

both Statutory Accounts and Partners' Accounts. As for the Statutory Accounts, as set out above, these are intended to demonstrate the factual position to any reader as at 30 April. Because as at 30 April there was no reason to believe that the debt would not be paid, those accounts ought to give the asset (i.e., the debt) its full value of £1 million – the unforeseeable catastrophe is clearly a non-adjusting post balance sheet event which can have no impact as to the actual financial position of the LLP as at 30 April. As for the Distributable Profits and, therefore, the Partners' Accounts, on the other hand, a commercial decision has to be made as to how much ought to be distributed to the relevant partners. As at the date of the preparation of those accounts it is <u>now</u> known that the asset of £1 million is completely worthless. In these circumstances, the partners would no doubt take the commercial decision not to grant themselves any Distributable Profits by writing off the debt in full as they now know that no money will be coming in after all; indeed, it could be said it would be foolhardy for them to do otherwise.

66. The present case, of course, is not at that extreme but it does, I think, demonstrate the different elements in play. In the present case, therefore, it seems to me that while for the reasons given, for the purposes of the Statutory Accounts (where of course the relevant date is 30 April 2016) the provision of 100% for F's debt was too high, for the purposes of the Distributable Profits and therefore the Partners' Accounts different considerations apply. While as at 30 April 2016, the LLP still had some confidence that F would be able to generate some fee income, by 31 October 2016 that confidence had evaporated and indeed F had handed in his resignation. It is true that following that date, there remained a glimmer of hope that F would be able to meet some of the debt from his own resources, but it seems to me that it was the smallest of glimmers and that Mr Brentnall was largely going through the motions rather than having any real belief that his formal demand would result in any recovery. In any event, given the position as it was then known to be as at 31 October 2016 when the resolution as to the Distributable Profits was made (and even more so as at 18 April 2018 when the Partner's Accounts were approved), it does not seem to me that the commercial decision to approve a distribution of profits which assumed that F's debt would not be recovered can be criticised.

<u>PART VII: CONCLUSION</u>

67. In conclusion, therefore, while the LLP was wrong to make full provision for F's debt in the Statutory Accounts, in my judgment the approval of the Partners' Accounts which also effectively made full provision for that debt cannot be criticised.

68. In short, therefore, the answer to the question:

> "Whether the LLP profits figure for the purposes of the partners' accounts for the 2015/2016 year should take account of a provision against the debt of £128,554 due from [F] to the LLP at the year end date."

is "yes".

69. I conclude by expressing my gratitude to all counsel and their respective instructing solicitors.

JPQC
July 2022