Business Protection

Partnership protection – the automatic accrual method

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What's automatic accrual?

Automatic accrual is an arrangement that lets a deceased partner's interest in a business pass automatically to the surviving partners. The beneficiaries of the deceased partner's estate will receive the value of the deceased partner's business interest in cash.

Although automatic accrual is a method of business protection, it's only suitable for partnerships and can't be used for shareholder protection.

Setting up an automatic accrual arrangement

The partners should complete an automatic accrual agreement drawn up by a solicitor in line with the terms of their partnership agreement. As part of this, each partner should set up a life protection policy for the value of their share in the business, and place it in trust for the benefit of their family. A flexible trust might be an appropriate solution.

For the trust to be effective for inheritance tax (IHT) purposes, their business partners shouldn't be beneficiaries of the trust.

Under the terms of the agreement, a deceased partner's share in the business passes automatically to the surviving partners when they die. The beneficiaries of the deceased partner's estate will receive the claim proceeds of the life protection policy from the trustees. But if the value of the claim proceeds is less than the value of their share of the business when they die, the surviving partners will have to make up the difference to compensate the deceased partner's estate for the shortfall.

Taxation of the policy payments and proceeds

If the policy is placed in trust for the benefit of the deceased partner's family, the claim proceeds won't normally form part of the deceased partner's estate for IHT purposes. It's important that all of the partners policies are placed in trust and that the arrangement is commercial. When the partner's interest in the partnership passes automatically to the other partners, it might be covered by an IHT exemption as a commercial arrangement or by business property relief. Business property relief is a valuable relief which reduces the value of a business or its assets when working out how much inheritance tax has to be paid. Read our Business property relief factsheet for more information.

The policy payments won't receive tax relief under any circumstances. It doesn't matter whether they're paid by the individual partners or from the partnership bank account – neither offers a financial or taxation advantage.

If you need any help with this, please speak to your usual Aegon sales representative, or visit our website for more business protection support.

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