

INFORMATION SHEET NO.46

UK Limited Liability Partnership*December 2006***Introduction**

The Limited Liability Partnerships Act 2000 introduced this type of business vehicle in England and Wales. Since their introduction in April 2001 many professional service providers have taken advantage of this type of entity to protect themselves from the risk arising from the careless or accidental negligence of a colleague. For example, partners in an accountancy firm would be protected from personal liability if a claim was successfully pursued by a major client. Partners in a construction business would be protected if a new building collapsed, causing high level claims against them.

Legal Form

A Limited Liability Partnership (LLP) is a legal entity and a body corporate. This means that it has a legal personality separate from that of its members. Like a limited company, LLP can do all the things an individual or company can do. It can enter into contracts, sue or be sued, hold property or become insolvent.

As the name suggests the LLP has features in common with both private limited companies and private partnerships.

Key features

Like a company the LLP is a corporate entity, legally separate and distinct from its members. The LLP enters into contracts in its own name and critically, liability rests with the LLP, not with the members. Interestingly, all the partners benefit from limited liability; there is no 'general partner'. Instead there are two 'designated partners' who have additional responsibilities in terms of the LLP's filing requirements.

Specifically, it is the designated partners who are held liable for the correct filing and recording of the LLP's affairs. It is these two who will be subject to the criminal penalties of failure to comply.

The designated members are not the management team of the LLP (management is discussed below) but are responsible for these defined statutory tasks which include:

- signing the accounts
- delivering the accounts to the registrar of companies
- appointment and removal of the auditors (if required)
- notification of membership changes (and changes to the registered office) to the registrar of companies
- preparing, signing and delivering the annual return
- applying for the LLP to be struck off the register

In default of notification to the registrar of companies of the designated members, all members are designated members. Given this default position and the tasks imposed on designated members, anyone who is a member of an LLP should check that there are designated members.

The LLP is required to place documents (excluding the partnership agreement) on public file with the Registrar of Companies. The Registrar of Companies issues an incorporation document stating the LLP's name and registration number. Its address (registered office), the names and addresses of the first members (partners), the names and addresses of the designated partners are held on public file. There are also annual filing requirements similar to those imposed on a company.

Like a partnership there are no shares. However, the proportion of the profits payable to each partner may vary according to terms laid out in the partnership agreement. And, indeed it is possible to have members with no entitlement to a share in the profits. It is also possible to have 'salaried members', who are remunerated by salary only.

Liability of the partners

The amount of a LLP partner's liability on a winding up is effectively the amount set out in the limited liability partnership agreement. The Act states that the amount subscribed by a member of a limited liability partnership is the amount of a partner's contribution to the limited liability partnership capital, less money:

- previously drawn out or taken back
- money drawn out or received back during a period of five years from the relevant date
- money entitled to be drawn but which has not been drawn
- money entitled to be sought from another partner

Partnership Agreement

Partners in a LLP are not obliged to enter into a formal partnership agreement. In practice, however, they will almost certainly get together to decide on the structure and regulation of all aspects of their LLP. The agreement they make is then binding on them after the LLP has been properly registered. The agreement itself is not registrable and so remains confidential. If there is no agreement, or the agreement is silent on an important point, then formal default provisions apply.

A comprehensive LLP agreement governing the duties and responsibilities of the members is a necessity, therefore, and it will need to make provision for:

- the management of the LLP
- the decision-making process
- the capital contributions required of the members, both while a going concern and (if any) on liquidation
- the division of profits
- changes to the membership
- dispute resolution
- termination of the LLP; and
- provision for the amendment of the LLP agreement

The partners may be of any nationality and they may be natural persons or corporate bodies. If the interest in the LLP of a member passes to another person (eg death, bankruptcy), the other person may not interfere with the management of the LLP but will be entitled to receive whatever would otherwise have been due to the member. There is not normally any restrictions on trading both within and outside the European Union.

Incorporation procedure

At least two people "carrying on a lawful business with a view to profit" must subscribe their names to a document called an "Incorporation Document". The Incorporation Document must be delivered to the Registrar of Companies at Companies House . A statement must also be delivered to the Registrar that there has been compliance with the requirement that at least two persons, associated for the purpose of carrying on a lawful business with a view to profit, have subscribed their names to the Incorporation Document. The statement must be made by a subscriber to the Incorporation Document or a solicitor engaged in the formation of the limited liability partnership. The Incorporation Document must include the following:

- the name of the limited liability partnership
- whether the registered office is to be situated in England or Wales
- the name and address of the persons who are to be members on incorporation
- whether some or all of the members are to be designated members

Partners obligation and authority

The law of "ostensible authority" applies to partner transactions. Every partner is an agent of the LLP. The LLP is bound by every contract made by any partner, unless first, the partner had no authority to make the contract and second, the third party was aware of that fact. The LLP is bound even by contracts by former partners, unless the other party has been told that the former partner is no longer a member, or the registrar has received a notice to that effect.

Taxation

Income tax is imposed on the members of the LLP, not on the LLP itself. Interestingly, if the partners are non-residents of UK, their income from the LLP is not subject to UK personal income tax or social security contributions. A LLP may however be registered for VAT in its own right.

This vehicle offers entrepreneurs wishing to protect themselves against business and civil claims a low cost solution, which does not involve the need for complex profit extraction methods and expensive compliance.

Advantages and disadvantages

The advantages of an LLP include:

- Limited liability: reduced risk to personal wealth from creditor's claims;
- Internal flexibility: facilitates participation in management and maintenance of ethos of partnership.

The disadvantages include:

- Lack of privacy – financial information must be disclosed (subject to exceptions)
- Requirement for an LLP agreement: needed to avoid default provisions applying and to cover situations not addressed by default provisions
- Legal uncertainty – novel structure – uncertainty is undesirable in commercial entities

If the position of an LLP is compared with a private limited company, such companies have:

- Limited liability – same as LLP

- Internal flexibility – the impact of the company law requirements for formal board and management structures on small companies can be overstated. In fact, the law facilitates informal and flexible decision-making in such companies, for example, allowing meetings to be called on short notice, use of written resolutions and acceptance of informal unanimous assent
- Privacy – same as LLP – disclosure subject to exemptions
- No need for LLP agreement – the memorandum and articles of association act as default standard provisions
- No legal uncertainty – tried and trusted business mechanism with high degree of legal certainty – structure familiar to advisers and well-developed and sophisticated body of law applicable

NOTES:

The above is intended to provide a brief guide only. It is essential that appropriate professional advice is obtained. Totalserve Management Ltd will be glad to assist you in this respect. Please do not hesitate to contact us.