

## Briefing Note: Limited Liability Partnerships

### An Introduction to the Guide

Prior to 6 April 2001, businesses could operate as limited companies, sole traders or partnerships. One of the most striking disadvantages of operating as a sole trader or partnership (as opposed to a limited company) related to liability. In a partnership every partner is liable jointly with his other partners for all the debts and obligations of the partnership incurred during his membership.

Limited liability partnerships (LLP) were initially designed to meet the requirements of major UK firms (e.g. accountants) with international practices to try to prevent them from incorporating overseas so that they could benefit from limited liability status. LLP status is now available to all UK professional partnerships (subject to the rules of their own professional bodies). It is also available to other types of businesses carried on in partnership. This guide should not be relied upon as legal advice and you should contact us for advice on your specific circumstances.

### 1. What is a Limited Liability Partnership?

LLPs are a relatively new form of business entity and have a separate legal identity (like a limited liability company). The LLP is the contracting party in contracts with clients or customers of the partnership and the ability of clients to claim is limited to the assets of the LLP.

However, generally an LLP benefits from the previously existing partnership position so far as internal management and tax are concerned.

### 2. Limited Liability

The LLP is treated as if it were a limited liability company for the purposes of accounts (Companies Act accounts need to be prepared, audited and filed publicly), winding up and insolvency. On insolvency there is the ability to "claw back" from members' distributions made in the 2 years previous to winding up which should not have been made. E.g. where the LLP was insolvent or the making of the distribution made it insolvent.

A note of caution is that individual members can still be sued for negligence notwithstanding their limited liability as members of an LLP. In a properly run business however the threat of negligence can be minimised.

### 3. Tax

LLPs are particularly valuable for businesses that would find Corporation Tax and other consequences of forming and operating a limited company onerous but still want to enjoy corporate status and limited liability for members.

LLPs are taxed differently to companies. Profits are treated as the personal income of the LLPs' members in the same way as are the profits of a normal partnership.

For existing partnerships that convert to LLPs there will be Stamp Duty relief on the instrument transferring property from the current partnership to the newly incorporated LLP if relevant conditions are met. The LLP may need to register for VAT depending on the level of income it generates.

#### Briefing Note

April 2007

#### Summary:

An introduction to the nature and purpose of Limited Liability Partnerships and how they differ from other Partnerships.

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### **4. Accounts**

LLPs will produce and publish financial accounts with a similar level of detail to a similar sized limited company and will have to submit accounts and an annual return to Companies House each year. This publication requirement does not exist for normal partnerships.

The audited accounts which are filed at Companies House will be available for public scrutiny.

### **5. Finance**

Capital is provided by the members. LLPs are similar to partnerships or sole traders in this respect. The members will provide working capital and share in any profits.

### **6. Administration**

In essence the members, in a way agreed between, run the LLP. One advantage of an LLP over a limited company is the flexibility the members have to organise and manage themselves.

A member is required to act in the best interests of the LLP and therefore it is prudent that the acts and obligations of the members both to the LLP and between themselves are regulated by a members' agreement. It is not compulsory for such an agreement to be in writing as the Limited Liabilities Partnership Act provides for a basic set of "default" terms. However there are very few default provisions within the Act and therefore we advise it is essential both commercially and practically for a written members' agreement to be put in place prior to incorporation.

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## 7. Summary

	<b>Partnership</b>	<b>LLP</b>
<b>Setting up</b>	Partners need to register as self-employed. A deed of partnership is advisable.	Need to register Form LLP2 with Companies House. Method is similar to those of a company. No Memorandum or Articles of Associations are required.
<b>Liability</b>	Unlimited liability for the debts of the partnership both jointly and severally.	Limited liability for its members.
<b>Structure</b>	No separate legal entity, but partnerships can be sued in the firm's name.	It is a separate legal entity. Has the organisational flexibility of a partnership.
<b>Tax</b>	Self employed status. Even if the partners don't draw on the profits they are still taxed. Losses can be offset against tax on other income.	It is taxed as a partnership.
<b>Ability to raise capital</b>	Cannot issue debentures or floating charges.	It has the ability to create floating charges.
<b>Accounts</b>	There is no express requirement for the partnership to prepare accounts or for accounts to be audited.	Its accounting and filing requirements are broadly the same as those of a company.
<b>Profits</b>	All profits are shared between the partners (as agreed within the deed of partnership).	Incomes derived by the members will be closer to that of a 'Partnership' than to the dividends paid by companies.
<b>Management</b>	The partners share responsibility for controlling the business.	The business is controlled by the designated members' (who have a similar responsibility to a directors / secretary of a Ltd Company) and the 'members'.

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