



# Limited Liability Partnerships

## Introduction

The Limited Liability Partnerships Act of 2000 came into force on 1 April 2001 and provided a hybrid alternative to the company versus partnership business structure tension. LLPs combine the organisational flexibility and tax status (with certain exceptions) of a partnership with limited liability for their members.

In summary, they are regarded in law as bodies corporate, but for tax purposes they are generally treated as partnerships. They have been used mainly by professional practices, who wish to maintain flexibility and tax status, whilst protecting members through limited liability.



## Formation of LLPs and their members

Broadly two or more persons associated with carrying on a lawful business with a view to profit can set up an LLP. One or more of those “persons” can be a company.



A Form LLP2 will need to be signed by the members and submitted to Companies House. The LLP2 will specify the registered office and the names of the members and must be accompanied by the relevant fee (usually £95).

Companies House will issue a registration certificate, which is akin to a certificate of incorporation for a company.

At least two of the members of the LLP must be designated members, usually appointed by agreement between the members. These designated members are responsible for appointing auditors if required, signing the accounts, delivering them to Companies House, notifying Companies House of any changes to, for example, the registered office and for signing and delivering the annual return to Companies House.

The annual return of the LLP must be filed every year with full details of each member. The small companies’ exemptions from the necessity of a statutory audit apply equally to LLPs.

## Internal workings of the LLP

The LLP will usually be governed by the LLP agreement signed by all members. Such an agreement will usually cover the following areas:

- Capital contributions and withdrawals
- Shares of profits and losses
- Basis for preparing accounts and establishing profits
- Any special rights of members
- Voting rights of members and procedures of meetings
- Management of the LLP
- Transfer of members interests
- New members
- Retirement and expulsion
- Winding up
- Dispute resolution

In the absence of such an agreement, a number of standard terms apply, such as all members have equal shares of capital and profits and new members need unanimous consent.

However it is best practice to ensure an LLP agreement is entered into to ensure that commercial reality is reflected in the way the LLP is run.

The LLP agreement is not a public document and as such the internal workings of the LLP will not be generally available through Companies House, unlike the Articles of Association of a company.

New members may be added at any time and members may also leave at any time, usually in accordance with the LLP agreement.

## Limited Liability

Unlike a company the members of an LLP do not obtain the benefit of limited liability per se. Each member is still liable personally for his/her own negligence, but is protected from the negligence of other members of the LLP as liability is limited to the extent it is not joint and several. Importantly, where a member of an LLP is liable to a third party for anything done in the course of the



LLP's business, then the LLP is liable to the same extent as the member, the other members are not liable.

This is a significant advantage over a standard partnership where liability is joint, several and unlimited.

That said, most LLPs will also have some form of professional indemnity insurance to protect members from claims and it is usual for each member to have an indemnity from the LLP in place should any claim be made.

## Taxation

LLPs are taxed in broadly the same way as a partnership, in that the profits of the LLP are split between its members (according to the membership agreement) and taxed as income of each member under the income tax rules.

The position with regard to LLP losses is slightly different. Losses are, as with profits, split between each member and can be offset against other income and gains of each member for the year in question. Therefore if a member has other income perhaps from employment or investments, the LLP loss can be used to offset that income and reduce the income or capital gains tax liability accordingly. This is called "sideways relief".

However, the losses of an LLP that may be offset against other income are restricted to the amount of capital that an LLP member has put into the LLP. Capital for these purposes is broadly defined as capital contributions made, less any withdrawn capital. Loans made to the LLP do not constitute capital.

Should losses of the LLP exceed capital contributed, no further sideways relief is available until further capital is contributed.



Any current year losses are available for carry back against profits of the prior year only and can be carried forward indefinitely. Brought forward losses are treated as losses of the current year.

It is possible to convert existing partnerships to an LLP structure, generally speaking tax free and the conversion provisions are designed to enable conversion on a tax neutral basis, with the LLP standing in the shoes of the old partnership as regards base costs of assets, capital allowance pools etc.

## Suitability

Many professional partnerships have been converted to LLPs, usually where there are a significant number of partners and it is more difficult to control partner activities due to the size of the partnership. In addition, if professional indemnity insurance is difficult to obtain or prohibitively

expensive, the LLP form may provide a more suitable business vehicle, although it is likely some (perhaps less comprehensive) professional indemnity insurance should also be obtained.

## Further Information

Monahans can assist you with all aspects of LLPs, their formation and the suitability to your business planning. For further advice and assistance our specialist Tax Consultancy Department will be pleased to help. Please contact **Dominic Bourquin** on **(01225) 472800** or e-mail **dominicbourquin@monahans.co.uk**