Limited Liability Partnerships vs. Limited Companies

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There are a number of factors to take into account when comparing Limited Liability Partnerships (LLP) and Limited Companies (LTD).

Legal Entity

LLP & LTD: Both are legal entities in their own right, capable of entering into contracts and holding the title to assets.

Liability of owners

LLP: On winding up, each partner's liability is restricted to their formal capital and certain unallocated profits, except that they have a joint and several liability for stamp duty land tax.

LTD: On winding up, the shareholders' liability is restricted to any outstanding calls on share capital.

Risk protection

LLP: Partners have protection under tort and contract law. A partner might still be liable for his own negligence.

LTD: Provides shareholders with protection under tort and contract law. A director might still be liable for his own negligence.

Formality

LLP: Governed by partnership deed which is a private document and will not be filed at Companies House. Partners in the LLP are called members. At least 2 must be designated members who have additional legal and other duties. All members must be registered at Companies House

LTD: Governed by The Memorandum and Articles of Association; which must be filed at Companies House. All directors must be registered at Companies House.

Capital - minimum

LLP: None. Partners can fund the business with debentures or unsecured loans ranking equally with other unsecured creditors.

LTD: Can be as little as one penny issued and paid up for a private company. PLCs must have at least £50,000 share capital with at least 25% paid up.

Employment rights

LLP: Partners only rights are those given in a partnership agreement.

LTD: Directors are generally employees, protected by employment law.

Incentives and rewards

LLP: Promotion to partnership for high flyers; bonus paid via profit share is taxed at up to 41%. Partners retain control via partnership agreement.

LTD: Bonuses subject to income tax and NIC at up to 41% also attract employer's NIC at 12.8%. Share option schemes are complex, and costly to administer.

Internal goodwill

LLP: Members of can decide to ascribe no value to its goodwill, so a retiring partner takes only his capital, loan and current account balances. Avoids costly valuation exercises whenever partners leave.

LTD: Retirement bonuses to retiring directors may be costly in tax terms.

Limited Liability Partnerships vs Limited Companies

There must be a formal share valuation agreed with HMRC if director sells his shares on retiring (or at any time).

Sale process

LLP: Buyers prefer to buy business assets because of reduced due diligence and less reliance on sellers' warranties and indemnities. Normally reduced transaction costs.

LTD: Shareholders prefer to sell a company to avoid duplicate tax cost (see below). Greater due diligence, warranties and indemnities risk for sellers. Normally increased transaction costs.

Tax on profits

LLP: The LLP is transparent. Partners are taxed on all profits.

LTD: Corporation tax at 20%.

Tax on owners' incomes

LLP: Self employed top rate is normally 46% including NIC. Tax liabilities are personal; if a partner defaults there is no come back on the LLP or the other partners.

LTD: Employees' top rate is 51% including NIC. BUT company suffers 13.8% employer's NIC on all remuneration. Dividends escape all NIC but are taxed at 32.5%. Must pay over PAYE & NI.

Tax on sale

LLP: Partners can sell business assets and are taxed personally on gain at 18% or 28%, subject to possible entrepreneurs' relief. The LLP will not be liable for any tax.

LTD: Gains from selling share capital are taxed at 18% or 28%, subject to possible entrepreneurs' relief. Sale of business assets by the company results in tax of 20% of the gain for the company, with the acquisition cost adjusted for inflation.

There is further tax on extraction of the net gain from the company.

Inheritance tax

LLP & LTD: Business property relief at 50% or 100% may apply to both an interest in an LLP's assets and shares in a Ltd company.

FCA Considerations

LLP: Regulatory capital rules probably mean an FCA member LLP must have some formal capital, use of subordinated loans from partners, but Tier 2:Tier 1 ratio restriction and all earnings of partners are excluded from Annual Expenditure calculation.

LTD: Paid up capital will be dictated by FCA capital requirements and only discretionary bonuses are excluded from Annual Expenditure calculation.

Other Considerations

LLP & LTD: Companies House Filing is required within 9 months of period end for LLPs and a private company and 6 months for a plc

LLP & LTD: Accounts will require an audit unless it is a small or dormant company or LLP. In general no exemption from audit is available for an FSA regulated entity.

Abbreviated accounts can be prepared and filed at Companies House provided the LLP or LTD meets the requirements.

Specific advice should be obtained before taking action, or refraining from taking action, on any of the subjects covered

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