



Future enterprise

Assessing forms of business

ICAEW MARKET FOUNDATIONS

1. Introduction

Human enterprise has depended on different legal forms of business over the centuries – from medieval monasteries to the multi-national companies of today, the forms are both shaped by the society they inhabit and help to shape it. We often take them for granted but they touch almost every aspect of business life, from finance and taxation to appetite for risk. It is in our power to change existing forms or to create new ones and the future prosperity of society depends upon us making the right choices. In this paper we consider whether a fresh approach is required for tomorrow's enterprises.

Forms of business are rooted in national law. We have included in Appendix 1 a short description of the main forms of business used in the UK, their characteristics and relative popularity, but many of the issues arising are of universal application, such as the relationship between form, regulation and trust in business (considered further in Appendix 2). From an international perspective, we might also question whether the existing jurisdictional approach is sustainable in an increasingly globalised world; it certainly results in complexity in the shape of large groups of companies and structures involving various combinations of forms across borders and may result in tax or other jurisdictional arbitrage. As global citizens we might well ask if there is a better way.

The limited liability company dominates the UK economy (and similar types of company, or corporation, are just as pervasive in other parts of the world). But this form and many other forms of company (such as co-operative societies) were, in essence, developed over a century ago. Since then, successive governments have adopted a relatively cautious approach, making small changes to existing forms or introducing variants (such as the community interest company (CIC) and limited liability partnership (LLP)) to address specific concerns in a 'mend and make do' approach. While it seems that this approach has provided sufficient choice to enable business to function, it has some disadvantages.

In particular, businesses need to invest time and effort in choosing the optimal form (or combination of forms) from those available and the regulatory environment, including the taxation regime, that has evolved alongside the forms has become increasingly complex (the Companies Act 2006 (CA 2006) alone ran to 1,300 sections when enacted and has grown since). Human energy that could be spent on the substance of productive enterprise is often diverted to dealing with unproductive matters of form and associated administration. In short, it is possible that we are being constrained or 'boxed in' by our forms of business rather than liberated by them: they may have become our masters rather than our servants.

Social and technological developments in recent times, including blockchains, mean that a new approach may now be possible. In particular, the need for artificial persons, in the shape of various company structures, may diminish and more natural approaches emerge if we allow them to do so. For instance, we might permit individuals to benefit from limited liability without the need to incorporate a limited liability company – something that the Office of Tax Simplification, in its small company taxation review of March 2016, advised the UK Government to consider. If this were to be linked to other changes, such as allowing individuals to form partnerships together without becoming jointly and severally liable as a result, enterprises of individuals and networks of individuals might develop in new and exciting ways better suited to the next era of human progress than the forms we have come to rely on today.

But radical change may also come at a price, and we conclude this paper by outlining some of the issues that would need to be considered in more detail for proposals of this kind to be taken forward.

2. The changing shape of society

Today's world is far removed from the times when our most popular forms of business entity evolved.

Social progress has resulted in universal rights for citizens to own property, to vote and to be treated equally. Economic and technological development has increased the wealth of much of the population, enabled human interaction in ways that would have been unimaginable even a hundred years ago and displaced many local markets with global (or virtual) markets.

Many traditional business models are already being challenged by developments such as social media, homeworking, the 'sharing society', crowdfunding and peer-to-peer lending and it does not take a great leap of imagination to see the scope for other developments such as 3D printing, artificial intelligence, the Internet of Things and driverless cars to disrupt many sectors of the economy. Above all, many of us now expect to have a high degree of control over our own lives and to have an impact on the world in which we live.

These developments have indeed transformed our personal lives; we now have ready access to information without use of traditional intermediaries (for instance, access to live train or bus times) and can share information to help others (for instance, by reporting road congestion or rating service providers online). Acquiring, selling or donating goods is increasingly easy. Society seems to be evolving in a way that enables us to interact with others in fluid and rapid ways with traditional distinctions between 'consumer' or 'business' becoming blurred; we are, perhaps, becoming more mutual in our way of life.

Yet while these developments seem natural enough to us in our personal lives and help us to fulfil our potential as human beings, the business environment is more rigid.

3. Today's forms of business: the constraints

3.1 The meaning of business

The term 'business' has no fixed meaning; it has been described as an 'etymological chameleon: it suits its meaning to the context in which it is found'. It is often associated with the pursuit of profit-making activity, but 'not-for-profit' organisations contribute to the economy too, providing employment, services and goods and are generally considered as businesses in this paper. Not for profit is also a fluid concept, potentially including not only charities but also businesses that make a profit, but do not have pursuit of profit as their object or which do not distribute profits to their members (or do not do so in proportion to capital contributed).

Business may be a fluid term, but it is frequently used in a limiting way that reinforces a segmented view of life with emphasis on economic measurement such as turnover or employment, for instance when contrasting business with personal or artistic pursuits. There are also a finite number of legal forms through which business may be conducted. In this paper we therefore also use the term 'enterprise' to refer to the output of human energy, creativity and endeavour more generally whether or not measurable in traditional economic terms.

3.2 The forms of business

There are three main types of business form in the UK private sector: businesses of individuals (or sole proprietorships), partnerships and companies.

Individuals are relatively free to pursue enterprise as they see fit and are not subject to many of the constraints we identify in relation to other forms of business. However, they have unlimited liability for the debts of their businesses and therefore suffer a disadvantage compared to many forms of company which confer limited liability on their owners.

Partnerships can only be established for 'for-profit' businesses and partners not only have unlimited liability but are also jointly and severally liable for partnership debts. This in itself goes some way to explaining the relative decline of this form in recent decades compared to forms of limited liability company.

The two most human forms of business have, therefore, effectively been disadvantaged in the UK compared to artificial persons in the shape of various forms of company. We outline below some reasons why this may not be good for human enterprise before considering alternatives.

3.3 Boxed in by companies?

'Company' can have a range of meanings, depending upon the context. It may refer to companies formed under a particular law, such as the UK CA 2006, or could be used in a broader sense akin to 'corporation' or 'body corporate', encompassing a variety of additional bodies such as international companies or companies formed by royal decree. Its natural meaning is broader still, suggesting a grouping of people, such as a company of actors. In this paper we use the term to mean the forms listed at the end of Appendix 1 whether or not they would typically be considered to be companies.

Companies are generally subject to a degree of externally imposed bureaucracy (for instance, requirements to file records on state controlled registers) and the resultant costs can have a significant impact on the efficiency of business generally and small businesses in particular. The Office of Tax Simplification estimates that the administrative burden on each of the around 1.3m companies with fewer than 10 employees (or 'micro' companies) equates to an average of £1,853 in agents' fees plus owners' own time in evenings and weekends.

Some forms of company are more suited to profit-making pursuit than others and some may be used only for specific purposes, such as building societies or charitable incorporated organisations (CIOs). This tends to lead to a compartmentalised view of enterprise: one organisation for profit, another for mutual benefits, another for charity and so on.

We are similarly compartmentalised in our interactions with these forms, for instance as 'shareholder', 'director' or 'employee'. The forms themselves are not, of course, solely responsible for this as our tax regime and other aspects of the business environment are built around distinctions of this kind. The result, however, is a degree of rigidity in our business environment that could be seen as boxing us in and may not be helpful in enabling us to shape our future as we might otherwise wish to do.

There are many times more companies limited by shares than companies of other kinds combined, and it is this form of company that dominates our economy. The popularity of the form is partly due to its inherent features including limited liability for its shareholders, broad powers and separate legal personality. It may be tempting to think that the dominance of this form is a natural state of affairs. But as the variety of alternative company forms testifies, it does not suit all types of business. Even a few decades ago the picture was very different as the tax regime, in effect, deterred its use for very small businesses, and accounting and audit requirements were more onerous.

A small minority of companies limited by shares are 'listed' (so that their shares can be traded on public stock exchanges). Just a couple of thousand of these companies employ more people and account for more turnover than the whole of state enterprise. Their influence on our lives is immense. In particular, the market infrastructure that has grown up around them means that a large proportion of the population is 'invested' in them through pension schemes or collective investment schemes.

Companies whose shares are sold to the public have given rise to concerns of abuse since their infancy. For instance, Anthony Trollope's fictional account of a fraudulent 'Great South Central Pacific and Mexican Railway' company in *The Way We Live Now* (1875) involved short-term trading of shares, individual greed, lack of transparency in accounts and dealings, inappropriate remuneration, unengaged and unskilled directors, lack of boardroom challenge with no female presence in the boardroom (but plenty of feminine influence elsewhere). While legal and regulatory reforms may have curtailed some of the excesses, many of the concerns linger on to some degree, including concerns about good governance, short-termism and financial probity. We might legitimately ask whether we have been going down the right path in facilitating the dominance of this form of business.

Yet there seem to be few alternatives to listed companies for very large-scale business. The co-operative society and many other mutual forms of business have been in decline in recent years and it remains to be seen whether changes to the legal regime such as the Mutuals' Deferred Shares Act of 2015 will dramatically alter the landscape (Deloitte's 2011 paper outlined the challenges faced by mutuals in the insurance and financial sector, while Mutuo's 2013 paper made suggestions for change, including on redeemable shares). In any case, very large mutual companies might themselves encounter some of the difficulties faced by very large listed companies. State enterprise remains significant but would not be considered an optimum form of business for economic progress by many. Could it be that individuals will in future interact in ways that might result in large-scale ventures without the need for any over-arching 'form' of business? Will the monolithic hierarchical structures we have become accustomed to seem archaic in years to come?

4. The potential of businesses of individuals

4.1 The power of individual endeavour

While limited liability companies dominate the economy by most measures, businesses of individuals (sole proprietorships) are becoming increasingly popular; there are now more than 3m of them, making this the most popular form for active business in the UK.

Although most sole proprietorships are small businesses with low turnover (and few if any employees), there are high earners among them; there is no inherent restriction in this respect.

But individuals may seek personal fulfilment rather than financial profit and it appears that the 'self-employed' may be happier with their lot than those who are employed by others, even if they are not wealthier as a result (see the RSA's 2014 report).

James Robertson foresaw in his book *Future Work* an increase in sole proprietorships or 'ownworking' in the 1980s at a time of high unemployment and reflected that this transition:

'... from employment to ownwork can be seen as the next stage of progression towards freedom, responsibility, and fuller participation in the life of society, that was marked at earlier historical times by the transitions from slavery to serfdom, and then from serfdom to employment. It can also be seen, by those who look at things this way, as one aspect of the next step towards fuller personal participation by human beings in the universal process of evolution.'

While it is natural for individuals to seek profit, and for-profit businesses have contributed enormously to our economic progress and well-being, some of the greatest contributions to our development have been motivated by a desire to profit society rather than by personal gain. For instance, Tim Berners-Lee did not seek to restrict use of the internet: 'This is for everyone', and Jonas Salk did not seek to patent his vaccine for polio: 'There is no patent. Could you patent the sun?' (a question which was perhaps more obviously rhetorical than than it would be now). Modern technology promises an even brighter future for those who wish mankind as a whole to benefit from their enterprise.

Of course, philanthropic contributions are not only made by sole proprietors, but by people more generally (including the unemployed) and by organisations from charities to profit-seeking limited liability companies (who may promote pro bono work by their staff or make charitable donations). But individuals carrying on business on their own are uniquely placed to pursue a variety of objectives in a way that reflects human nature.

4.2 Allowing individuals to limit their liability

The artificial person of the limited liability company has a number of intrinsic advantages over living people (as opposed to extrinsic reasons, such as tax treatment). Of these, limited liability is one of the most important features that has led to the popularity of the form.

The Limited Liability Act of 1855 laid the foundations for the modern limited liability company regime in permitting business people to form companies that insulate them from insolvency risk beyond their paid-up capital.

It was a bold and imaginative development which some opposed at the time on the basis that limited liability might lead to reckless endeavour and fraud. Requirements for companies to file accounts and maintain public registers were, and still are, intended to alleviate these risks and might be regarded as the price to be paid for the benefits of having limited liability. While there have been cases of abuse, the worst fears of the time have not materialised and it is generally considered that limited liability has been benign for business and wider society, although lack of trust, particularly in 'big business', is a matter of ongoing public concern, as noted in Appendix 2. The question then arises why, if limited liability has proved so beneficial, it should not be extended to natural persons.

Gilbert & Sullivan raised this question satirically in response to development of the limited liability company, envisaging (in *Utopia, Limited* or *The Flowers of Progress*, 1893) a world where 'every man, woman and child is now a Company Limited with liability restricted to the amount of his declared Capital!'. The operetta has not stood the test of time and neither, we suggest, has the antipathy to the limited liability company concept. We now have more than a century's experience of limited liability companies and individuals are able to operate through single person companies if they wish. The question of whether limited liability should be extended to natural persons deserves to be taken seriously – indeed, we might more naturally ask 'why not?'

Similar concerns about the potential for abuse might arise in relation to limited liability for individuals as for companies. Perhaps a similar 'price' for limited liability could be extracted, for instance, by imposing registration, accounting or disclosure requirements. The LLP model, flexible though it is, still requires certain registrations to be maintained, and might be adapted for use by sole proprietors.

But does our experience with limited liability companies justify such caution or should we consider a more radical approach? The recent reductions in the accounting and audit requirements for small limited liability companies mean that persons dealing with these companies now have little meaningful information about their financial affairs; there is still a price being paid, but is it of any value? Shareholders in limited liability companies may limit their liability to a nominal amount and the company may have no material assets of its own, but will members of the public who trade with it necessarily know or care? If individuals were to limit their liability in a similar way (that is, in effect, to zero) we might question the point of having them disclose financial information or segregate assets.

Of course, individuals who wish to accept a substantial amount of liability might find it useful to provide some assurance about their creditworthiness or they might be required to do so by major creditors (just as directors and shareholders of limited liability companies may be required to provide personal guarantees or other kinds of assurance today). They may also wish to accept different levels of liability for different ventures.

5. The potential of partnerships and other associations of individuals

5.1 The power of association in the not-for-profit sector

Human beings are naturally sociable; we form associations with others in our private lives without second thought and with few rules or regulations. For many, the most important and fulfilling aspects of our lives are based around our families and friends or in not-for-profit sector associations such as clubs and societies.

In some cases these associations have no formal structure or form. Others may develop a structure (for instance, a governance structure and rules on membership) as they grow in size and may use legal forms, such as companies, within their structure for particular purposes.

For instance, **Park Run** is a not-for-profit organisation which uses a company limited by guarantee for certain purposes but also has features of an unincorporated association as it is largely run by volunteers drawn from those that participate in it and who are not members of the company. It was started in 2004 by a small group of friends and is now a global movement in which more than a million people have taken part. The parks used by this organisation are essential to its purpose. The first event was held in Bushy Park, one of the royal parks. These parks are managed by government and are required to be maintained for future generations.

Not-for-profit associations may also have a significant economic impact. For instance, the **Church of England** has assets valued at more than £6bn, annual expenditure of around £1bn and around a million active churchgoers, but rather than being one body with a centralised structure of administrative authority, function, control and direction, the Court of Appeal noted (in *Sharpe v The Bishop of Worcester* [2015] EWCA Civ 399) that the title 'Church of England' might be considered to denote 'an amalgam of ... an infinite number of bodies with no precise or clear picture ... of how the various jigsaw parts interact and fit together'.

5.2 Constraints on for-profit associations

As John Donne observed in the 17th century, 'No man is an island entire of itself; every man is a piece of the continent, a part of the main' and a sole proprietor and other forms of for-profit business will depend upon others, such as suppliers, customers, landlords, funders, family, and friends. Some may loosely refer to their important contacts as 'partners' in acknowledgement of a mutual interest.

There is, however, an issue where two or more persons carry on business together with a view to a profit because a specific type of partnership then arises. Under the Partnership Act (which dates back to 1890), partners are jointly and severally liable for partnership debts on an unlimited basis. This occurs by operation of law irrespective of what the partners themselves may agree (although partners will usually enter into a partnership agreement, which may alter the liability position between the partners). The very sort of associations that are so attractive in the not-for-profit sector are therefore discouraged where pursuit of profit is concerned.

This form of business is declining in popularity and it is perhaps time to question whether joint liability remains appropriate in modern times. 'Unlimited liability' of a partner (or, as noted above, a sole proprietor) does not of itself give assurance on creditworthiness; if no partner has material assets, then the partnership is not worth suing. Also, partners may be limited liability companies with few assets (and so not worth suing).

5.3 Potential of networks or associations of limited liability individuals

If individuals could limit their liability and could choose to what extent they would share liability with their partners and others, new forms of organisation for enterprise might evolve.

It is relatively easy to see that small groups of individuals could form businesses with assets being shared between them (as already happens in some cases, for instance in barristers' chambers or dental surgeries). Assets could be held on trust by one or more individuals for the benefit of others, the trust being a very flexible form and widely used in the not-for-profit sector.

The participants might agree between themselves a wide variety of inputs (such as time and labour, goods or money) and outputs (for instance, prototype products, future discounts, profits, fixed monetary returns or, indeed, no return but the satisfaction of having taken part) in a more flexible way than is readily offered through existing forms of business.

These small groups could equally form clusters with other small groups, or single very large networks of individuals might form, with varying rights and objectives reflecting the varied aspirations of the individuals concerned.

Large-scale associations or networks of this kind would, no doubt, face many challenges; the different and ever changing interests of participants could become very complex, like a living organism with an infinite number of cells that fade away and are renewed in an ongoing process. But, for the first time in history we may soon have the technology to allow us to monitor and control such interactions without the need for traditional institutions and intermediaries such as banks and stock exchanges. Some see potential in the blockchain (or 'distributed ledger'), enabling secure records of ownership to be created without central control (a concept underlying the Bitcoin).

6. Conclusion

We have suggested in this paper that forms of business are one of the foundations of an economy. While the UK has a wide variety of forms and might appear to be well served in this respect, each has its own limitations, and individuals wishing to pursue productive enterprise face constraints and complexities that may reduce productivity.

The limited liability company is an artificial person of our own creation. While it has served us well over the past century or so, we question whether it should have such a dominant role in the future. In particular, we suggest that legal reforms might usefully promote enterprises of natural persons.

It is difficult to know how networks of individuals might develop if they were to be encouraged, but if we continue along the path we have pursued over the past few decades – patching and mending existing forms of business when required – we run the risk that the cracks identified here may over time become chasms that will hinder the development of tomorrow's enterprise.

We invite readers to share their views on the issues raised in this paper. In particular, we are looking for feedback on the following questions.

- Do you agree that society of the future is likely to demand more flexible forms for enterprise, and what would be the advantages or disadvantages of offering more business forms?
- What role should listed companies play in the economy and are there alternatives?
- How should taxation interact with forms of business?
- Is regulation of forms of business effective in creating trust or is there scope to develop alternatives, such as professional assurance?
- Is one form of business more trustworthy than another?

We would welcome comments on this report and its conclusions; please send them to marketfoundations@icaew.com.

APPENDIX 1: Today's forms of business

A. An overview of the business population and the forms it uses

The government's **business population estimates** are stated to be the only official estimate of the total number of private sector businesses in the UK and their associated employment and turnover at the start of each year. The business population statistics also give an overview of central and local government businesses and non-profit organisations. According to these statistics, in 2015 there were almost 5.5m businesses in the UK engaging more than 30m individuals as employees or working proprietors.

UK business population – overview

	Private sector	Central and local government	Non-profit organisations	Total
Number of businesses	5.39m	11,790	78,060	5.48m
Number employed	25.87m	5.09m	1.94m	32.89m
Turnover	£3.71tn	£180.14bn	£80.91bn	£3.97tn

The for-profit private sector businesses are categorised into just three different forms: sole proprietorships, general partnerships and companies. This sheds little light on the relative importance of different types of company and does not cover all types of business (for instance, trusts) but the statistics provide a useful overview of the landscape as a whole.

Summary of main forms of for-profit business

	Sole proprietorships	Partnerships	Companies
Number of businesses using each form	3.33m	435,995	1.63m ('active' companies)
Aggregate number employed within each form	4.15m	1.79m	19.93m
Aggregate turnover within each form	£171.08bn	£101.63bn	£3.44tn
Number of businesses with 0–249 employees in each form	3.33m	435,940	1.62m
Number of businesses with 500 or more employees in each form	0	15	3,365

Note: estimates and methods of calculation may differ from those referred to elsewhere in this paper. Numbers of employed include sole proprietors, partners and sole employees of companies (who are treated as working proprietors) but these are not counted in numbers of employees. Figures have been rounded in both tables and may not sum to totals.

B. Forms of business in more detail

We now consider the three forms of business identified in the business population estimates in more detail, together with a number of additional business forms or analogous structures.

Sole proprietors

A sole proprietor is an individual who carries on business as an individual, with the assets and liabilities of the business generally being treated as personal ones. It is clear from the business population estimates that, while there are an enormous number of sole proprietors, their businesses are generally very small. Most sole proprietorships had no employees at all and more than 2.8m of them were not registered for PAYE or VAT; none had more than 500 employees.

Partnerships

A partnership (as opposed to, for instance, an LLP or limited partnership) is a business carried on by two or more people with a view to making a profit; a partnership in England and Wales (but not Scotland) is not a separate legal entity and partners are taxed on a personal taxation basis. There are relatively few general partnerships and, like sole proprietorships, these are with some exceptions shown to be small businesses, a picture reinforced by an Office of Tax Simplification [report](#) on partnerships.

Companies

By contrast, the company form is widely used by businesses of all sizes.

We have provided more information on the main forms of company in the table in section E, including estimates of the number of each of them.

Of these forms, the private company limited by shares and the public limited company (or PLC) are the most significant in terms of numbers of employees. These two forms are close relations and we refer to them collectively in this paper for convenience as 'limited liability companies' but it should be noted that they are not the only company forms to confer limited liability.

There are far more private companies limited by shares than of any other type of company (indeed, there are more of these companies than of all other types combined). Some of them are inactive (for instance, holding or dormant companies), and the government's [impact assessment](#) to its consultation on Transparency and Trust, April 2014 estimated that more than 1m have only one shareholder (being a natural person). A significant number are used as personal service companies which 'employ' just one individual who may also be the sole shareholder and director (and these companies may be used simply to obtain limited liability or tax treatment not available to sole proprietors). However, some are used for large business and have tens of thousands of employees. There is no inherent limitation on the size of this kind of company.

While the private company limited by shares and the PLC are close relations, only a PLC can be a listed company whose shares can be offered to the public and traded on open markets.

Listed companies are typically ranked in size by reference to market capitalisation rather than to number of employees or amount of turnover. It is possible for a company with a large market capitalisation to have fewer than 250 employees (for instance, the FTSE 100 company British Land PLC operated an outsourced model and reported fewer than 250 employees in its 2014 annual report). However, many of these companies are large by any measure. Some of the hundred largest (the FTSE 100) each employ hundreds of thousands of people and according to the [Quoted Companies Alliance](#) there are around 2,000 other listed companies quoted on LSE's main list, AIM or ISDX (commonly referred to as 'small and mid-size quoted companies') employing approximately 4.6m people.

While the two varieties of limited liability company have many similarities in legal terms, in practice, particular concerns arise in relation to listed companies where members of the public become investors (ie, shareholders) through trading on markets and shareholdings are typically more diffuse than for private companies limited by shares. These companies are, therefore, at the heart of much debate about the role of companies and big business in society and we comment further on them, albeit briefly, in section D.

Trusts

Trusts are not covered in the UK business population statistics and some might question whether they are a form of business at all, but they play an important role in our business structures. There is no fixed definition of a trust, but it is generally understood to involve a legal construct where property may be held and controlled by one or more people (the trustees or legal owners) for the benefit of others (the beneficiaries or beneficial owners). The trustee has various duties, including to keep trust property separate from the trustee's own property, and generally has unlimited liability. There is currently no public register of trusts (although anti-money laundering regulations provide for certain information to be held privately) and there is little official public data about them, but they are likely to be very numerous indeed as they arise in many areas of UK life (for instance, where marital property is held in the name of only one spouse for the benefit of both).

Trusts are used in a variety of business structures, including for pension funds, and can carry on substantial business activity. For instance, the **Wellcome Trust** is a charitable trust and is one of the UK's leading supporters of bio-medical research. Its trustee is a company limited by guarantee employing some 500 people in the trust (with more in subsidiary undertakings which include both private companies limited by shares and private unlimited companies).

Unincorporated associations

Individuals may participate in not-for-profit shared endeavour on a continuing basis through unincorporated associations such as clubs. These organisations have no legal personality and are not generally considered to be forms of business at all. They may be informal, with few rules and may have no tangible assets. Alternatively, they may have a formal constitution and management structure and may use assets provided by the members or others, for instance assets loaned to, or held on trust for, the association. There is no public register of all organisations of this kind but they exist in traditional forms, such as book clubs with physical meetings in many towns and villages and increasingly in a 'virtual' world with online associations between individuals. While many will be very small and not have any monetary turnover, there is no inherent limit to the size of these organisations and they may involve payment of money (for instance, through membership fees).

The state

The state provides goods and services and can reasonably be regarded as a form of business, indeed the NHS states that it is the **largest single employer in the UK** (and one of the top five in the world) and it performs a function that in some countries is largely in the private sector. But the state is not a single monolithic entity. State assets (and debts) may, ultimately, be owned by the UK population at large, but in terms of management, organisational and legal structures, there is a huge diversity. This ranges from national and local government, army divisions and NHS trusts to corporate bodies such as the Bank of England or The Financial Conduct Authority (FCA).

A business may be in the state sector one day and privatised the next, with little obvious difference in the conduct of the underlying business or from the perspective of its users – the privatisation of the Royal Mail in 2013 being a recent example. This resulted in a new FTSE 100 company with around 170,000 employees. While the largest privatisations have generally been made through listed companies and sale to the public, this privatisation included a substantial element of employee ownership.

State-owned businesses may also derive income from commercial operations and in some cases they are structured so as to distance them from direct government intervention: the BBC (a company incorporated by Royal Charter) illustrates both of these features.

Groups, hybrids and other complications

Of course, many businesses use more than one legal form. Groups of companies are common, some containing dozens of subsidiaries; the partners in a general partnership may be limited liability companies (so, indirectly, conferring limited liability on the ultimate owners); a UK company may own forms of business in other countries and vice versa; and mutual organisations and trusts may operate through companies of various kinds.

The LLP is itself a mixture of the general partnership and limited liability company forms (but is treated as a form of company in the government's business population statistics). Shareholdings in companies can be held in ways that affect the nature of the company itself. For instance, a single individual might own all the shares in a large company and, in effect, operate it as a personal fiefdom. On the other hand, the shares in a company may be held on trust for employees and, if all the shares are held in this way, the company becomes a type of mutual organisation. John Lewis is a notable example of this.

A business may form joint ventures or collaborate in ways that can affect its nature as much as any form it has chosen to adopt. It may, for instance, outsource its activity so that it supports employment in other businesses rather than employing those people directly. It may franchise its business model, thus growing its brand and income through endeavours of independent businesses.

The subject of forms of business is further complicated by some popular misconceptions. For instance, charities, banks and mutuals are sometimes referred to as if they were themselves legal forms of business but this is not the case. A charity can be carried on through a variety of forms, including trusts, unincorporated associations, companies limited by guarantee and, more recently, CIOs. Currently a charity may, or may not, be registered with the Charity Commission (most English universities, for instance, are not registered). Similarly a bank (being a business which takes deposits from the public) may adopt one of a number of forms. Many are listed companies but not all. Co-operative societies are a specific form of business but a mutual is not in itself a legal form – the term is generally understood to mean a form of business owned by its customers, suppliers or employees, or a mixture of these where there is a shared community purpose. Mutuals can be carried on through various forms, including the limited liability company.

The position in the UK is further complicated by different laws in different parts of the UK. While the CA 2006 applies to the UK as a whole, Scotland has its own legal system and devolution results in some fragmentation in related areas, such as charity regulation. This paper focuses on UK-wide forms of business, where applicable, or the position in England and Wales, in other cases.

C. Key features of the various forms

While there are many different forms of business, they are, in essence, each built from just a handful of building blocks.

The limited liability company, for instance, has the following key features:

- legal personality separate from its owners and managers (the directors) and so the ability to own assets and sue and be sued in its own name;
- limited liability for its shareholders (and, in effect, directors);
- ability to raise capital through issue of shares representing ownership interests;
- shares that are transferable without affecting continuity of the company;
- capacity to conduct a range of activities akin to that of an individual;
- legal segregation of roles between its shareholders and directors; and
- formal legal requirements, including to keep and file accounts and registers of shareholders and directors and, in some cases, to hold general meetings and to undergo external audit.

Other forms may have some, but not all, of these characteristics and the choice of form by any business will largely be determined by reference to these factors (as well as broader external factors, such as tax treatment).

Whether or not a particular characteristic is considered a strength or weakness may depend upon the particular circumstances and, in some cases, is a matter of subjective judgement.

The following table shows how these building blocks are assembled in selected forms of business.

Form of business	Separate personality	Limited liability	Transferable shares	Broad purpose	Perpetual existence	Separate management requirements	Formality and disclosure
Sole proprietor	No	No	No	Yes	No	No	Low
Partnership	No	No	No	No (for profit)	No	No	Low
Limited liability company	Yes	Yes	Yes	Yes	Yes	Yes	High
LLP	Yes	Yes	No	Yes (but formed for profit)	Yes	No	Medium
Trust	No (but trust assets held separately)	No	No	No (purpose required to be identified)	Depends (rules apply to non-charitable trusts)	No	Low

D. Perspectives on listed companies

Given the importance of listed companies to the economy, any concerns about the form are particularly significant. It is beyond the scope of this paper to examine the potential issues in detail, but there are a variety of opinions about how these companies should operate and how they should be regulated. We have outlined in somewhat simplistic terms two broad schools of thought on this. While many people will have mixed views about some of these matters, here lies a dilemma for the listed company: it is being marketed to the public at large but cannot be all things to all people.

A traditional view	A social view
<p>The listed company is simply a variant of the private company limited by shares – it is owned by its shareholders and is collectively their private property.</p> <p>Unless otherwise stated, the purpose of the company is to make profit for shareholders, through dividends and capital growth. Matters of general public interest can be addressed through general laws, such as employment or environmental law.</p> <p>The shareholders have power to set the objectives of the company and the directors are required by statute to manage the company to meet those objectives, having regard to matters required by statute in doing so (see ‘Directors’ duties’ on p13 for more detail).</p> <p>If shareholders are ‘unengaged’ that is their choice and they should accept the consequences (unengaged shareholders are ones who do not exercise their voting rights or monitor the directors or do not actively assess whether or when to trade in the shares). Inexpert members of the public who choose to engage (for instance, participating in AGMs) are unlikely to sway an outcome but do add to the costs of administration.</p> <p>While proportionate regulation is necessary to contain risks of fraud or other abuse of shareholders/public investors in connection with the issue and trading of shares, levels of regulation (or quasi-regulation) are no longer proportionate and risk turning listed companies into vehicles for social change irrespective of shareholder priorities.</p>	<p>Most listed companies are so widely owned, or their impact on society is so extensive, that they should be treated, in some respects at least, as being publicly owned.</p> <p>Listed companies can, and should, be used to bring about social change, for instance regarding increasing female representation on boards or reporting on environmental issues.</p> <p>The matters to which directors are to ‘have regard’ in performing their duties require them to look beyond profit-making objectives.</p> <p>Unengaged shareholders are frequently members of the public akin to consumers and should be protected from at least some of the consequences of their investments. It is to be assumed that these unengaged shareholders seek to promote the long-term health of the company rather than pursuing short-term gain.</p> <p>Regulation (or quasi-regulation) is required to protect unengaged shareholders against those with short-term interests, such as institutions trading on an automated basis to profit from short-term movement in share prices and ‘activist’ shareholders seeking to push up the share price before selling (including, potentially, by courting takeover bids). Directors are also susceptible to short-term thinking, for instance their remuneration may be linked to the share price.</p>

Of the two views described in the table, it is perhaps the social view which is more influential today in terms of regulatory or quasi-regulatory initiatives. In particular, The **UK Corporate Governance Code** deals at some length with corporate governance issues including on independent directors, director remuneration and audit committees, and the **UK Stewardship Code** seeks to increase institutional shareholders' engagement in relevant companies.

As a matter of company law, directors' duties are the same for listed companies as for private limited liability companies and the dilemmas of the listed company arise not so much from the form itself, but the use to which it is being put and the market infrastructure that has grown up around it.

Directors' duties

Since 2006, directors' duties have largely been contained in codified form in the CA 2006. In brief, this provides that a director must act 'in the way he considers, in good faith, would be most likely to promote the success of the company' for the benefit of its members as a whole. In doing so, 'he must have regard to' a number of specific matters, including the long-term consequence of any decision, the interests of the company's employees and the impact of the company's operations on the community and the environment. Where the company has purposes other than the benefit of its members, then the duty applies to achieving those purposes. There are other duties including the requirement to use reasonable care, skill and diligence and to avoid conflicts of interest.

While the listed company is unique in having such widespread public shareholdings across many different businesses, the challenges it faces in terms of needing a clear purpose and good governance are not; these issues can be expected to arise wherever ownership is diffuse. For instance, the **Myners report, 2014** found that the directors of the Co-operative Group had failed to act in the interests of the society and that the potential for conflicting interests was particularly troublesome where the purpose of the enterprise itself was not always clear: 'some want a dividend, some want low prices, some want to do social good and some want free-range chickens'.

Directors' duties: co-operative societies

According to the Myners Report, 'Directors of co-operatives must act in the best interests of the society having regard primarily to the interests of its members. Directors must balance long- and short-term interests and consider both present and future members. They should also bear in mind that the nature of a membership interest in a co-operative (like any mutual organisation) is primarily an interest as a customer or user of its services, and secondarily an interest as an owner. This is different from the nature of a member's interest in a company, and is an important factor in shaping the directors' duties. Directors of a co-operative society must consider the interests of society members generally, and not just a section of them.'

Concerns about short-termism are not limited to organisations whose shares are traded on markets. Of all forms of business, the state might be expected to take a long-term view in the public interest but it is, in practice, often driven by short-term political imperatives.

A number of 'solutions' to the issues for listed companies have been proposed, including that share classes should be created with enhanced rights for long-term holdings or that long-term objectives of companies should be entrenched through a trust mechanism (see, for instance, Colin Mayers' *Firm Commitment* (2013)). These are, however, predicated on assumptions about the wishes of unengaged shareholders. An alternative approach might be to assume that unengaged shareholders are not interested in exercising full shareholder rights and should, therefore, not hold voting shares (or pay what is likely to be a premium for having voting rights compared to non-voting shares).

E. Main forms of company

The following table summarises the main forms of company available to UK businesses today. Unless otherwise stated, the statistics are taken from the Companies House (CH) annual breakdown of the [total register](#) (which includes companies in the process of liquidation or dissolution) for the year to 31 March 2015.

Type and number of company	Key characteristics
Private companies limited by shares (3.31m)	Incorporated under the CA 2006 and registered at CH. See also section C of Appendix 1.
Private companies limited by guarantee (138,332)	Incorporated under CA 2006 and registered at CH. This form is similar to the private company limited by shares, but capital from members is only paid on winding up rather than being for use by the company. The form is largely used for not-for-profit businesses, many of which are very small.
LLPs (59,996)	Incorporated under the Limited Liability Partnership Act 2000 and registered at CH. An LLP has a separate legal personality, limited liability for members and public filing requirements, but its members are responsible for managing the business as they see fit (with no requirement for directors). The form is widely used by professional services firms, with the four largest UK accounting firms having many hundreds of members (or partners) and tens of thousands of staff.
Limited partnerships (33,060)	A form of partnership conferring limited liability on 'limited' partners who do not take part in management of the partnership. Established under the Limited Partnerships Act 1907 and registered at CH. Largely used for investment purposes.
CICs (11,196) (of which 78% were companies limited by guarantee and 22% limited by shares)	These are CA 2006 companies subject to additional restrictions on asset distribution and required to provide a community benefit. Regulated by the Regulator of Community Interest Companies. A CIC cannot be a charity. Some spin-offs from the NHS have been into CICs. The statistics on this form are taken from the regulator's operational report for the first quarter of 2016.
Overseas companies (11,159)	Foreign companies operating through branches or 'establishments' in the UK are governed by the laws of the country in which they are incorporated and may have different characteristics to the UK companies considered in this paper.
Co-operative and community benefit societies (previously known as industrial and provident societies) (10,133)	Incorporated under the Co-operative and Community Benefit Societies Act 2014 (which consolidated earlier statutes) and registered with the FCA. They must serve a co-operative or community interest purpose and not have distribution of profit to members as their main objective. They are also expected to provide for one member one vote or other 'democratic' voting rights (for instance, based on amount of use of the society) rather than votes linked to capital investment. The Co-operative Group had some 8m members in 2014 and was, and remains, the largest UK co-operative society (and, indeed, the largest mutual business of any kind in the UK).
Public limited companies (7,532)	Incorporated under the CA 2006 and registered at CH. The form shares the main characteristics of the private company limited by shares. It is, however, able to offer shares to the public and there are some other differences. For instance, the PLC has a minimum share capital requirement (£50,000 of which a quarter must be paid up) and tighter restrictions on reduction of share capital than is the case for a private company limited by shares.
CIOs (6,500 approx.)	These have a separate legal personality and limited liability. Created and registered with the Charity Commission under the Charities Act 2011 (with no additional requirement to register at CH). A CIO can only be for a charitable purpose. Most are small. The number of CIOs is taken from the government's consultation of April 2016 on reform of the process to convert to CIOs.

Type and number of company	Key characteristics
Private unlimited companies with shares (4,931)	Incorporated under the CA 2006 and registered at CH. These companies have a separate personality and unrestricted purposes, but shareholders have unlimited liability (and there are fewer reporting requirements than for limited liability companies). One example is Hoare & Co , which is a bank and refers to its directors as 'partners'.
Friendly societies (1,258)	Unless pre-existing, incorporated under the Friendly Societies Act 1992 and registered with the FCA. May be incorporated or unincorporated (if pre-existing) and must provide on a mutual basis for insurance against loss of income arising out of sickness, unemployment or retirement. The largest friendly society is LV= which has over 1m members and more than 6,000 staff. The number of friendly societies is taken from a search as at June 2016 of the PRA's register of organisations listed under the categories in the Friendly Societies Act 1974 and Friendly Societies Act 1992.
Assurance companies (929)	Assurance and insurance businesses carried on through various forms (and regulated by the FCA).
Royal Charter (850)	Incorporated by Royal Charter rather than under a general act of parliament such as the CA 2006. The objects and constitutional framework of a Royal Charter company are set by the charter. Where not carried on for the acquisition of gain by the body or its individual members, it may be exempt from various filing obligations that apply to registered companies. ICAEW is an example of this form of company; it has more than 700 staff and 145,000 members.
Investment companies with variable capital (inc. umbrellas) (642)	An investment vehicle formed under the Open-Ended Investment Company Regulations without fixed capital and regulated by the FCA.
Credit unions (500)	Registered under the Credit Union Act 1979 and required to make returns to the Prudential Regulatory Authority. In aggregate these had around 2,200 employees in 2013. They are not-for-profit co-operatives owned and managed by their members who have some common bond such as employer, sector, location or faith. The number of credit unions is taken from the Bank of England's quarterly statistics to December 2015.
European Economic Interest Groupings with head office in UK (279)	An unincorporated association. It has an independent legal personality, taking a similar form and being recognised in all EU jurisdictions. It must have members based in at least two countries within the EU or the European Economic Area, and be non-profit making.
Special acts of parliament (45)	These are bodies established by acts of parliament, as opposed to under general statutes such as the CA 2006. They typically have no shareholders and the powers and constitution will be set out in the act. Examples include the British Museum .
Building societies (44)	Incorporated under the Building Societies Act 1986 and registered with the FCA. The principal activity of a building society is to make loans secured on residential property. The largest building society is Nationwide which has around 15,000 employees. The number of building societies is taken from a report of the Building Societies Association of May 2016.
European Public Limited Companies (Societas Europas) (43)	A form of public company introduced by the EU, with separate legal personality and share capital. It can have either a single or two-tier board structure. Formation of an SE requires involvement of companies from at least two member states. There must be an arrangement in place for involvement of employees. Various aspects of UK company law apply to SEs whose registered office is in the UK. According to information provided by the European Trade Union Institute , only a small fraction of SEs in Europe are understood to have more than five employees.

APPENDIX 2: Forms of business – regulation and trust

A. Form and regulation

The rule of law is traditionally regarded as one of the foundations for a trusted business environment. Without it, the distinctions between one form of business and another would become meaningless (for instance, a limited liability company depends upon courts upholding the concept of limited liability and recognising a company as a 'person').

But the legal environment for business has become so complex that it is questionable whether the average citizen can be expected to navigate through the rules without professional assistance (and resultant cost). According to the Law Commission (in a [2010 consultation paper](#)) many more regulatory offences were created in the 19 years between 1989 and 2008 than in the 637 years before. There is little to suggest that the position has improved since.

For instance, on top of the already lengthy CA 2006, new requirements, with criminal sanctions for breach, have been added for companies to keep a register of significant controllers. These requirements are contained in around 30 pages of amending legislation, more than 100 pages of implementing regulations and more than 100 pages of statutory guidance and unofficial guidance. This impacts not only those with a direct interest in a company (such as directors and shareholders) but anyone who might have significant influence over it, like family members. Recent efforts to cut red tape have had limited success: no sooner is one thread removed, than a new reel appears.

It is difficult to see how a 'mend and make do' approach to our forms of business will alleviate concerns about legal and regulatory complexity because each change appears simply to add another layer of regulation. However, if businesses of individuals and networks of individuals were to be encouraged, it seems that a simpler legal regime would need to evolve around them. After all, there is a limit to the sheer volume of regulation that any individual can realistically be expected to absorb while spending time on constructive pursuits. If the population at large were more involved in business activity, democratic checks might be more effective than they have been in recent times.

If there were to be a genuine will to reduce regulatory burdens, lessons might be learned from not-for-profit organisations that have been able to operate on a large scale with very few rules (Park Run for example, has just a handful of rules or principles, one of which is to be considerate to other park users) or from codes that have worked for masses of individuals (such as the Highway Code, which has generally been effective in identifying key issues required to enable millions of individuals to navigate our roads relatively safely).

B. Form and trust

There has been a great deal of commentary about lack of trust in 'big business' in the shape of the listed company, but it is doubtful that any form of business involving human beings is completely trustworthy, whatever its purpose or objective.

Financial failure has occurred not only in listed banks but also in building societies, credit unions and assurance companies. A steady stream of directors of small insolvent limited liability companies are disqualified each year for wrongful or fraudulent trading (or other misconduct) and thousands of individuals, a proportion of whom will be sole proprietors, are declared bankrupt. The amount of fraud in charities is causing concern and there have been cases of child abuse and money laundering in religious organisations. In the state sector, our politicians have from time to time failed to live up to the high levels of probity that we might wish and the level of fraud within the NHS is believed to be significant, as the Centre for Health and the Public Interest found in its [2013 report](#).

We cannot suppose, therefore, that the sort of networks or associations of individuals envisaged in this paper would be inherently more trustworthy than existing types of business. It is tempting to think that we can trust individuals we 'know' and that somehow modern society is more exposed to fraud and unethical conduct than in olden times, when there were local markets and dealings took place face to face. Indeed, even the most modern of businesses can hark back to such times with seeming nostalgia (albeit at the same time employing modern techniques to create trust), as illustrated by the following extract from Airbnb's commentary on its branding:

' ... But after the mechanization and Industrial Revolution of the last century, those feelings of trust and belonging were displaced ... We also stopped trusting each other. And in doing so, we lost something essential about what it means to be a community. After all, our relationships with people will always be the most meaningful part of our lives. You just need to get to know them ... At a time when new technologies have made it easier to keep each other at a distance, you're using them to bring people together. And you're tapping into the universal human yearning to belong—the desire to feel welcomed, respected, and appreciated for who you are, no matter where you might be.'

Yet history is littered with cases of fraudsters and quacks and some of the greatest frauds have been committed by individuals 'known' by those they have defrauded. Mr Madoff is a notable example – 'This was a man who didn't care what he did to his friends', according to one of his victims in 2009, as [reported by the Wall Street Journal](#).

We cannot be completely insulated from the risks of dealing with others and neither, we suggest, would it be healthy for us to lead, or even wish for, 'risk free' (or untrusting) lives. Individuals who participate in the new 'democratic' forms of business activity such as crowdfunding are engaging in something with a high degree of risk compared to, say, putting money on deposit (although less risk of loss than, say, gambling in a casino), but an economy without risk takers is likely to stagnate.

Nevertheless, if an enterprise wishes to raise finance or grow, it helps to be trusted. Networks or associations of individuals will face challenges in this area, as do existing forms of business.

It may be that technology will permit us to 'know' individuals (or at least, their transactional behaviours) better than we could at a personal level. For instance, online rating systems allow two-way feedback and may result in a large volume of 'transparent' information about users. However, tools of this kind may be susceptible to manipulation and there is a dark side to the power of crowds in social media, for instance through cyberbullying. More traditional forms of creating trust may therefore continue to be relevant. Modern equivalents of medieval guilds may undergo a renaissance and 'trusted professionals' may be asked to provide new types of assurance, for instance on the creditworthiness of 'limited liability individuals', essential contractual terms and entitlements arising from associations of individuals, or the appropriateness of automatic controls provided by technology.

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Chartered Accountants' Hall Moorgate Place London EC2R 6EA UK

T +44 (0)20 7920 8450

E marketfoundations@icaew.com

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