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UNDERSTANDING LIMITED LIABILITY PARTNERSHIPS IN THE SMALL AND MEDIUM-SIZED BUSINESS SECTOR

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EXECUTIVE SUMMARY

This research study provides insights into the use of the LLP form and how a legal form designed to address potential liabilities arising from negligence claims (mostly against auditors) has been widely (and, perhaps, unexpectedly) utilised in small business and new venture creation. Although there is an extensive body of academic literature on the setting up and development of small and medium-sized enterprises in the United Kingdom, studies do not typically address the legal form that SME enterprises adopt. The importance of legal form as a 'set-up' mechanism and a means of structural growth of SMEs has, therefore, largely been overlooked in the UK academic literature and in the majority of studies reference is made to 'business ownership' as if all business types are the same. Very little distinction is made on the basis of legal form adopted by SMEs and where studies do exist on the LLP as a vehicle for growth, there is conflicting evidence about the meaning and relevance of the LLP for the small business sector. This research examines, therefore, the take-up, meaning and relevance of the LLP format for the small and medium-sized business sector. More specifically, the objectives of the study are to:

1. Undertake an analysis of the distribution and sectoral breakdown of LLPs in the UK, and thus establish the extent of the small and medium-sized business sector (initially taken to be all registered LLPs employing up to 250 personnel – but see later).
2. Ascertain the extent to which businesses in the SME sector (whether previously sole traders, traditional partnerships or companies) have converted to the LLP form or not; to explain the growth in number of LLPs registered; and to determine whether this is because of conversion or new registrations and whether use of the traditional partnership has declined as a result.
3. Identify the factors which are relevant to new and existing SMEs in deciding which is the most appropriate form to adopt; and to identify the factors underlying decisions to adopt or not adopt the LLP form.
4. Assess whether the LLP form has encouraged greater economic activity/likelihood of starting a business.
5. Classify the characteristics of SMEs (whether they are home-based, couples working together; family businesses; professional LLPs; financial/legal LLPs; non-financial LLPs; size of businesses; how roles are distributed in LLPs).
6. Categorise different forms and types of LLPs within the SME sector.
7. Evaluate the tax benefits and tax incentives associated with setting up an LLP, and the effectiveness of LLPs (in assuring security to the partners and in terms of cost of set-up and maintaining the form), compared with other legal forms.
8. Assess the accountancy and advisory needs of LLPs per se and through any 'transition' stage, to determine whether they are (perceived as) different from other legal forms.

The study of LLPs in relation to SMEs is important because some criticism was levelled at the government as a result of the introduction of the Limited Liability Partnership (LLP) form (established by the Limited Liability Partnership Act 2000), as it was perceived as allowing accounting firms[1] (and also law firms) to create a business form which would enable them, through limited liability protection, to side-step their responsibilities for negligent activities and thus protect the personal assets of partners from liability arising out of professional negligence claims. As certain professional firms were not allowed to operate other than as partnerships and these partnership formats failed to protect the personal assets of partners, this issue was of great concern. It is commonly perceived that the new form of the LLP is distinctive in that it affords a measure of protection akin to that provided to shareholders of limited liability companies. In practice, however, the LLP has become a legal vehicle that is accessible and appealing beyond accountancy and professional firms. In particular, the LLP form has become attractive to the small and medium-sized business sector in that it provides more protection than a standard partnership and avoids some of the reporting requirements of incorporation, but by no means all (see Appendix 1). Until now, however, no systematic research has been undertaken to evaluate the wide scale adoption of the LLP and the effectiveness of this form for meeting the needs of small and medium-sized businesses. Although there is extensive empirical work on the management or business development of SMEs, the legal form of business adopted has never been a main focus. Also, although various studies have discussed the expected impact of the LLP on firms since its adoption, there is little or no empirical work into the impact of the LLP form with particular regard to the organisation, function and growth of SMEs.

1 PricewaterhouseCoopers was one of the leading protagonists among the then Big Five firms which particularly lobbied for the change in law to allow LLPs to be set up. (The other firms were KPMG, Ernst & Young, Deloitte & Touche and Arthur Andersen, now the 'Big Four' after the demise of Arthur Andersen in the wake of the Enron débâcle.)

Prior to implementation of the LLP (2000) legislation, it was expected that approximately 15% of all professional partnerships (90,000) would become LLPs in 2001 (Payne, 2000). This would equate to 13,500 LLP registrations, although this growth did not materialise with the immediacy expected. Since 2000, the LLP has experienced slower but significant growth (from 4,500 in 2002/3 to 24,555 in 2007 with 40,240 active LLPs evident in March 2011). This compares with a decrease in the number of non-limited partnerships from 568,000 in 2002/3 to 480,000 in 2007; and 407,000 in 2011).[2] At a first glance, this seems to suggest that limited liability has been a strong incentive for new firm creation. As highlighted by McCahery et al. (2007), three factors are important for influencing new firm creation: (1) private ordering;[3] (2) fiscal transparency; and (3) limited liability. In spite of this growth in use of the LLP, little is known about the composition and distribution of LLPs across size or sector categories, or the rationales underlying decisions to adopt the LLP form. The extent to which these LLPs have converted from the traditional partnership format or whether they are new registrations of businesses is unclear. In addition, it is unclear whether, in practice, the rise in the take up of LLPs may nurture a culture of suspicion towards firms which might otherwise have been viewed as catalysts for employment creation and economic growth.

In this report, the distribution and character of LLPs in the UK is revealed using the Financial Analysis Made Easy (FAME) database which is compiled from the financial data supplied by firms in the UK to Companies House. Use of the FAME database to analyse LLPs has not been undertaken hitherto. As many small LLPs are exempt from supplying detailed data, two criteria have been applied to assess the prevalence of SMEs in LLPs. First, the balance sheet total (BST) is used to identify SMEs. From the FAME database, it was identified that of the total active 40,420 LLPs, BSTs could only be derived for 23,709 LLPs (of this 21,086 were small firms; 1,642 were medium firms; and 981 were large firms). This meant that over 16,000 firms could not be classified according to size using BST. For this reason, it was decided to use an additional criterion to identify SME LLPs. This was: 'number of partners' in the LLP.

Using this search term, it was identified that the analysis of firms by reference to number of partners with and without BST showed a clear correlation with regard to numbers of partners. For both categories, having two partners was the most common form, with a slightly higher prevalence (16%) in the non-BST category of LLPs. Thus, of the total active LLPs on the FAME database, we find that all the non-BST LLPs are small firms (16,840 or 41.9%) and (22,728 or 56.5%) BST LLPs are SMEs. In summary, therefore, of the active LLPs listed on the FAME database, 98% are small and medium-sized LLPs. The high number of small LLPs is significant because, as stated above, the LLP was not a vehicle specifically designed with SMEs in mind (see Finch and Freedman, 1997; Freedman and Finch, 2002; Henning, 2004).

The analysis of the FAME database and categorisation of LLPs according to size and number of partners enabled a stratified sample frame to be derived. Following a pilot stage of questionnaire development with 40 selected LLPs, a survey was sent to 3,500 firms. In addition, follow up interviews were undertaken with 30 LLPs and advisory organisations and support organisations. The questionnaire was administered by a first contact letter inviting them to complete the questionnaire via a link on the project website to Survey Monkey. The survey focused on the reasons for choosing the LLP form over other legal forms and whether the LLP was a new registration or conversion from another business form. The respondent LLPs were analysed according to: number/roles of partners, geographic location, industry sector (where possible), numbers of negligence claims, source of advice on becoming an LLP, advantages/disadvantages experienced as an LLP, burdens placed by LLP, information on profit sharing between partners. The follow-up interviews also addressed how sector networks shaped the decision to become an LLP, how an LLP constrains or enables growth, the intention to stay as an LLP or move to incorporation. Also, responses were sought on views of compliance with LLP legislation. Interviews were also carried out with professional advisory firms (accounting and law).

A questionnaire was also administered to a control group of non-LLPs. The objective of obtaining data from non-LLPs was to provide some comparison with LLPs in terms of reasons for using a different form. As the focus of the project was on why there was an apparently high take-up of the form in the SME sector, asking questions of firms which did not adopt it aimed to shed further light on the decision-making process.

As well as finding evidence of existing accountancy and legal firms converting to the new form, evidence can be found of firms operating in other industry sectors adopting the LLP form, both by converting from another form and setting up from scratch. This suggests that the availability of the form has encouraged new economic activity. It has been difficult to assess the

2 For limited companies, the number has increased from 1.6m in 2002/3 to 2.3m in 2007 and levelled out at 2.3m in 2011.

3 The sharing of regulatory authority with private actors and non-governmental groupings.

sectoral distribution of LLPs because it is not compulsory for LLPs to state the Standard Industrial Classification (SIC) when returns are sent to Companies House, but 15,103 LLPs indicate a spread across a wide variety of business activity with service firms appearing most numerous – and located with different degrees of density across the UK. The majority of LLPs are located in London (37%) and the South East (17.3%), which is not surprising, given that this is a recognised centre for business and professional service firm activity (Sassen, 2001; Dicken, 2003). The North East (1.9%), Wales (2.8%), and Scotland (5.4%), however, show small numbers of LLPs (with Northern Ireland showing only 13 active LLPs). Firms operated from both home and office, but very small firms (with turnover not exceeding £100,000) tended to be home-based, with a dedicated study in the home being the most common business location. Of the respondents, 81% of the respondent firms chiefly did business within the UK, most commonly within what might be termed their 'local area'. Only 8.8% and 8.9% respectively undertook business elsewhere within the European Union or outside the EU.

Of the respondents, 73% of LLPs were established during the 2000-2011 period (with 58 firms originally being established prior to 1990), suggesting a conversion over time. It is, perhaps, surprising to see that many firms did not convert immediately to the LLP form, but waited some years for various reasons. While wishing to take advantage of the protection to partners' assets offered by limited liability, there was a considerable range of different reasons offered for using the LLP form, not least tax advantages or the particular type of business operated, as well as evolution of business and some 'copycat' behaviour to keep up with competitors moving to the LLP format.

From the survey data, three types of LLP forms are identifiable: 1) as a special vehicle for collaboration between two or possibly more firms; 2) as a purely investment/tax strategy; and 3) for small, usually professional, partnerships (eg, family firms, small professional partnership firms such as solicitors, accountants, civil engineers, architects). For example, property holding companies extensively used the form and it has proved popular as a mechanism for various types of business and tax planning and use of 'self-employed' status. In terms of concern about negligence claims against individual partners as a motivating factor in setting up the LLP, the evidence presented was that this was not a motivating factor. Instead, adoption of the LLP was more of a precautionary action. Most firms also carried professional indemnity insurance, though this was not applicable in certain cases and there were firms who found it too expensive to take out.

For LLPs converting to the LLP format, or setting up initially as an LLP, 71 LLPs reported that they 'advised themselves' or used 'in-house advice' to do so (viable if the firm was a legal or accounting firm) or advice was obtained from an accountant (80 respondents) or solicitor (30 respondents). Of the respondents, 9% reported some disadvantages of the LLP format (less flexible than anticipated and/or compliance burdens). However, less than 3% of LLPs professed complete dissatisfaction with the LLP (one case) or were displeased with advice to adopt the LLP (one case). These reasons related to the perceived unsuitability of the LLP for SMEs (two cases) and misunderstandings about the implications of the LLP (as too bureaucratic or inflexible – two cases). An overwhelming majority of respondents reported satisfaction with the advice they had received, and with the way the LLP operated. It was clear that there was an added burden of legal compliance, however, which not all firms had anticipated but in general the form was regarded as a very flexible means of doing business, and relatively easy for partners to leave and join.

In terms of the different kinds of partnership types (ie, equity holding, fixed and salaried), equity holdings were most common. Profit sharing ratios ranged from an equal division between partners, unequal but fixed division and variable, determinable annually. It was also not uncommon for firms to have a corporate partner, with various reasons for its presence. Other firms, however, were not even aware of what a corporate partner was, suggesting varying levels of knowledge, sophistication and planning within LLP members of their advisers. Quite often the presence of a corporate partner was associated with the financing arrangements for the firm, though the majority of firms relied on assets provided by partners themselves or bank funding for their main forms of finance.

Finally, LLPs were also asked if their accountancy and taxation needs had changed over time, as a result of LLP status. Out of 149 firms which responded to this question, 95 firms said that their needs had not changed, with 54 saying that they had. The reasons provided for the changes were generally added complexity in meeting financial reporting and accounting requirements, and more specialist tax advice being needed because of the financial circumstances of individual partners or because individuals had become partners (rather than being sole traders). However, some of the reasons for changes were clearly because of business expansion, for example, growth in staff numbers and the need to register for VAT as turnover increased. Of the respondents, 51% reported that they outsourced their taxation and accountancy requirements, while 46% undertook these activities in-house.

The report concludes that the LLP could be conceived as a form of collective self-employment, where self-employed members group together to pool expertise and skills while retaining liability protection. In this sense, the LLP format, rather than being an expression of entrepreneurship in the traditional sense of the single owner-managed business, is instead an expression of distributed entrepreneurship. Such practices also challenge the traditional notion of organisational form. What some LLP formats seem to be representing are what Miller et al. (2008, p 942) refer to as 'hybrid' forms 'that make possible lateral information flows and coordination across the boundaries of organisations, firms, and groups of experts or professionals' (especially in cases where the LLP is set up as a special purpose vehicle).

1. HISTORY AND ADOPTION OF THE LLP IN THE UK

The concept of the LLP was first introduced in the United States, following the prosecution by governments of law and accountancy LLPs that had represented failed savings and loan organisations (Henning, 2000; 2004). As a result of an increasing susceptibility to litigation, audit firms lobbied US states from as early as 1991 for the introduction of the LLP (Bush et al., 2007; Blair, 2008). Within the UK, the process of achieving the creation of the LLP took longer and was more complex. First, the UK introduced provisions under the Companies Act 1989 which permitted audit firms to incorporate as companies (Bush et al., 2007). Even so, this meant additional tax liability, compliance with the provisions of company law and publication of financial statements for companies (Finch and Freedman 1997; Bush et al., 2007). Second, Jersey introduced its own LLP (see Sikka, 2008 for an analysis of this) which did not require LLPs to publish their accounts and this pressurised the UK government into introducing the concept of the LLP to the UK in 2000 (Bush et al., 2007) in order to avoid the risk of UK LLPs moving their headquarters to Jersey, although it was argued this would be unlikely in practice (Finch and Freedman, 1997).

The UK LLP was introduced, therefore, following intense lobbying by some of the largest global accountancy, audit and legal partnership practices. Hence, the form was created with large professional partnerships in mind (Finch and Freedman, 1997) and this assumption continued to provide the main impetus shaping the new vehicle (Freedman and Finch, 2002, p478). An LLP was to take the form of a body corporate with separate legal personality and unlimited capacity (ie, it could do anything that a natural person could do). In view of this, the LLP is able to hold property and continue in spite of potential changes to its membership (Freedman and Finch, 2002).

The key elements of the LLP, as outlined by Payne (2000, pp1–2), include the following:

1. In cases of negligence, the innocent members of the LLP will have their liability limited to the extent of their stake in the firm (although the liability of the firm and the negligent partner will be unlimited).
2. Members of the LLP are agents, but the LLP is not responsible for members' actions where the member has no authority to act for the LLP and the third party is aware of this or does not know that the person is in fact a member of the LLP.
3. A person will cease to be a member on death, the dissolution of the LLP, or by agreement with the other members.
4. The LLP must be registered with the Registrar of Companies, with details including its name, its registered office, a list of its members, etc. These details must be kept updated.
5. An LLP must file an annual report and accounts at Companies House akin to that required for companies.
6. The LLP will be taxed as a partnership.

The regulations governing LLPs are set out briefly in Appendix 1.

In terms of take up of this legal form, it was suggested that approximately 15% of all professional partnerships (90,000) would become LLPs in 2001 (Payne, 2000). This would equate to 13,500 registrations. However, as Table 1 shows, the take up of the new legal form did not materialise as expected. There is considerable growth in LLPs, but it comes much later.

Table 1: Numbers of business entities

Date	LLPs	Non-partnerships	Companies limited by shares
2002–03[4]	4,500	568,000	1.6m
2007	24,555[5]	480,000[6]	2.3m[7]
2008	32,066[8]	474,000[9]	2.4m[10]
2011	40,482[11]	407,000[12]	2.3m[13]

There has been a substantial growth in LLPs since 2002–03, with a gradual decline in numbers of non-partnerships, although company numbers appear to have reached equilibrium. Of these (active) LLPs, 21,040 are small LLPs and 1,640 are medium-sized LLPs.[14] On the surface, this seems to suggest that limited liability has been a strong incentive for new firm creation. This is highlighted in a study by McCahery et al. (2007) who comment on the ways in which policy-makers use new company law initiatives to encourage entrepreneurship, innovation and cooperative arrangements. They distinguish three important factors that influence the incentives for new firm creation: (1) private ordering; (2) fiscal transparency; and (3) limited liability. In terms of the large take-up in the number of LLPs in the UK, it does appear on the surface that the change in company law and introduction of the LLP has encouraged new firm creation, but what is unclear as yet is whether these registrations are new LLPs or conversions from other formats. For these reasons, the objectives of this research study are listed below.

4 All figures on this line, as per the Companies House Register, as shown in the DTi report, 2003, 'Companies in 2002–03'

5 As at March 2007, given by French, Mayson and Ryan, 2008, p9, and from the 'Statistical Tables on Companies Register Activities 2006–2007', Table E4, p23, from the Companies House website.

6 As at August 2007, from the 'smestats2006.xls' spreadsheet, Department for Business Innovation & Skills 'Small and Medium-sized Enterprises for the UK and Regions', archived at the National Archives. This document gives a total figure of 504,660 as an estimate for all UK partnerships, so subtracting the 24,555 LLPs, gives an approximate figure of 480,000. This can only be a very rough estimate as the figures are not compiled at the same date.

7 As at March 2007, from the 'Statistical Tables on Companies Register Activities 2006–2007', Table A1, p2, from the Companies House website.

8 As at March 2008, given by French, Mayson and Ryan, 2009, p11, and from the 'Statistical Tables on Companies Registration Activities 2007–08', Table E4, p25, from the Companies House website.

9 As at July 2008, from the 'smestats2007.xls' spreadsheet, Department for Business Innovation & Skills 'Small and Medium-sized Enterprises for the UK and Regions', archived at the National Archives. This document gives a total figure of 506,805 as an estimate for all UK partnerships, so subtracting the 32,066 LLPs, gives an approximate figure of 474,000. This can only be a very rough estimate as the figures are not compiled at the same date.

10 As at March 2008, from the 'Statistical Tables on Companies Registration Activities 2007–08', Table A1, p3, from the Companies House website.

11 As at March 2011, from the 'Statistical Tables on Companies Registration Activities 2010/11', Table E4, p32, from the Companies House website.

12 As at October 2011, from 'Business Population Estimates for the UK and Regions', Published Editions 2011, Detailed Data Tables', on the Department for Business Innovation & Skills website. This is a new and current version of the 'Small and Medium-sized Enterprises for the UK and Regions' document used for earlier years, but for which the calculation methodology for the number of business enterprises has been revised.

13 As footnote 9 above. This document gives a total figure of 447,060 as an estimate for all UK partnerships, so subtracting the 40,482 gives an approximate figure of 407,000. This can only be a very rough estimate as the figures are not compiled at the same date.

14 Definitions of 'small' and 'medium' firm are explained in the methodology section of the report.

2. RESEARCH OBJECTIVES

1) To undertake an analysis of the distribution and sectoral breakdown of LLPs in the UK, and thus establish the extent of the small and medium-sized business sector (initially taken to be all registered LLPs employing up to 250 personnel – but see later).
2) Following (1), to ascertain the extent to which businesses in the SME sector (whether previously sole traders, traditional partnerships or companies) have converted to the LLP form or not; to explain the growth in number of LLPs registered; and to determine whether this is because of conversion or new registrations and whether use of the traditional partnership has declined as a result.
3) To identify the factors which are relevant to new and existing SMEs in deciding which is the most appropriate form to adopt; and to identify the factors underlying decisions to adopt or not adopt the LLP form, (ie, what were the drivers behind individuals' decisions to adopt this form, especially whether differences in the nature of the business itself create different incentives to adopt it (eg, because a service business in which financial liability might arise, or for other reasons).
4) To assess whether the LLP form has encouraged greater economic activity/likelihood of starting a business.
5) To classify the characteristics of SMEs (whether they are home-based; couples working together; family businesses; professional LLPs; financial/legal LLPs; non-financial LLPs; size of businesses; how roles are distributed in LLPs).
6) To categorise different forms and types of LLPs within the SME sector.
7) To evaluate the tax benefits and tax incentives associated with setting up an LLP, and the effectiveness of LLPs (in assuring security and in terms of cost of set-up and maintaining the form), compared with other legal forms.
8) To assess the accountancy and advisory needs of LLPs per se and through any 'transition' stage, to determine whether they are (perceived as) different from other legal forms.

3. LLPs AND THE SMALL AND MEDIUM-SIZED BUSINESS

A study of LLPs in relation to the SMEs is important because, although there is an extensive body of academic literature on the setting up and development of small and medium-sized enterprises in the United Kingdom (eg, Hughes and Storey, 1994) which might include 'new' LLPs, this literature does not typically address the legal form that SME enterprises adopt.[15] Studies, instead, often focus on the provision of finance in relation to business size, age or sector (Michaelas et al., 1999; Beck, et al., 2005a; Beck et al. 2005b; Beck et al., 2006; Brewer, 2007; Beck et al., 2008; Han and Benson, 2010) or bank lending in relation to firm size (Berry et al., 2004; de la Torre et al., 2010). Size is also the key factor in a study by Malach et al. (2006) who examine the most frequently addressed legal issues for small LLPs which are noted as: (1) business format; (2) intellectual property; (3) liability; (4) regulation; and (5) contract. Studies emphasising legal form as a characterising feature are rare to find. Given that business format is the prominent legal issue for small LLPs, it is surprising that little research work has been undertaken in the UK where legal form is selected as a variable that determines some business behaviours (an exception here is Carter et al., 2004, although LLPs represent only 0.6 % (approximately 100 firms) of their sample.

This is further evident in the small but empirically robust body of research on the characteristics of small business entities in terms of novice, portfolio or serial entrepreneurship (Birley and Westhead, 1993; Westhead and Wright, 1998; Westhead et al., 2003; Westhead et al., 2005). These investigations are important for identifying the behaviours and characteristics of entrepreneurs as they come to their first business venture (novice), add new business entities to ongoing business arrangements (portfolio), or sell up/move on from one business to set up another (serial). The legal form is not explicitly acknowledged in these studies and yet the choice of legal form also reflects particular behaviours. The importance of legal form as a 'set-up' mechanism and a means of structural growth of SMEs has, therefore, largely been overlooked in the UK academic literature and in the majority of studies reference is made to 'business ownership' as if all business types are the same. Very little distinction is made on the basis of legal form adopted by SMEs. However, where studies do exist on the LLP as a vehicle for growth, there is conflicting evidence. In some, it is identified that adopting a limited liability form is a signal of a growth intention and orientation to innovation (Lu and Sexton, 1997; McCahery et al., 2007). In other studies, the LLP form appears not widely used by small businesses, though having a beneficial effect on employment growth (Carter et al., 2004). More specifically, from this study, it was found that LLPs, as a percentage, reported a 23% growth in FTE employment, the second largest percentage after franchised operations. Also, 23% of LLPs make use of retained profits (again following the category of franchised firms[16]).

In relation to taxation, there is a body of research emphasising taxation benefits and implications for SMEs. Here there is more explicit attention to the legal form adopted as a means of minimising tax requirements. In the UK context, for example, Crawford and Freedman (2008) examine taxation of small, owner-managed businesses focusing on the difficulties created by treating employees, unincorporated and incorporated businesses differently for tax and social security purposes. The authors are critical of 'tax incentives for small LLPs and differentiation between legal forms and concentrate on issues arising from opportunities created on incorporation for the conversion of income from labour into income from capital (taxed at a lower rate)' (p2). Instead, Crawford and Freedman (2008) argue for the alignment of the tax treatment of different legal forms. Also, in the US literature, *Gordon and MacKie-Mason* (1994) and *MacKie-Mason and Gordon* (1991) consider the economic perspective of tax distortions affecting the choice of incorporation over non-incorporation; and Guenther (1992) considers corporations and Master Limited Partnerships (MLPs) from a tax point of view, particularly examining the trade-off that exists between tax costs and transaction costs in the choice of form. It is evident that where there is involvement of LLPs with corporate structures, tax considerations can be very complex (James,

15 Exceptions are US studies by Gordon and Mackie-Mason (1994) who examine the choice of organisational form in relation to tax, and Guenther (1992), who compares corporations and Master Limited Partnerships from a tax perspective.

16 The use of retained profits in an LLP, however, is not characteristic of professional firms in the UK.

2009) but in general LLPs are now extensively used by holding, property and investment types of businesses for avoiding a double charge to tax on extraction of profits from companies. This was evident in the current study, where one asset management LLP was a collective of 51 LLPs utilised for investment purposes (see also Section 5.3).

The professional literature also focuses directly on the LLP form. Here there is a wide range of literature discussing the advantages and disadvantages of the LLP form (Henning, 2000; 2005; 2007; Lawson, 2000; Payne, 2000; Eaglesham and Peel, 2002; Ives, 2005; Lambe, 2005; Hancock and Cearns, 2006; Wilson, 2006). Many of these reports emphasise the practical aspects of LLPs: (i) how to set up an LLP technically (Morse, 2001); and (ii) whether the form is appropriate to LLPs in different sectors, for example, builders, vets and pharmaceutical LLPs (see also McQueen, 2001; Openshaw, 2002; Tittensor, 2003; Banks, 2006). The extent to which the LLP is relevant or useful to non-professional LLPs is a key issue for the current study because, as noted above, the LLP was not a vehicle specifically designed with SMEs in mind (Finch and Freedman 1997; Freedman and Finch 2002; Henning 2004). It emerged in response to concerns about 'non level playing fields between potential competitors for business' whether classed as professional or not (Finch, 2001, p899, cited by Freedman, 2001). Several authors in the professional journals (McQueen, 2001; Openshaw, 2002; Tittensor, 2003. Banks, 2006) demonstrate how LLPs are being taken up by non-financial professional LLPs, although it is unclear as to the extent to which traditional partnerships have converted. Some micro case studies of LLPs have been developed to examine how businesses are using their LLP form ab initio (Manolova and Yan, 2002; Lu and Sexton, 2006), but this has not been systematically or extensively explored. Indeed, evidence suggests that some LLPs changed to or adopted the LLP form in situations when it may not have been necessarily to their advantage to do so (Freedman, 2001). For example, Gripton (2004) and Wastie, (2004) also note that UK firms have been urged to adopt an LLP format because others had done so and to avoid recruitment problems. The professional accountants, when interviewed for this study, also confirmed that they had frequently seen cases of this.

It is unclear, therefore, whether LLPs are primarily financial or professional service entities as was common within the non-limited partnership form. Studies indicate that the new form would predominate in professional or service organisations (Moizer and Hansford-Smith, 1998) but, also as noted above, limited liability is thought to encourage new firm creation across all sectors (McCahery et al., 2007). This is because using the LLP form as a limit to personal liability is important for partners in businesses that provide a service during which 'things can go wrong' and where litigation is possible or likely, and so protection of personal assets is required. The LLP is attractive in these situations as the liability of members of the LLP for debts is limited to their share of assets in the partnership unless agreed otherwise by members or if a liquidator brings a claim for unlawful trading (Young, 2000). In other words: 'As the LLP is a body corporate any acts of its members are as agents for their principal. Therefore, it is the LLP which is liable for any debts and obligations. This protects the individual member from personal liability' (Blair, 2008, p3). The Act makes the assumption, therefore, that third parties will usually contract with the LLP rather than an individual member of the LLP (Freedman and Finch, 2002). Therefore, contractual liability will be with the LLP only (Freedman and Finch, 2002), although, in respect of professional negligence, liability falls to the individual partner and the LLP. It also means that 'litigants [are] no longer able to pursue the individual assets of all partners, [and] LLPs should be able to trade their way through any actions over legal liability' (Ives, 2005, p1).

The visible liability protection that the LLP affords, combined with the fear of litigation, has contributed to the take-up of LLPs and their prevalence within professional/service LLPs (although by August 2001, only 20% of LLP registrations were by solicitors and accountants[17]). It is not clear, however, whether the LLP registrations are entities that existed before the change of legislation but which converted to the new legal form after 2000. Also, it is unclear whether they have been set up 'from scratch' as the chosen form for a new business. For 'first time' or new LLP registrations, the change in the legal system regarding LLPs implies that there are greater benefits (in lower tax and National Insurance Contribution (NIC) costs) to be gained from the start for this type of legal business form. They are also beneficial for assuring personal protection to members and are flexible in their internal constitution with few restrictions as to their uses (Blair, 2008). This suggests that LLPs are not legal forms that sole traders or other partnerships migrate to over time as their business grows or consolidates, but are instead new start up entities. Such benefits would be attractive for newly incorporating LLPs regardless of size or sector. As pointed out by Ward (2001, p2), in view of the limited liability for the members, tax transparency and organisational

17 Freedman, 2001, p907 reporting a study by Jordans, 'Businesses are choosing new status', at jordans.co.uk/Jordans2.nsf/StatusTopyStory!OpenForum (last visited 29 September 2011).

flexibility, 'these features are likely to make them the vehicle of choice for many small and medium-sized enterprises (SMEs)'. Indeed, some commentators proposed that the LLP could become the dominant legal structure for small businesses (Lowe, 2000).

3.1 LLPs as an unsuitable vehicle for SMEs?

Freedman (2001), however, is highly critical of the potential of the LLP form for 'small trading businesses'. She argues that the LLP 'is an outcome of a political reaction to pressures which has brought forth a strange legal vehicle of restricted value for small LLPs' (p898). As a result, she claims that the LLP form 'is an unsuitable vehicle for most small owner managed, non-professional LLPs and its importance should not be exaggerated' (p898). Furthermore, in her view, having the LLP form also dilutes the case for creating a new corporate vehicle designed specifically for small firms. The main problem, Freedman (2001) states, is that 'the LLP was not designed in response to small business concerns' (p902) and, as a result, six major shortcomings of the LLP can be identified in relation to the smaller enterprise. These are summarised from Freedman (2001, pp902–904).

First, Freedman (2001) argues that because the LLP has a lack of rules on internal governance, this means that that it offers no standard form constitution and would, therefore, be expensive to set up for small companies. Second, in its adoption of [modified] company law, 'this has resulted in greater complexity and a set of provisions which are very difficult to use' (p903). Third, Freedman (2001) states that the LLP 'has extensive disclosure and filing requirements relating to the link between limited liability and disclosure in UK doctrine' (p903). Even though small LLPs are exempt from full disclosure of accounts, Freedman (2001) argues that 'lack of formalities should not be presented as an advantage for LLPs' (p903). Fourth, the LLP requires at least two designated members (whether individual or corporate) – something which is not always relevant to a micro owner-managed business. For this reason, Freedman (2001, p909) argues that for one-person LLPs, it is simpler to incorporate. Fifth, the LLP format offers tax reduction, but she points out that commercial decision making may be distorted in that the LLP provides tax savings because of capital gains tax differences and a lower rate of NICs for the members who would pay more as employees in an incorporated situation (see also Freedman and Finch, 2002). For small LLPs, Freedman (2001, p904) argues that 'the LLP may be disadvantageous from a tax point of view...compared to a sole trader or general partners as losses available for relief against general income cannot exceed the capital contributed by the member'.

Lastly, Freedman (2001) is critical of the limited liability protection and argues that there is still a great deal of ambiguity as to whether the LLP or the individual member would be responsible. In such situations, the court would need to consider 'various factors, including the assumption of personal responsibility of the member, reliance on that assumption by the client and whether that reliance was reasonable' (Freedman and Finch, 2002, p480). The Act leaves this area purposefully ambiguous, suggesting that this will be resolved via the judicial process. Garry and Wano (2007) report on the cessation of membership by a partner in an LLP. In the absence of a partnership agreement neither the Act nor the regulations set out the financial consequences of a cessation of membership. This resulted in litigation and dispute between the remaining partners and existing partner. Indeed, this raises a set of questions regarding how clients were dealt with or whether the partner personally signed letters (Freedman and Finch, 2002). Furthermore, the situation is made more complex in closely held LLPs where the directors and shareholders are one and the same (Freedman and Finch, 2002). In spite of limited liability protection, there is also concern that, in practice, large creditors might also contract around the LLP to hold individual members liable (for example, if creditors consider they are dealing with high risk LLPs (Freedman and Finch, 2002)). These authors go on to argue that banks may also see LLPs as financially more risky than a private limited company. This situation is complicated when analysing the relative size of creditors and the borrowing firms involved. In the case of small firms with minimal capital investment by shareholders, such as in small private companies, large creditors and others in contractual relationships could use sophisticated contracts to circumvent the limited liability protection by requesting personal guarantees and individual member contracts (Cressey, 1993; Freedman, 2000; Freedman and Finch, 2002). This bestows two benefits on creditors: first, the larger creditors with resources can protect themselves against the risk being shifted to them; and second, the risk is ultimately pushed on to 'trade creditors' and 'involuntary creditors' with fewer means at their disposal to negotiate suitable protection and return the risk (Cressey 1993; Freedman 2000, p332).

Furthermore, 'additional guarantees' may be demanded or advice given against adopting the form (Freedman and Finch, 2002, p489) 'despite the fact that there is intended to be an extra protection over and above that provided in limited liability companies' (p489). It is possible, then, that there is no additional practical benefit offered by the LLP form, which is not already provided by other legal business forms, so an LLP may or may not encourage economic activity or make it more likely that persons will start a business. Indeed, the emphasis that this form places on protecting partnership members (and in turn the knock-on effects of creditors' and contractual partners' attempts to protect themselves from risk) begins to raise questions as to the degree to which this legal form encourages investment and/or calculated risk taking. Conversely, rather than encouraging growth and risk taking, the rise in the take up of LLPs may, in practice, nurture a culture of suspicion towards LLPs which previously would have been viewed as catalysts for employment creation and economic sustainability.

In summary, there is no clear evidence as to the effect that the rules and regulations of the LLP may have on SMEs. For example, the fulfilment of specific bureaucratic demands could place an extra burden in terms of time and costs on to small LLPs which previously they did not have. At the same time, an important aspect of the LLP legal structure is that it offers the opportunity for such persons to become more visible as formal partners in the business as well as providing them with a measure of tax and legal protection for their risk-taking, and rewarding it with a share in due course of partnership profits (Young, 2000; Blair, 2008). This affords a degree of credibility with external stakeholders over sole trader or non-limited partnership. Also, as Carney (1999) comments, 'the principal advantage of limited liability is in encouraging investment by passive investors in risky enterprises, particularly where these investors are poor monitors of managers' (p659). As yet, however, there is little empirical evidence addressing such questions and giving consideration to the motivations behind LLP choices. An empirical study regarding choice of legal form for New York law LLPs was undertaken by Baker and Krawiec (2005). These authors found that choice of legal form is shaped by a variety of factors (limited liability, lower tax, etc.) but is also affected by the behaviour of similarly situated competitor LLPs. This is an interesting finding which implies the importance of 'copy-cat' behaviour deployed to gain a strategic edge over competition (Enkel and Grassman, 2010; Shenkar, 2010), rather than other benefits such as tax reductions. Furthermore, it is unclear if the LLP is being utilised as a business start-up vehicle for the purpose of establishing the business in the vulnerable early years with a view to converting to a limited company at a later stage if growth is achieved.

Moreover, no systematic research has been undertaken on the characteristics of LLPs to assess whether they are home-based businesses (such as couples working together, or involving family businesses) and/or their sector and geographical location. More empirical data are also needed on the size of LLPs in terms of the number of members, the roles the different members play and how these are defined. In contrast to Freedman's (2001) critical perspective, Birds (2000, p2) argues that LLPs can be used by a one-person business, provided that there is another member subscribing to the incorporation document and 'provided that the former could place sufficient trust in the latter' (because of the statutory agency of members). The networks into which firm founders are linked, as well as the industries in which they are situated, are also likely significantly to inform the decision of whether to adopt the LLP. The network of small firms is a theme widely reported on in entrepreneurship (Birley and Westhead, 1993; Jack et al., 2008), but not in relation to legal form and how certain legal structures bestow different types of network advantages. Van Gils and Zwart (2009), however, examine cooperative and alliance relationships between SMEs, finding that a combination of organisational, partner-related and industry-related motives are key factors in alliance/cooperative formation. An example of this is found in a case study report (see Graham, 2006) which outlines the creation of an LLP as an umbrella co-alliance between the Midland Coop Inc and Impact Cooperative Inc 'who decided on the LLP business form to allow [them] to grow without the expense of merging memberships and establishing new identities in their home communities'. The three owners' coops continue to do business independently under their coop names but purchase supplies and sell grain under the co-alliance umbrella which 'allows [them] to grow...without changing their name' (p16). The relationship between the LLP legal form and business growth, therefore, needs closer examination, especially as there is also the possibility of 'clawback' or members' attempts to extract money from the LLP which could potentially hinder the growth of businesses.

In addition to the issue of growth, it is also argued that LLPs constrain the entrepreneurial and individualistic aspects that are central to the notion of 'profession' (Velayutham, 1996). In his view, organisational control in the form of regulatory mechanisms such as the LLP, has replaced occupational control and the means for self-regulation within professional practice (p366). This also raises questions about the relationship between risk and regulation (ie, whether they are entwined in the sense that 'the risk society is a regulatory society' (Morgan and Engwall, 1999, p2). By using LLPs to manage and spread risk, a discourse of risk and regulation (Imrie and Street, 2009) also becomes central to the meaning and practice of LLPs. This raises questions, as

Miller et al. (2008) note, about the implications of accounting and hybrids for the management of risk. Investigating the reasons for the take up of the LLP format, therefore, would help to explain if/how the use of LLPs is a nascent form of entrepreneurship – a vehicle for trying out entrepreneurial skills. Alternatively, the LLP could be conceived as a form of collective self-employment, where self-employed members group together to pool expertise and skills while retaining liability protection. In this sense, the LLP format, rather than being an expression of entrepreneurship in the traditional sense of the single owner-managed business, is instead an expression of distributed or team entrepreneurship. Such practices also challenge the traditional notion of organisational form. What some LLP formats seem to be representing is what Miller et al. (2008, p942) refer to as 'hybrid' forms 'that make possible lateral information flows and coordination across the boundaries of organisations, firms and groups of experts or professionals'. (For example, in the case of an LLP established as a special purpose vehicle (SPV) for a particular project or reason, where one or more corporate partners are involved, the partners will bring information, expertise and experience with them from their respective companies.) As these authors point out, 'accounting practices are central to these issues, in so far as accounting is constantly engaged in a dual hybridisation process, seeking to make visible and calculable the hybrids that it encounters' (Miller et al., 2008, p942). Thus, it may be inferred that the widespread adoption of LLPs (or more significantly, the way they are being used) has important implications for accountancy services.

Finally, much criticism was levelled at the UK government as a result of the introduction of the LLP form (Mitchell et al., 2002; Mitchell and Sikka, 2005), as it was perceived as allowing the (then) Big Five accounting LLPs to side-step responsibilities for negligent activities. By extending the LLP form to include firms from any industry or sector means that the LLP has become a legal vehicle that is accessible to the small and medium-sized business sector. The current research is distinctive in that the results will provide insight into the use of the LLP form and how a legal form designed to address potential liabilities arising from negligence claims (mostly against auditors) has been widely (and, perhaps, unexpectedly) utilised in small business and new venture creation. This research will reveal the extent to which LLPs are registered at the commencement of business activities or whether they are adopted over time as the business emerges, professionalises and needs greater legitimacy in the market place. In addition, this study will reveal the use of accountancy services and types of advice required by LLPs.

4. RESEARCH METHODS

The research has been undertaken in a series of stages, which are set out below.

Stage 1
The first stage involved a search of secondary data on LLPs (such as business reports, government surveys, professional journals and magazines and relevant academic journals) to establish the state of knowledge on this business form. This is reported on above.

Stage 2
In the second stage, an analysis of LLPs has been undertaken to determine the business sectors in which the LLPs are located and their size (by reference chiefly to balance sheet totals[18]). The FAME (Financial Analysis Made Easy) database was used for this purpose, and a list was compiled of the total population of LLPs across the UK. At this second stage also, five face-to-face interviews (with SMEs) were carried out to inform and develop the later telephone questionnaires (Stage 3) and wider questionnaire survey (Stage 4).

Stage 3
In Stage 3 a questionnaire was piloted with a small number of selected LLPs (40). The aim of the pilot was to test the questionnaire design and pertinence of questions across sectors. In addition, this pilot testing determined basic descriptive data in respect of specific objectives numbers (2) to (8) in the above list. This piloting also enabled the development of a full questionnaire.

Stage 4
The despatch of the full questionnaire to the larger sample of LLPs formed Stage 4 of the project. The questionnaire was administered by contacting by letter a stratified representative sample of 3,500 LLPs and inviting them to complete the questionnaire via a link on our project website to Survey Monkey. A questionnaire was also administered to a control group of non-LLPs.

Stage 5
The survey was followed by a further stage of research focusing on face-to-face semi-structured interviews with selected (23) LLPs from the stratified representative sample. The principal activities of the interviewed LLPs were:

- Law
- Accountancy
- Surveyors
- Architects
- Management Consultants in IT
- Quality improvement services in further education
- Management control consultancy
- Access to psychological services for the NHS
- Window cleaning
- Investment managers
- Property management
- Investment consultancy
- Commercial property leasing
- Physiotherapy.

18 These proved a more reliable and effective analysis mechanism than employee numbers – see Section 5.1.

The purpose of the face-to-face interviews was to collect in-depth data on the rationales for re-registering (or registering) a business as an LLP, the perceived benefits or challenges of adopting an LLP (including tax and other benefits), and the allocation of roles in LLPs. In addition, the interviews assessed in detail the professional needs of new and existing LLPs (such as costs of set-up and continuing in business with this form; how their accountancy, taxation, payroll requirements, etc., would be met), and to gather further data on such professional needs. In addition, interviews were undertaken with five business advisers (four accounting firms and one law firm[19]) to obtain their views.

19 A number of law firms that were contacted declined to give an interview. In one instance, this was because of weight of work, but in another, the firm was actively considering the use of an 'alternative business structure' (ABS), as permitted by recent changes in legislation, and did not feel able to comment on the use of LLPs. The law partner interviewed confirmed that the ABS is something with which law firms are currently getting to grips, as it is as yet very uncertain how this will work and impact on the LLP form that many law firms use.

5. ANALYSIS OF DATA ON LLPs FROM THE FAME DATABASE

In the following section, the results from the second stage of the research are presented. An analysis of LLPs was undertaken primarily to determine the size of LLPs by reference to balance sheet totals[20] and number of partners within the LLP. The FAME database, administered by Bureau Van Dijk, has been a key component in the analysis of LLPs and has been instrumental in providing a considerable amount of data, hitherto uncollated, about LLPs as well as being useful for providing a sample of LLPs to which to send a questionnaire survey. Although the number of LLPs on the database changes frequently as a result of daily updates, thus making it difficult to be precise about those actual numbers, within the period of the analysis, this factor has not proved distortionary. The analysis has enabled the discovery of the number of registered LLPs, and their initial classification by legal status (active, dormant, dissolved, in liquidation), location and industry, the balance sheet total (BST = total assets) and number of partners (referred to on the database as 'directors'). However, the analysis has been challenging to carry out, as the database is not typically used for this purpose.

5.1. CLASSIFYING LLPs FROM THE FAME DATABASE BY LEGAL STATUS, GEOGRAPHICAL LOCATION AND SIC

In Table 2, we present data drawn down from FAME which gives a breakdown of LLP registrations.

Table 2: Total number of LLP registrations

	No	%
Active	40,420	62.3
Active (receivership)	136	0.2
Active (dormant)	4,240	6.5
Dissolved	19,720	30.4
In liquidation	371	0.6
Total	64,887	100.0

Using Balance Sheet total to identify SMEs

As demonstrated in Table 2 above, from the FAME database, as at 21 March, 2011, there were 40,420 active LLPs operating in the UK (62% of total registrations). A first step in this analysis, however, was to categorise the active LLPs into small, medium and large. SMEs can be categorised according to three different criteria: total number of employees, annual turnover, or annual BST. The thresholds for medium-sized LLPs are: < 250 employees, annual turnover of no more than £25.9m and a BST of no more than £12.9m. The thresholds for small LLPs are: < 50 employees, annual turnover of no more than £6.5m and a BST of no more than £3.26m (Department for Business Innovation and Skills, 2010).[21] This definition is the UK equivalent of that outlined by the European Commission in their document 'The new SME definition' (European Commission, 2003). Both Companies House and the European Commission require LLPs to meet two of these criteria when classifying themselves.

In order to be able to classify by size as many LLPs as possible, it was decided as a first step to classify the total LLPs contained in the FAME database according to Balance Sheet Total (BST). Given that many LLPs do not actually have employees, using the number of employees was not a viable option for segregating small and medium-sized entities. Using the BST data, however, it was possible to classify 23,709 of the 40,420 active LLPs as small, medium-sized or large (Table 3). Indeed, classifying LLPs by BST indicates that 56% of LLPs are small or medium. In addition,

20 These proved a more reliable and effective analysis mechanism than employee numbers – see Section 5.1.
21 See also footnote 16 above.

in Table 3, it can be seen that of the registrations for small LLPs, 71% were active (compared to 91.5% and 93.7% respectively of the total number of active LLPs in each of the medium and large-sized categories of LLPs). Also, dormant LLPs represented 6.5% of the total registrations.

Table 3: All LLPs and LLPs with a BST by legal status

			Active LLPs classified by BST					
	All LLPs		Small LLPs		Medium LLPs		Large LLPs	
	No	%	No	%	No	%	No	%
Active	40,420	62.3	21,040	71.5	1,640	91.5	980	93.7
Active (receivership)	136	0.2	64	0.2	28	1.6	8	0.8
Active (dormant)	4,240	6.5	1,675	5.7	22	1.2	5	0.5
Dissolved	19,720	30.4	6,444	21.9	72	4.0	40	3.8
In liquidation	371	0.6	203	0.7	31	1.7	13	1.2
Total	64,887	100.0	29,426	100.0	1,793	100.0	1,046	100.0

NB: Figures based on balance sheet totals.
Date of retrieval: 21 March 2011.[22]

The analysis also demonstrates that an apparently large number of LLPs has been dissolved, are in liquidation or in receivership (total 31.2%). This appears comparable with the dissolution (etc) rate for private companies, where between 23% and 33% per annum are removed from the Companies House Register.[23] Looking across the size categories, in relation to the number of active LLPs, it is noted that a higher percentage of small LLPs are being dissolved or in liquidation/receivership (22.8%), than medium (7.3%) or large-sized (5.8%) LLPs. If LLPs have become medium-sized or large, it suggests, perhaps, that they are inherently more successful so fewer may be dissolved.

Since this legal form has only been available since 2000, this high level of dissolutions/liquidations for smaller LLPs poses a number of questions, such as whether the LLP is not really a suitable legal entity for small business or whether there are recessionary effects upon the stock of LLPs (as with limited companies). Alternatively, it is also likely that the large number of dissolved LLPs may be unrelated to the LLP format itself (eg, recession, no longer required, changing objectives, etc.). The pilot interviews indicated some complex ownership structures of LLPs, such as the inclusion of corporate members as well as natural persons (see more on this below). This suggests that LLPs, perhaps more so than limited companies, are constantly in flux and changing according to need, partner changes and evolving profit sharing arrangements. Equally, however, as is highlighted later in this report, there is evidence that the LLP is being used as a special purpose vehicle and is dissolved once its special purpose is achieved.[24] The pilot interviews yielded a variety of interesting material about the various special purpose uses to which LLPs were put. For example, one firm used the LLP form to enable the partners to undertake specific projects in land re-development, and to enter and exit the projects with ease. Another property re-development firm was comprised of two partners who were also sole traders. The LLP enabled them to work together but separately from their sole trader operations, thus giving flexible opportunities for collaboration and independence.

Classifying non-BST available LLPs

Not all LLPs, however, can be classified using a BST. The FAME database does not hold complete data on a firm's finances. The database is compiled using data from Companies House and, although all LLPs must be registered with Companies House, the activities in which LLPs are engaged determine the detail of accounts they are required to submit. Small LLPs must submit

22 It is necessary to state the date of extraction of data from FAME as figures vary as a result of daily updates.

23 Per 'Statistical Tables on Companies Registration Activities 2010/11' [online]. Companies House. Available at: URL www.companieshouse.gov.uk/about/companiesRegActivities.shtml [Accessed 27 December 2011]. No figures can be ascertained for traditional partnership dissolutions.

24 The law partner interviewed as one of the professional adviser firms was one of the few people to refer to an LLP 'going wrong', as there had been a large law firm which had gone into administration/receivership, though the reasons for it doing so were unclear. He also mentioned that, given the LLP form did not allow for a build up of profit reserves in the same way as for a limited company, it did not have financial resilience and would be likely to be immediately and adversely affected by economic downturns. In a partnership, all profits are allocated to members by the normal rules of accounting for partnership profits (see Appendix 1), and it was felt that these profits 'belonged' to individuals in a way that corporate profits did not.

full accounts if they fall into specific categories.[25] Small LLPs may be exempt from submitting full accounts and only required to provide an abbreviated balance sheet (if formatted using UK Generally Accepted Accounting Practice, though if they are using International Accounting Standards, they must submit full accounts). This meant that using BST alone was not sufficient for identifying the range of SME LLPs. Using BST alone also meant that there are 16,840 active LLPs which cannot be classified by this method – see Table 4.

Table 4: Active LLPs by BST and non-BST

	All LLPs	Small	Medium	Large
Non-BST	16,840	N/A	N/A	N/A
Total	40,549			

NB: Figures based on balance sheet totals and active LLPs.
Date of retrieval: 22 March 2011.

It was necessary, therefore, to identify additional methods for classifying SME LLPs. For some of these LLPs, a profit and loss account (income statement) or turnover figures (approximately 100 LLPs) could be found, but this was not reliable or consistent. Assessing the accounting status for the category of 16,840 LLPs was therefore difficult. The most prominent account type is 'type not available' (94.5%, Table 5). This is interesting for two reasons. First, these LLPs are up to 18 months old, and have not yet filed any account (details which indicates that a large percentage are new registrations); and second, because these LLPs are new, they may include sectors other than accountancy and legal services (which can be inferred by the fact that accountancy/legal LLPs are required to submit accounts). The second largest group of LLPs without a BST are 'total exemption small' (3.2%, Table 5). These LLPs have been able to defer presenting any accounts because they are small LLPs, and crucially, not involved in any services which come under the Financial Services Authorities' (FSA) regulations.

Table 5: Active LLPs without a BST by account types submitted

Classification of non-BST accounts	No	%
Type not available	15,390	94.4
Total exemption small	538	3.2
Total exemption full	215	1.3
Dormant	136	0.8
Full accounts	34	0.2
Small company	11	0.1
Group	1	0.0
Total	16,865	100.0

NB: Figures based on balance sheet totals and active LLPs.
Date of retrieval: 24 March 2011.

The large number of active LLPs without sufficient accounts to enable a BST to be calculated means that another method was required to categorise and analyse this large number of non-BST LLPs. One way to achieve this was through categorising LLPs by the number of partners they have (Table 6). It is a legal requirement that all LLPs have to submit the names and number of partners. For this reason, this was a useful criterion to use to assess size of the firm in that it is likely that LLPs with fewer partners are likely to be smaller.

5.2 NUMBER OF PARTNERS WITHIN LLPs

In Table 6, the breakdown of number of partners within LLPs from which we could not ascertain a BST is outlined. This demonstrates that in non-BST LLPs, 95.6% of respondents had five or fewer partners. For all BST-LLPs (see Table 7), those having five or fewer partners comprised 86%.

25 Small LLPs must file audited accounts if they fall into any of the following categories: (i) an LLP the securities of which are admitted to trading on a regulated market in an EEA state; (ii) an LLP that is an authorised insurance company, a banking , an e-money insurer, a MiFID investment firm or a UCITS management company or carries on insurance market activity; (iii) an employers' association; (iv) a parent or subsidiary undertaking except where the group qualifies as a small group, where the turnover of the whole group is not more than £6.5m net and the group's combined BST is not more than £3.26m net.

Table 6: Active LLPs without a BST by number of partners

Number of partners	No	%
0	97	0.6
1	126	0.7
2	11,737	69.7
3	2,581	15.3
4	1,094	6.5
5	473	2.8
6	229	1.4
7	133	0.8
8	84	0.5
9	51	0.3
10+	235	1.4
Total	16,840	100.0

NB: Figures based on balance sheet totals and active LLPs.
Date of retrieval: 22 March 2011.

Using this search term (number of partners), it was identified that the analysis of LLPs by reference to number of partners with and without BST, showed a clear correlation with regard to numbers of partners. For example, in the non-BST category of LLPs (Table 6), 71% (or 11,960 LLPs) had two partners (95.6% of respondents had five or fewer partners, equating to 15,635 LLPs). For BST-available LLPs (Table 7), 54.4% of LLPs (or 13,031) had two partners. This figure increases to 86% if we take into account LLPs with five or fewer partners. This means, therefore, that for both categories, having two partners was the most common form, with a slightly higher prevalence (16%) in the non-BST category of LLPs. This might be expected given that the LLPs in the non-BST category are 'small', as highlighted by their exemption status, and are possibly new registrations, meaning they do not need to submit accounts for 18 months. Overall, however, the distribution of LLPs across numbers of partners was very similar for both categories of LLPs with only marginal differences.

It was also noted, for example, that there was only a small number of LLPs with 10+ partners (1.4% for non-BST LLPs Table 6); and for BST LLPs, there were 3.8% small LLPs and 25.2% medium-sized LLPs, (Table 7). A further interesting observation was that for the LLPs identified as large (via BST figures), 33% were reported as having two partners.

Table 7: Active LLPs with a BST by number of partners

Number of partners	All BSTs		Small LLPs		Medium LLPs		Large LLPs	
	No	%	No	%	No	%	No	%
0	12	0.1	9	0.0	3	0.2	0	0.0
1	112	0.5	109	0.5	2	0.1	1	0.1
2	12,908	54.4	12,055	57.2	529	32.2	324	33.0
3	4,181	17.6	3,807	18.1	249	15.2	125	12.7
4	2,181	9.2	1,984	9.4	149	9.1	48	4.9
5	1,127	4.8	990	4.7	110	6.7	27	2.8
6	667	2.8	577	2.7	59	3.6	31	3.2
7	411	1.7	352	1.7	40	2.4	19	1.9
8	317	1.3	248	1.2	52	3.2	7	0.7
9	194	0.8	149	0.7	35	2.1	10	1.0
10+	1,599	6.8	796	3.8	414	25.2	389	39.7
Total	23,709	100.0	21,086	100.0	1,642	100.0	981	100.0

NB: Figures based on balance sheet totals and active LLPs.
Date of retrieval: 22 March 2011.

Overall, the use of 'number of partners' as a search term indicates that the BST and non-BST categorisations were fairly comparable in terms of numbers of partners and enabled us to categorise a larger number of LLPs for further analysis (rather than focusing only on those LLPs for which we could derive full BSTs). In summary, therefore, of the active LLPs listed on the FAME database, the following statements can be made:

- Using the criterion of two partners within the LLP, 71% of all non-BST LLPs and 54% of all BST-available LLPs can be classified.
- Using the criteria of five partners within the LLP, 95% of all non-BST LLPs and 86% of all BST LLPs can be classified.

This signifies that the overwhelming majority of LLPs are small and medium-sized LLPs. The high number of small LLPs is significant because, as stated above, the LLP was not a vehicle specifically designed with SMEs in mind (see Finch and Freedman, 1997; Freedman and Finch, 2002; Henning, 2004).

5.3 ADOPTION OF LLP ACCORDING TO INDUSTRY SECTOR

The main objective of the current study was to examine the adoption of the LLP according to the industry or activities in which they operate or are engaged. In March 2011, although there were more than 40,000 LLPs listed on the FAME database, only 2,213 had a Standard Industrial Classification (SIC) code assigned to them. This is partly because it is not compulsory for SICs to be noted on Companies House returns and for this reason they are often left blank. Identifying the industry sector, therefore, was more difficult than anticipated. In an attempt to identify more of the sectors in which the LLP format is being adopted, firms were classified according to words in their names (Table 8). The majority of the words used suggest professional or business service activities (eg, service, manage or solution). Of the 42,156 active LLPs on the FAME database at 24 May 2011, we have been able to classify 15,103 using key words to search FAME and the company's description of principal activity. These data are outlined in Table 8.

Table 8: Classification of LLPs in FAME by reference to business type

property	1,786	production	184	contractor	52
investment	1,499	energy	178	oil	52
service	1,395	tax	173	orthodontic	46
capital	1,244	health	173	photo	45
manage	1,229	construction	162	publish	42
solution	717	engineer	145	plumb	40
finance	709	planning	141	distribution	40
trading	478	training	133	transport	39
trade	473	marketing	131	child	35
estate	438	sport	109	pension	34
solicitor	408	electric	108	restaurant	31
consultant	345	music	106	chemicals	30
adviser	334	logistics	97	furniture	27
architect	293	clinic	95	metal	25
venture	283	marine	92	automation	25
farm	258	equity	90	equestrian	20
asset	252	survey	81	security	19
international	246	food	80	advert	19
technology	206	clean	79	manufacture	18
account	197	recruitment	77	doctor	14
film	196	resident	75	plaster	11
industry	186	environment	65	agriculture	4
build	185	motor	64		

NB: 15,103 LLPs classified out of a total 42,156.
Date of retrieval: 24 May 2011.

While the expected sectors, such as solicitors and accountants, are evident, there appears to be a plethora of consultants and advisers providing business-to-business services which could be within a range of industries from manufacturing to construction or general business management. It should also be noted that financial service industries are also well-represented, such as those providing investment, pension and asset management.

As one interviewee commented:

> 'Well, when we first set them up [51 LLPs] it was for the advantages of tax transparency and [then]… you were able to get business assets' taper relief for UK investors, instead of paying forty percent capital gains tax it was down to ten which held up investments for two years ...but what it did was enable us to pool all our investors together in one pot so that when we went out to a company it wouldn't look like [we were small]. Instead [the LLP enabled us to look bigger] with five hundred investing in fifty LLPs and then what we do is we pool those into five pots in what we call fund LLPs so there is sort of a tiered LLP structure; we have got fifty odd LLPs' clients investing and they basically invest in other LLPs' funds, they go out and invest in venture capital vehicles directly or part of financial initiative in essence. … By basically by pooling our clients in that way these vehicles can just collect investment schemes under the same regulations. … A bit complicated but that's what we set them up for. A lot of them have got 50 members, a lot of them have got five and they are basically done by family groups that have their own partnership as it were alongside us and one or two other things in there but we don't really connect all of our clients together.' (LLP 006[26])

Beyond finance and business services, a variety of healthcare firms has also begun to adopt the LLP form. Common among all of the professions are individuals giving advice to clients but operating within a partnership environment. Consequently, a desire for limited liability protection between partners and personal tax arrangements makes the LLP immediately attractive. Also, there is clear evidence from the survey and industry publications that as firms adopt the LLP form within a sector similar firms are 'encouraged' to follow suit. This was also confirmed by the law partner interviewed.

5.4 CLASSIFYING LLPs BY GEOGRAPHICAL LOCATION

In Table 9 on page 21, we have also been able to classify LLPs by reference to their geographical location.

While there is a regional bias in the distribution of LLPs in general (with a bias towards London and the South East), there is a fairly stable level of active LLPs across all regions. In the majority of regions, over 60% of LLPs are active (with the West Midlands 59% and Wales 56% dropping below the average). The majority of LLPs is located in London (37%) and the South East (17.3%), which is not surprising, given that this is a recognised centre for business and professional service firm activity (Sassen, 2001; Dicken, 2003). The North East (1.9%), Wales (2.8%), and Scotland (5.4%), however, show small numbers of LLP activity, with Northern Ireland showing only 13 active LLPs. A comment on the Welsh economy is that it is structured differently relative to that of the UK. For example, production represents 12% of the Welsh economy compared to 10% for the UK. However, between 2008 and 2009 there was a decrease in manufacturing by 17% and 7% respectively. Accountancy, legal and business services are heavily integrated into the manufacturing process and this may have impacted on the LLP firms operating in these linked in industrial sectors. Also, the Welsh and UK economies experienced significant growth in construction (10% and 8% respectively between 2001 and 2009). However, between 2008 and 2009 this fell by 12% and 6% respectively. There is evidence that the LLP is used as a special vehicle within construction industry, and consequently, the much greater fall for the sector in Wales may partly account for the lower levels of active LLPs compared to other UK regions. Similarly, real estate activities grew by 10% and 6% between 2008 and 2009 in Wales and the UK but contracted by 15% and 9% between 2008 and 2009. Once again these figures suggest that the movement of LLPs into dormancy or inactivity at a higher percentage compared to other regions.

26 Limited Liability Partnership interviewee number 006 (all interviewees were numbered).

Table 9: LLPs by geographical location

	Active							
	No	% of entire UK	% of UK region	Receivership	Dormant	Dissolved	In liquidation	Total
Nort East	646	1.9	62.7	4	70	302	8	1,030
North West	2,335	6.9	63.4	23	263	1,030	31	3,682
Yorkshire and The Humber	1,824	5.4	66.1	16	158	739	22	2,759
East Midlands	1,141	3.4	64.1	3	102	520	14	1,780
West Midlands	1,864	5.5	59.0	6	178	1,091	23	3,162
East of England	2,597	7.7	64.5	9	233	1,1162	27	4,028
London	12,749	37.6	61.6	15	1,420	6,415	92	20,691
South East	5,853	17.3	65.0	13	538	2,567	40	9,011
South West	2,089	6.2	63.7	3	178	996	14	3,280
Wales	946	2.8	56.1	3	78	652	7	1,686
Scotland	1,839	5.4	65.7	8	216	731	6	2,800
Northern Ireland	13	0.0	86.7	1	1	0	0	15
Total	33,896			104	3,435	16,205	284	53,924

NB: This analysis was undertaken using a primary trading address or any trading address if no primary trading address was available. Registered Offices were not used because they could be the addresses of a business's auditors or accountants.

Date of retrieval: 24 March 2011.

While there is a regional bias in the distribution of LLPs in general (with a bias towards London and the South East), there is a fairly stable level of active LLPs across all regions. In the majority of regions, over 60% of LLPs are active (with the West Midlands 59% and Wales 56% dropping below the average). The majority of LLPs is located in London (37%) and the South East (17.3%), which is not surprising, given that this is a recognised centre for business and professional service firm activity (Sassen, 2001; Dicken, 2003). The North East (1.9%), Wales (2.8%), and Scotland (5.4%), however, show small numbers of LLP activity, with Northern Ireland showing only 13 active LLPs.[27] A comment on the Welsh economy is that it structured differently relative to that of the UK. For example, production represents 12% of the Welsh economy compared to 10% for the UK. However, between 2008 and 2009 there was a decrease in manufacturing by 17% and 7% respectively. Accountancy, legal and business services are heavily integrated into the manufacturing process and this may have impacted on the LLP firms operating in these linked in industrial sectors. Also, the Welsh and UK economies experienced significant growth in construction (10% and 8% respectively between 2001 and 2009). However, between 2008 and 2009 this fell by 12% and 6% respectively. There is evidence that the LLP is used as a special vehicle within construction industry, and consequently, the much greater fall for the sector in Wales may partly account for the lower levels of active LLPs compared to other UK regions. Similarly, real estate activities grew by 10% and 6% between 2008 and 2009 in Wales and the UK but contracted by 15% and 9% between 2008 and 2009. Once again these figures suggest that the movement of LLPs into dormancy or inactivity at a higher percentage compared to other regions.

27 The North East, however, is heavily dependent on public sector services.

6. PHASE 4 DATA COLLECTION: JUSTIFYING SAMPLE SELECTION AND PRESENTATION OF SURVEY FINDINGS

6.1 SAMPLE SELECTION

Using Table 7 a sample frame for the survey of 3,500 LLPs was constructed[28] which enabled the most important independent variables to be included which would provide the most indicative sample of SME LLPs.

Following the analysis of LLPs from the database (by active/inactive, number of partners, BST, SIC code and UK regions), it was clear that the sample frame needed to be built to reflect the diverse set of factors and categories identified in the initial analysis of the FAME database. First, the sample frame was developed to include a sample of the active SMEs identifiable using the BST (Table 10: column A). Second, as there is a correlation between size and number of partners, it was important to acknowledge SMEs and the number of partners. Third, as noted above, some small LLPs are not required to provide a full set of accounts. However, this is not universal and the LLPs which can be categorised by BST will include most of those involved in some sort of activity regulated by the FSA. In view of this, by just sampling from these, a true understanding of LLPs adopting the format would not be achieved across all SIC codes. Consequently it is necessary to include some of the active LLPs which do not have a BST. At the time of selection (Table 10: column E) all non-BST LLPs have been included to provide a more balanced sample in terms of sector and these are selected by the number of partners.

The despatch of the full questionnaire to the larger sample of LLPs formed Stage 4 of the project. This questionnaire was aimed at acquiring data and was administered by contacting by letter 3,500 LLPs and inviting them to complete the questionnaire via a link on the project website to Survey Monkey.

A questionnaire survey was also administered to a control group of 350 non-LLP firms (contact details being derived from the *Yellow Pages*, internet sources and other publicly accessible sources). However, only six entities responded, four of which were limited companies, with the fifth being an unlimited company and the sixth not specifying. The businesses represented were carpentry (founded 2009), professional association/trade union (founded 1936), fund management (founded 1982), social care (founded 1994), construction (founded 1860) and a certificated bailiff (a family firm, founded 1977), with turnover ranging from under £100,000 to in excess of £15m, mostly derived from UK activities. Reasons for adopting their particular legal form was because it was most appropriate at the time, dictated by the business (one was a registered charity with a trading arm), unknown and because of a need to keep matters confidential (an unlimited company does not need to file accounts at Companies House). Advantages were the ability to grow, limited liability, personal liability of trustee directors, greater client confidence (the unlimited company), with taxation and confusion over the charitable status being disadvantages. The professional association/trade union had considered becoming a charity, but felt that this was too constrictive, and the bailiff had considered becoming an LLP, but did not because of the cost and tax implications on the transfer of business. In establishing their businesses they had advised themselves or used an accountant or solicitor (the 1860-founded business not specifying). In general, these businesses found a need for more detailed accounting, tax and legal advice as they grew in size. It is regrettable that these firms did not respond in greater numbers, but the few which did reply provide a certain amount of background and contextual material. None of these firms agreed to be interviewed.

28 This figure was originally based on an estimated 10% of the total population of LLPs, when funding was agreed for the research proposal.

Table 10: Sample Frame

Number of directors*	Active with BST						Active without BST		Active with SIC		Suggested sample Fame totals			
	SMEs		Small firms		Medium firms		All LLPs		All BST LLPs		SMEs (active with BST) (D)			
	No (A)	%	No	%	No	%	No (B)	Total %	No (C)	%	Total allocation for active with BST (D)	Small firms	Medium-sized firms	Active without BST (E)
0	12	0.1	9	0.0	3	0.2	97	0.6	0	0.0	1.1	0.8	0.3	8.6
1	111	0.5	109	0.5	2	0.1	126	0.7	1	0.1	9.8	9.6	0.2	11.1
2	12,584	55.4	12,055	57.2	529	32.2	11,737	69.7	543	37.3	1,112.9	1,066.1	46.8	1,038.5
3	4,056	17.8	3,807	18.1	249	15.2	2,581	15.3	218	15.0	358.7	336.7	22.0	228.4
4	2,133	9.4	1,984	9.4	149	9.1	1,094	6.5	121	8.3	188.6	175.5	13.2	96.8
5	1,100	4.8	990	4.7	110	6.7	473	2.8	80	5.5	97.3	87.6	9.7	41.9
6	636	2.8	577	2.7	59	3.6	229	1.4	71	4.9	56.2	51.0	5.2	20.3
7	392	1.7	352	1.7	40	2.4	133	0.8	42	2.9	34.7	31.1	3.5	11.8
8	310	1.4	258	1.2	52	3.2	84	0.5	31	2.1	27.4	22.8	4.6	7.4
9	184	0.8	149	0.7	35	2.1	51	0.3	26	1.8	16.3	13.2	3.1	4.5
10+	1,210	5.3	796	3.8	414	25.2	235	1.4	324	22.2	107.0	70.4	36.6	20.8
Total	22,728		21,086		1,642		16,840		1,457		2,010	1,864.8	145.2	1,490

Source: FAME: Bureau van Dijk. Date of retrieval: 24 March 2011.

* the FAME database refers to LLPs as having ‘directors’, rather than ‘partners’.

Description of respondent LLPs

Of the 3,500 LLPs invited to complete the questionnaire, 195 responded, although not all questions were answered by each respondent. This is a response rate of 5.57%, which is low. In absolute terms, however, a number of 195 is sufficient to provide a reasonably reliable analysis.

The first task in analysing the survey results was to establish the preponderance of SME LLPs in the respondent firms. Table 11 outlines the breakdown of LLPs according to turnover (which was established from the questionnaire results).

Table 11: Analysis of LLPs by turnover

	n=	%
<=£100,000 (A)	48	26.1
£100,001< >£1,000,000 (B)	83	45.1
£1,000,001< >£6,500,000 (C)	41	22.3
Small (=A+B+C) (D)	172	93.5
Medium (E)	10	5.4
Large (F)	2	1.1
Total (D+E+F)	184	100.0

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover <£6.5m; medium: turnover £6.5m < > £25.9m.

As intended through the sampling process, Table 11 identifies that 172 (93.5%) and 10 (5.4%) of the respondent LLPs were SMEs. In total, this equates to 99% of the respondent firms. The large LLP survey respondents were disregarded.[29] Of the very small LLP category (up to £100,000 in turnover), this represented 26.1% of the respondents. The majority of respondent LLPs were in the £100,001–£1,000,000 turnover category which represented 45%, with 22% in the £1,000,000+ turnover size band.

In order to assess the prevalence of accounting/legal LLPs among the respondent LLPs, we also asked if the LLP provided accounting or legal services. As stated earlier, accounting and legal partnerships were at the forefront of lobbying for the change in the law which allowed the use of the LLP format – particularly very large accounting and legal practices. This data is reported in Table 12.

Table 12: LLPs providing either legal or accountancy-based services

	Yes		No	
	No	%[30]	No	%
All[31]	32	21.1	120	78.9
<=£100,000 (A)	7	4.6	36	23.7
£100,001 < >£1,000,000 (B)	12	7.9	56	36.8
£1,000,001< >£6,500,000 (C)	9	5.9	18	11.8
Small (=A+B+C) (D)	28	18.4	110	72.4
Medium (E)	3	2.0	5	3.3
Large (F)	0	0.0	1	0.7
Total (D+E+F)	31	20.4	116	76.3

Source: Survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

Table 12 indicates that over 78% of the respondents did not provide either legal or accounting services. This indicates that over three-quarters of the respondents were non-accountancy/law LLPs. These data demonstrate the take up of the LLP format by LLPs in different sectors. A further check confirmed that 17% of the respondent LLPs were accountancy or law LLPs. This does not include investment/pension activities which are also FSA regulated and would be included in the 78% figure.

29 The identifiable large LLPs are highlighted in the table for comparative purposes. The 'all' line of the table includes those respondent firms who did not provide turnover data (along with those who did) and may therefore include more large firms.

30 All percentages are calculated using the total number of LLPs responding to the question as the denominator.

31 These figures include LLPs who did and did not provide turnover data (39 out of 191 did not answer this question).

6.2 DATE OF ESTABLISHMENT OF BUSINESS ENTITY AND WHETHER NEW OR CONVERSION FROM ANOTHER BUSINESS FORM

Table 13: Establishment of the LLP

	Started as an LLP		Not started as an LLP	
	No	%	No	%
All[32]	94	58.0	68	42.0
<=£100,000 (A)	37	40.7	6	9.2
£100,001 < >£1,000,000 (B)	39	42.9	32	49.2
£1,000,001< >£6,500,000 (C)	12	13.2	19	29.2
Small (=A+B+C) (D)	88	96.7	57	87.7
Medium (E)	2	2.2	7	10.8
Large (F)	1	1.1	1	1.5
Total (D+E+F)	91	20.4	65	

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

Respondents were also asked to provide details about the establishment of their LLPs, including the date when founded, and whether they were set up originally as LLPs or converted from some other legal form. Table 13 indicates that 58% of the respondents began their businesses as LLPs and 42% were original business entities prior to becoming an LLP. Of the new registrations 99% were SMEs, and of the conversion LLPs, 92% were SMEs.

For the 'converting' LLPs, Table 14 specifies the legal form prior to becoming an LLP. This indicates, perhaps not surprisingly, that 21.4% were traditional partnership forms, with 8.8% sole traders and 6.9% limited companies. The highest percentage of conversions was in the £100,001 to £1,000,000 turnover category which captured 18.9% of all conversions.

Table 14: Conversions – previous legal form

	Sole trader		Partnership		Ltd company	
	No	% [33]	No	%	No	%
All[34]	14	23.7	34	57.6	11	18..6
<=£100,000 (A)	3	5.1	2	3.4	0	0.0
£100,001< >£1,000,000 (B)	10	16.9	16	27.1	4	6.8
£1,000,001< >£6,500,000 (C)	1	1.7	9	15.3	6	10.2
Small (=A+B+C) (D)	14	23.7	27	45.8	10	16.9
Medium (E)	0	0.0	6	10.2	1	1.7
Large (F)	0	0.0	0	0.0	0	0.0
Total (D+E+F)	14	23.7	33	55.9	11	18.6

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

32 These figures include firms who did and did not provide turnover data (29 out of 191 firms did not answer this question).

33 These figures include firms who did and did not provide turnover data (132 out of 191 firms did not answer this question).

34 All percentages are calculated using the total number of firms responding to the question as the denominator.

A further observation is that it is unexpected to see limited liability companies converting to LLPs. Such entities already enjoy the benefit of limited liability, although conceivably a change of form might be beneficial for tax purposes.

Of the 59 respondents, 57 further advised of the date of their conversion. Table 15 shows the year in which they moved from the previous legal forms in relation to small or medium size.

Table 15: Move from previous legal form

	Small		Medium		All	
	n=	% [33]	n=	%	n=	%
2001	5	9.8	0	0.0	5	8.5
2002	4	7.8	0	0.0	4	6.8
2003	3	5.9	0	0.0	3	5.1
2004	6	11.8	1	14.3	7	11.9
2005	5	9.8	2	28.6	8	13.6
2006	3	5.9	0	0.0	3	5.1
2007	2	3.9	0	0.0	2	3.4
2008	6	11.8	0	0.0	6	10.2
2009	6	11.8	3	42.9	9	15.3
2010	10	19.6	1	14.3	11	18.6
2011	1	2.0	0	0.0	1	1.7
Total	51	100.0	7	100.0	59	100.0

Source: survey of LLPs, summer 2011.

NB: 132 out of 191 firms did not answer this question. No large firms answered this question. Percentages are calculated out of the total number of small, medium or all firms answering the question.

The five conversions in 2001 comprise one tax/accounting firm, one construction/engineering consultant, one marketing/sales/graphic designer/PR/media firm, one general retailer/wholesaler and one farming enterprise. Given the lobbying by accounting/law practices for this legal form, one might have expected a greater rate of early conversion of these types of businesses in the SME sector. It was suggested by one of the professional accountants interviewed that the take up of the form might have been quite slow where LLPs needed financing, as banks and other lenders were uncertain (or suspicious) as to the precise legal requirements of the new form, and that it is only relatively recently that lenders felt comfortable with this form. Furthermore, the increased take up in 2010 might be a result of greater asset protection being required in an economic downturn. It is becoming evident with the passage of time, however, that some of the consequences following upon the development of the LLP might not have been initially clear. For example, in the case of *Tiffin v Lester Aldridge LLP*, Mr Tiffin's case was about whether he was an employee or a partner of the LLP.

The reasons cited during the follow up interviews for conversions are now outlined (Table 16). Although the majority cites limited liability as the main motivating factor for conversion, it is also noted how other factors were also important, such as avoiding employee NIC costs, need for more corporate structure, tax reasons, succession planning and a means of formalising personal relationships into a business entity (LLP 017, architects' practice):

Table 16: Comments on reasons for conversion to LLP

> 'I didn't want to be handling dividends. I didn't want to be having to deal with all the national insurance side. If one is perfectly honest, we kept things slightly below the radar zero limit.' (LLP 004)
>
> 'We changed …'because of the limited liability as there was a significant amount of corporate debt within the business.' (LLP 005)
>
> 'It has advantages in terms of the limited liability element to it.' (LLP 007)
>
> 'There was the limitation of liability that was a key commercial consideration, although we have obviously got professional indemnity insurance we didn't want to be jointly and severally liable for our debts.' (LLP 008)
>
> 'Limited liability, which is the prime benefit. I think we thought the other benefit was that it gave us a slightly more corporate structure for running our business.' (LLP 009)
>
> 'LLP rather than a conventional partnership simply because of the need to protect against unlimited personal liability.' (LLP 010)
>
> 'The most pressing I suppose was the limited liability status.' (LLP 011)
>
> 'At the time they thought it would mean paying less tax.' (LLP 015)
>
> 'Save money on insurance especially indemnity insurance and dealing with revenue and customs it was altogether much easier. It is a nice legal relationship which builds on our personal relationship so it kind of works.' (LLP 017)
>
> 'It was succession planning to allow new partners to come in. Liability for us is a huge issue so that would definitely have been a driver had we not already had been a limited company.' (LLP 018)
>
> 'We wanted the limitation of liability as opposed to just a partnership so we liked the limitation of liability aspect of it.' (LLP 019)
>
> 'I think the limited liability.' (LLP 020)

The reasons are broadly similar to reasons for adopting the LLP as a first time business entity (see below). However, the evolution of the business and succession planning were two additional reasons cited for conversion in that the new LLP structure afforded greater flexibility. Consequently, the flexibility of the LLP appears to be particularly attractive alongside the potential tax and limited liability advantages.

An illustration of a newly established LLP is now outlined:

> 'The LLP was created specifically to service what they call the IAPT service for the NHS which is the improving access to psychological therapy. It was specifically created to handle the [location] contract for that service and we went into partners with joint venture initially with the private company based in [north] and ourselves who are a registered charity based up in [the North East]. So it is a joint venture with two other companies. They provide most of what I would call the clinical services the psychologists and we provide the accommodation and the finance and the HR and the sort of back office stuff. We didn't really want to form any sort of legal structure for this joint venture but when we tried to register for VAT, the HMRC basically said well we haven't got a vehicle which can cater for a joint venture which is not a limited company or a partnership and we took legal advice because we knew the liabilities of partnerships were quite stringent with joint and several liability which of course we didn't want because the partnership is effectively a partnership between us a health concern and a [private limited company]. We didn´t know what it would be like in terms of debts in the event of anything going wrong and the legal people suggested that we try the LLP route as opposed to a limited company. However, since then it has grown slightly but the initial consideration behind it was specific to service that particular contract. Also, now ... we actually acquired the other partners. We now own the partner, it is now operating as a wholly owned subsidiary of ours and we are probably going to change its name and run it as a separate limited company so the LLP would probably not continue.' (LLP 001, health services sector, £1.5m turnover).

6.3 LOCATION OF CLIENTS IN RELATION TO SALES REVENUE OF RESPONDENT LLPs

Respondents were also asked to indicate how their turnover was derived, in terms of location of clients. Table 17 shows these results.

Table 17: Percentage of income by location of clients

	Within a 20 mile radius	Within the UK	Within the EU (non UK)	Outside the EU	total providing useable figures for calculation
All[35]	33.6	48.8	8.8	8.9	120
<=£100,000 (A)	33.9	55.6	6.8	3.7	31
£100,001 < >£1,000,000 (B)	38.5	43.7	10.4	7.4	53
£1,000,001< >£6,500,000 (C)	23.0	50.5	8.2	18.3	29
Small (=A+B+C) (D)	33.3	48.7	8.8	9.2	113
Medium (E)	38.2	51.0	6.0	4.8	5
Large (F)	0.0	75.0	25.0	0.0	1
Total (D+E+F)	33.2	49.0	8.9	8.9	119

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover <£6.5m; medium: turnover £6.5m <> £25.9m.

Table 17 shows that, for those respondents who provided useable data, over 82% of LLPs' income is derived from within the UK. Hence, for the smallest LLPs, 33.9% of their income (as a mean average) is derived from within a 20 mile radius. Many small LLPs thus provide very locally-based services, which is what might be expected of service LLPs. Only 18% had a percentage of income derived from EU or other markets outside the UK (8.8% and 9.2% respectively) but it can be noted here that some small LLPs are equally active in overseas markets as medium LLPs (especially for investment purposes, LLP 006).

6.4 HOME OR BUSINESS LOCATION OF LLPs

A further objective of the project was to identify the extent to which LLPs are home-based businesses or not. Conceivably, working from home might be especially connected with the size of the business. Table 18 supports this. It shows an analysis of LLPs by reference to turnover and place of operation, and it is clear to see that very small LLPs (with turnover less than £100,000) are predominantly home-based (52%). Interestingly, in the middle turnover bands (£100,001–£1,000,000), there are comparable numbers of home-based (41%) and office-based (47%) LLPs. However, in the higher levels of turnover (over £100,001+), these LLPs tend to be office-based. This is not surprising given that higher levels of turnover (usually) cohere also with larger numbers of partners.

LLPs that are home-based operated from a variety of different places within the home – with bedroom, study, specially built office outside the main house and converted garage being identified. Most commonly a dedicated study was used. Some LLPs had operated from a number of different locations over the life of the business, but many respondents did not give a complete list, and only gave the latest address and a rough idea of how long the firm had operated from there. Sometimes this was because respondents were unwilling to disclose this information, but sometimes it was because they could not remember. One respondent explicitly referred to geographical location being unimportant in the Internet age. This issue of business location is important for assessing the evolution of business from home-based to office-based as the LLP increases by number of partners and turnover over time.

35 These figures include firms who did and did not provide turnover data. The figures in columns 'A' to 'D' are percentages: A+B+C+D = 100%.

Table 18: New business premises

	Home-based[36]		Office-based	
	No	%[37]	No	%
<=£100,000 (A)	30	15.8	17	8.9
£100,001 < >£1,000,000 (B)	24	12.6	58	30.5
£1,000,001< >£6,500,000 (C)	4	2.1	37	19.5
Small (=A+B+C) (D)	58	30.5	112	58.9
Medium (E)	0	0.0	10	5.3
Large (F)	0	0.0	2	1.1
Total (D+E+F)	58	30.5	124	65.3

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

6.5 NUMBER AND TYPES OF PARTNERS (INDIVIDUAL AND CORPORATE)

Survey respondents were asked how many people, including partners, worked for the partnership. The results are presented in Table 19.

Table 19: Total workforce, including partners and employees

Number of persons	n=	%
1	10	5.5
2	48	26.4
3–10	80	44.0
11–50	30	16.5
51–250	13	7.1
250+	1	0.5
Total	182	100.0

Source: survey of LLPs, summer 2011.

This result is representative of the sample frame in Table 10, where 82% of respondents had 10 or fewer partners/workforce (26.5% of respondents had two partners involved and 44% had between 3–10). While there are clearly LLPs in which individual partners are the chief protagonists, the more partners there are, the more persons generally operate within the partnership (in terms of office, administration or IT support). It is noted also that partners did not always refer to themselves as partners, but, for example, as 'finance director', 'chief executive', 'manager', etc, – descriptions which are suggestive of other legal forms, such as a limited company, and are seen perhaps as more commercially orientated. This is mirrored in the FAME database which refers to LLPs as having 'directors', rather than 'partners'. It should be noted that even though many LLPs might cite two partners, it is possible that some LLPs work in practice with only one partner/director, adding another partner's name (such as a family member or colleague) as a 'silent' or non-active partner. One LLP interviewed in the pilot interviews had set up a limited company to act as the second partner. The individual interviewed in this case was a director of the limited company as well as a partner in the LLP.

In Table 20, the number of partners in relation to size of LLP is outlined. This indicates that 66/155 respondents in the less than £1,000,000 turnover categories have two partners (42%), with eight LLPs in the higher threshold having two partners (total 74 LLPs). Overall, only 5/166 respondents had more than 10 partners and these were more evident in the higher turnover band. In the 3–5 partner category, these were evenly represented across all turnover bands with a slightly higher prevalence in the £100,001–£1,000,000 category.

36 These figures include firms who did and did not provide turnover data (1 out of 191 did not answer this question).

37 All percentages are calculated using the total number of firms responding to the question as the denominator.

Table 20: Number of partners by size of firm

	2	3–5	6–10	11–20	21+
<=£100,000 (A)	40	27	1	2	0
£100,001 < >£1,000,000 (B)	8	15	6	3	0
£1,000,001< >£6,500,000 (C)	74	58	8	5	0
Small (=A+B+C) (D)	74	58	8	5	0
Medium (E)	0	0	3	2	3
Large (F)	0	1	1	0	0
Total (D+E+F)	74	59	12	7	3

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

In Table 21, the number of partners is further illustrated in relation to the different types of partner.

Table 21: Numbers of partners

	Equity holding				Salaried partners				Fixed Share				Other			
Number of individual partners	1	2	3-10	11+	1	2	3-10	11+	1	2	3-10	11+	1	2	3-10	11+
All	13	68	58	5	14	9	5	1	3	22	6	2	4	5	4	0
<=£100,000 (A)	3	19	10	0	3	2	0	0	0	6	0	0	3	3	3	0
£100,001< >£1,000,000 (B)	5	39	23	0	6	3	3	0	2	11	4	0	0	2	0	0
£1,000,001< >£6,500,000 (C)	4	6	20	0	5	3	0	0	1	4	1	1	1	0	1	0
Small (=A+B+C) (D)	12	64	53	0	14	8	3	0	3	21	5	1	4	5	4	0
Medium (E)	1	1	3	1	0	1	2	1	0	1	1	1	0	0	0	0
Large (F)	0	0	2	4	0	0	0	0	0	0	0	0	0	0	0	0
Total (D+E+F)	13	65	58	5	14	9	5	1	3	22	6	2	4	5	4	0

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

Salaried partners are the most commonly found, although equity holding is a close second. Fixed share are rarer.

Acquisition of new partners is likely to be an indication of a business needing additional expertise in order to grow. Table 22 indicates that the majority of new partners is brought in as equity (capital contributing) partners, but salaried partners are more evident as new partners in the larger of these entities, with fixed share partners being relatively rare. One of the professional accounting firms interviewed indicated that fixed share arrangements (as regards profit allocation) were usually put in place for senior partners in the two or so years prior to retirement to provide greater certainty of income. In 38 (out of 145) cases, LLPs had not yet considered thinking about admitting new partners or they deemed this as applicable. This could indicate a lack of intention to grow the LLP, a desire to stay small or inattention to this issue.

Table 22: Level at which new partners are brought into LLPs by firm size

	Equity holding n=	Fixed share n=	Salary n=	Not yet applicable or considered
<=£100,000 (A)	15	8	2	14
£100,001 < >£1,000,000 (B)	27	4	13	20
£1,000,001< >£6,500,000 (C)	13	4	12	3
Small (=A+B+C) (D)	55	16	27	37
Medium (E)	2	2	3	1
Large (F)	1	0	1	0
Total (D+E+F)	58	18	31	38

Source: survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover: £6.5m <> £25.9m.

From the interviews, it was noted that a partner in a large firm might commence as a salaried partner, then proceed to equity holding status and later fixed profit share as part of a career progression, on the basis of successful performance (eg, bringing in new and profitable jobs or clients), although this is not so typical of law firms, where salaried partners are less common. This is often a way of differentiating between a large number of individuals of otherwise similar standing. Table 23 indicates that, to a large degree, this is not the case in SME LLPs (63% of respondents reported that career progression is not linked to starting level and performance). This may mirror what has traditionally and typically been the case in small professional partnerships, where it is time served and seniority which create a difference of status.

Table 23: Whether career progression is linked to starting level and ongoing performance

	Yes		No	
	No	% [38]	No	%
All[39]	54	32.5	112	67.5
<=£100,000 (A)	12	7.2	31	18.7
£100,001< >£1,000,000 (B)	20	12.0	54	32.5
£1,000,001< >£6,500,000 (C)	16	9.6	16	9.6
Small (=A+B+C) (D)	48	28.9	101	60.8
Medium (E)	5	3.0	4	1.2
Large (F)	0	0.0	2	1.2
Total (D+E+F)	53	31.9	107	64.5

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

38 All percentages are calculated using the total number of firms responding to the question as the denominator.
39 These figures include firms who did and did not provide turnover data (26 out of 191 firms did not answer this question).

6.6 EXTENT AND EASE OF PARTNER MOVEMENTS IN AND OUT OF THE LLP

Respondents were also asked about partner movements in and out of their LLPs, and whether leaving was an easy process. Table 24 reports the absolute numbers, though it is difficult to draw any particular conclusion here. It does appear that partner change is a relatively easy process to manage (just a 'form filling' exercise), although some appeared to need particular advice. However, of those reporting that a partner had left the firm, only five of these firms did not have a partnership agreement. It is clear (see earlier) that the absence of a partnership agreement can lead to difficulties when agreeing the terms upon which partners leave. For example, one window cleaning company reported that the process of adding/deleting partners was as follows: 'Well you just send in the forms saying you sacked one person and send another form saying this is the new one. For adding a partner, it is a matter of five pages, for deleting one, it is one page... as long as you do a contract for them you have actually got like legal terms and conditions for them' (LLP 003).

Table 24: Ease with which partners were able to leave the firm

	Easy	Just complete the form	Took time	Official guidelines unclear	Easier and cheaper than forming a ltd co	Need suitable advice
All[40]	33.6	48.8	8.8	8.9	120	5
<=£100,000 (A)	33.9	55.6	6.8	3.7	31	0
£100,001 < >£1,000,000 (B)	38.5	43.7	10.4	7.4	53	4
£1,000,001< >£6,500,000 (C)	23.0	50.5	8.2	18.3	29	0
Small (=A+B+C) (D)	33.3	48.7	8.8	9.2	113	4
Medium (E)	38.2	51.0	6.0	4.8	5	1
Large (F)	0.0	75.0	25.0	0.0	1	0
Total (D+E+F)	33.2	49.0	8.9	8.9	119	5

Source: survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover £6.5m< > £25.9m.

The admission of new partners also appeared to be overall a relatively easy process. In the survey 50 respondents stated that they had experienced new partners joining the firm. The ease with which partners joined was complicated when an existing partnership agreement needed to be amended, as is reported in Table 25 – because otherwise firms could again 'fill in forms', could obtain professional advice, or could carry out the process themselves because they had the necessary expertise (ie, they were legal firms). However, on balance, 17/39 respondents reported it was an 'easy' process with a further 11 LLPs reporting that it 'was easy with professional help' or 'using forms from Companies House'.

40 These figures include LLPs who did and did not provide turnover data (163 of 191 respondents did not answer this question).

Table 25: The ease with which new partners joined the LLP

	Easy	Easy with professional advice (law/ accountancy)	Easy – use forms from Companies House	Easy because we are a law firm	Need to alter existing agreement (but not a simple task)	N/A	Not simple	Easy if do not function as a partnership or ltd co.
All[41]	17	6	5	3	3	3	1	1
<=£100,000 (A)	2	3	3	0	0	2	0	0
£100,001 < >£1,000,000 (B)	5	2	1	1	0	1	0	0
£1,000,001< >£6,500,000 (C)	5	1	1	0	3	0	0	1
Small (=A+B+C) (D)	12	6	5	1	3	3	0	1
Medium (E)	4	0	0	2	0	0	0	0
Large (F)	1	0	0	0	0	0	0	0
Total (D+E+F)	17	6	5	3	3	3	0	1

Source: survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

The extent to which partners divide the profits of an LLP between themselves might be expected to reflect the nature of the types of partners and their contribution to the business. Table 26 reports on the profit sharing ratio between partners where equal division of profits predominates. However, it is also clear that some 24% of LLPs do not do this, while some 17% had variable arrangements, for example, changing the ratio from one year to another and some 9% considered this too confidential to disclose.

Table 26: Profit sharing ratio between partners

	Equal	Unequal	Variable	Undisclosed
All	76	36	25	14
<=£100,000 (A)	21	9	9	2
£100,001 < >£1,000,000 (B)	41	18	7	3
£1,000,001< >£6,500,000 (C)	10	6	5	6
Small (=A+B+C) (D)	72	33	21	11
Medium (E)	3	3	2	1
Large (F)	1	0	0	1
Total (D+E+F)	76	36	23	13

Source: survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m (40 out of 191 firms did not answer this question).

6.7 LLPs AND PARTICIPATION OF CORPORATE MEMBERS

In addition to individual partners, the pilot interviews also indicated that LLPs frequently had corporate members, and this was a feature even of very small LLPs. This was confirmed by the questionnaire survey, the results of which are shown in Table 27. (It is, of course, feasible for an LLP to have only corporate partners, for example, if it is set up as a joint venture or special purpose vehicle (SPV) between two companies, for a specific project or job.)

41 These figures include LLPs who did and did not provide turnover data (152 of 191 respondents did not answer this question).

Table 27: Partners: individuals and corporate members

	Individuals				Corporate members			
	Yes	%	No	%	Yes	%	No	%
All[42]	153	92.7	12	7.3	39	25.7	113	74.3
<=£100,000 (A)	39	23.6	4	2.4	6	3.9	33	21.7
£100,001< >£1,000,000 (B)	69	41.8	4	2.4	16	10.5	52	34.2
£1,000,001< >£6,500,000 (C)	30	18.2	2	1.2	10	6.6	19	12.5
Small (=A+B+C) (D)	138	83.6	10	6.1	32	21.1	104	68.4
Medium (E)	8	4.8	1	0.6	5	3.3	4	2.6
Large (F)	2	1.2	0	0.0	1	0.7	1	0.7
Total (D+E+F)	148	89.7	11	6.7	38	25.0	109	71.7

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

LLPs provided a variety of reasons for having one or more corporate members (see Table 28). Chief among these were that the corporate bodies provided finance generally or for specific reasons (eg, R&D) or could 'hold' profits to be used for the LLP in case of a 'rainy day' – useful as LLPs usually distribute all profits. Of the 44 respondents to this question, 32% mentioned the benefits of the LLP as an investment vehicle, with tax planning (27%) a close second (for the effective taxation of distributed profits, or avoidance of higher rates of capital gains, etc.), but also as part of a structural conversion from a limited company to an LLP without generating a taxable disposal. Corporate bodies also acted as SPVs for a variety of reasons (11%). Additionally, a corporate member was used simply so that a sole trader could effectively act as an LLP (ie, the company was wholly owned by an individual, and then used as an LLP partner with that same individual). There were also comments made by respondents which were unclear, and suggested that they might not really know why the LLP had a corporate member, with one respondent explicitly asking 'What the hell is a corporate member?' Overall, there was a varying range of sophistication in terms of the use of corporate members, suggesting on the one hand a considerable level of expertise or professional advice as to their use, but on the other total unawareness of their existence or potential.

Table 28: Reasons cited by firms for having corporate members

Reasons	No	%
Investment vehicle	14	31.8
Tax planning	12	27.3
SPV	5	11.4
Holding company	4	9.1
Reason undisclosed or unclear	4	9.1
So there are two partners	3	6.8
Owned by a partner	2	4.5
Total	44	100.0

Source: survey of LLPs, summer 2011.

NB: All percentages are calculated using the total number of firms responding to the question as the denominator (148 out of 191 did not answer this question).

42 These figures include firms who did and did not provide turnover data. 26 out of 191 firms did not supply details on the number of individual members. 39 out of 191 respondents did not supply details on the number of individual members. Percentages are calculated according to the number of firms answering questions.

An illustration of an LLP where corporate partners are used is LLP 013.

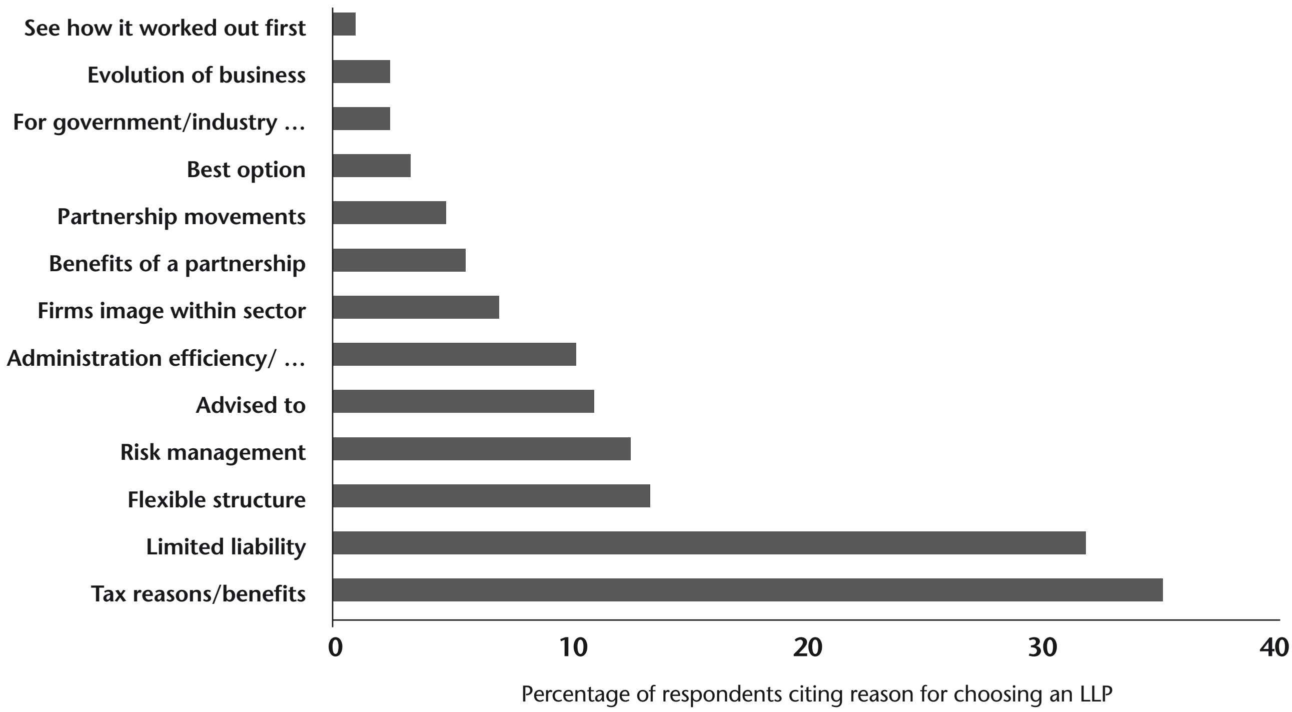
'Quite simply, we had what is in effect a quasi-partnership and so we had three individuals to start with wanting to get together to run a business, each with our own existing commercial structures and other business interests. It was a very effective way of giving us the transparency we needed for tax purposes so that our taxation affairs weren't interlinked and yet giving us a limited liability structure and indeed a formal structure. There is a formality about the formation of the LLP which gives you a nice neat package like a company but the main reason was the tax transparency. It is very flexible, in many ways it's more flexible than a straight company because you don't have articles of association and memorandum in the same way you do for a limited company and consequently your legal structure is entirely up to you, so it is quite capable of being moulded to your own situation and we have four or five different styles of governing documents; we have an LLP agreement for each of the ones that we operate but they are slightly different for each of them depending upon the nature of the trade. Our main trade is different from another LLP we have which is FSA authorised for instance, so it had very different things in its structure because what it is aiming to do is tick the boxes that the FSA require in terms of corporate governance.'

(LLP 013, property investment, £173,000 turnover with three LLP members each of which are limited companies and each partner member is also a director of each of the companies).

6.8 REASONS SHAPING DECISION TO ADOPT AN LLP

One of the key objectives in this research study was to identify the factors underlying decisions relevant to new and existing SMEs in deciding the most appropriate business form to adopt. Figure 1 provides details of the reasons LLPs adopted the LLP form.

Figure 1: Respondents' reasons for choosing LLP form



Source: survey of LLPs, summer 2011.

NB: Some firms mentioned more than one reason for deciding to become an LLP (63 out of 191 firms).

The main reasons cited by the respondent LLPs for choosing the legal form are tax advantages (35%) and limited liability benefits (32%). It is, perhaps, unexpected to see tax reasons ranked higher than limited liability, given that tax reasons were never one of the more publicised benefits of the form. Interestingly, there is a range of reasons which indicate that firms are reacting to the adoption of LLP form within their sector. This can be noted in responses such as being 'advised to adopt the LLP' (11%), or 'firm's image within the sector' (8%) or waiting to 'see how it worked out first' (1%). There was also a set of respondents for whom the LLP provides certain flexibility, for example, in the potential ease of partners joining and leaving (as discussed above) – although a partnership agreement is potentially crucial to ensure a smooth transition (Garry and Wano, 2007). In addition, some LLPs were using the LLP format to stay small (and under the VAT threshold), avoiding employee costs, at the same time as working with other LLPs to achieve growth (LLP 003, 014, 015, 016, 019). For example, an illustration is a small window cleaning company, as below:

> 'We originally started with me and my colleague and there was two workers and then suddenly we realised we needed to do something because we had got a little bit bigger and then we just created a partnership ...but as it got bigger, we have both split, so I've got one partnership and he has got another. That's right, so he's got his limited partnership with people and I've got mine with my people….A further advantage is that we can have flexible employment: we like to pay people for working so if you are employed you get paid for not working; but in our partnership if you don't work you don't get paid; so we have partners who are workers and we pay them by the hour (via a contract) and we deduct the cost of the materials and pay them 50% of the profit. I know it sounds harsh but it does work. Also, don't forget we are a small business, but it has actually gone in our favour because people view the LLP as "oh look those window cleaners they are like a registered proper business", so from our point of view it makes us look better and registered and bigger.' (LLP 003)

The LLPs were further asked what they consider to be the main advantages and disadvantages to small LLPs of becoming LLPs. In line with above, limited liability, along with flexibility and facility for tax planning are seen as predominant advantages, though there is a trade-off as these advantages also bring technical requirements which are seen as disadvantages.

From the follow-up interviews, some illustrations are extracted of direct comments about the benefits of the LLP format. These are presented in Table 29 (NB: This table refers to new LLP registrations and should be read in conjunction with the reasons/benefits for converting to LLP as outlined in Section 6.2)

Table 29: Benefits cited for new LLP registrations

'We find it suits our purposes very well; it gives us that protection on liability but allows us to service the contract and grow in other contracts as well so we find it very useful.' (LLP 001)
'Tax benefits. Individual taxation benefits, limited liability only partners.' (LLP 002)
'Because we wanted protection, basically. One, we wanted protection in case we got sued for any damages or work that went wrong and secondly we wanted everyone to be self-employed, so all of our people are self-employed and not employed. Also, the national insurance is lower and also you don't have employees' liability insurance which is a fortune. We haven't found any negatives with it so far.' (LLP 003)
'When we first set them up, the advantages of the tax transparency and …certainly the great advantage was you were able to get business assets' taper relief for UK investors.' (LLP 006)
'It is very flexible, you can add and remove partners, you can apportion profits and losses any way you want and you can pretty well choose the timing of your expenditure.' (LLP 012)
'Tax driven. The company gives you the ability to keep the money within the corporate veil and suffer a lower rate of tax until you take it out and so retained profits are the real answer.' (LLP 013)
'I think the key for us is that we earn our money because we are paid for our time and the less time we have to mess about with filling forms and answering silly questions and dealing with bureaucracy the more time we have to provide our service on our fee for service basis on an hourly rate.' (LLP 014)
'It is probably more flexible than a company so I suppose it is flexible enough for our needs.' (LLP 019)
'Purely the limited liability element.' (LLP 021)
'Fiscal transparency and limited liability were two key attributes.' (LLP 023)

In addition, the interviewees were asked if they intended to stay as an LLP. The responses are outlined in Table 30.

Table 30: Whether LLPs would remain as such

Ref LLP	Yes – Reasons	No – Reasons
001		'We actually acquired the other partners. We now own the partner; it is now operating as a wholly-owned subsidiary of ours and we are probably going to change its name and run it as a separate limited company so the LLP would probably not continue.'
002	'Yes but we might wind it up if we find its more hassle than to run the business separately.'	
003	'We are planning on growing it, yes. Definitely, as it will be an LLP and as I said we will never employ anyone.'	
004	'Don't see any reason for change at the moment, unless things change.'	
005	'There is no other format that fits.'	
006		'Structurally they still work but there are no benefits to being onshore as to offshore now and what they are we have found, especially with 500 partners in there, it's an administering nightmare.'
007	Topic not answered.	
008	'I think any professional partnership (should stay) because of the opportunity to limit one's liability.'	
009	Topic not answered.	
010	Topic not answered.	
011	Topic not answered.	
012	'For the foreseeable future, yes, which certainly means for the next three to five years.'	
013	'Yes, absolutely, unless they change the tax laws, in fact we have formed something like somewhere around ten businesses or subsidiary incorporated entities and all of the ones in this country have been LLPs.'	
014	'Indeed, there is no doubt about that, there is no reason why the LLP can't be a shareholder in a limited company and there are maybe opportunities where people, (it) would be more sensible for us to create a limited company in order to co-invest and the LLP would be a shareholder in that.'	

Ref LLP	Yes – Reasons	No – Reasons
015	'Well, it was such a hassle to become one that we are very reluctant to go through all that again.'	
016	'Yes, It is the right corporate form which gets us into the downside really, it is not well understood in the market in which we operate'.	
017	'Yes, partners can come and go without it generating tax issues to the remaining partners or tax issues for new partners.'	
018	'Unless somebody wants to buy us out at some point and then we cease to exist anyway. The reasons that my business partner and I decided to do this were that we wanted to run a small cost effective quality improvement support business to further education and therefore we don't have massive ambitions ….therefore LLP is the right model now and will remain the right model'.	
019	'If we converted back to a company I think there is probably a tax charge so it is probably a disincentive to do much with it.'	
020	'Because it suits us well, it gives us flexibility and its liability and we work for ourselves as self-employed people so we don't have the obligation to pay because with architecture it is very up and down – the income.'	
021	'I just find that it works for us; I can't see any negatives so I am not sure why we would want to change.'	

A factor which may influence a firm's decision to use the LLP form is whether any claim for negligence had been made against any partner, so the questionnaire explicitly asked about this. Table 31 shows that very few small LLPs had had claims made against partners prior to becoming an LLP, and that this had not had significant impact on the decision to use the LLP form (95% response). However, the overwhelming majority of respondents reported that they had had no claims levied against them. If indeed a need for limited liability to protect assets is a key driver behind the take up of the LLP format, these results suggest that the need might be a perceived one (ie, a precaution), rather than an actual one.

Table 31: Firms where partners have had claims against them prior to becoming an LLP

	Yes		No	
	No	%[43]	No	%
All[44]	8	5.1	150	94.9
<=£100,000 (A)	0	0.0	43	27.2
£100,001< >£1,000,000 (B)	3	1.9	67	42.4
£1,000,001< >£6,500,000 (C)	3	1.9	26	16.5
Small (=A+B+C) (D)	6	3.8	136	86.1
Medium (E)	0	0.0	9	5.7
Large (F)	0	0.0	1	0.6
Total (D+E+F)	6	3.8	146	92.4

Source: survey of LLPs, summer 2011.
NB: Definition of firms: small: turnover < £6.5m; medium £6.5m: turnover < > £25.9m.

Respondents were also asked whether their firm or any partners within theirs firm had had claims for negligence brought against them since establishing or moving to the LLP format. Table 32 reports the responses. Ten LLPs (or 7%) reported that claims had been made against partners within the LLP (with 93% reporting not). Of those having a negligence claim made, 0.7% were in the lower turnover threshold, 1.3% in the middle band and 2.6% in more than £1,000,000 turnover category.

Table 32: Claims of negligence against partners since becoming an LLP

	Yes		No	
	No	%[45]	No	%
All[46]	10	6.6	142	93.4
<=£100,000 (A)	1	0.7	42	27.6
£100,001< >£1,000,000 (B)	2	1.3	66	43.4
£1,000,001< >£6,500,000 (C)	4	2.6	23	15.1
Small (=A+B+C) (D)	7	4.6	131	86.2
Medium (E)	2	1.3	6	3.9
Large (F)	0	0.0	1	0.7
Total (D+E+F)	9	5.9	138	90.8

Source: survey of LLPs, summer 2011.
NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m< > £25.9m.

43 All percentages are calculated using the total number of firms responding to the question as the denominator.

44 These figures include firms who did and did not provide turnover data. Percentages given are out of the total sample of 191 firms (33 out of 191 firms did not answer this question).

45 All percentages are calculated using the total number of firms responding to the question as the denominator.

46 These figures include firms who did and did not provide turnover data (39 out of 191 did not answer this question).

In response to being asked if they had experienced any disadvantages with the LLP form, of 152 respondents, 39 said 'yes' (18 of these being LLPs with turnover between £100,001 and £1,000,000), and 113 'no'. The particular disadvantages identified are set out in Table 33. These are all, by and large, related to the technical side of accounting/taxation and compliance burdens, which inherently suggests that the new LLP partners did not fully realise the burdens which these matters would present or the responsibility they themselves would personally bear. The issue of 'institutions not understanding what an LLP is' was supported by one of the professional accountants interviewed, who commented specifically that banks and other lenders in early days did not fully appreciate the niceties of the legal form, treated it with some suspicion and were unwilling to lend funds. Although it is inherently a small number, four LLPs in the £100,001 to £1,000,000 category identified this as a disadvantage, and it is possible, given the level of turnover, that they might have wished to borrow money to finance further expansion.

Table 33: Disadvantages experienced as an LLP

	Taxation on partners/ all profits cannot shelter profits	Institutions not understanding what an LLP is	Compliance burdens	Lack of good submission software/ cannot submit accounts electronically	Late filing penalties	Other	Declaring annual results	None	Complicated structure	Owning a ltd co
All[47]	15	8	8	3	2	2	1	1	1	
<=£100,000 (A)	3	1	1	2	2	0	1	0	0	0
£100,001< >£1,000,000 (B)	7	4	4	0	0	2	0	1	10	0
£1,000,001< >£6,500,000 (C)	2	1	2	0	0	0	0	0	1	1
Small (=A+B+C) (D)	12	6	7	2	2	2	1	1	1	1
Medium (E)	1	2	0	1	0	0	0	0	0	0
Large (F)	1	0	0	0	0	0	0	0	0	0
Total (D+E+F)	14	8	7	3	2	2	1	1	1	1

Source: survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

From the interview material, the following commentary relating to disadvantages was identified (Table 34)

47 These figures include LLPs which did and did not provide turnover data (154 out of 191 did not answer this question).

Table 34: Disadvantages of LLPs

For LLP conversions
'The lack of appreciation that actually an LLP and a limited company have the same personal tax liabilities, ie, that some of the agencies haven't designated that they will only work with a limited company.' (LLP 004)
'Disadvantages are publishing your accounts, I imagine, the lower limit on liability – I guess the additional costs that might involve.' (LLP 007)
'One disadvantage which was potentially tax but we have still got an advantage over and above, I think, what would have been in an unincorporated practice.' (LLP 008)
'Before we didn't have to publish our accounts so I think there has been a certain cost involved in getting that initial set-up right.' (LLP 009)
'If the business is to be sold as a going concern then it may be more appropriate to have a company with a share capital.' (LLP 010)
'There is a small amount of formality which we have to keep up to date at Companies House with accounts, and publicity associated with that, publishing our accounts and also new members leaving and joining but it is a fairly small burden to bear.' (LLP 011)
'Hassle in moving from limited to LLP status with paperwork and banks, etc. In the end they may pay more tax.' (LLP 015)
'It is more of a burden administratively, having to do more tax returns that we are not technically responsible for but we still have to make sure it's done.' (LLP 017)
'We haven't really identified any yet.' (LLP 018)
'None really.' (LLP 020)

For new LLP registrations
None. (LLP 001)
None. (LLP 002)
None. (LLP 003)
'Historically, to hold some of these assets offshore you'd have been paying much higher tax rates but now that has all sort of gone away a bit so the benefits to us of having the LLP structure has slightly changed for investment purposes and in fact we are actually probably looking to get rid of them.' (LLP 006)
'The biggest challenge is having a regular shouting match with our software people because it is non-compliant with the Companies House reporting format.' (LLP 012)
'I find in the general business community a lack of understanding about what this thing is (LLP), ´is it a limited company, who do I sue if it goes wrong, can I get my money off those who own it, etc.´? I am sure that there is still an education issue in terms of the businesses that you will deal with.' (LLP 013)
None. (LLP 014)
'I don't think it does [present any problems].' (LLP 019)
'I can't see any negatives.' (LLP 021)
'The LLP is not so flexible; the biggest problem revolves around the need for members to take decisions to avoid becoming CIS. Would not use this structure again for quasi-investment fund.' LLP 023)

6.9 SOURCES OF FINANCE IN ESTABLISHING THE LLP

Respondents were also asked about the sources of finance used to finance their businesses. Table 35 reports the results.

Table 35: Methods used to finance the firm

	Partners personal assets	Banks	Family	Profits/ income/ businesses' savings	Corporate partner and/or venture capital	Friends	Not previously required	Building society	Holding company
All[48]	111	48	16	9	6	4	3	3	1
<=£100,000 (A)	27	12	7	2	2	2	2	1	0
£100,001 < >£1,000,000 (B)	52	20	7	3	2	2	1	2	1
£1,000,001< >£6,500,000 (C)	23	9	2	3	1	0	0	0	0
Small (=A+B+C) (D)	102	41	16	8	5	4	3	3	1
Medium (E)	5	6	0	0	1	0	0	0	0
Large (F)	1	1	0	0	0	0	0	0	0
Total (D+E+F)	108	48	16	8	6	4	3	3	1

Source: survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

The majority of LLPs is clearly financed by assets contributed by partners themselves, with banks being the most frequently used external source. LLPs also reported overwhelmingly that their LLP status had not affected their access to credit or borrowing. The accounting LLPs interviewed, did say, however, that in early days lenders were suspicious of the LLP as a legal form, and were generally unwilling to lend money to LLPs as they were an unknown quantity. That this has changed appears evident from the table above. It was also often the case that lenders would ask for personal guarantees from (particularly) directors of small companies which needed to borrow money, thus undermining the limited liability of such companies (see later discussion).

We also used the follow-up interviews to assess whether the LLPs had experienced problems in getting finance from banks. Table 36 outlines the responses.

48 These figures include LLPs which did and did not provide turnover data (45 of 191 respondents did not answer this question).

Table 36: Response from interviewees on problems raising finance

Ref	Comments
003	'We have never needed to raise finance but it has been a pain with the paperwork with the bank with signatories, every time we changed a partner they were expecting us to re-do all the forms and we change partners constantly so now we just don't tell them.'
004	'I've been in a fortunate situation in not having to have to do so and I've always lodged the accounts in Companies House on the basis that it was worth doing so for the transparency.'
005	'It certainly hasn't been detrimental in the slightest.'
007	No difference.
008	No difference
009	'I think our banks have become more wary of lending to law firms particularly because they're LLPs so they are recognising and so looking more for security and for personal guarantees, perhaps more than they were before.'
010	'I suspect this is of no relevance because we have not done so and have no intention of doing so (raising finance).'
011	'I think we had a very good relationship with our bank before we became an LLP and I don't think it has changed significantly since.'
012	'Strictly speaking the liability for default (within LLP) would fall on the partners without limit, and from a lender's perspective that has got to be beneficial for instance, compared with lending to a corporate enterprise whose liability would be restricted to its paid up capital and retained profits.'
013	No difference.
014	No need for funding.
015	No need for funding.
016	'Not easy because the market doesn't understand what the LLP does and they hear the word "partnership" and run away.'
017	No need for funding.
018	'I don't think that has been an issue.'
019	Not an issue.
020	Never needed finance.
021	'I haven't had to borrow any but I couldn't see that that would be a problem.'
022	'Banks need educating on what an LLP is; there is a lack of awareness from banks.'
023	'Neither good nor bad experience on this but more education needed on the LLP for investors.'

LLPs were asked if they had experienced any creditors/lenders requesting personal guarantees. Of 152 respondents, 67% reported they had not and 34% said they had, with banks being the lenders most frequently making such a request (see Tables 37 and 38).

Table 37: Firms experiencing creditors requesting personal guarantees on loans from partners

	Yes		No	
	No	%[49]	No	%
All[50]	51	33.8	101	66.9
<=£100,000 (A)	11	7.3	32	21.2
£100,001< >£1,000,000 (B)	24	15.9	44	29.1
£1,000,001< >£6,500,000 (C)	9	6.0	18	11.9
Small (=A+B+C) (D)	44	29.1	94	62.3
Medium (E)	5	3.3	3	2.0
Large (F)	1	0.7	0	0.0
Total (D+E+F)	50	33.1	97	64.2

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

Table 38: Types of creditors requesting personal guarantees

	Bank	Suppliers	Landlord	Insurance and/or finance companies
All[51]	38	8	2	1
<=£100,000 (A)	9	1	0	0
£100,001 < >£1,000,000 (B)	16	6	0	0
£1,000,001< >£6,500,000 (C)	7	1	0	1
Small (=A+B+C) (D)	32	8	0	1
Medium (E)	5	0	2	0
Large (F)	1	0	0	0
Total (D+E+F)	38	8	2	1

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

LLPs were also asked if they had professional indemnity insurance (PII) (see Table 39). Of 143 respondents, 96 did but 47 did not. Potential liabilities covered by the PII were general negligence and personal liability, provision of incorrect advice, faulty products, installations, constructions and buildings, accidents and damages (also in reference to employees). A number of respondents (12) reported that PII was not applicable to them. This might account for some of the 47 LLPs which did not carry PII, but not necessarily all, as one respondent reported that his/her firm did not carry PII, as this was simply too expensive. The level of PII cover is difficult to comment upon, as it ranges from 'not applicable' to 'undisclosed'. However, 10 respondents reported cover of > £1m, 54 in the range of £1m to £5m, 12 in the range of £6m to £10m and 3 < £11m.

49 All percentages are calculated using the total number of firms responding to the question as the denominator.

50 These figures include firms who did and did not provide turnover data (40 out of 191 did not answer this question).

51 These figures include firms who did and did not provide turnover data (144 out of 191 respondents did not answer this question).

Table 39: Firms with professional indemnity insurance

	Yes		No	
	No	%[52]	No	%
All[53]	99	66.9	49	33.1
<=£100,000 (A)	20	13.5	23	15.5
£100,001< >£1,000,000 (B)	45	30.4	21	14.2
£1,000,001< >£6,500,000 (C)	25	16.9	2	1.4
Small (=A+B+C) (D)	90	60.8	46	31.1
Medium (E)	5	3.4	1	0.7
Large (F)	1	0.7	0	0.0
Total (D+E+F)	96	64.9	47	31.8

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

6.10 COMPLIANCE REQUIREMENTS OF LLPs

Following up on the above, LLPs were also asked to identify the particular legal requirements LLPs were expected to meet. These are set out in Table 40.

52 All percentages are calculated using the total number of firms responding to the question as the denominator.

53 These figures include firms who did and did not provide turnover data (43 out of 191 did not answer this question).

Table 40: Requirements the firm is legally obliged to meet as an LLP

	Returns to Cos House	Tax returns (self-assessment)/ other compliance requirements	Same/ similar as for ltd co	Don't know	None/very little	Those required/ statutory	Tax more complicated/ other tax demands	Other	Unclear	Specific details on all companies media
All[54]	80	56	13	9	7	6	4	4	3	2
<=£100,000 (A)	28	18	2	2	2	0	1	0	0	1
£100,001< >£1,000,000 (B)	34	26	4	6	4	3	2	2	2	0
£1,000,001< >£6,500,000 (C)	10	8	6	1	1	3	1	1	0	1
Small (=A+B+C) (D)	72	52	12	9	7	6	4	3	2	2
Medium (E)	4	2	1	0	0	0	0	1	0	0
Large (F)	0	1	0	0	0	0	0	0	0	0
Total (D+E+F)	76	55	13	9	7	6	4	4	2	2

Source: survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

54 These figures include LLPs who did and did not provide turnover data (56 out of 191 did not answer this question). The last column refers to the requirement to place certain information such as LLP and company number on the letter head or company's media.

Table 40 supports to some extent the comments made in relation to Table 33, that is, that some partners (seven 'don't know' and two 'unclear') are unaware of the compliance requirements for an LLP. Table 41 identifies that the extra burden identified is predominantly accounting related, and overlaps to a degree with Table 33. Of 155 survey respondents, 42 said that these legal requirements placed an extra burden on the LLP (with returns to Companies House and tax returns being cited as the biggest burden). This is further supported in the follow-up interview material where the following comments were ascertained:

LLP 004	'It would be nice if the government would give the LLP the same space as a limited company with respect to the pension and the pension handling but I think it might be falling on deaf ears.'
LLP 006	'LLPs are caught by Companies House which means a lot of our partners have had to file accounts every year and had them audited again which is more cost than expected.'
LLP 009	'It's the ability to bring people in so every time you want to put someone in you have to effectively re-write the constitution.'
LLP 011	'Well, the disadvantage is probably there is much more formality to it.'
LLP 023	'We are much more transparent than some of our competitors so we get adverse press comment from the ill-informed.'

However, 115 LLPs reported that they did not experience compliance problems. Some further examples of this 'no problem with compliance' viewpoint were identified in the follow-up interviews, as below.

LLP 008	'I am not sure if we have actually [had any problems].'
LLP 010	'I don't think we regard the burdens as being any more onerous than when practising as a sole practitioner.'
LLP 014	'If we had set up as a limited company it would in many ways have made it more cumbersome to work with each other and also to work with the client.'
LLP 015	'From changing from a limited company to an LLP there was a lot of paper work because they wanted to keep the same name.'
LLP 016	'Easier to administrate.'
LLP 018	'Currently, it meets our needs totally.'

Table 41: Description of extra burdens placed on firm by legal obligations

	Government accounts demands/ complex compliance regulations/ timeframe to submit accounts	Additional time/money to compile accounts	Increased complexity of accounts because of partners/ different tax requirements	Other	Inadequate/ special software	Increased transparency	Self-employed partners and concomitant admin costs	Companies house details cannot be filed online – by post only
All[55]	80	56	13	9	7	6	4	4
<=£100,000 (A)	28	18	2	2	2	0	1	0
£100,001< >£1,000,000 (B)	34	26	4	6	4	3	2	2
£1,000,001< >£6,500,000 (C)	10	8	6	1	1	3	1	1
Small (=A+B+C) (D)	72	52	12	9	7	6	4	3
Medium (E)	4	2	1	0	0	0	0	1
Large (F)	0	1	0	0	0	0	0	0
Total (D+E+F)	76	55	13	9	7	6	4	4

Source: survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

55 These figures include LLPs which did and did not provide turnover data (155 out of 191 did not answer this question).

6.11 SOURCES OF INFORMATION REGARDING LLP TAKE UP AND SATISFACTION LEVELS

Respondents were also asked about where they had obtained advice in relation to their decision to use the LLP form. Table 42 shows a wide variety of sources used.

Table 42: Source of advice on becoming an LLP

	Advised ourselves	Accountants	Solicitor	Business link	Business adviser	Friends	Business associate	Internet/ other media source
All[56]	71	80	30	2	3	1	1	2
<=£100,000 (A)	21	22	3	2	1	0	0	1
£100,001 < >£1,000,000 (B)	33	37	9	0	2	1	1	1
£1,000,001< >£6,500,000 (C)	10	14	12	0	0	0	0	0
Small (=A+B+C) (D)	64	73	24	2	3	1	1	2
Medium (E)	3	5	3	0	0	0	0	0
Large (F)	0	0	1	0	0	0	0	0
Total (D+E+F)	67	78	28	2	3	1	1	2

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

A large number of firms used accountants or solicitors, which is to be expected, and the large number who 'advised themselves' includes a very large number of accountants and solicitors themselves who used the LLP form for their businesses. This is reflected also in the comments from LLPs in the follow-up interviews (Table 43).

Table 43: Comments from interviewees on where advice sought

Ref	Comments	Does this relate to your sector?
001	'A firm of lawyers. It was mainly because of the VAT and the liability.'	Yes
002	'Accountant's advice and my own professional expertise.'	Yes
003	'We did it all ourselves and downloaded the information.'	All sectors
004	'I did talk to my accountants and I did actually get my solicitor to draw up a proper partnership agreement which I then deposited at Companies House.'	Yes
005	'I am a qualified accountant anyway and it was under my recommendation really.'	Yes
006	'The accountants drew the tax strategy and obviously the solicitors basically just had to document the partnership agreements. Both of which were incredibly complicated.'	Yes
009	'Well, as lawyers I suppose we got a fairly good familiarity with it..'	Yes

56 These figures include firms which did and did not provide turnover data (38 out of 191 firms did not mention any reasons).

Ref	Comments	Does this relate to your sector?
012	'I am a registered member of ICAEW.'	Yes
013	'No (advice) except within my own head. So I think it is something that for most people setting up an LLP they ought to have some form of professional advice in doing it.'	Yes
014	'No, the company had sufficient knowledge and experience to set up.'	Yes
015	'Outside firm of accountants, because any of those things to do with the legal nature of the company and its tax affairs, we always consult professional advice.'	Yes
016	From the firm's accountant. Did own Internet research and then asked the accountant to weigh up the pros and cons.	Advice from accountant was about the firm's own type of business but the Internet research (mainly government websites) did not throw much light on this particular sector.
017	An accountancy firm advised mainly for tax considerations. Combination of DTI and Business Link research helped to enable them to ask more specific questions.	Advice given was more about the liability side but not so much on changes in accountancy practices.
018	'Well, clearly we both felt that we wanted a legal agreement, we set it all out so that there could be no confusion as to what each of our responsibilities and shares were so that was because of the solicitors advice and we thought that that was just good practice.'	'Well the accountant was somebody who had worked with my business partner on her limited company so he was already well aware of what we did and who we were.'
019	'Mainly the tax position of it and comparing that with doing it as a limited company, mainly that was the advice we were receiving.'	'They are the advisers for our other companies so we had an existing relationship with them.'
020	'We had a little bit of advice from our accountant but not a lot, we told them we were thinking of doing it and they thought it was a good idea and then it was up to us, so really I don't think we had proper advice from anyone.'	Yes
021	'In hindsight I could have done it myself. It was relatively new so less people knew about them.'	'They were handling my redundancy/ retirement and it seemed easier.'
022	Sought no professional advice; looked at CoHo website and did web searches.	No

Table 44: Reasons for being pleased or displeased with advice given

	Operates as expected	Pleased/ well-advised	Tax saving/ effective/ efficient	Provides limited liability	Simple to operate and hassle free	Good structure	Extra cost/ effort/no benefits	Advised ourselves
All[57]	27	22	13	9	6	5	5	5
<=£100,000 (A)	8	6	3	5	2	0	0	2
£100,001< >£1,000,000 (B)	11	10	9	3	4	1	4	2
£1,000,001< >£6,500,000 (C)	5	5	0	1	0	4	0	0
Small (=A+B+C) (D)	24	21	12	9	6	5	4	4
Medium (E)	2	1	0	0	0	0	0	0
Large (F)	0	0	0	0	0	0	0	0
Total (D+E+F)	26	22	12	9	6	5	4	4

Source: survey of LLPs, summer 2011.

NB: Definition of LLPs: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

The vast majority of those who responded (132 out of 144) confirmed that they were happy with the advice that they received. Reasons for firms being content or not with the advice they received are set out in Table 44. The reasons provided are fairly extensive as this was an open-ended question. Most respondents were happy that the LLP form operated as expected and that they had been well-advised to adopt it. We note again the comments that it had various tax advantages. This is supported by comments from the follow-up interviews with LLPs, which suggest that the need to file accounts gives the LLP the advantage of comparing itself with others in terms of overall financial performance, though this might not be such an advantage in years when performance is not as good as desired (LLP 008). One LLP (LLP 009) commented that the change to the LLP form had changed the business's culture, although the advice to use the form was good. The law partner interviewed indicated that sometimes law firms maintained a partnership or LLP form, although they could operate, if they chose, as a limited company. However, this was felt not as fitting for 'professional status' – and may shed some light on the reference to 'culture'. Overall, a picture emerges of a degree of complexity in tax and the legal set-up which businesses could deal with themselves because of members' own professional backgrounds in law/accountancy or general competency or on which they were prepared to seek professional advice.

Related to the above, the Limited Liability Partnership Act 2000 suggests that firms should draw up a constitution or formal partnership agreement, hence firms were asked if they had completed this process. Table 45 shows how the process of writing the partnership agreement was undertaken by 119 of the respondents.

57 Some firms mentioned more than one reason for deciding to become an LLP (84 out of 191 firms did not mention any reasons).

Improve image	Easier than a ltd co	Not relevant	Allows self-employed tax regime	Neither agree/ disagree	Use as an SPV eg, for property investment	Unsuitable for small firms	More complicated than a ltd co	In hindsight did not understand implications	No easier or harder than a ltd co	Displeased with our advice
3	3	3	3	3	2	2	2	2	1	1
0	1	2	2	2	0	1	1	0	0	0
3	2	0	1	0	1	1	1	2	0	1
0	0	1	0	1	1	0	0	0	1	0
3	3	3	3	3	2	2	2	2	1	1
0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0
3	3	3	3	3	2	2	2	2	1	1

Table 45: Undertaking the process of writing a partnership agreement

	Using a solicitor	Drafted internally in negotiation with partners	Using an accountant	Made use of 'off the peg' template (may have been modified for individual firms)	Business adviser	Misc answer	Built on/ evolution of previous partnership agreement	Written by one partner
All[58]	45	30	17	9	6	7	5	2
<=£100,000 (A)	4	4	5	2	2	0	0	1
£100,001 < >£1,000,000 (B)	20	13	7	5	3	3	2	1
£1,000,001< >£6,500,000 (C)	18	8	4	1	1	2	1	0
Small (=A+B+C) (D)	42	25	16	8	6	5	3	2
Medium (E)	2	4	0	1	0	1	2	0
Large (F)	1	0	1	0	0	0	0	0
Total (D+E+F)	45	29	17	9	6	6	5	2

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

58 These figures include firms which did and did not provide turnover data (89 of 191 respondents did not answer this question).

6.12 MEMBERSHIP OF PROFESSIONAL BODIES

Table 46: Professional groups of which firms are members

	ICAEW	FSA	RICS	Law Society	RIBA	SRA	ACCA	NAPIT	CIOT
All[59]	12	12	8	5	4	4	3	2	1
<=£100,000 (A)	3	1	1	1	0	1	0	2	0
£100,001< >£1,000,000 (B)	5	6	4	1	3	2	1	0	1
£1,000,001< >£6,500,000 (C)	3	5	2	2	1	1	2	0	0
Small (=A+B+C) (D)	11	12	7	4	4	4	3	2	1
Medium (E)	1	1	1	1	0	0	0	0	0
Large (F)	0	0	0	0	0	0	0	0	0
Total (D+E+F)	12	13	8	5	4	4	3	2	1

ICAEW – Institute of Chartered Accountants in England and Wales
FSA – Financial Services Authority
RICS – Royal Institution of Chartered Surveyors
RIBA – Royal Institute of British Architects
SRA – Solicitors' Regulation Authority
ACCA – Association of Chartered Certified Accountants
NAPIT – National Association of Professional Inspectors and Testers
CIOT – Chartered Institute of Taxation
CIMA – Chartered Institute of Management Accountants
CML – Council of Mortgage Lenders
MCA – Management Consultancies Association
ARB – Architects' Registration Board
CIOB – Chartered Institute of Building
IPRB – Intellectual Property Registration Board
PPA – Professional Publishers' Association
CIAT – Chartered Institute of Architectural Technologists

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

Respondents were asked whether they were members of any professional organisation or society which had placed extra compliance requirements on the firm. The results are reported in Table 47. About one-third of respondents belonged to professional organisations. The number which does not have professional affiliations is indicative of a large number of firms operating outside the professional advice sector and supports the notion of growth of LLPs among firms which are not lawyers or accountants, as the legal and accounting professional associations predominate among firms with professional affiliations, as is shown in Table 46.

59 These figures include firms which did and did not provide turnover data (141 of 191 respondents did not answer this question).

CIMA	CML	MCA	Construction-line	Simply biz	ARB	CIOB	IPRB	PPA	CIAT	CIT
1	1	1	1	1	1	1	1	1	1	1
0	0	0	0	0	0	0	0	0	1	0
1	0	0	0	0	1	1	0	1	0	1
0	0	0	1	0	0	0	0	0	0	0
1	0	0	1	0	1	1	0	1	1	0
0	1	1	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0
1	1	1	1	0	1	1	0	1	1	0

Table 47: Members of professional group

	Yes		No	
	No	%[60]	No	%
All[61]	55	36.2	97	63.8
<=£100,000 (A)	8	5.3	35	23.0
£100,001< >£1,000,000 (B)	25	16.4	42	27.6
£1,000,001< >£6,500,000 (C)	16	10.5	13	8.6
Small (=A+B+C) (D)	49	32.2	90	59.2
Medium (E)	5	3.3	3	2.0
Large (F)	0	0.0	1	0.7
Total (D+E+F)	54	35.5	94	61.8

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

6.13 DAY-TO-DAY PROFESSIONAL ADVICE REQUIRED BY LLPS

One of the particular objectives of this project has been to determine the type of professional advice that LLPs needed at an operational level (as opposed to on setting up/converting) and hence this was acquired, particularly on accountancy, taxation, payroll, etc., in terms of whether such expertise was bought in and provided on site, outsourced or undertaken in-house. Table 48 sets out details about the sources of accounting and taxation advice. The majority of small firms either deals with its own requirements (70) or outsources them (77). One of the professional accountants interviewed suggested that many of its small LLP clients did not have the in-house expertise necessary to deal with accounting and taxation, so it is likely that LLPs in Table 48 which outsource accounting and taxation requirements are chiefly non-accounting LLPs. The mid-tier LLP and small accounting practice interviewed offered a full range of accounting and advisory services for LLP clients, which were certainly taken up. Law firms would not typically provide advice on the same basis. For example, they would advise on the set-up or conversion of a business to LLP status, but thereafter would give legal advice on an individual transaction basis.

60 All percentages are calculated using the total number of firms responding to the question as the denominator.

61 These figures include firms which did and did not provide turnover data (39 out of 191 did not answer this question).

Table 48: Accountancy and taxation requirements

	Bought in and provided on site		Outsourced		Undertaken in-house	
	No	%[62]	No	%	No	%
All[63]	4	2.6	77	51.0	70	46.4
<=£100,000 (A)	2	1.3	16	10.6	25	16.6
£100,001< >£1,000,000 (B)	1	0.7	42	27.8	24	15.9
£1,000,001< >£6,500,000 (C)	1	0.7	13	8.6	15	9.9
Small (=A+B+C) (D)	4	2.6	71	47.0	64	42.4
Medium (E)	0	0.0	5	3.3	3	2.0
Large (F)	0	0.0	1	0.7	0	0.0
Total (D+E+F)	4	2.6	77	51.0	67	44.4

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

The respondents were also asked if their accountancy and taxation needs had changed over time, as a result of LLP status. Out of 149 firms which responded to this question, 95 firms said that their needs had not changed, with 54 saying that they had. The reasons provided for the changes were generally added complexity in meeting financial reporting and accounting requirements, and more specialist tax advice being needed because of the financial circumstances of individual partners or because individuals had become partners (rather than being sole traders). However, some of the reasons for changes were clearly because of business expansion, for example, growth in staff numbers and the need to register for VAT as turnover increased. Of the respondents, 51% reported that they outsourced their taxation and accountancy requirements, while 46% undertook these activities in house. One respondent did say that LLP status was 'simpler' because consolidated accounts were not now needed, which inherently suggest a change to LLP status from being a group of companies, which would appear, per se, unusual.

Respondents were also asked how they met their payroll requirements and whether these had changed as a result of LLP status. The majority of respondents undertook their payroll requirements themselves or outsourced them, with only 11% reporting any changes being required as a result of LLP status, because of taking on additional staff, making staff redundant and greater complexity in complying with regulations or moving to outsourcing.

Respondents were also asked how they met their legal requirements. The results are set out in Table 49. Clearly the majority of firms outsource legal requirements, though a substantial number undertakes this in-house, no doubt reflecting the fact that very many LLPs are themselves legal practices.

62 All percentages are calculated using the total number of firms responding to the question as the denominator.
63 These figures include firms who did and did not provide turnover data (40 out of 191 did not answer this question).

Table 49: Legal requirements

	Bought in and provided on site		Outsourced		Undertaken in-house	
	No	%[64]	No	%	No	%
All[65]	1	0.7	83	56.5	63	42.9
<=£100,000 (A)	0	0.0	17	11.6	25	17.0
£100,001< >£1,000,000 (B)	1	0.7	40	27.2	26	17.7
£1,000,001< >£6,500,000 (C)	0	0.0	19	12.9	6	4.1
Small (=A+B+C) (D)	1	0.7	76	51.7	57	38.8
Medium (E)	0	0.0	5	3.4	3	2.0
Large (F)	0	0.0	1	0.7	0	0.0
Total (D+E+F)	1	0.7	82	55.8	60	40.8

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

A significant number of respondents (134 out of 148 who answered the question) said, however, that their overall legal requirements had not changed as their business had grown. Those who reported change cited general additional legal requirements because of growth, the use of a partnership structure and employee matters as the main reasons for change, with partnership structure being the second most frequent reason.

LLPs were also asked to identify sources from which they obtained advice on how to develop their business. On page 58, Table 50 reports the results. Business contacts and professional advisers (especially accountants) appear to be the source of most advice, but as Table 50 reveals, there is still a substantial amount of advice that is derived from less formal sources (eg, friends and acquaintances), which might indicate, as suggested by the law partner interviewed, that professional advice is seen as expensive – and a new LLP might not have funds available to pay for this, even though it might be beneficial to do so.

Generally, though, the use of an LLP format was not regarded as impacting on any particular plans for expansion. The majority of firms reported that they had no problems in obtaining business development advice, but issues to do with LLP administration, operations and accounting, financing, marketing, fees/pricing and selling the business caused problems in terms of obtaining advice for some 21 firms overall of the 79 LLPs which responded on these matters.

64 All percentages are calculated using the total number of firms responding to the question as the denominator.

65 These figures include firms who did and did not provide turnover data (44 out of 191 did not answer this question).

Table 50: Source of business development advice

	Business contacts	Accountants	Colleagues	Solicitors	Friends	Business groups	Acquain-tances	Business link	External consultants' industry body	None sought/ advise ourselves	Internet and/ or own research	Business from existing contacts	Chamber of Commerce
All[66]	86	85	49	45	32	28	22	22	13	12	3	2	1
<=£100,000 (A)	25	24	11	8	11	7	4	14	5	5	0	0	0
£100,001< >£1,000,000 (B)	37	39	22	23	16	11	12	5	5	5	3	2	0
£1,000,001< >£6,500,000 (C)	16	15	10	8	3	6	3	2	1	1	0	0	1
Small (=A+B+C) (D)	78	78	43	39	30	24	19	21	11	11	3	2	1
Medium (E)	7	5	5	4	2	4	3	1	1	0	0	0	1
Large (F)	1	1	1	1	0	0	0	0	0	0	0	0	0
Total (D+E+F)	86	84	49	44	32	28	22	22	12	11	3	2	2

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m < > £25.9m.

66 These figures include firms which did and did not provide turnover data (47 of 191 respondents did not answer this question).

7. RESULTS FROM ADVISER FIRMS ON PERCEPTIONS REGARDING THE PROVISION OF SUPPORT FOR LLPs

The questionnaire survey also contained a section which specifically asked respondents to identify whether they themselves were providers of accountancy or legal services and to obtain their perceptions derived from advising clients who were LLPs. Of the respondents, 29% were either accounting or law LLPs. In addition, five professional adviser firms were interviewed as part of the follow-up interviews, comprising one sole practitioner accountant; a senior staff member in a small accounting firm (a limited company); a partner in a mid-tier national accounting LLP; a director in a Big Four accounting firm; and a partner in an international and national commercial law LLP.

Questionnaire respondents were asked to consider the extent to which advantages and disadvantages changed according to the sector in which an LLP operates, for example, an estate agent compared with a construction company or manufacturing firm. Some saw changes, whereas others did not, as reported in Table 51, although most could not say.

Table 51: Advantages and disadvantages of LLP for according to the sector in which they operate

	Unwilling/ unable to answer	Some change between sectors	Little change between sectors
All[67]	8	7	4
<=£100,000 (A)	2	0	1
£100,001 < >£1,000,000 (B)	4	4	1
£1,000,001< >£6,500,000 (C)	1	2	2
Small (=A+B+C) (D)	7	6	4
Medium (E)	1	1	0
Large (F)	0	0	0
Total (D+E+F)	8	7	4

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m <> £25.9m.

The mid-tier accounting LLP, Big Four LLP and legal LLP themselves had LLP clients which operated in a variety of industry sectors, but principally where protection of assets was required, given the nature of the business, for example, construction, nursing homes, etc, which could be sued for the provision of negligent services – although this was necessarily dictated by the type of businesses operating in the business area covered by their offices. As these were based in the north of England, they would not, for example, see much by the way of financial service activity or heavy manufacturing. It was felt that the drivers for firms converting to LLP status or setting up as LLPs were wholly commercial, for protection of assets, with a link to tax planning and other considerations, such as concerning goodwill.

Questionnaire respondents were also asked if there were firms which they would or would not advise to become LLPs, as reported in Tables 52 and 53.

67 These figures include firms which did and did not provide turnover data (172 of 191 respondents did not answer this question).

Table 52: Firms advised to become an LLP for the following reasons

	Business specific reason	Do not know	If are solicitors	If are professional firms	If useful for tax strategy	If are accountants	Anyone	If firm gives advice
All[68]	4	4	4	4	3	2	2	1
<=£100,000 (A)	0	1	0	1	1	0	0	0
£100,001 < >£1,000,000 (B)	2	1	2	2	0	2	1	0
£1,000,001< >£6,500,000 (C)	1	2	1	1	1	0	1	1
Small (=A+B+C) (D)	3	4	3	4	2	2	2	1
Medium (E)	1	0	1	0	1	0	0	0
Large (F)	0	0	0	0	0	0	0	0
Total (D+E+F)	4	4	4	4	3	2	2	1

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m<> £25.9m.

The above shows a perception that an LLP is useful for firms providing professional services/advice or a specific type of business, and also for tax reasons. Table 52 supports this, in that firms not giving advice or experiencing associated risk would not necessarily benefit from being LLPs. The need to comply with rules and regulations and keep good records would also mean that certain firms (eg, small or badly managed) could not operate in this form. Similarly firms which are already limited companies would have the benefit of limited liability and might not need to change to an LLP form, though earlier results suggest that some at least have done so. Firms needing to keep results or financial accounts secret would likewise not be able to use the LLP form. It is also clear from Table 52 that some advisers do not routinely think about advising on LLP form (the 'don't know' category is the largest here).

68 These figures include firms which did and did not provide turnover data (169 of 191 respondents did not answer this question).

Table 53: Firms advised against becoming an LLP

	Don't know	Most businesses	Those who desire financial discretion	Small firms	When compliance becomes too expensive	Non-professional sector businesses	Limited liability clients	Estate agents	Those without business risk	If incapable of keeping accounts or administering a business
All[69]	8	2	2	2	1	1	1	1	1	1
<=£100,000 (A)	2	0	0	0	0	0	0	0	0	0
£100,001< >£1,000,000 (B)	3	1	0	1	1	1	1	0	0	0
£1,000,001< >£6,500,000 (C)	2	1	0	1	0	0	0	1	0	0
Small (=A+B+C) (D)	7	2	0	2	1	1	1	1	0	0
Medium (E)	1	0	2	0	0	0	0	0	1	1
Large (F)	0	0	0	0	0	0	0	0	0	0
Total (D+E+F)	8	2	2	2	1	1	1	1	1	1

Source: survey of LLPs, summer 2011.

NB: Definition of firms: small: turnover < £6.5m; medium: turnover £6.5m<> £25.9m.

69 These figures include firms which did and did not provide turnover data (173 of 191 respondents did not answer this question).

In general, the above results were confirmed by the professional adviser interviewees. However, the Big Four director said that he had encountered extensive use of LLPs in the property investment sector, whereby an LLP was as an SPV for individual properties, as it allowed great flexibility, for instance, in dealing with property shares between partners. Indeed, he commented that the LLP was now the legal form 'of choice' for this industry sector. The law partner said that, as he had had some experience of the 1907 Limited Partnership Act being used for this type of activity, this use of the LLP was not surprising. In particular too, the LLP allowed for great tax transparency, which was also a significant characteristic, and the Big Four firm frequently advised on its use as a tax planning vehicle, subject to transactions being commercially driven in the first instance. All professional firms interviewed stressed that commercial considerations were always paramount.

The small accounting practice had four LLP clients – a solicitor, two computer businesses and a serial property entrepreneur, and had advised on the set-up of all except the solicitor's business. The rationale had been a combination of protection of assets and/or tax efficiency. For example, the serial entrepreneur found the form flexible and could take advantage of entrepreneurs' relief on the sale of businesses established and sold on. In this case, the entrepreneur had approached the firm with the idea of using an LLP. It was not necessarily what the firm might have advised as the best choice in the circumstances. Sometimes the LLP was not suggested as the most viable option, often in the case of a husband and wife partnership. It was, perhaps, more usual to advise its use where a number of non-family or unrelated people wished to set up in business.

It is interesting to note that the accounting sole practitioner interviewed had only once encountered an LLP, in terms of advising a client that this form might be worth considering, but had no LLP clients at all. He himself had not considered the form for his own business as he felt it would mean a certain loss of control. Were he to change form, he would be more likely to consider using a limited company. This latter appears to be common among small accounting practices which do not offer audit services, according to the small accounting practice interviewed. This latter practice had specifically not wanted to use the LLP form when moving from sole practitioner to limited company as it could not achieve the desired objectives of tax efficiency (use of taper relief at the time) and succession and continuity planning: a limited company allowed shares and share options to be offered as incentives to attract senior personnel, and as a legal person in its own right could survive beyond the lifespan of individual shareholders.

An acknowledged difficulty of working in a small advisory firm is keeping up to date with changes in legislation and regulations. Advisers who responded to the questionnaire and who were interviewed said that they kept up to date with developments in LLP regulations via professional courses, research on the Internet, via solicitors, reading the legislation, etc. The mid-tier partner and the Big Four director said that it was a great benefit to have national technical departments which issued technical update material on a regular basis, which made keeping up to date easier.

Questionnaire respondents who offered accounting or legal services were asked if they had noticed an increase in businesses converting to the LLP or establishing a firm using this legal format. Of respondents, 50% had, and 50% had not. When the same question was asked of the professional advisers interviewed, most were unaware of the significant increase evident, for example, on the FAME database, as reported on in this study, although not unduly surprised by it. The fact of businesses not immediately setting up or converting in great numbers was not a surprise, however. The mid-tier accounting partner said that his own firm had waited several years before converting, to avoid the 'pain' associated with being an early adopter. Both he and the small accounting practice suggested that some legal firms also took longer to convert than might have been anticipated. The law partner confirmed that this was the case. Particular issues that caused disquiet to law partnerships were whether use of the new form would cause additional (and high) tax liabilities to arise[70] and what would be the effects of disclosing financial information, which non-LLP partnerships were not obliged to do. A benefit of this disclosure was that clients were reassured by seeing robust financial information and details of how the firm was managed. Some more traditional law firms, however, still felt uneasy about the level of disclosure and had not converted, and disclosure meant a loss of control over information, as competitors and the press could use, interpret, etc, with freedom.

70 It was unclear initially as to what might happen, for example, as regards goodwill arising in the traditional partnership prior to conversion and whether this would deemed to be disposed of on conversion, thus generating a capital gain.

8. KEY HIGHLIGHTS/CONCLUSIONS

Key findings are highlighted and conclusions drawn by reference to the specific research objectives as set out in Section 2 of this report, although there is necessarily some overlap in the discussion.

(i) Objectives 1 and 5 (in part): To undertake an analysis of the distribution and sectoral/ geographical breakdown of LLPs in the UK, and thus establish the extent of the small and medium-sized business sector and its characteristics.

The distribution and character of LLPs in the UK is revealed using the Financial Analysis Made Easy (FAME) database which is compiled from the financial data supplied by firms in the UK to Companies House. Use of the FAME database to analyse LLPs has not been undertaken hitherto. As many small LLPs are exempt from supplying detailed data, two criteria have been applied to assess the prevalence of SMEs in LLPs. First, the balance sheet total (BST) was used to identify SMEs. From the FAME database, it was identified that of the total active 40,420 LLPs, BSTs could only be derived for 23,709 LLPs (of this 21,086 were small firms; 1,642 were medium firms; and 981 large firms). This meant that over 16,000 firms could not be classified according to size using BST. For this reason, it was decided to use an additional criterion to identify SME LLPs. This was: 'number of partners' in the LLP.

Using this search term, it was identified that the analysis of LLPs by reference to number of partners with and without BST, showed a clear correlation with regard to numbers of partners. For example, in the non-BST category of LLPs (Table 5), 71% (or 11,960 LLPs) had two partners (95.6% of respondents had five or fewer partners, equating to 15,635 LLPs). For BST-available LLPs (Table 6), 54.4% of LLPs (or 13,031) had two partners. This figure increases to 86% if we take into account LLPs with five or fewer partners. This means, therefore, that for both categories, having two partners was the most common form, with a slightly higher prevalence (16%) in the non-BST category of LLPs. This might be expected, given that the LLPs in the non-BST category are 'small', as highlighted by their exemption status, and are possibly new registrations, meaning that they not only need to submit accounts for 18 months (unless FSA-regulated), but also that they could be one-person businesses, provided that there is another member subscribing to the incorporation document. This was noted by Birds (2000, p2) and contrasts sharply with Freedman's (2001) critical perspective that LLPs were not suitable for micro businesses.

Overall, however, the distribution of LLPs across numbers of partners was very similar for both categories of LLPs with only marginal differences. It was also noted, for example, that there was only a small number of LLPs with 10+ partners (1.4% for non-BST LLPs; and for BST LLPs, there were 3.8% small LLPs and 25.2% medium-sized LLPs). However, a further interesting observation was that for the LLPs identified as large (via BST figures), 33% were reported as having two partners.

The use of 'number of partners' as a search term indicates that the BST and non-BST categorisations were fairly comparable in terms of numbers of partners and enabled us to categorise a larger number of LLPs for further analysis (rather than focusing only on those LLPs from which we could derive full BSTs). In summary, therefore, in terms of the active LLPs listed on the FAME database, the following statements can be made:

- Using the criteria of two partners within the LLP, 71% of all non-BST LLPs and 54% of all BST-available LLPs can be classified as SMEs.
- Using the criteria of five partners within the LLP, 95% of all non-BST LLPs and 86% of all BST LLPs can be classified as SMEs.

This signifies that the overwhelming majority of LLPs registered with Companies House are small and medium-sized LLPs. The high number of small LLPs is significant because, as stated above, the LLP was not a vehicle not designed specifically with SMEs in mind (see Finch and Freedman, 1997; Freedman and Finch, 2002; Henning, 2004.)

In terms of the LLPs responding to the survey, as was intended through the sampling process, 172 (93.5%) were small firms and 10 (5.4%) were medium-sized enterprises. In total, this equates to 99% of the respondent firms. Of the very small LLP category (up to £100,000 in turnover), this represented 26.1% of the respondents. The majority of respondent LLPs were in the £100,001–£1,000,000 turnover category which represented 45%, with 22% in the £1,000,000+ turnover band.

Of the respondent LLPs, 82% derive their income within the UK (48.8%) or within a 20 mile radius (33.6%). Many small LLPs thus provide very locally-based services, which is what might be expected of service LLPs. Only 17% had a percentage of income derived from EU or other markets outside the UK (8.8% and 8.9% respectively), but it can be noted here that some small LLPs are equally active in overseas markets as medium LLPs (especially for investment purposes, LLP 006).

In terms of the geographical distribution of LLPs, while there is a regional bias in the distribution of LLPs in general (with a bias towards London and the South East), there is a fairly stable level of active LLPs across all regions. In the majority of regions, over 60% of LLPs are active (with the West Midlands (59%) and Wales (56%) dropping below the average). The majority of LLPs is located in London (37%) and the South East (17.3%), which is not surprising, given that this is a recognised centre for business and professional service firm activity (Sassen, 2001; Dicken, 2003). The North East (1.9%), Wales (2.8%), and Scotland (5.4%), however, show small numbers of LLP activity (with Northern Ireland showing only 13 active LLPs).

(ii) Objectives 5 and 6: Key characteristics of SMEs and different forms and types.

As well as finding evidence of existing accountancy and legal firms converting to the new form, evidence can be found of firms operating in other industry sectors adopting the LLP form, both by converting initially and setting up from scratch. It has been difficult to assess the sectoral distribution of LLPs because it is not compulsory for LLPs to state the Standard Industrial Classification (SIC) when returns are sent to Companies House, but by using key word searches on company numbers, it was possible to classify 15,103 listings (with 1,786 property, 1,499 investment, 1,395 service and 1,229 management consulting LLPs at the top of the table, and 19 security, 19 advertising, 18 manufacturing, 11 plastering, 4 agricultural LLPs, at the lower end of the listing). The results indicate a spread across a wide variety of business activity with service firms appearing most numerous – and located with different degrees of density across the UK. While the expected sectors such as solicitors and accountants are evident (17% of the respondent LLPs were accountancy or law LLPs), there appears to be a plethora of consultants and advisers providing business to business services which could be within a range of industries from manufacturing to construction or general business management. This means that over 78% of the respondents did not provide either legal or accounting services. These data demonstrate the take up of the LLP format by LLPs in different sectors (McQueen, 2001; Openshaw, 2002; Tittensor, 2003; Banks, 2006) and the demand for a level playing field (Finch, 2001, p899, cited by Freedman, 2001). In addition, there is evidence from the survey and interviews that, as firms adopt the LLP format within a sector, similar firms are 'encouraged' to follow suit. This indicates that 'copycat' behaviour deployed to gain a strategic edge over competition (Enkel and Grassman, 2010; Shenkar, 2010) is also important alongside other benefits such as tax reductions.

A further objective of the project was to identify whether the extent to which LLPs are home-based businesses or not. Conceivably, working from home might be especially connected with the size of the business and the data support this in reporting that very small LLPs (with turnover less than £100,000) are predominantly home-based (52%). Interestingly, in the middle turnover bands (£100,001–£1,000,000) there are comparable numbers of home-based (41%) and office-based (47%) LLPs (which is indicative of flexible working patterns that tend to predominate in some professional sectors). However, in the higher levels of turnover (over £100,001+) these LLPs tend to be office-based. This is not surprising given that higher levels of turnover (usually) cohere also with larger numbers of partners.

(iii) Objectives 2, 3 and 4: Analysis of whether LLPs are registered as 'new start' LLPs, or whether they are existing businesses which evolve into LLPs; whether the LLP form has encouraged new firm start-up/economic activity.

Respondents were also asked to provide details about the establishment of their LLPs, including the date when founded, and whether they were set up originally as LLPs or converted from some other legal form. These data reflected that 58% of the respondents began their businesses as LLPs and 42% were original business entities prior to becoming an LLP. It can be noted that many firms did not immediately adopt the LLP form in 2001, but waited some years (waiting to see how the competition reacted was cited as a factor). 2010 saw an increase in numbers of registrations, perhaps reflecting economic recession factors. A further reason for late take up was that some larger customers and lenders viewed the new form with some suspicion in terms of how it operated legally and were not especially willing to trade with or lend money to LLPs until they had some better understanding of the form.

In spite of the slightly higher levels of new, rather than converted, registrations, it is difficult to claim that the LLP format is encouraging new economic activity per se because these entities may have been created via another form had the LLP not existed. What can be claimed, however, is that the 58% is indicative of the LLP format being used as a 'set up' vehicle for new venture creation. This is further supported by the fact that three-quarters of the LLPs are being set up with individual, as opposed to corporate partners. For the 'converting' LLPs, analysis is also given of previous legal form. Perhaps, not surprisingly, 21.4% were traditional partnership forms, with 8.8% sole traders and 6.9% limited companies. The highest percentages of conversions were in the £100,001–£1,000,000 turnover category, which captured 18.9% of all conversions. The reasons for conversion are broadly similar to the reasons for new adoption of an LLP (see discussion below). However, for conversion, the evolution of the business and succession planning were cited as two **additional** reasons, in that the new LLP structure afforded greater flexibility or the means to restructure in ways that were beneficial for succession planning. For example, it is relatively easy to change membership by completing forms (see Appendix 1). Consequently, the flexibility of the LLP appears to be particularly attractive alongside the potential tax and limited liability advantages.

Furthermore, it should be noted that just over 25% of the respondent LLPs have corporate partners (although many were not aware of what a corporate partner was, suggesting varying levels of knowledge, sophistication and planning within LLP members). The evidence of use of corporate members also indicates that some LLP formats were set up deliberately to take advantage of collective self-employment, where self-employed members group together to pool finance and skills while retaining liability protection. This concurs with Carney's (1999) observation that limited liability encourages investment in risky ventures. In this sense, for LLPs with corporate partners, rather than being an expression of entrepreneurship in the traditional sense of the single owner-managed business, creation of the LLP is instead an expression of distributed or team entrepreneurship. Such practices also challenge the traditional notion of organisational form, as some LLP formats seem to be representing what Miller et al. (2008, p942) refer to as 'hybrid' forms 'that make possible lateral information flows and coordination across the boundaries of organisations, firms, and groups of experts or professionals'. Such features are perhaps unique or special to the cultures of partnership organisational forms and the topic of LLP 'partnership cultures' is an interesting topic for further research. Expressed in another way, such practices are also consistent with portfolio entrepreneurship where business owners add new business entities to ongoing business arrangements (Birley and Westhead, 1993; Westhead and Wright, 1998; Westhead et al., 2003; Westhead et al., 2005).

This collective self-employment is further supported in the data on the different kinds of partnership types identified (ie, equity holding, fixed and salaried), with equity holdings being most common. Profit sharing ratios ranged from an equal division between partners, unequal but fixed division and variable, determinable annually. In some cases (6/175) the presence of a corporate partner was associated with the financing arrangements for the firm, though the majority of firms relied on assets provided by partners themselves (111/175) or bank funding (48/175) for their main forms of finance. LLPs also reported overwhelmingly that their LLP status had not affected their access to credit or borrowing. It was also often the case (38% of LLPs) that lenders would ask for personal guarantees from (particularly) directors of small entities which needed to borrow money, thus undermining the limited liability of such entities.

(iv) Objective 7: Understanding the rationales of small business owners for adopting the LLP format. A report on the actual and perceived benefits, the challenges of adopting an LLP (including tax and other benefits) and particular types of LLP.

There is a number of reasons why firms are reacting to the adoption of LLP format within their sector. This can be noted in responses such as being 'advised to adopt the LLP' (11%), or 'firm's image within the sector' (8%) or waiting to 'see how it worked out first' (1%). However, the main reasons cited by the respondent LLPs for choosing the legal form are tax advantages (35%), with limited liability benefits (32%) coming a close second. In spite of the limited liability attractiveness, it was reported that 96/143 respondents still had professional indemnity insurance (PII), although 47 did not (although 12 of these reported that PII was not applicable to them). The level of PII cover is difficult to comment upon, as it ranges from 'not applicable' to 'undisclosed'. It is, perhaps, unexpected to see tax reasons ranked higher than limited liability given that tax reasons were never one of the more publicised benefits of the form. Also, it is argued that being motivated by tax incentives can have a detrimental effect on commercial decision making (Freedman (2001, p909). No evidence was found on this point and if anything, partners gave strong commercial reasons for using the LLP which often centred on tax but also took into account other factors. There was also a set of respondents for whom the LLP provides certain flexibility, for example, in the potential ease of partners joining and leaving, or in gaining credibility with banks/customers, or enabling a more 'corporate' structure. In addition, some LLPs were using the LLP format to stay 'small' (and under the VAT threshold), avoiding employee costs/NICs and taking advantage of the self-employed status of their partners to circumvent employment law (see the case of *Tiffin v Lester Aldridge LLP* referred to earlier) at the same time as working with other LLPs to achieve growth. Moreover, many LLPs were set up purposefully as special purpose vehicles for particular short-term projects or investment strategies.

A factor reported in the literature review as potentially influencing a firm's decision to use the LLP form relates to whether any claim for negligence had been made against any partner. The evidence presented was that this was not a motivating factor prior to adopting the LLP (94% had not had a claim against them and 5% had prior to adopting the LLP; and post-LLP take-up, 93% had not had a claim made whereas 7% had). Instead, adoption of the LLP was more of a precautionary action. This suggests that organisational control in the form of regulatory mechanisms such as the LLP has **not** replaced occupational control and the means for self-regulation within professional practice as argued by Velayutham (1996, p366). Most firms also carried professional indemnity insurance, though this was not applicable in certain cases and there were firms who found it too expensive to take out.

In response to being asked if they had experienced any disadvantages with the LLP form, of 152 respondents, 39 said 'yes' (18 of these being LLPs with turnover between £100,001 and £1,000,000), and 113 'no'. The particular disadvantages identified by the survey respondents are by and large related to the technical side of accounting/taxation and compliance burdens, which inherently suggests that the new LLP partners did not fully realise the burdens which these matters would present or the responsibility they themselves would personally bear. The issue of 'institutions not understanding what an LLP is' was supported by one of the professional accountants interviewed, who commented specifically that banks and other lenders in early days did not fully appreciate the niceties of the legal form, treated it with some suspicion and were unwilling to lend funds (as noted also by Freedman, 2001). To verify this, respondents were asked if they had experienced any creditors/lenders requesting personal guarantees. Of 152 respondents, 67% reported they had not and 34% said they had, with banks being the lenders most frequently making such a request. This was an issue across all turnover categories but appeared to be more of a problem in the £100,001 to £1,000,000 category (with 15% of respondents). From the follow-up interviews 2/23 said that they were unhappy with the form and wanted to change but this related to the number of partners involved (more than 20) which made the accounting process very complex.

In conclusion to this part, it is clear that there are both advantages and disadvantages to the adoption of the LLP form. It seems evident that the technical disadvantages identified with the LLP prove challenging especially to the very small LLP (supporting Freedman, 2001), but that medium-sized firms use them with a higher degree of sophistication. We found extensive evidence that the LLP can be a useful vehicle for small business trading and the larger firms within the SME LLPs have been adept at utilising the form to good competitive advantage (eg, use of the form as an SPV for property transactions or for tax purposes), although the suggestion remains that some LLPs were set up and not used, possibly as a result of a certain trend/fashion developing or 'copycat' behaviour.

(v) Objective 8: Recommendation on the professional needs of small business sector LLPs, such as how their accountancy, taxation, payroll requirements are met (eg, whether this is done in-house, outsourced or by buy-in delivered on site; whether this changes as a business develops; and the types of accounting service provider used).

For LLPs converting to the LLP format, or setting up initially as an LLP, 71 LLPs reported that they 'advised themselves' or used 'in-house advice' to do so (viable if the firm was a legal or accounting firm) or obtained it from an accountant (80 respondents) or solicitor (30 respondents). Nine per cent of the respondents reported some disadvantages of the LLP format (less flexible than anticipated, compliance burdens). However, less than 3% of LLPs professed complete dissatisfaction with the LLP (one case) or were displeased with advice to adopt the LLP (one case). These reasons related to the perceived unsuitability of the LLP for SMEs (two cases) and misunderstandings about the implications of the LLP (as too bureaucratic or inflexible – two cases). An overwhelming majority of respondents reported satisfaction with the advice they had received, and with the way the LLP operated. It was clear that there was an added burden of legal compliance, however, which not all firms had anticipated, but in general the form was regarded as a very flexible means of doing business, and relatively easy for partners to leave and join.

Finally, LLP were also asked if their accountancy and taxation needs had changed over time, as a result of LLP status. Out of 149 firms that responded to this question, 95 firms said that their needs had not changed, with 54 saying that they had. The reasons provided for the changes were generally added complexity in meeting financial reporting and accounting requirements, and more specialist tax advice being needed because of the financial circumstances of individual partners or because individuals had become partners (rather than being sole traders). However, some of the reasons for changes were clearly because of business expansion, for example, growth in staff numbers and the need to register for VAT as turnover increased. Of the respondents, 51% reported that they outsourced their taxation and accountancy requirements, while 46% undertook these activities in-house.

As Miller et al (2008, p942) point out, 'accounting practices are central to these issues, in so far as accounting is constantly engaged in a dual hybridisation process, seeking to make visible and calculable the hybrids that it encounters'. Thus, the widespread of adoption of LLPs (or more significantly, the way they are being used) has important implications for accountancy services.

The professional advisory firms interviewed added considerable contextual background to the results of the questionnaire survey and LLP interviews, commenting on the LLP being used to limit partners' liability and as a tax planning, efficiency or minimisation vehicle. However, all stressed the need for appropriate commercial drivers in setting up or converting, hence the use of the form for SPVs, especially in the property sector, where it was now the legal form 'of choice' because it worked well, offering much needed flexibility, which other legal forms did not. It was acknowledged, however, that some firms (especially legal firms) had waited, often some years, before converting, as a result of initial lack of clarity over whether tax liabilities would result from the transition. A similar disquiet had existed among professional lenders, initially reported as unwilling to lend money to LLPs because of similar uncertainties over how the form would operate, and which had eased as greater familiarity with the form developed.

APPENDIX 1: REGULATIONS GOVERNING LLPs AND OTHER PARTNERSHIPS

There are three kinds of partnerships in the UK – general, limited liability (LLP) and limited.

General partnerships
A partnership exists where two or more persons (including legal persons, such as a company) act together, usually to make a profit. Profits (and losses) are shared between the partners, commonly to reflect the proportions in which they contributed capital to the business, although partners may agree to share profits in any way that they choose. Partners will usually include details of their profit sharing arrangements in a partnership agreement, which is a formal arrangement setting out the rules by which the partnership should be managed and administered. This is commonly reflected in a written document, but can be an oral agreement. If an agreement does not refer to profit sharing arrangements, profits will usually be shared equally, as per the provisions of the Partnership Act 1890 in the UK. Accounting for partnership profits/losses means that all profits/losses will automatically be allocated to partners at the end of a financial period. This is different from companies in that company profits are not automatically allocated to individuals, although they may be distributed to shareholders by way of dividends. (Company losses cannot be distributed.)

A partner's share of profits is added to his/her other income and taxed accordingly (mirroring the situation with a sole trader). The partnership is not itself taxed in respect of the business profits generated. A company, however, will pay corporation tax on its taxable profits and any dividends to ordinary shareholders will be paid out of the post-tax profits. If a company is itself a partner in a partnership, its share of partnership profits is added to other income subject to corporation tax. General partnerships are not required to be audited, although many choose to be, nor to disclose publicly their financial statements.

Partners have legal authority to act on behalf of the business to bind all the other partners in contracts with third parties that are in the normal course of the partnership's business. Partners (like sole traders) are personally liable for any debts incurred by the partnership, so there is no protection offered to their personal assets if there is any default on business debts. They have joint and several liability for debts. The death or withdrawal of a partner or an inability to act because of disability will terminate a partnership, but most agreements will contain provisions to deal with these types of events, and the share of a defunct partner will usually purchased by the remaining partners.

LLPs
All of the above apply similarly to an LLP (except as detailed below). The key difference is that liability of partners is restricted to the amount of capital they have invested such that their personal assets are not at risk and that an LLP is a legal person, which other kinds of partnership are not.

The main legislation that applies to limited liability partnerships is as follows:

- The Limited Liability Partnerships Act 2000.
- The Companies (Late Filing Penalties) and Limited Liability Partnerships (Filing Periods and Late Filing Penalties) Regulations 2008, SI 2008/497.
- The Limited Liability Partnerships (Accounts and Audit)(Application of Companies Act 2006) Regulations 2008, SI 2008/1911.
- The Small Limited Liability Partnerships (Accounts) Regulations 2008, SI 2008/1912.
- The Large and Medium-sized Limited Liability Partnerships (Accounts) Regulations 2008, SI 2008/1913.
- The Limited Liability Partnerships (Application of Companies Act 2006) Regulations 2009, SI 2009/1804.
- The Companies and Limited Liability Partnerships (Accounts and Audit Exemptions and Change of Accounting Framework) Regulations 2012, SI 2012/2310.

The provision of limited liability to partners came at the price of additional regulations. An LLP must be registered, like companies, at Companies House. The regulations set out below mirror those applicable to companies, except that LLPs are taxed in the same way as general partnerships. The details below are extracted from the Companies House website,[71] although the full set of regulations are much more extensive than those given here. An LLP must keep:

- a register of members and the register of members; and
- the register of members' residential addresses.

The register of members contains for each member who is an individual:

- his or her name and any former name;
- a service address (which may be stated to be 'the LLP's registered office');
- the country or state or part of the United Kingdom where he or she is usually resident; and
- whether the member is a designated member (two are required).

(A designated member can appoint an auditor, sign the accounts on the behalf of another member and perform the same sort of duties that a company secretary performs for a company.)

For members that are corporate members or firms, the register of members will include:

- its corporate or firm name;
- its registered or principal office;
- in the case of an European Economic Area (EEA) company, where it is registered and its registration number; otherwise, the legal form of the company or firm and the law by which it is governed and, if applicable, where registered and its registration number; and
- whether the member is a designated member.

It is relatively easy (compared with general partnerships) to change an LLP member, and the Companies House website provides forms to complete for doing so.

If the LLP issues debentures it must keep a register of debenture holders and if it enters into a charge it must keep a register of charges together with the instrument creating the charge.

All these registers (other than the members' residential address register) must also be kept available for inspection.

All or any of these records may be kept at the LLP's registered office. The LLP may choose an alternative location to make these records available for inspection. The LLP can only have one alternative location to the registered office at any given time.

Every LLP must deliver ('file') an annual return to Companies House within 28 days of its made-up date (usually the anniversary of the incorporation of the LLP or the made-up date of the previous annual return registered at Companies House). An LLP's designated members are responsible for ensuring that they deliver the annual return to Companies House and that it gives a true picture of the LLP at the made-up date. If an annual return is not delivered, the registrar may assume that the LLP is no longer in business or operation and take steps to strike it off the register.

An annual return is a snapshot of information at the made-up date. It is separate from the LLP annual accounts. An annual return must contain the following information:

- the name of the LLP;
- its registered number;
- the date to which the annual return is made up;
- its registered office address;
- the address where any LLP records are kept if not at the registered office, and the records that are kept there; and
- details of all the LLP's members (corporate or individual), and whether they are designated members.

71 'Latest guidance – Limited Liability Partnerships' [online]. Available at URL www.companieshouse.gov.uk/about/guidance.shtml, [accessed 5 November 2012 and 2 January 2013].

Every LLP must prepare accounts that report on the performance and activities of the LLP during the financial year. This starts on the day after the previous financial year ended or, in the case of a new LLP, on the day of incorporation.

LLPs normally have nine months to submit their accounts to Companies House after the end of each accounting reference period. The period allowed for submitting an LLP's first accounts and for changing its accounting reference date, however, is subject to different rules.

An LLP (and any subsidiaries) must keep accounting records at its registered office address or a place that the members think suitable. The records must be open to inspection by the LLP members at all times.

An LLP must keep its accounting records for three years from the date they were made.

Every LLP must send a copy of its annual accounts and auditor's report (where applicable) for each financial year to every member of the LLP and every holder of the LLP's debentures. The LLP must also send the accounts to Companies House.

Generally, a set of financial accounts must include:

- a profit and loss account (income statement);
- a balance sheet signed by a designated member on behalf of the board and the printed name of that member;
- notes to the accounts; and
- group accounts (if appropriate).

Accounts must be accompanied by an auditor's report stating the name of the auditor and signed and dated by him (unless the LLP is exempt from audit).

The auditor's report must include:

- an introduction identifying the accounts that are the subject of the audit;
- a description of the scope of the audit identifying the auditing standards and the financial reporting framework that has been used in the preparation of the accounts;
- a statement as to whether in the auditor's opinion the accounts have been prepared in accordance with the Companies Act 2006, as applied to LLPs and, where appropriate, in accordance with Article 4 of the EU Regulation on International Standards (Regulation (EC) 1606/2002, the 'IAS Regulation');
- a statement as to whether the accounts give a true and fair view of the LLP's or, (in the case of group accounts), the group's financial affairs;
- if the auditors are of the opinion that the LLP has not kept adequate accounting records, a statement to that effect; and
- if the LLP has not provided the auditors with all the information they need to complete the report, a statement to that effect.

The auditor's report must be either unqualified or qualified and must include a reference to any matters to which the auditors wish to draw attention by way of emphasis without qualifying the report. The auditor will qualify the report either where there has been a limitation on the scope of the auditor's work or where there is a material disagreement between the LLP and the auditors about the accounts.

There are three sizes of LLP to consider when preparing accounts: small, medium or large. There are thresholds for turnover, balance sheet total (meaning the total of the assets) and the average number of employees which determine whether the LLP is small or medium-sized. Any LLP that does not meet the criteria for small or medium is a large LLP and will have to prepare and file full accounts.

A small LLP can prepare and file accounts according to special provisions in the Companies Act 2006 as applied to LLPs and relevant regulations. This means that they can choose to disclose less information than medium-sized and large LLPs. They do not have to deliver a copy of the profit and loss account to Companies House. Small LLPs preparing non-IAS accounts can deliver an abbreviated balance sheet, but small LLPs preparing IAS accounts must deliver a full balance sheet to Companies House. If a small LLP files abbreviated accounts, a special auditor's report must also be filed, unless the LLP is exempt from audit.

A small LLP must meet at least two of the following conditions:

- annual turnover must be not more than £6.5m;
- the balance sheet total must be not more than £3.26m;
- the average number of employees must be not more than 50.

Certain LLPs cannot qualify as small, for example, those whose securities are admitted to trading on an EEA regulated market, those which are part of a group which has members who are public companies or certain financial services LLPs or companies.

There is also an exemption from having an audit for certain small LLPs if they are eligible and wish to take advantage of it. For financial years ending before 1 October 2012, to qualify for audit exemption as a small LLP, an LLP must:

- have a turnover of not more than £6.5m; and
- have a balance sheet total of not more than £3.26m.

For financial years ending on or after 1 October 2012, a small LLP must meet any two of the following:

- annual turnover must be not more than £6.5m;
- the balance sheet total must be not more than £3.26m; and
- the average number of employees must be not more than 50.

If a small LLP qualifies for audit exemption, it may submit unaudited accounts to Companies House in the form of an abbreviated balance sheet and notes or, if it chooses, full accounts.

As with a small LLP, a medium-sized LLP is determined by its turnover, balance sheet total (meaning the total of the assets) and average number of employees. A medium-sized LLP can prepare accounts according to special provisions applicable to medium-sized LLPs. It can also choose to submit reduced information to Companies House.

Certain financial services LLPs, and LLPs whose securities are admitted to trading on an EEA regulated market, cannot qualify as medium-sized LLPs. Similarly, LLPs which are part of a group which has members who are public companies or certain financial services LLPs or companies cannot qualify as medium-sized for accounting purposes.

To be a medium-sized LLP, at least two of the following conditions must be met:

- annual turnover must be no more than £25.9m;
- the balance sheet total must be no more than £12.9m; and
- the average number of employees must be no more than 250.

Generally, an LLP qualifies as 'medium-sized' in its first accounting period if it fulfils the conditions in that period. In any subsequent period, an LLP must fulfil the conditions in that period and the period before. This also applies to LLPs deemed small.

Abbreviated accounts of a medium-sized LLP must include:

- the abbreviated profit and loss account (this must be full if preparing IAS accounts);
- the full balance sheet, showing the printed name and signature of a designated member; and
- notes to the accounts.

They must be accompanied by a special auditor's report.

Limited partnerships
A limited partnership is characterised by the having one or more limited partners in addition to the general partners. The form was an earlier attempt to limit the liability of partners. The position of the general partners is the same as in a general partnership, but the limited partners, however, have limited liability. They are only liable on debts incurred by the firm to the amount of their registered investment. They have no management authority, which is the sacrifice they make for having limited liability. The limited partners usually receive from the general partners a return on their investment, the nature and extent of which will commonly be set out in the partnership agreement. Limited partnerships are still found (although they are rare in comparison with the occurrence of other partnership forms), and they are governed in the UK (except for Scotland) by the Limited Partnerships Act 1907 (the Companies Act 2006, s1286(1)(b) extended the enactments in force in Great Britain relating to limited partnerships to Northern Ireland).

The situation as regards Scottish limited partnerships is different, in that in addition to the characteristics outlined above, a Scottish limited partnership has separate legal personality, which means that it possesses a characteristic associated in the rest of the UK only with LLPs. This legal form has been used by various investment-type firms. It is outside the scope of this project to examine aspects of Scottish limited partnerships and the extent to which any might have changed to using the LLP format, other than as part of the general sample surveyed in this project.

APPENDIX 2: TABLES

Table of statutes
Companies Act 1989 (Elizabeth II. Chapter 40)

Companies Act 2006 (Elizabeth II. Chapter 46)

Limited Liability Partnership Act 2000 (Elizabeth II. Chapter 12)

Limited Liability Partnerships Act (Northern Ireland) 2002 (Elizabeth II. Chapter 12)

Limited Partnerships Act 1907 (7 Edw. VII, c.24)

Partnership Act 1890 (53 & 54 Vict., c.39)

Table of statutory instruments
Companies and Limited Liability Partnerships (Accounts and Audit Exemptions and Change of Accounting Framework) Regulations, SI 2012/2301

Companies (Late Filing Penalties) and Limited Liability Partnerships (Filing Periods and Late Filing Penalties) Regulations 2008, SI 2008/497

Large and Medium-sized Limited Liability Partnerships (Accounts) Regulations 2008, SI 2008/1913

Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008, SI 2008/1911

Limited Liability Partnerships (Application of Companies Act 2006) Regulations 2009, SI 2009/1804

Small Limited Liability Partnerships (Accounts) Regulations 2008, SI 2008/1912

Table of cases
Tiffin v Lester Aldridge LLP [2012] EWCA Civ 35

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