Structuring for success:
achieving the optimum business structure

An essential requirement for most business structures is limited liability: without this protection against failure many businesses would simply not assume the commercial risks necessary to succeed. This being so, the available choice of structure is not one of infinite variety but essentially between a Limited Liability Partnership (LLP) or Limited Company. Both provide limited liability to their members or shareholders.

While tax may dominate considerations of structure, it is not the only or main determinant. A number of commercial considerations should be taken into account and their relative importance may alter over the life cycle of the business. The main attribute therefore is flexibility: an ability to accommodate the changing commercial requirements of the business and its owners over time. In terms of flexibility, the LLP is the more attractive base structure. Its flexibility is evident in a number of important areas to business owners.

The profits of an LLP may be allocated on a wholly discretionary basis. By comparison, the allocation of profit by a Limited Company is necessarily constrained by the fixed shareholding percentages held by the owners.

Making distributions is completely flexible: the LLP may distribute profits, advance loans, and return capital with minimum formality. The Limited Company requires reserves to distribute and must meet strict company law requirements in making loans and returning share capital, whether by way of share buyback or liquidation.

The admission of new members (and retirement of old) does not involve any great formality – the simple execution of a deed of adherence to the Members Agreement being enough. Compare this with the relative difficulty in introducing new members into a Limited Company (in funding the acquisition of shares or in dilution of other shareholder's interests) and of removing director shareholders and in recovering their shares (employment rights, valuation, and funding the purchase).

If flexibility is the main advantage of the LLP, then it is taxation and the tax deferral benefits that bring the Limited Company into consideration. The profits of the LLP are charged directly on its members as they arise (are recognised in the accounts) and irrespective of whether the profits are distributed or retained in the business. In contrast, a Limited Company is taxed independently from its shareholders and pays Corporation Tax at a rate of 19% on its profits. There is no tax charge on the shareholders until those profits are distributed as dividends or returned on liquidation. The Limited Company therefore offers a material tax deferral (of as much as 28%) as compared to the members of an LLP where the individual might be paying Income Tax at a marginal rate as high as 47%.

Where profits are invested as working capital then a Limited Company may be the preferred option. Similarly, on an exit the Limited Company may be favoured as many purchasers still regard an LLP (unfairly) with some suspicion when it comes to making a corporate acquisition. Notwithstanding, flexibility is key and the LLP will generally be favoured, not least as it is a relatively simple matter to fully incorporate an LLP into a Limited Company (and on a tax neutral basis) than disincorporate a Limited Company!

Please contact Neil Simpson, or your usual haysmacintyre contact, for further details and assistance in relation to the above.

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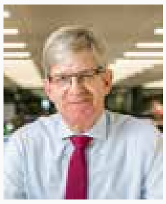

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