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lawyers for alternative investments

## LLP agreement questionnaire



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## 1. Introduction

One of the advantages of a limited liability partnership (LLP) is that the LLP is a corporate business vehicle with a legal personality separate from that of its members, who have a limited liability only. An LLP can do anything that a natural person can do, including hold property, enter into contracts, sue and be sued. An LLP may issue debentures and give fixed and floating charges over its assets in the same way as a company. The LLP owns the assets of the business and is liable for its own debts; the members act as its agents and only have liability up to the amount they have contributed to the LLP (subject to any regulatory requirements). As a separate legal entity, changes in the membership of the LLP do not therefore affect its continued existence.

However, the LLP also has the organizational flexibility of a partnership in that it is treated for tax purposes as a partnership. The Finance Act 2014 introduced new anti-avoidance rules, under which certain salaried members of LLPs are treated as employees for tax purposes, rather than partners. Assuming these deemed employment rules do not apply, the general position is that the actions and property of the LLP are attributed to the members of the LLP. Members are assessed to tax on their share of an LLP's income or gains in the same way as if they were members of a general partnership, subject to anti-avoidance provisions relating to the artificial allocation of excess partnership profits or losses. Individual members of an LLP will accordingly be liable to income tax or capital gains tax on their share of the income profits or gains and corporate members will be liable to corporation tax. NI contributions for members are also lower as for partners in a partnership.

For more information on the 2014 anti-avoidance rules, please see the publication entitled 'Taxation of Partnerships and LLPs' on our website at: [www.cummingslaw.com/publications2](http://www.cummingslaw.com/publications2).

Although it is a corporate vehicle and similar to a company in that its accounting and filing requirements are broadly the same, an LLP is unlike a company in that it has no share capital and members' capital can be withdrawn (unlike shares which have to be sold or transferred), is not subject to any capital maintenance requirements, although it may be subject to regulatory capital requirements where applicable, with the additional advantage that the LLP agreement is a private document which is confidential to the members.

Incorporation of an LLP creates legal obligations under the Limited Liability Partnerships Act 2000 (the "Act") and the members are strongly recommended to set up an LLP Agreement to agree how these obligations are to be shared. In the absence of specific agreement, a set of default regulations would apply which in many cases are not appropriate.

When drafting an LLP agreement, the following major issues should be considered, but please note that these are not comprehensive and do not address all issues which may be relevant in all circumstances:

## 2. Members

- 2.1 Who will be a member, of which there must be at least 2, and will there be a minimum and maximum number of members?
- 2.2 Who will be the designated members, of which there must be at least 2, who will be responsible for the compliance of the LLP with relevant legislation (similar to a company secretary)?
- 2.3 What will be the method for appointing new members?
- 2.4 How will members be expelled or removed (see also clause 6)?
- 2.5 Is a specific retirement age required and will retirement or death of any particular member affect the continuation of the LLP?
- 2.6 May a member dispose, transfer or assign his interest in the LLP (see also clause xxx)?



*NB. Under the default provisions, no power to expel exists and there is no automatic right to withdraw capital upon death or retirement.*

### 3. Capital contributions and profits

- 3.1 What will be the initial capital contribution of each member?
- 3.2 How will further contributions be decided and will any members be making a loan to the LLP?
- 3.3 How will the capital contributions of incoming/outgoing members be dealt with and will there be any pre-emption rights in respect of the introduction of new capital?
- 3.4 What arrangements are there for further funding and will it be necessary to take any regulatory capital requirements into account?
- 3.5 Will interest be payable on capital or undrawn profits?
- 3.6 What is the division of shares in capital, profit and losses to be and how will incoming/outgoing members affect the division of profits and losses?
- 3.7 Will any members have a fixed remuneration rather than a share in the profits i.e. deemed to be employed (albeit that the general position is that members are self-employed)?
- 3.8 Will advance drawings be permitted and, if so, how will these be funded and who will decide how much?
- 3.9 Will there be provision for future working/regulatory capital and how will expenses be divided or will these be deducted before profits are allocated?

*NB. Under the default provisions, all the members are entitled to share equally in the capital and profits of the LLP and the LLP shall bear its own losses.*

### 4. Management of the LLP

- 4.1 How will the LLP be managed and who will be responsible for decision making i.e. will this be through a managing member,

a management board or jointly by the members?

- 4.2 On what basis will decisions be made and what are the voting procedures?
- 4.3 Will any member have a veto or a deciding vote or are there any decisions on which a member will not be allowed to vote?
- 4.4 If applicable, how will a deadlock be resolved?
- 4.5 When, how and how often will meetings be called and what will be the quorum?
- 4.6 What protection is to be provided to minority members and will unfair prejudice be excluded?

*NB. Under the default provisions, all the members may take part in the management of the LLP and exclusion could lead to a claim for unfair prejudice, ordinary matters may be decided by majority vote and unanimous consent is required for transfers of interests, new members and change to the nature of the LLP's business*

### 5. Duties and obligation of the members

- 5.1 Will each member have the ability to bind the LLP (and every other member) as a whole?
- 5.2 If the business of the LLP is separated into various parts, what should the responsibility and liability of each member be in relation to each part?
- 5.3 What is the extent of the liability of the LLP: will it provide a blanket indemnity to the members or should liability be excluded for acts of negligence, breach of contract or dishonesty on the part of the particular member?
- 5.4 Should each member indemnify each of the other members for acts of negligence, breach of contract or dishonesty on their part?
- 5.5 Should certain fiduciary duties be expected of each member, such as duty to act in good faith, duty to use best endeavours to promote the business of the LLP etc.?



- 5.6 Should there be a duty to account for profits and benefits derived from a competing business or is there any carve out to consider?
- 5.7 Is each member required to devote his whole time and attention to the business or is there any carve out to consider?
- 5.8 Should there be a duty to promote the LLP for the success of all members?
- 5.9 Are any other specific obligations required?

*NB. Under the default provisions, there is no express duty of good faith and as agents, each member is likely to owe fiduciary duties to the LLP but not to each other. If a member carries on any business of the same nature as and competing with the LLP without the consent of the LLP, that member must account for and pay over to the LLP all profits made by him in that business. Further, every member must account to the LLP for any benefit derived by him without the consent of the LLP from any transaction concerning the LLP, or from any use by that member of the LLP property, name or business connection.*

## 6. Retirement, removal and exit

- 6.1 Upon what grounds may a member be removed or expelled from the LLP?
- 6.2 What is the length of notice to be given for removal and by whom?
- 6.3 What happens to an outgoing member's interest in the event of removal/retirement or death?
- 6.4 Consider good leaver/bad leaver provisions?
- 6.5 Consider capital and income entitlements, both past and future, and will there be a staged release?
- 6.6 Continuing obligation of confidentiality
- 6.7 Consider what restrictive covenants should apply, their duration and geographical scope and whether exclusions can be negotiated for certain clients
- 6.8 Consider garden leave and suspension and the procedure to be followed
- 6.9 Will the outgoing member give or receive an indemnity?

## 7. Transfer of interests

- 7.1 Will there be an initial lock-up period?
- 7.2 If transferable, under what circumstances e.g. death, bankruptcy, retirement, expulsion etc.?
- 7.3 Are transfers restricted and will pre-emption rights or drag and/or tag rights apply?
- 7.4 If transfers of interests are restricted, will there be exceptions for transfers agreed to by all the remaining members or permitted transfers (to which pre-emption rights will not apply) to families/family trusts or within a company group?
- 7.5 How will capital interests be valued for transfer purposes?
- 7.6 What are the rights/obligations of outgoing members regarding repayment of loans, return of assets etc.?

*NB: The default provisions are silent on transfer of interests.*

## 8. Winding up of the LLP

- 8.1 Do certain events cause automatic winding up e.g. insolvency, bankruptcy of member, transfer of capital interests, change of control of member, death of managing member, loss of licence etc.?
- 8.2 Do members have the right to wind up the LLP where there is a change of control, deadlock, material breach of LLP Agreement or on notice?
- 8.3 What are the consequences of winding up – how will capital and income profits be distributed?
- 8.4 Ensure there is a provision stating that members are not liable to contribute to the LLP's assets (losses) on its winding up

*NB: Under the default provisions, all members will be required to contribute to the LLP's assets on a winding up.*



## 9. Governing law

- 9.1 Which law is to apply?
- 9.2 Will there be any dispute resolution procedure?
- 9.3 Will arbitration apply?

## 10. Miscellaneous

- 10.1 Insurance
- 10.2 Ownership of property, including IP, of the LLP
- 10.3 Appointment of auditors
- 10.4 LLP bank account signatories
- 10.5 Holidays, sick leave, maternity/parental leave
- 10.6 Regulatory issues, such as FCA authorization
- 10.7 Confidentiality
- 10.8 Access to books and records
- 10.9 Employees



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