CARTER BOND SOLICITORS

What are the differences between a Partnership and a Limited Company?

Choosing the correct legal status for your company can be challenging. There are various differences between each type of entity and your decision can have far-reaching consequences for you and your business, ranging from tax benefits to your level of personal liability.

Firstly, let's look at the difference in setting up a limited company and a partnership. To set up a limited company the people or organisations who own shares in the company must register it with Companies House and advise HMRC of the commencement of business activities. To do so, there must be at least one director and one shareholder, and articles of association.

On the other hand, the Partnership Act 1890 provides that a partnership can be automatically formed simply by virtue of carrying out business with another person, with the purpose of making a profit. That being said, the procedures for setting up an 'ordinary' business partnership or limited liability partnership do not differ greatly from those involved in incorporating a limited company, except that there is no need for articles of association. Nor is there any need to name the directors who will run the company or the shareholders who own it, as partnerships are owned and run by individual partners.

Next, let's look at the liability differences.

Shareholders in a limited company cannot be held personally responsible for the business' liabilities, whereas partners can be held personally liable for a business' debts. However, LLPs offer a good middle ground, as each partner's level of liability depends on the terms of the partnership agreement and on their initial investment into the company.

As mentioned, in a partnership the partners are the business owners, but are also responsible for the day-to-day operations of the business. In a limited company, directors handle the running of the business and shareholders do not (although in practice, shareholders and directors are often the same people).

Next, let's talk about the differences in financial transparency.

When it comes to company accounts, limited companies are required to publish a basic financial summary of their annual accounts. On the other hand, partnerships are not required to audit or publish their accounts, no matter how much the company's turnover grows.

There are also differences in tax implications.

With a limited company, leaving any profits in the company accounts means your corporation tax may be lower than the income tax rates paid by the partners. If you are planning on re-investing profits into the business, then a limited company offers an advantage in this respect. Note, however, that while partners and directors pay the same income tax rates, directors in a limited company pay much higher National Insurance contributions than partners, which substantially increases the overall tax liability for both the business and the individual. As a result, to pay a director the same net salary as a partner, the company would need to be earning a great deal more than its partnership equivalent.

When deciding on a legal status, it is therefore imperative that you carefully consider your financial goals and how you plan to manage your capital accounts in the long run.

Tax is of course also very important and how this is treated can be quite different between a company and a partnership. This note does not cover tax but you should ensure to speak to an accountant or specialist tax advisor to understand the implications.

Finally, let's talk about the differences in ownership. Share ownership in a limited company is typically considered more flexible than ownership in a partnership. Share schemes and director positions can also be used to incentivise staff in a limited company.

In a partnership, 'salaried partners' and 'equity partners' can be appointed and enjoy partial ownership of the company, but in the case of the latter, legal complexities make this a more difficult process than in the case of share ownership.

So as you can see from some of the key differences between a limited company and a partnership the legal status of your business is integral to every aspect of how you will do business in the long term, so specialist legal advice and a detailed business plan are crucial.

For more information, or for expert advice on business or personal legal issues, call us on +44 (0)20 3475 6751 or via email at info@carterbond.co.uk

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Enis Rifat, MIYA Solicitors

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