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The Corporate that Dare not Speak its Name

ByChris Cook

There's only one thing worse than being wrong if you are a Civil Servant, and that is to be right by accident.

That is what the UK's Department of Trade and Industry have found since they were virtually blackmailed by the UK accountancy profession into legislating the "new" UK Limited Liability Partnership ("LLP") in 2001 about five years after two of the big accounting partnerships spent over £1m on procuring Jersey LLP legislation.

Enter the law of Unintended Consequences.

As they are perhaps beginning to realise, the DTI appears to have accidentally created an optimal and "non-toxic" Corporate form which potentially makes all existing corporate forms redundant.

Because despite its misleading name, the UK LLP is NOT (like the US LLP) a Partnership some of whose members limit their liability, but is instead - like a Company - a "Corporate" form with a continuing legal existence independent of its Members.

As with a Limited Company, a Member cannot lose more than he invests, but unlike a Limited Company, an LLP is tax transparent (ie it pays no tax itself, but Members do on the income or gains made through it)

Moreover there is none of the legal burden necessary under Companies legislation to manage the conflicts between shareholders, directors and other stakeholders. In fact there isn't even a requirement for a written LLP agreement at all.....

At a cost of just £20 is it any wonder that they are breeding like rabbits?

Although almost half of UK solicitors are LLPs or about to be, it is the other uses to which this new legal wrapper is being put in the commercial sector which are most fascinating, since they open up entirely new options for investment as the Hilton Group showed in late 2002 when they entered into a £350m "Capital Partnership" LLP with a consortium of financiers and developers (itself an LLP) where there is no mortgage, and no "sale and leaseback" but instead a 27 year revenue-sharing arrangement.

Such a sharing of risk and reward between "Capital provider" and Capital user" will be immediately recognisable to your Muslim readers as consistent with Islamic Values and they will point out that this way of doing business pre-dates Islam by a thousand years or more..

However, you will find that not only is the DTI racking their brains how to put the LLP genie back in the lamp but there appears to be almost a conspiracy of silence in the world of professionals and consultants.

Why? Because anyone paid by the hour, not the outcome, profits from the conflicts and complexity inherent in existing "enterprise models" and has no interest whatever in the sort of simple consensual agreements which have been the norm in collaborative societies such as Japan for centuries.

Just one example of what is possible using this form may be instructive.

Eurotunnel is now in the throes of a Court-supervised disputed restructuring at the heart of which is the irreconcilable conflict between the claims of "Equity" and "Debt" capital.

Imagine if a Eurotunnel Capital Partnership LLP were incorporated uniting Eurotunnel SA (as Capital user) and Investors in (say) a billion proportional "Equity shares" of Â£6.00 each created and used to repay the existing debt of Â£6bn.

Now the maximum amount of Eurotunnel gross revenues available for financing is maybe Â£240m which constitutes (say) 50% of Eurotunnel gross revenues.

First we repay this Capital over a pension fund time horizon of (say) 50 years. But the Alchemy is that we don't pay back Â£120m each year which then erodes in value with inflation. Instead we pay back as a Capital repayment each year 25% of Eurotunnel gross revenues.

Secondly, we pay a return on Capital of (say) 2%. Again, this Capital rental is initially Â£120m or 25% of Revenues, but this will decline over time as Capital is repaid so that after 25 years 12.5% is paid as a "Capital Rental", with the balance to the "Capital User" member ie Eurotunnel SA.

The outcome is a simple but elegant new synthesis - "Shares" but "not as we know them, Jim".

For the investors it's a share in GROSS Eurotunnel revenues BEFORE the management and operating staff get their hands on it. Would you rather drink the water before it goes into the bathtub, or after it comes out of the plug-hole?

So If Eurotunnel has a good year, then so do the investors, and even if revenues rise only with inflation the outcome is a 2% index-linked return with Capital protected against inflation.

It's not Rocket Science is it? Which is why you won't hear of it from the City or Wall Street.

The LLP is indeed the "Corporate that dare not speak its name"