A model partnership

Lockton is set to become the biggest intermediary yet to become an LLP broker. Edward Murray looks at the benefits of such a transformation.

LOCKTON INTERNATIONAL aims to complete its transformation to a limited liability partnership on 1 December and in doing so become the biggest insurance broker to make the change.

In April 2009, London market insurance and reinsurance broker Newman Martin and Buchan also made the move, but few others have been tempted despite legislation introducing LLPs to the UK landscape coming into force back in 2001.

Lockton International is very clear on its motivation for changing to LLP status and says it has been driven by a desire to change the culture of the organisation and to give a greater say to its senior people in the way the business is run.

Julian James, chief executive officer at the broker, says the decision was not taken quickly or lightly and is something the business has considered over 12 months.

He comments: "We feel that as part of the continuing culture change within Lockton International a partnership model gives our associates a greater say in the running of the business and it engenders more of a partnership style culture than a management led one."

Mr James says clients have been positive about the move and like the fact that the individuals they deal with will ultimately be partners in Lockton International.

Certainly he is pushing the cultural change that the LLP will deliver and there seems little doubt that it will have a material affect on the internal ethos of the organisation going forward.

Long-term alignment

Leonie Kerswill, a partner at Pricewaterhouse Coopers, says for businesses where people are their major profit earners and assets, LLP is the perfect model. She says: "It gives you limited liability, but it gives you a lot more flexibility to reward people, to give them an interest in the business and to allow them an ownership in the business, which is a good way to align people with the business in the longer term."

This long-term alignment of the interests of the business and its people is something that is favoured by the Financial Services Authority and it has proved very successful in other people-led businesses like legal firms and accountancy practices.

However, Ms Kerswill also says there are significant advantages in terms of tax and particularly in relation to National Insurance. Once people become partners, they are no longer employed by the LLP, but work for it on a self-employed basis.

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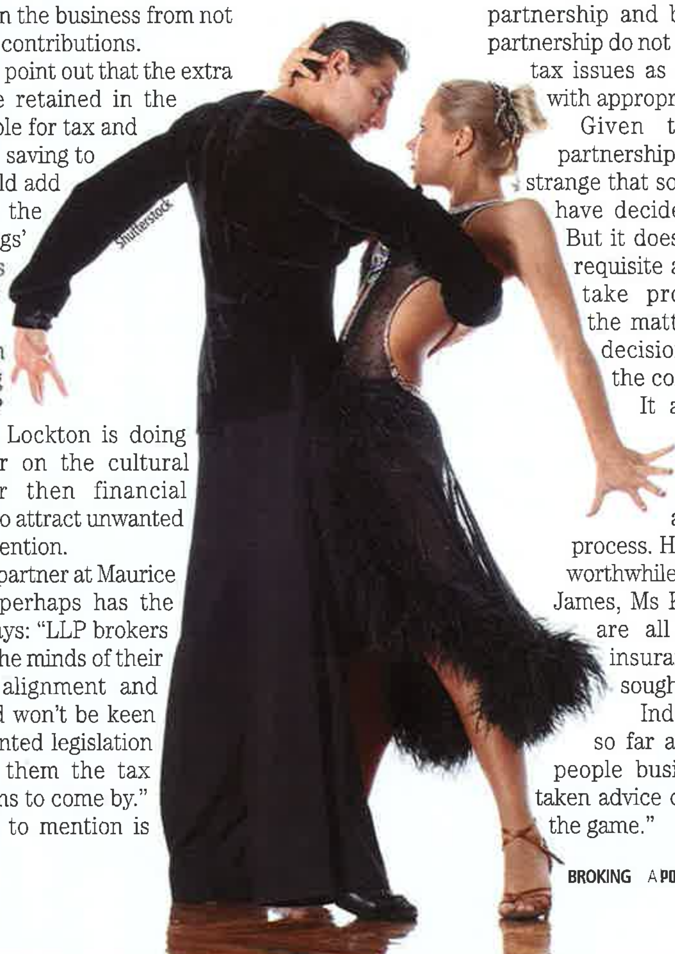
This means that the LLP does not pay NI contributions on behalf of its partners and that the NI contributions the individual pays are significantly lower than they would be as an employed person.

In round figures, Ms Kerswill says that for each £1m that is paid to partners in an LLP, there is almost £130 000 that can be retained by the business as it does not have to be paid in NI contributions.

Lockton International is seeking to announce somewhere between 70 and 90 partners when it moves to an LLP structure. Supposing annual average remuneration of £100 000 per partner, that would equate to up to £1.17m that is retained annually in the business from not having to make NI contributions.

It is important to point out that the extra profit that will be retained in the business is still liable for tax and so it is not a direct saving to the LLP, but it could add up to more than the 'pretty minor savings' that Mr James says will result from the new status.



Others reason that those seeking to move to LLP status may — as Lockton is doing — want to major on the cultural approach, rather then financial benefits, so as not to attract unwanted government intervention.

Richard Turnor, partner at Maurice Turnor Gardner, perhaps has the answer when he says: "LLP brokers will want to focus the minds of their partners on the alignment and cultural issues and won't be keen to to attract unwanted legislation changes to deny them the tax benefit that happens to come by."

A further point to mention is that although partners are self employed and liable for their own tax, many LLPs will retain a proportion of their partners' pay each month so that there is money kept aside for them to pay their self-assessed tax bills every six months.

This not only makes life easier for the partners, but it also means that a business can sit on this capital for six months, and this short-term finance has been a lifeline for many LLPs in these cash strapped times.

On top of the tax and cultural benefits that are derived by LLP status, the structure also gives brokers who pursue this model the ability to change the remuneration received by partners on an annual basis and so give them the flexibility to deal with changing market conditions and to pay their partners in line with the present performance of the business.

Making the move

Stephen Houston, corporate partner at law firm DWF, comments: "You can change someone's profit and capital share quickly, with confidentially and with few tax issues if planned properly. This means you can really provide incentives to the top performers quickly. It is much harder to do this with limited companies and share options just don't do it in people businesses."

In a limited liability company, the purchase and disposal of shares also have tax implications for senior management and this is particularly relevant when senior managers are leaving the company or retiring.

However in an LLP, buying into the partnership and being paid to exit the partnership do not tend to attract the same tax issues as long as they are dealt with appropriately.

Given the benefits of an partnership structure, it is perhaps strange that so few insurance brokers have decided to make the move. But it does take time to seek the requisite approval from the FSA, take professional advice on the matter and make sure the decision is the right one for the company.

It also requires securing the backing of staff and informing clients, which in itself can be a costly and time consuming process. However, it would seem a worthwhile move for many and Mr James, Ms Kerswill and Mr Turnor are all surprised that more insurance brokers have not sought to make the move.

Indeed, Mr Houston goes so far as to say: "If you are a people business and you haven't taken advice on LLPs you are behind the game." **POST**