

Following the trail of a new animal

Almost by accident, the Government has created a legal structure that could transform the financing of regeneration.

Antonia Swinson meets a strange hybrid named the Limited Liability Partnership

Throughout the regeneration sector, people are looking for organisational structures that can trade freely while protecting community interests. The Government's attention lies with Community Interest Companies (CICs), a new legal form designed for social enterprises. But at the cutting edge of economic thinking lurks a new animal; the curious hybrid of a commercial company and a partnership, known as a Limited Liability Partnership (LLP). This model could revolutionise the ability of the voluntary sector and social enterprises to make an impact in regeneration – and there is an irony here, given that the legal form was born at the very sharpest edge of commerce.

During the early 1990s, professional partnerships such as Arthur Andersen became concerned that their individual partners' acceptance of liability for their company's actions put them at risk of bankruptcy. Long before Enron's demise was a twinkle in regulators' eyes, the City persuaded Jersey's parliament to draw up an Act creating the LLP – and the British Government, fearing an exodus of partnerships to Jersey, passed the Limited Liability Partnership Act in April 2001. For the first time anywhere in the world, it became possible to form a corporate body – an entity with a legal existence independent of its individual members – which had both collective limited liability and the mutual, co-operative characteristics of partnerships.

There are now 7,000 LLPs around the country. In part, the growth is because they're so easy to create: two designated members must complete an application downloaded from the Companies House website, and pay £95. There is no Memorandum of Incorporation; no Articles of Association; no Shareholder Agreement.

Chris Cook, previously a civil servant and then a City regulator, was one of the first to grasp just what an extraordinary beast is the LLP. He has set up a consultancy to advise different bodies on the format. The LLP has, he says, created a new asset class: a co-operative, community-based medium of exchange.

"When I pointed it out, I don't think that civil servants in Whitehall were very pleased to find that they had accidentally created the essence of ethical economics," says Cook. "The LLP makes it possible for all stakeholders in an enterprise – staff, management, investors, suppliers and clients – to be members of an Open Capital Partnership, which replaces the



usual adversarial contracts of debt – and equity-based models." In essence, all these stakeholders are brought inside the partnership, so their interests are aligned; it's quite a change from traditional structures, which pit stakeholders in competition against each other. The LLP delivers an ideal combination of the collective and the individual; it's flexible and easy to establish for social enterprises, while its partnership system is robust enough to make it attractive to the private sector.

To understand how an LLP operates,

"Lots of different partnerships can come together and pool resources. It's surely only a matter of time before the regeneration industry wakes up to this"

it's best to consider a theoretical example. Let's say that Bloggside Regeneration holds a brownfield site, while Bloggside Islamic Community Arts (BICA) needs a workshop in which to train local people to produce patterned Islamic tiles for the growing UK market. BICA becomes the first 'occupier member' and Bloggside Regeneration becomes the 'capital member' of the new Bloggside Community LLP, with BICA paying Bloggside Regeneration a peppercorn land rent.

A new workshop, costing £100,000, is acquired using money from a Community Development Finance Institution (CDFI), which becomes the LLP's second capital member. The CDFI then receives two per cent of BICA's total revenue: as a 'capital rental' paid for the use of finance, equivalent to those paid for the occupation of land, this payment does not count as interest, making an LLP an acceptable

financial structure for strict Muslims. Hence, rather than a contract whereby a debtor organisation pays interest to a creditor, or an investor buys part-ownership of a company in the form of shares, both financier and beneficiary join a partnership whose revenues are then shared. In time, BICA may acquire ownership of the capital asset by making payments over and above the required capital rental. The rental payments will then decline with the outstanding capital.

The same structure, says neighbourhood renewal consultant Stephen Hill, could benefit future community land trusts. "Lots of different partnerships can come together and pool resources. It's surely only a matter of time before the regeneration industry wakes up to this."

The LLP structure is taking some of its biggest steps in Scotland, where the West Lothian Chamber of Commerce is plan-

A PFI replacement?

A theoretical example best demonstrates how an LLP could do the work of a PFI: drawing private cash into a public project, with the promise of repayment from the public purse over many years. Let's say that Bloggside Local Education Authority (LEA) funds ten schools held by five different boroughs, which require a £20 million refurbishment. The boroughs transfer the schools' land to an LLP named Bloggside Land Partnership (BLP) and the school buildings to another named Bloggside Schools Partnership (BSP), becoming capital members of both. BLP then becomes a capital member of the new Bloggside Education LLP, while BSP becomes an occupier member and agrees to pay BLP a peppercorn rent for use of the land.

BSP, which will carry out the refurbishment, then negotiates an agreement by which Bloggside LEA pays BSP £600,000 annually, linked to inflation. Over the 25-year life of the refurbished buildings, this will repay the £20 million capital. BSP is divided into ten million 'partnership interests' – or shares – each valued at two pounds, and these are offered for sale to Bloggside residents. Buyers become capital members: priority buying rights could be given to parents, government "baby bond" money could be used to purchase interests on behalf of pupils, and institutions such as the teachers' and Bloggside LEA employees' superannuation schemes could also invest. Thus buyers will receive a share of the LEA payments, recouping all their money over 25 years along with inflation compensation and a return on capital.

provider, a bank, which levies a percentage charge (say 0.25 per cent) to members for use of the guarantee. Half of this charge goes to the bank to defray administrative costs, and the rest to a pool in case of defaults.

In the event of a default, the pool pays the creditor half the loss, with the rest paid by the bank – this latter provision is a built-in disincentive, to stop the bank from granting guarantees to all comers in order to boost income. Yet because default rates are so low in this kind of scheme and a bank's participation brings it the goodwill of the entire membership, banks are keen to get involved.

Members of the societies, then, gain access to guaranteed credit at a minimal cost, and can offer credit to other members in a way that should minimise the risk of losing any of their cash. Within a community-based system like this, peer pressure is a powerful force against defaulting; but if a business does go under, members who have made loans can claim their money back from the pool and bank. Should the pool run dry, members are liable for defaults up to the full guarantee value, but borrowing costs and credit ratings are designed to avoid the need for this facility.

Perhaps the most potent application for LLPs, however, is their ability to draw in private finance for public projects, offering an alternative to private finance initiatives (see box). By drawing the users and stakeholders of a service into its ownership, LLPs could build community links and ensure that the aims of a service's financiers are aligned with those of its providers and users.

"I see a role here for council and trade union pension funds," says Cook. "The rate of 'rent' paid for use of the capital could be set perhaps 4 per cent above inflation. This would be unaffected by Bank of England interest rate decisions; it's not lending, but taking a proportionate share of gross revenues. With risk spread among the partners, it would be less risky than shares, more profitable than gilts, and more accountable and transparent."

At present the LLP animal is young, untested, and just lurking at the outer edges of the economy. But, given its consensual and pragmatic nature, it is surely only a matter of time before its tracks are more widely seen. How extraordinary it would be if the wee beastie of the LLP one day replaces the old debt and equity models of global capitalism.