

# PARLIAMENTARY DEBATES

HOUSE OF COMMONS  
OFFICIAL REPORT

Third Delegated Legislation Committee

DRAFT LIMITED LIABILITY PARTNERSHIPS,  
PARTNERSHIPS AND GROUPS (ACCOUNTS  
AND AUDIT) REGULATIONS 2016

*Thursday 21 April 2016*

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**The Committee consisted of the following Members:**

*Chair:* †GRAHAM STRINGER

† Barclay, Stephen (*North East Cambridgeshire*)  
(Con)  
Blenkinsop, Tom (*Middlesbrough South and East  
Cleveland*) (Lab)  
† Brennan, Kevin (*Cardiff West*) (Lab)  
† Churchill, Jo (*Bury St Edmunds*) (Con)  
† Cleverly, James (*Braintree*) (Con)  
Farrelly, Paul (*Newcastle-under-Lyme*) (Lab)  
† Grant, Peter (*Glenrothes*) (SNP)  
† Heaton-Harris, Chris (*Daventry*) (Con)  
Howarth, Sir Gerald (*Aldershot*) (Con)

† Johnson, Joseph (*Minister for Universities and  
Science*)  
Lammy, Mr David (*Tottenham*) (Lab)  
† McGinn, Conor (*St Helens North*) (Lab)  
Mackinlay, Craig (*South Thanet*) (Con)  
† Malthouse, Kit (*North West Hampshire*) (Con)  
† Smith, Henry (*Crawley*) (Con)  
† Stuart, Graham (*Beverley and Holderness*) (Con)  
† Woodcock, John (*Barrow and Furness*) (Lab/Co-op)  
  
Katy Stout, *Committee Clerk*  
† **attended the Committee**

## Third Delegated Legislation Committee

Thursday 21 April 2016

[GRAHAM STRINGER *in the Chair*]

### Draft Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) Regulations 2016

11.30 am

**The Minister for Universities and Science (Joseph Johnson):** I beg to move,

That the Committee has considered the draft Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) Regulations 2016.

It is a pleasure to serve under your chairmanship, Mr Stringer. I am standing in for my right hon. Friend the Minister for Small Business, Industry and Enterprise, who is on urgent business in Brussels in relation to the steel sector, so if the Committee finds that I am being probed to the limits of my knowledge, I will rapidly agree to write to the Committee to supply it with any information that I am unable to give now.

The Government and business agree that we should act when there are opportunities to deregulate and lighten the load of legislation. Today we have the opportunity to do just that. These regulations will introduce largely deregulatory changes to the financial reporting requirements for limited liability partnerships. They will also introduce a lighter-touch, “micro-entities” financial reporting regime for the smallest LLPs and qualifying partnerships.

Last year, implementation of the accounting directive provided an opportunity to reduce burdens imposed by the financial reporting regime for companies, especially small companies. We have now turned our attention to other types of business entity, and it is clear that similar burden reductions could be applied to LLPs. Following our consultation on proposed changes for companies, a number of stakeholders in the accountancy sector asked whether the same requirements would be extended to LLPs. For accountancy firms and other businesses, the LLP structure has the advantages of a partnership—the relative simplicity of internal governance—with the legal protections of a limited company. High-profile businesses registered as LLPs include PwC Legal and KPMG.

We believe that the financial reporting regimes for LLPs and companies should as far as possible be aligned. That avoids the unnecessary complexity of having regimes for LLPs and companies with similar structures but differences in content. Our consultation on aligning the LLP financial reporting regime with that for companies received unanimous support from stakeholders, and we were encouraged to introduce the revised regime as soon as possible. I am particularly grateful for the contributions of the Institute of Chartered Accountants in England and Wales, the Financial Reporting Council and firms such as EY and Deloitte, to name but a few.

The regulations will amend legislation that applies much of the financial reporting regime for companies to LLPs. That includes application of provisions of the

Companies Act 2006, as well as the supporting regulations that set out the form and content of accounts. The outcomes for business should be straightforward and easily understood, coming as they do on the back of changes to the financial reporting regime for companies.

What do the regulations actually do? I will now explain some of the detail of the proposed changes. The regulations will raise the thresholds for defining the size of LLPs, for the first time since 2008. That will enable about 400 medium-sized LLPs and 40 large LLPs to be re-categorised as small and medium-sized respectively. That means they will be able to access regimes that are more appropriate to their size.

The regulations will also introduce a micro-entities regime for the smallest LLPs and qualifying partnerships, thereby enabling about 3,500 of the smallest LLPs to access a much less burdensome financial reporting regime. Among other things, the micro-entities regime will permit greatly simplified accounts and exemption from the obligation to draw up notes to accounts. Other deregulatory changes include permitting small LLPs to prepare and publish abridged accounts if that decision has been unanimously supported by the members of an LLP. Those abridged accounts omit information required by the general formats in the regulations and will reduce the administrative burden on small LLPs.

It was announced in January that the Government had concluded that the audit exemption thresholds for companies should be allowed to rise in line with the accounting thresholds for small companies. The regulations will apply those increased company thresholds to LLPs, too. That will offer savings of approximately £2 million a year to LLPs. Increasing the threshold for audit will ensure that smaller LLPs are not constrained by a financial assurance regime that is more suited to larger businesses. However, this change will not remove the option for external audit if members, investors or creditors feel that is useful. Importantly, that exemption does not apply to LLPs involved in activities where users of accounts need a higher level of transparency, including where an LLP trades on a regulated market in a European Economic Area state or is involved in banking or insurance. The Government will monitor and gather evidence of the impact of the change to ensure that deregulation is not introduced at the expense of integrity. There will also be a full review by 2021 of the provisions amended by the regulations. We will respond if evidence indicates that action is required to address any shortcomings.

The regulations will not substantially change the way in which an LLP’s accounts are prepared and used, but they will achieve consistency across the UK’s financial reporting regimes for companies and LLPs and avoid unnecessary complexity for the users and preparers of accounts. The regulations potentially provide genuine deregulatory opportunities for LLPs. The vast majority—some 98%—of the UK’s 58,000 LLPs are small. They will be able to benefit the most from these deregulatory changes if they choose to do so, and the savings will support them in running their businesses and, I hope, finding new opportunities for growth. I commend the regulations to the Committee.

11.36 am

**Kevin Brennan (Cardiff West) (Lab):** It is a pleasure to serve under your chairmanship, Mr Stringer, I think for the first time. I thank the Minister for stepping in at

the last moment as super-sub for the Minister for Small Business, Industry and Enterprise. At least he acknowledges his ignorance at the outset rather than revelling in it, as the Minister he has replaced so often does when we are discussing detailed regulation. I welcome his offer to write to the Committee should he be unable to answer any of my questions, although I have great confidence in his ability to do so.

We do not intend to divide the Committee on the regulations, which are welcome and sensible measures to tidy up accounting arrangements, but I have a few questions that were raised, in particular by the ICAEW, during the consultation on the regulations. The ICAEW agrees that the Government should amend the accounting and audit regulatory framework to mirror the recent changes to the framework for limited companies, and we share that view. That seems sensible. It is also sensible to take steps in relation to the introduction of the micro-entities regime and amendments arising from the implementation of the new EU accounting directive. Having different rules for limited liability partnerships and companies is a burden on business that the Government are right to tidy up. We support the general thrust of what the Minister and the Government are trying to achieve.

Nevertheless, the ICAEW continues to have concerns about the long-term implications of the micro-entities regime and the revised regime for small companies. In particular, it is concerned about the impact that the reduced information in micro-entity accounts and abridged accounts under the revised small companies regime may have on the ability of businesses to access finance. I will come to my questions in a moment, but they will relate to what I am saying.

The ICAEW is also concerned about the limited disclosure requirements under the revised small companies regime in the context of the responsibility of directors to ensure that accounts show a true and fair view. On that basis, although the ICAEW believes that there are important benefits to aligning the framework for limited liability partnerships with the recent changes for limited companies, it continues to urge the Department to monitor the effects of the revised regime over time, particularly on the quality of financial statements produced by small and micro-entities. I think that the Minister said that the Department intends to do that and that he can give a commitment that it will do that. If I heard him correctly, he said that the intention was that the Department would monitor that over the next five years, with a full review in 2021. If he can confirm that my understanding is correct, that would be helpful.

Any findings will be important when the impact of the accounting directive is reviewed in due course by the European Commission. How will the changes be monitored by the Department? In particular, how will the effects on the quality of financial statements produced by micro-entities be monitored? I am grateful that the Minister has confirmed that the intention is to undertake a full review by 2021. Does he have any information for the Committee about when the European Commission will review the impact of the directive and the changes associated with it?

Has the Minister any comment to make about the impact of a decision—this is relevant to what we are discussing—in the referendum in June to leave the European

Union? What impact will that have on the statutory instrument we are discussing today? After all, it relates to, and is a consequence of, a European directive. If he can give us any feel for whether we will have to return to this issue in the near future should there be a vote to leave the EU, I would be grateful. Obviously, I would resist that vote to leave, but if it happens—we have to entertain that prospect—what are the implications for the regulations? If there are any unintended consequences, will he commit that the Department will come back to the House as quickly as possible to try to rectify them?

The ICAEW also expressed concerns about the time it has taken for the change to be brought about. It said that it is unfortunate that the process has been subject to “significant delay”. Can the Minister explain why that is? The ICAEW said:

“This has made it difficult for LLPs to plan ahead, resulting in costs and uncertainty for business that could... have been avoided.” Are any of those costs reflected in the impact assessment that I have read, which the Department published alongside the regulations? Are any of the costs of the delays in bringing about the changes, as mentioned by the ICAEW, reflected in the impact assessment? Why has there been a “significant delay” in bringing the changes about? The ICAEW urges that the Department updates the regulations “without any further undue delay in order to avoid uncertainty and costs for business.”

I hope the Minister can answer those questions, although I appreciate he is standing in at the last minute. If he is unable to answer all the questions I have asked, I would be grateful if he wrote to me and other members of the Committee with any answers.

11.43 am

**Kit Malthouse** (North West Hampshire) (Con): I am hesitant to rise and delay the Committee, because I realise that I will probably not be called to sit on one of these Committees again, but I have a short question for the Minister about which I am happy for him to write to me. I welcome the thrust of the proposal, although before I continue, I should declare that I am a member of the Institute of Chartered Accountants.

I am getting a little confused, as, I think, are a lot of small businesses, about the interaction between the EU-adopted international financial reporting standards, financial reporting standards 101 and the new FRS 102. As I understand it, small companies can choose which of those three they wish to participate in and therefore what disclosure requirements they have to make in their annual accounts. Will that apply to the new limited liability partnerships coming into the regime?

Does the Minister recognise that although the Government are taking away regulation with one hand, FRS 102, particularly in its small-entities regime, is adding significant regulation to small businesses? They will have to make significant extra disclosures and do things that directors of very small businesses have not had to do, such as making estimates that they have not had to make before, and that will necessarily put a greater burden on them at year end.

My final question is about the Government’s much-heralded plan to require small businesses to produce quarterly tax returns—the Government say they are quarterly updates, but most small businesses are interpreting

[Kit Malthouse]

them as quarterly tax returns. Will the complicated accounting requirements of the small-entities regime—financial reporting standards 101 and 102, or EU-adopted IFRS—apply on a quarterly basis to small businesses for corporation tax reporting? That would fulfil the fear of the Federation of Small Businesses and other groups that the quarterly regime being brought in by the Treasury may be more complicated than it first appears.

11.45 am

**Peter Grant** (Glenrothes) (SNP): It is a pleasure to serve under your chairmanship, Mr Stringer. I do not intend to divide the Committee or oppose the regulations either; they are heading in the right direction.

In a former life, I worked in financial management and audit in the public sector and am still a member of the Chartered Institute of Public Finance and Accountancy. Although it is not traditionally involved in the regulation of financial services in the private sector—its base is in local authorities, public sector bodies, health boards and so on—the interface between those bodies and small and medium-sized companies becomes closer every day. With my background in public sector finance, I understand how essential it is that a local authority thinking of entering into a contractual arrangement with a small business needs to know that that business is sound and well run; at the same time, it does not want to put such a burden of administration on the small business that it goes under.

Many of the businesses that became limited liability partnerships in the early days were small firms of solicitors and accountants—the people who provide professional services to all the other small businesses. If we can help those professional services firms become more efficient and effective, the knock-on effect on the small business sector could be quite significant, even though on the face of it the definition of a micro-entity is almost vanishingly small. Twenty years ago, I worked in a small neighbourhood shop run by my in-laws. At that time, its turnover was almost at the maximum for it to qualify as a micro-entity. In terms of turnover, we are talking about quite small businesses, but if that business—rather than buying and selling foodstuffs—provides professional services and advice to 50, 100 or 200 other small businesses, and anything goes wrong with that LLP, the impact on the local economy can be many times greater than the partnership's turnover would suggest. In assessing the size and importance of an LLP, we have to make sure that we are not simply looking at the balance sheet or at the profit and loss account. The impact of the failure of a firm of solicitors in a small town, for example, could be that many other businesses in that town start to struggle.

I have two questions for the Minister. The first is about the transition phase, when a business starts to grow, becomes medium sized and finds that it will no longer qualify as a micro-entity or a small business. How will we make sure that we are not building in incentives to businesses not to grow? A good comparison is with one of the earlier drafts of the regulations for credit unions, which would have meant that at a certain stage in its development, a credit union would have been under a perverse incentive to turn away savers

because the additional bureaucracy it would have incurred through having another £5,000 or £10,000 of deposits was simply disproportionate. I am pleased to say that those draft regulations have been amended to remove that danger, but I would appreciate if the Minister could clarify what steps are being built in to make sure that, as a company grows, it is not dragged down by the additional bureaucracy it is subject to, simply as a result of being more successful.

My second question is about how we make sure that we always keep ahead of the game. There is always a danger in anything that is seen to be lifting the burden of regulation, particularly on professional services businesses. The results of doing that with the big, big, big businesses 10 years ago were utterly catastrophic and we are still paying the cost. The difficulty is that when things go wrong with regulation, particularly of professional services businesses, often we do not see the warning signs until it is too late. By the time we are doing anything about it, the horse is not only out the door, it has usually disappeared to Panama or the Cayman Islands. If it turns out the regulations are creating loopholes and opportunities for misuse or abuse that were not supposed to be there, what are the Government able to do to ensure that those loopholes are closed before they are exploited to the potential detriment of a lot of businesses, residents and all of our nations?

I can understand why partners in small partnerships are concerned that the mistake, the negligence or the wrongdoing of one partner could lead to all the partners losing everything. That is the initial idea behind a partnership. It may not be appropriate in this context, but the fact is that a lot of my constituents, and a lot of constituents represented by all members of the Committee, lost everything because of the misconduct and negligence of a fairly small number of very senior people in the big accounting partnerships and in the big banking organisations. It would be wrong if we gave the impression that fellow partners in those organisations are somehow getting more protection than the small business owners that I know, who lost their businesses because a big firm of accountants were simply not looking after their interests properly. Is the Minister satisfied that, although we are protecting partners in limited liability partnerships from a disproportionate impact in cases where one of the partners gets it wrong, we are not creating a situation where the partners in a business are somehow better protected against mishaps than the shareholders, customers, service users and other small businesses that rely on their financial advisers for their own success?

I would be grateful for answers to those questions either now or later. We all wish the Minister's colleague, the Minister for Small Business, Industry and Enterprise, every success in the discussions that she is having on the future of our steel industry. I am happy to wait for replies to my questions if the Minister is not in a position to reply this morning.

11.52 am

**Joseph Johnson:** I thank the Committee again for its understanding. I will do my best to answer the questions and if I fall short, I will happily supplement my oral answers with written ones.

In terms of the impact of reduced disclosure requirements on the ability of the smallest firms to raise finance, we will ensure that the abridged accounts none the less provide users with important and relevant information about the financial position of LLPs. If a lender wants more information before providing credit, they are always able to request it.

I certainly can confirm the Government's commitment to review the arrangements. We will ensure that they are properly reviewed and monitored; post-implementation reviews are planned for 2020 for companies, and for 2021 for LLPs. We intend to use our work to inform the Commission's reviews.

On the question from the hon. Member for Cardiff West about true and fair, the duty of the members of a LLP to approve only those accounts that are true and fair will remain unchanged. However, in the case of micro-LLPs, the accounting items included in their accounts will be presumed to give the true and fair view that is required. Although the regulations will allow some simplification of accounts prepared and published by LLPs, that will not affect the overriding duty to prepare true and fair accounts. The hon. Gentleman queried the time it has taken to bring these measures forward, but it has been necessary for the Government to meet EU obligations for companies to meet the transposition deadline. We are now mirroring that implementation for LLPs. On his linked question about 23 June and the referendum, LLPs are not directly subject to EU legislation, so we would not need to review the regulations unless we chose to do so.

My hon. Friend the Member for North West Hampshire asked about EU-adopted IFRS and FRS 102 rules. UK companies and LLPs have a choice about which regime to adopt. They will choose the regime that best meets their business needs. We have ensured that no company will need to make repeated changes to their arrangements by making this reduced regime available for financial years commencing on or after 1 January 2015 on a voluntary basis.

To answer my hon. Friend's question on tax and quarterly updates or quarterly tax returns, the issue of quarterly updates for tax purposes is still under discussion. This is not about looking to change company reporting arrangements for annual accounts, but about looking to ensure that change does not increase burdens for business.

The hon. Member for Glenrothes spoke about the danger of lifting burdens for professional services. We will continue to work closely with business and professional bodies to monitor the impact of company law on the quality of financial information and take action to address issues identified as appropriate. The deregulation only relates to smaller-sized businesses.

With your permission, Mr Stringer, I will offer to provide written answers to the rest of the questions. The answers I need to give are detailed and I am not sure I will be able to communicate them effectively right here and now, but I will write to hon. Members later with your permission.

Lastly, I shall wrap up by saying that these regulations will not substantially change the way in which an LLP's accounts are prepared and used, but they will achieve consistency across the UK's financial reporting regime for companies and LLPs. The regulations are a positive step that has the support of stakeholders. They offer additional flexibility for LLPs and qualifying partnerships while ensuring that necessary protections are still in place. They will also meet the understandable desire of business for consistency in financial frameworks. Effective financial management underpins the success of every business. The Government remain committed to the good name of the UK's accounting regime while maintaining reporting requirements that are proportionate and flexible. The regulations will support that objective.

*Question put and agreed to.*

11.57 am

*Committee rose.*

