Statement of Recommended Practice

Accounting by Limited Liability Partnerships

Effective for periods commencing on or after 1 January 2019.

Early adoption is permitted for accounting periods beginning before 1 January 2019 provided all the amendments to this 6th edition of the SORP and the March 2018 edition of FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*, are adopted from the same date. There are some exceptions to this rule as set out in paragraph 1.18 of FRS 102.

14 December 2018

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This SORP does not purport to deal with all possible questions and issues that may arise in any given situation. CCAB and the authors do not accept responsibility for loss caused to any person who acts or refrains from acting in reliance on the material in this publication, whether such loss is caused by negligence or otherwise.

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PREFACE

Background to the SORP

This SORP is issued by CCAB, the members of which are:

- The Institute of Chartered Accountants in England and Wales
- The Association of Chartered Certified Accountants
- The Chartered Institute of Public Finance and Accountancy
- The Institute of Chartered Accountants of Scotland
- The Institute of Chartered Accountants in Ireland

The FRC has approved the CCAB bodies for the purpose of issuing a recognised SORP for LLPs incorporated in Great Britain under the Limited Liability Partnerships Act 2000 (the 2000 Act). As part of the process for obtaining this approval, the CCAB bodies agree to follow the FRC's *Policy on Developing SORPs*. These procedures do not include a comprehensive review of the proposed SORP by the FRC, but a limited review is performed focusing on those aspects relevant to the financial statements including aspects relevant to the FRC's broader responsibilities where appropriate.

SORPs issued by SORP-making bodies include a statement by the FRC that:

- outlines the limited nature of the review that the FRC has undertaken; and
- confirms that the SORP does not appear to contain any fundamental points ofprinciple that are unacceptable in the context of current accounting practice, or toconflict with an accounting standard.

CCAB Steering Group and Working Party

The SORP for LLPs differs from a number of other SORPs in that it does not apply to a specific industry or sector, but to a legal entity. The process of developing and reviewing the SORP is overseen by a Steering Group. Membership of the Steering Group is drawn both from trades and professions that have member firms that commonly have LLP status, including the accountancy and legal professions, and from among users of LLP accounts. The SteeringGroup deals with strategy and high-level issues, while the Working Party concentrates ontechnical detail. Membership of these two groups at 14 December 2018 is set out below.

Steering Group

Peter Saunders (Chairman)	Deloitte LLP
Richard Martin	The Association of Chartered Certified Accountants
Rowan Williams	RSM UK Tax and Accounting Limited
Amy Hutchinson	The Institute of Chartered Accountants of Scotland
Stephen Mathews	The Law Society
Kate Wolstenholme	SORP Working Party
Aster Crawshaw	Association of Partnership Practitioners

Working Party

Kate Wolstenholme (Chairman)	PricewaterhouseCoopers LLP
Phil Barden	Deloitte LLP
Janet Milligan	PricewaterhouseCoopers LLP
Andrew Marshall	KPMG LLP
Steve Gale	Crowe U.K. LLP
Peter Gamson	Grant Thornton
Kathy Greaves	Simmons & Simmons LLP
Nick Carter-Pegg	BDO LLP

The membership of both the Steering Group and Working Party is reviewed on an annual basis. If you would be interested in participating in either group please contact Sharon Grant at sharon.grant@ccab.org.uk for further details.

Review of the SORP

CCAB was first approved for the purposes of issuing a SORP on 2 March 2000. The first edition of the SORP *Accounting by Limited Liability Partnerships* was published on 29 May 2002, the second edition on 31 March 2006, the third edition on 31 March 2010, the fourth edition on 15 July 2014, and the fifth edition on 26 January 2017.

In keeping with the FRC's *Policy on Developing Statements of Recommended Practice*, CCAB regularly reviews the SORP for changes in accounting practice and new developments. As part of this review CCAB is required to consider new and revised accounting standards issued since the current edition of the SORP was published and to assess whether the SORP needs amending for these changes.

We published an exposure draft of a revised SORP for public comment on 1 August 2018, recommending several changes to reflect the amendments to FRS 102 arising from the 2017 Triennial review (the 'Triennial review 2017 amendments') and other minor clarifications.

All responses to the questions raised in the exposure draft and other matters raised by respondents were carefully considered during the development of the final version of the revised SORP.

The FRC issued its Statement on the SORP for publication on 13 December 2018 and the sixth edition of the SORP *Accounting by Limited Liability Partnerships* was published on 14 December 2018.

Future editions of the SORP

In keeping with the FRC's *Policy on Developing SORPs*, CCAB will keep the SORP under review for changes in accounting practice and new developments. However, users should be aware that any changes to accounting standards made subsequent to 14 December 2018 have not been reflected in this SORP.

Note on legal issues

The SORP discusses a number of legal issues relating to LLPs. Such discussion is included solely to explain the principles adopted in the SORP and should not be relied upon for any other purpose.

STATEMENT BY THE FINANCIAL REPORTING COUNCIL ON THE STATEMENT OF RECOMMENDED PRACTICE ACCOUNTING BY LIMITED LIABILITY PARTNERSHIPS

The aim of the Financial Reporting Council (FRC) is to promote transparency and integrity in business. In relation to accounting standards applicable in the UK and Republic of Ireland, the FRC's overriding objective is to enable users of accounts to receive high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs. In particular industries or sectors, clarification of aspects of those standards may be needed in order for the standards to be applied in a manner that is relevant and provides useful information to users of financial statements in that industry or sector.

Such clarification in connection with accounting standards is issued in the form of Statements of Recommended Practice (SORPs) by bodies recognised for this purpose by the FRC. The Consultative Committee of Accountancy Bodies has confirmed that it shares the FRC's aim of high-quality financial reporting and has been recognised by the FRC for the purpose of issuing SORPs for limited liability partnerships.

In accordance with the FRC's *Policy on Developing Statements of Recommended Practice (SORPs)* the FRC carried out a review of this SORP focusing on those aspects relevant to the financial statements but also including aspects relevant to the FRC's broader responsibilities where appropriate.

On the basis of its review, the FRC has concluded that the SORP has been developed in accordance with the FRC's Policy on SORPs and does not appear to:

(a) contain any fundamental points of principle that are unacceptable in the context of present financial reporting practices;

(b) conflict with an accounting standard; or

(c) undermine the FRC's broader objectives.

13 December 2018

Financial Reporting Council

STATEMENT OF RECOMMENDED PRACTICE: ACCOUNTING BY LIMITED LIABILITY PARTNERSHIPS

INTRODUCTION

Accounting requirements

1. The detailed accounting requirements relating to LLPs are currently set out in the following Statutory Instruments:

- The Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008 (SI 2008/1911);
- The Small Limited Liability Partnerships (Accounts) Regulations 2008 (SI 2008/1912); and
- The Large and Medium-sized Limited Liability Partnerships (Accounts) Regulations 2008 (SI 2008/1913).

These are collectively referred to in this SORP as the 'LLP Regulations'. The LLP Regulations apply to accounts for financial years commencing on or after 1 October 2008, replacing the accounting provisions previously contained in the Limited Liability Partnerships Regulations 2001 and the Limited Liability Partnerships Regulations (Northern Ireland) 2004. The LLP Regulations apply, with modifications, theaccounting and auditing provisions of the Companies Act 2006 to LLPs. The LLPRegulations apply to the whole of the United Kingdom, reflecting the scope of theCompanies Act 2006. Financial Reporting Standards (FRSs) and other components of UK GAAP also apply to any financial statements of LLPs intended to give a true and fairview. LLPs adopting FRS 101 *Reduced Disclosure Framework* will apply the modified recognition and measurement requirements of IFRS but with reduced disclosures. Their financial statements are nonetheless UK GAAP financial statements because applying the disclosure exemptions prevents them from complying fully with IFRS.Therefore, such LLPs must ensure that their financial statements comply with theCompanies Act and the LLP Regulations.

1A The LLP Regulations were amended in May 2016 by The Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) Regulations 2016 (SI 2016/575), which introduce similar changes to the financial reporting framework for LLPs as have been recently introduced for companies, including raising the size thresholds which determine when an LLP or group qualifies as small (SI 2008 1912 part 2 382 as amended by SI 2016/575) and the creation of a new micro-entities regime for very small LLPs. (SI 2008 1912 part 2 384A as introduced by SI 2016/575). These changes are effective for financial years beginning on or after 1 January 2016.

1B. While these changes do not fundamentally alter the financial reporting regime forLLPs, they allow LLPs – particularly small LLPs – to benefit from a less burdensome financial reporting regime and ensure that the legislative requirements for LLPs are aligned with those for limited companies. For a summary of the detail of all the changes refer to the explanatory note of SI 2016/575.

Scope and objectives

2. This SORP applies to LLPs incorporated in the United Kingdom under the Limited Liability Partnerships Act 2000, or which were incorporated prior to 1 October 2009 under the Limited Liability Partnerships Act (Northern Ireland) 2002, that report under FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*. The SORP, therefore, does not apply to LLPs complying with IFRS, FRS 101 *Reduced Disclosure Framework* or FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime*. It does not seek to set out all of the reporting requirements that apply to LLPs reporting under FRS 102, and it is intended to complement, not replace, the standard. This SORP should, therefore, be used in conjunction with the LLP Regulations and FRS 102 rather than on a stand-alone basis. Where a morerecently issued accounting standard or a change in legislation creates a conflict withany provisions of this SORP, the relevant provisions of the SORP will cease to haveeffect.

3. LLPs qualifying for and choosing to apply the micro-entities regime are not within the scope of this SORP. Such LLPs should apply FRS 105 only. As noted in paragraph 2 above, the SORP complements the requirements of FRS 102 not FRS 105. Where a micro-LLP enters into a transaction that is not covered by FRS 105, it is required to refer to the concepts and principles set out in Section 2 *Concepts and Pervasive Principles* of that standard when determining its accounting policies. Micro-LLPs applying FRS 105 are therefore not required to refer to this SORP.

3A. LLPs qualifying for and choosing to apply the small entities regime are within the scope of this SORP. See paragraphs 27-28 below for more details.

3B. The following table summarises the choices available to LLPs:

	Micro-LLPs *Turnover ≤ £632,000* *Balance sheet total ≤ £316,000* *Employees ≤ 10*	Small LLPs *Turnover ≤ £10.2m* *Balance sheet total ≤ £5.1m* *Employees ≤ 50*	Other LLPs *Breaches two of the three small entity thresholds*
Apply FRS 105 only			
Apply the small entities regime (Section 1A of FRS 102) together with the recognition and measurement requirements of this SORP and the disclosure requirements of paragraphs 63 and 64 of this SORP			
Apply FRS 102 and all the requirements of this SORP[1]			
Apply FRS 101 only	Qualifying entities only	Qualifying entities only	Qualifying entities only
Apply IFRSs only			

Measurement

4. Deleted

5. Deleted

Format and terminology

6. All the material in this SORP – other than Appendix 5 'Legal opinion' and Appendix 6 'Basis for conclusions' – is an integral part of the SORP. However, the central principles are printed in bold in order to distinguish them from explanatory paragraphs.

7. For simplicity, the term 'profits' has been used rather than 'profits or losses' where circumstances allow. Similarly, the term 'year' has been used rather than 'period'.

[1] Qualifying entities may wish to take advantage of the reduced disclosure regime set out in paragraphs 1.8-1.13 of FRS 102.

Definitions

8. The following definitions apply within this SORP.

Allocated profit

9. Profits (after deducting members' remuneration charged as an expense) that have been allocated during the year as a result of the members deciding on a division of profits.[2]

Automatic division of profits[3]

10. An automatic division of profits is one where the LLP has an unconditional obligation to divide those profits based on the LLP agreement in force at the time. Such a pre-agreed automatic division of profits could be in respect either of the entire profits for the year or a portion or fixed amount thereof. The fact that the actual amount to be divided is contingent on the existence of profits in the first place does not negate the LLP's unconditional obligation in respect of those profits nor the member's unconditional entitlement to those profits should they come into existence. A division of profits that requires a decision of the LLP does not constitute an automatic division because the LLP has an unconditional right to refuse payment of profits for a particular year.

Designated members

11. Designated members are those members specified as such in the incorporation document or otherwise in accordance with an agreement with the other members, as required under section 8 of the 2000 Act. Designated members perform certain duties in relation to the legal administration of an LLP that would, for a company, be performed by the secretary or directors. If there would otherwise be no designated members, or only one, all members are deemed to be designated members.

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[2] The decision to divide profits, which gives rise to a liability in respect of allocated profits, must be distinguished from the arrangements for profit sharing. A provision in an agreement between the members, which sets out the profit shares of the members, does not of itself constitute an agreement for the division of profits. It merely sets out the respective profit shares of the members that will apply to those profits that the members decide to divide among themselves. Accordingly, the default rule that is applied by virtue of Regulation 7(1) of the Limited Liability Partnerships Regulations 2001 (which provides for the members of an LLP to share equally in the capital and profits of an LLP in the absence of agreement to the contrary) does not constitute a default rule as to the automatic division of profits between the members. (As explained further in paragraph 48, where the agreement between the members provides for the automatic division of profits, those divided profits will form part of members' remuneration charged as an expense and will be credited directly to the current accounts of the members without first being shown under the balance sheet heading 'Other reserves'.) Allocated profits are debts due to members which, unless otherwise agreed by the members, rank pari passu with ordinary creditors in the event of a winding up. The total amount of profit allocated following a decision to divide may be less (or more) than the amount of profit earned by the LLP in the relevant year.

[3] Refer Appendix 5, BC26.

Drawings

12. The payment in cash (or kind) of amounts to members. Drawings may consist of regular monthly payments or ad hoc payments, for example, in respect of current year's and/or prior years' remuneration (as defined).

Limited liability partnership (LLP)

13. An LLP incorporated in the United Kingdom under the 2000 Act, or incorporated prior to 1 October 2009 under the Limited Liability Partnerships Act (Northern Ireland) 2002.

Loans and other debts due to members

14. Members' interests that are debts of the LLP and are included in balance sheet item J in the accounts formats set out in the LLP Regulations (SI 2008 1913/1912 schedule 1, part 1, section B).

Members

15. On incorporation, the members of an LLP are the persons who subscribe their names to the incorporation document. Persons may become or cease to be members in accordance with an agreement between existing members.

Members' agreement

16. Any express or implied agreement between an LLP and its members that determines the mutual rights and duties of the members in their capacity as such and their rights and duties in relation to the LLP. An agreement between the members, to which the LLP is not party – for example, an agreement to guarantee a minimum or specified remuneration for a particular member – does not constitute a members' agreement for the purposes of the SORP.

Members' capital

17. Amounts subscribed or otherwise contributed by members that are classified as capital by the constitutional arrangements of the LLP. Such amounts will require analysis as to whether they are considered equity or debt in accordance with section 22 of FRS 102. Members' capital is a component of 'Members' other interests' or 'Loans and other debts due to members' depending on its classification under this section of FRS 102.

Members' other interests

18. Members' interests other than debt due to them by the LLP, which constitute equity in the LLP, are included in balance sheet item K in the accounts formats set out in the LLP Regulations (SI 2008 1913/1912 schedule 1, part 1, section B). Members' other interests include 'Members' capital' that is classified as equity in accordance with section 22 of FRS 102, 'Revaluation reserve' and 'Other reserves'.

Members' participation rights

19. All the rights of a member against the LLP that arise under the members' agreement (for example, in respect of amounts subscribed or otherwise contributed, remuneration and profits).

Members' remuneration

20. Any outflow of benefits to a member. It may include or comprise, but is not limited to, one or more of the following elements: salary, interest, bonus, risk premium and allocated share of profits. The form that remuneration takes will be a matter of agreement between the members.

Members' remuneration charged as an expense

21. Remuneration that is payable to a member, which falls to be treated as a charge against profits and not an allocation of profits. The treatment of members' remuneration is determined by reference to the nature of the participation rights that give rise to the remuneration.[4] If those rights were to give the members an unconditional right to the division of profits or to other forms of remuneration, for example those items set out in paragraph 20 above, then they give rise to a liability for that remuneration in accordance with section 22 of FRS 102, and the remuneration is charged as an expense. Members' remuneration charged as an expense is not restricted to amounts that are payable by the LLP regardless of the existence or extent of profits; it also includes, for example, any profits that are automatically divided between members by virtue of a members' agreement. Members' remuneration charged as an expense may in some exceptional circumstances be a negative amount. A member may also have a contract to provide services to the LLP, which may be referred to as a contract of employment. Remuneration covered by such a contract is classified as members' remuneration charged as an expense, including amounts relating to pension obligations and share-based payments (if any).

Post-retirement payments to former members

22. Any post-retirement payments, whether in cash, in kind or any other benefits, including annuities and payments for goodwill, payable by the LLP as principal to former members of the LLP, other than where the payments are properly made in return for post-retirement services performed by the recipient for the LLP's benefit. Members who retire by or at the balance sheet date are regarded as former members. Such post-retirement payments include, but are not limited to, amounts payable to, for example, spouses, children and the estates of former members. In this context, former members may include former partners in a predecessor partnership of the LLP, where the LLP assumes responsibility for the post-retirement payments to the former partners.

[4] This SORP only considers the accounting treatment of members' remuneration. The tax treatment of that remuneration will be determined on a different basis by reference to relevant tax legislation in force at the time. A member who is, for tax purposes, treated as an employee will not necessarily be treated as such for accounting purposes and vice versa.

Puttable instrument

23. The definition of ‘puttable instrument’ is contained in section 22 of FRS 102. A puttable instrument is a financial instrument that gives the holder the right to sell that instrument back to the issuer for cash or another financial asset or is automatically redeemed or repurchased by the issuer on the occurrence of an uncertain future event or the death or retirement of the instrument holder (paragraph 22.4(a) of FRS 102). In practice for LLPs, puttable instruments may include certain types of capital or members' loans that carry rights for the member (or other holder) to obtain repayment from the LLP.

Unallocated profit

24. Profits of the LLP (after deducting members’ remuneration charged as an expense) that have been ascertained but which are not yet divided among the members. After the profits have been ascertained, in the absence of any agreement between members to the contrary, the balance will be unallocated profit and will need to be shown under ‘Other reserves’ on the balance sheet, pending a decision to divide the profits among the members. It is open to the members of an LLP to agree that all, or a proportion of, the profits of the LLP shall be automatically divided between the members after they have been ascertained; in that event, the LLP will not have an unconditional right to avoid delivering cash or other assets to a member in respect of those amounts. This is a matter of construction of the members’ agreement. Where this is the case, any amounts automatically divided will form part of members’ remuneration charged as an expense ie, they will be deducted in arriving at retained profit or loss for the financial year available for discretionary division among members. Accordingly, where all the profits are automatically divided, a nil amount will bereported as retained profit or loss for the financial year available for discretionarydivision among members, and there will be no unallocated profits.[5]

The contents of the annual report and financial statements

25. The annual report should comprise:

- the financial statements (SI 2008/1911);
- a statement of members’ responsibilities in relation to the production of financial statements; and
- a report on the financial statements by a registered auditor, if required by the LLP Regulations (SI 2008/1911).

26. The financial statements, as defined by the LLP Regulations (SI 2008 1911/1912/1913) and accounting standards, should, subject to exemptions for small entities, comprise:

- a statement of financial position;
- either:

[5] See the legal opinion in Appendix 5.

- a single statement of comprehensive income displaying all items of income and expense recognised during the period including those items recognised in determining profit or loss and items of other comprehensive income; or
- a separate income statement and a separate statement of comprehensive income;

- a statement of changes in equity;
- a statement of cash flows;[6] and
- notes, comprising a summary of significant accounting policies and other explanatory information.

26A. In certain circumstances, paragraph 3.18 of FRS 102 allows entities to present a single statement of income and retained earnings in place of the statement of comprehensive income and statement of changes in equity. However, this SORP does not recommend this approach for LLPs as it will be of little benefit to users of LLP financial statements in most cases.

26B. The 2008 Regulations as amended by SI 2016/575 (SI 2008 1913 schedule 1, part 1, paragraph 1A / SI 2008 1912 schedule 1 part 1 paragraph 1B) provides LLPs with the opportunity to adapt the formats of the balance sheet and profit and loss account, in a manner consistent with IAS 1. FRS 102 paragraphs 4.2A to 4.2D and 5.5B to 5.5C set out the requirements for large and medium sized LLPs and FRS 102 paragraphs 1AA.3 to 1AA.6 and 1AB.3 to 1AB.4 set out the requirements for small LLPs.

26C. An LLP choosing to adapt the formats is permitted to do so providing the information given is at least equivalent to the information required by the formats set out in the LLP Regulations. To meet this requirement this SORP requires separate disclosure in the balance sheet of 'Loans and other debts due to members' (balance sheet item J) and 'members' other interests' (balance sheet item K) and separate disclosure in the profit and loss account of 'Profit or loss for the financial year before members' remuneration and profit shares'.

Accounting by small LLPs

27. Section 1A *Small Entities* of FRS 102 sets out the information that must be presented and disclosed in the financial statements of small entities that qualify for and choose to apply the small entities regime. Small LLPs apply the recognition and measurement requirements of FRS 102 and this SORP. There are no recognition and measurement simplifications for small entities, except for the optional exemption provided in

[6] Qualifying entities (as defined by FRS 102) may wish to take advantage of the exemption from the requirement to produce a cash flow statement as set out in paragraph 1.12 (b) of FRS 102. Small LLPs are not required to prepare a cash flow statement.

paragraph 11.13A of FRS 102, which applies to certain financing transactions. This is discussed further in paragraph 57A.

27A. Subject to paragraphs 27B and 27C, small LLPs qualifying for and choosing to apply the small entities regime are required to comply with the disclosure requirements of Section 1A of FRS 102 rather than the disclosure requirements of this SORP.

27B. The accounts of small LLPs must, however, give a true and fair view. Judgement will therefore be needed when considering whether further disclosures over and above those required by Section 1A of FRS 102 will be needed in order to ensure that the accounts give a true and fair view. Depending on the individual facts and circumstances, some or all of the disclosures included in this SORP and the rest of FRS 102 may be needed in order to ensure that the accounts give a true and fair view.

27C. This SORP requires small LLPs to make the disclosures about how loans and otherdebts due to members rank in relation to other unsecured creditors as required by paragraphs 63 and 64 of this SORP. Such disclosures are considered necessary in order to ensure that the accounts give a true and fair view as LLPs do not have any of the capital maintenance provisions that apply to companies.

27D. This SORP encourages small LLPs to include the reconciliation of movements in'Members' other interests' and 'Loans and other debts due to members' detailed in paragraph 60 of the SORP, and that the reconciliation is provided for both the current and preceding period in line with paragraph 1A.10 of FRS 102.

28. As noted in paragraph 2 above, in the event of conflicting requirements, those in the LLP Regulations and accounting standards should take precedence over this SORP. Other than as set out in paragraph 27C, the SORP should not be interpreted asremoving or not permitting exemptions for certain smaller entities in legislation oraccounting standards, including those from the need to prepare group accounts orcash flow statements.

29. Deleted

Disclosures

30. This SORP requires LLPs to disclose the following information:

- the principal activities of the LLP and its subsidiary undertakings, indicating any significant changes during the year;
- an indication of the existence of any branches[7] outside the UK;
- the identity of anyone who was a designated member during the year; and
- the policy of the LLP regarding members' drawings and the subscription and repayment of amounts subscribed or otherwise contributed by members (see paragraph 69 below).

[7] As defined by s1046(3) Companies Act 2006 (CA 2006).

31. These disclosures – together with any other non-financial performance matters thatan LLP may wish to communicate to its members – may be presented anywhere in the annual report. Although not a statutory requirement, a separate Members' Report offers one possible vehicle for such communication.

MEMBERS' REMUNERATION AND INTERESTS

Analysing members' participation rights

32. Members' participation rights in the earnings or assets of an LLP should be analysed between those that give rise to, from the LLP's perspective, either a financial liability or equity, in accordance with section 22 of FRS 102. Members' different participation rights should be analysed separately into liability and equity elements. Depending on the terms of the members' agreement, members' participation rights may give rise to equity or liabilities or both.

33. Under section 22 of FRS 102, a critical feature in differentiating a financial liability from an equity instrument is the existence of a contractual obligation of one party to deliver either cash or another financial asset to another party. Critical, therefore, to determining whether the LLP has a financial liability to a member, or alternatively the member holds equity in the LLP, is whether there exists a contractual obligation on the part of the LLP to deliver cash (or other financial assets) to the member – for example, upon the member retiring from or otherwise leaving the LLP. Generally, a member's participation right will result in a liability unless the LLP has an unconditional right to avoid delivering cash or other assets to the member (ie, the right to any payment or repayment is discretionary on the part of the LLP). However, puttable instruments and amounts payable on liquidation meeting the conditions in paragraph 22.4 of FRS 102 are also classified as equity. Such instruments (or components of such instruments) will be classified as equity even though the LLP does not have an unconditional right to avoid delivering cash or other assets to the member. In the remainder of this document, we will refer to this equity classification by exception as the 'puttables exception'.

34. Participation rights in respect of amounts subscribed or otherwise contributed should be analysed separately from participation rights in respect of remuneration (which may include, inter alia, salary, interest, bonus, risk premium and allocated share of profits), except where the remuneration, or part thereof, is clearly identifiable as a return on amounts subscribed or otherwise contributed. To the extent that remuneration cannot be clearly identified as a return on amounts subscribed it is regarded, for accounting purposes, as separate from the instrument that consists of the amount subscribed and the return thereon. For example, profit share payable at the discretion of the LLP would be accounted for as an equity interest, even if the member's capital is treated as a liability. Where remuneration, or part thereof, is clearly identifiable as a return on the amounts subscribed – for example, non-discretionary interest payments – rather than a return for the services provided by the members, then the amounts subscribed and that part of the remuneration that is clearly identifiable as a return on the amounts subscribed would be analysed together for accounting purposes.

35. Non-discretionary amounts becoming due to members in respect of participation rights in the profits of the LLP for the financial year that give rise to liabilities should be presented as an expense within profit or loss (within the heading 'Members' remuneration charged as an expense').

36. Amounts becoming due to members in respect of equity participation rights, following a discretionary division of profits, should be debited directly to equity in the year in which the division occurs. Such amounts should not be presented as an expense within profit or loss. A discretionary division of profits that takes place after the balance sheet date is a non-adjusting event under section 32 of FRS 102 *Events after the End of the Reporting Period*.

36A. Deleted

37. Guidance on how to apply the principles set out above is given in paragraphs 38 to 50 below, as well as in the illustrative examples in Appendix 2.

Amounts contributed by members and returns thereon

38. For some LLPs, the terms of the members' agreement may result in all members' participation rights being classified as giving rise to financial liabilities ie, not equity participation rights. This may be the case if, for example, all profits are automatically divided between members (see paragraph 48 below), and if individual members have the right to demand payment of amounts subscribed or otherwise contributed to the LLP. The ability of a member to exercise a contractual right may be conditional on a future event, for example, a member may only be able to demand amounts subscribed or otherwise contributed on retirement. Despite the fact that the member's right is conditional on a future event, the LLP does not have an unconditional right to avoid making the payment, so, unless the conditions under the puttables exception are met, a financial liability exists.

39. If the LLP does not have an unconditional right to refuse repayment of amounts subscribed (and the conditions under the puttables exception have not been satisfied), such amounts will be classed as liabilities and included within loans and other debts due to members. Conversely, if the LLP has an unconditional right to refuse repayment of members' capital, the appropriate classification is determined by the other rights that attach to the capital, for example, if the LLP has an unconditional right to refuse repayment to members of amounts subscribed or otherwisecontributed by them then, providing there is no obligation to pay a return on thoseamounts, such amounts will be classed as equity. However, if interest is mandatorilypayable on members' capital, then a liability will be recognised on subscriptionreflecting the present value of minimum non-discretionary outflows. In many cases,this will be the same as the relevant amount of members' capital. However, followingthe principle set out in paragraph 34 above, any other remuneration (salary, bonus,risk premium and allocated share of profits etc) would fall to be accounted forseparately.

Puttables exception

40. The puttables exception affects the classification of puttable financial instruments and obligations arising on liquidation. In certain limited circumstances, rights of members which meet the definition of a financial liability under paragraph 22.3 of FRS 102 will fall to be classified as equity provided the conditions for the puttables exception are met.

41. In considering whether members' participation rights fall under the puttables exception it is first necessary to consider how the principles set out in paragraph 34 above are being applied. Accordingly, in cases where, under the principles of paragraph 34 above, participation rights in respect of remuneration are treated as separate instruments this does not in itself affect the classification of the capital under the puttables exception.

42. The requirements under the puttables exception are drafted so as to apply to individual classes of financial instrument. Depending on the structure of an LLP, members' interests may consist of one or more classes of financial instrument which themselves may comprise one or more 'components'. For example, members may invest in the capital of an LLP and may also be required to make loans to the LLP. If those loans are legally a separate financial instrument from the capital, then the LLP will have two classes of instrument with members. One of the requirements under the puttables exception is that the class of instruments is subordinate to all other instruments of the issuer. Accordingly, where members' interests include more thanone class of instrument, equity classification under the puttables exception is only possible for the class of instrument that is subordinate to all others.

42A. A puttable financial instrument is classified as a liability rather than equity if it obligesthe entity to make payments to the holder before liquidation, such as mandatory interest or other non-discretionary returns. This is because one of the conditions for that exception to apply is that, apart from the contractual obligation for the issuer to repurchase or redeem the instrument for cash, the instrument does not include any contractual obligation to deliver cash or another financial asset to another entity. However, there is no equivalent restriction for instruments redeemable only on liquidation.

42B. In considering the puttables exception it is also necessary to distinguish those transactions between members and the LLP that are undertaken in their role as non-owners from those undertaken in their role as owners.

42C. One example is a profit or loss sharing arrangement that allocated profit or loss to the instrument holders on the basis of services rendered or business generated during the current and previous years. Such arrangements are transactions with instrument holders in their role as non-owners and should not be considered when assessing the features listed in paragraph 22.4 of FRS 102. However, profit or loss sharing arrangements that allocate profit or loss to instrument holders based on the nominal amount of their instruments relative to others in the class may represent transactions with the instrument holders in their role as owners and should be considered further by applying the principles of paragraph 34.

42D. The holder of a puttable financial instrument or an instrument that imposes on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation may enter into transactions with the entity in a role other than that of an owner. For example, an instrument holder may also be an employee of the entity. Only the cash flows and the contractual terms and conditions of the instrument that relate to the instrument holder as an owner of the entity shall be considered when assessing whether the instrument should classified as equity.

42E. The cash flows and contractual terms and conditions of a transaction between the instrument holder (in the role as a non-owner) and the issuing entity must be similar to an equivalent transaction that might occur between a non-instrument holder and the issuing entity.

42F. Appendix 2 contains some additional guidance and a number of examples designed to demonstrate the impact of application of the puttables exception in various scenarios.

43. Deleted

44. Deleted

45. Deleted

Division of profits

46. Amounts becoming due to members in respect of participation rights in the profits of the LLP for the year that give rise to a liability might include, for example, salary, interest on capital balances and any automatic division of profits, to the extent that the LLP does not have an unconditional right to avoid delivering cash or other assets to a member in respect of such amounts.

47. Where there are no equity participation rights in the profits for the year, it follows that all amounts becoming due to members in respect of those profits will be presented within members' remuneration charged as an expense. In these circumstances, LLPs should refer to the presentational guidance given in paragraph 51 below and the illustrative examples in Appendix 1.

48. Where profits are automatically divided as they arise or are determined, so that the LLP does not have an unconditional right to refuse payment based on the LLP agreement in force at the time, the amounts arising that are due to members are in the nature of liabilities. They should therefore be treated as an expense in profit or loss in the relevant year and, to the extent they remain unpaid at the year end, they should be shown as liabilities in the balance sheet. This will also be the case where there is a requirement to divide some or all profits but the basis upon which those

profits are shared between individual members is not determined until after the balance sheet date. Conversely, where there is no automatic division of profits because the LLP has an unconditional right[8] to refuse payment of the profits of a particular year until those profits are divided by a decision taken by the LLP, those profits are classed as an appropriation of equity rather than as an expense. They are therefore shown as a residual amount available for appropriation. Once profits are divided, the amount of the divided profits is treated as an appropriation which is deducted from equity and, to the extent that any divided profits remain unpaid at the year end, the amount unpaid will be recorded as a liability.

49. It is possible that a combination of these circumstances may arise, for example, if 50% of profits are automatically divided, but the remaining profits are only divided at the discretion of the LLP, then the former will be treated as an expense/liability and the latter as an appropriation/equity.

50. Paragraph 3 of the Legal Opinion in Appendix 5 addresses the division of profits and may be helpful in determining whether payments are discretionary.

Members' remuneration: presentation and disclosure

50A. Under FRS 102, an entity has a choice whether to present total comprehensive income for the period in one statement (a statement of comprehensive income) or two statements (an income statement – which is the profit and loss account required by the LLP Regulations – and a statement of comprehensive income).

51. The prescribed formats set out in LLP Regulations require disclosure on the face of the profit and loss account (or statement of comprehensive income) of a sub-total, being 'Profit or loss for the financial year before members' remuneration and profit shares' (SI 2008 1913/1912 schedule 1, part 1, section B). The total of members' remuneration charged as an expense, as defined in paragraph 21 above, should be disclosed separately and deducted from this balance. Disclosure on the face of the profit and loss account (or statement of comprehensive income) should be as follows:

[8] Until the LLP takes a decision to divide the profits, the LLP has an unconditional right to refuse to pay the profits to individual members. The LLP is a body corporate with legal personality separate from that of its members. The LLP agreement in force at the time determines the contractual obligations of the LLP. When considering whether the LLP has an unconditional right to avoid payment, any collective rights of the members to vary the terms of the members' agreement are not relevant. Only the rights of the LLP to avoid making payment are taken into consideration. Refer also BC26.

Profit or loss for the financial year before members' remuneration and profit shares	X
Members' remuneration charged as an expense	(X)
Profit or loss for the financial year available for discretionary division among members	X

52. The basis on which each element of remuneration (as defined) has been treated in the accounts should be disclosed and explained by way of a note.

53. Members' remuneration charged as an expense is defined in paragraph 21 above. The prescribed formats in the LLP Regulations require disclosure on the face of the profit and loss account (or statement of comprehensive income) of a sub-total 'Profit or loss for the financial year before members' remuneration and profit shares'. Therefore, after the sub-total required by the prescribed formats in the LLP Regulations, a line item described as 'Members' remuneration charged as an expense' should be deducted as an additional expense. This includes any related employment costs. This also applies where the formats are adapted (see paragraph 26C)

54. The treatment of members' remuneration in the profit and loss account (or statement of comprehensive income) is summarised in the following table.

Nature of element of a member's remuneration	Treat as
Remuneration that is paid under a contract to provide services to the LLP, which may be referred to as a contract of employment	Expense, described as 'Members' remuneration charged as an expense', and deducted after arriving at 'Profit for the financial year before members' remuneration and profit shares'
Other payments, arising from components of members' participation rights in the profits for the year that give rise to liabilities in accordance with section 22 of FRS 102, such as mandatory interest payments	
Automatic division of profits	
Any share of profits arising from a division of profits that is discretionary on the part of the LLP (ie, where the decision to divide the profits is taken after the profits have been made)	Allocation of profit

Where it is considered that it will assist an understanding of the financial performance of the LLP, members' remuneration charged as an expense should be further analysed within the notes to the financial statements, for example, between that which is paid under a contract of employment and that which relates to amounts arising from participation rights that give rise to a liability. In the case of a group, members' remuneration from all entities in the group that are consolidated into the parent LLP's group accounts should be considered.

Members' interests: presentation and disclosure

55. 'Loans and other debts due to members' (balance sheet item J in the prescribed formats set out in the LLP regulations) and 'Members' other interests' (balance sheet item K in the prescribed formats in the LLP regulations) should be disclosed separately on the face of the balance sheet (SI 2008 1913/1912 schedule 1, part 1, section B). Balance sheet item J includes 'Loans and other debts due to members' and 'Members' capital' in so far as it is classified as a liability. Balance sheet item K includes 'Members' capital', 'Revaluation reserve' and 'Other reserves', in so far as they are classified as equity, which are also each required to be disclosed separately on the face of the balance sheet.

56. The prescribed formats in the LLP regulations require all amounts due to members to be presented within 'Loans and other debts due to members'. This heading will include any unpaid element of members' remuneration charged as an expense together with any unpaid allocated profits arising from a discretionary division of profits madeduring the year. It will also include members' capital classified as a liability.

57. Equity should not include members' capital that is classified as a liability in accordance with section 22 of FRS 102. For some LLPs, the terms of the members' agreement may result in all 'capital' subscribed by members being presented as financial liabilities. This will be the case where individual members have the right to demand repayment of such balances (for example, on retirement) and the LLP does not have the unconditional right to refuse such repayment, except where the conditions for the puttables exception are met.

57A. When members' capital is classified as a financial liability it may – depending on the terms of the members' agreement – constitute a financing arrangement and may therefore need to be discounted to present value in accordance with the requirements of paragraph 11.13 of FRS 102. However, discounting will not always be necessary as in many instances members' capital will be repayable on demand or at short notice eg, on termination of membership. In addition, there is an exemption for small companies and LLPs in paragraph 11.13A of FRS 102 from the requirement to discount basic loan financing transactions, provided it is a "…loan from a person who is within a director's group of close family members, when that group contains at least one [member of the LLP who is a person]." The meaning of director has not been defined in FRS 102 for an LLP. This SORP recommends that for the purposes of applying the exemption in paragraph 11.13A of FRS 102, a director is taken to mean a member, who is a person, with an equivalent role in the LLP. For some small LLPs that may be all members, for others, it may be a member who is part of a governing body or management board.

58. Whether an LLP presents its balance sheet and profit and loss account using either the prescribed formats in the LLP regulations or the adapted formats (see paragraph 26B) this SORP requires that the face of the balance sheet should show the net assets attributable to members of the LLP (that is, a balance sheet total before 'Loans and other debts due to members' and 'Members' other interests'). In addition, this SORP requires 'Total members' interests', being the total of items shown as 'Loans and other debts due to members' and 'Members' other interests' less any amounts due from members in debtors, should be disclosed as a memorandum item on the face of the balance sheet.

59. A statement of the changes in equity should be presented as a primary statement (paragraph 6.3 of FRS 102) detailing the movements in 'Members' other interests' (Balance sheet item K in the prescribed formats set out in the LLP regulations).

59A. A statement of changes in equity does not need to be prepared if the LLP has no equity. Where a statement of changes in equity is not included because the LLP has no equity and is not replaced as a primary statement by a reconciliation of members' interests, a statement should be made either on the face of one of the other primary statements or in the notes to the accounts that the LLP has no equity and consequently a statement of changes in equity is not given.

59B. Paragraph 4.12 of FRS 102 requires certain disclosures relating to an entity's share capital and reserves. For entities without share capital, such as an LLP, equivalent information is required by paragraph 4.13 of FRS 102, showing changes in the period for each category of equity, and the rights, preferences and restrictions attaching to each category of equity.

60. The Large and Medium sized LLP (Accounts) regulations require additional disclosuresof movements in 'Loans and other debts due to members' (SI 2008/1913 schedule 1, part 3, 47). Disclosure should include the amount brought forward from the previous year, the changes arising in the financial year and the balance carried forward at the end of the year. This SORP requires that disclosure of movements in 'Members' other interests' and 'Loans and other debts due to members' should be in the following format (although additional categories of members' interests or types of movements should be disclosed where this aids clarity or circumstances require it):

	EQUITY Members' Other Interests[9]				DEBT Loans and other debts due to members less any amounts due from members in debtors[10]			TOTAL MEMBERS' INTERESTS
	Members' Capital (Classified as equity)	Revaluation Reserve	Other Reserves	Total	Members' Capital (Classified as debt)	Other amounts	Total	Tota l 2XX1
Amounts due to members					X	X	X	
Amounts due from members						(X)	(X)	
Balance at [start of the period]	X	X	X	X	X	X	X	X
Members' remuneration charged as an expense, including employment and retirement benefit costs						X	X	X
Profit/(loss) for the financial year available for discretionary division among members			X	X				X
Members' interests after profit/(loss) for the year	X	X	X	X	X	X	X	X
Other divisions of profits			(X)	(X)		X	X	-
Surplus arising on revaluation of fixed assets		X		X				X
Introduced by members	X			X	X		X	X
Repayments of capital	(X)			(X)	(X)		(X)	(X)
Repayments of debt (including members' capital classified as a liability)					(X)		(X)	(X)
Drawings						(X)	(X)	(X)
Other movements	X	X	X	X	X		X	X
Amounts due to members					X	X	X	
Amounts due from members						(X)	(X)	
Balance at [end of the period]	X	X	X	X	X	X	X	X

60A. The reconciliation of members' interests may be presented as a primary statement instead of a statement of changes in equity. Where this option is taken comparative amounts should be presented by way of the full table relating to the prior period.

61. Any unallocated profits should appear under 'Other reserves' in 'Members' other interests' (balance sheet item K in the prescribed formats set out in the LLP regulations) (SI 2008 1913/1912 schedule 1, part 1, section B). Where the LLP makes a loss for the financial year that is not allocated to the members, the amount should be deducted from 'Other reserves'.

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[9] Balance sheet item K.

[10] Balance sheet item J less any amounts due from members in debtors. 'Loans and other debts due to members' would include any members' capital classified as a liability. The analysis of amounts due to members is required in order to comply with the LLP Regulations.

62. The members of the LLP may agree to allocate to the members a sum different fromthe amount shown as profit or loss for the financial year available for division among members. Amounts may, for example, be retained in the business as unallocated profits.

63. This SORP requires the notes to the accounts to explain where amounts in 'Loans and other debts due to members' (other than members' capital classified as debt) would rank in relation to other creditors who are unsecured in the event of a winding up. The notes should disclose details of any protection afforded to other creditors in such an event which is legally enforceable and cannot be revoked solely by a decision of the members. The notes should also disclose what restrictions or limitations exist on the ability of the members to reduce the amount of 'Members' other interests' or state that there are no such restrictions.

64. The capital (whether classified as a liability or equity) of an LLP may be reduced by agreement of the members either by repayment or by the conversion of equity capital into liability capital or other debt.[11] In the absence of agreement to the contrary, unsecured debt due to members will rank equally with debts due to other unsecured creditors in a winding up.

65. The Large and Medium sized LLP (Accounts) Regulations require disclosure in the notes of the amount of loans and other debts due to members falling due after more than one year (SI 2008/1913 schedule 1, part 3, 47).

66. The LLP Regulations require separate disclosure of the aggregate amount of money advanced by members by way of loan, the aggregate amount of money owed to members in respect of profits and any other amounts (SI 2008/1912/1913 schedule 1, part 1, section B (notes)).

67. This SORP requires the amount of debts owing to the LLP by members to be disclosed.

68. Amounts owing to and from members should not be offset in the financial statementsunless specifically required or permitted by FRS 102. Debits on members' balances (where, for example, drawings were made during the year in anticipation of profits) should be reviewed for recoverability and shown separately in debtors.

Other disclosures

69. This SORP requires LLPs to disclose the overall policy followed in relation to members' drawings, including an indication of the policy applicable where the cash requirements of the business compete with the need to allow cash drawings by members. Such disclosures should include any transfers of members' interests from

[11] Neither CA 2006 nor the LLP Regulations contain any provisions in relation to capital maintenance of an LLP, such as those in CA 2006 for limited liability companies.

equity to debt (and vice versa) during the year and up to the date the accounts are approved. The policy under which members contribute or subscribe amounts to the LLP by way of equity or debt and the policy under which their contributions and subscriptions are repayable by the LLP, should also be disclosed.

70. In the case of large and medium-sized LLPs, the LLP Regulations require disclosure of the average number of members in the financial year. This is determined by dividing the aggregate number of members of the LLP for each month or part thereof in the financial year by the number of months in the financial year (rounded to the nearest whole number) (SI 2008/1913 schedule 1, part 3, 66 (1)(2)).

71. In the case of large and medium-sized LLPs, the LLP Regulations also require disclosure of the profit (including remuneration) that is attributable to the member with the largest entitlement to profit (including remuneration) where the amount of the profit of the LLP for the financial year before members' remuneration and profit shares exceeds £200,000 (SI 2008/1913 schedule 1, part 3, 66 (3)). The identity of this member need not be disclosed.

72. When determining the disclosable amount, the LLP should take account of all the relevant factors and disclose the policy by which the amount was arrived at, as the LLP Regulations do not provide specific guidance as to how the disclosable amount should be determined. A consistent policy should be applied. Where the LLP has an unconditional right to avoid paying an amount of remuneration or profit, the policy for determining the disclosable amount should be disclosed and should explain how current year unallocated profits and current year allocations of both current and prior year profits are treated.

73. Where LLPs choose to disclose average members' remuneration, this should be calculated by dividing the 'Profit before members' remuneration and profit shares' by the average number of members (as discussed in paragraph 70 above), these being the two items that are required to be disclosed by the LLP Regulations. If any other figure for average members' remuneration is given, it should be reconciled to the figure calculated in accordance with this paragraph.

Cash flow statement presentation

74. In accordance with section 7 of FRS 102, LLPs should present a cash flow statement which analyses cash flows during the period between operating, investing and financing cash activities.[12]

74A. In some cases, judgement will be required to classify certain cash flows. However, foran LLP, transactions with members (and former members) will generally be classified as summarised in the following table.

Nature of transaction	Classification of cash flows
Remuneration that is paid under a contract to provide services to the LLP, which may be referred to as a contract of employment	Operating cash flow
Other remuneration (discretionary or non-discretionary) for services provided	Operating cash flow
Post-retirement payments to former members	Operating cash flow
Capital introduced by members (classified as equity or liability)	Financing cash flow
Repayment of capital or debt to members	Financing cash flow
Payments to members that represent a return on amounts subscribed or otherwise contributed	Financing cash flow

74B. In order to assist with an understanding of an LLP's ability to generate cash flows, andthe needs of that LLP to utilise those cash flows, the LLP should disclose transactions with members (and former members) separately from transactions with non- members.

74C. Paragraph 7.22 of FRS 102 requires an entity to disclose the changes in net debt between the beginning and end of the reporting period. The glossary to FRS 102 defines net debt as consisting of the borrowings of an entity, together with any related derivatives and obligations under finance leases, less any cash and cash equivalents. Although ‘loans and other debts due to members’ would be considered borrowings for the purposes of the definition of net debt they are not external financing. This SORP recommends therefore that LLPs present in the notes to the financial statements an analysis of the movements in net debt for the period, with appropriate subtotals to show the changes in net debt before members’ debt separately from debt relating to members. An example presentation for the net debt reconciliation disclosure requirement is set out below:

[12] Qualifying entities (as defined by FRS 102) may wish to take advantage of the exemption from the requirement to produce a cash flow statement as set out in paragraph 1.12 (b) of FRS 102. Small LLPs are not required to prepare a cash flow statement.

Example presentation for the net debt reconciliation disclosure:

	Balance at beginning of period	Arising from cash flows	New financ e leases	Other non-cash changes	Acquisition or disposal of subsidiaries	Changes in market value and exchange rate movements	Balance at end of period
Cash at bank	x	x	-	-	x	x	X
Overdrafts	(x)	x	-	-	x	x	(x)
Bank borrowings (less than one year)	(x)	x	-	(x)	x	x	(x)
Bank borrowings (more than one year)	(x)	-	-	x	x	x	(x)
Finance leases	(x)	x	(x)	-	x	x	(x)
Net debt (before members' debt)	(x)	x	x	-	x	x	(x)
Loans and other debts due to members							
Members ' capital	(x)	x	-	-	-	x	(x)
Other amounts due to members	(x)	x	-	(x)	-	x	(x)
Net debt	(x)	x	x	(x)	x	x	(x)

RETIREMENT BENEFITS

Retirement benefits of employees and members

75. Post-employment benefits provided for employees of the LLP should be accounted for as required by section 28 *Employee Benefits* of FRS 102. This will include post-employment benefits payable to members that are based on any salary paid to the member under an employment contract. Where members are not employees, section 28 of FRS 102 does not apply.

Other post-retirement payments to members

76. LLPs should analyse their contractual or constructive obligations (including any relating to early retirement options) to make payments to members in their capacity as members at and after the point of their ceasing to be members of the LLP, between:

- those that meet the definition of an insurance contract and, therefore, fall within the scope of FRS 103 *Insurance Contracts*;
- those that give rise to financial liabilities falling within the scope of section 11 *Basic Financial Instruments* of FRS 102;
- those that give rise to financial liabilities falling within the scope of section 12 *Other Financial Instruments Issues* of FRS 102; and
- those that give rise to non-financial liabilities of uncertain timing and amount falling within the scope of section 21 *Provisions and Contingencies* of FRS 102.

In the case of an unconditional contractual obligation that meets the definition of an insurance contract, this will fall within the scope of FRS 103. As explained further in paragraph 80A, this will be the case where, for example, the total amount payable by the LLP may be significantly affected by how long the former member lives.

In the case of an unconditional contractual obligation to deliver cash or other financial assets, this will give rise to a financial liability and will fall within the scope of either section 11 or section 12 of FRS 102 unless it meets the definition of an insurance contract. In the case of a constructive obligation of uncertain timing or amount, or a contractual obligation that is conditional on further service from a member, any obligation for past service will fall within the scope of section 21 of FRS 102.

In the case of a constructive obligation of certain timing and amount, this will fall to be accounted for as a liability under the general provisions of the Companies Act/GAAP.

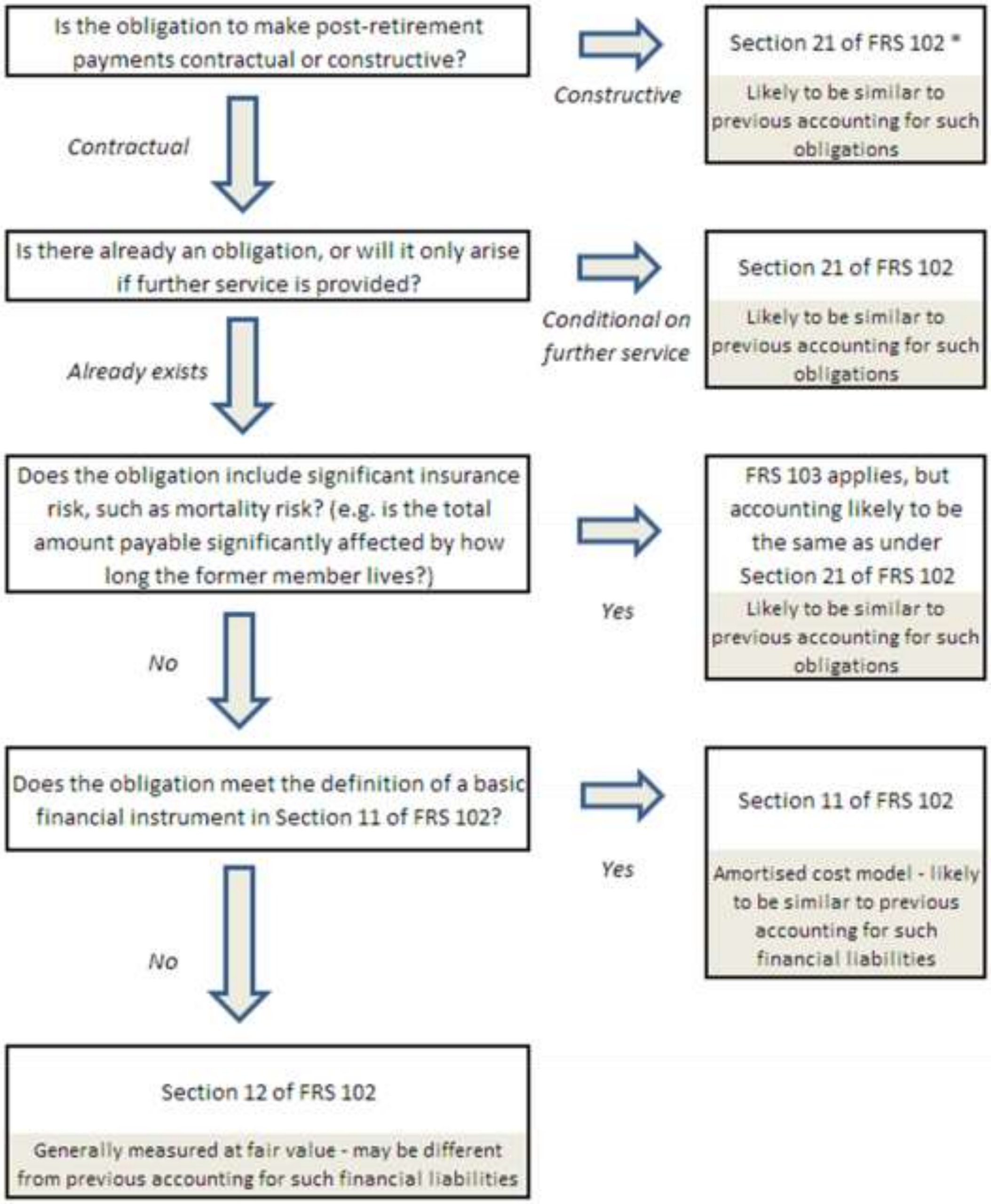
76A. The required accounting and disclosures will differ depending on whether anobligation falls within the scope of FRS 102 or FRS 103 and, if the former, depending on whether the obligation falls within the scope of section 11, section 12 or section 21.[13]

- FRS 103 allows entities, generally, to continue with their existing accounting policies for liabilities within its scope, while permitting limited improvements to those policies.
- Section 11 of FRS 102 requires liabilities within its scope to be measured at amortised cost using the effective interest method.
- Section 12 of FRS 102 generally requires liabilities within its scope to be measured at fair value.
- Section 21 of FRS 102 requires liabilities within its scope to be measured at the best estimate of the amount required to settle the obligation at the reporting date, and gives further guidance on how this is to be determined.[14]

[13] As an accounting policy choice, paragraph 11.2 of FRS 102 allows that, rather than applying the recognition and measurement provisions of sections 11 and 12, an entity can choose to apply either (1) the recognition and measurement provisions of IAS 39 *Financial Instruments: Recognition and Measurement* or (2) the recognition and measurement provisions of IFRS 9 *Financial Instruments* (together with those provisions of IAS 39 that have not yet been superseded by IFRS 9). In all cases, the disclosure requirements of sections 11 and 12 continue to be applicable.

[14] This approach is similar to that previously required by FRS 12 *Provisions, Contingent Liabilities and Contingent Assets*.

76B. The flowchart below summarises how to determine which guidance applies to aparticular obligation. Further guidance on the matters summarised is included below the flowchart.



* unless the obligation is of certain timing and amount, in which case the general provisions of the Companies Act/GAAP apply.

77. Payments by an LLP to members after they have retired, often referred to as annuities, can take many different forms. It will be necessary to examine the nature of the contractual or constructive obligations in order to determine the governingaccounting requirements.

78. Annuity payments may be either 'pre-determined' or 'profit-dependent'.

- 'Pre-determined' annuity payments are amounts payable that are fixed at the time of retirement, for example, by reference to historical earnings (such as a percentage of the final year's profit share) or fixed at an amount, which may be index-linked or linked to a measure independent of the LLP's future profit. The period for which they are payable may or may not be pre-determined. The payment of the retirement benefit is thus not dependent on the LLP earning profits in the post-retirement period.
- 'Profit-dependent' annuity payments are amounts payable to former members that are, in effect, a share of the LLP's on-going profits, by way of a preferential first share, profit points, profit-dependent bonus or some other mechanism. Many different arrangements exist, and there may be no amount payable in a year in which no or insufficient profits are earned.

Constructive obligations

79. Deleted

79A. Arrangements whereby an LLP provides post-retirement benefits can arise from theactions of the LLP in the absence of a formal plan. Where post-retirement payments have been offered consistently to previous members at the point of, but not prior to, retirement this could build an expectation that all members would be offered this benefit at retirement. If such a constructive obligation were to arise, then the point of recognition of the liability would be earlier than retirement, in accordance with the principles of section 21 of FRS 102.

Conditional and unconditional obligations

79B. Often a member of an LLP will obtain an absolute entitlement to an annuity only on reaching a specific milestone, such as reaching a particular age or achieving a specified number of years' service. A member choosing to leave before reaching the milestone will not be entitled to an annuity. On reaching the milestone while remaining a member of the LLP, the member will be entitled to an annuity based on past service. The LLP cannot avoid the liability that is accruing through the service period through its own actions without the agreement of the member (unless it has the right to terminate their membership without compensation for the loss of annuity rights, which is unlikely to be the case). In these circumstances, therefore, a liability should be built up over the period of service rather than just recognised at the date on which the milestone is reached.

79C. A contractual obligation to deliver cash is a financial liability. An obligation to delivercash that is conditional on a member providing further service is not a financial liability. Therefore, to the extent that post-retirement obligations arising in respect of current members are conditional on future service, the liability will fall within the scope of section 21 of FRS 102.

80. Annuities are likely in many cases to be subject to uncertainties. This will be the case, for example, where the payments are dependent on future profits or there is significant mortality risk. It should be noted that uncertainty of timing or amount per se is not the factor that determines whether section 21 of FRS 102 is applicable. Instead, it is important to establish whether the liability is or is not an unconditional contractual liability. An unconditional contractual liability will meet the definition of a financial liability and will, therefore, be excluded from the scope of section 21 of FRS 102.[15]

Mortality risk

80A. An unconditional contractual obligation will meet the definition of an insurancecontract under FRS 103 if the LLP accepts significant insurance risk (typically mortality risk). This will be the case if the total amount payable by the LLP may be significantly affected by how long the former member lives (eg, the LLP agrees to make payments only for as long as the former member is alive, and there is no terminal payment). For accounting purposes, such annuities fall within the scope of FRS 103, unless they are conditional on future service (in which case section 21 of FRS 102 applies).

80B. In practice, obligations to make post-retirement payments to members will often beset out in the members' agreement, and will often reflect significant mortality risk[16] (eg, because the LLP agrees to make payments only for as long as the former member is alive, and there is no terminal payment). Where this is the case, it is likely that the LLP will historically have accounted for the obligations as provisions within the scope of FRS 12 *Provisions, Contingent Liabilities and Contingent Assets*. On adoption of FRS 102, the obligations will fall within the scope of FRS 103; however FRS 103 will permit the LLP to continue its previous accounting policies.[17] Nevertheless, the LLP should consider whether it needs to provide any additional disclosures in order to meet the requirements of FRS 103.

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[15] Financial liabilities outside the scope of section 21 of FRS 102 also include insurance liabilities within the scope of FRS 103.

[16] Appendix II to FRS 103 gives guidance on the definition of an insurance contract. It explains how insurance risk can be distinguished from financial risk, and discusses mortality risk as a form of insurance risk).

[17] For practical purposes, the outcome should be the same as if the entity had applied section 21 of FRS 102, because the requirements of section 21 of FRS 102 are similar to those of FRS 12.

80C. If an annuity is an unconditional contractual obligation for the LLP to deliver cash or a financial asset to a member, and the LLP has not accepted significant insurance risk, the annuity will meet the definition of a financial liability and will fall within the scope of section 11 or section 12 of FRS 102. Paragraphs 11.9 and 11.9A of FRS 102 specify the conditions that must be met for such a financial liability to fall within the scope of section 11. If these conditions are not met, the financial liability will fall within the scope of section 12. Profit-dependent annuity payments will not meet the conditions in paragraphs 11.9 and 11.9A of FRS 102. Therefore, if such annuity payments arise under a contract, and they do not expose the LLP to significant insurance risk, they will be accounted for in accordance with section 12 of FRS 102.

81. Deleted

Recognition and measurement – general

82. A liability in respect of an annuity is recognised when a member obtains an actual or constructive right to the annuity, which the LLP has no discretion to withhold.

83. If the rights to an annuity are earned over a period, then costs should be recognised over that period. This is consistent with the guidance on executory contracts in section 21 of FRS 102, under which the LLP has either an obligation or a constructive obligation to pay the annuity which builds up over time.

84. Deleted

Recognition and measurement – applying section 21 of FRS 102

85. To the extent that the liability falls within the scope of section 21 of FRS 102 eg, because it is conditional on future service, the LLP should assess the probability of a future cash outflow applying the measurement requirements of that section. Any such liability for post-retirement payments to members earned to date and therefore recognised in the accounts should reflect the latest expectations in respect of:

- the likely date of ceasing to be a member; and
- the amounts likely to be payable from that date.

86. The value of the liability should be based on the best estimate of the present value of future cash flows. In practice, it will often be appropriate to value the liability on an actuarial basis consistent with the principles of section 28 of FRS 102 for the measurement of pension liabilities. Where, because of their nature and/orcomplexity, the arrangements are such that it is appropriate to apply the guidance insection 28, then that guidance should be applied in arriving at the measurement ofthe liability. In the case of profit-dependent payments, it will be necessary for the LLPto make a best estimate of the level of future profits of the LLP. Only in extremely rarecases will no reliable estimate be capable of being made. In these extremely rare

cases, if accounting for the liability under section 21 of FRS 102, then a liability exists that cannot be recognised. This is disclosed as a contingent liability.

87. The liability should be recalculated annually to take account of changes inmembership, eligibility for post-retirement payments, financial estimates andactuarial assumptions.

87A. The table below sets out examples of the applicable guidance for particular scenarios.

Example of post-retirement benefit	Applicable guidance
Former member is contractually entitled to an agreed percentage of annual LLP profits each year until death.	Obligation includes significant mortality risk, so FRS 103 applies (see paragraph 80C for discussion of accounting treatment).
Former member is contractually entitled to payment of pre-determined amounts annually for five years after retirement (amounts continue to be payable after death).	No mortality risk and liability qualifies as a 'basic financial instrument', so section 11 of FRS 102 applies.
Former member is contractually entitled to an agreed percentage of annual LLP profits for five years after retirement (amounts continue to be payable after death).	No mortality risk and liability does not qualify as a 'basic financial instrument', so section 12 of FRS 102 applies.
No contractual obligation to pay post-retirement benefits to members, but past practice has established a constructive obligation to do so.	Obligation does not qualify as a financial liability, so section 21 of FRS 102 applies.
An individual has to be a member for five years in order to become entitled to receive post-retirement benefits. A particular individual has only been a member for three years.	Obligation does not qualify as a financial liability during the initial five year period, because it is conditional on future service, so section 21 of FRS 102 applies in that period.

Post-retirement payments to members: presentation

88. Amounts recognised in respect of current members should be charged to the profit and loss account (or statement of comprehensive income) within members' remuneration charged as an expense. This SORP requires that the recognition of and changes in the liability for post-retirement payments to or in respect of current members and to or in respect of former members should be shown separately. The change in the liability in respect of former members should be expensed in the relevant expense item (that is, not in members' remuneration) in the profit and loss account (or statement of comprehensive income). The change in the liability in respect of current members should be charged to the profit and loss account (or statement of comprehensive income) within members' remuneration charged as an expense.

89. This SORP requires that the liability for post-retirement payments to or in respect of current members and to or in respect of former members should be shown separately. The liability in respect of former members should be shown in the prescribed balance sheet formats set out in the LLP regulations under 'Provisions for liabilities'[18] or 'Creditors'[19] as appropriate, as 'Post-retirement payments to former members'. The liability in respect of current members should be shown separately, if material, as a component of 'Loans and other debts due to members' in the prescribed balance sheet formats in the LLP regulations. In the year in which a member retires, a transfer should be made between the balance in respect of current members and the balance in respect of former members.

90. Where the liability has been discounted (for example, as required by section 21 of FRS 102 where the effect is material), this SORP requires that the unwinding of the discount should be presented next to the interest cost line in the profit and loss account (or statement of comprehensive income), to the extent that it relates to former members. Where it relates to current members it should be included in members' remuneration charged as an expense.

91. Additional annuities granted after the date of a member's retirement should be recognised in full in the profit and loss account (or statement of comprehensive income) within operating profit as soon as the award is granted to the former member.

Post-retirement payments to members: disclosure

92. This SORP requires that the LLP's accounting policy note should disclose the LLP's policy in respect of post-retirement payments to members.

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[18] This classification will be appropriate if the liability arises from a constructive obligation (eg, it is within the scope of section 21 of FRS 102).

[19] This classification will be appropriate if the liability is a contractual liability (ie, it is within the scope of FRS 103, or either section 11 or section 12 of FRS 102).

On transition of a partnership or other undertaking to an LLP

93. Where an LLP makes post-retirement payments to members of a predecessor partnership or other organisation, the extent to which the LLP has an actual or constructive liability for such payments should be considered. Where an actual or constructive liability exists, this should be recognised in the balance sheet of the LLP. Where there is merely recourse to the LLP in the event of a default of a third party and such default has not occurred and is not probable, this should be disclosed as a contingent liability.

94. It is possible that an LLP which succeeds to the business of a partnership will not assume actual or constructive liability for post-retirement payments payable by the predecessor partnership or partners therein. However, it may, as agent for the members of the LLP, disburse the related cash to the former members.[20] In such circumstances, the payments to the former members represent amounts in respect of their services to the former partnership which the LLP is distributing to the former members as agent of the continuing members and do not represent liabilities of the LLP. Reference to these arrangements is encouraged by this SORP where this would aid clarity.

TAXATION

95. Where tax (whether current or deferred) to be paid on members' remuneration is a personal liability of the members, it falls within 'Members' interests' on the balance sheet. It should not appear in the profit and loss account (or statement of comprehensive income).

96. Amounts retained by an LLP in respect of a member's tax liability do not require separate disclosure. In such cases, the LLP is simply acting as agent of the member by settling the liability direct to the tax authorities. Amounts retained for tax should be included in 'Loans and other debts due to members'.

97. Tax withheld from members who subsequently retire from membership should be dealt with as any other balance due to former members.

98. Where tax is not a personal liability of the members and the LLP itself is subject to tax on profits, then the LLP should report such taxes in their accounts as required by section 29 of FRS 102.

99. In the group accounts of an LLP which include entities or organisations that are not partnerships or LLPs, such as companies, the tax of such entities should be recorded in the profit and loss account (or statement of comprehensive income) under the relevant heading and any related liability carried as a creditor in the balance sheet.

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[20] Whether such arrangements exist will depend on the terms of the agreement between the predecessor partners and the former members, as varied by any agreements entered into at the time the LLP succeeds to the business of the predecessor partnership.

INVENTORIES

100. To the extent that an LLP has inventories carried at cost, the cost of members' time and related overheads should be accounted for in accordance with section 13 *Inventories* of FRS 102. Contracts should be accounted for in accordance with section 23 *Revenue* of FRS 102.

101. When calculating the cost of inventories in accordance with section 13 of FRS 102, thecost of members' time should be considered. The cost of members' time will include only those elements that would be expensed in the profit and loss account (or statement of comprehensive income) ie, members' remuneration charged as an expense as defined in paragraph 21 above. However, regardless of whether the time input by a member is a cost to be included in inventories, any overhead related to that time should be included in the cost of inventories.

BUSINESS COMBINATIONS AND GROUP ACCOUNTS

Entity and group accounts

102. An LLP should follow the rules on the requirement to prepare group accounts (and the exemptions therefrom) and the contents of the group accounts (and on inclusion and exclusion of subsidiaries and consolidation of special purpose entities) set out in section 9 of FRS 102, together with the relevant sections of the LLP Regulations.

Accounting for business combinations

103. Application of GAAP with respect to business combinations should be considered in the context of both the group accounts and the entity accounts of the LLP.

104. When two LLPs combine, there may be only one surviving LLP, or a new LLP may be created or one LLP may become a member of the other. The recommended accounting treatment may therefore apply both to the entity accounts of an LLP and, if relevant, to its group accounts.

105. Consideration will be required to determine whether a particular business combination represents a group reconstruction because such transactions may be accounted for using the merger method instead of the purchase method. The LLP regulations (SI 2008 1912 schedule 3, 10 / SI 2008 1911 schedule 4, part 1, 7) allow an acquisition to be accounted for as a merger if adoption of the merger method of accounting accords with generally accepted accounting principles or practice ('GAAP'). FRS 102's glossary sets out the arrangements that meet the definition of a group reconstruction and paragraph 19.27 sets out conditions that must be met for a group reconstruction to be accounted for using the merger method. One of the conditions in paragraph 19.27 is that the use of the merger accounting method is not prohibited by company law or other relevant legislation. The LLP regulations do not prohibit the use of the merger method and refers to 'GAAP' as the authoritative guidance on whether use of the merger method is appropriate.

105A. The circumstances of business combinations will vary greatly. Where a business combination is not simply the granting of membership to one or more individuals, it will need to be assessed against section 19 of FRS 102.

Acquisition accounting

106. The purchase method is required for all business combinations except for:

- group reconstructions where the conditions in paragraph 19.27 of FRS 102 are met; and
- certain public benefit entity combinations.[21]

107. Where the purchase method is used, the fair value of the purchase consideration used in the calculation of goodwill arising on an acquisition should be assessed carefully. In particular, this SORP requires the profit share promised to the new members in the enlarged LLP to be assessed to determine whether any portion of that remuneration represents consideration for the business acquired, rather than future members' remuneration. For example, if members of the purchased entity were awarded an increased profit share for a limited period of time after the acquisition, falling back to 'normal' remuneration levels thereafter, this may suggest that the short-term excess amounts were part of the purchase consideration. In all cases, the sale and purchase agreement will need to be closely examined to determine the substance of the arrangement.

108. Where it is not possible to value the consideration given in accordance with the requirements of paragraph 19.11 of FRS 102, the best estimate of its value may be obtained by valuing the entity acquired.

108A. Negative goodwill arises when the cost of a business combination is less than the fair value of the net amount of identifiable assets and liabilities recognised on acquisition. For example, a business combination that involves two independent LLPs coming together but where no cash is paid by either party and no additional amounts of purchase consideration are identified in accordance with paragraph 107. If significant intangible assets are recognised on acquisition this can result in negative goodwill. Paragraph 19.24 of FRS 102 sets out the requirements for accounting for negative goodwill.

108B. Intangible assets acquired in a business combination are required to be recognised separately from goodwill when the general recognition criteria in paragraph 18.4 of FRS 102 are met and the intangible assets arise from contractual/legal rights and are separable. Paragraph 18.8 of FRS 102 also allows an LLP to choose whether or not to recognise additional intangible assets if they meet the general recognition criteria in paragraph 18.4 and arise from either contractual/legal rights or are separable. The policy choice should be applied to all intangibles in the same class and be applied consistently to all business combinations. Taking up this policy choice could potentially

[21] LLPs will rarely be public benefit entities as defined under FRS 102.

increase the amount of negative goodwill recognised in certain business combinations, such as those outlined in paragraph 108A. In such circumstances, an LLP might conclude that it is preferable to have a policy of not recognising such additional intangible assets.

109. Deleted

110. Deleted

111. Deleted

Group reconstructions

112. The transfer of all or the majority of the assets, liabilities and business of an existing partnership, limited company or other undertaking into an LLP incorporated for that purpose could be dealt with as a group reconstruction where the requirements of paragraph 19.27 of FRS 102 are met. Although FRS 102 provides a choice in these cases, this SORP recommends that the merger accounting method should be used where permitted, to reflect the substance of initial 'conversion' to LLP.[22] The initial 'opening' balance sheet should follow the accounting policies of the LLP.

Considerations on transition from an existing undertaking (including from a partnership)

113. Deleted

114. Both start-up businesses and existing undertakings, including partnerships and limited companies, may choose to incorporate as LLPs. This SORP requires that where there is a transfer of an existing undertaking to an LLP, it should be accounted for using the merger accounting method provided that the transfer meets the definition of a group reconstruction and the conditions of paragraph 19.27 of FRS 102.

115. Single-entity LLPs that are formed for the purpose of the transfer of existing undertakings or partnerships, which meet the definition of a group reconstruction and the requirements of paragraph 19.27 of FRS 102 should, as noted above use merger accounting for the initial transfer of business, and reflect the transfer of the assets and liabilities at book value.[23] They should also disclose comparative pro-forma amounts in the financial statements of the first period after incorporation. Those comparative amounts should be stated on the basis of the accounting policies adopted by the LLP. The initial statutory reporting period may or may not be a 12-month period.

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[22] Typically such transfers are transacted at book value not fair value and therefore the merger accounting method reflects the substance of the transaction.

[23] Where the transfer takes place in the year FRS 102 is adopted or in the comparative year, then the book values and pro-forma amounts carried across from the transferor should be FRS 102 compliant.

116. In some cases there may be a hiatus between the formation of the LLP and the transferof the existing undertaking. Where this occurs, and the merger accounting method is used, the principles of merger accounting are such that the net assets at book values should be reflected in the financial statements at the date of the transfer, and the results should be included for the period from the transfer to the end of the accounting period. A pro-forma profit and loss account (or statement of comprehensive income), including corresponding amounts, should be given for the whole of the original entity's accounting period spanning the transfer. These issues are considered in Appendix 4.

117. The restatement of comparatives to consistent accounting policies will often result in a difference between the amount reported as attributable to owners by the predecessor undertaking (eg, the total interests of partners in the predecessor firm shown by its final balance sheet), and the members' interests in the opening balance sheet of the LLP. This SORP requires that such differences are not dealt with in the financial statements of the LLP.

117A. When identifying adjustments to comparatives that may be needed, this SORPrequires that an entity should consider:

- whether any accounting policies applied by the predecessor undertaking need to be amended because they are not in accordance with FRS 102;
- whether any other accounting policies applied by the predecessor undertaking are to be amended voluntarily; and
- whether any changes to members' rights arise on transition and, if so, their effects. For example, profit distributions and repayments of capital may have been discretionary for the predecessor undertaking but will be non-discretionary for the LLP. In such a scenario, members' interests previously reported as equity by the predecessor undertaking may be reported as liabilities by the LLP.

118. The disclosures required by section 19 of FRS 102, SI 2008/1913 schedule 3, 7–16Aand SI 2008/1912 schedule 4, part 1, 7–16A will be required.

119. Existing groups that use merger accounting for a group reconstruction that puts a new LLP at the top of the group should present corresponding amounts in the financial statements of the period of the merger, as required by paragraph 19.30 of FRS 102.

PROVISIONS AND OTHER IMPLICATIONS OF SECTION 21 OF FRS 102

120. Section 21 of FRS 102 applies in all respects to LLPs.[24]

[24] Professional services firms will apply section 21 of FRS 102 in relation to claims against them and associated insurance reimbursements. Such matters are not specific to LLPs and so are not addressed in this SORP.

121. While the application of section 21 of FRS 102 is unlikely to present any unusual problems for LLPs, applying it fully may require a significant change in practice for existing partnerships that are incorporated as an LLP. Historically, partnership accounting has focused heavily on what was perceived as equitable between partners and different year groups of partners, since there are often different partners and/or differing profit shares in successive years. By agreement, major liabilities may have been spread over several years, often to match cash flows, rather than being fully provided immediately.

122. When considering section 21 of FRS 102, an LLP should have regard to all contracts and all relevant circumstances, including side agreements and promises whether or not in writing.

123. The basis of allocation of profits between members is a private matter and will usually be governed by the members' agreement referred to in the LLP legislation. There is no reason why the determination of profits to be allocated to members cannot be based on different accounting policies from those applied to the financial statements of the LLP.

124. If the LLP has entered into any guarantee or indemnity with respect to the borrowings of a member or members personally, the existence of such a guarantee or indemnity should either be disclosed as a note to the accounts (SI 2008/1913 schedule 1, part 3, 60 and SI 2008/1912 schedule 1, part 3, 55) (where it is unlikely that the guarantee or indemnity would be called) or provided for in the primary statements where there is an actual or constructive liability as defined under section 21 of FRS 102 and it is probable that the guarantee or indemnity will be called.[25]

125. It is common practice within partnerships for partners to borrow to fund their capital and similar interests in a firm. Such arrangements may involve the firm entering into guarantees, indemnities or undertakings with the lender concerned. Broadly similar arrangements may occur with regard to members of LLPs and the LLP itself.

126. Of itself, the extent to which members' interests have been financed by lenders, who have lent funds to the member or members concerned, is not a matter for disclosure. Similarly, any undertaking that the LLP may give to act as agent for a member, in remitting funds from members' interests to a lender or other third party, need not be disclosed.

127. A provision would be required where, for example, an LLP has undertaken to repay a loan of a member, such that the LLP is under a legal or constructive obligation to ensure that the full liability to the lender is settled, and it is more likely than not that

[25] LLPs applying the recognition and measurement provisions of IFRS 9 or IAS 39 (as allowed by paragraphs 11.2 and 12.2 of FRS 102) will need to follow the recognition and measurement rules for financial guarantees set out in those standards. Entities may also choose to apply FRS 103 to financial guarantee contracts.

the guarantee will be called upon.[26] Where a provision of this nature has been made in relation to a member who is a related party (see paragraphs 128 – 131 below), further disclosures should be given in accordance with section 33 *Related Party Disclosures* of FRS 102.

RELATED PARTIES

128. The provisions of section 33 of FRS 102, including the definition of related parties, apply to LLPs. An LLP which is under the control of another LLP, partnership, company or other entity will be a related party of that other entity. The fact that some members of an LLP are members of another LLP or another partnership does not in itself make the businesses related parties: the extent of common control and/or influence determines this. This SORP requires that predecessor partnerships of LLPs should be treated as related parties of the LLP.

129. The nature and extent of members' involvement in the management of the LLP should be considered, to determine whether a member is a related party.

130. In the case of smaller LLPs, where all members play a part in the management of the entity, it will frequently be the case that all members are related parties. However, in larger LLPs, it may not be appropriate for all members of an LLP to be considered as related parties. Section 33 of FRS 102 includes directors of companies as key management personnel by definition, and the key management personnel of a reporting entity are defined as related parties of that entity. Key management personnel of an LLP are those persons – whether designated members, members or employees – having authority and responsibility for planning, directing and controlling the activities of the LLP, directly or indirectly.

130A. Paragraph 33.7 of FRS 102 requires the disclosure of the total of compensation paidto key management personnel which may comprise elements of employee remuneration and profit attributable to members.

131. The controlling party and ultimate controlling party of an LLP, if different, should be disclosed in accordance with section 33 of FRS 102. This includes an individual or entity which has the ability to direct the financial and operating policies of the LLP so as to obtain benefits from its activities even though that party may not be entitled to the majority of profits or have invested the majority of capital represented by equity or debt.

COMPLIANCE STATEMENT

132. Paragraph 6 of FRS 100 *Application of Financial Reporting Requirements* requires an LLP, other than a small LLP applying the small entities regime, to provide certain disclosures regarding the application of the SORP or of any areas of non-compliance.

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[26] The LLP will need to consider the extent to which it has the legal right to offset the aggregate 'capital' and undrawn profits of the member concerned against the outstanding debt.

Although small LLPs applying the small entities regime are not required to provide the disclosures outlined in paragraph 6 of FRS 100 they are encouraged to do so.

EFFECTIVE DATE AND TRANSITION

133. The revised SORP should be applied for accounting periods beginning on or after 1 January 2019.

133A. Early adoption is permitted for accounting periods beginning before 1 January 2019 provided all the amendments to this 6th edition of the SORP and the March 2018 edition of FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland,* are adopted from the same date. There are some exceptions to this rule as set out in paragraph 1.18 of FRS 102.

134. In implementing the provisions of this SORP that relate to changes introduced by the Triennial review 2017 amendments, LLPs should have regard to paragraph 1.19 of FRS 102 which provides two exceptions to the requirement for retrospective application. This SORP recommends that consideration should be given to the impact of resulting accounting policy changes and their impact not only on the division of current period profits but also on profits arising from prior years where appropriate.

APPENDIX 1: EXAMPLES SHOWING THE PRESENTATION OF MEMBERS' INTERESTS[27]

(The LLP has no retirement benefit arrangements for current members in these examples)

EXHIBIT A – LLP Balance Sheet

LLP WITH NO EQUITY	20X5 £'000	20X4 £'000
Fixed assets		
Tangible assets	9,500	8,200
Current assets		
Debtors		
Amounts recoverable on contracts	8,000	7,500
Trade debtors	17,500	16,000
Amounts due from members	1,500	1,200
Other debtors and prepayments	4,000	3,800
Cash at bank and in hand	6,000	4,500
Current assets	37,000	33,000
Creditors: amounts falling due within one year		
Bank overdraft and loans	3,000	2,800
Other creditors and accruals	6,500	6,000
Current liabilities	9,500	8,800
Net current assets	27,500	24,200
Total assets less current liabilities	37,000	32,400
Creditors: amounts falling due after more than one year		
Bank loans	4,000	3,200
Provisions for liabilities		
Post-retirement payments to former members	4,500	4,800
Other provisions	2,000	1,900
	6,500	6,700
NET ASSETS ATTRIBUTABLE TO MEMBERS	26,500	22,500
REPRESENTED BY:	20X5 £000	20X4 £000
Loans and other debts due to members within one year		
Members' capital classified as a liability	8,000	6,000
Other amounts	18,500	16,500
	26,500	22,500
TOTAL MEMBERS' INTERESTS		
Amounts due from members	(1,500)	(1,200)
Loans and other debts due to members	26,500	22,500
	25,000	21,300

Note: in this example, Members' other interests are nil.

[27] The exhibits in this appendix do not reflect the increased flexibility in balance sheet and profit & loss formats introduced by SI 2016/575. See paragraph 26B for more details.

EXHIBIT B – LLP Balance Sheet

LLP WITH SOME EQUITY	20X5	20X4
	£'000	£'000
Fixed assets		
Tangible assets	9,500	8,200
Current assets		
Debtors		
Amounts recoverable on contracts	8,000	7,500
Trade debtors	17,500	16,000
Amounts due from members	1,500	1,200
Other debtors and prepayments	4,000	3,800
Cash at bank and in hand	6,000	4,500
Current assets	37,000	33,000
Creditors: amounts falling due within one year		
Bank overdraft and loans	3,000	2,800
Other creditors and accruals	6,500	6,000
Current liabilities	9,500	8,800
Net current assets	27,500	24,200
Total assets less current liabilities	37,000	32,400
Creditors: amounts falling due after more than one year		
Bank loans	4,000	3,200
Provisions for liabilities		
Post-retirement payments to former members	4,500	4,800
Other provisions	2,000	1,900
	6,500	6,700
NET ASSETS ATTRIBUTABLE TO MEMBERS	26,500	22,500
REPRESENTED BY:	20X5	20X4
	£000	£000
Loans and other debts due to members within one year		
Members' capital classified as a liability	5,000	4,000
Other amounts	9,000	8,000
	14,000	12,000
Members' other interests		
Members' capital classified as equity	3,000	2,000
Members' other interests – other reserves classified as equity	9,500	8,500
	26,500	22,500
TOTAL MEMBERS' INTERESTS		
Amounts due from members	(1,500)	(1,200)
Loans and other debts due to members	14,000	12,000
Members' other interests	12,500	10,500
	25,000	21,300

EXHIBIT C – LLP Profit and Loss Account (Format 2)

LLP WITH AUTOMATIC DIVISION OF PROFIT EQUIVALENT TO SALARIED REMUNERATION	20X5 £'000	20X4 £'000
Turnover	55,500	49,500
Other operating income	3,500	2,000
	59,000	51,500
Other external charges	(8,500)	(7,500)
Staff costs	(21,500)	(18,500)
Depreciation	(2,000)	(2,000)
Other operating expenses	(11,000)	(9,000)
Operating profit	16,000	14,500
Interest receivable and similar income	1,000	1,000
Interest payable and similar charges	(500)	(750)
Profit for the financial year before members' remuneration and profit shares	16,500	14,750

Profit for the financial year before members' remuneration and profit shares	16,500	14,750
Members' remuneration charged as an expense	(3,000)	(2,500)
Profit for the financial year available for discretionary division among members	13,500	12,250

Note 1: This example may apply to an LLP which has a members' agreement or other profit sharing arrangement which gives members the equivalent of a salary. It is not intended to suggest that all LLPs should impute notional salaries.

EXHIBIT D – LLP Profit and Loss Account (Format 2)

LLP WITH AUTOMATIC DIVISION OF ALL PROFITS

	20X5	20X4
	£'000	£'000
Turnover	55,500	49,500
Other operating income	3,500	2,000
	59,000	51,500
Other external charges	(8,500)	(7,500)
Staff costs	(21,500)	(18,500)
Depreciation	(2,000)	(2,000)
Other operating expenses	(11,000)	(9,000)
Operating profit	16,000	14,500
Interest receivable and similar income	1,000	1,000
Interest payable and similar charges	(500)	(750)
Profit for the financial year before members' remuneration and profit shares	16,500	14,750

Profit for the financial year before members' remuneration and profit shares	16,500	14,750
Members' remuneration charged as an expense	(16,500)	(14,750)
Result for the financial year available for discretionary division among members	–	–

This example may apply to an LLP which has a members' agreement or other profit sharing arrangement which has arrangements which automatically divide the full amount of theearned profit among members.

EXHIBIT E – LLP Profit and Loss Account (Format 2)

LLP WITH NO AUTOMATIC DIVISION OF ANY PROFIT	20X5 £'000	20X4 £'000
Turnover	55,500	49,500
Other operating income	3,500	2,000
	59,000	51,500
Other external charges	(8,500)	(7,500)
Staff costs	(21,500)	(18,500)
Depreciation	(2,000)	(2,000)
Other operating expenses	(11,000)	(9,000)
Operating profit	16,000	14,500
Interest receivable and similar income	1,000	1,000
Interest payable and similar charges	(500)	(750)
Profit for the financial year before members' remuneration and profit shares available for discretionary division among members	16,500	14,750

This example may apply to an LLP which has a members' agreement or other profit sharing arrangement which has no element of automatic division of profit and does not give members any rights to a share in the profits until it is divided.

EXHIBIT F – LLP Statement of Comprehensive Income (single statement (Profit and loss account Format 2)

LLP WITH SOME AUTOMATIC DIVISION OF PROFIT

	20X5 £'000	20X4 £'000
Turnover	55,500	49,500
Other operating income	3,500	2,000
	59,000	51,500
Other external charges	(8,500)	(7,500)
Staff costs	(21,500)	(18,500)
Depreciation	(2,000)	(2,000)
Other operating expenses	(11,000)	(9,000)
Operating profit	16,000	14,500
Interest receivable and similar income	1,000	1,000
Interest payable and similar charges	(500)	(750)
Profit for the financial year before members' remuneration and profit shares	16,500	14,750
Profit for the financial year before members' remuneration and profit shares	16,500	14,750
Members' remuneration charged as an expense	(3,000)	(2,500)
Profit for the financial year available for discretionary division among members	13,500	12,250
<u>Other comprehensive income:</u>		
Revaluation of freehold property	2,500	1,000
Actuarial loss on defined benefit pension scheme	(3,000)	(1,500)
Total comprehensive income	13,000	11,750

EXHIBIT G – LLP Statement of Comprehensive Income (single statement (Profit and loss account Format 2)

LLP WITH NO AUTOMATIC DIVISION OF ANY PROFIT

	20X5 £'000	20X4 £'000
Turnover	55,500	49,500
Other operating income	3,500	2,000
	59,000	51,500
Other external charges	(8,500)	(7,500)
Staff costs	(21,500)	(18,500)
Depreciation	(2,000)	(2,000)
Other operating expenses	(11,000)	(9,000)
Operating profit	16,000	14,500
Interest receivable and similar income	1,000	1,000
Interest payable and similar charges	(500)	(750)
Profit for the financial year before members' remuneration and profit shares available for discretionary division among members	16,500	14,750
<u>Other comprehensive income:</u>		
Revaluation of freehold property	2,500	1,000
Actuarial loss on defined benefit pension scheme	(3,000)	(1,500)
Total comprehensive income	16,000	14,250

APPENDIX 2: LIABILITY AND EQUITY ELEMENTS OF MEMBERS' INTERESTS

General

1. The interests of members in an LLP are typically governed by the LLP's members' agreement. Compared to the articles of association for limited companies, LLPs have considerable flexibility over how that agreement is drafted, and there is wide diversity in practice. The absence of standard arrangements makes it necessary to analyse each members' agreement with care so that members' equity and liability interests are properly reflected in the financial statements.

2. The members' agreement will specify what members are expected to provide to the LLP and what they will receive in return. Depending on the nature of the LLP and what has been agreed, members may or may not provide services or expertise to the LLP, and they may or may not be required to provide cash, or other assets, as members' capital. They may receive equity or liability interests in the LLP or a combination of the two. One purpose of the examples below is to illustrate that there need not be symmetry between the treatment of amounts subscribed as members' capital and the 'returns' arising. For example, a member may be able to demand repayment of capital subscribed (liability, unless the conditions for the puttables exception are met) but the LLP may have discretion over the division of profits (equity).

3. It will generally be necessary when analysing members' interests between equity and liabilities, to ascertain the rights that may be exercised by an individual member against the LLP. For example, where the profits are only divided if the LLP[28] so decides, an individual member will not be entitled to a share of those profits unless and until a decision to divide them is taken; accordingly, the profits will constitute an equity interest (and will continue to do so even if a decision by the LLP to divide the profits is taken during the year in which the profits are earned; although, so far as the balance sheet is concerned, the taking of such a decision will convert the profits into a liability owed by the LLP to its members).[29] By contrast, where the members have agreed in the LLP agreement in force at the time to an automatic division of profits, such that no further decision needs to be made to determine the amount of profit to be divided among members, the individual will be entitled to a share of those profits based on his percentage profit share, and accordingly his profit share will fall to be treated as an expense in profit or loss (and also as a liability in the balance sheet insofar as the profit remains unpaid at the balance sheet date).

3A. For example, the LLP agreement may require that all profits are divided (often the term 'allocated' is used in LLP agreements) such that the LLP has no discretion as to how much profit is divided but does allow the LLP discretion as to how the divided profit is shared between members. There may be different 'layers' in this sharing process whereby some members only have a fixed share, others only have a discretionary share (or have both fixed and discretionary share) and others only a share in the balance. Even though the LLP has some discretion as to member's profit

[28] Members as whole or a committee of the members with relevant authority.

[29] See Appendix 1 Exhibit E and Exhibit G.

share entitlements it cannot avoid the obligation to divide all the profits as thisdecision is automatic. Such an arrangement is called automatic division. This wouldalso be the case where there is a requirement to divide some or all profits but thebasis upon which those profits are shared between individual members is notdetermined until after the balance sheet date. This is because for an obligation to existat the balance sheet date it is not necessary to know the precise identity of the partiesto whom the obligation is owed or how the amounts to satisfy the obligation are to beshared. [30]

3B. Another common example seen in practice is where the LLP agreement specifies thatthe profit to be divided is that as stated in the LLP's audited accounts as approved by the members. Although the amount of the profits to be divided will not be known until the audit is complete, the LLP cannot avoid the obligation to divide all the profits reported in the LLP's audited accounts as this decision is automatic. In addition, the fact that members have to approve the audited accounts does not mean that the LLP can avoid the obligation to divide all the profits. Once the members approve the accounts the LLP has to divide all the profits as this decision is automatic. The LLP is a body corporate with legal personality separate from that of its members. The LLP agreement in force at the time determines the contractual obligations of the LLP. Therefore, the requirement for members to approve the LLP's accounts does not enable the LLP to avoid its obligation.

3C. Some LLP agreements specify that the profit to be divided is that as stated in a'distribution account'; this being distinct from the statutory accounts. The basis of preparation of the 'distribution account' is usually set out in the LLP agreement. Although the amount of the profits to be divided will not be known until the amount in the 'distribution account' is determined, the LLP cannot avoid the obligation to divide the profits in the 'distribution account' as this decision is automatic.

Capital and remuneration

4. The examples set out below, which are provided for guidance only, illustrate how the principles set out in the SORP should be applied to participation rights. The matters set out in the following paragraphs are relevant when considering those examples.

5. Paragraph 34 above deals with the issue of when to treat remuneration and amounts subscribed (capital) separately for accounting purposes because there is no clearly identifiable return on capital and the substance of the arrangement makes it inappropriate to treat remuneration as a return on capital. This separate analysis will most often apply in situations where the members of the LLP provide services to that LLP (for example, professional services firms). In such situations remuneration and profit shares are often payable to members in return for participation in the business as well as representing a financial return on amounts invested by members, and the

[30] See Appendix 1 Exhibit A and Exhibit D.

latter element will represent a relatively insignificant proportion of total remuneration.

6. When considering whether a particular payment to a member is a return on capital subscribed or, for example, a payment in relation to services, an entity should apply paragraph 34 of the SORP. Accordingly this SORP requires:

- where a member provides both capital and services to an LLP and no element of the return to the member is clearly identifiable as a return on the amount subscribed or otherwise contributed, no part of the return to the member (which may include inter alia salary, bonus, risk premium and allocated share of profits) will be regarded as a return on capital;
- where a member provides both capital and services to an LLP but an element of the return to the member is clearly identifiable as a return on amounts subscribed or otherwise contributed, only that element will be regarded as a return on capital; and
- where a member provides no services to an LLP then the whole of the return to the member will be regarded as a return on capital.

7. In relation to the consideration of the puttables exception only cash flows and contractual terms and conditions relating to the instrument holder as an owner of the entity should be considered. For example, if certain partners are remunerated for providing a guarantee to the entity this would be disregarded when considering the requirements under the puttables exception. If it is determined that the cash flows and contractual terms and conditions relate to the instrument holder as an owner of the entity then provisions of the puttable exception should be considered. In doing so it is first necessary to establish whether the capital and remuneration are beinganalysed together or separately (see paragraph 34 of the SORP and the discussion inparagraphs 5 and 6 above).

8. To summarise, based on the analysis above, part or all of the capital subscribed by a member will be accounted for as a liability a) if the LLP is obliged to make payments to the member which are clearly identifiable as a return on that capital (eg, interest on an annual basis), or b) there are circumstances in which the member can demand repayment of capital (eg, on retirement) and the conditions under the puttables exception are not met.

Example 1 – Discretionary repayment of capital and discretionary division of profits

The analysis in this example applies irrespective of whether the members provide services to the LLP.

An LLP has ten members. Under the terms of the members' agreement, each member subscribes £100,000 as initial capital and will receive a 10% share of any profits that are divided. Upon retirement of a member, the LLP is required to pass a resolution before any capital is repaid. If no such resolution is passed, the LLP is entitled to retain the capital indefinitely. Any decision to divide profits must be approved by a majority of the members. All cash outflows to members are at the discretion of the LLP. For example, a positive resolution is required to repay capital, and without it the LLP has no obligation to repay the amounts. Accordingly:

- the capital subscribed of £1,000,000 is presented within equity; and
- divisions of profit are reported as equity appropriations when they occur (whether during or after the end of the period).

Thus, if the LLP made profits of £500,000 before profit sharing, and £300,000 was paid out to members as drawings during the year, the profit reported for the year would be £500,000. The drawings of £300,000 would be included in debtors as required by paragraph 68 of this SORP, because they are made before the approval to divide any profits has occurred, and the £500,000 of unallocated profits would be included within equity at the year end, assuming that at that point in time, the decision to divide profits had not been made. Once the profits are divided, the amount of drawings in debtors would be offset against the liability then created.

Example 2 – Discretionary repayment of capital and mandatory interest payment

The analysis in this example applies irrespective of whether the members provide services to the LLP.

An LLP's constitution requires that members subscribe capital to the LLP. Upon retirement, the LLP is required to pass a resolution before any capital is repaid. If no such resolution is passed, the LLP is entitled to retain the capital indefinitely. Interest at a market rate is automatically payable on all capital subscribed. Any decision to divide the balance of profits must be approved by a majority of the members.

In this example, although a positive resolution is required to repay capital, the LLP is obliged to pay a return on that capital. Accordingly, a liability will be recognised on subscription to reflect the present value of the minimum non-discretionary outflows. In this case, as the return is at a market rate at the time the capital is subscribed, the entire capital will be classified as a liability.

Example 3 – Discretionary repayment of capital and remuneration for services provided

An LLP's constitution requires that members subscribe capital to the LLP. Members provide services to the LLP. Upon retirement, the LLP is required to pass a resolution before any capital is repaid. If no such resolution is passed, the LLP is entitled to retain the capital indefinitely. The membership agreement specifies that all profits made during a year will be divided automatically. No element of members' remuneration is clearly identifiable as a return on amounts subscribed or otherwise contributed. Accordingly, no part of the return to the members is regarded as a return on capital and their remuneration is considered separate from the capital for accounting purposes.

In this example, a positive resolution is required to repay capital, and without it the LLP is neither obliged to repay the amounts nor to pay any return on that capital. Accordingly, the capital is presented as equity. An expense is charged in profit or loss (under the heading 'Members' remuneration charged as an expense') and a liability recognised equal to the amount of profits.

Example 4 – Mandatory repayment of capital (but puttables exception applies) and discretionary division of profits

An LLP has been set up as an investment vehicle, and has ten members. Members do not provide services to the LLP. Hence the whole of the return to the members is regarded as a return on capital. The LLP's investments are managed by a third party who is not a member. Under the terms of the members' agreement, each member subscribes £1,000,000. The agreement specifies certain dates on which a member can require the LLP to repurchase their interest. On repurchase the member will receive the £1,000,000 originally subscribed, adjusted for the member's share of any losses or any profits not yet divided. Any decision to divide profits must be approved by a majority of the members. On such a division, the profits are divided equally between all ten members.

The LLP has no discretion over cash outflows in respect of the repurchase of members' interests. However, it considers the conditions under the puttables exception and because the total cash flows attributable to the instrument over its life are based on profit and loss/net assets, it concludes that they are met in relation to the members' initial capital. Accordingly:

- the capital subscribed of £10,000,000 is presented within equity; and
- any divisions of profit are reported as equity appropriations when they occur (whether during or after the end of the period).

Thus, if the LLP made profits of £500,000 before profit sharing, of which £300,000 was paid out to members as drawings during the year, the profit reported for the year would be £500,000. Members' remuneration charged as an expense would be nil and the drawings of £300,000 would be included in debtors. The unallocated balance of £500,000 would be included within equity at the year end, assuming that at that point in time, the decision to divide profits had not been made.

Example 5 – Mandatory repayment of capital (but puttables exception applies), automatic division of profits to one member for services rendered and discretionary division of the remainder

An LLP has been set up as an investment vehicle, and has ten members. Apart from the one member noted below, members do not provide services to the LLP. Under the terms of the members' agreement, each member subscribes £1,000,000. The agreement specifies certain dates on which a member can require the LLP to repurchase their interest. On repurchase the member will receive the £1,000,000 originally subscribed, adjusted for the member's share of any losses or any profits not yet divided. One of the members, Company X, is responsible for managing the LLP's investments. It has been agreed that 5% of the reported profits for each period will be paid to Company X, as compensation for providing these investment management services. The LLP does not have an unconditional right to avoid dividing 5% of the reported profits as this decision is automatic. Any decision by the LLP to divide theremaining balance of profits must be approved by the members. On such a division, thebalance of profits is divided equally between all ten members ie, including Company X. Thisdecision is not an automatic division of profits.

As noted above, the LLP has no discretion over the 5% profit share payable to Company X. In order to assess whether the capital should be presented as equity or liability, the LLPconsiders, as one of the tests, whether the profits payable to Company X representremuneration for services provided. The LLP judges that the non–discretionary amountspayable to Company X each year are purely for Company X's investment managementservices to the LLP and of an amount that is equivalent to what would have been payable toa non-member for such services. Therefore (as explained in paragraph 34 of the SORP) theremuneration should, for accounting purposes, be regarded as separate from the capitalsubscribed by Company X and disregarded in the analysis under the puttables exception.

As far as the capital of all ten members is concerned, the LLP considers the tests under the puttables exception. Because the total cash flows attributable to the capital over its life are based on profit and loss/net assets, it concludes that the tests are met in relation to the members' initial capital. Accordingly:

- the capital subscribed of £10,000,000 is presented within equity;
- an expense is charged in profit or loss (under the heading 'Members' remuneration charged as an expense') and a corresponding liability recognised equal to the amount of profits (5%) automatically payable to Company X each year; and
- any further divisions of profit are reported as equity appropriations when they occur (whether during or after the end of the period).

Thus, if the LLP made profits of £500,000 before profit sharing, of which £25,000 (5%) was divided automatically to Company X, and a further £300,000 was paid out to members as drawings during the year, the profit reported for the year would be £475,000. Members' remuneration charged as an expense would be £25,000 (ie, 5% of available profits) and the additional drawings of £300,000 would be included in debtors. The unallocated balance of £475,000 would be included within equity at the year end, assuming that at that point in time, the decision to divide profits had not been made.

Example 6 – Mandatory repayment of capital and interest, discretionary division of profits

An LLP has ten members who provide services to the LLP. Under the terms of the members' agreement, each member subscribes £100,000 as initial capital and has a 10% share of any profits that are divided. Capital is returned automatically when a member retires or otherwise leaves the LLP, except that the LLP can refuse the return of capital in certain defined circumstances which are outside its control, for example, when a retiring member is a 'bad leaver'. Interest at a market rate of 6% is automatically payable on the capital subscribed. Any decision to divide the balance of profits must be approved by a majority of the members.

The LLP has no discretion over the return of capital. It can only refuse the return of capital in certain circumstances, but these are outside its control for leavers and the LLP is unable to control the actions of members so as to 'force' bad leaver status. In addition, the tests under the puttables exception are not met because the payment of interest is a non-discretionary return on the capital. Cash outflows to members in respect of profits after interest, however, are at the discretion of the LLP. Accordingly:

- the capital subscribed of £1,000,000 is presented within liabilities; and
- interest expense of £60,000 is charged in profit or loss (within the heading 'Members' remuneration charged as an expense'), and a corresponding liability recognised; but
- any other divisions of profit are reported as an equity appropriation when they occur (whether during or after the end of the period).

Example 7 – Two distinct classes of capital

An LLP has twelve members. Two members ('non-working members') only provide capital of £200,000 each to the LLP and receive a fixed return on the capital provided. That capital isnot redeemable at the holder's option and is subordinate to all other classes of instrumentsof the LLP. Accordingly:

- given that the LLP has an unconditional right to refuse repayment of the non-working members' capital, the appropriate classification of that capital is determined by the other rights attaching to it; and
- since the capital attracts a fixed mandatory return, the LLP must recognise a liability on subscription reflecting the present value of the minimum non-discretionary outflows. In many cases, this will be the same as the relevant amount of members' capital. Interest expense is charged in the profit or loss account and a corresponding liability recognised.

The other ten members ('working members') provide both capital and services to the LLP. Under the terms of the members' agreement, each of these ten members subscribes £100,000 as initial capital and has a 10% share of profits (after payment of the fixed return to the two non-working members). Any decision to divide profits must be approved by a majority of the members, but a working member may demand the return of initial capital (for example, upon retirement). No element of the working members' remuneration is clearly identifiable as a return on amounts subscribed or otherwise contributed. Accordingly, no part of the return to the working members is regarded as a return on capital.

The LLP has no discretion over cash outflows to working members in respect of capital redemption. In addition, the tests under the puttables exception are not met because working members' capital is not in the class of instruments that is subordinate to all other classes of instruments. Accordingly:

- the working members' capital subscribed of £1,000,000 is presented within liabilities; but
- divisions of profit between the working members are reported as appropriations (not an expense) when they occur (whether during or after the end of the period).

Example 8 – Limited life LLP, discretionary repayment of capital and profits during the life of the LLP, pro rata return of net assets on liquidation

An LLP has been set up as an investment vehicle, and has ten members. Members do not provide services to the LLP. The LLP's investments are managed by a third party who is not a member. Under the terms of the members' agreement, each member subscribes £1,000,000. No member can require the LLP to repurchase their interest, but the LLP has been set up with a limited life of ten years at which point it will be liquidated. On liquidation, each member will receive a pro rata share (ie, 10%) of the LLP's net assets.

During the LLP's life, any decision to divide profits must be approved by a majority of the members. On such a division, the profits are divided equally between all ten members.

The LLP has no discretion over cash outflows on liquidation in respect of the members' interests in its net assets. However, it considers the tests under the puttables exception (paragraph 22.4(b) of FRS 102) and concludes that they are met in relation to the members' initial capital. Accordingly:

- the capital subscribed of £10,000,000 is presented within equity; and
- any divisions of profit are reported as equity appropriations when they occur (whether during or after the end of the period).

Example 9 – Limited life LLP with pro rata return of net assets on liquidation. During the life of the LLP there is mandatory payment of interest but discretionary repayment of capital and profits

An LLP has been set up as an investment vehicle, and has ten members. Members do not provide services to the LLP, and hence the whole of the return to members is regarded as a return on capital. The LLP's investments are managed by a third party who is not a member. Under the terms of the members' agreement, each member subscribes £1,000,000. No member can require the LLP to repurchase their interest, but the LLP has been set up with a limited life of ten years, at which point it will be liquidated. On liquidation, each member will receive a pro rata share (ie, 10%) of the LLP's net assets.

During the LLP's life, interest at a rate of 1% is automatically payable on the capital subscribed. Any decision to divide the balance of profits must be approved by a majority of the members. On such a division, the profits are divided equally between all ten members.

The LLP has no discretion over cash outflows in respect of interest payable on members' interests. It therefore recognises a liability reflecting the present value of the future interest payments.

The LLP then considers the remaining components of the instrument (capital plusdiscretionary profit allocation). Although the LLP has no discretion over cash outflows onliquidation, it considers the tests under the puttables exception (paragraph 22.4(b) of FRS 102) and concludes that they are met in relation to the members' capital. Accordingly:

- that component of the capital subscribed that corresponds to the interest payable is presented within liabilities (this will be the present value of the future interest payments ie, the present value of ten annual payments of £100,000), and the remaining balance of the capital subscribed is presented within equity;
- each year an expense is charged in profit or loss (under the heading 'Members' remuneration charged as an expense') and a liability recognised equal to the unwinding of the discount on the liability component; and
- any further divisions of profit are reported as equity appropriations when they occur (whether during or after the end of the period).

Example 10 – Repayment of capital permitted on retirement only if replacement capital from continuing members is contributed.

An LLP's constitution requires that members subscribe capital to the LLP. Upon retirement of a member, the LLP is required to repay capital to the retiring member to the extent that replacement capital is contributed by continuing members.

In this situation, the LLP has the unconditional right to refuse repayment of capital below the total amount of capital currently subscribed. It has, in effect, a permanent layer of capital because the level of capital will never fall below a certain amount. Accordingly, this amount of permanent capital will be shown as equity in accordance with the principle set out in paragraph 22.6 of FRS 102. To the extent that the level of replacement capital required is below the amount to be repaid on retirement, that excess will be classified as a liability (unless the tests under the puttables exception are met).

If, in another fact pattern, a resolution of the LLP is required to repay the capital to the retiring member – whether or not replacement capital is contributed – then the entire amount of existing capital contributed will be classified as equity since the LLP has discretion to repay the amount.

APPENDIX 3: FLOWCHARTS FOR ANALYSING THE APPLICATION OF THE PUTTABLES EXCEPTION
(THIS APPENDIX FORMS PART OF THE SORP)

Deleted

APPENDIX 4: MERGER ACCOUNTING ON INITIAL TRANSITION OF AN EXISTING UNDERTAKING TO A SINGLE-ENTITY LLP FORMED FOR THE PURPOSE

Introduction

1. This note explains how the SORP applies section 19 of FRS 102 in certain special circumstances that arise when merger accounting is adopted on initial transition of an existing undertaking to a single-entity LLP formed for the purpose.

2. Paragraph 115 of the SORP states that a single-entity LLP formed by the transfer or incorporation of existing undertakings should present corresponding pro-forma amounts.

3. Paragraph 116 of the SORP deals with a situation that is common in LLP incorporations, where the undertaking is transferred to the LLP part way through anaccounting period and the LLP is not itself a parent undertaking. Paragraph 116 statesthat where there is a hiatus between formation of the LLP and the transfer, the netassets at book values should be reflected in the accounts at the date of the transfer,and results should be included for the period from the transfer to the end of theaccounting period. This is the commonly adopted practice.

4. Paragraph 116 also suggests that a pro-forma profit and loss account (or statement of comprehensive income), including corresponding amounts, should be given for the whole of the original entity's accounting period spanning the transfer.

Illustrative scenario and analysis

5. The owners of entity A (a partnership) establish a new LLP with the same owners (partners) on 1 April. The business of the partnership is then transferred to the new LLP on 1 July. The LLP has a 31 December year end and prepares entity-only accounts.

   The transfer of a business to a new entity whose equity holders are the same as those of the entity transferring the business meets the definition of a group reconstruction in FRS 102.

   Therefore, assuming the conditions in paragraph 19.27 of FRS 102 are met; the merger accounting principles of reflecting the transfer at book value (as set out in paragraph 19.29 of FRS 102) may be applied to the entity-only accounts of the LLP in the above scenario. There are potentially two alternative ways of presenting its results:

   a) bring in the net asset book values at the date of the transfer of trade and assets, and only recognise profits arising in the LLP from the date of incorporation – 1 April – which will, in effect, only include transactions from 1 July to 31 December since the LLP had no trade before the date of transfer; or
   b) bring in the net asset book values at 1 January and include the results for the 12-month period 1 January to 31 December, to be consistent and comparable with entity A's reporting period.

6. Deleted

7. From a statutory viewpoint, the accounting period being reported on is for the nine months to 31 December, and therefore profits and losses relating to the period before that should not be recognised in the LLP's first statutory accounts.

8. In addition, for companies combining with a trade and assets, common practice is to adopt option (a) and only bring in profits from the date of the transfer of trade. One rationale for this is that SI 2008/410 schedule 1 paragraph 13(a) only permits profits realised at the balance sheet date to be included in profit or loss. For companies the pre-transfer profits are not profits and certainly not realised profits, of the company and therefore should not be included in the entity profit and loss account (or statement of comprehensive income).

9. On that basis, CCAB sees no reason for the accounting in LLP entity accounts to be any different. In addition, SI 2008/410 schedule 1 paragraph 13(a) also applies to LLPs under the LLP Regulations (SI 2008/1912 schedule 1 paragraph 13 (a) for small LLPs and SI 2008/1913 schedule 1 paragraph 13 (a) for large and medium-sized LLPs), even though the concept of realised and unrealised profits is not relevant for distribution purposes for LLPs.

10. In view of the above considerations, the SORP recommends that LLPs should present alternative (a) as the statutory profit or loss set out in paragraph 5 above.

11. However, as paragraph 19.30 of FRS 102 states that the results of all the combining entities should be brought into the financial statements of the combined entity from the beginning of the financial year in which the combination occurred, then alternative (b) is also a relevant presentation assuming that the 'financial year' is the accounting period of the underlying business.

12. Furthermore, on the basis that the concept of realised profits is irrelevant to LLPs for distribution purposes and that paragraphs 19.29–19.32 of FRS 102 should be complied with then the SORP also recommends disclosure of the 12-month profit or loss (ie, option (b)) and comparatives as pro-forma numbers. This approach is in line with the general requirement of section 19 of FRS 102 to present such transactions as group reconstructions using merger accounting.

13. LLPs in their first accounting period may choose to use a three column profit and loss account (or statement of comprehensive income) format, or include the statutory profit and loss account (or statement of comprehensive income) in the form of alternative (a) as set out in paragraph 5 above as a separate statement for legal reasons, but give equal prominence to the pro-forma numbers (alternative (b)).

APPENDIX 5: LEGAL OPINION

In June 2001, before the issue of FRS 25 and UITF 39, CCAB consulted Robin Potts QC on certain matters relating to the profits of a limited liability partnership, and received the following advice.

1. The profits of a limited liability partnership (LLP) are only converted into a debt due to its members when the members have agreed to divide the profits among themselves. The division of profits is a matter of the internal management of the LLP, as it is in the case of a company and a partnership (*Stevens v South Devon Railway Company [1851] 9 Hare 313* and *21 LJ Ch 816* and *Burland v Earle [1902] AC 83*).

2. The Limited Liability Partnership Regulations do not provide for an LLP (unlike a company) to include in its balance sheet the balance on its profit and loss account under the separate heading of 'Profit and loss account'. Accordingly, after the profits have been ascertained and in the absence of any agreement between the members to the contrary, the balance on profit and loss account would need to be included under the balance sheet heading 'Other reserves' pending an agreement to divide the profits among the members. The heading of 'Other reserves' is wide enough to encompass the balance on profit and loss account.

3. It is open to the members of an LLP to agree that the profits of the LLP shall be automatically divided between the members after they have been ascertained. Whether or not an agreement between the members has this effect is a matter of construction. The division of profits must be distinguished from the arrangements for profit sharing. A provision in an agreement between the members which sets out the profit shares of the members does not of itself constitute an agreement for the division of profits. It merely sets out the respective profit shares of the members which will apply to profits after the members have decided to divide them among themselves. Accordingly, the default rule which is applied by virtue of Regulation 7 (1) of the Limited Liability Partnerships Regulations 2001 (which provides for the members of an LLP to share equally in the capital and profits of an LLP in the absence of agreement to the contrary) does not constitute a default rule as to the automatic division of profits between the members.

4. If the members agree to the automatic division of profits, then albeit that there is a scintilla of time between the ascertainment of the profits and their division among the members and notwithstanding that the balance sheet is contemporaneous with the profit and loss account, it would be acceptable to credit the profits directly to the current accounts of the members without first including the profits under the balance sheet heading 'Other reserves'.

5. An LLP could only have a revaluation reserve if there was no agreement between the members for the automatic division of profit. This is because the old common law rules regarding distributions would apply to LLPs and under these rules a revaluation reserve was distributable.

6. Whether a contribution made by the members to an LLP constituted capital or debt was a matter of construction of the intention of the members. For a contribution to constitute capital it must clearly be designated as capital. Otherwise the presumption will be that it constitutes debt.

7. Where the members make a contribution of capital to an LLP, they can subsequently convert the capital into debt by agreement. What constitutes an agreement between the members and in particular what majority is required to convert capital into debt is a matter of construction of the agreement between the members.

8. On an insolvency of an LLP amounts credited to capital and reserves in its books immediately prior to the commencement of the winding up would disappear and would not constitute debt which could be proved for in the winding up.

Robin Potts, QC

27 June 2001

Note: Although the above opinion was given prior to the introduction of FRS 102 and the implementation of the 2008 LLP Regulations, the advice given nonetheless remains relevant. Although the opinion is repeated above in its entirety, only paragraphs 1 to 5 relate to accounting matters dealt with by this SORP. Paragraphs 6 to 8 deal with legal matters that are not addressed by this SORP.

In paragraphs 6 and 7, the opinion deals with the distinction between capital and debt. In FRS 102 the equivalent accounting distinction is between equity and financial liability. Although the test for distinguishing between the two is somewhat different, the references in the above opinion to the fact that it is the division of profits, automatic or otherwise, that converts profits into debt, are nevertheless consistent with the general principles of the amended SORP and specifically those in paragraph 24.

APPENDIX 6: BASIS FOR CONCLUSIONS

Introduction

BC1. This 'Basis for conclusions' summarises CCAB's considerations in reaching itsconclusions on revising the SORP *Accounting by Limited Liability Partnerships* in 2006, 2010, 2013, 2016, and 2018, and has been updated to reflect the deliberations for all five revisions.

BC2. The first edition of the SORP was published on 29 May 2002 ('SORP 2002'). Inaccordance with the FRC's *Policy on Developing SORPs*, CCAB reviews the SORP annually for changes in accounting practice and new developments.

BC3. In September 2005 CCAB published its proposals in an exposure draft of a revised SORP ('ED SORP 2005') and a revised SORP was published in March 2006 ('SORP 2006'). The subsequent changes made to SORP 2006 as a result of the amendment to FRS 25 (IAS 32) *Financial Instruments: Disclosure and Presentation* in 2008 (the puttables amendment) are also referred to in the text below where appropriate and, in particular, in BC15–19. The amended SORP was issued in March 2010 ('SORP 2010').

BC3A. Because of the significance of the changes made by SORP 2006 and SORP 2010, in particular the former, this 'Basis for conclusions' retains much of the text from the bases of conclusions in those versions of the SORP so that an explanation of the development of the SORP is retained in one document.

BC3B. Following the publication of FRS 102 in March 2013, CCAB proposed further changes to this SORP in an exposure draft ('ED SORP 2013') issued in October 2013. A revised SORP ('SORP 2014') was issued in July 2014. The changes made by this update to the SORP are discussed further in paragraphs BC39–BC48 below.

BC3C. Further changes to this SORP were proposed in an exposure draft ('ED SORP 2016') issued in July 2016. A revised SORP ('SORP 2017') was issued in January 2017.The changes made by this update to the SORP are discussed further in paragraphs BC50 – BC68 below.

BC3D. Further changes to this SORP were proposed in an exposure draft ('ED SORP 2018') issued in August 2018. A revised SORP ('SORP 2018') was issued in December 2018. The changes made by this update to the SORP are discussed further in paragraphs BC69 – BC77 below.

The distinction between debt and equity

BC4. ED SORP 2005 proposed that members' participation rights in the assets of an LLP should be analysed between those that are, from the LLP's perspective, either a financial liability or equity, in accordance with FRS 25 and UITF Abstract 39 *Members'*

Shares in Co-operative Entities and Similar Instruments.[31] The accounting implications of this requirement, as set out in the SORP, are considered in paragraphs BC5–BC11 below. The majority of respondents to ED SORP 2005 who considered this issue agreed that a revision of the SORP was required and that the proposals were consistent with the standards.

BC5. SORP 2002 distinguished between debt due to members and 'Members' interests other than debt due to them by the LLP, which constitute equity in the LLP'. 'Members' capital' is a subset of 'Members' other interests', comprising 'amounts subscribed or otherwise contributed by members for longer-term retention in the business'. The term 'Members' capital' is used in the relevant legislation. This distinction was considered no longer appropriate in the light of FRS 25 and UITF 39, but applying these standards to LLPs is not straightforward. The constitutions and capital structures of LLPs can vary significantly. Amounts subscribed or contributed by members as 'capital' of an LLP may be withdrawn or converted to debt by agreement between the members. Accordingly, whether or not an instrument is debt or equity will depend entirely on the specific terms of the members' agreement.

BC6. The basis for the accounting required in the SORP is that the members' agreement, in dealing with the financial arrangements between an LLP and its members (for example, in respect of amounts subscribed or otherwise contributed and remuneration (discussed in paragraphs BC20 et seq below)), will give rise to rights against the LLP. Such members' rights against the LLP are referred to for the purpose of this analysis as 'participation rights'. Participation rights may meet the definition in FRS 25 of a financial instrument: that is, 'a contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity'.[32] Participation rights that are financial instruments will be within the scope of FRS 25 and, by extension, UITF 39.

BC7. Under FRS 25 and UITF 39, prior to any consideration of the amendment made to FRS25 in August 2008 dealing with puttable instruments ('the puttables amendment'), members' shares would be equity only 'if the entity has an unconditional right to refuse redemption of the members' shares' (paragraph 7 of UITF 39).[33] The implication of this for LLPs is that, subject to consideration of the impact of the puttables amendment, members' interests will always be debts of the LLP unless the LLP has an unconditional right to refuse to pay the related amount. (There are also implications for the profit and loss account, including remuneration and profit shares, discussed in paragraphs BC20 et seq below.) There may be instances, therefore, where members will have no interests classified as equity in the LLP.

BC8. Following the above analysis, the SORP requires members' participation rights in the assets of an LLP to be analysed between those that are, from the LLP's perspective, either a financial liability or equity, in accordance with FRS 25 and UITF 39. For the

[31] FRS 25 and UITF 39 have since been superseded by FRS 102, but the approach taken by FRS 102 to distinguishing between debt and equity is the same.
[32] The same definition is included in FRS 102.
[33] The same requirement is reflected in paragraph 22.6 of FRS 102.

purpose of this analysis, the SORP requires participation rights in respect of amounts subscribed or otherwise contributed and remuneration (which may include salary, interest, bonus, risk premium and allocated share of profits) to be analysed separately, except where the remuneration is clearly identifiable as a return on amounts subscribed or otherwise contributed – for example, non-discretionary interest payments (see paragraph 39 of the SORP). As set out in the SORP, this means that, for example, a profit share payable at the discretion of the LLP would be accounted for as an equity appropriation even if the member's capital is treated as a liability because the LLP cannot refuse repayment of that capital (and the tests for equity treatment in the puttables amendment are not met). This reflects the reality that in many cases members' remuneration is based on participation in the activity of the business rather than providing a return on the capital invested (see paragraph BC23 below). Unless the tests for equity treatment in the puttables amendment are met, a member's participation rights will result in a liability of the LLP, except to the extent that the right to any payment or repayment is discretionary on the part of the LLP; that is the LLP has an unconditional right to refuse payment until the LLP has taken a decision to divide profits. This will depend on the construction of the members' agreement and the policy and mechanism for the LLP to divide profits.

BC9. ED SORP 2005 suggested pro-forma balance sheets for use by LLPs, based on examples in FRS 25.[34] This format was intended to allow LLPs to designate balances with members correctly as debt or equity, but also encourages presentation in a manner that provides useful information regarding the members' net interests in the LLP at the balance sheet date. Respondents to ED SORP 2005 welcomed this presentation, which was retained in SORP 2006.

BC10. The classification of capital and other members' interests in an LLP is not straightforward and will differ from one LLP to another. CCAB believes it is likely, however, that many 'traditional' LLPs will need to classify capital as a liability. This issue has been complicated further following the amendment to FRS 25 in August 2008 (see BC15–BC19 below).

BC11. Applying the principles of FRS 25 and UITF 39, a critical issue is whether the LLP retains discretion to withhold some or all of the profits to members, irrespective of whether it intends to, and invariably does, allocate all the profits to members. CCAB accepts that any amounts that the LLP has no discretion to withhold should be classified as liabilities, unless the tests for equity treatment in the puttables amendment are met. It is possible therefore, that profits may be shown as liabilities in an LLP balance sheet, where the members' agreement provides for profits to be automatically divided. This will be the case where the LLP does not have an unconditional right to refuse paying the profits to members under the terms of the LLP agreement and therefore decision to divide profits is automatic. Any rights of the members to vary the terms of the LLP agreement are not relevant: see further in BC26.

[34] The FRS 25 examples are not reproduced in FRS 102.

BC12. Although some respondents to ED SORP 2005 expressed concern at the outcomes set out in paragraphs BC10 and BC11, CCAB concluded that they followed inevitably from applying FRS 25 and UITF 39 to LLPs.

BC13. There was some concern that the distinction drawn in ED SORP 2005 between debt and equity was spurious, because members of the LLP control the LLP and can therefore control whether or not the LLP has discretion to make payments to members. According to this view, members' interests would always be equity interests. However, this ignores the fact that, unlike a partnership, an LLP is a legal entity separated from its members by a 'corporate veil'. It is therefore correct to impute discretion to the LLP, even though this can be countermanded by the members.

BC14. Some respondents to ED SORP 2005 felt that the SORP should deal with FRS 26 *Financial Instruments: Measurement*. Given that FRS 26 is not mandatory in many cases and that the standard itself contains a significant amount of implementation guidance, CCAB concluded that the SORP should not deal with this standard in any detail. However, paragraphs 4 and 5 were included to provide guidance on which accounting standard is relevant when considering how to measure the type of financial liabilities, provisions and other financial instruments dealt with in the SORP.[35] These paragraphs have, however, since been deleted following the publication of FRS 102.

BC15. One of the more difficult aspects of applying UK GAAP to LLPs is accounting for the interests of members in the profit or loss of the LLP and of the members' interests in the assets and liabilities of the entity. For the purposes of the guidance provided by the SORP, these interests are described as 'participation rights'. The analysis of members' interests in the assets and liabilities of an LLP needed to be reassessed as a result of revisions to FRS 25 effective for accounting periods commencing on or after 1 January 2010 ('the puttables amendment'). The amendment was made following a similar amendment to the equivalent International Financial Reporting Standard which arose following comments that certain types of entity may, under the previous version, have no equity shown in their balance sheet. The result of applying the amendment to LLPs was that certain members' interests which would otherwise have been classified as liabilities were subsequently classified as equity, particularly in situations where members do not provide services to the LLP. However, the criteria for reclassification are detailed and complex.[36] In practice, CCAB concluded that it would be likely that many LLPs would not be affected by the amendment.

BC16. The exposure draft of a revised SORP published on 29 July 2009 ('ED SORP 2009') contained further guidance on the application of the amended FRS 25 in the context

[35] FRS 26 has since been superseded by FRS 102. The requirements of FRS 102 are simplified compared to those of FRS 26, but are nevertheless more complex and more prescriptive than previous UK GAAP for entities that had not adopted FRS 26. The SORP has been updated where necessary to reflect the changes made by FRS 102.

[36] Very similar criteria, but with small differences, are reflected in FRS 102.

of classification of members' interests as debt or equity, together with a flowchart and examples to illustrate some, but not all, possible scenarios.

BC17. The number of responses to ED SORP 2009 was small. A theme of some of theresponses was that the guidance in the SORP was highly technical, and was for some considered difficult to interpret and use in a practical sense. CCAB had a great deal of sympathy with this view, but was ultimately constrained by the highly technical and complex underlying amendment to FRS 25 which was itself not simple to understand or apply in practice. However, the role of the SORP was to apply that standard to UK LLPs and a degree of technical analysis was inevitable. The two most substantive responses focused on the same issue: a potential inconsistency between the principles in the SORP on members' participation rights, in particular paragraph 34, and the approach to analysing the members' interests in an LLP as financial instruments.

BC18. A member of an LLP can interact with the LLP in a number of capacities, andthroughout the development of the SORP there has been a consistent principle that those different capacities (for example, service provider, investor, lender) should, where appropriate, be viewed separately and the accounting for any resulting transactions should follow the capacity in which the member acts. Respondents to ED SORP 2009 felt that some of the material on puttable financial instruments, particularly in some of the examples in Appendix 2, contradicted this principle and had sought to treat, for example, a members' agreement as a single financial instrument. CCAB debated these responses and agreed that this underlying principle should still apply ie, participation rights in respect of amounts subscribed or otherwise contributed should be analysed separately from participation rights in respect of remuneration except where the remuneration, or part thereof, is clearly identifiable as a return on amounts subscribed or otherwise contributed.

BC19. The final SORP published on 31 March 2010 ('SORP 2010') therefore made it much clearer that the interests of a member in an LLP are likely in many cases to be viewed as more than one 'instrument'. This is particularly likely in, for example, professional services LLPs where members are not simply investors or funders of the business, but also work in the business and provide services. Accordingly, SORP 2010 required the remuneration to members in respect of services provided to be viewed separately from the remuneration in respect of capital or funding provided except where the remuneration, or part thereof, is clearly identifiable as a return on amounts subscribed or otherwise contributed. This approach is in many respects simpler and avoids a number of potentially complex accounting issues such as compound instrument accounting for amounts subscribed. It would in many cases (particularly for professional services LLPs) lead to there being no change in the designation of capital from liability to equity as a result of the puttables amendment. Given that the main change from ED SORP 2009 was to align more closely the examples and flowcharts with the principles set out in the body of the ED and that the expected result of SORP 2010 would be less change in some cases than previously expected, the Steering Group concluded it was not necessary to submit the revised SORP to a further exposure period.

Profit and loss account implications

BC20. ED SORP 2005 recommended that the treatment of the members' remuneration element in the profit and loss account should be based on the same principles as are used for determining debt and equity in the balance sheet. This means that participation rights in respect of amounts subscribed or otherwise contributed should be analysed separately from participation rights in respect of remuneration except where the remuneration is clearly identifiable as a return on amounts subscribed or otherwise contributed. Members' remuneration is 'any outflow of benefits to a member', and may include or comprise, inter alia, salary, interest, bonus, risk premium and allocated share of profits. This principle, set out in ED SORP 2005, would mean that remuneration comprising a profit share payable at the discretion of the LLP should be accounted for as an equity appropriation even if the member's capital is treated as a liability. Respondents to ED SORP 2005 broadly agreed with this approach as a practical solution to a difficult problem, in line with the analysis set out below.

BC21. Some respondents to ED SORP 2005 felt there should be a closer link between the balance sheet classification of the capital instrument (debt or equity) and the way in which members' remuneration is dealt with in the profit and loss account. This is akin in the corporate situation to the linkage of a debt instrument with interest in the profit and loss account and an equity instrument with dividend payments. In addition, some respondents to ED SORP 2005 felt that members' participation rights had certain features of compound instruments.

BC22. However, it is extremely difficult to apply to an LLP the provisions in FRS 25 on compound financial instruments (paragraphs 28–32 of FRS 25) and 'interest, dividends, losses and gains' (paragraphs 35–36 of FRS 25). The relationship between capital introduced and remuneration in an LLP is very different to that in a company, where there would normally be a clearly identifiable relationship between return on the investment and the investment itself. At one extreme, for example, there may be LLPs that have no members' capital, being entirely funded from external sources, in which case the profit and loss account treatment of remuneration must be assessed in isolation from any balance sheet amount.

BC23. In this respect, paragraph 36 of FRS 25 states that the classification of a financial instrument as a financial liability or an equity instrument determines whether interest, dividends, losses and gains relating to that instrument are recognised as income or expense in profit or loss.[37] However, while it may be possible to consider that the remuneration and profit shares of members amount to 'interest, dividends, losses and gains' as a result of the amounts invested by members in an LLP, in many or most cases this does not reflect the substance of the arrangements in LLPs. Remuneration and profit shares are often payable to members in return for participation in the business, as well as representing a financial return on amounts invested by members. In many

[37] Although an equivalent paragraph is not reflected in FRS 102, the same logic is equally valid under FRS 102.

LLPs, the latter will represent a relatively insignificant proportion of the total remuneration.

BC24. Because, in many cases members' remuneration constitutes a share of profits based on participation in the activity of the business, and given the difficulty of identifying the specific capital to which participation rights might attach, CCAB considers that to treat all shares of profit in an LLP as some form of return on a financial instrument, even where the share of profit is a financial liability of the LLP once divided, would result in misleading and inappropriate accounting presentation. Accordingly, CCAB decided to retain the principle that participation rights in respect of amounts subscribed or otherwise contributed should be analysed separately from participation rights in respect of remuneration, except where an element of the remuneration is clearly identifiable as a return of capital (see paragraph 39 of the SORP). As a result of comments received on ED SORP 2009, this principle has continued to be applied subsequently to the puttables amendment to FRS 25.

BC25. With regard to compound instrument accounting, while members' participation rights might include both equity and liability elements, and thus be thought of as 'compound instruments' under FRS 25, it will often be impossible to ascribe these rights to identifiable elements of members' capital, which itself will vary over time.

BC26. A minority of respondents to ED SORP 2005 expressed concern at the line taken in the exposure draft with regard to automatic division of profits. The view was expressed that automatic division is, in effect, dependent on the agreement of the members, and so it is not correct to charge it as an expense. However, CCAB continues to believe that an agreement for automatic division of profits does have the substance of establishing profits of the LLP as debts due to the members as they accrue. Although the members could agree among themselves to terminate the agreement, the accounting must be on the basis of the agreement that is in fact in force at the time which would be binding on the parties unless and until terminated or varied.

BC27. The position whereby an LLP had no agreement for the automatic division of profits, but had divided some of the profits during the accounting year was considered. Some views had been expressed that since at the time the accounts were drawn up the LLP had already divided the profit, it was therefore no longer discretionary and should be accounted for in the same way as an automatic division of profit; that is, shown as members' remuneration charged as an expense rather than as an equity appropriate of profit. CCAB is of the view that this is not the correct position. The position is no different in principle from that of a limited company declaring an interim dividend on ordinary shares. The LLP has an unconditional right to avoid dividing the profits and therefore any decision to divide the profits is an equity appropriation. Accordingly, CCAB considers that the discretionary division of profit during the year that is not clearly identifiable as a return on capital should be accounted for as an appropriation of profit in the year in which it occurs in line with the treatment of an interim dividend paid by the company on its ordinary shares.

BC28. Appendix 1 to the SORP sets out example balance sheets and profit and loss accounts for an LLP. Appendix 2 provides illustrations of how the principles set out in the SORP would be applied to some simple LLP membership arrangements.

BC29. Some respondents to ED SORP 2005 suggested that FRS 20 *Share-based Payment* is applicable to members' remuneration because any share of profits a member receives is at least in part consideration for services rendered to the LLP.[38] While the SORP cannot cover all remuneration arrangements, and it may be that in some circumstances FRS 20 is relevant, CCAB concluded that typically members' remuneration arrangements would be outside the scope of FRS 20. The standard defines a share-based payment as 'a transaction in which the entity receives goods or services as consideration for equity instruments of the entity (including shares or share options), or acquires goods or services by incurring liabilities to the supplier of those goods or services for amounts that are based on the price of an entity's shares or other equity instruments of the entity'.[39] CCAB believes that what the member receives in exchange for any services given ie, typically a share of one year's profits, does not meet the definition of an equity instrument, which is 'a contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities'.[40] In this respect, an equity instrument is representative of the total value of the entity (for example, the price of an equity share in a corporate entity is representative of both the value of the existing assets and also of future cash flows). Accordingly, CCAB believes that a share of one year's profits does not meet the definition of an equity instrument because it reflects only one year's earnings rather than a share in the overall value of the entity.

Post-retirement payments to members ('Annuities')

BC30. SORP 2002 required the present value of the best estimate of the expected liability for or in respect of payments to a former member to be provided in the accounts at the date of the member's retirement, in accordance with FRS 12 *Provisions, Contingent Liabilities and Contingent Assets*. (Such post-retirement payments are often described as 'annuities'.)

BC31. The introduction of FRS 25 led to developments in the thinking behind the treatment of annuities by LLPs. The previous treatment, of recognising a liability only on the retirement of the member, was consistent with the principle of not reflecting transactions with members in the profit and loss account (except in the limited instance of salaried remuneration). However, FRS 25 brought members' remuneration within the scope of the profit and loss account, and it would be inconsistent to treat annuities differently. Furthermore, an annuity to which a member has a contractual entitlement is a contractual obligation to deliver cash or another financial asset to

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[38] FRS 20 has since been superseded by FRS 102. The current requirements in respect of share-based payment are set out in section 26 of FRS 102.

[39] The definition included in FRS 102 is different in certain respects but does not alter the rationale here.

[40] Similarly, FRS 102 defines equity as 'the residual interest in the assets of the entity after deducting all its liabilities'.

another entity, and so meets the definition of a financial liability under FRS 25, although if it contains a life-contingent element it is scoped out of FRS 25 and would fall to be accounted for under FRS 12, as would annuities in respect of which the LLP only has a constructive obligation.[41] Whichever is the relevant standard, the obligation in respect of the annuity should be accounted for at the time the member becomes entitled to a future payment that the LLP has no discretion to withhold (in line with the distinction between discretionary and non-discretionary participation rights, discussed in paragraphs BC7 et seq above). As regards an unconditional annuity right, the granting thereof is the obligating event and it will normally be correct to recognise a liability at the time of such grant. As regards a conditional annuity obligation (for example, conditional on continuing future service), this should be accrued as the rights to that annuity accrue (whereas SORP 2002 required the liability to be crystallised at the time of the member's retirement).

BC32. The appropriate accounting guidance for an annuity will depend on the characteristics of the annuity. The detailed guidance in FRS 102 differs from that in previous UK GAAP, and some LLPs will find that the appropriate accounting for an annuity changes as a consequence. As noted in the above paragraph, there may be cases in which the LLP considers that the right to an annuity meets the definition of a financial instrument and falls within the scope of sections 11 or 12 of FRS 102. A life-contingent annuity is likely to be an insurance contract and outside the scope of FRS 102 (such an annuity will instead fall within the scope of FRS 103). Annuities that have not yet vested will fall within the scope of section 21 of FRS 102. In this respect, the SORP deals in paragraphs 76 to 84A with the relationship and boundaries between sections 11, 12 and 21 of FRS 102 and FRS 103.

BC33. FRS 17 *Retirement Benefits* explicitly defines retirement benefits as 'consideration given by an employer in exchange for services rendered by employees …'.[42] It is thus designed to deal with employer-employee relationships and how the costs of a pension liability for a defined benefit scheme should be reflected in an entity's accounts. However, the relationship between an LLP and a member is not generally an employer-employee relationship, and it therefore requires a distinct accounting treatment. Furthermore, the amount of post-retirement annuity payable is not likely to be based on a proportion of final 'salary' that is 'earned' over time, but, in the case of profit-dependent annuities at least, is normally measured in relation to events and profits arising after the retirement date. For these reasons, CCAB believes that these types of arrangement of post-retirement payments paid by LLPs to former members fall outside the scope of FRS 17.[43]

BC34. However, measurement of the liability raises a number of issues. Although CCAB is of the view that FRS 17 is not the governing standard, where, because of their nature

[41] Different sections of FRS 102 apply to different types of annuity, but the rationale here in respect of timing of recognition is unaltered.

[42] FRS 17 has since been superseded by FRS 102. The corresponding requirements are set out in section 28 of FRS 102.

[43] Section 28 of FRS 102 instead deals with 'employee benefits' and FRS 102 defines a retirement benefit plan in relation to employees, but the rationale here is unaffected.

and/or complexity, the arrangements are such that it is appropriate to apply the guidance in FRS 17, then that guidance should be applied in arriving at the measurement of the liability. In order to arrive at the best estimate of the expected liability (ie, just for measurement purposes), CCAB believes that it will often be necessary to adopt actuarial principles and techniques.

BC35. However, where a member of an LLP is also an employee and receives retirement benefits under their employment contract, then FRS 17 will be applied in full, as reflected in the SORP.[44]

Merger accounting on initial transition of an existing undertaking

BC36. Appendix 4 to the SORP explains the reasoning behind the treatment the SORP adopts for applying FRS 6 *Acquisitions and Mergers* in certain special circumstances that arise when merger accounting is adopted on initial transition of an existing undertaking to a single-entity LLP formed for the purpose.[45] Commentators on ED SORP 2005 generally welcomed this approach.

Revenue recognition

BC37. Paragraph 65A of ED SORP 2005, which stated that revenue on service contracts should be recognised in accordance with UITF Abstract 40 *Revenue recognition and service contracts*, was deleted on the grounds that it was not specific to LLPs.

Losses

BC38. Certain commentators on ED SORP 2005 requested guidance on the accounting treatment of losses. This was felt to be impracticable, as the treatment will vary depending on the precise provisions of the members' agreement.

Changes made by SORP 2014

BC39. The publication of FRS 100 *Application of Financial Reporting Requirements*, FRS 101 *Reduced Disclosure Framework* and FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* ushers in a new reporting regime for UK entities.

BC40. All extant FRSs, SSAPs and UITF abstracts are withdrawn when FRS 102 becomeseffective, although the FRSSE currently continues to be available for small entities, though there are some consequential amendments to this standard.

[44] By the same logic, section 28 of FRS 102 should be applied where a member receives retirement benefits under an employment contract.

[45] FRS 6 has since been superseded by FRS 102. The corresponding requirements are set out in section 19 of FRS 102.

BC41. The FRC believes that there continues to be space for supplementary guidance, where relevant, in the form of SORPs. Therefore, this SORP – and many of the other existing SORPs – has been updated to bring it into line with the requirements of FRS 102.

BC42. Many of the changes that have been made are straightforward and will not affect existing practice. For example, references to extant SSAPs, FRSs and UITF abstracts have been replaced with references to the relevant sections or paragraphs of FRS 102. Similarly, the terminology used throughout has been updated to reflect the language used by FRS 102.

BC43. There are, however, some more substantive changes that have been made to this SORP following the publication of FRS 102. These include:

- updating the guidance on business combinations and group accounts (paragraphs 102–119) to reflect the fact that FRS 102 only allows merger accounting to be used for group reconstructions and some public benefit entity combinations;
- updating the guidance on contractual or constructive obligations (paragraph 76) and annuities (paragraph 80) to reflect the fact that FRS 102's requirements relating to financial liabilities differ from current UK GAAP requirements; and
- updating references throughout to reflect the introduction of the option to produce a single statement of comprehensive income, including adding an additional exhibit in Appendix 1.

BC44. The section of the SORP on retirement benefits – which includes the revised requirements on contractual or constructive obligations and annuities referred to above – applies the requirements of FRS 102. While it is not a simple solution, it is in accordance with the standard. While a simpler, more pragmatic solution was considered, it was rejected as our role as a SORP-making body is not to override the requirements of the standard but to apply them to the LLP sector.

BC45. In practice, obligations to make post-retirement payments to members will often reflect significant mortality risk and LLPs are therefore likely to have historically accounted for these obligations as provisions within the scope of FRS 12. On adoption of FRS 102, these obligations will be considered to be 'insurance contracts' and will therefore fall within the scope of FRS 103 *Insurance Contracts*. FRS 103 allows entities, generally, to continue their existing accounting policies. Therefore, in many cases LLPs will be able to continue with their existing approach to accounting for retirement benefits.

BC46. Further changes have been made to clarify SORP 2010's existing requirements where there were known issues or misunderstandings, including:

- clarifying the requirements in relation to automatic division of profits to make it clear that payment is unavoidable where profits are automatically divided among members in accordance with the LLP agreement in force at the time, and that in such instances a liability should be recognised;

- clarifying that if a reconciliation of members' interests is to be shown as a primary statement in place of the statement of changes in equity then comparatives must be shown for all figures presented;
- improving the table that follows paragraph 60 to ensure the recommended format not only provides a reconciliation of members' interests but also meets related Companies Act requirements;
- providing more guidance on cash flow statement presentation to reduce divergent practices; and
- refining the examples in Appendix 2 to focus on more commonly encountered scenarios and to eliminate some duplication.

Although the wording has been clarified, no changes to existing requirements are intended.

BC47. In addition, changes have been made to reflect the fact that SORP 2010 included a significant amount of guidance on the debt vs. equity debate that resulted from the fundamental changes introduced by FRS 25 and the subsequent 'puttables amendment' to that standard. While the basic accounting will be unchanged under the new regime, it was nonetheless felt appropriate to amend some of the wording – and delete the flowcharts in Appendix 3 – to reflect the fact that the transition is behind us and what once was new and unfamiliar accounting practice is now the accepted norm.

BC48. Previous versions of the SORP required LLPs to produce a separate Members' Report. However, this is not a requirement of the LLP Regulations and some respondents commented that mandating such a report was therefore 'gold plating' the legal requirements. While the October 2012 exposure draft did not specifically consult on this point, as it does not relate to the introduction of FRS 102, the SORP has nonetheless been updated in response to the feedback received and this requirement has been removed. However, the disclosures that previously had to be included in the Members' Report have been retained as they are considered helpful. LLPs may still wish to produce a Members' Report, but the SORP now allows them to include these disclosures elsewhere in the financial statements if they prefer.

BC49. Some respondents also pointed out that paragraphs 63 and 64 of the SORP, which require disclosure of how loans and debt due to members would rank in relation to other creditors in the event of a winding up and any restrictions on the ability of the members to reduce the 'members other interests', were onerous and overly burdensome in comparison to financial reporting by other types of entities. While these requirements have been retained for now, they will be specifically consulted on when the SORP is next updated.

Changes made by SORP 2017

BC50. Amendments were made to UK accounting standards in July 2015 that resulted in:

- the withdrawal of the FRSSE;
- amendments being made to FRS 102 to add a new section outlining presentation and disclosure requirements for small entities and making other changes necessary for continued compliance with company law; and
- the publication of FRS 105, a new standard available to entities choosing to apply the micro-entities regime.

BC51. The LLP Regulations were amended in May 2016 by The Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) Regulations 2016 (SI 2016/575), which introduce similar changes to the financial reporting framework for LLPs as have been recently introduced for companies, including raising the size thresholds which determine when an LLP or group qualifies as small and the creation of a new micro-entities regime for LLPs.

BC52. Consequential amendments to FRS 105 were issued in May 2016 to align the standard with recent changes to UK company law and make the micro-entities regime available to LLPs and qualifying partnerships.

BC53. This SORP incorporates a number of amendments arising as a consequence of these changes. Other minor changes have also been made, one of which is to reflect the findings in *Reinhard vs. Ondra* – which clarified that an individual cannot be both a member and an employee of an LLP – in the definition of members' remuneration charged as an expense.

BC54. Section 1A *Small Entities* of FRS 102 sets out the information that must be presented and disclosed in the financial statements of small entities that qualify for and choose to apply the small entities regime. There are no recognition and measurement simplifications for small entities. Small LLPs will therefore have to comply with the recognition and measurement requirements of FRS 102 and this SORP.

BC55. Section 1A goes on to explain that a small entity may need to provide additional disclosures to those set out in this section of the standard in order to ensure that their financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the entity for the reporting period.

BC56. Rather than prescribing which disclosures are required to ensure that the financial statements give a true and fair view, CCAB concluded that such LLPs – like other small entities – should be allowed to apply their own judgement when determining what, if any, additional disclosures are needed over and above those required by the standard. Depending on the individual facts and circumstances, some or all of the disclosures included in this SORP may be needed in order to ensure that the accounts give a true and fair view.

BC57. The Small LLP (Accounts) regulations as amended by SI 2016/575 no longer require additional disclosure of movements in 'Loans and other debts due to members'. As a consequence, CCAB concluded that there was no need to require all small LLPs to include such a reconciliation in their financial statements. However, it should be noted that Section 1A of FRS 102 encourages small entities to present a statement of changes in equity. This SORP therefore encourages small LLPs to include the reconciliation of the movement in members' other interests detailed in paragraphs 59 of the SORP.

BC58. As noted in paragraph BC49 above, when we last consulted on changes to the SORP, some respondents said that they felt the disclosures about how loans and other debts due to members rank in relation to other unsecured creditors required by paragraph 63 and 64 of the SORP were onerous and overly burdensome in comparison to financial reporting by other types of entities. However, as LLPs do not have any of the capital maintenance provisions that apply to companies, CCAB's view is that such disclosures are necessary in order to ensure a true and fair view regardless of the size of the LLP. These are the only disclosures that small LLPs are required to make by the SORP over and above those required by Section 1A of FRS 102.

BC59. There was some variation in views among respondents to the exposure draft that preceded this edition of the SORP about which additional disclosures should be required to ensure a true and fair view and which should be encouraged. For example, one respondent suggested that disclosures about the ranking of loans and other debts should be encouraged rather than required while another suggested that a reconciliation of members' interests should be required rather than encouraged. However, most respondents were supportive of approach proposed. Consequently no changes have been made to the proposals made in the draft SORP.

BC 60. One respondent suggested that further clarity was needed about the extent to which small LLPs should comply with paragraph 69's requirements in relation to the policy for members' drawings. While this disclosure will sometimes be needed to ensure a true and fair view, we do not believe that it is necessary for the SORP to either require or encourage it.

BC61. FRS 105 is available to entities choosing to apply the micro-entities regime. The new standard allows qualifying entities – including the smallest LLPs – to follow a far simpler reporting regime.

BC62. FRS 105 is based on FRS 102, but it has been adapted significantly to accommodate the legal requirements of the micro-entities regime. For example, the standard reflects the new regime's prohibition of fair values and its very limited disclosure requirements. In addition, further simplifications – over and above those required by law – have been made in order to reflect the smaller size and simpler nature of micro- entities. For example, there are no accounting policy options and accounting for deferred tax is not permitted. Moreover, micro-entity accounts that include the statutory minimum accounting items are presumed by law to give a true and fair view.

BC63. When deciding whether or not LLPs applying FRS 105 should be included within the scope of this SORP, CCAB were guided by The Accounting Council's Advice to the FRC to issue FRS 105 which was published alongside the standard. Paragraph 31 of which states:

A micro-entity that enters into a transaction that is not specifically covered by FRS 105 is required to refer to the concepts and pervasive principles set out in Section 2Concepts and Pervasive Principles in determining its accounting policies. TheAccounting Council notes that micro-entities are not required to refer to otheraccounting standards or authoritative guidance because these requirements may beinconsistent with the legal requirements of the micro-entities regime.

BC64. The significant differences between FRS 105 and FRS 102 – the standard upon which this SORP is based – lead CCAB to conclude that LLPs applying the former standard should be scoped out of this SORP. Instead, such LLPs should simply follow the relevant requirements of FRS 105.

BC65. Two respondents raised concerns about the lack of guidance for micro-LLPs applying FRS 105. CCAB concluded it is not, however, appropriate to include any specific guidance for micro-LLPs in this SORP as it is based on the recognition and measurement requirements of FRS 102 rather than FRS 105. Moreover, following the SORP's requirements will not necessarily result in a solution that is in compliance with the requirements of FRS 105. Micro-LLPs applying FRS 105 can, nonetheless, refer to the SORP's requirements if they wish but they must satisfy themselves that in doing so they are also complying with the relevant requirements of FRS 105.

BC66. CCAB are aware that there are some inconsistencies in how 'automatic divisions' of profits are accounted for in practice. Some minor clarifications have therefore been made to paragraph 48 and paragraph 3A of appendix 2. Although the wording has been clarified, no changes to existing requirements are intended.

BC67. CCAB are aware that there has been some confusion around whether or not astatement of changes in equity needs to be prepared if an LLP has no equity. The SORP has therefore been updated to explicitly state that where the LLP has no equity, and the reconciliation of members' interests is not presented as a primary statement, a statement should be made either on the face of one of the other primary statements or in the notes to the accounts that the LLP has no equity and consequently a statement of changes in equity is not given.

BC68. As part of this review of the SORP, consideration was also given to amendments madeto FRS 102 in July 2014, February 2015 and March 2016. It was concluded that no changes were needed as a consequence of these amendments as they do not create any issues that are specific to LLPs.

Changes made by SORP 2018

BC69. In December 2017, amendments were made to FRS 102 as a result of the 2017 Triennial review. As part of the 2018 annual review of the SORP, consideration has been given to whether the amendments to FRS 102 create any issues specific to LLPs, and whether any other consequential amendments are needed to align the SORP to the revised standard. This SORP incorporates a number of amendments arising as a consequence of the changes to FRS 102. Details of these amendments are set out in paragraphs BC71 – 76.

BC 71. The guidance on accounting by small LLPs (paragraph 27) has been updated to refer to the fact that paragraph 11.13A of FRS 102 provides the option for small LLPs to adopt simpler recognition and measurement requirements for certain financial transactions ie, basic loans from a person within a director's group of close family members when that group contains at least one member of the LLP who is a person. The guidance on the accounting for members' capital classified as a financial liability (paragraph 57A) has also been updated to refer to this simplification for small LLPs. The meaning of director has not been defined in FRS 102 for an LLP. Therefore, CCAB concluded that further guidance should be given to clarify that for the purpose of applying the exemption in paragraph 11.13A of FRS 102, the term 'director' should be taken to mean a member, who is a person, with an equivalent role in the LLP. CCAB also notes that further guidance on the application of the relief is given in paragraphs B11.32 to B11.39 of the Basis for Conclusions accompanying FRS 102.

BC 72. FRS 102 has been updated to require that an entity presents the tax income (or expense) effects of distributions to owners in profit or loss. CCAB considered whether or not it should update paragraph 36A but concluded that, on reflection, this matter did not create any specific issue for LLPs, and that paragraph 36A should instead be deleted.

BC 73. The guidance on cash flow statement presentation (paragraphs 74A - 74C) has been updated to reflect the new requirement for an entity to disclose the changes in net debt between the beginning and end of the financial period. CCAB concluded that guidance on this requirement was needed to address the fact that although 'loans and other debts due to members' would be considered borrowings for the purposes of the definition of net debt they are not external financing. It was concluded that it would be helpful for the SORP to include an example of how this information could be presented by an LLP.

BC 74. CCAB considered whether paragraph 130A should be updated to reflect the fact that FRS 102 has been updated to include an exemption from disclosing key management personnel compensation when an entity is subject to a legal or regulatory requirement to disclose directors' remuneration (or equivalent) and the key management personnel and directors are the same. CCAB concluded that it did not expect this exemption to have the effect of reducing the amount of information disclosed by LLPs and that the SORP, therefore, did not need to be updated for this amendment.

BC 75. A new paragraph 108A has been added to the Business Combinations and Group Accounts section to reflect the new recognition rules for intangible assets acquired as part of a business combination. As a result of the Triennial review 2017 amendments, intangible assets must be recognised separately from goodwill if they are separable and arise from contractual or other legal rights, subject to the general recognition requirements for all intangibles being met. However, those entities wishing to recognise more intangibles separately from goodwill may still do so by way of accounting policy choice. To qualify for separate recognition, an intangible asset must still meet the general recognition criteria for all intangibles but need only be separable or arise from contractual or legal rights. CCAB noted that this amendment might be particularly relevant for certain business combinations involving LLPs, for example, when two LLPs come together but where no cash is paid and no additional amounts of purchase consideration are identified. In this situation, if substantial intangibleassets are recognised on acquisition it can give rise to negative goodwill. CCABconcluded that further guidance on the new accounting policy choice would be helpfulas taking up this policy choice could potentially increase the amount of negativegoodwill recognised in such situations.

BC 76. The definition of a group reconstruction in FRS 102 has been extended to include the transfer of the business of one group entity to another; and the transfer of the business of one group entity to a new entity that is not a group entity but whose equity holders are the same as those of the parent. Although the extended definition does not alter the accounting treatment set out in Appendix 4 (paragraph 5) of the SORP, the appendix has been updated to reflect the amended definition.

BC 77. Two respondents raised concerns about inconsistencies in how 'automatic divisions' of profit are accounted for in practice. While no clarifications to the SORP have been made for now, CCAB concluded that this matter will be specifically considered as part of the 2019 annual review with any proposed amendments consulted on when the SORP is next updated.

About CCAB

The combined membership of the five CCAB bodies – ICAEW, ACCA, CIPFA, ICAS and Chartered Accountants Ireland – amounts to 275,000 professional accountants in the UK and the Republic of Ireland (over 415,000 worldwide).

CCAB provides a forum for the bodies to work together collectively in the public interest on matters affecting the profession and the wider economy.

CCAB's credibility stems from its insight into all areas of finance and accounting, from finance director and audit partner to management accountants, professional advisers, public sector finance leaders and entrepreneurs. CCAB's members work through the financial value chain in all sectors as key decision makers and business leaders within the UK and around the world.