

## A STUDY OF DEVELOPMENT OF LIMITED LIABILITY PARTNERSHIP IN INDIA

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### INTRODUCTION

One of the oldest forms of business relationships is Partnership. It can be evidenced that in terms of the complex business, partnerships have been replaced by the limited liability companies, but still it is preferred form of business for small trading and business enterprises, especially the professionals in India as well as abroad. But gradually, the general form of partnership has lost its demand because of inherent disadvantages in it; the primary is unlimited liability of partners. Each partner has risk of exposure to personal assets in case any liability arises. For a long time, a need has been felt to provide for a business format that would combine the flexibility of a partnership and the advantages of limited liability of a company at a low compliance cost. The beginning of the twenty first century have witnessed an amount of activity around the law relating to business forms operating within the world not seen since the private company and limited partnership were introduced in 1907. Since then there has been reviews of partnership law carried on by law commissions in various countries with a view to reform and modernization. Given the emphasis on law reform and modernization for small businesses it may not seem surprising that the first new form available for such businesses to be introduces as the Limited Liability Partnership or LLP. The importance of the subject of Limited Liability Partnerships has been growing day by day with the increasing trend of LLP registrations and the conversion of traditional unlimited partnerships to LLP status in the world panorama. One can experience an increasing level of serious interest in conversion to LLP status in recent years in the whole world. The move towards conversion to LLP is building momentum day by day. There are now over 13,000 LLPs in the UK. Many are special purpose vehicles but an increasing number are professional firms. The main drivers are risk management and succession. For most professional firms the question now is not whether they will convert to LLP, but when. The latest surveys suggest that the majority of the Top 50% accounting firms and about 60% of the Top law firms will be LLPs by the end of 20015. However, we are also seeing

an increase in conversions and an interest in the concept from smaller professional firms who were previously operating a wait and see approach.

The professional and entrepreneurs are attracted by lower compliance cost, better control and management, greater flexibility in operations and limited liability of member of the LLP. With effect from 1st April, 2008 any two or more persons wishing to carry on business together have an additional choice of vehicle for that purpose. This is the limited liability partnership and those persons are referred to as the members of the LLP.

The origin of this relatively new institution is generally attributed to the German law of 1892. This business form has its origin in the 1892 German company law known as Gesellschaft mit beschränkter Haftung (GmbH). Once established in Germany, the concept of the Limited Liability Company had a very active and fast growth. A corporate business vehicle that enables professional expertise and entrepreneurial initiative to combine and operate in flexible, innovative and efficient manner, providing benefits of limited liability while allowing its members the flexibility for organizing their internal structure as a partnership. Its primary advantage is the benefit of limited liability, a feature not prevalent in general partnerships. The partners in an LLP are liable only to the extent of their individual contributions; they would not be held responsible for loss caused on account of other partners, of which they had no knowledge.

### OBJECTIVES OF TH STUDY

- 1) To study the present Status of LLP in India.
- 2) To study the origin and development of LLP.
- 3) To study the need of LLP in India.
- 4) To give meaningful conclusions and suggestions on th basis study.

### RESEARCH METHODOLOGY

Secondary data collected from the Books, Internet, magazines, Journals and different types of research papers etc.

### SCOPE AND LIMITATIONS:

The researcher has made the best possible effort to point out the various loopholes present in current legal position related to the Limited Liability Partnerships in India, particularly in relation to the taxation and convertibility. The study has been made in the light of the current legal position in various countries like U.S.A., Germany, Australia and U.K. etc. The researcher also thinks there is ample scope for further research in this issue.

## LIMITED LIABILITY PARTNERSHIP IN INDIA-

The aspirations of the people and the situation keep on changing time to time and the States, particularly with a democratic setup, tend to keep pace with that. These aspirations can be as much commercial or economic, as they can be political. In order to secure better for the commercial aspirations, the States have, from time to time, provided regulatory legitimacy to several forms of business organization. The spectrum of State responsiveness varies from a mere "recognition" of newer manners of conducting business activities to "creation" of newer business forms. 7 India has witnessed considerable growth in the recent years and the quality of our entrepreneurs, and technical and professional man power has been acknowledged globally. This is also widely accepted that the service sector in the Indian economy has grown in its role to a great extent. It has thus become necessary to combine the entrepreneurship knowledge and risk capital to provide a further boost to the economic growth. For particularly this purpose the introduction of a new corporate entity was felt needed, which could combine the characteristics of both the corporate and noncorporate entities. As a result of which the Limited Liability Partnership (LLP) came into existence with the enactment of Limited Liability Partnership Act in the year 2008. The professionals and entrepreneurs will now be able to organize and provide a wide range of services to the corporate sector in an efficient manner.

The law, as the name suggests, is to provide the advantage of limited liability by creating a corporate form of partnership. According to section 2(n) of the Limited Liability Partnership Act, 2008, Limited Liability Partnership means a partnership formed and registered under the Act. Again section 3(1) of the Act says that a limited liability partnership is a body corporate formed and incorporated under this act and is a legal entity separate from its partners.

In an LLP form of business there is an advantage of limited liability of a company along the flexibility of organizing the internal management on the basis of a mutual agreement like any partnership firm. It is a model which amalgamates in it the features of both of a corporate structure' as well as 'a partnership firm structure' providing an efficient combination of professional expertise and entrepreneurial initiative in an innovative manner. LLP is be a Body Corporate formed and registered under the LLP Act 2008 that gives the flexibility of a partnership firm. It is to be organized and operated on the basis of an agreement known as "LLP Agreement" and shall have the following characteristics:

- Perpetual succession.
- Capacity and power of suing and being sued.
- Capacity to buy and sell property in its own name.
- Common seal.

**ORIGIN AND DEVELOPMENT:**

- 1957: The 7th Law Commission on Partnership Act, 1932 rejected the suggestion to introduce LLP legislation made by the iron, steel and hardware merchants' chamber, because they did not want to fail the purpose of recent Companies Act amendment.
- 1997- The Abid Hussain Committee on Small Scale Industries recommended legislation on LLP in India.
- 2003- The Naresh Chandra Committee set up on regulation of private companies and Partnerships suggested application of Limited Liability Partnerships to service industry.
- 2005- The recommendation for introducing a LLP law was again made by the JJ Irani Expert Committee on Company Law (2005). It suggested to have a separate LLP Act and to include the small enterprises with the scope of LLPs. They were of the view that in this way flexibility could be provided to the small enterprises to enter into the joint venture agreements and to access technology.
- 23rd July 2005- The 2<sup>nd</sup> Naresh Chandra Committee submitted its report and made the following observations: "In increasing litigious market environment, prospect of being a member of a partnership firm with unlimited liability is, to say the least, risky and unattractive. Indeed, the chief reason why the firms of professionals, such as accountants, have not grown in size to successfully meet the challenge of the international competition. This makes an L.L.P a most attractive vehicle for partnership among professionals such as lawyers and accountants."8
- 2006- On December 7th, LLP bill was approved by Union Cabinet. On December 15th, LLP bill was introduced in Rajya Sabha.
- 2007- The LLP bill of 2006 was referred to Parliamentary Standing Committee (PSC). On November 27th, PSC submitted its report to the Parliament with recommends for some changes to the 2006 LLP bill.
- 2008- On May 1st, the introduction of new bill (2008 LLP bill) was approved by the Union Cabinet replacing the 2006 LLP bill. On October 21st, the LLP bill was introduced in the Parliament. On October 24th, the LLP bill was passed by the Rajya Sabha. On December 13th, LLP bill was passed by Lok Sabha.
- 2009- On January 7th, President gave his assent to the LLP bill 2008. On January 9 th, LLP Act 2008 was published in the Official Gazette. The rules in respect of operational aspects under the LLP Act, 2008 (the LLP Rules 2009), were brought on 1st April, 2009. The rules in respect of conversion of a partnership firm, a private company and an unlisted public company into LLPs were made effective w.e.f. 31st May, 2009. The Government has also launched a website namely, [www.llp.gov.in](http://www.llp.gov.in) on 1st April, 2009 for operationalization of various processes provided under the LLP Rules, 2009.

## NEED FOR THE LIMITED LIABILITY PARTNERSHIP IN INDIA –

It may be possible that in the coming years various useful services like legal, accountancy and other technical/professional services will be provided by the Indian professionals to a large number of entities across the world. In order to provide variety of solutions to the international clients, the multidisciplinary combinations will be required. But in an increasingly litigious environment, it is really a very risky job to be a member of a partnership firm with unlimited personal liability and hence unattractive. Indeed, this is the prime reason that the partnership firms of professionals, such as accountants, lawyers etc. have not grown in size to successfully meet the challenges posed today by international competition. So, it is felt needed that there should be a new corporate entity as an alternative to the traditional partnership with limited liability and flexible business environment to organize and operate in flexible and efficient manner. It will be possible for the entrepreneurs, professionals and service providers to combine and operate in an efficient manner to give competition in the international market.

Many professionals in India, such as advocates/lawyers, chartered accountants and doctors are precluded from practicing through companies. The LLP structure would be particularly advantageous for providing such professional services.<sup>10</sup> Hence it would be a suitable vehicle for partnership among professionals who are already regulated such as company Secretaries, Chartered Accountants, Cost Accountants, Lawyers, and Architects, Engineers and Doctors etc., particularly accountants and auditors who are not legally permitted to operate as company. As is the practice outside India, LLPs could prove very useful for certain professionals who are unable to use the corporate structure and who do not find the partnership structure viable.

Further, allowing FDI in entrepreneurial projects carried out through the LLP model would encourage small entrepreneurs in India to explore business ventures with foreign investment/collaboration. It may also be considered for small enterprises not seeking access to capital markets through listing on stock exchange. Other than professionals and small entrepreneurs, the LLP structure may also be preferred by small businesses. Additionally, foreign entities having project offices in India could consider reducing risk by using the LLP structure. Further, any structure where different members want to control different segments and also bear full responsibility for their acts could conveniently use the LLP structure. This includes infrastructure project SPVs where different partners bring in different expertise into the project.

A LLP is indeed advantageous because of comparatively lower cost of formation, lesser compliance requirements, easy to manage and run and also easy to wind-up and dissolve, no requirement of minimum capital contributions, partners are not liable for the acts of the other partners and importantly no minimum alternate tax (as of date).

## CONCLUSION

We all know that no law is perfect. The law is volatile in nature because it always tries to keep pace with the changing situations and to fulfill the aspirations of the people. It is the degree and extent of objectives achieved by the law which makes a good law. After economic liberalization, a more dynamic business environment calls for entrepreneurs to have a free hand to manage their business in an efficient manner, without wasting resources on non-essentials. Such resources can be conserved, to a considerable extent, by addressing concerns which arise from certain avoidable regulatory measures. Businesses should have an open but accountable environment to operate in, to maximize resource utilization. One of the appreciable steps forward in this regard is the introduction of Limited Liability Partnerships in India. But unfortunately, there are still some loopholes left by the government which may be of a great concern in future. One of the areas in which reform is required is the regulatory regime governing private companies in India. While this distinction has been recognized, it has not yet resulted in a fully facilitative regime for private companies. The law reflects a "common minimum standard" approach in order to regulate both types of companies, instead of regulating each category differently. The justification for such differential treatment lies in the fact that while public companies involve public funds and interest, as they have access to equity contributions and deposits from the public, in the case of private companies such public interest is minimal. The argument has greater force for private companies that are really small in terms of paid-up capital and/or turnover.

The Ministry of Company Affairs has made efforts to do away with such lacunae in the legal system of our country, but it is yet in an embryonic stage. While a great deal of thought yet needs to be put into certain aspects of the law, some features can be adopted from the laws of other countries. Nevertheless, even a law that is tried and tested in any other country has to be moulded to suit Indian conditions and circumstances. LLP is, after all, a new concept and will require a lot of deliberation. The Centre must try to involve more and more people in the law-making process. The content of the law and its manner of implementation must ensure maximum advantage to everyone involved, and efforts must be made to make the LLP form of corporate governance widely accepted and popular. As the saying goes, a project well begun is half done. The Ministry has made a great beginning, and we hope that in future it culminates in the beginning of a new law in the country.

It appears that the tax department has not visualized the above issues relating to conversion of firm/company into LLP while drafting the provisions of the Finance Act. The amendments made in the Income-tax Act appear to be half-hearted. Unless these and several other related issues are amicably resolved, the new provisions for LLP will not become popular. For this purpose, the Central and State Governments will have to pass appropriate legislation granting exemption of any tax or duty payable on such transfer.

## SUGGESTIONS

- An amendment should be made in the Finance Act, 2009 and the pass-through mechanism should be introduced.
- There should be provision for the conversion back of the LLPs.
- Position should be made clear in case of taxation liability after the conversion.
- Exemption from Capital gains taxation should also be provided under Section 47.
- The policy of Government should be to promote the LLP, and not to discourage it by the introduction of higher taxation.
- Position should be clear with regard to the investment by foreign partners under the FEMA, 1999.

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