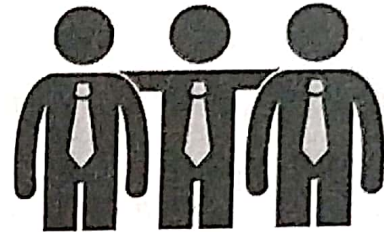


CHAPTER 1

Nature and Incorporation of Limited Liability Partnership



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A Limited Liability Partnership, popularly known as LLP, combines the advantages of both the 'Company' and 'Partnership' into a single form of organisation. It is a renowned and accepted business form worldwide. The Limited Liability Partnership Act, 2008 was enacted by the Parliament of India to introduce and legally introduce the invisible concept of LLP in India. The Limited Liability Partnership (LLP) Bill, 2008 received the assent of the President on 7th January, 2009. The Limited Liability Partnership Act, 2008 became operational with effect from 31 March, 2009.

RATIONALE OF LAW OF LLP

As per the Statement of Objects and Reasons, the rationale of the law of limited liability partnership is as under:

1. With the growth of the Indian economy, the role played by its entrepreneurs as well as its technical and professional manpower has been acknowledged internationally. Moreover entrepreneurship, knowledge and risk capital combine to provide a further impetus to India's economic growth. In this background, a need was felt for a new corporate form that would provide an alternative to the traditional partnership, with unlimited personal liability on the one hand, and, the statute-based governance structure of the limited liability company on the other, in order to enable professional expertise and entrepreneurial initiative to combine, organise and operate in flexible, innovative and efficient manner.

2. The Limited Liability Partnership (LLP) is viewed as an alternative corporate business vehicle that provides the benefits of limited liability but allows its members the flexibility of organising their internal structure as a partnership based on a mutually arrived agreement. The LLP form would enable entrepreneurs, professionals and enterprises providing services of any kind or engaged in scientific and technical disciplines, to form commercially efficient vehicles suited to their requirements. Owing to flexibility in its structure and operation, the LLP would also be a suitable vehicle for small enterprises and for investment by venture capital

The Scheme of the LLP Act, 2008

The Act comprises of 14 chapters and four schedules. Chapter I is preliminary (Sections 1 and 2); Chapter II deals with the nature of LLP (Sections 3 to 10); Chapter III explains provisions relating to incorporation of the LLP (Sections 11 to 21); Chapter IV lays down the eligibility of partners and their relations (Sections 22 to 25); Chapter V deals with the extent of liability of a partner and of LLP (Sections 26 to 30); Chapter VI with the obligation of the partner to contribute and the form of contribution; Chapter VII lays down obligation of LLP to make financial disclosure and maintain books of account and other records (Sections 33 to 40); Chapter VIII with assignment and transfer of partnership rights (Section 41); Chapter IX with investigation of the affairs of an LLP (Section 42 to 53); Chapter X with conversion to LLP from a firm, private company, unlisted public company (Section 54 to 56); Chapter XI with foreign limited liability partnership (Section 57); Chapter XII with compromise, arrangement or reconstruction of LLP (Section 58); Chapter XIII with winding up and dissolution of LLP (Sections 59 to 61) and Chapter XIV with miscellaneous matters (Section 62 to 73)

The First Schedule deals with mutual rights and duties of partners and of the LLP, in the absence of an agreement between the partners. The Second, Third and the Fourth Schedules deal with conversion of a firm, private company, and unlisted public company to LLP respectively.

Further, LLP Rules 2009 as amended from time to time are also to be complied with.

SALIENT FEATURES OF THE LLP ACT, 2008

The salient features of the LLP Act, 2008, *inter alia* are as follows:

- (i) The LLP is a **body corporate** and a legal entity separate from its partners.
- (ii) Any **two or more** persons, associated for carrying on a lawful business with a view to profit, may by subscribing their names to an incorporation document and filing the same with the Registrar, form a Limited Liability Partnership.
- (iii) The LLP will have **perpetual succession**.
- (iv) The **mutual rights and duties of partners** of an LLP *inter se* and those of the LLP and its partners shall be governed by an agreement between partners or between the LLP and the partners subject to the provisions of the LLP Act, 2008. It provides flexibility to devise the agreement as per their choice. In the absence of any such agreement, the mutual rights and duties governed by the provisions of LLP Act, 2008.

- (v) The LLP is a *separate legal entity*, liable to the full extent of its assets, with the liability of the partners being limited to their agreed contribution in the LLP which may be of tangible or intangible nature or both tangible and intangible in nature.
- (vi) No partner is liable on account of the independent or unauthorised actions of other partners or their misconduct. The liabilities of the LLP and partners who are found to have acted with intent to defraud creditors or for any fraudulent purpose shall be unlimited for all or any of the debts or other liabilities of the LLP.
- (vii) Every LLP shall have at least two partners and shall also have at least two individuals as *Designated Partners*, of whom at least one shall be resident in India. The duties and obligations of Designated Partners shall be as provided in the law.
- (viii) The LLP shall be under an obligation *to maintain annual accounts* reflecting a true and fair view of its state of affairs. A statement of accounts and solvency shall be filed by every LLP with the Registrar every year.
- (ix) The accounts of LLPs shall also be *audited*, subject to any class of LLPs being exempted from this requirement by the Central Government;
- (x) The Central Government shall have powers to *investigate the affairs* of an LLP, if required, by appointment of competent Inspector for the purpose;
- (xi) A partnership firm, private company or an unlisted public company would be allowed to be converted into LLP in accordance with the provisions of the LLP, Act, 2008.
- (xii) The winding up of the LLP may be either voluntary or by the Tribunal to be established under the Companies Act, 2013
- (xiii) The Indian Partnership Act, 1932 shall not be applicable to LLPs.

DEFINITION AND NATURE OF LLP

The LLP Act, 2008, simply defines LLP as "limited liability partnership means a partnership formed and registered under this Act."

Section 3 deals with the nature of LLP as under:

1. An LLP is a body corporate formed and incorporated under the LLP Act and as such it is a legal entity separate from that of its partners.
2. An LLP shall have perpetual succession.
3. Any change in the partners of an LLP shall not affect the existence, rights or liabilities of the LLP.

Section 4 provides that unless specifically provided, the provisions of the Indian Partnership Act, 1932 shall not apply to a limited liability partnership.

Accordingly, the characteristics are discussed as follows:

Characteristics of LLP

The aforesaid definition reveals the following significant characteristics of a limited liability partnership as under:

1. **Body corporate.** A 'body corporate' is an artificial legal person distinct and separate having perpetual existence. An LLP is formed by the registration of an incorporation document with the Registrar of Companies of the State in which the registered office of the LLP is to be situated.

2. **Separate legal entity.** A limited liability partnership is an artificial legal person having a distinct legal personality distinct from the individual persons who are its partners. It has the right to own and transfer the title to property in any way it likes. No partner can either individually or jointly claim any ownership rights in the assets of the LLP during its existence or in its winding up. It can sue and be sued in its own name by its partners as well as outsiders. Creditors of the LLP are creditors of the LLP alone and they cannot directly proceed against the partners personally.

Students may note that the principle of separate legal entity as laid down for the companies in the famous case of *Salomon vs Salomon & Co. Ltd.* are equally applicable to LLPs as well.

3. **Artificial Legal Person.** LLP is an artificial legal person because it is created by law by following the process of incorporation. But it does not have any physical characteristics and, thus, is invisible and intangible. Since it is a legal artificial person, it is universal and can be dissolved only by the process of law: Since LLP is a legal person, it can enter into contract, own property like a natural person.

4. **Perpetual existence.** A limited liability partnership just like a company, does not cease to exist on account of death, insolvency or retirement of any or all partner(s). Partners may come and go but the LLP can go on forever. Section 42 provides for transfer of rights by a partner. Thus, a LLP has perpetual existence, irrespective of changes in its partners.

5. **Common seal.** A limited liability partnership acts through its partners and designated partners. Being a legal person, it may have a common seal, if it decides to have one (Sec. 14). Thus, it is optional for an LLP to have a common seal. The seal shall be used as a substitute for its signature in accordance with the provisions of the limited liability partnership agreement and in the presence of at least two of the designated partners of the LLP.

6. **Limited liability.** It is one of the significant characteristics of a LLP. Liability of partners of a LLP shall be limited only to the extent of their investment except in case of unauthorised acts, fraud and negligence. Moreover a partner shall not be personally liable for the wrongful acts or omissions of any other partner. A partner is an agent of LLP and, thus cannot bind other partners. An obligation of LLP, whether arising in contract or otherwise, shall solely be the obligation of the LLP only [Sec. 27(3)]. The liabilities of the LLP shall be met out of the property of the LLP [Sec. 27(4)].

7. **Number of Partners.** Every LLP shall have at least two partners. The law also requires that at least there should be two individuals as designated partner and one of them should be resident of India. There is no maximum limit in number of partners in LLP.

COMPARISON OF LLP VIS A VIS PARTNERSHIP AND COMPANY

Basis of Difference	Traditional Partnership	Limited Liability Partnership (LLP)	Limited Liability Company (LLC)
Applicable Law	The Indian Partnership Act, 1932	The Limited Liability Partnership Act, 2008	The Companies Act, 2013
Distinct Entity	Not a distinct legal entity	Distinct legal entity	Distinct legal entity
Name of Entity	Any name as per choice -No Guidelines	'Limited Liability Partnership' or 'LLP' as suffix to the name.	Name to contain 'Limited' in case of Public Company or 'Private Limited' in case of Private Company or 'OPC' in case of One-Person Company as suffix
Perpetual Existence	No. The death, retirement or insolvency of partners may affect its existence	Yes. The death, insolvency retirement or insolvency of the partner(s) does not affect the existence of LLP: Partners may join or leave but is continue to exist forever	Existence is not affected by death, insolvency, etc. of shareholders of the company.
Legal Proceedings	Only registered partnership can sue third party	Can sue and be sued	Can sue and be sued
Number of Partners (in case of Partnership) Members (in case of a Company)	Minimum 2 and Maximum 100	Minimum 2 partners and there is no limitation of maximum number of partners	2 to 200 members in case of Private Company/ Minimum 7 members in case of Public Company/ Minimum 1 member in case of OPC
Liability of Partners/ Members	Unlimited - Each partner is personally liable	Limited except in case of fraud, wrongful or negligent act by the partner and then only such delinquent partner would be liable	Generally limited to the amount required to be paid up on each share
Audit of Accounts	No requirement of statutory Audit. Tax audit of account as per the provisions of the Income Tax Act, 1961 in case turnover exceeds prescribed limit.	All LLP except for those having turnover less than ₹ 40 Lacs or ₹ 25 Lacs contribution in any financial year are required to get their accounts audited annually as per the provisions of LLP Act, 2008	Companies are required to get their accounts audited annually as per the provisions of the Companies Act, 2013

Digital Signature	There is no requirement of obtaining Digital Signature	As e-forms are filled electronically, at least one Designated Partner should have Digital Signatures	As e-forms are filled electronically, at least one Director should have Digital Signatures
Authority of Partner	Each partner can bind the firm as well as its all partners by his own acts.	Each partner can bind the LLP only by his own acts and not other partners.	Not applicable since no shareholder/member has such authority
Designated Partner	No provision of designated partner	At least two designated partners and at least one of them shall be resident of India	Board of Directors elected by shareholders is responsible.
Legal compliance	All partners are equally responsible for all compliances	Only designated partners are responsible	Board of Directors