

Limited Liability Partnership- A New Gateway To Corporate India

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Abstract

LLP is a new corporate form that enables professional expertise and entrepreneurial initiative to combine, organize and operate in an innovative and efficient manner. In India, this need has long been recognised for businesses which may require a framework that provides flexibility suited to requirements of service, knowledge and technology based enterprises. Services sector is playing a major role in the national economy and there is a growing diversity in the range of services being offered. The services sector also finds this form very useful. LLP Bill, 2008 was introduced in the Rajya Sabha on 21st October, 2008. This was passed by the Rajya Sabha on 24th October, 2008. The Bill was passed by Lok Sabha on 12th December, 2008. The President gave assent to this Bill on 7th January, 2009. This has opened a new gateway to entrepreneurs to enter the corporate world.

Introduction

After a long wait, Government of India has finally brought Limited Liability Partnership (LLP) Act, 2008, into the picture by its notification on January 9, 2009. The original bill was introduced in Rajya Sabha in December, 2006. The current Act is the refined form of that particular Bill. The concept of LLP has been on the cards from the day of submission of reports on the regulation of private company and partnership by Naresh Chandra Committee and on company law by J J Irani expert Committee. Undoubtly, LLP will give a new dimension to Indian Corporate world sooner or later as LLP is a combination of various positive characteristics of a Limited Liability Company and a Partnership firm.

The LLP is a flexible form of entity, which is a body corporate formed and incorporated under the LLP Act,

and having perpetual succession. Any individual or body corporate may be a partner in an LLP, subject to certain disqualifications such as insolvency or a person being of unsound mind. The LLP does not have a cap on the maximum number of partners. Given the above and stricter compliance requirements for a company as well as certain tax inefficiencies built into a corporate structure, an LLP could be a very attractive vehicle in various situations, especially for professional firms such as architects, as well as in situations of infrastructure consortiums, family run businesses which are unlikely to require public funding and indeed, for promoter holding companies.

Comarision with Other Forms

The existing forms of organizations are having certain drawbacks in terms of stringent government regulations

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and flotation and maintenance costs when compared with a LLP. The following table will explain how various

conditions are varying from one form of organization to other form.

S.N:	Conditions	Partnership	Company	LLP
1	Governing Statute	The Indian Partnership Act,1932 and various Rules Made under	Companies Act, 1956	The Limited Liability Partnership Act,2008 and various Rules made under
2	Creation	Created by Contract	Created by law	Created by Law
3	Registration	It is optional	It is compulsory	It is compulsory.
4	Status on separate entity	Not a separate legal entity	It is a separate legal entity	It is a separate legal entity
5	Name	As per choice	It should contain Pvt. Ltd, if it is a Private company or Limited in the case of Public Company as a suffix	It should contain Limited Liability Partnership or LLP as suffix
6	Perpetual Succession	It does not have Perpetual succession	It has perpetual succession	It has perpetual succession
7	Basic Document	Partnership Deed	Memorandum of Association	LLP Agreement
8	Legal Proceedings	Only registered Firms can sue third party	It can sue and be sued	It can sue and be sued
9	Foreign Members	Foreign Nationals cannot be a partner	Foreign Nationals can be a member of a company	Foreign Nationals can be a partner
10	Minimum members	Minimum 2 partners	2 in the case of Private Company and 7 in the case of Public Company	Minimum 2 partners
11	Maximum Members	10 in the case of Banking business and 20 in any other business	50 in the case of Private Company and no maximum limit in the case of Public Company	No maximum limit
12	Ownership of Assets	Partners are having joint ownership of all the assets of the firm	The Company independent of the members	The LLP independent of the partners has ownership of assets

			has ownership of assets	
13	Liability of Partners/members	Unlimited. Partners are severally and jointly liable for the actions of other partners and the firm and liability will extend to their personal assets	Generally limited to the amount required to be paid up on each share.	Limited to the extent of their contribution towards LLP
14	Principal/Agent relationship	Partners are Agents of the firm and other partners	The Directors act as agents of the company and not of the members	Partners act as Agents of LLP and not of other partners
15	Transfer/Inheritance of Rights	Not transferable. In case of death the legal heir receives the final value of share	Ownership is easily transferable	Regulations related to transfer are governed by LLP Agreement
16	Dissolution	By agreement, mutual consent, insolvency, certain contingencies and by court order	Voluntary or by order of National Company Law Tribunal	Voluntary or by order of National Company Law Tribunal
17	Admission of a partner/member	Can be admitted as per the agreement	Can become a member by buying shares	Can be admitted as per agreement of LLP
18	Cessation as partner/member	Can be done as per agreement	Can do by selling the shares	Can cease to be a partner as per the LLP Agreement or in the absence of the same by giving 30 days prior notice to the LLP
19	Recruitment of Managerial Personnel for Management	Partners themselves administer the business	Directors are appointed to manage the business and other statutory compliances on behalf of the Company	Designated Partners are responsible for managing day to day business and other statutory compliances
20	Statutory Meetings	There is no provision in regard to holding of any meeting	Board meetings and general meetings are required to conduct at	There is no provision in regard to holding of any meeting

			appropriate time	
21	Maintenance of Minutes	There is no concept of any minutes	The proceedings of meeting of the board of directors / shareholders are required to be recorded in minutes	A LLP by agreement may decide to record the proceedings of meetings of the partners / designated partners
22	Voting Rights	It depends upon the partnership Agreement	Voting rights are decided as per the number of shares held by the members	Voting rights shall be as decided as per the terms of LLP Agreement
23	Remuneration of Managerial Personnel for day to day administration	The firm can pay remuneration to its partners	Company can pay remuneration to its Directors subject to law	Remuneration to partners will depend upon LLP Agreement
24	Contracts with Partners / Director	Partners are free to enter into any contract	Restrictions on board regarding some specified contracts, in which directors are interested	Partners are free to enter into any contract
25	Maintenance of Statutory Records	Required to maintain books of accounts as tax laws	Required to maintain books of accounts, statutory registers, minutes etc.	Required to maintain books of accounts
26	Annual Filings	No return is required to be filed with Registrar of Firms	Annual Financial Statement and Annual Return is required to be filed with the Registrar of companies every year	Annual Statement of Accounts and solvency & Returns is required to be filed, with Registrar of Companies every year
27	Share Certificate	The ownership of the partners in the firm is evidenced by Partnership Deed, if any	Share Certificates are proof of ownership of shares held by	The ownership of the partners in the firm is evidenced by LLP Agreement

			the members in the company	
28	Audit of Accounts	Partnership firms are only required to have tax audit of their accounts as per the provisions of the Income Tax Act	Companies are required to get their accounts audited as per the provisions of the Companies Act, 1956.	All LLP except for those having turnover less than Rs.40 Lacs or 25 Lacs contribution in any financial year are required to get their accounts audited annually
29	Applicability of Accounting Standards	No Accounting Standards are applicable	Mandatory	Applicable Rules are not yet issued
30	Merger/Amalgamation	Partnership cannot merge with another firm	Can go for merger/amalgamation	Can enter into merger/amalgamation
31	Oppression and mismanagement	No remedy exist	Provision providing remedy exist	No provision currently exist
32	Whistle Blowing	No such provision exist	No such provision exist	Provision has been made to provide protection to employees and partners providing useful information during an investigation or convicting any partner

Incorporation Procedure of LLP

Step 1: Deciding the Partners and Designated Partners

A LLP can be incorporated with a minimum of at least two partners who can be Individuals or Body Corporate through their nominees. Further for incorporating an LLP, of the total number no. of partners, at least two shall be Designated Partners, of which at least one must be an Indian Resident.

Parameters for deciding the Partners and Designated Partners:

1. At least Two Partners; Individuals or Body Corporate through individual nominees.
2. Minimum of Two Individuals as Designated Partners, of total no. of Partners.
3. At least One Designated Partner to be Resident Indian.

A person 'Resident in India' means a person who has stayed in India for a period of not less than one hundred

and eighty two days during the immediately preceding one year. (Explanation to Section-7)

'Designated Partner' means a partner who is designated as such in the incorporation documents or who become a designated partner by and in accordance with the Limited Liability Partnership Agreement

Step 2 : Obtaining DPIN and Digital Signature Certificate

Designated Partner Identification Number (DPIN): Section 7 (6) of LLP Act 2008, provides that every Designated Partner to obtain a DPIN from the Central Government.

DPIN is an eight digit numeric number allotted by the Central Government in order to identify a particular partner and can be obtained by making an online application in eForm 7 to Central Government and submitting the physical application along with necessary identity and Address proof of the person applying with prescribed fees.

Digital Signature Certificate: As all the documents and forms required for incorporating an LLP in India to be filed electronically and under the signatures of Designated Partners, thus at least one Designated Partner to obtain the digital signature certificates from government recognized DSA's. The signatures shall also be required for signing and filing of all relevant forms and documents to be filed, annually or event based after incorporation of the LLP, asking for approvals or as intimation.

Likewise the manual signatures, digital signature certificates are individual specific and no partner needs to obtain more than one.

Step 3 : Checking the Name Availability

The next step is to decide the name for the proposed LLP to be incorporated, anyone intending to incorporate an LLP has to evaluate his proposed name under the prescribed parameters and make an application in Form 1 of Rule 18(5) of the Limited Liability Partnership Act 2008, for reservation of the desired name.

The name of the limited liability partnership shall not be similar or identical with Company or LLP already registered in India and it should not contains words prohibited under the 'Emblems and Names (Prevention of improper use) Act, 1950' or which are also not 'Undesirable' in the opinion of Central Government or which satisfies the conditions prescribed under rule 18(2). For more information one has to check Name Availability Guidelines. In case any Body Corporate is partner, copy of Board resolution authorizing the incorporation of LLP shall be attached

Undesirable Names:- If in the opinion of the department, the name by which a Company is registered gives so misleading an indication of the nature of its activities as to be likely to cause harm to the public, the department may direct it to change its name. A Company registered under the Companies Act, is not entitled to carry on its business in such a way or under such a name, as to represent that its business is the business of any other company or firm or person; and the absence of fraud is immaterial. In such cases, the old company or firm can apply to the court for an injunction, and in such cases the principles that apply to individuals trading under identical or similar names would become applicable.

Step 4 : Drafting of LLP Agreement

The next pertinent step is drafting of Limited Liability Partnership Agreement governing the mutual rights and duties among the partners and among the LLP and its partners.

The basic contents of Agreement are:

- Name of LLP
- Name of Partners & Designated Partners
- Form of contribution
- Profit Sharing ratio
- Rights & Duties of Partners
- Proposed Business
- Rules for governing the LLP

In case no agreement is entered into, the rights & duties as prescribed under Schedule I to the LLP Act shall be applicable

It is not necessary to have the LLP Agreement signed at the time of incorporation, as the details of the same needs to field in eform 3 within 30 days of incorporation but in order to avoid any dispute between the partners as to the terms & conditions of the agreement after the formation of LLP, it is always beneficial to have the LLP Agreement drafted and executed before the incorporation of the LLP.

Step 5 : Filing of Incorporation Documents

Next is the filing of Incorporation documents, consent of Partners and declaration electronically through the medium of e-forms prescribed with the Registrar of LLP for incorporation of the LLP on payment of prescribed fees based on the total monetary value of contribution of partners in the proposed LLP.

eForm 2: Incorporation Document

This is an informative document setting down the details of LLP, its Partners including designated partners along with their amount of contribution and consent for forming a Limited Liability Partnership to carry on a lawful business with profit motive along with declaration stating that all the requirements of Limited Liability Partnership Act, 2008 regarding incorporation of LLP in India have been complied with.

eForm 3: Details of LLP Agreement

This form provides for the necessary information in

respect to the LLP Agreement entered into between the partners.

eForm 4: Consent of Partners Consent of each partner to become a partner of Limited Liability Partnership along with their address and identity proof to be filed with the Registrar of Companies.

Subscription Sheet: Just like in case of Company formation, the partners are required to subscribe their names along with signatures to the subscription sheet, which shall be witnessed by any chartered Accountant/Company Secretary/Advocate in practice.

eForm 3 & 4 are required to be filed within 30 days of the incorporation.

All the eforms will be digitally signed by any Designated partner and shall be certified by an advocate/company secretary/chartered accountant/cost accountant in practice engaged in the formation of LLP.

Step 6 : Obtaining Certificate of Incorporation

After the Registrar is satisfied that all the formalities with respect to the incorporation has been complied. He will issue a Certificate of Incorporation as to formation of the LLP within maximum of 14 days from date of filing of documents. The Certificate of Incorporation issued shall be the conclusive evidence of formation of the LLP.

Taxation of LLP

LLPs are considered as partnerships for tax purposes as a result of the amendments made in the Income-Tax Act by the Finance Act, 2009, which was presented in Parliament on July 6. There were several alternatives for taxation of LLPs which were under consideration: taxation at the LLP level, taxation at the partner level (pass through status) and an option between the two. What has now been legislated is taxation at the LLP level. Also, the Finance Act has removed the surcharge for non-corporate assesses and LLPs will therefore, be taxed at 30.9%, including the education cess (there is a possible view that even the education cess could not apply to LLPs, in which case, the rate would be 30%).

There are a variety of tax benefits that an LLP would enjoy and some of these are as under:

- A lower rate of tax as compared to corporates; i.e. 30.9% (or 30%) compared to 33.99%.
- No minimum alternate tax (MAT), since MAT applies only to companies.
- No dividend distribution tax (DDT) (16.995% saving).

Given the above benefits, it seems to make considerable sense for many businesses to be formed as LLPs or be converted into LLPs. For the latter to happen, several other things have to fall in place and this article seeks to examine some of those issues. The draft direct tax code (DTC) issued by the finance ministry on August 12 seeks to reduce the tax rates for companies to 25% and the DDT to 15%. Even so, if the reduced rates come through, there is an approximately 5% saving for a LLP structure, since there is no DDT on a distribution by a LLP, as opposed to a situation of a company which will have a combination of corporate tax and DDT (in addition, of course, to a cash trap, as a result of the requirement to statutorily transfer 10% of profits to reserve)

Conclusion

The first LLP was registered on 2nd April 2009. As on 26th October 2009, 308 LLPs have been registered. Though their number is increasing in a high rate, certain issues are to be properly addressed. Rules of conversion of a company into a LLP are not so clear. In relation to the tax aspect of conversion, the issue that arises is whether the company would be liable to capital gains tax. The explanatory notes to the Finance Act mention regarding the tax neutrality for conversion of partnerships into LLPs, but nothing about the conversion of companies into an LLP. Clarity is needed on Stamp Duty related issues. To solve this issue Ministry of Company Affairs has to write to state governments and various market regulators. Another key area on which clarifications are needed is Foreign Direct Investment (FDI). The FDI regime currently does not appear to accommodate FDI in an LLP. In relation to multinational companies or indeed infrastructure SPVs, the issue of FDI in an LLP assumes great significance. One understands that the government is actively looking at this and amendments on this aspect should happen sooner rather than later.

One can expect that in the near future government will come out with various notifications in support of LLPs and a wide range of entrepreneurs will choose LLPs as their gate way to the corporate world.

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