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Limited Liability Partnership Suitable to Emerging Enterprises in Current Trends

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ABSTRACT

The Partnership Act, 1932, places unlimited responsibility on the partner, whereas the company laws viz. Companies Act, 1956, seeks to pay heavy punishment including imprisonment for the individuals operating the business to comply with multiple clauses otherwise. A fresh company form, i.e. Limited Liability Partnership (LLP) emerged with the enactment of the Limited Liability Partnership Act, 2008 (the Act), informed on March 31, 2009. This structure has become quite common among Small and Medium Enterprises (SMEs), Professional Services and Small Enterprises as this business form seeks to integrate the partnership's operational flexibility with advantages of limited liability and a company's distinct legal identity.

Therefore this paper discusses significantly about the various features of LLPs, their advantages and disadvantages, the LLP Act 2008 and also the taxation of LLPs in India .

I. WHAT IS A LIMITED LIABILITY PARTNERSHIP (LLP)?

It is best to begin with the general partnership in order to comprehend a limited liability partnership. A general partnership is a for-profit organization formed between two or more parties through a mutual comprehension. This is a very technical way to say that two or more individuals are working to create cash together. It can be quite informal to have a general partnership.

Of course, there is a downside with the casual nature of a general partnership. Legal liability is the most evident danger. All partners share responsibility for any problem that may occur in a general partnership. For instance, if A and B are partners in a cookie project and a poor batch results in individuals getting sick, both can be sued for damages personally. Therefore, many individuals rapidly transform general partnerships into official legal entities such as a limited liability company (LLC). An LLC², like AB's Cookie Factory, can stand up as a legal entity for A and B and safeguard their private property from being part of any legal action.

You need something a little more tailored in some jobs, however, than a limited liability

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² Limited liability company hereby known as LLC

company with a fixed framework. Enter the partnership with limited liability. The LLP is a formal framework that involves a written partnership agreement and generally includes criteria for annual reporting depending on your legal jurisdiction.

Like in a general partnership, all partners in an LLP³ can be involved in partnership leadership. This is an significant point because there is another type of relationship-a limited partnership-where one partner has all the authority and most of the responsibility and the other partners are silent but have a monetary interest. Liability is also shared with the shared leadership of an LLP-although, as the name indicates, it is very restricted.

(A) Why opt for an LLP ?

They tend to depend strongly on reputation for professionals using LLPs. Most LLPs are developed and managed between them by a group of experts with a lot of experience and customers. By pooling funds, partners reduce company expenses while improving the growth ability of the LLP. They can share office room, staff, etc. Most importantly, cost reduction enables partners to make more earnings from their operations than they can separately.

In the company, the partners in an LLP may also have a number of junior partners working for them in the hopes of becoming a full partner one day. These junior partners are paid a wage and the partnership often has no interest or liability.

The significant point is that they are appointed skilled professionals to do the job the partners do. This is another way to assist LLPs scale their activities to partners. Junior partners and staff take away the detailed job and free the partners to concentrate on starting fresh company.

The capacity to bring in partners and let out partners is another benefit of an LLP. Because there is a partnership agreement for an LLP, as described in the arrangement, partners can be added or retired. This is useful as the LLP can always add partners to take with them current company. Usually the choice to add needs all current partners to approve it.

Overall, making it a superior choice for an LLC or other corporate entity is the flexibility of an LLP for a certain sort of specialist. Like an LLC, the LLP itself is a tax-related flow-through entity. This implies the partners receive untaxed earnings and they have to pay their own taxes. Both an LLC and LLP are preferred to a corporation that is taxed as an organization and then again taxes its shareholders on distributions.

In short , the advantages can be pointed out to be as follows

³ Limited liability partnership hereby known as LLP

- Easy to form
- Liability
- Perpetual succession
- Management of the company
- Easy transferability
- Ownership
- No compulsory audit required

(B) Why not opt for an LLP ?

- Less credibility- One of Limited Liability Partnership's significant demerits is that this is not considered by many as a reliable company. People still have more confidence in companies or alliances.
- Partners not consulting- Limited Liability Partners do not consult with one another in the event of choices and agreement.
- Interest transfer- Although interest and property may be transferred, it generally requires a lengthy process. In order to comply with the regulations of the law, various formalities are needed.
- Lack of recognition- It is not acknowledged by all as LLP is launched in India in 2009 on its own. Because of its less acceptance, the firm's smooth functioning is hampered. It is unlikely that people will form LLP.

(C) How limited is a Limited Liability Partnership (LLP) ?

Where you create it depends on the real information of a limited liability partnership. Your private assets, however, will generally be shielded as a partner from legal intervention. Basically, the liability is restricted in the sense that in the relationship you will lose property, but not resources outside the partnership (your private assets). The partnership is the first target for any suit, although if he or she personally did something wrong, a particular partner might be responsible.

II. ALL ABOUT THE LIMITED LIABILITY PARTNERSHIP ACT , 2008⁴

It would be helpful for small and medium-sized enterprises in general, and for businesses in the services industry in specific, due to flexibility in their structure and operation. LLPs are

⁴ Choosing a Form of Business Organisation : Limited Liability Partnership (LLP)
https://archive.india.gov.in/business/starting_business/limited_liability.php

the preferred company vehicle internationally, especially for the service industry or for professional operations.

LLP is regulated by the 2008 Limited Liability Partnership Act , whose significant features are as follows :

- a) The LLP shall be a body corporate and a legal entity separate from its partners. 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. The LLP will have perpetual succession.
- b) 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 . The act provides flexibility to devise the agreement as per their choice.
- c) The LLP will be 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. No partner would be liable on account of the independent or un-authorized 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.
- d) 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.
- e) The LLP shall be under an obligation to maintain annual accounts reflecting 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. The accounts of LLPs shall also be audited, subject to any class of LLPs being exempted from this requirement by the Central Government.
- f) The Central Government has powers to investigate the affairs of an LLP, if required, by appointment of competent Inspector for the purpose.
- g) The compromise or arrangement including merger and amalgamation of LLPs shall be in accordance with the provisions of the LLP Act 2008.

- h) A firm, private company or an unlisted public company is allowed to be converted into LLP in accordance with the provisions of the Act. Upon such conversion, on and from the date of certificate of registration issued by the Registrar in this regard, the effects of the conversion shall be such as are specified in the LLP Act. On and from the date of registration specified in the certificate of registration, all tangible (moveable or immovable) and intangible property vested in the firm or the company, all assets, interests, rights, privileges, liabilities, obligations relating to the firm or the company, and the whole of the undertaking of the firm or the company, shall be transferred to and shall vest in the LLP without further assurance, act or deed and the firm or the company, shall be deemed to be dissolved and removed from the records of the Registrar of Firms or Registrar of Companies, as the case may be.
- i) The winding up of the LLP may be either voluntary or by the Tribunal to be established under the Companies Act, 1956. Till the Tribunal is established, the power in this regard has been given to the High Court.
- j) The LLP Act 2008 confers powers on the Central Government to apply provisions of the Companies Act, 1956 as appropriate, by notification with such changes or modifications as deemed necessary. However, such notifications shall be laid in draft before each House of Parliament for a total period of 30 days and shall be subject to any modification as may be approved by both Houses.
- k) The Indian Partnership Act, 1932 shall not be applicable to Limited Liability Partnerships.

III. TAXATION WITH REGARD TO LLPS

A company's or a partnership's tax concerns are not addressed in the 1956 Companies Act⁵ or the 1932 Indian Partnership Act⁶, respectively. Tax law deals with them. It was therefore inevitable that the LLP Act would remain silent on the tax consequences for an LLP.

In multiple overseas jurisdictions, there are two common taxation alternatives that provide for LLPs. The first is the practice of treating an LLP as a tax-transparent entity, as seen in the French LLP model, and taxing only the partners' income and not the transparent entity.

The option to this, based on the UK and Singapore LLP models, is to treat an LLP as a partnership with comparable cable therapy. The latter practice has been embraced by India.

⁵ Refer to The Companies Act, 1956

⁶ Refer to Indian Partnership Act, 1932

According to the amended Section 140 of the Income Tax Act, 1961⁷, the designated partner must sign the income return and may be signed by any other partner for some unavoidable reasons. The words ' partner, ' ' company ' and ' partnership ' pursuant to Section 2(23) of the Income Tax Act, 1961⁸ were revised in accordance with the Finance Act, 2010 to include LLPs within its scope.

For tax purposes, an LLP will be considered an equivalent of a general partnership and will reap all the tax benefits available to a partnership. Income tax will be levied on the LLP itself and the LLP profits obtained by the partners will not be calculated for their personal income as it will be regarded as ' company revenue ' within the range of a ' computational revenue deduction. ' In case of non-compliance with Section 184 of the LLP Act⁹, the remuneration paid to the partners will not be permitted as deductions on their personal income.

In addition, any contribution of capital assets by a partner to its LLP or distribution of such assets by the LLP to any partner shall be deemed to be income of the partner and LLP respectively and subject to income tax. 40(b) The Income Tax Act, which gives for limitations on interest payments and remuneration to partners, has now been amended to apply evenly to professional and non-professional companies. LLPs are beneficiaries of the change, making them an appealing company choice for association-forming practitioners.

While an LLP is usually regarded as an equivalent of a general partnership for tax purposes, the Union Budget 2011-12¹⁰ announced an Alternate Minimum Tax (' AMT ') levy on LLPs comparable to that imposed on firms by the Minimum Alternate Tax (' MAT '). In this regard, the Union budget has proposed the introduction of a new Chapter XII-BA under the Income Tax Act, 1961, which provides for an AMT levy of 18.5% of the adjusted total income of LLPs.

Thus, the tax base for LLPs would be the complete adjusted income rather than book earnings as in the situation of businesses. Although the introduction of the AMT on LLPs may be viewed as a disadvantage to the LLP business form, owing to its intrinsic flexible structure and the exemption from dividend distribution tax, the LLP still remains an appealing business form.

However, the tax system for LLPs may discourage potential foreign investors as investment in LLPs may lead to double taxation-first at the level of the LLP in India and second at the

⁷ Refer to Income Tax Act , 1961

⁸ Refer to Income Tax Act , 1961

⁹ Refer to The Limited Liability Partnership Act, 2008

¹⁰ Refer to <https://www.indiabudget.gov.in/budget2011-2012/budget.asp>

rate of revenues for the overseas jurisdiction investor. However, it may be convenient for an Indian LLP doing company overseas depending on the laws that prevail in overseas jurisdiction, as the LLP may be regarded as tax-free and taxed as a distinct entity. It will therefore take advantage of the tax credit advantages.

Even India's double tax avoidance treaties with some states did not provide an appropriate solution. It is important to note at this stage that a truly distinctive scheme is adopted in the US that, in accordance with the LLP's inner framework, provides the choice of taxation either at the LLP stage or at the partner level. This allows an LLP to determine its structure in accordance with the legislation of the nations where the LLP invests and does company in order to take advantage of the tax credit benefit. Had India embraced such a system, it could have efficiently placed the issue of double taxation to rest.

IV. LLPS' NEED IN INDIA

The two main reasons for implementing LLP were the risk factor and the Indian experts improved worldwide competitive advantage. The liability would be restricted to the accountable partner in the case of a business failure. There would be no recourse to attach the other members' private property. This reduces the risk factor associated with unlimited partnership liability and introduces the company law concept of limited liability to make such bodies more adaptive to international competition. In the years ahead, it may be feasible that a big pool of Indian experts will provide the numerous helpful services to the international clientele. But, in an increasingly litigious setting, being a partner company with unlimited liability is really very dangerous. There was therefore a need for a new corporate entity to be created as an alternative to the traditional partnership with limited liability and flexible company climate in order to function effectively to offer the international market competition.

Many Indian practitioners, such as advocates / lawyers, chartered accountants and physicians, are excluded from corporate practice. In the age of satisfying worldwide clients with utmost honesty, the LLP structure would be particularly advantageous for offering such professional services.

It would therefore be an appropriate vehicle for collaboration between experts who are already regulated, such as company secretaries, chartered accountants, cost accountants, lawyers and architects, engineers and doctors, etc., especially accountants and auditors who are not legally authorized to function as a business. Furthermore, as India attracts FDI in entrepreneurial initiatives carried out through the LLP format, the same would encourage tiny

Foreign organizations with project offices in India also consider the use of the LLP framework to reduce danger. Any framework where distinct participants want to regulate distinct sections and also bear complete accountability for their actions could use the LLP framework that contains SPVs for infrastructure projects where distinct partners bring distinct skills to the project. businesses in India to explore foreign investment company enterprises.

(A) Indian precedents in some cases related to LLPs

1) Wind World (India) Limited and Others Vs. Enercon GmbH and Another - Court Judgment¹¹

78. In my view there is no merit in the submission of the learned senior counsel for the respondents that the petitioners themselves had voluntarily filed an undertaking before the arbitral tribunal to preserve the partnership assets, to maintain status quo, to prevent distribution of the partnership assets etc. and the impugned order passed by the majority arbitrators having been passed in line of the undertakings rendered by the petitioner nos.2 and 3 and thus cannot be interfered with by this court. The petitioner nos.2 and 3 at the first instance could not have rendered such undertaking on behalf of those limited liability partnerships or on behalf of the other partners at all, contrary to the provisions of the Limited Liability Partnerships Act, 2008. Be that as it may, in my view the majority arbitrators could not have passed such interim orders by which the two partners have been directed to preserve the assets of the limited liability partnerships or to prevent any distribution of assets of such limited liability partnership or to dispose of or deal with or diminishing the value of the assets except with the prior permission of the tribunal or otherwise.

79. In my view, the majority arbitrators could not have subjected the other partners of the limited liability partnership or shareholders of a private limited company to obtain prior permission to deal with or dispose off the assets of those limited liability partnerships which is not permissible in law. The majority arbitrators in my view have directed the petitioner nos.2 and 3 to force other partners of those limited liability partnerships not to take any independent decision and to accept whatsoever would be the decision or the order of the petitioner nos.2 and 3. The order passed by the majority arbitrators in my view shows patent illegality and thus deserves to be set aside.

2) Fatesh Kishanchand Mirchandani vs Sanjay Bhagwandas Lohia¹²

9. The Court Receiver will make a report also as to who is found in actual physical

¹¹ 2016 SCC OnLine Bom 1404

¹² 2017 SCC OnLine Bom 6319

possession of the premises. The Petitioner and the Respondent both are entitled to inspect and examine the books of accounts of the Limited Liability Partnership that are in the premises. These books of accounts will then be handed over to the Receiver.

3) M/s. Brolly Dealcom LLP vs. Principal Commissioner of Income Tax, Kol-2¹³

4. However, what is of importance is that even though a previous notice under Section 263 of the Act is not a *sine qua non* for the jurisdiction to be exercised there under by the commissioner, the provision mandates an opportunity of hearing to be afforded to the assessee. In the present case, upon the assessee company being dissolved, such opportunity of hearing ought to have been given to the present appellant, particularly, since it appears that the present appellant kept the authorities informed of the company being dissolved upon the appellant limited liability partnership taking over its business, assets and liabilities as a going concern .

V. WHAT ABOUT LLPS AROUND THE WORLD?

In many nations with differing degrees of divergence from the U.S. model, limited liability partnerships exist. An LLP is a tax flow-through entity in most nations designed for experts who will all play an active part in managing the partnership. LLPs, such as attorneys, accountants, advisors, and architects, often have a list of authorized jobs. Liability protection also ranges, but the LLPs of most nations safeguard the partner from any other partner's negligence.

VI. CONCLUSION

Limited liability partnerships can be a boon to newly emerging enterprises due to the mixed benefits of both a company as well as a partnership . but however , before deciding to have this specific type of enterprise , it is suggested to have a detailed talk a legal entity regarding the implications of the same in concern of the situations and conditions surrounding the emerging enterprise to check the suitability .

¹³ 2018 SCC OnLine Cal 2058 : (2018) 406 ITR 542