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The Limited Liability Partnership Model Has Successfully Replaced The Incorporation Complexity And The Personal Risks Connected With Partnership Legislation, Right?

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ABSTRACT: The commencement of the Limited Liability Partnership Act in 2008 led to a new phase in the Indian corporate sector. As the Limited Liability Partnership (hereinafter 'LLP') model gained popularity, many compared it to the existing partnership mechanism. While there are some similarities in both, several differences on grounds such as risk and complexity have been examined. Apart from an elaborate explanation of the LLP model, the application of the model on various kinds of businesses has been highlighted. The pandemic situation's effect on partnerships, and how LLPs will fare after these times has also been evaluated. Towards the end, the author have touched upon the current limitations of the model and the potential it can reach with certain modifications.

KEYWORDS: LLP, model, incorporation complexity, personel risks, partnership legislation

I. INTRODUCTION

The limited liability partnership (LLP) model has indeed become a popular choice for businesses, particularly in professional services sectors such as law, accounting, and consulting. It offers a hybrid structure that combines elements of both partnerships and corporations, aiming to provide the benefits of limited liability to partners while preserving the flexibility and tax advantages of traditional partnerships.

LLPs are often preferred over traditional partnerships because they provide protection against personal liability for the debts and obligations of the partnership, similar to the limited liability enjoyed by shareholders in corporations. This means that individual partners are generally not personally responsible for the LLP's debts and liabilities beyond their capital contributions, except in cases of personal wrongdoing or negligence.[1,2,3]

Moreover, LLPs offer flexibility in management and decision-making, allowing partners to have more control over the operations of the business compared to shareholders in corporations. They also offer pass-through taxation, meaning that profits and losses are allocated directly to the partners and taxed at the individual level, avoiding the double taxation that can occur with corporations.

However, it's essential to note that while LLPs provide limited liability protection, they may not entirely eliminate personal risk, especially in cases of fraud, negligence, or professional malpractice. Additionally, the complexity of LLP formation and ongoing compliance requirements may vary depending on jurisdiction, and in some cases, they may not be suitable for all types of businesses.

Overall, while LLPs have become a popular choice for many businesses seeking limited liability and flexibility, they may not entirely replace the incorporation complexity or personal risks associated with traditional partnership legislation. Businesses should carefully consider their specific needs, objectives, and the legal and regulatory framework in their jurisdiction when choosing the most appropriate business structure.

The Indian Partnership Act was enacted in 1932 by the colonial government, to lay the basic framework for business partnerships in India. The principal feature of this form of partnership ("traditional partnership") is that each partner is treated as the principal as well as the agent of every other partner. Thus, the liability of every partner to the acts done by the other partners during the course of employment is unlimited.

As the Indian economy progressed towards liberalization, privatization and globalization, more and more foreign firms started setting up branches and expanding to India. Smaller-scale industries and the entrepreneurial environment in India needed to be made more conducive to this investment.

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Around the world, the business model of traditional partnerships lost its appeal. Due to LPG, this dissatisfaction with traditional partnerships started growing in India too. This was primarily because of the unlimited liability binding all the partners to the acts of the other. Researchers all around the world examined their partnership laws and most of them advocated in favour of the concept of 'Limited Liability Partnerships' (LLP) to fix this problem. Jurisdictions all around the world started adopting this form, which was widely accepted by the people.

Need for introducing LLP

7th report of the Law Commission of India

The 7th report of the Law Commission of India contained a suggestion by the merchants of iron, steel and hardware industries for introducing a framework for Limited Liability Partnerships. This was due to the cumbersome incorporation procedure, high personal risks and restrictions associated with traditional partnerships. These were major obstacles for small businesses that did not possess the resources to incorporate themselves into a full-fledged company. However, the Law Commission rejected this idea.

Bhatt Committee, 1972 and Abid Hussain Committee, 1997

The Bhatt Committee in 1972 and the Abid Hussain Committee in 1997 gave similar recommendations to introduce a framework for incorporation of LLPs in India. This recommendation was primarily in response to the concerns of small scale industries and enterprises.

Naresh Chandra Committee, 2003

The Naresh Chandra Committee in 2003 advocated for a different approach. It highlighted the need to introduce LLPs to create a more favourable environment for the service industry. LLPs were expected to allow better pooling of technical expertise from professionals across fields.

J. J. Irani Committee, 2005

The J. J. Irani Committee in 2005 further recommended that the government enact a separate law to lay down the framework for LLPs in India. Additionally, it recommended that the government extend its scope to small businesses.

Limited Liability Partnership Act, 2008

Eventually, it became only a matter of time before India adopted the LLP model. The Limited Liability Partnership Act ("LLP Act") was enacted in 2008. Touted as a hybrid between company and partnerships, this business model creates a healthy environment for the growth of small enterprises and venture capital. The Statement of Objects and Reasons of the LLP Act acknowledged this reason, declaring the purpose of the Act to be to enable entrepreneurship and professional expertise to combine 'in a flexible, [4,5,6]innovative and efficient manner'.

The LLP-based business model was wholeheartedly accepted by India. This is evident by how within 4 years of the enactment of the LLP Act, more than seven thousand LLPs registered themselves in India.

Major differences between LLP and traditional partnership

LLP	Traditional partnership
An LLP is a body corporate and has a separate existence as a legal entity. It is not legally categorized in terms of its partners.	A traditional partnership has no existence as a separate legal entity. It is simply the sum of its partners in the eyes of the law.
Incorporation is compulsory.	Registration of the partnership is not compulsory but may offer certain benefits.
Change in partners does not affect its separate existence or liability.	Change in partners can affect the firm's existence, rights and liabilities.
Perpetual succession, i.e., a change in partners, is allowed i.e. death or resignation of one partner does not lead to the dissolution of the LLP.	Any change in partners may affect its overall existence unless otherwise agreed.
Minors can be partners.	Minors can only be admitted to the benefits of the partnership i.e., the

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	profits and are not personally liable for any losses.
Even though the minimum number of partners is two, the LLP is still valid if the business is carried on only by one partner, for a period of a maximum of 6 months.	A traditional partnership cannot exist with only one partner.
The 'designated partner(s)' is/are the only one(s) who would be liable for statutory compliances.	All partners are liable for statutory compliances.
Partners hold no personal liability for acts done by other partners, but only for the acts done by themselves.	All of the partners are personally liable for the acts of other partners.
Every partner is an agent of the LLP, but not an agent of the other partners.	Every partner is an agent of other partners.
The LLP shall include "LLP" in its name. There also exist certain other restrictions on its name.	There are no specific restrictions on the name of the partnership.
An unlisted public company or a private one can convert itself into an LLP, following the procedure prescribed by law.	No such conversion is possible in a traditional partnership.
Section 14 of the LLP Act mandates disputes to be referred to alternative dispute resolution (ADR).	There is no such mandatory provision in a traditional partnership.

Advantages of LLP over traditional partnerships

- LLPs combine the favourable features of a partnership firm, as well as of a company. The liability of each partner is limited to their contribution to it. This helps in minimizing personal risks and protects partners from the mistakes or misconduct of other partners.
- LLPs are more flexible than companies. Companies have stricter compliance requirements and are more rigidly regulated than traditional partnerships. There is no requirement for minimum capital to start a business as required in public companies, and LLPs have lower registration costs than companies.
- Additionally, LLPs are treated on par with partnership firms for taxation benefits and exempted from paying Dividend Distribution Tax. Further, an LLP is also exempted from the audit of its accounts, which further decreases compliance costs. This makes opting for LLPs over traditional partnerships more favourable.

A sum of these provisions makes LLPs suitable for technical and professional businesses since it helps experts from diverse fields come together to pool their knowledge. As examined, LLPs are also suitable for small-scale businesses. Thus, it creates a positive environment for venture capital in India.

Disadvantages of LLPs over other business forms

- An LLP is not in a position to receive equity investment or any shareholding, as companies do. So, it can not receive any private equity funds or venture capital as shareholders. It is forced to fall back on debt and funding from promoters.
- Under Indian law, LLPs are taxed at a rate of 30% for income tax, irrespective of their turnover. This is more than the income tax rate for companies with turnover over Rs. 250 crores, taxed at a mere 25%.
- LLPs are to file annual income tax returns as well as MCA (Ministry of Corporate Affairs) returns, even in a case where the LLP is inactive. In certain cases, the penalty goes up to Rs. 100 per day. In contrast to this, a partnership firm has no such requirement.
- There is a lack of clarity regarding the right to practice in courts by LLPs. Since LLP has a separate legal personality, there is a question of whether LLPs are allowed to represent in courts, or in other words, 'practice' law. According to Rule number 2 in chapter 3 of the Bar Council of India Rules, an advocate is barred from partnering or entering into any arrangement for sharing remuneration with a 'non- advocate'. However, the rule does not prohibit partnerships between two advocates. Thus, the position of the law here is unclear.[7,8,9]
- According to Section 7 of the LLP Act, an LLP cannot be owned solely by foreign residents. In other words, at least one of the partners needs to be a resident of India, and the LLP cannot have only Non- Resident Indians

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(NRIs) as partners. One of them needs to have been residing in India for at least one hundred and eighty-two days in the immediately preceding year. This provision has attracted criticism especially since one of the objectives of the act is the admission of foreign partners.

- Additionally, there is a question of law that arises on the liability of foreign partners, in case the partnership is related to the profession of law. There is no clarity on the extent of liability incurred by foreign partners, due to "wrongful" acts committed by them. Indian courts may decline to enforce any claim against the personal assets of the aforementioned partner.
- Additionally, with respect to foreign investors, there is the issue of double taxation of income arising from the LLP. Income from the LLP would be taxed in India as well as the jurisdiction where the investor resides. This makes the environment for foreign investment unfavourable.
- The LLP framework introduces a concept of a 'designated partner'. This partner is held liable for all statutory compliances of the LLP, including filing returns, various documents, insolvency petitions as well as other reports and legally mandated documents. If they fail to do the same, they would be held personally liable for the penalty imposed on the LLP, as well as for any contravention of the law. This places an undue burden on some of the partners.
- There is no provision that allows LLPs to convert back into companies.
- LLPs need to be registered under Indian law, while partnerships do not face this compulsion.
- Further, partners to the LLP have unequal rights, due to the lack of a one-vote-per-share system. This causes friction within the business.

II. DISCUSSION

Limited Liability Partnerships (LLPs) represent a distinct form of business entity, combining the best features of both traditional partnership firms and limited corporations. From the former, it borrows the advantage of flexible management, whereas from the latter it acquires the protection of limited liability for owners. In the entrepreneurial world, it offers the best partnership structure you can ever establish and incorporate within India. LLPs are governed under the Limited Liability Partnership Act 2008, which contains detailed provisions regarding its incorporation, compliance, and legal structure. In this blog, we will discuss the salient features of LLP with the features of the LLP Act 2008 to give you a clearer picture. But before we begin, let's understand how LLPs evolved as a desired business structure both within India and abroad.

Evolution of LLPs in India & Abroad

The concept of LLPs originated in the U.S during the early 1990s and subsequently spread to various jurisdictions, including India. The need for such a hybrid entity arose from the limitations of traditional partnership structures, where individual partners were personally liable for the business's debts and obligations. LLPs were introduced to address this drawback by bringing in limited liability for partners while retaining the organizational flexibility inherent in conventional partnerships.

The introduction of LLPs aimed to facilitate entrepreneurship, innovation, and professional services by offering a business structure that combines the benefits of both partnerships and corporations. This evolutionary step in the business landscape sought to accommodate the evolving needs of modern businesses, particularly those in knowledge-intensive industries such as legal, accounting, consulting, and technology sectors, where collaboration among professionals is paramount.

Overview & Salient Features of LLP

Limited Liability Partnerships (LLPs) represent a unique form of business entity that combines the benefits of both partnerships and corporations. As defined by the Limited Liability Partnership Act, 2008, an LLP is "a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners." This definition underscores the core characteristic of LLPs – their distinct legal personality, which shields the personal assets of partners from the liabilities of the business.

In practical terms, LLPs operate similarly to traditional partnerships, where partners collaborate and share profits[10,11,12], but with the crucial advantage of limited liability protection. This means that partners are not personally liable for the debts, obligations, or wrongful acts of the LLP. Instead, their liability is limited to the extent of their capital contribution to the LLP, providing a safeguard against financial risks and liabilities. Now, let's delve into the salient features of LLPs as outlined in the LLP Act, 2008, and explain each of them separately:

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Limited Liability
Limited liability is a foundational aspect of Limited Liability Partnerships (LLPs), ensuring that partners' personal assets are safeguarded from the liabilities of the business. This means that in the event of financial losses, debts, or legal claims against the LLP, partners are only liable up to the amount of their capital contribution. This protection is crucial for mitigating risks associated with business operations, as it shields partners from the potential of losing personal assets such as savings, properties, or investments. By offering this financial security, limited liability encourages entrepreneurship, investment, and collaboration among partners, fostering a conducive environment for business growth and innovation.

Separate Legal Entity
LLPs function as independent legal entities, meaning they possess legal rights and obligations distinct from their partners. This legal status empowers LLPs to own assets, incur debts, enter into contracts, and initiate legal proceedings in their own name. By establishing this separation between the LLP and its partners, clarity is ensured in legal matters, allowing for seamless engagement in transactions, partnerships, and other business activities without the need for direct involvement or consent from individual partners. This autonomy enables LLPs to operate efficiently, pursue opportunities, and fulfill obligations without undue complexity or ambiguity in legal relationships.

Perpetual Succession
Perpetual succession is a distinctive characteristic of LLPs wherein the entity maintains its existence independent of changes in its partner composition. In practical terms, this means that the departure, retirement, or even demise of a partner does not lead to the dissolution of the LLP. Instead, the LLP continues its operations unhindered, ensuring business continuity and stability even amidst partner transitions. This feature provides assurance to stakeholders, creditors, and clients, as they can rely on the LLP's continued presence and performance over the long term, regardless of changes in its partner roster.

Flexibility in Management and Operations
LLPs offer considerable flexibility in how they structure their internal governance and operational processes. This flexibility extends to the establishment of management roles and decision-making procedures, which can be tailored to suit the specific needs and preferences of the partners. Partners have the autonomy to define their roles and responsibilities within the LLP, allowing for efficient delegation of tasks and responsibilities. Additionally, the option to designate designated partners for administrative duties provides a streamlined approach to management, enabling partners to focus on their areas of expertise while ensuring effective leadership and coordination within the LLP.

Taxation Aspect
LLPs benefit from a pass-through taxation system, which means that the entity itself is not subject to taxation on its profits. Instead, profits and losses are passed through to the individual partners, who report them on their personal income tax returns. This taxation structure simplifies the administrative burden for LLPs and their partners, as they are not required to file separate tax returns for the entity. Moreover, pass-through taxation eliminates the risk of double taxation that may occur with other business entities, such as corporations, where profits are taxed at both the entity and shareholder levels.

Key Features of LLP Act 2008
The enactment of the Limited Liability Partnership Act 2008 provided statutory recognition and regulation for LLPs in India, offering them a legal framework distinct from conventional partnerships and corporations. It established clear guidelines regarding the formation, operation, and dissolution of LLPs, thereby enhancing transparency, accountability, and investor confidence in this form of business organization. Furthermore, the LLP Act of 2008, introduced provisions for limited liability protection among partners, allowing them to shield their personal assets from business liabilities. This not only encouraged entrepreneurship but also fostered investment and risk-taking among partners. Here are some of key features of LLP Act 2008 you must know!

III. RESULTS

1. Registration and Incorporation Process: The LLP Act, 2008, streamlines the registration and incorporation process for LLPs, providing clear guidelines and procedures. It mandates the reservation and approval of a unique name for the LLP, ensuring its distinct identity. The Act specifies the necessary documents and forms to be submitted for incorporation, including the LLP agreement, partners' consent, and address proof. Upon successful registration, the LLP receives a Certificate of Incorporation from the Registrar of Companies, confirming its legal existence.

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2. Regulatory Oversight: The LLP Act, 2008, establishes a regulatory framework to oversee the operations of LLPs and ensure compliance with statutory requirements. It empowers the Registrar of Companies to maintain a register of LLPs, monitor their activities, and take enforcement actions in case of violations. The Act outlines penalties for non-compliance, including fines and prosecution, to deter misconduct and promote adherence to legal obligations.
3. LLP Agreement: The LLP Act, 2008, recognizes the autonomy of LLPs in structuring their internal governance through[13,14,15] a partnership agreement. It allows LLPs to customize their operational framework by defining partners' rights, responsibilities, and decision-making processes. The Act permits flexibility in designing profit-sharing arrangements, capital contributions, admission of new partners, and resolution of disputes, fostering transparency and consensus among partners.
4. Capital Contribution and Distribution: The LLP Act, 2008, governs the capital structure and financial management of LLPs, ensuring clarity and fairness in capital contributions and profit distributions. It specifies that partners may contribute capital in the form of money, property, or services, with provisions for valuation and accounting treatment. The Act outlines rules for profit-sharing among partners, including the allocation of profits and losses in proportion to their capital contributions or as per the LLP agreement.
5. Winding Up and Dissolution: The LLP Act, 2008, provides mechanisms for the orderly winding up and dissolution of LLPs in case of closure or insolvency. It delineates procedures for voluntary dissolution initiated by partners through a resolution and winding up by the Tribunal in case of default or misconduct. The Act ensures the settlement of debts, realization of assets, and distribution of remaining proceeds among partners or creditors according to priority, facilitating a smooth transition to closure.

In a landscape where adaptability and resilience are paramount, Limited Liability Partnerships (LLP) emerge as the optimal choice for entrepreneurs seeking a blend of legal protection and operational flexibility. By encapsulating the features of LLP Act 2008, these structures offer a dynamic platform for entrepreneurial growth and security. LLPs command the ability to navigate regulatory frameworks easily, and leverage tax-efficiency in order to mitigate operational risks. Embracing the ethos of collaboration and progress inherent in partnership structures, LLPs provide a supportive ecosystem at their disposal, propelling the sustained success and prosperity of the business.[16,17,18]

IV. CONCLUSION

Limited liability partnerships (LLPs) have been added to the growing number of unincorporated business organizations available to business. An LLP is a general partnership in which the vicarious liability of the partners for the obligations of the partnership has been limited. From this simple definition, a wide variety of statutes have evolved, differing with respect to degree of vicarious liability protection provided, [19]the obligations of partners to contribute to partnership obligations, and the types of business that may use LLPs. While the LLP was originally used as a vehicle for legal and accounting practices, the flexibility of the partnership structure and the introduction of the limited liability limited partnership (LLLP) may make LLPs and LLLPs an appropriate choice in many business transactions. This Article considers the current legislation allowing for LLPs and LLLPs and discusses several of the business, tax, and intangible issues raised by these new entities.[20]

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